

The Awty International School

Consolidated Financial Statements
and Independent Auditors' Report
for the years ended June 30, 2009 and 2008

Independent Auditors' Report

To the Board of Directors of
The Awty International School:

We have audited the accompanying consolidated statements of financial position of The Awty International School and subsidiaries as of June 30, 2009 and 2008 and the related consolidated statements of activities and of cash flows for the years then ended. These financial statements are the responsibility of the management of The Awty International School. 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. Those standards require that we plan and perform our audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of The Awty International School and subsidiaries as of June 30, 2009 and 2008 and the changes in their net assets and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Blazek & Vetterling

November 11, 2009

The Awty International School

Consolidated Statements of Financial Position as of June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
ASSETS		
Cash and cash equivalents (<i>Note 2</i>)	\$ 2,782,951	\$ 1,909,466
Textbook and uniform inventory	269,757	359,848
Prepaid expenses and other assets	257,100	273,952
Pledges receivable, net (<i>Note 3</i>)	4,153,425	4,206,691
Investments (<i>Notes 4 and 5</i>)	2,902,958	3,464,342
Cash and cash equivalents restricted to capital projects	2,517,281	743,581
Property and equipment, net (<i>Note 6</i>)	<u>28,124,829</u>	<u>28,832,394</u>
TOTAL ASSETS	<u>\$ 41,008,301</u>	<u>\$ 39,790,274</u>
LIABILITIES AND NET ASSETS		
Liabilities:		
Accounts payable	\$ 320,411	\$ 533,753
Accrued expenses	942,272	837,448
Deferred tuition and fees	1,905,213	1,748,743
Notes payable (<i>Note 7</i>)	4,107,605	4,462,571
Fair value of derivative agreement (<i>Notes 5 and 7</i>)	<u>241,848</u>	<u>98,787</u>
Total liabilities	<u>7,517,349</u>	<u>7,681,302</u>
Net assets:		
Unrestricted (<i>Note 8</i>)	26,460,746	26,910,676
Temporarily restricted (<i>Note 9</i>)	<u>7,030,206</u>	<u>5,198,296</u>
Total net assets	<u>33,490,952</u>	<u>32,108,972</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 41,008,301</u>	<u>\$ 39,790,274</u>

See accompanying notes to consolidated financial statements.

The Awty International School

Consolidated Statement of Activities for the year ended June 30, 2009

	<u>UNRESTRICTED</u>	TEMPORARILY <u>RESTRICTED</u>	<u>TOTAL</u>
REVENUE:			
Tuition and fees	\$ 19,382,428		\$ 19,382,428
Auxiliary service fees	1,056,845		1,056,845
Other program service fees	745,609		745,609
Contributions	625,269	\$ 2,240,874	2,866,143
Loss on valuation of pledges receivable		(255,000)	(255,000)
Fundraising events	567,408	196,254	763,662
Direct donor benefit costs	(144,207)		(144,207)
Investment return (<i>Note 4</i>)	(389,304)		(389,304)
Other	<u>13,375</u>		<u>13,375</u>
Total revenue	21,857,423	2,182,128	24,039,551
Net assets released from restrictions:			
Program and fundraising expenditures	<u>350,218</u>	<u>(350,218)</u>	
Total	<u>22,207,641</u>	<u>1,831,910</u>	<u>24,039,551</u>
EXPENSES:			
Instructional and student activities	19,118,498		19,118,498
Management and general	2,946,637		2,946,637
Fundraising	<u>449,375</u>		<u>449,375</u>
Total expenses	<u>22,514,510</u>		<u>22,514,510</u>
Changes in net assets before change in value			
of derivative agreement	(306,869)	1,831,910	1,525,041
Change in value of derivative agreement (<i>Note 7</i>)	<u>(143,061)</u>		<u>(143,061)</u>
CHANGES IN NET ASSETS	(449,930)	1,831,910	1,381,980
Net assets, beginning of year	<u>26,910,676</u>	<u>5,198,296</u>	<u>32,108,972</u>
Net assets, end of year	<u>\$ 26,460,746</u>	<u>\$ 7,030,206</u>	<u>\$ 33,490,952</u>

See accompanying notes to consolidated financial statements.

