STATE OF
NORTH CAROLINA

MCDOWELL TECHNICAL COMMUNITY COLLEGE

MARION, 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

MCDOWELL TECHNICAL COMMUNITY COLLEGE

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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, McDowell Technical Community College

We have completed a financial statement and compliance audit of McDowell Technical Community College 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 College'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 College's response is included following each finding.

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

Leslie W. Merritt, Jr.

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

March 13, 2008

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
McDowell Technical Community College
Marion, North Carolina

We have audited the accompanying basic financial statements of McDowell Technical Community College, 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 College'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 the McDowell Technical Community College Foundation, Inc., which represent 3.2 percent, 3.7 percent, and .5 percent, respectively, of the assets, net assets and revenues of the College. 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 McDowell Technical Community College Foundation, Inc., 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. The financial statements of the McDowell Technical Community College Foundation, Inc., 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 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 McDowell Technical Community College 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 February 26, 2008, on our consideration of the College's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

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

February 26, 2008

This section of McDowell Technical Community College's Financial Report presents Management's Discussion and Analysis of the College's financial activity during the fiscal year ended June 30, 2007. Since Management's Discussion and Analysis is designed to focus on current activities, resulting changes and currently known facts, please read it in conjunction with the College's basic financial statements and notes to the financial statements. Responsibility for the completeness and fairness of this information rests with the College.

Using This Report

This annual report consists of financial statements, prepared in accordance with Governmental Accounting Standards Board Statement No. 35. These financial statements focus on the financial condition of the College, results of operations, and cash flows of the College as a whole. The College's basic financial statements are designed to emulate corporate presentation models whereby all College activities are consolidated into one total. They are prepared under the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service, regardless of when cash is exchanged. In summary, the reporting format is intended to condense and simplify the user's analysis of costs of various College services to students and the public. The three financial statements are featured below with brief descriptions of each financial focus.

The Statement of Net Assets is designed to be similar to bottom line results for the College. This Statement combines and consolidates current financial resources (short-term consumable resources) with capital assets. The Statement of Net Assets includes all assets and liabilities. Over time, increases or decreases in net assets (the difference between assets and liabilities) are one indicator of the improvement or erosion of the College's financial health when considered with non-financial facts such as enrollment levels and the condition of facilities.

The Statement of Revenues, Expenses, and Changes in Net Assets focuses on both the gross costs and the net costs of College activities, which are supported mainly by State, local, federal and other revenues. This Statement presents the revenues earned and expenses incurred during the year. Activities are reported as either operating or nonoperating. A Community College's dependency on State aid and gifts could result in operating deficits because the financial reporting model classifies State appropriations and gifts as nonoperating revenues. The utilization of capital assets is reflected in the financial statements as depreciation, which amortizes the cost of an asset over its expected useful life.

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, and helps measure the ability to meet financial obligations as they mature. The direct method is used to present the Cash Flow Statement.

Financial Information

In this year's report, a comparative analysis is presented showing prior year information. This analysis includes condensed Statements of Net Assets and of Revenues, Expenses, and Changes in Net Assets.

Financial Highlights

The 2007 fiscal year was impacted by two issues. First, overall student enrollment declined as the local economy began to recover. This decrease results in a decline in Federal financial aid. Funds provided for training dislocated employees declined as well. Next, the W. H. Smith building became fully operational during the 2007 fiscal year, increasing the costs of operating expenses.

Financial Analysis

Analysis of Current Assets and Net Assets

As of June 30, 2007, the College's current assets decreased $375,509.55 primarily due to correction of the classification of cash from the previous year's presentation and a decline in inventories. The total change in net assets was $1,922,420.87 which included a $1,034,581.58 restatement of the beginning balance for reassessment of capital assets' useful lives as well as $772,867.39 for current year growth in investment in capital assets and funds received for capital projects.

Analysis of Net Capital Assets

This account includes the College's capital assets, which are presented on an accrual basis of accounting whereby assets are capitalized and depreciated. Net invested in capital assets increased $1,930,377.58 with completion of construction on the William Harold Smith classroom building and the restatement of capital assets discussed in the previous paragraph.

