

Challenge Preparatory Charter School

Financial Statements and
Uniform Guidance Schedules
Together With Independent Auditors' Reports

June 30, 2022 and 2021

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Independent Auditors' Report

Board of Trustees
Challenge Preparatory Charter School

Report on the Audit of the Financial Statements

Opinion

We have audited the accompanying financial statements of Challenge Preparatory Charter School (a nonprofit organization), which comprise the statements of financial position as of June 30, 2022 and 2021, and the related statements of activities, functional expenses and cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Challenge Preparatory Charter School as of June 30, 2022 and 2021, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

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. Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of Challenge Preparatory Charter School and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Responsibilities of Management for the Financial Statements

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

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about Challenge Preparatory Charter School's ability to continue as a going concern within one year after the date that the financial statements are available to be issued.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with generally accepted auditing standards and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Challenge Preparatory Charter School's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about Challenge Preparatory Charter School's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters that we identified during the audit.

Report on Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards, as required by Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, is presented for purposes of additional analysis and is not a required part of the 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 financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the 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 financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 13, 2022, on our consideration of Challenge Preparatory Charter School's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely 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 effectiveness of Challenge Preparatory Charter School's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Challenge Preparatory Charter School's internal control over financial reporting and compliance.

PKF O'Connor Davies, LLP

Harrison, New York
October 13, 2022

Challenge Preparatory Charter School

Statements of Financial Position

	June 30,	
	2022	2021
ASSETS		
Current Assets		
Cash	\$ 2,829,496	\$ 6,635,874
Grants and contracts receivable	527,246	365,449
Prepaid expenses and other current assets	805,047	542,925
Due from related party	5,000	-
Total Current Assets	4,166,789	7,544,248
Property and equipment, net	1,631,974	1,366,039
Restricted cash	70,000	70,000
Security deposits	925,999	925,999
	\$ 6,794,762	\$ 9,906,286
LIABILITIES AND NET ASSETS		
Current Liabilities		
Accounts payable and accrued expenses	\$ 329,846	\$ 363,585
Accrued payroll and payroll taxes	1,429,516	1,152,059
Refundable advances	142,329	315,546
Deferred rent, current portion	1,643,524	103,919
Total Current Liabilities	3,545,215	1,935,109
Paycheck Protection Program loan payable	-	1,792,512
Deferred rent	1,399,119	2,556,245
Total Liabilities	4,944,334	6,283,866
Net assets, without donor restrictions	1,850,428	3,622,420
	\$ 6,794,762	\$ 9,906,286

See notes to financial statements

Challenge Preparatory Charter School

Statements of Activities

	Year Ended June 30,	
	2022	2021
REVENUE AND SUPPORT		
State and local per pupil operating revenue	\$ 17,643,377	\$ 15,854,084
State and local per pupil facilities funding	1,721,827	1,064,272
Federal grants	1,606,708	582,156
State grants	69,621	59,460
Contributions, grants and other income	45,509	8,345
Rental income	-	9,408
Total Revenue and Support	21,087,042	17,577,725
EXPENSES		
Program Services		
Regular education	17,165,805	11,200,358
Supporting services	5,583,589	2,714,491
Total Program Services	22,749,394	13,914,849
Supporting Services		
Management and general	3,134,400	2,011,517
Fundraising	60,301	33,925
Total Expenses	25,944,095	15,960,291
OTHER REVENUE		
Gain on forgiveness of		
Paycheck Protection Program Loan	1,813,019	-
Gain on transfer of lease to related party	1,272,042	-
	3,085,061	-
Change in Net Assets	(1,771,992)	1,617,434
NET ASSETS		
Beginning of year	3,622,420	2,004,986
End of year	\$ 1,850,428	\$ 3,622,420

