STATE OF NORTH CAROLINA

EAST CAROLINA UNIVERSITY

GREENVILLE, NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT

FOR THE YEAR ENDED JUNE 30, 2007

OFFICE OF THE STATE AUDITOR

LESLIE W. MERRITT, JR., CPA, CFP

STATE AUDITOR

East Carolina University

Greenville, North Carolina

Financial Statement Audit Report

For the Year Ended June 30, 2007

Administrative Officers

Dr. Steven C. Ballard, Chancellor

Kevin Seitz, Vice Chancellor for Administration and Finance

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, East Carolina University

We have completed a financial statement and compliance audit of East Carolina University for the year ended June 30, 2007, 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 and our consideration of the University's administration of federal programs in accordance with applicable laws, regulations, contracts and grants disclosed certain deficiencies and/or instances of noncompliance that are detailed in the Audit Findings and Responses section of this report. The University'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

March 10, 2008

TABLE OF CONTENTS

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

Board of Trustees
East Carolina University
Greenville, North Carolina

We have audited the accompanying financial statements of East Carolina University, a constituent institution of the multi-campus University of North Carolina System, which is a component unit of the State of North Carolina, and its discretely presented component unit, as of and for the year ended June 30, 2007, which collectively comprise the University's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the East Carolina University's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of East Carolina University Foundation, Inc., and Consolidated Affiliate, the University's discretely presented component unit. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinions, insofar as they relate to the amounts included for the discretely presented component unit, are based on the report of the other auditors.

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. The financial statements of East Carolina University Foundation, Inc., and Consolidated Affiliate were not audited in accordance with *Government Auditing Standards*. 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 and the report of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of East Carolina University and its discretely presented component unit as of June 30, 2007, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 1, 2008, on our consideration of the University'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 required 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 8, 2008

Introduction

Management's Discussion and Analysis of the financial report provides an overview of the financial position and activities of East Carolina University for the fiscal year ended June 30, 2007, with comparative information for the fiscal year ended June 30, 2006. Management has prepared the discussion and analysis to be read in conjunction with the Notes to Financial Statements, which follow this narrative.

Financial Highlights

The University's net assets increased from $621 million in 2006 to $659 million in 2007. The increase of $38 million represents the residual interest in the assets after liabilities are deducted. This increase is mostly due to an increase in capital reserves and the housing department.

Operating revenues increased from $327 million in 2006 to $366 million in 2007. Revenues represent the amounts received or accrued as operating or nonoperating. The increase of $39 million is represented mostly by an increase in student tuition and fees and patient services.

Operating expenses increased from $570 million in 2006 to $627 million in 2007. Operating expenses represent the amounts paid or accrued for operating purposes. A major part of the $56.4 million increase is due to an increase in instructional expenses, student services, institutional support and auxiliary enterprises.

Using the Financial Statements

The discussion and analysis are intended to serve as an introduction to the basic financial statements. There are three statements included in the University's financial report: the Statement of Net Assets, the Statement of Revenues, Expenses, and Changes in Net Assets, and the Statement of Cash Flows. These financial statements are prepared in accordance with generally accepted accounting principles prescribed by the Governmental Accounting Standards Board (GASB), which establishes standards for external financial reporting for public colleges and universities. The full scope of the University's activities is considered to be a single business-type activity and accordingly, is reported within a single column in the basic financial statements.

Statement of Net Assets

The Statement of Net Assets presents a fiscal snapshot of the University's financial position as of June 30, 2007, and includes all assets and liabilities of the University. Assets and liabilities are classified as either current or noncurrent. The difference between total assets and total liabilities is net assets. Net assets are an indicator of the current financial condition of the University. This data provides information on assets available to continue operations;

amounts due to vendors, investors, and lending institutions; and the net assets available for expenditure by the University. A summarized comparison of the University's assets, liabilities and net assets at June 30, 2007, and 2006 is as follows:

Assets, Liabilities, and Net Assets
(Dollars in Thousands)

	2007	2006	Variance	Percent Change
Assets				
Current Assets	$ 200,466	$ 189,703	$ 10,763	5.7 %
Noncurrent Assets:				
Endowment Investments	17,908	14,410	3,498	24.3 %
Other Long-Term Investments	5,087	7,118	(2,031)	(28.5) %
Capital Assets, Net	582,245	561,517	20,728	3.7 %
Other Noncurrent Assets	37,804	31,529	6,275	19.9 %
Total Noncurrent Assets	643,044	614,574	28,470	4.6 %
Total Assets	843,510	804,277	39,233	4.9 %
Liabilities				
Current Liabilities	48,338	46,147	2,191	4.7 %
Noncurrent Liabilities:				
Funds Held for Others	7,612	7,270	342	4.7 %
Long-Term Liabilities	113,642	114,405	(763)	(0.7) %
Other Noncurrent Liabilities	15,087	15,137	(50)	(0.3) %
Total Noncurrent Liabilities	136,341	136,812	(471)	(0.3) %
Total Liabilities	184,679	182,959	1,720	0.9 %
Net Assets				
Invested in Capital Assets, Net of Related Debt	481,810	454,439	27,371	6.0 %
Restricted:				
Nonexpendable	12,094	10,922	1,172	10.7 %
Expendable	31,728	44,750	(13,022)	(29.1) %
Unrestricted	133,199	111,207	21,992	19.8 %
Total Net Assets	$ 658,831	$ 621,318	$ 37,513	6.0 %

The Statement of Net Assets at June 30, 2007, indicates an improvement of financial position compared to last fiscal year. The University had total assets of $844 million. Current assets increased $11 million to over $200 million. The increase is primarily due to the increase in cash and cash equivalents. One significant factor which resulted in the increase in cash and cash equivalents was the increase of capital reserves in auxiliary funds of $5.5 million. The cash generated by the housing department also increased by $4.7 million. This can be attributed to the increased demand for on-campus housing and operating efficiency.

Noncurrent assets increased $28 million largely because of capital assets. Capital assets increased over $20 million. This increase is mostly attributable to the construction of the College Hill-Phase I project. Endowment investments increased 24.3 percent while other long-term investments decreased 28.5 percent. The main factor causing the increase in endowment investments was capital appreciation on endowment investments of $1.9 million.

Also, contributions to distinguished professorships totaled over $1 million and the contributions for scholarships totaled over $3 million. The decrease in other long-term investments was due to $2.3 million of 2004 Banner COPS proceeds that were spent on Banner implementation.

Current liabilities increased $2 million, 4.7 percent, from last fiscal year. Variable supplemental adjustments of $1.2 million for Medical Faculty Practice Plan employees caused accrued payroll to increase. Other factors causing accrued payroll to increase include salary increases for 9/12 and 10/12 month employees and new positions that were added during the fiscal year. Funds held for others also increased 4.7 percent to $7.6 million. Overall total liabilities had a minimal increase.

Working capital was $152 million at June 30, 2007, an increase of 6 percent, or $8.6 million, over the previous year. Working capital discloses the University's short-term financial health and overall operating efficiency. It is the difference between current assets and current liabilities. The significant factor which resulted in the working capital improvement was an increase in cash and cash equivalents of $13.5 million. As stated earlier, this increase was a result of capital reserves increasing by $5.5 million and of the increase in cash generated by housing of $4.7 million.

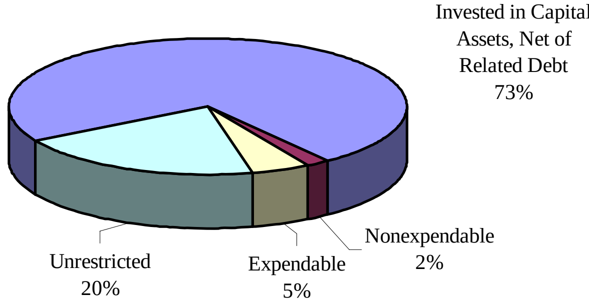
Net assets represent the value of the University's assets after all liabilities have been deducted. The University's net assets were $659 million, an increase of $38 million, or 6 percent, over the prior year. For reporting purposes, net assets are divided into four categories: invested in capital assets, net of related debt; restricted nonexpendable; restricted expendable; and unrestricted net assets.

Invested in capital assets, net of related debt, encompasses the University's capital assets net of accumulated depreciation and the outstanding principal balances of debt resulting from the acquisition, construction or improvement of those assets. Investments in capital assets make up $482 million of the $659 million in net assets. The accumulated depreciation balance as of June 30, 2007, was $197 million.

Restricted nonexpendable net assets primarily include the University's permanent endowment fund, accounting for $12 million of net assets. Restricted expendable net assets are subject to externally imposed restrictions governing its use. This category of net assets made up $32 million of net assets.

Although unrestricted net assets are not subject to externally imposed stipulations, substantially all of the University's unrestricted net assets have been designated for various academic and research programs and initiatives, as well as capital projects. For the fiscal year 2007, unrestricted net assets were $133 million of the $659 million in net assets. There was little change in the makeup of net assets compared to last fiscal year. The following chart displays the contribution of each category to total net assets for 2007.

