

COMMUNITY EDUCATION ASSOCIATION, INC.

FINANCIAL STATEMENTS

YEARS ENDED JUNE 30, 2011 and 2010

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September 26, 2011

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of  
Community Education Association, Inc.  
Newnan, Georgia

I have audited the accompanying statement of financial position of Community Education Association, Inc., as of June 30, 2011 and June 30, 2010 and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that I 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. I believe that my audit provides a reasonable basis for my opinion.

In my opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Community Education Association, Inc. as of June 30, 2011 and June 30, 2010 and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

*C. Douglas Erwin, Jr. CPA*

**COMMUNITY EDUCATION ASSOCIATION, INC.**  
**STATEMENT OF FINANCIAL POSITION**  
**AS OF JUNE 30, 2011 & 2010**

- ASSETS -

	<u>2011</u>	<u>2010</u>
<u>Current Assets</u>		
Cash and Cash Equivalents	\$ 4,607,526	\$ 1,796,314
Accounts Receivable	82,364	48,631
Prepaid Expenses	3,114	3,352
Total Current Assets	4,693,004	1,848,297
Property & Equipment (Net of Accumulated Depreciation of \$355,238 & \$311,653, Respectively)	1,562,906	1,606,491
Other Assets	5,171	6,592
Total Assets	\$ 6,261,081	\$ 3,461,380

- LIABILITIES & NET ASSETS -

<u>Current Liabilities</u>		
Accounts Payable	\$ 4,269,361	1,655,310
Accrued Expenses	48,194	36,576
Line of Credit	50,000	55,000
Current Portion Long-Term Debt	56,627	53,134
Total Current Liabilities	4,424,182	1,800,020
Long-Term Debt	1,103,501	1,159,141
Total Liabilities	5,527,683	2,959,161
<u>Net Assets</u>		
Unrestricted	733,398	502,219
Temporarily Restricted	-	-
Permanently Restricted	-	-
Total Net Assets	733,398	502,219
Total Liabilities and Net Assets	\$ 6,261,081	\$ 3,461,380

See Independent Auditor's Report and the Notes to Financial Statements

**COMMUNITY EDUCATION ASSOCIATION, INC.**  
**STATEMENT OF ACTIVITIES**  
**YEARS ENDED JUNE 30, 2011 & JUNE 30, 2010**

	<u>2011</u>	<u>2010</u>
<b>Revenues, Gains &amp; Other Support</b>		
Charter Schools Facilities Grant	\$ 90,000	\$ 120,000
Enterprise Operations	30,691	36,845
Other Grants, Donations, & Revenues	3,070	2,858
Program Revenue	26,848,230	19,219,553
<b>Total Revenues, Gains &amp; Other Support</b>	<b>26,971,991</b>	<b>19,379,256</b>
 <b>Program Expenditures</b>		
Instruction	15,475,991	11,588,295
Support Services		
Pupil Services	1,728,015	741,178
Improvement of Instructional Services	8,612,362	6,114,597
Educational Media Services	15,470	84,644
Administration and Business Support Services	370,077	356,067
Maintenance and Operation of Plant Services	433,740	307,187
Enterprise Operations	22,783	25,801
Debt Service	82,374	85,242
<b>Total Program Expenditures</b>	<b>26,740,812</b>	<b>19,303,011</b>
 Changes in Net Assets	 231,179	 76,245
 Net Assets - Beginning of Year	 502,219	 425,974
 Net Assets - End of Year	 <b>\$ 733,398</b>	 <b>\$ 502,219</b>

