ART ACADEMY OF CINCINNATI AND AFFILIATE

May 31, 2014

CONSOLIDATED FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT INCLUDING SUPPLEMENTARY INFORMATION

Art Academy of Cincinnati
EST. 1869

ART ACADEMY OF CINCINNATI AND AFFILIATE
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VonLehman CPA & ADVISORY FIRM

INDEPENDENT AUDITORS' REPORT

The Board of Trustees
Art Academy of Cincinnati
and Affiliate
Cincinnati, Ohio

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of the Art Academy of Cincinnati and Affiliate (nonprofit organizations), which comprise the consolidated statements of financial position as of May 31, 2014 and 2013, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Art Academy of Cincinnati and Affiliate as of May 31, 2014 and 2013, and the changes in its consolidated net assets and its consolidated cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Other Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating statement of financial position and consolidating statement of activities on pages 35 and 36 are presented for purposes of additional analysis and are not a required part of the basic consolidated financial statements. The accompanying schedule of expenditures of federal awards, as required by Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, is also presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards* we have also issued our report dated August 22, 2014, on our consideration of the Art Academy of Cincinnati and Affiliate'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 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 Art Academy of Cincinnati and Affiliate's internal control over financial reporting and compliance.

VonLehman & Company Inc.

Fort Mitchell, Kentucky
August 22, 2014

ART ACADEMY OF CINCINNATI AND AFFILIATE
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
May 31, 2014

ASSETS

	Unrestricted				Permanently Restricted	
	General	Board Designated	Plant	Temporarily Restricted	Endowment	Total
Current Assets						
Cash and Cash Equivalents	$ 171,323	$ -	$ -	$ 189,247	$ 8,662	$ 369,232
Accounts Receivable, Net	98,564	-	-	-	-	98,564
Investments	36,880	576,435	-	70,675	-	683,990
Grant Receivable	-	-	-	40,000	-	40,000
Investment Receivable	(49,400)	-	-	49,400	-	-
Prepaid Expenses	90,925	-	-	-	-	90,925
Total Current Assets	348,292	576,435	-	349,322	8,662	1,282,711
Buildings and Equipment, Net	-	-	3,673,934	-	-	3,673,934
Investments	-	-	-	125,980	828,962	954,942
Art Inventory	-	-	288,271	-	-	288,271
Grant Receivable	-	-	-	520,000	-	520,000
Beneficial Interest in Perpetual Trust	-	-	-	-	201,234	201,234
Beneficial Interest in Charitable Remainder Trusts	-	-	-	85,786	-	85,786
Deposits	-	-	13,175	-	-	13,175
Other Assets, Net	-	-	9,716	-	-	9,716
Total Assets	$ 348,292	$ 576,435	$ 3,985,096	$ 1,081,088	$ 1,038,858	$ 7,029,769

LIABILITIES AND NET ASSETS

	General	Board Designated	Plant	Temporarily Restricted	Endowment	Total
Current Liabilities						
Line of Credit	$ 650,000	$ -	$ -	$ -	$ -	$ 650,000
Accounts Payable	160,697	-	-	-	-	160,697
Accrued Expenses	112,347	-	-	188,247	-	300,594
Capital Lease - Current Portion	-	-	6,238	-	-	6,238
Note Payable - Current Portion	-	-	5,132	-	-	5,132
Total Current Liabilities	923,044	-	11,370	188,247	-	1,122,661
Long-Term Liabilities						
Charitable Remainder Trust	-	-	-	21,972	-	21,972
Deferred Revenue	-	-	-	560,000	-	560,000
Capital Lease - Long-Term	-	-	5,208	-	-	5,208
Note Payable - Long-Term	-	-	169,026	-	-	169,026
Total Long-Term Liabilities	-	-	174,234	581,972	-	756,206
Total Liabilities	923,044	-	185,604	770,219	-	1,878,867
Net Assets	(574,752)	576,435	3,799,492	310,869	1,038,858	5,150,902
Total Liabilities and Net Assets	$ 348,292	$ 576,435	$ 3,985,096	$ 1,081,088	$ 1,038,858	$ 7,029,769

See accompanying notes.

ART ACADEMY OF CINCINNATI AND AFFILIATE
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
May 31, 2013

ASSETS

	Unrestricted				Permanently Restricted	
	General	Board Designated	Plant	Temporarily Restricted	Endowment	Total
Current Assets						
Cash and Cash Equivalents	$ 43,500	$ -	$ -	$ 177,385	$ 6,580	$ 227,465
Accounts Receivable, Net	165,786	-	-	-	-	165,786
Investments	29,737	499,810	-	61,368	-	590,915
Grant Receivable	-	-	-	40,000	-	40,000
Investment Receivable	(81,386)	-	-	81,386	-	-
Prepaid Expenses	93,112	-	-	-	-	93,112
Total Current Assets	250,749	499,810	-	360,139	6,580	1,117,278
Buildings and Equipment, Net	-	-	4,217,872	-	-	4,217,872
Investments	-	-	-	36,841	828,963	865,804
Grant Receivable	-	-	-	560,000	-	560,000
Beneficial Interest in Perpetual Trust	-	-	-	-	192,972	192,972
Beneficial Interest in Charitable Remainder Trusts	-	-	-	97,532	-	97,532
Deposits	-	-	12,810	-	-	12,810
Other Assets, Net	-	-	14,495	-	-	14,495
Total Assets	$ 250,749	$ 499,810	$ 4,245,177	$ 1,054,512	$ 1,028,515	$ 7,078,763

LIABILITIES AND NET ASSETS

	General	Board Designated	Plant	Temporarily Restricted	Endowment	Total
Current Liabilities						
Line of Credit	$ 665,000	$ -	$ -	$ -	$ -	$ 665,000
Accounts Payable	192,496	-	-	-	-	192,496
Accrued Expenses	157,038	-	-	176,385	-	333,423
Capital Lease - Current Portion	-	-	5,525	-	-	5,525
Note Payable - Current Portion	-	-	4,834	-	-	4,834
Total Current Liabilities	1,014,534	-	10,359	176,385	-	1,201,278
Long-Term Liabilities						
Charitable Remainder Trust	-	-	-	32,668	-	32,668
Deferred Revenue	-	-	-	600,000	-	600,000
Capital Lease - Long-Term	-	-	11,445	-	-	11,445
Note Payable - Long-Term	-	-	173,735	-	-	173,735
Long-Term Liabilities	-	-	185,180	632,668	-	817,848
Total Liabilities	1,014,534	-	195,539	809,053	-	2,019,126
Net Assets	(763,785)	499,810	4,049,638	245,459	1,028,515	5,059,637
Total Liabilities and Equity	$ 250,749	$ 499,810	$ 4,245,177	$ 1,054,512	$ 1,028,515	$ 7,078,763

See accompanying notes.