2007 Net Assets: $658,831,387



Statement of Revenues, Expenses, and Changes in Net Assets

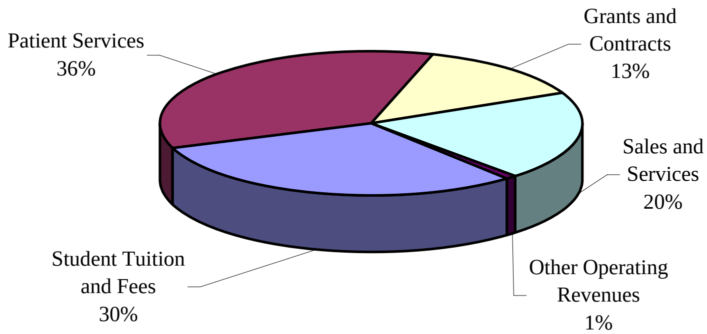
The Statement of Revenues, Expenses, and Changes in Net Assets portrays the University's results of operations and maintenance of financial strength. The Statement of Revenues, Expenses, and Changes in Net Assets as of June 30, 2007, compared with that of 2006, are summarized as follows:

Statement of Revenues, Expenses, and Changes in Net Assets
(Dollars in Thousands)

	2007	2006	Variance	Percent Change
Operating Loss				
Operating Revenues	$ 365,807	$ 327,035	$ 38,772	11.9 %
Operating Expenses	626,522	570,163	56,359	10.0 %
Operating Loss	(260,715)	(243,128)	(17,587)	(7.2) %
Total Nonoperating Revenues	254,442	226,743	27,699	12.2 %
Loss Before Other Revenues	(6,273)	(16,385)	10,112	(61.7) %
Other Revenues	43,786	39,443	4,343	11.0 %
Change in Net Assets	37,513	23,058	14,455	62.7 %
Net Assets - July 1	621,318	598,260	23,058	3.9 %
Change in Net Assets (above)	37,513	23,058	14,455	
Net Assets - June 30	$ 658,831	$ 621,318	$ 37,513	6.0 %

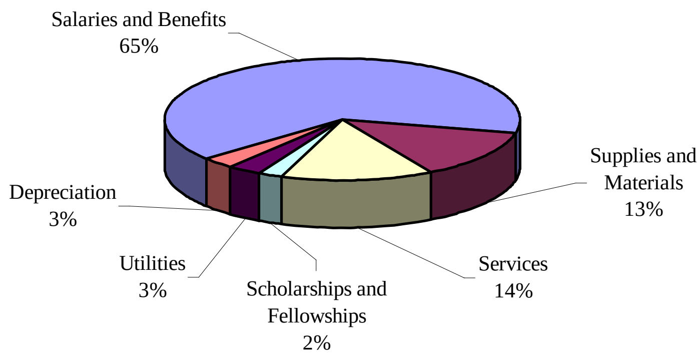
Operating revenues are generated by providing goods and services related to instruction, research, and public service. Total operating revenues increased by $39 million, or 11.9 percent from the prior year. Student tuition and fees, net the tuition discount, increased $12.7 million, or 12.9 percent. The tuition discount is an offset to revenues for the scholarships and fellowships that are applied to student accounts. There were several factors that caused student tuition and fees to increase. Tuition rates increased $200 for undergraduate students and $300 for graduate students for both residents and nonresidents. Mandatory student fees increased by $176, or 11.8 percent. Also, the total enrollment for the University increased by 5 percent. Patient services increased $12.3 million, or 10.5 percent. The following chart shows each component of operating revenue as it relates to total operating revenues as a whole.

2007 Operating Revenues: $365,807,470



Operating expenses are the day-to-day expenses incurred to carry out the mission of the University. Operating expenses increased $56.4 million to $626.5 million. This balance is mainly attributed to salaries and benefits. Salaries and benefits increased $37.5 million to $406 million. This increase is mainly due to the state legislative increases. The following chart shows each component of operating expenses as it relates to total operating expenses as a whole.

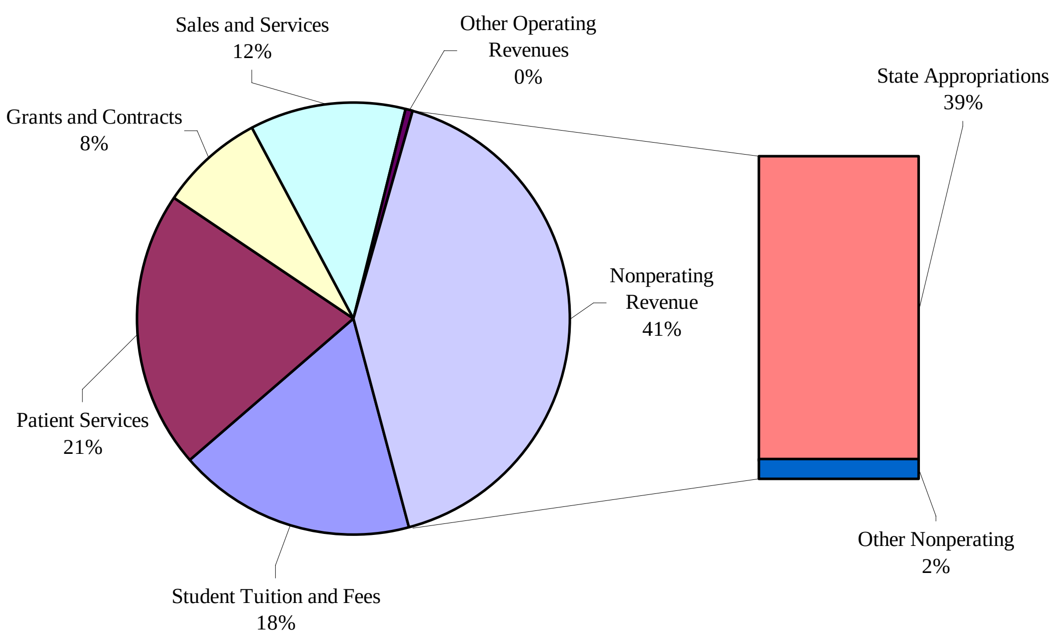
2007 Operating Expenses: $626,521,596



Nonoperating revenues and expenses are not generated by the principal operations of the University. Total nonoperating revenues increased $28 million. State appropriations were the main cause of this increase with an increase of $26 million. Of this amount, $13 million was to cover State legislative salary increases and $10.9 million was for enrollment increases. Nonoperating expenses were mostly comprised of interest and fees on capital asset-related debt.

State appropriations were a significant component of total revenues for the University accounting for 39 percent of total revenue. The following chart illustrates the University's operating and nonoperating revenues which total $625 million for fiscal year 2006-2007.

2007 Total Revenues: $624,917,332



Capital appropriations increased tremendously by 144 percent or $8.8 million. In fiscal year 2006, the total capital appropriations of $6 million were designated for repairs and replacements. In fiscal year 2007, $3 million was designated for the upcoming Dental School, over $1 million was designated for the Flanagan Building, and over $10 million was designated for repairs and replacement allowing the University to enhance and renew its capital assets.

Capital gifts had a significant decrease from 2006 to 2007. This decrease was due to the contribution of $2.6 million made by the ECU Educational Foundation in 2006 for two major projects in the Athletics department.

Statement of Cash Flows

The Statement of Cash Flows provides detail on the cash activity for the year. The sources and uses of cash are categorized as operating, noncapital financing, capital financing or investing. Net cash used is reconciled to the operating income or loss reflected on the Statement of Revenues, Expenses, and Changes in Net Assets. The following is a condensed version of the Statement of Cash Flows for the year ended June 30, 2007, and 2006.

Cash Flows
(Dollars in Thousands)

	2007	2006	Variance	Percent Change
Cash Flows Provided (Used)				
Operating Activities	$ (234,075)	$ (218,867)	$ (15,208)	6.9 %
Noncapital Financing Activities	250,187	225,371	24,816	11.0 %
Capital Financing Activities	(8,795)	(37,037)	28,242	(76.3) %
Investing Activities	10,724	7,679	3,045	39.7 %
Net Change in Cash	18,041	(22,854)	40,895	(178.9) %
Cash - July 1	165,022	187,876	(22,854)	(12.2) %
Cash - June 30	$ 183,063	$ 165,022	$ 18,041	10.9 %

Operating activities are those activities that result from providing goods and services and include the cash effects of transactions that enter into the determination of operating income. This is also the residual category, meaning that it covers transactions that do not fit into any of the other categories. The most significant source of operating cash is amounts received from customers, which increased to $368 million. This includes tuition and fees, grants and contracts, patient services, and sales and services of educational and auxiliary nature. The most notable use of operating cash was for payments to employees and fringe benefits which totaled $401 million.

Noncapital financing activities include state appropriations for operations and noncapital gifts. State appropriations make up $245 million of the $250 million provided from noncapital financing activities. The remaining balance was noncapital gifts.

Capital financing activities include borrowing money for the acquisition, construction, improvement and disposal of capital assets used in providing services or producing goods. This also includes repayments of principal as well as interest. There was significant change in the balance of capital financing activities from the end of fiscal year 2006 to the end of fiscal year 2007. The main sources of capital financing activities were $28 million in capital grants, $19.6 million in proceeds from capital debt, and $13 million from State capital appropriations. The proceeds from capital debt were a sizeable factor of the balance change because in fiscal year 2006, there were no proceeds from capital debt. In fiscal year 2007, a $4 million short-term note and a $3.8 permanent note were issued for financing the College Hill Suite project. Also, there was a refunding of debt for the Student Health Center renovations for $2.1 million and a refunding for Jones Residence Hall and the Galley Dining Facility renovations for $8.8 million. The most significant uses of capital financing activities were $45 million in the acquisition and construction of capital assets and $20.8 million in the principal paid on capital debt and leases.

Investing activities include making and collecting loans and acquiring or disposing of debt or equity instruments. Proceeds from sales and maturities of investments make up $24 million of the $31 million of investing activities sources. The use of these funds was $20 million of purchase of investments and related fees.

Cash increased by $18 million during the fiscal year 2007, compared with a decrease of $22.9 million in fiscal year 2006. The primary factors which caused the increase in cash position were the increase in the amount received by customers and the decrease in the amount used by the acquisition and construction of capital assets.

Capital Assets

A vital aspect for enhancing and maintaining the quality of the University's academic, research, and service programs and its residential life is the acquisition, construction and improvement of its capital assets. The University continues to implement its long-range plan to modernize its complement of older teaching and research facilities, balanced with new construction. This goal has been significantly enhanced by the 2000 Higher Education Bond issue that has provided East Carolina University with $190 million of funding to construct new academic buildings, renovate older facilities and update or replace campus infrastructure. There has been $181.7 million of the 2000 Higher Education Bond funds spent as of June 30, 2007. The major projects are Science and Technology Building; Nursing, Allied Health, and Developmental Evaluation Clinic; Flanagan Building Renovation; and Infrastructure Repairs.

