



Dave Yost • Auditor of State

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

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Dave Yost • Auditor of State

INDEPENDENT AUDITOR'S REPORT

Stepstone Academy
Cuyahoga County
2121 East 32nd Street
Cleveland, Ohio 44115

To the Board of Directors:

Report on the Financial Statements

We have audited the accompanying financial statements of the Stepstone Academy, Cuyahoga County, Ohio, (the School), as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the School's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for preparing and fairly presenting these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes designing, implementing, and maintaining internal control relevant to preparing and fairly presenting financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to opine on these financial statements based on our audit. We audited in accordance with auditing standards generally accepted in the United States of America and the financial audit standards in the Comptroller General of the United States' *Government Auditing Standards*. Those standards require us to plan and perform the audit to reasonably assure the financial statements are free from material misstatement.

An audit requires obtaining evidence about financial statement amounts and disclosures. The procedures selected depend on our judgment, including assessing the risks of material financial statement misstatement, whether due to fraud or error. In assessing those risks, we consider internal control relevant to the School's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not to the extent needed to opine on the effectiveness of the School's internal control. Accordingly, we express no opinion. An audit also includes evaluating the appropriateness of management's accounting policies and the reasonableness of their significant accounting estimates, as well as our evaluation of the overall financial statement presentation.

We believe the audit evidence we obtained is sufficient and appropriate to support our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Stepstone Academy, Cuyahoga County as of June 30, 2016, and the changes in its financial position and its cash flows for the year then ended in accordance with the accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require this presentation to include *Management's discussion and analysis*, and schedules of net pension liabilities, and pension contributions listed in the table of contents, to supplement the basic financial statements. Although this information is not part of the basic financial statements, the Governmental Accounting Standards Board considers it essential for placing the basic financial statements in an appropriate operational, economic, or historical context. We applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, consisting of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries to the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not opine or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to opine or provide any other assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 31, 2017, 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. That report describes the scope of our internal control testing over financial reporting and compliance, and the results of that testing, and does not opine on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the School's internal control over financial reporting and compliance.



Dave Yost
Auditor of State
Columbus, Ohio

March 31, 2017

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2016
(UNAUDITED)**

The discussion and analysis of the Stepstone Academy (the School) financial performance provides an overall review of the School's financial activities for the fiscal year ended June 30, 2016. The intent of this discussion and analysis is to look at the School's financial performance as a whole; readers should also review the basic financial statements and notes to the basic financial statements to enhance their understanding of the School's financial performance.

The Management's Discussion and Analysis (the 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. Certain comparative information between the current fiscal year and the prior fiscal year is required to be presented in the MD&A

FINANCIAL HIGHLIGHTS

Key Financial Highlights for the School for the 2015-16 school year are as follows:

- Total assets and deferred outflows of resources increased by \$666,688.
- Total liabilities and deferred inflows of resources increased by \$664,560.
- Total net position increased by \$2,128.
- Total operating and non-operating revenues were \$4,119,236. Total operating expenses were \$4,117,108.

USING THIS ANNUAL 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 Position, a Statement of Revenues, Expenses and Change in Net Position, and a Statement of Cash Flows.

The Statement of Net Position and Statement of Revenues, Expenses, and Change in Net Position reflect how the School did financially during fiscal year 2016. These statements include all assets and deferred outflows and liabilities and deferred inflows using the accrual basis of accounting similar to the accounting used by most private-sector companies. This basis of accounting includes all of the current year revenues and expenses regardless of when cash is received or paid.

These statements report the School's net position and changes in those assets. This change in net position is important because it tells the reader whether the financial position of the School has improved or diminished. The causes of this change may be the result of many factors, some financial, some not. Non-financial factors include the School's student enrollment, per-pupil funding as determined by the State of Ohio, change in technology, required educational programs and other factors.

The School uses enterprise presentation for all of its activities.

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2016
(UNAUDITED)**

Statement of Net Position

The Statement of Net Position answers the question of how the School did financially during 2016. This statement includes all assets, deferred outflows of resources, liabilities, and deferred inflows of resources, both financial and capital, and short-term and long-term using the accrual basis of accounting and economic resource 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.

Table 1 provides a summary of the School's Net Position for fiscal years 2016 and 2015.

**Table 1
Statement of Net Position**

| | <u>2016</u> | <u>2015</u> |
|--|-----------------------|-----------------------|
| Assets | | |
| Current Assets | \$ 261,722 | \$ 256,394 |
| Capital Assets, Net of Accumulated Depreciation | <u>366,857</u> | <u>414,646</u> |
| Total Assets | <u>628,579</u> | <u>671,040</u> |
| Deferred Outflows of Resources | <u>1,599,309</u> | <u>890,160</u> |
| Liabilities | | |
| Current Liabilities | 403,375 | 812,523 |
| Net Pension Liability | <u>3,370,122</u> | <u>2,206,672</u> |
| Total Liabilities | <u>3,773,497</u> | <u>3,019,195</u> |
| Deferred Inflows of Resources | <u>371,895</u> | <u>461,637</u> |
| Net Position | | |
| Net Investment in Capital Assets | 366,857 | 414,646 |
| Unrestricted | <u>(2,284,361)</u> | <u>(2,334,278)</u> |
| Total Net Position | <u>\$ (1,917,504)</u> | <u>\$ (1,919,632)</u> |

During 2015, the School adopted GASB Statement 68, "Accounting and Financial Reporting for Pensions— an Amendment of GASB Statement 27," which significantly revises accounting for pension costs and liabilities. For reasons discussed below, many end users of this financial statement will gain a clearer understanding of the School's actual financial condition by adding deferred inflows related to pension and the net pension liability to the reported net position and subtracting deferred outflows related to pension.

Governmental Accounting Standards Board standards are national and apply to all government financial reports prepared in accordance with generally accepted accounting principles. When accounting for pension costs, GASB 27 focused on a funding approach. This approach limited pension costs to contributions annually required by law, which may or may not be sufficient to fully fund each plan's *net pension liability*. GASB 68 takes an earnings approach to pension accounting; however, the nature of Ohio's statewide pension systems and state law governing those systems requires additional explanation in order to properly understand the information presented in these statements.

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2016
(UNAUDITED)**

Under the new standards required by GASB 68, the net pension liability equals the School's proportionate share of each plan's collective:

1. Present value of estimated future pension benefits attributable to active and inactive employees' past service
2. Minus plan assets available to pay these benefits

GASB notes that pension obligations, whether funded or unfunded, are part of the "employment exchange" – that is, the employee is trading his or her labor in exchange for wages, benefits, and the promise of a future pension. GASB noted that the unfunded portion of this pension promise is a present obligation of the government, part of a bargained-for benefit to the employee, and should accordingly be reported by the government as a liability since they received the benefit of the exchange. However, the School is not responsible for certain key factors affecting the balance of this liability. In Ohio, the employee shares the obligation of funding pension benefits with the employer. Both employer and employee contribution rates are capped by State statute. A change in these caps requires action of both Houses of the General Assembly and approval of the Governor. Benefit provisions are also determined by State statute. The employee enters the employment exchange with the knowledge that the employer's promise is limited not by contract but by law. The employer enters the exchange also knowing that there is a specific, legal limit to its contribution to the pension system. In Ohio, there is no legal means to enforce the unfunded liability of the pension system *as against the public employer*. State law operates to mitigate/lessen the moral obligation of the public employer to the employee, because all parties enter the employment exchange with notice as to the law. The pension system is responsible for the administration of the plan.

Most long-term liabilities have set repayment schedules or, in the case of compensated absences (i.e. sick and vacation leave), are satisfied through paid time-off or termination payments. There is no repayment schedule for the net pension liability. As explained above, changes in pension benefits, contribution rates, and return on investments affect the balance of the net pension liability, but are outside the control of the local government. In the event that contributions, investment returns, and other changes are insufficient to keep up with required pension payments, State statute does not assign/identify the responsible party for the unfunded portion. Due to the unique nature of how the net pension liability is satisfied, this liability is separately identified within the long-term liability section of the statement of net position.

