Merrick Academy – Queens Public Charter School

Independent Auditor's Reports and Financial Statements

June 30, 2018

Merrick Academy – Queens Public Charter School

June 30, 2018

Contents

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Independent Auditor's Report on Financial Statements and Supplementary Information

Board of Trustees
Merrick Academy – Queens Public Charter School
Laurelton, New York

We have audited the accompanying financial statements of Merrick Academy – Queens Public Charter School, which comprise the balance sheet as of June 30, 2018, and the related statements of activities and cash flows for the year 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.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *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 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 auditor's 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.

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 Merrick Academy – Queens Public Charter School as of June 30, 2018, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The Schedule of Functional Expenses is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 31, 2018, on our consideration of Merrick Academy – Queens Public Charter School's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of Merrick Academy – Queens Public Charter School's 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 Merrick Academy – Queens Public Charter School's internal control over financial reporting and compliance.

BKD, LLP

New York, New York
October 31, 2018

Merrick Academy – Queens Public Charter School

Balance Sheet

June 30, 2018

Assets

Current Assets	
Cash	$ 2,037,670
Grants and contracts receivable	384,646
Prepaid expenses	69,616
Total current assets	2,491,932
Security deposits	127,770
Cash – reserve	75,342
Fixed assets – net	608,009
Total assets	$ 3,303,053

Liabilities and Net Assets

Current Liabilities	
Accounts payable and accrued expenses	$ 235,588
Accrued salaries and related liabilities	694,681
Total current liabilities	930,269
Deferred rent	237,127
Total liabilities	1,167,396
Net Assets – Unrestricted	2,135,657
Total liabilities and net assets	$ 3,303,053

Merrick Academy – Queens Public Charter School

Statement of Activities

Year Ended June 30, 2018

	Unrestricted	Temporarily Restricted	Total
Operating Revenues and Other Support			
Resident student enrollment	$ 8,081,280	$ -	$ 8,081,280
Students with disabilities	1,253,949	-	1,253,949
Total state and local per-pupil operating revenues	9,335,229	-	9,335,229
Government grants and contracts	322,313	-	322,313
Contributions	1,450	-	1,450
Interest	10,922	-	10,922
Miscellaneous income	74,714	-	74,714
Net assets released from restriction	1,500	(1,500)	-
Total operating revenues and other support	9,746,128	(1,500)	9,744,628
Expenses			
Program services			
Education	5,797,330	-	5,797,330
Special education	2,606,903	-	2,606,903
Total program services	8,404,233	-	8,404,233
Supporting services			
Management and general	1,246,433	-	1,246,433
Total expenses	9,650,666	-	9,650,666
Change in Net Assets	95,462	(1,500)	93,962
Net Assets, Beginning of Year	2,040,195	1,500	2,041,695
Net Assets, End of Year	$ 2,135,657	$ -	$ 2,135,657

Merrick Academy – Queens Public Charter School

Statement of Cash Flows

Year Ended June 30, 2018

Operating Activities	
Change in net assets	$ 93,962
Adjustments to reconcile change in net assets to net cash provided by operating activities	
Depreciation	256,805
Increase in assets	
Grants and contracts receivable	(95,350)
Prepaid expenses	(1,698)
Increase (decrease) in liabilities	
Accounts payable and accrued expenses	83,857
Accrued salaries and related liabilities	96,602
Deferred revenue	(35,284)
Deferred rent	5,078
Net cash provided by operating activities	403,972
Investing Activities	
Fixed asset acquisitions	(334,015)
Cash – deposits in escrow	(338)
Net cash used in investing activities	(334,353)
Net Change in Cash	69,619
Cash, Beginning of Year	1,968,051
Cash, End of Year	$ 2,037,670

Merrick Academy – Queens Public Charter School

Notes to Financial Statements

June 30, 2018

Note 1: Nature of Organization

Merrick Academy – Queens Public Charter School (the School) is an educational corporation that operates as a charter school in the borough of Queens, New York City. On January 1, 2000, the Board of Regents and the Board of Trustees of the University of the State of New York, for and on behalf of the State Education Department, granted the School a charter from grades K-6. On February 3, 2015 the School's charter renewal was approved for an additional five years, which currently expires on June 20, 2020. During the fiscal year ended June 30, 2018, the School operated classes for approximately 540 students in grades K-5.