The University had $582 million invested in capital assets at year end. There was a net increase from $562 million from last year, which is mostly attributable to the construction of the College Hill – Phase I project.

Capital assets for the University were comprised of nondepreciable and depreciable assets. Nondepreciable assets were land and construction in progress. Depreciable assets were buildings, machinery and equipment, and general infrastructure. The University 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. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. Buildings and general infrastructure are depreciated over their estimated useful lives, generally 10 to 50 years for buildings and 10 to 75 years for general infrastructure. Machinery and equipment are usually depreciated 2 to 25 years. Most of the University's capital assets are in the form of buildings which have been completed or that are construction in progress.

Capital assets at June 30, 2007, and June 30, 2006, were as follows:

Capital Assets
(Dollars in Thousands)

	2007	2006	Variance	Percent Change
Construction in Progress	$ 55,053	$ 76,682	$ (21,629)	(28.2) %
Land and Other Nondepreciable Assets	26,592	25,865	727	2.8 %
Buildings	567,519	509,871	57,648	11.3 %
General Infrastructure	37,962	37,885	77	0.2 %
Machinery and Equipment	92,438	91,063	1,375	1.5 %
Total Capital Assets	779,564	741,366	38,198	5.2 %
Accumulated Depreciation	197,319	179,850	17,469	9.7 %
Capital Assets, Net	$ 582,245	$ 561,516	$ 20,729	3.7 %

Capital additions consist primarily of replacement, renovation and new construction of capital assets as well as significant investments in equipment, including information technology. Capital additions totaled $46 million. A major component of this was funded from the $2.5 billion Higher Education Bond issue allocated to the University system that was approved by the voters in North Carolina in 2000 and the addition of College Hill-Phase 1.

College Hill-Phase 1 is a five story, 155,000 square foot housing facility with 4-bed suite style rooms with a semi-kitchenette in each suite that was completed in 2007. Each floor has full kitchen and laundry facilities, the ground floor has a lobby and meeting rooms, it has a large outdoor courtyard, and a breezeway connecting the new residence hall to Todd Dining Hall and Tyler Residence Hall.

Another project completed in 2007 was a 17,000 square foot expansion of the Fletcher School of Music on the southwest corner of campus. It will provide rehearsal and practice space as well as an expanded recital hall. The renovated Fletcher will offer three large rehearsal rooms, seven general classrooms, a recording studio, a keyboard laboratory, a computer/keyboard laboratory, an electronic music studio, and a music library. It will also have administrative offices, 48 faculty offices/studios, 50 practice rooms, 23 graduate assistant offices, and larger storage areas. This newly renovated facility will better provide for the growth of the School of Music.

In order to continue to provide quality educational experiences, it is imperative that the University maintains a constant level of growth in regards to capital assets. A plan of this nature will assist the University in avoiding obsolescence and will also provide a marketable tool for attracting more students to the school. Significant capital additions already committed for next fiscal year are depicted below.

Description	Funding Source	Amount in Thousands
Cardiovascular Diseases Inst.	COPS	$ 60,000
Mendenhall/Ledonia Wright	University Revenues	39,000
Dental School	Appropriated	90,000
Brody School of Medicine Family Medical Center	Medical Faculty Practice Plan Revenues/Bond Sales	39,000

The University has several upcoming projects; one being a new dental school. This project will consist of a new, approximately 112,500 square foot building with classrooms, offices, labs and clinical operatories on the Health Science Campus and will include up to ten community based dental clinic sites located through the region. It will focus on getting dental students into the field in underserved areas and poor counties of eastern North Carolina. It is planned that the first class will begin in 2011.

Another project is the Family Medicine Complex. This new building will house both the Family Medicine Center and the Geriatric Clinic. It will include faculty and staff offices, exam rooms, clinic support spaces, teaching rooms, and the required building support functions.

A Coastal Studies Institute will be constructed on 40 acres of land in Manteo, NC. This 90,000 square foot complex will have an academic/administrative area, laboratory area, research plots, and residential facilities.

More detailed information on the University's capital assets is presented in note 5 to the financial statements.

Debt

The University uses bonds, certificates of participation, and capital leases to finance construction projects and purchase equipment. As reflected in the following chart, total bonds, certificates of participation, and capital leases payable decreased by $2.8 million in 2007.

Dollars in Thousands	2007	2006	Change
Revenue Bonds Payable-Fixed Rate	$ 81,820	$ 82,275	$ (455)
Revenue Bonds Payable-Variable Rate	14,460	15,715	(1,255)
Certificates of Participation	6,845	7,695	(850)
Capital Leases Payable	1,115	1,392	(277)
	$ 104,240	$ 107,077	$ (2,837)

The University issued $14.7 million of bonds in November of 2006 to payoff a $4 million short-term note that was issued to fund the remaining amount of construction of the College Hill Dormitory, to refund $2.1 million of the Student Fee Revenue Bonds, Series 1999, and to refund $8.6 million of Housing and Dining System Bonds, Series 2001A. As reflected in note 8E, the refunding saved the University a $469 thousand economic gain in debt service requirements.

In September 2004, Moody's Investors Services rated the University A1 with a positive outlook. The University had a ratings review with Moody's Investors Services in December 2007. The goal of this review is to achieve a higher bond rating, thus decreasing the University's future borrowing costs. A new rating is pending.

Economic Forecast

As indicated in the University's financial statements, the University demonstrated improved financial performance highlighted by a $38 million dollar increase in net assets during the year ended June 30, 2007. The University expects this positive trend to continue. One of the primary reasons for this belief is that the North Carolina General Assembly continues to demonstrate strong support for public higher education. Budgeted state appropriations for the 2007-2008 fiscal year total $262.8 million, an increase of $18.2 million or 7.5 percent. The increased appropriation will be used to fund legislative salary increases of $8.1 million, enrollment increases of $5.2 million, and $2.5 million for indigent patient care for the University's Medical Faculty Practice Plan.

Fiscal year 2008 tuition and fee increases of $96 and $269, respectively, will continue the upward trend in tuition and fee revenues. The University's headcount enrollment increased by 1,639 students, 25,990 students for the Fall 2007 semester as compared with 24,351 students for the Fall 2006 semester. This 6.7 percent increase indicates that demand for the University's instructional services remains strong.

Contacting the University's Financial Management

This financial report is designed to provide our citizens, investors and creditors with a general overview of the University's finances and show accountability for all funds received. If you have any questions or need additional financial information, please contact David Price, Financial Director for East Carolina University, at (252) 737-1140.

East Carolina University
Statement of Net Assets
June 30, 2007 — *Exhibit A-1*

ASSETS		
Current Assets:		
Cash and Cash Equivalents	$	142,304,722.64
Restricted Cash and Cash Equivalents		18,282,429.20
Receivables, Net (Note 4)		32,426,266.02
Due from State of North Carolina Component Units		1,505,000.00
Due from University Component Units		108.50
Inventories		4,635,508.41
Notes Receivable, Net (Note 4)		869,878.65
Other Assets		442,682.89
Total Current Assets		200,466,596.31
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		22,476,327.29
Restricted Due from Primary Government		5,261,952.21
Endowment Investments		17,907,689.18
Other Investments		5,087,616.78
Notes Receivable, Net (Note 4)		10,065,487.73
Capital Assets - Nondepreciable (Note 5)		81,644,705.27
Capital Assets - Depreciable, Net (Note 5)		500,600,217.82
Total Noncurrent Assets		643,043,996.28
Total Assets		843,510,592.59
LIABILITIES		
Current Liabilities:		
Accounts Payable and Accrued Liabilities (Note 6)		30,212,503.33
Due to Primary Government		64,236.46
Unearned Revenue		8,957,164.22
Interest Payable		797,083.19
Long-Term Liabilities - Current Portion (Note 8)		8,307,130.93
Total Current Liabilities		48,338,118.13
Noncurrent Liabilities:		
Deposits Payable		2,490,943.53
Funds Held for Others		7,611,480.64
U. S. Government Grants Refundable		12,596,327.09
Long-Term Liabilities (Note 8)		113,642,336.01
Total Noncurrent Liabilities		136,341,087.27
Total Liabilities		184,679,205.40

NET ASSETS

Invested in Capital Assets, Net of Related Debt		481,809,909.82
Restricted for:		
Nonexpendable:		
Scholarships and Fellowships		1,648,788.84
Endowed Professorships		7,505,283.00
Departmental Uses		327,702.27
Loans		2,612,104.97
Expendable:		
Scholarships and Fellowships		2,863,994.92
Endowed Professorships		1,320,298.97
Departmental Uses		135,024.68
Capital Projects		23,161,407.00
Debt Service		3,144,434.89
Other		1,103,230.68
Unrestricted		133,199,207.15
Total Net Assets	$	658,831,387.19

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

East Carolina University
Statement of Revenues, Expenses, and Changes in Net Assets
For the Fiscal Year Ended June 30, 2007

Exhibit A-2

REVENUES	
Operating Revenues:	
Student Tuition and Fees, Net (Note 10)	$ 111,531,753.47
Patient Services, Net (Note 10)	129,368,358.18
Federal Grants and Contracts	29,934,210.96
State and Local Grants and Contracts	10,675,376.58
Nongovernmental Grants and Contracts	8,274,930.11
Sales and Services, Net (Note 10)	73,272,829.65
Interest Earnings on Loans	30,209.69
Other Operating Revenues	2,719,801.03
Total Operating Revenues	365,807,469.67
EXPENSES	
Operating Expenses:	
Salaries and Benefits	406,117,988.30
Supplies and Materials	80,785,639.54
Services	86,808,778.54
Scholarships and Fellowships	15,045,292.41
Utilities	18,831,484.34
Depreciation	18,932,412.56
Total Operating Expenses	626,521,595.69
Operating Loss	(260,714,126.02)
NONOPERATING REVENUES (EXPENSES)	
State Appropriations	244,548,741.41
Noncapital Gifts	5,638,035.25
Investment Income (Net of Investment Expense of $29,463.76)	8,923,086.14
Interest and Fees on Debt	(4,575,718.77)
Other Nonoperating Expenses	(92,605.44)
Net Nonoperating Revenues	254,441,538.59
Loss Before Other Revenues	(6,272,587.43)
Capital Appropriations	13,031,200.00
Capital Grants	30,487,078.35
Capital Gifts	268,060.26
Increase in Net Assets	37,513,751.18
NET ASSETS	
Net Assets - July 1, 2006	621,317,636.01
Net Assets - June 30, 2007	$ 658,831,387.19

