

Mary Taylor, CPA
Auditor of State

LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY

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Mary Taylor, CPA

Auditor of State

INDEPENDENT ACCOUNTANTS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS REQUIRED BY *GOVERNMENT AUDITING STANDARDS*

Life Skills Center of Middletown
Butler County
631 S. Breiel Blvd.
Middletown, Ohio 45042

To the Board of Directors:

We have audited the financial statements of the Life Skills Center of Middletown, Butler County, Ohio, (the School) as of and for the year ended June 30, 2006 and have issued our report thereon dated May 31, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the Comptroller General of the United States *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the School's internal control over financial reporting to determine our auditing procedures to express our opinions on the financial statements and not to opine on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the School's ability to record, process, summarize, and report financial data consistent with management's assertions in the financial statements. A reportable condition is described in the accompanying Schedule of Findings as item 2006-002.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts material to the financial statements we audited may occur and not be timely detected by employees when performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered material weaknesses. However, we do not believe the reportable condition described above is a material weakness. In a separate letter to the School's management dated May 31, 2007, we reported other matters involving internal control over financial reporting which we did not deem reportable conditions.

Compliance and Other Matters

As part of reasonably assuring whether the School's financial statements are free of material misstatement, we tested its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could directly and materially affect the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express an opinion. The results of our tests disclosed an instance of noncompliance or other matter that we must report under *Government Auditing Standards* which is described in the accompanying Schedule of Findings as item 2006-001. In a separate letter to the School's management dated May 31, 2007, we reported other matters related to noncompliance we deemed immaterial.

The School's response to the finding identified in our audit is described in the accompanying Schedule of Findings. We did not audit the School's response and, accordingly, we express no opinion on it.

We intend this report solely for the information and use of the audit committee, management and the Board of Directors. It is not intended for anyone other than these specified parties.

A handwritten signature in cursive script that reads "Mary Taylor".

Mary Taylor, CPA
Auditor of State

May 31, 2007

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**SCHEDULE OF FINDINGS
JUNE 30, 2006**

FINDINGS RELATED TO THE FINANCIAL STATEMENTS REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS
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FINDING NUMBER 2006-001

Noncompliance - Credit Card Expenses

The Board's Credit Card Policy states "upon receipt of original itemized documentation, credit card expenditures will be paid through the Board of Director's bank account." It further provides that "failure to submit an original itemized receipt for any purchase made on the Board credit card shall result in rejection of payment for any and all charges not properly documented. The Board Member for said purchase will then be held responsible for the incurred charges." Further, the policy provides that "the Board of Directors and the Fiscal Officer are responsible for the supervision, distribution, use, and documentation of the credit card.

The following deficiencies were noted with respect to credit card expenses:

- A. A check for \$149.70 was issued to the Board President by the bank for a credit balance on a Board-issued credit card and subsequently cashed by the Board President. This amount, which was allocated proportionally across 19 schools the (the Board President serves as Board President for 19 community schools) by the Fiscal Officer, amounting to \$7.88 per school, was not returned during the audit period by Board President.

- B. Contrary to Auditor of State Bulletin 2003-005 and Ohio Attorney General Opinion 82-006 there was no Board approval for the following expenses:
 - A credit card purchase totaling \$110 was made for two tickets to the Cleveland Zoo's Twilight at the Zoo and allocated proportionally across 18 schools, amounting to \$6.11 per school, for which no business purpose was provided by the Board President.

 - Registration fees totaling \$850 were paid in order for the Board President and a guest to attend the National League of Cities 2005 National Summit on Your City's Families and allocated proportionally across 18 schools, amounting to \$47.22 per school, for which no business purpose was provided by the Board President, nor was a reason provided to substantiate the payment of expenses for a non-Board member.

- C. Contrary to the School's credit card policy, an unsubstantiated credit card purchase totaling \$26.62 at Corky & Lenny's was made by the Board President and allocated proportionally across 18 schools, amounting to \$1.48 per school.

The Board President voluntarily repaid the amounts under audit to each respective School on February 27, 2007.

In order to further correct these deficiencies, the Fiscal Officer and all Board members should review the School's credit card policy to ensure all requirements are adhered to including proper documentation requirements and review of documentation prior to payment of the charges. Additionally, the Fiscal Officer and all Board members should review Auditor of State Bulletin 2003-005 and Ohio Attorney General Opinion 82-006 to ensure all expenses clearly meet the definition of proper public purpose.

Officials' Response: Total errors in calculation for this finding were \$62.69. This expense was incurred during a board members travel on verified and official board business. However, receipts were misplaced. Internal controls have been put in place to ensure that proper documentation requirements and review of documentation prior to payment of the charges are adhered to.

FINDING NUMBER 2006-002

Reportable Condition - Bookkeeping Errors/Adjustments

Throughout the audit, the following deficiencies were noted with respect to the accounting records:

- Although bank reconciliations were performed on each account, no reconciliation was performed to encompass the entire school.
- The accounting system was not properly closed at year end, which allowed system reports to reflect changes made subsequent to year end, such as the voiding of checks.
- GAAP schedules and/or workpapers were not complete
- Checks were not always written in sequential order.
- A check number was used more than once within the system.
- Voided checks were not always maintained.
- Similar expenses were not always consistently charged to the same line items.
- Expenses were improperly allocated to schools for which the expense did not apply.
- Supporting documentation was not always maintained for all expenses.
- Expense Reimbursement Forms and Request for Travel Forms were not provided for all expenses in which they apply.
- Accounting errors resulting in various receivables and/or payables were not corrected in a timely manner.
- Although the Fiscal Officer was generally able to provide immediate explanations, repeated requests were required in order to obtain sufficient supporting documentation.

In order to correct these deficiencies, the Fiscal Officer should:

- Include investments on the reconciliation so the School's cash balance reconciles to the School's book balance.
- Perform month end and year end closing procedures as prescribed by the accounting system software to ensure the integrity of activity performed during the period and achieve proper period cut-off.
- Ensure all GAAP schedules are complete and tie to the trials.
- Write all checks in sequential order.
- Ensure all check numbers are only used once.
- Properly deface and maintain all voided checks for inspection under audit.
- Establish guidelines to ensure all similar expenses are uniformly charged to the same line item.
- Allocate expenses only across schools who received a benefit.
- Maintain supporting documentation for all transactions.
- Maintain all Board policy required forms.
- Ensure all receivables and/or payables resulting from accounting errors are resolved in a timely manner.
- Ensure the existence of a clear audit trail supported by proper documentation for all transactions.

FINDING NUMBER 2006-002 (Continued)

Officials' Response:

Account reconciliations-All bank accounts are reconciled within QuickBooks. The system requires that each bank account be reconciled separately. The system then generates financial statements that reconcile all cash accounts. Thus, the accounting system has already performed this function.

GAAP Schedules and Work papers-The current fiscal officer maintains that GAAP schedules and work papers were prepared appropriately. The current fiscal officer disagrees with the AOS to discuss relative to the accruals of federal revenues, expenses, and their related receivables and payables, as well as the need to breakout small dollar items who's amounts are immaterial to the financial statements.

Netting of State Funding and Continuing Fees Payable and Receivable-The Fiscal Officer contends that netting of payables and receivables is an acceptable practice under generally accepted accounting principles. As such, this error is immaterial as a matter of course.

Sequential checks-The QuickBooks accounting software has a feature called missing checks that allows for every check to be accounted for regardless of date written. Because the fiscal officer had to travel to the school and pay bills on site, some schools checks may have been out of sequence. It does not make sense to void a check that was not used on a particular date when the accounting system accounts for it.

Voided Checks-The majority of voided checks were lost in the mail. Others were destroyed during printing. As such, it is not possible to keep a copy of the actual voided check in these instances.

Similar Expenses not coded consistently-Each school is its own separate school district and legal entity. As such, the fiscal officer may determine that coding for one school does not make sense for a similar school based upon individual circumstances. However, similar coding where practicable will be used.

Allocation of expenses-For certain low dollar expenses shared among 19 schools, the fiscal officer felt that writing small checks (i.e. \$2, 5, \$10, etc. 19 times) to allocate out payments was immaterial as a matter of course.

Supporting documentation- Due to the decentralization of management, physical documents are now generated from a variety of custodians such as the management company, board counsel, board secretary and board fiscal officer. Further, the fiscal officer maintains files in the office by vendor by date. However, the AOS prefers filing by date without regard to the vendor. The fiscal officer's staff works to rearrange its files in accordance with the AOS' preference, but some documents must be verified and re-arranged from other custodians causing delay in some instances in supporting documentation. The school is working to centralize its documentation at the Board office.

Depreciation-The predecessor accountant used a computerized fixed asset system for small items and a spreadsheet for large leasehold improvements. As a result, some schools schedules may not have tied out totally. As a result, a computerized fixed asset system will be used for all assets henceforth.

Expense Reimbursements-Expense reimbursement checks and credit card payments were all signed by an executive officer/board member, not the fiscal officer. All payments were reviewed as part of the financial report and approved by the Board. As such, the need for these forms is rendered moot since the Board member(s) (who would normally sign the reimbursement or travel form) instead, signed the check.