See notes to financial statements

Challenge Preparatory Charter School

Statement of Functional Expenses
Year Ended June 30, 2022

	No. of Positions	Program Services			Management and General	Fundraising	Total
		Regular Education	Special Education	Total			
Personnel Services Costs							
Administrative staff personnel	27	\$ 534,758	\$ 296,094	\$ 830,852	\$ 949,091	\$ 17,409	\$ 1,797,352
Instructional personnel	96	4,783,722	1,728,145	6,511,867	-	-	6,511,867
Non-Instructional personnel	39	2,437,099	639,081	3,076,180	423,805	-	3,499,985
Total Personnel Services Costs	<u>162</u>	<u>7,755,579</u>	<u>2,663,320</u>	<u>10,418,899</u>	<u>1,372,896</u>	<u>17,409</u>	<u>11,809,204</u>
Fringe benefits and payroll taxes		1,416,369	486,391	1,902,760	250,726	3,179	2,156,665
Retirement		140,505	48,251	188,756	24,872	315	213,943
Legal services		-	-	-	38,388	-	38,388
Accounting and auditing services		-	-	-	33,250	-	33,250
Other professional and consulting services		882,387	253,379	1,135,766	195,735	18,062	1,349,563
Building and land rent		4,555,443	1,564,371	6,119,814	812,016	10,226	6,942,056
Repairs and maintenance		90,873	31,207	122,080	16,086	204	138,370
Insurance		109,795	37,704	147,499	19,436	246	167,181
Utilities		383,982	131,862	515,844	67,973	862	584,679
Supplies and materials		720,927	163,892	884,819	50,401	1,562	936,782
Equipment and furnishings		29,551	7,454	37,005	2,270	7,597	46,872
Staff development		243,835	44,471	288,306	164,387	-	452,693
Marketing and recruiting		85,340	15,564	100,904	-	-	100,904
Technology		107,433	34,198	141,631	18,068	522	160,221
Food service		642	117	759	-	-	759
Student service		67,540	12,318	79,858	-	-	79,858
Office expense		151,956	36,134	188,090	9,898	117	198,105
Depreciation and amortization		423,648	52,956	476,604	52,956	-	529,560
Other		-	-	-	5,042	-	5,042
Total Expenses		<u>\$ 17,165,805</u>	<u>\$ 5,583,589</u>	<u>\$ 22,749,394</u>	<u>\$ 3,134,400</u>	<u>\$ 60,301</u>	<u>\$ 25,944,095</u>

See notes to the financial statements

Challenge Preparatory Charter School

Statement of Functional Expenses
Year Ended June 30, 2021

	No. of Positions	Program Services			Management and General	Fundraising	Total
		Regular Education	Special Education	Total			
Personnel Services Costs							
Administrative staff personnel	19	\$ 539,589	\$ 152,812	\$ 692,401	\$ 754,734	\$ 16,597	\$ 1,463,732
Instructional personnel	86	3,887,783	1,051,861	4,939,644	-	-	4,939,644
Non-Instructional personnel	33	1,701,855	330,236	2,032,091	320,791	-	2,352,882
Total Personnel Services Costs	<u>138</u>	<u>6,129,227</u>	<u>1,534,909</u>	<u>7,664,136</u>	<u>1,075,525</u>	<u>16,597</u>	<u>8,756,258</u>
Fringe benefits and payroll taxes		1,205,472	304,583	1,510,055	216,080	3,334	1,729,469
Retirement		123,461	31,194	154,655	22,130	342	177,127
Legal services		-	-	-	10,086	-	10,086
Accounting and auditing services		-	-	-	29,000	-	29,000
Other professional and consulting services		657,665	142,120	799,785	164,042	1,195	965,022
Building and land rent		1,918,336	484,701	2,403,037	343,860	5,306	2,752,203
Repairs and maintenance		59,481	15,029	74,510	10,662	165	85,337
Insurance		87,099	22,007	109,106	15,612	241	124,959
Utilities		190,207	48,059	238,266	34,094	526	272,886
Supplies and materials		269,712	45,685	315,397	11,275	300	326,972
Equipment and furnishings		8,374	1,550	9,924	549	5,085	15,558
Staff development		56,374	8,239	64,613	18,473	-	83,086
Marketing and recruiting		78,770	11,512	90,282	-	-	90,282
Technology		67,889	14,079	81,968	10,261	723	92,952
Student service		34,884	5,098	39,982	-	-	39,982
Office expense		106,943	19,918	126,861	7,216	111	134,188
Depreciation and amortization		206,464	25,808	232,272	25,808	-	258,080
Other		-	-	-	16,844	-	16,844
Total Expenses		<u>\$ 11,200,358</u>	<u>\$ 2,714,491</u>	<u>\$ 13,914,849</u>	<u>\$ 2,011,517</u>	<u>\$ 33,925</u>	<u>\$ 15,960,291</u>