Analysis of Liabilities

Total liabilities decreased $184,632.85 with a decline in current liabilities of $136,784.02, reflecting a decrease in accounts payable attributable to a decline in contracts payable for construction projects completed during the fiscal year. Noncurrent liabilities decreased $47,848.83, attributable to several employees who had a long tenure with the College retiring during the fiscal year and being paid for their accumulated leave.

Analysis of Revenues

Total operating revenues decreased $294,803.15 in fiscal year 2007, primarily due to a decrease in enrollment and the associated loss in Federal grants for financial aid and a decrease in Sales and Services. Nonoperating revenues increased $661,560.09, as the result of an increase in State Aid. Capital contributions increased $1,239,074.23 with the funding for the Smith Classroom Building.

Analysis of Expenditures

The College experienced an overall increase of $832,963.78 in operating expenses for fiscal year ended June 30, 2007, primarily due to increases in expenses for Personal Services, Supplies and Materials, and Utilities. These increases were attributable to the legislative salary increase for employees and the cost of operating a new facility on campus.

Long-Term Debt

The College has no long-term debt.

Condensed Financial Statements
Statement of Net Assets

	2007	2006	Difference
Assets			
Current Assets	$ 681,191.06	$ 1,056,700.61	$ (375,509.55)
Noncurrent Assets			
Capital Assets	7,734,311.25	5,803,933.67	1,930,377.58
Other	445,086.10	262,166.11	182,919.99
Total Assets	8,860,588.41	7,122,800.39	1,737,788.02
Liabilities			
Current Liabilities	315,189.46	451,973.48	(136,784.02)
Noncurrent Liabilities	790,793.59	838,642.42	(47,848.83)
Total Liabilities	1,105,983.05	1,290,615.90	(184,632.85)
Net Assets			
Invested in Capital Assets	7,734,311.25	5,803,933.67	1,930,377.58
Restricted	618,201.15	490,394.63	127,806.52
Unrestricted	(597,907.04)	(462,143.81)	(135,763.23)
Total Net Assets	$ 7,754,605.36	$ 5,832,184.49	$ 1,922,420.87

Statement of Revenues, Expenses, and Changes in Net Assets

	2007	2006	Difference
Operating Revenues			
Tuition and Fees	$ 759,539.51	$ 864,750.08	$ (105,210.57)
Federal Grants and Contracts	1,144,387.10	1,316,683.14	(172,296.04)
Sales and Services	618,409.02	639,611.19	(21,202.17)
Other	6,457.32	2,551.69	3,905.63
Total Operating Revenues	2,528,792.95	2,823,596.10	(294,803.15)
Less Operating Expenses	12,007,615.31	11,174,651.53	832,963.78
Net Operating Loss	(9,478,822.36)	(8,351,055.43)	(1,127,766.93)
Nonoperating Revenues (Expenses)			
State Aid	6,853,698.32	6,189,833.23	663,865.09
County Appropriations	664,850.00	585,850.00	79,000.00
Noncapital Contributions	890,399.17	1,006,338.67	(115,939.50)
Investment Income	20,657.26	15,180.74	5,476.52
Other Nonoperating Revenues(Expenses)	824.52	(28,333.46)	29,157.98
Total Nonoperating Revenues	8,430,429.27	7,768,869.18	661,560.09
Loss Before Other Revenues	(1,048,393.09)	(582,186.25)	(466,206.84)
Capital Contributions	1,936,232.38	697,158.15	1,239,074.23
Increase in Net Assets	887,839.29	114,971.90	772,867.39
Net Assets, as Restated	6,866,766.07	5,717,212.59	1,149,553.48
Net Assets	$ 7,754,605.36	$ 5,832,184.49	$ 1,922,420.87

In summary, this annual report is designed to provide our community, students, donors, and creditors with a general overview of the College's finances and to demonstrate the College's accountability for the funding it receives through grants, donations, and tuition revenues.

