Hillcrest Academy

Financial Performance Framework Response

8/1/2014

Arizona State Board for Charter Schools
1616 West Adams Street Suite 170
Phoenix, Arizona 85007

To Whom It May Concern:

The IRS Taxes have been paid. Attached is a copy of the checks that were cut and mailed to the IRS. Once we have a copy of canceled checks we will send to ASBCS Staff.

I hope that this letter helps explain what we are trying to accomplish. If you have any questions please feel free to give me a call at 480-399-0655

Sincerely,

Ryan Christensen
President

4710 E Baseline Road • Mesa • Arizona • Phone: 480.325.8950 • Fax: 480.353.2832
www.hillcresthawks.com

5154

Hillcrest Academy, Inc.
4710 East Baseline Road
Mesa, Arizona 85206
480-924-0888

MIDFIRST BANK
PHOENIX, AZ 85016

91-8744-1221

EZShield™ Check Fraud Protection for Business

8/7/2014

PAY TO THE ORDER OF United States Treasury $ **18,201.73

Eighteen Thousand Two Hundred One and 73/100********** DOLLARS

Security features. Details on back.

United States Treasury
Internal Revenue Service
Ogden, UT 84201-0039

MEMO 86-0658004 - 2011 - Q4 Final Payoff

AUTHORIZED SIGNATURE

⑈005154⑈ ⑆122187445⑆ ⑈2453007417⑈

Hillcrest Academy, Inc

5154

United States Treasury 8/7/2014
2011 - Q4 Final Payoff 18,201.73

MidFirst Checking 741 86-0658004 - 2011 - Q4 Final Payoff 18,201.73

Hillcrest Academy, Inc.

5154

United States Treasury 8/7/2014
2011 - Q4 Final Payoff 18,201.73

MidFirst Checking 741 86-0658004 - 2011 - Q4 Final Payoff 18,201.73

PRODUCT SSLT104 USE WITH 91663 ENVELOPE

5155

Hillcrest Academy, Inc.
4710 East Baseline Road
Mesa, Arizona 85206
480-924-0888

MIDFIRST BANK
PHOENIX, AZ 85016

91-8744-1221

EZShield™ Check Fraud Protection for Business

8/7/2014

PAY TO THE ORDER OF United States Treasury $ **27,875.70

Twenty-Seven Thousand Eight Hundred Seventy-Five and 70/100********** DOLLARS

Security features. Details on back.

United States Treasury
Internal Revenue Service
Ogden, UT 84201-0039

AUTHORIZED SIGNATURE

MEMO 86-0658004 - 2012 - Q1 Final Payoff

⑈005155⑈ ⑆122187445⑆ ⑈2453007417⑈

Hillcrest Academy, Inc

5155

United States Treasury 8/7/2014
2012 - Q1 Final Payoff 27,875.70

MidFirst Checking 741 86-0658004 - 2012 - Q1 Final Payoff 27,875.70

Hillcrest Academy, Inc.

5155

United States Treasury 8/7/2014
2012 - Q1 Final Payoff 27,875.70

MidFirst Checking 741 86-0658004 - 2012 - Q1 Final Payoff 27,875.70

PRODUCT SSLT104 USE WITH 91663 ENVELOPE

5156

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4710 East Baseline Road
Mesa, Arizona 85206
480-924-0888

MIDFIRST BANK
PHOENIX, AZ 85016

91-8744-1221

EZShield™ Check Fraud Protection for Business

8/7/2014

PAY TO THE ORDER OF United States Treasury $ **14,744.32

Fourteen Thousand Seven Hundred Forty-Four and 32/100********** DOLLARS

Security features. Details on back.

United States Treasury
Internal Revenue Service
Ogden, UT 84201-0039

MEMO 86-0658004 - 2012 - Q2 Final Payoff

AUTHORIZED SIGNATURE

⑈005156⑈ ⑆122187445⑆ ⑈2453007417⑈

Hillcrest Academy, Inc

5156

United States Treasury 8/7/2014

2012 - Q2 Final Payoff 14,744.32

MidFirst Checking 741 86-0658004 - 2012 - Q2 Final Payoff 14,744.32

Hillcrest Academy, Inc.

5156

United States Treasury 8/7/2014

2012 - Q2 Final Payoff 14,744.32

MidFirst Checking 741 86-0658004 - 2012 - Q2 Final Payoff 14,744.32

PRODUCT SSLT104 USE WITH 91663 ENVELOPE

5157

Hillcrest Academy, Inc.
4710 East Baseline Road
Mesa, Arizona 85206
480-924-0888

MIDFIRST BANK
PHOENIX, AZ 85016

91-8744-1221

EZShield™ Check Fraud Protection for Business

8/7/2014

PAY TO THE ORDER OF United States Treasury $ **1,562.11

One Thousand Five Hundred Sixty-Two and 11/100********** DOLLARS

Security features. Details on back.

United States Treasury
Internal Revenue Service
Ogden, UT 84201-0039

MEMO 86-0658004 - 2012 - Q4 Final Payoff

AUTHORIZED SIGNATURE

⑈005157⑈ ⑆122187445⑆ ⑈2453007417⑈

Hillcrest Academy, Inc

5157

United States Treasury 8/7/2014

2012 - Q4 Final Payoff	1,478.02
2012 - Q4 Final Payoff, balance to reconcile with stat	84.09

MidFirst Checking 741 86-0658004 - 2012 - Q4 Final Payoff 1,562.11

Hillcrest Academy, Inc.

5157

United States Treasury 8/7/2014

2012 - Q4 Final Payoff	1,478.02
2012 - Q4 Final Payoff, balance to reconcile with stat	84.09

MidFirst Checking 741 86-0658004 - 2012 - Q4 Final Payoff 1,562.11

PRODUCT SSLT104 USE WITH 91663 ENVELOPE

Near Term Indicators

1a. Going Concern

The Audited Financials for Fiscal Year 2013 included a Going Concern Finding.

The Going Concern Finding for 2013 is directly attributable to recording a Net Operating Loss for the same period. This was the result of the factors explained under Net Income, and will reoccur again in the 2013-2014 fiscal year.

The Audited Financials for Fiscal Year 2014 (not complete at this time) are likely to included a Going Concern Finding.

The likely Going Concern Finding for 2014 is directly attributable to recording a Net Operating Loss for the same period. This was the result of the factors explained under Net Income, and will not reoccur past the 2013-2014 fiscal year.

As indicated in Audited Financials for Fiscal Year 2013 (Note 14), Management of the school developed a plan to reduce expenses wherever possible, increase student enrollment, borrow additional funds if necessary, and restructure debt. Note 14 of the Audited Financials for Fiscal Year 2013 goes on to state that the ability of the school to continue as a going concern is dependent upon it's success with the above mentioned endeavors.

The school was successful in its endeavor to restructure debt and provide for the availability of suitable facilities (see Settlement Statement for Facilities Purchase). Additionally, the school was awarded a private grant to be used for the purpose of securing new facilities (see Grant Award Letter). Based on the revenues generated through both the Facilities Purchase (see Settlement Statement for Facilities Purchase) and the private grant award (see Grant Award Letter), the school will satisfy all current liabilities (see Balance Sheet Comparison). These factors, combined with recording a positive Net Income through the measures described under Net Income 2a. ensures that the school will avoid a repeat Going Concern Finding in FY 2015.

Administrative Oversight & Governance

Budgeted revenue and spending as compared to actual activities are reviewed on a day to day basis by Administration. All adjustments to spending in response to anticipated underperformance in revenue or projected overspending are also made on a weekly basis by Administration. All unscheduled expenses (expenses not included in the school's operating budget at the beginning of the operating period) are first reviewed to establish whether or not budget capacity exists for the expenditure prior to authorization.

Upon review by administration, should an unscheduled expense be deemed necessary, budget capacity will be moved from an expense line where it is not needed to the expense line where the unscheduled expense will be booked, prior to encumbrance of the expense. The school has also established additional contingency as part of each expense object grouping. This funding can be used as a last resort for unscheduled expenses occurring later in the fiscal year that are deemed necessary but cannot be paid for through reallocation of budget capacity from another expense line.

Budget performance is reviews weekly by the Corporate Executives (President, Vice President and Secretary), who also monitor and report to the Board of Directors the Statements of Activities, Budget Performance, and statement of Cash Flows as part of their weekly meetings.

