

**PRIORITY SYSTEMS, INC.**

Financial Statements

August 31, 2018

## TABLE OF CONTENTS

Certificate of Board .....	1
Independent Auditor's Report .....	3
Financial Statements:	
Statement of Financial Position.....	6
Statement of Activities.....	7
Statement of Cash Flows .....	9
Notes to Financial Statements .....	10
Supplemental Information:	
Schedule of Expenses .....	21
Schedule of Capital Assets .....	22
Budgetary Comparison Schedule .....	23
Compliance and Internal Controls Section	
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i> .....	25
Schedule of Findings and Questioned Costs.....	29

**PRIORITY SYSTEMS, INC.**  
**T. I. N. 74-2886638**  
**C.D.N. 014803**  
**CERTIFICATE OF BOARD**

We, the undersigned, certify that the attached annual financial reports of the above named school were reviewed and ( ) approved ( ) disapproved for the year ended August 31, 2018, at a meeting of the governing body of said charter school on the \_\_\_\_ day of \_\_\_\_\_, 2019.

\_\_\_\_\_  
Signature of Board Secretary

\_\_\_\_\_  
Signature of Board President

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## INDEPENDENT AUDITOR'S REPORT

Board of Directors  
**PRIORITY SYSTEMS, INC.**  
275 FM 2483  
Morgan's Point Resort, TX 76513

We have audited the accompanying statements of Priority Systems, Inc. (a nonprofit Charter School), which comprise the statement of financial position as of August 31, 2018, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements.

### **Management's Responsibility for the Financial Statements**

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

### **Auditor's Responsibility**

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the 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 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 financial statements referred to above present fairly, in all material respects, the financial position of Priority Systems, Inc. as of August 31, 2018, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

## Other Matters

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying supplemental information is presented for purposes of additional analysis and is required by the Texas Education Agency. 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 January 4, 2019, on our consideration of Priority Systems Inc'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 Priority Systems Inc'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 Priority Systems Inc's internal control over financial reporting and compliance.



Evans & Knauth, PLLC  
Frisco, TX  
January 4, 2019

## **FINANCIAL STATEMENTS**

**PRIORITY SYSTEMS, INC.**  
Statement of Financial Position  
August 31, 2018

**ASSETS**

Current Assets:

Cash and Cash Equivalents	\$ 1,698,940
Due From State	275,050
Prepays	10,841
Other Assets	4,168
Total Current Assets	1,988,999

Non-Current Assets:

Capital Assets, Net	9,152,807
Total Non-Current Assets	9,152,807

Total Assets	\$ 11,141,806
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**LIABILITIES & NET ASSETS**

Current Liabilities:

Accounts Payable	\$ 294,402
Accrued Expenses	11,031
Payroll Tax and Other Withholdings	126,097
Current Portion of Long-Term Debt	345,961
Total Current Liabilities	777,491

Long-Term Debt	2,843,668
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Total Liabilities	3,621,159
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Net Assets:

Unrestricted	353,177
Temporarily Restricted	7,167,470
Total Net Assets	7,520,647

Total Liabilities & Net Assets	\$ 11,141,806
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The notes to the financial statements are an integral part of this statement.

**PRIORITY SYSTEMS, INC.**  
Statement of Activities  
For the Year Ended August 31, 2018

	Unrestricted	Temporarily Restricted	Total
<b>REVENUES</b>			
Local Support:			
5742 Earnings from Temporary Investments	\$ 21,306	-	21,306
5749 Other Revenues from Local Sources	111,304	-	111,304
5751 Food Service Activity	38,466	-	38,466
5759 Student Activities	33,305	-	33,305
Total Local Support	204,381	-	204,381
State Program Revenues:			
5810 Foundation School Program	-	7,688,353	7,688,353
5829 Other State Aid	-	95,735	95,735
Total State Program Revenues	-	7,784,088	7,784,088
Federal Program Revenues:			
ESEA Title I, Part A	-	201,989	201,989
IDEA Part B - Formula	-	118,266	118,266
IDEA Part B - Preschool	-	5,488	5,488
Child Nutrition	-	319,642	319,642
ESEA Title II	-	22,669	22,669
ESEA Title IV	-	10,000	10,000
E-Rates	-	2,285	2,285
Total Federal Program Revenues	-	680,339	680,339
Net Assets Released from Restrictions:			
Restrictions Satisfied by Payments	9,222,277	(9,222,277)	-
Total Revenues	\$ 9,426,658	(757,850)	8,668,808

The notes to the financial statements are an integral part of this statement.

