REPORT OF THE AUDIT OF THE
KENTUCKY EDUCATIONAL DEVELOPMENT CORPORATION

For The Fiscal Year Ended
June 30, 2004

CRIT LUALLEN
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CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

To the People of Kentucky
Honorable Ernie Fletcher, Governor
Robbie Rudolph, Secretary, Finance and Administration Cabinet
Gene Wilhoit, Commissioner, Department of Education
Robert S. Sherman, Director, Legislative Research Commission
Stan Riggs, Executive Director, Kentucky Educational Development Corporation
Board of Directors of the Kentucky Educational Development Corporation

The enclosed report prepared by Berger & Company, CPA, PSC, Certified Public Accountants, presents the financial statements of the Kentucky Educational Development Corporation, Ashland, Kentucky, as of June 30, 2004.

We engaged Berger & Company, CPA, PSC to perform the financial audit of this educational cooperative. We worked closely with the firm during our report review process; Berger & Company, CPA evaluated the Kentucky Educational Development Corporation's internal controls and compliance with applicable laws and regulations.

Respectfully submitted,

Crit Luallen
Auditor of Public Accounts

Enclosure

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KENTUCKY EDUCATIONAL DEVELOPMENT CORPORATION

FINANCIAL STATEMENTS

June 30, 2004

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BERGER & COMPANY CPA, PSC

Independent Auditors' Report

To the Board of Directors of
Kentucky Educational Development Corporation
Ashland, Kentucky

We have audited the accompanying statement of financial position of the Kentucky Educational Development Corporation (KEDC), a nonprofit organization, as of June 30, 2004, and the related statements of revenues, expenses and changes in net assets, statement of functional expenses and statement of cash flows for the year then ended. These financial statements are the responsibility of the Organization'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 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 assets, liabilities and net assets of the Kentucky Educational Development Corporation as of June 30, 2004 and the results of its revenues, expenses and change in net assets for the year then ended.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 28, 2004 on our consideration of KEDC's internal control over financial reporting and on tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

To the Board of Directors of
Kentucky Educational Development Corporation
Ashland, Kentucky

The accompanying schedule of expenditures of federal awards listed in the table of contents as supplementary information is presented for purposes of additional analysis as required by the OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the general purpose financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly presented in all material respects in relation to the general purpose financial statements taken as a whole.

Respectfully Submitted,

Berger & Company CPA PSC

Berger & Company CPA, PSC

Audit fieldwork completed –
October 28, 2004

KENTUCKY EDUCATIONAL DEVELOPMENT CORPORATION
STATEMENT OF FINANCIAL POSITION
June 30, 2004

ASSETS

CURRENT ASSETS		
Cash and Cash Equivalents	$	95,846
Restricted Cash		7,403,572
Accounts Receivable		594,577
Grants Receivable		169,573
Accrued Interest Receivable		2,805
Deposits and Overpayments		610
Total Current Assets		8,266,983
PROPERTY, PLANT & EQUIPMENT		
Land		60,000
Building and Improvements		307,871
Furniture and Equipment		672,406
Big East Educational Cooperatvie Equipment		50,106
Adult and Family Literacy Equipment		91,132
Vehicles		270,362
		1,451,877
Less: Accumulated Depreciation		(930,852)
Property, Plant & Equipment, Net		521,025
TOTAL ASSETS	**$**	**8,788,008**

LIABILITIES AND NET ASSETS

CURRENT LIABILITIES		
Deferred Revenue	$	256,937
Accounts Payable		275,762
Flexible Benefits Payable		7,257,561
Accrued Flexible Account Interest Payable		3,741
Accumulated Sick Leave		85,048
Current Portion, Long-Term Debt		20,000
Total Current Liabilities		7,899,049
Long-Term Debt, less current portion		115,000
Total Liabilities		8,014,049
NET ASSETS		
Unrestricted		773,959
Temporarily Restricted		-
Total Net Assets		773,959
TOTAL LIABILITIES AND NET ASSETS	**$**	**8,788,008**

The accompanying notes are an integral part of these financial statements.