The Awty International School

Consolidated Statement of Activities for the year ended June 30, 2008

	<u>UNRESTRICTED</u>	TEMPORARILY <u>RESTRICTED</u>	<u>TOTAL</u>
REVENUE:			
Tuition and fees	\$ 18,535,054		\$ 18,535,054
Auxiliary service fees	1,089,793		1,089,793
Other program service fees	730,283		730,283
Contributions	263,161	\$ 5,193,254	5,456,415
Fundraising events	797,939	261,282	1,059,221
Direct donor benefit costs	(157,524)		(157,524)
Investment return (<i>Note 4</i>)	431,777		431,777
Other	<u>27,928</u>		<u>27,928</u>
Total revenue	21,718,411	5,454,536	27,172,947
Net assets released from restrictions:			
Program and fundraising expenditures	<u>446,508</u>	<u>(446,508)</u>	
Total	<u>22,164,919</u>	<u>5,008,028</u>	<u>27,172,947</u>
EXPENSES:			
Instructional and student activities	18,010,743		18,010,743
Management and general	2,802,399		2,802,399
Fundraising	<u>492,981</u>		<u>492,981</u>
Total expenses	<u>21,306,123</u>		<u>21,306,123</u>
Changes in net assets before change in value of derivative agreement	858,796	5,008,028	5,866,824
Change in value of derivative agreement (<i>Note 7</i>)	<u>(169,596)</u>		<u>(169,596)</u>
CHANGES IN NET ASSETS	689,200	5,008,028	5,697,228
Net assets, beginning of year	<u>26,221,476</u>	<u>190,268</u>	<u>26,411,744</u>
Net assets, end of year	<u>\$ 26,910,676</u>	<u>\$ 5,198,296</u>	<u>\$ 32,108,972</u>

See accompanying notes to consolidated financial statements.

The Awty International School

Consolidated Statements of Cash Flows for the years ended June 30, 2009 and 2008

	<u>2009</u>	<u>2008</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Changes in net assets	\$ 1,381,980	\$ 5,697,228
Adjustments to reconcile changes in net assets to net cash provided by operating activities:		
Depreciation	1,540,018	1,142,436
Contributions restricted to capital projects	(311,989)	(5,125,441)
Loss on valuation of pledges receivable	255,000	
Net realized and unrealized loss on investment	641,075	149,143
Change in value of derivative agreement	143,061	169,596
Changes in operating assets and liabilities:		
Textbook and uniform inventory	90,091	(2,897)
Prepaid expenses and other assets	16,852	59,419
Pledges receivable	(1,713,536)	318,750
Accounts payable and accrued expenses	(108,518)	(20,564)
Funds held for others		(57,892)
Deferred tuition and fees	<u>156,470</u>	<u>(10,136)</u>
Net cash provided by operating activities	<u>2,090,504</u>	<u>2,319,642</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sale of investments	41,629	122,284
Purchases of investments	(82,095)	(1,105,789)
Change in money market mutual funds held for investment	(39,225)	35,183
Purchases of property and equipment	<u>(832,453)</u>	<u>(7,594,433)</u>
Net cash used by investing activities	<u>(912,144)</u>	<u>(8,542,755)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Change in cash restricted to capital projects	(1,773,700)	(743,581)
Principal repayments of notes payable	(354,966)	(458,940)
Proceeds from contributions restricted to capital projects	<u>1,823,791</u>	<u>919,500</u>
Net cash used by financing activities	<u>(304,875)</u>	<u>(283,021)</u>
NET CHANGE IN CASH AND CASH EQUIVALENTS	873,485	(6,506,134)
Cash and cash equivalents, beginning of year	<u>1,909,466</u>	<u>8,415,600</u>
Cash and cash equivalents, end of year	<u>\$ 2,782,951</u>	<u>\$ 1,909,466</u>
<i>Supplemental disclosure of cash flow information:</i>		
Interest paid	\$211,792	\$226,112

See accompanying notes to consolidated financial statements.

