STATE OF
NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT OF

HALIFAX COMMUNITY COLLEGE

WELDON, NORTH CAROLINA

FOR THE YEAR ENDED JUNE 30, 2005

OFFICE OF THE STATE AUDITOR

LESLIE W. MERRITT, JR., CPA, CFP

STATE AUDITOR

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STATE OF NORTH CAROLINA
Office of the State Auditor

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

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AUDITOR'S TRANSMITTAL

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

We have completed a financial statement audit of Halifax 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.

Special Review – In addition, a separate report has been issued by the Office of the State Auditor related to a concurrent investigation. This report has the following findings:

1. A new employment contract for the President approved without advance notice of significant contract amendments.

2. The President received $12,755.66 in questionable payments for insurance-related fringe benefits.

3. The President received $3,050.48 in questionable travel expense reimbursements.

4. The President's Executive Secretary deleted files from her computer after the College received a cease and desist letter from the State Auditor.

5. The Automotive Tech Instructor performed automotive services for the President's personal vehicle outside of classroom instruction.

6. The President authorized the lease of College property without obtaining approval from the State Board of Community Colleges.

AUDITOR'S TRANSMITTAL (CONCLUDED)

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

June 21, 2006

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Halifax Community College
Weldon, North Carolina

We have audited the accompanying basic financial statements of Halifax 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 Halifax 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 April 19, 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.

INDEPENDENT AUDITOR’S REPORT (CONCLUDED)

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

April 19, 2006

Purpose

The information in this section is intended to provide a general overview of the College's financial statements and is based upon the information contained in the financial statements accompanying this discussion and analysis. The user is encouraged to reference the appropriate section of the financial statements for the supporting detailed information. For more information, please contact the Business Office at 252-536-2551.

Overview of the Financial Statements

Halifax Community College's discussion and analysis provides a summary of the College's financial statements and a comparison of prior year information. Halifax Community College Foundation, Inc. is blended into the financial statements for Halifax Community College. The Foundation had total net assets of $667,361.87 at June 30, 2005.

Institutional Assets

The assets of the College are divided between current and noncurrent assets. Current assets include cash, receivables, inventories, and notes receivable. The large decrease in cash and increase in receivables is due to $239,954.37 spent from federal grants and was due to be reimbursed from the Department of Education through Grant Administration Payment System (GAPS) drawdown.

Current Assets

	2005	2004	Difference
Cash	$ 815,805.00	$ 1,240,296.10	$ (424,491.10)
Short-Term Investments	148,535.87	126,339.06	22,196.81
Receivables	505,770.87	149,816.86	355,954.01
Inventories	148,113.09	135,904.50	12,208.59
Notes Receivable	4,641.45	426.98	4,214.47
Total Current Assets	$ 1,622,866.28	$ 1,652,783.50	$ (29,917.22)

Noncurrent assets include cash, notes receivable, due from the State for construction projects, endowment investments, and capital assets. At June 30, 2004 we were due $150,000.00 from Economic Development Administration (EDA) for construction funds of our Allied Health Building. We finished that construction project, thus the $150,000.00 decrease in receivables. The $437,837.67 decrease in capital assets is due to additions to capital assets being only $136,404.01 and depreciation being $574,241.68.

Noncurrent Assets

	2005	2004	Difference
Cash	$ 106,807.97	$ 13,651.60	$ 93,156.37
Receivables	300.00	150,300.00	(150,000.00)
Due from Primary Govt.	264,354.24	257,456.15	6,898.09
Endowment Investments	468,489.14	460,334.75	8,154.39
Capital Assets	15,182,903.24	15,620,740.91	(437,837.67)
Total Noncurrent Assets	16,022,854.59	16,502,483.41	(479,628.82)
Total Assets	$ 17,645,720.87	$ 18,155,266.91	$ (509,546.04)

The College's capital assets are stated at their purchase price or, in the case of donations, assigned a fair market value when they are accepted. The College records purchases as a capital asset when the purchased items cost more than $5,000.00 at the date of purchase and have a useful life of more than one year. Library books are not included as assets.