FINDING NUMBER 2006-002 (Continued)

Officials' Response:

Accounting Errors not corrected in timely manner-The school contends that the errors identified are immaterial as a matter of course.

Auditor of State's Conclusion: The bullet points listed in the finding above represent conditions within the internal control structure identified during the audit of this school. While the Auditor of State relies on supporting documentation maintained by the client to determine the propriety of tested transactions, as well as, client-created system documentation to determine the accounting treatment employed in the creation of the entity's financial statements, the Auditor of State has no requirements regarding the filing methods and/or format in which this information is maintained. Rather the errors noted in this finding were the result of; system documentation that did not agree to the reported amounts, improper or inconsistent accounting treatment of transactions, and incomplete or missing supporting documentation of recorded transactions. In addition to any resulting quantitative differences, these errors had unfavorable qualitative impact and taken collectively, represent a significant reportable condition within internal control requiring disclosure in this report.

Comprehensive Annual Financial Report

For the Year Ended June 30, 2006



Life Skills Center of Middletown

Middletown, Ohio

**Life Skills Center of Middletown
Middletown, Ohio**

**Comprehensive Annual Financial Report
For the Year Ended June 30, 2006**

Prepared by Ohio Community School Consultants, Ltd. on behalf of the Board of Directors

LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY

COMPREHENSIVE ANNUAL FINANCIAL REPORT
FOR THE YEAR ENDED JUNE 30, 2006

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Introductory Section

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631 S Breiel Blvd
Middletown, Ohio 45042

(513) 423-1800 (p)
(513) 423-1818 (f)
www.lifeskillscenters.com

June 30, 2007

Life Skills Center of Middletown Community
Members of the Board of Directors

We are pleased to present the Comprehensive Annual Financial Report (CAFR) of the Life Skills Center of Middletown (the School) for the fiscal year ended June 30, 2006. The CAFR is designed to assist and guide the reader in understanding its contents. The report consists of three major sections:

Introductory Section The Introductory Section includes the Transmittal Letter, a list of our Board members and GFOA Certificate of Achievement.

Financial Section The Financial Section consists of the Independent Accountants' Report, Management's Discussion and Analysis, and the Basic Financial Statements as well as the Notes to the Basic Financial Statements that provide an overview of the School's financial position and operating results.

Statistical Section The Statistical Section includes selected financial and demographic information about the School on a multi-year basis.

The School's management is responsible for the reliability of the data presented and the completeness of the presentation, including all disclosures. To the best of our knowledge, the enclosed data is accurate in all material respects and is reported in a manner designed to present fairly the financial position and results of operations of the School. All disclosures necessary to enable the reader to gain an understanding of the School's financial activities have been included.

Further, the School has established a comprehensive framework that is designed to compile sufficient reliable information for the preparation of its financial statements in accordance with generally accepted accounting principles (GAAP). Because the cost of internal controls should not outweigh their benefits, the School's comprehensive framework of internal controls has been designed to provide reasonable rather than absolute assurance that the financial statements will be free from material misstatements.

Ohio law requires independent audits be performed on all financial operations of the School either by the Auditor of State or an independent public accounting firm in accordance with generally accepted accounting principles (GAAP) and generally accepted auditing standards (GAAS). The Auditor of State's Office rendered an opinion on the School's financial statements as of June 30, 2006 and the Independent Accountants' Report on the Basic Financial Statements is included in the Financial Section herein.

As required by GASB Statement No. 34, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments", management is also responsible for preparing a discussion and analysis of the School. This Letter of Transmittal is designed to complement the Management's Discussion and Analysis and should be read in conjunction with it. This discussion follows the Independent Accountants' Report and provides an assessment of the School's finances for fiscal year 2006 and the outlook for the future.

Profile of the Government

Ohio charter schools began operating after the passage of a 1997 State law. Charter schools, commonly referred to as “community schools” in Ohio, are public, non-profit, non-sectarian schools established to operate independently of any School District. These schools also are exempt from many of the education laws of the State allowing them to bring innovation and efficiency to the traditional education model. More importantly, the passage of this law made the concept of school choice a reality in Ohio. As required by law, each of these community schools must have a sponsor. Effective July 1, 2005, the School entered into a contract with a new sponsor, St. Aloysius Orphanage. St. Aloysius Orphanage provides oversight and advisory services to 29 community schools throughout the State serving nearly 7,000 children.

Life Skills Center of Middletown is a School that brings an innovative approach to addressing the high school dropout epidemic head on. This alternative high school program offers at-risk students ages 16-21 years old an opportunity to have a second chance at obtaining a quality education and vocational training and placement. Participation in this program leads students to a high school diploma, not a GED and places them on a path to success (see more at www.lifeskillscenters.com). The School, which first opened its doors in September 2001 in Middletown, Ohio, is run by a three member Board of Directors. The School looks to its nearly five-year history of consistently graduating students from its program twice a year as a measure of its success. The School has contracted with LS Middletown, LLC, a subsidiary of White Hat Management, LLC (the Company) to operate the School on a day-to-day basis. White Hat Management is a national leader in professional education management that serves nearly 18,000 students across multiple states. The Company has managed the school since its inception.

Economic Issues

Since the enactment of community school legislation, the School has been funded solely on the per pupil funding set forth by State of Ohio (see Statistical Section for historical funding levels). Historically, the School has seen increases in the base level per pupil funding amount (currently 2.2 percent for fiscal years 2007 and 2006). However, this amount is still less than the amount that traditional school districts in the State receive per pupil, primarily because community schools are not authorized by statute to levy taxes in the communities that they operate in. By comparison, the Middletown City School District receives over \$10,000 in average per pupil funding from all sources whereas the School (which is also located in the City of Middletown) receives only \$8,023 from all sources. These disparities in funding are in part, the reason why contracting with a professional educational management firm like White Hat Management was an attractive option. By managing multiple schools, the Company is able to gain operational efficiencies that are more difficult to achieve in a stand-alone school. In November 2005, the School renewed its management agreement with White Hat and its affiliates. (See Note 8 for a full description of services provided by the Company.)

As discussed later, the School was funded on 283 full-time equivalent students for fiscal year 2006. As of the date of this letter, it is expected that the School will maintain that enrollment with the possibility of a slight decline consistent with declines seen in other Life Skills Centers throughout the State. Obviously, any decline in enrollment would have a direct corresponding impact to current year revenues.

As a result of legislative changes, management companies that operate schools in the State of Ohio are now required to provide more disclosure on how monies paid by the School to the company are spent. Auditor of State Bulletin No. 2004-009 provided the guidelines of how management companies are expected to comply with this new provision and Note 9 to the basic financial statements under the Financial Section includes the required information for fiscal year ended June 30, 2006.

Awards and Acknowledgements

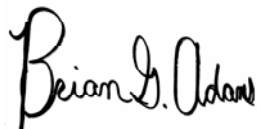
The Government Finance Officer's Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the Life Skills Center of Middletown for its CAFR for the year ended June 30, 2005. This was the second year that the School has received the award. The School was also acknowledged by the Ohio Department of Education as being one of the first community schools in the State to ever receive such an award. The Certificate of Achievement is a prestigious national award, recognizing conformance with the highest standards for preparation of state and local government financial reports.

In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and effectively organized CAFR, whose contents conform to program standards. The CAFR must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid for a period of one year only. We believe our current report, which is included herein, will conform to the high standards required by the Certificate of Achievement program.

The Comprehensive Annual Financial Report was prepared by the fiscal management team for the School. Their commitment to this process has helped to make this report possible. We would also like to thank Mr. Townsend and other members of the Board of Directors and Finance Committee for their support in this endeavor. It is truly appreciated.

Finally, we would like to thank our School community for entrusting us with the education of your children. You are the reason we are here. We are committed to bettering our students, their parents, and the communities we serve by providing the very best alternative in public education.

Sincerely,



Brian G. Adams MBA, CMA, CFM, CGFM
Fiscal Officer/Internal Auditor
Life Skills Center of Middletown



Robert C. Townsend II
President, Board of Directors
Life Skills Center of Middletown



James E. Haynes
Finance Committee Chairman
Life Skills Center of Middletown

Life Skills Center of Middletown
Board of Directors
June 30, 2006

Robert C. Townsend II
James E. Haynes
Edward D. Wilkins, Sr.