Merrick Academy – Queens Public Charter School is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code. However, the School is subject to federal income tax on any unrelated business taxable income. The School is supported primarily by state and local per-pupil operating revenues.

Note 2: Summary of Significant Accounting Policies

Basis of Accounting

The financial statements are prepared on the accrual basis of accounting.

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, expenses and other changes in net assets during the reporting period. Actual results could differ from those estimates.

Cash – Reserve

As part of the School's charter agreement, the School agreed to establish a long-term reserve account to pay for legal and audit expenses that would be associated with a dissolution should it occur.

Grants and Contracts Revenue and Receivables

Revenues from government grants and contracts to which the School is entitled are recognized mostly on student enrollment. Some grants are provided for specific educational endeavors which are not based on student enrollment and are recorded when related expenditures are incurred by the School. Receivables are recorded when the revenue is earned.

Allowance for Doubtful Accounts

Bad debt expense is charged if a receivable is determined to be uncollectible based on periodic review by management. Factors used to determine whether an allowance should be recorded include the age of the receivable and a review of payments subsequent to year end. Management deemed no allowance necessary for the year ended June 30, 2018.

Fixed Assets

Fixed assets are recorded at cost less accumulated depreciation. Items with a cost of $1,000 and an estimated useful life of more than one year are capitalized. Depreciation is provided on the straight-line basis over the estimated useful lives of assets. Leasehold improvements are amortized over the term of the lease or the life of the asset, whichever is shorter.

Unrestricted Net Assets

Unrestricted net assets include funds having no restrictions as to use or purpose imposed by donors.

Temporarily Restricted Net Assets

Temporarily restricted net assets are those whose use by the School has been limited by donors to a specific time period or purpose. For the year ended June 30, 2018 there was $1,500 released from restriction for the construction of a new playground.

State and Local per-Pupil Operating Revenues

Revenues from the state and local governments resulting from the School's charter status and based on the number of students enrolled are recorded when services are performed in accordance with the charter agreement. These grants are recorded as revenue by the School when services are rendered.

Contributions

Unconditional contributions, including promises to give cash and other assets, are reported at fair value at the date the contribution is received. All contributions are considered to be available for unrestricted use unless specifically restricted by donors.

Deferred Rent

Operating leases are straight-lined over the term of the lease. Deferred rent has been recorded for the difference between the fixed payment and the rent expense.

Functional Allocation of Expenses

The costs of providing the School's programs and other activities have been summarized on a functional basis. Accordingly, certain costs have been allocated among the programs and supporting services benefited based on actual expenditures and cost allocations estimated by the School's personnel.

Subsequent Events

Subsequent events have been evaluated through October 31, 2018, which is the date the financial statements were available to be issued.

Note 3: Fixed Assets

		Useful Lives
Leasehold improvements	$ 841,931	5-20 years
Furniture and fixtures	385,252	7 years
Office and classroom equipment	293,895	3 years
Computer equipment	640,389	3 years
Software	86,511	3 years
	2,247,978	
Accumulated depreciation and amortization	(1,639,969)	
	$ 608,009	

Note 4: Lease Commitments

The School has a lease on the school building which will expire on December 31, 2022. Rent expense for the year ended June 30, 2018 was $830,278.

The future minimum lease payments as of June 30, 2018 are:

Year Ending June 30	
2019	$ 845,829
2020	866,975
2021	888,649
2022	910,865
2023	461,055
	$ 3,973,373

The leases for the building is being straight-lined over the life of the lease. The deferred rent liability as of June 30, 2018 was $237,127.

The School entered into noncancelable lease agreements for office equipment expiring at various dates through November 2021. Rent expense for the year ended June 30, 2018 was $72,331.

The future minimum lease payments as of June 30, 2018 are:

Year Ending June 30	
2019	$ 58,500
2020	42,900
2021	42,900
2022	10,400
	$ 154,700

Note 5: Contingencies and Concentrations

Certain grants and contracts may be subject to audit by the funding sources. Such audits might result in disallowances of costs submitted for reimbursement. Management is of the opinion that such cost disallowances, if any, will not have a material effect on the accompanying financial statements. Accordingly, no amounts have been provided in the accompanying financial statements for such potential claims.