The College uses straight-line depreciation to determine the current value of capital assets. In general, infrastructure is depreciated over a 10 to 25 year period, buildings are depreciated over a 15 to 40 year period, and equipment is depreciated in 3 to 15 years, depending on the expected useful life of the infrastructure, equipment, or building. This is done in accordance to the North Carolina Community College System Class Codes and Useful Lives Chart.

Institutional Liabilities

The College's liabilities are divided between current liabilities payable within 12 months and noncurrent liabilities that extend beyond a year. Long-term liabilities include the portion of accrued employee annual leave that will not be paid within the next fiscal year, calculated at the current salary rates for each employee, consistent with the institution's leave policies. Halifax Community College had numerous long-term employees either retire or contracts were not renewed during 2005, thus decreasing our long-term liabilities.

Liabilities

	2005	2004	Difference
Current	$ 98,620.42	$ 205,292.92	$ (106,672.50)
Long-Term	377,044.71	568,926.67	(191,881.96)
Total Liabilities	$ 475,665.13	$ 774,219.59	$ (298,554.46)

Net Assets

Net Assets are a measure of the value of all the College's assets after liabilities and depreciation are deducted. The College's net assets decreased by $210,991.58 for the fiscal year to $17,170,055.74. This decrease is due to the fact that last year we added our new Allied Health Building to capital assets and this year was the first year where depreciation was figured on it. The increase of $255,458.88 in depreciation this year over last year would account for the overall decrease in Net Assets; otherwise we would have stayed basically the same as last year.

Net Assets

	2005	2004	Difference
Invested In Capital Assets	$ 15,182,903.24	$ 15,620,740.91	$ (437,837.67)
Restricted	983,542.62	1,016,918.19	(33,375.57)
Unrestricted	1,003,609.88	743,388.22	260,221.66
Total Net Assets	$ 17,170,055.74	$ 17,381,047.32	$ (210,991.58)

Revenues

The College's revenues are classified as operating and nonoperating revenues. Operating revenues include student tuition and fees, federal, State and local grants and contracts, and the revenue received from sales and services, principally comprised of the revenue received from the bookstore, vending and food service operation. Student tuition, though identified as revenue, is remitted back to the State Treasurer and is not netted against the College's State aid identified as nonoperating revenue. The operating revenue of $3,193,502.97 accrues from the College's participation in the Federal Title IV financial aid programs, including Pell Grants of $3,036,307.00.

Operating Revenues

	2005	2004	Difference
Student Tuition and Fees, Net	$ 750,966.86	$ 740,182.67	$ 10,784.19
Federal Grants and Contracts	3,193,502.97	3,312,297.06	(118,794.09)
State/Local Grants and Contracts	169,910.31	187,091.90	(17,181.59)
Sales and Services, Net	461,101.80	440,451.80	20,650.00
Other Operating Revenues	4,045.45	0.00	4,045.45
Total Operating Revenues	$ 4,579,527.39	$ 4,680,023.43	$ (100,496.04)

Nonoperating revenue comprise the major portion of the College's income and include formula allocations from the North Carolina State Board of Community Colleges for current expense, equipment, and capital improvements as well as funds appropriated from the Halifax and Northampton County Board of Commissioners.

Nonoperating Revenues

	2005	2004	Difference
State Aid	$ 7,176,801.06	$ 6,657,973.85	$ 518,827.21
County Appropriations	1,001,339.00	981,745.00	19,594.00
Noncapital Grants	1,277,240.05	1,553,765.23	(276,525.18)
Noncapital Gifts	102,498.17	76,367.15	26,131.02
Investment Income	53,564.52	49,498.99	4,065.53
Other Nonoperating Revenues	76,562.22	128,933.06	(52,370.84)
Total Nonoperating Revenues	$ 9,688,005.02	$ 9,448,283.28	$ 239,721.74

Capital Contributions

Capital contributions are received from appropriations from the North Carolina State Board of Community Colleges under a formula allocation for educational equipment and library books. The Board also provides construction funds as a part of the North Carolina 2000 Higher Education Bond Referendum and previous legislative action providing funds for renovations and repairs. The decrease in State capital aid and in capital grants resulted from the completion of our Allied Health Building, therefore the reduction of draw downs of the Higher Education Bond Funds.

