ART ACADEMY OF CINCINNATI AND AFFILIATES

May 31, 2012

CONSOLIDATED FINANCIAL STATEMENTS AND INDEPENDENT AUDITORS' REPORT INCLUDING SUPPLEMENTAL INFORMATION

VonLehman
CPA & ADVISORY FIRM

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ART ACADEMY OF CINCINNATI AND AFFILIATES
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VonLehman
CPA & ADVISORY FIRM

INDEPENDENT AUDITORS' REPORT

To the Board of Trustees
Art Academy of Cincinnati
and Affiliates
Cincinnati, Ohio

We have audited the accompanying consolidated statements of financial position of the Art Academy of Cincinnati (a nonprofit organization) and Affiliates as of May 31, 2012 and 2011, and the related consolidated statements of activities, members' equity and cash flows for the years then ended. These financial statements are the responsibility of the Academy's management. Our responsibility is to express an opinion on these 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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our 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 Affiliates as of May 31, 2012 and 2011, and the changes in its consolidated net assets and its consolidated cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated September 14, 2012 on our consideration of the Art Academy of Cincinnati and Affiliates' internal control over financial reporting and on our tests of its compliance with certain provisions, 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* and should be considered in assessing the results of our audit.

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*, and is not a required part of the financial statements. The consolidating statement of financial position, consolidating statement of activities, and consolidated statement of member's equity are presented for purposes of additional analysis and are 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 audit 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 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 taken as a whole.

VonLehman & Company Inc.

Fort Mitchell, Kentucky
September 14, 2012

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ART ACADEMY OF CINCINNATI AND AFFILIATES
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
May 31, 2012

ASSETS

	Unrestricted				Permanently Restricted	
	General	Board Designated	Plant	Temporarily Restricted	Endowment	Total
Current Assets						
Cash and Cash Equivalents	$ 144,933	$ -	$ 1,689	$ 185,637	$ 8,582	$ 340,841
Accounts Receivable	144,338	-	-	-	-	144,338
Pledges Receivable	-	-	-	2,445	-	2,445
Investment Receivable	(110,138)	-	-	110,138	-	-
Prepaid Expenses	68,145	-	-	-	-	68,145
Total Current Assets	247,278	-	1,689	298,220	8,582	555,769
Buildings and Equipment, Net	-	-	10,553,865	-	-	10,553,865
Investments	25,467	1,376	-	177,233	1,192,012	1,396,088
Pledges Receivable	-	-	-	1,895	-	1,895
Beneficial Interest in Perpetual Trust	-	-	-	-	171,741	171,741
Beneficial Interest in Charitable Remainder Trusts	-	-	-	102,530	-	102,530
Deposits	-	-	16,610	-	-	16,610
Other Assets, Net	-	-	16,519	-	-	16,519
Total Assets	$ 272,745	$ 1,376	$ 10,588,683	$ 579,878	$ 1,372,335	$ 12,815,017

LIABILITIES AND EQUITY

	General	Board Designated	Plant	Temporarily Restricted	Endowment	Total
Current Liabilities						
Line of Credit	$ 400,000	$ -	$ -	$ -	$ -	$ 400,000
Accounts Payable	172,526	-	-	-	-	172,526
Accrued Expenses	183,527	-	69,645	166,456	-	419,628
Note Payable - Current Portion	-	-	167,339	-	-	167,339
Total Current Liabilities	756,053	-	236,984	166,456	-	1,159,493
Long-Term Liabilities						
Charitable Remainder Trust	-	-	-	34,342	-	34,342
Total Liabilities	756,053	-	236,984	200,798	-	1,193,835
Equity						
Members' Equity	-	-	1,689	-	-	1,689
Net Assets	(483,308)	1,376	10,350,010	379,080	1,372,335	11,619,493
Total Equity	(483,308)	1,376	10,351,699	379,080	1,372,335	11,621,182
Total Liabilities and Equity	$ 272,745	$ 1,376	$ 10,588,683	$ 579,878	$ 1,372,335	$ 12,815,017

See accompanying notes.

ART ACADEMY OF CINCINNATI AND AFFILIATES
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
May 31, 2011

	Unrestricted				Permanently Restricted	
ASSETS	**General**	**Board Designated**	**Plant**	**Temporarily Restricted**	**Endowment**	**Total**
Current Assets						
Cash and Cash Equivalents	$ 283,589	$ -	$ 39,693	$ 158,562	$ 14,414	$ 496,258
Accounts Receivable	118,373	-	-	-	-	118,373
Pledges Receivable	-	-	-	2,445	-	2,445
Interest and Dividends Receivable	-	29	-	-	-	29
Prepaid Expenses	85,567	-	16,551	-	-	102,118
Total Current Assets	487,529	29	56,244	161,007	14,414	719,223
Buildings and Equipment, Net	-	-	10,916,251	-	-	10,916,251
Investments	25,263	2,316,241	25,099	2,248,176	1,245,222	5,860,001
Pledges Receivable	-	-	-	11,895	-	11,895
Beneficial Interest in Perpetual Trust	-	-	-	-	180,707	180,707
Beneficial Interest in Charitable Remainder Trusts	-	-	-	125,721	-	125,721
Deposits	-	-	13,386	-	-	13,386
Other Assets, Net	-	-	131,790	-	-	131,790
Total Assets	$ 512,792	$ 2,316,270	$ 11,142,770	$ 2,546,799	$ 1,440,343	$ 17,958,974
LIABILITIES AND EQUITY						
Current Liabilities						
Accounts Payable	$ 143,161	$ -	$ 6,445	$ -	$ -	$ 149,606
Accrued Expenses	173,138	-	110,164	148,829	-	432,131
Note Payable - Current Portion	-	-	3,378	-	-	3,378
Bond Payable - Current Portion	-	-	4,300,000	-	-	4,300,000
Total Current Liabilities	316,299	-	4,419,987	148,829	-	4,885,115
Long-Term Liabilities						
Charitable Remainder Trust	-	-	-	46,842	-	46,842
Note Payable (Less Current Portion)	-	-	167,383	-	-	167,383
Total Long Term Liabilities	-	-	167,383	46,842	-	214,225
Fair Market Value of Interest Rate Swap	-	-	60,784	-	-	60,784
Total Liabilities	316,299	-	4,648,154	195,671	-	5,160,124
Equity						
Members' Equity	-	-	1,561,695	-	-	1,561,695
Fair Market Value of Interest Rate Swap	-	-	(60,784)	-	-	(60,784)
Net Assets	196,493	2,316,270	4,993,705	2,351,128	1,440,343	11,297,939
Total Equity	196,493	2,316,270	6,494,616	2,351,128	1,440,343	12,798,850
Total Liabilities and Equity	$ 512,792	$ 2,316,270	$ 11,142,770	$ 2,546,799	$ 1,440,343	$ 17,958,974

See accompanying notes.