Budget performance is reviewed quarterly by the Board of Directors, who also monitors the Statement of Activities, Budget Performance, and Statement of Cash Flows as part of their quarterly regular session meetings.

Sustainability Indicators

2a. Net Income

The Audited Financials for Fiscal Year 2013 state a Change in Net Assets of ($705,139).

The net operating loss for FY 2013 was the result of a combination of factors that will reoccur again in the 2013-2014 fiscal year, and are explained below.

The Preliminary Unaudited Financials for Fiscal Year 2014 state a Change in Net Assets of ($1,287,447), (see Profit & Loss FY 2014).

The net operating loss for FY 2014 was the result of a combination of factors that will not reoccur past the 2013-2014 fiscal year, and are explained below.

Increased Spending in FY 2013 and FY 2014 Related to debt restructuring and a Facilities Project

From FY 2011 through FY 2012 the previous board members (the "DCS Board") of the Charter were experiencing financial difficulties.

These financial difficulties were a result that the DCS Board incorrectly identified the market they were moving to in 2010 and continued to identify themselves as a low income school participating in a national free and reduced lunch program, with an emphasis in Special Needs Children. This marketing effort, combined with an inferior facility to that of surrounding competitors, caused enrollment to decline over time as existing students moved to other schools. New enrollment was minimal because the DCS Board targeted its marketing toward a very small percentage of the population in the area.

The DCS Board acknowledged the severe financial difficulties the organization was experiencing and, consequently, the DCS Board sought cash flow assistance from outside sources. As a result, the DCS Board approved the taking of certain hard money loans the interest costs associated with which were beyond the ability of the DCS Board to repay. Facing closure of the School, the management approached Lawson Financial Corporation (the "*Bondholder Representative*") in its capacity as bondholder representative of the Series 2010 Bonds to seek additional funding, counsel and a potential restructuring of the Series 2010 Bonds. After several attempts to work with the management, the DCS Board acknowledged that the Bondholder Representative possessed the remedy of replacing the management and the persons constituting the DCS Board. All but one of the members of the DCS Board resigned and, in 2012, the Bondholder Representative replaced the previous DCS Board members with the current Corporate Board members (the "*Hillcrest Board*"). With the Hillcrest Board in place, the Bondholder Representative continued to work cooperatively with the Hillcrest Board.

Once established, the Hillcrest Board went into immediate action to address and correct the problems of previous leadership. Within the first four months of institution of the new Hillcrest Board, the School has experienced a complete turnaround. The Hillcrest Board found and fixed many previously existing issues involving the budget, curriculum, teaching staff, enrollment, and academic accountability. These changes have attracted surrounding students and families to the School. The School has experienced an overall increase in academic performance and student enrollment.

Consequently, in December of the 2012-2013 school year the school began to record much higher than normal operating costs related to facilities, improvements, and staffing as they began positioning to grow substantially in the 2014-2015 school year. This resulted in a Change in Net Assets of ($705,139), (see Audited Financial Statements for FY 2013).

The Hillcrest Board made the decision to facilitate growth and to operate in the negative during the 2013-2014 fiscal year (see Profit & Loss FY 2014), relying on short term loans and lines of credit that were available to the school at the time (see Audited Financials FY 2013 - Note 9 - Lines of Credit). This decision was made with the knowledge that these short term loans would not only keep the school's operations in tact, but would be satisfied in full upon entering into the agreement to secure the new facilities referenced above (see Facilities Settlement Statement).

This decision allowed the new administrative staff to use the 2013-2014 school year as a planning year to establish the operational processes upon which to build a solid foundation, and to ensure the success of the 2014-2015 academic year and growth.

Increased Funding and Positive Net Income in 2015 Related to Facilities Project

The school's facilities plan is complete, and receipt of funding is well underway (see Facilities Settlement Statement). This will ensure a positive Functional Net Operating Income for FY 2015 based on a substantial increase in local funding via the award of a local grant designed to be used for securing suitable facilities (see Grant Award Letter), as well as the anticipated additional income that will coincide with increased student enrollment driven by the school's new facilities.

Based on current budgetary projections, the school should record a Functional Net Income in excess of $725,000 in FY 2015 (see Profit & Loss Projection FY 2015). Based on the school's ongoing financial plan, this will serve to ensure the sustainability of the organization, and would increase the school's rating to "Meets Standard" for item 2a. Net Income.

Administrative Oversight & Governance

Budgeted revenue and spending as compared to actual activities are reviewed on a day to day basis by Administration. All adjustments to spending in response to anticipated underperformance in revenue or projected overspending are also made on a weekly basis by Administration. All unscheduled expenses (expenses not included in the school's operating budget at the beginning of the operating period) are first reviewed to establish whether or not budget capacity exists for the expenditure prior to authorization.

Upon review by administration, should an unscheduled expense be deemed necessary, budget capacity will be moved from an expense line where it is not needed to the expense line where the unscheduled expense will be booked, prior to encumbrance of the expense. The school has also established additional contingency as part of each expense object grouping. This funding can be used as a last resort for unscheduled expenses occurring later in the fiscal year that are deemed necessary but cannot be paid for through reallocation of budget capacity from another expense line.

Budget performance is reviews weekly by the Corporate Executives (President, Vice President and Secretary), who also monitor and report to the Board of Directors the Statements of Activities, Budget Performance, and statement of Cash Flows as part of their weekly meetings.

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2c. Fixed Charge Coverage Ratio

The Audited Financials for Fiscal Year 2013 indicate a Fixed Charge Coverage Ratio of -.41.

The net operating loss recorded in FY 2013 led to the fixed charge coverage ratio deficit. This was directly attributable to the causes outlined in the response to item 2a. Net Income: increased expenses related to facilities, improvements, and administrative staffing.

The school has sufficient cash available (in the form of short term lines of credit and loans) to augment cash flow to fund the fixed charge deficit for the foreseeable future (see Note 9 - Lines of Credit, Audited Financials FY 2013).

The Preliminary Unaudited Financials for Fiscal Year 2014 indicate a Fixed Charge Coverage Ratio of -2.17 (see Fixed Charge Coverage Ration Comparison).

The net operating loss recorded in FY 2014 led to the fixed charge coverage ratio deficit. This is directly attributable to the causes outlined in the response to item 2a. Net Income: increased expenses related to facilities, improvements, and administrative staffing.

The school has sufficient cash available (in the form of short term lines of credit and loans) to augment cash flow to fund the fixed charge deficit for the foreseeable future (see Note 9 - Lines of Credit, Audited Financials FY 2013).

Net Income for FY 2015 will be significantly improved over previous years (see Profit & Loss Projection FY 2015) due to significantly increased local revenue from donations, and increased student enrollment driven by the new facilities.

Based on current budgetary projections, the school should record a Functional Net Income in excess of $725,000 in FY 2015 (see Profit & Loss Projection FY 2015). Should the school perform to plan in FY 2015, a Change in Net Assets in excess of $725,000 will be achieved, resulting in a Fixed Charge Coverage Ratio of 1.70 (see Fixed Charge Coverage Ratio Comparison). This would increase the school's rating to "Meets Standard" for item 2c. Fixed Charge Coverage Ratio.

Administrative Oversight & Governance

Budgeted revenue and spending as compared to actual activities are reviewed on a day to day basis by Administration. All adjustments to spending in response to anticipated underperformance in revenue or projected overspending are also made on a weekly basis by Administration. All unscheduled expenses (expenses not included in the school's operating budget at the beginning of the operating period) are first reviewed to establish whether or not budget capacity exists for the expenditure prior to authorization.

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HILLCREST ACADEMY, INC.

FINANCIAL STATEMENTS AND
INDEPENDENT AUDITOR'S REPORTS

FOR THE YEARS ENDED JUNE 30, 2013 AND 2012

HILLCREST ACADEMY, INC.
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Brett V. Backlund CPA, PC

1757 East Baseline Road • Suite 137 • Gilbert, Arizona 85233
Phone (480) 361-4150 • Fax (480) 361-6840 • brett@bvbcpa.com

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Independent Auditor's Report

Board of Directors
Hillcrest Academy, Inc.

