VIRTUAL COMMUNITY SCHOOL OF OHIO
FRANKLIN COUNTY

SINGLE AUDIT

FOR THE FISCAL YEAR ENDED JUNE 30, 2004

Auditor of State
Betty Montgomery

VIRTUAL COMMUNITY SCHOOL OF OHIO
FRANKLIN COUNTY

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INDEPENDENT ACCOUNTANTS' REPORT

Virtual Community School of Ohio
Franklin County
7244 East Main Street
Reynoldsburg, Ohio 43068

To the Board of Trustees:

We have audited the accompanying basic financial statements of the Virtual Community School of Ohio, Franklin County, Ohio, (the VCS), as of and for the year ended June 30, 2004, as listed in the table of contents. These financial statements are the responsibility of the VCS' management. 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 the standards applicable to financial audits contained in the Comptroller General of the United States' *Government Auditing Standards*. Those standards require that we plan and perform the audit to reasonably assure whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Virtual Community School of Ohio, Franklin County, Ohio, as of June 30, 2004, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 3, the VCS restated its 2003 capital assets balance to reflect a change in the capital asset capitalization threshold and include unaccounted for capital assets.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 28, 2005, on our consideration of the VCS' internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. While we did not opine on the internal control over financial reporting or on compliance, that report describes the scope of our testing of internal control over financial reporting and compliance and the results of that testing. That report is an integral part of an audit performed in accordance with *Government Auditing Standards*. You should read it in conjunction with this report in assessing the results of our audit.

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Management's Discussion and Analysis is not a required part of the basic financial statements but is supplementary information the Governmental Accounting Standards Board requires. We have applied certain limited procedures, consisting principally of inquiries of management regarding the methods of measuring and presenting the required supplementary information. However, we did not audit the information and express no opinion on it.

We conducted our audit to opine on the financial statements that collectively comprise the VCS' basic financial statements. The Federal Awards Receipts and Expenditures Schedule is required by U.S. Office of Management and Budget Circular A-133 *Audits of States, Local Governments, and Non-Profit Organizations,* and is not a required part of the basic financial statements. We subjected the Federal Awards Receipts and Expenditures Schedule to the auditing procedures applied in the audit of the basic financial statements. In our opinion, this information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Betty Montgomery

Betty Montgomery
Auditor of State

April 28, 2005

The management's discussion and analysis of the Virtual Community School of Ohio (the VCS) financial performance provides an overall review of the VCS' financial activities for the fiscal year ended June 30, 2004. The intent of this discussion and analysis is to look at the VCS' financial performance as a whole; readers should also review the notes to the basic financial statements and financial statements to enhance their understanding of the VCS' financial performance.

Financial Highlights

Key financial highlights for 2004 are as follows:

- In total, net assets were $237,407 at June 30 2004.

- The VCS had operating revenues of $9,357,724 and operating expenses of $10,096,883 for fiscal year 2004. The VCS also received $652,046 in federal and state grants during fiscal year 2004. Total change in net assets for the fiscal year was a decrease of $82,225.

Overview of the Financial Statements

This annual report consists of a series of financial statements and notes to those statements. These statements are organized so the reader can understand the VCS' financial activities and financial position. The *Statement of Net Assets* and *Statement of Revenues, Expenses and Changes in Net Assets* provide information about the activities of the VCS, including all short-term and long-term financial resources and obligations. Enterprise accounting uses a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities are included in the Statement of Net Assets. The Statement of Net Assets represents the financial position of the VCS. The Statement of Revenues, Expenses, and Changes in Net Assets presents increases (e.g., revenues) and decreases (e.g., expenses) in net total assets. The Statement of Cash Flows reflects how the VCS finances and meets its cash flow needs. Finally, the notes to the basic financial statements provide additional information that is essential to a full understanding of the data provided on the basic financial statements.

Statement of Net Assets, Statement of Revenues, Expenses and Changes in Net Assets and the Statement of Cash Flows

These financials look at all financial transactions and asks the question, How did we do financially during 2004?" The Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Net Assets answer this question. These statements include *all assets, liabilities, revenues and expenses* using the *accrual basis of accounting,* similar to the accounting used by most private-sector companies. This basis of accounting takes into account all of the current year's revenues and expenses regardless of when cash is received or paid.

These two statements report the VCS' *net assets* and changes in those assets. This change in net assets is important because it tells the reader that, for the VCS as a whole, the *financial position* of the VCS has improved or diminished. The causes of this change may be the result of many factors, some financial, some not. These statements can be found on pages 9 and 10 of this report.

The Statement of Cash Flows provides information about how the VCS finances and meets the cash flow needs of its operations. The Statement of Cash Flows can be found on page 11 of this report.

Financial Analysis

The VCS is not required to present government-wide financial statements as the VCS is engaged in only business-type activities. Therefore, no condensed financial information derived from government-wide financial statements is included in the discussion and analysis.

The following tables represent the VCS' condensed financial information derived from the Statement of Net Assets and the Statement of Revenues, Expenses, and Changes in Net Assets. The 2003 amounts have been restated due to changes made to the capital assets, which is detailed in Note 3 and Note 5A to the basic financial statements.

The table below provides a comparison of the VCS' net assets for fiscal years 2004 and 2003.

Net Assets

	2004	2003
Assets		
Current assets	$ 2,975,914	$ 412,739
Non-current assets:		
Security deposit	1,850	1,850
Capital assets, net	671,368	573,766
Total assets	3,649,132	988,355
Liabilities		
Current liabilities	1,660,254	629,281
Long -term liabilities:		
Payable to ODE	1,709,591	-
Compensated absences payable	39,069	39,442
Capital lease obligation	2,811	-
Total liabilities	3,411,725	668,723
Net Assets		
Invested in capital assets, net of related debt	575,053	524,554
Unrestricted	(337,646)	(204,922)
Total net assets	$ 237,407	$ 319,632

Over time, net assets can serve as a useful indicator of a government's financial position. At June 30, 2004, the VCS' net assets totaled $237,407, a decrease of $82,225 from 2003. The liabilities of the VCS increased significantly during the fiscal year due to the liability to the ODE in the amount of $2,209,591, $1,709,591 considered long-term.

Financial Analysis (Continued)

At fiscal year-end, capital assets represented 18% of total assets. Capital assets consisted of copiers and computer equipment. Capital assets, net of related debt, totaled $575,053. Capital assets are used to provide services to the students and are not available for future spending. Current assets increased to $2.975 million from $412,739 in 2003, a 621% increase. This variance is caused by the increase in cash on-hand. Current liabilities increased to $1,660,254, from $629,681, a 164% increase from the prior year. This increase occurred for two reasons: the increase in accrued wages and benefits due to the student enrollment increase and the $500,000, the current portion, owed to the ODE.

The table below provides a comparative analysis of the changes in net assets for fiscal years 2004 and restated 2003.