ART ACADEMY OF CINCINNATI AND AFFILIATE
CONSOLIDATED STATEMENT OF ACTIVITIES
Year Ended May 31, 2014

	Unrestricted				Permanently Restricted	
	General	**Board Designated**	**Plant**	**Temporarily Restricted**	**Endowment**	**Total**
Revenue and Support						
Grants, Contributions and Gifts	$ 294,697	$ -	$ -	$ -	$ 2,082	$ 296,779
Tuition Income	5,166,424	-	-	-	-	5,166,424
Investment Income	-	16,402	-	28,278	-	44,680
Other Income	47,159	-	714,698	-	-	761,857
Total Revenue and Support	5,508,280	16,402	714,698	28,278	2,082	6,269,740
Net Assets Released from Restrictions	2,000	-	-	(2,000)	-	-
Total Revenue, Support and Reclassifications	5,510,280	16,402	714,698	26,278	2,082	6,269,740
Expenses						
Program Services	5,335,864	-	383,109	-	-	5,718,973
Management and General	564,864	3,118	9,974	-	-	577,956
Fundraising	24,919	-	954	-	-	25,873
Total Expenses	5,925,647	3,118	394,037	-	-	6,322,802
(Deficit) Excess of Revenue, Support and Reclassifications Over Expenses	(415,367)	13,284	320,661	26,278	2,082	(53,062)
Interfund Equity Transfers	572,414	-	(570,807)	(1,607)	-	-
Realized Gain on Investments	-	68,714	-	79,983	-	148,697
Unrealized Loss on Investments	-	(5,373)	-	(6,208)	-	(11,581)
Change in Excess Loss on Endowment Investments	31,986	-	-	(31,986)	-	-
Change in Beneficial Interest in Perpetual Trust	-	-	-	-	8,261	8,261
Change in Beneficial Interest in Charitable Remainder Trusts	-	-	-	(1,050)	-	(1,050)
Change in Net Assets	189,033	76,625	(250,146)	65,410	10,343	91,265
Net Assets Beginning of Year	(763,785)	499,810	4,049,638	245,459	1,028,515	5,059,637
Net Assets End of Year	$ (574,752)	$ 576,435	$ 3,799,492	$ 310,869	$ 1,038,858	$ 5,150,902

See accompanying notes.

ART ACADEMY OF CINCINNATI AND AFFILIATE
CONSOLIDATED STATEMENT OF ACTIVITIES
Year Ended May 31, 2013

	Unrestricted				Permanently Restricted	
	General	Board Designated	Plant	Temporarily Restricted	Endowment	Total
Revenue and Support						
Grants, Contributions and Gifts	$ 279,730	$ -	$ -	$ (4,340)	$ 6,580	$ 281,970
Tuition Income	4,811,650	-	-	-	-	4,811,650
Investment Income	-	16,568	-	33,912	-	50,480
Investment Income Allocation	70,000	(20,538)	-	(49,462)	-	-
Other Income	419,843	-	173,691	-	-	593,534
Total Revenue and Support	5,581,223	(3,970)	173,691	(19,890)	6,580	5,737,634
Net Assets Released from Restrictions	18,180	555,533	-	(202,082)	(371,631)	-
Total Revenue, Support and Reclassifications	5,599,403	551,563	173,691	(221,972)	(365,051)	5,737,634
Expenses						
Program Services	5,375,348	-	609,029	-	-	5,984,377
Management and General	484,944	1,842	17,550	-	-	504,336
Fundraising	9,561	-	2,068	-	-	11,629
Total Expenses	5,869,853	1,842	628,647	-	-	6,500,342
(Deficit) Excess of Revenue, Support and Reclassifications Over Expenses	(270,450)	549,721	(454,956)	(221,972)	(365,051)	(762,708)
Interfund Equity Transfers	(38,779)	(100,000)	143,114	(4,335)	-	-
Realized Gain on Investments	-	36,671	-	57,292	-	93,963
Unrealized Gain on Investments	-	12,042	-	67,470	-	79,512
Change in Excess Loss on Endowment Investments	28,752	-	-	(28,752)	-	-
Change in Beneficial Interest in Perpetual Trust	-	-	-	-	21,231	21,231
Change in Beneficial Interest in Charitable Remainder Trusts	-	-	-	(3,324)	-	(3,324)
Impairment for Reduction in Carrying Value to Market Value	-	-	(5,990,219)	-	-	(5,990,219)
Change in Net Assets	(280,477)	498,434	(6,302,061)	(133,621)	(343,820)	(6,561,545)
Net Assets Beginning of Year	(483,308)	1,376	10,351,699	379,080	1,372,335	11,621,182
Net Assets End of Year	$ (763,785)	$ 499,810	$ 4,049,638	$ 245,459	$ 1,028,515	$ 5,059,637

See accompanying notes.

ART ACADEMY OF CINCINNATI AND AFFILIATE
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended May 31, 2014	Years Ended May 31, 2013
Cash Flows from Operating Activities		
Change in Net Assets	$ 91,265	$ (6,561,545)
Adjustments to Reconcile Change in Net Assets to Net Cash Used by Operating Activities		
Depreciation	172,077	396,035
Amortization	1,781	2,024
Realized Gain on Investments	(148,697)	(93,963)
Unrealized Loss (Gain) on Investments	11,581	(79,512)
Donated Art Inventory	(346,371)	-
Change in Beneficial Interest in Perpetual Trust	(8,261)	(21,231)
Change in Beneficial Interest in Charitable Remainder Trusts	1,050	3,324
Impairment for Reduction in Carrying Value to Market Value	-	5,990,219
Gain on Disposal of Buildings and Equipment	(133,099)	-
Changes in		
Accounts Receivable	67,222	(21,448)
Grant Receivable	40,000	-
Pledges Receivable	-	4,340
Inventory	58,100	-
Prepaid Expenses	2,187	(24,967)
Deposits	(365)	3,800
Accounts Payable	(31,799)	19,970
Accrued Expenses	(32,829)	(86,205)
Deferred Revenue	(40,000)	-
Net Cash Used by Operating Activities	(296,158)	(469,159)
Cash Flows from Investing Activities		
Proceeds from Sale of Investments	1,307,889	815,383
Purchase of Investments	(1,352,986)	(702,539)
Proceeds from Disposal of Assets	544,265	-
Acquisition of Building and Equipment	(36,308)	(16,623)
Net Cash Provided by Investing Activities	462,860	96,221
Cash Flows from Financing Activities		
Net Change in Line of Credit	(15,000)	265,000
Payments on Note Payable	(4,411)	(4,158)
Payments on Capital Lease	(5,524)	(1,280)
Net Cash (Used) Provided by Financing Activities	(24,935)	259,562
Net Change in Cash and Cash Equivalents	141,767	(113,376)
Beginning Balance - Cash and Cash Equivalents	227,465	340,841
Ending Balance - Cash and Cash Equivalents	$ 369,232	$ 227,465

See accompanying notes.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Art Academy of Cincinnati's (the Academy) purpose is to serve as an accredited educational institution of degreed and non-degreed students from across the country with diverse majors in studio art and design, notably drawing, painting, printmaking, photography, sculpture, visual communications design, digital arts, photo design, illustration, art history, and art education.