ART ACADEMY OF CINCINNATI AND AFFILIATES
CONSOLIDATED STATEMENT OF ACTIVITIES
Year Ended May 31, 2012

	Unrestricted				Permanently Restricted	
	General	Board Designated	Plant	Temporarily Restricted	Endowment	Total
Revenue and Support						
Grants, Contributions and Gifts	$ 258,214	$ -	$ -	$ 1,847	$ 12,081	$ 272,142
Tuition Income	5,335,302	-	-	-	-	5,335,302
Investment Income	-	2,952	-	51,457	-	54,409
Investment Income Allocation	72,917	(1,894)	-	(71,023)	-	-
Other Income	13,836	-	224,556	-	-	238,392
Total Revenue and Support	5,680,269	1,058	224,556	(17,719)	12,081	5,900,245
Net Assets Released from Restrictions	73,523	-	-	(2,400)	(71,123)	-
Total Revenue, Support and Reclassifications	5,753,792	1,058	224,556	(20,119)	(59,042)	5,900,245
Expenses						
Program Services	5,359,928	-	946,665	-	-	6,306,593
Management and General	597,594	3,782	3,864	-	-	605,240
Fundraising	20,809	-	1,932	-	-	22,741
inc						
Total Expenses	5,978,331	3,782	952,461	-	-	6,934,574
Deficit of Revenue, Support and Reclassifications Over Expenses	(224,539)	(2,724)	(727,905)	(20,119)	(59,042)	(1,034,329)
Interfund Equity Transfers	(345,124)	(2,377,586)	4,524,154	(1,801,444)	-	-
Realized Loss on Investments	-	(19,727)	-	(90,647)	-	(110,374)
Unrealized (Loss) Gain on Investments	-	(7,037)	50	(67,105)	-	(74,092)
Excess Loss on Endowment Investments	(110,138)	92,180	-	17,958	-	-
Change in Beneficial Interest in Perpetual Trust	-	-	-	-	(8,966)	(8,966)
Change in Beneficial Interest in Charitable Remainder Trusts	-	-	-	(10,691)	-	(10,691)
Change in Net Assets	(679,801)	(2,314,894)	3,796,299	(1,972,048)	(68,008)	(1,238,452)
Change in Fair Market Value of Interest Rate Swap	-	-	60,784	-	-	60,784
	(679,801)	(2,314,894)	3,857,083	(1,972,048)	(68,008)	(1,177,668)
Net Assets Beginning of Year	196,493	2,316,270	6,494,616	2,351,128	1,440,343	12,798,850
Net Assets End of Year	$ (483,308)	$ 1,376	$ 10,351,699	$ 379,080	$ 1,372,335	$ 11,621,182

See accompanying notes.

ART ACADEMY OF CINCINNATI AND AFFILIATES
CONSOLIDATED STATEMENT OF ACTIVITIES
Year Ended May 31, 2011

	Unrestricted				Permanently Restricted	
	General	Board Designated	Plant	Temporarily Restricted	Endowment	Total
Revenue and Support						
Grants, Contributions and Gifts	$ 338,026	$ -	$ -	$ (8,376)	$ 12,833	$ 342,483
Tuition Income	4,804,294	-	-	-	-	4,804,294
Investment Income	-	24,706	-	131,685	-	156,391
Investment Income Allocation	351,108	(57,033)	-	(294,075)	-	-
Other Income	5,313	-	161,133	-	-	166,446
Total Revenue and Support	5,498,741	(32,327)	161,133	(170,766)	12,833	5,469,614
Net Assets Released from Restrictions	11,042	(1,933)	-	(9,109)	-	-
Total Revenue, Support and Reclassifications	5,509,783	(34,260)	161,133	(179,875)	12,833	5,469,614
Expenses						
Program Services	4,992,552	-	844,165	-	-	5,836,717
Management and General	479,111	20,263	98,220	-	-	597,594
Fundraising	25,582	-	2,836	-	-	28,418
Total Expenses	5,497,245	20,263	945,221	-	-	6,462,729
Excess (Deficit) of Revenue, Support and Reclassifications Over Expenses	12,538	(54,523)	(784,088)	(179,875)	12,833	(993,115)
Interfund Equity Transfers	549,883	(956,096)	423,184	(16,971)	-	-
Realized Loss on Investments	-	(105,208)	-	(542,362)	-	(647,570)
Unrealized Gain on Investments	-	250,186	-	1,289,864	-	1,540,050
Excess Gain on Endowment Investments	-	41,669	-	(41,669)	-	-
Change in Beneficial Interest in Perpetual Trust	-	-	-	-	19,462	19,462
Change in Beneficial Interest in Charitable Remainder Trusts	-	-	-	6,575	-	6,575
Other Members' Interest	-	-	44,820	-	-	44,820
Change in Net Assets	562,421	(823,972)	(316,084)	515,562	32,295	(29,778)
Other Members' Interest	-	-	(44,820)	-	-	(44,820)
Buyout of Other Members	-	-	(30,000)	-	-	(30,000)
Change in Fair Market Value of Interest Rate Swap	-	-	86,085	-	-	86,085
	562,421	(823,972)	(304,819)	515,562	32,295	(18,513)
Net Assets Beginning of Year, As Restated	(365,928)	3,140,242	6,799,435	1,835,566	1,408,048	12,817,363
Net Assets End of Year	$ 196,493	$ 2,316,270	$ 6,494,616	$ 2,351,128	$ 1,440,343	$ 12,798,850

See accompanying notes.