See Independent Auditor's Report and the Notes to Financial Statements

**COMMUNITY EDUCATION ASSOCIATION, INC.**  
**STATEMENT OF CASH FLOWS**  
**YEARS ENDED JUNE 30, 2011 & JUNE 30, 2010**

	<u>2011</u>	<u>2010</u>
<b>Net Cash Provided by Operating Activities</b>		
<b>Increase (Decrease) in Net Assets</b>	\$ 231,179	\$ 76,245
<b>Adjustments to Reconcile Change in Net Assets To Net Cash Provided by Operating Activities</b>		
Depreciation Expense	43,585	94,792
(Increase)/Decrease in Accounts Receivable	(33,733)	(10,015)
(Increase)/Decrease in Deposits	1,421	(375)
(Increase)/Decrease in Prepaid Expense	238	6,852
Increase/(Decrease) in Accounts Payable	2,614,051	(1,229,942)
Increase/(Decrease) in Accrued Expenses	11,618	(41,494)
<b>Net Cash Provided by Operating Activities</b>	<u>2,868,359</u>	<u>(1,103,937)</u>
 <b>Cash Provided by Investing Activities</b>		
Purchase of Fixed Assets	-	(254,755)
<b>Net Cash Provided by Investing Activities</b>	<u>-</u>	<u>(254,755)</u>
 <b>Cash Provided by Financing Activities</b>		
Line of Credit Proceeds/(Payments)	(5,000)	35,000
Long-Term Debt Proceeds/(Payments)	(52,147)	1,212,275
Short-Term Notes Proceeds/(Payments)	-	(1,113,527)
<b>Net Cash Provided by Financing Activities</b>	<u>(57,147)</u>	<u>133,748</u>
 <b>Net Increase in Cash and Cash Equivalents</b>	<u>2,811,212</u>	<u>(1,224,944)</u>
 <b>Cash and Cash Equivalents at Beginning of Year</b>	1,796,314	3,021,258
 <b>Cash and Cash Equivalents at End of Year</b>	<u>\$ 4,607,526</u>	<u>\$ 1,796,314</u>

See Independent Auditor's Report and the Notes to Financial Statements

COMMUNITY EDUCATION ASSOCIATION, INC.  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2011 & JUNE 30, 2010

NOTE 1 – ORGANIZATION & SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Community Education Association, Inc., “the School”, was incorporated in the state of Georgia on October 30, 1998 pursuant to the provisions of the *Georgia Non-Profit Corporation Code*. The School operates a public state chartered special school under an agreement with the Georgia Department of Education which expires on June 30, 2016. The School operates in both a "brick and mortar" physical location in Newnan, Georgia and a virtual school which provides education via internet and computerized learning (see notes below).

The financial accounting policies and procedures of the School conform to generally accepted accounting principles as well as to the general accounting policies required of charter schools. The following is a summary of the most significant accounting policies.

Method of Accounting

The School utilizes the accrual method of accounting. The School is subject to Statement of Financial Standards (SFAS) 117, “Financial Statements of Not-for-Profit Organizations”. Under SFAS 117, the School is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted, temporarily restricted, and permanently restricted. In addition, the School is required to present a statement of cash flows. The School has classified its financial statements according to three classes of net assets as follows:

- Unrestricted Net Assets – Net assets which are not subject to donor-imposed stipulations.
- Temporarily Restricted Net Assets - Net assets subject to donor-imposed stipulations that may or will be met, either by actions of the School and/or the passage of time. When a restriction expires, temporarily restricted net assets are classified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. There were no temporarily restricted net assets in these financial statements
- Permanently Restricted Net Assets – Net assets subject to donor-imposed stipulations that they be maintained permanently by the School. Generally, the donors of these assets permit the School to use all or part of the income earned on any related investments for general purposes. There were no permanently restricted net assets in these financial statements.

The School also adopted SFAS No. 116, “Accounting for Contributions Received and Contributions Made”, whereby contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor restrictions. Restricted net assets are reclassified to unrestricted net assets upon satisfaction of the time or purpose of the restrictions. The adoption had no cumulative effect on net assets at the date of adoption.

Gifts, donations, and contributions which are not restricted by the donor or other outside party for particular purposes are deemed to be earned and reported as revenue of the Unrestricted Fund. Expenditures from the Unrestricted Fund are made in compliance with the intentions of the School’s board of directors.

COMMUNITY EDUCATION ASSOCIATION, INC.  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2011 & JUNE 30, 2010

NOTE 1 – ORGNANIZATION & SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Inventories

The School maintains no significant supply of inventory therefore all supplies are expensed as incurred.