In accordance with GASB 68, the School's statements prepared on an accrual basis of accounting include an annual pension expense for their proportionate share of each plan's *change* in net pension liability not accounted for as deferred inflows/outflows.

As a result of implementing GASB 68, the School is reporting a net pension liability and deferred inflows/outflows of resources related to pension on the accrual basis of accounting.

Over time, net position can serve as a useful indicator of a government's financial position. At June 30, 2016, the School's net position totaled \$(1,917,504).

Current assets represent cash and cash equivalents, intergovernmental receivable, accounts receivable, and other assets. Current liabilities represent advances payable to the management company, intergovernmental payables, accrued expenses and accrued wages and benefits at fiscal year-end.

Current liabilities decreased \$409,148 or 50% from the prior fiscal year due to the decrease in advances payable.

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2016
(UNAUDITED)**

Statement of Revenues, Expenses and Change in Net Position

Table 2 shows the change in net position for fiscal years 2016 and 2015, as well as a listing of revenues and expenses. This change in net position 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.

**Table 2
Change in Net Position**

| | <u>2016</u> | <u>2015</u> |
|--|-----------------------|-----------------------|
| Operating Revenue | | |
| State Aid | \$ 2,477,829 | \$ 2,021,382 |
| Intergovernmental Revenue | 15,447 | 12,732 |
| Other | 132 | - |
| | <u>2,493,408</u> | <u>2,034,114</u> |
| Total Operating Revenues | | |
| Operating Expenses | | |
| Purchased Services | 3,528,621 | 3,006,561 |
| State Retirement | - | 2,479 |
| Pension Expense | 404,452 | 277,046 |
| Sponsor Fees | 72,790 | 59,890 |
| Depreciation | 111,245 | 145,756 |
| | <u>4,117,108</u> | <u>3,491,732</u> |
| Total Operating Expenses | | |
| Operating (Loss) | (1,623,700) | (1,457,618) |
| Non-Operating Revenues | | |
| Federal Grants | 648,630 | 399,170 |
| Other Intergovernmental Revenue | 269,527 | 267,326 |
| Other Grants | 56,150 | 114,540 |
| Fundraising Revenue | 651,521 | 768,746 |
| | <u>1,625,828</u> | <u>1,549,782</u> |
| Total Non-Operating Revenues | | |
| Change in Net Position | <u>2,128</u> | <u>92,164</u> |
| Net Position – Beginning of Year, | <u>(1,919,632)</u> | <u>(2,011,796)</u> |
| Net Position, End of Year | <u>\$ (1,917,504)</u> | <u>\$ (1,919,632)</u> |

State Aid increased by \$456,447 due to an increase in full-time equivalent enrollment of approximately 49 students. Federal grant funds increased as a result of the increase in enrollments.

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2016
(UNAUDITED)**

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 (with the exception section 5705.391 – Five Year Forecasts), 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 must prepare and submit a detail budget for every fiscal year to the Board of Directors and its Sponsor. The five-year forecast is also submitted to the Ohio Department of Education, annually.

CAPITAL ASSETS

At fiscal year end, the School's net capital asset balance was \$366,857. This balance represents current year additions of \$63,456, offset by current year depreciation of \$111,245. For more information on capital assets, see Note 5 of the Basic Financial Statements.

CURRENT FINANCIAL ISSUES

The School is a community school and is funded through the State of Ohio Foundation Program. The School relies on this, as well as, State and Federal funds as its primary source of revenue. In fiscal year 2016, the State raised the base per pupil funding to \$5,900, which is up from the \$5,800 in the previous year.

The full-time equivalent enrollment of the School for the years ended June 30, 2016 and 2015 was approximately 301 and 252, respectively.

Overall, the School will continue to provide learning opportunities and apply resources to best meet the needs of students.

CONTACTING THE SCHOOL'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizen's, taxpayers, investors and creditors with a general overview of the School's finances and to demonstrate accountability for the money it receives. If you have questions about this report or need additional information contact C. David Massa, CPA, of Massa Financial Solutions, LLC, 2121 East 32nd Street, Cleveland, Ohio 44115 or e-mail at dave@massasolutionsllc.com.

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**STEPSTONE ACADEMY
CUYAHOGA COUNTY**
Statement of Net Position
At June 30, 2016

Assets

Current Assets:

| | |
|------------------------------|---------------|
| Cash and Cash Equivalents | \$ 54,533 |
| Intergovernmental Receivable | 142,660 |
| Accounts Receivable | 14,613 |
| Other Assets | <u>49,916</u> |

| | |
|----------------------|----------------|
| Total Current Assets | <u>261,722</u> |
|----------------------|----------------|

Noncurrent Assets:

| | |
|---------------------------------|----------------|
| Depreciable Capital Assets, net | <u>366,857</u> |
|---------------------------------|----------------|

| | |
|-------------------------|----------------|
| Total Noncurrent Assets | <u>366,857</u> |
|-------------------------|----------------|

| | |
|--------------|----------------|
| Total Assets | <u>628,579</u> |
|--------------|----------------|

| | |
|---------------------------------------|------------------|
| Deferred Outflows of Resources | <u>1,599,309</u> |
|---------------------------------------|------------------|

Liabilities

Current Liabilities:

| | |
|----------------------------|----------------|
| Advances Payable | 202,881 |
| Intergovernmental Payable | 44,328 |
| Accrued Expenses | 12,571 |
| Accrued Wages and Benefits | <u>143,595</u> |

| | |
|---------------------------|----------------|
| Total Current Liabilities | <u>403,375</u> |
|---------------------------|----------------|

Long-Term Liabilities:

| | |
|------------------------------------|------------------|
| Net Pension Liability (See Note 9) | <u>3,370,122</u> |
|------------------------------------|------------------|

| | |
|-----------------------------|------------------|
| Total Long-Term Liabilities | <u>3,370,122</u> |
|-----------------------------|------------------|

| | |
|-------------------|------------------|
| Total Liabilities | <u>3,773,497</u> |
|-------------------|------------------|

Deferred Inflows of Resources

| | |
|---------------|----------------|
| Miscellaneous | 242,933 |
| Pension | <u>128,962</u> |

| | |
|-------------------------------------|---------|
| Total Deferred Inflows of Resources | 371,895 |
|-------------------------------------|---------|

Net Position

| | |
|----------------------------------|--------------------|
| Net Investment in Capital Assets | 366,857 |
| Unrestricted | <u>(2,284,361)</u> |

| | |
|--------------------|-----------------------|
| Total Net Position | <u>\$ (1,917,504)</u> |
|--------------------|-----------------------|

See accompanying notes to the basic financial statements

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**Statement of Revenues,
Expenses and Change in Net Position
For the Year Ending June 30, 2016**

| | |
|--|------------------------------|
| <u>Operating Revenues</u> | |
| State Aid | \$ 2,477,829 |
| Intergovernmental Revenue | 15,447 |
| Other Revenue | <u>132</u> |
| Total Operating Revenues | <u>2,493,408</u> |
| <u>Operating Expenses</u> | |
| Purchased Services | 3,528,621 |
| Pension Expense | 404,452 |
| Sponsor Fees | 72,790 |
| Depreciation | <u>111,245</u> |
| Total Operating Expenses | <u>4,117,108</u> |
| Operating (Loss) | (1,623,700) |
| <u>Non-Operating Revenues</u> | |
| Federal Grants | 648,630 |
| Other Intergovernmental Revenue | 269,527 |
| Other Grants | 56,150 |
| Fundraising Revenue | <u>651,521</u> |
| Total Non-Operating Revenues | <u>1,625,828</u> |
| Change in Net Position | 2,128 |
| Net Position, Beginning of Year | <u>(1,919,632)</u> |
| Net Position, End of Year | <u><u>\$ (1,917,504)</u></u> |

See accompanying notes to the basic financial statements

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**Statement of Cash Flows
For the Fiscal Year Ended June 30, 2016**