ART ACADEMY OF CINCINNATI AND AFFILIATES
CONSOLIDATED STATEMENT OF MEMBERS' EQUITY

	Members' Equity (Deficit)	Other Members' Equity	Fair Market Value of Interest Rate Swap	Total
Balance - May 31, 2010	$ (37,481)	$ 1,676,322	$ (146,869)	$ 1,491,972
Net Loss	(2,326)	-	-	(2,326)
Other Members' Net Loss	-	(44,820)	-	(44,820)
Buyout of Other Members		(30,000)	-	(30,000)
Transfer of Other Members' Equity	1,601,502	(1,601,502)	-	-
Change in Fair Market Value of Interest Rate Swap	-	-	86,085	86,085
Balance - May 31, 2011	1,561,695	-	(60,784)	1,500,911
Net Loss	(386,395)	-	-	(386,395)
Dissolution of Entity	(1,173,611)	-	-	(1,173,611)
Change in Fair Market Value of Interest Rate Swap	-	-	60,784	60,784
Balance - May 31, 2012	$ 1,689	$ -	$ -	$ 1,689

See accompanying notes.

ART ACADEMY OF CINCINNATI AND AFFILIATES
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended May 31, 2012	2011
Cash Flows from Operating Activities		
Change in Net Assets	$ (1,238,452)	$ (29,778)
Adjustments to Reconcile Change in Net Assets to Net Cash Provided by Operating Activities		
Depreciation	430,088	420,551
Amortization	115,271	10,934
Realized Loss on Investments	110,374	647,570
Unrealized Loss (Gain) on Investments	74,092	(1,540,050)
Change in Beneficial Interest in Perpetual Trust	8,966	(19,462)
Change in Beneficial Interest in Charitable Remainder Trusts	10,691	(6,575)
Other Members' Interest	-	(44,820)
Contributions Restricted for Capital Purchases	(1,847)	(8,376)
Change in Operating Assets		
Accounts Receivable	(25,965)	415,299
Pledges Receivable	10,000	13,701
Interest and Dividends Receivable	29	7
Prepaid Expenses	33,973	(45,567)
Deposits	(3,224)	(3,751)
Change in Operating Liabilities		
Accounts Payable	22,920	7,756
Accrued Expenses	(12,503)	(11,162)
Net Cash Used by Operating Activities	(465,587)	(193,723)
Cash Flows from Investing Activities		
Proceeds from Sale of Investments	5,928,560	2,478,890
Purchase of Investments	(1,649,113)	(2,237,213)
Acquisition of Building and Equipment	(67,702)	(81,025)
Net Cash Provided by Investing Activities	4,211,745	160,652
Cash Flows from Financing Activities		
Net Change in Line of Credit	400,000	-
Contributions Restricted for Capital Purchases	1,847	8,376
Payments on Note Payable	(3,422)	(3,191)
Payment to Other Members	-	(30,000)
Payments on Bond Payable	(4,300,000)	-
Net Cash Used by Financing Activities	(3,901,575)	(24,815)
Net Change in Cash and Cash Equivalents	(155,417)	(57,886)
Beginning Balance - Cash and Cash Equivalents	496,258	554,144
Ending Balance - Cash and Cash Equivalents	$ 340,841	$ 496,258

See accompanying notes.

NOTE 1 – ACCOUNTING POLICIES

The Art Academy of Cincinnati's 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.

Academy Advancement Limited is organized in the State of Ohio as a limited liability company. Academy Advancement Limited was formed during fiscal year 2004 to be the managing member of 1212 Jackson, LLC. Academy Advancement Limited is a wholly owned subsidiary of the Art Academy of Cincinnati. In December, 2011, the Art Academy of Cincinnati as the sole owner of Academy Advancement Limited voted to dissolve the entity. The majority of the assets and liabilities were transferred to the Art Academy of Cincinnati.

1212 Jackson, LLC is organized in the State of Ohio as a limited liability company. 1212 Jackson, LLC was formed during fiscal year 2004 to own and operate the real estate facilities for the benefit of the Art Academy of Cincinnati. In May 2011, Academy Advancement Limited purchased the majority interest of 1212 Jackson, LLC.

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 May 31, 2012, the consolidated financial statements include Art Academy of Cincinnati and Art Academy Housing.

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

Principles of Consolidation

The consolidated financial statements also include the accounts of Academy Advancement Limited and Art Academy Housing, Inc. These entities are related to the Academy because the Academy has assumed the financial and day-to-day operational management functions for these entities. Under U.S. generally accepted accounting principles, the Academy is required to present consolidated financial statements reflecting the financial position and results of operations of all four 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 May 31, 2012 and 2011.

NOTE 1 – ACCOUNTING POLICIES (Continued)

Investments

Investments in equity securities and debt securities are stated at fair market value. 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 financial statements in conformity with U.S. generally accepted accounting principles 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 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.

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.

Donated Facility

The Academy utilized one donated facility in downtown Cincinnati. The Academy has no ownership rights in this facility. The value of rent for this donated facility has not been recorded since it is not readily measured or valued. During the year ended May 31, 2011, the Academy discontinued their glass blowing program and thus no longer utilizes the donated facility. As of May 31, 2012, the Academy has no donated facilities that are being utilized.

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.

NOTE 1 – ACCOUNTING POLICIES (Continued)

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.

Collections

The collections, which were acquired through purchases and contributions since the Art Academy of Cincinnati's inception, are not recognized as assets on the statement 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 financial statements. Proceeds from sales or insurance recoveries are reflected as increases in temporarily restricted net assets.

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 fiscal year 2012 or 2011.

Advertising Costs

Advertising costs are expensed as 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.

Costs associated with the issuance of bonds were capitalized and are being amortized over the life of the bonds using the straight-line method. During 2012, the unamortized issuance costs were written off in connection with the bond retirement.

Cost associated with the organization of 1212 Jackson LLC have been capitalized and were amortized over five years using the straight-line method. During 2012, the cost and accumulated amortization were written off in connection with the closing of 1212 Jackson LLC.

Income Tax Status

The Academy 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.

Academy Advancement Limited has elected to be taxed as a corporation and therefore is subject to federal, state and local income taxes. This entity was dissolved as of December 31, 2011.

1212 Jackson LLC is a limited liability company and all of the tax liabilities and benefits are passed directly to its members (effective May 31, 2011, Academy Advancement Limited is the only member of 1212 Jackson, LLC).

NOTE 1 – ACCOUNTING POLICIES (Continued)

Art Academy Housing 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 Affiliates has adopted the provisions of the accounting pronouncement related to accounting for uncertainty in income taxes. The Art Academy of Cincinnati and Affiliates recognized no interest or penalties in the consolidated statement of activities for the years ended May 31, 2012 and 2011. If the situation arose in which the Art Academy of Cincinnati and Affiliates would have interest to recognize, it would recognize this as interest expense and penalties would be recognized in other expenses. Tax years still open under federal and state statute of limitations remain subject to review and change.