Challenge Preparatory Charter School

Statements of Cash Flows

	Year Ended June 30,	
	2022	2021
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	\$ (1,771,992)	\$ 1,617,434
Adjustments to reconcile change in net assets to net cash from operating activities		
Depreciation and amortization	529,560	258,080
Deferred rent	1,654,521	172,454
Gain on forgiveness of Paycheck Protection Program loan	(1,813,019)	-
Gain on transfer of leases to related party	(1,272,042)	-
Changes in operating assets and liabilities		
Grants and contracts receivable	(161,797)	86,791
Prepaid expenses and other current assets	(262,122)	(168,444)
Due from related party	(5,000)	-
Security deposits	-	7,000
Accounts payable and accrued expenses	(13,232)	142,705
Accrued payroll and payroll taxes	277,457	124,808
Refundable advances	(173,217)	315,546
Net Cash from Operating Activities	(3,010,883)	2,556,374
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property and equipment	(795,495)	(730,725)
Net Change in Cash and Restricted Cash	(3,806,378)	1,825,649
CASH AND RESTRICTED CASH		
Beginning of year	6,705,874	4,880,225
End of year	\$ 2,899,496	\$ 6,705,874

See notes to financial statements

Challenge Preparatory Charter School

Notes to Financial Statements
June 30, 2022 and 2021

1. Organization and Tax Status

Challenge Preparatory Charter School (the “School”) is a New York State, not-for-profit educational corporation that was incorporated on February 9, 2010 to operate a charter school pursuant to Article 56 of the Education Law of the State of New York. The School was granted a provisional charter on February 9, 2010 valid for a term of five years and renewable upon expiration by the Board of Regents of the University of the State of New York. During 2019, the Board of Regents extended the School’s charter through June 30, 2024. The School’s educational philosophy promotes high levels of academic achievement and tailoring instruction to ensure that academic needs of all students are met. The School’s founders believe that good instruction recognizes the interrelation of content knowledge and higher order thinking and that, accordingly, good instruction should reflect a balanced approach to learning. Classes commenced in Far Rockaway, New York in August 2011 and the School provided education to approximately 950 students in kindergarten through tenth grade during the 2021-2022 academic year. The most recent charter renewal allows the School to serve grades 9-12.

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

Except for taxes that may be due for unrelated business income, the School is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code and from state and local income taxes under comparable laws.

2. Summary of Significant Accounting Policies

Basis of Presentation and Use of Estimates

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”), which requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Accordingly, actual results could differ from those estimates.

Challenge Preparatory Charter School

Notes to Financial Statements
June 30, 2022 and 2021

2. Summary of Significant Accounting Policies *(continued)*

Net Asset Presentation

Resources for various purposes are classified for accounting and reporting purposes into net asset categories established according to nature and purpose as follows:

Net assets without donor restrictions - consist of resources available for the general support of the School's operations. Net assets without donor restrictions may be used at the discretion of the School's management and/or the Board of Trustees.

Net assets with donor restrictions – represents amounts restricted by donors for specific activities of the School or to be used at a future date. The School records contributions as net assets with donor restrictions if they are received with donor stipulations that limit their use either through purpose or time restrictions. When a donor restriction expires, that is, when a time restriction ends or a purpose restriction is fulfilled, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the statements of activities as net assets released from restrictions. The School had no net assets with donor restrictions as of June 30, 2022 and 2021.

