

**PENN HILLS CHARTER SCHOOL
OF ENTREPRENEURSHIP**

Financial Statements

June 30, 2013 and 2012

**PENN HILLS CHARTER SCHOOL
OF ENTREPRENEURSHIP**

Financial Statements

June 30, 2013 and 2012

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Independent Auditors' Report

To the Board of Directors
Penn Hills Charter School of Entrepreneurship
Verona, Pennsylvania

We have audited the accompanying financial statements of Penn Hills Charter School of Entrepreneurship (the School), which comprise the balance sheets as of June 30, 2013 and 2012, and the related statements of activities and changes in net assets, functional expenses and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

Auditors' Responsibility (Continued)

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Penn Hills Charter School of Entrepreneurship as of June 30, 2013 and 2012, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

ALDERN ROSENTHAL

Pittsburgh, Pennsylvania

February 20, 2014

**PENN HILLS CHARTER SCHOOL
OF ENTREPRENEURSHIP**

Balance Sheets

June 30	2013	2012
ASSETS		
Current Assets		
Cash	\$ 614,400	\$ 337,164
Tuition and accounts receivable	<u>1,600,488</u>	<u>660,648</u>
Total Current Assets	2,214,888	997,812
Non-current Assets		
Property and equipment - net - Note 3	<u>157,451</u>	<u>156,686</u>
Total Assets	<u>\$ 2,372,339</u>	<u>\$ 1,154,498</u>
LIABILITIES AND NET ASSETS		
Current Liabilities		
Note payable - related party - current portion - Note 6	\$ 11,189	\$ 6,495
Accounts payable and accrued expenses	342,515	75,327
Accrued payroll and related liabilities - Note 4	266,273	300,066
Deferred revenue	-	77,569
Due to related party - Notes 5 and 6	<u>662,000</u>	<u>513,962</u>
Total Current Liabilities	<u>1,281,977</u>	<u>973,419</u>
Non-current Liabilities		
Due to related party - Notes 5 and 6	468,037	-
Note payable - related party - net of current portion - Note 6	<u>237,880</u>	<u>242,574</u>
Total Non-current Liabilities	<u>705,917</u>	<u>242,574</u>
Total Liabilities	1,987,894	1,215,993
Total Net Assets (Deficit)	<u>384,445</u>	<u>(61,495)</u>
Total Liabilities and Net Assets	<u>\$ 2,372,339</u>	<u>\$ 1,154,498</u>

The accompanying notes are an integral part of these financial statements.

**PENN HILLS CHARTER SCHOOL
OF ENTREPRENEURSHIP**

Statements of Activities and Changes in Net Assets

For the Years Ended June 30	2013	2012
Revenue and Support		
Tuition and fees	\$ 3,963,570	\$ 2,500,726
Contributions - Note 5	886	176,214
Government grants - Note 4	189,263	78,755
Other income	1,588	1,150
Total Revenue and Support	4,155,307	2,756,845
Expenses		
Program Services		
Education	2,212,395	1,805,838
Food service	272,021	204,115
Total Program Services	2,484,416	2,009,953
Supporting Services		
Management and general	1,224,951	808,387
Total Expenses	3,709,367	2,818,340
Increase (Decrease) in Net Assets	445,940	(61,495)
Net Deficit - Beginning of year	(61,495)	-
Net Assets (Deficit) - End of year	\$ 384,445	\$ (61,495)

The accompanying notes are an integral part of these financial statements.

**PENN HILLS CHARTER SCHOOL
OF ENTREPRENEURSHIP**

Statement of Functional Expenses

For the Year Ended June 30, 2013

	<u>Program Expenses</u>		Management and General	Total Program Expenses
	<u>Education</u>	<u>Food Services</u>		
Salaries and benefits	\$ 1,367,636	\$ 57,822	\$ 197,790	\$ 1,623,248
Management fee - Note 5	-	-	488,526	488,526
Loss mitigation fee - Note 5	-	-	101,776	101,776
Contracted services	132,227	184,334	4,543	321,104
Rent - Note 7	247,012	17,644	35,287	299,943
Utilities	52,611	3,758	7,516	63,885
Legal fees	-	-	146,845	146,845
Books, periodicals and supplies	166,046	3,422	67,157	236,625
Professional fees	192,846	-	107,972	300,818
Insurance	16,303	1,164	2,329	19,796
Repairs and maintenance	2,653	189	379	3,221
Miscellaneous	3,443	155	34,599	38,197
Interest	-	-	25,773	25,773
Depreciation	31,618	3,533	4,459	39,610
	<u>\$ 2,212,395</u>	<u>\$ 272,021</u>	<u>\$ 1,224,951</u>	<u>\$ 3,709,367</u>

The accompanying notes are an integral part of these financial statements.