Capital Contributions

	2005	2004	Difference
State Capital Aid	$ 370,104.36	$ 2,967,606.21	$ (2,597,501.85)
County Capital Aid	32,500.00	32,500.00	0.00
Capital Grants	42,789.04	774,050.00	(731,260.96)
Total Capital Contributions	$ 445,393.40	$ 3,774,156.21	$ (3,328,762.81)

Operating Expenses

The operating expenses of the College are comprised principally of the direct cost of personnel and their fringe benefits.

Operating Expenses

	2005	2004	Difference
Personal Services	$ 9,446,685.99	$ 9,332,611.26	$ 114,074.73
Supplies & Materials	1,464,699.03	1,413,298.61	51,400.42
Services	1,103,112.75	1,289,642.88	(186,530.13)
Scholarship & Fellowships	1,961,554.68	1,988,874.55	(27,319.87)
Utilities	373,623.26	333,039.38	40,583.88
Depreciation	574,241.68	318,782.80	255,458.88
Total Operating Expenses	$ 14,923,917.39	$ 14,676,249.48	$ 247,667.91

Economic Forecast

Halifax Community College believes that the economic future of the College looks very good. We have discussions in progress with our two service counties (Halifax and Northampton) which should address our needs. Although growth has slowed, we still believe that this will turn around and the College will move forward with its mission of serving the students and the community.

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

ASSETS		
Current Assets:		
Cash and Cash Equivalents	$	713,763.83
Restricted Cash and Cash Equivalents		102,041.17
Short-Term Investments		113,918.80
Restricted Short-Term Investments		34,617.07
Receivables, Net (Note 4)		505,770.87
Inventories		148,113.09
Notes Receivable, Net (Note 4)		4,641.45
Total Current Assets		1,622,866.28
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		106,807.97
Restricted Due from Primary Government		264,354.24
Endowment Investments		468,489.14
Notes Receivable (Note 4)		300.00
Capital Assets - Nondepreciable (Note 5)		134,800.00
Capital Assets - Depreciable, Net (Note 5)		15,048,103.24
Total Noncurrent Assets		16,022,854.59
Total Assets		17,645,720.87
LIABILITIES		
Current Liabilities:		
Accounts Payable and Accrued Liabilities (Note 6)		56,784.40
Funds Held for Others		13,300.34
Long-Term Liabilities - Current Portion (Note 7)		28,535.68
Total Current Liabilities		98,620.42
Noncurrent Liabilities:		
Long-Term Liabilities (Note 7)		377,044.71
Total Liabilities		475,665.13
NET ASSETS		
Invested in Capital Assets		15,182,903.24
Restricted for:		
Nonexpendable:		
Scholarships and Fellowships		468,489.14
Expendable:		
Scholarships and Fellowships		72,079.94
Capital Projects		346,728.44
Other		96,245.10
Unrestricted		1,003,609.88
Total Net Assets	$	17,170,055.74

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

Halifax 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)	$	750,966.86
Federal Grants and Contracts		3,193,502.97
State and Local Grants and Contracts		169,910.31
Sales and Services, Net (Note 8)		461,101.80
Other Operating Revenues		4,045.45
Total Operating Revenues		4,579,527.39
EXPENSES		
Operating Expenses:		
Personal Services		9,446,685.99
Supplies and Materials		1,464,699.03
Services		1,103,112.75
Scholarships and Fellowships		1,961,554.68
Utilities		373,623.26
Depreciation		574,241.68
Total Operating Expenses		14,923,917.39
Operating Loss		(10,344,390.00)
NONOPERATING REVENUES		
State Aid		7,176,801.06
County Appropriations		1,001,339.00
Noncapital Grants		1,277,240.05
Noncapital Gifts		102,498.17
Investment Income		53,564.52
Other Nonoperating Revenues		76,562.22
Nonoperating Revenues		9,688,005.02
Loss Before Other Revenues		(656,384.98)
State Capital Aid		370,104.36
County Capital Appropriations		32,500.00
Capital Grants		42,789.04
Decrease in Net Assets		(210,991.58)
NET ASSETS		
Net Assets, July 1, 2004		17,381,047.32
Net Assets, June 30, 2005	$	17,170,055.74

