

**SOUTH BRONX CHARTER SCHOOL FOR  
INTERNATIONAL CULTURES AND THE ARTS**

**FINANCIAL STATEMENTS**

**JUNE 30, 2010 AND 2009**

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES  
AND THE ARTS

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INDEPENDENT AUDITORS' REPORT

To The Board of Trustees  
South Bronx Charter School for International Cultures and the Arts  
Bronx, New York

We have audited the accompanying statements of financial position of South Bronx Charter School for International Cultures and the Arts at June 30, 2010 and 2009, and the related statements of activities, functional expenses and cash flows for the years then ended. These financial statements are the responsibility of the School's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

As described in Note 12, the School restated certain balances of net assets at June 30, 2009.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of South Bronx Charter School for International Cultures and the Arts at June 30, 2010 and 2009, and the results of its operations and cash flows for year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report, dated November 1, 2010, 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. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and results of testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

*Grassi & Co., CPAs, P.C.*

GRASSI & CO., CPAs, P.C.

Jericho, New York  
November 1, 2010

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SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
 STATEMENTS OF FINANCIAL POSITION  
 JUNE 30, 2010 AND 2009

ASSETS

	<u>2010</u>	<u>2009</u>
Cash	\$ 112,245	\$ 102,213
Restricted cash	230,000	230,000
Receivables from governmental agencies, net of allowance for doubtful accounts of \$0	300,454	220,438
Prepaid and other assets	8,931	48,149
Property and equipment - net	<u>2,842,434</u>	<u>3,454,278</u>
 Total Assets	 <u>\$ 3,494,064</u>	 <u>\$ 4,055,078</u>

LIABILITIES AND NET ASSETS

Liabilities		
Notes payable	\$ 1,900,000	\$ 1,900,000
Accounts payable	94,743	50,604
Due to management company	1,321,223	1,132,206
Accrued salaries and benefits	476,860	419,598
Accrued expenses	154,355	267,200
Obligations under capital lease	<u>13,723</u>	<u>25,076</u>
 Total Liabilities	 <u>3,960,904</u>	 <u>3,794,684</u>
 Commitments and Contingencies		
 Net Assets		
Unrestricted	<u>(466,840)</u>	<u>260,394</u>
 Total Liabilities and Net Assets	 <u>\$ 3,494,064</u>	 <u>\$ 4,055,078</u>

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

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
STATEMENTS OF ACTIVITIES  
FOR THE YEARS ENDED JUNE 30, 2010 AND 2009

	<u>2010</u>	<u>2009</u>
REVENUE AND SUPPORT:		
Resident student enrollment	\$ 4,295,635	\$ 3,927,011
Federal funding	396,754	269,957
State funding	120,000	237,832
Contributions-in-kind	368,032	413,253
Food service	148,484	127,799
Students with disabilities	2,058	8,609
Government grants	48,342	7,676
Contributions	0	1,970
Other income	29	0
Interest income	<u>19</u>	<u>267</u>
 Total Revenue and Support	 <u>5,379,353</u>	 <u>4,994,374</u>
 EXPENSES:		
Program Services		
Regular education	4,465,891	4,070,900
Special education	<u>91,143</u>	<u>169,620</u>
	4,557,034	4,240,520
 Supporting Services		
Management and general	<u>808,341</u>	<u>1,072,616</u>
 Total Expenses	 <u>5,365,375</u>	 <u>5,313,136</u>
 Change in Unrestricted Net Assets Before Other Changes in Net Assets	 13,978	 (318,762)
OTHER CHANGES IN NET ASSETS:		
Loss on impairment of property and equipment	<u>(741,212)</u>	<u>0</u>
 Change in Unrestricted Net Assets	 (727,234)	 (318,762)
 Net Assets, Beginning of Year	 <u>260,394</u>	 <u>579,156</u>
 Net Assets, End of Year	 <u>\$ (466,840)</u>	 <u>\$ 260,394</u>

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

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
STATEMENT OF FUNCTIONAL EXPENSES  
FOR THE YEAR ENDED JUNE 30, 2010

