STATE OF
NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT OF

CRAVEN COMMUNITY COLLEGE

NEW BERN, NORTH CAROLINA

FOR THE YEAR ENDED JUNE 30, 2005

OFFICE OF THE STATE AUDITOR

LESLIE W. MERRITT, JR., CPA, CFP

STATE AUDITOR

Financial Statement Audit Report Of

Craven Community College

New Bern, North Carolina

For the Year Ended June 30, 2005

State Board of Community Colleges

The North Carolina Community College System

H. Martin Lancaster, President

Administrative Officers

Dr. Scott Ralls, President

Johnny L. Peterson, Vice President for Financial and Administrative Services

STATE OF NORTH CAROLINA
Office of the State Auditor

Leslie W. Merritt, Jr., CPA, CFP
State Auditor

2 S. Salisbury Street
20601 Mail Service Center
Raleigh, NC 27699-0601
Telephone: (919) 807-7500
Fax: (919) 807-7647
Internet
http://www.ncauditor.net

AUDITOR'S TRANSMITTAL

The Honorable Michael F. Easley, Governor
The General Assembly of North Carolina
Board of Trustees, Craven Community College

We have completed a financial statement audit of Craven Community College for the year ended June 30, 2005, and our audit results are included in this report. You will note from the independent auditor's report that we determined that the financial statements are presented fairly in all material respects.

Our consideration of internal control over financial reporting and compliance and other matters based on an audit of the financial statements disclosed certain deficiencies and/or instances of noncompliance that are detailed in the Audit Findings and Recommendations section of this report. The College's response is included following each finding.

North Carolina General Statutes require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.

Leslie W. Merritt, Jr.

Leslie W. Merritt, Jr., CPA, CFP
State Auditor

February 21, 2006

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STATE OF NORTH CAROLINA

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2 S. Salisbury Street
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State Auditor

INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Craven Community College
New Bern, North Carolina

We have audited the accompanying basic financial statements of Craven Community College, a component unit of the State of North Carolina, as of and for the year ended June 30, 2005, as listed in the table of contents. These financial statements are the responsibility of the College'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 opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Craven Community College as of June 30, 2005, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 14 to the financial statements, the College implemented Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures*, during the year ended June 30, 2005.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 23, 2006, on our consideration of the College's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis, as listed in the table of contents, is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of 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.

Leslie W. Merritt, Jr.

Leslie W. Merritt, Jr., CPA, CFP
State Auditor

January 23, 2006

CRAVEN COMMUNITY COLLEGE
MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of Craven Community College's Annual Financial Report presents Management's Discussion and Analysis of the College's financial activity during the fiscal years ended June 30, 2005, and June 30, 2004. Since this Management's Discussion and Analysis is designed to focus on current activities, resulting change and currently known facts, please read it in conjunction with the transmittal letter, the College's basic financial statements and the notes to the financial statements. Responsibility for the completeness and fairness of this information rests with the College.

Using This Annual Report

The College's basic financial statements are designed to emulate corporate presentation models whereby all College activities are consolidated into one total. The focus of the Statement of Net Assets is designed to be similar to bottom line results for the College. This statement combines and consolidates current financial resources (short-term consumable resources) with capital assets. The Statement of Revenues, Expenses, and Changes in Net Assets focuses on both the gross costs and the net costs of College activities which are supported mainly by State, local, federal and other revenues. This approach is intended to summarize and simplify the user's analysis of costs of various College services to students and the public.

The College's net assets are one indicator of its financial stability. The Statement of Net Assets includes all assets and liabilities. The increase or decrease in net assets is an indicator of the improvement or erosion of the College's financial condition.

The Statement of Revenues, Expenses, and Changes in Net Assets presents the revenues earned and expenses incurred during the fiscal year. Activities are reported as operating or nonoperating. The College's dependency on State aid, county appropriations, and gifts could result in operating deficits because the financial reporting model classifies State aid, county appropriations, and gifts as nonoperating revenues. The utilization of capital assets is reflected in the financial statements as depreciation.

The Statement of Cash Flows presents information related to cash inflows and outflows summarized by operating, noncapital financing, capital and related financing, and investing activities. The direct method is used to present cash flows.

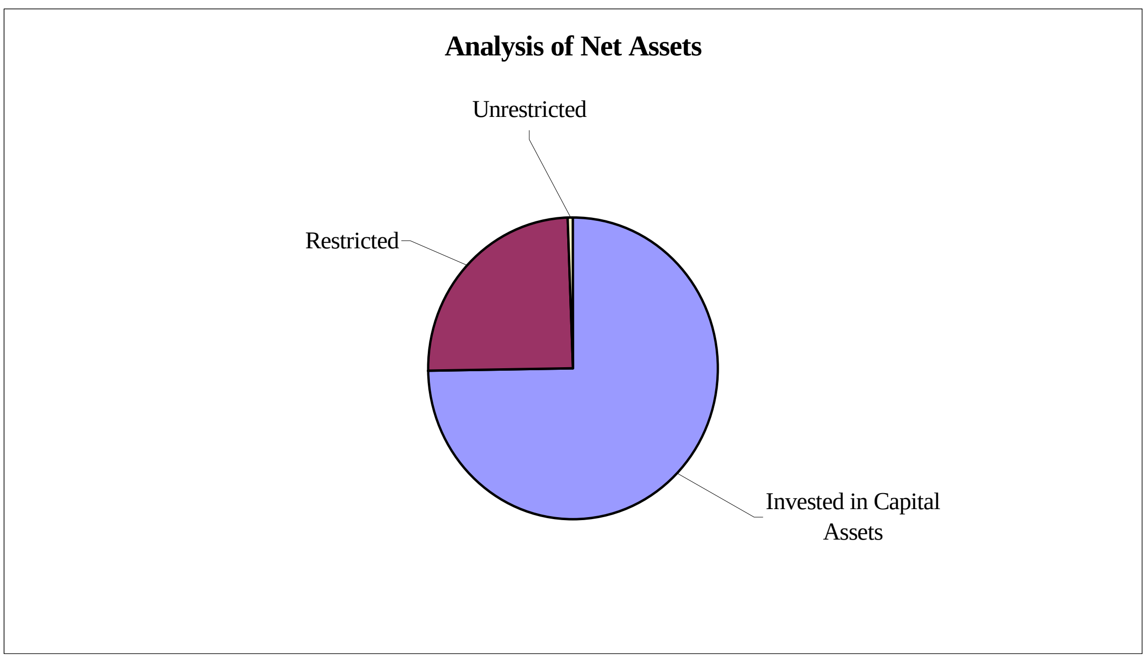
The notes to financial statements provide additional information that is essential to a full understanding of the data provided.

Financial Analysis of the College as a Whole

Analysis of Net Assets
June 30,
(in thousands)

		2005		2004		Increase (Decrease)	Percent Change
Net Assets:							
Invested in Capital Assets	$	22,645.06	$	21,239.76	$	1,405.30	6.62%
Restricted		7,455.26		6,384.95		1,070.31	16.76%
Unrestricted		208.50		254.00		(45.50)	-17.91%
Total	$	30,308.82	$	27,878.71	$	2,430.11	

The following is a graphic illustration of net assets:



Condensed Statement of Net Assets
June 30,
(in thousands)

	2005	2004	Increase (Decrease)	Percent Change
Current Assets	$ 1,810.35	$ 2,426.48	$ (616.13)	-25.39%
Noncurrent Assets:				
Capital Assets, Net of Depreciation	22,645.06	21,239.76	1,405.30	6.62%
Other	6,807.18	5,593.84	1,213.34	21.69%
Total Assets	31,262.59	29,260.08	2,002.51	
Current Liabilities	554.80	931.83	(377.03)	-40.46%
Noncurrent Liabilities	398.97	449.54	(50.57)	-11.25%
Total Liabilities	953.77	1,381.37	(427.60)	
Net Assets:				
Invested in Capital Assets	22,645.06	21,239.76	1,405.30	6.62%
Restricted	7,455.26	6,384.95	1,070.31	16.76%
Unrestricted	208.50	254.00	(45.50)	-17.91%
Total Net Assets	$ 30,308.82	$ 27,878.71	$ 2,430.11	

These schedules were prepared from the College's Statement of Net Assets, which is presented on an accrual basis of accounting whereby assets are capitalized and depreciated. Depreciation expense was recorded due to implementation of GASB Statements No. 34 and 35.