Report on the Financial Statements
We have audited the accompanying financial statements of Hillcrest Academy, Inc. (a nonprofit organization), which comprise the statements of financial position as of June 30, 2013 and 2012, and the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

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

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 Hillcrest Academy, Inc. as of June 30, 2013 and 2012, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis-of-Matter Regarding Going Concern

The accompanying financial statements have been prepared assuming that the School will continue as a going concern. As discussed in Note 14 to the financial statements, the School has suffered recurring significant deficits in unrestricted net assets and has a net deficiency in net assets that raise substantial doubt about its ability to continue as a going concern. Management's plans regarding those matters also are described in Note 14. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to that matter.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated February 5, 2014, 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 grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and 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* in considering the School's internal control over financial reporting and compliance.

Brett V. Backlund, CPA, PC

Brett V. Backlund, CPA, PC
Gilbert, Arizona
February 5, 2014

HILLCREST ACADEMY, INC.
STATEMENTS OF FINANCIAL POSITION
JUNE 30, 2013 AND 2012

	2013	2012
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 18,965	$ 8,499
Due from governmental agencies	54,189	23,073
Total Current Assets	73,154	31,572
Non-Current Assets:		
Cash held by trustee	8,212	-
Refundable deposits	5,966	5,520
Deferred financing costs, net	493,179	511,444
Property and equipment, net	2,639,432	2,600,964
Total Non-Current Assets	3,146,789	3,117,928
TOTAL ASSETS	$ 3,219,943	$ 3,149,500
LIABILITIES AND NET ASSETS		
Current Liabilities:		
Accounts payable and accrued expenses	$ 125,452	$ 109,130
Accrued payroll and related benefits	43,957	93,942
Accrued interest payable	19,542	-
Due to others	16,568	-
Lines of credit	771,961	49,981
Capital leases payable, current portion	6,792	-
Loans payable, current portion	-	10,000
Loans payable to related parties, current portion	11,423	16,700
Notes payable, current portion	150,000	53,467
Notes payable to IDA, current portion	45,833	-
Total Current Liabilities	1,191,528	333,220
Long-Term Liabilities:		
Capital leases payable, less current portion	10,754	-
Notes payable, less current portion	-	96,533
Notes payable to IDA, less current portion	3,616,846	3,613,793
Total Long-Term Liabilities	3,627,600	3,710,326
TOTAL LIABILITIES	4,819,128	4,043,546
NET ASSETS		
Unrestricted:		
Undesignated	(1,599,185)	(906,786)
Designated for classroom site fund	-	12,740
TOTAL NET ASSETS/(DEFICIT)	(1,599,185)	(894,046)
TOTAL LIABILITIES AND NET ASSETS	$ 3,219,943	$ 3,149,500

See accompanying notes to financial statements.

HILLCREST ACADEMY, INC.
STATEMENTS OF ACTIVITIES
FOR THE YEARS ENDED JUNE 30, 2013 AND 2012

	2013	2012
UNRESTRICTED NET ASSETS		
Unrestricted Revenues and Gains:		
Revenue from local sources	$ 29,379	$ 206,805
Revenue from state sources	527,834	770,867
Revenue from federal sources	84,718	113,216
Total Unrestricted Revenues and Gains	641,931	1,090,888
Total Unrestricted Revenues, Gains, and Other Support	641,931	1,090,888
Expenses and Losses:		
Personal services - salaries	47,778	419,156
Personal services - benefits	30,586	40,848
Purchased professional and technical services	469,975	99,575
Purchased property services	105,006	35,072
Other purchased services	65,769	75,595
Supplies	99,903	33,411
Depreciation and amortization	153,274	140,755
Other expenses and losses	374,779	415,094
Total Expenses and Losses	1,347,070	1,259,506
CHANGES IN UNRESTRICTED NET ASSETS	(705,139)	(168,618)
CHANGES IN NET ASSETS	(705,139)	(168,618)
NET ASSETS/(DEFICIT) AT BEGINNING OF YEAR	(894,046)	(725,428)
NET ASSETS/(DEFICIT) AT END OF YEAR	$ (1,599,185)	$ (894,046)

See accompanying notes to financial statements.

HILLCREST ACADEMY, INC.
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2013 AND 2012

	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Changes in net assets	$ (705,139)	$ (168,618)
Adjustments to reconcile changes in net assets to net cash provided/(used) by operating activities:		
Depreciation and amortization	153,274	140,755
(Increase)/decrease in operating assets:		
Due from governmental agencies	(31,116)	42,138
Refundable deposits	(446)	-
Increase/(Decrease) in operating liabilities:		
Accounts payable and accrued expenses	16,322	(112,675)
Accrued payroll and related benefits	(49,985)	93,942
Accrued interest payable	19,542	-
Due to others	16,568	-
NET CASH PROVIDED/(USED) BY OPERATING ACTIVITIES	(580,980)	(4,458)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property and equipment	(153,100)	(1,249)
NET CASH PROVIDED/(USED) BY INVESTING ACTIVITIES	(153,100)	(1,249)
CASH FLOWS FROM FINANCING ACTIVITIES		
Cash held by trustee	8,212	-
Net borrowing/(repayment) on lines of credit	721,980	(520)
Repayments on capital leases payable	(2,831)	(21,210)
Proceeds from notes and loans payable	8,482	515,263
Repayments on notes and loans payable	(25,270)	(479,327)
Proceeds from notes payable to IDA	33,973	-
NET CASH PROVIDED/(USED) BY FINANCING ACTIVITIES	744,546	14,206
NET CHANGES IN CASH AND CASH EQUIVALENTS	10,466	8,499
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	8,499	-
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 18,965	$ 8,499
SUPPLEMENTAL INFORMATION		
Noncash investing and financing activities:		
Acquisition of equipment through capital leases payable	$ 20,376	$ -
Interest paid	$ 331,465	$ 361,036

See accompanying notes to financial statements.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Hillcrest Academy, Inc. (the "School") is an Arizona not-for-profit organization located in Mesa, Arizona. Effective April 19, 2013, the School changed its name from DCS Partners, Inc., d.b.a. Destiny Community School to Hillcrest Academy, Inc. The School was established in 1997 under a charter contract with the Arizona State Board for Charter Schools (Sponsor), which mandates policies and operational guidelines. The School renewed its charter contract with its Sponsor on January 18, 2012 with an effective date of July 1, 2012. The new charter contract is for a term of twenty-years with an ending date of June 30, 2032. The School endeavors to provide a positive, individualized curriculum designed to maximize students' potential and success. The School provides educational services to approximately 80 students in kindergarten through eighth grades, and is funded primarily through the State of Arizona based on student membership.

The School prepares its financial statements in accordance with generally accepted accounting principles promulgated in the United States of America (U.S. GAAP) for not-for-profit organizations. The significant accounting and reporting policies used by the School are described below to enhance the usefulness and understandability of the financial statements.

Cash and Cash Equivalents – Cash and cash equivalents can be short term, interest bearing, highly liquid investments with original maturities of three months or less, unless the investments are held for meeting restrictions of a capital nature.

Gifts-in-Kind Contributions – The School periodically receives contributions in a form other than cash or investments. If the School receives a contribution of property and equipment, the contributed asset is recognized as an asset at its estimated fair value at the date of gift, provided that the value of the asset and its estimated useful life meets the School's capitalization policy. Donated use of facilities is reported as contributions and as expenses at the estimated fair value of similar space for rent under similar conditions. If the use of the space is promised unconditionally for a period greater than one year, the contribution is reported as a contribution and an unconditional promise to give at the date of gift, and the expense is reported over the term of use. Donated supplies are recorded as contributions at the date of gift and as expenses when the donated items are placed into service or distributed.

The School may benefit from personal services provided by a substantial number of volunteers. Those volunteers have donated significant amounts of time and services in the School's program operations. However, the majority of the contributed services do not meet the criteria for recognition in the financial statements. GAAP allows recognition of contributed services only if (a) the services create or enhance non-financial assets, or (b) the services would have been purchased if not provided by contribution, require specialized skills, and are provided by individuals possessing those skills. No amounts have been reflected in the financial statements for donated services since they do not meet the criteria for recognition.

Grant Revenue – Grant revenue is recognized when the qualifying costs are incurred for cost-reimbursement grants or contracts or when a unit of service is provided for performance grants. Grant revenue from federal agencies is subject to independent audit under the Office of Management and Budget Circular A-133 and review by grantor agencies. The review could result in the disallowance of expenditures under the terms of the grant or reductions of future grant funds. Based on prior experience, the School's management believes that costs ultimately disallowed, if any, would not materially affect the financial position of the organization.