	Program Services			Management and General	Total 2010
	Regular Education	Special Education	Total Program		
EXPENSES:					
Personnel Expenses					
Salaries and Wages	\$ 2,317,187	\$ 47,290	\$ 2,364,477	\$ 0	\$ 2,364,477
Fringe Benefits	573,708	11,708	585,416	0	585,416
Total Personnel Expenses	2,890,895	58,998	2,949,893	0	2,949,893
OPERATING EXPENSES:					
Contracted Services - Management Company	0	0	0	644,345	644,345
Consultants - Other	2,352	48	2,400	0	2,400
Food	199,004	4,061	203,065	0	203,065
Insurance	58,787	1,200	59,987	0	59,987
Supplies and Materials	111,292	2,271	113,563	0	113,563
Textbooks	74,202	1,514	75,716	0	75,716
Telephone	13,829	282	14,111	0	14,111
Occupancy	783,327	15,986	799,313	0	799,313
Printing	1,887	39	1,926	0	1,926
Staff Development	69,023	1,409	70,432	0	70,432
Equipment Rental/Lease	5,170	106	5,276	0	5,276
Legal	0	0	0	25,637	25,637
Maintenance and Repairs	6,560	134	6,694	0	6,694
Transportation (Student)	92,354	1,885	94,239	0	94,239
Travel	3,244	66	3,310	0	3,310
Depreciation	77,713	1,586	79,299	0	79,299
Advertising	6,940	142	7,082	0	7,082
Administrative Fees	13,991	286	14,277	0	14,277
Interest	0	0	0	138,359	138,359
Other	55,321	1,130	56,451	0	56,451
Total Operating Expenses	1,574,996	32,145	1,607,141	808,341	2,415,482
Total Expenses	\$ 4,465,891	\$ 91,143	\$ 4,557,034	\$ 808,341	\$ 5,365,375

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

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
STATEMENT OF FUNCTIONAL EXPENSES  
FOR THE YEAR ENDED JUNE 30, 2009

	Program Services			Management and General	Total 2009
	Regular Education	Special Education	Total Program		
<b>EXPENSES:</b>					
<b>Personnel Expenses</b>					
Salaries and Wages	\$ 1,969,748	\$ 82,073	\$ 2,051,821	\$ 0	\$ 2,051,821
Fringe Benefits	431,715	17,988	449,703	0	449,703
Total Personnel Expenses	<u>2,401,463</u>	<u>100,061</u>	<u>2,501,524</u>	<u>0</u>	<u>2,501,524</u>
<b>OPERATING EXPENSES:</b>					
Contracted Services - Management Company	0	0	0	864,277	864,277
Consultants - Other	1,720	72	1,792	0	1,792
Food	156,046	6,502	162,548	0	162,548
Insurance	45,314	1,888	47,202	0	47,202
Supplies and Materials	93,586	3,899	97,485	0	97,485
Textbooks	93,308	3,888	97,196	0	97,196
Telephone	8,772	365	9,137	0	9,137
Occupancy	873,738	36,406	910,144	0	910,144
Printing	1,428	59	1,487	0	1,487
Staff Development	188,323	7,847	196,170	0	196,170
Equipment Rental/Lease	3,565	149	3,714	0	3,714
Legal	0	0	0	37,502	37,502
Accounting/Audit Fee	0	0	0	22,023	22,023
Maintenance and Repairs	9,824	409	10,233	0	10,233
Transportation (Student)	75,041	3,127	78,168	0	78,168
Travel	3,409	142	3,551	0	3,551
Depreciation	62,840	2,618	65,458	0	65,458
Advertising	4,712	196	4,908	0	4,908
Administrative Fees	18,268	761	19,029	0	19,029
Interest	0	0	0	148,814	148,814
Other	29,543	1,231	30,774	0	30,774
Total Operating Expenses	<u>1,669,437</u>	<u>69,559</u>	<u>1,738,996</u>	<u>1,072,616</u>	<u>2,811,612</u>
Total Expenses	<u>\$ 4,070,900</u>	<u>\$ 169,620</u>	<u>\$ 4,240,520</u>	<u>\$ 1,072,616</u>	<u>\$ 5,313,136</u>