**PENN HILLS CHARTER SCHOOL
OF ENTREPRENEURSHIP**

Statement of Functional Expenses

For the Year Ended June 30, 2012

	<u>Program Expenses</u>		Management and General	Total Program Expenses
	<u>Education</u>	<u>Food Services</u>		
Salaries and benefits	\$ 1,087,126	\$ 40,124	\$ 186,454	\$ 1,313,704
Management fee - Note 5	-	-	309,476	309,476
Loss mitigation fee - Note 5	-	-	64,474	64,474
Contracted services	158,646	149,084	5,881	313,611
Rent - Note 7	73,073	2,811	11,242	87,126
Utilities	39,361	1,514	6,055	46,930
Legal fees	-	-	98,687	98,687
Books, periodicals and supplies	262,424	8,332	53,357	324,113
Professional fees	104,859	-	38,804	143,663
Insurance	20,968	806	3,226	25,000
Repairs and maintenance	3,679	141	566	4,386
Miscellaneous	27,853	-	4,311	32,164
Interest	-	-	21,801	21,801
Depreciation	27,849	1,303	4,053	33,205
	<u>\$ 1,805,838</u>	<u>\$ 204,115</u>	<u>\$ 808,387</u>	<u>\$ 2,818,340</u>

The accompanying notes are an integral part of these financial statements.

**PENN HILLS CHARTER SCHOOL
OF ENTREPRENEURSHIP**

Statements of Cash Flows

For the Years Ended June 30	2013	2012
Cash Provided by (Used for) Operating Activities		
Increase (decrease) in net assets	\$ 445,940	\$ (61,495)
Adjustments to reconcile change in net assets to net cash provided by (used for) operating activities		
Depreciation and amortization	39,610	33,205
Provision for bad debts	117,500	26,000
Changes in		
Tuition and accounts receivable	(1,057,340)	(686,648)
Accounts payable and accrued expenses	267,188	344,058
Accrued payroll and related liabilities	(33,793)	300,066
Deferred revenue	(77,569)	77,569
Net Cash Provided by (Used for) Operating Activities	<u>(298,464)</u>	<u>32,755</u>
Cash Used for Investing Activities		
Purchase of property and equipment	<u>(40,375)</u>	<u>(189,891)</u>
Cash Provided by (Used for) Financing Activities		
Due to related party - advances and accrued interest	666,075	445,231
Due to related party - payments	(50,000)	(200,000)
Note payable proceeds	-	250,000
Payments on note payable	<u>-</u>	<u>(931)</u>
Net Cash Provided by Financing Activities	<u>616,075</u>	<u>494,300</u>
Net Increase in Cash and Cash Equivalents	277,236	337,164
Cash and Cash Equivalents - Beginning of year	<u>337,164</u>	<u>-</u>
Cash and Cash Equivalents - End of year	<u>\$ 614,400</u>	<u>\$ 337,164</u>

Supplemental Disclosure of Cash Flow Information

Cash paid during the year for interest	<u>\$ -</u>	<u>\$ 6,570</u>
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The accompanying notes are an integral part of these financial statements.

PENN HILLS CHARTER SCHOOL OF ENTREPRENEURSHIP

Notes to the Financial Statements

Note 1 - Organization

Penn Hills Charter School of Entrepreneurship (the School), a Pennsylvania Charter School, is a public school operated under a charter granted by the Penn Hills Board of School Directors. The charter was approved on April 26, 2011 and is effective until June 30, 2016.

The School's mission is to provide a world-class education for the students in the Penn Hills community - a school that will not only prepare students academically but to develop into informed and responsible world citizens, creative problem solvers, and effective communicators.

Note 2 - Summary of Significant Accounting Policies

A. Basis of Accounting

The financial statements have been prepared on the accrual basis in accordance with accounting principles generally accepted in the United States of America.

B. Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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.

C. Cash

At June 30, 2013 and 2012, the School's cash was on deposit with one large financial institution and exceeded the Federal Deposit Insurance Corporation limit. The School believes it has placed these temporary cash investments with a high credit quality financial institution and does not believe it is exposed to any significant credit risk.