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

East Carolina University
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2007 *Exhibit A-3*

CASH FLOWS FROM OPERATING ACTIVITIES	
Received from Customers	$ 367,779,329.22
Payments to Employees and Fringe Benefits	(401,087,252.29)
Payments to Vendors and Suppliers	(186,602,937.59)
Payments for Scholarships and Fellowships	(15,045,292.41)
Loans Issued	(1,686,504.50)
Collection of Loans	2,641,008.20
Interest Earned on Loans	37,088.50
Student Deposits Received	4,354,341.60
Student Deposits Returned	(4,464,601.84)
Net Cash Used by Operating Activities	(234,074,821.11)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
State Appropriations	244,548,741.41
Noncapital Gifts	5,638,035.25
Cash Provided by Noncapital Financing Activities	250,186,776.66
CASH FLOWS FROM CAPITAL FINANCING AND RELATED FINANCING ACTIVITIES	
Proceeds from Capital Debt	19,554,616.70
State Capital Appropriations	13,031,200.00
Capital Grants	28,266,794.43
Capital Gifts	268,060.26
Proceeds from Sale of Capital Assets	159,466.56
Acquisition and Construction of Capital Assets	(41,451,600.36)
Principal Paid on Capital Debt and Leases	(20,835,799.84)
Interest and Fees Paid on Capital Debt and Leases	(4,519,964.12)
Net Cash Used by Capital Financing and Related Financing Activities	(5,527,226.37)
CASH FLOWS FROM INVESTING ACTIVITIES	
Proceeds from Sales and Maturities of Investments	20,880,101.88
Investment Income	7,049,950.97
Purchase of Investments and Related Fees	(20,473,566.89)
Net Cash Provided by Investing Activities	7,456,485.96
Net Increase in Cash and Cash Equivalents	18,041,215.14
Cash and Cash Equivalents - July 1, 2006	165,022,263.99
Cash and Cash Equivalents - June 30, 2007	$ 183,063,479.13

RECONCILIATION OF NET OPERATING REVENUES (EXPENSES) TO NET CASH USED BY OPERATING ACTIVITIES

Operating Loss	$	(260,714,126.02)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:		
Depreciation Expense		18,932,412.56
Changes in Assets and Liabilities:		
Receivables (Net)		4,332,180.59
Due from State of North Carolina Component Units		(1,000,000.00)
Due from University Component Units		4,873.36
Inventories		(926,416.81)
Accounts Payable and Accrued Liabilities		(135,485.87)
Due to Primary Government		3,166,317.52
Due to State of North Carolina Component Units		341,957.51
Unearned Revenue		42,716.93
Arbitrage Rebate Payable		(1,321,160.21)
Compensated Absences		2,340,285.21
Deposits Payable		(92,879.58)
Note Principal Repayments		2,641,008.20
Notes Issued		(1,686,504.50)
Net Cash Used by Operating Activities	$	(234,074,821.11)

RECONCILIATION OF CASH AND CASH EQUIVALENTS

Current Assets:		
Cash and Cash Equivalents	$	142,304,722.64
Restricted Cash and Cash Equivalents		18,282,429.20
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		22,476,327.29
Total Cash and Cash Equivalents - June 30, 2007	$	183,063,479.13

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

Change in Fair Value of Investments	$	1,873,168.61
Loss on Disposal of Capital Assets		252,072.00

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

East Carolina University Foundation, Inc. and Consolidated Affiliate
Consolidated Statement of Financial Position
June 30, 2007 ***Exhibit B-1***

ASSETS		
Cash and Cash Equivalents	$	6,346
Investments		69,635,376
Investment in Joint Venture		2,784,700
Cash Surrender Value of Life Insurance		166,956
Assets Held in Charitable Trusts and Annuities		1,985,857
Real Estate Held for Investment, Net		625,470
Receivables, Net		8,090,001
Prepaid Expenses		8,062
Total Assets		83,302,768
LIABILITIES		
Accounts Payable and Accrued Expenses		96,068
Due to University and Other Foundations		1,253,592
Funds Held for Others		45,029
Split Interest Agreement Obligations		401,836
Annuities Payable		777,096
Total Liabilities		2,573,621
NET ASSETS		
Unrestricted		10,500,106
Temporarily Restricted		29,266,262
Permanently Restricted		40,962,779
Total Net Assets	$	80,729,147

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

East Carolina University Foundation, Inc. and Consolidated Affiliate
Consolidated Statement of Activities
For the Fiscal Year Ended June 30, 2007 ***Exhibit B-2***

REVENUES, GAINS, AND OTHER SUPPORT	
Contributions	$ 6,459,911
Gifts in Kind	898,723
Contributed Services and Facilities	1,805,646
Interest and Dividends	1,395,521
Net Unrealized and Realized Gains on Investments	8,327,553
Loss on Sale or Transfer of Property	(20,916)
Revaluation of Real Estate	554,700
Change in Value of Split Interest Agreements	365,881
Other Income	325,226
Total Revenues, Gains, and Other Support	20,112,245
EXPENSES AND LOSSES	
Program Services	4,117,606
General and Administrative	609,089
Fund Raising	1,840,280
Bad Debt Losses	51,720
Total Expenses and Losses	6,618,695
Increase Net Assets	13,493,550
NET ASSETS	
Net Assets at Beginning of Year	67,235,597
Net Assets at End of Year	$ 80,729,147

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. East Carolina University is a constituent institution of the multi-campus University of North Carolina System, which 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 belonging to the University and its component units. While the Board of Governors of the University of North Carolina System has ultimate responsibility, the Chancellor, the Board of Trustees, and the Board of Trustees of the Endowment Fund have delegated responsibilities for financial accountability of the University's funds. The University's component units are discretely presented in the University's financial statements. Discretely presented component units' financial data are reported in separate financial statements because of their use of different GAAP reporting models and to emphasize their legal separateness.

Discretely Presented Component Unit – The East Carolina University Foundation, Inc. is a legally separate not-for-profit corporation and is reported as a discretely presented component unit based on the nature and significance of its relationship to the University. The East Carolina University Real Estate Foundation, Inc. is the consolidated affiliate of the East Carolina University Foundation, Inc.

The East Carolina University Foundation, Inc. is a legally separate, tax-exempt component unit of the University. The Foundation acts primarily as a fund-raising organization to supplement the resources that are available to the University in support of its programs. The Foundation board consists of 37 members. Although the University does not control the timing or amount of receipts from the Foundation, the majority of resources, or income thereon, that the Foundation holds and invests are restricted to the activities of the University by the donors. Because these restricted resources held by the Foundation can only be used by, or for the benefit of the University, the Foundation is considered a component unit of the University and is reported in separate financial statements because of the difference in its reporting model, as described below.

The East Carolina University Foundation, Inc. is a private not-for-profit organization that reports its financial results under Financial Accounting Standards Board (FASB) Statements. As such, certain revenue recognition criteria and presentation features are different from the Governmental Accounting Standards Board (GASB) revenue recognition criteria and presentation features. No modifications have been made to the Foundation's financial information in the University's financial reporting entity for these differences.

During the year ended June 30, 2007, the Foundation distributed $4,117,606.00 to the University for both restricted and unrestricted purposes. Complete financial statements for the Foundation can be obtained from the University Financial Services' Office, 120 Reade Street, Greenville, NC 27858, or by calling (252) 737-1133.

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 University'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 University does not apply Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless the GASB amends its pronouncements to specifically adopt FASB pronouncements issued after that date.

C. Basis of Accounting - The financial statements of the University 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, regardless of the timing of the cash flows.

Nonexchange transactions, in which the University receives (or gives) value without directly giving (or receiving) equal value in exchange includes State appropriations, certain grants, and donations. Revenues are recognized, net of estimated uncollectible amounts, as soon as all eligibility requirements imposed by the provider have been met, if probable of collection.

D. Cash and Cash Equivalents – This classification includes undeposited receipts, petty cash, cash on deposit with private bank accounts, money market accounts, cash on deposit with fiscal agents, and deposits held by the State Treasurer in the short-term investment fund. The short-term investment fund 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 fixed income investments, equity investments, mutual funds, money market funds, and limited partnerships. Except for money market funds and limited partnerships, 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.

Money market funds and limited partnerships 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, which include charges for services rendered to patients. 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 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 cost using the first-in, first-out method. Merchandise for resale is valued at the lower of cost or market using the retail inventory 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 value of assets constructed includes all material direct and indirect construction costs. Interest costs incurred are capitalized during the period of construction.

The University capitalizes assets that have a value or cost in excess of $5,000 at the date of acquisition and an estimated 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 and/or units of output method over the estimated useful lives of the assets, generally 10 to 75 years for general infrastructure, 10 to 50 years for buildings, and 2 to 25 years for equipment.

The University does not capitalize library and art collections. These collections adhere to the University'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 proceeds of revenue bonds and unexpended capital contributions are classified as restricted assets because their use is limited by applicable bond covenants or donor/grantor agreements. These assets are also classified as noncurrent since they cannot be used for current operations. 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 principal amounts of bonds payable, capital lease obligations, and compensated absences that will not be paid within the next fiscal year.