Restricted Cash

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

The following table provides a reconciliation of cash and restricted cash reported within the statements of financial position to the amounts presented in the statements of cash flows for the years ended June 30:

	<u>2022</u>	<u>2021</u>
Cash	\$ 2,829,496	\$ 6,635,874
Restricted Cash	<u>70,000</u>	<u>70,000</u>
	<u>\$ 2,899,496</u>	<u>\$ 6,705,874</u>

Challenge Preparatory Charter School

Notes to Financial Statements
June 30, 2022 and 2021

2. Summary of Significant Accounting Policies (*continued*)

Property and Equipment

The School follows the practice of capitalizing all expenditures for property and equipment with costs in excess of \$3,000 and a useful life in excess of one year. Leasehold improvements are amortized over the shorter of the term of the lease, inclusive of all renewal periods, which are reasonably assured, or the estimated useful life of the asset which is up to twenty years. Purchased property and equipment are recorded at cost at the date of acquisition. Maintenance and repairs are expensed as incurred. All property and equipment purchased with government funding is capitalized, unless the government agency retains legal title to such assets, in which case it is expensed as incurred.

Depreciation and amortization is recognized on the straight-line method over the estimated useful lives of such assets as follows:

Computers and equipment	3 to 5 years
Furniture and fixtures	5 years
Software	3 years
Standby generator	15 years
Website development	15 years

Property and equipment are reviewed for impairment if the use of the asset significantly changes or another indicator of possible impairment is identified. If the carrying amount for the asset is not recoverable, the asset is written down to its fair value. There were no asset impairments for the years ended June 30, 2022 and 2021.

Refundable Advances

The School records certain government operating revenue as refundable advances until related services are performed, at which time they are recognized as revenue.

The School is entitled to receive a rent subsidy that is calculated at the lower of 30 percent of the state and city per pupil amount or actual lease costs as approved by the New York City Department of Education (“NYCDOE”). There were no refundable advances associated with rent subsidy at June 30, 2022. During the year ended June 30, 2021, the school received funds from NYCDOE in excess of the amounts earned. A liability of \$315,546 was established at June 30, 2021 and is reflected in the accompanying statements of financial position.

Deferred Rent

The School records its rent in accordance with U.S. GAAP whereby all rental payments, including fixed rent increases, are recognized on a straight-line basis as an offset to rent expense. The difference between the straight-line rent expense and the required lease payments is reflected in deferred rent in the accompanying statements of financial position.

Challenge Preparatory Charter School

Notes to Financial Statements
June 30, 2022 and 2021

2. Summary of Significant Accounting Policies (*continued*)

Revenue and Support

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

Contributions are recognized when the donor makes a promise to give to the School that is, in substance, unconditional. Grants and other contributions of cash are reported as net assets with donor restrictions if they are received with donor stipulations. Restricted contributions and grants that are made to support the School's current year activities are recorded as net assets without donor restrictions. Contributions of assets other than cash are recorded at their estimated fair value at the date of donation.

Marketing and Recruitment

Marketing and recruitment costs are expenses as incurred. Marketing and recruitment costs for the years ended June 30, 2022 and 2021 amounted to \$100,904 and \$90,282.

Functional Expense Allocation

The majority of expenses can generally be directly identified with the program or supporting service to which they relate and are charged accordingly. Other expenses by function have been allocated among program and supporting services classifications on the basis of periodic time and expense studies and other bases as determined by management of the School to be appropriate.

Accounting for Uncertainty in Income Taxes

The School recognizes the effect of income tax positions only if those positions are more likely than not to be sustained. Management has determined that the School had no uncertain tax positions that would require financial statement recognition or disclosure. The School is no longer subject to examinations by the applicable taxing jurisdictions for years prior to June 30, 2019.

Subsequent Events Evaluation by Management

Management has evaluated subsequent events for disclosure and/or recognition in the financial statements through the date that the financial statements were available to be issued, which date is October 13, 2022.

Challenge Preparatory Charter School

Notes to Financial Statements
June 30, 2022 and 2021

3. Grants and Contracts Receivable

Grants and contracts receivable consist of federal, state, city entitlements and grants. The School expects to collect these receivables within one year. Management has assessed the need for an allowance and has determined that such allowance is not necessary.