The Awty International School

Notes to Consolidated Financial Statements for the years ended June 30, 2009 and 2008

NOTE 1 – ORGANIZATION AND SUMMARY OF ACCOUNTING POLICIES

Organization – The Awty International School (Awty) is a private day school that provides instruction to both American and international students in Houston, Texas. Awty's enrollment is approximately 1,200 students in preschool through 12th grade. Founded in 1956, the purpose of Awty is to give its students an innovative and comprehensive education at all levels. The students are expected to acquire fluency in a second language and to participate in academic and extracurricular activities to increase their understanding of other societies and cultures and of global affairs.

7502 Old Katy Road Company (Old Katy) was incorporated in May 2002 to own, invest in, operate, maintain, lease, finance, pledge, and sell real property for the benefit of Awty. Awty is the sole member of Old Katy.

1495 POP, Inc. (POP) was incorporated in May 2004 to own, invest in, operate, maintain, lease, finance, pledge, and sell real property for the benefit of Awty. Awty is the sole member of POP.

Basis of consolidation – The accompanying financial statements include the consolidated activities of Awty, Old Katy, and POP (collectively the School). Significant intercompany transactions have been eliminated in consolidation.

Federal income tax status – Awty, Old Katy and POP are exempt from federal income tax under §501(c)(3) of the Internal Revenue Code. Awty is classified as a public charity under §509(a)(1) and §170(b)(1)(A)(ii). Old Katy and POP are classified as Type I supporting organizations under §509(a)(3).

Net asset classification – Contributions and the related net assets are classified based on the existence or absence of donor-imposed restrictions, as follows:

- *Unrestricted net assets* include those net assets whose use is not restricted by donor-imposed stipulations, even though their use may be limited in other respects, such as by contract or board designation.
- *Temporarily restricted net assets* include contributions restricted by the donor to specific purposes or time periods. When a purpose restriction is accomplished or a time restriction ends, temporarily restricted net assets are released to unrestricted net assets.

Cash equivalents include highly liquid investments with original maturities of three months or less.

Textbook and uniform inventory is stated at the lower of cost or market.

Pledges receivable that are expected to be collected within one year are recorded at net realizable value. Pledges receivable that are expected to be collected in future years are discounted to estimate the present value of future cash flows.

Investments in marketable securities are recorded at fair value. Investment return is reported in the statement of activities as an increase in unrestricted net assets unless its use is limited by donor-imposed restrictions. Investment return whose use is restricted by the donor is reported as an increase in temporarily restricted net assets until expended in accordance with donor-imposed restrictions.

Property and equipment is recorded at cost if purchased or at fair value at the date of gift if donated. The School records depreciation on the straight-line method over estimated useful lives of the assets, which range from 3 to 5 years for furniture, fixtures, and equipment and 30 years for buildings and improvements.

Funds held for others – The School holds funds for several related school groups. The School has limited discretion over the use of these funds. Funds held for others are included in the School’s cash and cash equivalents and as a liability of the School.

Tuition and fees are recognized in the period in which the services are provided and are shown net of student financial aid of \$561,207 in 2009 and \$568,637 in 2008. Tuition and fees include tuition paid by the French government of \$513,617 in 2009 and \$512,421 in 2008. Amounts received for future periods are recorded as deferred tuition and fees until earned.

Contributions are recorded as revenue at fair value when an unconditional commitment is received from the donor. Contributions received with donor stipulations that limit their use are recorded as restricted revenue. Conditional promises to give are included in contribution revenue when the conditions are substantially met.