Bonds payable are reported net of unamortized premiums or discounts and deferred losses on refunds. The University amortizes bond premiums/discounts over the life of the bonds using the straight-line method. If considered immaterial, the University expenses bond premiums/discounts at the time of issuance. The deferred losses on refunds are amortized over the life of the old debt or new debt (whichever is shorter) using the straight-line method unless considered immaterial. Issuance costs are expensed.

K. **Compensated Absences -** The University'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. When classifying compensated absences into current and noncurrent, leave is considered taken using a last-in, first-out (LIFO) method. 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 include the accumulated unused portion of the special annual leave bonuses awarded by the North Carolina General Assembly. The bonus leave balance on December 31 is retained by employees and transferred into the next calendar year. It is not subject to the limitation on annual leave carried forward described above and is not subject to conversion to sick leave.

There is no liability for unpaid accumulated sick leave because the University has no obligation to pay sick leave upon termination or retirement. However, additional service credit for retirement pension benefits is given for accumulated sick leave upon retirement.

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

Invested in Capital Assets, Net of Related Debt – This represents the University's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of invested in capital assets, net of related debt.

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 University 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, royalties, 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 University. For projects funded by tax-exempt debt proceeds and other sources, the debt proceeds are always used first.

M. **Scholarship Discounts –** Student tuition and fees revenues and certain other revenues from University 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 University 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 University has recorded a scholarship discount.

N. **Revenue and Expense Recognition –** The University 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 University'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, (3) certain federal, State and local grants and contracts that are essentially contracts for services, and (4) interest earned on loans. 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 appropriations that represent subsidies or gifts to the University, 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. Internal Sales Activities – Certain institutional auxiliary operations provide goods and services to University departments, as well as to its customers. These institutional auxiliary operations include activities such as central stores, printing and graphics, motor pool, postal services, and telecommunications. In addition, the University has other miscellaneous sales and service units that operated either on a reimbursement or charge basis. All internal sales activities to University departments from auxiliary operations and sales and service units have been eliminated in the accompanying financial statements. These eliminations are recorded by removing the revenue and expense in the auxiliary operations and sales and service units and, if significant, allocating any residual balances to those departments receiving the goods and services during the year.

NOTE 2 - DEPOSITS AND INVESTMENTS

A. Deposits – Unless specifically exempt, the University is required by *North Carolina General Statute* 147-77 to deposit moneys received with the State Treasurer or with a depository institution in the name of the State Treasurer. In addition, the University of North Carolina Board of Governors, pursuant to G.S. 116-36.1, requires the University to deposit its institutional trust funds, except for funds received for services rendered by health care professionals, with the State Treasurer. Although specifically exempted, the University may voluntarily deposit endowment funds, special funds, revenue bond proceeds, debt service funds, and funds received for services rendered by health care professionals with the State Treasurer. Special funds consist of moneys for intercollegiate athletics and agency funds held directly by the University.

At June 30, 2007, the amount shown on the Statement of Net Assets as cash and cash equivalents includes $182,853,825.68 which represents the University'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 1.6 years as of June 30, 2007. 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.

Cash on hand at June 30, 2007 was $115,225.00. The carrying amount of the University's deposits not with the State Treasurer was $94,428.45 and the bank balance was $211,669.49. Custodial credit risk is the risk that in the event of a bank failure, the University's deposits may not be returned to it. Pursuant to G.S. 116-36.1, funds received for health care services not deposited with the State Treasurer shall be fully secured in the manner as prescribed by the State Treasurer for the security of public deposits. The University does not have a deposit policy for custodial credit risk. As of June 30, 2007, $18,452.65 of the University's bank balances were uninsured and uncollateralized.

B. Investments

University - The University is authorized by The University of North Carolina Board of Governors pursuant to G.S. 116-36.2 and Section 600.2.4 of the Policy Manual of the University of North Carolina, to invest its special funds and funds received for services rendered by health care professionals in the same manner as the State Treasurer is required to invest, as discussed below.

G.S. 147-69.1(c), applicable to the State's General Fund, and G.S. 147-69.2, applicable to institutional trust funds, authorize the State Treasurer to invest in the following: obligations of or fully guaranteed by the United States; obligations of certain federal agencies; repurchase agreements; obligations of the State of North Carolina; time deposits of specified institutions; prime quality commercial paper, and asset-backed securities with specified ratings. Also, G.S. 147-69.1(c) authorizes the following: specified bills of exchange or time drafts and corporate bonds and notes with specified ratings. G.S. 147-69.2 authorizes the following: general obligations of other states; general obligations of North Carolina local governments; and obligations of certain entities with specified ratings.

In accordance with the bond resolutions, bond proceeds and debt service funds are invested in obligations that will by their terms mature on or before the date funds are expected to be required for expenditure or withdrawal.

G.S. 116-36(e) provides that the trustees of the Endowment Fund shall be responsible for the prudent investment of the Fund in the exercise of their sound discretion, without regard to any statute or rule of law relating to the investment of funds by fiduciaries but in compliance with any lawful condition placed by the donor upon that part of the Endowment Fund to be invested.

Investments of the University's component unit, the East Carolina University Foundation, Inc. and Consolidated Affiliate, 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.

Investments are subject to the following risks.

Interest Rate Risk: Interest rate risk is the risk the University may face should interest rate variances affect the fair value of investments. The University's Endowment Board has a formal investment policy that addresses interest rate risk. The policy expects fixed income managers to maintain a duration no greater than +/- 40 percent than that of the Lehman Brothers Aggregate Bond Index.

Credit Risk: Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The University's Endowment Board has a formal policy that addresses credit risk. The policy states that the funds are to be allocated 70 percent equity and equity-like securities and 30 percent fixed income and fixed income substitutes. Each fixed income portfolio must have an overall weighted average credit rating of "A" or better by Moody's and Standard & Poor's rating services. In addition, there shall be no bond investments rated below "B".

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

Concentration of Credit Risk: Concentration of credit risk is the risk of loss attributable to the magnitude of an investment in a single issuer. The University has a formal policy for concentration of credit risk. Each equity and fixed income investment manager must assure that no position of any one issuer shall exceed 8 percent of the manager's portfolio at market value with the exception of securities issued by the U.S. government and its agencies.

The following table presents the fair value of investments by type and investments subject to interest rate risk at June 30, 2007, for the University's investments.

Investments

	Fair Value	Investment Maturities (in Years) Less Than 1	1 to 5	6 to 10
Investment Type				
Debt Securities				
U.S. Treasuries	$ 778,353.31	$ 692,020.23	$ 58,526.55	$ 27,806.53
U.S. Agencies	46,907.60	3,992.52	32,430.65	10,484.43
Mutual Bond Funds	5,984.65			5,984.65
Money Market Mutual Funds	4,476,227.62	4,476,227.62		
		$ 5,172,240.37	$ 90,957.20	$ 44,275.61
Other Securities				
International Mutual Funds	3,248,735.26			
Other Mutual Funds	10,229,913.54			
Hedge Funds	2,718,764.22			
Limited Partnerships	1,274,785.15			
Domestic Stocks	215,634.61			
Total Investments	$ 22,995,305.96			

At June 30, 2007, the University's investments had the following credit quality distribution for securities with credit exposure:

	Fair Value	AAA Aaa
U.S. Agencies	$ 46,907.60	$ 46,907.60
Mutual Bond Funds	5,984.65	5,984.65
Money Market Mutual Funds	4,476,227.62	4,476,227.62

Rating Agency: Moody's / Standard & Poors

At June 30, 2007, the University's investments were exposed to custodial credit risk as follows:

Investment Type	Held by Counterparty	Held by Couterparty's Trust Dept or Agent not in University's Name
U.S. Treasuries	$ 93,353.31	$ 685,000.00
U.S. Agencies	46,907.60	
Domestic Stock	215,634.61	
Total	$ 355,895.52	$ 685,000.00

Component Unit - Investments of the University's discretely presented component unit, the East Carolina University Foundation, Inc. and Consolidated Affiliate, 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. Because the Foundation reports under the FASB reporting model, disclosures of the various investment risks are not required. The following is an analysis of investments by type:

Common Stock	$ 165,763.00
Mutual Funds	54,185,074.00
Limited Partnerships	15,284,539.00
Total	$ 69,635,376.00

NOTE 3 - ENDOWMENT INVESTMENTS

Investments of the University'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 University's endowment funds is predicated on the total return concept (yield plus appreciation). Annual payouts from the University's endowment funds are based on an adopted spending policy which limits spending to 4 percent of the endowment principal's market value. To the extent that the total return for the current year exceeds the payout and a 1 percent administrative fee, the excess is added to principal. If current year earnings do not meet the payout requirements, the University uses accumulated income and appreciation from restricted, expendable net asset endowment balances to make up the difference. At June 30, 2007, net appreciation of $3,997,573.41 was available to be spent, all of which was restricted to specific purposes.

