



CONSOLIDATED FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT

June 30, 2018 and 2017

HERITAGE CHRISTIAN SCHOOLS, INC.

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Independent Auditors' Report

Board of Directors
Heritage Christian Schools, Inc.

We have audited the accompanying consolidated financial statements of Heritage Christian Schools, Inc. (a not-for-profit organization) and Affiliate, which comprise the consolidated statements of financial position as of June 30, 2018 and 2017, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Heritage Christian Schools, Inc. and Affiliate as of June 30, 2018 and 2017, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Katz, Sapper & Miller, LLP

Indianapolis, Indiana
October 26, 2018

HERITAGE CHRISTIAN SCHOOLS, INC.
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
June 30, 2018 and 2017

	2018	2017
ASSETS		
Cash	\$ 2,663,836	\$ 1,932,614
Accounts receivable	29,848	
Tuition receivable, net of allowance of \$195,148 in 2018 and \$45,000 in 2017	363,943	279,856
Pledges receivable, net of allowance of \$54,000 in 2018 and \$79,374 in 2017	425,540	542,415
Receivable from charitable remainder trust		425,574
Inventory	6,637	7,751
Prepaid expenses	53,205	68,501
Land held for investment	270,000	270,000
Property and equipment, net	15,377,048	15,665,391
Collections	<u>72,219</u>	<u>60,219</u>
TOTAL ASSETS	<u><u>\$ 19,262,276</u></u>	<u><u>\$ 19,252,321</u></u>
LIABILITIES		
Accounts payable	\$ 280,060	\$ 289,243
Accrued expenses	645,742	756,562
Deferred tuition revenue	1,197,081	1,219,358
Derivative contract	6,678	46,371
Debt, net of bond issuance costs	<u>2,066,859</u>	<u>2,179,875</u>
Total Liabilities	<u>4,196,420</u>	<u>4,491,409</u>
NET ASSETS		
Unrestricted:		
Board designated - annual fund	572,510	569,478
Undesignated	<u>13,186,567</u>	<u>13,255,425</u>
	13,759,077	13,824,903
Temporarily restricted	1,303,209	932,439
Permanently restricted	<u>3,570</u>	<u>3,570</u>
Total Net Assets	<u>15,065,856</u>	<u>14,760,912</u>
TOTAL LIABILITIES AND NET ASSETS	<u><u>\$ 19,262,276</u></u>	<u><u>\$ 19,252,321</u></u>

See accompanying notes.

HERITAGE CHRISTIAN SCHOOLS, INC.
CONSOLIDATED STATEMENTS OF ACTIVITIES
Years Ended June 30, 2018 and 2017

	2018			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
REVENUE AND SUPPORT				
Tuition and fees, net of tuition assistance	\$ 11,781,543			\$ 11,781,543
Auxiliary services	1,106,865			1,106,865
Contributions	79,864	\$ 926,963		1,006,827
Bad debt losses		(3,383)		(3,383)
Special events	345,463			345,463
Interest and dividends	150			150
Change in fair value of derivative contract	39,693			39,693
Other income	53,984			53,984
	<u>13,407,562</u>	<u>923,580</u>		<u>14,331,142</u>
Net assets released from restrictions	552,810	(552,810)		
Total Revenue and Support	<u>13,960,372</u>	<u>370,770</u>		<u>14,331,142</u>
EXPENSES				
Salaries and benefits	9,442,196			9,442,196
Curriculum and supplies	585,911			585,911
Repairs and maintenance	599,760			599,760
Utilities	495,485			495,485
Cleaning service	429,568			429,568
Insurance	142,659			142,659
Food and supplies	336,429			336,429
Special events	319,333			319,333
Travel and meals	59,995			59,995
Workshops and continuing education	28,849			28,849
Depreciation	937,097			937,097
Interest	114,369			114,369
Other	534,547			534,547
Total Expenses	<u>14,026,198</u>			<u>14,026,198</u>
INCREASE (DECREASE) IN NET ASSETS	(65,826)	370,770		304,944
NET ASSETS				
Beginning of Year	<u>13,824,903</u>	<u>932,439</u>	\$ 3,570	<u>14,760,912</u>
End of Year	<u>\$ 13,759,077</u>	<u>\$ 1,303,209</u>	<u>\$ 3,570</u>	<u>\$ 15,065,856</u>

See accompanying notes.