A significant portion of the School's operating revenue is paid by New York State Education Department.

In addition, all grants and contracts receivable due at year end were all due from the New York State Education Department.

Financial instruments which potentially subject the School to a concentration of credit risk are cash accounts with a financial institution in excess of FDIC insurance limits. At June 30, 2018, the School's cash accounts exceeded federally insured limits by approximately $1.85 million.

Note 6: Retirement Plan

The School sponsors a 401(k) retirement plan for its employees. All employees are immediately eligible to participate in the plan. Employees can make pretax contributions up to a maximum of 100% of the annual compensation, subject to IRS restrictions. The School matches the employee contribution up to 4% of the employee's annual compensation. Pension expense under this plan for the year ended June 30, 2018 was $77,056.

Supplementary Information

Merrick Academy – Queens Public Charter School

Schedule of Functional Expenses

Year Ended June 30, 2018

	No. of Positions	Program Services			Supporting Services	Total
		Education	Special Education	Total	Management and General	
Personnel service costs						
Administrative staff personnel	7	$ 517,213	$ 323,258	$ 840,471	$ 452,562	$ 1,293,033
Instructional personnel	54	2,617,158	1,155,985	3,773,143	-	3,773,143
Noninstructional personnel	7	-	-	-	264,017	264,017
Salaries		3,134,371	1,479,243	4,613,614	716,579	5,330,193
Payroll taxes and employee benefits		761,107	359,199	1,120,306	109,894	1,230,200
Retirement		47,673	22,499	70,172	6,884	77,056
Legal service		-	-	-	52,648	52,648
Accounting/audit services		-	-	-	159,900	159,900
Other purchased/professional/ consulting services		309,293	115,674	424,967	40,974	465,941
Building and land rent/lease		513,681	242,428	756,109	74,169	830,278
Repairs and maintenance		80,934	38,196	119,130	11,686	130,816
Insurance		33,396	15,761	49,157	4,822	53,979
Utilities		71,836	33,902	105,738	10,372	116,110
Supplies/materials		154,132	39,399	193,531	3,706	197,237
Equipment/furnishings		19,219	9,070	28,289	2,775	31,064
Staff development		171,912	45,917	217,829	5,232	223,061
Marketing/recruitment		24,716	9,689	34,405	2,470	36,875
Technology		24,918	11,760	36,678	3,598	40,276
Student services		168,078	51,049	219,127	-	219,127
Office expense		97,697	46,107	143,804	14,106	157,910
Depreciation		158,882	74,983	233,865	22,940	256,805
Other		25,485	12,027	37,512	3,678	41,190
Total expenses		$ 5,797,330	$ 2,606,903	$ 8,404,233	$ 1,246,433	$ 9,650,666

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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*

Independent Auditor's Report

Board of Trustees
Merrick Academy – Queens Public Charter School
Laurelton, New York

We have audited, 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, the financial statements of Merrick Academy – Queens Public Charter School, which comprise the balance sheet as of June 30, 2018, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated October 31, 2018.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Merrick Academy – Queens Public Charter School's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Merrick Academy – Queens Public Charter School's internal control. Accordingly, we do not express an opinion on the effectiveness of Merrick Academy – Queens Public Charter School's internal control.

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. 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 deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify a certain deficiency in internal control, described in the accompanying schedule of findings and responses as item 2018-001 that we consider to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Merrick Academy – Queens Public Charter School's financial statements are free from 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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards.*

Merrick Academy – Queens Public Charter School's Response to Finding

Merrick Academy – Queens Public Charter School's response to the finding identified in our audit is described in the accompanying Schedule of Findings and Responses. Merrick Academy – Queens Public Charter School's response was not subject to the auditing procedures applied in the audit of the financial statements, and accordingly, we express no opinion on it.

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

BKD, LLP

New York, New York
October 31, 2018

Merrick Academy – Queens Public Charter School

Schedule of Findings and Responses

Year Ended June 30, 2018

2018-001 – Segregation of Duties – Review of Journal Entries

Criteria

The accounting functions should be properly segregated to ensure proper internal controls over financial reporting, including the review of journal entries made during the year.

