STATE OF NORTH CAROLINA

ELIZABETH CITY STATE UNIVERSITY

ELIZABETH CITY, 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

ELIZABETH CITY STATE UNIVERSITY

ELIZABETH CITY, NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT

FOR THE YEAR ENDED JUNE 30, 2007

STATE OF NORTH CAROLINA
Office of the State Auditor

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

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AUDITOR'S TRANSMITTAL

The Honorable Michael F. Easley, Governor
The General Assembly of North Carolina
Board of Trustees, Elizabeth City State University

We have completed a financial statement audit of Elizabeth City State 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 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

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Elizabeth City State University
Elizabeth City, North Carolina

We have audited the accompanying basic financial statements of Elizabeth City State University, a constituent institution of the multi-campus University of North Carolina System, which is a component unit of the State of North Carolina, as of and for the year ended June 30, 2007, as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the financial statements of Elizabeth City State University Foundation, Inc. and Subsidiary, which represent seven percent, six percent, and four percent, respectively, of the assets, net assets and revenues of the University. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for the foundation, is 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. 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 the other auditors provide a reasonable basis for our opinion.

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 financial position of Elizabeth City State University as of June 30, 2007, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 27, 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

June 27, 2008

Elizabeth City State University prepared its financial statements in accordance with Governmental Accounting Standards Board (GASB) Statement Number 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended by GASB Statement Number 35, *Basic Financial Statements - and Management's Discussion and Analysis - for Public Colleges and Universities.* The standards require three basic financial statements: the Statement of Net Assets, the Statement of Revenues, Expenses, and Changes in Net Assets, and the Statement of Cash Flows.

The Statement of Net Assets includes all assets and liabilities. The University's net assets (the difference between assets and liabilities) are one indicator of the University's financial health. Over time, increases or decreases in net assets are indicators of the improvement or erosion of the University's financial health when considered with nonfinancial facts such as enrollment levels and the condition of the facilities.

The Statement of Net Assets provides information about assets and liabilities in a format that distinguishes between current and noncurrent. Individual assets and liabilities are classified as current or noncurrent based on whether they are expected to generate or use cash within the next 12 months after the end of the fiscal period.

Net assets, or the difference between total assets and total liabilities, are divided into three major components. The first component, invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages or notes that are attributable to the acquisition, construction, or improvement of those assets. The next component, restricted net assets, is divided into two categories: expendable and nonexpendable. Net assets are restricted when constraints are placed on them by either external parties (creditors, grantors, donors, etc.) or by enabling legislation or constitutional provisions. Nonexpendable net assets are those that are required to be retained in perpetuity. The final component is unrestricted net assets. These are net assets that are available to the University for any lawful purpose of the University.

The Statement of Revenues, Expenses and Changes in Net Assets represents the revenues earned and expenses incurred during the year. Activities are reported as either operating or nonoperating. All things being equal, a public university's dependency on state appropriations and gifts will result in operating deficits, because GASB Statement No.35 classifies state appropriations and gifts as nonoperating revenues.

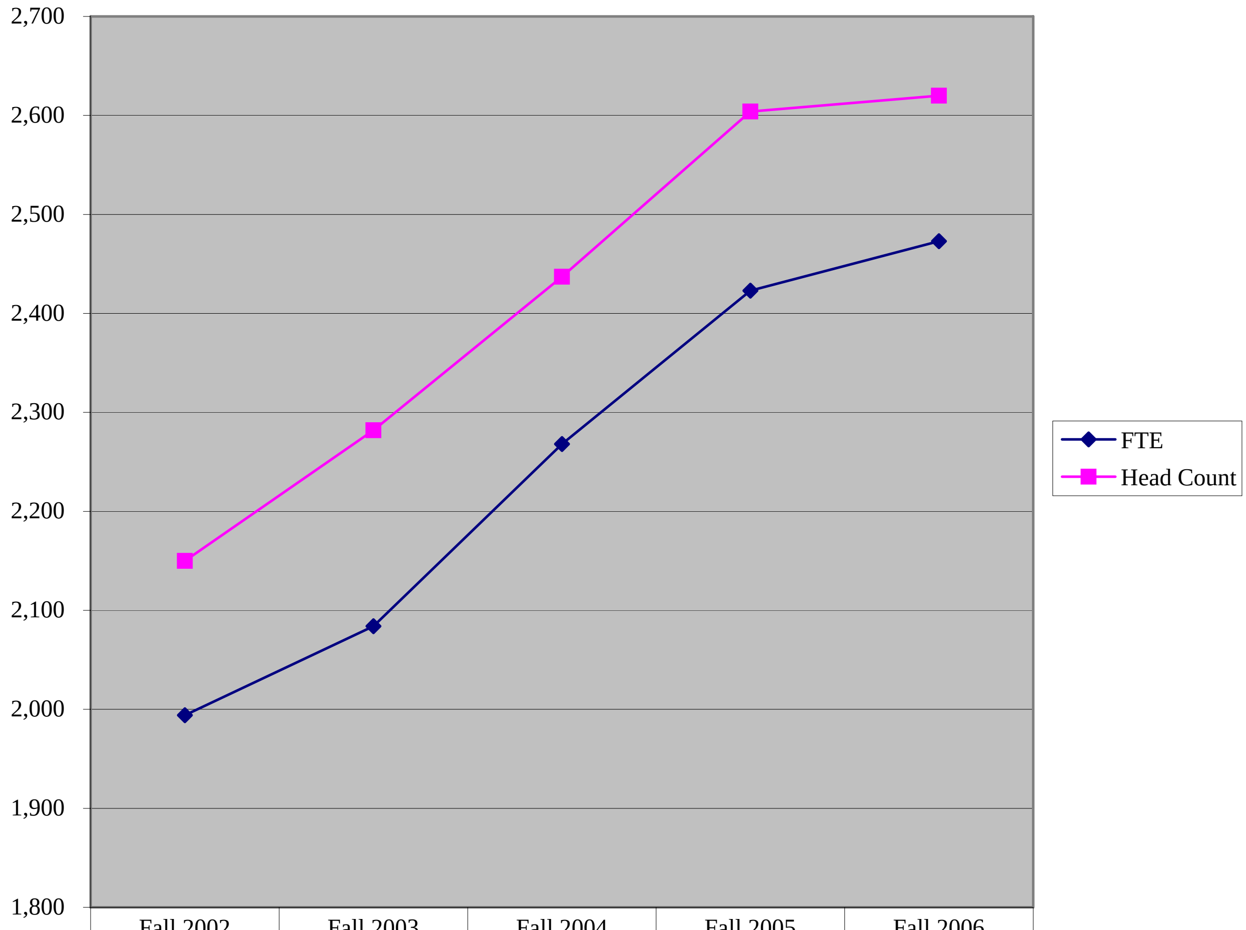
The Statement of Revenues, Expenses and Changes in Net Assets distinguishes between operating and nonoperating revenues and expenses. Operating revenues and expenses generally result from providing goods and services and the cost of providing those goods and services. Nonoperating revenues are revenues received for which goods and services are not provided. This includes state appropriations for operating and capital purposes.