D. Tuition and Accounts Receivable

Tuition and accounts receivable are stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. The allowance for tuition and accounts receivable was approximately \$118,000 at June 30, 2013 and \$26,000 at June 30, 2012.

**PENN HILLS CHARTER SCHOOL
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Notes to the Financial Statements (Continued)

Note 2 - Summary of Significant Accounting Policies (Continued)

E. Revenue Recognition

Revenue is recognized when earned. Tuition revenue represents the tuition paid by various Allegheny County school districts for the students enrolled in the School who reside with that particular school district. Revenues from tuition and fees are reported in the fiscal year in which educational programs are conducted. Tuition revenues received in advance of the year to which they relate are deferred. Deferred revenue primarily consists of advances received to be earned in the subsequent school year.

As of June 30, 2013, approximately 66% of the School tuition revenue is received from Penn Hills School District, with approximately 33% of outstanding tuition receivable. As of June 30, 2012, approximately 65% of the School tuition revenue was received from Penn Hill School District, with approximately 42% of outstanding tuition receivable.

Contributions received are recorded as increases in unrestricted, temporarily restricted, or permanently restricted net assets, depending on the existence and/or nature of any donor restrictions. As of June 30, 2013 and 2012, the School had no temporarily restricted or permanently restricted net assets.

F. Property and Equipment

Expenditures for additions and improvements are capitalized and are stated at cost.

Donations of property and equipment are recorded as contributions at fair value at the date of donation. Such donations are reported as increases in unrestricted net assets unless the donor has restricted the donated asset to a specific purpose.

Depreciation of property and equipment is provided by the straight-line method over the estimated useful lives of the assets. The lives used in computing depreciation range from 5 to 7 years.

Maintenance and repairs which are not considered to extend the useful lives of assets are charged to operations as incurred.

Upon sale or retirement, the cost of assets and related allowances are removed from the accounts and any gains or losses are included in income (expense) for the year.

G. Books, Periodicals and Supplies

The School expenses its books, periodicals and supplies as they are purchased.

**PENN HILLS CHARTER SCHOOL
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Notes to the Financial Statements (Continued)

Note 2 - Summary of Significant Accounting Policies (Continued)

H. Expense Allocation

The costs of providing the School's various program services are presented on a functional basis in the statements of activities and changes in net assets, and functional expenses. Directly identifiable expenses are charged to programs and supporting services. Expenses related to more than one function are charged to programs and supporting services based on the allocation of full-time employee classifications and the space utilized per the School building.

I. Income Taxes

The School is in the process of applying for a tax-exempt status under Section 501(c)(3) of the Internal Revenue Code. The School has received extensions from the Internal Revenue Service (IRS). During the fiscal year ended June 30, 2013, the School re-submitted its application to the IRS. On November 15, 2013, the School received notice that its application was in the initial review process.

The accounting standard on accounting for uncertainty in income taxes addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under that guidance, the School may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by taxing authorities based on the technical merits of the position. Examples of tax positions include the tax-exempt status of the School and various positions related to the potential sources of unrelated business taxable income (UBIT). The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. There were no unrecognized tax benefits identified or recorded as liabilities for fiscal years 2013 and 2012.

J. Adoption of New Accounting Standards

In September 2011, the Financial Accounting Standards Board issued updated guidance on additional disclosures for entities who participate in multiemployer pension plans. The guidance requires expanded disclosures about an employer's participation in multiemployer plans, including the plan name, identifying number, the level of an employer's participation, information about funding status of the plan and the nature of the commitments to the plans. The revisions do not change the current recognition and measurement guidance for an employer's participation in a multiemployer plan. The amendments are effective for annual periods for fiscal years ending after December 15, 2012 and should be applied retrospectively for all prior periods presented. The implementation of this guidance did not have a material impact on the financial statements.

**PENN HILLS CHARTER SCHOOL
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Notes to the Financial Statements (Continued)

Note 2 - Summary of Significant Accounting Policies (Continued)

K. Reclassifications

Certain reclassifications have been made to the 2012 financial statements to conform with the 2013 presentation. During 2013, the School reclassified accruals associated with agreements with a related party (Note 5) to due to related party on the balance sheet. The amount reclassified from accounts payable and accrued expenses to due to related party was approximately \$267,000 at June 30, 2012.

L. Consideration of Subsequent Events

Management evaluated subsequent events and transactions for potential recognition or disclosure in the financial statements through February 20, 2014, the day the financial statements were approved and authorized for issue.