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

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED JUNE 30, 2010 AND 2009

	<u>2010</u>	<u>2009</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash received from resident student enrollment funding	\$ 4,295,635	\$ 3,927,011
Cash received from federal funding	323,159	334,730
Cash received from state funding	113,579	237,832
Cash received from food service program	148,484	127,799
Cash received from students with disabilities program	2,058	8,609
Cash received from government grants	48,342	7,676
Cash received from contributions	0	1,970
Other income received	29	0
Interest income received	<u>19</u>	<u>267</u>
Cash Provided By Operating Activities	<u>4,931,305</u>	<u>4,645,894</u>
Cash paid for regular education program	(4,008,205)	(3,365,099)
Cash paid for special education program	(73,724)	(140,211)
Cash paid for management and general expenses	<u>(454,324)</u>	<u>(688,670)</u>
Cash Disbursed For Operating Activities	<u>(4,536,253)</u>	<u>(4,193,980)</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>395,052</u>	<u>451,914</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Increase in restricted cash	0	(230,000)
Purchase of property and equipment	<u>(208,667)</u>	<u>(357,912)</u>
NET CASH USED IN INVESTING ACTIVITIES	<u>(208,667)</u>	<u>(587,912)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
(Repayment of) advances from management company	(165,000)	240,000
Principal payments of obligations under capital lease	<u>(11,353)</u>	<u>(14,367)</u>
NET CASH (USED IN) PROVIDED BY FINANCING ACTIVITIES	<u>(176,353)</u>	<u>225,633</u>
NET INCREASE IN CASH	10,032	89,635
CASH, BEGINNING OF YEAR	<u>102,213</u>	<u>12,578</u>
CASH, END OF YEAR	<u>\$ 112,245</u>	<u>\$ 102,213</u>

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

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
 STATEMENTS OF CASH FLOWS (CONT'D.)  
 FOR THE YEARS ENDED JUNE 30, 2010 AND 2009

	<u>2010</u>	<u>2009</u>
<u>RECONCILIATION OF CHANGE IN UNRESTRICTED NET ASSETS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:</u>		
CHANGE IN UNRESTRICTED NET ASSETS	\$ (727,234)	\$ (318,762)
ADJUSTMENTS TO RECONCILE CHANGE IN UNRESTRICTED NET ASSETS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Depreciation	79,299	65,458
Loss on impairment of property and equipment	741,212	0
Accrued interest on due to management company	(13,208)	64,087
Changes in Assets (Increase) Decrease:		
Receivables from governmental agencies	(80,016)	64,773
Prepaid and other assets	39,218	(31,890)
Changes in Liabilities Increase (Decrease):		
Accounts payable	44,139	(72,010)
Due to management company	367,225	319,859
Accrued salaries and benefits	57,262	239,844
Accrued expenses	<u>(112,845)</u>	<u>120,555</u>
Total Adjustments	<u>1,122,286</u>	<u>770,676</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 395,052</u>	<u>\$ 451,914</u>
<u>SCHEDULE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:</u>		
Property and equipment purchased through capital lease financing	<u>\$ 0</u>	<u>\$ 38,000</u>

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

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
NOTES TO FINANCIAL STATEMENTS

Note 1 - Summary of Significant Accounting Policies

Nature of Activities

South Bronx Charter School for International Cultures and the Arts (the "School") is a charter school for children located in the Bronx, New York. In its fifth year of operation 2009-2010, the School operated from kindergarten to fifth grade. Under the charter agreement, the school educates children on a completely nondiscriminatory and secular basis. The purpose is for founders and supporters of the School to provide access to a public education of high quality for all children.

Basis of Accounting and Presentation

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. Net assets and revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the School and changes therein are classified and reported as follows:

Unrestricted net assets - Net assets of the School which have not been restricted by an outside donor or by law are available for use in carrying out the operations of the School.

Fair Value of Financial Instruments

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. To increase the comparability of fair value measurements, a three-tier fair value hierarchy, which prioritizes the inputs used in the valuation methodologies, is as follows:

Level 1 - Valuations based on quoted prices for identical assets and liabilities in active markets.

Level 2 - Valuations based on observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets and liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data.

Level 3 - Valuations based on unobservable inputs reflecting the School's own assumptions, consistent with reasonably available assumptions made by other market participants. These valuations require significant judgment.

At June 30, 2010, the fair value of the School's financial instruments including cash, restricted cash, receivables from governmental agencies, accounts payable and accrued expenses, approximated book value due to the short maturity of these instruments.

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
NOTES TO FINANCIAL STATEMENTS

Note 1 - Summary of Significant Accounting Policies (cont'd.)

Fair Value of Financial Instruments (cont'd.)