Another important factor to consider when evaluating financial viability is the University's ability to meet financial obligations as they occur. The Statement of Cash Flows presents information related to cash inflows and outflows summarized by operating, noncapital financing, capital and related financing and investing activities.

The following discussion and analysis provides an overview of the University's financial activities.

Enrollment increased from 2,604 students in Fall 2005 to 2,620 in Fall 2006 based on headcount.

FTE and Head Count from Fall 2002 to Fall 2006



	Fall 2002	Fall 2003	Fall 2004	Fall 2005	Fall 2006
FTE	1,994	2,084	2,268	2,423	2,473
Head Count	2,150	2,282	2,437	2,604	2,620

Comparative, Condensed Statement of Net Assets

	2007	2006	% Change
Assets			
Current Assets	$ 13,862,596	$ 16,227,858	(7.0) %
Capital Assets, Net	98,066,670	97,228,504	0.9 %
Other Assets	12,321,095	10,922,611	1.5 %
Total Assets	124,250,361	124,378,973	(0.1) %
Liabilities			
Current Liabilities	17,912,383	17,743,099	1.0 %
Noncurrent Liabilities	8,302,618	8,799,890	(5.7) %
Total Liabilities	26,215,001	26,542,989	(1.2) %
Net Assets			
Invested in Capital Assets, Net of Related Debt	79,142,483	77,720,753	1.8 %
Restricted - Expendable	8,102,086	9,911,719	(18.3) %
Restricted - Nonexpendable	4,975,181	3,151,597	57.9 %
Unrestricted	5,815,610	7,051,915	(17.5) %
Total Net Assets	$ 98,035,360	$ 97,835,984	0.2 %

As of June 30, 2007, total University assets were $124.2 million. Buildings, less accumulated depreciation, make up $79 million of this total. The University's current construction in progress is $6 million.

University liabilities totaled $26 million at June 30, 2007. Bonds payable totaling $19 million is the largest liability.

Comparative, Condensed Statement of Revenues, Expenses, and Changes in Net Assets

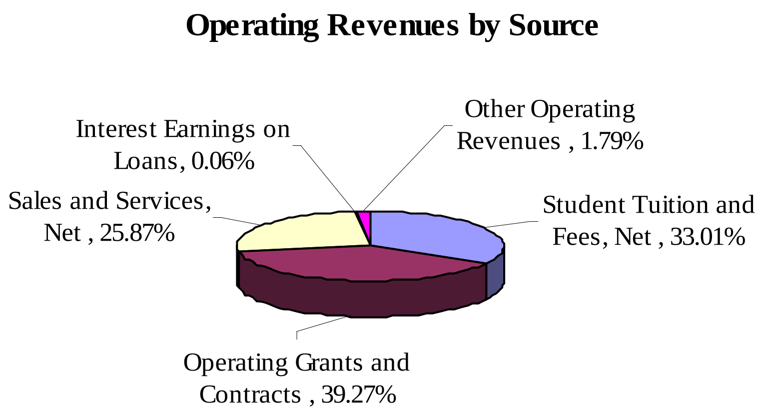
	2007	2006	% Change
Operating Revenues			
Student Tuition and Fees, Net	$ 6,622,149	$ 5,451,006	21.5 %
Federal Contracts and Grants	7,851,886	5,821,534	34.9 %
Sales and Services, Net	5,189,472	4,418,913	17.4 %
Other Operating Revenues	397,901	480,166	(17.1) %
Total Operating Revenues	20,061,409	16,171,619	24.1 %
Operating Expenses	64,127,311	58,034,146	10.5 %
Operating Loss	(44,065,903)	(41,862,527)	5.3 %
Nonoperating Revenues and Expenses:			
State Appropriations	31,793,997	29,569,866	7.5 %
Noncapital Grants	6,139,463	6,872,123	(10.7) %
Other Nonoperating Revenues	1,389,625	2,230,071	(37.7) %
Interest and Fees on Debt	(998,054)	(985,744)	1.2 %
Net Nonoperating Revenues	38,325,031	37,686,316	1.7 %
Loss Before Other Revenues	(5,740,872)	(4,176,211)	37.5 %
Capital Appropriations	3,114,300	1,375,800	126.4 %
Capital Grants	4,307,674	4,338,780	(0.7) %
Additions to Permanent Endowment	100,952	157,293	(35.8) %
Total Other Revenues	7,522,926	5,871,873	28.1 %
Increase in Net Assets	1,782,054	1,695,662	5.1 %
Net Assets at the Beginning of Year	97,835,984	96,140,322	1.8 %
Restatements	(1,582,679)		
Net Assets at the End of the Year	$ 98,035,360	$ 97,835,984	0.2 %