Based on the evaluation of the Art Academy of Cincinnati and Affiliates' 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 the years ended May 31, 2012 and 2011.

Classes of Net Assets

The accompanying 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.

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. In addition, the FDIC insures 100% of all non-interest bearing accounts through December 31, 2012. Using these criteria, the Academy had no cash in excess of insured limits at both December 31, 2012 and 2011.

The Art Academy of Cincinnati 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 cash flows statement, 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 $79,610 and $156,976 in 2012 and 2011, respectively.

NOTE 3 – BUILDINGS AND EQUIPMENT

Buildings and equipment and related accumulated depreciation consist of the following at May 31, 2012 and 2011.

	Cost	Accumulated Depreciation	Net Book Value
2012			
Land	$ 362,100	$ -	$ 362,100
Buildings and Improvements	12,331,108	2,277,966	10,053,142
Office Furniture and Equipment	1,070,578	931,955	138,623
	$ 13,763,786	$ 3,209,921	$ 10,553,865
2011			
Land	$ 362,100	$ -	$ 362,100
Buildings and Improvements	12,331,108	1,947,820	10,383,288
Office Furniture and Equipment	1,002,876	832,013	170,863
	$ 13,696,084	$ 2,779,833	$ 10,916,251

Included in the above amounts for May 31, 2012 is the Walnut Street building which is partially being used in operations. At May 31, 2011 the Walnut Street building was not being used in operations with a small portion being leased. The cost and accumulated depreciation of that land and building as of May 31, 2012 were $508,144 ($508,144 as of May 31, 2011) and $63,946 ($49,384 as of May 31, 2011), respectively.

NOTE 4 – PLEDGES RECEIVABLE

The Academy's pledges receivable are as follows:

	May 31, 2012	May 31, 2011
Receivable in Less than One Year	$ 2,500	$ 2,500
Less Allowance for Uncollectible Pledges Receivable	55	55
Net Receivable in Less than One Year	2,445	2,445
Receivable in One to Five Years	2,500	12,500
Less Present Value Discount (6%)	550	550
Less Allowance for Uncollectible Pledges Receivable	55	55
Net Receivable in One to Five Years	1,895	11,895
Net Receivable	$ 4,340	$ 14,340

NOTE 5 – COLLECTIONS

The Art Academy of Cincinnati collections are made up of art objects that are held for public exhibition, education and research for furtherance of public service. The collection, acquired through donations, is not recognized in the accompanying financial statements. 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 the years ended May 31, 2012 and 2011, sales of art totaled $-0-. During the years ended May 31, 2012 and 2011, there were no items in the Art Academy of Cincinnati's collections that were damaged or destroyed.

NOTE 6 – INVESTMENTS

The Academy's investments are summarized as follows:

	May 31,			
	2012		2011	
	Cost	Fair Value	Cost	Fair Value
Unrestricted Fund	$ 27,847	$ 26,843	$ 2,410,216	$ 2,366,603
Temporarily Restricted	175,082	177,233	2,062,100	2,248,176
Permanently Restricted	1,125,037	1,192,012	1,245,222	1,245,222
	$ 1,327,966	$ 1,396,088	$ 5,717,538	$ 5,860,001

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

	May 31,			
	2012		2011	
	Cost	Fair Value	Cost	Fair Value
Cash Equivalents	$ 15,449	$ 15,449	$ 53,341	$ 53,341
U.S. Government Securities	8,795	10,079	37,173	38,490
Corporate Stocks and Bonds	416,699	488,957	1,986,473	1,819,083
Collective and Mutual Funds	838,651	832,566	3,378,191	3,591,132
Exchange-Traded Fund	48,372	49,037	262,360	357,955
	$ 1,327,966	$ 1,396,088	$ 5,717,538	$ 5,860,001

NOTE 6 – INVESTMENTS (Continued)

The following schedules summarize investment return and its classification in the statements of activities for the years ended May 31, 2012 and 2011.

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
2012				
Interest and Dividends	$ 2,952	$ 51,457	$ -	$ 54,409
Realized Losses	(19,727)	(90,647)	-	(110,374)
Unrealized Losses	(6,987)	(67,105)	-	(74,092)
Fees	(3,782)	-	-	(3,782)
Total Investment Return	$ (27,544)	$ (106,295)	$ -	$ (133,839)
2011				
Interest and Dividends	$ 24,706	$ 131,685	$ -	$ 156,391
Realized Losses	(105,208)	(542,362)	-	(647,570)
Unrealized Gains	250,186	1,289,864	-	1,540,050
Fees	(20,263)	-	-	(20,263)
Total Investment Return	$ 149,421	$ 879,187	$ -	$ 1,028,608

With Board of Trustee 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, 2012 and 2011, respectively. The distribution is recognized in the general fund as investment income.

NOTE 7 – BENEFICIAL INTEREST IN PERPETUAL TRUSTS

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

Trust	Academy's Percentage of Trust	May 31, 2012	May 31, 2011
Wilmer D. Glenn Trust	100%	$ 171,741	$ 180,707

NOTE 8 – OTHER ASSETS

The following is a summary of other assets:

	May 31, 2012			
	Closing Cost	Bond Issuance Cost	Organizational Cost	Total
Cost	$ 30,361	$ -	$ -	$ 30,361
Accumulated Amortization	13,842	-	-	13,842
Other Assets, Net	$ 16,519	$ -	$ -	$ 16,519

	May 31, 2011			
	Closing Cost	Bond Issuance Cost	Organizational Cost	Total
Cost	$ 30,361	$ 172,237	$ 50,817	$ 253,415
Accumulated Amortization	11,817	58,991	50,817	121,625
Other Assets, Net	$ 18,544	$ 113,246	$ -	$ 131,790

Estimated amortization for the five years subsequent is as follows:

Years Ending May 31,	
2013	$ 2,025
2014	2,025
2015	2,025
2016	2,025
2017	2,025
Thereafter	6,394
	$ 16,519

NOTE 9 – LINE OF CREDIT

The Academy has an unsecured revolving line of credit agreement. In June, 2011, the bank increased the line of credit from $400,000 to $1,000,000.The line of credit charges interest at LIBOR plus 1.75% at May 31, 2012 (2.01% at May 31, 2012) and at LIBOR rate plus 1.75% at May 31, 2011 (6.73% at May 31, 2011). The line matures in December, 2012. At May 31, 2012 and 2011, the outstanding balance on the line of credit was $400,000 and $-0-, respectively.