Cash Flows from Operating Activities

| | |
|---|--------------------|
| Cash Received from State of Ohio | \$ 2,472,696 |
| Cash Received from Intergovernmental | 13,805 |
| Cash Payments to Suppliers for Goods and Services | <u>(3,573,483)</u> |
| Net Cash (Used for) Operating Activities | (1,086,982) |

Cash Flows from Non-capital Financing Activities

| | |
|--|----------------|
| Cash Received from Federal Grants | 669,574 |
| Cash Received from Other Grants | 56,282 |
| Cash Advances from Fundraising | 661,178 |
| Cash Received from Cleveland Municipal School District | <u>265,886</u> |
| Net Cash Provided by Non-capital Financing Activities | 1,652,920 |

Cash Flows from Capital and Related Financing Activities

| | |
|--|--------------------|
| Cash Payments for Capital Acquisitions | (63,456) |
| Cash Advances from Guidestone | 2,667,069 |
| Cash Payments to Guidestone | <u>(3,169,913)</u> |
| Net Cash (Used for) Capital Financing Activities | (566,300) |

Net Decrease in Cash and Cash Equivalents (362)

Cash and Cash Equivalents, Beginning of Year 54,895

Cash and Cash Equivalents, End of Year \$ 54,533

(Continued)

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**Statement of Cash Flows
For the Fiscal Year Ended June 30, 2016
(Continued)**

**RECONCILIATION OF OPERATING LOSS TO NET
CASH (USED FOR) OPERATING ACTIVITIES**

| | |
|---|----------------------------|
| Operating Loss | \$ (1,623,700) |
| Depreciation | 111,245 |
| Changes in Assets, Deferred Outflows, Liabilities and Deferred Inflows: | |
| (Increase) in Intergovernmental Receivable | (6,906) |
| (Increase) in Deferred Outflows | (709,149) |
| (Increase) in Other Assets | (25,337) |
| (Decrease) in Deferred Inflows | (89,742) |
| Increase in Net Pension Liability | 1,163,450 |
| Increase in Intergovernmental Payable | 35,672 |
| Increase in Accrued Expenses | 1,980 |
| Increase in Accrued Wages and Benefits | 55,505 |
| Net Cash (Used for) Operating Activities | <hr/> \$ (1,086,982) <hr/> |

See accompanying notes to the basic financial statements

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

1. DESCRIPTION OF THE ENTITY

Stepstone Academy, (the School) is a nonprofit corporation established pursuant to Ohio Revised Code Chapters 3314 and 1702. The School's mission is to provide an orderly and supportive environment whereby students experience preparations for college, career and life. The School operates on a foundation, which fosters character building for all students, parents and staff members. The School, which is part of the State's education program, is independent of any school district and is nonsectarian in its programs, admission policies, employment practices, and all other operations. The School may acquire facilities as needed and contract for any services necessary for the operation of the School.

The School was approved for operation under a contract with Ohio Council of Community Schools, ("OCCS") (the Sponsor) for a five year period commencing on July 1, 2012. The Sponsor is responsible for evaluating the performance of the School and has the authority to deny renewal of the contract at its expiration or terminate the contract prior to its expiration.

The School operates under the direction of a Board of Directors (the Board). The Board is responsible for carrying out the provisions of the contract which include, but are not limited to, state mandated provisions regarding student populations, curriculum, academic goals, performance standards, admissions standards, and qualifications of teachers. The Board controls the School's instructional and administrative staff.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements of the School have been prepared in conformity with generally accepted accounting principles (GAAP) 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 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 Position, a Statement of Revenue, Expenses and Change in Net Position, and a Statement of Cash Flows. Enterprise fund reporting focuses on the determination of the changes net position, financial position and cash flows.

The Government Accounting Standards Board identifies the presentation of all financial activity to be reported within one enterprise fund for year-ending reporting purposes. Enterprise accounting is used to account for operations that are financed and operated in a manner similar to private business enterprise where the intent is that the cost (expense) of providing goods and 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 is determined by measurement focus. Under this measurement focus, all assets and deferred outflows and all liabilities and deferred inflows are included on the balance sheet. The operating statement presents increases (e.g., revenues) and decreases (e.g., expenses) in net total position.

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Measurement Focus and Basis of Accounting (Continued)

Basis of accounting refers to when revenues and expenses are recognized in the accounts and reported in the financial statements. Basis of accounting is used for reporting purposes. Revenues are recognized when they are earned, and expenses are recognized when they are incurred.

C. Budgetary Process

Unlike other public schools located in the state of Ohio, community schools are not required to follow budgetary provisions set forth in Ohio Revised Code Chapter 5705 (with the exception section 5705.391 – Five Year Forecasts), unless specifically provided for in the School’s sponsorship agreement. The contract between the School and its Sponsor requires a detailed budget for each year of the contract.

D. Cash and Cash Equivalents

Cash received by the School is reflected as “Cash and Cash Equivalents” on the Statement of Net Position. The School did not have any investments during the period ended June 30, 2016.

E. Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from these estimates.

F. Capital Assets and Depreciation

Capital assets are capitalized at cost. Donated capital assets are recorded at their fair market values as of the date received. The costs of additions are capitalized and expenditures for repairs and maintenance are expensed when incurred. When property is sold or retired, the related costs and accumulated depreciation are removed from the financial records and any gain or loss is included in additions to or deductions from net position. Capital assets were \$366,857 as of June 30, 2016, net of accumulated depreciation. Depreciation of capital assets is calculated utilizing the straight-line method over the estimated useful lives of the assets which are as follows:

| <u>Asset Class</u> | <u>Useful Life</u> |
|----------------------------------|--------------------|
| Computers & Technology Assets | 3 years |
| Leasehold Improvements | 5 years |
| Furniture, Fixtures, & Equipment | 5 years |
| Textbooks | 3 years |

The School’s policy for asset capitalization threshold is \$5,000. Assets or certain asset groups not meeting the capitalization threshold are not capitalized and are not included in the assets represented in the accompany statement of net position.

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

G. Intergovernmental Revenues

The School currently participates in the State Foundation Program. Revenues received from this program are recognized as operating revenues in the accounting period in which all eligibility requirements have been met.

Grants and entitlements are recognized as non-operating revenues in the accounting period in which 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.

The School also participates in various federal programs passed through the Ohio Department of Education.

Also, during the fiscal year, the School received prorated shares of property tax distributions from the Cleveland Municipal School District (CMSD) as part of a partnership agreement executed between the School and CMSD.

Under the above programs the School recorded \$2,477,829 this fiscal year from the State Foundation Program, \$648,630 from Federal Grants, and \$269,527 from CMSD property taxes distributions.

H. Compensated Absences

Vacation is taken in a manner which corresponds with the school calendar; therefore the School does not accrue vacation time as a liability.

Sick/personal leave benefits are earned by full-time employees at the rate of eight days per year and cannot be carried into the subsequent years. No accrual for sick time is made since unused time is not paid to employees upon employment termination.

I. Accrued Liabilities

Obligations incurred but unpaid at June 30 are reported as accrued liabilities in the accompanying financial statements. These liabilities consisted of advances from the management company of \$202,881, accrued expenses of \$12,571, accrued wages and benefits of \$143,595, and an intergovernmental payable of \$44,328 at June 30, 2016.

J. Exchange and Non-Exchange Transactions

Revenue resulting from exchange transactions, in which each party gives and receives essentially equal value, is recorded on the accrual basis when the exchange takes place. Non exchange transactions, in which the School receives value without directly giving equal value in return, include grants, entitlements and donations. Revenue from grants, entitlements and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied. 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,

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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

J. Exchange and Non-Exchange Transactions (Continued)

matching requirements, in which the School must provide local resources to be used for a specified purpose, and expenditures requirements, in which the resources are provided to the School on a reimbursement basis.