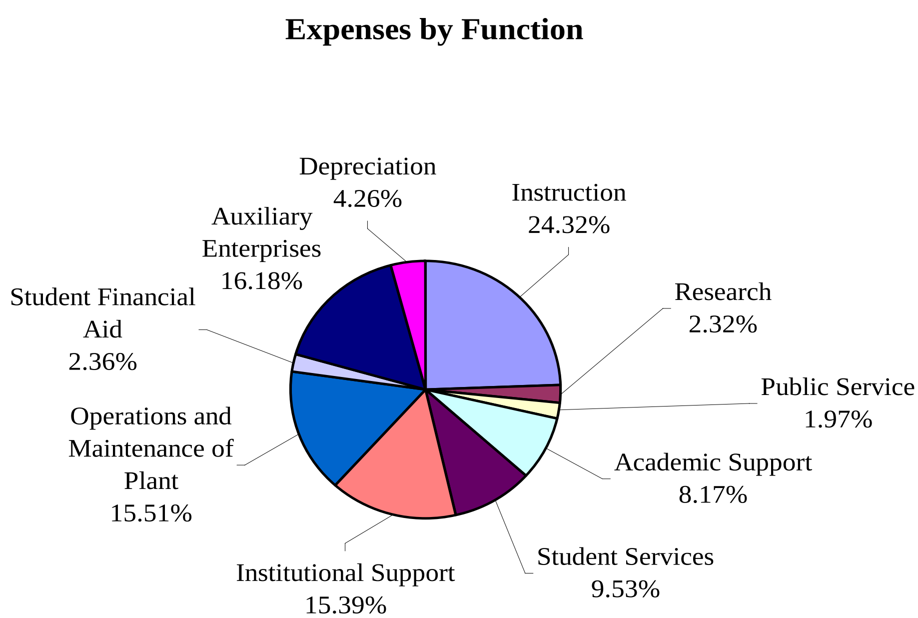
Tuition and fees, net of scholarship allowances, increased by $1,171,143 over the prior year. This increase was due to an increase in tuition and fees charged to students, as well as a small increase in enrollment. Federal Contracts and Grants increased by $2,030,352 over the prior year. This increase was due to more faculty writing grants, which led to an increase in grants awarded to the University.

Operating Expenses increased by $6 million. This increase was due to legislative increases in salaries and corresponding benefits totaling $4.2 million. Capital Appropriations reflect a $1,738,500 increase due to increased funding from the State of North Carolina.

Total operating loss for fiscal year 2007 was $44 million. Since the State of North Carolina appropriation is not included within operating revenue per GASB Statement No. 35, the University will show an operating loss.

The sources of operating revenue for the University include tuition and fees, certain grants and contracts, and auxiliary services.





Capital Asset and Long-Term Debt Activity

The UNC Higher Education Bond Referendum projects were well under way with $42,863,106 expended of the University's total allotment of $46.8 million. Major capital expenditures for the year ended June 30, 2007 include the Lane Hall Renovation of $1,880,086; Johnson Renovation of $305,807; Mitchell-Lewis Renovation of $255,038; Electrical Distribution System Upgrade of $286,454; and the Technology Infrastructure of $189,430. Furthermore, no new debt was issued during the year ended June 30, 2007.

The amount recorded as current bonds payable reflects the recording of Viking Village bond series as a current liability. The bond agreement includes a requirement that was not met which allows bond trustee to require the acceleration of the bond payments. This will be corrected in future years and the University does not anticipate having to pay the full amount of the bond principal in the current year.

Economic Outlook

The economic environment has shown signs of modest growth. The University's net assets grew from $97.8 million to $98 million over the fiscal year ending June 30, 2007.

Enrollment increased from 2,604 students in Fall 2005 to 2,620 in Fall 2006 based on headcount. The University expects enrollment to continue to increase.

Elizabeth City State University
Statement of Net Assets
June 30, 2007 *Exhibit A-1*

ASSETS		
Current Assets:		
Cash and Cash Equivalents	$	2,703,611.08
Restricted Cash and Cash Equivalents		3,178,639.88
Restricted Short-Term Investments		1,143,425.86
Receivables, Net (Note 4)		5,314,077.33
Due from Primary Government		163,435.54
Due from State of North Carolina Component Units		92,595.04
Inventories		1,187,040.60
Notes Receivable (Note 4)		79,770.51
Total Current Assets		13,862,595.84
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		3,883,480.60
Restricted Due from Primary Government		1,356,326.94
Endowment Investments		3,465,530.38
Other Investments		1,619,257.18
Notes Receivable, Net (Note 4)		760,703.70
Bond Issuance Costs		1,235,797.03
Capital Assets - Nondepreciable (Note 5)		8,430,622.38
Capital Assets - Depreciable, Net (Note 5)		89,636,047.19
Total Noncurrent Assets		110,387,765.40
Total Assets		124,250,361.24
LIABILITIES		
Current Liabilities:		
Accounts Payable and Accrued Liabilities (Note 6)		2,785,529.67
Due to Primary Government		4,145.28
Unearned Revenue		1,137,502.45
Interest Payable		119,270.86
Long-Term Liabilities - Current Portion (Note 7)		13,865,934.37
Total Current Liabilities		17,912,382.63
Noncurrent Liabilities:		
Deposits Payable		273,133.17
Funds Held for Others		83,834.58
U. S. Government Grants Refundable		704,278.52
Long-Term Liabilities (Note 7)		7,241,371.92
Total Noncurrent Liabilities		8,302,618.19
Total Liabilities		26,215,000.82

NET ASSETS		
Invested in Capital Assets, Net of Related Debt		79,142,482.89
Restricted for:		
Nonexpendable:		
Scholarships and Fellowships		3,448,698.48
Endowed Professorships		1,526,482.95
Expendable:		
Scholarships and Fellowships		1,460,040.03
Endowed Professorships		166,721.44
Loans		146,905.12
Capital Projects		3,899,809.97
Debt Service		2,428,609.50
Unrestricted		5,815,610.04
Total Net Assets	$	98,035,360.42