2017

Unrestricted	Temporarily Restricted	Permanently Restricted	Total
\$ 11,559,325			\$ 11,559,325
1,121,719			1,121,719
513,077	\$ 709,002		1,222,079
	(65,040)		(65,040)
310,420			310,420
132			132
58,732			58,732
100,372			100,372
<u>13,663,777</u>	<u>643,962</u>		<u>14,307,739</u>
<u>1,407,742</u>	<u>(1,407,742)</u>		
<u>15,071,519</u>	<u>(763,780)</u>		<u>14,307,739</u>
9,808,385			9,808,385
613,922			613,922
688,632			688,632
503,820			503,820
431,654			431,654
138,381			138,381
291,167			291,167
345,383			345,383
64,628			64,628
44,215			44,215
920,885			920,885
151,774			151,774
539,152			539,152
<u>14,541,998</u>			<u>14,541,998</u>
529,521	(763,780)		(234,259)
<u>13,295,382</u>	<u>1,696,219</u>	<u>\$ 3,570</u>	<u>14,995,171</u>
<u>\$ 13,824,903</u>	<u>\$ 932,439</u>	<u>\$ 3,570</u>	<u>\$ 14,760,912</u>

HERITAGE CHRISTIAN SCHOOLS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended June 30, 2018 and 2017

	2018	2017
OPERATING ACTIVITIES		
Increase (decrease) in net assets	\$ 304,944	\$ (234,259)
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities:		
Depreciation	937,097	920,885
Amortization of deferred financing costs in interest expense	14,805	14,806
Bad debt expense	91,292	58,615
(Gain) loss on sales and disposition of property and equipment	7,325	(14,712)
Decrease in derivative contract liability	(39,693)	(58,732)
(Increase) decrease in certain assets:		
Accounts receivable	(29,848)	33,906
Tuition receivable	(175,379)	(39,178)
Pledges receivable	116,875	548,934
Receivable from charitable remainder trusts	425,574	(425,574)
Inventory	1,114	4,368
Prepaid expenses	15,296	33,748
Increase (decrease) in certain liabilities:		
Accounts payable	(9,183)	86,731
Accrued expenses	(110,820)	186,190
Deferred tuition revenue	(22,277)	(180,177)
Net Cash Provided by Operating Activities	<u>1,527,122</u>	<u>935,551</u>
INVESTING ACTIVITIES		
Purchases of property and equipment	(530,045)	(289,562)
Proceeds from sales of property and equipment		20,600
Net Cash Used by Investing Activities	<u>(530,045)</u>	<u>(268,962)</u>
FINANCING ACTIVITIES		
Payments on bonds	(200,000)	(1,085,000)
Payments on capital lease obligations	(65,855)	(49,088)
Net Cash Used by Financing Activities	<u>(265,855)</u>	<u>(1,134,088)</u>
NET INCREASE (DECREASE) IN CASH	731,222	(467,499)
CASH		
Beginning of Year	<u>1,932,614</u>	<u>2,400,113</u>
End of Year	<u>\$ 2,663,836</u>	<u>\$ 1,932,614</u>
SUPPLEMENTAL DISCLOSURES		
Cash paid for interest	\$ 114,369	\$ 151,774
Noncash investing and financing activities:		
Obligations assumed for acquisition of equipment	138,034	78,967

See accompanying notes.

HERITAGE CHRISTIAN SCHOOLS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS June 30, 2018 and 2017

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Consolidated Financial Statements: The accompanying consolidated financial statements include the accounts of Heritage Christian Schools, Inc. (Heritage) and its affiliate, HCS Real Estate, LLC (HCS Real Estate) (together, the Organization). Heritage is the sole member of HCS Real Estate. HCS Real Estate was organized on April 21, 2016 to hold donated land that is held for investment. All significant intra-entity accounts and transactions have been eliminated in consolidation.