**PRIORITY SYSTEMS, INC.**  
Statement of Activities  
For the Year Ended August 31, 2018

	Unrestricted	Temporarily Restricted	Total
<b>EXPENSES</b>			
Program Services:			
11 Instruction	\$ 4,808,615	-	4,808,615
13 Curriculum Development & Instructional Staff Development	328,216	-	328,216
21 Instructional Leadership	201,173	-	201,173
23 School Leadership	749,775	-	749,775
31 Guidance, Counseling & Evaluation Services	162,601	-	162,601
33 Health Services	4,656	-	4,656
34 Student Transportation	377,248	-	377,248
35 Food Services	471,834	-	471,834
36 Extra Curricular Activities	28,993	-	28,993
Total Program Services	7,133,111	-	7,133,111
Support Services:			
41 General Administration	390,202	-	390,202
51 Plant Maintenance & Operations	1,302,538	-	1,302,538
52 Security & Monitoring Services	13,454	-	13,454
53 Data Processing Services	220,735	-	220,735
61 Community Services	24,901	-	24,901
71 Debt Service	137,336	-	137,336
Total Support Services	2,089,166	-	2,089,166
Total Expenses	9,222,277	-	9,222,277
Change in Net Assets	204,381	(757,850)	(553,469)
Net Assets, Beginning of Year	148,796	7,925,320	8,074,116
Net Assets, End of Year	\$ 353,177	7,167,470	7,520,647

The notes to the financial statements are an integral part of this statement.

**PRIORITY SYSTEMS, INC.**  
Statement of Cash Flows  
For the Year Ended August 31, 2018

Cash Flows from Operating Activities:	
State Program Revenues	\$ 7,733,329
Federal Program Revenues	699,083
Local Revenues	203,786
Payments to Employees	(5,702,189)
Payments to Vendors	(2,653,203)
Net Cash Provided/(Used) by Operating Activities	<u>280,806</u>
Cash Flows from Financing Activities:	
Proceeds from Long-Term Debt	115,800
Principal Payments on Long-Term Debt	(332,759)
Net Cash Provided/(Used) by Financing Activities	<u>(216,959)</u>
Cash Flows from Investing Activities:	
Purchase of Capital Assets	(1,239,274)
Disposal of Capital Assets	520,107
Net Cash Provided/(Used) by Investing Activities	<u>(719,167)</u>
Net Increase/(Decrease) in Cash	(655,320)
Cash at Beginning of Year	<u>2,354,260</u>
Cash at End of Year	<u><u>\$ 1,698,940</u></u>

RECONCILIATION OF CHANGE IN NET ASSETS TO NET CASH  
PROVIDED BY OPERATING ACTIVITIES:

Increase/(Decrease) in Net Assets \$ (553,469)

Adjustments to Reconcile Change in Net Assets to Net Cash  
Provided by Operating Activities:

Depreciation Expense	393,113
(Increase)/Decrease in:	
Due From Federal Agencies	5,817
Due From State	(50,759)
Due From ESC 12	12,927
Receivables	405
Prepays	235,121
Other Assets	(1,000)
Increase/(Decrease) in:	
Accounts Payable	233,011
Accrued Expenses	(26,969)
Payroll Tax and Other Withholdings	32,609
Net Cash Provided by Operating Activities	<u><u>\$ 280,806</u></u>

The notes to the financial statements are an integral part of this statement.

**PRIORITY SYSTEMS, INC.**  
Notes to Financial Statements  
For the Year Ended August 31, 2018

**ORGANIZATION & NATURE OF ACTIVITIES**

Priority Systems, Inc. provides an alternative learning environment for students. The School operates under an open enrollment charter granted by the State of Texas Board of Education. This charter was issued for a period of five years starting October 1998 and is subject to review and renewal periodically. The School's charter was extended until July 31, 2025. The School is part of the public school system of the State of Texas and is therefore entitled to distribution from the State's available school fund. The School does not have the authority to impose ad valorem taxes or to charge tuition. The organization does business as Priority Charter Schools and there is not currently any additional financial activity outside of the charter schools.

The Organization was incorporated in 1998 and has been recognized as an organization exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code.

**SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Basis of Accounting

The basic financial statements of the School were prepared in conformity with accounting principles generally accepted in the United States of America. Encumbrances representing outstanding purchase orders and other commitments for materials or services not yet received are not liabilities as of the reporting date.