Change in Net Assets

	2004	2003
Operating Revenues:		
State foundation	$ 9,353,847	$ 5,358,540
Tuition and fees	-	118,598
Other	3,877	18,746
Total operating revenue	9,357,724	5,495,884
Operating Expenses:		
Salaries and wages	1,781,332	1,207,610
Fringe benefits	537,932	326,685
Purchased services	7,198,994	3,673,578
Materials and supplies	200,565	36,204
Depreciation	376,473	206,880
Other	1,587	30,246
Total operating expenses	10,096,883	5,481,203
Non-operating revenues/expenses:		
Federal and state grants	652,046	298,630
Interest revenue	12,089	2,700
Interest and fiscal charges	(7,201)	-
Loss on disposals	-	(27,300)
Total non-operating revenues/expenses	656,934	274,030
Change in net assets	(82,225)	288,711
Net assets at beginning of year (restated)	319,632	30,921
Net assets at end of year	$ 237,407	$ 319,632

The net assets at July 1, 2003 have been restated to reflect a change in the VCS capital asset policy, to reflect a change in the useful lives of computer equipment and to correct for errors and omissions in the amounts reported in the previous year. See Note 3 and Note 5.A. to the basic financial statements for more details.

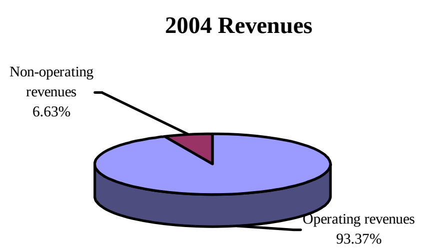
The VCS' operating revenues increased 70%, due to an increase in foundation revenues, which is the direct result of the increased enrollment experienced in 2004. Also, non-operating revenues increased 140%, due to increases in federal grants, which is also attributable to the increase in enrollment. Total expenses increased 84% to provide more services to the increased number of students served. Salaries and fringe benefits cost increased 51% and purchased services increased 96%, from 2003.

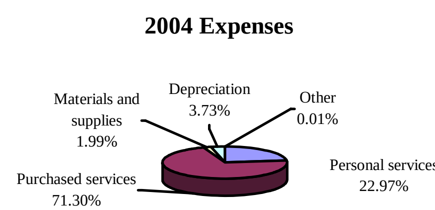
Financial Analysis (Continued)

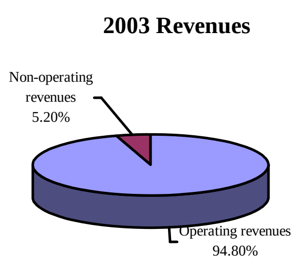
Foundation collections are the primary source of funding received by VCS representing 99.95% of total operating revenues, in 2004 The VCS also received state and federal restricted grant and aid which comprised 98.18% of non-operating revenue. Most aid came from the Ohio Department of Education in the form of Charter School start-up, Title I and Special Education grant funds. These monies were used to finance educational opportunities to those students participating in the VCS' programs.

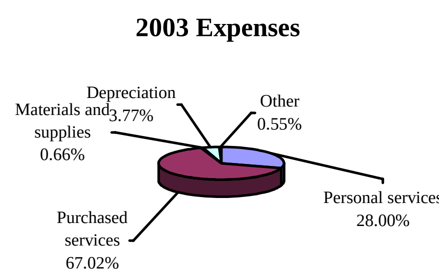
Payroll and fringe benefits totaled $2,319,264 or 23% of total revenues and 23% of the expenses, operating and non-operating, respectively. Purchased services expense includes expenses incurred from fees charged by the management company. The VCS spent 94.97% of its revenues (operating and non-operating) on payroll, fringe benefits, computer equipment and management fees.

The charts below illustrate the revenues and expenses for the School during fiscal 2003 and 2004.









Capital Asset and Debt Administration

Capital Assets

The VCS has $575,053 invested in capital assets, net of depreciation. Acquisitions for FY04 totaled $474,075 and depreciation was $376,473. The majority of the acquisitions were for leased computer and copier equipment. Detailed information regarding capital asset activity is included in the notes to the basic financial statements, (Note 5).

Debt

At June 30, 2004, the VCS had $96,315 in capital lease obligation payable, inclusive of implicit interest. The VCS paid $320,573 in principal on the capital leases during the fiscal year. The VCS issued new capital leases in the amount of $367,676 during fiscal year 2004. Detailed information regarding long-term debt activity is included in the notes to the basic financial statements (Note 9 and 10).

Current Financial Related Activities

Enrollment had declined to approximately 1,127 students at the start of fiscal year 2005; however, due to increased marketing efforts, the VCS' enrollment has increased again to approximately 1,321 students during fiscal year 2005.

Contacting Financial Management

This financial report is designed to provide our clients, citizens, taxpayers and creditors with a general overview of the VCS' finances and to demonstrate the VCS' accountability for the money it receives. If you have questions about this report or need additional financial information, contact Mr. Mitchell Biederman, Treasurer, Virtual Community School of Ohio, 7244 East Main Street, Reynoldsburg, Ohio 43068.

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VIRTUAL COMMUNITY SCHOOL OF OHIO
FRANKLIN COUNTY

STATEMENT OF NET ASSETS
JUNE 30, 2004

Assets:	
Current Assets:	
Cash and cash equivalents. . .	$ 2,899,084
Receivables:	
Intergovernmental	76,830
Total Current Assets	2,975,914
Non-Current Assets:	
Security deposit	1,850
Depreciable capital assets, net	671,368
Total Non-current Assets.	673,218
Total assets	3,649,132
Liabilities:	
Current Liabilities:	
Accounts payable.	336,671
Accrued wages and benefits	508,933
Pension obligation payable.	74,785
Intergovernmental payable	126,221
Current portion of payable to ODE.	500,000
Current portion of capital lease obligation . . .	93,504
Current portion of compensated absences . . .	20,140
Total Current Liabilities	1,660,254
Long-term liabilities:	
Payable to ODE	1,709,591
Compensated absences payable	39,069
Capital lease obligation.	2,811
Total Long-term Liabilities	1,751,471
Total Liabilities	3,411,725
Net Assets:	
Invested in Capital Assets, net of related debt.	575,053
Unrestricted	(337,646)
Total net assets.	$ 237,407

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

VIRTUAL COMMUNITY SCHOOL OF OHIO
FRANKLIN COUNTY

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

Operating revenues:	
State foundation	$ 9,353,847
Other	3,877
Total revenue	9,357,724
Operating expenses:	
Salaries and wages	1,781,332
Fringe benefits	537,932
Purchased services	7,198,994
Materials and supplies	200,565
Other.	1,587
Depreciation	376,473
Total expenses	10,096,883
Operating loss	(739,159)
Non-operating revenues/(expenses):	
Federal and state grants	652,046
Interest income.	12,089
Interest and fiscal charges	(7,201)
Total non-operating revenues/(expenses) . . .	656,934
Change in net assets.	(82,225)
Net assets at beginning of year (restated). .	319,632
Net assets at end of year.	$ 237,407

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

VIRTUAL COMMUNITY SCHOOL OF OHIO
FRANKLIN COUNTY

STATEMENT OF CASH FLOWS
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

Cash flows from operating activities:	
Cash received from foundation	$ 11,507,822
Cash received from other operations.	5,483
Cash payments for salaries and wages	(1,448,546)
Cash payments for fringe benefits	(476,932)
Cash payments for purchased services.	(7,016,520)
Cash payments for materials and supplies	(174,427)
Cash payments for other expenses	(4,097)
Net cash provided by operating activities	2,392,783
Cash flows from noncapital financing activities:	
Federal and state grants.	670,790
Net cash provided by noncapital financing activities	670,790
Cash flows from capital and related financing activities:	
Acquisition of capital assets	(106,399)
Principal retirement.	(369,053)
Interest and fiscal charges.	(7,201)
Net cash used in capital and related financing activities	(482,653)
Cash flows from investing activities:	
Interest received	12,457
Net cash provided by investing activities	12,457
Net increase in cash and cash equivalents	2,593,377
Cash and cash equivalents at beginning of year	305,707
Cash and cash equivalents at end of year.	$ 2,899,084