As of June 30, 2005, the College's net assets have increased to $30,308,816 from $27,878,713 at June 30, 2004. The resulting change is due to an increase in construction in progress of $951,725 (ongoing projects include the Havelock Campus Parking Lot, Machine Shop Addition, Advanced Manufacturing Center, Information and Technology Building and Roadway, Parking and Maintenance Building) and capital assets donations of $905,200 consisting mostly of a cutaway engine which is to be used in the Aviation System Technology program located at the Havelock campus.

Condensed Statement of Revenues, Expenses, and Changes in Net Assets
for the Years Ended June 30,
(in thousands)

	2005	2004	Increase (Decrease)	Percent Change
Operating Revenues:				
Tuition and Fees	$ 2,322.86	$ 2,465.33	$ (142.47)	-5.78%
Federal Grants and Contracts	2,935.93	2,926.69	9.24	0.32%
State Grants and Contracts	94.41	289.14	(194.73)	-67.35%
Auxiliary	1,196.05	1,400.86	(204.81)	-14.62%
Other	50.30		50.30	
Total	6,599.55	7,082.02	(482.47)	
Less Operating Expenses	21,990.71	21,054.59	936.12	4.45%
Net Operating Loss	(15,391.16)	(13,972.57)	(1,418.59)	10.15%
Nonoperating Revenues:				
State Aid	9,870.02	7,556.64	2,313.38	30.61%
County Appropriations	2,629.18	2,367.59	261.59	11.05%
Noncapital Grants	967.34	974.65	(7.31)	-0.75%
Noncapital Gifts	707.96	639.63	68.33	10.68%
Investment Income	165.21	237.59	(72.38)	-30.46%
Other Nonoperating	3.32	46.25	(42.93)	-92.82%
Total	14,343.03	11,822.35	2,520.68	
Loss Before Other Revenues	(1,048.13)	(2,150.22)	1,102.09	-51.25%
Other Revenues:				
State Capital Aid	2,066.53	2,690.74	(624.21)	-23.20%
County Capital Appropriations	493.61	550.00	(56.39)	-10.25%
Capital Grants	12.90		12.90	
Capital Gifts	905.20	2,938.60	(2,033.40)	-69.20%
Increase in Net Assets	2,430.11	4,029.12	(1,599.01)	-39.69%
Net Assets, July 1	27,878.71	23,849.59	4,029.12	16.89%
Net Assets, End of Year	$ 30,308.82	$ 27,878.71	$ 2,430.11	8.72%
Total Revenues	$ 24,420.82	$ 25,083.71	$ (662.89)	

Operating Expenses
For the Years Ended June 30,
(in thousands)

	2005	2004	Increase (Decrease)	Percent Change
Operating Expenses:				
Personal Services	$ 13,006.76	$ 11,794.13	$ 1,212.63	10.28%
Supplies and Materials	2,566.29	2,789.70	(223.41)	-8.01%
Services	2,523.73	2,504.05	19.68	0.79%
Scholarships/Fellowships	2,269.36	2,375.82	(106.46)	-4.48%
Utilities	587.23	554.95	32.28	5.82%
Depreciation	1,037.34	1,035.94	1.40	0.14%
Total	$ 21,990.71	$ 21,054.59	$ 936.12	

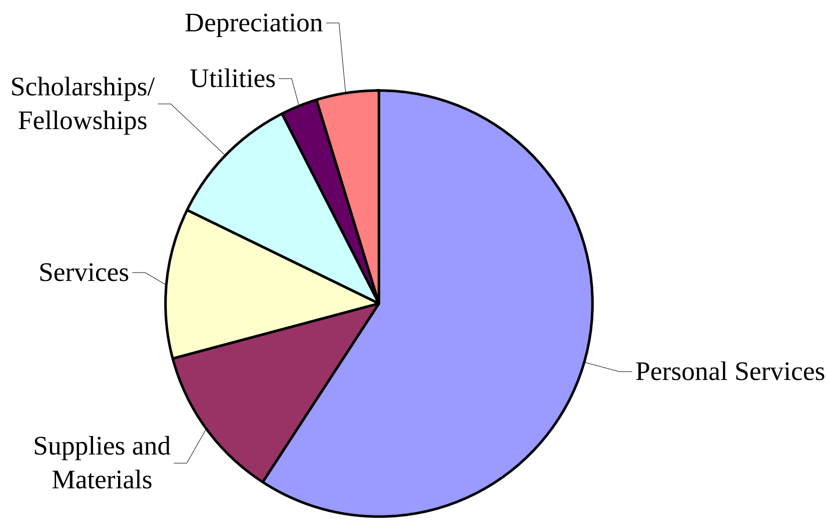
These schedules were prepared from the College's Statement of Revenues, Expenses, and Changes in Net Assets.

Operating expenses at June 30, 2005, increased over the same period in fiscal year 2004. This increase was caused primarily by an increase in personal services of $1,212,628 primarily due to raises of 8%.

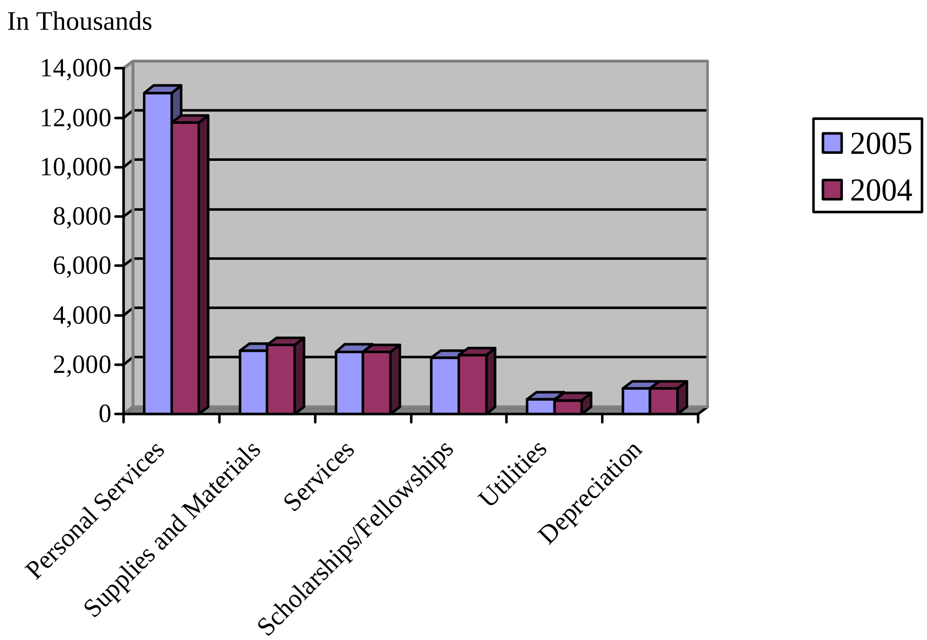
Operating revenue decreased by $482,462 due to a decrease in bookstore sales of $234,535 and a reduction of State grants received of $194,727. Enrollment growth leveled off and tuition and fees decreased by $142,471. State aid and county appropriations increased by $2,313,383 and $261,595 respectively, which contributed to the increase in total nonoperating revenue of $2,520,677.

