HARLEM SUCCESS ACADEMY CHARTER SCHOOL 2

(A Not-For-Profit Corporation)

FINANCIAL STATEMENTS

JUNE 30, 2010 AND 2009

HARLEM SUCCESS ACADEMY CHARTER SCHOOL 2
(A Not-For-Profit Corporation)
FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

CONTENTS

FRUCHTER ROSEN & COMPANY, P.C.
CERTIFIED PUBLIC ACCOUNTANTS
156 WEST 56TH STREET
NEW YORK, NEW YORK 10019

TEL: (212) 957-3600
FAX: (212) 957-3696

INDEPENDENT AUDITORS' REPORT

TO THE BOARD OF TRUSTEES
HARLEM SUCCESS ACADEMY CHARTER SCHOOL 2

We have audited the accompanying statements of financial position of Harlem Success Academy Charter School 2 (the "School") (a not-for-profit corporation) as of June 30, 2010 and 2009, the related statements of activities, and cash flows for the year ended June 30, 2010 and the period from March 11, 2008 (inception) to June 30, 2009. 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. The prior period summarized comparative information has been derived from the School's 2009 financial statements and, in our report dated October 5, 2009, we expressed an unqualified opinion on those financial statements.

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 audits 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.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the School as of June 30, 2010 and 2009, and the changes in its net assets and its cash flows for the year ended June 30, 2010 and the period from March 11, 2008 (inception) to June 30, 2009, 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 September 15, 2010 on our consideration of the School's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and on compliance and the results of that 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.

Fruchter Rosen & Company P.C.

FRUCHTER ROSEN & COMPANY, P.C.
Certified Public Accountants

New York, New York
September 15, 2010

HARLEM SUCCESS ACADEMY CHARTER SCHOOL 2
(A Not-For-Profit Corporation)
STATEMENTS OF FINANCIAL POSITION
JUNE 30,

	2010	2009
ASSETS		
Current assets:		
Cash and cash equivalents	$ 832,947	$ 784,180
Grants and contracts receivable	121,858	349,976
Prepaid expenses	31,782	33,389
Other current assets	13,709	19,147
Total current assets	1,000,296	1,186,692
Property and equipment, net of accumulated depreciation and amortization of $120,936 and $36,691, respectively	811,429	415,078
Long-term investment	1,000,000	-
Restricted cash	50,469	25,000
TOTAL ASSETS	$ 2,862,194	$ 1,626,770
LIABILITIES AND UNRESTRICTED NET ASSETS		
Current liabilities:		
Accounts payable and accrued expenses	$ 66,602	$ 56,488
Accrued payroll and payroll taxes	169,372	91,234
Due to related parties	174,269	104,438
Total current liabilities	410,243	252,160
Unrestricted net assets	2,451,951	1,374,610
TOTAL LIABILITIES AND UNRESTRICTED NET ASSETS	$ 2,862,194	$ 1,626,770

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

HARLEM SUCCESS ACADEMY CHARTER SCHOOL 2
(A Not-For-Profit Corporation)
STATEMENTS OF ACTIVITIES

	For the year ended June 30, 2010	For the period from March 11, 2008 (date of inception) to June 30, 2009
Revenue and support:		
State and local per pupil operating revenue	$ 4,700,560	$ 2,334,381
Federal grants	495,525	490,640
State and city grants	55,549	150,604
Contributions and private grants	229,110	1,035,050
Donated services	11,756	18,567
Interest and other income	2,500	2,596
Total revenue and support	5,495,000	4,031,838
Expenses:		
Program services		
Regular education	3,346,086	2,030,249
Special education	349,110	204,988
Total program services	3,695,196	2,235,237
Supporting service		
Management and general	722,463	421,991
Total expenses	4,417,659	2,657,228
Changes in unrestricted net assets	1,077,341	1,374,610
Unrestricted net assets - beginning of period	1,374,610	-
Unrestricted net assets - end of period	$ 2,451,951	$ 1,374,610

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

HARLEM SUCCESS ACADEMY CHARTER SCHOOL 2
(A Not-For-Profit Corporation)
STATEMENTS OF CASH FLOWS