KENTUCKY EDUCATIONAL DEVELOPMENT CORPORATION

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

For The Year Ended June 30, 2004

Changes in Unrestricted Net Assets:	
Revenues:	
Sales	$ 2,488,885
Miscellaneous Receipt	150,767
Vendor Fair Receipt	24,500
Bid Book Receipt	7,807
Building Rental	850
Service to Kentucky School Districts	918,384
Board Memberships	262,636
Admin Fiscal Agent Fee	532,092
Coop Exchange Agree. Admin Fee	7,402
Local Miscellaneous Reimbursement	293,016
Proceeds from Sale of Surplus Property	3,559
Interest Income	104,671
Total Unrestricted Revenues	4,794,569
Net Assets Released From Restrictions:	
Satisfaction of Program Restrictions:	
Federal and State Programs	2,427,755
Total Unrestricted Revenues and Other Support	7,222,324
Expenses:	
Program Services	2,624,829
Management and General	4,643,038
Total Expenses	7,267,867
Decrease in Unrestricted Net Assets	(45,543)
Changes in Temporarily Restricted	
Federal and State Programs	2,427,755
Net Assets Released From Restrictions	(2,427,755)
Decrease in Temporarily Restricted Net Assets	-
Increase in Net Assets	(45,543)
Net Assets - Beginning of Year	819,502
Net Assets - End of Year	$ 773,959

KENTUCKY EDUCATIONAL DEVELOPMENT CORPORATION
STATEMENT OF CASH FLOWS
For The Year Ended June 30, 2004

CASH FLOWS FROM OPERATING ACTIVITIES		
Excess Expenditures over Revenues	$	(45,543)
Adjustments to Reconcile Net Income to Net Cash Provided by by Operating Activities		
Operating Activities		
Depreciation		168,537
(Decrease) Increase in Accumulated Sick Leave		(2,477)
(Increase) Decrease in Accounts Receivable		(239,962)
(Increase) Decrease in Accounts Receivable		(48,434)
(Increase) Decrease in Deposits and Overpayments		(610)
Increase (Decrease) in Accounts Payable		(607,209)
Increase (Decrease) Deferred Revenue		(97,612)
NET CASH PROVIDED BY OPERATING ACTIVITIES		**(873,310)**
CASH FLOWS FROM INVESTING ACTIVITIES		
Decrease in accrued interest receivable		672
Cash payments for the purchase of property		(89,586)
NET CASH PROVIDED (USED) BY INVESTING ACTIVITIES		**(88,914)**
CASH FLOWS FROM FINANCING ACTIVITIES		
Increase in accrued interest payable		3,741
Principal payments on long-term debt		(20,000)
NET CASH PROVIDED (USED) BY FINANCING ACTIVITIES		**(16,259)**
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		**(978,483)**
CASH AND CASH EQUIVALENTS, Beginning of the Year		**8,477,901**
CASH AND CASH EQUIVALENTS, End of the Year	**$**	**7,499,418**

The accompanying notes are an integral part of these financial statements.