K. Deferred Inflows and Deferred Outflows of Resources

In addition to assets, the statements of financial position will sometimes report a separate section for deferred outflows of resources. Deferred outflows of resources represent a consumption of net position that applies to a future period and will not be recognized as an outflow of resources (expense/expenditure) until then. For the School, deferred outflows of resources are reported on the statement of net position for pension. The deferred outflows of resources related to pension are explained in Note 9.

In addition to liabilities, the statements of financial position report a separate section for deferred inflows of resources. Deferred inflows of resources represent an acquisition of net position that applies to a future period and will not be recognized until that time. These amounts are deferred and recognized as an inflow of resources in the period the amounts become available. Deferred inflows of resources related to pension are reported on the statement of net position. (See Note 9)

L. Net Position

Net position represents the difference between assets, deferred outflows of resources, liabilities, and deferred inflows of resources. Net position is reported as restricted when there are limitations imposed on their use through external restriction imposed by creditors, grantors, or laws and regulations of other governments. The School applies restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net position is available. Net position invested in capital assets consist of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowings used for the acquisition, construction, or improvement of those assets.

M. Operating Revenues and Expenses

Operating revenues are those revenues that are generated directly from the primary activities of the School. For the School, these revenues are primarily the State Foundation program. Operating expenses are necessary costs incurred to provide the good or service that is the primary activity of the School. All revenues and expenses not meeting this definition are reported as non-operating. There were no non-operating expenses reported at June 30, 2016.

N. Pensions

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions and pension expense, information about the fiduciary net position of the pension plans and additions to/deletions from their fiduciary net position have been determined on the same basis as they are reported by the pension systems. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. The pension systems report investments at fair value.

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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

O. Implementation of New Accounting Principles

For the fiscal year ended June 30, 2016, the School has implemented Governmental Accounting Standards Board (GASB) Statement No. 72, *Fair Value Measurement and Application*, GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68*, and *Amendments to Certain Provisions of GASB Statements 67 and 68*, GASB Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments* and GASB Statement No. 79, *Certain External Investment Pools and Pool Participants*.

GASB Statement No. 72 clarifies the definition of fair value for financial reporting purposes, establishes general principles for measuring fair value, provides additional fair value application guidance, and enhances disclosures about fair value measurements. The implementation of GASB Statement No. 72 did not have an effect on the financial statements of the School.

GASB Statement No. 73 establishes requirements for defined benefit pensions that are not within the scope of GASB Statement No. 68 as well as for the assets accumulated for purposes of providing those pensions. In addition, it establishes requirements for defined contribution pensions that are not within the Scope of Statement 68. It also clarifies the application of certain provisions of GASB Statements 67 and 68. The implementation of GASB Statement No. 73 did not have an effect on the financial statements of the School.

GASB Statement no. 76 reduces the GAAP hierarchy to two categories of authoritative GAAP and address the use of authoritative and nonauthoritative literature in the event that the accounting treatment for a transaction or other event is not specified within a source of authoritative GAAP. The implementation of GASB Statement No. 76 did not have an effect on the financial statements of the School.

GASB Statement No. 79 addresses accounting and financial reporting for certain external investment pools and pool participants. Specifically, it establishes criteria for and external investment pool to qualify for making the election to measure all of its investments at amortized cost for financial reporting purposes. The implementation of GASB Statement No. 79 did not have an effect on the financial statements of the School.

3. CASH AND CASH EQUIVALENTS

The following information classifies deposits by category of risk as defined in GASB Statement No.3 "Deposits with Financial Institutions, Investments (including Repurchase Agreements) and Reverse Repurchase Agreements," as amended by GASB Statement No.40, "Deposit, and Investment Risk Disclosures".

The School maintains its cash balances at one financial institution, PNC Bank, located in Ohio. The balances are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000, per qualifying account. At June 30, 2016, the book amount of the School's deposits was \$54,533 and the bank balance was \$60,452.

The School had no deposit policy for custodial risk beyond the requirement of state statute. Ohio law requires that deposits either be insured or be protected by eligible securities pledged to and deposited either with the School or a qualified trustee by the financial institution as security for repayment or by a collateral pool of eligible securities deposited with a qualified trustee to secure repayment of all public monies deposited in the financial institution whose market value shall be at least 105% of deposits being

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

3. CASH AND CASH EQUIVALENTS (Continued)

secured. At June 30, 2016, none of the bank balance was exposed to custodial credit risk.

4. RECEIVABLES

A. Accounts Receivable

The School has accounts receivables of \$14,613 at June 30, 2016. These receivables represented monies earned, but not received as of June 30, 2016.

B. Intergovernmental Receivable

The School has intergovernmental receivables totaling \$142,660 at June 30, 2016. These receivables represented monies due to the School from government sources, but not received as of June 30, 2016.

5. CAPITAL ASSETS

For the period ending June 30, 2016, the School's capital assets consisted of the following:

| | Balance 06/30/15 | Additions | Deletions | Balance 06/30/16 |
|---------------------------------------|-----------------------------|---------------------|------------------|-----------------------------|
| Capital Assets: | | | | |
| Leasehold Improvements | \$ 18,620 | \$ - | \$ - | \$ 18,620 |
| Computers & Technology Assets | 262,877 | - | - | 262,877 |
| Furniture, Fixtures, & Equipment | 349,500 | 9,515 | - | 359,015 |
| Textbooks | 12,099 | - | - | 12,099 |
| Construction-in-Progress | 113,914 | 53,941 | - | 167,855 |
| Total Capital Assets | 757,010 | 63,456 | - | 820,466 |
| Less Accumulated Depreciation: | | | | |
| Leasehold Improvements | | | | |
| Computers & Technology Assets | (4,133) | (2,382) | - | (6,515) |
| Furniture, Fixtures, & Equipment | (181,214) | (36,721) | - | (217,935) |
| Textbooks | (145,258) | (71,802) | - | (217,060) |
| Total Accumulated Depreciation | (11,759) | (340) | - | (12,099) |
| | \$ (342,364) | \$ (111,245) | \$ - | \$ (453,609) |
| Capital Assets, Net | \$ 414,646 | \$ (47,789) | \$ - | \$ 366,857 |

6. ADVANCES PAYABLE

The School received advances from the management company. The total amount of advances outstanding at June 30, 2016 was \$202,881.

**STEPSTONE ACADEMY
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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

7. LONG-TERM OBLIGATIONS

The changes in the School's long-term obligations during fiscal year 2016 were as follows:

| | Principal Outstanding 06/30/15 | Additions | Deductions | Principal Outstanding 06/30/16 |
|---------------------------------|---|------------------------|-------------------|---|
| Net Pension Liability: | | | | |
| STRS | \$1,916,579 | \$1,132,655 | \$ | \$3,049,234 |
| SERS | 290,093 | 30,795 | - | 320,888 |
| Total Net Pension Liability | <u>2,206,672</u> | <u>1,163,450</u> | <u>-</u> | <u>3,370,122</u> |
| Total Long-Term Obligations | <u>\$2,206,672</u> | <u>\$1,163,450</u> | <u>\$ -</u> | <u>\$3,370,122</u> |

8. RISK MANAGEMENT

Property & Liability

The School is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. During the fiscal year ending June 30, 2016, the School contracted with The Cincinnati Insurance Company for nonprofits and maintained general liability insurance with a \$1,000,000 single occurrence limit and \$2,000,000 annual aggregate and a combined policy aggregate coverage for various liability coverage in the amount of \$10,000,000.

9. DEFINED BENEFIT PENSIONS PLANS

A. Net Pension Liability

The net pension liability reported on the statement of net position represents a liability to employees for pensions. Pensions are a component of exchange transactions—between an employer and its employees—of salaries and benefits for employee services. Pensions are provided to an employee—on a deferred-payment basis—as part of the total compensation package offered by an employer for employee services each financial period. The obligation to sacrifice resources for pensions is a present obligation because it was created as a result of employment exchanges that already have occurred.