Property and Equipment – Land, buildings, and improvements with a cost of $3,000 or more and vehicles, furniture, and equipment with both a cost of $1,000 or more and an estimated useful life of one year or more are capitalized. Assets are stated at cost. Assets donated are recorded at their estimated fair market value as of the date received. Repairs and maintenance that does not significantly increase the useful life of the asset are expensed as incurred. Amortization of buildings and improvements and depreciation of furniture and equipment are provided on a straight–line basis over the useful life of the respective assets, which ranges from 2 to 30 years. Property and equipment are reviewed for impairment when a significant change in the asset's use or another indicator of possible impairment is present. No impairment losses were recognized in the financial statements during the current period.

Net Assets – The financial statements can report net assets and changes in net assets in three classes that are based upon the existence or absence of restrictions on use that are placed by its donors, as follows:

- Unrestricted Net Assets – Unrestricted net assets are resources available to support operations. The only limits on the use of unrestricted net assets are the broad limits resulting from the nature of the organization, the environment in which it operates, the purposes specified in its corporate documents and its application for tax-exempt status, and any limits resulting from contractual agreements with creditors and others that are entered into in the normal course of its operations.

- Temporarily Restricted Net Assets – Temporarily restricted net assets are resources that are restricted by a donor for use for a particular purpose or in a particular future period. The School's unspent contributions are classified in this class if the donor limited their use, as are the unspent appreciation of its donor-restricted funds. When a donor's restriction is satisfied, either by using the resources in the manner specified by the donor or by the passage of time, the expiration of the restriction is reported in the financial statements by reclassifying the net assets from temporarily restricted to unrestricted net assets. Net assets restricted for acquisition of property or equipment (or less commonly, the contribution of those assets directly) are reported as temporarily restricted until the specified asset is placed in service by the School, unless the donor provides more specific directions about the period of its use.

- Permanently Restricted Net Assets – Permanently restricted net assets are resources whose use by the School is limited by donor-imposed restrictions that neither expires by being used in accordance with a donor's restriction nor by the passage of time.

All revenues and net gains are reported as increases in unrestricted net assets in the statement of activities unless the use of the related resources is subject to temporarily or permanent donor restrictions. All expenses and net losses are reported as decreases in unrestricted net assets.

Accounting for Contributions – Contributions are recognized when received. All contributions are reported as increases in unrestricted net assets unless use of the contributed asset is specifically restricted by the donor. Amounts received that are restricted by the donor to use in future periods or for specific purposes are reported as increases in either temporarily restricted or permanently restricted net assets, consistent with the nature of the restriction. However, if a restriction is fulfilled in the same time period in which the contribution is received, the School reports that support as unrestricted. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and are reported in the statement of activities as net assets released from restrictions.

Advertising Costs – All costs associated with advertising and promotion are expensed in the period incurred. Advertising costs for years ended June 30, 2013 and 2012 were $19,372 and $3,196, respectively.

Use of Estimates – The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of revenues and expenses during the reporting period and the reported amounts of assets and liabilities at the date of the financial statements. On an ongoing basis, the School's management evaluates the estimates and assumptions based upon historical experience and various other factors and circumstances. The School's management believes that the estimates and assumptions are reasonable in their circumstances; however, actual results could differ from those estimates.

Tax Status – The School is incorporated exempt from federal income taxation under Section 501(c)(3) of the Internal Revenue Code and state income taxation under Arizona Revised Statute (A.R.S.) §43-1201, though it would be subject to tax on income unrelated to its exempt purposes (unless that income is otherwise excluded by the Code or A.R.S.). Contributions to the School are tax deductible to donors under section 170 of the Code. The School is not classified as a private foundation. The School's Form 990, *Return of Organization Exempt from Income Tax*, is generally subject to examination by the Internal Revenue Service for three years after the date filed. As of June 30, 2013, the returns for 2012, 2011, 2010, and 2009 remain subject to examination. Lastly, the School has not taken any uncertain tax positions, and, therefore, has no policy for evaluating them.

Expense Recognition and Allocation – The cost of providing the School's programs and other activities is summarized on a functional basis in Note 3. Expenses that can be identified with a specific program or support service are charged directly to that program or support service. Costs common to multiple functions have been allocated among the various functions benefited.

General and administrative expenses include those costs that are not directly identifiable with any specific program, but which provide for the overall support and direction of the School.

Fundraising costs are expensed as incurred, even though they may result in contributions received in future years. The School generally does not conduct its fundraising activities in conjunction with its other activities. In the few cases in which it does, joint costs have been allocated between fundraising and management and general expenses in accordance with standards for accounting for costs of activities that include fundraising.

Subsequent Events – The School has reviewed all subsequent events through February 5, 2014, which was the date the financial statements were available to be issued. Events occurring after that date have not been evaluated to determine whether a change in the financial statements would be required.

Prior Year Amounts – Certain prior year amounts have been reclassified to conform to current year presentation.

NOTE 2 – CASH AND CASH EQUIVALENTS

The School maintains all of its cash with multiple financial institutions. The carrying amount of deposits at June 30, 2013 and 2012 were $18,965 and $8,499, respectively; the bank balances were $32,438 and $10,063, respectively. The entire bank balances were covered by federal depository insurance.

Cash Held by Trustee - As of June 30, 2010, the School received $4,000,000 of proceeds from notes payable to IDA. The proceeds are available to pay issuance costs, fund reserve accounts, repay outstanding principal of prior notes payable, and for acquiring, constructing, renovating and equipping educational facilities. The proceeds were deposited in the accounts of the Trustee in accordance with the Indenture of Trust. The Gables LLC Escrow Fund is available for repaying existing indebtedness. The Expense Fund is available to pay for extraordinary maintenance and replacements, which are required to keep the facilities in sound condition. The Tax and Insurance Fund is available to pay property taxes and property insurance, which are also required to keep the facilities in sound condition. The balances held by the Trustee are as follows:

	2013	2012
Restricted Cash Held By Trustee:		
Restricted Cash - Gables LLC Escrow Fund	$ 1,500	$ -
Restricted Cash - Expense Fund	4,747	-
Restricted Cash - Tax and Insurance Fund	1,965	-
Total Restricted Cash Held by Trustee	$ 8,212	$ -

NOTE 3 – FUNCTIONAL CLASSIFICATION OF EXPENSES

The School's expenses by function for the fiscal years ended June 30, 2013 and 2012 are summarized as follows:

	2013	2012
Program Services:		
Charter school	$ 980,703	$ 966,865
Total Program Services	980,703	966,865
Support Services:		
Management and general	384,367	292,641
Total Support Services	384,367	292,641
Total Expenses and Losses	$ 1,365,070	$ 1,259,506

NOTE 4 – PROPERTY AND EQUIPMENT

The School's property and equipment as of June 30, 2013 and 2012 are summarized as follows:

	2013	2012
Property and equipment:		
Building and improvements	$ 2,643,802	$ 2,617,899
Equipment	301,049	231,475
Construction in progress	78,000	-
Property and equipment, total	3,022,851	2,849,374
Accumulated depreciation and amortization	(383,419)	(248,410)
Property and equipment, net	$ 2,639,432	$ 2,600,964

Depreciation and amortization expense totaled $135,008 and $122,489, respectively, for the years ended June 30, 2013 and 2012.

NOTE 5 – OTHER ASSETS

As of June 30, 2013 and 2012, a portion of other assets consist of deferred financing charges associated with the note payable to IDA. Amortization of the deferred loan costs is provided on a straight-line basis over the life of the underlying financial instrument, which is thirty years. As of June 30, 2013 and 2012, the costs of the deferred financing costs were summarized as follows:

	2013	2012
Deferred financing costs	$ 547,976	$ 547,976
Accumulated amortization	(54,797)	(36,532)
Deferred financing costs, net	$ 493,179	$ 511,444

Amortization expense was $18,266 and $18,266 for the years ended June 30, 2013 and 2012, which was included as part of depreciation and amortization expense on the statements of activities.

