

PENNSYLVANIA CYBER CHARTER SCHOOL

FINANCIAL STATEMENTS

FISCAL YEAR ENDED JUNE 30, 2005

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Pennsylvania Cyber Charter School
652 Midland Avenue
Midland, Pennsylvania 15059

We have audited the accompanying financial statements of the governmental activities and each major fund of the Pennsylvania Cyber Charter School, as of and for the fiscal year ended June 30, 2005, which collectively comprise the basic financial statements of the Pennsylvania Cyber Charter School, as listed in the table of contents. These financial statements are the responsibility of the Pennsylvania Cyber Charter School's 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 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 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 the 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 opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of the Pennsylvania Cyber Charter School, as of June 30, 2005, and the respective changes in financial position of those activities and funds and the budgetary comparison for the general fund for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated March 21, 2006 on our consideration of the Pennsylvania Cyber Charter School's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of our audit in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

The management's discussion and analysis on pages 3 through 12 are not required parts of the basic financial statements, but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquires on management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

McVey + Associates LLC

March 21, 2006

PENNSYLVANIA CYBER CHARTER SCHOOL
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD& A)

JUNE 30, 2005

Required Supplementary Information (RSI)

The discussion and analysis of Pennsylvania Cyber Charter School's financial performance provides an overall review of the School's financial activities for the fiscal year ended June 30, 2005. The intent of this discussion and analysis is to look at the School's financial performance as a whole; readers should also review the financial statements and the notes to the financial statements to enhance their understanding of the School's financial performance.

The Management Discussion and Analysis (MD&A) section is an element of the new reporting model adopted by the Governmental Accounting Standards Board (GASB) in their Statement No. 34 – Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments issued in June 1999

FINANCIAL HIGHLIGHTS

During the fiscal year 2004-2005, The Pennsylvania Cyber Charter School experienced a year of significant increases in student enrollment. The increase in enrollment has made it difficult to budget for additional revenues and related expenses. In the budgeting process, the Board of School Directors have balanced the budget with increased enrollment amounts. The revenues related to the increased enrollment resulted in an increase in the School's fund balance.

The School entered into a 20 year lease with the Lincoln Park Performing Arts Center in May, 2005 for administrative and instruction purposes. In accordance with the terms of the lease agreement, the School has elected to prepay the all the lease payments due under the 20 year lease agreement at a discounted rate. Prepaid lease payments as of June 30, 2005 amounted to \$6,000,000.

The School provides certain computer equipment to students enrolled in the program. In September 2004, the School entered into a capital lease obligation in the amount of \$1,542,400 to purchase computer equipment for students enrolling in the program. The School retains the ownership to all computer and education equipment supplied to enrolled students.

- The School's total assets exceeded total liabilities as of June 30, 2005 by \$12,439,479, and consisted of the following:

Invested in Capital Assets, net of related debt	\$ 3,329,568
Reserved for Long-Term Lease Prepayments	<u>9,109,911</u>
Total Net Assets	\$ <u>12,439,479</u>

(Note – The actual net cash balance as of June 30, 2005 amounted to \$11,025)

PENNSYLVANIA CYBER CHARTER SCHOOL
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD& A)

JUNE 30, 2005

USING THE ANNUAL FINANCIAL REPORT

The Annual Financial Report consists of a series of financial statements and notes to those financial statements as well as the Auditor's Report and the Management Discussion and Analysis section. These pages are organized so that the reader can readily understand the operations of Pennsylvania Cyber Charter School as a financial entity. The summary statements are followed by detailed statements that illustrate specific financial activities.

The first two statements are government-wide financial statements – The Statement of Net Assets and the Statement of Activities. These provide specific information about the School's overall financial status.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

There are two government-wide financial statements presented in this report. The first is a Statement of Net Assets, and the second, a Statement of Activities. These government-wide financial statements present, as their name suggests, aggregated information for the overall School; they do not display individual fund or fund types. They do not include activities reported in fiduciary funds since those activities are reported only in the fund financial statements.

Statement of Net Assets

This statement follows a balance sheet format where the difference between assets and liabilities is labeled "net assets" which are displayed in three components called "investment in capital assets, net of related debt", "restricted", or "unrestricted".

Statement of Activities

This statement reports the expenses, net of program revenue, of the government's individual functions, most commonly by function, which groups related activities that are aimed at accomplishing a major service. An additional component included in this statement is the reporting of depreciation expense for capital assets in a function's direct expense if the depreciation is specifically identifiable with the function.

FUND FINANCIAL STATEMENTS

The District will report governmental, proprietary, and fiduciary fund activity as they have in the past. The governmental fund types found in this report consist of the General Fund. The School has no proprietary or fiduciary funds.

PENNSYLVANIA CYBER CHARTER SCHOOL
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD& A)

JUNE 30, 2005

FUND FINANCIAL STATEMENTS

Figure A-1 shows how the required parts of the Financial Section are arranged and relate to on another:

Figure A-1
Required components of the Pennsylvania
Cyber Charter School's
Financial Report

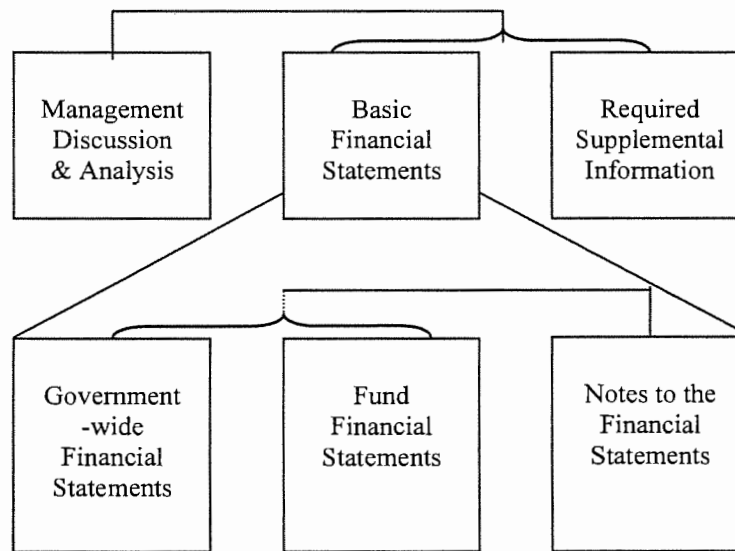


Figure A-2 summarizes the major features of the School's financial statements. Including the portion of the School the cover and the types of information they contain. The remainder of this overview section of management discussion and analysis explains the structure and contents of each of the statements.

PENNSYLVANIA CYBER CHARTER SCHOOL

MANAGEMENT’S DISCUSSION AND ANALYSIS (MD& A)

JUNE 30, 2005

Figure A-2
Major Features of the Pennsylvania Cyber Charter School’s
Government-wide and Fund Financial Statements

	Fund Statements			
	Government-Wide Statements	Governmental Funds	Proprietary Funds	Fiduciary Funds
Scope	Entire School (except fiduciary funds)	The activities of the School that are not proprietary or fiduciary, such as education, administration, and community services	Activities the School operates similar to private business – Food Service	Instances in which the School is the trustee or agent to someone else’s resources – Scholarship Funds
Required Financial Statements	Statement of net assets Statement of activities	Balance sheet Statement of revenues, expenditures, and changes in fund balance	Statement of net assets, Statement of revenues, expenses and changes in net assets; Statement of cash flows	Statement of fiduciary net assets Statement of changes in fiduciary net assets
Accounting basis and measurement focus	Accrual accounting and economic resources focus	Modified accrual accounting and current financial resources focus	Accrual accounting and economic resources focus	Accrual accounting and economic resources focus
Type of asset and liability information	All assets and liabilities, both financial and capital and short- term and long-term	Only assets expected to be used up and liabilities that come due during the year or soon thereafter; no capital assets included	All assets and liabilities, both financial and capital and short-term and long-term	All assets and liabilities, both short- term and long-term
Type of inflow and outflow information	All revenues and expenses during year, regardless of when cash is received or paid	Revenues for which cash is received during or soon after the end of the year; expenditures when goods or services have been received and payment is due during the year or soon thereafter	All revenues and expenses during year, regardless of when cash is received or paid	All revenues and expenses during year, regardless of when cash is received or paid