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

Halifax 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	$ 4,317,998.31
Payments to Employees and Fringe Benefits	(9,716,246.20)
Payments to Vendors and Suppliers	(2,979,509.38)
Payments for Scholarships and Fellowships	(1,961,554.68)
Other Receipts	69,219.25
Net Cash Used by Operating Activities	(10,270,092.70)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
State Aid Received	7,176,801.06
County Appropriations	1,001,339.00
Noncapital Grants Received	1,175,917.03
Noncapital Gifts and Endowments Received	102,498.17
Cash Provided by Noncapital Financing Activities	9,456,555.26
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
State Capital Aid Received	370,104.36
County Capital Appropriations	32,500.00
Capital Grants Received	192,789.04
Acquisition and Construction of Capital Assets	(136,404.01)
Net Cash Provided by Capital and Related Financing Activities	458,989.39
CASH FLOWS FROM INVESTING ACTIVITIES	
Proceeds from Sales and Maturities of Investments	236,472.96
Investment Income	53,564.52
Purchase of Investments and Related Fees	(266,824.16)
Net Cash Provided by Investing Activities	23,213.32
Net Decrease in Cash and Cash Equivalents	(331,334.73)
Cash and Cash Equivalents, July 1, 2004	1,253,947.70
Cash and Cash Equivalents, June 30, 2005	$ 922,612.97
RECONCILIATION OF OPERATING LOSS TO NET CASH USED BY OPERATING ACTIVITIES	
Operating Loss	$ (10,344,390.00)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:	
Depreciation Expense	574,241.68
Provision for Uncollectible Loans and Write-Offs	(4,214.47)
Miscellaneous Nonoperating Income	76,562.22
Changes in Assets and Liabilities:	
Receivables, Net	(261,529.08)
Inventories	(12,208.59)
Accounts Payable and Accrued Liabilities	(75,513.82)
Funds Held for Others	(7,342.97)
Compensated Absences	(215,697.67)
Net Cash Used by Operating Activities	$ (10,270,092.70)

RECONCILIATION OF CASH AND CASH EQUIVALENTS

Current Assets:		
Cash and Cash Equivalents	$	713,763.83
Restricted Cash and Cash Equivalents		102,041.17
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		106,807.97
Total Cash and Cash Equivalents - June 30, 2005	$	922,612.97

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

Change in Fair Value of Investments	$	12,144.68
Increase in Receivables Related to Nonoperating Income		6,898.09

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

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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. Halifax 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 the component unit for which the College's Board of Trustees is financially accountable. The College's component unit is blended in the financial statements. The blended component unit, although legally separate, is, in substance, part of the College's operations and therefore, is reported as if it were part of the College.

Blended Component Unit – Although legally separate, Halifax Community College Foundation, Inc., is reported as if it were part of the College. The Foundation is governed by a 16-member board consisting of one ex officio director and 15 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. Because the elected directors of the Foundation are appointed by the members of the Halifax Community College Board of Trustees and the Foundation's sole purpose is to benefit Halifax Community College, its financial statements have been blended with those of the College.

Separate financial statements for the Foundation may be obtained from the College Controller's Office, P.O. Drawer 809, Weldon, NC 27890, or by calling (252) 536-7243. 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 petty cash, cash on deposit with private bank accounts, savings accounts, and money market accounts

E. **Investments –** This classification includes long-term fixed income investments, mutual funds, money market funds and certificates of deposit. Except for money market funds and certificates of deposit, 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 in the fair value of investments is recognized as a component of investment income.