At June 30, 2010, the School does not have assets or liabilities required to be measured at fair value in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 820, *Fair Value Measurements*.

Property and Equipment

Property and equipment is stated at cost. The costs of additions and betterments are capitalized when they exceed \$500, and expenditures for repairs and maintenance are expensed in the period incurred. When items of property and equipment are sold or retired, the related costs and accumulated depreciation are removed from the accounts and any gain or loss is included in income.

Depreciation of property and equipment is provided utilizing the straight-line method over the estimated useful lives of the respective assets as follows:

Furniture and fixtures	7 years
Computer equipment	3 years
Office equipment	3 years

No depreciation is recorded on construction in progress until the construction is completed (see Note 13).

The School reviews the carrying value of property and equipment for impairment whenever events and circumstances indicate that the carrying value of an asset may not be recoverable from the estimated future cash flows expected to result from its use and eventual disposition. In cases where undiscounted expected future cash flows are less than the carrying value, an impairment loss is recognized equal to an amount by which the carrying value exceeds the fair value of assets. The factors considered by management in performing this assessment include current operating results, trends and prospects, the manner in which the property is used, and the effects of obsolescence, demand, competition, and other economic factors.

Tax Status

The School is exempt from Federal income and excise taxes under Internal Revenue Code Section 501(c)(3) and is a publicly supported organization as described in Section 509(a). It is classified by the Internal Revenue Service as other than a private foundation.

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
NOTES TO FINANCIAL STATEMENTS

Note 1 - Summary of Significant Accounting Policies (cont'd.)

Contributions

The School records contributions of cash and other assets as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and/or nature of any donor restrictions. The School records contributions as restricted support if they are received with donor stipulations that limit their use through purpose or time restrictions. When a restriction expires, that is, when a stipulated time restriction ends or a purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the Statements of Activities as net assets released from restrictions.

Functional Allocation of Expenses

The costs of providing the various programs and other activities have been summarized on a functional basis in the Statements of Functional Expenses. Accordingly, certain costs have been allocated among programs and supporting services benefited. Salaries, wages and fringe benefits were allocated as direct costs to programs and supporting activity, other costs to programs, and as direct costs based on actual costs associated with the activity.

Advertising Costs

Advertising costs are expensed as incurred and amounted to \$7,082 and \$4,908 for the years ended June 30, 2010 and 2009, respectively.

Use of 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.

Subsequent Events

The School has evaluated all events and transactions that occurred after June 30, 2010 through the date of the audit of these financial statements. During this period, there were no material subsequent events requiring disclosure.

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
NOTES TO FINANCIAL STATEMENTS

Note 1 - Summary of Significant Accounting Policies (cont'd.)

New Accounting Pronouncements

In July 2010, the FASB issued Accounting Standards Update (“ASU”) No. 2010-20, *Receivables (Topic 310): Disclosure about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*. The objective of this ASU is for an entity to provide disclosures that facilitate financial statement users’ evaluation of the following:

- The nature of credit risk inherent in the entity’s portfolio of financing receivables;
- How that risk is analyzed and assessed in arriving at the allowance for credit losses; and
- The changes and reasons for those changes in the allowance for credit losses.

To achieve these objectives, an entity should provide disclosures on a disaggregated basis on two defined levels: (1) portfolio segment; and (2) class of financing receivable. The ASU makes changes to existing disclosure requirements and includes additional disclosure requirements about financing receivables, including:

- Credit quality indicators of financing receivables at the end of the reporting period by class of financing receivables;
- The aging of past due financing receivables at the end of the reporting period by class of financing receivables; and
- The nature and extent of troubled debt restructurings that occurred during the period by class of financing receivables and their effect on the allowance for credit losses.

For nonpublic entities, the disclosures are effective for annual reporting periods ending on or after December 15, 2011. The School has not yet determined whether the adoption of this statement will have a material impact on its financial statements.