Condition

The current staff size of the School does not always allow for the proper segregation of duties related to recording of journal entries in the general ledger.

Effect

It is possible that the financial statements could be manipulated by recording inappropriate journal entries.

Cause

Current staffing sizes restricted the ability to segregate certain functions.

Recommendation

We recommended that the School establish a procedure that all journal entries are reviewed and approved by someone other than the preparer.

Views of Responsible Officials

New procedures are being implemented for the Executive Director to review and approve all journal entries. See management's corrective action plan.

Merrick Academy
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October 30, 2018

Subject: Management Response to BKD Audit Letter Dated October 30, 2018

Finding: Segregation of Duties – Review of Journal Entries

The accounting functions should be properly segregated to ensure proper internal controls over financial reporting, including the review of journal entries made during the year.
The current staff size of the School does not always allow for the proper segregation of duties related to recording of journal entries in the general ledger.
It is possible that the financial statements could be manipulated by recording inappropriate journal entries.
We recommend that the School establish a procedure that all journal entries are reviewed and approved by someone other than the preparer.

Management Response: We concur with the finding. The finding has been reviewed with management and staff. Corrective action has been taken and new procedures have already been implemented for the Executive Director to review and approve all journal entries prior to releasing the financial statements.

Aubrey Featherstone, Executive Director

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Board of Trustees, and Management
Merrick Academy – Queens Public Charter School
Laurelton, New York

As part of our audit of the financial statements of Merrick Academy – Queens Public Charter School (the School) as of and for the year ended June 30, 2018, we wish to communicate the following to you.

AUDIT SCOPE AND RESULTS

Auditor's Responsibility Under 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

An audit performed 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 is designed to obtain reasonable, rather than absolute, assurance about the financial statements. In performing auditing procedures, we establish scopes of audit tests in relation to the financial statements taken as a whole. Our engagement does not include a detailed audit of every transaction. Our engagement letter more specifically describes our responsibilities.

These standards require communication of significant matters related to the financial statement audit that are relevant to the responsibilities of those charged with governance in overseeing the financial reporting process. Such matters are communicated in the remainder of this letter or have previously been communicated during other phases of the audit. The standards do not require the auditor to design procedures for the purpose of identifying other matters to be communicated with those charged with governance.

An audit of the financial statements does not relieve management or those charged with governance of their responsibilities. Our engagement letter more specifically describes your responsibilities.

Qualitative Aspects of Significant Accounting Policies and Practices

Significant Accounting Policies

The School's significant accounting policies are described in Note 2 of the audited financial statements.

Alternative Accounting Treatments

No matters are reportable.

Management Judgments and Accounting Estimates

Accounting estimates are an integral part of financial statement preparation by management, based on its judgments. The following areas involve significant areas of such estimates for which we are prepared to discuss management's estimation process and our procedures for testing the reasonableness of those estimates:

- Receivables and allowance for doubtful accounts

Financial Statement Disclosures

The following areas involve particularly sensitive financial statement disclosures for which we are prepared to discuss the issues involved and related judgments made in formulating those disclosures:

- Significant estimates and concentrations

Audit Adjustments

During the course of any audit, an auditor may propose adjustments to financial statement amounts. Management evaluates our proposals and records those adjustments which, in its judgment, are required to prevent the financial statements from being materially misstated. There were no proposed audit adjustments not recorded.

Proposed Audit Adjustments Recorded

- To adjust depreciation expense
- To adjust deferred rent
- To fully amortize the deferred lease incentive liability

Auditor's Judgments About the Quality of the School's Accounting Principles

No matters are reportable.

Other Material Communications

Listed below are other material communications between management and us related to the audit:

- Management representation letter (attached)

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements of Merrick Academy – Queens Public Charter School as of and for the year ended June 30, 2018 in accordance with auditing standards generally accepted in the United States of America, we considered the School's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the School's internal control. Accordingly, we do not express an opinion on the effectiveness of the School's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all deficiencies, significant deficiencies or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies.