Board President
Board Treasurer
Board Secretary

Certificate of Achievement for Excellence in Financial Reporting

Presented to
Life Skills
Center of Middletown
Ohio

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2005

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



Carla E. Perry

President

Jeffrey R. Emer

Executive Director

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Financial Section

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Mary Taylor, CPA

Auditor of State

INDEPENDENT ACCOUNTANTS' REPORT

Life Skills Center of Middletown
Butler County
631 S. Breiel Blvd.
Middletown, Ohio 45042

To the Board of Directors:

We have audited the accompanying basic financial statements of the Life Skills Center of Middletown, Butler County, Ohio, (the School) as of and for the year ended June 30, 2006, as listed in the Table of Contents. These financial statements are the responsibility of the School's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the Comptroller General of the United States' *Government Auditing Standards*. Those standards require that we plan and perform the audit to reasonably assure whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net assets of Life Skills Center of Middletown, Butler County, Ohio, as of June 30, 2006, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 31, 2007, on our consideration of the School's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. While we did not opine on the internal control over financial reporting or on compliance, that report describes the scope of our testing of internal control over financial reporting and compliance and the results of that testing. That report is an integral part of an audit performed in accordance with *Government Auditing Standards*. You should read it in conjunction with this report in assessing the results of our audit.

Management Discussion and Analysis is not a required part of the basic financial statements but is supplementary information accounting principles generally accepted in the United States of America requires. We have applied certain limited procedures, consisting principally of inquiries of management regarding the methods of measuring and presenting the required supplementary information. However, we did not audit the information and express no opinion on it.

We conducted our audit to opine on the School's basic financial statements. The introductory and statistical sections provide additional information and are not a required part of the basic financial statements. We did not subject the introductory and statistical sections to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

A handwritten signature in black ink that reads "Mary Taylor". The signature is written in a cursive, flowing style.

Mary Taylor, CPA
Auditor of State

May 31, 2007

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2006
(Unaudited)**

The discussion and analysis of the Life Skills Center of Middletown's (the School) financial performance provides an overall review of the School's financial activities for the fiscal year ended June 30, 2006. The intent of this discussion and analysis is to look at the School's financial performance as a whole; readers should also review the transmittal letter, the basic financial statements and the notes to the basic financial statements to enhance their understanding of the School's financial performance.

The Management's Discussion and Analysis (MD&A) is an element of the reporting model adopted by the Governmental Accounting Standards Board (GASB) in their Statement No. 34 *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments* issued June 1999. Certain comparative information between the current year and the prior year is required to be presented in the MD&A.

Financial Highlights

- In total, net assets increased \$54,821, which represents a 51.8 percent increase from 2005. The increase is the result of the decrease in funding to the management company from 97 percent to 95 percent and payment of outstanding liabilities to the management company in 2006.
- Total assets increased \$9,480, which represents a 2.9 percent increase from 2005. This was primarily due to an increase in cash and cash equivalents.
- Liabilities decreased \$45,341, which represents an 20.6 percent decrease from 2005. The decrease in liabilities is a direct result of the decrease in State Funding Payable (which directly decreases revenue paid by the State) and Federal Grants Funding Payable (which directly decreases expenses owed as management fees).

Using this Financial Report

This report consists of three parts, the MD&A, the basic financial statements, and notes to those statements. The basic financial statements include a Statement of Net Assets, a Statement of Revenues, Expenses and Changes in Net Assets, and a Statement of Cash Flows.

The School uses enterprise presentation for all of its activities.

Statement of Net Assets

The Statement of Net Assets answers the question of how the School did financially during 2006. This statement includes all assets and liabilities, both financial and capital, and short-term and long-term using the accrual basis of accounting and economic resources focus, which is similar to the accounting used by most private-sector companies. This basis of accounting takes into account all revenues and expenses during the year, regardless of when the cash is received or paid.

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2006
(Unaudited)**

Table 1 provides a summary of the School's net assets for fiscal years 2006 and 2005.

(Table 1)
Statement of Net Assets

	2006	2005
Assets		
Current Assets	\$ 335,691	\$ 326,211
Liabilities		
Current Liabilities	\$ 175,079	\$ 220,420
Net Assets		
Unrestricted Net Assets	\$ 160,612	\$ 105,791

Total assets increased \$9,480. This was primarily due to an increase in cash and cash equivalents from the previous year. Liabilities decreased \$45,341 from 2005. This decrease directly corresponds to the receivables and subsequent payables due under the management agreement with WHLS of Ohio, LLC (WHLS). Under the terms of the management agreement, WHLS is paid a specific percentage of the State and Federal revenues the School receives.

Statement of Revenues, Expenses and Changes in Net Assets

Table 2 shows the changes in net assets for fiscal years 2006 and 2005, as well as a listing of revenues and expenses. This change in net assets is important because it tells the reader that, for the School as a whole, the financial position of the School has improved or diminished. The cause of this may be the result of many factors, some financial, some not. Non-financial factors include the current laws in Ohio restricting revenue growth, facility conditions, required educational programs and other factors.

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2006
(Unaudited)**

(Table 2)
Change in Net Assets

	2006	2005
<u>OPERATING REVENUE</u>		
State Aid	\$ 2,096,605	\$ 2,286,563
<u>NON-OPERATING REVENUES</u>		
Grants	166,945	226,213
Interest Income	7,095	2,859
Total Revenues	2,270,645	2,515,635
<u>OPERATING EXPENSES</u>		
Purchased Services: Management Fees	2,004,354	2,217,971
Purchased Services: Grant Programs	166,945	226,213
Sponsorship Fees	10,200	-
Legal	14,171	15,797
Auditing & Accounting	9,239	5,124
Insurance	3,503	2,552
Board of Education	5,851	5,796
Miscellaneous	1,078	79
Total Operating Expenses	2,215,341	2,473,532
<u>NON-OPERATING EXPENSES</u>		
Income Tax Expense	483	3,600
Total Expenses	2,215,824	2,477,132
Change in Net Assets	\$ 54,821	\$ 38,503

The primary reason for the decrease in overall revenues from 2005 was the decrease in students from 321 in fiscal year 2005 to 283 in fiscal year 2006. The School's most significant expenses, "Purchased Services" decreased as well because of the management agreement in place between the School and WHLS. As stated previously, the agreement provides that specific percentages of the revenues received by the School will be paid to WHLS to fund operations. (See Notes to the Basic Financial Statements, Note 8)

Budgeting Highlights

Unlike other public schools located in the State of Ohio, community schools are not required to follow budgetary provisions set forth in Ohio Rev. Code Chapter 5705, unless specifically provided in the community school's contract with its Sponsor. The contract between the School and its Sponsor does prescribe a budgetary process. The School has developed a one year spending plan and a five-year projection that is reviewed periodically by the Board of Trustees. The five-year projections are also submitted to the Sponsor and the Ohio Department of Education.

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2006
(Unaudited)**

Capital Assets

At the end of fiscal year 2006, the School had \$0 invested in capital assets.

For more information on capital assets, see Note 2 (F) in the Notes to the Basic Financial Statements.

Current Financial Issues

The Life Skills Center of Middletown received revenue for 283 students in 2006 (a decrease from 2005 of 38) and continues to enroll students on a daily basis. State law governing community schools allows for the School to have open enrollment across traditional school district boundaries. The School receives its support almost entirely from State Aid. Per pupil revenue from State Aid for the School averaged \$7,408 in fiscal year 2006 with a 2.2 percent increase in State Basic Aid planned in fiscal year 2007. The School receives additional revenues from grant subsidies.

On July 1, 2005, the School contracted with the Saint Aloysius Orphanage as its new sponsor. State law allows sponsors to assess the schools up to 3 percent of State revenues as an oversight fee, a cost that has not been incurred through the sponsorship by ODE. Saint Aloysius Orphanage charged a half-percent of State Aid to be paid by the School for fiscal year 2006 and will charge one percent for fiscal year 2007.

Contacting the School's Financial Management

This financial report is designed to provide our readers with a general overview of the School's finances and to show the School's accountability for the money it receives. If you have questions about this report or need additional information, contact Brian G. Adams, Fiscal Officer for the Life Skills Center of Middletown, 7215 Sawmill Rd, Suite 050, Dublin, OH 43016 or e-mail at badams@ocscltd.com.

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**STATEMENT OF NET ASSETS
JUNE 30, 2006**

ASSETS

Current Assets

Cash and Cash Equivalents	\$192,477
Accounts Receivable	863
Grants Funding Receivable	78,391
Continuing Fees Receivable	<u>63,960</u>

Total Assets \$335,691

LIABILITIES

Current Liabilities

Accounts payable	\$ 6,768
State Funding Payable	67,326
Grants Funding Payable	100,224
Payable to Schools	<u>761</u>

Total Liabilities \$175,079

NET ASSETS

Unrestricted \$160,612

Total Net Assets \$160,612

See accompanying notes to the basic financial Statements.

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**STATEMENT OF REVENUES,
EXPENSES AND CHANGES IN NET ASSETS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006**

OPERATING REVENUES

State Aid \$2,096,605

OPERATING EXPENSES

Purchased Services: Management Fees 2,004,354

Purchased Services: Grant Programs 166,945

Sponsorship Fees 10,200

Legal 14,171

Auditing and Accounting 9,239

Insurance 3,503

Board of Education 5,851

Miscellaneous 1,078

Total Operating Expenses 2,215,341

Operating (Loss) (118,736)

NON-OPERATING REVENUES (EXPENSES)

Grants 166,945

Interest Income 7,095

Income Tax (483)

Total Non-Operating Revenues 173,557

Change in Net Assets 54,821

Net Assets Beginning of Year 105,791

Net Assets End of Year \$ 160,612

See accompanying notes to the basic financial statements.