PENNSYLVANIA CYBER CHARTER SCHOOL
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD& A)

JUNE 30, 2005

OVERVIEW OF FINANCIAL STATEMENTS

Government-wide Statements

The government-wide statements report information about the Pennsylvania Cyber Charter School as a whole using accounting methods similar to those used by private-sector companies. The statement of net assets includes all of the government's assets and liabilities. All of the current year's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two government-wide statements report the School's net assets and how they have changed. Net assets, the difference between the School's assets and liabilities, is one way to measure the School's financial health. Over time, increases or decreases in the School's net assets are an indication of improving or deteriorating financial health, respectively.

To accurately assess the complete financial health of the School, non-financial factors such as changes in enrollment and costs related to enrollment should be considered.

The government-wide financial statement of the School is:

Governmental activities – All of the School's basic services are included here such as instruction, administration, and community service. Tuition charges to the participating students' district and state subsidy grants programs finance most of these activities.

Fund Financial Statements

The School's fund financial statements provide detailed information about the most significant funds, and not the School as a whole. Some of these funds are required by the Commonwealth of Pennsylvania and by bond requirements.

Governmental funds – Most of the School's activities are reported in governmental funds, which focus on the determination of financial position and change in financial position, not on income determination. They are reported using an accounting method called modified accrual accounting, which measures cash and all other financial assets that can readily be converted to cash. The government fund statements provide a detailed short-term view of the District's operations and the services it provides. Governmental fund information helps the reader determine whether there exists enough financial resources to finance future School programs. The relationship (or differences) between governmental activities (reported in the Statement of Net Assets and the Statement of Activities) and governmental funds is reconciled in the financial statements.

PENNSYLVANIA CYBER CHARTER SCHOOL
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD& A)

JUNE 30, 2005

FINANCIAL ANALYSIS OF THE DISTRICT AS A WHOLE

The School's total net assets were \$12,439,479 at June 30, 2005.

Table A-1
 Fiscal Year ended June 30, 2005
 Net Assets

	Governmental Activities <u>2005</u>	Comparative Total <u>2004</u>
Current & other assets	\$ 4,480,665	\$ 5,205,531
Capital & Non-current assets	<u>10,627,963</u>	<u>3,449,831</u>
Total assets	<u>\$ 15,108,628</u>	<u>\$ 8,655,362</u>
Current & other liabilities	\$ 2,002,748	\$ 968,880
Long-term liabilities	<u>666,401</u>	<u>119,653</u>
Total liabilities	<u>\$ 2,669,149</u>	<u>\$ 1,088,533</u>
Net Assets		
Invested in capital assets, Net of related debt	\$ 3,329,568	\$ 1,449,831
Designated	-	-
Reserve for Long-Term Prepayments	<u>9,109,911</u>	<u>6,116,998</u>
Total net assets	<u>\$ 12,439,479</u>	<u>\$ 7,566,829</u>

Most of the School's net assets are invested in receivables due from other governments (amounts represent tuition due from local educational agencies for enrolled students), prepaid lease expense (amounts paid for 20 year lease with the Lincoln Performing Arts Center). The remaining unrestricted net assets are for undesignated amounts.

The results of this year's operations as a whole are reported in the Statement of Activities. All expenses are reported in the first column. Specific charges, grants, revenues, and subsidies that directly related to specific expense categories are represented to determine the final amount of the School's activities that are supported by other general revenues. The largest general revenue is the tuition charged to local educational agencies for enrolled students residing in those educational agencies.

Table A-2 takes the information from the statement and rearranges it so total revenues are presented for the year.

PENNSYLVANIA CYBER CHARTER SCHOOL
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD& A)

JUNE 30, 2005

Table A-2
 Fiscal Year ended June 30, 2005
 Changes in Net Assets

	Governmental Activities <u>2005</u>	Comparative Total <u>2004</u>
Revenues:		
Program revenues:		
Charges for services	\$ 22,531,943	\$ 13,969,012
Operating grants & contributions	78,850	249,360
General revenues:		
Property taxes	-	-
Other taxes	-	-
Grants, subsidies & contributions	484,879	-
Investment Earnings	10,468	-
Other	175,343	-
Total Revenues	<u>\$ 23,281,483</u>	<u>\$ 14,218,372</u>
Expenses:		
Instruction	\$ 9,337,300	\$ 6,969,339
Instructional student support	234,751	60,600
Administrative & financial support	5,461,159	2,266,035
Operation & maintenance of plant	935,022	912,944
Other support services - technology	1,220,178	147,386
Student activities	78,887	27,156
Community services	73,308	169
Interest on long-term debt	118,621	30,642
Unallocated depreciation expense	949,607	437,816
Food service	-	-
Total Expenses	<u>18,408,833</u>	<u>10,852,087</u>
Increase (decrease) in net assets	<u>\$ 4,872,650</u>	<u>\$ 3,366,285</u>

The tables below present the expenses of the Governmental Activities of the School

PENNSYLVANIA CYBER CHARTER SCHOOL

MANAGEMENT'S DISCUSSION AND ANALYSIS (MD& A)

JUNE 30, 2005

Table A-3 shows the School's five largest functions (See Statement of Activities for list of functions) – instructional programs, administrative, operation and maintenance of plant, other support services, student activities community services, as well as each program's net cost (total cost less revenues generated by these activities). This table also shows the net costs offset by the other unrestricted grants, subsidies and contributions to show the remaining financial needs supported by local and other miscellaneous revenues.

Table A-3
Fiscal Year ended June 30, 2004
Governmental Activities

<u>Functions/Programs</u>	Fiscal Year 2005		2004 Comparative	
	<u>Total Cost</u> <u>of Services</u>	<u>Net Cost</u> <u>of Services</u>	<u>Total Cost</u> <u>of Services</u>	<u>Net Cost</u> <u>of Services</u>
Instruction	\$ 9,337,300	\$ (13,239,738)	\$ 6,969,339	\$ (7,143,084)
Administrative	5,461,159	5,425,404	2,266,035	2,191,560
Operation & maintenance	935,022	935,022	912,944	884,470
Other Support Services	1,220,178	1,220,178	147,386	147,386
Unallocated depreciation expense	<u>949,607</u>	<u>949,607</u>	<u>437,816</u>	<u>437,816</u>
Total governmental activities	<u>\$ 17,903,266</u>	<u>\$ (4,709,527)</u>	<u>\$ 10,733,520</u>	<u>\$ (3,481,852)</u>
Total needs from local revenues		<u>NONE</u>		<u>NONE</u>

THE SCHOOL FUNDS

At June 30, 2005, the School governmental funds reported a combined fund balance of \$9,109,911, which is an increase of \$2,390,887. The primary reason for the increase was due to increased student enrollment and related tuition charges.

General Fund Budget

During the fiscal year, the Board of School Directors did not authorize revisions to the original budget to accommodate differences from the original budget to the actual expenditures of the School. A schedule comparing budgeted to actual results is presented in the Statement of Revenues, Expenditures, and Changes in Fund Balance – Budget and Actual – General Fund.

PENNSYLVANIA CYBER CHARTER SCHOOL
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD& A)

JUNE 30, 2005

CAPITAL ASSETS

At June 30, 2004, the District had \$817,895 invested in a broad range of capital assets including furniture, computer and educational equipment, and vehicles.