4. Property and Equipment

Property and equipment consisted of the following at June 30:

	<u>2022</u>	<u>2021</u>
Computers and equipment	\$ 1,563,703	\$ 1,110,086
Furniture and fixtures	722,908	448,755
Software and website development	55,217	55,217
Standby generator	127,589	127,589
Leasehold improvements	1,101,667	713,269
Construction in progress	-	320,673
	<u>3,571,084</u>	<u>2,775,589</u>
Accumulated depreciation and amortization	<u>(1,939,110)</u>	<u>(1,409,550)</u>
	<u>\$ 1,631,974</u>	<u>\$ 1,366,039</u>

Construction in progress at June 30, 2021 consisted of soft costs associated with the new facilities at 15-20 Central Avenue, Queens, New York (see Note 10). The construction was completed, and the facilities were placed into service during the year ended June 30, 2022.

5. Liquidity and Availability of Financial Assets

Financial assets available for general expenditure, that is, without donor or other restrictions limiting their use within one year of the statement of financial position date, are comprised of the following at June 30:

	<u>2022</u>	<u>2021</u>
Cash	\$ 2,829,496	\$ 6,635,874
Grants and contracts receivable	527,246	365,449
Due from related party	5,000	-
	<u>\$ 3,361,742</u>	<u>\$ 7,001,323</u>

As part of the School's liquidity management plan, the status of grants and contracts receivable is monitored regularly and any excess cash is held in liquid instruments until it is required for operational use. To help manage unanticipated liquidity needs, the School has a letter of credit in the amount of \$50,000, which it could draw upon as further disclosed in Note 11. The School will continue to rely on funding received from the New York City Department of Education to cover its future operating costs (see Note 8).

Challenge Preparatory Charter School

Notes to Financial Statements
June 30, 2022 and 2021

6. Employee Benefit Plan

The School maintains a defined pension plan qualified under Internal Revenue Code 403(b), for the benefit of its eligible employees. Under the plan, the School provided matching contributions up to 3% of annual compensation. Employer match for the years ended June 30, 2022 and 2021 amounted to \$213,943 and \$177,127.

7. Concentration of Credit Risk

Financial instruments that potentially subject the School to concentrations of credit and market risk consist principally of cash on deposit with financial institutions, which from time to time may exceed the Federal Deposit Insurance Corporation ("FDIC") limit. The School does not believe that a significant risk of loss due to the failure of a financial institution presently exists. As of June 30, 2022 and 2021, approximately \$2,580,000 and \$6,390,000 of cash was maintained with an institution in excess of FDIC limits.

8. Concentration of Revenue and Support

The School receives a substantial portion of its revenue and support from the New York City Department of Education. For the years ended June 30, 2022 and 2021, the School received approximately 92% and 96% of total revenue and support from the New York City Department of Education. If the charter school laws were modified, reducing or eliminating these revenues, the School's finances could be materially adversely affected.

9. Related Party Transactions (not disclosed elsewhere)

The School is an affiliate of Friends of Challenge Prep. Inc. ("FOCP"), a New York State not-for-profit corporation, through common management. FOCP supports the School through real estate and facilities-related needs. At June 30, 2022 and 2021, the balance due from FOCP was \$5,000 and \$0.

Effective May 1, 2022, the lease agreement for one facility used by the School was transferred to FOCP (see Note 10) and a new sublease agreement was entered into between FOCP (sublandlord) and the School (subtenant). As a result of this transfer, an unamortized deferred rent liability was written off resulting in a non-operating gain of \$1,272,042 which is reported as gain on transfer of lease to related party in the statements of activities for year ended June 30, 2022.

Challenge Preparatory Charter School

Notes to Financial Statements
June 30, 2022 and 2021

10. Commitments

On December 10, 2010, the School entered into a non-cancelable operating lease for office and classroom space at 710 Hartman Lane, Far Rockaway, New York, expiring on May 31, 2032. The lease includes a yearly rent escalation of 3%, and requires the School to pay for utilities and other office costs. The School moved into this facility on April 16, 2012, and it currently houses grades K-3.