Fixed Assets and Depreciation

Fixed assets are carried at cost less accumulated depreciation if purchased by the School, or, if acquired by gift, the asset is carried at the estimated fair market value at the date of the gift. Depreciation is computed by using the Modified Accelerated Cost Recovery System as promulgated by the Internal Revenue Service over the statutory lives of the asset. The School capitalizes asset purchases in excess of \$1,000 and expenses those under that amount.

Statement of Cash Flows

For purposes of the statement of cash flows, the Company considers all highly liquid accounts with an original maturity of three months or less as cash equivalents. Interest and income taxes paid during the year ended June 30, 2011 totaled \$81,075 and \$-0-, respectively, and during the year ended June 30, 2010 totaled \$81,725 and \$-0-, respectively.

Financial Instruments

Financial instruments, principally receivables, payables, and accrued expenses are reported at values which management believes are not significantly different from their fair values. The School believes no significant credit risk exists with respect to any of its financial instruments.

Management 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 and disclosures. Accordingly, actual results could differ from those estimates.

NOTE 2 – REVENUES

The School is organized as a state of Georgia "Charter School", which means the school receives funding from the state of Georgia under the "Quality Basic Education" (QBE) program which allocates revenues from the education budget to public schools based upon the average number of full-time equivalent students (FTE). The School does not receive local or county property tax funds.

Donated investments, materials and equipment are recorded in the financial statements at their estimated fair values at the date of receipt. The School receives from time to time certain federal and state grants for reading programs, teacher quality programs, and facilities funding. These programs have restricted use requirements placed upon the funding which requires that the funds be used as stipulated by the grant.

COMMUNITY EDUCATION ASSOCIATION, INC.  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2011 & JUNE 30, 2010

NOTE 3 - INCOME TAXES

The corporation was notified in February 1999 by the Internal Revenue Service that it will be recognized henceforth as an exempt organization under the terms and conditions of section 501(a) and 501(c)(3) of the Internal Revenue Code. The corporation is required to file Form 990 *Return of Organization Exempt From Income Tax* to report its activities.

Under the exempt status, the corporation generally pays no income tax on its income as long as it does not receive income which is considered to be used outside the purposes for which the school was granted its exemption. Donations to the School are generally tax deductible under Internal Revenue Code Section 170.

NOTE 4 - RISK MANAGEMENT

Insurance

The School is exposed to various risks of loss related to torts, theft of, damage to, and destruction of assets, errors or omissions, job related illness or injuries to employees, acts of God and unemployment compensation but has reduced its risks by purchasing insurance as follows: property insurance coverage of \$1,750,000 on buildings and \$600,000 on contents, general liability and teacher/professional liability coverage of \$2,000,000 aggregate and \$1,000,000 per claim, workers compensation liability of \$500,000, misconduct insurance of \$1,000,000, umbrella coverage of \$4,000,000, business auto coverage of \$1,000,000, directors and officers liability of \$1,000,000. The School is self-insured to the degree it carries a deductible.

Custodial Credit Risk

The school maintains its accounts at two commercial banks. Cash accounts are guaranteed by the Federal Deposit Insurance Corporation (FDIC) to a maximum of \$250,000. Cash balances exceeded the FDIC insurance on June 30, 2011 and 2010 by \$4,355,858 and \$1,526,143, respectively, at one of the banks. These uninsured balance pose a risk that the bank could close at a time in which its balances exceed the insurable amount which could result in a significant loss to the School. There are no material risks from creditors of the school.

Economic Dependency

The school, being a state chartered institution is subject to the risk that the state legislature, courts, or other state or federal agencies could revoke the laws which grant charter schools the right to receive federal and state funds to provide education using taxpayer funds. In addition, the school must apply for renewal of its charter every five years and must remain in compliance with all laws and regulations of the state and federal departments of education and the Internal Revenue Service. The risk of non-compliance with these laws and regulations poses a material risk to continued operation of the school.