During the fiscal year ended June 30, 2005, the School purchased an additional \$2,396,728 of furniture and equipment. Depreciation on furniture and equipment for the fiscal year ended June 30, 2005 amounted to \$906,332.

During the fiscal year ended June 30, 2005, the School purchased three (3) buildings for administrative and instructional use. Purchase and related building costs amounted to \$1,731,011. Depreciation for the fiscal year ended June 30, 2005 amounted to \$43,275.

More detailed information regarding the School's capital assets is included in the Notes to the Financial Statements.

DEBT ADMINISTRATION

As of June 30, 2004, the School had a long-term capital lease outstanding in the amount of \$602,026. In September 2004, the School entered into a long-term capital lease for the purchase of computer equipment for students. The proceeds from the lease amounted to \$1,542,400. During the fiscal year ended June 30, 2005, the School repaid \$846,031 in principal on the outstanding capital lease obligations. As of June 30, 2005, the outstanding capital lease obligations amounted to \$1,298,395

More detailed information regarding the School's debt structure is included in the Notes to the Financial Statements.

ECONOMIC FACTORS AND BUDGETS

Given the response to the Cyber School concept on a state-wide basis, the School expects significant growth in student enrollment and tuition charges as well as the related educational and technology costs for the 2005-2006 fiscal year.

The revenue budget for 2004-2005 is \$5,755,371 higher than the original budget for 2003-2004. This represents an increase of 51% in budgeted revenues. In addition, the actual revenue for the 2004-2005 fiscal year is \$9,090,119 higher than the actual revenues for the 2003-2004 fiscal year. This represents an increase of 64% in actual revenues for the 2004-2005 fiscal year.

The expenditure budget instruction, instructional support and non-instructional services for 2004-2005 is \$5,786,262 higher than the original budget for 2003-2004. This represents an increase of 88% in budgeted expenditures. In addition, the actual expenditures for instruction, instructional support and non-instructional services for the 2004-2005 fiscal year is \$9,292,332 higher than the actual expenditures for the 2003-2004 fiscal year. This represents an increase of 89% in actual expenditures for the 2004-2005 fiscal year.

PENNSYLVANIA CYBER CHARTER SCHOOL
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD& A)

JUNE 30, 2005

As of June 30, 2005, the School's General Fund reported an unreserved fund balance of \$9,109,911 that may be used at the District's discretion. This amount equates to 41% of total General Fund expenditures.

CONTACTING THE SCHOOL

Our financial report is designed to provide our citizens, parents, students, investors, and creditors with a general overview of the School's finances, and to show the Board's accountability for the money it receives. If you have questions about this report, or wish to request additional information, please contact Donald Mills, Business Manager, at the Pennsylvania Cyber Charter School, 652 Midland Avenue, Midland, PA 15069.

PENNSYLVANIA CYBER CHARTER SCHOOL

Statement of Net Assets

June 30, 2005

	<u>Governmental Activities</u>
ASSETS	
Current Assets:	
Cash and Cash Equivalents	\$ 11,025
Intergovernmental Receivables	4,172,985
Other Receivables - Midland School District	223,645
Other Receivables	38,010
Other Prepaid Expenses	<u>35,000</u>
Total Current Assets	<u>4,480,665</u>
Noncurrent Assets:	
Buildings and Building Improvements (net of depreciation)	1,687,736
Furniture and Equipment (net of depreciation)	1,133,382
Equipment Acquired Under Capital Lease (net of depreciation)	1,806,845
Long-Term Prepayments	
Prepaid Lease Expense	<u>6,000,000</u>
Total Noncurrent Assets	<u>10,627,963</u>
TOTAL ASSETS	<u>\$ 15,108,628</u>
LIABILITIES	
Current Liabilities:	
Accounts Payable	\$ 1,003,632
Payables - Bank Overdraft	72,897
Current Portion of Capital Lease Obligations	631,994
Credit Line Payable	86,865
Accrued Salaries and Benefits	102,758
Payroll Deductions and Withholdings	<u>104,602</u>
Total Current Liabilities	<u>2,002,748</u>
Noncurrent Liabilities:	
Long-Term Portion of Capital Lease Obligations	<u>666,401</u>
Total Noncurrent Liabilities	<u>666,401</u>
TOTAL LIABILITIES	<u>2,669,149</u>
NET ASSETS	
Invested in Capital Assets, Net of Related Debt	3,329,568
Reserved for Long-term Prepayments	<u>9,109,911</u>
Total Net Assets	<u>12,439,479</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 15,108,628</u>

The accompanying notes are an integral part of these financial statements

PENNSYLVANIA CYBER CHARTER SCHOOL
Statement of Activities
For The Fiscal Year Ended June 30, 2005

Governmental Activities:	Program Revenues			Net (Expense) Revenue and Changes in Net Assets			
	Expenses	Charges For Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business- Type Activities	Total
Instruction	\$ 8,256,544	\$ 19,861,710			\$ 11,605,166		\$ 11,605,166
Regular Instruction	705,667	2,670,233			2,007,661		2,007,661
Special Education	375,089		\$ 43,095		(375,089)		(375,089)
Adult Education Programs							
Support Services							
Pupil Personnel	133,558				(133,558)		(133,558)
Instructional Staff	101,193				(101,193)		(101,193)
Administration	1,259,687				(1,259,687)		(1,259,687)
Pupil Health	86,446		35,755		(50,691)		(50,691)
Business Services	4,115,026				(4,115,026)		(4,115,026)
Operation and Planrt Maintenance Services	935,022				(935,022)		(935,022)
Other Support Services - Technology	1,220,178				(1,220,178)		(1,220,178)
Non-Instructional Services							
Student Activities	78,887				(78,887)		(78,887)
Community Services	73,308				(73,308)		(73,308)
Interest on Long-Term Debt	118,621				(118,621)		(118,621)
Unallocated Depreciation Expense	949,607				(949,607)		(949,607)
Total Governmental Activities	\$18,408,833	\$ 22,531,943	\$ 78,850	\$ -	\$ 4,201,960	\$ -	\$ 4,201,960
General Revenues:							
Taxes:							
Property Taxes, Levied for General Purposes					\$ -		\$ -
Other Taxes Levied for General Purposes					-		-
Grants, Subsidies and Contributions not Restricted					484,879		484,879
Investment Earnings					10,468		10,468
Miscellaneous Income					175,343		175,343
Total General Revenues, Special Items, Extraordinary Items and Transfers					670,690	-	670,690
Change in Net Assets					4,872,650	-	4,872,650
Net Assets - July 1, 2004					7,566,829		7,566,829
Net Assets - June 30, 2005					\$ 12,439,479	\$ -	\$ 12,439,479

The accompanying notes are an integral part of these financial statements

PENNSYLVANIA CYBER CHARTER SCHOOL

Balance Sheet
 Governmental Funds
 June 30, 2005

	<u>General Fund</u>
ASSETS	
Cash and Cash Equivalents	\$ 11,025
Intergovernmental Receivables	4,172,985
Other Receivables - Midland School District	223,645
Other Receivables	38,010
Prepaid Lease Expenses	6,000,000
Other Prepaid Expenses	<u>35,000</u>
 TOTAL ASSETS	 <u>\$ 10,480,665</u>
 LIABILITIES	
Accounts Payable	\$ 1,003,632
Payables - Bank Overdraft	72,897
Credit Line Payable	86,865
Accrued Salaries and Benefits	102,758
Payroll Deductions and Withholdings	<u>104,602</u>
 TOTAL LIABILITIES	 <u>1,370,754</u>
 FUND BALANCES	
Reserved for Long-term Prepayments	<u>9,109,911</u>
 TOTAL FUND BALANCES	 <u>9,109,911</u>
 TOTAL LIABILITIES AND FUND BALANCES	 <u>\$ 10,480,665</u>