	For the year ended June 30, 2010	For the period from March 11, 2008 (date of inception) to June 30, 2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Changes in unrestricted net assets	$ 1,077,341	$ 1,374,610
Adjustments to reconcile changes in unrestricted net assets to net cash provided by operating activities:		
Depreciation and amortization	86,571	36,691
Reclassification of leasehold improvements	(2,326)	-
Changes in certain assets and liabilities:		
Decrease (Increase) in grants and contracts receivable	228,118	(349,976)
Decrease (Increase) in prepaid expense	1,607	(33,389)
Decrease (Increase) in other current assets	5,438	(19,147)
(Increase) in restricted cash	(25,469)	(25,000)
Increase in accounts payable and accrued expenses	10,114	56,488
Increase in accrued payroll and payroll taxes	78,138	91,234
Increase in due to related parties	69,831	104,438
NET CASH PROVIDED BY OPERATING ACTIVITIES	1,529,363	1,235,949
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment	(480,596)	(451,769)
Long-term investment	(1,000,000)	-
NET CASH (USED IN) INVESTING ACTIVITIES	(1,480,596)	(451,769)
NET INCREASE IN CASH AND CASH EQUIVALENTS	48,767	784,180
CASH AND CASH EQUIVALENTS - BEGINNING OF PERIOD	784,180	-
CASH AND CASH EQUIVALENTS - END OF PERIOD	$ 832,947	$ 784,180

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

NOTE 1 - PRINCIPAL BUSINESS ACTIVITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Organization

Harlem Success Academy Charter School 2 (the "School") is a New York State, not-for-profit educational corporation that was incorporated on March 11, 2008 to operate a Charter School pursuant to Article 56 of the Education Law of the State of New York. The School was granted a provisional charter on March 11, 2008 valid for a term of five years and renewable upon expiration by the Board of Regents of the University of the State of New York. The School is dedicated to providing a high quality education to primarily disadvantaged students and to prevent the achievement gap from rising. Classes commenced in Harlem, New York, in August 2008 and the School provided education to approximately 359 students in grades kindergarten through second during the 2009-2010 academic year.

The School shares space with a New York City public school beginning in July 2008. The School is not responsible for rent, utilities, custodial services, maintenance and school safety services other than security related to the school's programs that take place outside the district's school day.

Food and Transportation Services

The New York City Department of Education provides free lunches and transportation directly to a majority of the School's students. Such costs are not included in these financial statements. The School covers the cost of lunches for children not entitled to the free lunches.

Tax Status

The School is exempt from Federal income tax under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(3) and a similar provision under New York State income tax laws. The School has also been classified as an entity that is not a private foundation within the meaning of Section 509(a) and qualifies for deductible contributions as provided in section 170(b)(l)(A)(ii).

Basis of Presentation

The financial statement presentation follows the requirements of the Financial Accounting Standards Board ("FASB") in its Accounting Standards Codification ("ASC") No. 958-205 which provides guidance for the classification of net assets. The amounts for each of the three classes of net assets are based on the existence or absence of donor-imposed restrictions described as follows:

NOTE 1 - PRINCIPAL BUSINESS ACTIVITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Basis of Presentation (Continued)

Unrestricted

Net assets of the School whose use has not been restricted by an outside donor or by law. They are available for any use in carrying out the operations of the School.

Temporarily Restricted

Net assets of the School whose use has been limited by donor-imposed stipulations that either expire with the passage of time or can be fulfilled and removed by actions of the School. When such stipulations end or are fulfilled, such temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities and changes in net assets, as net assets released from restrictions.

Permanently Restricted

Net assets of the School whose use has been permanently limited by donor-imposed restrictions. Such assets include contributions required to be invested in perpetuity, the income from which is available to support charitable purposes designated by the donors.

As of June 30, 2010 and 2009, the School had no temporarily or permanently restricted net assets.

Revenue and Support

Contributions are recognized when the donor makes a Promise to Give to the School that is, in substance, unconditional. Grants and other contributions of cash are reported as temporarily restricted support if they are received with donor stipulations. Restricted contributions and grants that are made to support the school's current year activities are recorded as unrestricted revenue. Contributions of assets other than cash are recorded at their estimated fair value.