NOTE 4 - RECEIVABLES

Receivables at June 30, 2007, were as follows:

	Gross Receivables	Less Allowance for Doubtful Accounts	Net Receivables
Current Receivables:			
Students	$ 1,910,636.52	$ 412,065.02	$ 1,498,571.50
Patients	62,091,971.85	36,981,785.00	25,110,186.85
Investment Earnings	2,303.92		2,303.92
Interest on Loans	184,401.75		184,401.75
Other	5,630,802.00		5,630,802.00
Total Current Receivables	$ 69,820,116.04	$ 37,393,850.02	$ 32,426,266.02
Notes Receivable - Current:			
Federal Loan Programs	$ 1,515,000.74	$ 667,672.09	$ 847,328.65
Institutional Student Loan Programs	22,550.00		22,550.00
Total Notes Receivable - Current	$ 1,537,550.74	$ 667,672.09	$ 869,878.65
Notes Receivable - Noncurrent:			
Federal Loan Programs	$ 10,065,487.73	$ 0.00	$ 10,065,487.73

NOTE 5 - CAPITAL ASSETS

A summary of changes in the capital assets for the year ended June 30, 2007, is presented as follows:

	Balance July 1, 2006	Increases	Decreases	Balance June 30, 2007
Capital Assets, Nondepreciable:				
Land	$ 25,864,553.59	$ 727,286.84	$ 0.00	$ 26,591,840.43
Construction in Progress	76,682,272.05	37,161,943.15	58,791,350.36	55,052,864.84
Total Capital Assets, Nondepreciable	102,546,825.64	37,889,229.99	58,791,350.36	81,644,705.27
Capital Assets, Depreciable:				
Buildings	509,638,606.94	57,880,987.94		567,519,594.88
Machinery and Equipment	91,296,372.73	9,127,065.33	7,985,629.51	92,437,808.55
General Infrastructure	37,884,720.03	77,293.00		37,962,013.03
Total Capital Assets, Depreciable	638,819,699.70	67,085,346.27	7,985,629.51	697,919,416.46
Less Accumulated Depreciation/Amortization for:				
Buildings	117,849,953.79	10,867,473.97		128,717,427.76
Machinery and Equipment	56,864,491.57	7,027,717.10	1,463,469.46	62,428,739.21
General Infrastructure	5,135,810.18	1,037,221.49		6,173,031.67
Total Accumulated Depreciation	179,850,255.54	18,932,412.56	1,463,469.46	197,319,198.64
Total Capital Assets, Depreciable, Net	458,969,444.16	48,152,933.71	6,522,160.05	500,600,217.82
Capital Assets, Net	$ 561,516,269.80	$ 86,042,163.70	$ 65,313,510.41	$ 582,244,923.09

NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2007, were as follows:

	Amount
Accounts Payable	$ 10,869,270.12
Accrued Payroll	15,184,353.21
Contract Retainage	3,188,630.96
Intergovernmental Payables	935,135.00
Other	35,114.04
Total Accounts Payable and Accrued Liabilities	$ 30,212,503.33

NOTE 7 - SHORT-TERM DEBT

On August 15, 2006, the University issued $4,000,000 of notes payable. The note proceeds were used to complete the College Hill Dormitory Project. On November 30, 2006, the note was refinanced with long-term bonds, the University of North Carolina System Pooled Bonds, Series 2006A.

Short-term debt activity for the year ended June 30, 2007, was as follows:

	Balance July 1, 2006	Draws	Repayments	Balance June 30, 2007
Bond Anticipation Notes	$ 0.00	$ 4,000,000.00	$ 4,000,000.00	$ 0.00

NOTE 8 - LONG-TERM LIABILITIES

A. Changes in Long-Term Liabilities - A summary of changes in the long-term liabilities for the year ended June 30, 2007, is presented as follows:

	Balance July 1, 2006	Additions	Reductions	Balance June 30, 2007	Current Portion
Revenue Bonds Payable	$ 97,990,000.00	$ 14,690,000.00	$ 16,400,000.00	$ 96,280,000.00	$ 5,985,000.00
Certificates of Participation Payable	7,695,000.00		850,000.00	6,845,000.00	875,000.00
Total Bonds and Certificates of Participation Payable	105,685,000.00	14,690,000.00	17,250,000.00	103,125,000.00	6,860,000.00
Capital Leases Payable	1,392,039.58		277,026.31	1,115,013.27	285,346.09
Compensated Absences	15,369,168.46	11,358,767.54	9,018,482.33	17,709,453.67	1,161,784.84
Total Long-Term Liabilities	$ 122,446,208.04	$ 26,048,767.54	$ 26,545,508.64	$ 121,949,466.94	$ 8,307,130.93

Additional information regarding capital lease obligations is included in Note 9.

B. Revenue Bonds Payable and Certificates of Participation - The University was indebted for revenue bonds payable and certificates of participation for the purposes shown in the following table:

Purpose	Series	Interest Rate/ Ranges	Final Maturity Date	Original Amount of Issue	Principal Paid Through June 30, 2007	Principal Outstanding June 30, 2007
Housing and Dining Services						
Residence Hall Renovation-Jarvis	1998	4.00-4.75	11/01/2018	$ 5,095,000.00	$ 1,505,000.00	$ 3,590,000.00
Jones Hall and Gallery Dining Facility Renovation	2001 A	4.25-5.75	11/01/2021	12,570,000.00	9,620,000.00	2,950,000.00
Housing and Dining Revenue Refunding Bonds	2001 B	4.25-5.75	11/01/2015	11,985,000.00	6,330,000.00	5,655,000.00
West End Dining Project	2003 A	2.60-5.00	05/01/2024	14,960,000.00	1,195,000.00	13,765,000.00
Housing HVAC Renovation	2004	variable	05/01/2014	4,290,000.00	1,050,000.00	3,240,000.00
College Hill Dormitory Construction	2004 C	3.00-5.00	06/30/2034	27,530,000.00	1,025,000.00	26,505,000.00
College Hill Dormitory Supplemental Loan	2006 A	4.00-5.00	10/01/2033	3,805,000.00		3,805,000.00
Refunding of Series 2001A Bonds	2006 A	4.00-5.00	10/01/2021	8,775,000.00		8,775,000.00
Total Housing and Dining Services				89,010,000.00	20,725,000.00	68,285,000.00
Student Services System						
Student Health Center	1999	4.75-5.25	05/01/2019	3,500,000.00	3,180,000.00	320,000.00
Student Recreation Center Refunding Bonds	2001 C	3.00-4.75	05/01/5019	14,555,000.00	3,880,000.00	10,675,000.00
University of North Carolina System Pooled Bonds	2004	variable	05/01/2009	1,245,000.00	690,000.00	555,000.00
Refunding of Series 1999 Bonds	2006 A	4.00-5.00	10/01/2018	2,110,000.00		2,110,000.00
Total Student Services System				21,410,000.00	7,750,000.00	13,660,000.00
Athletic Facilities Revenue System						
Athletic Facilities Student Fee Refunding Bonds	2003 A	2.00-4.00	05/01/2009	4,630,000.00	2,985,000.00	1,645,000.00
Dowdy-Ficklen Stadium Expansion Refunding	2004	variable	05/01/2017	5,145,000.00	900,000.00	4,245,000.00
Baseball (Clark-LeClair) Stadium Construction	2004 C	variable	05/01/2024	7,110,000.00	690,000.00	6,420,000.00
Dowdy-Ficklen Stadium Repairs	2004 C	3.00-5.00	06/30/2024	2,530,000.00	505,000.00	2,025,000.00
Total Athletic Facilities Revenue System				19,415,000.00	5,080,000.00	14,335,000.00
University of North Carolina Foundation Certificates of Participation						
Banner System Certificates of Participation	2004	3.00-5.00	06/01/2014	8,875,000.00	2,030,000.00	6,845,000.00
Total Bonds Payable and Certificates of Participation (principal only)				$ 138,710,000.00	$ 35,585,000.00	$ 103,125,000.00

C. Demand Bonds - Included in bonds payable are several variable rate demand bond issues. Demand bonds are securities that contain a "put" feature that allows bondholders to demand payment before the maturity of the debt upon proper notice to the University's remarketing or paying agents.

With regards to the following demand bonds, the University has entered into legal agreements, which would convert the demand bonds not successfully remarketed into another form of long-term debt.

East Carolina University Variable Rate General Revenue Bonds, Series 2004: In 2004 the University issued tax exempt variable rate demand bonds in the amount of $17,790,000.00 that have a final maturity date of May 1, 2024. $14,460,000.00 is outstanding at June 30, 2007. The bonds are subject to mandatory sinking fund redemption that began on May 1, 2005. The proceeds of this issuance were used for (i) renovating three residence halls known as Clement, White, and Greene Residence Halls located on the campus of East Carolina University, (ii) constructing and equipping a new baseball facility located on the

University campus, (iii) refunding in advance of their maturities all of the outstanding East Carolina University Athletic Department Variable Rate Demand Revenue Bonds, Series 1996, the proceeds of which were applied to expanding the Dowdy-Ficklen Stadium located on the University campus, (iv) prepaying the East Carolina University Parking System Revenue Promissory Note dated November 3, 1998, the proceeds of which were used to refinance the construction of a parking lot at Dowdy-Ficklen Stadium located on the University campus, (v) prepaying the East Carolina University Student Fee Revenue Promissory Note dated November 3, 1998, the proceeds of which were used to refinance the improvements to the Blount Intramural Fields Complex located on the University campus, and (vi) paying the costs incurred in connection with the issuance of the 2004 Bonds.

While bearing interest at a weekly rate, the bonds are subject to purchase on demand with seven days' notice and delivery to the bank paying agent, Wachovia Bank, National Association. Upon notice from the bond paying agent, the remarketing agent, US National Bank, National Association, has agreed to exercise its best efforts to remarket the bonds for which a notice of purchase has been received.

Under a Standby Bond Purchase Agreement (Agreement) between the Board of Governors of the University of North Carolina and Wachovia Bank, N.A. a Liquidity Facility has been established for the Trustee (Wachovia Bank, N.A.) to draw amounts sufficient to pay the purchase price and accrued interest on bonds delivered for purchase when remarketing proceeds or other funds are not available. This Agreement required a commitment fee equal to 0.14 percent of the available commitment, payable semiannually in arrears, beginning on November 1, 2004, and on each May 1 and November 1 thereafter until the expiration date or the termination date of the Agreement.

Under the Agreement, any bonds purchased through the Liquidity Facility become Liquidity Provider Bonds and shall, from the date of such purchase and while they are Liquidity Provider Bonds, bear interest at the Liquidity Provider Rate (the greater of the bank prime commercial lending rate and the Bond Interest Rate.) Upon remarketing of Liquidity Provider Bonds and the receipt of the sales price by the Liquidity Provider, such bonds are no longer considered Liquidity Provider Bonds. Payment of the interest on the Liquidity Provider Bonds is due the first business day of each month in which Liquidity Provider Bonds are outstanding. At June 30, 2007, there were no Liquidity Provider Bonds held by the Liquidity Facility. The original Liquidity Facility expired on August 5, 2007, and was extended for an additional three year period ending August 5, 2010.