Basis of Presentation

In order to comply with accounting principles generally accepted in the United States of America, the School must prepare its external financial statements in accordance with statements issued by the Financial Accounting Standard Board as described in the AICPA Audit and Accounting Guide for not for profit organizations.

The Financial Accounting Standards Board requires classification of the School's net assets and its revenues, expenses, gains, and losses based on the existence or absences of donor-imposed restrictions. It requires that the amounts for each of three classes of net assets - permanently restricted, temporarily restricted, and unrestricted - be displayed in a statement of financial position and that the amount of change in each of those classes of net assets be displayed in a statement of activities.

*Unrestricted* - Net assets that are not subject to donor-imposed stipulations.

*Temporarily Restricted* - Net assets subject to donor-imposed stipulations that may or will be met, either by actions of the School and/or the passage of time. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

*Permanently Restricted* - Net assets required to be maintained in perpetuity with only the income to be used for the School's activities due to donor-imposed restrictions. The School does not have any permanently restricted net assets.

Cash & Cash Equivalents

For financial statement purposes, the School considers all highly liquid investment instruments with an original maturity of three months or less to be cash equivalents. The School, at times, maintains cash in excess of FDIC coverage.

**PRIORITY SYSTEMS, INC.**  
Notes to Financial Statements  
For the Year Ended August 31, 2018

**SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** *(continued)*

Capital Assets

Capital assets, which include buildings and improvements, furniture and equipment, vehicles, and other personal property, are reported in the financial statements. Capital assets are defined by the School as assets with an individual cost of more than \$5,000. Such assets are recorded at historical cost and are depreciated over the estimated useful lives of the assets, which range from three to thirty years, using the straight-line method of depreciation. Expenditures for additions, major renewals and betterments are capitalized, and maintenance and repairs are charged to expense as incurred. Donations of assets are recorded as direct additions to net assets at fair value at the date of donation, which is then treated as cost.

Contributions

Contributions are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and/or nature of any donor restrictions.

Support that is restricted by the donor is reported as an increase in temporarily restricted or permanently restricted net assets in the reporting period in which the support is recognized. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Federal Income Taxes

The School is exempt from Federal income taxes under Section 501(c)(3) of the Internal Revenue Code (the "Code") and has been determined by the Internal Revenue Service not to be a "private foundation" within the meaning of Section 509(a) of the Code.

Compensated Absences

All full year employees earn ten days of local paid vacation per year. Additionally, employees earn five days of state paid personal and sick leave per year. However, unused balances do not accumulate; therefore, there is no liability accrued on the financial statements.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

**TEMPORARILY RESTRICTED NET ASSETS**

The School reports gifts of cash and other assets as temporarily restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are classified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. Donor restricted contributions whose restrictions are met in the same reporting period are reported as unrestricted support.

**PRIORITY SYSTEMS, INC.**  
Notes to Financial Statements  
For the Year Ended August 31, 2018

**TEMPORARILY RESTRICTED NET ASSETS** *(continued)*

The School reports gifts of land, buildings, 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 long those long-lived assets must be maintained, the School reports expiration of donor restrictions when the donated or acquired long-lived assets are placed in service.

Temporarily restricted net assets were released from restrictions by incurring expenses satisfying the following restricted purposes:

State Funded Educational Programs	\$ 8,541,938
Federally Funded Educational Programs	<u>680,339</u>
Total	<u>\$ 9,222,277</u>

Temporarily restricted net assets, as of August 31, 2018, are available for the following purposes:

State Funded Educational Programs	<u>\$ 7,167,470</u>
Total	<u>\$ 7,167,470</u>

**CAPITAL ASSETS**

A summary of changes in capital assets is as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Retirements</u>	<u>Ending Balance</u>
Land	\$ 988,590	-	-	988,590
Buildings & Improvements	7,871,183	556,109	-	8,427,292
Vehicles	563,398	132,849	-	696,247
Furniture & Equipment	553,792	47,409	-	601,201
Construction in Progress	<u>17,200</u>	<u>502,907</u>	<u>(520,107)</u>	<u>-</u>
	<u>9,994,163</u>	<u>1,239,274</u>	<u>(520,107)</u>	<u>10,713,330</u>
Accumulated Depreciation	<u>(1,167,410)</u>	<u>(393,113)</u>	<u>-</u>	<u>(1,560,523)</u>
Net Fixed Assets	<u>\$ 8,826,753</u>	<u>846,161</u>	<u>(520,107)</u>	<u>9,152,807</u>

Current year depreciation was \$393,113.