Heritage is a nonprofit religious/educational organization incorporated under the laws of the state of Indiana. Heritage's objective is to provide, based upon the Word of God, a Christian education to preschool through twelfth grade students in the Indianapolis area. Revenues are derived primarily from students' tuition and related service fees. Heritage also receives contributions from friends and the general public.

Heritage is a member of Indiana Non-Public Education Association, Association of Christian Schools International (ACSI), and Indianapolis Christian School Association. Heritage is accredited by ACSI. The high school is also accredited by AdvancED.

Basis of Presentation: The accompanying consolidated financial statements were prepared on the accrual basis of accounting.

The Organization reports information regarding their consolidated financial position and activities according to three classes of net assets: unrestricted, temporarily restricted and permanently restricted.

- The unrestricted net asset class includes general assets and liabilities which may be used at the discretion of management to support the purposes and operations of the Organization.
- The temporarily restricted net asset class includes assets related to gifts with explicit donor-imposed restrictions that have not been met as to specified purpose, or to later periods of time or after specified dates. Unconditional promises to give that are due in future periods and are not permanently restricted are classified as temporarily restricted net assets.
- The permanently restricted net assets class includes assets for which the donor has stipulated that the contribution be maintained in perpetuity. Donor-imposed restrictions limiting the use of the assets or their economic benefit neither expire with the passage of time nor can be removed by satisfying a specific purpose.

Estimates: The preparation of consolidated financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities and the reported amounts of revenues and expenses. Actual results could differ from those estimates.

Cash consists of checking, savings, and money market accounts at banks. While at times cash balances may exceed federally insured limits, Heritage has not experienced any losses in such accounts. Management believes the Organization is not exposed to any significant credit risk on these accounts.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Tuition Receivable: The carrying amount of accounts receivable for tuition and fees is reduced by an allowance that reflects management's best estimate of the amounts that will not be collected. Past due amounts are reviewed regularly by management. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance.

Pledges Receivable: Pledges receivable represent the remaining balance of unconditional promises to give that have not yet been paid. Pledges that are expected to be collected within one year or less are recorded at net realizable value. Pledges that are expected to be collected beyond one year are recorded at the present value of their estimated future cash flows. The pledges have been discounted using a risk-free interest rate applicable during the time the pledge was made. Management uses historical collection and aging of receivables to estimate an allowance for doubtful accounts.

Self-Insurance Plan: Heritage has elected to act as a self-insurer for certain costs related to employee health and accident benefits. Such costs are charged to operations when incurred. Heritage's stop-loss health insurance policy states that any claims paid in excess of a specified dollar amount will be reimbursed. At June 30, 2018 and 2017, Heritage estimated the self-insurance liability, net of insurance recoveries, to be approximately \$175,000 and \$201,000, respectively.

Inventory consists of bookstore supplies and various resale items on hand. Inventory is reported at the lower of cost or market, with cost determined using the first-in, first-out method.

Land Held for Investment consists of land that was donated and reflected as contributions at the appraised value.

Property and Equipment and Depreciation: Property and equipment over \$1,000 are capitalized at cost, at the date of acquisition, or at fair value at the date of gift. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets, ranging from 3 to 40 years.

Property and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability is measured by comparison of the carrying amount of an asset to the future net undiscounted cash flows expected to be generated by the asset. If the asset is considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount exceeds the fair market value of the asset. To date, no adjustments to the carrying amount of such long-lived assets have been required.

Collections consist of sculptures donated to Heritage. Donated items are reported at their appraised or fair market value on the date of the gift.

Revenue and Support: Tuition amounts received or billed in advance but not earned are reported as deferred tuition. Tuition and fees are recognized as earned over the school year.

Support is reported when contributions are made, which is generally when cash is received, unconditional promises are made, or when ownership of donated assets is transferred to the Organization. Bequests are reported as support at the time Heritage has established its right to the bequest and the proceeds are measurable. The Organization reports gifts of cash and other assets as restricted revenue if they are received with donor stipulations that limit the use of the donated assets. Net assets are reported as released from restrictions when expenses have been incurred in satisfaction of these donor restrictions.

The Organization reports gifts of property and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how those long-lived assets must be maintained, the Organization reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Advertising Costs are expensed as incurred. Such costs totaled \$60,215 and \$67,096 in fiscal years 2018 and 2017, respectively.