The following is a graphic illustration of operating expenses:

Operating Expenses



Comparison of Operating Expenses
Fiscal Years 2005 and 2004



Capital Assets

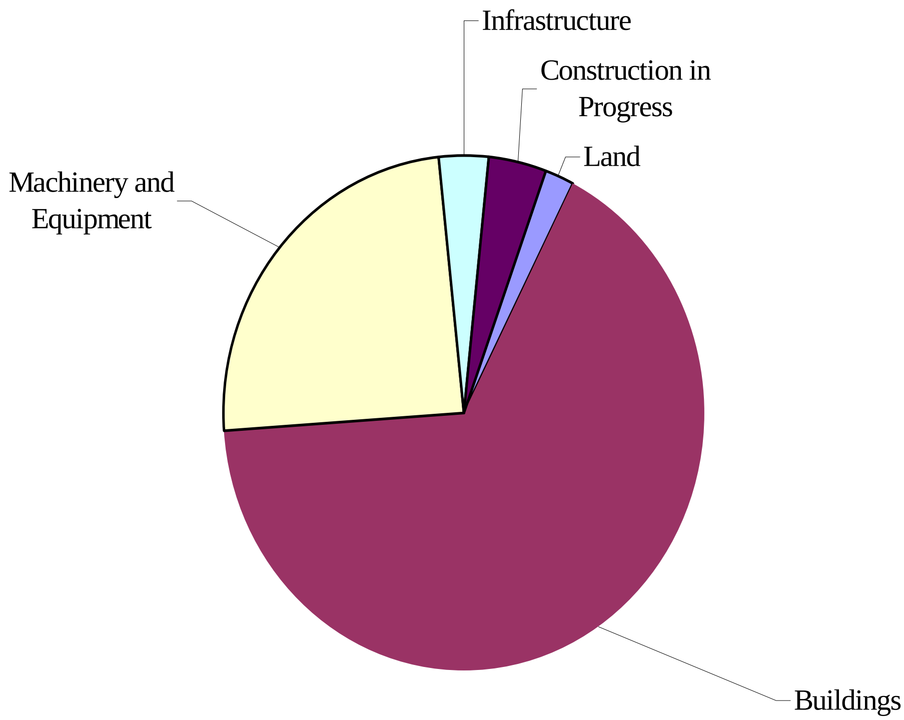
As of June 30, 2005, the College had recorded $30,633,804 in capital assets, $7,988,743 in accumulated depreciation, and $22,645,061 in net capital assets. Construction in progress consists of the Havelock Campus Parking Lot (a $320,750 project), Machine Shop Addition (a $1,104,000 project), Advanced Manufacturing Center (a $7,900,000 project), Information and Technology Building (a $5,325,711 project), Roadway, Parking and Maintenance Building (a $1,500,922 project), Reroofing of Buildings B and G (a $470,141 project), and Repairs and Renovations to the Library (a $264,000 project). As of June 30, 2005, the College has commitments of $1,787,564 for ongoing construction projects. The 2000 State Bond Referendum as authorized by Senate Bill 912 will fund the majority of these projects. The Legislature has also approved in the 2005-2006 budget a total of $7,400,000 for the Advanced Manufacturing Center of which $3,700,000 is to be received in the 2005-2006 fiscal year and $3,700,000 is to be received in the 2006-2007 fiscal year. Additional funding for some projects is provided through campus access fees, bookstore funds, local funds, and the U.S. Department of Economic Development Administration.

These schedules are prepared from the College's Statement of Net Assets, which is presented on an accrual basis of accounting whereby assets are capitalized and depreciated.

Capital Assets, Net
For Years Ended June 30,
(in thousands)

	2005	2004	Increase (Decrease)	Percent Change
Capital Assets:				
Land	$ 596.50	$ 596.50	$ 0.00	0.00%
Buildings	20,372.43	20,068.39	304.04	1.52%
Machinery and Equipment	7,449.20	6,321.03	1,128.17	17.85%
Construction in Progress	1,007.12	998.93	8.19	0.82%
	1,208.55	256.83	951.72	370.56%
Total	30,633.80	28,241.68	2,392.12	
Less: Accumulated Depreciation	7,988.74	7,001.92	986.82	14.09%
Net Capital Assets	$ 22,645.06	$ 21,239.76	$ 1,405.30	

Capital Assets, Net



Economic Forecast

The New Bern Area Chamber of Commerce reports that the New Bern/Craven County area is experiencing steady growth in population, education, and economic development. The decade 1990-2000 saw a population growth of 12% for Craven County. By 2010 the area is projected to have more than 100,000 residents (US Census Bureau reports an estimated population of 91,754 in 2003). The fastest growing segment of the population is the relocation/early retirement age group (55+). The mild climate, excellent health care and affordable lifestyle in the area make it an attractive destination for many retirees, who add immeasurably to the area's available experienced workforce. Because of the well-trained workforce, a growing population with increased buying power, affordable cost of living and doing business, available resources and technology, and an overall favorable environment, the New Bern/Craven County area is inviting to new businesses.

Major industries in the area include Naval Aviation Depot (NADEP) at Cherry Point, Moen, Inc., BSH Home Appliances, Hatteras Yachts, and Weyerhaeuser Company. Major employers enjoy the support and job training provided by the College's industry training and workforce continuing education programs. BSH Home Appliances announced expansion plans that would add approximately 1,200 more jobs over the course of the next three years. This would bring their total number of employees up to approximately 1,900. With their expansion also comes the advantage of other businesses relocating to the area to meet their supply needs as in Carolina Technical Plastics and Prettl Systems. Hatteras Yachts has expansion plans which will add approximately 100-150 jobs.

Craven Community College monitors the changes in technology and economy and strives to meet the needs of our growing community. To meet industry needs, the College is in the process of expanding the machining technology program, which includes a building addition to house the new technology necessary for the program. The College has secured funding for the Bosch-Siemens Advanced Manufacturing Center which will house a new manufacturing program, provide facilities for the Early College initiative and provide facilities for local industry to utilize for training. The recent addition of an aviation systems technology program will provide a skilled workforce for NADEP which employs approximately 4,133 people. In an effort to meet the needs of the health care providers, the College is expanding its offerings with programs such as medical assisting in the fall, 2005. The College is also looking into starting new programs such as central sterile processing and surgical technology.

Overall, the economic forecast for the region and Craven Community College appears positive.

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Craven Community College
Statement of Net Assets
June 30, 2005 *Exhibit A-1*

ASSETS		
Current Assets:		
Cash and Cash Equivalents	$	233,452.74
Restricted Cash and Cash Equivalents		811,095.87
Receivables, Net (Note 4)		441,419.62
Due from State of North Carolina Component Units		21,420.00
Inventories		299,867.03
Notes Receivable, Net (Note 4)		3,097.10
Total Current Assets		1,810,352.36
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		2,204,798.29
Receivables, Net (Note 4)		95,866.78
Restricted Due from Primary Government		3,326,093.23
Endowment Investments		1,180,416.99
Capital Assets - Nondepreciable (Note 5)		1,805,053.61
Capital Assets - Depreciable, Net (Note 5)		20,840,007.60
Total Noncurrent Assets		29,452,236.50
Total Assets		31,262,588.86
LIABILITIES		
Current Liabilities:		
Accounts Payable and Accrued Liabilities (Note 6)		366,245.85
Due to Primary Government		3,538.00
Deferred Revenue		8,169.32
Funds Held for Others		33,098.15
Long-Term Liabilities - Current Portion (Note 7)		143,751.81
Total Current Liabilities		554,803.13
Noncurrent Liabilities:		
Long-Term Liabilities (Note 7)		398,969.49
Total Liabilities		953,772.62
NET ASSETS		
Invested in Capital Assets		22,645,061.21
Restricted for:		
Nonexpendable:		
Scholarships and Fellowships		1,242,264.58
Expendable:		
Scholarships and Fellowships		138,108.05
Loans		18,887.37
Capital Projects		5,408,746.55
Other		647,245.26
Unrestricted		208,503.22
Total Net Assets	$	30,308,816.24