Estimates – Management must make estimates and assumptions to prepare financial statements in accordance with generally accepted accounting principles. These estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, the amounts of reported revenues and expenses, and the allocation of expenses among various functions. Actual results could vary from the estimates that were used.

Reclassifications – Certain reclassifications have been made to the prior year financial statements to conform to current year presentations.

NOTE 2 – CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of the following:

	<u>2009</u>	<u>2008</u>
Money market mutual funds	\$ 1,437,384	\$ 1,659,778
Cash in foreign banks	539,242	108,420
Commercial paper	478,144	
Cash in domestic banks	<u>328,181</u>	<u>141,268</u>
Total cash and cash equivalents	<u>\$ 2,782,951</u>	<u>\$ 1,909,466</u>

Domestic bank deposits exceed the federally insured limit per depositor per institution.

NOTE 3 – PLEDGES RECEIVABLE

Pledges receivable are as follows:

	<u>2009</u>	<u>2008</u>
Pledges receivable	\$ 4,785,575	\$ 4,791,875
Allowance for uncollectible accounts	(400,140)	(361,734)
Discount to net present value at 1.64% to 3.34%	<u>(232,010)</u>	<u>(223,450)</u>
Pledges receivable, net	<u>\$ 4,153,425</u>	<u>\$ 4,206,691</u>

Pledges receivable as of June 30, 2009 are expected to be collected as follows:

Within one year	\$ 2,058,175
In one to five years	2,327,400
In more than five years	<u>400,000</u>
Total pledges receivable	<u>\$ 4,785,575</u>

At June 30, 2009, approximately 54% of pledges are due from two donors. These gifts included a pledge from an individual for \$200,000 a year over the donor's remaining lifetime that has been recognized based on a period life table published by the United States Social Security Administration. It is possible that management's estimate of the collectability of pledges receivable balances will change in the near term resulting in a change in the carrying value of pledges receivable.

NOTE 4 – INVESTMENTS

Investments primarily represent amounts designated by the board of directors for endowment (See Notes 8 and 10) and consist of the following:

	<u>2009</u>	<u>2008</u>
Equity mutual funds	\$ 1,034,275	\$ 1,299,133
Bond mutual funds	945,066	893,471
Equity securities	881,715	1,269,061
Money market mutual funds	<u>41,902</u>	<u>2,677</u>
Total investments	<u>\$ 2,902,958</u>	<u>\$ 3,464,342</u>

Investments are exposed to various risks such as interest rate, market, and credit risks. Because of these risks, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the statement of financial position and statement of activities.

Investment return includes earnings on cash and cash equivalents and consists of the following:

	<u>2009</u>	<u>2008</u>
Interest and dividends	\$ 251,771	\$ 580,920
Net realized and unrealized loss	<u>(641,075)</u>	<u>(149,143)</u>
Total investment return	<u>\$ (389,304)</u>	<u>\$ 431,777</u>

NOTE 5 – FAIR VALUE MEASUREMENTS

Effective July 1, 2008, Awty adopted Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (SFAS 157), which provides a framework for measuring the fair value of certain assets and liabilities and expands disclosures about fair value measurements. As defined in SFAS 157, fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the reporting date. SFAS 157 establishes a three-tier hierarchy that prioritizes the assumptions, referred to as inputs, used in valuation techniques to measure fair value.

The three levels of the fair value hierarchy defined by SFAS 157 are as follows:

- *Level 1* – Pricing inputs include quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the reporting date.
- *Level 2* – Pricing inputs other than quoted prices included in Level 1, that are either directly observable or that can be derived from or corroborated by observable market data as of the reporting date.
- *Level 3* – Pricing inputs include those that are generally less observable for the asset or liability and reflect the reporting entity’s own assumptions about the assumptions market participants would use in pricing the asset or liability. These inputs may be used with internally developed techniques that result in management’s best estimate of fair value.