NOTE 6 - CAPITAL LEASES PAYABLE

During the year ended June 30, 2013, the School acquired equipment under the provisions of long-term lease agreements classified as capital leases for accounting purposes due to the present value of the minimum lease payments exceeding 90% of the assets fair market value. Accordingly, the original cost of the assets as of June 30, 2013, totaling $20,376, less $3,396 of accumulated depreciation, has been capitalized. Amortization expense related to the leased equipment for the fiscal year ended June 30, 2013 totaled $3,396 and is included in depreciation and amortization expense on the statements of activities. The future minimum lease payments under the capital leases, together with the present value of the net minimum lease payments as of June 30, 2013, are as follows:

Maturities of the capital leases payable are summarized as follows:

Fiscal year ending June 30:	
2014	$ 7,200
2015	7,200
2016	4,200
Total capital lease payments	18,600
(Less) Amount representing interest	(1,054)
Present value of capital lease payments	17,546
(Less) current portion	(6,792)
Capital leases payable, less current portion	$ 10,754

NOTE 7 – NOTES PAYABLE

The School's notes payable outstanding as of June 30, 2013 and 2012 are summarized as follows:

	2013	2012
Note payable to a financial institution with an original amount of $100,000 an interest rate of 8.00%, and payable monthly through March 31, 2014. The Note is unsecured.	$ 100,000	$ 100,000
Note payable to a financial institution with an original amount of $50,000 an interest rate of 8.00%, and payable monthly through March 31, 2014. The Note is unsecured.	50,000	50,000
Total notes payable	$ 150,000	$ 150,000

Maturities of the notes payable are summarized as follows:

Fiscal year ending June 30:	
2014	$ 150,000
Total	$ 150,000

Interest expense under the promissory notes for the years ended June 30, 2013 and 2012 were $18,000 and zero, respectively.

NOTE 8 – NOTES PAYABLE TO IDA

Education Revenue and Refunding Bonds - The Industrial Development Authority of the County of Pima, Arizona (IDA) issued tax-exempt Education Facilities Bonds (Bonds) under an Indenture of Trust dated as of June 1, 2010. The proceeds of the bonds were loaned to the School for the purpose of financing and/or refinancing the costs of acquiring, constructing, renovating, and/or equipping educational facilities; paying the issuance costs of the bonds; and establishing reserves to be used in the event of default by the School.

Loan Agreement - The School is obligated to the IDA under its Loan Agreement and Promissory Note to make payments sufficient to pay the principal, premium, and interest on its loan.

The School has pledged substantially all of its revenues in order to meet its obligations under the Loan Agreement and Promissory Note. The primary revenues of the School are state equalization assistance, which are statutorily owed by the State to the School based on student enrollment. The School has irrevocably directed the State to make its monthly state equalization payments directly to the trustee of the bonds so long as any of its obligations under the Loan Agreement remain outstanding and unsatisfied. The trustee of the bonds calculates and retains the amount due under the Loan Agreement and remits the remaining state equalization payments to the School. In addition, the Loan Agreement contains restrictive covenants including minimum amounts of insurance, maintenance of its tax exempt status, compliance with the Charter School Act, and limits on additional indebtedness.

The Loan Agreement and Promissory Note remain in force until either all payments required by the Promissory Note have been paid or there are sufficient monies in the reserve funds to redeem all outstanding bonds.

Reserve Funds – The reserve funds are held in trust solely for the benefit of the bondholders. The School does not have a legal, equitable, or reversionary right to the reserve funds. In the event of default of the Loan Agreement by the School, amounts held in the reserve funds and any proceeds from the sale of collateral will be used to satisfy/repay the Promissory Note of the School.

If at any time the amount in the reserve funds exceeds the aggregate principal amount of bonds outstanding plus any redemption premium, the reserve funds will be used to redeem all outstanding bonds and, accordingly, the School's obligation under the Loan Agreement and Promissory Note ceases. Therefore, the School's initial and continuing contributions to the reserve funds are accounted for as prepayments of its Promissory Note payable to the IDA. However, the School remains contingently liable for all payments required by the Loan Agreement and Promissory Note if the reserve funds are used in the event of default by one or more participating charter schools.

	2013	2012
Note payable to IDA with an original amount of $4,000,000 an interest rate of 7.25%, and payable monthly through August 1, 2040. The Note is secured by a Deed of Trust on the School's property.	$ 4,000,000	$ 4,000,000
Total note payable to IDA	4,000,000	4,000,000
(Less) Amounts held in reserve funds	(337,321)	(386,207)
Total note payable to IDA	$ 3,662,679	$ 3,613,793

The aggregate maturities of the note payable to IDA as of June 30, 2013 are summarized as follows:

Year ending June 30:	Maturities
2014	$ 45,833
2015	54,583
2016	59,583
2017	64,583
2018	69,583
Thereafter	3,368,514
Total	$ 3,662,679

Interest expense under the promissory note for the years ended June 30, 2013 and 2012 were $311,465 and $313,972, respectively.

NOTE 9 – LINES OF CREDIT

The School has a short-term line of credit with a financial institution with an available credit limit totaling $50,000. The line of credit has an interest rate of 11.0% and is unsecured. As of June 30, 2013 and 2012, the outstanding balance against the line of credit totaled $52,825 and $49,981, respectively.

During the year ended June 30, 2013, the School entered into a revolving line of credit with Gables Development Group, LLC with an available credit limit totaling $1,200,000. The line of credit has an interest rate of 10.0% and is unsecured. As of June 30, 2013, the oustanding balance against the line of credit totaled $716,636. Interest expense charged on the outstanding balance for the year ended June 30, 2013 totaled $19,542, which remained unpaid as of June 30, 2013 and was included as a part of accrued interest payable on the statements of financial position.

During the year ended June 30, 2013, the School entered into a revolving line of credit with Varsity Staffing, LLC, a related party owned by the director, with an available credit limit totaling $500,000. The line of credit has an interest rate of 10.0% and is unsecured. As of June 30, 2013, the oustanding balance against the line of credit totaled $2,500.

During the year ended June 30, 2013, the School entered into a revolving line of credit with the director and president of the board of directors, a related party, with an available credit limit totaling $10,000. The line of credit has an interest rate of 10.0% and is unsecured. As of June 30, 2013, the School has no oustanding balance against the line of credit.

During the year ended June 30, 2013, the School entered into a revolving line of credit with the vice-president of the board of directors, a related party, with an available credit limit totaling $10,000. The line of credit has an interest rate of 10.0% and is unsecured. As of June 30, 2013, the School has no oustanding balance against the line of credit.

During the year ended June 30, 2013, the School entered into a revolving line of credit with the secretary of the board of directors, a related party, with an available credit limit totaling $10,000. The line of credit has an interest rate of 10.0% and is unsecured. As of June 30, 2013, the School has no oustanding balance against the line of credit.

NOTE 10 – COMMITMENTS AND CONTINGENT LIABILITIES

Litigation – The School is contingently liable for claims, either asserted or unasserted, and judgments resulting from lawsuits incidental to the normal operation of a school. While the outcome of these claims cannot be predicted with certainty, management does not believe that the outcome of any of these matters will have a material adverse effect on the School's financial position, results of operations, or liquidity. Accordingly, no provision for possible losses is reflected in the financial statements.

Compliance – The School's compliance with certain laws and regulations is subject to review by its Sponsor. Although such reviews could result in a reduction of state equalization assistance, any required reductions are not expected to be significant. As of June 30, 2013 and 2012, the School was out of compliance with the Internal Revenue Service, the Arizona Department of Revenue, and the Arizona Department of Economic Security. As of the date of the audit report, the School has not entered into an installment agreement to resolve the outstanding taxes, penalties, and interest. The balance outstanding totaled $43,957 and $58,676, which was included as accrued payroll and related expenses on the statement of financial position.

Construction Contracts – During the year ended June 30, 2013, the School entered into a Development Services Agreement with Locke Financial, LLC, a related party company owned by the director, totaling $124,500 to assist the School in development of a new facility complete with initial cost feasibility, interview and selection of a general contractor, etc. As of June 30, 2013, the School had paid Locke Financial, LLC a total of $78,000 against the agreement. Those costs have been capitalized as construction in progress on the statements of financial position.

NOTE 11 - CONCENTRATIONS OF RISK

Amounts held in financial institutions can occasionally be in excess of the Federal Deposit Insurance Corporation and Securities Investor Protection Corporation limits. The School deposits its cash with high quality financial institutions, and management believes the School is not exposed to significant credit risk on those amounts.