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**STATEMENT OF CASH FLOWS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006**

INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS

CASH FLOWS FROM OPERATING ACTIVITIES

Cash Received from State of Ohio	\$2,039,046
Cash Payments to Suppliers for Goods and Services	<u>(2,146,807)</u>

Net Cash Used For Operating Activities (107,761)

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

Cash Received from Grant Programs	162,429
Cash Paid for Income Taxes	<u>(483)</u>

Net Cash Provided by Noncapital Financing Activities 161,946

CASH FLOWS FROM INVESTING ACTIVITIES

Cash Received from Interest on Investments	7,095
--	-------

Net Increase in Cash and Cash Equivalents 61,280

Cash and Cash Equivalents Beginning of Year 131,197

Cash and Cash Equivalents End of Year \$ 192,477

**RECONCILIATION OF OPERATING LOSS TO NET
CASH PROVIDED USED FOR OPERATING ACTIVITIES**

Operating Loss	\$ (118,736)
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**ADJUSTMENTS TO RECONCILE OPERATING LOSS TO NET
CASH USED FOR OPERATING ACTIVITIES**

Changes in Assets and Liabilities:

Accounts Receivable	(863)
Continuing Fees Receivable	57,178
Accounts Payable	2,488
State Funding Payable	(57,559)
Grants Funding Payable	8,970
Payable to Schools	<u>761</u>

Net Cash Used For Operating Activities \$ (107,761)

See accompanying notes to the basic financial statements

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**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2006
(Continued)**

1. DESCRIPTION OF THE SCHOOL AND REPORTING ENTITY

Life Skills Center of Middletown (the School) is a federal 501(c) (3), state nonprofit corporation established pursuant to Ohio Rev. Code Chapters 3314 and 1702 to maintain and provide a school exclusively for any educational, literary, scientific and related teaching service. The School, which is part of the State's education program, is independent of any school district. The School may sue and be sued, acquire facilities as needed, and contract for any services necessary for the operation of the School.

The School contracts with LS Middletown, LLC, a Nevada limited liability company, for most of its functions. LS Middletown, LLC is a single member entity of WHLS of Ohio, LLC, and is the entity which the School's board interacts with regarding day-to-day operations (see note 8 for details).

The School was originally approved for operation under contract with the Ohio State Board of Education (Sponsor) for a period of five years from May 16, 2000 through June 30, 2005. Effective July 1, 2005, House Bill 364 required schools sponsored by the Ohio Department of Education to have new sponsorship in place by June 30, 2005. The School signed a contract with a new sponsor, Saint Aloysius Orphanage, to operate for a period from July 1, 2005 through June 30, 2010.

The School operates under a self-appointing, three-member Board of Directors (the Board). Currently, the Board only has three active members. The School's Code of Regulations specify that vacancies that arise on the Board will be filled by the appointment of a successor director by a majority vote of the then existing directors. The Board is responsible for carrying out the provisions of the contract with the Sponsor, which includes, but is not limited to, state-mandated provisions regarding student population, curriculum, academic goals, performance standards, admission standards, and qualifications of teachers. The School began operations in September 2001 and has one instructional/support facility, which is leased by WHLS. The facility is staffed with teaching personnel employed by WHLS, who provide services to 283 students. The Board also operates the Life Skills Center of Springfield in the city of Springfield. The current three members of the Board also serve on other boards of the Life Skill Centers and Hope Academies. However, these three members do not constitute a majority of those Boards's membership as they do with the Life Skills Center of Springfield.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements of the School have been prepared in conformity with generally accepted accounting principles as applied to governmental nonprofit organizations. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The School also applies Financial Accounting Standards Board (FASB) statements and interpretations issued on or before November 30, 1989, provided they do not conflict with GASB pronouncements. The School does not apply FASB statements and interpretations issued after November 30, 1989. The more significant of the School's accounting policies are described below.

A. Basis of Presentation

The School's basic financial statements consist of a Statement of Net Assets, a Statement of Revenues, Expenses and Changes in Net Assets, and a Statement of Cash Flows. Enterprise fund reporting focuses on the determination of the change in net assets, financial position and cash flows.

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2006
(Continued)**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

A. Basis of Presentation (Continued)

Auditor of State of Ohio Bulletin No. 2000-005 requires the presentation of all financial activity to be reported within one enterprise fund for year-end reporting purposes. Enterprise accounting is used to account for operations that are financed and operated in a manner similar to private business enterprises where the intent is that the costs (expenses) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

B. Measurement Focus and Basis of Accounting

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. Enterprise accounting uses a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities are included on the Statement of Net Assets. Operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets. The accrual basis of accounting is utilized for reporting purposes. Revenues are recognized when they are earned, and expenses are recognized when they are incurred.

C. Budgetary Process

Unlike traditional public schools located in the State of Ohio, community schools are not required to follow budgetary provisions set forth in Ohio Rev. Code Section 5705, unless specifically provided in the School's contract with its Sponsor. The contract between the School and its Sponsor requires a detailed school budget for each year of the contract. In addition, the Board adopted an operating budget at the beginning of fiscal year 2006. However, the budget does not have to follow the provisions of Ohio Rev. Code Section 5705, except for section 5705.391 as it relates to five-year forecasts.

D. Cash and Cash Equivalents

All cash received by the School is maintained in a demand deposit account, certificates of deposit, and STAROhio. For purposes of the Statement of Cash Flows and for presentation on the Statement of Net Assets, investments with an original maturity of three months or less at the time they are purchased are considered to be cash equivalents.

During fiscal year 2006, investments were limited to the State Treasurer's Investment Pool, STAROhio. STAROhio is an investment pool managed by the State Treasurer's Office, which allows governments within the State to pool their funds for investment purposes. STAROhio is not registered with the SEC as an investment company, but does operate in a manner consistent with Rule 2a7 of the Investment Company Act of 1940. Investments in STAROhio are valued at STAROhio's share price, which is the price the investment could be sold for on June 30, 2006.

E. Intergovernmental Revenues

The School currently participates in the State Foundation Program, the State Disadvantaged Pupil Impact Aid (DPIA) Program, and the Career Based Intervention (CBI) Program, which are reflected under "State Aid" on the Statement of Revenues, Expenses and Changes in Net Assets. Revenues received from these programs are recognized as operating revenues in the accounting period in which all eligibility requirements have been met.

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2006
(Continued)**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

E. Intergovernmental Revenues (Continued)

Non-exchange transactions, in which the School receives value without directly giving equal value in return, include grants, entitlements, and contributions. Grants, entitlements, and contributions are recognized as non-operating revenues in the accounting period in which all eligibility requirements have been met.

Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the fiscal year when use is first permitted; matching requirements, in which the School must provide local resources to be used for a specified purpose; and expenditure requirements, in which the resources are provided to the School on a reimbursement basis. Amounts awarded under the above programs for the 2006 school year totaled \$2,263,550.

F. Capital Assets and Depreciation

For purposes of recording capital assets, the Board has a capitalization threshold of \$5,000. The School has no capital assets, as the School operates under a management agreement with WHLS. (See Note 8)

G. Use of Estimates

In preparing the financial statements, management is sometimes required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

H. Net Assets

Net assets represent the difference between assets and liabilities. All of the School's net assets at June 30, 2006 were unrestricted.

I. Operating Revenues and Expenses

Operating revenues are those revenues that are generated directly from the School's primary activities. For the School, these revenues are primarily State Aid payments. Operating expenses are necessary costs incurred to provide the goods and services that are the primary activities of the School. Revenues and expenses not meeting this definition are reported as non-operating.

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2006
(Continued)**

3. DEPOSITS AND INVESTMENTS

A. Deposits with Financial Institutions

At June 30, 2006, the carrying amount of all School deposits was \$75,209. Based on the criteria described in GASB Statement No. 40, "Deposits and Investment Risk Disclosures", as of June 30, 2006, \$75,209 was covered by the Federal Deposit Insurance Corporation.

Custodial credit risk is the risk that, in the event of bank failure, the School's deposits may not be returned. All deposits are collateralized with eligible securities in amounts equal to at least 105 percent of the carrying value of the deposits. Such collateral, as permitted by the Ohio Revised Code, is held in single financial institution collateral pools at Federal Reserve Banks, or at member banks of the federal reserve system, in the name of the respective depository bank and pledged as a pool of collateral against all of the public deposits it holds or as specific collateral held at the Federal Reserve Bank in the name of the School.

B. Investments

As of June 30, 2006, the School had the following investments and maturities:

<u>Investment Type</u>	<u>Balance at Fair Value</u>	<u>Investment Maturities</u>		
		<u>6 months or less</u>	<u>7 to 12 months</u>	<u>Greater than 12 months</u>
STAROhio	\$117,268	\$117,268	\$ -	\$ -

Interest Rate Risk: As a means of limiting its exposure to fair value losses arising from rising interest rates and according to state law, the School's investment policy limits investment portfolio maturities to five years or less.