Tax Status: Heritage is exempt from federal and state income taxes under Section 501(c)(3) of the Internal Revenue Code and a corresponding state tax law. Therefore, no provision or liability for income taxes has been included in the consolidated financial statements. In addition, Heritage has been determined by the Internal Revenue Service not to be a private foundation within the meaning of Section 509(a) of the Internal Revenue Code. There was no unrelated business income for fiscal years 2018 and 2017.

Heritage files U.S. federal and state of Indiana information tax returns. Heritage is no longer subject to U.S. federal and state income tax examinations by tax authorities for years before fiscal year 2015.

HCS Real Estate is single member LLC and is a disregarded entity for income tax purposes. All income, gains, losses and deductions of HCS Real Estate are included in Heritage's tax filings.

Subsequent Events: Management has evaluated the consolidated financial statements for subsequent events occurring through October 26, 2018, the date the consolidated financial statements were available to be issued. See Note 6.

NOTE 2 - FAIR VALUE MEASUREMENTS

The Organization has categorized its assets and liabilities that are measured at fair value into a three-level fair value hierarchy. The hierarchy 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) and the lowest priority to unobservable inputs (Level 3). 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.

The three levels of the fair value hierarchy 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 Organization has the ability to access.

Level 2 – Inputs to the valuation methodology may 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; and/or 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. In situations where there is little or no market activity for the asset or liability, the Organization makes estimates and assumptions related to the pricing of the asset or liability including assumptions regarding risk.

Following is a description of the valuation methodology used by Heritage for a derivative liability that is measured at fair value on a recurring basis. There have been no changes in the methodology used at June 30, 2018 and 2017.

Derivative Contract: The fair value of the derivative contract liability related to an interest rate swap agreement was computed at the net settlement amount, which is determined by applying the rates to notional amounts that equal the amount of principal outstanding under the hedged notes.

NOTE 2 - FAIR VALUE MEASUREMENTS (CONTINUED)

Following is a summary of Heritage's derivative contract liability, by level of the fair value hierarchy, that is measured at fair value on a recurring basis as of June 30, 2018 and 2017:

2018	Level 3	Total
Derivative contract liability	<u>\$ 6,678</u>	<u>\$ 6,678</u>
2017	Level 3	Total
Derivative contract liability	<u>\$46,371</u>	<u>\$46,371</u>

Changes in the fair value of the Level 3 derivative contract liability were net unrealized gains of \$39,693 and \$58,732 in fiscal years 2018 and 2017, respectively.

At June 30, 2018 and 2017, the Organization had no assets and no other liabilities that are measured at fair value on a recurring basis.

NOTE 3 - PLEDGES RECEIVABLE

Heritage conducts fund-raising campaigns to help pay down debt and support other initiatives detailed out in the campaigns. Heritage determined that a discount of the pledges receivable was immaterial to the consolidated financial statements. Pledges receivable as of June 30, 2018 and 2017, are all temporarily restricted and are summarized as follows:

	2018	2017
Due within one year	\$473,190	\$467,614
Due in one to five years	<u>6,350</u>	<u>154,175</u>
	479,540	621,789
Allowance for uncollectible pledges	<u>(54,000)</u>	<u>(79,374)</u>
	<u>\$425,540</u>	<u>\$542,415</u>

Heritage had pledges receivable from two contributors totaling 58% of the total pledges receivable balance at June 30, 2018. Heritage had pledges receivables from two contributors totaling 27% of the total pledges receivable balance at June 30, 2017.

NOTE 4 - PROPERTY AND EQUIPMENT

Property and equipment consisted of the following at June 30, 2018 and 2017:

	2018	2017
Buildings and improvements	\$ 28,162,334	\$ 27,841,925
Furnishings and equipment	4,098,746	3,781,391
Transportation equipment	<u>367,768</u>	<u>361,184</u>
	32,628,848	31,984,500
Less: Accumulated depreciation	<u>(18,084,832)</u>	<u>(17,152,141)</u>
	14,544,016	14,832,359
Land	<u>833,032</u>	<u>833,032</u>
Total Property and Equipment, net	<u>\$ 15,377,048</u>	<u>\$ 15,665,391</u>