Revenue from the state and local governments resulting from the School's charter status and based on the number of students enrolled is recorded when services are performed in accordance with the charter agreement. Federal and other state and local funds are recorded when expenditures are incurred and billable to the government agencies.

NOTE 1 - PRINCIPAL BUSINESS ACTIVITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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 revenue and expenses during the reporting period. Accordingly, actual results could differ from those estimates.

Cash and Cash Equivalents
For the purpose of the Statement of Cash Flows, the School considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents.

Concentration of Credit Risk
Financial instruments which potentially subject the School to concentrations of credit risk are cash and cash equivalents. The School places its cash and cash equivalents on deposit in what it believes to be highly credited financial institutions. Cash balances may exceed the FDIC insured levels of $250,000 per institution at various times during the year. The School believes that there is little risk in any losses and has not experienced any losses in such accounts.

Restricted Cash
Under the provisions of its charter, the School established an escrow account to pay for legal and audit expenses that would be associated with a dissolution should it occur.

Property and Equipment
Purchased property and equipment are recorded at cost. Property and equipment acquired with certain government funding are recorded as expenses pursuant to the terms of the contract, in which ownership of such property and equipment is retained by the funding source. Maintenance and repairs are expensed as incurred. No depreciation is recorded on construction-in-progress until property and equipment is placed into service. Depreciation and amortization is provided on the straight line method over the estimated useful lives as follows:

Equipment	5 years
Furniture and fixtures	7 years
Website development	3 years
Software	3 years
Leasehold improvements	15 years

Deferred Revenue
The School records grant revenue as deferred revenue until it is expended for the purpose of the grant, at which time it is recognized as revenue.

NOTE 1 - PRINCIPAL BUSINESS ACTIVITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Recent Accounting Pronouncements

In June 2009, the FASB issued FASB ASC 105, Generally Accepted Accounting Principles, which establishes the FASB Accounting Standards Codification as the sole source of authoritative generally accepted accounting principles. Pursuant to the provisions of FASB ASC 105, the School has updated references to GAAP in its financial statements issued for the year ending June 30, 2010. The adoption of FASB ASC 105 did not impact the School's financial position or results of operations.

The School adopted the provisions of ASC 740, Income Taxes, as of July 1, 2009. This standard clarifies the accounting for uncertainty in income taxes recognized in an organization's financial statements and prescribes a recognition threshold and measurement standard for the financial statement recognition and measurement of income tax position taken or expected to be taken in a tax return. The School has reviewed its tax positions for open tax years and has concluded that the adoption of this standard did not have an impact on the financial statements of the School.

NOTE 2 - GRANTS AND CONTRACTS RECEIVABLE

Grants and contracts receivable consist of federal and city entitlements and grants. The School expects to collect these receivables within one year.

NOTE 3 - FAIR VALUE MEASUREMENTS

FASB ASC 820-10, *Fair Value Measurements,* establishes a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy under FASB ASC 820-10 are described as follows:

- Level 1 – Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the plan has the ability to access.

- Level 2 – Inputs other than quoted prices included in level 1 that are observable for the asset or liability, either directly or indirectly including inputs in markets that are not considered to be active.

- Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

NOTE 3 - FAIR VALUE MEASUREMENTS (Continued)

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

The primary uses of fair value measures in the School's financial statements are:

- initial measurement of noncash gifts, including gifts of investment assets and unconditional promises to give.
- recurring measurement of investments.

The School's investments at June 30, 2010, consisted of a certificate of deposit in the amount of $1,000,000, which is classified as level 1 in the fair value hierarchy. The School had no investments at June 30, 2009.

NOTE 4 - PROPERTY AND EQUIPMENT

Property and equipment consist of the following at June 30,:

	2010	2009
Equipment	$ 289,184	$ 130,220
Furniture and fixture	236,658	85,717
Website design	5,000	-
Software	5,823	5,204
Leasehold improvements	395,700	230,628
	932,365	451,769
Less: Accumulated depreciation and amortization	120,936	36,691
	$ 811,429	$ 415,078

Depreciation and amortization expense was $86,571 and $36,691 for the year ended June 30, 2010 and the period from March 11, 2008 (inception) to June 30, 2009, respectively.