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

Elizabeth City State 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 9)	$	6,622,149.25
Federal Grants and Contracts		7,851,886.31
State and Local Grants and Contracts		17,731.93
Nongovernmental Grants and Contracts		8,818.14
Sales and Services, Net (Note 9)		5,189,471.91
Interest Earnings on Loans		12,204.44
Other Operating Revenues		359,147.63
Total Operating Revenues		20,061,409.61
EXPENSES		
Operating Expenses:		
Salaries and Benefits		37,198,604.97
Supplies and Materials		5,884,898.01
Services		14,077,809.84
Scholarships and Fellowships		1,506,400.99
Utilities		2,535,107.49
Depreciation		2,924,489.85
Total Operating Expenses		64,127,311.15
Operating Loss		(44,065,901.54)
NONOPERATING REVENUES (EXPENSES)		
State Appropriations		31,793,996.73
Noncapital Grants		6,139,463.07
Noncapital Gifts, Net (Note 9)		523,073.31
Investment Income (Net of Investment Expense of $29,865.00)		836,524.81
Interest and Fees on Debt		(998,054.09)
Other Nonoperating Revenues		30,026.45
Net Nonoperating Revenues		38,325,030.28
Income Before Other Revenues, Expenses, Gains, or Losses		(5,740,871.26)
Capital Appropriations		3,114,300.00
Capital Grants		4,307,674.28
Additions to Endowments		100,951.91
Increase in Net Assets		1,782,054.93
NET ASSETS		
Net Assets - July 1, 2006, as Restated (Note 15)		96,253,305.49
Net Assets - June 30, 2007	$	98,035,360.42

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

Elizabeth City State University
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2007

Exhibit A-3

CASH FLOWS FROM OPERATING ACTIVITIES	
Received from Customers	$ 20,500,321.07
Payments to Employees and Fringe Benefits	(37,263,904.04)
Payments to Vendors and Suppliers	(22,094,054.49)
Payments for Scholarships and Fellowships	(1,506,706.13)
Loans Issued	(116,630.63)
Collection of Loans	56,226.37
Other Receipts	218,895.39
Net Cash Used by Operating Activities	(40,205,852.46)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
State Appropriations	31,793,996.73
Noncapital Grants	4,536,982.29
Noncapital Gifts	1,042,094.51
Additions to Endowments	100,951.91
Related Activity Agency Payments	(406,250.17)
Net Cash Provided by Noncapital Financing Activities	37,067,775.27
CASH FLOWS FROM CAPITAL FINANCING AND RELATED FINANCING ACTIVITIES	
Capital Appropriations	3,114,300.00
Capital Grants	4,943,652.80
Acquisition and Construction of Capital Assets	(5,003,358.86)
Principal Paid on Capital Debt and Leases	(585,000.00)
Interest Paid on Capital Debt and Leases	(970,366.96)
Net Cash Provided by Capital Financing and Related Financing Activities	1,499,226.98
CASH FLOWS FROM INVESTING ACTIVITIES	
Proceeds from Sales and Maturities of Investments	1,909,698.69
Investment Income	592,704.77
Purchase of Investments and Related Fees	(2,322,342.18)
Net Cash Provided by Investing Activities	180,061.28
Net Increase (Decrease) in Cash and Cash Equivalents	(1,458,788.93)
Cash and Cash Equivalents - July 1, 2006	11,224,520.49
Cash and Cash Equivalents - June 30, 2007	$ 9,765,731.56

RECONCILIATION OF OPERATING LOSS TO NET CASH USED BY OPERATING ACTIVITIES

Operating Loss	$	(44,065,901.54)
Adjustments to Reconcile Operating (Loss) to Net Cash Used by Operating Activities:		
Depreciation Expense		2,924,489.85
Provision for Uncollectible Loans and Write-Offs		7,058.61
Miscellaneous Nonoperating Income		88,926.04
Changes in Assets and Liabilities:		
Receivables (Net)		288,648.79
Inventories		(155,974.47)
Notes Receivable, Net		(60,478.92)
Accounts Payable and Accrued Liabilities		469,187.76
Due to Primary Government		(12,845.07)
Unearned Revenue		77,845.70
Compensated Absences		55,690.79
Deposits Payable		177,500.00
Net Cash Provided Used by Operating Activities	$	(40,205,852.46)

RECONCILIATION OF CASH AND CASH EQUIVALENTS

Current Assets:		
Cash and Cash Equivalents	$	2,703,611.08
Restricted Cash and Cash Equivalents		3,178,639.88
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		3,883,480.60
Total Cash and Cash Equivalents - June 30, 2007	$	9,765,731.56

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

Assets Acquired through the Assumption of a Liability	$	122,997.83
Change in Fair Value of Investments		273,652.05

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

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NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

A. Financial Reporting Entity - The concept underlying the definition of the financial reporting entity is that elected officials are accountable to their constituents for their actions. As required by accounting principles generally accepted in the United States of America, the financial reporting entity includes both the primary government and all of its component units. An organization other than a primary government serves as a nucleus for a reporting entity when it issues separate financial statements. Elizabeth City State 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 unit. 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 unit is blended in the University's financial statements. The blended component unit, although legally separate, is, in substance, part of the University's operations and therefore, is reported as if they were part of the University.

Blended Component Unit - Although legally separate, Elizabeth City State University Foundation, Inc. and Subsidiary (Foundation), a component unit of the University, is reported as if it were part of the University. The Foundation is governed by a 25-member board consisting of the Chancellor of Elizabeth City State University, 13 ex officio directors appointed by the Chancellor, and 11 elected directors. The Foundation's purpose is to aid, support and promote teaching, research, and service in the various educational, scientific, scholarly, professional, artistic, and creative endeavors of the University. Because the ex officio directors of the Foundation are appointed by the Chancellor of Elizabeth City State University, elected directors of the Foundation are appointed by the members of the Elizabeth City State University Board of Trustees, and the Foundation's sole purpose is to benefit Elizabeth City State University, its financial statements have been blended with those of the University.

Separate financial statements for the Foundation may be obtained from the University Controller's Office, 1704 Weeksville Road, Elizabeth City, NC 27909, or by calling (252) 335-3211. Other related foundations and similar nonprofit corporations for which the University is not financially accountable are not part of the accompanying financial statements.