On December 5, 2014, the School entered into an agreement to lease additional property at 15-26 Central Avenue, Queens, New York, expiring on May 31, 2026. The lease commenced on September 19, 2015 and includes a yearly rent escalation of 3%, and requires the School to pay for utilities and other office costs. This location was the home of Challenge Preparatory Middle School from the 2015-2016 through the 2017-2018 academic years and is currently houses grades 4-5.

On September 29, 2015, the School entered into an agreement to lease additional property at 15-20 Central Avenue, Queens, New York, expiring on August 31, 2042. The lease commenced in August 2021 and includes a yearly rent escalation of 3%, and requires the School to pay for utilities and other office costs. This location is being used to house grades 9-10. In May 2022, the lease agreement was transferred to FOCP (see Note 9) and a new sublease agreement between FOCP (sublandlord) and the School (subtenant) was executed effective May 1, 2022 for a period of 29 years ending on June 30, 2051.

On September 1, 2018, the School entered into an agreement to lease additional property at 12-79 Redfern Avenue, Queens, New York, expiring on August 31, 2034. The lease commenced on September 1, 2018 and includes a yearly rent escalation of 3%, and requires the School to pay for utilities and other office costs. This location became the home of Challenge Preparatory Middle School starting with the 2018-2019 academic year. It currently houses grades 6-8.

Challenge Preparatory Charter School

Notes to Financial Statements
June 30, 2022 and 2021

10. Commitments (continued)

The future minimum lease payments for the four facility leases are as follows for years ending June 30:

2023	\$ 5,294,612
2024	5,453,452
2025	5,617,054
2026	5,221,208
2027	5,265,627
Thereafter	<u>124,177,935</u>
	<u>\$151,029,888</u>

The School recognizes rent expense on a straight-line basis over the term of the leases. Rent expense in excess of payments is recorded as deferred rent in the accompanying statements of financial position. Occupancy expense under the leases for the years ended June 30, 2022 and 2021 amounted to \$6,942,056 and \$2,752,203.

11. Line of Credit

On December 6, 2010, the School established a \$50,000 line of credit with a local financial institution. The line of credit is payable on demand and bears interest at prime rate plus 2.75%. The line of credit is secured by substantially all assets of the School. There was no outstanding balance as of June 30, 2022 and 2021.

12. Paycheck Protection Program Loan Payable

On May 4, 2020, the School received loan proceeds in the amount of \$1,792,512 under the Paycheck Protection Program (the "PPP"). The PPP, established as part of the Coronavirus Aid, Relief and Economic Security Act (the "CARES Act"), provides for loans to qualifying entities for amounts up to 2.5 times the 2019 average monthly payroll expenses of the qualifying entity. The PPP loan bears an interest rate of 1% per annum. All or a portion of the PPP loan principal and accrued interest were forgivable as long as the borrower used the loan proceeds for eligible purposes, as described in the CARES Act, over a period of between eight and twenty-four weeks (the "Covered Period"). Loan payments of principal or interest are deferred until the amount of loan forgiveness is determined by the United States Small Business Administration ("SBA").

On November 4, 2021, \$1,792,512 of principal and \$20,507 of accrued interest were forgiven by the SBA, and as such, the School has recognized the proceeds as gain on forgiveness of Paycheck Protection Program Loan in the accompanying statements of activities.

Challenge Preparatory Charter School

Notes to Financial Statements
June 30, 2022 and 2021

13. Contingency

Certain grants and contracts may be subject to audit by the funding sources. Such audits might result in disallowances of costs submitted for reimbursement. Management is of the opinion that such cost disallowances, if any, will not have a material effect on the accompanying financial statements. Accordingly, no amounts have been provided in the accompanying financial statements for such potential claims.