NOTE 10 – BOND PAYABLE

In October, 2004, 1212 Jackson, LLC authorized the issuance of Adjusted Rate Taxable Securities, Series 2004, with a maximum aggregate principal amount up to $8,000,000. The proceeds were used for the renovation of the Jackson Street building. The bond was paid off in September, 2011.

NOTE 11 – NOTE PAYABLE

	2012	2011
Note payable to bank; due in monthly installments of $1,272, including interest of 7.00%, due April, 2013. The note is collateralized by a parcel of land.	$ 167,339	$ 170,761
Current Portion	167,339	3,378
Long-Term Portion	$ -	$ 167,383

The remaining maturities on this note are as follows:

Year Ending May 31,	
2013	$ 167,339

NOTE 12 – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are restricted as follows:

	May 31,	
	2012	2011
Time Restricted		
Investments - Cash	$ 60,794	$ 46,750
Beneficial Interest in Charitable Remainder Trusts	68,188	78,879
Purpose Restricted		
Building on Rich Tradition Campaign	4,340	16,740
Contributions and Gifts	14,757	17,157
Endowments	231,001	2,191,602
Net Receivable	$ 379,080	$ 2,351,128

NOTE 13 – ENDOWMENTS

The Academy's endowment consists of 63 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.

NOTE 13 – ENDOWMENTS (Continued)

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 4.66%, while growing the funds if possible. Therefore, the Academy expects its endowment assets, over time, to produce an average rate of return of approximately 5.50% – 7.50% 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 4.66% of its endowment fund's average fair value of the prior 4 quarters through the calendar year-end preceding the fiscal year in which the distribution is planned. 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 1.00% – 2.00% 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)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net asset composition by type of fund as of May 31, 2012:				
	$ 1,376	$ 120,863	$ 1,192,012	$ 1,314,251

Changes in endowment net assets for the year ended May 31, 2012 are as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment Net Assets, Beginning of Year	$ 2,316,241	$ 2,191,602	$ 1,245,222	$ 5,753,065
Investment Return				
Investment Income	2,952	51,659	-	54,611
Net Appreciation (Realized and Unrealized)	(26,764)	(157,752)	-	(184,516)
Total Investment Return	(23,812)	(106,093)	-	(129,905)
Contributions	-	-	17,913	17,913
Withdrawals for Bond Retirement	(2,270,607)	(1,903,139)	-	(4,173,746)
Appropriation of Endowment Assets for Expenditures	(2,488)	(79,465)	(71,123)	(153,076)
Transfer of Restricted Endowments Whose Balance Is Below the Restricted Amount	(17,958)	17,958	-	-
Endowment Net Assets, End of Year	$ 1,376	$ 120,863	$ 1,192,012	$ 1,314,251

As of May 31, 2012, the amount of permanently restricted endowment funds whose balance dropped below the restricted amount had increased to $110,138. This was a change from the amount at May 31, 2011 of $17,958.

NOTE 13 – ENDOWMENTS (Continued)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net asset composition by type of fund as of May 31, 2011:				
	$ 2,316,241	$ 2,191,602	$ 1,245,222	$ 5,753,065

Changes in endowment net assets for the year ended May 31, 2011 are as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment Net Assets, Beginning of Year	$ 2,165,206	$ 1,669,434	$ 1,245,222	$ 5,079,862
Investment Return				
Investment Income	24,706	127,382	-	152,088
Net Appreciation (Realized and Unrealized)	144,978	747,502	-	892,480
Total Investment Return	169,684	874,884	-	1,044,568
Appropriation of Endowment Assets for Expenditures	(60,318)	(311,047)	-	(371,365)
Transfer of Restricted Endowments Whose Balance Is Below the Restricted Amount	41,669	(41,669)	-	-
Endowment Net Assets, End of Year	$ 2,316,241	$ 2,191,602	$ 1,245,222	$ 5,753,065

As of May 31, 2011, the amount of permanently restricted endowment funds whose balance dropped below the restricted amount had decreased to $92,180. This was a change from the amount at May 31, 2010 of $41,669.

NOTE 14 - FUNCTIONAL EXPENSES

The detail of functional expenses is as follows:

	Years Ended May 31,							
	2012				2011			
	Program Services	Management and General	Fundraising	Total	Program Services	Management and General	Fundraising	Total
Salaries	$ 1,676,677	$ 250,006	$ -	$ 1,926,683	$ 1,634,777	$ 287,965	$ -	$ 1,922,742
Payroll Taxes	174,632	16,461	-	191,093	132,264	22,343	-	154,607
Employee Benefits	182,055	29,002	-	211,057	159,476	38,292	-	197,768
Rent	171,252	-	-	171,252	114,839	-	-	114,839
Telephone	848	9,063	-	9,911	1,111	9,479	-	10,590
Utilities	254,563	7,985		262,548	306,047	3,107	1,554	310,708
Security	195,755	-	-	195,755	200,713	-	-	200,713
Insurance	-	34,440	-	34,440	-	31,533	-	31,533
Bank Charges	491	15,484	-	15,975	6,036	34,562	-	40,598
Parking	52,086	5,275	-	57,361	52,078	830	-	52,908
Supplies	97,333	21,641	10	118,984	71,726	18,124	58	89,908
Purchased Services	50,153	94,585	-	144,738	44,689	55,425	10,035	110,149
Model Fees	15,410	-	-	15,410	16,631	-	-	16,631
Lecturer's Honorarium	13,095	-	-	13,095	20,496	-	-	20,496
Hospitality	24,952	4,991	1,179	31,122	26,848	2,173	472	29,493
Memberships and Fees	20,452	26,702	-	47,154	9,454	24,411	-	33,865
Books, Videos, and Subscriptions	1,722	79	-	1,801	2,940	78	-	3,018
Email and Internet	6,403	6,403	-	12,806	6,594	6,569	-	13,163
Postage and Mail Service	-	10,115	-	10,115	-	12,628	-	12,628
Travel	21,863	3,149	48	25,060	19,884	1,170	97	21,151
Per Diem	8,751	1,067	-	9,818	8,814	154	-	8,968
Promotion	162,091	1,494	3,812	167,397	151,642	443	3,770	155,855
Newsletter	30	-	10,908	10,938	15	-	8,065	8,080
Equipment Maintenance and Rental	41,104	26,396	3,167	70,667	44,221	20,777	394	65,392
Plant Maintenance	28,498	-	-	28,498	58,994	-	-	58,994
Student Activities	51,275	-	-	51,275	41,788	-	-	41,788
Student Exhibition	4,532	-	-	4,532	12,920	-	-	12,920
Information Technology	1,672	-	-	1,672	79	1,617	-	1,696
Scholarships	2,336,352	-	-	2,336,352	1,907,341	-	-	1,907,341
Depreciation and Amortization	525,190	17,503	2,666	545,359	413,925	15,467	2,093	431,485
Interest Expense	78,416	796	398	79,610	154,621	1,570	785	156,976
Taxes	89,990	914	457	91,361	138,911	1,410	705	141,026
Bond Cost	18,950	192	96	19,238	76,843	780	390	78,013
Miscellaneous Expense	-	21,497	-	21,497	-	6,687	-	6,687
	$ 6,306,593	$ 605,240	$ 22,741	$ 6,934,574	$ 5,836,717	$ 597,594	$ 28,418	$ 6,462,729