NOTE 5 - RELATED PARTY TRANSACTIONS

The School is an affiliate of Success Charter Network (the "Network"), a not-for-profit charter management organization dedicated to helping start and manage charter schools, provide management and other administrative support services to the schools.

Pursuant to the terms of the Academic and Business Service Agreement by and between the Network and the School, dated March 2008, the Network shall provide educational management and operational services to the School. As compensation to the Network for these services rendered, the School shall pay to the Network an amount each year equal to the total full-time equivalent enrollment of students in the School multiplied by "the per pupil fee" of $1,243. The 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 in the New York City school district commencing with and including the 2008-2009 school year. The per pupil fee was $1,243 for the year ended June 30, 2010 and the period from March 11, 2008 (inception) to June 30, 2009. For operational efficiency and purchasing power, the School also shares expenses with three other charter schools related by common management.

For the year ended June 30, 2010, the School incurred $447,064 in management fees and there were no material transactions between the School and the related charter schools. The balance due to the Network from the School at June 30, 2010 amounted to $174,269. This balance represents expenses paid by the Network on behalf of the School. The School fully repaid this balance prior to the issuance of this report.

For the period from March 11, 2008 (inception) to June 30, 2009, the School incurred $227,294 in management fees. The balance due to the Network from the School at June 30, 2009 amounted to $103,808. This balance consists of $144,421 in School expenses paid by the Network on behalf of the School, ($50,000) in private contributions made payable to the Network, and $9,387 in management fees. The School repaid the entire balance during the year ended June 30, 2010. At June 30, 2009, balance due to one of the charter schools was $630, which was paid in full during the year ended June 30, 2010.

NOTE 6 - CONTINGENCY

Certain grants and contracts may be subject to audit by the funding sources. Such audits might result in disallowances of costs submitted for reimbursements. 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.

NOTE 7 - REVENUE CONCENTRATION

The School receives a substantial portion of its support and revenue from the New York City Department of Education. If the charter school laws were modified, reducing or eliminating these revenues, the School's finances could be materially adversely affected.

NOTE 8 - FUNCTIONAL ALLOCATION OF EXPENSE

Directly identifiable expenses are charged to programs and supporting services. Expenses related to more than one function are charged to programs and supporting services on the basis of periodic time and expense studies. Management and general expense includes those expenses that are not directly identifiable with any other specific function, but provide for the overall support and direction of the School.

NOTE 9 - DONATED SERVICES

Donated services are recognized as contributions in accordance with FASB ASC 605, "Accounts for Contributions Received and Contributions Made," if the services (a) create or enhance non-financial assets or (b) require specialized skills, are performed by people with those skills, and would otherwise be purchased by the School.

One individual provided legal services to the School at no charge. The value of these services meets the criteria for recognition in the financial statements and was recorded at fair value of $5,000 and $18,000 for the year ended June 30, 2010 and the period from March 11, 2008 (inception) to June 30, 2009, respectively. In addition, $6,756 and $567 of in-kind advertising was donated to the School during the year ended June 30, 2010 and the period from March 11, 2008 (inception) to June 30, 2009, respectively.

NOTE 10 - RETIREMENT PLAN

The School maintains a pension plan qualified under Internal Revenue Code 403(b), for the benefit of its eligible employees. Under the plan, the School will match employee contributions up to 3% of annual compensation. Employee match for the year ended June 30, 2010 and the period from March 11, 2008 (inception) to June 30, 2009 amounted to $19,411 and $12,072, respectively.