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

Pursuant to the provisions of GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*, the full scope of the 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 U.S. Treasuries, equity investments, mutual funds, and money market funds. Except for money market funds, 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 are reported at cost, if purchased, or at fair value or appraised value at date of gift, if donated.

F. **Receivables –** Receivables consist of tuition and fees charged to students and charges for auxiliary enterprises' sales and services. Receivables also include amounts due from the federal government, State and local governments, private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants, and pledges that are verifiable, measurable, and expected to be collected and available for expenses 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 either first-in, first-out. Merchandise for resale is valued using the retail inventory method. Textbooks for rental are valued at the lower of cost or market.

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.

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 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. The deferred losses on refunds are amortized over the life of the new debt using the straight-line method. Issuance costs are expensed when not material. The issuance costs associated with the Elizabeth City State University Housing Foundation are capitalized and amortized using the straight-line method over the life of the bond which is 30 years.

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, copy centers, 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 $9,688,948.47 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 $1,745.00. The carrying amount of the University's deposits not with the State Treasurer was $75,038.09 and the bank balance was $74,048.54. 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.

B. Investments - 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 Foundation, are subject to and restricted by G.S. 36B "Uniform Management of Institutional Funds Act" (UMIFA) and any requirements placed on them by contract or donor agreements.

Investments of various funds may be pooled unless prohibited by statute or by terms of the gift or contract. The University utilizes investment pools to manage investments and distribute investment income.

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 does not have a formal policy that addresses interest rate risk.

Credit Risk: Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The University does not have a formal policy that addresses credit risk.

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 does not have a formal policy for custodial credit risk.

Foreign Currency Risk: Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. The University does not have a formal policy for foreign currency risk.

Long-Term Investment Pool - This is an internal investment pool that is utilized for the investment of the endowment funds. Fund ownership is measured using the unit value method. Under this method, each participating fund's investment balance is determined on a market value basis. The investment strategy, including the selection of investment managers, is based on the directives of the University's Endowment Board.

The following table presents the fair value of investments by type and investments subject to interest rate risk at June 30, 2007, for the Long-Term Investment Pool.

Long-Term Investment Pool

		Investment Maturities (in Years)	
	Fair Value	1 to 5	6 to 10
Investment Type			
Debt Securities			
Mutual Bond Funds	$ 1,313,926.76	$ 257,084.70	$ 1,056,842.06
Other Securities			
International Mutual Funds	442,659.06		
Other Mutual Funds	1,847,753.66		
Common Stock	65,886.72		
Total Long-Term Investment Pool	$ 3,670,226.20		

At June 30, 2007, investments in the Long-Term Investment Pool had the following credit quality distribution for securities with credit exposure:

	Fair Value	AAA Aaa	AA Aa	A	BBB Baa	BB/Ba and below
Mutual Bond Funds	$ 1,313,926.76	$ 999,991.98	$ 67,810.71	$ 141,617.77	$ 101,935.45	$ 2,570.85

Rating Agency: Standard & Poor's and Moody's

Non-Pooled Investments - 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 non-pooled investments.

Non-Pooled Investments

	Fair Value	Investment Maturities Less Than 1 Year
Investment Type		
Debt Securities		
U.S. Treasuries	$ 276,394.15	$ 276,394.15
Money Market Mutual Funds	2,281,593.07	2,281,593.07
Total Non-Pooled Investments	$ 2,557,987.22	$ 2,557,987.22

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

	Fair Value	AAA Aaa
Money Market Mutual Funds	$ 2,281,593.07	$ 2,281,593.07

Rating Agency: Standard & Poor's and Moody's

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

Investment Type	Held by Counterparty
U.S. Treasuries	$ 276,394.15

Total Investments – The following table presents the fair value of the total investments at June 30, 2007:

		Fair Value
Investment Type		
Debt Securities		
U.S. Treasuries	$	276,394.15
Mutual Bond Funds		1,313,926.76
Money Market Mutual Funds		2,281,593.07
Other Securities		
International Mutual Funds		442,659.06
Other Mutual Funds		1,847,753.66
Common Stock		65,886.72
Total Investments	$	6,228,213.42

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). The non-mandatory spending policy is to take annual withdrawals on August 1 of each year in the annual amount of 5% of a three-year rolling average of the market value of the endowment. The investment manager is expected to liquidate such investments as may be necessary to accomplish this objective, while still maintaining a balanced portfolio. At June 30, 2007, net appreciation of $1,626,975.88 was available to be spent, of which $1,581,350.03 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	$ 836,177.45	$ 88,218.83	$ 747,958.62
Accounts	180,393.08		180,393.08
Intergovernmental	3,341,454.48		3,341,454.48
Pledges	441,629.09	195,359.09	246,270.00
Investment Earnings	20,933.80		20,933.80
Interest on Loans	323,811.91		323,811.91
Other	453,255.44		453,255.44
Total Current Receivables	$ 5,597,655.25	$ 283,577.92	$ 5,314,077.33
Notes Receivable:			
Notes Receivable - Current:			
Federal Loan Programs	$ 62,494.75	$ 0.00	$ 62,494.75
Institutional Student Loan Programs	17,275.76		17,275.76
Total Notes Receivable - Current	$ 79,770.51	$ 0.00	$ 79,770.51
Notes Receivable - Noncurrent:			
Federal Loan Programs	$ 755,030.28	$ 434,415.49	$ 320,614.79
Institutional Student Loan Programs	480,572.55	40,483.64	440,088.91
Total Notes Receivable - Noncurrent	$ 1,235,602.83	$ 474,899.13	$ 760,703.70