KENTUCKY EDUCATIONAL DEVELOPMENT CORPORATION

STATEMENT OF FUNCTIONAL EXPENSES

For The Year Ended June 30, 2004

	Program Services	Management & General	Total Expenses
Accounting	$ -	$ 29,598	$ 29,598
Advertising		786	786
Auto Expense		18,862	18,862
Books and Periodicals	19,447		19,447
Capital Outlay	199,936		199,936
Consultants	140,155		140,155
Crisis Response		740	740
Evaluation	4,500		4,500
Federal Funded Benefits	49,587		49,587
Food	562		562
Insurance	4,708	54,737	59,445
Interest		7,205	7,205
Legal		68,429	68,429
Meetings	3,573	15,221	18,794
Miscellanous	167,646	302,126	469,772
Noncap Equipment	14,625	7,001	21,626
Open House	10,469		10,469
Payroll Taxes	34,197	41,301	75,498
Postage and Shipping	1,346	11,790	13,136
Printing	5,576	10,950	16,526
Professional Services	39,075		39,075
Registration	52,760		52,760
Rental Expense	30,995		30,995
Repairs and Maintenance	9,434	23,116	32,550
Retirement	65,767	38,565	104,332
Salaries	1,220,767	1,011,793	2,232,560
Sick Leave	2,766		2,766
Software		56,819	56,819
Stipends	18,138		18,138
Supplies	195,488	2,615,029	2,810,517
Telephone	17,593	16,557	34,150
Tests		2,771	2,771
Training	604	21,915	22,519
Travel	285,021	109,953	394,974
Utilities	7,779	20,828	28,607
Depreciation	22,315	146,222	168,537
Vendor Fair		10,724	10,724
	$ 2,624,829	$ 4,643,038	$ 7,267,867

KENTUCKY EDUCATIONAL DEVELOPMENT CORPORATION
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

NOTE A - NATURE OF ACTIVITIES AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Activities

Kentucky Educational Development Corporation (KEDC) was established in 1969 as a nonprofit corporation exempt under Section 501(c)(3) of the Internal Revenue Code of 1954. In July 1978, the Corporation entered into an interlocal cooperation agreement under KRS 65.160 whereby it was deemed mutually advantageous for KEDC to provide certain services, programs and/or facilities to all member school districts.

Currently, KEDC has a membership of sixty-six school districts and three universities and the Board of Directors is comprised of Superintendents of the various districts.

Basis of Accounting

The records of the Cooperative's financial statements are maintained on the accrual basis of accounting to conform with accounting principles generally accepted in the United States of America.

Inventories

Supplies and materials are charged to expenditures when purchased.

Basis of Presentation

Financial statements of the Cooperative are prepared in accordance with the American Institute of Certified Public Accountants industry audit and accounting guide, *Not-For-Profit Organizations*.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. This will affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Property, Plant and Equipment

Acquisitions of property, plant and equipment in excess of $1,000 are capitalized. Property, plant and equipment are carried at cost or fair value at the date of donation in the case of gifts. All capitalized assets are depreciated over their useful lives using the straight-line method. Furniture and equipment are being depreciated over their estimated useful lives of five years. Buildings are being depreciated over their estimated useful life of 30 years. Mechanical updates to buildings are being depreciated over their estimated useful life of 10 years.

NOTE A - NATURE OF ACTIVITIES AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Deferred Revenue

Deferred revenue consist of professional development funds held on behalf of the member districts, membership fees received in the current year for the following year and prepayments by member districts for supplies.

Donor Restrictions

Contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Support that is restricted by the donor is reported as an increase in unrestricted net assets if the restriction expires in the reporting period in which the support is recognized. All other donor-restricted support is reported as an increase in temporarily or permanently restricted net assets depending on the nature of the restriction. When a restriction expires, temporarily restricted assets are reclassified to unrestricted net assets. The Cooperative receives a substantial amount of its support from the Kentucky Department of Education and local school districts. A significant reduction in the level of this support could have an effect on the Cooperative's programs and activities.

Cash and Cash Equivalents

The Cooperative considers all monies in banks and highly liquid investments with a maturity of three months or less to be cash equivalents.

Donated Materials and Services

Donated material and equipment are reflected as contributions in the accompanying statements at their estimated value at date of receipt. No amounts have been reflected in the statements for donated services inasmuch no objective basis is available to measure the value of such services.

Income Taxes

The Cooperative is a not-for-profit organization as described in Section 501(c)(3) of the Internal Revenue Code and is exempt from federal and state income taxes. Accordingly, the accompanying financial statements include no provision for such taxes.