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

Craven Community College
Statement of Revenues, Expenses, and Changes in Net Assets
For the Fiscal Year Ended June 30, 2005 ***Exhibit A-2***

REVENUES	
Operating Revenues:	
Student Tuition and Fees, Net (Note 8)	$ 2,322,860.40
Federal Grants and Contracts	2,935,934.73
State and Local Grants and Contracts	94,409.13
Sales and Services, Net (Note 8)	1,196,049.66
Other Operating Revenues	50,300.06
Total Operating Revenues	6,599,553.98
EXPENSES	
Operating Expenses:	
Personal Services	13,006,760.45
Supplies and Materials	2,566,294.99
Services	2,523,734.02
Scholarships and Fellowships	2,269,361.94
Utilities	587,225.58
Depreciation	1,037,335.43
Total Operating Expenses	21,990,712.41
Operating Loss	(15,391,158.43)
NONOPERATING REVENUES	
State Aid	9,870,020.27
County Appropriations	2,629,183.00
Noncapital Grants	967,341.14
Noncapital Gifts	707,963.38
Investment Income, Net	165,208.14
Other Nonoperating Revenues	3,314.23
Total Nonoperating Revenues	14,343,030.16
Loss Before Other Revenues	(1,048,128.27)
State Capital Aid	2,066,532.04
County Capital Appropriations	493,613.00
Capital Grants	12,886.42
Capital Gifts	905,200.00
Increase in Net Assets	2,430,103.19
NET ASSETS	
Net Assets, July 1, 2004	27,878,713.05
Net Assets, June 30, 2005	$ 30,308,816.24

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

Craven Community College
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2005 — *Exhibit A-3*

CASH FLOWS FROM OPERATING ACTIVITIES	
Received from Customers	$ 6,793,380.19
Payments to Employees and Fringe Benefits	(13,034,221.32)
Payments to Vendors and Suppliers	(5,680,560.52)
Payments for Scholarships and Fellowships	(2,245,140.80)
Loans Issued to Students	(39,704.64)
Collection of Loans to Students	42,940.45
Other Receipts	92,411.39
Net Cash Used by Operating Activities	(14,070,895.25)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
State Aid Received	9,870,020.27
County Appropriations	2,629,183.00
Noncapital Grants Received	882,301.14
Noncapital Gifts Received	707,963.38
Cash Provided by Noncapital Financing Activities	14,089,467.79
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
State Capital Aid Received	1,310,854.28
County Capital Appropriations	493,613.00
Capital Grants Received	29,953.42
Capital Gifts Received	35,355.25
Acquisition and Construction of Capital Assets	(1,854,890.40)
Net Cash Provided by Capital and Related Financing Activities	14,885.55
CASH FLOWS FROM INVESTING ACTIVITIES	
Proceeds from Sales and Maturities of Investments	1,622.90
Investment Income	100,291.77
Purchase of Investments and Related Fees	(29,944.60)
Net Cash Provided by Investing Activities	71,970.07
Net Increase in Cash and Cash Equivalents	105,428.16
Cash and Cash Equivalents, July 1, 2004	3,143,918.74
Cash and Cash Equivalents, June 30, 2005	$ 3,249,346.90

RECONCILIATION OF OPERATING LOSS TO NET CASH USED BY OPERATING ACTIVITIES

Operating Loss	$	(15,391,158.43)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:		
Depreciation Expense		1,037,335.43
Provision for Uncollectible Loans and Write-Offs		(3,206.73)
Miscellaneous Nonoperating Income		3,314.23
Changes in Assets and Liabilities:		
Receivables, Net		313,080.23
Inventories		(3,349.43)
Notes Receivable, Net		3,235.81
Accounts Payable and Accrued Liabilities		(28,070.69)
Due to Primary Government		3,538.00
Deferred Revenue		2,195.60
Funds Held for Others		(8,131.32)
Compensated Absences		322.05
Net Cash Used by Operating Activities	$	(14,070,895.25)

RECONCILIATION OF CASH AND CASH EQUIVALENTS

Current Assets:		
Cash and Cash Equivalents	$	233,452.74
Restricted Cash and Cash Equivalents		811,095.87
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		2,204,798.29
Total Cash and Cash Equivalents - June 30, 2005	$	3,249,346.90

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

Assets Acquired through a Gift	$	905,200.00
Change in Fair Value of Investments		62,646.74
Increase in Receivables Related to Nonoperating Income		829,977.49

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

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

A. Financial Reporting Entity - The concept underlying the definition of the financial reporting entity is that elected officials are accountable to their constituents for their actions. As required by accounting principles generally accepted in the United States of America, the financial reporting entity includes both the primary government and all of its component units. An organization other than a primary government serves as a nucleus for a reporting entity when it issues separate financial statements. Craven Community College is a component unit of the State of North Carolina and an integral part of the State's *Comprehensive Annual Financial Report*.

The accompanying financial statements present all funds of the College and component units for which the College's Board of Trustees is financially accountable. The College's component units are blended in the financial statements. The blended component units, although legally separate, are, in substance, part of the College's operations and therefore, are reported as if they were part of the College.

Blended Component Units – Although legally separate, Craven Community College Foundation, Inc., and Public Radio East Foundation are reported as if they were part of the College. The Craven Community College Foundation, Inc., is governed by a 26-member board consisting of two ex officio directors and 24 elected directors. The Foundation's purpose is to aid, support, and promote teaching, research, and service in the various educational, scientific, scholarly, professional, artistic, and creative endeavors of the College. The Public Radio East Foundation is governed by a 21-member board consisting of all elected directors. The Foundation's purpose is to perform the functions of and to carry out the purposes of Public Radio East, a public radio station that is operated as part of Craven Community College. Because the elected directors of both Foundations are appointed by the members of the Craven Community College Board of Trustees and the Foundations' sole purpose is to benefit Craven Community College, their financial statements have been blended with those of the College.

Separate financial statements for the Foundations may be obtained from the College Controller's Office, 800 College Court, New Bern, NC 28562, or by calling (252) 638-7304. Other related foundations and similar nonprofit corporations for which the College is not financially accountable are not part of the accompanying financial statements.

B. **Basis of Presentation** - The accompanying financial statements are presented in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

Pursuant to the provisions of GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments,* as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*, the full scope of the College's activities is considered to be a single business-type activity and accordingly, is reported within a single column in the basic financial statements.

In accordance with GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the College does not apply Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, for proprietary activities, unless the GASB amends its pronouncements to specifically adopt FASB pronouncements issued after that date.

C. **Basis of Accounting** - The financial statements of the College have been prepared using the economic resource measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

D. **Cash and Cash Equivalents –** This classification includes undeposited receipts, petty cash, cash on deposit with private bank accounts, and deposits held by the State Treasurer in the short-term investment portfolio. The short-term investment portfolio maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit and withdraw cash at any time without prior notice or penalty.

E. **Investments** - This classification includes mutual funds held by the College. Investments are accounted for at fair value, as determined by quoted market prices, or an amount determined by management if quoted market prices are not available. The net increase (decrease) in the fair value of investments is recognized as a component of investment income.