Assets measured at fair value at June 30, 2009:

	<u>LEVEL 1</u>	<u>LEVEL 2</u>	<u>LEVEL 3</u>	<u>TOTAL</u>
Commercial paper		\$ 2,995,425		\$ 2,995,425
Money market mutual funds	\$ 1,479,286			1,479,286
Equity mutual funds	1,034,275			1,034,275
Bond mutual funds	945,066			945,066
Equity securities	<u>881,715</u>			<u>881,715</u>
Total	<u>\$ 4,340,342</u>	<u>\$ 2,995,425</u>	<u>\$ 0</u>	<u>\$ 7,335,767</u>

Liabilities measured at fair value at June 30, 2009:

	<u>LEVEL 1</u>	<u>LEVEL 2</u>	<u>LEVEL 3</u>	<u>TOTAL</u>
Derivative agreement	<u> </u>	\$ (241,848)	<u> </u>	\$ (241,848)
Total	<u>\$ 0</u>	<u>\$ (241,848)</u>	<u>\$ 0</u>	<u>\$ (241,848)</u>

Valuation methods used for assets measured at fair value are as follows:

- *Commercial paper and derivative agreement* are valued based upon prices for similar instruments at the reporting date.
- *Mutual funds* are valued at the reported net asset value of shares held.
- *Equity securities* are valued at the closing price reported on the active market on which the individual securities are traded.

The inputs used to measure the fair value of investments are not necessarily indicative of the risk of investing in a particular security. The valuation methods may produce a fair value that may not be indicative of the net realizable value or reflective of future fair values. Furthermore, while Awty believes its valuation methods are appropriate, the use of different methods or assumptions could result in a different fair value measurement at the reporting date.

NOTE 6 – PROPERTY AND EQUIPMENT

Property and equipment are comprised of the following:

	<u>2009</u>	<u>2008</u>
Land	\$ 9,424,324	\$ 9,424,324
Buildings and improvements	25,903,447	25,517,128
Furniture, fixtures, and equipment	<u>4,316,830</u>	<u>3,870,696</u>
Total property and equipment, at cost	39,644,601	38,812,148
Accumulated depreciation	<u>(11,519,772)</u>	<u>(9,979,754)</u>
Property and equipment, net	<u>\$ 28,124,829</u>	<u>\$ 28,832,394</u>

NOTE 7 – NOTES PAYABLE

Notes Payable

In 2002, the School obtained a \$6,000,000 tax-exempt loan from a bank. Proceeds from the loan were used to repay the outstanding balance of \$2,134,102 on the previous bank loan and to finance the purchase and renovation of a new lower school building. The loan bears interest at 65% of LIBOR plus 1.6% (1.9% at June 30, 2009) and is collateralized by unrestricted revenue and investments of the School, together with certain real property of Old Katy.

Notes payable are due as follows:

2010	\$ 372,960
2011	391,420
2012	410,792
2013	431,123
2014	452,460
Thereafter	<u>2,048,850</u>
Total	<u>\$ 4,107,605</u>

The School capitalized interest of approximately \$9,172 in 2009 and \$168,524 in 2008 in connection with the new athletic field and other property additions. Interest expense totaled approximately \$212,000 in 2009 and \$57,000 in 2008.

Interest Rate Swap Agreement

The School is party to an interest rate swap agreement with a bank that effectively converts its variable-rate notes payable to a fixed rate. The agreement has a notional amount of \$6,000,000 and a term of fifteen years. Under the terms of the agreement, the School pays an effective interest rate of 4.86% with sixty equal quarterly payments of principal and interest of \$141,420 to retire the note. The School has an offset arrangement that allows it to offset against the note principal any amounts defaulted by the swap agreement counterparty.

Line of credit

The School has a \$1,500,000 revolving line of credit with a bank. At June 30, 2009, no balance was outstanding on this line of credit.