The accompanying notes are an integral part of these financial statements

PENNSYLVANIA CYBER CHARTER SCHOOL
 Reconciliation of the Governmental Fund Balance
 Sheet to the Statement of Net Assets
 June 30, 2005

Total Fund Balances - Governmental Funds		\$ 9,109,911
 Amounts reported for governmental activities in the statement of net assets are different because:		
 Capital assets used in governmental activities are not financial resources and therefore are not reported as assets in governmental funds.		
Cost of Property and Equipment	\$ 6,421,959	
Less Accumulated Depreciation	<u>(1,793,996)</u>	4,627,963
 Long-term liabilities are not due and payable in the current period, and therefore are not reported as liabilities in the governmental funds. Long-term liabilities at year-end consist of:		
Capital Lease Obligations		<u>(1,298,395)</u>
 TOTAL NET ASSETS - GOVERNMENTAL ACTIVITIES		 <u>\$ 12,439,479</u>

The accompanying notes are an integral part of these financial statements

PENNSYLVANIA CYBER CHARTER SCHOOL
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
For The Fiscal Year Ended June 30, 2005

	Governmental Funds
REVENUES	
Local Sources:	
Tuition Charges	\$ 22,531,943
Earnings from Investments	10,468
Grants from Intermediate Sources	43,095
Other Revenue	175,343
Total Local Sources	22,760,849
State Revenue and Grants	520,634
TOTAL REVENUES	23,281,483
EXPENDITURES	
Current:	
Instruction	11,162,355
Support Services	8,302,710
Operation of Noninstructional Services	272,268
Refund of Prior Year Receipts	-
Total Current Expenditures	19,737,333
Capital Outlay:	
Facilities Acquisition, Construction and Improvement Services	1,731,011
Total Capital Outlay	1,731,011
Debt Service:	
Principal, Interest and Fiscal Charges	964,652
Total Debt Service	964,652
TOTAL EXPENDITURES	22,432,996
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	848,487
OTHER FINANCING SOURCES (USES)	
Proceeds from Extended Term Financing	1,542,400
Total Other Financing Sources (Uses)	1,542,400
Net Change in Fund Balances	2,390,887
Fund Balance - July 1, 2004	6,719,024
Fund Balance - June 30, 2005	\$ 9,109,911

The accompanying notes are an integral part of these financial statements

PENNSYLVANIA CYBER CHARTER SCHOOL
 Reconciliation Of The Governmental Fund
 Statement Of Revenues, Expenditures And Changes In Fund Balance
 To The Statement Of Activities
 For The Fiscal Year Ended June 30, 2005

Total Net Change in Fund Balances - Governmental Funds \$ 2,390,887

Amounts reported for governmental activities in the statement of activities are diferent because:

Capital outlays are reported in governmental funds as expenditures. However, in the statement of activities, the cost of those assets is capitalized and allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlays exceed depreciation expense in the period.

Capital Outlays	\$ 4,127,739	
Less Depreciation Expense	<u>(949,607)</u>	3,178,132

The governmental funds report proceeds from the issuance of debt as revenue from an other financing source. However, in the government-wide financial statements, the issuance of debt is reported as an increase in liabilities on the statement of net assets. This is the amount of debt proceeds during the fiscal year.

Proceeds from Capital Lease Obligation	(1,542,400)
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The governmental funds report the repayment of long-term debt as an expenditure. However, in the government-wide financial statements, the repayment of long-term debt is treated as a reduction in liabilities on the statement of net assets. This is the amount of principal repaid on the long-term debt during the fiscal year.

Reduction in Capital Lease Obligations	<u>846,031</u>
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Change in Net Assets of Governmental Activities \$ 4,872,650

The accompanying notes are an integral part of these financial statements

PENNSYLVANIA CYBER CHARTER SCHOOL
Statement Of Revenues, Expenditures And Change In Fund Balances -
Budget And Actual
General Fund
For The Fiscal Year Ended June 30, 2005

	Budgeted Amounts		Actual (Budgetary Basis)	Variance With Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Local Sources:				
Tuition Charges			\$ 22,531,943	
Earnings from Investments			10,468	
Grants from Intermediate Sources			43,095	
Other Revenue			<u>175,343</u>	
Total Local Sources	16,776,496	16,776,496	22,760,849	5,984,353
State Revenues and Grants	<u>233,504</u>	<u>233,504</u>	<u>520,634</u>	<u>287,130</u>
TOTAL REVENUES	17,010,000	17,010,000	23,281,483	6,271,483
EXPENDITURES				
Instruction:				
Regular Programs	6,153,675	6,153,675	10,081,599	(3,927,924)
Special Programs	324,591	324,591	705,667	(381,076)
Vocational Programs	458	458	-	458
Community / Junior College Instructional Programs	259,861	259,861	375,089	(115,228)
Support Services:				
Pupil Personnel	43,448	43,448	133,558	(90,110)
Instructional Staff	14,248	14,248	175,190	(160,942)
Administration	738,785	738,785	1,277,784	(538,999)
Pupil Health	64,360	64,360	86,446	(22,086)
Business	3,548,461	3,548,461	4,126,497	(578,036)
Plant Operation and Maintenance	943,297	943,297	955,922	(12,625)
Student Transportation	-	-	-	-
Other Support Services	253,270	253,270	1,547,313	(1,294,043)
Operation of Noninstructional Services:				
Student Activities	26,836	26,836	78,887	(52,051)
Community Services	172	172	193,381	(193,209)
Capital Outlay:				
Facilities Acquisition, Construction and Improvement Services	-	-	1,731,011	(1,731,011)
Debt Service:				
Principal, Interest and Fiscal Charges	<u>4,151,096</u>	<u>4,151,096</u>	<u>964,652</u>	<u>3,186,444</u>
Total Expenditures	<u>16,522,558</u>	<u>16,522,558</u>	<u>22,432,996</u>	<u>(5,910,438)</u>
Excess (Deficiency) of Revenues over Expenditures	<u>\$ 487,442</u>	<u>\$ 487,442</u>	<u>\$ 848,487</u>	<u>\$ 361,045</u>

The accompanying notes are an integral part of these financial statements

PENNSYLVANIA CYBER CHARTER SCHOOL
Statement Of Revenues, Expenditures And Change In Fund Balances -
Budget And Actual
General Fund
For The Fiscal Year Ended June 30, 2005

	Budgeted Amounts		Actual (Budgetary Basis)	Variance With Final Budget Positive (Negative)
	Original	Final		
OTHER FINANCING SOURCES AND (USES)				
Proceeds from Extended Term Financing	\$ -	\$ -	\$ 1,542,400	\$ 1,542,400
Budgetary Reserve	-	-	-	-
Total Other Financing Sources (Uses)	-	-	1,542,400	1,542,400
Net Change in Fund Balances	487,442	487,442	2,390,887	1,903,445
Fund Equity - July 1, 2004	-	-	6,719,024	6,719,024
Fund Equity - June 30, 2005	<u>\$ 487,442</u>	<u>\$ 487,442</u>	<u>\$ 9,109,911</u>	<u>\$ 8,622,469</u>

The accompanying notes are an integral part of these financial statements

PENNSYLVANIA CYBER CHARTER SCHOOL
Notes To Financial Statements
June 30, 2005

NOTE 1 – REPORTING ENTITY

The Pennsylvania Cyber Charter School was formed under the laws of the state of Pennsylvania to provide elementary and secondary education to students through a computer managed learning system designed to meet individual student's needs and styles.