The net pension liability represents the School's proportionate share of each pension plan's collective actuarial present value of projected benefit payments attributable to past periods of service, net of each pension plan's fiduciary net position. The net pension liability calculation is dependent on critical long-term variables, including estimated average life expectancies, earnings on investments, cost of living adjustments and others. While these estimates use the best information available, unknowable future events require adjusting this estimate annually.

Ohio Revised Code limits the School's obligation for this liability to annually required payments. The School cannot control benefit terms or the manner in which pensions are financed; however, the School does receive the benefit of employees' services in exchange for compensation including pension.

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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

9. DEFINED BENEFIT PENSIONS PLANS (Continued)

A. Net Pension Liability (Continued)

GASB 68 assumes the liability is solely the obligation of the employer, because (1) they benefit from employee services; and (2) State statute requires all funding to come from these employers. All contributions to date have come solely from these employers (which also includes costs paid in the form of withholdings from employees). State statute requires the pension plans to amortize unfunded liabilities within 30 years. If the amortization period exceeds 30 years, each pension plan's board must propose corrective action to the State legislature. Any resulting legislative change to benefits or funding could significantly affect the net pension liability. Resulting adjustments to the net pension liability would be effective when the changes are legally enforceable.

The proportionate share of each plan's unfunded benefits is presented as a long-term *net pension liability* on the accrual basis of accounting. Any liability for the contractually-required pension contribution outstanding at the end of the year is included in *intergovernmental payable* on both the accrual and modified accrual bases of accounting.

B. Plan Description - School Employees Retirement System (SERS)

Plan Description – The School's non-teaching employees participate in SERS, a cost-sharing multiple-employer defined benefit pension plan administered by SERS. SERS provides retirement, disability and survivor benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Authority to establish and amend benefits is provided by Ohio Revised Code Chapter 3309. SERS issues a publicly available, stand-alone financial report that includes financial statements, required supplementary information and detailed information about SERS' fiduciary net position. That report can be obtained by visiting the SERS website at www.ohsers.org under Employers/Audit Resources.

Age and service requirements for retirement are as follows:

| | Eligible to Retire on or before August 1, 2017* | Eligible to Retire on or after August 1, 2017 |
|------------------------------|---|--|
| Full Benefits | Any age with 30 years of service credit | Age 67 with 10 years of service credit; or Age 57 with 30 years of service credit |
| Actuarially Reduced Benefits | Age 60 with 5 years of service credit Age 55 with 25 years of service credit | Age 62 with 10 years of service credit; or Age 60 with 25 years of service credit |

* Members with 25 years of service credit as of August 1, 2017, will be included in this plan.

Annual retirement benefits are calculated based on final average salary multiplied by a percentage that varies based on year of service; 2.2 percent for the first thirty years of service and 2.5 percent for years of service credit over 30. Final average salary is the average of the highest three years of salary. One year after an effective benefit date, a benefit recipient is entitled to a three percent cost-of-living adjustment (COLA). This same COLA is added each year to the base benefit amount on the anniversary date of the benefit.

**STEPSTONE ACADEMY
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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

9. DEFINED BENEFIT PENSIONS PLANS (Continued)

B. Plan Description – School Employees Retirement System (SERS) (Continued)

Funding Policy – Plan members are required to contribute 10 percent of their annual covered salary and the School is required to contribute 14 percent of annual covered payroll. The contribution requirements of plan members and employers are established and may be amended by the SERS' Retirement Board up to statutory maximum amounts of 10 percent for plan members and 14 percent for employers. The Retirement Board, acting with the advice of the actuary, allocates the employer contribution rate among four of the System's funds (Pension Trust Fund, Death Benefit Fund, Medicare B Fund, and Health Care Fund). For the fiscal year ended June 30, 2016, the allocation to pension, death benefits, and Medicare B was 14 percent. SERS did not allocate any employer contributions to the Health Care Fund for fiscal year 2016.

The School's contractually required contribution to SERS was \$51,747 for fiscal year 2016.

C. Plan Description - State Teachers Retirement System (STRS)

Plan Description – School licensed teachers and other faculty members participate in STRS Ohio, a cost-sharing multiple-employer public employee retirement system administered by STRS. STRS provides retirement and disability benefits to members and death and survivor benefits to beneficiaries. STRS issues a stand-alone financial report that includes financial statements, required supplementary information and detailed information about STRS' fiduciary net position. That report can be obtained by writing to STRS, 275 E. Broad St., Columbus, OH 43215-3771, by calling (888) 227-7877, or by visiting the STRS Web site 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. Benefits are established by Ohio Revised Code Chapter 3307. The DB plan offers an annual retirement allowance based on final average salary multiplied by a percentage that varies based on years of service. Effective August 1, 2015, the calculation will be 2.2 percent of final average salary for the five highest years of earnings multiplied by all years of service. With certain exceptions, the basic benefit is increased each year by two percent of the original base benefit. For members retiring August 1, 2013, or later, the first two percent is paid on the fifth anniversary of the retirement benefit. Members are eligible to retire at age 60 with five years of qualifying service credit, or age 55 with 25 years of service, or 30 years of service regardless of age. Age and service requirements for retirement will increase effective August 1, 2015, and will continue to increase periodically until they reach age 60 with 35 years of service or age 65 with five years of service on August 1, 2026.

The DC Plan allows members to place all their member contributions and 9.5 percent of the 14 percent employer contributions into an investment account. Investment allocation decisions are determined by the member. The remaining 4.5 percent of the 14 percent employer rate is allocated to the defined benefit unfunded liability. A member is eligible to receive a retirement benefit at age 50 and termination of employment. The member may elect to receive a lifetime monthly annuity or a lump sum withdrawal.

The Combined Plan offers features of both the DB Plan and the DC Plan. In the Combined Plan, member contributions are allocated among investment choices by the member, and employer contributions are used to fund the defined benefit payment at a reduced level from the regular DB Plan. The defined benefit portion of the Combined Plan payment is payable to a member on or after age 60 with five years of services. The defined contribution portion of the account may be taken as a lump sum payment or converted to a lifetime monthly annuity at age 50.

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

9. DEFINED BENEFIT PENSIONS PLANS (Continued)

C. Plan Description - State Teachers Retirement System (STRS) (Continued)

New members who choose the DC plan or Combined Plan will have another opportunity to reselect a permanent plan during their fifth year of membership. Members may remain in the same plan or transfer to another STRS plan. The optional annuitization of a member's defined contribution account or the defined contribution portion of a member's Combined Plan account to a lifetime benefit results in STRS bearing the risk of investment gain or loss on the account. STRS has therefore included all three plan options as one defined benefit plan for GASB 68 reporting purposes.

A DB or Combined Plan member with five or more years of credited service who is determined to be disabled may qualify for a disability benefit. Eligible survivors of members who die before service retirement may qualify for monthly benefits. New members on or after July 1, 2013, must have at least ten years of qualifying service credit that apply for disability benefits. Members in the DC Plan who become disabled are entitled only to their account balance. If a member of the DC Plan dies before retirement benefits begin, the member's designated beneficiary is entitled to receive the member's account balance.

Funding Policy – Employer and member contribution rates are established by the State Teachers Retirement Board and limited by Chapter 3307 of the Ohio Revised Code. The statutory maximum employee contribution rate was increased one percent July 1, 2014, and will be increased one percent each year until it reaches 14 percent on July 1, 2016. For the fiscal year ended June 30, 2016, plan members were required to contribute 13 percent of their annual covered salary. The School was required to contribute 14 percent; the entire 14 percent was the portion used to fund pension obligations. The fiscal year 2016 contribution rates were equal to the statutory maximum rates.

The School's contractually required contribution to STRS was \$178,220 for fiscal year 2016. There were no contributions to the DC and Combined Plans for fiscal year 2016.

D. Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

The net pension liability was measured as of June 30, 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The School's proportion of the net pension liability was based on the School's share of contributions to the pension plan relative to the contributions of all participating entities. Following is information related to the proportionate share and pension expense:

| | STRS | SERS | Total |
|--|-------------|-------------|-------------|
| Proportionate Share of the Net Pension Liability | \$3,049,234 | \$320,888 | \$3,370,122 |
| Proportion of the Net Pension Liability | 0.01103313% | 0.00562360% | |
| Pension Expense | \$341,571 | \$65,079 | \$406,650 |

**STEPSTONE ACADEMY
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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

9. DEFINED BENEFIT PENSIONS PLANS (Continued)

D. Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions (Continued)

At June 30, 2016, the School reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

| | STRS | SERS | Total |
|---|-------------|-----------|-------------|
| Deferred Outflows of Resources | | | |
| Differences between expected and actual experience | \$133,468 | \$5,203 | \$138,671 |
| Changes in proportion and differences School contributions subsequent to the measurement date | 1,098,523 | 137,071 | 1,235,594 |
| | 173,297 | 51,747 | 225,044 |
| Total Deferred Outflows of Resources | \$1,405,288 | \$194,021 | \$1,599,309 |
| Deferred Inflows of Resources | | | |
| Net difference between projected and actual earnings on pension plan investments | \$112,865 | \$11,299 | \$124,164 |
| Changes in proportion and differences | - | 4,797 | 4,797 |
| Total Deferred Inflows of Resources | \$112,865 | \$16,096 | \$128,961 |

\$225,044 reported as deferred outflows of resources related to pension resulting from School contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ending June 30, 2017. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pension will be recognized in pension expense as follows:

| | STRS | SERS | Total |
|-----------------------------|--------------|------------|--------------|
| Fiscal Year Ending June 30: | | | |
| 2017 | \$ 290,211 | \$ 40,085 | \$ 330,296 |
| 2018 | 290,211 | 40,085 | 330,296 |
| 2019 | 290,212 | 40,064 | 330,276 |
| 2020 | 248,492 | 5,943 | 254,435 |
| | \$ 1,119,126 | \$ 126,178 | \$ 1,245,304 |

E. Actuarial Assumptions - SERS

SERS' total pension liability was determined by their actuaries in accordance with GASB Statement No. 67, as part of their annual actuarial valuation for each defined benefit retirement plan. Actuarial Valuations of an ongoing plan involve estimates of the value of reported amounts (e.g., salaries, credited service) and assumptions about the probability of occurrence of events far into the future (e.g., mortality, disabilities, retirements, employment termination). Actuarially determined amounts are subject to continual review and potential modifications, as actual results are compared with past expectations and new estimates are made about the future.

**STEPSTONE ACADEMY
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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

9. DEFINED BENEFIT PENSIONS PLANS (Continued)

E. Actuarial Assumptions – SERS (Continued)

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employers and plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing benefit costs between the employers and plan members to that point. The projection of benefits for financial reporting purposes does not explicitly incorporate the potential effects of legal or contractual funding limitations.

Actuarial calculations reflect a long-term perspective. For a newly hired employee, actuarial calculations will take into account the employee's entire career with the employer and also take into consideration the benefits, if any, paid to the employee after termination of employment until the death of the employee and any applicable contingent annuitant. In many cases actuarial calculations reflect several decades of service with the employer and the payment of benefits after termination.

Key methods and assumptions used in calculating the total pension liability in the latest actuarial valuation, prepared as of June 30, 2015, are presented below:

| | |
|--|--|
| Wage Inflation | 3.25 percent |
| Future Salary Increases, including inflation | 4.00 percent to 22 percent |
| COLA or Ad Hoc COLA | 3.00 percent |
| Investment Rate of Return | 7.75 percent net of investments expense, including inflation |
| Actuarial Cost Method | Entry Age Normal |

For post-retirement mortality, the table used in evaluating allowances to be paid is the 1994 Group Annuity Mortality Table set back one year for both men and women. Special mortality tables are used for the period after disability retirement.

The most recent experience study was completed June 30, 2010.

The long-term return expectation for the Pension Plan Investments has been determined using a building-block approach and assumes a time horizon, as defined in SERS' *Statement of Investment Policy*. A forecasted rate of inflation serves as the baseline for the return expectation. Various real return premiums over the baseline inflation rate have been established for each asset class. The long-term expected nominal rate of return has been determined by calculating a weighted averaged of the expected real return premiums for each asset class, adding the projected inflation rate, and adding the expected return from rebalancing uncorrelated asset classes. The target allocation and best estimates of arithmetic real rates of return for each major assets class are summarized in the following table:

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**NOTES TO THE BASIC FINANCIAL STATEMENTS
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9. DEFINED BENEFIT PENSIONS PLANS (Continued)

E. Actuarial Assumptions – SERS (Continued)

| Asset Class | Target Allocation | Long Term Expected Real Rate of Return |
|------------------------|----------------------|---|
| Cash | 1.00 % | 0.00 % |
| US Stocks | 22.50 | 5.00 |
| Non-US Stocks | 22.50 | 5.50 |
| Fixed Income | 19.00 | 1.50 |
| Private Equity | 10.00 | 10.00 |
| Real Assets | 10.00 | 5.00 |
| Multi-Asset Strategies | 15.00 | 7.50 |
| | <u>100.00 %</u> | |

Changes Between Measurement Date and Report Date In April 2016, the SERS Board adopted certain assumption changes which impacted their annual actuarial valuation prepared as of June 30, 2016. The most significant change is a reduction in the discount rate from 7.75 percent to 7.5 percent. Although the exact amount of these changes is not known, the impact to the School's net pension liability is expected to be significant.

Discount Rate The total pension liability was calculated using the discount rate of 7.75 percent. The projection of cash flows used to determine the discount rate assumed the contributions from employers and from the members would be computed based on contribution requirements as stipulated by State statute. Projected inflows from investment earning were calculated using the long-term assumed investment rate of return (7.75 percent). Based on those assumptions, the plan's fiduciary net position was projected to be available to make all future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefits to determine the total pension liability.

Sensitivity of the School's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate Net pension liability is sensitive to changes in the discount rate, and to illustrate the potential impact the following table presents the net pension liability calculated using the discount rate of 7.75 percent, as well as what each plan's net pension liability would be if it were calculated using a discount rate that is one percentage point lower (6.75 percent), or one percentage point higher (8.75 percent) than the current rate.

| | 1% Decrease (6.75%) | Current Discount Rate (7.75%) | 1% Increase (8.75%) |
|--|------------------------|-------------------------------------|------------------------|
| School's proportionate share of the net pension liability | \$444,956 | \$320,888 | \$216,412 |

**STEPSTONE ACADEMY
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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

9. DEFINED BENEFIT PENSIONS PLANS (Continued)

F. Actuarial Assumptions - STRS

The total pension liability in the June 30, 2015, actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

| | |
|-----------------------------------|--|
| Inflation | 2.75 percent |
| Projected salary increase | 2.75 percent at 70 to 12.25 percent at age 20 |
| Investment Rate of Return | 7.75 percent, net of investment expenses |
| Cost-of-Living Adjustments (COLA) | 2.00 percent simple applied as follows: for members retiring before August 1, 2013, 2 percent per year, for members retiring August 1, 2013, or later, 2 percent COLA paid on fifth anniversary of retirement date |

Mortality rates were based on the RP-2000 Combined Mortality Table (Projection 2022—Scale AA) for Males and Females. Males' ages are set-back two years through age 89 and no set-back for age 90 and above. Females younger than age 80 are set back four years, one year set back from age 80 through 89 and not set back from age 90 and above.

Actuarial assumptions used in the June 30, 2014, valuation are based on the results of an actuarial experience study, effective July 1, 2012.