**PRIORITY SYSTEMS, INC.**  
Notes to Financial Statements  
For the Year Ended August 31, 2018

**LONG TERM DEBT**

Changes in long-term debt are as follows:

	Beginning Balance	Additions	Retirements	Ending Balance	Due Within One Year
Notes Payable:					
ExtraCo Bank - Temple	\$ 368,386	-	(53,730)	314,656	55,844
ExtraCo Bank - Georgetown	528,850	-	(70,650)	458,200	73,538
ExtraCo Bank - Killeen	730,125	-	(48,003)	682,122	49,963
ExtraCo Bank - Cedar Park	1,688,227	-	(64,559)	1,623,668	67,186
Capital Lease:					
Government Capital Corp.	91,000	-	(52,000)	39,000	39,000
Government Capital Corp.	-	115,800	(43,817)	71,983	60,430
Totals	<u>\$ 3,406,588</u>	<u>115,800</u>	<u>(332,759)</u>	<u>3,189,629</u>	<u>345,961</u>

The School purchased a building at 7177 Airport Road, Temple, Texas for the school location, on March 23, 2009. The note was refinanced May 2014 with payments of \$5,622 including interest at 3.95%.

The School purchased a building at 302 Serenada, Georgetown, Texas for the school location, on April 10, 2014. The resultant note of \$745,000 amortizes over 10 years with payments of \$7,546 including interest at 3.95%.

The School purchased a building at 3209 Atkinson Ave, Killeen, Texas for the school location, on September 30, 2014. The resultant note of \$860,000 amortizes over 15 years with payments of \$6,364 including interest at 3.95%.

The School purchased a building at 201 Buttercup Creek Blvd, Cedar Park, Texas for the school location, on April 29, 2015. The resultant note of \$ 1,800,000 amortizes over 20 years with payments of \$10,916 including interest at 3.95%.

The School leased two 71-passenger school buses, from Government Capital Corporation as of January 26, 2017. Quarterly payments of \$14,276 (including interest) began on June 1, 2017 and extend through March 1, 2019. The School has the option to purchase, for an additional fee, beginning June 1, 2018.

The School leased two 72-passenger school buses, from Government Capital Corporation as of December 13, 2017. Quarterly payments of \$15,729 (including interest) began on February 16, 2018 and extend through November 16, 2019.

Debt service requirements, by year, are as follows:

Fiscal Year End	Principal	Interest	Total
2019	345,961	125,155	471,116
2020	267,896	109,172	377,068
2021	267,076	98,294	365,370
2022	277,970	87,400	365,370
2023	289,293	76,077	365,370
2024-2028	926,884	227,655	1,154,539
2029-2033	543,475	111,469	654,944
2034-2036	271,074	12,372	283,446
	<u>\$ 3,189,629</u>	<u>847,594</u>	<u>4,037,223</u>

**PRIORITY SYSTEMS, INC.**  
Notes to Financial Statements  
For the Year Ended August 31, 2018

**LONG TERM DEBT** *(continued)*

The School is required to meet specific debt covenants to comply with their loan agreements, as follows: liquidity requires a minimum cash balance of \$250,000, leverage requires a maximum debt to net worth ratio of 1:1, and cash flow requires a minimum debt service ratio of 1.50. At August 31, 2018, the school maintained a debt to net worth ratio of 0.42:1.00 and a debt service ratio of -0.05. Therefore, the school failed to comply with the debt service ratio. The school also failed to provide an Annual Financial Statement Audit by December 31, 2018 (120 days after the fiscal year). The school is not in compliance with all debt covenants.

**LEASES**

The School entered into a lease agreement for classroom and office space at 2205 FM 3046, Copperas Cove, TX 76522. The lease term was August 15, 2013 through July 15, 2017 at a monthly rental of \$5,462. The lease has now expired and was not renewed. The lease is running month-to-month at the same rental rate.