NOTE 8 – UNRESTRICTED NET ASSETS

Unrestricted net assets consist of the following:

	<u>2009</u>	<u>2008</u>
Undesignated	\$ 23,179,006	\$ 23,275,446
Board designated for endowment	2,860,231	3,413,721
Board designated for capital fund	<u>421,509</u>	<u>221,509</u>
Total unrestricted net assets	<u>\$ 26,460,746</u>	<u>\$ 26,910,676</u>

NOTE 9 – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are as follows:

	<u>2009</u>	<u>2008</u>
Capital projects	\$ 4,955,421	\$ 4,949,522
Use in future periods	1,429,520	
Student activities	<u>645,265</u>	<u>248,774</u>
Total temporarily restricted net assets	<u>\$ 7,030,206</u>	<u>\$ 5,198,296</u>

NOTE 10 – ENDOWMENT FUNDS

Effective July 1, 2008, the School adopted Financial Accounting Standards Board Staff Position No. 117-1, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds* (FSP 117-1). FSP 117-1 uses the term endowment to refer to a fund established to provide income for the maintenance of an organization whether those funds are permanently or temporarily restricted by the donor or are unrestricted assets set aside by board designation. The School’s endowment consists only of board-designated funds.

Changes in endowment funds for the years ended June 30, 2009 and 2008 are as follows:

	<u>UNRESTRICTED</u>	<u>TEMPORARILY RESTRICTED</u>	<u>PERMANENTLY RESTRICTED</u>	<u>TOTAL</u>
Endowment net assets, July 1, 2007	\$ 2,794,535	\$ 0	\$ 0	\$ 2,794,535
Investment return:				
Interest and dividends	93,250			93,250
Net realized and unrealized loss	<u>(177,740)</u>			<u>(177,740)</u>
Total investment return	<u>(84,490)</u>			<u>(84,490)</u>
Additions	<u>703,676</u>			<u>703,676</u>
Endowment net assets, June 30, 2008	<u>3,413,721</u>	<u>0</u>	<u>0</u>	<u>3,413,721</u>
Investment return:				
Interest and dividends	80,177			80,177
Net realized and unrealized loss	<u>(633,667)</u>			<u>(633,667)</u>
Total investment return	<u>(553,490)</u>			<u>(553,490)</u>
Endowment net assets, June 30, 2009	<u>\$ 2,860,231</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 2,860,231</u>

Investment Policies and Strategy

Endowment funds are maintained in an investment account which is managed by an independent financial firm that follows guidance provided in an investment policy approved by the Board of Directors. The fund is to be invested for the long term. The Board of Directors recognizes that higher long-term returns are realized through higher exposure to equity and is willing to tolerate declines in the fund value in the short term, with the understanding that this may be necessary to maximize long-term return. The fund is currently in growth phase and has no regular expenditures. During this time, fund assets are invested to maximize total return while maintaining a reasonable level of risk.

Spending Policy

When the fund assets exceed \$1.5 million in value, yearly distributions from the fund shall be calculated according to the following:

<u>Value of fund</u>	<u>Distribution of fund</u>
\$1,500,000 to \$3,000,000	1% of 3-year trailing average value of fund
\$3,000,000 to \$5,000,000	2% of 3-year trailing average value of fund
\$5,000,000 and above	3% of 3-year trailing average value of fund

NOTE 11 – EMPLOYEE BENEFIT PLAN

Awty has a defined contribution money purchase retirement plan covering full-time employees who have completed two years of continuous service. Awty contributed approximately \$424,000 and \$411,000 to the plan during 2009 and 2008, respectively.

NOTE 12 – CONDITIONAL CONTRIBUTION

At June 30, 2009, Awty has a \$250,000 conditional pledge receivable. The commitment is conditioned upon the donor's approval of the capital project plan and certain contractual matters related to the ownership of the assets developed by the School. This gift will be recognized as contribution revenue when the conditions are substantially met.

NOTE 13 – SUBSEQUENT EVENTS

Management has evaluated subsequent events through November 11, 2009, which is the date that the financial statements were available for issuance. As a result of this evaluation, no events were identified that need to be disclosed or would have an impact on reported net assets or change in net assets.