Note 3 - Property and Equipment

Property and equipment consist of the following at June 30:

	<u>2013</u>	<u>2012</u>
Furniture, fixtures and office equipment	\$187,065	\$146,692
Leasehold improvements	<u>43,199</u>	<u>43,199</u>
	230,264	189,891
Less: Accumulated depreciation	(<u>72,813</u>)	(<u>33,205</u>)
	<u>\$157,451</u>	<u>\$156,686</u>

**PENN HILLS CHARTER SCHOOL
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Notes to the Financial Statements (Continued)

Note 4 - Public School Employees' Retirement System (PSERS)

Plan Description

Substantially all full-time and part-time employees of the School participate in the Public School Employees' Retirement System (PSERS), a cost sharing, multiemployer public employee retirement system. The Employer Identification Number of PSERS is 27-3920298. The PSERS provides retirement and disability benefits, legislative mandated ad hoc cost of living adjustments, and health care insurance premium assistance to qualifying annuitants. The PSERS was established under the Public School Employees' Retirement Code (Code). The PSERS issues a publicly available financial report that includes financial statements and required supplementary information for the plan. The report may be obtained by making a request in writing to the Office of Financial Management, Public School Employees' Retirement System, P.O. Box 125, Harrisburg, PA 17108-0125. The report is also available in the publications section of the PSERS site on the internet, www.psers.state.pa.us. PSERS is not subject to the benefit accrual and participation requirements of the Employee Retirement Income Security Act of 1974 (ERISA). As a result, certain multiemployer plan disclosures, including the certified zone status, are not applicable to PSERS.

Funding Policy

Contributions are required by active members, school districts, and the Commonwealth of Pennsylvania as established by the Public School Employees' Retirement Board in accordance with the Code. Active members who joined the system prior to July 22, 1983 must contribute 5¼% (Membership Class TC) or 6½% (Membership Class TD) of their salaries, and 6¼% or 7½% of their salaries if they were hired afterwards. Members who joined PSERS after June 30, 2001 contribute at 7½%. For all new hires or those who elected to do so, the higher contribution rates began with service rendered on or after January 1, 2002.

Schools must contribute at rates based upon an actuarial valuation. The rate of employer contribution was 12.36% for fiscal year ended June 30, 2013 and 8.65% for fiscal year ended June 30, 2012. The contribution rate for school districts will increase to 16.93% for fiscal year 2014.

**PENN HILLS CHARTER SCHOOL
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Notes to the Financial Statements (Continued)

Note 4 - Public School Employees' Retirement System (PSERS) (Continued)

The risks of participating in multiemployer plans are different from single-employer plans in the following aspects:

- a) Assets contributed to the multiemployer plan by one employer may be used to provide benefits to employees of other participating employers.
- b) If a participating employer stops contributing to the plan, the unfunded obligations of the plan may be required to be assumed by the remaining participating employers.
- c) If the School chooses to stop participating in any of its multiemployer plans, it may be required to pay those plans a withdrawal amount based on the underfunded status of the plan, referred to as a withdrawal liability.

PSERS operates on a fiscal year from July 1 through June 30. The following table presents certain financial information about PSERS from the most recent actuarial certification as of June 30:

	<u>2013</u>	<u>2012</u>
Total plan assets	\$58,200,000,000	\$59,100,000,000
Present value of accumulated plan benefits	\$87,800,000,000	\$85,600,000,000
Underfunded plan assets	\$29,600,000,000	\$26,500,000,000
Funded status	66%	69%

The total amount of contributions paid to the plan in fiscal year June 30, 2013 is approximately \$177,000. No contribution payments were made in fiscal year June 30, 2012. The School has accrued its contribution of approximately \$73,000 in 2013 and approximately \$90,000 in 2012, which was equal to its required contribution for the year. The amounts are included in accrued payroll and related liabilities as of June 30, 2013 and 2012. In accordance with Act 29, the Commonwealth of Pennsylvania reimburses school districts for at least one-half of contributions made to PSERS. The School received a reimbursement of \$81,784 in the fiscal year June 30, 2013.