NOTE 15 – OPERATING LEASES

The Academy is the lessee in the following lease agreements:

Equipment

The Academy leases equipment for total monthly payments of $772. The leases have varying expiration dates ranging from April, 2013 to November, 2013. The Academy incurred lease expense of $8,073 and $9,265 for 2012 and 2011, respectively.

Housing

Art Academy Housing leases apartments for the students of the Academy for a base rent of $7,500 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 incurred lease expense related to this lease of $111,498 and $97,917 for 2012 and 2011, respectively.

In August, 2009, Art Academy Housing entered an operating lease for an apartment. The monthly lease payment is $558. The lease expired in July, 2010. Lease expense was $-0- and $558 for 2012 and 2011, respectively.

During 2012, the Academy entered into additional leases for student housing. The lease payments vary from $400 to $1,000 and have expiration dates ranging from February, 2012 to June, 2013. The Academy incurred lease expense of $59,754 for 2012.

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

Years Ending May 31,	Housing	Equipment	Total
2013	$ 148,905	$ 9,265	$ 158,170
2014	25,274	-	25,274
	$ 174,179	$ 9,265	$ 183,444

The Academy is the lessor in the following lease agreement:

In July, 2008, the Academy started leasing a portion of its Walnut Street building. The lease term is thirty-six months and expired in June, 2011. As part of the lease agreement, the Academy was offsetting utility expense with the tenant. The net annual rental income was $-0- for the years ended May 31, 2012 and 2011.

NOTE 16 – RELATED PARTIES

The Academy does business with companies who are either owned by or employ a Board of Trustees member. During fiscal year 2012, the Academy received $3,500 from one company for storage space and had $-0- due from this company as of May 31, 2012. The Academy also spent $12,374 with one company for legal services and had $-0- due to this company as of May 31, 2012. During fiscal year 2011, the Academy spent $10,952 with one company for printing and had $-0- due to this company as of May 31, 2011. The Academy also spent $7,572 with two companies for legal services and had $50 due to one of these companies as of May 31, 2011.

NOTE 17 – HEDGING ACTIVITIES

1212 Jackson held derivative financial instruments for the purpose of hedging the risks of certain identifiable and anticipated transactions. In general, the types of risks hedged are those relating to the changes in interest rates. In hedging the transactions 1212 Jackson LLC, in the normal course of business, holds the following type of derivate:

Type of Derivative	Type of Transaction Being Hedged
Interest rate swap	Cash flows of variable rate debt

Derivatives were held only for the purpose of hedging such risks, not for speculation. Generally, the LLC entered into hedging relationships such that changes in the fair values or cash flows of items and transactions being hedged are expected to be offset by corresponding changes in the values of the derivatives. At May 31, 2011, hedging relationships exist for bond indebtedness.

The LLC recognized net gains of $60,784 and $86,085 for 2012 and 2011 from cash flow hedges, respectively. In September, 2011, the bond payable was paid off along with the interest rate swap.

NOTE 18 – 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 statement 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 estimated fair values of the Academy's financial instruments as of May 31, 2012, none of which are held for trading purposes, are as follows:

	Carrying Value	Fair Value
Financial Assets		
Cash and Cash Equivalents	$ 340,841	$ 340,841
Accounts and Other Receivables	144,338	144,338
Pledges Receivable	4,340	4,340
Investments	1,396,088	1,396,088
Beneficial Interests	239,929	239,929
Financial Liabilities		
Line of Credit	400,000	400,000
Accounts Payable, Accrued and Other Liabilities	592,154	592,154
Note Payable	167,339	167,339

NOTE 19 – FAIR VALUE MEASUREMENTS

Financial Accounting Standards Board (FASB) *Accounting Standards Codification (ASC) 820, Fair Value Measurements and Disclosures*, 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 measurement) and the lowest priority to unobservable inputs (Level 3 measurement). 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.

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

Following is a description of the valuation methodologies used for assets and liabilities measured at fair value. There have been no changes in the methodologies used at May 31, 2012 and 2011

Fair values for investments are determined by reference to quoted market prices and other relevant information generated by market transactions. 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 fair value of the interest rate swap is determined by market values provided by the bank.

NOTE 19 – FAIR VALUE MEASUREMENTS (Continued)

The following assets and liabilities were measured at fair value as of May 31, 2012:

	Level 1 Quoted Price In Active Markets for Identical Assets	Level 2 Significant Other Observable Inputs	Level 3 Significant Unobservable Inputs
Cash & Cash Equivalents	$ 15,449	$ -	$ -
Mutual Funds			
Money Market Funds	12,004	-	-
Value Funds	114,524	-	-
Blended Funds	13,686	-	-
Growth Funds	125,899	-	-
Fixed Funds	442,344	-	-
International Funds	124,109	-	-
Total Mutual Funds	832,566	-	-
Stocks			
Consumer Discretionary	68,082	-	-
Consumer Staples	50,506	-	-
Energy	46,716	-	-
Financial	73,467	-	-
Health Care	62,224	-	-
Industrials	44,286	-	-
Information Technology	97,919	-	-
Materials	20,161	-	-
Telecommunication Services	9,112	-	-
Utilities	16,484	-	-
Total Stocks	488,957	-	-
Fixed Income	10,079	-	-
Exchange-Traded Funds	49,037	-	-
Total Investments	$ 1,396,088	$ -	$ -
Beneficial Interest In Trusts	$ 274,271	$ -	$ (34,342)
Fair Market Value of Interest Rate Swap	$ -	$ -	$ -