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 of the School's financial statements on a timely basis. A deficiency in design exists when a control necessary to meet a control objective is missing or an existing control is not properly designed so that, even if the control operates as designed, a control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or when the person performing the control does not possess the necessary authority or competence to perform the control effectively.

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 School's financial statements will not be prevented or detected and corrected on a timely basis.

A significant deficiency is a deficiency, or 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 observed the following matter that we consider to be a significant deficiency.

Segregation of Duties – Review of Journal Entries

Refer to the Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters based on an audit of the financial statements performed in accordance with *Government Auditing Standards*.

OTHER MATTERS

Although not considered material weaknesses, significant deficiencies or deficiencies in internal control over financial reporting, we observed the following matters and offer these comments and suggestions with respect to matters which came to our attention during the course of the audit of the financial statements. Our audit procedures are designed primarily to enable us to form an opinion on the financial statements and, therefore, may not bring to light all weaknesses in policies and procedures that may exist. However, these matters are offered as constructive suggestions for the consideration of management as part of the ongoing process of modifying and improving financial and administrative practices and procedures. We can discuss these matters further at your convenience and may provide implementation assistance for changes or improvements.

Significant New FASB Accounting Standards

FASB Releases NFP Accounting Standard for Financial Reporting

Accounting Standards Update (ASU) 2016-14 changes requirements for financial statements and notes of all not-for-profit (NFP) entities and is effective for fiscal years beginning after December 15, 2017. Early adoption is permitted and should be applied on a retrospective basis; however, NFPs have the option in the year adopted to omit certain disclosures shown in comparative financials.

A summary of the changes by financial statement area is as follows:

Statement of financial position:

- The NFP statement of financial position will distinguish between two new classes of net assets – those with donor-imposed restrictions and those without. The ASU retains the current requirements to provide information on the nature and amount of different types of donor restrictions in the notes to the financial statements.

- Underwater donor-restricted endowment funds are to be shown within the donor-restricted fund class. This is a change from the previously required classification as unrestricted.

Statement of activities:

- The standard requires NFPs to report expenses by both nature and function, either on the face of the statement of activities, as a separate statement or within the notes.

- NFPs are required to use the placed-in-service approach for reporting expirations of restrictions on gifts of cash or other assets to be used to acquire or construct a long-lived asset, in the absence of explicit donor stipulations. This eliminates the option to release the donor-imposed restriction over the estimated useful life of the acquired asset.

- Investment income will be shown net of external and direct internal investment expenses. There is no longer a requirement to include a disclosure of those netted expenses.

Statement of cash flows:

- An NFP can continue to choose to either use the indirect or direct method of reporting to present operating cash flows. If the direct method is used, there is no longer a requirement to present or disclose cash flows using the indirect (reconciliation) method.

Notes to the financial statements:

- FASB requires enhanced quantitative and qualitative disclosures to provide additional information useful in assessing liquidity and cash flows.

- Provide disclosures on amounts and purposes of governing board or self-imposed designations and appropriations as of the end of the period.

For many NFPs, adoption of the ASU will result in significant changes to financial reporting and disclosures which likely will require significant hours to implement correctly. Management should examine its current reporting system to identify what changes are necessary to comply with the new standard for both its internal and external reporting requirements. Based on your financial statement reporting changes, BKD will need to spend additional time in formatting these changes within our audit reporting system if you outsource your annual report and disclosure preparation to BKD. Please contact your BKD Advisor if you would like assistance converting the School's financial statements to the new model and preparing the new disclosures.

The *Tax Cuts and Jobs Act of 2017*

In late December, President Donald J. Trump signed into law tax legislation, informally known as the *Tax Cuts and Jobs Act* (TCJA), representing one of the largest overhauls of the Internal Revenue Code (IRC) in more than 30 years. Many TCJA provisions took effect January 1, 2018, and affect virtually all U.S. taxpayers, including tax-exempt organizations. Some of the important provisions that may affect the School are as follows:

- **Excise tax on executive compensation:** For tax years beginning after December 31, 2017, the TCJA imposes an excise tax on excess tax-exempt organization executive compensation. This excise tax will be 21 percent of the remuneration paid by a tax-exempt organization – and related organizations – to any covered employee in excess of $1,000,000 plus any excess parachute payment paid by the organization to any covered employee. Covered employees include the five highest compensated employees of the organization for the taxable year and any employee that was a covered employee of the organization for any preceding taxable year beginning after December 31, 2016. The term remuneration does not include any compensation paid to a licensed medical professional (including a veterinarian) for the performance of medical or veterinary services by the professional.