A significant portion of the School's annual funding comes from agencies of the federal and state governments, including primarily the Arizona Department of Education. As such, the School's ability to generate resources via contributions and grants is dependent upon the economic health of the federal government and the state of Arizona. An economic downturn could cause a decrease in contributions and grants that coincides with an increase in demand for the School's services. In addition, if the state of Arizona and its agencies significantly reduced the level of support provided to the School it would have a material effect on the School's operations. The School's management is aware of the concentration and its potential impact on its programs, and would take appropriate action if any reduction did occur.

NOTE 12 - RELATED PARTY TRANSACTIONS

For the years ended June 30, 2013 and 2012, the School had engaged in the following related party transactions:

During the year ended June 30, 2013, the School purchased supplies and other related items for reimbursement, and incurred purchased professional services from family members of various board members totaling $11,658. As of June 30, 2013, the family members of various board members were fully reimbursed or paid for the services rendered to the School.

During the year ended June 30, 2013, various board members were reimbursed for items purchased on behalf of the School totaling $15,204. As of June 30, 2013, the various board members were fully reimbursed.

During the year ended June 30, 2013, the School entered into an agreement with Varsity Staffing Solutions, LLC, a related party company owned by the director, to provide leased employees to the School. The School puchased $110,190 in leased employees during the year. As of June 30, 2013, the School had paid the related company $81,916, which left 28,274 outstanding as part of accounts payable and accrued expenses on the statements of financial position.

Beginning July 2011, the School entered into an agreement with a member of the board of directors to provide accounting and administrative services to the School at a rate of $3,000 per month. The total amount billed for these services during the years ended June 30, 2013 and 2012 was $6,000 and $24,000, respectively. As of June 30, 2013, the School had paid the entire balance owed to the vendor. As of June 30, 2012, the School owed the vendor $11,260, which was included as part of accounts payable and accrued expenses on the statements of financial position.

Beginning July 2011, the School entered into an agreement with a member of the board of directors to provide Principal and administrative services to the school at a rate of $4,200 per month. The total amount billed for these services during the year ended June 30, 2012 was $33,200.

In July 2011, the School borrowed funds as a short-term loan from a company (Ed Dev I, LLC) wholly owned by a member of the board of directors. The loan was for $12,000 with no stated rate of interest and payable on demand. This loan, when combined with previous loans from prior years, totaled $68,686. As of June 30, 2012, the School had repaid $42,217 and $6,667 was forgiven as a donation to the School, which left $19,803 owed to the related company. As of June 30, 2013, the School had only made payments totaling $4,803, which left $15,000 outstanding as part of accounts payable and accrued expenses on the statements of financial position.

In March 2011, the School borrowed funds as a short-term loan from a member of the board of directors for the amount of $22,200. Payments totaling $6,000 were paid in the prior year. As of June 30, 2012, the School had repaid the entire balance.

From December 2011 to June 2012, the School again borrowed funds as short-term loans with no stated rate of interest and payable upon demand from a member of the board of directors totaling $29,178. As of June 30, 2012, the School had repaid $25,205 and had an outstanding balance of $3,973, which was listed as part of loans payable to related parties on the statements of financial position. As of June 30, 2013, the School had repaid the entire balance.

In June 2011, the School borrowed funds as a short-term loan from the spouse of a member of the board of directors in the amount of $25,000. As of June 30, 2012, the School had repaid the outstanding balance.

In November 2011, the School borrowed funds as a short-term loan from a family member of a member of the board of directors for the amount of $10,000 with no stated rate of interest and payable upon demand. As of June 30, 2012, the School had made payments totaling $9,506 and had an outstanding balance of $494, which was listed as part of loans payable to related parties on the statements of financial position. As of June 30, 2013, the School had repaid the entire balance.

During the year ended June 30, 2011, the School borrowed funds as a short-term loan from the spouse of a member of the board of directors totaling $25,000. As of June 30, 2012, the School had repaid the entire balance.

In July 2011, the School borrowed funds as a short-term loan totaling $27,700 from the spouse of a member of the board of directors. As of June 30, 2012, the School had repaid the entire balance.

In August 2011, the School borrowed funds as a short-term loan totaling $20,000 from the spouse of a member of the board of directors. As of June 30, 2012, the School had repaid the entire balance.

In September 2011, the School borrowed funds as a short-term loan totaling $35,000 from the spouse of a member of the board of directors. As of June 30, 2012, the School had repaid the entire balance.

In November, 2011, the School borrowed funds as a short-term loan totaling $23,000 from the spouse of a member of the board of directors. As of June 30, 2012, the School had repaid the entire balance.

In the previous year, the School had entered into a capital lease agreement with the spouse of a member of the board of directors. During the year ended June 30, 2012, the remaining balance of the lease totaling $21,210 was forgiven as a donation to the School.

NOTE 13 - DESIGNATED UNRESTRICTED NET ASSETS

Classroom Site Project – In June of 2000, the Arizona Legislature created a Classroom Site Fund (CSF) to be administered by the Arizona Department of Education (ADE). The CSF was created to provide funding to school districts and charter schools for designated purposes. The measure (Proposition 301) was approved by the voters of Arizona and was implemented after May 31, 2001. Proposition 301 authorizes the State to levy and collect 0.60% sales tax for educational purposes. The ADE administers and allocates CSF funds to the School based on student count and other factors specified by statute. The School must allocate funding from CSF according to the following statutory parameters:

- 40% of the funds must be used for performance based teacher compensation increases and teacher employment related expenses;
- 40% of the funds must be used for maintenance and operations purposes including class-size reduction, teacher compensation increases, AIMS intervention programs, teacher development, dropout prevention programs, and teacher liability insurance premiums;
- 20% of the funds must be used for teacher base salary increases and employment related expenses.

The CSF funds are nonreverting, therefore unspent monies at fiscal year end may be used in future years. However, restrictions placed on the original allocation of revenues apply in future years. Therefore, the unexpended balance must be carried forward in each of the three categories. As of June 30, 2013, the School had no accrual and cash carryover balances. As of June 30, 2012, the School had accrual and cash carryover balances of $12,740 and $9,764, respectively.

NOTE 14 - GOING CONCERN

As indicated in the accompanying financial statements, the School has incurred significant decreases in unrestricted net assets such that the School has net assets of $1,599,185 as of June 30, 2013. In addition, the School's current liabilities exceeded current assets by $1,118,374 as of June 30, 2013. These factors create an uncertainty about the School's ability to continue as a going concern. Management of the School is developing a plan to reduce or delay expenses, increase student enrollment, and if necessary, borrow additional funds or re-structure debt. The ability of the School to continue as a going concern is dependent upon its success with these endeavors. The financial statements do not include any adjustments that might be necessary if the School is unable to continue as a going concern.

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Independent Auditor's 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*

Board of Directors
Hillcrest Academy, Inc.

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 Hillcrest Academy, Inc. (a nonprofit organization), which comprise the statement of financial position as of June 30, 2013, and the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements, and have issued our report thereon dated February 5, 2014. In our report, the accompanying financial statements were prepared assuming that the School will continue as a going concern. As discussed in Note 14 to the financial statements, the School suffered recurring significant deficits in unrestricted net assets and has a net deficiency in net assets that raise substantial doubt about it ability to continue as a going concern.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the 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 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 material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and responses, we identified certain deficiencies in internal control that we consider to be material weaknesses and 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 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. We consider the deficiencies described in the accompanying schedule of findings and responses as items 2012-1, 2012-4, and 2013-1 to be material weaknesses.

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*.

The School's Response to Findings
The School's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. The School's response was not subjected 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 School'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 School's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Brett V. Backlund, CPA, PC

Brett V. Backlund, CPA, PC
Gilbert, Arizona
February 5, 2014

HILLCREST ACADEMY, INC.
SCHEDULE OF FINDINGS AND RESPONSES
MATERIAL WEAKNESSES IN INTERNAL CONTROL
JUNE 30, 2013

PARTIAL DAY ABSENCES
REFERENCE: 2012-1

CONDITION
The School did not report students arriving late or leaving early in accordance with the Arizona Department of Education's (ADE) School Finance Procedures Manual to ADE. The School setup the computerized attendance system to track half day absences, but did not carry those changes through to the reports submitted to ADE, therefore half day absences were not reported.