McDowell Technical Community College
Statement of Net Assets
June 30, 2007 — *Exhibit A-1*

ASSETS	
Current Assets:	
Cash and Cash Equivalents	$ 44,301.96
Restricted Cash and Cash Equivalents	90,186.87
Short-Term Investments	10,754.74
Restricted Short-Term Investments	3,404.94
Receivables, Net (Note 4)	196,128.85
Inventories	210,850.73
Notes Receivable, Net (Note 4)	125,562.97
Total Current Assets	681,191.06
Noncurrent Assets:	
Restricted Cash and Cash Equivalents	313,698.98
Restricted Due from Primary Government	15,338.49
Endowment Investments	116,048.63
Capital Assets - Nondepreciable (Note 5)	250,815.88
Capital Assets - Depreciable, Net (Note 5)	7,483,495.37
Total Noncurrent Assets	8,179,397.35
Total Assets	8,860,588.41
LIABILITIES	
Current Liabilities:	
Accounts Payable and Accrued Liabilities (Note 6)	140,114.70
Due to Primary Government	2,203.84
Unearned Revenue	41,273.40
Funds Held for Others	7,670.86
Long-Term Liabilities - Current Portion (Note 7)	123,926.66
Total Current Liabilities	315,189.46
Noncurrent Liabilities:	
Long-Term Liabilities (Note 7)	790,793.59
Total Liabilities	1,105,983.05

NET ASSETS		
Invested in Capital Assets		7,734,311.25
Restricted for:		
Nonexpendable:		
Scholarships and Fellowships		13,610.00
Foundation Endowment		200,697.03
Crook Fellowship Foundation		3,201.00
Expendable:		
Scholarships and Fellowships		27,616.63
Loans		3,683.57
Capital Projects		276,515.80
Crook Fellowship		6,096.47
System-Wide Fees		31,222.59
Duke Energy Grant		51,780.65
Other		3,777.41
Unrestricted		(597,907.04)
Total Net Assets	$	7,754,605.36

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

McDowell Technical Community College
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)	$	759,539.51
Federal Grants and Contracts		1,144,387.10
Sales and Services, Net (Note 9)		618,409.02
Other Operating Revenues		6,457.32
Total Operating Revenues		2,528,792.95
EXPENSES		
Operating Expenses:		
Personal Services		7,565,451.61
Supplies and Materials		1,522,929.22
Services		1,495,477.84
Scholarships and Fellowships		948,508.97
Utilities		172,045.34
Depreciation		303,202.33
Total Operating Expenses		12,007,615.31
Operating Loss		(9,478,822.36)
NONOPERATING REVENUES (EXPENSES)		
State Aid		6,853,698.32
County Appropriations		664,850.00
Noncapital Grants		808,441.22
Noncapital Gifts		81,957.95
Investment Income, Net		20,657.26
Other Nonoperating Revenues		824.52
Net Nonoperating Revenues		8,430,429.27
Loss Before Other Revenues		(1,048,393.09)
State Capital Aid		1,474,839.22
County Capital Appropriations		304,893.16
Capital Gifts		156,500.00
Increase in Net Assets		887,839.29
NET ASSETS		
Net Assets, July 1, 2006 as Restated (Note 15)		6,866,766.07
Net Assets, June 30, 2007	$	7,754,605.36

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

McDowell Technical Community College
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2007

Exhibit A-3

CASH FLOWS FROM OPERATING ACTIVITIES	
Received from Customers	$ 2,572,790.81
Payments to Employees and Fringe Benefits	(7,562,280.45)
Payments to Vendors and Suppliers	(3,329,800.52)
Payments for Scholarships and Fellowships	(948,508.97)
Other Receipts	994.81
Net Cash Used by Operating Activities	(9,266,804.32)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
State Aid Received	6,853,698.32
County Appropriations	664,850.00
Noncapital Grants Received	807,219.11
Noncapital Gifts and Endowments Received	81,957.95
Net Cash Provided by Noncapital Financing Activities	8,407,725.38
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
State Capital Aid Received	1,605,618.21
County Capital Appropriations	304,893.16
Capital Grants Received	58,545.82
Capital Gifts Received	156,500.00
Proceeds from Sale of Capital Assets	824.52
Acquisition and Construction of Capital Assets	(1,198,998.33)
Net Cash Provided by Capital and Related Financing Activities	927,383.38
CASH FLOWS FROM INVESTING ACTIVITIES	
Investment Income	20,657.26
Purchase of Investments and Related Fees	(5,774.68)
Net Cash Provided by Investing Activities	14,882.58
Net Increase in Cash and Cash Equivalents	83,187.02
Cash and Cash Equivalents, July 1, 2006	365,000.79
Cash and Cash Equivalents, June 30, 2007	$ 448,187.81