- **Computation of unrelated business taxable income (UBTI):** Under the TCJA, for tax years beginning after December 31, 2017, UBTI will be computed separately with respect to each trade or business for organizations with more than one unrelated trade or business activity. Therefore, net operating losses (NOLs) from one unrelated trade or business activity will not be allowed to offset profits from another. Please note that corporate law changes will affect controlled corporations of tax-exempt organizations and the computation of unrelated business income. For more information on the corporate law changes, please view the appropriate charts on the following website: http://www.bkd.com/services/tax/tax-reform-resource-center.

- **Excise tax on private colleges and universities:** The TCJA enacted a 1.4 percent excise tax on the net investment income of private colleges and universities that is an "applicable educational institution." An applicable educational institution is a school that has 500 or more tuition-paying students, more than 50 percent of the tuition-paying students are located within the United States and has assets with a value of at least $500,000 per full-time student, not including those used directly in carrying out the institution's educational purpose. Assets and related net investment income of related organizations would be treated as part of the private college or university. The excise tax is effective for tax years beginning after December 31, 2017.

- **Tax-exempt bond financing:** The TCJA repealed the exclusion from gross income for interest on advance refunding bonds for such bonds issued after December 31, 2017.

Also important to consider is the elimination of the deduction for qualified transportation fringe benefits, as this affects tax-exempt employers in a unique way. Instead of losing a deduction, IRC §512(a)(7) provides that any disallowed benefit provided to an employee after December 31, 2017, and not associated with any unrelated business that is regularly carried on by the organization must be included as additional UBTI. The UBTI increase also may apply to expenditures for any parking facility used in connection with qualified parking and any on-premises athletic facility (as defined under IRC §132(j)(4)(B)). Tax-exempt employers face the same issues as taxable employers in regard to the actual calculation of these benefits. Nevertheless, the amount of any disallowed fringe benefits must either be included as UBTI and reported on Form 990-T, *Exempt Organization Business Income Tax Return*, or included as taxable wages to employees on Form W-2.

FASB Releases Not-for-Profit Accounting Standard for Grants and Contributions

On June 21, 2018, the Financial Accounting Standards Board issued Accounting Standards Update (ASU) 2018-08. This standard clarifies existing guidance on determining whether a transaction with a resource provider, *e.g.*, the receipt of funds under a government grant or contract, is a contribution or an exchange transaction. The guidance requires all organizations to evaluate whether the resource provider is receiving commensurate value in a transfer of assets transaction, and whether contributions are conditional or unconditional.

If commensurate value is received by the resource provider, the transaction would be accounted for as an exchange transaction by applying Topic 606, *Revenue from Contracts with Customers*, or other topics. The standard clarifies that a resource provider is not synonymous with the general public. Indirect benefit received by the public as a result of the assets transferred is not equivalent to commensurate value received by the resource provider. If commensurate value is not received by the resource provider, *i.e.*, the transaction is nonexchange, the recipient organization would record the transaction as a contribution under Topic 958 and determine whether the contribution is conditional or unconditional.

FASB expects that the new standard could result in more grants and contracts being accounted for as contributions (often conditional contributions) than under current generally accepted accounting principles. Because of this, it believes the clarifying guidance about whether a contribution is conditional or unconditional, which affects the timing of revenue recognition, is important. Both the recipient and resource provider would equally apply the guidance.

For the School, the standard will be effective for reporting periods beginning on or after December 15, 2018.

This communication is intended solely for the information and use of management, the board of trustees and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.

BKD, LLP

New York, New York
October 31, 2018

Merrick Academy
Queens Public Charter School
136-25 218th Street, Springfield Gardens, NY 11413
Phone: (718) 479-3753 • Fax: (718) 479-8108

October 31, 2018

BKD, LLP
Certified Public Accountants
655 Third Ave.
New York, NY 10017

We are providing this letter in connection with your audit of our financial statements as of and for the year ended June 30, 2018. We confirm that we are responsible for the fair presentation of the financial statements in conformity with accounting principles generally accepted in the United States of America. We are also responsible for adopting sound accounting policies, establishing and maintaining effective internal control over financial reporting, operations and compliance, and preventing and detecting fraud.