Reconciliation of operating loss to net cash provided by operating activities:	
Operating loss	$ (739,159)
Adjustments:	
Depreciation.	376,473
Changes in assets and liabilities:	
Decrease in accounts receivable	31,322
Increase in intergovernmental receivable.	(20,232)
Increase in accounts payable	71,824
Increase in accrued wages and benefits	307,291
Increase in compensated absences payable.	19,767
Increase in payable to ODE	61,121
Increase in intergovernmental payable	2,209,591
Increase in pension obligation payable	74,785
Net cash provided by operating activities.	$ 2,392,783

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

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NOTE 1 - DESCRIPTION OF REPORTING ENTITY

The Virtual Community School of Ohio, Franklin County, Ohio (the "VCS") is a nonprofit corporation established pursuant to Ohio Revised Code Chapters 3314 and 1702, to maintain and provide a school exclusively for any educational, literary, scientific and related teaching service, that qualifies as an exempt organization under Section 501(c)(3) of the Internal Revenue Code. Management is not aware of any course of action or series of events that have occurred that might adversely affect its' tax exempt status. The VCS' objective is to deliver a comprehensive educational program of high quality, tied to state and national standards, which can be delivered to students in the K-12 population entirely through distance learning technologies. It is to be operated in cooperation with the public schools to provide an innovative and cost-effective solution to the special problems of disabled students, students removed from school for disciplinary reasons, students needing advanced or specialized courses which are not available locally, and others, including home schooled students who are not currently enrolled in any public school and who are not receiving a meaningful, comprehensive, and standards-based educational program. The VCS, which is part of the State's education program, is nonsectarian in its programs, admissions policies, employment practices, and all other operations. The VCS may acquire facilities as needed and contract for any services necessary for its' operation.

The VCS was approved for operation under a contract with the Reynoldsburg City School District (the "Sponsor") for a period of five academic years commencing after July 1, 2001. The Sponsor is responsible for evaluating the performance of the VCS and has the authority to deny renewal of the contract at its expiration or terminate the contract prior to its expiration.

The VCS operates under the direction of a self-appointed three-member Board of Trustees (the Board), althougth House Bill 364 and Ohio Rev. Code Section 3314.02(E) requires the Board to consist of 5 members. The Board is responsible for carrying out the provisions of the contract, which include, but are not limited to, state-mandated provisions regarding student population, curriculum, academic goals, performance standards, admission standards and qualifications of teachers. The Board controls the VCS' one instructinal/support facility staffed by eleven non-certified staff members and forty-eight certificated full time teaching personnel who provide services to 1,523 students.

The VCS contracts with eSchool Consultants, LLC for a variety of services including management of personnel and human resources, the program of instruction, purchasing strategic planning, public relations, financial reporting, recruiting, compliance issues, budgets, contracts, and equipment and facilities.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements of the VCS have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The VCS also applies Financial Accounting Standards Board (FASB) Statements and Interpretations issued prior to November 30, 1989, provided those pronouncements do not conflict with or contradict GASB pronouncements. The VCS has the option to also apply FASB Statements and Interpretations issued after November 30, 1989, subject to this same limitation. The VCS has elected not to apply these FASB Interpretations. The VCS' significant accounting policies are described below.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

A. Basis of Presentation

The VCS uses enterprise accounting to report on its financial activities. Enterprise accounting focuses on the determination of operating income, changes in net assets, financial position, and cash flows. Enterprise accounting may be used to account for any activity for which a fee is charged to external users for goods or services.

Operating revenues are those revenues that are generated directly from the primary activity of the VCS. Operating expenses are necessary costs incurred to provide the service that is the primary activity of the VCS. All revenues and expenses not meeting this definition are reported as non-operating.

B. Measurement Focus and Basis of Accounting

Enterprise accounting uses a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities are included on the Statement of Net Assets. Operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets. Basis of accounting refers to when revenues and expenses are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made. The accrual basis of accounting is utilized for reporting purposes. Revenues are recognized when they are earned, and expenses are recognized when they are incurred.

C. Budgetary Process

Unlike district public schools located in the State of Ohio, community schools are not required to follow budgetary provisions set forth in Ohio Revised Code Section 5705. Except House Bill 364, which took effect April 8, 2003, added Ohio Rev. Code Section 3314.03 (11) (d), which states that community schools must comply with Ohio Rev. Code Section 5705.391. This section requires each community school to submit to the Ohio Department of Education (ODE) a five year forecast no later than October 31 of each year.

D. Cash

All monies received by the VCS are deposited into a demand deposit account.

E. Capital Assets and Depreciation

All capital assets are capitalized at cost and updated for additions and reductions during the year. Donated capital assets are recorded at their fair market value on the date donated. The VCS has presented a change in capitalization threshold from $500 to $700. The VCS does not have any infrastructure. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend an asset's life are not capitalized, but are expended when incurred.

All capital assets are depreciated. Depreciation is computed using the straight-line method. Computer equipment is depreciated over three years and copiers are depreciated over five years.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

F. Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowings used for the acquisition, construction or improvement of those assets. Net assets are reported as restricted when there are limitations imposed on their use through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

The VCS applies restricted resources first when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

G. Intergovernmental Revenue

The VCS currently participates in the State Foundation Program through the Ohio Department of Education. Revenue from this program is recognized as operating revenue in the accounting period in which all eligibility requirements have been met.

Grants and entitlements are recognized as non-operating revenues in the accounting period in which all eligibility requirements have been met. Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the fiscal year when use is permitted, matching requirements, in which the VCS must provide local resources to be used for a specified purpose, and expenditure requirements, in which the resources are provided to the VCS on a reimbursement basis. Federal and State grants for the fiscal year 2004 received by the VCS were $652,046.

Included in the aforementioned, the VCS received $150,000 for participation in the Federal Charter School Grant Program through the Ohio Department of Education. The VCS was awarded these monies to offset startup costs. Revenue received from this program is recognized as non-operating revenue in the accompanying financial statements. Amounts awarded under the State Foundation program for the 2004 school year, excluding federal and state grants, totaled $9,353,847. The VCS received in total intergovernmental revenues $10,005,893.

H. Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

I. Compensated Absences Policy

Vacation benefits are accrued as a liability as the benefits are earned if the employees' rights to receive compensation are attributable to services already rendered and it is probable that the VCS will compensate the employees for the benefits through paid time off. The VCS records a liability for accumulated unused vacation time when earned by employees. Personal leave benefits are not a liability as it is the policy of the VCS to convert all unused personal leave at school year end to sick leave. Personal leave benefits are not carried over from one year to the next. Sick leave benefits are prescribed by Ohio Rev. Code Section 3319.141. Employees accumulate leave at a rate of 1 ¼ days per month to a maximum of 240 days.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - (Continued)

J. Security Deposit

At June 30, 2004, the VCS had on deposit $1,850 with Taggart Management and Real Estate Services, LLC as security deposit for the faithful performance of all lease terms, covenants, and conditions of the property lease. The deposit is recorded in the Statement of Net Assets as a non-current asset.