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	$ 2,414,538.32	$	$	$ 2,414,538.32
Construction in Progress	7,751,392.27	4,221,219.51	5,956,527.72	6,016,084.06
Total Capital Assets, Nondepreciable	10,165,930.59	4,221,219.51	5,956,527.72	8,430,622.38
Capital Assets, Depreciable:				
Buildings	98,754,410.61	3,608,762.30		102,363,172.91
Machinery and Equipment	8,164,792.80	1,078,705.51	116,204.92	9,127,293.39
General Infrastructure	7,007,427.36	2,048,161.48		9,055,588.84
Total Capital Assets, Depreciable	113,926,630.77	6,735,629.29	116,204.92	120,546,055.14
Less Accumulated Depreciation/Amortization for:				
Buildings	21,497,217.03	1,957,794.72		23,455,011.75
Machinery and Equipment	5,002,364.45	595,868.95	104,835.98	5,493,397.42
General Infrastructure	1,590,772.60	370,826.18		1,961,598.78
Total Accumulated Depreciation	28,090,354.08	2,924,489.85	104,835.98	30,910,007.95
Total Capital Assets, Depreciable, Net	85,836,276.69	3,811,139.44	11,368.94	89,636,047.19
Capital Assets, Net	$ 96,002,207.28	$ 8,032,358.95	$ 5,967,896.66	$ 98,066,669.57

NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

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

	Amount
Accounts Payable	$ 2,257,118.84
Accrued Payroll	332,328.04
Contract Retainage	153,762.92
Other	42,319.87
Total Accounts Payable and Accrued Liabilities	$ 2,785,529.67

NOTE 7 - 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	$ 19,570,000.00	$ 0.00	$ 585,000.00	$ 18,985,000.00	$ 13,685,000.00
Add/Deduct Premium/Discount	16,489.02		2,314.26	14,174.76	
Deduct Deferred Charge on Refunding	(78,737.48)		(3,749.40)	(74,988.08)	
Total Bonds Payable	19,507,751.54		583,564.86	18,924,186.68	13,685,000.00
Compensated Absences	2,127,428.82	1,316,292.52	1,260,601.73	2,183,119.61	180,934.37
Total Long-Term Liabilities	$ 21,635,180.36	$ 1,316,292.52	$ 1,844,166.59	$ 21,107,306.29	$ 13,865,934.37

The Elizabeth City State University Housing Foundation Series A bonds' "Use Agreement" contains debt service requirements related to Viking Village and also to the entire Elizabeth City State University housing system. The requirements were not met as of June 30, 2007. The bond documents contain a provision for acceleration of bond payments if requirements are not met. A waiver of the requirements was not obtained causing the entire balance of the bond to be shown as a current liability as of June 30, 2007.

B. Revenue Bonds Payable - The University was indebted for revenue bonds payable 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
Dormitory System Revenue Bonds of 1981						
Wamack Hall and Mitchell-Lewis Hall	A	3.00%	10/01/2017	$ 675,000.00	$ 425,000.00	$ 250,000.00
Wamack Hall and Mitchell-Lewis Hall	B	3.00%	10/01/2020	1,680,000.00	850,000.00	830,000.00
Total Dormitory System Revenue Bonds of 1981				2,355,000.00	1,275,000.00	1,080,000.00
Educational Facilities Revenue Bonds						
Elizabeth City State University Housing Foundation	A	2.00%-5.25%	06/01/2033	13,895,000.00	535,000.00	13,360,000.00
Total Educational Facilities Revenue Bonds				13,895,000.00	535,000.00	13,360,000.00
The University of North Carolina System Pool Revenue Bonds						
Refinance of Dormitory0200 Bed (1992-Series C Bonds)	(B)	3.5%-5.375%	04/01/2027	3,410,000.00	602,310.00	2,807,690.00
Bedell Cafeteria Renovation	(B)	3.5%-5.375%	04/01/2027	1,225,000.00	216,372.00	1,008,628.00
Dormitory Furniture	(B)	3.5%-5.375%	04/01/2027	885,000.00	156,318.00	728,682.00
Total The University of North Carolina System Pool Revenue Bonds				5,520,000.00	975,000.00	4,545,000.00
Total Bonds Payable (principal only)				$ 21,770,000.00	$ 2,785,000.00	18,985,000.00
Less: Unamortized Loss on Refunding						(74,988.08)
Less: Unamortized Discount						(139,145.29)
Plus: Unamortized Premium						153,320.05
Total Bonds Payable						$ 18,924,186.68

(B) The University of North Carolina System Pool Revenue Bonds, Series 2000

C. 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	
Fiscal Year	Principal	Interest
2008	$ 610,000.00	$ 784,384.39
2009	630,000.00	769,309.38
2010	650,000.00	752,384.38
2011	685,000.00	732,409.38
2012	715,000.00	710,646.88
2013-2017	4,100,000.00	3,167,696.27
2018-2022	3,545,000.00	2,385,721.25
2023-2027	3,360,000.00	1,663,500.00
2028-2032	3,810,000.00	809,750.00
2033-2037	880,000.00	44,000.00
Total Requirements	$ 18,985,000.00	$ 11,819,801.93

NOTE 8 - OPERATING LEASE OBLIGATIONS

The University entered into operating leases for equipment and temporary facilities. Future minimum lease payments under noncancelable operating leases consist of the following at June 30, 2007:

Fiscal Year	Amount
2008	$ 166,959.00
2009	41,966.16
2010	7,584.00
Total Minimum Lease Payments	$ 216,509.16

Rental expense for all operating leases during the year was $170,379.80.