In September 2009, the FASB issued ASU No. 2009-06 (“ASU 2009-06”), *Implementation Guidance on Accounting for Uncertainty in Income Taxes and Disclosure Amendments for Nonpublic Entities*, which clarifies whether income taxes paid by the entity are attributable to the entity or its owners, the nature of a tax position for a pass-through entity or a tax-exempt not-for-profit entity, and how uncertainty in income taxes should be applied when a group of related entities comprise both taxable and non-taxable entities. In addition, ASU 2009-06 eliminates the tabular disclosure requirements of uncertain tax positions under FASB ASC Topic 740, *Income Taxes*, for non-public entities. For entities that are currently applying the standards for accounting for uncertainty in income taxes, the guidance and disclosure amendments are effective for financial statements issued for interim and annual periods ending after September 15, 2009. For those entities that have deferred the application of accounting for uncertainty in income taxes in accordance with paragraph 740-10-65-1(e), the guidance and disclosure amendments are effective upon adoption of those standards. The amendments in ASU 2009-06 do not affect the effective date guidance for certain non-public entities in paragraph 740-10-65-1. The adoption of ASU 2009-06 had no material impact on the School’s financial statements.

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
NOTES TO FINANCIAL STATEMENTS

Note 2 - Reclassifications

Certain accounts relating to the prior year have been reclassified to conform to the current year's presentation. These reclassifications have no effect on changes in unrestricted net assets as previously reported.

Note 3 - Concentration of Credit Risk

The School maintains cash balances in two financial institutions. The balances are insured by the Federal Deposit Insurance Corporation up to \$250,000 per institution. From time to time, the School's balances may exceed this limit. At June 30, 2010, uninsured cash balances were approximately \$72,000. The School believes it is not exposed to any significant credit risk on cash and restricted cash.

The School is dependent on various government agencies for funding, and is responsible for meeting the requirements of such agencies. If the School were to lose students or the related government funding, it could have a substantial effect on its ability to continue operations.

Note 4 - Restricted Cash

At June 30, 2010, restricted cash of \$230,000 is held in a non-interest bearing account. The cash is held as collateral in relation to the \$1,400,000 note payable (see Note 8).

Note 5 - Pupil Enrollment and Receivables from Governmental Agencies and New York State ("NYS") Stimulus Facility Financing Grant

Under the School's Charter School Agreement and the Charter Schools Act, the School is entitled to receive funding from both State and Federal sources that is available to public schools. These funds include State pupil enrollment funds, planning and implementation fund, the NYS Stimulus Facility financing grant, Federal food subsidies and Title I, II, IV, V and IID funds. The calculation of the amounts to be paid to the School under these programs is determined by the State, and is based on complex laws and regulations, enrollment levels, and economic information related to the home school districts of the children enrolled in the School. If these regulations, some of which are relatively new in the State of New York, were to change, or other factors included in the calculations were to change, the level of funding that the School receives could vary significantly.

Amounts due from governmental agencies and the NYS Stimulus Facility financing grant and included in federal and state funding as revenue in the Statements of Activities for the years ended June 30, 2010 and 2009 are \$300,454 and \$220,438, respectively.

The amounts are based upon actual amounts received as well as estimates by the management of the School. Management believes these estimates are based upon the best information available at this time. However, actual amounts received, as determined by NYS, could vary based on changes in the factors used to calculate the amounts owed.

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
NOTES TO FINANCIAL STATEMENTS

Note 6 - Property and Equipment

Property and equipment, net is summarized as follows:

	<u>2010</u>	<u>2009</u>
Furniture and fixtures	\$ 196,771	\$ 176,360
Computer equipment	121,871	78,605
Office equipment	109,367	108,067
Land	273,451	384,632
Construction in progress	<u>2,393,431</u>	<u>2,879,772</u>
	3,094,891	3,627,436
Less: Accumulated depreciation	<u>252,457</u>	<u>173,158</u>
	<u>\$ 2,842,434</u>	<u>\$ 3,454,278</u>

Included in construction in progress is the building, which is not being utilized and therefore is not being depreciated, totaling \$2,179,580.

Depreciation expense related to property and equipment amounted to \$79,299 and \$65,458 for the years ended June 30, 2010 and 2009, respectively.

Note 7 - Management Company

Victory Schools, Inc. ("Victory") manages the operations of the School under a management agreement entered into by the School and Victory. The agreement was executed on March 28, 2005. Per the terms of the Agreement, Victory assumes responsibility for tasks and functions associated with the educational services to be provided to the children at the School in accordance with the terms of the Charter and the Charter Schools Act, subject to the appropriate oversight from the School's Board of Trustees. Victory is responsible for designing the curriculum, acquiring educational materials, hiring all staff and providing all financial and accounting functions.