NOTE 3 – RESTATEMENT OF CAPITAL ASSETS

The VCS has restated the June 30, 2003 balances of capital assets and accumulated depreciation due to a change in capitalization policy and to correct errors and omissions from prior reporting periods. See Note 5.A. for the restated capital asset balances. The effect of this restatement on net assets at June 30, 2003 is as follows:

Net Assets at June 30, 2003	Restatement	Restated Net Assets at June 30, 2003
$ 658,629	$(338,997)	$ 319,632

NOTE 4 - DEPOSITS

At fiscal year-end, the carrying amount of the VCS' deposits was $2,899,084 and the bank balance was $2,950,686. Of the bank balance $100,000 was covered by federal depository insurance and $2,850,686 was collateralized by the financial institution's public entity deposit pool. The VCS holds no investments at June 30, 2004.

NOTE 5 - CAPITAL ASSETS

A. The capital asset balances have been restated due to changes to the VCS' capital asset policy, which included a change in threshold and change in useful lives for computer equipment, in addition to errors and omissions. The restated capital asset balance is illustrated in the following table:

	Balance at 6/30/03	Adjustments	Restated Balance 6/30/03
Equipment	$ 1,119,643	$ (301,997)	$ 817,646
Accumulated depreciation	(206,880)	(37,000)	(243,880)
Capital assets, net	$ 912,763	$ (338,997)	$ 573,766

NOTE 5 - CAPITAL ASSETS (Continued)

B. Capital asset activity for the fiscal year ended June 30, 2004, was as follows:

	Restated Balance at 7/01/03	Additions	Disposals	Balance at 6/30/04
Equipment	$ 817,646	$ 474,075	$ -	$ 1,291,721
Less: accumulated depreciation	(243,880)	(376,473)	-	(620,353)
Capital assets, net	$ 573,766	$ 97,602	$ -	$ 671,368

NOTE 6 - RECEIVABLES

At June 30, 2004, receivables consisted of intergovernmental revenues which are considered collectible and due within one year and is presented on the Statement of Net Assets in the amount of $76,830.

NOTE 7 - PURCHASED SERVICES

For fiscal year ended June 30, 2004, purchased services expenses were as follows:

Professional technical services	$5,972,176
Property services	153,156
Travel and meetings	23,433
Utilities	894,709
Craft or Trade services	2,472
Communication services	13,447
Postage, Advertising and Shipping	139,601
Total	$7,198,994

NOTE 8 - CAPITALIZED LEASES - LESSEE DISCLOSURE

During fiscal year 2003, the VCS entered into two separate agreements to finance the purchase of additional computer equipment for use in its computer based school. An executed capital lease agreement was made with Falcon Capital, LLC on November 12, 2002. In addition, a promissory note was issued on March 1, 2003 (see Note 10 for details). During fiscal year 2004, the VCS entered into a lease for computer equipment with Fifth Third Bank and a copier lease with GFC Leasing. These leases meet the criteria of a capital lease as defined by FASB Statement No. 13, "Accounting for Leases", which defines a capital lease generally as one which transfers benefits and risks of ownership to the lessee at the conclusion of the lease term.

NOTE 8 - CAPITALIZED LEASES - LESSEE DISCLOSURE (Continued)

All these capital leases were capitalized and are reported in the accompanying financial statements as capital assets, net of accumulated depreciation. The capital assets acquired by capital lease on November 12, 2002 and March 1, 2003 are paid in full as of June 30, 2004. The remaining capital lease, executed in 2004, has a remaining balance at June 30, 2004 of $96, 315. The following is a schedule of the future minimum lease payments required under the capital lease and the present value of the future minimum lease payments as of June 30, 2004:

Year Ending June 30	Amount
2005	$ 94,519
2006	2,976
Total	97,495
Amount representing interest	(1,180)
Present value of lease payments	$ 96,315

Total principal payments paid under the aforementioned capital leases in the 2004 fiscal year totaled $320,573.

NOTE 9 - LONG-TERM OBLIGATIONS

A. Changes in the VCS' long-term obligations during fiscal year 2004 were as follows:

	Balance at 7/1/03	Additions	Reductions	Balance at 06/30/04	Due Within One Year
Capital lease obligation payable	$ 49,212	$ 367,676	$ (320,573)	$ 96,315	$ 93,504
Payable to ODE	-	2,209,591	-	2,209,591	500,000
Compensated absences	39,442	30,929	(11,162)	59,209	20,140
Total governmental activities long-term liabilities	$ 88,654	$ 2,608,196	$ (331,735)	$ 2,365,115	$ 613,644

Payable to ODE: the VCS has recorded a liability for foundation overpayments due to the Ohio Department of Education (ODE). The interest rate is 0% and the repayment will be made over 42 months beginning January, 2005, by pre-determined monthly reductions from future VCS' foundation payments. See Note 9B and 20C. for details regarding the overpayment.

Compensated Absences: Compensated absences will be paid from the fund the employees salaries were paid.

Capital Lease Obligation: See Note 8 for details.

NOTE 9 - LONG-TERM OBLIGATIONS (Continued)

B. Schedule of payments for the amount payable to ODE is as follows:

Year Ending June 30	Amount
2005	$ 500,000
2006	569,864
2007	569,864
2008	569,863
Total payments	$ 2,209,591

NOTE 10 - NOTE PAYABLE

On March 1, 2003, the VCS issued a promissory note in the amount of $96,960, including interest at a five percent (5%) annual rate. The Note was issued to purchase equipment for the VCS and was retired during the fiscal year by the payment of $48,480 in the current fiscal year.

NOTE 11 - OPERATING LEASE-OFFICE SPACE

The VCS entered into an agreement with Robert T. Taggart Company on June 24, 2002, for premises located at 5969 Livingston Avenue, Suite 102, to house its administrative offices. An addendum dated September 19, 2003, modified the original lease term by increasing the monthly lease payments from $1,850 to $2,534 effective November 1, 2003, through the original lease period - October 31, 2005. The modification was caused by adding the rental of Suite 210 at 5969 Livingston Avenue. The VCS has made no leasehold improvements on the leased property.

During fiscal year 2004, the VCS entered into two operating leases for office space in the Channingway office building located at 6100 Channingway Boulevard. The lease of Suites 404 and 505 is a sublease with eSchool Consultants, LLC. The lease of Suite 202 is with Gold Properties, LLC. The VCS also entered into a lease agreement with Blacklick Properties, Ltd. for Suites 102 and 210 at 6715 East Livingston Avenue. This lease ended June 30, 2004, and the lease payments for the property were $551.25 per month.

Lease payments for these offices totaled $32,603, during fiscal year 2004, with $1,291, payable to eSchool Consultants, LLC, at June 30, 2004. Over the term of the leases there are no scheduled rent increases or rent holidays, but the leases are renewable by either party at expiration. The future minimum lease payments are noted in the following table.

Year Ending June 30	Payment
2005	$ 68,624
2006	48,356
Total lease payments	$ 116,980

NOTE 12 - FISCAL AGENT - REYNOLDSBURG CITY SCHOOL DISTRICT

The sponsorship agreement states the Treasurer of Reynoldsburg City Schools; the Sponsor, shall serve as the Treasurer of the VCS. As part of this agreement, the VCS shall compensate the Sponsor two percent (2%) of the per pupil allocation (foundation) paid to the VCS by the State of Ohio.

The Treasurer of the Sponsor shall perform the following functions while serving as the Treasurer of the School.

A. Maintain the financial records of the School in the same manner as are financial records of school districts, pursuant to rules of the Auditor of State.