F. **Receivables –** Receivables consist of tuition and fees charged to students and charges for auxiliary enterprises' sales and services. Receivables also include amounts due from the federal government, State and local governments, private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants, and pledges that are verifiable, measurable, and expected to be collected and available for expenditures for which the resource provider's conditions have been satisfied. Receivables are recorded net of estimated uncollectible amounts.

G. **Inventories –** Inventories, consisting of expendable supplies, are valued at the lower of cost or market value using the last invoice method. Merchandise for resale is valued using the moving weighted average cost method.

H. **Capital Assets –** Capital assets are stated at cost at date of acquisition or fair value at date of donation in the case of gifts. The College capitalizes assets that have a value or cost in excess of $5,000 at the date of acquisition and an expected useful life of more than one year. Library books are generally not considered to have a useful life of more than one year unless part of a collection and are expensed in the year of acquisition.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 15 to 75 years for general infrastructure, 10 to 50 years for buildings, and 3 to 15 years for equipment.

The College does not capitalize the Godwin Library collection. This collection adheres to the College's policy to maintain for public exhibition, education or research; protect, keep unencumbered, care for and preserve; and requires proceeds from their sale to be used to acquire other collection items. Accounting principles generally accepted in the United States of America permit collections maintained in this manner to be charged to operations at time of purchase rather than be capitalized.

I. **Restricted Assets –** Unexpended capital contributions are classified as restricted assets because their use is limited by donor/grantor agreements. Certain other assets are classified as restricted because their use is limited by external parties or statute.

J. **Noncurrent Long-Term Liabilities –** Noncurrent long-term liabilities include compensated absences that will not be paid within the next fiscal year.

K. Compensated Absences - The College's policy is to record the cost of vacation leave when earned. The policy provides for a maximum accumulation of unused vacation leave of 30 days which can be carried forward each January 1 or for which an employee can be paid upon termination of employment. Also, any accumulated vacation leave in excess of 30 days at year end is converted to sick leave. Under this policy, the accumulated vacation leave for each employee at June 30 equals the leave carried forward at the previous December 31 plus the leave earned, less the leave taken between January 1 and June 30.

In addition to the vacation leave described above, compensated absences includes the accumulated unused portion of the special annual leave bonuses awarded by the College to all full-time permanent employees as of September 30, 2002, and as of July 1, 2003. The unused portion of this leave remains available until used, notwithstanding the limitation on annual leave carried forward described above.

When classifying compensated absences into current and noncurrent, leave is considered taken using a last-in, first-out method.

L. Net Assets – The College's net assets are classified as follows:

Invested in Capital Assets – This represents the College's total investment in capital assets.

Restricted Net Assets – Nonexpendable – Nonexpendable restricted net assets include endowments and similar type assets whose use is limited by donors or other outside sources, and, as a condition of the gift, the principal is to be maintained in perpetuity.

Restricted Net Assets – Expendable – Expendable restricted net assets include resources for which the College is legally or contractually obligated to spend in accordance with restrictions imposed by external parties.

Unrestricted Net Assets – Unrestricted net assets include resources derived from student tuition and fees, sales and services, unrestricted gifts, and interest income.

Restricted and unrestricted resources are tracked using a fund accounting system and are spent in accordance with established fund authorities. Fund authorities provide rules for the fund activity and are separately established for restricted and unrestricted activities. When both restricted and unrestricted funds are available for expenditure, the decision for funding is transactional based within the departmental management system in place at the College.

M. Scholarship Discounts – Student tuition and fees revenues and certain other revenues from College charges are reported net of scholarship discounts in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. The scholarship discount is the difference between the actual charge for goods and services provided by the College and the amount that is paid by students or by third parties on the students' behalf. Student financial assistance grants, such as Pell grants, and other federal, State, or nongovernmental programs, are recorded as either operating or nonoperating revenues in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. To the extent that revenues from these programs are used to satisfy tuition, fees, and other charges, the College has recorded a scholarship discount.

N. Revenue and Expense Recognition – The College classifies its revenues and expenses as operating or nonoperating in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the College's principal ongoing operations. Operating revenues include activities that have characteristics of exchange transactions, such as (1) student tuition and fees, (2) sales and services of auxiliary enterprises, and (3) certain federal, State and local grants and contracts. Operating expenses are all expense transactions incurred other than those related to capital and noncapital financing or investing activities as defined by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*.

Nonoperating revenues include activities that have the characteristics of nonexchange transactions. Revenues from nonexchange transactions and State aid that represent subsidies or gifts to the College, as well as investment income, are considered nonoperating since these are either investing, capital or noncapital financing activities. Capital contributions are presented separately after nonoperating revenues and expenses.

O. County Appropriations - County appropriations are provided to the College primarily to fund its plant operation and maintenance function and to fund construction projects, motor vehicle purchases, and maintenance of equipment. Unexpended county current appropriation and county capital appropriation do not revert and are available for future use by the College.

NOTE 2 - DEPOSITS AND INVESTMENTS

A. Deposits - All funds of the College are deposited in board-designated official depositories and are required to be collateralized in accordance with *North Carolina General Statute* 115D-58.7. Official depositories may be established with any bank or savings and loan association whose principal office is located in North Carolina. Also, the College may establish time deposit accounts, money market accounts, and certificates of deposit. The amount shown on the Statement of Net Assets as cash and cash equivalents includes cash on hand totaling $3,275.00, and deposits in private financial institutions with a carrying value of $0.00 and a bank balance of $560,239.99.

The North Carolina Administrative Code (20 NCAC 7) requires all depositories to collateralize public deposits in excess of federal depository insurance coverage by using one of two methods, dedicated or pooled. Under the dedicated method, a separate escrow account is established by each depository in the name of each local governmental unit and the responsibility of monitoring collateralization rests with the local unit. Under the pooling method, each depository establishes an escrow account in the name of the State Treasurer to secure all of its public deposits. This method shifts the monitoring responsibility from the local unit to the State Treasurer.

Custodial credit risk is the risk that in the event of a bank failure, the College's deposits may not be returned to it. As of June 30, 2005, the College's bank balance in excess of federal depository insurance coverage was covered under the pooling method.

B. Investments – The College is authorized to invest idle funds as provided by G.S. 115D-58.6. In accordance with this statute, the College and the Board of Trustees manage investments to ensure they can be converted into cash when needed.

Generally, funds belonging to the College may be invested in the form of investments pursuant to G.S. 159-30(c), as follows: a commingled investment pool established and administered by the State Treasurer pursuant to G.S. 147-69.3 (STIF), obligations of or fully guaranteed by the United States; obligations of the State of North Carolina; bonds and notes of any North Carolina local government or public authority; obligations of certain nonguaranteed federal agencies; prime quality commercial paper bearing specified ratings and banker's acceptances; The North Carolina Capital Management Trust, an SEC registered mutual fund; repurchase agreements; and evidences of ownership of, or fractional undivided interests in, future interest and principal payments on either direct obligations of or fully guaranteed by the United States government, which are held by a specified bank or trust company or any state in the capacity.

At June 30, 2005, the amount shown on the Statement of Net Assets as cash and cash equivalents includes $3,246,071.90 which represents the College's equity position in the State Treasurer's Short-Term Investment Fund. The Short-Term Investment Fund (a portfolio within the State Treasurer's Investment Pool, an external investment pool that is not registered with the Securities and Exchange Commission and does not have a credit rating) had a weighted average maturity of 1.41 years as of June 30, 2005. Assets and shares of the Short-Term Investment Fund are valued at amortized cost, which approximates fair value. Deposit and investment risks associated with the State Treasurer's Investment Pool (which includes the State Treasurer's Short-Term Investment Fund) are included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page http://www.ncosc.net/ and clicking on "Financial Reports", or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

Except as specified by the donor, endowment funds belonging to the College may be invested pursuant to G.S. 147-69.2. This statute authorizes investments for special funds held by the State Treasurer and includes the following investments: obligations of or fully guaranteed by the United States; obligations of certain federal agencies; repurchase agreements; obligations of the State of North Carolina; certificates of deposit of specified institutions; prime quality commercial paper; specified bills of exchange; asset-backed securities, corporate bonds and notes with specified ratings; general obligations of other states; general obligations of North Carolina local governments; certain venture capital limited partnerships; and the obligations or securities of the North Carolina Enterprise Corporation.