Art Academy Housing, Inc. is organized in the State of Ohio as a nonprofit corporation. Art Academy Housing, Inc. was formed during fiscal year 2006 to lease and operate student housing for the benefit of the Art Academy of Cincinnati. Art Academy Housing, Inc. is a wholly owned subsidiary of the Art Academy of Cincinnati.

As of both May 31, 2014 and 2013, the consolidated financial statements include the Art Academy of Cincinnati and Art Academy Housing, Inc.

A summary of significant accounting policies applied in the accompanying consolidated financial statements follows:

Principles of Consolidation

The consolidated financial statements also include the accounts of Art Academy Housing, Inc. This entity is related to the Academy because the Academy has assumed the financial and day-to-day operational management functions for this entity. Under accounting principles generally accepted in the United States of America (U.S. GAAP), the Academy is required to present consolidated financial statements reflecting the financial position and results of operations of both entities. All significant inter-entity transactions have been eliminated.

Accounts Receivable

Accounts receivable are stated at their contractual outstanding balances, net of any allowance for doubtful accounts. Accounts are considered past due if any portion of an account has not been paid in full within the contractual terms of the account. The Academy begins to assess its ability to collect receivables that are over 90 days past due and provides for an adequate allowance for doubtful accounts based on the Academy's collection history, the financial stability and recent payment history of the student, and other pertinent factors. Based on these criteria, the Academy has estimated an allowance for doubtful accounts of $7,287 as of both May 31, 2014 and 2013.

Investments

Investments in equity securities and debt securities are stated at fair market value. Investments available for current operations are classified as current assets. Investments not available for current operations are classified as long-term. Investment income and dividends are included in unrestricted revenue unless restricted by donor or law. Realized and unrealized gains (losses) are shown as increases (decreases) in net assets in the period in which the gain (loss) is recognized.

Use of Estimates

The process of preparing consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires the use of estimates and assumptions regarding certain types of assets, liabilities, revenues and expenses. Certain estimates relate to unsettled transactions and events as of the date of the consolidated financial statements. Other estimates relate to assumptions about the ongoing operations and may impact future periods. Accordingly, upon settlement, actual results may differ from estimated amounts.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue and Support Recognition

The Academy records revenue from contributions, tuition and interest when earned. Temporarily restricted support from governmental grants, which reimburse actual costs of the programs, is recognized as such costs are incurred and reimbursements are determinable.

Recognition of Donor Restrictions

Donor restricted support is reported as an increase in temporarily or permanently restricted net assets depending on the nature of the restriction. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets. The Academy reflects temporary restricted support as unrestricted when the restrictions are met in the same reporting period.

Contributions

Contributions, including unconditional promises to give, are recorded as made. All contributions are available for unrestricted use unless specifically restricted by a donor. Conditional promises to give are recognized when the conditions on which they depend are substantially met. Unconditional promises to give due in the next year are recorded net of estimated uncollectible pledges. Unconditional promises to give due in subsequent years are reported at present value net of estimated uncollectible pledges, using risk-free interest rates applicable to the years in which the promises are to be received.

Buildings and Equipment

Buildings and equipment are recorded at cost and depreciated over the estimated useful lives of the related assets. Depreciation is computed on the straight-line method. Maintenance and repairs are charged to operations when incurred. Significant betterments and renewals greater than $1,000 are capitalized. When buildings and equipment are sold or otherwise disposed of, the asset account and related accumulated depreciation account are relieved, and any gain or loss is included in operations.

The useful lives of buildings and equipment for purposes of computing depreciation range from five to forty years.

Beneficial Interest in Perpetual Trusts

The beneficial interest in perpetual trusts is valued based on quoted market values.

Charitable Remainder Trusts

Charitable remainder trusts are valued using payment streams discounted at market rates over the remaining lives of the donors using standard mortality tables.

Art Inventory

The Academy's art inventory is made up of art objects that have been acquired through donations. As of May 31, 2013, this inventory was not recognized in the accompanying consolidated financial statements due to inconsistent appraisals and valuations for the items individually and as a whole. During fiscal year 2014, appraisals were obtained and the art inventory is reflected on the consolidated financial statements. The art inventory is recorded at 60% of the appraised value. Each of the items is catalogued, preserved and cared for as would be appropriate for each of the items within the art inventory. All items within the art inventory that may have been subject to a minimum holding period covenant from the original donor are no longer subject to those covenants, having surpassed the holding periods specified in each of those covenants. Therefore, all items within the art inventory are free of restrictions that would prevent the sale or liquidation of portions of the inventory or the entire inventory. During the years ended May 31, 2014 and 2013, sales of art inventory totaled $58,100 and $-0-, respectively.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Collections

The Academy's collections are made up of art objects that are held for public exhibition, education and research for furtherance of public service. The collections, which were acquired through purchases and contributions since the Academy's inception, are not recognized as assets on the consolidated statements of financial position. Purchases of collection items are recorded as decreases in unrestricted net assets in the year in which the items are acquired. Contributed collection items are not reflected on the consolidated financial statements. Proceeds from sales or insurance recoveries are reflected as increases in temporarily restricted net assets. Each of the items is cataloged, preserved and cared for, and activities verifying their existence and assessing their condition are performed continuously. The collections are subject to a policy that requires proceeds from their sales to be used to acquire other items for collections. During both the years ended May 31, 2014 and 2013, sales of art totaled $-0-. During both the years ended May 31, 2014 and 2013, there were no items in the Academy's collections that were damaged or destroyed.

Retirement Plan

The Academy has a defined contribution plan for all employees. Under the plan, eligible employees may contribute a percentage of their salaries with a matching contribution by the Academy of up to four percent of compensation. Matching contributions were suspended as of July 31, 2009. In addition, the Academy can contribute a discretionary percentage of compensation to the plan for each eligible participant annually. The discretionary contribution was not made for either of the fiscal years 2014 or 2013.

Advertising Costs

The Academy expenses advertising costs as they are incurred.

Amortization

Closing costs associated with the purchase of a building were capitalized and are being amortized over fifteen years using the straight-line method.

Income Tax Status

The Art Academy of Cincinnati is a nonprofit organization as described in Section 501(c)(3) of the Internal Revenue Code and is exempt from federal and state income taxes.

Art Academy Housing, Inc. is a nonprofit organization as described in Section 501(c)(3) of the Internal Revenue Code and is exempt from federal and state income taxes.

The Art Academy of Cincinnati and Affiliate have adopted the provisions of the accounting pronouncement related to accounting for uncertainty in income taxes. The Art Academy of Cincinnati and Affiliate recognized no interest or penalties in the consolidated statements of activities for either of the years ended May 31, 2014 and 2013. If the situation arose in which the Art Academy of Cincinnati and Affiliate would have interest to recognize, it would recognize this as interest expense and penalties would be recognized in other expenses. Currently, the prior three years are open under federal and state statute of limitations and remain subject to review and change. The Academy is not currently under audit nor has the Academy been contacted by these jurisdictions.