RECONCILIATION OF OPERATING LOSS TO NET CASH USED BY OPERATING ACTIVITIES

Operating Loss	$	(9,478,822.36)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:		
Depreciation Expense		303,202.33
Provision for Uncollectible Loans and Write-Offs		5,898.05
Changes in Assets and Liabilities:		
Receivables, Net		39,929.75
Inventories		30,892.60
Accounts Payable and Accrued Liabilities		(169,777.20)
Due to Primary Government		1,101.92
Unearned Revenue		4,068.11
Funds Held for Others		994.81
Compensated Absences		(4,292.33)
Net Cash Used by Operating Activities	$	(9,266,804.32)

RECONCILIATION OF CASH AND CASH EQUIVALENTS

Current Assets:		
Cash and Cash Equivalents	$	44,301.96
Restricted Cash and Cash Equivalents		90,186.87
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		313,698.98
Total Cash and Cash Equivalents - June 30, 2007	$	448,187.81

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

Capital Asset Write-Offs	$	261,316.85

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. McDowell Technical Community College is a component unit of the State of North Carolina and an integral part of the State's *Comprehensive Annual Financial Report*.

The accompanying financial statements present all funds of the College and its component unit for which the College's Board of Trustees is financially accountable. The College's component unit is blended in the financial statements.

Blended Component Unit - Although legally separate, McDowell Technical Community College Foundation, Inc., is reported as if it were part of the College. The Foundation is governed by a 20-member board consisting of 12 members elected by Foundation Board of Trustees, two members of the College's Board of Trustees, one student and five ex-officio members of the Foundation Board who are also employees of the College. The Foundation's purpose is to aid, support, and promote teaching, research, and service in the various educational, scientific, scholarly, professional, artistic, and creative endeavors of the College. Because the elected directors of the Foundation are appointed by the members of the McDowell Technical Community College Board of Trustees and the Foundation's sole purpose is to benefit McDowell Technical Community College, its financial statements have been blended with those of the College.

Separate financial statements for the Foundation may be obtained from the College Business Office, 54 College Drive, Marion, North Carolina 28752-8728 or by calling (828) 652-0627. Other related foundations and similar nonprofit corporations for which the College is not financially accountable are not part of the accompanying financial statements.

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

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

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

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

D. **Cash and Cash Equivalents** - This classification includes undeposited receipts, petty cash, cash on deposit with private bank accounts, and money market accounts.

E. **Investments** - This classification includes certificates of deposit. Certificates of deposit are reported at cost, if purchased, or at fair value or appraised value at date of gift, if donated.

F. **Receivables** - Receivables consist of tuition and fees charged to students and charges for auxiliary enterprises' sales and services. Receivables also include amounts due from the federal government, State and local governments, and private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants. Receivables are recorded net of estimated uncollectible amounts.

G. **Inventories** - Inventories, consisting of expendable supplies and merchandise for resale, are stated at the lower of cost or market value using the first-in, first-out method.

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

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 10 to 50 years for buildings and 5 to 25 years for equipment.

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

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

K. **Compensated Absences** - The College's policy is to record the cost of vacation leave when earned. The policy provides for a maximum accumulation of unused vacation leave of 30 days which can be carried forward each July 1 or for which an employee can be paid upon termination of employment. Also, any accumulated vacation leave in excess of 30 days at year end is converted to sick leave.

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 June 30 is retained by employees and transferred into the next fiscal year. It is not subject to the limitation on annual leave carried forward described above and is not subject to conversion to sick leave.

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

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

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

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

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

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

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

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

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

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

O. Internal Sales Activities - Certain institutional auxiliary operations provide goods and services to College departments, as well as to its customers. These institutional auxiliary operations include activities such as central store and bookstore. In addition, the College has other miscellaneous sales and service units that operated either on a reimbursement or charge basis. All internal sales activities to College 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.