The School entered into five copier lease agreements as follows:

<u>Date of Lease</u>	<u>Length of Lease</u>	<u>Monthly Payment</u>
08/14/13	60 Months	\$ 568
11/13/13	60 Months	\$ 549
08/04/14	48 Months	\$ 225
10/20/15	60 Months	\$ 469
03/21/17	60 Months	\$ 565

Future minimum lease payments under operating leases as of August 31, 2018 are as follows:

<u>Fiscal Year</u>	<u>Amount Due</u>
2019	\$ 14,049
2020	\$ 12,403
2021	\$ 6,778
2022	\$ 3,954

**DEFINED BENEFIT PENSION PLAN**

Plan Description

The School participates in a cost-sharing multiple-employer defined benefit pension that has a special funding situation. The plan is administered by the Teacher Retirement System of Texas (TRS). TRS's defined benefit pension plan is established and administered in accordance with the Texas Constitution, Article XVI, Section 67 and Texas Government Code, Title 8, Subtitle C. The pension trust fund is a qualified pension trust under Section 401(a) of the Internal Revenue Code. The Texas Legislature establishes benefits and contribution rates within the guidelines of the Texas Constitution. The pension's Board of Trustees does not have the authority to establish or amend benefit terms. There is not a collective-bargaining agreement.

Funding Policy

Under provisions of State law, plan members are required to contribute 7.7% of their annual covered salary and the State of Texas contributes an amount equal to 6.8% of the Schools covered payroll. The Schools employee contributions to the System for the fiscal year ending August 31, 2018 were \$348,944.

**PRIORITY SYSTEMS, INC.**  
Notes to Financial Statements  
For the Year Ended August 31, 2018

**DEFINED BENEFIT PENSION PLAN** *(continued)*

All employees of public, state-supported educational institutions in Texas who are employed for one-half or more of the standard work load and who are not exempted from membership under Texas Government Code, Title 8, Section 822.002 are covered by the system.

Charter Schools are legally separate entities from the State and each other. Assets contributed by one Charter School may be used for the benefit of another Charter School. Unfunded pension obligations get passed along to other plan participants. There is no penalty for leaving the TRS system.

Pension Plan Fiduciary Net Position

Detailed information about the Teacher Retirement System's fiduciary net position is available in a separately-issued Comprehensive Annual Financial Report that includes financial statements and required supplementary information. That report may be obtained on the Internet at <http://www.trs.state.tx.us/about/documents/cafr.pdf#CAFR>; by writing to TRS at 1000 Red River Street, Austin, TX, 78701-2698; or by calling (512) 542-6592.

The information provided in the Notes to the Financial Statements in the 2017 Comprehensive Annual Financial Report for TRS provides the following information regarding the Pension Plan:

Total Plan Assets	\$	146,282,044,842
Accumulated Benefit Obligations	\$	181,752,796,715
Percentage of the Plan that is Funded		80.5%

Benefits Provided

TRS provides service and disability retirement, as well as death and survivor benefits, to eligible employees (and their beneficiaries) of public and higher education in Texas. The pension formula is calculated using 2.3 percent (multiplier) times the average of the five highest annual creditable salaries times years of credited service to arrive at the annual standard annuity except for members who are grandfathered, the three highest annual salaries are used. The normal service retirement is at age 65 with 5 years of credited service or when the sum of the member's age and years of credited service equals 80 or more years. Early retirement is at age 55 with 5 years of service credit or earlier than 55 with 30 years of service credit. There are additional provisions for early retirement if the sum of the member's age and years of service credit total at least 80, but the member is less than age 60 or 62 depending on date of employment, or if the member was grandfathered in under a previous rule. There are no automatic post-employment benefit changes; including automatic COLAs. Ad hoc postemployment benefit changes, including ad hoc COLAs can be granted by the Texas Legislature as noted in the Plan description in (A) above.

Contributions

Contribution requirements are established or amended pursuant to Article 16, section 67 of the Texas Constitution which requires the Texas legislature to establish a member contribution rate of not less than 6% of the member's annual compensation and a state contribution rate of not less than 6% and not more than 10% of the aggregate annual compensation paid to members of the system during the fiscal year. Texas Government Code section 821.006 prohibits benefit improvements, if as a result of the particular action, the time required to amortize TRS' unfunded actuarial liabilities would be increased to a period that exceeds 31 years, or, if the amortization period already exceeds 31 years, the period would be increased by such action.

**PRIORITY SYSTEMS, INC.**  
Notes to Financial Statements  
For the Year Ended August 31, 2018

**DEFINED BENEFIT PENSION PLAN** *(continued)*

Contributions *(continued)*

Employee contribution rates are set in state statute, Texas Government Code 825.402. Senate Bill 1458 of the 83<sup>rd</sup> Texas Legislature amended Texas Government Code 825.402 for member contributions and established employee contribution rates for fiscal years 2014 thru 2017. The 84th Texas Legislature, General Appropriations Act (GAA) established the employer contribution rates for fiscal year 2017.