NOTE 5 - CHARITABLE REMAINDER TRUST

At June 30, 2017, Heritage was the remainder beneficiary of a charitable remainder trust held by a third-party trustee. The charitable remainder trust provides for the payment of distributions to the grantor or another designated beneficiary over the designated beneficiary's lifetime. Upon the death of the designated beneficiary, the remaining assets are available for Heritage's use. The lifetime beneficiary of the trust was deceased as of June 30, 2017, thus the fair value of the trust assets were reflected in the consolidated statement of financial position as a receivable from charitable remainder trust. The value of the trust was \$425,574 at June 30, 2017. The trust was distributed to Heritage in August 2017 in the amount of \$433,532.

NOTE 6 - DEBT

Debt outstanding at June 30, 2018 and 2017, was as follows:

	2018	2017
Economic Development Revenue Bonds payable in semi-annual principal installments from June 2006 through maturity in 2020. Interest computed at a variable rate is payable monthly (effective interest rate of 4.71% at June 30, 2018). A derivative contract has been entered to protect Heritage from interest rate fluctuations through December 1, 2020. The bonds are secured by a first mortgage on specific Heritage property. The bonds require compliance with certain restrictive covenants and performance requirements.	\$1,870,000	\$2,070,000
Capital lease obligation due in monthly installments of \$1,579, with a purchase option at the conclusion of the lease in fiscal year 2020. Imputed interest on the lease is immaterial. Secured by equipment recorded at a cost of \$94,762 and accumulated depreciation of \$56,857 at June 30, 2018.	37,905	56,857
Capital lease obligation due in monthly installments of \$829, with a purchase option at the conclusion of the lease in fiscal year 2022. Imputed interest on the lease is immaterial. Secured by equipment recorded at a cost of \$49,515 and accumulated depreciation of \$14,029 at June 30, 2018.	34,818	44,767
Capital lease obligation due in monthly installments of \$483, with a purchase option at the conclusion of the lease in fiscal year 2022. Imputed interest on the lease is immaterial. Secured by equipment recorded at a cost of \$28,913 and accumulated depreciation of \$8,192 at June 30, 2018.	20,301	26,103
Capital lease obligation due in monthly installments of \$1,221. Repaid during fiscal year 2018.		26,576
Capital lease obligation due in monthly installments of \$1,044, with a purchase option at the conclusion of the lease in fiscal year 2021. Imputed interest on the lease is immaterial. Secured by equipment recorded at a cost of \$96,495 and accumulated depreciation of \$48,085 at June 30, 2018.	37,594	

NOTE 6 - DEBT (CONTINUED)

	2018	2017
Capital lease obligation due in monthly installments of \$2,188, with a purchase option at the conclusion of the lease in fiscal year 2022. Interest is imputed on the lease at 5.714%. Secured by equipment recorded at a cost of \$131,265 and accumulated depreciation of \$24,065 at June 30, 2018.	<u>\$ 95,864</u>	<u>\$2,224,303</u>
Less: Debt issuance costs, net	<u>(29,623)</u>	<u>(44,428)</u>
Total Debt, net	<u>\$2,066,859</u>	<u>\$2,179,875</u>

Debt issuance costs are being amortized on the effective interest rate method. Amortization of the debt issuance costs is reported as interest expense in the consolidated statements of activities. At June 30, 2018 and 2017, debt issuance costs totaled \$207,294 and accumulated amortization totaled \$177,671 and \$162,866, respectively. Related amortization reported as interest expense was \$14,805 and \$14,806 in fiscal years 2018 and 2017, respectively.

In July 2018, Heritage paid an additional \$900,000 on their bond debt, decreasing the amount due at final maturity. This payment is not reflected in the required payments schedule below. At June 30, 2018, the required capital lease payments and the scheduled bond principal payments on the Economic Development Revenue Bonds were as follows:

Payable In Fiscal Year	Capital Lease Payments	Bond Principal Payments
2019	\$ 73,485	\$300,000
2020	73,485	400,000
2021	54,533	270,000
2022	<u>36,315</u>	
Total Capital Lease Payments	237,818	
Less: Amount representing interest	<u>(11,336)</u>	
Net Capital Lease Obligation	<u>\$226,482</u>	

As a strategy to maintain acceptable levels of exposure to the risk of changes in future cash flows due to interest rate fluctuations, Heritage entered into a ten-year interest rate swap agreement for its variable rate bond debt. Heritage does not engage in speculative derivative transactions for trading purposes. The agreement provides for Heritage to pay a fixed interest rate and receive a variable interest rate through December 2020. The fixed interest rate provided by the swap is 2.12%.