Money market funds and certificates of deposit are reported at cost, if purchased, or at fair value or appraised value at date of gift, if donated.

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, and private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants. Receivables are recorded net of estimated uncollectible amounts.

G. **Inventories** – Inventories, consisting of expendable supplies and merchandise for resale are stated at the lower of cost or market value using the first-in, first-out 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 10 to 25 years for general infrastructure, 15 to 40 years for buildings, and 3 to 15 years for equipment.

The College does not capitalize the Halifax Community College 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 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 $3,015.55, and deposits in private financial institutions with a carrying value of $969,597.42 and a bank balance of $1,064,075.15.

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 – In addition to donated securities held by the College, 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.

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 unit, the Halifax Community College Foundation, Inc., 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 by type and investments subject to interest rate risk at June 30, 2005, for the College's investments. 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.

Investments

		Investment Maturities (in Years)			
	Fair Value	Less Than 1	1 to 5	6 to 10	More than 10
Investment Type					
Debt Securities					
Domestic Corporate Bonds	$ 323,716.25	$ 25,183.25	$ 198,094.00	$ 0.00	$ 100,439.00
Other Securities					
Certificates of Deposit	50,000.00				
Other Mutual Funds	207,073.37				
Corporate Securities	3,719.80				
Other	32,515.59				
Total Investments	$ 617,025.01				

Certificates of deposit reported as investments are also a component of the deposit totals reported in the deposits section of this note.

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

	Fair Value	AAA Aaa	A	Unrated
Domestic Corporate Bonds	$ 323,716.25	$ 198,094.00	$ 75,873.25	$ 49,749.00

Rating Agency: Standard and Poor's

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. At June 30, 2005, the College did not have any investments requiring disclosure of 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	$ 3,015.55
Carrying Amount of Deposits with Private Financial Institutions	969,597.42
Investments reported above excluding certificates of deposit	567,025.01
Total Deposits and Investments	$ 1,539,637.98
Current:	
Cash and Cash Equivalents	$ 713,763.83
Restricted Cash and Cash Equivalents	102,041.17
Short-Term Investments	113,918.80
Restricted Short-Term Investments	34,617.07
Noncurrent:	
Restricted Cash and Cash Equivalents	106,807.97
Endowment Investments	468,489.14
Total	$ 1,539,637.98

NOTE 3 - ENDOWMENT INVESTMENTS

Investments of the College's endowment funds are pooled, unless required to be separately invested by the donor. 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. 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.

NOTE 4 - RECEIVABLES

Receivables at June 30, 2005, were as follows:

	Gross Receivables	Less Allowance for Doubtful Accounts	Net Receivables
Current Receivables:			
Students	$ 100,103.20	$ 69,843.34	$ 30,259.86
Accounts	80,792.81		80,792.81
Intergovernmental	394,718.20		394,718.20
Total Current Receivables	$ 575,614.21	$ 69,843.34	$ 505,770.87
Notes Receivable:			
Notes Receivable - Current:			
Institutional Student Loan Programs	$ 87,474.84	$ 82,833.39	$ 4,641.45
Notes Receivable - Noncurrent:			
Vocational Technical Loan	$ 300.00	$ 0.00	$ 300.00

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	Increases	Balance June 30, 2005
Capital Assets, Nondepreciable:			
Land	$ 134,800.00	$ 0.00	$ 134,800.00
Capital Assets, Depreciable:			
Buildings	18,034,298.66		18,034,298.66
Machinery and Equipment	1,428,646.89	127,412.01	1,556,058.90
General Infrastructure	312,514.35	8,992.00	321,506.35
Total Capital Assets, Depreciable	19,775,459.90	136,404.01	19,911,863.91
Less Accumulated Depreciation:			
Buildings	3,566,442.16	449,215.97	4,015,658.13
Machinery and Equipment	619,130.19	107,266.30	726,396.49
General Infrastructure	103,946.64	17,759.41	121,706.05
Total Accumulated Depreciation	4,289,518.99	574,241.68	4,863,760.67
Total Capital Assets, Depreciable, Net	15,485,940.91	(437,837.67)	15,048,103.24
Capital Assets, Net	$ 15,620,740.91	$ (437,837.67)	$ 15,182,903.24

NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

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

	Amount
Accounts Payable	$ 50,172.74
Accrued Payroll	6,611.66
Total Accounts Payable and Accrued Liabilities	$ 56,784.40

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	$ 621,278.06	$ 23,290.30	$ 238,987.97	$ 405,580.39	$ 28,535.68

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	$ 1,474,289.67	$ 695,669.46	$ 27,653.35	$ 750,966.86
Sales and Services:				
Sales and Services of Auxiliary Enterprises:				
Patron Fees - Cosmetology	$ 28,508.33	$ 0.00	$ 0.00	$ 28,508.33
Esthetician Fees	44.00			44.00
Patron Fees - Child Care	228,908.45		10,875.87	218,032.58
Patron Fees - Dental Hygiene	11,938.50			11,938.50
The Centre	80,875.15			80,875.15
Bookstore	861,966.75	774,104.37	3,423.93	84,438.45
Vending	25,307.17			25,307.17
Wellness Center	5,720.02			5,720.02
Other	6,237.60			6,237.60
Total Sales and Services	$ 1,249,505.97	$ 774,104.37	$ 14,299.80	$ 461,101.80

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	$ 5,086,335.49	$ 425,205.06	$ 408,538.33	$ 10,941.45	$ 0.00	$ 0.00	$ 5,931,020.33
Public Service			65.55	375.00			440.55
Academic Support	1,134,843.09	46,950.12	22,348.13				1,204,141.34
Student Services	1,044,999.12	70,505.81	104,027.01				1,219,531.94
Institutional Support	1,580,903.92	61,011.55	403,836.33				2,045,751.80
Operations and Maintenance of Plant	412,654.15	200,573.10	68,895.86		373,623.26		1,055,746.37
Student Financial Aid		11.33	20,802.03	1,950,238.23			1,971,051.59
Auxiliary Enterprises	186,950.22	660,442.06	74,599.51				921,991.79
Depreciation						574,241.68	574,241.68
Total Operating Expenses	$ 9,446,685.99	$ 1,464,699.03	$ 1,103,112.75	$ 1,961,554.68	$ 373,623.26	$ 574,241.68	$ 14,923,917.39

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 $8,139,364.88, of which $7,020,668.47 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were $421,240.11 and $152,348.51, respectively. The College made 100% of its annual required contributions for the years ended June 30, 2005, 2004, and 2003, which were $152,348.51, $15,080.95, 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 $12,292.84 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. The voluntary contributions by employees amounted to $101,003.28 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 $90,678.50 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 $224,661.39. 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 $31,241.97. 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 the Public School Insurance Fund, a State-administered public entity risk pool. This fund is financed by premiums and interest and incurs a $10 million self-insured deductible per occurrence. Reinsurance is purchased by the fund to cover catastrophic events in excess of the $10 million deductible. 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. Employees paid from county and institutional funds are covered by commercial insurance with coverage of $100,000 and a $1,000 deductible.

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.

Teachers and students are covered for malpractice through HealthCare Providers Services Organization. Students pay $16 per year for coverage, while teachers are covered free. The limits of liability are $2,000,000 each claim and $4,000,000 aggregate.

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. **Pending Litigation and Claims –** On January 13, 2006, the Board of Trustees terminated the contract of the President of the College. The College is negotiating the buyout of his contract and the dollar amount is currently not known. The College has coverage under its commercial general liability insurance policy for any potential liability associated with this matter.