Certain representations in this letter are described as being limited to matters that are material. Items are considered material, regardless of size, if they involve an omission or misstatement of accounting information that, in light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement.

We confirm, to the best of our knowledge and belief, the following:

1. We have fulfilled our responsibilities, as set out in the terms of our engagement letter dated June 23, 2018, for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America.

2. We acknowledge our responsibility for 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.

3. We acknowledge our responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud.

4. We acknowledge the Organization is not a conduit debt obligor whose debt securities are listed, quoted or traded on an exchange or an over-the-counter market. As a result, we acknowledge the Organization does not meet the definition of a "public entity" under generally accepted accounting principles for certain accounting standards.

5. We have reviewed and approved a draft of the financial statements and related notes referred to above, which you prepared in connection with your audit of our financial statements. We acknowledge that we are responsible for the fair presentation of the financial statements and related notes.

6. We have provided you with:

   (a) Access to all information of which we are aware that is relevant to the preparation and fair presentation of the financial statements such as records, documentation and other matters.

   (b) Additional information that you have requested from us for the purpose of the audit.

   (c) Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.

   (d) All minutes of trustees' meetings held through the date of this letter.

   (e) All significant contracts and grants.

7. All transactions have been recorded in the accounting records and are reflected in the financial statements.

8. We have informed you of all current risks of a material amount that are not adequately prevented or detected by Organization procedures with respect to:

   (a) Misappropriation of assets.

   (b) Misrepresented or misstated assets, liabilities or net assets.

9. We understand the potential penalties for failure to disclose reportable tax transactions to the taxing authorities and have fully disclosed to BKD any and all known reportable tax transactions.

10. We have no knowledge of any known or suspected:

    (a) Fraudulent financial reporting or misappropriation of assets involving management or employees who have significant roles in internal control.

    (b) Fraudulent financial reporting or misappropriation of assets involving others that could have a material effect on the financial statements.

11. We have no knowledge of any allegations of fraud or suspected fraud affecting the Organization received in communications from employees, customers, regulators, suppliers or others.

12. We have disclosed to you the identity of the entity's related parties and all the related party relationships and transactions of which we are aware. Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with accounting principles generally accepted in the United States of America. We understand that the term related party refers to an affiliate; management, and members of their immediate families, subsidiaries accounted for by the equity method; and any other party with which the Organization may deal if the Organization can significantly influence, or be influenced by, the management or operating policies of the other. The term affiliate refers to a party that directly or indirectly controls, or is controlled by, or is under common control with, the Organization.

13. Except as reflected in the financial statements, there are no:

    (a) Plans or intentions that may materially affect carrying values or classifications of assets and liabilities.

    (b) Material transactions omitted or improperly recorded in the financial records.

    (c) Material gain/loss contingencies requiring accrual or disclosure, including those arising from environmental remediation obligations.

    (d) Events occurring subsequent to the statement of financial position date through the date of this letter requiring adjustment or disclosure in the financial statements.

    (e) Agreements to purchase assets previously sold.

    (f) Restrictions on cash balances or compensating balance agreements.

    (g) Guarantees, whether written or oral, under which the Organization is contingently liable.

14. We have disclosed to you all known instances of noncompliance or suspected noncompliance with laws and regulations whose effects should be considered when preparing financial statements.

15. We have no reason to believe the Organization owes any penalties or payments under the Employer Shared Responsibility Provisions of the Patient Protection and Affordable Care Act nor have we received any correspondence from the IRS or other agencies indicating such payments may be due.

16. We have disclosed to you all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements. The effects of all known actual or possible litigation and claims have been accounted for and disclosed in accordance with accounting principles generally accepted in the United States of America.

17. Adequate provisions and allowances have been accrued for any material losses from:

    (a) Uncollectible receivables, including pledges.

    (b) Purchase commitments in excess of normal requirements or above prevailing market prices.