In considering whether there were other entities that should be reported as component units on the School's financial statements, Government Accounting Standards Board Statement No. 14, The Financial Reporting Entity, was used for guidance in determining the activities, organizations and functions of government to be included in the financial statements of the School. The criteria used in determining whether such organizations should be included in the School's financial reporting entity were as follows:

Oversight responsibility
Scope of public service
Other financial relationships

Based upon the above criteria, there are no component units as defined in Government Accounting Standards.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Pennsylvania Cyber Charter School have been prepared in accordance with generally accepted accounting principles as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the authoritative standard-setting body for the establishment of government accounting and financial reporting principles. The Pennsylvania Cyber Charter School also applies Financial Accounting Standards Board (FASB) statements and interpretations issued on or before November 30, 1989, to its governmental and business-type activities provided they do not conflict with or contradict GASB pronouncements. The more significant of these accounting policies are as follows.

BASIS OF PRESENTATION

The School's basic financial statements consist of government-wide statements, including a statement of net assets and a statement of activities, and fund financial statements that provide a more detailed level of financial information.

Government-wide Financial Statements

Government-wide financial statements, the statement of net assets and the statement of activities, report on all of the financial activities of the School except for fiduciary funds. As a general rule, the effect of interfund activity has been eliminated from these financial statements. Governmental activities, which are normally supported by intergovernmental revenues, are reported separately from business-type activities, which rely, to a significant extent on fees and charges for support.

The Statement of Net Assets presents the financial condition of the governmental activities of the School at year-end. The statement of activities presents a comparison between direct expenses and program revenues for each program or function of the School's governmental activities. Direct expenses are those that are specifically associated with a service, program or department and therefore clearly identifiable to a particular function. Program revenues include charges paid by the recipient of the goods and services offered by the program, grants and contributions that are restricted to meeting the operational or capital requirements of a particular program and interest earned on grants that is required to be used to support a particular program. Revenues that are not classified as program revenues are presented as general revenues of the School. The comparison of direct expenses with program revenues identifies the extent to which each governmental function is self-financing or draws from the revenues of the School.

PENNSYLVANIA CYBER CHARTER SCHOOL
Notes To Financial Statements
June 30, 2005

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

MEASUREMENT FOCUS / BASIS OF ACCOUNTING

The Pennsylvania Cyber Charter School uses funds to maintain its financial records during the year. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts. There are three categories of funds: governmental, proprietary, and fiduciary.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Expenditures, other than interest on long-term debt, are recorded when the related fund liability is incurred, if measurable.

The Pennsylvania Cyber Charter School reports the following major governmental funds:

General Fund – The general fund is the general operating fund of the School and accounts for all financial resources except those required to be accounted for in another fund.

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. Net assets (total assets less total liabilities) are used as a practical measure of economic resources and the net operating statement includes all transactions and events that increased or decreased net assets. Depreciation as an expense against current operations and accumulated depreciation is reported on the statement of net assets.

BUDGETARY PROCESS

The Pennsylvania Cyber Charter School passed an appropriated budget for the general fund for the fiscal year ended June 30, 2005 with revenues totaling \$17,010,000 and expenditures totaling \$16,522,558.

The School is required by state law to adopt an annual budget for the General Fund. The budget is presented on the modified accrual basis of accounting which is consistent with generally accepted accounting principles. The following procedures are followed in relation to the adoption of an annual budget reporting of its financial statements.

1. Prior to June 1 of the preceding fiscal year, the School prepares a budget for the next succeeding fiscal year beginning July 1. The operating budget includes proposed expenditures and the means of financing them.
2. A meeting of the School Board is then called for the purpose of adopting the proposed budget, after ten days' public notice of the meeting has been given.
3. Prior to July 1, the budget is legally enacted through passage of a resolution by the School Board.
4. The budget for the general fund must be file with the Office of the Department of Public Instruction within fifteen (15) days after the adoption of the budget.

Once the budget is approved, it can be amended at the function and fund level only by approval of a majority of the members of the School Board. Amendments are presented to the School Board at their regular meetings. Each amendment must have School Board approval. Such amendments are made before the fact and are reflected in the official minutes of the School Board, and are not made after fiscal year-end as dictated by law.

PENNSYLVANIA CYBER CHARTER SCHOOL
Notes To Financial Statements
June 30, 2005

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

BUDGETARY PROCESS (continued)

Each budget is prepared and controlled by the budget coordinator at the revenue and expenditure function/object level. Budgeted amounts are as amended by the School Board. All budget appropriations lapse at year-end. Encumbrances outstanding at year-end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be re-appropriated during the subsequent year.

CASH AND CASH EQUIVALENTS

The School's policy is to maintain cash balances in interest-bearing accounts such as money market or flex funds. The market values of the funds approximate cost. All highly liquid investments of three months or less in duration are reported as cash equivalents.

INVESTMENTS

Investments are reported in accordance with GASB Statement No. 31. Money market investments and short-term interest-earning investment contracts at amortized cost and to report nonparticipating interest-earning investment contracts using a cost-based measure. However, if the fair value of an investment is significantly affected by the impairment of the credit standing of the issuer or by other factors, it is reported at fair value. All other investments are reported at fair value unless a legal contract exists that guarantees a higher value. The term nonparticipating refers to an investment whose value does not fluctuate with market interest rate changes.

INVENTORIES

On the government-wide financial statements inventories are stated at cost using the purchase method, materials and supplies are charged as expenditures when acquired. Inventories at the end of the fiscal year have not been recorded as an asset because the amount of inventory on hand is not considered to be material to the financial statements.

CAPITAL ASSETS

General capital assets generally result from expenditures in the governmental funds. These assets are reported in the government-wide statement of net assets but are not reported in the fund financial statements.

All capital assets are recorded at cost (or estimated historical cost) and updated for additions and retirements during the year. Donated capital assets are recorded at their fair market values at the date of donation. Improvements and non-routine maintenance that adds to the value of the asset or materially extend an asset's life are capitalized.

All reported capital assets, except land and construction in progress, are depreciated. Depreciation is computed straight-line method over the following useful lives:

Site Improvements	5 – 40 years
Buildings and Improvements	10 – 40 years
Furniture and Equipment	3 – 15 years

ACCRUED LIABILITIES AND LONG-TERM DEBT

All payables, accrued liabilities and long-term obligations are reported in the government-wide financial statements. Payables and accrued liabilities paid in full from current financial resources are reported as liabilities in the fund financial statements.

PENNSYLVANIA CYBER CHARTER SCHOOL
Notes To Financial Statements
June 30, 2005

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

NET ASSETS

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt, consists of net assets, net of accumulated depreciation, reduced by the outstanding balances of any long-term obligations used to financial the acquisition, construction or improvement of a capital asset. Net assets are reported as restricted when there are limitations imposed on their use either through enabling adopted by the School or through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

The Pennsylvania Cyber Charter School applies restricted resources first when as expense is incurred for purposes for which both restricted and unrestricted net assets are available.

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 of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

Total Columns on Combined Statements - The total columns presented in the combined financial statements are captioned "Memorandum Only" to indicate that they are presented only to facilitate financial analysis. No consolidating entries or other eliminations were made in the aggregation of the totals; thus, they do not present consolidated information and do not purport to present financial position, results of operations or changes in financial position in conformity with generally accepted accounting principles.

NOTE 3 – CASH AND INVESTMENTS

Pennsylvania statutes provide for investment of governmental funds into certain authorized investment types including U.S. Treasury Bills, other short-term U.S. and Pennsylvania government obligations, and insured or collateralized time deposits and certificates of deposit. The statutes do not prescribe regulations related to demand deposits; however, they do allow the pooling of governmental funds for investment purposes.