CRITERIA
In accordance with the ADE's School Finance Procedures Manual, for first through eighth grades in which attendance is based on half days, the attendance of at least three-quarters of the instructional time scheduled for the day shall be counted as a full day's attendance and attendance at a minimum of one-half but less than three-quarters of the instructional time scheduled for the day equals one-half day of attendance. In addition, in accordance with the ADE's School Finance Procedures Manual, student membership and absences must be recorded and reported accurately by each charter school to ADE.

EFFECT
The ADE's School Finance Procedures Manual has not been complied with.

CAUSE
The School did not completely understand the computerized attendance system reporting and was not adequately trained on the computerzied attendance system.

RECOMMENDATION AND BENEFIT
The School should review the ADE's School Finance Procedures Manual on Daily Attendance and Average Daily Attendance and Attendance Recordkeeping and setup the computerized attendance system accordingly to comply. In addition, the School should better understand the computerized attendance system utilized and become adequately trained to ensure the reports are accurate. This will help ensure compliance with the ADE's School Finance Procedures Manual and that membership and absences are accurately reported to the ADE.

CLIENT RESPONSE
We concur with the condition.

Individual responsible for implementation of corrective action plan:
Ryan Christensen, President.

Corrective action plan:
We will review the ADE's School Finance Procedures Manual on Daily Attendance and Average Daily Attendance and setup the attendance system to comply. In addition, we hired an outside attendance consultant to help ensure compliance.

Estimated completion date:
Fiscal year 2013-2014.

HILLCREST ACADEMY, INC.
SCHEDULE OF FINDINGS AND RESPONSES
MATERIAL WEAKNESSES IN INTERNAL CONTROL
JUNE 30, 2013

NON-PAYROLL EXPENSES
REFERENCE: 2012-4

CONDITION
For 107 non-payroll disbursements, which totaled $68,846, the School did not provide invoices or supporting documentation for review. However, upon further investigation, the School was able to identify and/or provide additional documentation to determine that $48,637 were legitimate business expenses, which left $20,209 undetermined, but appearing business related.

CRITERIA
In accordance with the USFRCS, Records Management Manual, accounting records for expenses including requisitions, purchase orders, vendor invoices, vouchers, and other supporting documents must be retained for three fiscal years after prepared.

EFFECT
The USFRCS was not complied with.

CAUSE
The School went through a management change during the year ended June 30, 2013, which caused record keeping errors. However, the new administration was able to resolve most issues.

RECOMMENDATION AND BENEFIT
The School should maintain all supporting documentation including, but not limited to, purchase requisitions, purchase orders, receiving reports, vouchers, vendor invoices, etc. Records should provide adequate support for non-payroll expenses and account distribution, and serve as a basis for preparing non-payroll vouchers and reports. Maintaining non-payroll records for all expenditures should help the School comply with the USFRCS.

CLIENT RESPONSE
We concur with the condition.

Individuals responsible for implementation of corrective action:
Ryan Christensen, President.

Corrective action plan:
The School underwent remodeling during the school year. During that time, we filed prior year information in labeled storage boxes and left the current year supporting documentation in the filing cabinet. Some of the files were then misplaced resulting in our inability to locate the missing supporting documentation. We were able to obtain copies from the vendors during the audit.

Estimated completion date:
Fiscal year 2013-2014.

HILLCREST ACADEMY, INC.
SCHEDULE OF FINDINGS AND RESPONSES
MATERIAL WEAKNESSES IN INTERNAL CONTROL
JUNE 30, 2013

BEGINNING BALANCES
REFERENCE: 2013-1

CONDITION
The School did not record accounting transactions occurring during the prior fiscal years in accordance with GAAP, therefore the beginning balances were reported incorrectly and required additional time to correct.

CRITERIA
In accordance with the School's Charter Contract, the School must follow Generally Accepted Accounting Principles (GAAP). Accordingly, the matching principle requires that revenues be recorded in the fiscal year the items were earned. Also, fiscal year ended accounts receivable consists of assets for revenues earned on or before June 30th that have not been collected as of that date. To properly establish these revenues and assets, the School should review cash collections and other relevant information subsequent to June 30th to determine the dollar amount of the revenues earned but not yet paid by June 30th.

EFFECT
The School's Charter Contract has not been complied with. As a result, revenues and/or accounts receivable for the fiscal year end may be recorded incorrectly.

CAUSE
The School went through a management change during the year ended June 30, 2013, which caused record keeping errors. The School's focus was on current and subsequent years accounting and bookkeeping. However, the new administration has been able to resolve most issues

RECOMMENDATION AND BENEFIT
The School should establish procedures to review cash collections and other relevant information subsequent to June 30th to determine the dollar amount of revenues earned but not paid for by June 30th. This will help ensure compliance with the School's Charter Contract and that all revenues and accounts receivable are properly recorded.

CLIENT RESPONSE
We concur with the condition.

Individual responsible for implementation of corrective action plan:
Ryan Christensen, Director.

Corrective action plan:
We will establish procedures to ensure proper accounting and financial reporting of revenues and assets.

Estimated completion date:
Fiscal year 2013-2014.

HILLCREST ACADEMY, INC.
STATUS OF PRIOR YEAR AUDIT FINDINGS
JUNE 30, 2013

We have reviewed the School's prior year schedule of findings and responses contained in the prior year audit report dated March 19, 2013. The School's corrective action did not correct all prior year deficiencies in internal control over financial reporting and/or instances of noncompliance or other matters, therefore, items 2012-1 and 2012-4 repeated during the year ended June 30, 2013.

First American Title Insurance Company
National Commercial Services
2425 E. Camelback Road, Suite 300 • Phoenix, AZ 85016

Office Phone:(602)567-8100 Office Fax:(602)567-8101

Estimated Settlement Statement

Property: 3916 East Paradise Lane, Phoenix, AZ 85032

File No: NCS-646117A-PHX1
Officer: Sheila Hunter/sfh
Estimated Settlement Date:
Disbursement Date:
Print Date: 07/31/2014, 6:32 AM

Buyer: CIC Hillcrest I LLC
Address:
Seller: Hillcrest Academy, Inc.
Address: 3916 East Paradise Lane, Phoenix, AZ 85032
Lender: Available
Address:
New Loan No.:

Buyer Charge	Buyer Credit	Charge Description	Seller Charge	Seller Credit
		Consideration:		
24,508,500.00		Total Consideration		24,508,500.00
		Title/Escrow Charges to:		
		Sub Escrow Fee to First American Title Insurance Company National Commercial Services	750.00	
		Policy-Extended ALTA 2006 Lender's (24,508,500.00) to First American Title Insurance Company National Commercial Services	30,610.00	
		Endorsement-Zoning-ALTA 3.1 - L to First American Title Insurance Company National Commercial Services	3,056.00	
		Endorsement(s)-Loan Policy - L Bunder Rate to First American Title Insurance Company National Commercial Services	500.00	
		Estimated Recording Fees to First American Title Insurance Company National Commercial Services	100.00	
		Disbursements Paid:		
		Mesa Gilbert Land Purchase (652976) to Hillcrest Academy, Inc.	2,454,810.27	
		Phoenix Pardes Jewish Purchase (646117) to Hillcrest Academy, Inc.	4,680,603.47	
		Phoenix adjacent land Purchase Wyatt (664775) to Hillcrest Academy, Inc.	415,252.17	
		Monies Due to Gables Development	2,942,245.98	
		Monies Due to Christensen Holdings, LLC	901,087.00	
		Monies Due to Varsity Staffing, LLC	278,502.16	
		Monies Due to American Charter Development	160,000.00	
		Monies Due to Gen Corp Mortgage	202,500.00	
		Rehab & Construction to Bank of America	12,433,498.95	
	24,508,500.00	**Cash (X From) (To) Buyer**		
		Cash (X To) (From) Seller	4,984.00	
24,508,500.00	24,508,500.00	**Totals**	24,508,500.00	24,508,500.00

Notice – This Estimated Settlement Statement is subject to changes, corrections or additions at the time of final computation of Escrow Settlement Statement.