Under the interest rate swap agreement, Heritage has agreed to exchange, at specified intervals, the difference between the fixed and variable interest amounts calculated by reference to the agreed-upon notional amount. The notional amount outstanding at June 30, 2018 was \$1,870,000 and will decline throughout the term of the bonds based on amortization of principal amounts.

Under the agreement, Heritage pays or receives the net interest amount monthly, with the monthly settlements included in interest expense. The derivative contract liability arising from the interest rate swap is stated at the settlement amount that Heritage would have to pay if the swap agreement was terminated at June 30, 2018 and 2017. Heritage has no intention of terminating the swap agreement.

NOTE 7 - RESTRICTED NET ASSETS

Temporarily restricted net assets at June 30, 2018 and 2017, consisted of the following:

	2018	2017
Development	\$ 449	\$129,248
Thrive	483,918	542,415
School activities	181,123	73,730
Athletics	64,878	63,499
Turf Field	458,500	
Facilities	19,851	25,191
Wish List	43,350	28,838
Extracurricular	17,637	16,668
Academic Director		5,914
Athena grant	5,425	5,425
Benevolent fund	26,977	27,986
Other	<u>1,101</u>	<u>13,525</u>
Total Temporarily Restricted Net Assets	<u>\$1,303,209</u>	<u>\$932,439</u>

Net assets released from donor restrictions by incurring expenses satisfying the restricted purposes or by the occurrence of other events specified by the donors for fiscal years 2018 and 2017, were comprised of:

	2018	2017
Development	\$ 21,275	\$ 52,076
Thrive	224,091	1,073,061
School activities	99,205	26,607
Athletics	37,173	37,269
Wish List	10,061	6,849
Worthy Servants	139,532	184,013
Other	<u>21,473</u>	<u>27,867</u>
Total Net Assets Released from Restrictions	<u>\$552,810</u>	<u>\$1,407,742</u>

Permanently restricted net assets at June 30, 2018 and 2017, consisted of the following:

	2018	2017
Scooby Gerbig Scholarship Fund	<u>\$3,570</u>	<u>\$3,570</u>
Total Permanently Restricted Net Assets	<u>\$3,570</u>	<u>\$3,570</u>

NOTE 8 - ENDOWMENT

Heritage's endowment consists of one individual fund established to provide financial support to Heritage in perpetuity. As required by accounting principles generally accepted in the United States of America, net assets associated with endowment funds, including funds designated by the Board to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions. Heritage classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment and any accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument 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 Heritage.

NOTE 8 - ENDOWMENT (CONTINUED)

Interpretation of Relevant Law

The Uniform Prudent Management of Institutional Funds Act (UPMIFA) was adopted by Indiana in 2007. Heritage interprets UPMIFA to permit Heritage to appropriate for expenditure or accumulate so much of a donor-restricted endowment fund that Heritage determines is prudent for the uses, purposes, and duration of the endowment fund, unless there are explicit donor stipulations to the contrary. In accordance with UPMIFA, Heritage considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- The duration and preservation of the fund
- The purposes of the donor-restricted endowment fund
- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of Heritage
- The investment policies of Heritage

There were no changes in the endowment for the Scooby Gerbig Scholarship Fund as of June 30, 2018 and 2017.

Return Objectives and Risk Parameters

Heritage's current practice is to hold endowment assets in cash to safeguard the original endowment corpus until the Board of Directors adopts an investment policy. Endowment assets are composed of those assets of donor-restricted funds that Heritage must hold in perpetuity.

Spending Policy and How the Investment Objectives Relate to Spending Policy

The Board of Directors has chosen not to spend the endowment funds until it adopts an investment policy and spending policy. It is the Board of Directors' current practice to not spend from the endowment assets.