B. Comply with the policies and procedures regarding internal financial control of the school;

C. Comply with the requirements and procedures for financial audits by the Auditor of the State.

During the fiscal year the VCS accrued cost payable to the Sponsor of $207,322, which $122,681 was paid during the year. At June 30, 2004, $84,641 is owed and included in the accompanying financial statements as a current liability.

NOTE 13 - MANAGEMENT CONSULTING CONTRACT

The VCS entered into a consulting contract with eSchool Consultants, LLC, an Ohio Corporation on March 28, 2002 for fifty-one months. Contract provisions requires eSchool Consultants to design, develop, implement curriculum and instruction programs, recruitment programs, marketing and public relations programs, exemplary interactive computer requirements, staff requirement program, comprehensive grant-seeking programs, a continuous improvement plan and to facilitate and manage the computer/technology lease/purchase agreements. Under the agreement, eSchool consultants shall bill the VCS for services rendered. As services are incurred, theVCS is billed. All billings are due within 30 days.

For the fiscal year 2004 eSchool Consultants billed the VCS $3,327,268, for support and services rendered under the contractual agreement of which $271,731 is payable at June 30, 2004. This amount is included in the accompanying financial statements as a current liability.

NOTE 14 - DEFINED BENEFIT PENSION PLANS

A. School Employees Retirement System

The VCS contributes to the School Employees Retirement System of Ohio (SERS), a cost-sharing, multiple-employer defined benefit pension plan. SERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Authority to establish and amend benefits is provided by State Statute Chapter 3309 of the Ohio Revised Code. SERS issues a publicly available, stand-alone financial report that includes financial statements and required supplementary information. The report may be obtained by writing to the School Employees Retirement System, 300 East Broad Street, Suite 100, Columbus, Ohio 43215-3476, or by calling (614) 222-5853.

NOTE 14 - DEFINED BENEFIT PENSION PLANS (Continued)

A. School Employees Retirement System (Continued)

Plan members are required to contribute 10% of their annual covered salary and the VCS is required to contribute at an actuarially determined rate. The current rate is 14% of annual covered payroll. A portion of the VCS' contribution is used to fund pension obligations with the remainder being used to fund health care benefits. For fiscal year 2004, 9.09% of annual covered salary was the portion used to fund pension obligations. For fiscal year 2003, 8.17% of annual covered salary was the portion used to fund pension obligations. The contribution requirements of plan members and employers are established and may be amended, up to a statutory maximum amount, by the SERS' Retirement Board. The adequacy of the contribution rates is determined annually. The VCS' required contributions to SERS for the fiscal years ended June 30, 2004 and 2003 were $73,319, and $35,813, respectively; 43% has been contributed for fiscal year 2004 and 100% for the fiscal year 2003. $41,460, represents the unpaid contribution for fiscal year 2004.

B. State Teachers Retirement System

The VCS contributes to the State Teachers Retirement System of Ohio (STRS), a cost-sharing, multiple-employer public employee retirement system administered by the State Teachers Retirement Board. STRS provides retirement and disability benefits, annual cost-of-living adjustments, and death and survivor benefits to plan members and beneficiaries. Authority to establish and amend benefits is provided by Chapter 3307 of the Ohio Revised Code. STRS issues a publicly available, stand-alone financial report that includes financial statements and required supplementary information. The report may be obtained by writing to the State Teachers Retirement System, 275 East Broad Street, Columbus, Ohio 43215-3771, or by calling (614) 227-4090.

New members have a choice of three retirement plans, a Defined Benefit (DB) Plan, a Defined Contribution (DC) Plan and a Combined Plan. The DB plan offers an annual retirement allowance based on final average salary times a percentage that varies based on years of service, or an allowance based on member contributions and earned interest matched by STRS Ohio funds times an actuarially determined annuity factor. The DC Plan allows members to place all their member contributions and employer contributions equal to 10.5% of earned compensation into an investment account. Investment decisions are made by the member. A member is eligible to receive a retirement benefit at age 50 and termination of employment. The Combined Plan offers features of both the DC Plan and the DB Plan. In the Combined Plan, member contributions are invested by the member, and employer contributions are used to fund the defined benefit payment at a reduced level from the regular DB Plan. DC and Combined Plan members will transfer to the Defined Benefit Plan during their fifth year of membership unless they permanently select the DC or Combined Plan. Benefits are established by Chapter 3307 of the Ohio Revised Code.

A DB or Combined Plan member with five or more years credited service who becomes disabled may qualify for a disability benefit. Eligible spouses and dependents of these active members who die before retirement may qualify for survivor benefits. Members in the DC Plan who become disabled are entitled only to their account balance. If a member dies before retirement benefits begin, the member's designated beneficiary is entitled to receive the member's account balance.

NOTE 14 - DEFINED BENEFIT PENSION PLANS (Continued)

Plan members are required to contribute 10% of their annual covered salary and the School is required to contribute at an actuarially determined rate. The current VCS rate is 14% of annual covered payroll. A portion of the School's contribution is used to fund pension obligations with the remainder being used to fund health care benefits. For fiscal years 2004 and 2003, 13% of annual covered salary was the portion used to fund pension obligations. Contribution rates are established by the State Teachers Retirement Board, upon recommendation of its consulting actuary, not to exceed statutory maximum rates of 10% for members and 14% for employers. Chapter 3307 of the Ohio Revised Code provides statutory authority for member and employee contributions. The VCS' required contributions to STRS for the fiscal years ended June 30, 2004 and 2003 were $266,292, and $135,252, respectively; 90% has been contributed for fiscal year 2004 and 100% for the fiscal year 2003. $25,844 represents the unpaid contribution for fiscal year 2004. Contributions to the DC and Combined Plans for fiscal 2004 were $1,637 made by the School and $1,940 made by plan members.

C. Social Security System

Effective July 1, 1991, all employees not otherwise covered by SERS or STRS have an option to choose Social Security or SERS/STRS. As of June 30, 2004, two members of the Board of Trustees have elected to contribute to Social Security. The VCS' liability is 6.20 percent of wages paid.

NOTE 15 - POSTEMPLOYMENT BENEFITS

The VCS provides comprehensive health care benefits to retired teachers and their dependents through STRS, and to retired non-certified employees and their dependents through SERS. Benefits include hospitalization, physicians' fees, prescription drugs, and partial reimbursement of monthly Medicare Part B premiums. Benefit provisions and the obligations to contribute are established by STRS and SERS based on authority granted by state statute. Both STRS and SERS are funded on a pay-as-you-go-basis.

The State Teachers Retirement Board has statutory authority over how much, if any, of the health care costs will be absorbed by STRS. Most benefit recipients pay a portion of the health care cost in the form of a monthly premium. By Ohio law, the cost of coverage paid from STRS funds shall be included in the employer contribution rate, currently 14% of covered payroll. For this fiscal year, the State Teachers Retirement Board allocated employer contributions equal to 1% of covered payroll to the Health Care Reserve fund. For the School, this amount equaled $13,162 during fiscal 2004.

STRS pays health care benefits from the Health Care Reserve fund. The balance in the Health Care Reserve fund was $3.1 billion at June 30, 2004. For the fiscal year ended June 30, 2004, net health care costs paid by STRS were $268.739 million and STRS had 111,853 eligible benefit recipients.