FRUCHTER ROSEN & COMPANY, P.C.
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156 WEST 56TH STREET
NEW YORK, NEW YORK 10019

TEL: (212) 957-3600
FAX: (212) 957-3696

INDEPENDENT AUDITORS' REPORT ON ADDITIONAL INFORMATION

TO THE BOARD OF TRUSTEES
HARLEM SUCCESS ACADEMY CHARTER SCHOOL 2

Our report on our audits of the basic financial statements of Harlem Success Academy Charter School 2 (a not-for-profit corporation) as of June 30, 2010 and 2009, appears on Page 1. We conducted our audits in accordance with auditing standards generally accepted in the United States of America for the purpose of forming an opinion on the basic financial statements taken as a whole. The schedule of functional expenses is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements as a whole.

Fruchter Rosen & Company PC
FRUCHTER ROSEN & COMPANY, P.C.
Certified Public Accountants

New York, New York
September 15, 2010

HARLEM SUCCESS ACADEMY CHARTER SCHOOL 2
(A Not-For-Profit Corporation)
SCHEDULE OF FUNCTIONAL EXPENSES

	For the year ended June 30, 2010					For the period from March 11, 2008 (date of inception) to June 30, 2009
	Regular Education	Special Education	Total Program Service	Management and General	Total	
Salaries	$ 1,943,487	$ 202,771	$ 2,146,258	$ 175,328	$ 2,321,586	$ 1,215,776
Payroll taxes and employee benefits	402,616	42,006	444,622	36,323	480,945	257,040
Professional development	44,843	4,680	49,523	-	49,523	48,779
Legal	-	-	-	15,596	15,596	20,420
Audit and accounting	-	-	-	12,750	12,750	14,861
Professional fees - other	21,681	2,262	23,943	1,956	25,899	26,813
Travel and entertainment	9,042	943	9,985	816	10,801	6,215
Student food service	52,560	5,484	58,044	-	58,044	43,383
Field trips	26,448	2,760	29,208	-	29,208	18,467
Instructional supplies and textbooks	323,379	33,740	357,119	-	357,119	280,723
Management fee	-	-	-	447,064	447,064	227,294
Teacher recruitment	63,244	6,598	69,842	-	69,842	64,063
Student recruitment	42,790	4,464	47,254	-	47,254	74,078
Marketing	7,767	811	8,578	-	8,578	25,128
Consulting	14,417	1,504	15,921	1,301	17,222	6,472
Uniforms	12,933	1,349	14,282	-	14,282	16,505
Office supplies	43,933	4,584	48,517	3,962	52,479	36,963
Computer supplies	17,719	1,849	19,568	1,599	21,167	26,678
School culture	9,411	982	10,393	-	10,393	17,360
Special events	10,782	1,125	11,907	973	12,880	12,366
Equipment rental	6,663	695	7,358	601	7,959	4,535
Student assessments	24,162	2,521	26,683	-	26,683	11,542
Telephone and internet services	57,329	5,981	63,310	5,172	68,482	85,378
Postage and delivery	19,109	1,994	21,103	1,723	22,826	21,476
Insurance	23,525	2,454	25,979	2,123	28,102	24,291
Facilities expense	65,801	6,865	72,666	5,936	78,602	13,425
Information technology	24,502	2,556	27,058	2,211	29,269	20,403
Depreciation and amortization	72,472	7,561	80,033	6,538	86,571	36,691
Miscellaneous	5,471	571	6,042	491	6,533	103
Total	$ 3,346,086	$ 349,110	$ 3,695,196	$ 722,463	$ 4,417,659	$ 2,657,228

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TEL: (212) 957-3600
FAX: (212) 957-3696

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
HARLEM SUCCESS ACADEMY CHARTER SCHOOL 2

We have audited the financial statements of Harlem Success Academy Charter School 2 (the "School") as of and for the year ended June 30, 2010, and have issued our report thereon dated September 15, 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 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 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 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.

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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to the management of the School in a separate letter dated September 15, 2010.

This report is intended solely for the information and use of management, Board of Trustees, federal, state and local awarding agencies, The Charter State Schools Institute of the State University of New York, The State Education Department of the State University of New York, and others within the School and is not intended to be and should not be used by anyone other than these specified parties.

Fruchter Rosen & Company P.C.

FRUCHTER ROSEN & COMPANY, P.C.
Certified Public Accountants

New York, New York
September 15, 2010