Credit Risk: Standard & Poor's has assigned STAROhio an AAAM money market rating.

Concentration of Credit Risk: The School places no limit on the amount that may be invested in any one issuer. The following table includes the percentage of each investment type held by the School at June 30, 2006:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Percent to Total</u>
STAROhio	\$117,268	100.00

4. STATE FUNDING PAYABLE

The School has also recognized on its Statement of Net Assets a "State Funding Payable" for the amount of State Aid directly related to FTE, estimated to be repaid by the School to the Ohio Department of Education (ODE) based on the difference in the amount the School actually received versus the amount earned through student FTE enrollment as determined at the end of the year. A payable reflects that the School was funded on a higher estimated enrollment figure throughout the year than what the actual FTE enrollment figure was calculated to be at year-end. At June 30, 2006, the amount of "State Funding Payable" was \$67,326.

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2006
(Continued)**

5. CONTINUING FEES RECEIVABLE

A "Continuing Fees Receivable" from WHLS has been recorded by the School in the amount of \$63,960 for 95 percent of the "State Funding Payable" due to the State for the FTE liability. (See Note 4)

6. GRANTS FUNDING RECEIVABLE/PAYABLE

The School has recorded "Grants Funding Receivable" in the amount of \$78,391 to account for the remainder of State and Federal awards allocated to the School, but not received as of June 30, 2006.

Additionally, under the terms of the management agreement (See Note 8), the School has recorded a liability to WHLS in the amount of \$100,224 for 100 percent of any State and Federal monies uncollected or unpaid to WHLS as of June 30, 2006.

7. RISK MANAGEMENT

Property and Liability - The School is exposed to various risks of loss related to torts; theft or damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. As part of its management agreement with WHLS, WHLS has contracted with an insurance company for property and general liability insurance pursuant to the Management Agreement. There was no significant reduction in insurance coverage from the prior year and claims have not exceeded insurance coverage over the past three years. (See Note 8)

Director and Officer - Coverage has been purchased by the School with a \$1,000,000 aggregate limit and no deductible.

8. AGREEMENT WITH WHLS

Effective November 1, 2005, the School entered into a multi-year Management Agreement (Agreement) with WHLS (through its subsidiary LS Middletown, LLC), which is an educational consulting and management company. The Agreement's term runs through June 30, 2007 and will renew for additional one year terms ending on June 30, 2010 unless terminated for cause by either party. Substantially all functions of the School have been contracted to WHLS. WHLS is responsible and accountable to the School's Board of Directors for the administration and day-to-day operations. As part of the terms of this agreement, the "Continuing Fee" percentage of the School is 95 percent. "Continuing Fees" are defined in the Agreement as, "...the revenue per student received by the School from the State of Ohio Department of Education pursuant to Title 33 and other provisions of the Ohio Revised Code...". With regard to grant funding, the agreement reads as follows: "Federal Title Programs, lunch programs revenue, and other such federal, state and local government grant funding designated." The continuing fee is paid to WHLS based on the previous month's qualified gross revenues to compensate the school for the education of its students shall be fully paid to the Company". As such, WHLS receives 95 percent of "State Aid" (see note 2 E) and 100 percent of all other federal, state, and local grants. The School retains 5 percent of the "State Aid" as well as miscellaneous revenues generated from interest on deposits and donations.

The School had purchased service expenses for the year ended June 30, 2006, to WHLS of \$2,171,299, receivables of \$63,960, and payables to WHLS at June 30, 2006 aggregating \$100,224. WHLS will be responsible for all costs incurred in providing the educational program at the School, which include but are not limited to, salaries and benefits of all personnel, curriculum materials, textbooks, library books, computers and other equipment, software, supplies, building payments, maintenance, capital, and insurance.

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2006
(Continued)**

9. MANAGEMENT COMPANY EXPENSES

For the year ended June 30, 2006, White Hat Ventures, LLC and its affiliates incurred the following expenses on behalf of the School.

	<u>2006</u>
Expenses	
Direct Expenses:	
Salaries & wages	\$ 697,253
Employees' benefits	171,465
Professional & technical services	215,287
Property services	240,446
Travel	8,677
Communications	38,967
Utilities	44,426
Books, periodicals, & films	3,940
Other supplies	150,498
Depreciation	63,054
Other direct costs	54,471
Indirect Expenses:	
Overhead	<u>449,642</u>
Total Expenses	<u>\$ 2,138,126</u>

Overhead charges are assigned to the School based on a percentage of revenue. These charges represent the indirect cost of services provided in the operation of the School. Such services include, but are not limited to facilities management, equipment, operational support services, management and management consulting, board relations, human resources management, training and orientation, financial reporting and compliance, purchasing and procurement, education services, technology support and marketing and communications.

10. DEFINED BENEFIT PENSION PLANS

The School has contracted with WHLS to provide employee services and to pay those employees. However, these contract services do not relieve the School of the obligation for remitting pension contributions. The retirement systems consider the School as the Employer-of-Record and the School ultimately responsible for remitting retirement contributions to each of the systems noted below: (See Note 8)

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2006
(Continued)**

10. DEFINED BENEFIT PENSION PLANS (Continued)

A. School Employees Retirement System

WHLS, on behalf of the School, contributes to the School Employees Retirement System of Ohio (SERS), a cost-sharing multiple-employer defined benefit pension plan. SERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Authority to establish and amend benefits is provided by Chapter 3309 of the Ohio Revised Code. SERS issues a publicly available, stand-alone financial report that includes financial statements and required supplementary information. The report may be obtained by writing to the School Employees Retirement System, 300 East Broad Street, Suite 100, Columbus, Ohio 43215-3746 by calling (800) 878-5853 or by visiting the SERS website at www.ohsers.org.

Plan members are required to contribute 10 percent of their annual covered salary and the School is required to contribute at an actuarially determined rate. The current School rate is 14 percent of annual covered payroll. A portion of the School's contribution is used to fund pension obligations with the remainder being used to fund health care benefits; for fiscal year 2006, 10.58 percent of annual covered salary was the portion used to fund pension obligations. For fiscal year 2005, 10.57 percent of annual covered salary was the portion used to fund pension obligations. The contribution requirements of plan members and employers are established and may be amended, up to statutory maximum amounts, by the SERS Retirement Board. The School's required contribution for pension obligations to SERS for the years ended June 30, 2006, 2005, and 2004 were \$18,868, \$21,222, and \$15,234, respectively, of which 100 percent has been contributed.

B. State Teachers Retirement System

WHLS, on behalf of the School, contributes to the State Teachers Retirement System of Ohio (STRS Ohio), which is a cost-sharing, multiple-employer public employee retirement system. STRS Ohio provides retirement and disability benefits to members, and death and survivor benefits to beneficiaries. STRS Ohio issues a stand-alone financial report, which may be obtained by writing to STRS Ohio, 275 East Broad Street, Columbus, Ohio 43215-3371 or by calling (614) 227-4090, or by visiting the STRS Ohio website at www.strsoh.org.

New members have a choice of three retirement plans, a Defined Benefit (DB) Plan, a Defined Contribution (DC) Plan, and a Combined Plan. The DB plan offers an annual retirement allowance based on final average salary times a percentage that varies based on years of service, or an allowance based on member contributions and earned interest matched by STRS Ohio funds times an actuarially determined annuity factor. The DC Plan allows members to place all their member contributions and employer contributions equal to 10.5 percent of earned compensation into an investment account. Investment decisions are made by the member. A member is eligible to receive a retirement benefit at age 50 and termination of employment. The Combined Plan offers features of both the DB Plan and the DC Plan. In the Combined Plan, member contributions are invested by the member, and employer contributions are used to fund the defined benefit payment at a reduced level from the regular DB Plan. DC and Combined Plan members will transfer to the Defined Benefit Plan during their fifth year of membership unless they permanently select the DC or Combined Plan. Existing members with less than five years of service credit as of June 30, 2001, were given the option of making a one time irrevocable decision to transfer their account balances from the existing DB Plan into the DC Plan or the Combined Plan. This option expired on December 31, 2001. Benefits are established by Chapter 3307 of the Ohio Revised Code.

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2006
(Continued)**

10. DEFINED BENEFIT PENSION PLANS (Continued)

B. State Teachers Retirement System (Continued)

A DB or Combined Plan member with five or more years credited service that becomes disabled may qualify for a disability benefit. Eligible spouses and dependents of these active members who die before retirement may qualify for survivor benefits. Members in the DC Plan who become disabled are entitled only to their account balance. If a member dies before retirement benefits begin, the member's designated beneficiary is entitled to receive the member's account balance.

For the fiscal year ended June 30, 2006, plan members were required to contribute 10 percent of their annual covered salaries. The School was required to contribute 14 percent; 13 percent was the portion used to fund pension obligations. For fiscal year 2005, the portion used to fund pension obligations was also 13 percent. Contribution rates are established by the State Teachers Retirement Board, upon recommendations of its consulting actuary, not to exceed statutory maximum rates of 10 percent for members and 14 percent for employers. Chapter 3307 of the Ohio Revised Code provides statutory authority for member and employer contributions.