For SERS, coverage is made available to service retirees with 10 or more years of qualifying service credit, and disability and survivor benefit recipients. Effective January 1, 2004, all retirees and beneficiaries are required to pay a portion of their health care premium. The portion is based on years of service, Medicare eligibility and retirement status. A safety net is in place for retirees whose household income falls below federal poverty levels. Premiums are reduced by 50% for those who apply.

NOTE 15 - POSTEMPLOYMENT BENEFITS - (Continued)

For this fiscal year, employer contributions to fund health care benefits were 4.91% of covered payroll. In addition, SERS levies a surcharge to fund health care benefits equal to 14% of the difference between a minimum pay and the member's pay, pro-rated for partial service credit. For fiscal year 2004, the minimum pay has been established at $25,400. The surcharge, added to the unallocated portion of the 14% employer contribution rate, provides for maintenance of the asset target level for the health care fund.

The target level for the health care reserve is 150% of annual health care expenses, before premium deduction. Gross expenses for health care at June 30, 2004 were $223.444 million and the target level was $335.2 million. At June 30, 2004, SERS had net assets available for payment of health care benefits of $300.8 million and SERS had approximately 62,000 participants receiving health care benefits. For the VCS, the amount to fund health care benefits, includes a surcharge, equaled to $10,761 during the 2004 fiscal year.

NOTE 16 - SCHOOL FUNDING DECISION

On December 11, 2002, the Ohio Supreme Court issued its latest opinion regarding the state's school funding plan. The decision reaffirmed earlier decisions that Ohio's current school funding plan is unconstitutional.

The Supreme Court relinquished jurisdiction over the case and directed "…the Ohio General Assembly to enact a school funding scheme that is thorough and efficient…". The School is currently unable to determine what effect, if any, this decision will have on its future state funding and its financial operations.

NOTE 17 - OTHER EMPLOYEE BENEFITS

A. Medical, Life, Dental and Vision Insurance Benefits

The VCS provides medical and life insurance benefits through Pacific Life. Dental benefits are through AFLAC and vision through Vision Service Plan (VSP). The VCS offers individual and family health plans. The Board pays 100% of the premium amounts on individual and picks-up 90% of the premium difference between individual and group policies.

Employees who qualify for individual group benefits are offered an option of compensation of $250 per month and those who qualify for family group benefits are offered an option of compensation of $450 per month if they choose to decline the group medical coverage offered.

B. Compensated Absences

Employees accumulate sick leave at a rate of 1.25 days per month. Unused sick leave may accumulate up to 240 days. Accumulated sick leave earned from other governments can be carried over by certifying the unused sick leave balance to the Treasurer. New employees are credited five sick days in advance which is part of the 15 days that can be accumulated for the year.

Vacation is earned by twelve month employees at the rate indicted in their respective employment contracts.

Employees are allowed three personal days per school year. Unused personal leave within a given year is converted to sick leave.

NOTE 18 - RISK MANAGEMENT

A. Property and Liability

The VCS is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The School maintains insurance coverage for rental/theft, general liability and contents liability. The general liability coverage is in the amount of $2,000,000 aggregate.

The VCS has coverage for employee dishonesty, forgery and alternation coverage and computer equipment in the amount of $10,000 for each, per instance.

Settled claims have not exceeded these commercial coverages in any of the past 3 years.

The VCS owns no real estate, but leases facilities located at 5969 E Livingston Ave., Suites 102 and 210, in Columbus, Ohio; and 6100 Channingway Blvd., Suites 202, 404 and 505.

B. Workers' Compensation

The VCS pays the State Workers' Compensation System a premium for employee injury coverage. The premium is calculated by multiplying the monthly gross total payroll by a factor that is calculated by the State.

NOTE 19 - RELATED PARTY TRANSACTIONS

A. Sponsor

As part of the VCS' contractual agreement with the Sponsor, the VCS is required to pay the Sponsor two percent (2%) of the per pupil allocation paid from the State of Ohio for various fiscal services and support. In fiscal year 2004, the VCS paid the Sponsor $122,681 during the year and $84,641 was payable at June 30, 2004.

B. eSchool Consultants, LLC

The president of eSchool Consultants, LLC is Dr. Coletta Musick. The Superintendent of the Virtual Community School of Ohio is Mr. Donnie P. Musick. Dr. Coletta Musick is the wife of Superintendent Mr. Donnie P. Musick. The VCS paid eSchool Consultants, LLC monthly for support and services rendered. During fiscal year 2004, this amount was $3,327,268 and $271,731 payable at June 30, 2004.

During fiscal year 2004, the VCS entered into a sublease agreement with eSchool Consultants, LLC for office space. The location of the office space is 6100 Channingway Boulevard, Suites 404 and 505. The monthly lease payment is $1,291

C. Board Members

Mr. James McCord is a board member of the VCS who also receives fees for providing consulting services. The School paid Mr. James McCord $5,608 in consulting fees during fiscal year 2004. In addition, Mr. McCord's wife, Judy McCord, received $3,000 in consulting fees during fiscal year 2004. On June 24, 2004, the Board approved a contract with Judy McCord to provide consultant services and supervision of the EMIS database for $7,500 ($50 per hour for 150 hours), although the hours are subject to change.

NOTE 20 - CONTINGENCIES

A. Grants

The VCS received financial assistance from federal and state agencies in the form of grants. The expenditure of funds received under these programs generally requires compliance with terms and conditions specified in the grant agreements and is subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become a liability. However in the opinion of management, any such disallowed claims will not have a material adverse effect on the overall financial position of the VCS at June 30, 2004.

B. Litigation Regarding Community Schools in Ohio

A suit was filed in Franklin County Common Pleas Court, on May 14, 2001, alleging that Ohio's Community (i.e., Charter) Schools program violates the state's Constitution and state laws. On April 21, 2003 the court dismissed the counts containing constitutional claims and stayed the other counts pending appeal of the constitutional issues. The plaintiffs appealed to the Court of Appeals, the issues have been briefed, and the case was heard for oral argument on November 18, 2003. On August 24, 2004, the Court of Appeals rendered a decision that community schools are part of the State Public Educational System and this matter was sent to the Ohio Supreme Court. The effect of this suit, if any, on the VCS is not presently determinable.

C. State Foundation Funding

The Ohio Department of Education (ODE) conducts reviews of enrollment data and full-time equivalency (FTE) calculations made. These reviews are conducted to ensure the schools are reporting accurate student enrollment data to the State, upon which state foundation funding is calculated. The VCS was reviewed two times during this year of operations and errors were found in enrollment, withdrawals and attendance. The ODE estimates a total overpayment during fiscal year 2004 was $2,209,591, which will be repaid by the VCS over a period of 42 months by reducing the foundation payments they will receive during fiscal years 2005 through 2008. This is recorded as a long-term liability on the Statement of Net Assets, with the amount due to be repaid during fiscal year 2005 is recorded as current liability.

D. Litigation against the School

The VCS is currently involved in pending litigation. The legal proceedings are not expected to have a material adverse financial impact on the VCS.