NOTE 9 - CONTRIBUTIONS

Contributions for fiscal years 2018 and 2017 included the following:

	2018	2017
Unrestricted Contributions:		
Jog-a-thon	\$ 69,779	\$ 80,211
Charitable remainder trust		425,574
Other unrestricted	<u>10,085</u>	<u>7,292</u>
Total Unrestricted Contributions	79,864	513,077
Temporarily Restricted Contributions	<u>926,963</u>	<u>709,002</u>
Total Contributions	<u>\$1,006,827</u>	<u>\$1,222,079</u>

NOTE 10 - CLASSIFICATION OF EXPENSES

Expenses are reported when incurred and the costs of providing various program services and supporting activities have been summarized below on a functional basis. Accordingly, certain costs, such as depreciation and payroll, have been allocated among the program services and supporting activities benefited. Expenses for fiscal years 2018 and 2017 were classified according to the following functional categories:

	2018	2017
Program activities	\$11,152,859	\$11,454,330
General and administrative	2,254,597	2,457,975
Fundraising	<u>618,742</u>	<u>629,693</u>
Total Expenses	<u>\$14,026,198</u>	<u>\$14,541,998</u>

NOTE 11 - RETIREMENT PLAN

Heritage has adopted a 401(k) retirement plan. Heritage's faculty and certain administrative employees can participate in the Plan, provided they have attained the age of 21, and have completed one year of service. Heritage may make a discretionary matching contribution, as well as a discretionary profit sharing contribution to the Plan. Heritage made no contributions to the Plan in fiscal years 2018 and 2017. Additionally, all participants may contribute to the Plan.

NOTE 12 - TUITION AND FEES - NET OF TUITION ASSISTANCE

Revenue from tuition and fees for fiscal years 2018 and 2017 included the following:

	2018	2017
Tuition:		
Preschool thru middle school	\$ 7,282,147	\$ 7,419,286
High school	4,843,939	4,507,223
Hidden treasures	115,998	125,797
Explorers	132,369	108,934
Directed study hall	37,395	33,883
Educational support services	11,953	18,464
Distance learning	9,380	26,265
Resource	<u>85,852</u>	<u>45,548</u>
	<u>12,519,033</u>	<u>12,285,400</u>
Fees:		
Enrollment fees	208,354	191,519
After-school care	170,629	158,064
Enrichment		3,550
Late payment and NSF charges	7,315	4,168
Application fees	7,470	10,123
Other	15,422	14,085
Testing fees	<u>9,054</u>	<u>25,594</u>
	<u>418,244</u>	<u>407,103</u>
Total Revenue from Tuition and Fees	12,937,277	12,692,503
Less: Prepaid tuition discount	(11,441)	(11,819)
Less: Tuition assistance	<u>(1,144,293)</u>	<u>(1,121,359)</u>
Net Revenue from Tuition and Fees	<u>\$11,781,543</u>	<u>\$11,559,325</u>

NOTE 13 - AUXILIARY SERVICES

Auxiliary services revenue for fiscal years 2018 and 2017 included the following:

	2018	2017
Athletics	\$ 226,845	\$ 238,524
Bookstore	5,564	23,075
Booster club/extracurricular	94,053	79,762
Cafeteria	626,903	612,086
Transportation	132,690	131,479
Other	<u>20,810</u>	<u>36,793</u>
	<u>\$1,106,865</u>	<u>\$1,121,719</u>

Auxiliary services expenses for fiscal years 2018 and 2017 included the following:

	2018	2017
Athletics	\$ 757,137	\$ 783,171
Bookstore	1,113	21,419
Booster club/extracurricular	219,465	188,408
Cafeteria	533,004	480,139
Transportation	<u>239,000</u>	<u>227,367</u>
	<u>\$1,749,719</u>	<u>\$1,700,504</u>

NOTE 14 - COMMITMENTS

In May 2018, Heritage entered into an agreement with a contractor to replace the turf field with a total cost of \$458,500. Heritage paid \$229,250 prior to June 30, 2018, and the remainder was paid in two installments in August and September 2018. The cost of this field was reimbursed to Heritage in full by a donor contribution.