Based on the evaluation of the Art Academy of Cincinnati and Affiliate's tax positions, management believes all positions taken would be upheld under an examination. Therefore, no provision for the effects of uncertain tax positions has been recorded for either of the years ended May 31, 2014 or 2013.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Classes of Net Assets

The accompanying consolidated financial statements have been prepared in conformity with the requirements of accounting pronouncements. Accordingly, the net assets of the Academy are reported in each of the following three classes: a) unrestricted net assets, b) temporarily restricted net assets and c) permanently restricted net assets.

Net assets of the two restricted classes are created only by donor-imposed restrictions on their use. All other net assets, including board designated amounts, are legally unrestricted, and are reported as part of the unrestricted class.

The Academy's temporarily restricted net assets are restricted by donors for specific operating purposes or currently not available for use until commitments regarding their use have been fulfilled.

The Academy's permanently restricted net assets consist of various endowment funds.

Subsequent Events

The Academy has evaluated subsequent events through August 22, 2014, which is the date on which the consolidated financial statements were available to be issued.

NOTE 2 – CASH AND CASH FLOW INFORMATION

At various times throughout the year, the Academy may have cash in financial institutions in excess of insured limits. The Federal Deposit Insurance Corporation (FDIC) insures account balances up to $250,000 for each business depositor. As of May 31, 2014 and 2013, the Academy had $45,808 and $-0-, respectively, in cash in financial institutions in excess of insured limits.

The Academy utilizes a separate bank account for receiving federal financial aid funding and monitors interest income relative to these funds in accordance with federal guidelines.

For purposes of the consolidated cash flows statements, the Academy considers all highly liquid investments available for current use with an initial maturity of three months or less to be a cash equivalent.

Cash paid for interest was $20,667 and $28,107 in 2014 and 2013, respectively.

The Academy had noncash financing or investing activities as follows:

	Years Ended May 31,	
	2014	2013
Equipment Acquired through Capital Lease	$ -	$ 18,250
Leasehold Improvement Paid through Long-Term Debt	$ -	$ 15,388

NOTE 3 – BUILDINGS AND EQUIPMENT

Buildings and equipment and related accumulated depreciation consist of the following at May 31, 2014 and 2013.

	Cost	Accumulated Depreciation	Net Book Value
2014			
Land	$ 89,170	$ -	$ 89,170
Buildings and Improvements	3,650,751	120,351	3,530,400
Office Furniture and Equipment	1,089,764	1,035,400	54,364
	$ 4,829,685	$ 1,155,751	$ 3,673,934
2013			
Land	$ 189,520	$ -	$ 189,520
Buildings and Improvements	3,976,369	53,136	3,923,233
Office Furniture and Equipment	1,104,318	999,199	105,119
	$ 5,270,207	$ 1,052,335	$ 4,217,872

Included in the above amounts for May 31, 2013 is the Walnut Street land and building which was partially being used in operations. The cost and the accumulated depreciation of that land and building as of May 31, 2013, were $476,430 and $64,794, respectively. In September, 2013, the Walnut Street building was sold. The building sale price was $550,000.

At May 31, 2013, the Academy recognized an asset impairment on the 1212 Jackson Street property. A commercial appraisal of the property is $3,705,864 and the book value of the property is $9,696,083, therefore an impairment loss of $5,990,219 was recognized.

NOTE 4 – INVESTMENTS

The Academy's investments are summarized as follows:

	May 31,			
	2014		2013	
	Cost	Fair Value	Cost	Fair Value
Unrestricted Fund	$ 558,457	$ 613,315	$ 469,317	$ 529,547
Temporarily Restricted	182,059	196,655	91,264	98,209
Permanently Restricted	749,888	828,962	743,679	828,963
	$ 1,490,404	$ 1,638,932	$ 1,304,260	$ 1,456,719

NOTE 4 – INVESTMENTS (Continued)

The approximate cost and fair values of investments in securities are summarized as follows:

	May 31, 2014 Cost	May 31, 2014 Fair Value	May 31, 2013 Cost	May 31, 2013 Fair Value
Cash Equivalents	$ 15,679	$ 15,679	$ 15,631	$ 15,631
U.S. Government Securities	5,171	5,816	11,134	11,244
Corporate Stocks and Bonds	207,773	273,701	351,990	446,210
Collective and Mutual Funds	1,055,037	1,107,572	748,829	798,893
Exchange-Traded Fund	206,744	236,164	174,267	181,876
Partnership	-	-	2,409	2,865
	$ 1,490,404	$ 1,638,932	$ 1,304,260	$ 1,456,719

The following schedules summarize investment return and its classification in the consolidated statements of activities for the years ended May 31, 2014 and 2013.

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
2014				
Interest and Dividends	$ 16,402	$ 28,278	$ -	$ 44,680
Realized Gains	68,714	79,983	-	148,697
Unrealized Losses	(5,373)	(6,208)	-	(11,581)
Fees	(3,118)	-	-	(3,118)
Total Investment Return	$ 76,625	$ 102,053	$ -	$ 178,678
2013				
Interest and Dividends	$ 16,568	$ 33,912	$ -	$ 50,480
Realized Gains	36,671	57,292	-	93,963
Unrealized Gains	12,042	67,470	-	79,512
Fees	(1,842)	-	-	(1,842)
Total Investment Return	$ 63,439	$ 158,674	$ -	$ 222,113

With Board of Trustees approval, the Academy is permitted to receive a monthly cash distribution from the investments. The spending rate is based on the market value of the investments over a four quarter rolling average and a twelve quarter rolling average for the years ended May 31, 2014 and 2013, respectively. The distribution is recognized in the general fund as investment income. For fiscal year 2014, the monthly cash distribution was not made from the investment accounts.

NOTE 5 – GRANT RECEIVABLE

In August, 2013, the Academy finalized a grant agreement with the Ohio Facilities Construction Commission (OFCC). As part of the agreement, the OFCC will hold $600,000 in escrow to be used as part of the Cultural Project constituting the Commission-funded improvements to reimburse the Academy for a portion of the costs of the acquisition of the 1212 Jackson Street building and the adjacent parking lot. The grant will be amortized on a fifteen year straight line basis. The first draw on the grant was in January, 2014 for $40,000.

NOTE 6 – BENEFICIAL INTEREST IN PERPETUAL TRUSTS

The Academy's beneficial interest in perpetual trusts consists of the following:

Trust	The Academy's Percentage of Trust	May 31, 2014	2013
Wilmer D. Glenn Trust	100%	$ 201,234	$ 192,972

NOTE 7 - INVENTORY

Inventory consists of the following:

Works of Art	$ 288,271	$ -

NOTE 8 – OTHER ASSETS

The following is a summary of other assets:

Cost	$ 25,247	$ 30,361
Accumulated Amortization	15,531	15,866
Other Assets, Net	$ 9,716	$ 14,495

Estimated amortization for the five years subsequent is as follows:

Years Ending May 31,	
2015	$ 1,683
2016	1,683
2017	1,683
2018	1,683
2019	1,683
Thereafter	1,301
	$ 9,716

NOTE 9 – LINE OF CREDIT

The Academy has an unsecured revolving line of credit agreement with a bank for $1,000,000. The line of credit charges interest at LIBOR plus 1.75% (1.90% and 2.01% at May 31, 2014 and 2014, respectively). The line matures in December, 2014. At May 31, 2014 and 2013, the outstanding balance on the line of credit was $650,000 and $665,000, respectively.