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VIRTUAL COMMUNITY SCHOOL OF OHIO
FRANKLIN COUNTY

FEDERAL AWARDS RECEIPTS AND EXPENDITURES SCHEDULE
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

Federal Grantor/ *Pass Through Grantor* Program Title	Pass-Through Entity Number	Federal CFDA Number	Receipts	Disbursements
U.S. DEPARTMENT OF EDUCATION				
The Secretarty's Fund for the Improvement of Education	N/A	84.215F	$ 48,987	$ 48,987
Passed Through Ohio Department of Education:				
Title I Grants to Local Education Agencies	C1-S1-2003	84.010	(26,040)	0
Title I Grants to Local Education Agencies	C1-S1-2004	84.010	316,528	244,231
Total Title I Grants to Local Education Agencies			290,488	244,231
Special Education Grants to States	6B-CM-2003	84.027	75,342	62,653
Special Education Grants to States	6B-SF-2004	84.027	90,126	91,223
Total Special Education Grants to States			165,468	153,876
Safe and Drug-Free Schools and Communities State Grant	DR-S1-2003	84.186	(672)	0
Safe and Drug-Free Schools and Communities State Grant	DR-S1-2004	84.186	1,006	674
Total Safe and Drug-Free Schools and Communities State Grant			334	674
Public Charter Schools	CH-S1-2004	84.282	150,000	146,473
State Grants for Innovative Programs	C2-S1-2003	84.298	(192)	0
State Grants for Innovative Programs	C2-S1-2004	84.298	1,056	235
Total State Grants for Innovative Programs			864	235
Education Technology State Grants	TJ-S1-2003	84.318	(1,013)	0
Education Technology State Grants	TJ-S1-2004	84.318	1,860	0
Total Education Technology State Grants			847	0
Special School Renovation	AT-S4-2002	84.352	2,536	2,536
Improving Teacher Quality State Grant	TR-S1-2003	84.367	(2,112)	0
Improving Teacher Quality State Grant	TR-S1-2004	84.367	4,625	0
Total Improving Teacher Quality State Grant			2,513	0
Total Passed Through Ohio Department of Education			**613,050**	**548,025**
TOTAL U.S. DEPARTMENT OF EDUCATION			**662,037**	**597,012**
TOTAL AWARDS			**$ 662,037**	**$ 597,012**

The accompanying Notes to the Federal Awards Receipts and Expenditures Schedule are an integral part of this schedule.

VIRTUAL COMMUNITY SCHOOL
FRANKLIN COUNTY

NOTES TO THE FEDERAL AWARDS RECEIPTS AND EXPENDITURES SCHEDULE
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

NOTE A - SIGNIFICANT ACCOUNTING POLICIES

The accompanying Federal Awards Receipts and Expenditures Schedule (the Schedule) summarizes activity of the VCS' federal award programs. The Schedule has been prepared on the cash basis of accounting.

NOTE B – TRANSFERS DUE TO ODE ADMINISTRATIVE ACTION

The VCS transferred funds between special cost centers, 2003 to 2004, during fiscal year 2004, to comply with the Ohio Department of Education's (ODE), Continuous Improvement Plan. The following illustrates those transfers by CFDA # and the amount transferred from the 2003 to 2004 program year: CFDA # 84.010 -$26,040; CFDA # 84.186 -$672; CFDA # 84.298 -$192; CFDA # 84.318 -$1,013; and CFDA # 84.367 -$2,112. This was due to the revised Comprehensive Continuous Improvement Plan Strategy (CCIP) as of July, 2002, which is an attempt to promote consistency between fiscal periods, and allow the local agencies to manage one project at a time. The accompanying Schedule reflects these transfers.

Auditor of State
Betty Montgomery

INDEPENDENT ACCOUNTANTS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS REQUIRED BY *GOVERNMENT AUDITING STANDARDS*

Virtual Community School of Ohio
Franklin County
7244 East Main Street
Reynoldsburg, Ohio 43068

To the Board of Trustees:

We have audited the basic financial statements of the Virtual Community School of Ohio, Franklin County, Ohio, (the VCS) as of and for the year ended June 30, 2004, which collectively comprise the VCS' basic financial statements and have issued our report thereon dated April 28, 2005, wherein we noted the VCS restated its 2003 capital asset balance. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the Comptroller General of the United States' *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the VCS' internal control over financial reporting to determine our auditing procedures in order to express our opinion on the financial statements and not to opine on the internal control over financial reporting. Our consideration of the internal control would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts material to the financial statements we audited may occur and not be timely detected by employees when performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider material weaknesses. In a separate letter to the VCS' management dated April 28, 2005, we reported other matters involving internal control over financial reporting which we did not deem reportable conditions.

Compliance and Other Matters

As part of reasonably assuring whether the VCS' financial statements are free of material misstatement, we tested its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could directly and materially affect 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 an opinion. The results of our tests disclosed an instance of noncompliance or other matters that we must report under *Government Auditing Standards* which is described in the accompanying schedule of findings and questioned costs as item 2004-001. In a separate letter to the VCS' management dated April 28, 2005, we reported other matters related to noncompliance we deemed immaterial.

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We intend this report solely for the information and use of the finance committee, management, the Board of Trustees, federal awarding agencies, and pass-through entities. It is not intended for anyone other than these specified parties.

Betty Montgomery

Betty Montgomery
Auditor of State

April 28. 2004

Auditor of State
Betty Montgomery

INDEPENDENT ACCOUNTANTS' REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR FEDERAL PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

Virtual Community School of Ohio
Franklin County
7244 East Main Street
Reynoldsburg, Ohio 43068

To the Board of Trustees:

Compliance

We have audited the compliance of the Virtual Community School of Ohio, Franklin County, Ohio, (the VCS) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133, Compliance Supplement that apply to each of its major federal programs for the year ended June 30, 2004. The summary of auditor's results section of the accompanying schedule of findings and questioned costs identifies the VCS' major federal programs. The VCS' management is responsible for complying with the requirements of laws, regulations, contracts, and grants applicable to each major federal program. Our responsibility is to express an opinion on the VCS' compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to reasonably assure whether noncompliance occurred with the types of compliance requirements referred to above that could directly and materially affect a major federal program. An audit includes examining, on a test basis, evidence about the VCS' compliance with those requirements and performing other procedures we considered necessary in the circumstances. We believe our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the VCS' compliance with those requirements.

In our opinion, the Virtual Community School of Ohio, Franklin County, Ohio, complied, in all material respects, with the requirements referred to above that apply to each of its major federal programs for the year ended June 30, 2004. However, the results of our auditing procedures disclosed an instance of noncompliance with those requirements that OMB Circular A-133 requires us to report, which is described in the accompanying schedule of findings and questioned costs as item 2004-002. In a separate letter to the VCS' management dated April 28, 2005, we reported other matters related to federal noncompliance not requiring inclusion in this report.

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Internal Control Over Compliance

The VCS' management is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the VCS' internal control over compliance with requirements that could directly and materially affect a major federal program to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be timely detected by employees when performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

We intend this report solely for the information and use of the finance committee, management, the Board of Trustees, federal awarding agencies, and pass-through entities. It is not intended for anyone other than these specified parties.