**PENN HILLS CHARTER SCHOOL
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Notes to the Financial Statements (Continued)

Note 5 - Related Parties

On June 28, 2013, the School and Imagine Schools, Inc. (Imagine) entered into a Charter School Administrative Services Agreement (Administrative Services Agreement) for Imagine to provide certain school management services for the School. From the commencement of School operations through to date of the signed Administrative Services Agreement, a disagreement existed between the School and Imagine as to whether the parties had entered into a valid and binding operating agreement in May 2011 to organize and operate the School (the Disputed Operating Agreement). Under the terms of the Administrative Services Agreement:

- The School pays Imagine an Indirect Cost Allocation fee equal to 12% of the School's revenue as defined by the Administrative Services Agreement. These fees totaled \$488,526 for 2013 and \$309,476 for 2012. Approximately \$711,000 as of June 30, 2013 and \$220,000 as of June 30, 2012 is payable to Imagine related to the indirect cost allocation fee and is included in due to related party.
- Approximately \$416,000 in start-up and development costs were paid by Imagine on behalf of the School in 2012. Imagine is entitled to repayment of the development allocation paid to the School of \$250,000 (Note 6). The balance of \$166,000 was recorded as a contribution in fiscal year June 30, 2012.
- The School is able to request advances from Imagine to pay for operating expenses of the School and, as of June 30, 2013 and 2012, an outstanding balance for advances received is \$230,000 and is included in due to related party.

**PENN HILLS CHARTER SCHOOL
OF ENTREPRENEURSHIP**

Notes to the Financial Statements (Continued)

Note 5 - Related Parties (Continued)

Under the terms of the Disputed Operating Agreement, there was an additional annual fee related to the operating advances requested by the School:

- In consideration of Imagine's commitment to make operating advances under the terms of the Disputed Operating Agreement, the School was to pay Imagine a loss mitigation allocation fee based on a percentage of revenue, 2½% for 2013 and 2012. The loss mitigation fee totaled \$101,776 for 2013 and \$64,474 for 2012. Approximately \$148,000 as of June 30, 2013 and \$46,000 as of June 30, 2012 is payable to Imagine related to the loss mitigation allocation fee and is included in due to related party. In conjunction with the finalization of the Administrative Services Agreement, the School and Imagine entered into a Payment Agreement and Mutual Release (Payment Agreement). Through the Payment Agreement, the School is required to make the following payments: \$140,000 payment on June 30, 2013; thirteen payments of \$58,000 paid on the last day of each month beginning October 2013 and ending October 2014; a payment of \$45,111 on or before December 31, 2014 provided the amount of this payment shall be adjusted if necessary if the revenue of the School for the fiscal year ended June 30, 2013 is greater or less than \$3,608,820; a make-up payment on or before December 31, 2014 only to the extent that the payment amount does not exceed 30% of revenues of the School during the preceding month; a payment of \$130,000 on or before December 31, 2014. Payments are expected provided that the School's expenditures for the fiscal year do not exceed the approved budgeted expenditures by more than 5% and the amounts collected during such fiscal year with respect to unpaid amounts from the school districts are less than amounts projected to be collected by more than \$200,000, the parties will negotiate to modify the payments.

The School also has entered into a lease agreement with Schoolhouse Finance, LLC, a wholly owned subsidiary of Imagine, for the School's building (Note 7).

Note 6 - Note Payable

As part of the Administrative Services Agreement with Imagine, a development allocation was provided to the School in order to facilitate the start-up of the School. The principal amount of the note is \$250,000. Pursuant to the Administrative Service Agreement, the note is to be repaid at an interest rate of 10½% over 20 years at \$2,500 per month.

**PENN HILLS CHARTER SCHOOL
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Notes to the Financial Statements (Continued)

Note 6 - Note Payable (Continued)

Approximate future maturities of the note payable consistent with the Administrative Services Agreement are as follows:

Year Ending <u>June 30</u>	<u>Amount</u>
2014	\$ 11,000
2015	5,000
2016	6,000
2017	6,000
2018	7,000
Thereafter	<u>214,000</u>
	<u>\$249,000</u>

The School incurred interest expense of approximately \$26,000 for 2013 and \$21,000 for 2012. Accrued interest, recorded in due to related parties, was approximately \$41,000 as of June 30, 2013 and approximately \$15,000 as of June 30, 2012.

Note 7 - Leases

The lease agreement for the School building commenced on August 24, 2011 and will continue until June 30, 2016, but automatically terminates upon the termination or non-renewal of the School's charter. For 2013, lease expense includes \$104,000 for the School building as well as rental expense related to lease of modular units utilized during the School year ended June 30, 2013 of \$195,000. Lease expense was approximately \$87,000 for the year ended June 30, 2012. The annual amounts of lease payments required are as follows:

Year Ending <u>June 30</u>	<u>Amount</u>
2014	\$107,000
2015	109,000
2016	<u>112,000</u>
	<u>\$328,000</u>