	2017	2018%
Member	7.7%	7.7%
Non-Employer Contributing Entity (State)	6.8%	6.8%
Employers	6.8%	6.8%

The School's fiscal year contributions to the plan as of August 31, 2018 were \$348,944.

Contributors to the plan include members, employers and the State of Texas as the only non-employer contributing entity. The State is the employer for senior colleges, medical schools and state agencies including TRS. In each respective role, the State contributes to the plan in accordance with state statutes and the General Appropriations Act (GAA).

As the non-employer contributing entity for public education and junior colleges, the State of Texas contributes to the retirement system an amount equal to the current employer contribution rate times the aggregate annual compensation of all participating members of the pension trust fund during that fiscal year reduced by the amounts described below which are paid by the employers. Employers (public school, junior college, other entities or the State of Texas as the employer for senior universities and medical schools) are required to pay the employer contribution rate in the following instances:

- On the portion of the member's salary that exceeds the statutory minimum for members entitled to the statutory minimum under Section 21.402 of the Texas Education Code.
- During a new member's first 90 days of employment.
- When any part or all of an employee's salary is paid by federal funding sources, a privately sponsored source, from non-educational and general, or local funds.

When the employing district is a public junior college or junior college district, the employer shall contribute to the retirement system an amount equal to 50% of the state contribution rate for certain instructional or administrative employees; and 100% of the state contribution rate for all other employees.

In addition to the employer contributions listed above, when employing a retiree of the Teacher Retirement System the employer shall pay both the member contribution and the state contribution as an employment after retirement surcharge.

When a school district or charter school does not contribute to the Federal Old-Age, Survivors and Disability Insurance (OASDI) Program for certain employees, they must contribute 1.5% of the state contribution rate for certain instructional or administrative employees; and 100% of the state contribution rate for all other employees.

**PRIORITY SYSTEMS, INC.**  
Notes to Financial Statements  
For the Year Ended August 31, 2018

**DEFINED BENEFIT PENSION PLAN** *(continued)*

Actuarial Assumptions

The total pension liability in the August 31, 2017 Actuarial valuation was determined using the following actuarial assumptions:

Valuation Date	August 31, 2017
Actuarial Cost Method	Individual Entry Age Normal
Amortization Method	Level Percentage of Payroll, Open
Asset Valuation Method	5 Year Smoothed Market
Discount Rate	8.00%
Long-term expected Investment Rate of Return	8.00%
Salary Increases	3.50% to 9.50%
Payroll Growth Rate	2.50%
Inflation Rate	2.50%

The actuarial methods and assumptions are primarily based on a study of actual experience for the four-year period ending August 31, 2014 and adopted on September 24, 2015.

Discount Rate

The discount rate used to measure the total pension liability was 8.0%. There was no change in the discount rate since the previous year. The projection of cash flows used to determine the discount rate assumed that contributions from plan members and those of the contributing employers and the non-employer contributing entity are made at the statutorily required rates. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all future benefit payments of current plan members. Therefore, the longterm expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability. The long-term rate of return on pension plan investments is 8%. The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimates ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class.

**PRIORITY SYSTEMS, INC.**  
Notes to Financial Statements  
For the Year Ended August 31, 2018

**DEFINED BENEFIT PENSION PLAN** *(continued)*

Discount Rate *(continued)*

These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of geometric real rates of return for each major asset class included in the Systems target asset allocation as of August 31, 2017 are summarized below:

Asset Class	Target Allocation	Real Return Geometric Basis	Long-Term Expected Portfolio Real Rate of Return*
Global Equity			
U.S.	18%	4.6%	1.0%
Non-U.S. Developed	13%	5.1%	0.8%
Emerging Markets	9%	5.9%	0.7%
Directional Hedge Funds	4%	3.2%	0.1%
Private Equity	13%	7.0%	1.1%
Stable Value			
U.S. Treasuries	11%	0.7%	0.1%
Absolute Return	0%	1.8%	0.0%
Stable Value Hedge Funds	4%	3.0%	0.1%
Cash	1%	-0.2%	0.0%
Real Return			
Global Inflation Linked Bonds	3%	0.9%	0.0%
Real Assets	16%	5.1%	1.1%
Energy & Natural Resources	3%	6.6%	0.2%
Commodities	0%	1.2%	0.0%
Risk Parity			
Risk Parity	5%	6.7%	0.3%
Inflation Expectation	-	-	2.2%
Alpha	-	-	1.0%
Total	100%		8.7%

\* The expected Contribution to Returns incorporates the volatility drag resulting from the conversion between Arithmetic and Geometric mean returns.