The deposit and investment policy of the District adheres to state statute and prudent business practice. Deposits of the Governmental Funds are either maintained in demand deposits and highly liquid money market funds, and are classified as cash or cash equivalents in the financial statements.

Deposits

At June 30, 2005, the deposits of the School can be categorized to indicate the level of risk assumed. Category 1 includes bank balances insured by the FDIC. Category 2 includes bank balances collateralized with securities held by the pledging financial institution's trust department or agent in the School's name. Category 3 includes bank balances collateralized with securities held by the pledging financial institution, or its trust department or agent, but not in the School's name.

	<u>Carrying Amount</u>	<u>Bank Balance</u>	<u>Category 1</u>	<u>Category 2</u>	<u>Category 3</u>
General Fund: Cash	\$ <u>0</u>	\$ <u>414,493</u>	\$ <u>100,000</u>		\$ <u>314,493</u>

PENNSYLVANIA CYBER CHARTER SCHOOL
Notes To Financial Statements
June 30, 2005

NOTE 3 – CASH AND INVESTMENTS (continued)

Cash Equivalents and Investments

The investments of the School as of June 30 2004 have been categorized to indicate the level of risk assumed by the School. Category 1 includes investments that are insured or registered and are held by the School's agent in the School's name. Category 2 includes uninsured and unregistered investments held by the financial institution's trust department or agent in the School's name. Category 3 includes uninsured and unregistered investments by the financial institution's trust department or agent, but not in the School's name.

	Category 1	Category 2	Category 3	Carrying Value	Market Value
General Fund:					
Merrill Lynch		\$ <u>10,410</u>		\$ <u>10,410</u>	\$ <u>10,410</u>

NOTE 4 – PREPAID LEASE EXPENSE

In May 2005 the School entered into a lease agreement with the Lincoln Park Performing Arts Center for the use of space within the Lincoln Performing Arts Center which is currently under construction. The facilities include 88,000 rentable square feet and the school will have exclusive use of a portion of the facilities and first priority used of the space containing classrooms, office space, storage, and performance areas. The remainder of the space in the facilities will be shared by various entities including the School, the Midland Borough School District, the Lincoln Park Performing Arts Center, Beaver County, Buckeye Online School for Success and other community and professional organizations.

The lease offers the option of annual payments of \$947,692 for 20 years totaling \$18,953,840 or \$10,000,000 paid in advance. The School opted for the advance payment option. The \$6,000,000 in prepaid lease expense as of June 30, 2005 was applied toward this advance payment. Total advance payments of \$10,000,000 are due by March 1, 2006. The 20 year lease commences November 1, 2005.

NOTE 5 – PROPERTY, PLANT AND EQUIPMENT

A summary of fixed assets recorded as of June 30, 2005 is as follows:

	<u>Site Improvements</u>	<u>Building & Improvements</u>	<u>Equipment & Fixtures</u>	<u>Accumulated Depreciation</u>
Governmental Activities				
Balance, July 1, 2004			\$1,338,813	\$ (844,389)
Additions / Provision		\$1,731,011	2,396,728	(949,607)
Dispositions				
Balance, June 30, 2005	\$ <u>0</u>	\$ <u>1,731,011</u>	\$ <u>3,735,541</u>	\$ <u>(1,793,996)</u>

PENNSYLVANIA CYBER CHARTER SCHOOL
Notes To Financial Statements
June 30, 2005

NOTE 6 – CREDIT LINE PAYABLE

The School currently has a credit line with Sky Bank for short-term financing needs. The maximum borrowing amount of the credit line is \$2,500,000. The credit line is payable upon demand, and is renewed annually. Interest is charged at the Bank's going prime rate plus two percent, 2.00%. At June 30, 2005 the rate charged amounted to 8.250%. During the fiscal year ended June 30, 2005, the School had repaid \$61,940 on the line. As of June 30, 2005 the outstanding obligation on the credit line in the amount of \$86,865. Due to the short-term nature of the credit line, this obligation has been recorded as a current liability in both the government-wide and the fund financial statements.

NOTE 7 – CAPITAL LEASE OBLIGATIONS

The School currently holds two (2) capital lease obligations with Sky Bank for the acquisition of computer equipment used for educational and instructional purposes. The following is a summarization of lease purchase obligations capitalized and currently being serviced by the general fund of the school.

- Lease #1 Dated September 4, 2003, payable in eight quarterly installments of \$124,865 including interest. Total payments over the term of the lease amount to \$998,911. The market value of the lease equipment was \$955,407 at the beginning of the lease term. Ownership will transfer to the School upon payment of all installments under the lease. As of June 30, 2005 the outstanding balance on the lease amounted to \$123,621.
- Lease #2 Dated September 10, 2004, payable in thirty-six (36) monthly installments of \$45,707.11 including interest. Total Payments over the term of the lease amount to \$1,645,456. The market value of the lease equipment was \$1,542,400 at the beginning of the lease term. Ownership will transfer to the School upon payment of all installments under the lease. As of June 30, 2005 the outstanding balance on the lease amounted to \$1,174,774.

Future minimum lease payments under the lease obligations are as follows:

<u>Fiscal Year</u>	<u>Amount</u>
2005-2006	\$ 631,994
2006-2007	530,154
2007-2008	<u>136,247</u>
	<u>\$1,298,395</u>

NOTE 8 – OPERATING LEASES

The School has entered into the following leases for facilities and equipment.

<u>Lease Description</u>	<u>Lease Date</u>	<u>Expiration Date</u>	<u>Obligation Amount .</u>
Sky Bank – Ford Expedition Wagon Payable in 36 monthly installments of \$1,191.03	Jan 2003	Jan 2006	\$ 8,337

PENNSYLVANIA CYBER CHARTER SCHOOL
Notes To Financial Statements
June 30, 2005

NOTE 8 – OPERATING LEASES (continued)

<u>Lease Description</u>	<u>Lease Date</u>	<u>Expiration Date</u>	<u>Obligation Amount</u>
Sky Bank – Chrysler Mini Van Payable in 36 monthly installments of \$1,444.00	May 2003	May 2006	\$ 15,884
Midland Boro School District - Building (a related party) Payable in monthly installments of \$3,500	June 2005	June 2006	<u>42,000</u>
Total Obligation			<u>\$ 66,221</u>

Future minimum lease payments on the lease obligation are as follows:

<u>Fiscal Year</u>	<u>Amount</u>
2005-2006	\$ <u>66,221</u>

NOTE 9 – RETIREMENT PLAN

All eligible employees of the School participate in the Pennsylvania Public School Employees' Retirement System (PSERS), as established by authority of the Public School Employees' Retirement Code (Act No. 96 of October 2, 1975, as amended). PSERS is a statewide Governmental cost sharing multiple employer retirement system covering all employees of local school districts within the state of Pennsylvania. PSERS provides retirement and disability, legislatively mandated ad hoc cost-of-living adjustments, and healthcare insurance. The Public School Employees' Retirement System issues a publicly available financial report that may be obtained by writing to Public Employees' Retirement System of Pennsylvania, P. O. Box 125, Harrisburg, PA 17108, or at the PSERS website at www.psers.state.pa.us.

Active members who joined the system prior July 22, 1983 contribute at 5.25 percent (membership class TC) or at 6.50 percent (membership class TD) of the member's qualifying compensation. Members who joined the system on or after July 22, 1983 contribute at 6.25 percent (membership class TC) or at 7.50 percent (membership class TD) of the member's qualifying compensation. Members who joined the system after June 30, 2001 contribute 7.50 percent (automatic membership class T-D). For all new hires and for members who elected Class T-D membership, the higher contribution rates began with service rendered on or after January 1, 2002. The Pennsylvania Cyber Charter School is required to contribute at an actuarially determined rate. The rates applied to covered payroll were 4.23 percent at June 30, 2005 and 3.77 percent at June 30, 2004. The 4.23 percent at June 30, 2005 is entirely attributed to actuarial requirement for healthcare insurance premiums.