Upon expiration or termination of the Agreement, the University is required to redeem (purchase) the Liquidity Provider Bonds held by the Liquidity Facility in 10 equal semi-annual installments, beginning the first business day that is at least 180 days following such expiration date or termination date along with accrued interest at the prime rate plus one-half of one percent (1/2%).

D. Annual Requirements - The annual requirements to pay principal and interest on the long-term obligations at June 30, 2007, are as follows:

	Annual Requirements			
	Revenue Bonds Payable		Certificates of Participation	
Fiscal Year	Principal	Interest	Principal	Interest
2008	$ 5,985,000.00	$ 4,172,247.45	$ 875,000.00	$ 264,200.00
2009	6,195,000.00	3,943,095.36	905,000.00	237,950.00
2010	5,290,000.00	3,691,645.03	935,000.00	206,362.50
2011	5,495,000.00	3,489,428.84	970,000.00	168,962.50
2012	5,710,000.00	3,271,408.84	1,005,000.00	133,487.50
2013-2017	26,215,000.00	13,065,953.04	2,155,000.00	127,012.50
2018-2022	20,075,000.00	7,449,456.01		
2023-2027	9,470,000.00	3,956,517.11		
2028-2032	8,070,000.00	2,029,155.00		
2033-2037	3,775,000.00	253,330.00		
Total Requirements	$ 96,280,000.00	$ 45,322,236.68	$ 6,845,000.00	$ 1,137,975.00

Interest on the variable rate 2004 revenue bonds is calculated at 4% at June 30, 2007.
Debt is remarketed, so interest rates fluctuate based on supply and demand.

E. Bond Defeasance - The University has extinguished long-term debt obligations by the issuance of new long-term debt instruments as follows:

On November 30, 2006, the University issued $10,885,000 in The University of North Carolina System Pool Revenue Bonds, Series 2006A refunding bonds with an average interest rate of 4.67%. The bonds were issued to advance refund $2,120,000 of outstanding Student Fee Revenue Bonds, Series 1999, and $8,605,000 of Housing and Dining System Bonds, Series 2001A bonds with an average interest rate of 5.30%. The net proceeds of the refunding bonds were used to purchase U.S. government securities. These securities were deposited into an irrevocable trust to provide for all future debt service payments on the refunded bonds. As a result, the refunded bonds are considered to be defeased and the liability has been removed from the University's Statement of Net Assets. This advance refunding was undertaken to reduce total debt service payments by $685,802.78 over the next 15 years and resulted in an economic gain of $469,351.42. At June 30, 2007, the outstanding balance was $2,120,000.00 for the defeased Student Fee

Revenue Bonds, Series 1999, and $8,605,000 for the Housing and Dining System Bonds, Series 2001A.

NOTE 9 - LEASE OBLIGATIONS

A. Capital Lease Obligations - Capital lease obligations relating to medical equipment are recorded at the present value of the minimum lease payments. Future minimum lease payments under capital lease obligations consist of the following at June 30, 2007:

Fiscal Year	Amount
2008	$ 315,303.52
2009	315,303.52
2010	315,303.52
2011	236,477.64
Total Minimum Lease Payments	1,182,388.20
Amount Representing Interest (2.97% Rate of Interest)	67,374.93
Present Value of Future Lease Payments	$ 1,115,013.27

Machinery and equipment acquired under capital lease amounted to $1,986,174.06 at June 30, 2007.

B. Operating Lease Obligations – The University entered into operating leases for equipment and buildings. Future minimum lease payments under noncancelable operating leases consist of the following at June 30, 2007:

Fiscal Year	Amount
2008	$ 2,404,256.28
2009	1,986,497.98
2010	1,263,884.25
2011	797,583.02
2012	489,334.50
2013-2017	1,023,772.50
2018-2022	34,125.75
Total Minimum Lease Payments	$ 7,999,454.28

Rental expense for all operating leases during the year was $2,709,487.40.

NOTE 10 - REVENUES

A summary of eliminations and allowances by revenue classification and revenues pledged as security for revenue bonds is presented as follows:

	Gross Revenues	Internal Sales Eliminations	Less Scholarship Discounts	Less Allowance for Uncollectibles	Less Indigent Care and Contractual Adjustments	Net Revenues	
Operating Revenues:							
Student Tuition and Fees	$ 123,141,463.02	$ 0.00	$ 11,197,644.53	$ 412,065.02	$ 0.00	$ 111,531,753.47	(B), (C), (D)
Patient Services	$ 329,200,323.15	$ 0.00	$ 0.00	$ 12,764,595.27	$ 187,067,369.70	$ 129,368,358.18	
Sales and Services:							
Sales and Services of Auxiliary Enterprises:							
Residential Life	$ 21,574,665.55	$ 0.00	$ 1,757,250.42	$ 0.00	$ 0.00	$ 19,817,415.13	(A)
Dining	18,283,110.50	751,124.09	1,340,141.77			16,191,844.64	(A)
Student Union Services	19,667.62					19,667.62	
Health, Physical Education, and Recreation Services	2,070,516.13					2,070,516.13	
Bookstore	13,111,810.22					13,111,810.22	
Parking	2,229,076.34					2,229,076.34	
Athletic	10,420,356.75					10,420,356.75	
Other	2,202,275.18					2,202,275.18	
Sales and Services of Education and Related Activities	7,209,867.64					7,209,867.64	
Total Sales and Services	$ 77,121,345.93	$ 751,124.09	$ 3,097,392.19	$ 0.00	$ 0.00	$ 73,272,829.65	

Revenue Bonds Secured by Pledged Revenues:
(A) Housing and Dining System
(B) Student Services System
(C) University of North Carolina Foundation Certificates of Participation
(D) Athletics Facilities Revenues System

NOTE 11 - OPERATING EXPENSES BY FUNCTION

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

	Salaries and Benefits	Supplies and Materials	Services	Scholarships and Fellowships	Utilities	Depreciation	Total
Instruction	$ 194,340,048.95	$ 13,337,486.09	$ 12,954,147.39	$ 0.00	$ 79,009.28	$ 0.00	$ 220,710,691.71
Research	11,802,215.97	3,693,981.62	4,157,968.38	20,355.00	7,175.26		19,681,696.23
Public Service	10,279,266.50	1,327,598.19	2,805,725.59	22,008.34			14,434,598.62
Academic Support	13,903,836.59	8,005,353.46	1,459,233.83	9,429.00	5,659.62		23,383,512.50
Student Services	6,538,140.96	1,076,319.02	2,596,285.33	12,168.00	315.00		10,223,228.31
Institutional Support	27,111,395.19	6,469,741.91	10,694,974.61		121,094.56		44,397,206.27
Operations and Maintenance of Plant	21,540,944.57	15,474,228.40	4,415,892.93		12,591,353.86		54,022,419.76
Student Financial Aid	537,348.95	3,365.57	85,067.95	10,313,145.56			10,938,928.03
Auxiliary Enterprises	120,064,790.62	31,397,565.28	47,639,482.53	4,668,186.51	6,026,876.76		209,796,901.70
Depreciation						18,932,412.56	18,932,412.56
Total Operating Expenses	$ 406,117,988.30	$ 80,785,639.54	$ 86,808,778.54	$ 15,045,292.41	$ 18,831,484.34	$ 18,932,412.56	$ 626,521,595.69

NOTE 12 - PENSION PLANS

A. Retirement Plans - Each permanent full-time employee, as a condition of employment, is a member of either the Teachers' and State Employees' Retirement System or the Optional Retirement Program. Eligible employees can elect to participate in the Optional Retirement Program at the time of employment, otherwise they are automatically enrolled in the Teachers' and State Employees' Retirement System.

The Teachers' and State Employees' Retirement System is a cost sharing multiple-employer defined benefit pension plan established by the State to provide pension benefits for employees of the State, its component units and local boards of education. The plan is 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, 2007, these rates were set at 2.66% of covered payroll for employers and 6% of covered payroll for members.

For the year ended June 30, 2007, the University had a total payroll of $336,688,809.70, of which $152,623,559.84 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were $9,157,413.59 and $4,059,786.70, respectively. The University made 100% of its annual required contributions for the years ended June 30, 2007, 2006, and 2005, which were $4,059,786.70, $3,225,529.47, and $2,712,065.41, 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.ncosc.net/ and clicking on "Financial Reports," or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

The Optional Retirement Program (Program) is a defined contribution retirement plan that provides retirement benefits with options for payments to beneficiaries in the event of the participant's death. Administrators and eligible faculty of the University may join the

Program instead of the Teachers' and State Employees' Retirement System. The Board of Governors of The University of North Carolina is responsible for the administration of the Program and designates the companies authorized to offer investment products. The Board has authorized the following carriers: Teachers' Insurance and Annuity Association - College Retirement Equities Fund (TIAA-CREF), Lincoln Life Insurance Company, Variable Annuity Life Insurance Company (VALIC), and Fidelity Investments. Participants may elect to allocate their contributions and the University contributions to the carrier of their choice. Each carrier offers a variety of investment funds, including both fixed and variable account investment options and mutual funds.

Participants in the Program are immediately vested in the value of employee contributions. The value of employer contributions is vested after five years of participation in the Program. Participants become eligible to receive distributions when they terminate employment or retire.

Participant eligibility and contributory requirements are established by General Statute 135-5.1. Employer and member contribution rates are set each year by the North Carolina General Assembly. For the year ended June 30, 2007, these rates were set at 6.84% of covered payroll for employers and 6% of covered payroll for members. The University assumes no liability other than its contribution.

For the year ended June 30, 2007, the University had a total payroll of $336,688,809.70, of which $143,421,993.17 was covered under the Optional Retirement Program. Total employee and employer contributions for pension benefits for the year were $ 8,605,319.59 and $9,810,064.33, respectively.

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 University. The voluntary contributions by employees amounted to $2,098,742.44 for the year ended June 30, 2007.