NOTE 19 – FAIR VALUE MEASUREMENTS (Continued)

The following assets and liabilities were measured at fair value as of May 31, 2011:

	Level 1 Quoted Price In Active Markets for Identical Assets	Level 2 Significant Other Observable Inputs	Level 3 Significant Unobservable Inputs
Cash & Cash Equivalents	$ 53,341	$ -	$ -
Mutual Funds			
Money Market Funds	25,042	-	-
Value Funds	689,235	-	-
Blended Funds	221,869	-	-
Growth Funds	943,260	-	-
Fixed Funds	1,379,693	-	-
International Funds	332,033	-	-
Total Mutual Funds	3,591,132	-	-
Stocks			
Consumer Discretionary	134,753	-	-
Consumer Staples	97,335	-	-
Energy	127,213	-	-
Financial	891,550	-	-
Health Care	131,214	-	-
Industrials	133,401	-	-
Information Technology	193,043	-	-
Materials	49,045	-	-
Telecommunication Services	24,917	-	-
Utilities	36,612	-	-
Total Stocks	1,819,083	-	-
Fixed Income	38,490	-	-
Exchange-Traded Funds	357,955	-	-
Total Investments	$ 5,860,001	$ -	$ -
Beneficial Interest In Trusts	$ 306,428	$ -	$ (46,842)
Fair Market Value of Interest Rate Swap	$ -	$ (60,784)	$ -

NOTE 19 – FAIR VALUE MEASUREMENTS (Continued)

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

	Contribution Receivable
May 31, 2011	$ (46,842)
Change in Value	12,500
May 31, 2012	$ (34,342)

NOTE 20 – SUBSEQUENT EVENTS

The date to which events occurring after May 31, 2012, the date of the most recent statement of financial position, have been evaluated for possible adjustment to the financial statements or disclosure is September 14, 2012 which is the date on which the financial statements were available to be issued.

ADDITIONAL INFORMATION

ART ACADEMY OF CINCINNATI AND AFFILIATES
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended May 31, 2012

Federal Grantor/Program Title	Pass-Through Grantor Number	Federal CFDA Number		Federal Expenditures
U.S. Department of Education:				
Federal Direct Student Loans		84.268	$	1,930,036
Federal Pell Grant Program	P063P101983	84.063		406,659
Supplemental Education				
Opportunity Grant Program	P007A103229	84.007		11,637
College Work Study Program	P033A103229	84.033		20,686
			$	2,369,018

The accompanying notes are an integral part of this schedule.

ART ACADEMY OF CINCINNATI AND AFFILIATES
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended May 31, 2012

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 financial statements.

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

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

We have audited the consolidated financial statements of the Art Academy of Cincinnati (a nonprofit organization) and Affiliates as of and for the year ended May 31, 2012, and have issued our report thereon dated September 14, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

Management of the Art Academy of Cincinnati is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Art Academy of Cincinnati and Affiliates' internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose expressing an opinion on the effectiveness of Art Academy of Cincinnati and Affiliates' internal control over financial reporting. Accordingly, we do not express on an opinion on the effectiveness of the Art Academy of Cincinnati and Affiliates' internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Art Academy of Cincinnati and Affiliates' consolidated 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 that are required to be reported under *Government Auditing Standards*.

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We noted certain additional matters that we reported to management of the Academy in a separate letter dated September 14, 2012.

This report is intended solely for the information and use of the board of trustees, management and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Von Lehman & Company Inc.

Fort Mitchell, Kentucky
September 14, 2012

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INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

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

<u>Compliance</u>

We have audited the Art Academy of Cincinnati and Affiliates' compliance with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Art Academy of Cincinnati and Affiliates' major federal programs for the year ended May 31, 2012. The Art Academy of Cincinnati and Affiliates' major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Art Academy of Cincinnati and Affiliates' management. Our responsibility is to express an opinion on the Art Academy of Cincinnati and Affiliates' compliance based on our audit.

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 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 Affiliates' 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. Our audit does not provide a legal determination on the Art Academy of Cincinnati and Affiliates' compliance with those requirements.

In our opinion, the Art Academy of Cincinnati and Affiliates complied, in all material respects, with the 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, 2012. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, 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 Item 12-01.

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Internal Control over Compliance

Management of the Art Academy of Cincinnati and Affiliates is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the Art Academy of Cincinnati and Affiliates' internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine our auditing procedures for the purpose of expressing our opinion on compliance 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 Art Academy of Cincinnati and Affiliates' 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.

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

The Art Academy of Cincinnati and Affiliates' response to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit the Art Academy of Cincinnati and Affiliates' responses and, accordingly, we express no opinion on the responses.

This report is intended solely for the information and use of the board of trustees, management and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Von Lehman & Company Inc.

Fort Mitchell, Kentucky
September 14, 2012

ART ACADEMY OF CINCINNATI AND AFFILIATES
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Year Ended May 31, 2012

SECTION I – SUMMARY OF AUDITORS' RESULTS

FINANCIAL STATEMENTS	
Type of Auditor's Report Issued	Unqualified
Material weakness(es) identified?	No
Significant Deficiencies identified not considered to be material weaknesses?	None Reported
Noncompliance material to 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:	Unqualified
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] College Work Study Program [CFDA 84.033]
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 12-01 Return of Funds:

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 the Education Department (ED) to the appropriate Direct Loan lender within forty five days after the institution determines the student withdrew.

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

Corrective Action:

During a complex financial aid application process, one student's eligibility and disbursements changed multiple times. It was uncovered during a reconciliation of direct lending loan disbursements that the reports from the financial aid department to the finance office did not clearly communicate some of these changes. A new process has been created to indicate when special circumstances exist on specific disbursements.

ART ACADEMY OF CINCINNATI AND AFFILIATES
SUMMARY SCHEDULE OF PRIOR YEAR AUDIT FINDINGS AND QUESTIONED COSTS

SECTION II – FINANCIAL STATEMENT FINDINGS

None

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

Item 11-01 Return of Funds:

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 the Education Department (ED) to the appropriate Direct Loan lender within forty five days after the institution determines the student withdrew.

Out of a sample of twenty-one returns of Title IV Funds selected for testing, five returns representing three students were not returned to the appropriate account within the required time frame.

Corrective Action:

Due to competing professional demands of the Finance Office the return of funds for three students were processed late. Management has discussed the issue with the Finance Office and has created a schedule to review the status of all return of funds.