Betty Montgomery

Betty Montgomery
Auditor of State

April 28, 2005

VIRTUAL COMMUNITY SCHOOL OF OHIO
FRANKLIN COUNTY

SCHEDULE OF FINDING AND QUESTIONED COST
OMB CIRCULAR A -133 § .505
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

1. SUMMARY OF AUDITOR'S RESULTS

(d)(1)(i)	**Type of Financial Statement Opinion**	Unqualified
(d)(1)(ii)	**Were there any material control weakness conditions reported at the financial statement level (GAGAS)?**	No
(d)(1)(ii)	**Were there any other reportable control weakness conditions reported at the financial statement level (GAGAS)?**	No
(d)(1)(iii)	**Was there any reported material noncompliance at the financial statement level (GAGAS)?**	Yes
(d)(1)(iv)	**Were there any material internal control weakness conditions reported for major federal programs?**	No
(d)(1)(iv)	**Were there any other reportable internal control weakness conditions reported for major federal programs?**	No
(d)(1)(v)	**Type of Major Programs' Compliance Opinion**	Unqualified
(d)(1)(vi)	**Are there any reportable findings under § .510?**	Yes
(d)(1)(vii)	**Major Programs (list):**	**Title I Grants to Local Education Agencies** – CFDA # 84.010 **Special Education Grants to States** – CFDA # 84.027
(d)(1)(viii)	**Dollar Threshold: Type A\B Programs**	Type A: > $ 300,000 Type B: all others
(d)(1)(ix)	**Low Risk Auditee?**	No

2. FINDINGS RELATED TO THE FINANCIAL STATEMENTS REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS

Finding Number	2004-001

Duplicate Payment for Laptop Computers- Finding for Recovery Repaid Under Audit–

The VCS purchased three laptop computers from Micro Systems in the amount of $3,975, using monies from the Special Education Program Fund, (516.9904). Due to clerical errors, the VCS was billed twice for the same three laptops, resulting in a total payment of $7,950, and an overpayment of $3,975.

**SCHEDULE OF FINDING AND QUESTIONED COST
OMB CIRCULAR A -133 § .505
FOR THE FISCAL YEAR ENDED JUNE 30, 2004
(Continued)**

2. FINDINGS RELATED TO THE FINANCIAL STATEMENTS REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS (Continued)

Finding Number	2004-001

Duplicate Payment for Laptop Computers- Finding for Recovery Repaid Under Audit–

In accordance with the foregoing facts, and pursuant to Ohio Rev. Code Section 117.28, we hereby issue a Finding for Recovery against Daryl Wolfe, owner of Micro Systems, and Mitchell Biederman, VCS Treasurer, jointly and severally, in the amount of three thousand nine hundred and seventy-five dollars, ($3,975), for public monies illegally expended, in favor of the VCS' Special Education Program Fund. (516.9904)

The amount of $3,975 was repaid by Micro Systems on April 5, 2005.

3. FINDING AND QUESTIONED COST FOR FEDERAL AWARDS

Finding Number	**2004-002**
CFDA Title and Number	**Title I Grants to Local Education Agencies, #84.010**
Federal Award Number / Year	**143537-C1S1-2004**
Federal Agency	**U.S. Department of Education**
Pass-Through Agency	**Ohio Department of Education**

Title I – Eligibility- Questioned Cost

34 CFR 74.53(b) states, except as otherwise provided in part (1) and (2) of the same section, financial records, supporting documentation, statistical records, and all other records pertinent to an award shall be retained for a period of three years from the date of submission of the final expenditure report or, awards that are renewed quarterly or annually, from the date of the submission of the quarterly or annual financial report, as authorized by the Secretary.

34 CFR 200.78(a)(1) provides that an Local Education Agency (LEA) must allocate funds under subpart A of this part to school attendance areas and schools, identified as eligible and selected to participate under Section 1113(a) or (b) of the ESEA, in rank order on the basis of the total number of children from low-income families in each area or school.

The VCS submitted its final expenditure report to the Ohio Department of Education, (ODE), the awarding agency, on September 30, 2004 for the Title I 2003-2004 program year. The VCS was required under the aforementioned Sections to retain all financial reports, supporting documents, statistical records and all other records pertinent to the award. The Title I program is renewed each program year.

SCHEDULE OF FINDING AND QUESTIONED COST
OMB CIRCULAR A -133 § .505
FOR THE FISCAL YEAR ENDED JUNE 30, 2004
(Continued)

FINDING AND QUESTIONED COST FOR FEDERAL AWARDS (Continued)

Finding Number	2004-002
CFDA Title and Number	Title I Grants to Local Education Agencies, #84.010
Federal Award Number / Year	143537-C1S1-2004
Federal Agency	U.S. Department of Education
Pass-Through Agency	Ohio Department of Education

Title I – Eligibility- Questioned Cost (Continued)

At VCS, Title I forms are completed and signed by the student's parent or guardian to document the students' poverty measures. [The student's family size, annual income and/or whether the family is receiving public assistance are the "measures" documented on the Title I form and used to assess eligibility] Students who qualify as low income are included, by their personal identification number, in the Federal Low Income Count System (FLICS). Aggregated data from the FLICS is used by the ODE to determine the amount of Title I federal funding the VCS receives, as an allocation for eligible students under 34 CFR 200.78(a)(1). VCS also reports the percent of low income students enrolled in the Building Eligibility section of the Title I grant application. The ODE uses that information to determine the eligibility of the service area for Title I funding. The Title I form is considered supporting documentation for the entries reported in the FLICS system from which funding is based and building eligibility determined. The Title I form is reasonably considered as pertinent to the program regulation and grant agreement, since the Title I form is the documented source of the information contained in the FLICS. Without the Title I form, it is impossible to conclude whether the students for which the VCS received funding are eligible, to assess the accuracy of the building poverty level reported to ODE, or to determine whether the VCS complied with 34 CFR 200.78(a)(1).

Of the Title I forms tested from the 2003-2004 FLICS report, 26 percent did not have Title I forms on file. An additional three percent had a Title I form filed, but were not attested by the signature of the parents or guardians, making the forms incomplete. The VCS received $11,302 in Federal funding for students whose eligibility could not be determined, due to the lack of supporting documentation or otherwise invalid Title I forms. Therefore, a questioned cost is issued in the amount of eleven thousand three hundred and two dollars ($11,302), for those applications which were not on file and not signed by a parent or guardian. With the absence of these Title I forms, it is not possible to determine the eligibility of these students.

All of the students for which properly-completed Title I forms were not on file were students who resided in various juvenile centers throughout the State and were "wards" of the court. Incorrectly, these students were automatically considered low-income students by the VCS.

Additionally, VCS was not able to provide supporting documentation for the percentage of low income students that were reported in the Building Eligibility section of the Title I grant application. VCS reported 54 percent of the enrolled students as being low income; however, AOS re-calculation, from the presented Title I forms, indicated VCS should have reported 38 percent. However, the building eligibility was met, since the percentage re-calculated was above the 35 percent requirement for such building eligibility. VCS funding is not dependent upon the building eligibility but rather on the FLICS. Therefore, no funding adjustment is warranted.

We recommend the VCS maintain the Title I forms to support the poverty measure of the students considered and from which Title I funding is received through the FLICS. We further recommend the VCS maintain on file the documentation that supports the percent of low income students reported in the Building Eligibility section of the Title I grant application.

VIRTUAL COMMUNITY SCHOOL OF OHIO
FRANKLIN COUNTY

SCHEDULE OF PRIOR AUDIT FINDING
FOR THE FISCAL YEAR ENDED JUNE 30, 2004

Finding Number	**Finding Summary**	**Fully Corrected?**	**Not Corrected, Partially Corrected; Significantly Different Corrective Action Taken; or Finding No Longer Valid; *Explain***
2003-001	Lack of capital assets tracking system.	Partially	Partially corrected and included as current year management letter comment.

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VIRTUAL COMMUNITY SCHOOL OF OHIO

FRANKLIN COUNTY

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

CERTIFIED
JULY 5, 2005