The School's required contribution for pension obligations to STRS Ohio for the fiscal years ended June 30, 2006, 2005, and 2004 were \$66,236, \$62,279, and \$54,414 respectively, of which 100 percent has been contributed.

11. POSTEMPLOYMENT BENEFITS

WHLS, on behalf of the School, provides comprehensive health care benefits to retired teachers and their dependents through the State Teachers Retirement System (STRS Ohio), and to retired non-certified employees and their dependents through the School Employees Retirement System (SERS). Benefits include hospitalization, physicians' fees, prescription drugs, and partial reimbursement of monthly Medicare premiums. Benefit provisions and the obligations to contribute are established by the Systems based on authority granted by State statute. Both Systems are funded on a pay-as-you-go basis.

STRS Ohio retirees who participated in the DB or Combined Plans and their dependents are eligible for health care coverage. The STRS Ohio Board has statutory authority over how much, if any, of the health care costs will be absorbed by STRS Ohio. All benefit recipients pay a portion of health care cost in the form of a monthly premium. By law, the cost of coverage paid from STRS Ohio funds is included in the employer contribution rate, currently 14 percent of covered payroll. For the fiscal year ended June 30, 2006, the STRS Ohio Board allocated employer contributions equal to 1 percent of covered payroll to the Health Care Stabilization Fund. For the School, this amount equaled \$5,095 for fiscal year 2006.

STRS Ohio pays health care benefits from the Health Care Stabilization Fund. At June 30, 2005, (the latest information available) the balance in the Fund was \$3.3 billion. For the fiscal year ended June 30, 2005, net health care costs paid by STRS Ohio were \$254,780,000 and STRS Ohio had 115,395 eligible benefit recipients.

For SERS, coverage is made available to service retirees with ten or more years of qualifying service credit, and to disability and survivor benefit recipients. All retirees and beneficiaries are required to pay a portion of their premium for health care. The portion is based on years of service, Medicare eligibility, and retirement status.

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2006
(Continued)**

11. POSTEMPLOYMENT BENEFITS (Continued)

After the allocation for basic benefits, the remainder of the employer's 14 percent contribution is allocated to providing health care benefits. For the fiscal year ended June 30, 2006, employer contributions to fund health care benefits were 3.42 percent of covered payroll, compared to 3.43 percent of covered payroll for fiscal year 2005. In addition, SERS levies a surcharge to fund health care benefits equal to 14 percent of the difference between a minimum pay and the member's pay, pro-rated for partial service credit. For fiscal year 2006, the minimum pay was established at \$35,800. However, the surcharge is capped at 2 percent of each employer's SERS salaries. For the 2006 fiscal year, the School paid \$8,832 to fund health care benefits, including the surcharge.

The surcharge, added to the unallocated portion of the 14 percent employer contribution rate, provides for maintenance of the asset target level for the health care fund. The target level for the health care reserve is 150 percent of the projected claims less premium contributions for the next fiscal year. Expenses for health care for the fiscal year ended June 30, 2005 (the latest information available), were \$178,221,113. At June 30, 2005, SERS had net assets available for payment of health care benefits of \$267.5 million. SERS has approximately 58,123 participants eligible to receive health care benefits.

12. CONTINGENCES

A. Grants

Amounts received from grantor agencies are subject to audit and adjustment by the grantor. Any disallowed costs may require refunding to the grantor. Amounts which may be disallowed, if any, are not presently determinable. However, in the opinion of the School, any such adjustments will not have a material adverse effect on the financial position of the School.

B. Pending Litigation

A suit was filed in the US District Court, Southern District of Ohio, Western Division on October 6, 2004, which challenges the funding of charter schools under Equal Protection, Due Process and claims violation of a right to vote on the bodies administering public schools. The case is still pending. The effect of this suit, if any, on the School is not presently determinable.

C. Full Time Equivalency

The Ohio Department of Education conducts reviews of enrollment data and full-time equivalency (FTE) calculations made by the schools. These reviews are conducted to ensure the schools are reporting accurate student enrollment data to the State, upon which state foundation funding is calculated. The conclusions of this review could result in state funding being adjusted. Adjustments as of June 30, 2006 are described in Note 4. However, in the opinion of the School, any such adjustments will not have a material adverse effect on the financial position of the School.

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2006
(Continued)**

13. STATE SCHOOL FUNDING DECISION

On December 11, 2002, the Ohio Supreme Court issued its latest opinion regarding the State's school funding plan. The decision reaffirmed earlier decisions that Ohio's current school-funding plan is unconstitutional.

The Supreme Court relinquished jurisdiction over the case and directed "...the Ohio General Assembly to enact a school-funding scheme that is thorough and efficient..." The School is currently unable to determine what effect, if any, this decision will have on its future State funding and on its financial operations.

14. FEDERAL TAX STATUS

In August 2004 the School filed its application for tax-exempt status under Section 501(c)(3) of the Internal Revenue Code. In the interim, the School has begun the process to file IRS Form 990, "Return of Organization Exempt from Income Tax".

15. SPONSORSHIP FEES

The school contracted with Saint Aloysius Orphanage as its sponsor effective July 1, 2005. The school pays the Sponsor one-half percent of the State Aid. Total fees for fiscal year 2006 were \$10,200. The contract is for five years ending on June 30, 2010. The Sponsor is to provide oversight, monitoring, and technical assistance for the School.

16. RECEIVABLES/PAYABLES FROM SCHOOLS

As described in Note 1, this School has common board members with other Hope Academies and Life Skills Centers. These Board members typically have common costs that are to be shared between the schools. As of June 30, 2006, the School has \$761 due to other schools (payable).

17. SUBSEQUENT EVENTS

During fiscal year 2007, the Ohio Legislature passed H.B 79 which modified certain provisions of the charter school statute. On March 28, 2007, the School initiated a lawsuit in Franklin County challenging the legality of certain provisions of H.B. 79. The effects of this lawsuit are presently not determinable.

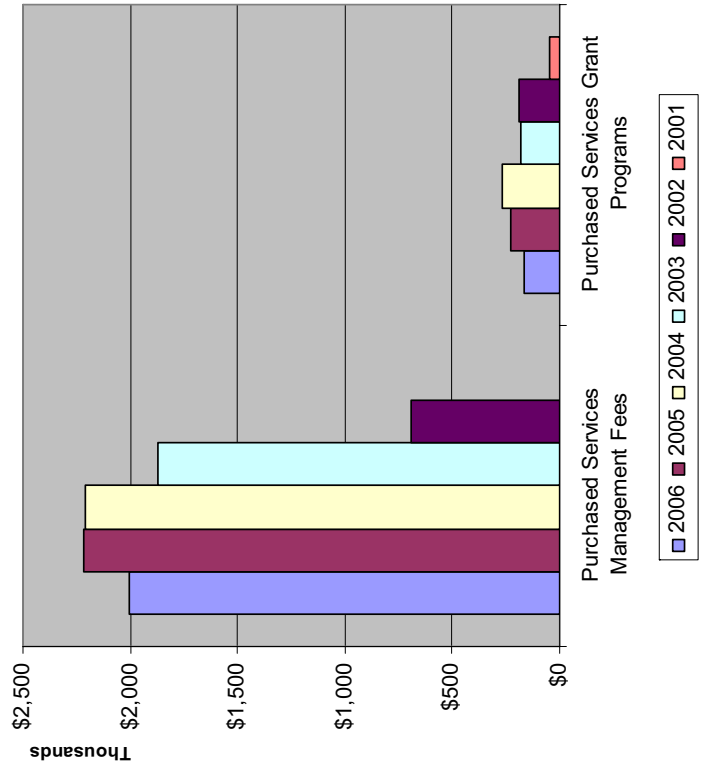
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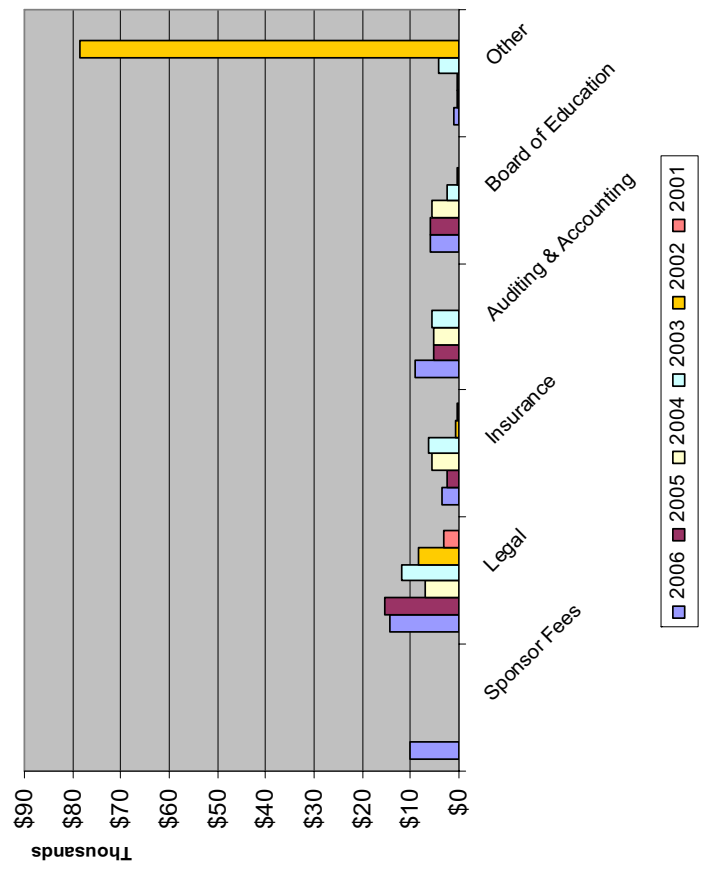
**Life Skills Center of Middletown
Operating Expenses by Category
Last Six Fiscal Years**