In providing the above services, Victory is paid a management fee in an amount equal to the product of the total full-time equivalent enrollment of students in the School as defined under Section 119.1 of the New York State Commissioner of Education Regulation multiplied by two thousand dollars (\$2,000) (the "Per Pupil Fee"). This Per Pupil Fee shall be increased or decreased each year by the percentage increase or decrease in the Final Adjusted Expense Per Pupil for charter schools of the New York City school district, as calculated by the New York State Education Department annually.

Victory is entitled to receive the management fee on a bi-monthly basis. Any Victory fee, or portion thereof, not paid within (30) days of its due date shall bear interest at an annualized rate of 15% per annum on the outstanding past due amount, provided such past due payments are not as a result of the New York City Department of Education's failure to timely remit the Adjusted Expense Per Pupil to the Charter School.

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
NOTES TO FINANCIAL STATEMENTS

Note 7 - Management Company (cont'd.)

The management and central services fee expense for the year ended June 30, 2010 was \$644,345 based on \$1,866 per pupil. An agreed-upon interest rate of 5.125% per annum was charged on the outstanding balance during the year ended June 30, 2010. Interest accrued on the balance totals \$50,879.

The amount due to the management company of \$1,321,223 at June 30, 2010 relates to management and central services fees discussed above totaling \$1,060,344 and accrued interest of \$50,879. The remaining \$210,000 represents cash advances from the management company. \$165,000 was paid back during the year ended June 30, 2010. During the year ended June 30, 2010, the School made net payments to the management company of \$1,100,000 related to operating activities, which is included in cash paid for regular education program in the Statement of Cash Flows.

The management and central services fee expense for the year ended June 30, 2009 was \$864,277 based on \$2,739 per pupil. An agreed-upon interest rate of 6% per annum was charged on the outstanding balance during the year ended June 30, 2009. Interest accrued on the balance totals \$64,087.

The amount due to the management company of \$1,132,206 at June 30, 2009 relates to management and central services fees discussed above totaling \$693,119 and accrued interest of \$64,087. The remaining \$375,000 represents cash advances from the management company, of which \$240,000 was advanced during the year ended June 30, 2009. During the year ended June 30, 2010, the School made net payments to the management company of \$840,000 related to operating activities, which is included in cash paid for regular education program in the Statement of Cash Flows.

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
NOTES TO FINANCIAL STATEMENTS

Note 8 - Notes Payable

Notes payable at June 30, 2010 and 2009 are summarized as follows.

	<u>2010</u>	<u>2009</u>
<p>Loan - interest only at LIBOR plus 2.25% (totaling 3.31% at June 30, 2010) per annum, with a balloon payment of all outstanding and unpaid principal due in July 2010, secured by property with a net book value of \$2,564,212. The loan was extended to October 15, 2010. The Board is in the process of renewing the expired loan with new terms. The loan is subject to certain financial covenants. At June 30, 2010, the School is in violation of a covenant on the loan, and has not obtained a waiver, since the bank and the School are in the process of refinancing the loan.</p>	\$ 1,400,000	\$ 1,400,000
<p>Loan - interest only at prime rate plus 1% (totaling 4.25% at June 30, 2010) per annum, with a balloon payment of all outstanding and unpaid principal due in July 2010, secured by property with a net book value of \$2,564,212, and subordinated to the \$1,400,000 loan noted above. The loan was extended to October 15, 2010. The Board is in the process of renewing the expired loan with new terms. The loan is subject to certain financial covenants. At June 30, 2010, the School is in violation of a covenant on the loan, and has not obtained a waiver, since the bank and the School are in the process of refinancing the loan.</p>	<u>500,000</u>	<u>500,000</u>
	<u>\$ 1,900,000</u>	<u>\$ 1,900,000</u>

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
NOTES TO FINANCIAL STATEMENTS

Note 9 - Obligations Under Capital Lease

The School's property under a capital lease, which is included in property and equipment, is summarized as follows:

	<u>2010</u>	<u>2009</u>
Office equipment	\$ 37,796	\$ 37,796
Less: Accumulated depreciation	<u>25,325</u>	<u>11,634</u>
	<u>\$ 12,471</u>	<u>\$ 26,162</u>

The capital lease requires monthly payments of \$528 per annum through August 2011.