Allocation of Functional Expenses

It is the Cooperative's policy to allocate functional expenses according to various fixed percentages. The percentages are determined by management and are based on management's estimate of functional usage.

Federal Grant Revenue

Grant revenue is recognized when program expenditures are incurred in accordance with program guidelines. Such revenue is subject to review by the funding agency and may result in retroactive adjustment in subsequent periods.

NOTE A - NATURE OF ACTIVITIES AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

<u>Member District Dues</u>

All member districts are required to pay dues to KEDC. Dues are determined annually and are recognized as revenues when assessed because they are measurable and collectible within the current period.

<u>Other Revenues</u>

Sales and charges for services are recorded as earned since they are measurable and available. Miscellaneous charges are recorded as revenue when received because they are generally not measurable until actually received.

NOTE B - CASH AND CASH EQUIVALENTS

The Corporation maintains funds through a fiduciary relationship with the member districts in which KEDC administers the districts' flexible benefit plans. These funds are invested in the Kentucky Class Portfolio administered by AMBAC securities. All investments are carried at cost which approximates market and may be liquidated at any time. The investment pools have not been assigned a risk category since KEDC is not issued securities, but rather owns an undivided beneficial interest in the assets of the pools. These funds are entirely invested in obligations of the federal government.

The Corporation's operating funds are on deposit at a local financial institution. At June 30, 2004, the carrying amount of the Cooperative's cash was $238,119 and the bank balances were $492,628. The difference between the carrying amount and the bank balances results from deposits in transit and outstanding checks. As of June 30, 2004, the bank balances were either insured up to $100,000 by the Federal Deposit Insurance Corporation (FDIC) or they were invested in obligations of the federal government leaving all funds fully insured. However, on October 27, 2003, $377,102 of the Corporation's bank balances were uninsured and unsecured.

NOTE C - RESTRICTED CASH

Restricted cash at June 30, 2004 consists of the following:

Flex Plan Assets Held for Member Districts	$7,261,299
Retainers Received from Districts for Supplies	54,180
Professional Development Funds	50,910
State and Federal Grant Funds	37,183
	$7,403,572

NOTE D - BONDED DEBT AND LEASE OBLIGATION

In October 1994, KEDC entered into a lease/option contract with Kentucky Education Finance Corporation to make semi-annual payments to the principal and interest requirements of its 1994 issue of First Mortgage Revenue Bonds totaling $275,000 and bearing interest rates of 5.6% to 6.0%. The purpose of this issue was to provide funds to retire a mortgage note held by KEDC with First and Peoples Bank and Trust Company of Russell, Kentucky, for the purchase of the land and building currently occupied by KEDC. Changes in bonds payable for the year ended June 30, 2004 are outlined below:

Balance outstanding at June 30, 2003	$155,000
Bonds retired during the current year	(20,000)
Balance outstanding at June 30, 2004	$135,000

The bonds have been prepared as two fully registered Term Bonds maturing October 1, 2004 and October 1, 2009. The minimum obligations of KEDC at June 30, 2004 for debt service (principal and interest) are as follows.

YEAR ENDED JUNE 30:	PRINCIPAL	INTEREST	TOTAL
2005	$ 20,000	$ 7,460	$ 27,460
2006	20,000	6,300	26,300
2007	20,000	5,100	25,100
2008	25,000	3,750	28,750
2009	25,000	2,250	27,250
2010	25,000	750	25,750
TOTAL	$ 135,000	$ 25,610	$160,610

NOTE E - TEMPORARILY RESTRICTED NET ASSETS

There are no temporarily restricted net assets. Consistent with KEDC's accounting policies as discussed in Note A, grant revenue is considered receivable when the expenditures are incurred and grant and professional development funds received before expended are considered deferred revenue. Thus, assets and liabilities for special revenue accounts on the Statement of Financial Position are equal and none of the net asset balance is generated from these accounts.