Current Status:

During the year, Management and the Finance Office reviewed the status of funds. Special emphasis was placed on reconciling enrollment status with loan eligibility. Frequent reconciliations between the financial aid and the finance department were conducted.

SUPPLEMENTAL INFORMATION

ART ACADEMY OF CINCINNATI AND AFFILIATES
CONSOLIDATING STATEMENT OF FINANCIAL POSITION
May 31, 2012

ASSETS

	Art Academy of Cincinnati	Academy Advancement Limited	Art Academy Housing, Inc.	Eliminations	Total
Current Assets					
Cash and Cash Equivalents	$ 339,152	$ 1,689	$ -	$ -	$ 340,841
Accounts Receivable	144,338	-	-	-	144,338
Pledges Receivable	2,445	-	-	-	2,445
Note Receivable - Related Party	886,800	-	901,594	(1,788,394)	-
Interest and Dividends Receivable	-	-	-	-	-
Prepaid Expenses	68,145	-	-	-	68,145
Total Current Assets	1,440,880	1,689	901,594	(1,788,394)	555,769
Buildings and Equipment, Net	10,552,774	-	1,091	-	10,553,865
Investments	1,396,088	-	-	-	1,396,088
Pledges Receivable	1,895	-	-	-	1,895
Beneficial Interest in Perpetual Trust	171,741	-	-	-	171,741
Beneficial Interest in Charitable Remainder Trusts	102,530	-	-	-	102,530
Deposits	-	-	16,610	-	16,610
Other Assets, Net	16,519	-	-	-	16,519
Total Assets	$ 13,682,427	$ 1,689	$ 919,295	$ (1,788,394)	$ 12,815,017

LIABILITIES AND EQUITY

	Art Academy of Cincinnati	Academy Advancement Limited	Art Academy Housing, Inc.	Eliminations	Total
Current Liabilities					
Line of Credit	$ 400,000	$ -	$ -	$ -	$ 400,000
Accounts Payable	172,526	-	-	-	172,526
Accrued Expenses	405,028	-	14,600	-	419,628
Note Payable - Related Party	901,594	-	886,800	(1,788,394)	-
Note Payable - Current Portion	167,339	-	-	-	167,339
Total Current Liabilities	2,046,487	-	901,400	(1,788,394)	1,159,493
Long-Term Liabilities					
Charitable Remainder Trust	34,342	-	-	-	34,342
Total Liabilities	2,080,829	-	901,400	(1,788,394)	1,193,835
Equity					
Member's Equity	-	1,689	-	-	1,689
Net Assets	11,601,598	-	17,895	-	11,619,493
Total Equity	11,601,598	1,689	17,895	-	11,621,182
Total Liabilities and Equity	$ 13,682,427	$ 1,689	$ 919,295	$ (1,788,394)	$ 12,815,017

ART ACADEMY OF CINCINNATI AND AFFILIATES
CONSOLIDATING STATEMENT OF ACTIVITIES
Year Ended May 31, 2012

	Art Academy of Cincinnati	Academy Advancement Limited	1212 Jackson LLC	Art Academy Housing, Inc.	Eliminations	Total
Revenue and Support						
Grants, Contributions and Gifts	$ 272,142	$ -	$ -	$ -	$ -	$ 272,142
Tuition Income	5,335,302	-	-	-	-	5,335,302
Investment Income	54,409	-	-	-	-	54,409
Other Income	13,791	50	-	224,551	-	238,392
Total Revenue and Support	5,675,644	50	-	224,551	-	5,900,245
Expenses						
Program Services	5,722,988	380,649	-	202,956	-	6,306,593
Management & General	601,376	3,864	-	-	-	605,240
Fundraising	20,809	1,932	-	-	-	22,741
Total Expenses	6,345,173	386,445	-	202,956	-	6,934,574
Excess (Deficit) of Revenue, Support and Reclassifications Over Expenses	(669,529)	(386,395)	-	21,595	-	(1,034,329)
Realized Loss on Investments	(110,374)	-	-	-	-	(110,374)
Unrealized Loss on Investments	(74,092)	-	-	-	-	(74,092)
Change in Beneficial Interest in Perpetual Trust	(8,966)	-	-	-	-	(8,966)
Change in Beneficial Interest in Charitable Remainder Trusts	(10,691)	-	-	-	-	(10,691)
Change in Net Assets	(873,652)	(386,395)	-	21,595	-	(1,238,452)
Dissolution of Entity	1,173,611	(2,667,838)	(4,533,380)	-	6,027,607	-
Change in Fair Market Value of Interest Rate Swap	-	60,784	-	-	-	60,784
	299,959	(2,993,449)	(4,533,380)	21,595	6,027,607	(1,177,668)
Net Assets Beginning of Year	11,301,639	2,995,138	4,533,380	(3,700)	(6,027,607)	12,798,850
Net Assets End of Year	$ 11,601,598	$ 1,689	$ -	$ 17,895	$ -	$ 11,621,182

ART ACADEMY OF CINCINNATI AND AFFILIATES
CONSOLIDATING STATEMENT OF MEMBERS' EQUITY
Year Ended May 31, 2012

	Academy Advancement LTD.	1212 Jackson LLC	Subtotal	Eliminations	Total
Members' Equity - May 31, 2010	$ 2,965,038	$ 4,494,441	$ 7,459,479	$ (5,967,507)	$ 1,491,972
Contributed Capital	30,000	30,000	60,000	(60,000)	-
Buyout of Other Members	-	(30,000)	(30,000)	-	(30,000)
Net Income (Loss)	100	(2,326)	(2,226)	(100)	(2,326)
Subtotal	2,995,138	4,492,115	7,487,253	(6,027,607)	1,459,646
Other Members' Net Loss	-	(44,820)	(44,820)	-	(44,820)
Change in Fair Market Value of Interest Rate Swap	-	86,085	86,085	-	86,085
Members' Equity - May 31, 2011	2,995,138	4,533,380	7,528,518	(6,027,607)	1,500,911
Dissolution of Entity	(2,667,838)	(4,533,380)	(7,201,218)	6,027,607	(1,173,611)
Net Loss	(386,395)	-	(386,395)	-	(386,395)
Subtotal	(59,095)	-	(59,095)	-	(59,095)
Change in Fair Market Value of Interest Rate Swap	60,784	-	60,784	-	60,784
Members' Equity - May 31, 2012	$ 1,689	$ -	$ 1,689	$ -	$ 1,689