Future minimum lease payments under the capital lease at June 30, 2010 are as follows:

Years Ending June 30:

2011	\$ 12,667	
2012		<u>1,056</u>
Present value of future minimum lease payments		13,723
Less: Current portion		<u>12,667</u>
		<u>\$ 1,056</u>

Note 10 - Defined Contribution Plan

The School offers a 401(k) plan (the "Plan") for substantially all of its employees. Employees are eligible for the Plan immediately upon employment, and participation in the Plan is voluntary. Employees can make pre-tax contributions up to 100% of their compensation, subject to Internal Revenue Service guidelines. The School matches the employee contribution 100% up to 4% of the employee's annual compensation. The School's contribution recognized in the Statements of Activities in fringe benefits was \$23,167 and \$19,181 for the years ended June 30, 2010 and 2009, respectively. The Plan assets are held in a separate trust and are not included in the accompanying financial statements. All Plan assets are held for the exclusive benefit of the Plan's participants and beneficiaries.

Note 11 - Contingencies

The School participates in a number of Federal and State programs. These programs require that the School complies with certain requirements of laws, regulations, contracts, and agreements applicable to the programs in which it participates. All funds expended in connection with government grants and contracts are subject to audit by government agencies. While the ultimate liability, if any, from such audits of government contracts by government agencies is presently not determinable, it should not, in the opinion of the management, have a material effect on the School's financial statements. Accordingly, no provision for any such liability that may result has been made in the accompanying financial statements.

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
NOTES TO FINANCIAL STATEMENTS

Note 12 - Restatement of Net Assets

Based on the information developed as a result of the current year's inquiry into the accounting for certain accounts, the School determined that a restatement of the June 30, 2009 financial statements is appropriate to correct accounting errors due to accruals not recorded which related to property and equipment purchases, as follows:

	<u>As Previously Stated</u>	<u>As Restated</u>	<u>Effect on Net Assets</u>
Property and equipment - net	\$ 3,352,165	\$ 3,454,278	\$ 102,113
Accrued expenses	(165,087)	\$ (267,200)	<u>(102,113)</u>
Net adjustment from restatement			-0-
 Net Assets, as previously stated			 <u>260,394</u>
 Net Assets, as restated			 <u>\$ 260,394</u>

The above adjustment had no net effect on the fiscal 2009 Statements of Activities and Net Assets, or previous periods.

Note 13 - Impairment Loss

During the year ended June 30, 2010, the School determined that the carrying value of the land and building held for development exceeded the fair value. The fair value was based on the appraised value. The School recognized an impairment loss of \$741,212 due to the adjustment to fair value.



**INDEPENDENT AUDITORS' REPORT  
ON INTERNAL CONTROL OVER FINANCIAL REPORTING  
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF  
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH  
GOVERNMENT AUDITING STANDARDS**

To The Board of Trustees  
South Bronx Charter School for International Cultures and the Arts  
Bronx, New York

We have audited the financial statements of South Bronx Charter School for International Cultures and the Arts (the "School") at June 30, 2010 and 2009, which collectively comprise the School's basic financial statements and have issued our report thereon dated November 1, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the School's internal control over financial reporting as a basis for designing our audit procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the School's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the School's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and questioned costs that we consider to be significant deficiencies in internal control over financial reporting. 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. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs in item 2010-01 to be a significant deficiency.

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## Compliance and Other Matters

As part of obtaining reasonable assurance about whether the School's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and questioned costs in item 2010-01.

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

This report is intended solely for the information and use of management, the Board of Directors, others within the School, federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

*Grassi & Co., CPAs, P.C.*

GRASSI & CO., CPAs, P.C.

Jericho, New York  
November 1, 2010

SOUTH BRONX CHARTER SCHOOL FOR INTERNATIONAL CULTURES AND THE ARTS  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Financial Statement Findings

2010-01 - Bank Account at School

Observation:

During the course of our audit, the management company made us aware that a bank account had been opened at the School a number of years ago and that the bank account activity had never been recorded on the School's books, as the management company was not aware that the bank account existed.

Recommendation:

We recommend that management prepare the activity from when the account was opened and provide bank statements, bank reconciliations and an adjustment to record the activity.

Management's Corrective Action Plan:

Management and the Board of Directors will be informed any time a new bank account is opened. All activity was provided to the management company and the activity has been recorded. There was no material activity related to prior years.