The Pennsylvania Cyber Charter School's contribution to PSERS for the years ended June 30, 2005 and 2004 amounted to \$197,894 and \$96,248, respectively.

PENNSYLVANIA CYBER CHARTER SCHOOL
Notes To Financial Statements
June 30, 2005

NOTE 10 – COMMITMENTS AND CONTINGENCIES

Litigation

The Pennsylvania Cyber Charter School is involved in two litigation concerning payments from Pennsylvania School Districts to cyber charter schools. The Pennsylvania Cyber Charter School is defending its position as a legitimate charter school under Pennsylvania law. As of the date of these financial statements, none of the cases the School is party to have been settled.

Grant Programs

The School participates in various state and federal grant programs that are governed by various rules and regulations of the grantor agencies. Costs charged to the respective programs are subject to audit and adjustments by the grantor agencies; therefore, to the extent that the School has not complied with the rules and regulations applicable to the grant programs, refunds of and grant funds received may be required and the collectibility of any related receivable may be impaired. In the opinion of the School, there are no significant contingent liabilities relating to compliance with the rules and regulations applicable to the state and federal grants; therefore, no provision has been recorded in the accompanying general-purpose financial statements for such contingencies.

Management Agreement with RODIS, LLC

On June 30, 2004 the School entered into a management agreement with RODIS, LLC. Under the terms of this agreement, RODIS will provide management, administrative, consulting and other services required by the School to conduct business. In return for these services, the School will pay RODIS, LLC an annual management fee equal to 14% of the revenue received by the School for educational services provided. In addition, the School will reimburse RODIS for all costs incurred in providing its services under this agreement. On March 6, 2005, the School exercised its option to terminate the management agreement with RODIS for cause. Total payments made to RODIS for the year ended June 30, 2005 amounted to \$242,833. RODIS has filed lawsuits against naming the School and its Chief Administrative Officer relative to the termination of the management agreement.

NOTE 11 – RELATED PARTY TRANSACTIONS

Midland Borough School District

1. The Chief Administrative Officer of the Pennsylvania Cyber Charter School is also the Superintendent of the Midland Borough School District. The Chief Administrative Officer of the Pennsylvania Cyber Charter School is compensated for services rendered to the School. The School reimburses the Midland Borough School District for its share the Chief Administrative Officer's salary and related benefit costs. Allocation between the Pennsylvania Cyber Charter School and the Midland Borough School District is based on the enrollment. During the fiscal year ended June 30, 2005, the Pennsylvania Cyber Charter School owed the Midland Borough School District \$92,837 in payroll and related benefits costs.
2. During the fiscal years ended June 30, 2005, 2004 and 2003, the Pennsylvania Cyber Charter School provided psychological, principal and technology services to the Midland Borough School District. The School failed to bill the Midland Borough School District for services rendered in the fiscal years ended June 30, 2004 and 2003. In September 2005 the School caught this oversight and billed the Midland School District \$214,482 for payroll and related benefits costs.

PENNSYLVANIA CYBER CHARTER SCHOOL
Notes To Financial Statements
June 30, 2005

NOTE 11 – RELATED PARTY TRANSACTIONS (continued)

Midland Borough School District

- 3 The School currently leases a portion of its facilities from the Midland Borough School District. The lease is payable in monthly installments of \$3,500. Lease expense for the fiscal year amounted to \$42,000.

The following is a summary of the financial transactions between the Pennsylvania Cyber Charter School and the Midland Borough School District.

Due from Midland Borough School District at June 30, 2004	
– Excess lease payments during the fiscal years ended June 30, 2004 and 2003	\$ 54,000
Excess lease payments made during the fiscal year Ended June 30, 1005	48,000
Payroll and related benefit costs for psychological, Principal and technology services	214,482
Chief Administrative Officer salary and related Benefit costs due to Midland Borough School District	<u>(92,837)</u>
Due from Midland Borough School District at June 30, 2005	\$ <u>223,645</u>

Lincoln Park Performing Arts Center

1. In May 2005 the School entered into a lease agreement with the Lincoln Park Performing Arts Center for the use of space within the Lincoln Performing Arts Center which is currently under construction. The facilities include 88,000 rentable square feet and the school will have exclusive use of a portion of the facilities and first priority used of the space containing classrooms, office space, storage, and performance areas. The remainder of the space in the facilities will be shared by various entities including the School, the Midland Borough School District, the Lincoln Park Performing Arts Center, and other community and professional organizations.

The lease offers the option of annual payments of \$947,692 for 20 years totaling \$18,953,840 or \$10,000,000 paid in advance. The School opted for the advance payment option. The \$6,000,000 in prepaid lease expense as of June 30, 2005 was applied toward this advance payment. Total advance payments of \$10,000,000 are due by March 1, 2006. The 20 year lease commences November 1, 2005.

2. The School has contracted with an individual to provide consulting services regarding the acquisition, developing and financing of various properties in the Borough of Midland and the surrounding areas, not including the development of Lincoln Park Performing Arts Center. Additional services include assisting the School in structuring agreements and leases with non-profit entities and working with county and state governments to secure funding for each of the various projects. This individual is a principal of the firm that is developing the Lincoln Park Center for Performing Arts. During the fiscal years ended June 30, 2005 and 2004, the School paid \$140,000 and \$120,000, respectively.

NOTE 12 – BANK OVERDRAFT

As of June 30, 2005, the School had disbursed \$72,897 in funds in excess of available bank account and savings account reserves. This overdraft has been reported as a current liability in the government-wide and fund financial statements.

PENNSYLVANIA CYBER CHARTER SCHOOL

OTHER FINANCIAL INFORMATION

FISCAL YEAR ENDED JUNE 30, 2005

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

To The Board of Directors
Pennsylvania Cyber Charter School
652 Midland Avenue
Midland, Pennsylvania 15059

We have audited the financial statements of the governmental activities, and each major fund of the Pennsylvania Cyber Charter School as of and for the year ended June 30, 2005, which collective comprise the Pennsylvania Cyber Charter School's basic financial statements, and have issued our report thereon dated March 21, 2006. 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 Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Pennsylvania Cyber Charter School's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over the financial reporting that, in our judgment, could adversely affect the Pennsylvania Cyber Charter School's ability to record, process, summarize and report financial data consistent with management's assertions in the financial statements. Reportable conditions are described in the accompanying schedule of findings and questioned costs as item 05-1.

A material weakness is a 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 that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe the reportable condition noted above is not a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Pennsylvania Cyber Charter School's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, 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 no instances of noncompliance that are required to be reported under Government Auditing Standards.

We also noted certain additional matters that we reported to management of the Pennsylvania Cyber Charter School in a separate letter dated March 21, 2006.

This report is intended solely for the use of management of the Pennsylvania Cyber Charter School, others within the organization, and federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

McVey + Associates LLC

March 21, 2006

PENNSYLVANIA CYBER CHARTER SCHOOL
Schedule of Findings and Questioned Costs
Year Ended June 30, 2005

Financial Statement Finding

05-1

Criteria – Management of the School is responsible for establishing and maintaining a system of internal controls over financial reporting to provide assurance that assets are properly safeguarded against loss from unauthorized use or disposition, financial transactions are properly recorded and supported by adequate documentation, and fair presentation of financial information.

Condition – During our audit we noted the absence of written procedures for the proper review and reconciliation of the monthly account balances. Certain account balances were not properly reviewed and reconciled to the underlying journals and supporting documentation.