NOTE 10 – NOTE PAYABLE

		May 31,		
		2014		2013
Note payable to bank; due in monthly installments of $1,272 including interest of 7%, due April, 2013. The note was refinanced in February, 2013; due in monthly installments of $1,284, including interest of 6%, due February, 2018. The note is collateralized by a parcel of land.	$	174,158	$	178,569
Current Portion		5,132		4,834
Long-Term Portion	$	169,026	$	173,735

The remaining maturities on this note are as follows:

Years Ending May 31,		
2015	$	5,132
2016		5,448
2017		5,784
2018		157,794
	$	174,158

NOTE 11 – CAPITAL LEASE OBLIGATION

The Company incurred a capital lease obligation in 2013, collateralized by the computer server purchased, that charged interest at 12.2%. Depreciation expense for equipment held under the capital lease obligation was $6,083 and $1,521 for the years ended May 31, 2014 and 2013, respectively.

The following is a summary of equipment at cost less accumulated depreciation that was held under the capital lease obligation:

		May 31,		
		2014		2013
Computer Server	$	18,250	$	18,250
Less Accumulated Depreciation		7,604		1,521
Net Capital Lease Obligation Property	$	10,646	$	16,729

NOTE 11 – CAPITAL LEASE OBLIGATION (Continued)

Minimum future lease payments under capital leases for the remainder of the leases:

Years Ending May 31,		
2015	$	7,293
2016		5,470
Total Minimum Lease Payments		12,763
Less Amounts Representing Interest		(1,317)
Present Value of Net Minimum Lease Payments		11,446
Less Current Portion		6,238
Long-Term Capital Lease Obligation	$	5,208

NOTE 12 – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are restricted as follows:

	May 31, 2014		May 31, 2013
Time Restricted			
Investments - Cash	$ 58,918	$	47,610
Beneficial Interest in Charitable Remainder Trusts	63,814		64,864
Purpose Restricted			
Contributions and Gifts	12,757		14,757
Endowments	175,380		118,228
Temporarily Restricted Net Assets	$ 310,869	$	245,459

NOTE 13 – ENDOWMENTS

The Academy's endowment consists of 51 individual funds established for a variety of purposes. Its endowment includes donor-restricted funds and funds designated by the Board of Trustees to function as endowments. As required by generally accepted accounting principles, net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

The Board of Trustees of the Academy has interpreted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the contributed value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Academy classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instruction at the time the accumulation is added to the fund The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Academy in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Academy considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (1) the duration and preservation of the various funds, (2) the purposes of the donor-restricted endowment funds, (3) general economic conditions, (4) the possible effect of inflation and deflation, (5) the expected total return from income and the appreciation of investments, (6) other resources of the Academy and (7) the Academy's investment policies.

Investment Return Objectives, Risk Parameters and Strategies. The Academy has adopted investment and spending policies, approved by the Board of Trustees, for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment funds while also maintaining the purchasing power of those endowment assets over the long-term. Accordingly, the investment process seeks to achieve an after-cost total real rate of return, including investment income as well as capital appreciation, which exceeds the annual distribution with acceptable levels of risk. Endowment assets are invested in a well-diversified asset mix, which includes equity and debt securities, that is intended to result in a consistent inflation-protected rate of return that has sufficient liquidity to make an annual distribution of 4% to 6%, while growing the funds if possible. Therefore, the Academy expects its endowment assets, over time, to produce an average rate of return of approximately 7% annually. Actual returns in any given year may vary from this amount. Investment risk is measured in terms of the total endowment fund; investment assets and allocation between asset classes and strategies are managed to not expose the fund to unacceptable levels of risk.

Spending Policy. The Academy has a policy of appropriating for distribution each year 4% to 6% of its endowment fund's average fair value using one of the following methods 1) average value of the endowment using the trailing 12 quarters; 2) average value of the endowment using the trailing 4 quarters or; 3) value of the endowment using the most recent quarter. In establishing this policy, the Academy considered the long-term expected return on its investment assets, the nature and duration of the individual endowment funds, many of which must be maintained in perpetuity because of donor-restrictions, and the possible effects of inflation. The Academy expects the current spending policy to allow its endowment funds to grow at a nominal average rate of 7% annually. This is consistent with the Academy's objective to maintain the purchasing power of the endowment assets as well as to provide additional real growth through new gifts and investment return.

NOTE 13 – ENDOWMENTS (Continued)

Endowment net asset composition by type of fund as of May 31, 2014 is as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
	$ 576,435	$ 125,980	$ 828,962	$ 1,531,377

Changes in endowment net assets for the year ended May 31, 2014 are as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment Net Assets, Beginning of Year	$ 499,810	$ 36,841	$ 828,963	$ 1,365,614
Investment Return				
Investment Income	16,402	18,972	-	35,374
Net Appreciation (Realized and Unrealized)	63,341	73,774	-	137,115
Total Investment Return	79,743	92,746	-	172,489
Appropriation of Endowment Assets for Expenditures	(3,118)	(3,607)	(1)	(6,726)
Endowment Net Assets, End of Year	$ 576,435	$ 125,980	$ 828,962	$ 1,531,377

As of May 31, 2014, the amount of permanently restricted endowment funds whose balance dropped below the restricted amount had decreased to $49,400. This was a change from the amount at May 31, 2013 of $31,986.

NOTE 13 – ENDOWMENTS (Continued)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net asset composition by type of fund as of May 31, 2013 is as follows:				
	$ 499,810	$ 36,841	$ 828,963	$ 1,365,614
Changes in endowment net assets for the year ended May 31, 2013 are as follows:				
Endowment Net Assets, Beginning of Year	$ 1,376	$ 120,863	$ 1,192,012	$ 1,314,251
Investment Return				
Investment Income	16,568	28,916	-	45,484
Net Appreciation (Realized and Unrealized)	48,713	124,762	-	173,475
Total Investment Return	65,281	153,678	-	218,959
Contributions	-	-	8,582	8,582
Withdrawals for Bond Retirement	(151,131)	(25,047)	-	(176,178)
Appropriation of Endowment Assets for Expenditures	555,533	(183,902)	(371,631)	-
Transfer of Restricted Endowments Whose Balance Is Below the Restricted Amount	28,751	(28,751)	-	-
Endowment Net Assets, End of Year	$ 499,810	$ 36,841	$ 828,963	$ 1,365,614

As of May 31, 2013, the amount of permanently restricted endowment funds whose balance dropped below the restricted amount had decreased to $81,386. This was a change from the amount at May 31, 2012 of $28,752.

During 2013, in accordance with UPMIFA, the Academy had released into unrestricted an endowment fund that was previously recorded as permanently restricted. Therefore, $555,533 was transferred from permanently and temporarily restricted to unrestricted.