NOTE 9 - 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	Net Revenues	Revenues Pledged as Security for Debt	
Operating Revenues:							
Student Tuition and Fees	$ 11,418,784.19	$ 0.00	$ 4,718,546.72	$ 78,088.22	$ 6,622,149.25	$ 0.00	
Sales and Services:							
Sales and Services of Auxiliary Enterprises:							
Residential Life	$ 3,476,265.20	$ 0.00	$ 1,524,135.33	$ 21,267.83	$ 1,930,862.04	$ 1,930,862.04	(A)
Dining	2,470,393.95		1,057,326.55	20,083.14	1,392,984.26		
Viking Village	1,332,672.36		600,690.54	8,659.95	723,321.87	723,321.87	(B)
Bookstore	1,183,830.42		346,331.76	6,552.43	830,946.23		
Athletics	171,693.36				171,693.36		
Vending Commissions	44,595.06				44,595.06		
Other	390,366.60	292,594.82		2,702.69	95,069.09		
Total Sales and Services	$ 9,069,816.95	$ 292,594.82	$ 3,528,484.18	$ 59,266.04	$ 5,189,471.91	$ 2,654,183.91	
Nonoperating - Noncapital Gifts	$ 1,256,167.00	$ 0.00	$ 0.00	$ 733,093.69	$ 523,073.31	$ 0.00	

Revenue Bonds Secured by Pledged Revenues:
(A) Dormitory System Revenue Bonds of 1981 A and B
(B) Elizabeth City State University Housing Foundation A and B

NOTE 10 - 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	$ 14,587,188.58	$ 421,826.08	$ 544,542.93	$ 0.00	$ 0.00	$ 0.00	$ 15,553,557.59
Research	476,649.97	137,368.97	870,355.61				1,484,374.55
Public Service	578,074.03	252,205.79	428,998.07				1,259,277.89
Academic Support	3,526,192.52	818,942.13	879,564.84				5,224,699.49
Student Services	4,023,476.18	661,179.23	1,409,227.90				6,093,883.31
Institutional Support	6,425,800.00	491,222.87	2,851,964.31				9,768,987.18
Operations and Maintenance of Plant	4,132,560.91	1,978,386.17	1,920,631.15		1,929,665.54		9,961,243.77
Student Financial Aid				1,506,400.99			1,506,400.99
Auxiliary Enterprises	3,448,662.78	1,123,766.77	5,172,525.03		605,441.95		10,350,396.53
Depreciation						2,924,489.85	2,924,489.85
Total Operating Expenses	$ 37,198,604.97	$ 5,884,898.01	$ 14,077,809.84	$ 1,506,400.99	$ 2,535,107.49	$ 2,924,489.85	$ 64,127,311.15

NOTE 11 - 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 $30,661,346.28, of which $21,803,993.52 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were $1,308,239.61 and $579,986.23, respectively. The University made 100% of its annual required contributions for the years ended June 30, 2007, 2006, and 2005, which were $579,986.23, $448,679.74, and $393,514.44, 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 $30,661,346.28, of which $4,653,588.78 was covered under the Optional Retirement Program. Total employee and employer contributions for pension benefits for the year were $279,215.33 and $318,305.47, 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 $73,018.00 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 $19,714.65. The voluntary contributions by employees amounted to $242,826.00 for the year ended June 30, 2007.

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 $169,673.54 for the year ended June 30, 2007.

NOTE 12 - OTHER POSTEMPLOYMENT BENEFITS

A. **Health Care for Long-Term Disability Beneficiaries and Retirees** - The University participates in State-administered programs that provide postemployment health insurance to eligible former employees. Eligible former employees include long-term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers' and State Employees' Retirement System 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

$1,005,388.12. 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 $137,579.43. 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 13 - 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 for building and contents to cover windstorm, explosions or damage caused by vehicle or aircraft impacts. The extended coverage applies to all campus buildings and contents with coverage amounts varying based on the value of each building and its contents.

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.

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 14 - 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 $3,350,878.29 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.

NOTE 15 - NET ASSET RESTATEMENTS

As of July 1, 2006, net assets as previously reported was restated as follows:

	Amount
July 1, 2006 Net Assets as Previously Reported	$ 97,835,984.30
Restatements:	
Correct Pledges Receivable Balance	(356,382.00)
Correct Capital Assets for Failure to Record Depreciation and Amounts Capitalized in Error	(1,226,296.81)
July 1, 2006 Net Assets as Restated	$ 96,253,305.49

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

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

Board of Trustees
Elizabeth City State University
Elizabeth City, North Carolina

We have audited the financial statements of Elizabeth City State University, a constituent institution of the multi-campus University of North Carolina System, which is a component unit of the State of North Carolina, as of and for the year ended June 30, 2007, and have issued our report thereon dated June 27, 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 Elizabeth City State University Foundation, Inc. and Subsidiary, as described in our report on the University's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors.

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 opinions 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 deficiencies described in findings 1 through 5 in the Audit Findings and Responses section of this report to be significant deficiencies 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 consider all the deficiencies described above to be material weaknesses.

Compliance and Other Matters

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 an instance of noncompliance that is required to be reported under *Government Auditing Standards* and which is described in finding 6 in the Audit Findings and Responses section of this report.

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

June 27, 2008

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AUDIT FINDINGS AND RESPONSES

Matters Related to Financial Reporting

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. INADEQUATE BANK RECONCILIATIONS

   The University did not perform bank reconciliations for the Short-term Investment Fund, the State Disbursing account and Capital Improvement account for any month in our audit period. A majority of the University's transactions are processed through these three accounts. The University was unable to completely reconcile the accounts until April 2008. As a result, there was an increased risk of error and misappropriation of assets.

   Recommendation: The University should improve internal control to ensure that all its bank accounts are reconciled completely, accurately, and timely.

   University's Response: We concur with the recommendation.

   The following steps have been accomplished:

   - We have reconciled the bank statement balances to the Banner bank fund balances for all three Banks.
   - We are finalizing procedures and plan to have all reconciliations current at June 30, 2008.

2. FINANCIAL STATEMENTS AND NOTES REQUIRED SIGNIFICANT CORRECTIONS

   The financial statements and notes prepared by Elizabeth City State University presented for audit contained significant errors. Without our audit adjustments, users of the financial statements could have been misled about the University's financial condition and results of operations.

   During our audit of the 2007 financial statements, the following errors were found:

   a. The University posted two erroneous journal entries resulting in the overstatement of Unearned Revenue by $1,012,318.
   b. The University had capital assets totaling $2,285,813 recorded as General Infrastructure that was not being depreciated. The assets were in the subsidiary ledger but depreciation expense for the assets had not been

recorded in prior years. This resulted in Depreciable Capital Assets being overstated by $1,021,009.

c. The University had projects recorded as Construction in Progress that had been completed and placed in service during prior years or the current year. As a result, Nondepreciable Capital Assets was overstated by $5,300,070.

d. Amounts totaling $256,031 due from the Primary Government or State of North Carolina Component Units were recorded as Accounts Receivable.

e. There were numerous errors related to the Net Pledges Receivable balance including a prior period adjustment.

f. The Allowance for Uncollectible Noncapital Gifts in the amount of $1,120,146 was erroneously netted against the operating revenue account Sales and Services, resulting in a negative balance in the note to the financial statements.

g. Various other errors were noted in the financial statements, notes to the financial statements and management's discussion and analysis.