Investments of the College's component units, Craven Community College Foundation, Inc. and Public Radio East Foundation, are subject to and restricted by G.S. 36B "Uniform Management of Institutional Funds Act" (UMIFA) and any requirements placed on them by contract or donor agreements.

The following table presents the fair value of investments at June 30, 2005

Investments

		Fair Value
Investment Type		
Other Securities		
Other Mutual Funds	$	1,180,416.99

Interest Rate Risk: Interest rate risk is defined by GASB Statement No. 40 as the risk a government may face should interest rate variances affect the fair value of investments. The College does not have a formal investment policy that addresses interest rate risk; however, the College's investments were not subject to interest rate risk.

Credit Risk: The College does not have a formal policy that addresses credit risk. As of June 30, 2005, the College's investments were not rated.

Custodial Credit Risk: For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the College will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The College does not have a formal policy for custodial credit risk.

A reconciliation of deposits and investments for the College to the basic financial statements at June 30, 2005, is as follows:

Cash on Hand	$	3,275.00
Investments in the Short Term Investment Fund		3,246,071.90
Other Investments		1,180,416.99
Total Deposits and Investments	$	4,429,763.89
Current:		
Cash and Cash Equivalents	$	233,452.74
Restricted Cash and Cash Equivalents		811,095.87
Noncurrent:		
Restricted Cash and Cash Equivalents		2,204,798.29
Endowment Investments		1,180,416.99
Total	$	4,429,763.89

NOTE 3 - ENDOWMENT INVESTMENTS

Investments of the College's endowment funds are both separately invested and pooled. The College has endowment assets that are pooled with State agencies and similar institutions in short-term investments with the State Treasurer's Cash and Investment Pool and are reported as restricted cash and cash equivalents – noncurrent on the accompanying financial statements. The remainder of the endowment funds are separately invested with Wachovia Investments. If a donor has not provided specific instructions, State law permits the Board of Trustees to authorize for expenditure the net appreciation, realized and unrealized, of the investments of the endowment funds.

Investment return of the College's endowment funds is predicated under classical trust doctrines. Unless the donor has stipulated otherwise, capital gains and losses are accounted for as part of the endowment principal and are not available for expenditure. Annual payouts from the College's endowment funds are based on an adopted spending policy which limits spending to 6% of the endowment principal's market value. Under this policy, the prior year spending percentage is increased by the inflation rate to determine the current year spending percentage. To the extent that the income for the current year exceeds the payout, the excess is added to principal. If current year earnings do not meet the payout requirements, the College uses accumulated income from restricted, expendable net asset endowment balances to make up the difference. At June 30, 2005, net appreciation of $95,988.11 was available to be spent, of which $23,065.53 was restricted to specific purposes.

NOTE 4 - RECEIVABLES

Receivables at June 30, 2005, were as follows:

	Gross Receivables	Less Allowance for Doubtful Accounts	Net Receivables
Current Receivables:			
Students	$ 133,044.82	$ 19,894.85	$ 113,149.97
Accounts	100,371.15		100,371.15
Intergovernmental	183,535.19		183,535.19
Pledges	64,797.17	23,740.29	41,056.88
Investment Earnings	1,758.57		1,758.57
Other	1,547.86		1,547.86
Total Current Receivables	$ 485,054.76	$ 43,635.14	$ 441,419.62
Noncurrent Receivables:			
Intergovernmental	$ 90,000.00	$ 0.00	$ 90,000.00
Investment Earnings	4,798.10		4,798.10
Other	1,068.68		1,068.68
Total Noncurrent Receivables	$ 95,866.78	$ 0.00	$ 95,866.78
Notes Receivable:			
Notes Receivable - Current:			
Institutional Student Loan Programs	$ 6,320.97	$ 3,223.87	$ 3,097.10

NOTE 5 - CAPITAL ASSETS

A summary of changes in the capital assets for the year ended June 30, 2005, is presented as follows:

	Balance July 1, 2004	Adjustments	Increases	Decreases	Balance June 30, 2005
Capital Assets, Nondepreciable:					
Land	$ 596,500.00	$ 0.00	$ 0.00	$ 0.00	$ 596,500.00
Construction in Progress	256,828.37	(304,035.59)	1,255,760.83		1,208,553.61
Total Capital Assets, Nondepreciable	853,328.37	(304,035.59)	1,255,760.83		1,805,053.61
Capital Assets, Depreciable:					
Buildings	20,068,394.09	304,035.59			20,372,429.68
Machinery and Equipment	6,321,032.21		1,178,681.31	50,513.52	7,449,200.00
General Infrastructure	998,924.12		8,196.65		1,007,120.77
Total Capital Assets, Depreciable	27,388,350.42	304,035.59	1,186,877.96	50,513.52	28,828,750.45
Less Accumulated Depreciation:					
Buildings	4,973,148.28		508,408.90		5,481,557.18
Machinery and Equipment	1,428,514.78		493,324.87	50,513.52	1,871,326.13
General Infrastructure	600,257.88		35,601.66		635,859.54
Total Accumulated Depreciation	7,001,920.94		1,037,335.43	50,513.52	7,988,742.85
Total Capital Assets, Depreciable, Net	20,386,429.48	304,035.59	149,542.53		20,840,007.60
Capital Assets, Net	$ 21,239,757.85	$ 0.00	$ 1,405,303.36	$ 0.00	$ 22,645,061.21

NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2005, were as follows:

	Amount
Accounts Payable	$ 72,470.50
Accrued Payroll	236,620.23
Contract Retainage	22,695.40
Other	34,459.72
Total Accounts Payable and Accrued Liabilities	**$ 366,245.85**

NOTE 7 - LONG-TERM LIABILITIES

A summary of changes in the long-term liabilities is presented as follows:

	Balance July 1, 2004	Additions	Reductions	Balance June 30, 2005	Current Portion
Compensated Absences	$ 542,399.25	$ 352,511.51	$ 352,189.46	$ 542,721.30	$ 143,751.81

NOTE 8 - REVENUES

A summary of eliminations and allowances by revenue classification is presented as follows:

	Gross Revenues	Less Scholarship Discounts	Less Allowance for Uncollectibles	Net Revenues
Operating Revenues:				
Student Tuition and Fees	$ 2,852,110.28	$ 509,416.49	$ 19,833.39	$ 2,322,860.40
Sales and Services:				
Sales and Services of Auxiliary Enterprises:				
Food Services	$ 122,393.62	$ 0.00	$ 0.00	$ 122,393.62
Bookstore	1,340,132.87	299,369.83		1,040,763.04
Other	32,893.00			32,893.00
Total Sales and Services	$ 1,495,419.49	$ 299,369.83	$ 0.00	$ 1,196,049.66

NOTE 9 - OPERATING EXPENSES BY FUNCTION

The College's operating expenses by functional classification are presented as follows:

	Personal Services	Supplies and Materials	Services	Scholarships and Fellowships	Utilities	Depreciation	Total
Instruction	$ 7,345,691.35	$ 802,375.96	$ 665,388.29	$ 9,826.20	$ 0.00	$ 0.00	$ 8,823,281.80
Public Service	680,610.88	34,777.47	515,263.61		36,592.84		1,267,244.80
Academic Support	1,395,104.73	81,366.87	71,645.98				1,548,117.58
Student Services	876,542.36	28,174.23	80,589.13				985,305.72
Institutional Support	1,763,398.91	476,143.25	708,727.76	31,701.00			2,979,970.92
Operations and Maintenance of Plant	783,420.98	67,087.25	350,486.02		550,632.74		1,751,626.99
Student Financial Aid			20,194.20	2,227,834.74			2,248,028.94
Auxiliary Enterprises	161,991.24	1,076,369.96	111,439.03				1,349,800.23
Depreciation						1,037,335.43	1,037,335.43
Total Operating Expenses	$ 13,006,760.45	$ 2,566,294.99	$ 2,523,734.02	$ 2,269,361.94	$ 587,225.58	$ 1,037,335.43	$ 21,990,712.41

NOTE 10 - PENSION PLANS

A. Retirement Plans - Each permanent full-time employee, as a condition of employment, is a member of the Teachers' and State Employees' Retirement System. The Teachers' and State Employees' Retirement System (System) is a cost sharing multiple-employer defined benefit pension plan administered by the North Carolina State Treasurer.