**COMMITMENTS & CONTINGENCIES**

The School receives funds through state and federal programs that are governed by various statutes and regulations. State program funding is based primarily on student attendance data submitted to the Texas Education Agency and is subject to audit and adjustment. Expenses charged to federal programs are subject to audit and adjustment by the grantor agency. The programs administered by the School have complex compliance requirements, and should state or federal auditors discover areas of non-compliance, charter school funds may be subject to refund if so determined by the Texas Education Agency or the grantor agency.

Litigation

The charter has been named in a lawsuit which is currently awaiting judgement on a motion to dismiss. If the motion is unsuccessful, the charter will seek mediation and a reasonable settlement. Based on demands of the Plaintiff, the charter may be required to pay approximately \$150,000.

**PRIORITY SYSTEMS, INC.**  
Notes to Financial Statements  
For the Year Ended August 31, 2018

**HEALTH CARE COVERAGE**

Employees of the School are covered by a group insurance plan. The School pays the employee's premium and the employee pays the premiums for dependent coverage through payroll deductions. All premiums were paid to licensed insurers.

**CONCENTRATION OF CREDIT RISK**

At August 31, 2018 and throughout the school year, the School's cash in bank accounts was not entirely covered by Federal Deposit Insurance Corporation (FDIC) insurance, but has been covered all year by pledged collateral held by the School's agent bank.

**EVALUATION OF SUBSEQUENT & FUTURE EVENTS**

The School has evaluated subsequent events through January 4, 2019, the date which the financial statements were available to be issued. No significant events have been noted.

## **SUPPLEMENTAL INFORMATION**

**PRIORITY SYSTEMS, INC.**  
Schedule of Expenses  
For the Year Ended August 31, 2018

<b>EXPENSES</b>	<u>2018</u>
6100 Payroll Costs	\$ 5,702,189
6200 Professional and Contracted Services	1,482,370
6300 Supplies and Materials	1,187,056
6400 Other Operating Costs	713,326
6500 Debt	<u>137,336</u>
Total	<u><u>\$ 9,222,277</u></u>

**PRIORITY SYSTEMS, INC.**  
Schedule of Capital Assets  
For the Year Ended August 31, 2018

<u>Description</u>	<u>Ownership Interest</u>		
	<u>Local</u>	<u>State</u>	<u>Federal</u>
1110 Cash	\$ -	1,698,940	-
1510 Land	-	988,590	-
1520 Buildings & Improvements	538,909	7,888,383	-
1539 Furniture & Equipment	180,258	1,024,025	93,165
Total	<u>\$ 719,167</u>	<u>11,599,938</u>	<u>93,165</u>