There were other problems and a lack of controls related to the financial reporting process as well. Specifically:

- Journal entries posted by the University did not have adequate explanations or supporting documentation.
- There was limited, if any, review for many journal entries posted to the general ledger throughout the year.
- There was also limited management review of the financial statements and the notes to the financial statements prior to submission to the Office of the State Controller and the Office of the State Auditor. This review was not adequate to identify misstatements on the financial statements and notes.

Recommendation: The University should place greater emphasis on the year-end financial reporting process and implement effective internal control procedures to ensure the completeness and accuracy of the financial statements. The University should perform an adequate review of the journal entries posted to the general ledger to ensure the entries are appropriate and adequately supported.

University's Response: We concur with the recommendation. Since June 30, 2007, we have hired additional staff. Procedures for adequate preparation and review will be in place by June 30, 2008 to ensure accuracy and timeliness for management approval.

The Banner accrual system for June 30, 2008, was made available in May 2008. For June 30, 2007, the system became available near the end of August 2007. The additional time for processing accrual transactions and additional staff will provide for greater accuracy in preparing and reviewing financial statements.

3. INFORMATION SYSTEM ACCESS RIGHTS INCONSISTENT WITH JOB DUTIES

The University did not have adequate procedures in place to ensure that employees only had information systems access rights necessary to perform their job duties. This could result in unauthorized or inappropriate transactions.

Appropriate University personnel did not periodically review access rights to determine if the correct access was granted to an employee consistent with their job duties. As a result, we noted 117 user id's with maintenance/update access to post journal entries to the general ledger. Maintenance access indicates that a user can update information in the system. Of these 117 user id's, only 20 had been approved by the Module Security Administrator to have maintenance access. Journal entries are posted without any electronic approval necessary, which also increases the risk that inaccurate and/or inappropriate entries will be included in the financial records.

Adequately designed internal controls require transactions and other significant events to be authorized and executed only by persons acting within the scope of their authority. Therefore, system access rights should be reviewed on a regular basis.

Recommendation: Management should implement policies and procedures to ensure that users are assigned access levels consistent with their job duties. Such policies and procedures should include allowing the Module Security Administrator to perform review of access to determine if it is appropriate.

University's Response: We concur with the recommendation and have corrected the inappropriate system access. The following steps will be taken by June 30, 2008 to prevent inappropriate information system access.

- ECSU Banner Security System Guidelines will be updated to provide reconciliation between user roles and actual access.
- The Banner Security Administrator (Information Technology) will provide the Module Security Administrator (Accounting) with a monthly report on user system access. This task will be included in Accounting's monthly close-out schedule.
- The Module Security Administrator along with the Banner Security Administrator will review user system access (BANSECR) every ninety (90) days.
- A review process has been added to monthly close-out matrix.

4. DEFICIENCIES IN INTERNAL CONTROLS OVER CAPITAL ASSETS

During our audit period the University failed to reconcile the capital asset subsidiary system to the general ledger and amounts ultimately reported in the financial statements. As a result, there was an increased risk of error in the financial statements.

The University policy manual states that "Fixed Assets should be reconciled monthly by the Fixed Asset Office Officer and the Accounting Department. The Capitalized assets recorded on the fixed asset system should be balanced to the assets recorded on the general ledger. Any differences must be researched and resolved. The reconciliation must be documented and remain on file in accordance with record retention policies."

Recommendation: The University should adhere to its policies and procedures to ensure the fixed asset subsidiary system is reconciled to the general ledger.

University's Response: We concur with the recommendation and will ensure the fixed asset subsidiary system is reconciled to the general ledger.

5. STUDENT ACCOUNTS SYSTEM NOT RECONCILED TO THE FINANCIAL STATEMENTS

The University failed to reconcile the subsidiary ledger (Student Information System) that supports the student accounts to the general ledger and amounts ultimately reported in the financial statements. If the subsidiary ledger is not reconciled to the general ledger there is a risk that the amounts reported in the financial statements are incorrect.

During our audit, we identified numerous misstatements in the financial statements and notes related to student accounts including:

- Student Accounts Receivable was overstated by $1,167,063.49.
- Amounts disclosed with the components of the Sales and Services revenue account were misstated.

Recommendation: The University should implement proper policies and procedures to ensure subsidiary systems are reconciled to the general ledger.

University's Response: We concur with the recommendation and will ensure that all subsidiary systems are reconciled to the general ledger.

6. NONCOMPLIANCE WITH BOND COVENANTS

The University has not complied with certain debt service covenants for the Elizabeth City State University Housing Foundation Series A bonds. As a result, the bond trustee could require immediate repayment of the debt, though only from its dormitory system net revenues.

The "Use Agreement" between the University and Elizabeth City State University Housing Foundation, LLC requires the University to operate the foundation-owned apartments Viking Village such that it shall maintain a certain debt service coverage ratio. In addition the use agreement also requires University and the Board of Governors of the University of North Carolina System to revise fees, rents, and charges for the use of and for services furnished by the Viking Village so that the University will meet the covenant stated above.

Recommendation: The University should revise fees, rents, and charges for the use of and for their services furnished by Viking Village so that the debt service bond covenants are met.

University's Response: In concurrence with this recommendation the University has executed the following steps to ensure compliance with bond covenants.

- In 2007, a responsibility matrix was created detailing the staff assignments related to bond covenants
- The Elizabeth City State University Board of Trustees approved a rate increase of $200 per resident per year for Viking Village
- Revenues and expenditures are being closely monitored.

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