NOTE 14 - FUNCTIONAL EXPENSES

The detail of functional expenses is as follows:

	Years Ended May 31,							
	2014				2013			
	Program Services	Management and General	Fundraising	Total	Program Services	Management and General	Fundraising	Total
Salaries	$ 1,420,329	$ 284,885	$ -	$ 1,705,214	$ 1,693,013	$ 213,192	$ -	$ 1,906,205
Payroll Taxes	124,449	20,783	-	145,232	161,082	22,633	-	183,715
Employee Benefits	127,208	29,723	-	156,931	172,349	26,842	-	199,191
Rent	174,898	-	-	174,898	190,002	-	-	190,002
Telephone	-	7,072	-	7,072	-	6,920	-	6,920
Utilities	269,525	1,670	-	271,195	258,823	8,050	-	266,873
Security	194,870	-	-	194,870	193,599	-	-	193,599
Insurance	-	34,365	-	34,365	-	35,750	-	35,750
Bank Charges	-	15,429	-	15,429	70	12,404	-	12,474
Parking	36,503	-	-	36,503	57,514	-	-	57,514
Supplies	65,070	13,571	1,797	80,438	74,863	34,412	-	109,275
Purchased Services	200,898	96,785	6,063	303,746	151,854	66,806	-	218,660
Model Fees	12,066	-	-	12,066	14,340	-	-	14,340
Lecturer's Honorarium	2,655	-	-	2,655	6,690	-	-	6,690
Hospitality	12,713	3,057	2,313	18,083	17,957	1,179	553	19,689
Memberships and Fees	19,268	18,976	-	38,244	13,477	19,170	-	32,647
Books, Videos, and Subscriptions	697	72	-	769	1,127	142	90	1,359
Email and Internet	5,851	5,851	-	11,702	8,440	8,440	-	16,880
Postage and Mail Service	-	5,174	-	5,174	-	4,896	-	4,896
Travel	21,279	1,314	119	22,712	21,961	1,948	-	23,909
Per Diem	7,246	812	-	8,058	7,874	656	-	8,530
Promotion	190,948	658	11,193	202,799	99,037	-	5,648	104,685
Equipment Maintenance and Rental	90,885	22,502	3,434	116,821	105,012	24,067	3,270	132,349
Plant Maintenance	41,866	-	-	41,866	30,636	-	-	30,636
Student Activities	35,942	-	-	35,942	25,860	-	-	25,860
Student Exhibition	11,383	-	-	11,383	26,932	-	-	26,932
Equipment Purchases	-	208	-	208	-	-	-	-
Information Technology	-	-	-	-	434	-	-	434
Scholarships	2,460,437	-	-	2,460,437	2,244,047	-	-	2,244,047
Other Grants	3,890	-	-	3,890	-	-	-	-
Depreciation and Amortization	167,740	5,267	851	173,858	379,699	16,433	1,927	398,059
Interest Expense	20,357	207	103	20,667	27,685	281	141	28,107
Miscellaneous Expense	-	9,575	-	9,575	-	115	-	115
	$ 5,718,973	$ 577,956	$ 25,873	$ 6,322,802	$ 5,984,377	$ 504,336	$ 11,629	$ 6,500,342

NOTE 15 – OPERATING LEASES

The Academy is the lessee in the following lease agreements:

Equipment

The Academy leases equipment for total monthly payments of $2,786. The leases have varying expiration dates ranging from July, 2015 to December, 2017. The Academy incurred lease expense of $28,061 and $19,518 for 2014 and 2013, respectively.

Housing

Art Academy Housing, Inc. leases apartments for the students of the Academy for a base rent of $10,110 per month under an operating lease. The lease expires in August, 2014, with an option to renew for an additional five years. Art Academy Housing, Inc. incurred lease expense related to this lease of $121,317 and $124,657 for 2014 and 2013, respectively.

During 2013, the Academy entered into additional leases for student housing. The lease payments vary from $400 to $2,200 and have an expiration date ending August 31, 2015. The Academy incurred lease expense of $18,645 and $57,754 for 2014 and 2013, respectively.

The following are the net minimum lease payments for the remainder of these leases:

Years Ending May 31,	Housing	Equipment	Total
2015	$ 141,120	$ 28,061	$ 169,181
2016	127,920	14,052	141,972
2017	121,320	11,019	132,339
2018	121,320	5,509	126,829
2019	121,320	-	121,320
Thereafter	626,820	-	626,820
	$ 1,259,820	$ 58,641	$ 1,318,461

NOTE 16 – RELATED PARTIES

The Academy does business with companies who are either owned by or employ a Board of Trustees member. For the fiscal years ended May 31, 2014 and 2013, the Academy had transactions with related parties as follows:

	Years Ended May 31, 2014	2013
Storage Rental	$ 7,500	$ 2,500
Legal Services	$ 34,637	$ 20,238
Consulting Expense	$ 145,198	$ 67,929

NOTE 17 – FAIR VALUES OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used by the Academy in estimating its fair value disclosures for financial instruments:

Cash, cash equivalents, short-term pledges receivable, accounts and other receivables, short-term notes payable and accounts payable and accrued liabilities: The carrying amounts reported in the consolidated statements of financial position approximate fair values because of the short maturities of those instruments.

Short-term and endowment investments: The fair values of investments are based on quoted market prices for those or similar investments.

Long-term pledge receivables and long-term bonds payable: The fair values are estimated by discounting the future cash flows using a current risk free rate of return based on the yield of a U.S. Treasury security with a maturity date similar to the expected collection period, or using stated interest rates.

The fair value for the contribution receivable from a beneficial interest in a charitable remainder trust is determined by using payment streams discounted at 6% over the remaining lives of the donors using standard mortality tables.

The estimated fair values of the Academy's financial instruments as of May 31, 2014, none of which are held for trading purposes, are as follows:

	Carrying Value	Fair Value
Financial Assets		
Cash and Cash Equivalents	$ 369,232	$ 369,232
Accounts and Other Receivables	658,564	658,564
Prepaid Expenses	90,925	90,925
Inventory	288,271	288,271
Investments	1,638,932	1,638,932
Beneficial Interests	265,048	265,048
Financial Liabilities		
Line of Credit	650,000	650,000
Accounts Payable, Accrued and Other Liabilities	1,021,291	1,021,291
Capital Lease	11,446	11,446
Note Payable	174,158	174,158

NOTE 18 – FAIR VALUE MEASURMENTS

U.S. GAAP provides the 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 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 Academy has the ability to access.

Level 2 - Inputs for the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

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

Following is a description of the valuation methodologies used for marketable securities measured at fair value. There have been no changes in the methodologies used at May 31, 2014 and 2013.

The preceding methods described may provide a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Academy believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the operating date.