The 10 year expected real rate of return on pension plan investments was determined by STRS' investment consultant by developing best estimates of expected future real rates of return for each major asset class. The target allocation and best estimates of geometric real rates of return for each major asset class are summarized as follows:

| <u>Asset Class</u> | <u>Target Allocation</u> | <u>Long-Term Expected Real Rate of Return</u> |
|----------------------|--------------------------|---|
| Domestic Equity | 31.00 % | 8.00 % |
| International Equity | 26.00 | 7.85 |
| Alternatives | 14.00 | 8.00 |
| Fixed Income | 18.00 | 3.75 |
| Real Estate | 10.00 | 6.75 |
| Liquidity Reserves | <u>1.00</u> | 3.00 |
| Total | <u>100.00 %</u> | |

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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

9. DEFINED BENEFIT PENSIONS PLANS (Continued)

F. Actuarial Assumptions – STRS (Continued)

Discount Rate The discount rate used to measure the total pension liability was 7.75 percent as of June 30, 2015. The projection of cash flows used to determine the discount rate assumes member and employer contributions will be made at the statutory contribution rates in accordance with rate increases described above. For this purpose, only employer contributions that are intended to fund benefits of current plan members and their beneficiaries are included. Projected employer contributions that are intended to fund the service costs of future plan members and their beneficiaries, as well as projected contributions from future plan members, are not included. Based on those assumptions, STRS' fiduciary net position was projected to be available to make all projected future benefit payments to current plan members as of June 30, 2015. Therefore, the long-term expected rate of return on pension plan investments of 7.75 percent was applied to all periods of projected benefit payment to determine the total pension liability as of June 30, 2015.

Sensitivity of the School's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate The following table presents the School's proportionate share of the net pension liability calculated using the current period discount rate assumption of 7.75 percent, as well as what the School's proportionate share of the net pension liability would be if it were calculated using a discount rate that is one-percentage-point lower (6.75 percent) or one-percentage-point higher (8.75 percent) than the current rate:

| | 1% Decrease (6.75%) | Current Discount Rate (7.75%) | 1% Increase (8.75%) |
|--|------------------------|-------------------------------------|------------------------|
| School's proportionate share of the net pension liability | \$4,235,617 | \$3,049,234 | \$2,045,971 |

10. POSTEMPLOYMENT BENEFITS

A. School Employees Retirement System

Health Care Plan Description - The School contributes to the SERS Health Care Fund, administered by SERS for non-certificated retirees and their beneficiaries. For GASB 45 purposes, this plan is considered a cost-sharing, multiple-employer, defined benefit other postemployment benefit (OPEB) plan. The Health Care Plan includes hospitalization and physicians' fees through several types of plans including HMO's, PPO's, Medicare Advantage, and traditional indemnity plans as well as a prescription drug program. The financial report of the Plan is included in the SERS Comprehensive Annual Financial Report which can be obtained on SERS' website at www.ohsers.org under Employers/Audit Resources.

Access to health care for retirees and beneficiaries is permitted in accordance with Section 3309 of the Ohio Revised Code. The Health Care Fund was established and is administered in accordance with Internal Revenue Code Section 105(e). SERS' Retirement Board reserves the right to change or discontinue any health plan or program. Health care is financed through a combination of employer contributions and retiree premiums, copays and deductibles on covered health care expenses, investment returns, and any funds received as a result of SERS' participation in Medicare programs. Active employee members do not contribute to the Health Care Plan. Retirees and their beneficiaries are required to pay a health care premium that varies depending

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

10. POSTEMPLOYMENT BENEFITS (Continued)

A. School Employees Retirement System (Continued)

on the plan selected, the number of qualified years of service, Medicare eligibility and retirement status. Funding Policy - State statute permits SERS to fund the health care benefits through employer contributions. Each year, after the allocation for statutorily required basic benefits, the Retirement Board allocates the remainder of the employer contribution of 14 percent of covered payroll to the Health Care Fund. For fiscal year 2016, SERS did not allocate any employer contributions to the Health Care Fund. In addition, employers pay a surcharge for employees earning less than an actuarially determined minimum compensation amount, pro-rated according to service credit earned. For fiscal year 2016, this amount was \$23,000. Statutes provide that no employer shall pay a health care surcharge greater than 2 percent of that employer's SERS-covered payroll; nor may SERS collect in aggregate more than 1.5 percent of the total statewide SERS-covered payroll for the health care surcharge.

The School's contributions for health care (including surcharge) for the fiscal years ended June 30, 2016, 2015, and 2014 were \$3,026, \$1,388, \$1,266, respectively. The full amount has been contributed for fiscal years 2016, 2015 and 2014.

B. School Teachers Retirement Systems

Plan Description – The School participates in the cost-sharing multiple-employer defined benefit Health Plan administered by the State Teachers Retirement System of Ohio (STRS) for eligible retirees who participated in the defined benefit or combined pension plans offered by STRS. Ohio law authorizes STRS to offer this plan. Benefits include hospitalization, physicians' fees, prescription drugs and reimbursement of monthly Medicare Part B premiums. The Plan is included in the report of STRS which can be obtained by visiting www.strsoh.org or by calling (888) 227-7877.

Funding Policy – Ohio Revised Code Chapter 3307 authorizes STRS Ohio to offer the Plan and gives the Retirement Board authority over how much, if any, of the health care costs will be absorbed by STRS. Active employee members do not contribute to the Health Care Plan. All benefit recipients, for the most recent year, pay a monthly premium. Under Ohio law, funding for post-employment health care may be deducted from employer contributions. For fiscal year 2016, STRS did not allocate any employer contributions to post-employment health care. The School's contributions for health care for the fiscal years ended June 30, 2016, 2015 and 2014 were \$0, \$0 and \$8,856 respectively. The full amount has been contributed for fiscal years 2016, 2015 and 2014.

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

11. CONTINGENCIES

A. Grants

The School received financial assistance from federal and state agencies in the form of 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. Litigation

There are currently no matters in litigation with the School as defendant.

C. Full-Time Equivalency

The School foundation funding is based on annualized full-time equivalent (FTE) enrollment of each student. Effective for the 2014-2015 school year, the community schools must comply with the minimum hours of instruction, instead of a minimum number of school days each year. The funding formula the Ohio Department of Education (ODE) is legislatively required to follow will continue to adjust enrollment information is updated by the school, which can extend past the fiscal year end. As a of the date of this report, ODE has not finalized the impact of enrollment adjustments to the June 30, 2016 foundation funding for the School; therefore, the financial statement impact is not determinable at this time. ODE and management believe this will result in either a receivable to or a liability of the School.

12. SPONSOR AND MANAGEMENT CONTRACTS

Sponsor

The School contracted with Ohio Council of Community Schools as its sponsor and oversight services as required by law. Sponsorship fees are calculated as a three percent of state funds received by the School from the State of Ohio. For the fiscal year ended June 30, 2016, the total sponsorship fees paid totaled \$72,790.

Management Company

The School entered into an agreement with Guidestone, a local nonprofit management company, to provide legal, financial, and other management support services for fiscal year 2016. The agreement was for a period of five years beginning July 1, 2012. Management fees are calculated as 10% of the total revenues received from the State of Ohio in 2016. The total amount paid by the School for the fiscal year ending June 30, 2016 was \$243,708 and is included under "Purchased Services" on the Statement of Revenues, Expenses and Change in Net Position. The management company also entered into a five year lease for the facility which ends May 31, 2017, and subleases the facility to the School.

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2016**

13. PURCHASED SERVICES

For the period of July 1, 2015 through June 30, 2016, the School made the following purchased services commitments.

| | |
|-------------------------------------|----------------------------|
| Salaries and Wages and Benefits | \$ 2,027,336 |
| Property Services | 481,979 |
| Professional and Technical Services | 457,641 |
| Curriculum and materials | 187,252 |
| Other Direct Costs | 374,413 |
| Total Purchased Services | <u><u>\$ 3,528,621</u></u> |

14. FISCAL DISTRESS

Several factors have caused the School to experience fiscal distress. The School's cash balance at June 30, 2016 was \$54,533. Additionally, the School has significant liabilities at June 30, 2016 which has resulted in a deficit net position of (\$1,917,504). Overcoming this deficit may be difficult without significant increases to revenues in order to pay off outstanding liabilities and cover ongoing operating costs.