14. Risks and Uncertainties

The School's operations and financial performance may be affected by the recent COVID-19 outbreak which has spread globally and is expected to adversely affect economic conditions throughout the world. If the outbreak continues and conditions worsen, the School may experience a disruption in operations as well as a decline in revenue activities. Economic uncertainty is related to the potential reduction and/or delays in state and local per pupil operating revenue, shortfalls and variations in enrollment, and operational and other changes that could increase expenses. The outbreak may adversely affect the School's activities, financial condition, results of operations, and cash flows. Management is closely monitoring the impact of COVID-19 and believes the School is taking appropriate actions to mitigate the negative impact. However, management is unable to estimate the financial impact, if any, related to this matter.

Challenge Preparatory Charter School

Uniform Guidance
Schedules and Reports

June 30, 2022

Challenge Preparatory Charter School

Schedule of Expenditures of Federal Awards
Year Ended June 30, 2022

Federal Grantor/Pass-Through Grantor/ Program or Cluster Title	Federal Assistance Listing Number	Pass-Through Entity Identifying Number	Provided to Subrecipients	Total Federal Expenditures
U.S. Department of Education				
Pass-Through New York State Education Department:				
Title I Grants to Local Educational Agencies	84.010	0021-22-4785	\$ -	\$ 192,479
Title I Grants to Local Educational Agencies	84.010	0021-21-4785	-	13,598
			<u>-</u>	<u>206,077</u>
Supporting Effective Instruction State Grants (Formerly Improving Teacher Quality State Grants)	84.367	0147-22-4785	-	38,698
Student Support and Academic Enrichment Program	84.424	0204-22-4785	-	14,030
Student Support and Academic Enrichment Program	84.424	0204-19-4785	-	11,618
			<u>-</u>	<u>25,648</u>
Education Stabilization Fund/Elementary and Secondary School Emergency Relief Fund	84.425D	5890-21-4785	-	70,456
Education Stabilization Fund/Elementary and Secondary School Emergency Relief Fund II	84.425D	5891-21-4785	-	237,983
Education Stabilization Fund/Elementary and Secondary School Emergency Relief Fund ARP	84.425U	5880-21-4785	-	722,990
			<u>-</u>	<u>1,031,429</u>
Total U.S. Department of Education			<u>-</u>	<u>1,301,852</u>
Total Expenditures of Federal Awards			<u>\$ -</u>	<u>\$ 1,301,852</u>

See independent auditors' report and notes to schedule of expenditures of federal awards

Challenge Preparatory Charter School

Notes to Schedule of Expenditures of Federal Awards
Year Ended June 30, 2022

1. Basis of Presentation

The accompanying schedule of expenditures of federal awards (the "Schedule") includes the federal award activity of Challenge Preparatory Charter School (the "School"), under programs of the federal government for the year ended June 30, 2022. The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* ("Uniform Guidance"). Because the Schedule presents only a selected portion of the operations of the School, it is not intended to and does not present the financial position, changes in net assets or cash flows of the School.

2. Summary of Significant Accounting Policies

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

3. Indirect Cost Rate

The School has elected not to use the 10-percent de minimis indirect cost rate allowed under the Uniform Guidance.

**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**

Independent Auditors' Report

**Board of Trustees
Challenge Preparatory Charter School**

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Challenge Preparatory Charter School (the "School") (a nonprofit organization), which comprise the statement of financial position as of June 30, 2022, and the related statements of activities, functional expenses and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated October 13, 2022.

Report on Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the School's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the School's internal control. Accordingly, we do not express an opinion on the effectiveness of the School's internal control.

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

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

Report on Compliance and Other Matters

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

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

PKF O'Connor Davies, LLP

Harrison, New York
October 13, 2022

**Report on Compliance for Each Major Federal Program and Report on Internal Control
Over Compliance Required by the Uniform Guidance**

Independent Auditors' Report

**Board of Trustees
Challenge Preparatory Charter School**

Report on Compliance for Each Major Federal Program

Opinion on Each Major Federal Program

We have audited Challenge Preparatory Charter School's (the "School") compliance with the types of compliance requirements identified as subject to audit in the OMB *Compliance Supplement* that could have a direct and material effect on each of the School's major federal programs for the year ended June 30, 2022. The School's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

In our opinion, the School complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2022.