NOTE 18 – FAIR VALUE MEASURMENTS (Continued)

The following assets and liabilities were measured at fair value as of May 31, 2014:

	Level 1 Quoted Price In Active Markets for Identical Assets	Level 2 Significant Other Observable Inputs	Level 3 Significant Unobservable Inputs
Cash and Cash Equivalents	$ 15,679	$ -	$ -
Mutual Funds			
Money Market Funds	6,304	-	-
Government Agency Funds	-		
Value Funds	-	-	-
Institutional Funds	35,835	-	-
Blended Funds	99,994	-	-
Growth Funds	178,748	-	-
Fixed Funds	506,400	-	-
International Funds	280,291	-	-
Total Mutual Funds	1,107,572	-	-
Stocks			
Consumer Discretionary	39,853	-	-
Consumer Staples	21,909	-	-
Energy	24,327	-	-
Financial	46,278	-	-
Health Care	39,572	-	-
Industrials	39,108	-	-
Information Technology	47,980	-	-
Materials	7,059	-	-
Telecommunication Services	2,982	-	-
Utilities	4,633	-	-
Total Stocks	273,701	-	-
Fixed Income	5,816	-	-
Exchange-Traded Funds	236,164	-	-
Total Investments	$ 1,638,932	$ -	$ -
Beneficial Interest In Trusts	$ 287,020	$ -	$ (21,972)

NOTE 18 – FAIR VALUE MEASURMENTS (Continued)

The following assets and liabilities were measured at fair value as of May 31, 2013:

	Level 1 Quoted Price In Active Markets for Identical Assets	Level 2 Significant Other Observable Inputs	Level 3 Significant Unobservable Inputs
Cash and Cash Equivalents	$ 15,631	$ -	$ -
Mutual Funds			
Money Market Funds	14,840	-	-
Government Agency Funds	6,187	-	-
Value Funds	16,355	-	-
Institutional Funds	92,215	-	-
Blended Funds	15,500	-	-
Growth Funds	77,236	-	-
Fixed Funds	372,117	-	-
International Funds	204,443	-	-
Total Mutual Funds	798,893	-	-
Stocks			
Consumer Discretionary	63,986	-	-
Consumer Staples	46,991	-	-
Energy	33,737	-	-
Financial	82,563	-	-
Health Care	54,485	-	-
Industrials	55,924	-	-
Information Technology	71,551	-	-
Materials	19,259	-	-
Telecommunication Services	5,042	-	-
Utilities	12,672	-	-
Total Stocks	446,210	-	-
Fixed Income	11,244	-	-
Exchange-Traded Funds	181,876	-	-
Partnerships	2,865	-	-
Total Investments	$ 1,456,719	$ -	$ -
Beneficial Interest In Trusts	$ 290,504	$ -	$ (32,668)

NOTE 18 – FAIR VALUE MEASURMENTS (Continued)

Assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3 inputs):

		Beneficial Interest In Trust
May 31, 2013	$	(32,668)
Change in Value		10,696
May 31, 2014	$	(21,972)

NOTE 19 – RISKS AND UNCERTAINTIES

The Academy invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market and credits risks. Due to the level of risks associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect account balances and amounts reported in the consolidated statements of financial position.

NOTE 20 – CHANGES IN ESTIMATE

For the year ended May 31, 2014, the Academy changed its estimates of the value of the works of art it maintains as inventory based on appraisals obtained. The result of this change in estimate resulted in an increase compared to the year ended May 31, 2013 to the art inventory of $346,371 and a change in net assets of $346,371 for the year ended May 31, 2014.

ADDITIONAL INFORMATION

ART ACADEMY OF CINCINNATI AND AFFILIATE
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended May 31, 2014

Federal Grantor/Program Title	Pass-Through Grantor Number	Federal CFDA Number		Federal Expenditures
U.S. Department of Education:				
Federal Direct Student Loans		84.268	$	1,733,163
Federal Pell Grant Program		84.063		419,578
Supplemental Education				
Opportunity Grant Program		84.007		13,212
Federal Work Study Program		84.033		21,607
			$	2,187,560

The accompanying notes are an integral part of this schedule.

ART ACADEMY OF CINCINNATI AND AFFILIATE
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended May 31, 2014

NOTE 1 – BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Art Academy of Cincinnati and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments and Nonprofit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic consolidated financial statements.

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

The Board of Trustees
Art Academy of Cincinnati
and Affiliate
Cincinnati, Ohio

We have audited, in accordance with the 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 consolidated financial statements of the Art Academy of Cincinnati and Affiliate (nonprofit organizations), which comprise the consolidated statement of financial position as of May 31, 2014, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated August 22, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered the Art Academy of Cincinnati and Affiliate'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 consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Art Academy of Cincinnati and Affiliate's internal control. Accordingly, we do not express an opinion on the effectiveness of the organization's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's consolidated financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Art Academy of Cincinnati and Affiliate's consolidated financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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 organization'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 organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

We noted certain additional matters that we reported to management of the Academy in a separate letter dated August 22, 2014.

VonLehman & Company Inc.

Fort Mitchell, Kentucky
August 22, 2014

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133

The Board of Trustees
Art Academy of Cincinnati
and Affiliate
Cincinnati, Ohio

Report on Compliance for Each Major Federal Program

We have audited the Art Academy of Cincinnati and Affiliate's compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Art Academy of Cincinnati and Affiliate's major federal programs for the year ended May 31, 2014. The Art Academy of Cincinnati and Affiliate's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for each of the Art Academy of Cincinnati and Affiliate's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Art Academy of Cincinnati and Affiliate's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the Art Academy of Cincinnati and Affiliate's compliance.

Opinion on Each Major Federal Program

In our opinion, the Art Academy of Cincinnati and Affiliate complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended May 31, 2014.

Other Matters

The results of our auditing procedures disclosed instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 14-01 and 14-02. Our opinion on each major federal program is not modified with respect to these matters.

The Art Academy of Cincinnati and Affiliate's response to the noncompliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The Art Academy of Cincinnati and Affiliate's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Internal Control Over Compliance

Management of the Art Academy of Cincinnati and Affiliate is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Art Academy of Cincinnati and Affiliate's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Art Academy of Cincinnati and Affiliate's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

VonLehman & Company Inc.

Fort Mitchell, Kentucky
August 22, 2014

ART ACADEMY OF CINCINNATI AND AFFILIATE
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Year Ended May 31, 2014

SECTION I – SUMMARY OF AUDITORS' RESULTS

CONSOLIDATED FINANCIAL STATEMENTS	
Type of Auditors' Report Issued	Unmodified
Material weakness(es) identified?	No
Significant deficiencies identified not considered to be material weaknesses?	None Reported
Noncompliance material to consolidated financial statements noted?	No
FEDERAL AWARDS	
Material weakness(es) identified?	No
Significant deficiencies identified not considered to be material weakness?	None Reported
Type of auditors' report issued on compliance for major programs:	Unmodified
Are there any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?	Yes
Major Programs (list):	Federal Direct Student Loans [CFDA 84.268] Federal Pell Grant Program [CFDA 84.063] Supplemental Education Opportunity Grant Program [CFDA 84.007] Federal Work Study Program [CFDA 84.003]
Dollar Threshold: Type A/B Programs	Type A: > $300,000 Type B: > all others
Low Risk Auditee?	No

SECTION II – FINANCIAL STATEMENT FINDINGS

None

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

Item 14-01:

Enrollment Reporting

Criteria: Unless the school expects to complete its next roster within 60 days, the school must notify the lender or the guaranty agency within 30 days, if it discovers that a student who received a loan either did not enroll or ceased to be enrolled on at least a half-time basis.