NOTE F - ACCUMULATED UNPAID SICK LEAVE BENEFITS

Upon retirement from KEDC, an employee will receive from the Corporation an amount equal to 30% of the value of accumulated sick leave. At June 30, 2004, twenty-three employees were eligible for retirement and thus, an $85,048 of net assets are reserved for accumulated sick leave at June 30, 2004.

NOTE G - FAIR VALUES OF FINANCIAL INSTRUMENTS

The carrying amount of the following financial instruments approximate fair value because of the short maturity of the instruments: cash equivalents, restricted capital fund, deferred revenue and note payable.

NOTE H - CONCENTRATION OF CREDIT RISK AND ECONOMIC DEPENDENCE

The Cooperative receives a substantial amount of its support from the Kentucky Department of Education, the federal government and local school districts. A significant reduction in the level of this support would have an effect on the Cooperative's programs and activities.

NOTE I - RISK MANAGEMENT

KEDC is exposed to various risk of loss related to the theft of, damage to and destruction of assets, errors and omissions, fiduciary responsibilities and natural disasters for which it carries commercial insurance. There have been no significant reductions in coverage from the prior year and there have been no significant settlements in the past two years.

NOTE J - COMMITMENTS AND CONTINGENCIES

The Corporation participates in numerous state and federal grant programs which are governed by various rules and regulations of the grantor agencies. Costs charged to the respective programs are subject to audit and adjustment by the grantor agencies; therefore, to the extent that the Corporation has not complied with the rules and regulations governing the grants, refunds of any money received may be required and the collectibility of any related receivable at June 30, 2004 may be impaired. In the opinion of the Corporation, there are no significant contingent liabilities relating to compliance with the rules and regulations governing the respective grants; therefore, no provision has been recorded in the accompanying financial statements for such contingencies.

NOTE K - RETIREMENT PLANS

Kentucky Teachers' Retirement System

Plan Description – The Kentucky Teachers' Retirement System (KTRS) is an "actuarial reserve, joint contributing" defined benefit public employee retirement system. The plan provides benefit pension plan coverage for local school districts and other public educational agencies within the state. All full-time employees occupying a position requiring certification by the Kentucky Department of Education are covered under the defined benefit plan administered by KTRS. Full-time employees whose job description requires a degree and have a four-year college or university degree are also covered.

The Plan provides for retirement, disability, death, survivor, and health benefits of its members. The KTRS annual financial report and other required disclosure information are available by writing the Kentucky Teacher Retirement System, 479 Versailles Road, Frankfort Kentucky 40601-3868; or by calling 800-618-1687.

NOTE K - RETIREMENT PLANS (Continued)

<u>Kentucky Teachers' Retirement System</u>

Service retirement – A member is fully vested after five years of creditable service and entitled to any benefit for which eligibility requirements have been met. Special provisions may apply to members who accept a covered position after retirement.

<u>Normal</u>

27 years of covered service, or
Any combination of age plus years of service, which equals 72

<u>Reduced benefits</u>

Age 55 with 5 years of covered service, or
A minimum of 20 years covered service

Funding Status and Progress – The Commonwealth of Kentucky contributes to the retirement system an amount equal to the current authorized rate times the aggregate annual compensation of eligible KTRS members. Therefore, all risks and employer matching costs are not shared by the District but are a liability of the Commonwealth. The authority for employer contributions is defined in Chapter 161, Section 540(1) and Chapter 161, Section 555 of the Kentucky Revised Statutes. The following are the KTRS contribution rates for the year ended June 30, 2004:

Employee Contribution	State of Kentucky
9.855 %	9.855 % plus 3.25 %

Funding for the plan is provided by contributions from eligible employees and an employer contribution at a rate of 12.305% of salaries. During the year ended June 30, 2004, the Corporation contributed $42,694 and employees contributed $144,743 to the plan.

<u>County Employees Retirement System</u>

The County Employees Retirement System of Kentucky ("System") is a multi-employer public retirement plan created by and operating under Kentucky Law.