Basis for Opinion on Each Major Federal Program

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 the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Our responsibilities under those standards and the Uniform Guidance are further described in the Auditors' Responsibilities for the Audit of Compliance section of our report.

We are required to be independent of the School and to meet our other ethical responsibilities, in accordance with relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion on compliance for each major federal program. Our audit does not provide a legal determination of the School's compliance with the compliance requirements referred to above.

Responsibilities of Management for Compliance

Management is responsible for compliance with the requirements referred to above and for the design, implementation, and maintenance of effective internal control over compliance with the requirements of laws, statutes, regulations, rules, and provisions of contracts or grant agreements applicable to the School's federal programs.

Auditors' Responsibilities for the Audit of Compliance

Our objectives are to obtain reasonable assurance about whether material noncompliance with the compliance requirements referred to above occurred, whether due to fraud or error, and express an opinion on the School's compliance based on our audit. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with generally accepted auditing standards, *Government Auditing Standards*, and the Uniform Guidance will always detect material noncompliance when it exists. The risk of not detecting material noncompliance resulting from fraud is higher than for that resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Noncompliance with the compliance requirements referred to above is considered material if there is a substantial likelihood that, individually or in the aggregate, it would influence the judgment made by a reasonable user of the report on compliance about the School's compliance with the requirements of each major federal program as a whole.

In performing an audit in accordance with generally accepted auditing standards, *Government Auditing Standards*, and the Uniform Guidance, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material noncompliance, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the School's compliance with the compliance requirements referred to above and performing such other procedures as we considered necessary in the circumstances.
- Obtain an understanding of the School's internal control over compliance relevant to the audit in order to design audit procedures that are appropriate in the circumstances and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of the School's internal control over compliance. Accordingly, no such opinion is expressed.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and any significant deficiencies and material weaknesses in internal control over compliance that we identified during the audit.

Report on 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 a combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the Auditors' Responsibilities for the Audit of Compliance section above and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies in internal control over compliance. Given these limitations, during our audit we did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above. However, material weaknesses or significant deficiencies in internal control over compliance may exist that were not identified.

Our audit was not designed for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, no such opinion is expressed.

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

PKF O'Connor Davies, LLP

Harrison, New York
October 13, 2022

Challenge Preparatory Charter School

Schedule of Findings and Questioned Costs
Year Ended June 30, 2022

Section I - Summary of Auditors' Results

Financial Statements

Type of report the auditor issued on whether the financial statements audited were prepared in accordance with U.S. GAAP:

Unmodified

Internal control over financial reporting:

Material weakness(es) identified?

_____ yes X no

Significant deficiency(ies) identified?

_____ yes X none reported

Noncompliance material to the financial statements noted?

_____ yes X no

Federal Awards

Internal control over major federal programs:

Material weakness(es) identified?

_____ yes X no

Significant deficiency(ies) identified?

_____ yes X none reported

Type of auditors' report issued on compliance for major federal programs:

Unmodified

Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)?

_____ yes X no

Identification of major federal programs:

Federal Assistance Listing Number(s)

Name of Federal Program or Cluster

84.425D

Education Stabilization Fund/Elementary and Secondary School Emergency Relief Fund

84.425D

Education Stabilization Fund/Elementary and Secondary School Emergency Relief Fund II

84.425U

Education Stabilization Fund/Elementary and Secondary School Emergency Relief Fund ARP

Dollar threshold used to distinguish between Type A and Type B programs:

\$750,000

Auditee qualified as low-risk auditee?

_____ yes X no

Section II – Financial Statement Findings

During our audit, we noted no material findings for the year ended June 30, 2022.

Section III – Federal Award Findings and Questioned Costs

During our audit, we noted no material instance of noncompliance and none of the costs tested which were reported in the federal financially assisted programs are questioned or recommended to be disallowed.

Section IV – Prior Year Findings

There were no findings in the prior year.