Condition: During the Enrollment Reporting testing, it was noted a student took a leave of absence on February 1, 2012 but did not update the Enrollment Reporting roster file for the leave of absence.

Cause: The data provider never reported the loan to the NSLDS and therefore, the Academy could not add the record.

Effect: The lender was not notified of the student's leave of absence.

Recommendation: The Academy should put policies and procedures in place to identify all students with changes in status that received financial aid.

Management's Response: A new procedure to reconcile students that are not listed with the NSLDS register with the Financial Aid department has been implemented.

Item 14-02:

Cash Management

Criteria: The institution must make the disbursements as soon as administratively feasible, but no later than 3 business days following the receipt of funds.

Condition: During the Disbursement testing, it was noted that funds received by the Academy on June 27, 2013 and on August 22, 2013 were disbursed 7 business days after receipt of funds. The total received on June 27, 2013 was $5,836 and the total received on August 22, 2013 was $39,680.

Cause: The accounting department was understaffed and busy with student tuition payments therefore causing these funds to be disbursed late.

Effect: $45,516 is considered to be excess cash and is generally required to be returned to the Department of Education.

Recommendation: The Academy should put policies and procedures in place to ensure that the funds are disbursed as soon as administratively feasible, but no later than 3 days following the receipt of funds.

Management's Response: An accounting department restructure with a new employee beginning in August brought about a greater than usual demand in time that caused the delay in posting payments. As this was an extraordinary event, and the new personnel have subsequently improved department effectiveness, this matter should be resolved.

SECTION II – FINANCIAL STATEMENT FINDINGS

None

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

Item 13-01

Return of Funds

Criteria: If a student withdraws or drops out, the institution must determine if a return of Title IV funds is necessary. If a return is necessary, the institution is required to deposit the funds to the Student Financial Assistance (SFA) accounts or return the funds to the Education Department (ED) or to the appropriate Direct Loan lender within forty five days after the institution determines the student withdrew.

Condition: Out of a sample of seventeen returns of Title IV Funds selected for testing, one return was not returned to the appropriate account within the required time frame.

Cause: While a student and academic advisor were developing a plan of study, multiple methods of communication from both individuals to the Financial Aid Office caused the student's financial aid eligibility to be based on a higher credit hour basis than she finally registered for.

Effect: When this inaccuracy was discovered, a return of funds was initiated.

Recommendation: The Academy should put policies and procedures in place to ensure each student's financial aid eligibility is based on credit hours actually registered for.

Managements Response: As a result of this situation the Financial Aid Office revised the procedures to determine financial aid eligibility to include an additional reconciliation process with the student enrollment software.

SUPPLEMENTARY INFORMATION

ART ACADEMY OF CINCINNATI AND AFFILIATE
CONSOLIDATING STATEMENT OF FINANCIAL POSITION
May 31, 2014

ASSETS

	Art Academy of Cincinnati	Art Academy Housing, Inc.	Eliminations	Total
Current Assets				
Cash and Cash Equivalents	$ 369,232	$ -	$ -	$ 369,232
Accounts Receivable, Net	98,564	-	-	98,564
Investments	683,990	-	-	683,990
Grant Receivable	40,000	-	-	40,000
Note Receivable - Related Party	1,308,829	1,308,078	(2,616,907)	-
Prepaid Expenses	90,925	-	-	90,925
Total Current Assets	2,591,540	1,308,078	(2,616,907)	1,282,711
Buildings and Equipment, Net	3,673,652	282	-	3,673,934
Investments	954,942	-	-	954,942
Art Inventory	288,271	-	-	288,271
Grant Receivable	520,000	-	-	520,000
Beneficial Interest in Perpetual Trust	201,234	-	-	201,234
Beneficial Interest in Charitable Remainder Trusts	85,786	-	-	85,786
Deposits	-	13,175	-	13,175
Other Assets, Net	9,716	-	-	9,716
Total Assets	$ 8,325,141	$ 1,321,535	$ (2,616,907)	$ 7,029,769

LIABILITIES AND NET ASSETS

	Art Academy of Cincinnati	Art Academy Housing, Inc.	Eliminations	Total
Current Liabilities				
Line of Credit	$ 650,000	$ -	$ -	$ 650,000
Accounts Payable	160,697	-	-	160,697
Accrued Expenses	283,296	17,298	-	300,594
Capital Lease - Current Portion	6,238	-	-	6,238
Note Payable - Related Party	1,311,878	1,305,029	(2,616,907)	-
Note Payable - Current Portion	5,132	-	-	5,132
Total Current Liabilities	2,417,241	1,322,327	(2,616,907)	1,122,661
Long-Term Liabilities				
Charitable Remainder Trust	21,972	-	-	21,972
Deferred Revenue	560,000	-	-	560,000
Capital Lease - Long-Term	5,208	-	-	5,208
Note Payable - Long-Term	169,026	-	-	169,026
Total Long-Term Liabilities	756,206	-	-	756,206
Total Liabilities	3,173,447	1,322,327	(2,616,907)	1,878,867
Net Assets	5,151,694	(792)	-	5,150,902
Total Liabilities and Net Assets	$ 8,325,141	$ 1,321,535	$ (2,616,907)	$ 7,029,769

ART ACADEMY OF CINCINNATI AND AFFILIATE
CONSOLIDATING STATEMENT OF ACTIVITIES
Year Ended May 31, 2014

	Art Academy of Cincinnati	Art Academy Housing, Inc.	Eliminations	Total
Revenue and Support				
Grants, Contributions and Gifts	$ 296,779	$ -	$ -	$ 296,779
Tuition Income	5,166,424	-	-	5,166,424
Investment Income	44,680	-	-	44,680
Other Income	532,362	229,495	-	761,857
Total Revenue and Support	6,040,245	229,495	-	6,269,740
Expenses				
Program Services	5,514,343	204,630	-	5,718,973
Management and General	577,956	-	-	577,956
Fundraising	25,873	-	-	25,873
Total Expenses	6,118,172	204,630	-	6,322,802
(Deficit) Excess of Revenue, Support and Reclassifications Over Expenses	(77,927)	24,865	-	(53,062)
Realized Gain on Investments	148,697	-	-	148,697
Unrealized Loss on Investments	(11,581)	-	-	(11,581)
Change in Beneficial Interest in Perpetual Trust	8,261	-	-	8,261
Change in Beneficial Interest in Charitable Remainder Trusts	(1,050)	-	-	(1,050)
Change in Net Assets	66,400	24,865	-	91,265
Net Assets Beginning of Year	5,085,294	(25,657)	-	5,059,637
Net Assets End of Year	$ 5,151,694	$ (792)	$ -	$ 5,150,902