IRC Section 401(k) Plan - All members of the Teachers' and State Employees' Retirement System and the Optional Retirement Program 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 University except for a 5% employer contribution for the University's law enforcement officers, which is mandated under General Statute 143-166.30(e). Total employer contributions on behalf of University law enforcement officers for the year ended June 30, 2007, were $118,334.41. The voluntary contributions by employees amounted to $1,613,120.72 for the year ended June 30, 2006.

IRC Section 403(b) and 403(b)(7) Plans - Eligible University 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 universities 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 University. The voluntary contributions by employees amounted to $7,116,978.60 for the year ended June 30, 2007.

NOTE 13 - OTHER POSTEMPLOYMENT BENEFITS

A. **Health Care for Long-Term Disability Beneficiaries and Retirees** - The University participates in State-administered programs that provide post employment 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 or the Optional Retirement Program. 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 University contributed 3.8% of the covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program for these health care benefits. For the fiscal year ended June 30, 2007, the University's total contribution to the Plan was $11,249,731.02. The University 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. Disability Income - The University 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 and the Optional Retirement Program. Long-term disability income benefits are advance funded on an actuarially determined basis using the one-year term cost method. The University contributes .52% of covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the DIPNC. For the year ended June 30, 2007, the University's total contribution to the DIPNC was $1,539,436.88. The University 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 14 - RISK MANAGEMENT

The University 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, including 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 University pays the premium, based on a composite rate, directly to the private insurer.

The University is required to maintain fire and lightning coverage on all State-owned buildings and contents through the State Property Fire Insurance Fund (Fund), an internal service fund of the State. Such coverage is provided at no cost to the University for operations supported by the State's General Fund. Other operations not supported by the State's General Fund are charged for the coverage. Losses covered by the Fund are subject to a $500 per occurrence deductible.

The University also purchased through the Fund extended coverage on fifty-four buildings, sprinkler leakage coverage on twelve buildings, vandalism on two buildings, flood coverage on four buildings, and all-risk coverage on three buildings. Losses covered by the Fund are subject to a $500 per occurrence deductible. Extended coverage against losses caused by windstorm or hail, explosion, smoke, aircraft or vehicle, riot or civil commotion is provided on University buildings by the Fund and its reinsurer with a deductible of $500 per occurrence where coverage is purchased.

All State-owned vehicles are covered by liability insurance through a private insurance company and handled by the North Carolina Department of Insurance. The liability limits for losses occurring in-State are $500,000 per claim and $5,000,000 per occurrence and out-of-State are $1,000,000 per claim and $5,000,000 per occurrence. The University pays premiums to the North Carolina Department of Insurance for the coverage.

The University is protected for losses from employee dishonesty and computer fraud. This coverage is with a private insurance company and is handled by the North Carolina Department of Insurance. Universities are charged a premium by the private insurance company. Coverage limit is $5,000,000 per occurrence with a $75,000 deductible and a 10% participation in each loss above the deductible.

University employees and retirees are provided comprehensive major medical care benefits. Coverage is funded by contributions to the State Health Plan (Plan), a pension and other employee benefit trust fund of the State of North Carolina. The Plan has contracted with third parties to process claims.

The North Carolina Workers' Compensation Program provides benefits to workers injured on the job. All employees of the State and its component units are included in the program. When an employee is injured, the University's primary responsibility is to arrange for and provide the necessary treatment for work related injury. The University is responsible for paying medical benefits and compensation in accordance with the North Carolina Workers' Compensation Act. The University is self-insured for workers' compensation.

The University provides medical malpractice insurance for faculty physicians and independently licensed allied health providers (Nurse Practitioners, Certified Registered Nurse Anesthetists, Certified Nurse Midwives, and Physician Assistants). The medical malpractice is with a private insurance company with coverage of $3,000,000 per occurrence, $5,000,000 aggregate, and a $200,000 deductible, as well as an excess policy in the amount of

$10,000,000. As part of the medical malpractice insurance agreement, the University was required to establish a $1,000,000, non-cancelable letter of credit. There have been no draws against this letter of credit to date.

Term life insurance (death benefits) of $25,000 to $50,000 is provided to eligible workers. This Death Benefit Plan is administered by the State Treasurer and funded via employer contributions. The employer contribution rate was .16% 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 15 - COMMITMENTS AND CONTINGENCIES

A. Commitments - The University has established an encumbrance system to track its outstanding commitments on construction projects and other purchases. Outstanding commitments on construction contracts were $46,749,516.32 and on other purchases were $14,916,972.48 at June 30, 2007.

B. Pending Litigation and Claims – The University 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. University 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 University.

C. Other Contingent Receivables – The University has received notification of other gifts and grants for which funds have not been disbursed by the resource provider and for which conditions attached to the gift or grant have not been satisfied or, in the case of permanent endowments, cannot begin to be satisfied. In accordance with accounting principles generally accepted in the United States of America, these amounts have not been recorded on the accompanying financial statements. The purpose and amount of other contingent receivables at year end is as follows:

Purpose	Amount
General Obligation Bonds	$ 5,751,133.00

NOTE 16 - RELATED PARTIES

Foundations - There are three separately incorporated nonprofit foundations associated with the University. These foundations are the East Carolina University Educational Foundation, Inc., the East Carolina University Medical and Health Sciences Foundation, Inc, and the East Carolina University Alumni Association, Inc.

These organizations serve as the primary fundraising arm of the University through which individuals, corporations, and other organizations support University programs by providing scholarships, fellowships, faculty salary supplements, and unrestricted funds to specific colleges and the University's overall academic environment. The University's financial statements do not include the assets, liabilities, net assets, or operational transactions of the foundations, except for support from each organization to the University.

The East Carolina University Educational Foundation, Inc. provided $1,232,224.43 for construction projects and $4,250,555.26 to the Department of Athletics in primary support of student athlete scholarships. The Medical Foundation of East Carolina University, Inc. provided indirect support to the University by distributing funds directly to recipients. The East Carolina University Alumni Association, Inc. provides support for the graduates of the University. The activities of the above Foundations are not included in the accompanying financial statements.

[This Page Left Blank Intentionally]

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

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
East Carolina University
Greenville, North Carolina

We have audited the financial statements of East Carolina University, a constituent institution of the multi-campus University of North Carolina System, which is a component unit of the State of North Carolina, and its discretely presented component unit as of and for the year ended June 30, 2007, which collectively comprise the University's basic financial statements and have issued our report thereon dated January 8, 2008. Our report was modified to include a reference to other auditors.

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. Other auditors audited the financial statements of the discretely presented component unit, as described in our report on the University's financial statements. The financial statements of the discretely presented component unit were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the University's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the University's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the University's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the University's financial statements that is more than inconsequential will not be prevented or detected by the University's internal control. We consider the deficiency described in finding 1 in the Audit Findings and Responses section of this report to be significant deficiency in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the University's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that the significant deficiency described above is not a material weakness.

<u>Compliance and Other Matters</u>

As part of obtaining reasonable assurance about whether the University'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*.

The University's responses to the findings identified in our audit are described in the Audit Findings and Responses section of this report. We did not audit the University's response and, accordingly, we express no opinion on it.

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)

This report is intended solely for the information and use of management of the University, the Board of Governors, the Board of Trustees, the Audit Committee, the Governor, the General Assembly, and the State Controller, 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 8, 2008

[This Page Left Blank Intentionally]

Matters Related to Financial Reporting or Federal Compliance Objectives

The following audit findings were identified during the current audit and describe conditions that represent significant deficiencies in internal control or noncompliance with laws, regulations, contracts, grant agreements or other matters.

1. ESTIMATED USEFUL LIFE OF CAPITAL ASSETS NEEDS TO BE RE-EVALUATED

   The University has not periodically evaluated the appropriateness of the estimated useful lives of its capital assets. After we requested that the University perform such an evaluation, staff identified an estimated overstatement of accumulated depreciation of approximately $6.6 million.

   When the University implemented GASB 34/35, it used the suggested Office of the State Controller useful lives of assets but has not adjusted those suggested guidelines based on actual experience. A periodic review of useful lives is necessary to ensure that costs are allocated based on actual use of the assets.

   Recommendation: The University should establish and implement procedures to ensure that the useful lives of capital asset classes are periodically re-evaluated.

   University Response: The University will implement procedures to periodically study and re-evaluate the useful lives of its capital asset classes.

2. LACK OF ACCOUNTABILITY FOR EQUIPMENT PURCHASED WITH FEDERAL RESEARCH AND DEVELOPMENT FUNDS

   The University did not perform a complete physical inventory of equipment purchased with research and development grant funds and reconcile counts to its equipment records. The OMB Circular A-133 Compliance Supplement requires that a physical inventory of equipment purchased with federal funds be taken at least every two years and the results reconciled with equipment records.

   Two departments purchased equipment with research and development funds and did not complete and return the equipment inventory listing as required. According to equipment records, one department held six pieces of equipment purchased with federal funds totaling $29,165, and the other department held five pieces of equipment purchased with federal funds totaling $108,955. We also noted that these same departments failed to return signed equipment listings in the 2006 fiscal year. Total equipment dollars examined was $473,215, which resulted in a total error rate of 29%.

   Recommendation: The University should ensure the departments improve their controls over capital assets and comply with applicable federal requirements.

University Response: The Office of Grants and Contracts will work with Materials Management/Fixed Assets (Administration & Finance) to ensure that the departments are in compliance with applicable State and federal requirements regarding fixed assets.

ORDERING INFORMATION

Audit reports issued by the Office of the State Auditor can be obtained from the web site at www.ncauditor.net. Also, parties may register on the web site to receive automatic email notification whenever reports of interest are issued. Otherwise, copies of audit reports may be obtained by contacting the:

Office of the State Auditor
State of North Carolina
2 South Salisbury Street
20601 Mail Service Center
Raleigh, North Carolina 27699-0601

Telephone: 919/807-7500

Facsimile: 919/807-7647