15. MANAGEMENT PLAN

The amount owed to Guidestone at June 30, 2016 is for unpaid operating expenses and outstanding advances. Guidestone remains committed to the success of the School both academically and financially. During the current year, stronger student recruitment and enrollments and the use of Federal funds improved the financial performance of the School.

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

REQUIRED SUPPLEMENTARY INFORMATION

**SCHEDULE OF THE SCHOOL'S PROPORTIONATE SHARE OF NET PENSION LIABILITY
SCHOOL EMPLOYEES RETIREMENT SYSTEM OF OHIO
LAST THREE FISCAL YEARS (1)**

| | <u>2015</u> | <u>2014</u> | <u>2013</u> |
|--|-------------|-------------|-------------|
| School's Proportion of the Net Pension Liability | 0.00562360% | 0.00573200% | 0.00573200% |
| School's Proportionate Share of the Net Pension Liability | \$ 320,888 | \$ 290,093 | \$ 340,864 |
| School's Covered-Employee Payroll | \$ 169,302 | \$ 166,568 | \$ 54,964 |
| School's Proportionate Share of the Net Pension Liability as a Percentage of its Covered-Employee Payroll | 189.54% | 174.16% | 620.16% |
| Plan Fiduciary Net Position as a Percentage of the Total Pension Liability | 69.16% | 71.70% | 65.52% |

(1) Information prior to 2013 is not available.

Note: The amounts presented for each fiscal year were determined as of the measurement date.

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

REQUIRED SUPPLEMENTARY INFORMATION

**SCHEDULE OF THE SCHOOL'S PROPORTIONATE SHARE OF NET PENSION LIABILITY
STATE TEACHERS RETIREMENT SYSTEM OF OHIO
LAST THREE FISCAL YEARS (1)**

| | <u>2015</u> | <u>2014</u> | <u>2013</u> |
|--|--------------|--------------|--------------|
| School's Proportion of the Net Pension Liability | 0.01103313% | 0.00787955% | 0.00787955% |
| School's Proportionate Share of the Net Pension Liability | \$ 3,049,234 | \$ 1,916,579 | \$ 2,283,017 |
| School's Covered-Employee Payroll | \$ 1,151,121 | \$ 867,000 | \$ 627,577 |
| School's Proportionate Share of the Net Pension Liability as a Percentage of its Covered-Employee Payroll | 264.89% | 221.06% | 363.78% |
| Plan Fiduciary Net Position as a Percentage of the Total Pension Liability | 72.10% | 74.70% | 69.30% |

(1) Information prior to 2013 is not available.

Note: The amounts presented for each fiscal year were determined as of the measurement date.

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

REQUIRED SUPPLEMENTARY INFORMATION

**SCHEDULE OF THE SCHOOL'S CONTRIBUTIONS
SCHOOL EMPLOYEES RETIREMENT SYSTEM OF OHIO
LAST FOUR FISCAL YEARS (1)**

| | <u>2016</u> | <u>2015</u> | <u>2014</u> | <u>2013</u> |
|---|-----------------|-----------------|-----------------|----------------|
| Contractually Required Contribution | \$ 51,747 | \$ 22,314 | \$ 23,086 | \$ 7,607 |
| Contributions in Relation to the Contractually Required Contribution | <u>(51,747)</u> | <u>(22,314)</u> | <u>(23,086)</u> | <u>(7,607)</u> |
| Contribution Deficiency (Excess) | <u>\$ 0</u> | <u>\$ 0</u> | <u>\$ 0</u> | <u>\$ 0</u> |
| School's Covered-Employee Payroll | \$ 369,621 | \$ 169,302 | \$ 166,566 | \$ 54,964 |
| Contributions as a Percentage of Covered-Employee Payroll | 14.00% | 13.18% | 13.86% | 13.84% |

(1) - Information prior to 2013 is not available.

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

REQUIRED SUPPLEMENTARY INFORMATION

**SCHEDULE OF THE SCHOOL'S CONTRIBUTIONS
STATE TEACHERS RETIREMENT SYSTEM OF OHIO
LAST FOUR FISCAL YEARS (1)**

| | <u>2016</u> | <u>2015</u> | <u>2014</u> | <u>2013</u> |
|---|------------------|------------------|------------------|-----------------|
| Contractually Required Contribution | \$ 173,297 | \$ 161,157 | \$ 112,710 | \$ 81,585 |
| Contributions in Relation to the Contractually Required Contribution | <u>(173,297)</u> | <u>(161,157)</u> | <u>(112,710)</u> | <u>(81,585)</u> |
| Contribution Deficiency (Excess) | <u>\$ 0</u> | <u>\$ 0</u> | <u>\$ 0</u> | <u>\$ 0</u> |
| School's Covered-Employee Payroll | \$ 1,237,836 | \$ 1,151,121 | \$ 867,000 | \$ 627,576 |
| Contributions as a Percentage of Covered-Employee Payroll | 14.00% | 14.00% | 13.00% | 13.00% |

(1) - Information prior to 2013 is not available.

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION
FOR FISCAL YEAR ENDED JUNE 30, 2016**

SCHOOL EMPLOYEES RETIREMENT SYSTEM (SERS) OF OHIO

Changes in benefit terms: There were no changes in benefit terms from the amounts reported for fiscal year 2015 and 2016.

Changes in assumptions: There were no changes in methods and assumptions used in the calculation of actuarial determined contributions for fiscal year 2015 and 2016. See the notes to the basic financials for the methods and assumptions in this calculation.

STATE TEACHERS RETIREMENT SYSTEM (STRS) OF OHIO

Changes in benefit terms: There were no changes in benefit terms from the amounts reported for fiscal year 2015 and 2016.

Changes in assumptions: There were no changes in methods and assumptions used in the calculation of actuarial determined contributions for fiscal year 2015 and 2016. See the notes to the basic financials for the methods and assumptions in this calculation.

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Dave Yost • Auditor of State

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

Stepstone Academy
Cuyahoga County
2121 East 32nd Street
Cleveland, Ohio 44115

To the Board of Directors:

We have audited, in accordance with auditing standards generally accepted in the United States and the Comptroller General of the United States' *Government Auditing Standards*, the financial statements of Stepstone Academy, Cuyahoga County, (the School) as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the School's basic financial statements and have issued our report thereon dated March 31, 2017.

Internal Control Over Financial Reporting

As part of our financial statement audit, we considered the School's internal control over financial reporting (internal control) to determine the audit procedures appropriate in the circumstances to the extent necessary to support our opinion on the financial statements, but not to the extent necessary to opine on the effectiveness of the School's internal control. Accordingly, we have not opined on it.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, when performing their assigned functions, to prevent, or detect and timely correct misstatements. A *material weakness* is a deficiency, or combination of internal control deficiencies resulting in a reasonable possibility that internal control will not prevent or detect and timely correct a material misstatement of the School's financial statements. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all internal control deficiencies that might be material weaknesses or significant deficiencies. Given these limitations, we did not identify any deficiencies in internal control that we consider material weaknesses. However, unidentified material weaknesses may exist.

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, opining 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 no instances of noncompliance or other matters we must report under *Government Auditing Standards*.

Purpose of this Report

This report only describes the scope of our internal control and compliance testing and our testing results, and does not opine on the effectiveness of the School's internal control or on compliance. This report is an integral part of an audit performed under *Government Auditing Standards* in considering the School's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in black ink that reads "Dave Yost". The signature is written in a cursive style with a large, looping "D" and "Y".

Dave Yost
Auditor of State
Columbus, Ohio

March 31, 2017

**STEPSTONE ACADEMY
CUYAHOGA COUNTY**

**SCHEDULE OF PRIOR AUDIT FINDINGS
2 CFR 200.511(b)
JUNE 30, 2016**

| Finding Number | Finding Summary | Status | Additional Information |
|-----------------------|---|---------------|-------------------------------|
| 2015-001 | Expenditure of Public Fund/Proper "Public Purpose" - Donation | Corrected | None. |

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STEPSTONE ACADEMY

CUYAHOGA 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
APRIL 18, 2017**