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

NOTE 2 - DEPOSITS AND INVESTMENTS

A. Deposits - All funds of the College are deposited in board-designated official depositories and are required to be collateralized in accordance with *North Carolina General Statute* 115D-58.7. Official depositories may be established with any bank or savings and loan association whose principal office is located in North Carolina. Also, the College may establish time deposit accounts, money market accounts, and certificates of deposit. The amount shown on the Statement of Net Assets as cash and cash equivalents and as investments (certificates of deposit) includes cash on hand totaling $900.00, and deposits in private financial institutions with a carrying value of $577,496.12, and a bank balance of $542,534.40.

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

Custodial credit risk is the risk that in the event of a bank failure, the College's deposits may not be returned to it. As of June 30, 2007, the College's bank balance in excess of federal depository insurance coverage was covered under the pooling method.

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

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

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

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

A reconciliation of deposits and investments for the College to the basic financial statements at June 30, 2007, is as follows:

Cash on Hand	$ 900.00
Carrying Amount of Deposits with Private Financial Institutions	577,496.12
Total Deposits and Investments	$ 578,396.12
Current:	
Cash and Cash Equivalents	$ 44,301.96
Restricted Cash and Cash Equivalents	90,186.87
Short-Term Investments	10,754.74
Restricted Short-Term Investments	3,404.94
Noncurrent:	
Restricted Cash and Cash Equivalents	313,698.98
Endowment Investments	116,048.63
Total	$ 578,396.12

NOTE 3 - ENDOWMENT INVESTMENTS

Investments of the College's endowment funds are pooled, unless required to be separately invested by the donor. If a donor has not provided specific instructions, State law permits the Board of Trustees to authorize for expenditure the net appreciation, realized and unrealized, of the investments of the endowment funds.

Investment return of the College's endowment funds is predicated under classical trust doctrines. Unless the donor has stipulated otherwise, capital gains and losses are accounted for as part of the endowment principal and are not available for expenditure. Annual payouts from the College's endowment funds are limited to earnings available from interest income and realized gains. At June 30, 2007, net appreciation of $32,650.92 was available to be spent, of which $8,333.08 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	$ 56,704.16	$ 1,572.32	$ 55,131.84
Accounts	47,347.59	945.00	46,402.59
Intergovernmental	81,666.34		81,666.34
Other	12,928.08		12,928.08
Total Current Receivables	$ 198,646.17	$ 2,517.32	$ 196,128.85
Notes Receivable - Current:			
Mortgage Receivable	$ 9,500.00	$ 0.00	$ 9,500.00
Institutional Student Loan Programs	175,533.24	59,470.27	116,062.97
	$ 185,033.24	$ 59,470.27	$ 125,562.97

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 (as restated)	Increases	Decreases	Balance June 30, 2007
Capital Assets, Nondepreciable:				
Land	$ 230,684.88	$ 0.00	$ 0.00	$ 230,684.88
Construction in Progress	1,823,858.75	1,049,872.74	2,853,600.49	20,131.00
Total Capital Assets, Nondepreciable	2,054,543.63	1,049,872.74	2,853,600.49	250,815.88
Capital Assets, Depreciable:				
Buildings	6,850,300.88	2,853,600.49		9,703,901.37
Machinery and Equipment	1,079,741.71	149,125.59	284,753.32	944,113.98
Total Capital Assets, Depreciable	7,930,042.59	3,002,726.08	284,753.32	10,648,015.35
Less Accumulated Depreciation:				
Buildings	2,724,984.95	211,008.66		2,935,993.61
Machinery and Equipment	421,086.02	92,193.67	284,753.32	228,526.37
Total Accumulated Depreciation	3,146,070.97	303,202.33	284,753.32	3,164,519.98
Total Capital Assets, Depreciable, Net	4,783,971.62	2,699,523.75		7,483,495.37
Capital Assets, Net	$ 6,838,515.25	$ 3,749,396.49	$ 2,853,600.49	$ 7,734,311.25

NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

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

	Amount
Accounts Payable	$ 81,348.39
Accrued Payroll	25,088.28
Intergovernmental Payables	33,678.03
Total Accounts Payable and Accrued Liabilities	$ 140,114.70

NOTE 7 - LONG-TERM LIABILITIES

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

	Balance July 1, 2006	Additions	Reductions	Balance June 30, 2007	Current Portion
Compensated Absences	$ 919,012.58	$ 570,530.56	$ 574,822.89	$ 914,720.25	$ 123,926.66

NOTE 8 - LEASE OBLIGATIONS

Future minimum lease payments under noncancelable operating leases consist of the following at June 30, 2007:

Fiscal Year	Amount
2008	$ 211,224.84
2009	104,683.56
2010	18,296.64
2011	5,074.20
2012	2,959.95
Total Minimum Lease Payments	$ 342,239.19

Rental expense for all operating leases during the year was $234,613.95.

NOTE 9 - REVENUES

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

	Gross Revenues	Internal Sales Eliminations	Less Scholarship Discounts	Change in Allowance for Uncollectibles	Net Revenues
Operating Revenues:					
Student Tuition and Fees	$ 1,077,768.16	$ 0.00	$ 336,832.47	$ (18,603.82)	$ 759,539.51
Sales and Services:					
Sales and Services of Auxiliary Enterprises:					
Bookstore	$ 581,197.37	$ 26,417.50	$ 173,519.76	$ (3,992.46)	$ 385,252.57
Child Development Center	157,398.55			827.00	156,571.55
Other	46,774.30	9,074.67		(1,951.07)	39,650.70
Sales and Services of Education and Related Activities	36,934.20				36,934.20
Total Sales and Services	$ 822,304.42	$ 35,492.17	$ 173,519.76	$ (5,116.53)	$ 618,409.02

NOTE 10 - OPERATING EXPENSES BY FUNCTION

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

	Personal Services	Supplies and Materials	Services	Scholarships and Fellowships	Utilities	Depreciation	Total
Instruction	$ 4,557,214.81	$ 491,496.31	$ 738,877.90	$ 0.00	$ 0.00	$ 0.00	$ 5,787,589.02
Public Service	74,735.50	14,120.83	62,419.02		965.40		152,240.75
Academic Support	614,868.49	27,324.23	17,147.13				659,339.85
Student Services	534,238.29	9,594.84	42,682.49				586,515.62
Institutional Support	1,286,656.59	90,325.77	447,453.14				1,824,435.50
Operations and Maintenance of Plant	238,434.00	369,093.58	149,098.77		171,079.94		927,706.29
Student Financial Aid				948,508.97			948,508.97
Auxiliary Enterprises	259,303.93	520,973.66	37,799.39				818,076.98
Depreciation						303,202.33	303,202.33
Total Operating Expenses	$ 7,565,451.61	$ 1,522,929.22	$ 1,495,477.84	$ 948,508.97	$ 172,045.34	$ 303,202.33	$ 12,007,615.31

NOTE 11 - PENSION PLANS

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

Benefit and contribution provisions for the Teachers' and State Employees' Retirement System are established by *North Carolina*

General Statutes 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contribution rates are set each year by the North Carolina General Assembly based on annual actuarial valuations. For the year ended June 30, 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 College had a total payroll of $6,391,282.62, of which $5,504,044.92 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were $330,242.70 and $146,407.59, respectively. The College made 100% of its annual required contributions for the years ended June 30, 2007, 2006, and 2005, which were $146,407.59, $117,339.34, and $106,485.95, respectively.

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

B. **Deferred Compensation and Supplemental Retirement Income Plans** - IRC Section 401(k) Plan - All members of the Teachers' and State Employees' Retirement System are eligible to enroll in the Supplemental Retirement Income Plan, a defined contribution plan, created under Internal Revenue Code Section 401(k). All costs of administering the Plan are the responsibility of the Plan participants. No costs are incurred by the College. The voluntary contributions by employees amounted to $133,237.00 for the year ended June 30, 2007.

The voluntary contributions by employees for the Roth 401(k) Plan amounted to $2,780.00 for the year ended June 30, 2007.