Year	Purchased Services Management Fees	Purchased Services Grant Programs	Sponsor Fees	Legal	Insurance	Auditing & Accounting	Board of Education	Other	Total	Enrollment	Per Pupil Expense
2006	\$ 2,004,354	\$ 166,945	\$10,200	\$ 14,171	\$ 3,503	\$ 9,239	\$ 5,851	\$ 1,078	\$ 2,215,341	283	\$ 7,828
2005	\$ 2,217,971	\$ 226,213	\$ -	\$ 15,440	\$ 2,552	\$ 5,124	\$ 5,796	\$ 436	\$ 2,473,532	321	\$ 7,706
2004	\$ 2,205,411	\$ 265,017	\$ -	\$ 6,849	\$ 5,692	\$ 5,145	\$ 5,671	\$ 499	\$ 2,494,284	354	\$ 7,046
2003	\$ 1,867,339	\$ 181,070	\$ -	\$ 11,916	\$ 6,300	\$ 5,500	\$ 2,563	\$ 4,309	\$ 2,078,997	307	\$ 6,772
2002	\$ 688,178	\$ 186,765	\$ -	\$ 8,473	\$ 593	\$ -	\$ 240	\$ 78,418	\$ 962,667	144	\$ 6,685
2001	\$ -	\$ 45,001	\$ -	\$ 3,274	\$ 188	\$ -	\$ -	\$ 76	\$ 48,539	N/A	N/A

Purchased Services Expenses By Fiscal Year



Other Operating Expenses by Fiscal Year



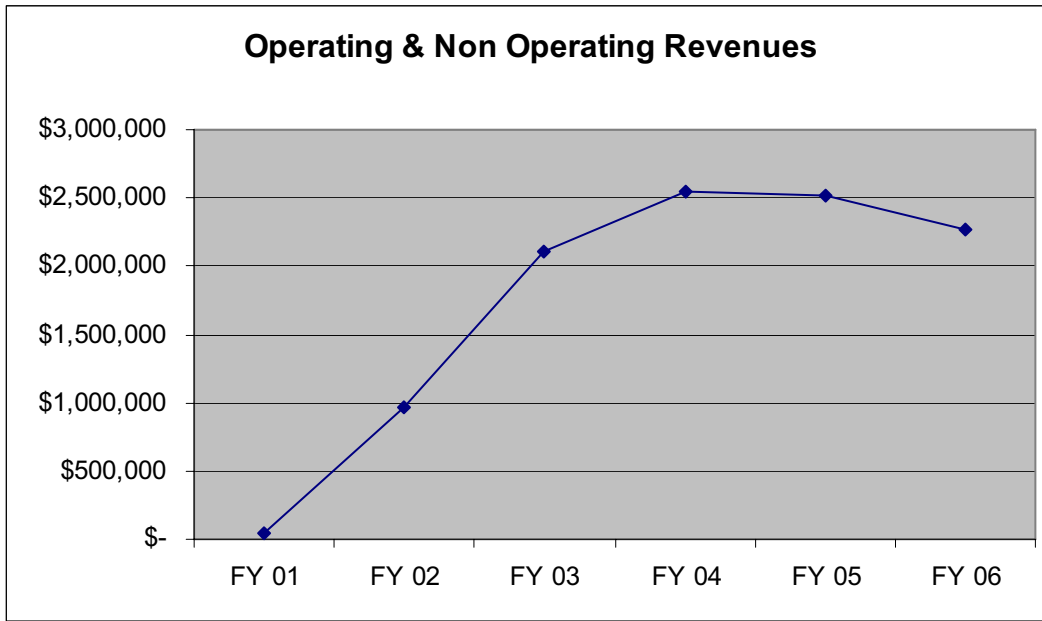
Note 1: On June 20, 2002, the School amended its management agreement with WHLS so that all facility costs would be paid by the management company in exchange for a higher management fee.

Note 2: The School began enrolling students in FY 02.

Source: School Financial Records

Life Skills Center of Middletown
 Operating and Non-Operating Revenues
 Last Six Fiscal Years

Year	State Aid	Grants	Other	Total
2006	\$ 2,096,605	\$ 166,945	\$ 7,095	\$ 2,270,645
2005	\$ 2,286,563	\$ 226,213	\$ 2,859	\$ 2,515,635
2004	\$ 2,276,181	\$ 265,017	\$ 1,047	\$ 2,542,245
2003	\$ 1,925,091	\$ 181,070	\$ -	\$ 2,106,161
2002	\$ 780,215	\$ 186,765	\$ -	\$ 966,980
2001	\$ -	\$ 50,000	\$ -	\$ 50,000

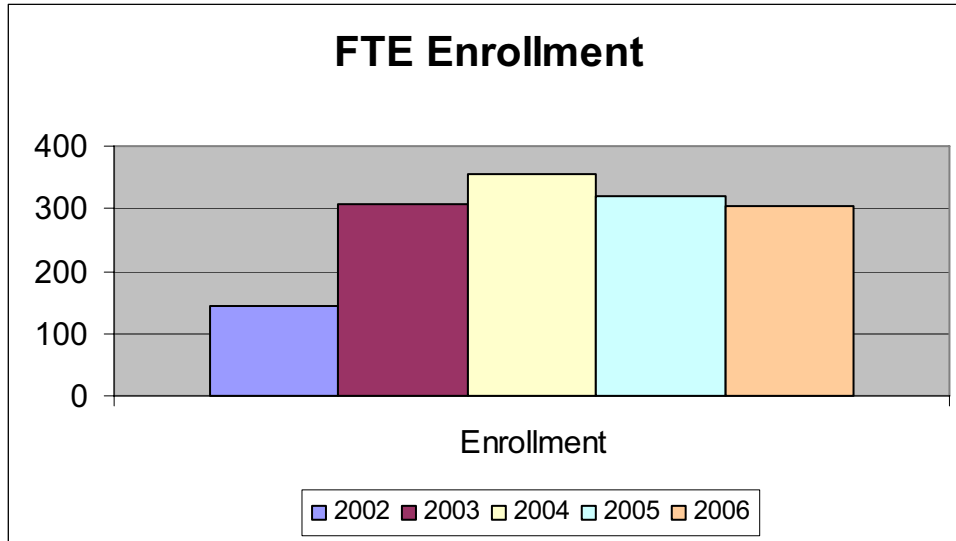


Note: The School began enrolling students in FY 02.

Source: School Financial Records

Life Skills Center of Middletown
Full-Time Equivalent (FTE) Enrollment
Last Five Fiscal Years

<u>Year</u>	<u>Enrollment</u>
2006	283
2005	321
2004	354
2003	307
2002	144

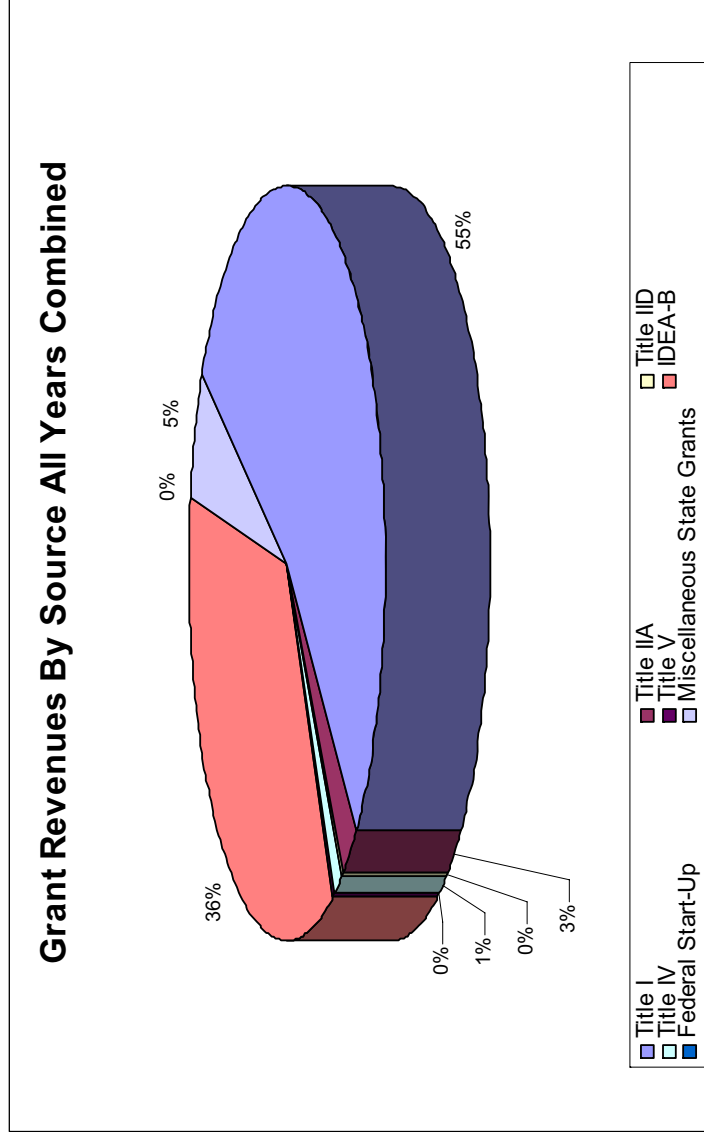


Note: The School began enrolling students in FY 02.