COMMUNITY EDUCATION ASSOCIATION, INC.  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2011 & JUNE 30, 2010

NOTE 5 – LINE OF CREDIT

The School entered into a promissory note with BB&T Bank to borrow up to \$85,000 for the purpose of providing operating capital. The loan functions as a line of credit as funds can be borrowed, repaid, and borrowed again at any time during the term of the loan. As of June 30, 2011, \$50,000 was due under this agreement. This loan extended a previous loan made by BB&T in the amount of \$85,000 which matured on January 5, 2010 on which \$55,000 was due as of June 30, 2010. The loans bear interest at the bank's variable prime rate plus 0.25% and are secured by a blanket lien on all equipment and machinery. The renewed loan matures on January 5, 2012 at which time all unpaid interest and principal are due. The loans are classified as short-term obligations.

NOTE 6 – GEORGIA CYBER ACADEMY

The School's charter was amended on July 18, 2007 by the Georgia Department of Education to approve the establishment of the Georgia Cyber Academy ("GCA") (formerly known as Georgia Virtual Academy) as a program of the Odyssey School. This program allows students to perform course work from home using an internet based learning system with instruction by the program's teachers. This program was created by an agreement dated July 9, 2007 between the School and K12 Georgia, LLC titled *Educational Products and Services Agreement*, "the Agreement".

On June 30, 2008, K12 Georgia LLC was merged with K12 Virtual Schools LLC. By virtue of this merger and the assignment clause contained in the Agreement, the contract to operate the virtual school program was transferred to K12 Virtual Schools LLC, a Delaware limited liability company. K12 Virtual Schools, LLC is owned by K12, Inc. ("K12").

Under the Agreement, Odyssey School approves the GCA budget for the virtual school program each year but the day to day management and operation of the school including decisions about employment and purchasing is performed by K12 Virtual Schools, LLC and K12. Odyssey School receives funding (program revenue) from the state of Georgia based upon the number of students enrolled which is then allocated between itself and K12 Virtual Schools, LLC based upon the number of students enrolled in each program (Odyssey and GCA). Odyssey School deducts from program revenue any costs budgeted for the GCA program which it has paid, if any, and an oversight fee as defined below. The oversight fee is included in program revenue in the statement of activities. The balance of the funds are payable to K12 Virtual Schools, LLC within 30 days which are then used by K12 Virtual Schools, LLC to pay the operating costs of the GCA program to include curriculum, books, materials, and computers and other general and management expenses. The Odyssey School oversight fee is a percentage of the revenue received as follows:

<u>School Year</u>	<u>Oversight Fee</u>
2007-2008	3.5%
2008-2009	3.0%
2009-2010	2.5%
2010-2011	2.0%
2011-2012	2.0%

COMMUNITY EDUCATION ASSOCIATION, INC.  
 NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2010 & JUNE 30, 2009

NOTE 7 – GEORGIA CYBER ACADEMY - Continued

As of June 30, 2011 and June 30, 2009, \$4,152,535 and \$1,587,637, respectively, was due under this agreement for program revenues to K12 Virtual Schools, LLC which is included in the caption “Accounts Payable” in the financial statements.

The students of GCA are considered by the state of Georgia to be students of Odyssey School under its charter, and Odyssey School is responsible for providing for the education of those students just as it is the students enrolled in its brick and mortar location. However, K12 Virtual Schools, LLC operates the program, employs teachers and other professionals, enters into lease agreements, contracts for services and purchases educational materials and other items under its separate corporate identity over which Odyssey School exercises no control other than through its approval of an annual budget and oversight of the program.

Periodically and at the conclusion of its own fiscal year, K12 Virtual Schools, LLC submits reports including a report of program costs to Odyssey School. Costs which have been paid to 3rd party vendors by K12 and K12 Virtual Schools, LLC are included in the financial statements of Odyssey School in the appropriate functional category. Because K12 Virtual Schools, LLC manages numerous other schools, it has developed curriculum and instructional materials which it then sells to the schools which it manages including GCA. K12 and K12 Virtual Schools, LLC also purchase computers, books, and other materials in bulk to obtain discounts which they then sell to schools managed by K12 Virtual Schools including GCA based upon their National Price List for similarly managed schools. Odyssey School has no control over the prices reflected on this K12 price list although it approves the overall program budget. In addition, K12 and K12 Virtual Schools, LLC also employs management and administrative personnel which it provides to the schools they manage including Georgia Cyber Academy.