18. Except as disclosed in the financial statements, the Organization has:

    (a) Satisfactory title to all recorded assets, and they are not subject to any liens, pledges or other encumbrances.

    (b) Complied with all aspects of contractual and grant agreements, for which noncompliance would materially affect the financial statements.

19. The financial statements disclose all significant estimates and material concentrations known to us. Significant estimates are estimates at the statement of financial position date which could change materially within the next year. Concentrations refer to volumes of business, revenues, available sources of supply, or markets for which events could occur which would significantly disrupt normal finances within the next year. Significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable.

20. The fair values of financial and nonfinancial assets and liabilities, if any, recognized in the financial statements or disclosed in the notes thereto are reasonable estimates based on the methods and assumptions used. The methods and significant assumptions used result in measurements of fair value appropriate for financial statement recognition and disclosure purposes and have been applied consistently from period to period, taking into account any changes in circumstances. The significant assumptions appropriately reflect market participant assumptions.

21. We have not been designated as a potentially responsible party (PRP or equivalent status) by the Environmental Protection Agency (EPA) or other cognizant regulatory agency with authority to enforce environmental laws and regulations.

22. With respect to any nonattest services you have provided us during the year, including preparing a draft of the financial statement:

    (a) We have designated a qualified management-level individual to be responsible and accountable for overseeing the nonattest services.

(b) We have established and monitored the performance of the nonattest services to ensure that they meet our objectives.

(c) We have made any and all decisions involving management functions with respect to the nonattest services and accept full responsibility for such decisions.

(d) We have evaluated the adequacy of the services performed and any findings that resulted.

23. We are an organization exempt from income tax under Section 501(c) of the Internal Revenue Code and a similar provision of state law and, except as disclosed in the financial statements, there are no activities that would jeopardize our tax-exempt status or subject us to income tax on unrelated business income or excise tax on prohibited transactions and events.

24. We have identified to you any activities conducted having both fund raising and program or management and general components (joint activities) and have allocated the costs of any joint activities in accordance with the provisions of FASB ASC 958-720-45.

25. We acknowledge that we are responsible for compliance with applicable laws, regulations and provisions of contracts and grant agreements.

26. We have identified and disclosed to you all laws, regulations and provisions of contracts and grant agreements that have a direct and material effect on the determination of amounts in our financial statements or other financial data significant to the audit objectives.

27. We have identified and disclosed to you any violations or possible violations of laws, regulations and provisions of contracts and grant agreements whose effects should be considered for recognition and/or disclosure in the financial statements or for your reporting on noncompliance.

28. We have taken or will take timely and appropriate steps to remedy any fraud, abuse, illegal acts or violations of provisions of contracts or grant agreements that you or other auditors report.

29. We have a process to track the status of audit findings and recommendations.

30. We have identified to you any previous financial audits, attestation engagements, performance audits or other studies related to the objectives of your audit and the corrective actions taken to address any significant findings and recommendations made in such audits, attestation engagements or other studies.

31. We have provided our views on any findings, conclusions and recommendations, as well as our planned corrective actions with respect thereto, to you for inclusion in the findings and recommendations referred to in your report on internal control over financial reporting and on compliance and other matters based on your audit of the financial statements performed in accordance with *Government Auditing Standards*.

32. With regard to supplementary information:

    (a) We acknowledge our responsibility for the presentation of the supplementary information in accordance with the applicable criteria.

    (b) We believe the supplementary information is fairly presented, both in form and content, in accordance with the applicable criteria.

    (c) The methods of measurement and presentation of the supplementary information are unchanged from those used in the prior period.

    (d) We believe the significant assumptions or interpretations underlying the measurement and/or presentation of the supplementary information are reasonable and appropriate.

    (e) If the supplementary information is not presented with the audited financial statements, we acknowledge we will make the audited financial statements readily available to intended users of the supplementary information no later than the date such information and the related auditor's report are issued.

33. We have evaluated whether there are conditions or events known or reasonably knowable, considered in the aggregate, that raise substantial doubt about the Organization's ability to continue as a going concern within one year of the date of this letter without consideration of potential mitigating effects of management's plans not yet fully implemented and concluded substantial doubt does not exist.

Charnay Phaire
Director of Operations

Josh Moreau
Financial Consultant

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