Benefit and contribution provisions for the Teachers' and State Employees' Retirement System are established by *North Carolina General Statutes*. 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contribution rates are set each year by the North Carolina General Assembly based on annual actuarial valuations. For the year ended June 30, 2005, these rates were set at 2.17% of covered payroll for employers and 6% of covered payroll for members.

For the year ended June 30, 2005, the College had a total payroll of $11,131,076.35, of which $8,462,259.86 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were $507,733.24 and $183,631.04, respectively. The College made 100% of its annual required contributions for the years ended June 30, 2005, 2004, and 2003, which were $183,631.04, $16,792.52, and $0.00, respectively.

The Teachers' and State Employees' Retirement System's financial information is included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page http://www.osc.state.nc.us/ and clicking on "Financial Reports", or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

B. Deferred Compensation and Supplemental Retirement Income Plans - IRC Section 457 Plan - The State of North Carolina offers its permanent employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457 through the North Carolina Public Employee Deferred Compensation Plan (the Plan). The Plan permits each participating employee to defer a portion of his or her salary until future years. The deferred compensation is available to employees upon separation from service, death, disability, retirement, or financial hardships if approved by the Board of Trustees of the Plan. The Board, a part of the North Carolina Department of Administration, maintains a separate fund for the exclusive benefit of the participating employees and their beneficiaries, *the North Carolina Public Employee Deferred Compensation Trust Fund*. The Board also contracts with an external third party to perform certain administrative requirements and to manage the trust fund's assets. All costs of administering and funding the Plan are the responsibility of the Plan participants. No costs are incurred by the College. The voluntary contributions by employees amounted to $57,748.20 for the year ended June 30, 2005.

IRC Section 401(k) Plan - All members of the Teachers' and State Employees' Retirement System are eligible to enroll in the Supplemental Retirement Income Plan, a defined contribution plan, created under Internal Revenue Code Section 401(k). All costs of administering the Plan are the responsibility of the Plan participants. No costs are incurred by the College except for a 5% employer contribution for the College's law enforcement officers, which is mandated under G.S. 143-166.30(e). Total employer contributions on behalf of College law enforcement officers for the year ended June 30, 2005, were $50.00. The voluntary contributions by employees amounted to $139,036.00 for the year ended June 30, 2005.

IRC Section 403(b) and 403(b)(7) Plans - Eligible College employees can participate in tax sheltered annuity plans created under Internal Revenue Code Sections 403(b) and 403(b)(7). The employee's eligible contributions, made through salary reduction agreements, are exempt from federal and State income taxes until the annuity is received or the contributions are withdrawn. These plans are exclusively for employees of colleges and certain charitable and other nonprofit institutions. All costs of administering and funding these plans are the responsibility of the Plan participants. No costs are incurred by the College. The voluntary contributions by employees amounted to $43,880.00 for the year ended June 30, 2005.

NOTE 11 - OTHER POSTEMPLOYMENT BENEFITS

A. **Health Care for Long-Term Disability Beneficiaries and Retirees** - The College participates in State-administered programs which provide postemployment health insurance to eligible former employees. Eligible former employees include long-term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers' and State Employees' Retirement System. These benefits were established by Chapter 135, Article 3, Part 3, of the General Statutes and may be amended only by the North Carolina General Assembly. Funding for the health care benefit for long-term disability beneficiaries and retirees is financed on a pay-as-you-go basis. The College contributed 3.2% of the covered payroll under the Teachers' and State Employees' Retirement System for these health care benefits. For the fiscal year ended June 30, 2005, the College's total contribution to the Plan was $270,792.32. The College assumes no liability for retiree health care benefits provided by the programs other than its required contribution. Additional detailed information about these programs can be located in the State of North Carolina's *Comprehensive Annual Financial Report*.

B. **Long-Term Disability** - The College participates in the Disability Income Plan of North Carolina (DIPNC). Established by Chapter 135, Article 6, of the General Statutes, DIPNC provides short-term and long-term disability benefits to eligible members of the Teachers' and State Employees' Retirement System. Long-term disability income benefits are advance funded on an actuarially determined basis using the one-year term cost method. The College contributes .445% of covered payroll under the Teachers' and State Employees' Retirement System to the DIPNC. For the year ended June 30, 2005, the College's total contribution to the DIPNC was $37,657.06. The College assumes no liability for long-term disability benefits under the Plan other than its contribution. Additional detailed information about the DIPNC is disclosed in the State of North Carolina's *Comprehensive Annual Financial Report*.

NOTE 12 - RISK MANAGEMENT

The College is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These exposures to loss are handled via a combination of methods, and can include participation in State-administered insurance programs, purchase of commercial insurance, and self-retention of certain risks. There have been no significant reductions in insurance coverage from the previous year and settled claims have not exceeded coverage in any of the past three fiscal years.

Tort claims of up to $500,000 are self-insured under the authority of the State Tort Claims Act. In addition, the State provides excess public officers’ and employees’ liability insurance up to $5,000,000 via contract with a private insurance company. The premium, based on a composite rate, is paid by the North Carolina Community College System Office directly to the private insurer.

Fire and other property losses are covered by contracts with private insurance companies. There have been no significant reductions in insurance coverage from the previous year and settled claims have not exceeded coverage in any of the past three fiscal years.

State-owned vehicles used for instructional purposes are covered by liability insurance handled by the State Department of Insurance. Liability insurance for other College-owned vehicles is covered by contracts with private insurance companies.

The College is protected for losses from employee dishonesty and computer fraud for employees paid in whole or in part from State funds. The blanket honesty bond is with a private insurance company and is handled by the North Carolina Department of Insurance with coverage of $5,000,000 per occurrence and a $50,000 deductible. Losses for employees paid from county and institutional funds are covered under a private insurance policy.

Employees and retirees are provided health care coverage by the Comprehensive Major Medical Plan (Plan), a component unit of the State. The Plan is funded by employer and employee contributions and is administered by a third-party contractor.

The State Board of Community Colleges makes the necessary arrangements to carry out the provisions of the Workers’ Compensation Act which are applicable to employees whose wages are paid in whole or in part from State funds. The College purchases workers’ compensation insurance for employees whose salaries or wages are paid by the Board entirely from county or institutional funds.

Term life insurance of $25,000 to $50,000 is provided to eligible workers. This self-insured death benefit program is administered by the State Treasurer and funded via employer contributions. There were no employer contributions required for the current fiscal year.

Additional details on the State-administered risk management programs are disclosed in the State's *Comprehensive Annual Financial Report*, issued by the Office of the State Controller.