After allocating costs charged by K12 and K12 Virtual Schools, LLC, the program costs of Georgia Cyber Academy at times, reflects a program deficit whereby costs have exceeded the revenues received from Odyssey School. Because Odyssey School is not responsible for any program deficit, the costs allocated by K12 to Georgia Cyber Academy are adjusted so that the program does not end a fiscal year with a loss. Costs charged by K12 to Georgia Cyber Academy as described above and which are included in the statement of activities are as follows:

<u>Cost Description</u>	<u>June 30, 2011</u>	<u>June 30, 2010</u>
Curriculum Expense	\$ 8,571,263	\$ 6,058,834
Equipment Rent	861,619	612,521
Instructional Materials	<u>4,972,902</u>	<u>4,103,425</u>
Total K12 Costs	<u>\$ 14,405,784</u>	<u>\$ 10,774,780</u>

COMMUNITY EDUCATION ASSOCIATION, INC.  
 NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2011 & JUNE 30, 2010

NOTE 8 –BUILDING ACQUISTION/DEBT

On April 1, 2008, the School entered into a purchase contract to acquire 5.02 acres land and a 27,000 square foot building and closed on the purchase on July 18, 2008 for a permanent facility for its students. The purchase price was \$750,000 plus closing costs. The School entered into a promissory note with The Bank of Georgia in the amount of \$680,000 to facilitate the purchase and on March 18, 2009 entered into a construction lending agreement with The Bank of Georgia in the amount of \$585,000 to finance improvements to the purchased facility.

On December 21, 2009, the School entered into a new lending agreement with The Bank of Georgia in the amount of \$1,240,000. The proceeds of this loan were used to repay the purchase note and construction note above. The terms of the new loan include interest at six and a half percent (6.5%) with 59 payments due in the amount of \$10,863.97 and a balloon payment of all unpaid principal and interest on December 20, 2014. The loan is secured by the School's main campus building. Maturities of long-term debt are as follows:

<u>Fiscal Year Ended</u>	<u>Amount</u>
June 30, 2012 (Current)	\$ 56,627
June 30, 2013	60,419
June 30, 2014	64,465
June 30, 2015	978,617
June 30, 2016	<u>- 0 -</u>
Total	<u>\$ 1,160,128</u>

NOTE 9 - FINANCIAL PRESENTATION & SALARY ACCRUAL

The School functions in an environment in which its financial information is compiled and used by educators, auditors, the general public, and state officials who need information based upon the state of Georgia state chart of accounts. Therefore, the School utilizes the state of Georgia's chart of accounts and has presented its financial reports in a format which reports on its expenditures by program function.

Management has determined that the School should record as a liability the cost of teachers whose contracts end on May 30 but who are paid over a twelve month period which ends in July. The intent of accruing these costs is to better match program revenue with program expenses. Therefore, the School has recorded a liability of \$41,424 and \$32,591 in the statement of financial position at June 30, 2011 and 2010 respectively under the caption "Accrued Expenses" which represents the salaries and associated taxes due in July.

COMMUNITY EDUCATION ASSOCIATION, INC.  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2011 & JUNE 30, 2010

NOTE 10 - EQUIPMENT LEASE COMMITMENTS

The School leases copying equipment under the terms of an agreement dated December 29, 2009. Monthly payments are due in the amount of \$549 for a term of sixty months commencing February 1, 2010. Annual lease commitments for the next five years and thereafter are as follows:

<u>Fiscal Year Ended</u>	<u>Amount</u>
June 30, 2012	\$ 6,588
June 30, 2013	6,588
June 30, 2014	6,588
June 30, 2015	6,588
June 30, 2016	<u>3,843</u>
Total	<u>\$ 30,195</u>

NOTE 11 - SUBSEQUENT EVENTS

Management of the Association reviewed the financials as of September 26, 2010, the date of issuance, for any events which occurred subsequent to the end of the fiscal year ended June 30, 2011. No events were noted which would require disclosure in the financial statements.