Effect of Condition – Documentation supporting certain transactions was not present or readily available for review, and tuition revenue and certain receivable accounts required reconciliation and adjustment in amounts that were significant to the financial statements when the supporting documentation was located.

Cause of Condition – The School did not have written review and reconciliation procedures of the monthly financial transactions that allowed for the proper documenting, recording and reporting of financial activity.

Recommendation – We recommend the School establish and implement written policies and procedures for reviewing and reconciling monthly accounting activity to assure that assets are properly safeguarded against loss from unauthorized use or misappropriation, supported by documentation, properly recorded in the financial reporting system.

We noted during our audit, and subsequent to the financial statement date, that the School had contracted with an outside firm to provide accounting and consulting services to provide adequate accounting of financial activity, and assist in the review, reconciliation of financial activity and the establishment of accounting procedure policies.

Response – The School is in the process writing and implementing board approved accounting policies and procedures for reviewing and reconciling monthly accounting activity to assure that assets are properly safeguarded against loss or misappropriation, supported by documentation, properly recorded in the financial reporting system. The Business Office and outside consulting firm anticipate presenting for Board approval, the written accounting policies and procedures at the May 2006 Board meeting. The Business Office and outside consulting firm will review each month of the current fiscal year according to the new accounting policies prior to June 30, 2006.

To The Board of Directors
Pennsylvania Cyber Charter School
652 Midland Avenue
Midland, Pennsylvania 15059

We have audited the financial statements of the Pennsylvania Cyber Charter School for the year ended June 30, 2005. As part of our audit we made a study and evaluation of the School's system of internal accounting control to the extent we considered necessary to evaluate the system as required by generally accepted auditing standards. Under those standards, the purpose of such evaluation is to establish a basis for reliance on the system of internal accounting control to determine the nature, timing and extent of other auditing procedures that are necessary for expressing an opinion on the general-purpose financial statements and to assist the auditors in planning and performing the audit of the financial statements.

The objective of internal accounting control is to provide reasonable, but not absolute, assurance as to the safeguarding of assets against loss from unauthorized use or disposition, and the reliability of financial records for preparing financial statements and maintaining accountability for assets. The concept of reasonable assurance recognizes that the cost of a system of internal accounting control should not exceed the benefits derived and also recognizes that the evaluation of these factors necessarily requires estimates and judgments by management.

There are inherent limitations that should be recognized in considering the potential effectiveness of any system of internal accounting control. In the performance of most control procedures, errors can result from misunderstanding of instructions, mistakes of judgments, carelessness or other personal factors. Control procedures whose effectiveness depends upon the segregation of duties can be circumvented by collusion. Similarly, control procedures can be circumvented intentionally by management either with respect to the execution and recording of transactions or with respect to the estimates and judgments required in the preparation of financial statements. Further, projection of any evaluation of internal accounting control to future periods is subject to the risk that the procedures may become inadequate because changes in conditions that the degree of compliance with the procedures may deteriorate.

Our audit of the general-purpose financial statements made in accordance with generally accepted auditing standards, including the study and evaluation of the School's internal accounting control for the year ended June 30, 2003 that was made for the purpose set forth in the first paragraph of this report, would not necessarily disclose all weaknesses in the system because it was based on selective tests of accounting records and data. However, such study and evaluation disclosed the following.

SEGREGATION OF DUTIES

The School has limited staff responsible for or with access to receipts, check writing, bank reconciliation, account coding, and general ledger posting.

Due to limited staff, segregation of the above duties is not practical, if not impossible. The responsibility of management is greatly increased because the Board must rely on their knowledge of the everyday operations to discover any material changes in the School's financial position. Management should take a greater role in the review and approval of accounting transactions and financial reports. All material changes in monthly reports and/or accounting transactions and data should be thoroughly investigated.

RELATED PARTY TRANSACTIONS

During the audit, it was noted the Pennsylvania Cyber Charter School engaged in several related party transactions with the Midland Borough School District, and the Lincoln Park Performing Arts Center. These transactions were considered to be related party transactions due to the involvement of School Administration and members of the School Board are also administrators and board members of the Midland Borough School District and the Lincoln Park Performing Arts Center.

The School needs to establish policy to define the criteria and documentation requirement for related party transactions to ensure that related party transactions are properly recorded, and that the transactions are consummated on terms equivalent to those that prevail in an "arm's-length" transaction.

POLICIES AND PROCEDURES

We noted that the School continues to grow rapidly and employees continue to be added due to this growth. There are currently no formally established and documented policies and procedures for the finance department. In the absence formalized policies and procedures, the transition of duties to new personnel and the consistency of procedures can be hindered. New personnel are not able to adequately understand transactions performed by previous personnel. The School needs to establish written policies and implement written procedures governing school finances for the following:

1. Job descriptions and responsibilities
2. Purchasing, budgetary accounting and investing
3. Supervision, review and reconciliation of accounting activity
4. Proper approval of transactions
5. Maintenance of documentation supporting the underlying transactions
6. Proper coding of transactions
7. Proper handling of grant programs
8. Employee expense reimbursements

As part of this process, the policies and procedures should clearly outline the job responsibility of each employee or class of employees. In addition, relevant policies and procedures as well as job responsibilities should be disseminated to all applicable employees.

CODING OF TRANSACTIONS

Transactions should be carefully coded to the appropriate general ledger accounts to ensure proper classification. Personnel responsible for coding should be familiar with the School chart of accounts, and supervisory review of the coding should take place to ensure that transactions are coded in an accurate and consistent manner.

CREDIT CARDS

Policies and procedures need to be established that requires complete and accurate documentation of all expenses charged on School owned credit cards. Policy should discourage the charging of personal expenses and provide for the reimbursement of any undocumented or personal expense charged to the School's credit card.

Proper review of credit card charges should be made to ensure adherence with policy. All credit card purchases should be approved by management prior to payment.

FRAUD POLICY

Statement on Auditing Standards No. 99 – Consideration of Fraud in a Financial Statement Audit – is effective for audits of financial statements for periods beginning on or after December 15, 2002. As part of this new statement, we must ensure that the School has adopted programs and controls which are established to mitigate specific fraud risks the entity has identified, or that otherwise help to prevent, deter and detect fraud, and how management monitors those programs and controls. We noted management that management has not yet adopted a fraud policy in accordance with SAS No. 99 specifically addressing the aforementioned items. We suggest that management establish a formal fraud policy and begin working now to adopt programs and controls in an effort to comply with SAS 99 requirements.

GASB 40

Due to new GASB 40 requirements, the School is required to disclose more information regarding deposit and investment risk. In doing so, it was determined that the School does not have provisions in any investment policy that would limit its investment choices to certain credit ratings. In addition, the School places no limit on the amount the School may invest in any one issuer. We recommend the School specifically address these items in an investment policy.

GASB 45

Beginning with the fiscal year 2007-2008, the School will be required by GASB 45 to measure an annual Other Post Employment Benefit (OPEB) cost and the Net OPEB obligation. OPEB includes post-employment healthcare benefits including medical, dental, vision, and other health-related benefits or other forms of post-employment benefits such as life insurance, disability, long-term care and other benefits. The School will be required to use an actuary to perform this calculation. We recommend the School begin this process in order to ensure compliance in 2007-2008.

The foregoing conditions were considered in determining the nature, timing and extent of auditing procedures to be applied in our audit of the financial statements.

The foregoing comments and recommendations are submitted to assist you in your efforts for the continued improvements and development of policies, procedures and controls. Our comments are not intended to be critical of individual persons, but rather constructive suggestions to assist you in these efforts. We would be happy to discuss these matters with you at any time and to furnish any additional information you may require.

McVey + Associates LLC

March 21, 2006

PENNSYLVANIA CYBER CHARTER SCHOOL
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JUNE 30, 2005

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