VERTEX NONPROFIT ORGANIZATION

PO Box 456 ▪ Price ▪ Utah ▪ 84501

FROM THE OFFICE OF:

JARED HADDOCK
Chairman

435-650-2066

April 3, 2014

SENT VIA ELECTRONIC MAIL

HILLCREST ACADEMY
4710 East Baseline Rd
Mesa, AZ 84526

RE: Approval of Grant Application

To Whom It May Concern:

I am pleased to inform you that your application for a grant has been approved. Concurrent with this letter, I have included a resolution of the Board of Directors authorizing me to contribute an amount up to $1,408,280.00 directly to Hillcrest Academy. It should be noted, however, that Hillcrest is required to demonstrate its financial ability to complete the construction of its facilities prior to being awarded the funds.

If you have any questions, please do not hesitate to call or otherwise contact me. I look forward to your successful project and wish you well in your mission to provide excellent education to your students.

Sincerely,

Jared Haddock

Resolution of the Board of Directors of
Vertex Nonprofit Organization
(Agreement to Make Donation)

At a special meeting of the Board of Directors of Vertex Nonprofit Organization, a Utah non-profit corporation ("Corporation"), on the 31 day of March, 2014, the following items were discussed:

As the Corporation's main purpose is to assist charter schools with their financing and physical facility's needs, the Corporation has reviewed an application for grant requested by Hillcrest Academy, Inc., an Arizona non-profit corporation, a public charter school, located at 4710 East Baseline Road, Mesa, Arizona 85206 (EIN 86-0658004) ("School"), requesting financial assistance from the Corporation, to allow the School to obtain the remaining funds necessary to construct its physical facilities.

The Corporation has determined that an effective way to assist charter schools with their financing of physical facilities is to assist the charter school operator with financial stability.

Notwithstanding the agreement of the Corporation to make the Donation to the School, the School must demonstrate sufficient funds to complete the construction of a new charter school facility to be leased and purchased (or controlled) by the charter operator.

To ensure that the School utilizes the funds from the Donation, as described below, for its intended purposes, the Corporation may require the School to submit the monthly construction draws to the Corporation, in a form acceptable to the Corporation.

The Corporation will pay a percentage of the Donation to the School, based upon the percentage of construction completion, to the School.

The following resolutions were adopted:

"Resolved that the Chairman of the Corporation, Jared Haddock, is directed to make a charitable contribution from the Corporation in the amount not to exceed $1,408,280 ("Donation") to the School, payable in monthly installments, based upon the percentage of completion of the School's facilities, as evidenced by the School's construction draws, upon the satisfaction of the terms and conditions listed herein.

In witness whereof the Chairman of the Board of Directors has signed this certificate.

Jared Haddock, Chairman

Hillcrest Academy, Inc
Profit & Loss - Preliminary
July 2013 through June 2014

	Jul '13 - Jun 14
Ordinary Income/Expense	
Income	
1000 · Revenue From Local Sources	62,024.42
3000 · Revenue From State Sources	556,469.60
4000 · Revenue From Federal Sources	56,643.07
Total Income	675,137.09
Gross Profit	675,137.09
Expense	
6200 · Employee Benefits	1,984.35
6300 · Purch Professional Services	886,906.80
6400 · Purchased Property Services	140,316.48
6500 · Other Purchased Services	164,742.62
6600 · Supplies	174,207.29
6800 · Other Expenses.	439,248.06
Total Expense	1,807,405.60
Net Ordinary Income	-1,132,268.51
Other Income/Expense	
Other Income	
Other Income	10,625.85
Total Other Income	10,625.85
Other Expense	
Depreciation	147,538.36
Amortization	18,265.92
Total Other Expense	165,804.28
Net Other Income	-155,178.43
Net Income	**-1,287,446.94**

Hillcrest Academy, Inc.
Profit & Loss Projection
FY 2015

	2014-2015
Student Enrollment (Campus 1)	**694**
Student Enrollment (Campus 2)	**466**
Total Enrollment	**1160**
Ordinary Income/Expense	
Income	
Total Revenue From Fed & State Grants	212,530.00
Total Revenue From Local Sources	26,268,080.00
Total Revenue From State Sources	6,955,590.00
Total Income	**33,436,200.00**
Debt Service	
Total Debt Service	864,724.67
Expense	
Total Personal Services	4,795,950.44
Total Purch Professional & Tech Svcs	71,900.00
Total Purchased Property Services	124,120.00
Total Other Purchased Services	227,790.00
Total Supplies	154,120.00
Total Other Expenses.	775,745.00
Utilities	102,500.00
Total Expense	7,116,850.11
Balance Sheet Activity*	25,591,075.60
Net Income**	**728,274.29**

**Balance Sheet Activity is used in the above fincial report to denote the expenses and costs related to the acquisition of assets, the sale of assets, and the satisfaction of liabilities. These items would not normally appear on a Profit and Loss Statement, however for the purposes of deriving a Functional Net Operating Income they were included.*

*** Net Income has been adjusted for the purpose of this report to include items that would normally be expressed in a Statement of Cash Flows. The Net Income listed above is Net of the Balance Sheet Activity listed above. The result is a conceptual Functional Net Operating Income (similar to Cash Position at close).*

Hillcrest Academy
Fixed Charge Coverage Ratio Comparison
FY 2013, FY 2014, FY 2015

	Jul '14 - Jun 15	Jul '13 - Jun 14	Jul '12 - Jun 13
Ordinary Income/Expense			
Adjusted Earnings			
Change in Net Assets	728,274.29	-1,287,447.00	-705,139.00
Deprecitaion & Amortization	165,804.00	165,804.00	153,274.00
Interest Expense	290,004.00	314,939.00	350,917.00
Lease Expense	871,925.00	7,200.00	39,792.00
Total Adjusted Earnings	2,056,007.29	-799,504.00	-161,156.00
Fixed Costs			
Interest Expense*	290,004.00	314,939.00	350,917.00
Lease Expense	871,925.00	7,200.00	39,792.00
Current Portion	50,000.00	45,833.00	0.00
Total Fixed Costs	1,211,929.00	367,972.00	390,709.00
Fixed Charge Coverage Ratio	**1.70**	**-2.17**	**-0.41**

Hillcrest Academy, Inc
Balance Sheet Comparison
As of June 30, 2013, 2014 and 2015

	Jun 30, 13	Jun 30, 14	Jun 30, 15
ASSETS			
Current Assets			
Checking/Savings			
Total Checking/Savings	9,738.30	42,631.41	781,425.05
Accounts Receivable			
Total Accounts Receivable	92,893.61	51,123.55	0.00
Other Current Assets			
Total Other Current Assets	4,449.17	162,017.87	4,449.17
Total Current Assets	107,081.08	255,772.83	785,874.22
Fixed Assets			
Total Fixed Assets	2,639,431.87	2,710,226.47	2,573,963.11
Other Assets			
Total Other Assets	863,138.56	842,676.83	822,215.10
TOTAL ASSETS	**3,609,651.51**	**3,808,676.13**	**4,182,052.43**
LIABILITIES & EQUITY			
Liabilities			
Current Liabilities			
Accounts Payable			
Total Accounts Payable	121,760.16	90,122.96	12,000.00
Other Current Liabilities			
Current Notes Payable	1,006,908.66	2,529,887.80	55,000.00
Payroll Liabilities	43,956.95	62,175.22	0.00
Total Other Current Liabilities	1,050,865.61	2,592,063.02	55,000.00
Total Current Liabilities	1,172,625.77	2,682,185.98	67,000.00
Long Term Liabilities			
Pima County IDA Bond	3,954,166.63	3,904,166.66	3,849,166.66
Ford Motor Credit - 8557	0.00	16,851.66	11,851.66
Ford Motor Credit - 7651	0.00	16,851.66	11,851.66
Pacific Office Automation	10,754.00	3,962.00	0.00
Total Long Term Liabilities	3,964,920.63	3,941,831.98	3,872,869.98
Total Liabilities	5,137,546.40	6,624,017.96	3,939,869.98
Equity			
Net Assets	-341,865.66	-341,865.66	31,663.10
1110 · Retained Earnings	-588,438.48	-1,186,029.23	-517,754.94
Net Income	-597,590.75	-1,287,446.94	728,274.29
Total Equity	-1,527,894.89	-2,815,341.83	242,182.45
TOTAL LIABILITIES & EQUITY	**3,609,651.51**	**3,808,676.13**	**4,182,052.43**