Source: School Financial Records

Life Skills Center of Middletown
Grant Revenues by Source
Last Six Fiscal Years

Year	Title I	Title IIA	Title IID	Title IV	Title V	IDEA-B	Federal Start-Up	Miscellaneous State Grants	Total
2006	\$ 90,325	\$ 4,637	\$ 734	\$ 2,357	\$ 468	\$ 59,349	\$ -	\$ 9,075	\$ 166,945
2005	\$ 134,697	\$ 6,912	\$ 2,252	\$ 1,820	\$ 1,340	\$ 65,900	\$ -	\$ 13,292	\$ 226,213
2004	\$ 59,316	\$ 5,044	\$ 1,606	\$ 1,143	\$ 1,854	\$ 33,876	\$ 150,000	\$ 12,178	\$ 265,017
2003	\$ 15,334	\$ 6,717	\$ 454	\$ 500	\$ 598	\$ 1,165	\$ 150,000	\$ 6,302	\$ 181,070
2002	\$ 15,300	\$ 1,405	\$ -	\$ -	\$ 566	\$ 13,818	\$ 150,000	\$ 5,676	\$ 186,765
2001	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 50,000	\$ 50,000

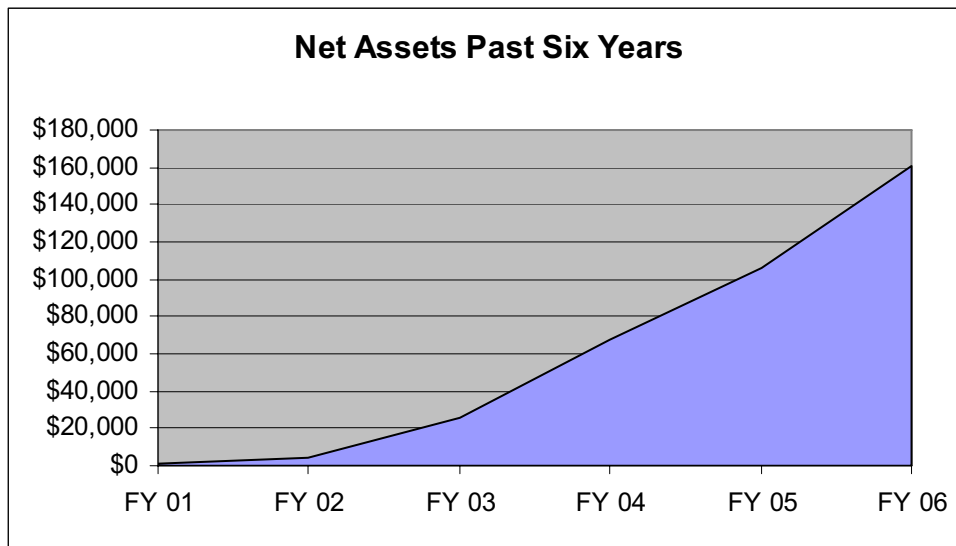


Note: The School began enrolling students in FY 02.

Source: School Financial Records

Life Skills Center of Middletown
Net Assets
Last Six Fiscal Years

<u>Year</u>	<u>Unrestricted</u>	<u>Total</u>	<u>Change in Net Assets</u>
2006	\$ 160,612	\$ 160,612	\$ 54,821
2005	\$ 105,791	\$ 105,791	\$ 38,503
2004	\$ 67,288	\$ 67,288	\$ 41,289
2003	\$ 25,999	\$ 25,999	\$ 22,064
2002	\$ 3,935	\$ 3,935	\$ 2,474
2001	\$ 1,461	\$ 1,461	\$ 1,461

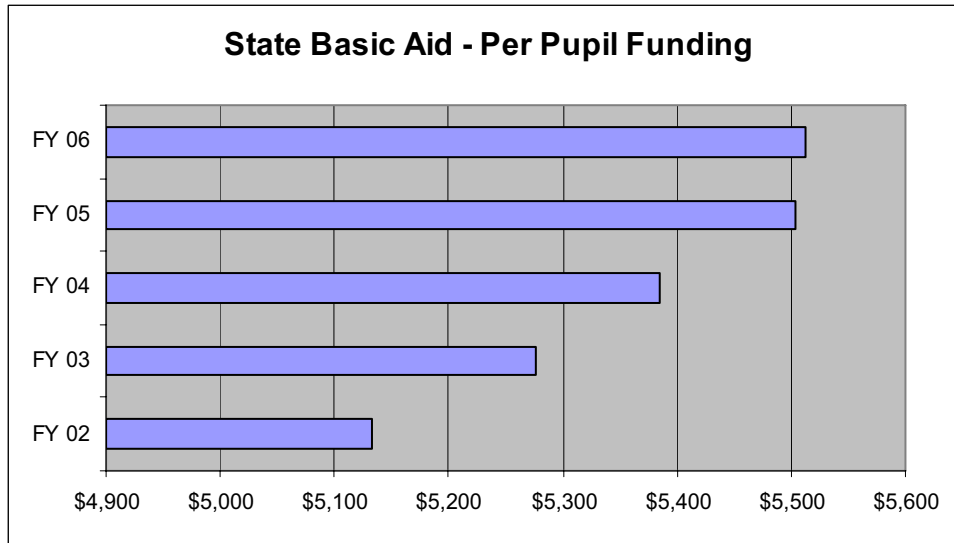


Note: The School began enrolling students in FY 02.

Source: School Financial Records

Life Skills Center of Middletown
 State Basic Aid – Per Pupil Funding Amount
 Last Five Fiscal Years

Year	Per Pupil Funding	Cost of Doing Business	Total Per Pupil
2006	\$ 5,283	1.0431	\$ 5,511
2005	\$ 5,169	1.0646	\$ 5,503
2004	\$ 5,058	1.0646	\$ 5,385
2003	\$ 4,949	1.0663	\$ 5,277
2002	\$ 4,814	1.0663	\$ 5,133



Note 1: In addition to the above, The School also receives other sources of State Aid including (but not limited to) Career Based Intervention Funding, Disadvantaged Pupil Impact, Parity Aid, and Special Education funding. The revenues have collectively been identified on the Statement of Revenues, Expenses, and Changes in Net Assets as “State Aid”.

The Cost of Doing Business Factors are determined by the State of Ohio and vary by region.

Note 2: The School began enrolling students in FY 02.

Source: Ohio Department of Education

Life Skills Center of Middletown
Student Population by Resident District
2006 Fiscal Year

<u>Resident District</u>	<u>%</u>
Carlisle	4.75%
Edgewood	4.28%
Fairfield	3.61%
Franklin	7.64%
Hamilton	2.89%
Lakota	8.75%
Lebanon	3.75%
Madison	4.29%
Middletown	49.25%
Preble Shawnee	4.02%
Monroe	2.87%
All Other Districts	11.07%

Note 1: The school has open enrollment and draws its population from a large surrounding area. The traditional school district that the student resides in is referred to as the Resident District.

Note 2: Districts representing less than 2 percent of the student population are combined under the heading "All Other Districts".

Source: Ohio Department of Education

Life Skills Center of Middletown
Miscellaneous Statistics

School Address: 631 South Breiel Boulevard
Middletown, Ohio 45042

Square Footage: 13,182 sq. ft.

Date of Incorporation: 10/23/2000

Instructional Staff: 14

Total FY 06 Staff: 19

} **Note: All Staff are employees of WHLS of Ohio, LLC. See Note 8 in Notes to the Basic Financial Statements.**

**Instructional Staff/
Student Ratio:** 20:1

**Number of Graduates
since inception:** 444

**Percent of Low
Income Students:** 39.32%

Source: School Records



Mary Taylor, CPA
Auditor of State

**LIFE SKILLS CENTER OF MIDDLETOWN
BUTLER COUNTY**

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

**CERTIFIED
AUGUST 14, 2007**