The County Employees Retirement System is a defined benefit plan which covers substantially all regular non-certified, full-time employees of each county and school board, and any additional eligible local agencies electing to participate in the System. The Plan provides for retirement, disability and death benefits.

For the year ended June 30, 2004, participating employees contributed 5.00% of creditable compensation to the System. The total payroll of KEDC was $2,030,179 of which $823,685 was eligible to participate in the system.

NOTE K - RETIREMENT PLANS (Continued)

County Employees Retirement System

Employer contribution rates are intended to fund the System's normal cost on a current basis, plus an amount equal to the amortization of unfunded past service costs over thirty years, using the level percentage of payroll method. Such contribution rates are determined by the Board of Trustees of Kentucky Teachers Retirement Systems each biennium. Participating employers contributed 7.34% of members' non-hazardous compensation for the year ended June 30, 2004. The contribution requirement for the year ended June 30, 2004 was $101,642 which consisted of $60,458 from the Corporation and $41,184 from the Employees.

Vesting in a retirement benefit begins immediately upon entry into the System. The participant has a fully-vested interest after the completion of sixty months of service, twelve of which are current service. At a minimum, terminated employees are refunded their contributions with credited interest at 3% compounded annually through June 30, 1980, 6% thereafter through June 30, 1986, and 4% thereafter.

The pension benefit obligation, which is the actuarial present value of credited projected benefits, is a standardized disclosure measure of the present value of pension benefit, adjusted for the effects of projected salary increases, estimated to be payable in the future as a result of employee service to date. The System does not make separate measurements of assets and benefit obligations for individual employers.

The pension benefit obligation, determined as a part of actuarial valuation, at June 30, 2003 (the most recent date for which audited information is available), for the System as a whole, was $5,917,227,000. The System's net assets available for benefits on June 30, 2003 (based on a five – year moving average of market value to book value) were $6,753,585,000, leaving a funded pension benefit obligation of $12,670,812,000.

Ten-year historical trend information designed to provide information about the System's progress in accumulating sufficient assets to pay benefits when due is presented in the Kentucky Retirement System's Annual Report for the fiscal year ending June 30, 2003.

NOTE L - RESTATEMENT OF BEGINNING NET ASSETS / CHANGE IN REPORTING MODEL

In prior years, the financial statements of KEDC have been presented consistent with the entity being a governmental unit. Since the entity is incorporated as a not-for-profit organization and it files a tax return as a not-for-profit exempt from federal income taxes, management feels that reporting under the not-for-profit reporting model is more consistent with the nature of its operations. As a result of this change, the financial statements reflect the changes in KEDC's net assets as opposed to changes in its fund balances. To conform with accounting principles generally accepted in the United States of America, the entity also began depreciating it capital assets during the year ended June 30, 2004. As a result of these changes, the entity's beginning net assets at July 1, 2003 had to be restated as follows:

NOTE L - RESTATEMENT OF BEGINNING NET ASSETS / CHANGE IN REPORTING MODEL (Continued)

Prior Year Fund Balances	$ 2,009,539
Prior Year Sick Pay	(87,525)
Prior Year Capital Assets < $1,000	(185,197)
Beginning Accumulated Depreciation	(762,315)
Prior Year Long-Term Debt	(155,000)
Beginning Net Assets, July 1, 2003	$ 819,502

In the prior year, $87,525 of the fund balance was reserved for accumulated sick pay. As restated, this amount is included as a liability in the Statement of Financial Position. Prior year capital assets with a carrying value of less than $1,000 which were reported in the fixed asset account group in the prior year were removed from KEDC's capitalized assets. Beginning accumulated depreciation on capital assets was calculated and offset against the related historical cost as noted in Note M. Prior year long-term debt was accounted for in the Long-term debt account group in the prior year. As restated, it is included as a liability in the Statement of Financial Position.