The College is a party to litigation and claims in the ordinary course of its operations. Since it is not possible to predict the ultimate outcome of these matters, no provision for any liability has been made in the financial statements. College management is of the opinion that the liability, if any, for any of these matters will not have a material adverse effect on the financial position of the College.

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 has no remaining authorization.

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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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
Halifax Community College
Weldon, North Carolina

We have audited the financial statements of Halifax 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 April 19, 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.

Finding

1. Access Rights Inconsistent with Adequate Separation of Duties
2. Inadequate Internal Controls Over Bank Reconciliations

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.

<u>Compliance and Other Matters</u>

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, which are reported in the Audit Findings and Recommendations section of this report, disclosed instances of noncompliance that are required to be reported under *Government Auditing Standards.*

Finding

3. Financial Statement Package Not Submitted Within the Statutory Deadline

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

April 19, 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 or noncompliance with laws and regulations.

1. ACCESS RIGHTS INCONSISTENT WITH ADEQUATE SEPARATION OF DUTIES

The College granted access rights inconsistent with adequate separation of duties. The Accounts Payable Clerk had access rights to Accounts Payable and Purchasing system modules. She could create vendor address files, process vouchers, print checks (access to blank check stock), and mail checks. Management did not review any vendor exception reports which would indicate changes to the vendor file. No one outside Accounts Payable reviewed voucher packets against printed checks prior to their release. Nothing precluded the Accounts Payable Clerk from concealing payments for personal purchases and/or manipulating the vendor files.

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. This would reduce the opportunities for 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 either removing the Accounts Payable Clerk's access to the vendor file or reviewing vendor exception reports. The College should also remove the Accounts Payable Clerk's access to blank check stock and independently review all voucher packets against checks prior to their disbursement.

College's Response: The College concurs in the need for a separation of the duties of Accounts Payable and the Purchasing system. Accordingly, management has initiated action to separate these two functions with the expectations that proper internal controls will be in place no later than the end of July 2006. This action should remove the opportunity for improper action by any staff member performing either of the functions.

2. INADEQUATE INTERNAL CONTROLS OVER BANK RECONCILIATIONS

The College did not properly complete reconciliations for the special/federal fund bank account. The bank account was last reconciled in March 2005 and remains unreconciled on a current basis. The College's review was not sufficient to investigate and resolve unreconciled items in the bank reconciliation process. Furthermore, a change in personnel resulted in insufficient staffing to complete the bank reconciliations timely.

Recommendation: For adequate controls over cash, we recommend that the College reconcile bank statements and post reconciling items each month, as bank reconciliations are prepared. Any variances with the general ledger cash balances should be investigated and reconciled in a timely manner. Internal controls should include strengthening the review process to ensure that bank reconciliations are prepared properly and timely.

College's Response: The College concurs that properly completed reconciliations for the special/federal fund bank accounts should have been done on a monthly basis. The required reconciliations have been accomplished and are current as of this date. Management would like for it to be noted that bank reconciliations had never been a finding in previous audits, and the primary affecting factors were another special audit and an investigation that consumed much of the time that should have been used for bank reconciliations. Management is confident controls are now in place that will strengthen the review process.

3. FINANCIAL STATEMENT PACKAGE NOT SUBMITTED WITHIN THE STATUTORY DEADLINE

Halifax Community College submitted its financial statements to the Office of the State Controller after the mandatory date established by General Statute 143-20.1. The June 30, 2005, financial statement package, due within 60 days after year end, was submitted to the Office of the State Controller seven business days after the statutory deadline. The College did not provide formal notes to the financial statements to the Office of the State Auditor until March 29, 2006.

Recommendation: We recommend that the College place greater emphasis on the financial reporting function. Management should allocate adequate resources to the task to ensure timely and accurate reporting.

College's Response: The College concurs that its submission of its financial statements to the Office of the State Controller failed to meet the mandatory date, and the formal notes were late. Again, Management would like for it to be noted that management issues beyond the control of Business Office personnel were contributing factors to the late submission. The College has taken action to ensure that greater emphasis will be place upon future financial reporting functions.

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