NOTE 13 - COMMITMENTS AND CONTINGENCIES

A. Commitments - The College has established an encumbrance system to track its outstanding commitments on construction projects and other purchases. Outstanding commitments on construction contracts were $1,787,564.00

B. Community College General Obligation Bonds – The 1999-2000 Session of the General Assembly of North Carolina authorized the issuance of $600 million of general obligation bonds of the State, as subsequently approved by a vote of qualified voters of the State, to provide funds for capital improvements for the North Carolina Community College System. The funds authorized are to be used solely to construct new buildings and to renovate and modernize existing buildings on the North Carolina Community College System campuses. The bond legislation specifies the amount of bond funding for each College campus as well as the intended amount for new construction and repair and replacement. The legislation further provides that the State Board of Community Colleges shall be responsible for the approval of projects in accordance with provisions of the legislation. The bonds were authorized for issuance over a six-year period beginning in 2001 at a level not to exceed amounts provided in the legislation. Using a cash flow financing approach, The Community College System's Office (CCSO) establishes annual amounts not to exceed for each approved project. The amounts not to exceed are subject to change due to actual cash availability and needs during the year. Subsequent to the bond sales and the availability of bond proceeds, CCSO notifies the Office of State Budget and Management (OSBM) of the amount not to exceed for the total of the approved projects. Within this amount, based on an official request of cash needs from the State Board of Community Colleges, OSBM authorizes allotments. These allotments are then recorded to specific community college allotment accounts by the CCSO. The College records the allotments as revenue on the accompanying financial statements. The College's remaining authorization of $2,114,946.00 is contingent on future bond sales and CCSO allotment approval. Because of uncertainty and time restrictions the remaining authorization is not recorded as an asset or revenue on the accompanying financial statements.

NOTE 14 - CHANGE IN FINANCIAL ACCOUNTING AND REPORTING

For the fiscal year ended June 30, 2005, the College implemented Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures*. This Statement establishes and modifies disclosure requirements related to investment risks: credit risk, interest rate risk, and foreign currency risk. This statement also establishes and modifies disclosure requirements for deposit risks: custodial credit risk and foreign currency risk.

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STATE OF NORTH CAROLINA
Office of the State Auditor

2 S. Salisbury Street
20601 Mail Service Center
Raleigh, NC 27699-0601
Telephone: (919) 807-7500
Fax: (919) 807-7647
Internet
http://www.ncauditor.net

Leslie W. Merritt, Jr., CPA, CFP
State Auditor

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Board of Trustees
Craven Community College
New Bern, North Carolina

We have audited the financial statements of Craven Community College, a component unit of the State of North Carolina, as of and for the year ended June 30, 2005, and have issued our report thereon dated January 23, 2006.

As discussed in Note 14 to the financial statements, the College implemented Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures*, during the year ended June 30, 2005.

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 College'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 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 we 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 financial reporting that, in our judgment, could adversely affect the College's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the Audit Findings and Recommendations section of this report.

Findings

1. Inadequate Separation of Duties and Management Oversight
2. Access Rights Inconsistent with Adequate Separation of Duties

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS* (CONCLUDED)

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts 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 none of the reportable conditions described above is a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the College's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Board of Trustees, the State Board of Community Colleges, management of the College, the Governor, the State Controller, the General Assembly, 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.

Leslie W. Merritt, Jr.

Leslie W. Merritt, Jr., CPA, CFP
State Auditor

January 23, 2006

AUDIT FINDINGS AND RECOMMENDATIONS

Matters Related to Financial Reporting

The following findings were identified during the current audit and describe conditions that represent significant deficiencies in internal control.

1. INADEQUATE SEPARATION OF DUTIES AND MANAGEMENT OVERSIGHT

The College did not have adequate controls in place to assure proper segregation of duties and proper review and approval procedures. The Controller reconciled all bank accounts; however, there was no further review of upper management. Although the Controller did not have duties involving cash receipting or cash disbursements, she did have access to the general ledger which provided a means of manipulating the system via journal entry as well as access to blank check stock. Because the Controller had access to blank check stock, fraudulent checks could be created and processed outside the College's Financial System without being detected. The Controller maintained a spreadsheet of all cash-in/cash-out details; however, no one else was responsible for reviewing this cash reconciliation spreadsheet.

Recommendation: To ensure proper controls over cash receipts and disbursements, bank reconciliations should be performed on a monthly basis by an employee independent of duties involving cash processing. Management oversight should be involved in the review and approval of completed bank reconciliations.

College's Response: The College has moved the responsibility for bank reconciliations to the Financial Operations Coordinator. This position is now responsible for the monthly reconciliation of all the College accounts. The Controller will provide management oversight by reviewing the reconciliations. In order to ensure that the Financial Operations Coordinator's position does not have duties involving cash receipting or cash disbursements, that position will no longer be involved in reviewing checks prior to disbursement.

2. ACCESS RIGHTS INCONSISTENT WITH ADEQUATE SEPARATION OF DUTIES

The College had granted access rights inconsistent with adequate separation of duties. The Accounts Receivable Assistant was granted several access rights that would allow her the opportunity to perpetrate or conceal errors or fraud. She assisted with preparing third party billings, received third party payments through the mail while not maintaining a mail receipts log, and served as a back-up cashier with capabilities of voiding transactions, closing out her own cash drawer and preparing the daily deposit. Furthermore, she could post journal entries to conceal any other activity not already concealed through the billing and receipting process. This employee could also vouch payments, access the vendor file, print checks, and add new employees to the payroll file.

It was also determined that the Purchasing Agent who grants approval rights for electronic requisitions could force a requisition through the system by circumventing the approval process.

Segregation of duties is a basic internal control that requires assigning different people the responsibilities of authorizing transactions, recording transactions, and maintaining custody of assets to reduce the opportunities to allow any person to be in a position to both perpetrate and conceal errors or fraud in the normal course of his or her duties.

Recommendation: The College should strengthen internal controls by removing cash collection rights from the Accounts Receivable Assistant and removing the ability to circumvent the approval process for requisitions from the Purchasing Agent.

College's Response: The College has moved the responsibility for opening and disbursing the mail to the Financial Operations Coordinator. This position is now responsible for maintaining a log of checks received by the business office through the mail. Those payments would then be directed to the Head Cashier to receipt. In the event the Head Cashier is absent, then one of the other two Accounting Assistants (Accounts Payable or Payroll) would then receipt the funds since the Accounts Receivable Assistant/Backup Cashier would then assume the Head Cashier responsibilities.

Access to set up vendors has been removed from the Accounts Receivable Assistant but would still be available to the Accounts Payable Assistant. A review of the new vendors set up will be done on a monthly basis by the Financial Operations Coordinator.

Access to post journal entries has been removed from the Accounts Receivable Assistant as this was a temporary assignment during the maternity leave of the Financial Operations Coordinator.

Also, the College has initiated running a daily A/R adjustments report that will be verified by the Accountant and reviewed by the Controller.

Void receipts shall be logged and reviewed by the Financial Operations Coordinator on a daily basis.

The responsibility for setting up the purchasing approvals will be moved from the Purchasing Agent to the Computer Services division based on approval by the proper administrator. A printout will be attached to each purchase order showing that the proper approvals were received prior to the creation of the purchase order.

DISTRIBUTION OF AUDIT REPORT

In accordance with General Statutes 147-64.5 and 147-64.6(c)(14), copies of this report have been distributed to the public officials listed below. Additional copies are provided to other legislators, state officials, the press, and the general public upon request.

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Dr. Scott Ralls	President, Craven Community College
Mr. Johnny L. Peterson	Vice President for Financial and Administrative Services Craven Community College
Mr. Donald Brinkley	Chairman, Board of Trustees Craven Community College

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February 21, 2006

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