NOTE M - FIXED ASSETS

During the year, the Corporation began depreciating assets with a historical cost in excess of $1,000. The beginning accumulated depreciation based upon the Corporation's policies as listed in Note A was $762,315. Prior year assets with a historical cost of less than $1,000 were treated as disposals and were removed from the Corporation's fixed asset listing. This resulted in $185,197 of disposals. No gain or loss is recognized on these disposals since they were treated as expenditures in the Corporation's general or special revenue fund when they were originally purchased.

A summary of changes in the fixed asset accounts for the year ended June 30, 2004 are as follows:

	BALANCE 6/30/2003	ADDITIONS	DISPOSALS	BALANCE 6/30/2004
Land	$ 60,000	$ -	$ -	$ 60,000
Building and Improvements	307,871	-	-	307,871
Furniture and Equipment	699,605	83,997	111,196	672,406
Big East Educational Cooperatvie Equipment	58,092	-	7,986	50,106
Adult and Family Literacy Equipment	85,543	5,589	-	91,132
Vehicles	336,377	-	66,015	270,362
	$1,547,488	$ 89,586	$ 185,197	$1,451,877
Accumulated Depreciation				
Buildings and Improvements	71,269	8,420	-	79,689
Furniture and Equipment	412,214	137,803	-	550,017
Big East Educational Cooperative Equipment	39,930	4,680	-	44,610
Adult and Family Literacy Equipment	26,722	17,634	-	44,356
Vehicles	212,180	-	-	212,180
	762,315	168,537	-	930,852
Net Fixed Assets	$ 785,173	$ (78,951)	$ 185,197	$ 521,025

KENTUCKY EDUCATIONAL DEVELOPMENT CORPORATION
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For The Year Ended June 30, 2004

Federal Grantor/Pass Through Grant/Program Title	Federal CFDA Number		Pass Through Grantor Number	Federal Expenditures
U.S. DEPARTMENT OF EDUCATION				
Passed Through from Kentucky Cabinet for Workforce Development:				
Adult Education	84.002		DAEL-2004-010	$ 251,911
Passed Through from Kentucky Department of Education:				
IDEA-B	84.027	*	0581-02-04	527,457
Smaller Learning Communities (OVAE)	84.215L		Direct	231,053
Total U.S. Department of Education				1,010,421
TOTAL EXPENDITURES OF FEDERAL AWARDS				$ 1,010,421

* Denotes Major Program

See auditors' report.

KENTUCKY EDUCATIONAL DEVELOPMENT CORPORATION
Notes to Schedule of Expenditures of Federal Awards
For the Year Ended June 30, 2004

Note A: Basis of Presentation

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Kentucky Educational Development Corporation and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of State, Local Governments, and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in preparation of, the financial statements.

BERGER & COMPANY CPA, PSC

To the Board of Directors of
Kentucky Educational Development Corporation
Ashland, Kentucky

Report On Compliance And On Internal Control
Over Financial Reporting Based On An Audit Of The Financial
Statements Performed In Accordance With Government Auditing Standards

We have audited the financial statements of the Kentucky Educational Development Corporation (a nonprofit organization) as of and for the year ended June 30, 2004, and have issued our report thereon dated October 28, 2004. 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.

Compliance

As part of obtaining reasonable assurance about whether the Kentucky Educational Development Corporation'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 an instance of noncompliance that is required to be reported under *Government Auditing Standards* and which is described in the accompanying comment and recommendation.

- The Cooperative Should Require The Depository Institution To Pledge Or Provide Sufficient Collateral And Enter Into A Written Agreement To Protect Deposits

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Kentucky Educational Development Corporation's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses.

Internal Control Over Financial Reporting (Continued)

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 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. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of management and is not intended to be and should not be used by anyone other than the specified party.