**PRIORITY SYSTEMS, INC.**  
 Budgetary Comparison Schedule  
 For the Year Ended August 31, 2018

	Budgeted Amounts		Actual Amounts	Variance (Over)/Under Final Budget
	Original	Final		
<b>REVENUE &amp; OTHER SUPPORT:</b>				
Local Support:				
5742 Earnings from Temporary Investments	\$ 5,000	21,306	21,306	-
5749 Other Revenues from Local Sources	75,900	111,304	111,304	-
5751 Food Service Activity	58,500	38,466	38,466	-
5759 Student Activities	53,100	33,305	33,305	-
Total Local Support	<u>192,500</u>	<u>204,381</u>	<u>204,381</u>	<u>-</u>
State Program Revenues:				
5810 Foundation School Program	7,568,326	7,688,353	7,688,353	-
5829 Other State Aid	-	95,735	95,735	-
Total State Program Revenues	<u>7,568,326</u>	<u>7,784,088</u>	<u>7,784,088</u>	<u>-</u>
Federal Program Revenues:				
5920 Federal Program Revenues	292,607	680,339	680,339	-
Total Federal Program Revenues	<u>292,607</u>	<u>680,339</u>	<u>680,339</u>	<u>-</u>
Total Revenues	<u>8,053,433</u>	<u>8,668,808</u>	<u>8,668,808</u>	<u>-</u>
<b>EXPENSES:</b>				
Program Services:				
11 Instruction	4,388,333	4,808,615	4,808,615	-
13 Curriculum Development & Instructional Staff Development	293,816	328,216	328,216	-
21 Instructional Leadership	172,651	201,173	201,173	-
23 School Leadership	744,117	749,775	749,775	-
31 Guidance, Counseling & Evaluation Services	30,497	162,601	162,601	-
33 Health Services	4,750	4,656	4,656	-
34 Student Transportation	305,386	377,248	377,248	-
35 Food Services	461,235	471,834	471,834	-
36 Extracurricular Activities	24,000	28,993	28,993	-
Total Program Services	<u>6,424,785</u>	<u>7,133,111</u>	<u>7,133,111</u>	<u>-</u>
Support Services:				
41 General Administration	385,833	390,202	390,202	-
51 Facilities Maintenance & Operations	805,410	1,302,538	1,302,538	-
52 Security & Monitoring Services	18,175	13,454	13,454	-
53 Data Processing Services	205,678	220,735	220,735	-
61 Community Services	20,210	24,901	24,901	-
71 Debt Service	129,870	137,336	137,336	-
Total Support Services	<u>1,565,176</u>	<u>2,089,166</u>	<u>2,089,166</u>	<u>-</u>
Total Expenses	<u>7,989,961</u>	<u>9,222,277</u>	<u>9,222,277</u>	<u>-</u>
Change in Net Assets	63,472	(553,469)	(553,469)	-
Net Assets, Beginning of Year	<u>8,074,116</u>	<u>8,074,116</u>	<u>8,074,116</u>	<u>-</u>
Net Assets, End of Year	<u>\$ 8,137,588</u>	<u>7,520,647</u>	<u>7,520,647</u>	<u>-</u>

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**COMPLIANCE AND INTERNAL CONTROL**

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**INDEPENDENT AUDITOR'S 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***

Board of Directors  
**PRIORITY SYSTEMS, INC.**  
Morgan's Point, Texas

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 Priority Systems, Inc. (a nonprofit organization), which comprise the statement of financial position as of August 31, 2018, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated January 4, 2019.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Priority Systems, Inc.'s internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the 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 Priority Systems, Inc.'s internal control.

A *deficiency in control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. 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, and therefore, material weaknesses or significant deficiencies may exist that have not been identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Findings and Responses, as items 2018-01 , 2018-02 and 2018-03, that we consider to be significant deficiencies.

### Compliance and Other Matters

As part of obtaining reasonable assurance about whether Priority Systems, Inc.'s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Questioned Costs as items 2018-01, 2018-02 and 2018-03.

### Priority Systems, Inc.'s Response to Findings

Priority Systems, Inc.'s response to the findings identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. Priority Systems, Inc.'s response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

### Purpose of this Report

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

A handwritten signature in black ink that reads "Evans & Knauth, PLLC". The signature is written in a cursive, slightly slanted style.

Evans & Knauth, PLLC  
Frisco, TX  
January 4, 2019

**PRIORITY SYSTEMS, INC.**  
Schedule of Findings and Questioned Costs  
For the Year Ended August 31, 2018

**2018-01**

**Finding**

During the year, the School was not properly reconciling all bank accounts. An audit adjustment was required at year end in order to balance general ledger to the bank.

**Recommendation**

Make sure proper amounts of qualified staff are in place and performing bank reconciliations on a monthly basis for all accounts.

**Management Response**

Staff will take additional trainings on accounting system, bank reconciliation and general ledger features. The reconciliation will be verified by other staff in the business office and consultant to create the checks and balances.

**2018-02**

**Finding**

During the year, the School was not properly reconciling outstanding accounts payable amounts to the general ledger. An audit adjustment was required at year end to property balance accounts payable subsidiary ledger to the general ledger.

**Recommendation**

Make sure proper amounts of qualified staff are in place and performing accounts payable reconciliations on a monthly basis for all accounts.

**Management Response**

The school will hire or allocate additional staff to perform the accounts payable reconciliation. Consultant will review accounts payable general ledger details on a monthly basis as well.

**2018-03**

**Finding**

When vendor invoices are received, they are not entered immediately into the accounting system. They are entered when the bills are paid, thus creating a cash basis system.

**Recommendation**

All vendor invoices must be entered into the accounting system as soon as they are received. This creates the proper tracking and accounting of accounts payable during the year and an accurate record of year end balances.

**Management Response**

The school will hire or allocate additional staff to perform the accounts payable recording timely. Consultant will review accounts payable accrual on a monthly basis as well.