Respectfully Submitted,

Berger & Company CPA PSC

Berger & Company CPA, PSC

Audit fieldwork completed –
October 28, 2004

BERGER & COMPANY
CPA, PSC

To the People of Kentucky
Honorable Ernie Fletcher, Governor
Gene Wilhoit, Commissioner, Department of Education
Board of Directors, Kentucky Educational Development Corporation

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

Compliance

We have audited the compliance of Kentucky Educational Development Corporation (KEDC) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the year ended June 30, 2004. Kentucky Educational Development Corporation's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of Kentucky Educational Development Corporation's management. Our responsibility is to express an opinion on Kentucky Educational Development Corporation's 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, Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above, that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about KEDC's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on Kentucky Educational Development Corporation's compliance with those requirements.

In our opinion Kentucky Educational Development Corporation's complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2004.

Internal Control Over Compliance

The management of Kentucky Educational Development Corporation's 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 Kentucky Educational Development Corporation's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order 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 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 that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the Members of the Board, management, Kentucky Department of Education, 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.

Respectfully Submitted,

Berger & Company CPA PSC

Berger & Company, CPA, PSC

Audit Fieldwork Completed -
October 28, 2004

Schedule of Findings and Questioned Costs
For the Period Ended June 30, 2004

Sections I - Summary of Auditor's Results

Financial Statements

Type of auditor's report issued:	Unqualified			
Internal control over financial reporting:				
Material weakness(es) identified?		yes	X	no
Reportable condition(s) identified that are not considered to be material weaknesses?		yes	X	none reported
Noncompliance material to financial statements noted?		yes	X	no

Federal Awards

Internal control over major programs:				
Material weakness identified?		yes	X	no
Reportable condition(s) identified that are not considered to be material weaknesses?		yes	X	none reported
Type of auditor's report issued on compliance for major programs:			Unqualified	
Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133?		yes	X	no

Identification of major programs:

CFDA Number(s)	Name of Federal Program or Cluster
84.027	IDEA, Part B

Dollar threshold used to distinquish between Type A and B Programs:			$ 300,000	
Auditee qualified as low-risk auditee?		yes	x	no

Sections II - Financial Statement Audit Findings

The Cooperative Should Require The Depository Institution To Pledge Or Provide Sufficient Collateral And Enter Into A Written Agreement To Protect Deposits. See comment and recommendation.

Sections III - Major Federal Award Program Audit Findings and Questioned Costs

No matters were reported.

KENTUCKY EDUCATIONAL DEVELOPMENT CORPORATION
COMMENT, RECOMMENDATION AND SUMMARY OF PRIOR YEAR AUDIT FINDINGS

For The Year Ended June 30, 2004

STATE LAWS AND REGULATIONS:

The Cooperative Should Require The Depository Institution To Pledge Or Provide Sufficient Collateral And Enter Into A Written Agreement To Protect Deposits

Kentucky Educational Development Corporation ("KEDC") maintained deposits of public funds with depository institutions insured by the Federal Deposit Insurance Corporation (FDIC). According to KRS 66.480(1)(d) and KRS 41.240(4), the depository institution should pledge or provide sufficient collateral which, together with FDIC insurance, equals or exceeds the amount of public funds on deposit at all times. In order to be valid against the FDIC in the event of failure or insolvency of the depository institution, this pledge or provision of collateral should be evidenced by an agreement between KEDC and the depository institution, signed by both parties, that is (a) in writing, (b) approved by the board of directors of the depository institution or its loan committee, which approval must be reflected in the minutes of the board or committee, and (c) an official record of the depository institution. As of October 27, 2003, the collateral and FDIC insurance together did not equal or exceed the amount on deposit, leaving $377,102 of public funds uninsured and unsecured. In addition, KEDC did not have a written agreement with its depository institution securing KEDC's interest in the collateral.

We recommend that KEDC get a written collateral security agreement with its banks and put procedures in place to assure that both banks are pledging assets within the terms of their written agreements.

Cooperative's Response:
From now on we will make large deposits directly into our sweep account which is invested in U.S. Government obligations which are fully insured.

PRIOR YEAR

No matters were reported.