IRC Section 403(b) and 403(b)(7) Plans - Eligible College employees can participate in tax sheltered annuity plans created under Internal Revenue Code Sections 403(b) and 403(b)(7). The employee's eligible contributions, made through salary reduction agreements, are exempt from federal and State income taxes until the annuity is received or the contributions are withdrawn. These plans are exclusively for employees of colleges and certain charitable and other nonprofit institutions. All costs of administering and funding these plans are the responsibility of the Plan participants. No costs are incurred by the College. The voluntary contributions by employees amounted to $12,098.57 for the year ended June 30, 2007.

NOTE 12 - OTHER POSTEMPLOYMENT BENEFITS

A. Health Care for Long-Term Disability Beneficiaries and Retirees - The College participates in State-administered programs which provide postemployment health insurance to eligible former employees. Eligible former employees include long-term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers' and State Employees' Retirement System. These benefits were established by Chapter 135, Article 3, Part 3, of the General Statutes and may be amended only by the North Carolina General Assembly. Funding for the health care benefit for long-term disability beneficiaries and retirees is financed on a pay-as-you-go basis. The College contributed 3.8% of the covered payroll under the Teachers' and State Employees' Retirement System for these health care benefits. For the fiscal year ended June 30, 2007, the College's total contribution to the Plan was $209,153.71. The College assumes no liability for retiree health care benefits provided by the programs other than its required contribution. Additional detailed information about these programs can be located in the State of North Carolina's *Comprehensive Annual Financial Report*.

B. Disability Income - The College participates in the Disability Income Plan of North Carolina (DIPNC). Established by Chapter 135, Article 6, of the General Statutes, DIPNC provides short-term and long-term disability benefits to eligible members of the Teachers' and State Employees' Retirement System. Long-term disability income benefits are advance funded on an actuarially determined basis using the one-year term cost method. The College contributes .52% of covered payroll under the Teachers' and State Employees' Retirement System to the DIPNC. For the year ended June 30, 2007, the College's total contribution to the DIPNC was $28,621.03. The College assumes no liability for long-term disability benefits under the Plan other than its contribution. Additional detailed information about the DIPNC is disclosed in the State of North Carolina's *Comprehensive Annual Financial Report*.

NOTE 13 - RISK MANAGEMENT

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

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

Fire and other property losses are covered by the Public School Insurance Fund, a State-administered public entity risk pool. This fund is financed by premiums and interest and incurs a $10 million self-insured deductible per occurrence. Reinsurance is purchased by the fund to cover catastrophic events in excess of the $10 million deductible. There have been no significant reductions in insurance coverage from the previous year and settled claims have not exceeded coverage in any of the past three fiscal years.

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

The College is protected for losses from employee dishonesty and computer fraud for employees paid in whole or in part from State funds. The blanket honesty bond is with a private insurance company and is handled by the North Carolina Department of Insurance with coverage of $5,000,000 per occurrence and a $75,000 deductible. In addition, losses for all employees are covered on contracts with private insurance companies with coverage of $10,000 per occurrence and a $250 deductible.

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

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

Term life insurance of $25,000 to $50,000 is provided to eligible workers. This self-insured death benefit program is administered by the State Treasurer and funded via employer contributions. 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

The College has established an encumbrance system to track its outstanding commitments on construction projects and other purchases. Outstanding commitments on construction contracts were $616,669.00 and on other purchases were $32,970.81 at June 30, 2007.

NOTE 15 - NET ASSET RESTATEMENT

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

	Amount
July 1, 2006 Net Assets as Previously Reported	$ 5,832,184.49
Error in Establishing Useful Lives of Capital Assets	1,034,581.58
July 1, 2006 Net Assets as Restated	$ 6,866,766.07

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

Board of Trustees
McDowell Technical Community College
Marion, North Carolina

We have audited the financial statements of McDowell Technical Community College, 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 February 26, 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 McDowell Technical Community College Foundation, Inc., as described in our report on the College's financial statements. The financial statements of the foundation were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the College'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 College's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the College'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.

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

A 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 College'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 College's financial statements that is more than inconsequential will not be prevented or detected by the College's internal control. We consider the deficiencies described in the finding 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 College'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, the significant deficiencies described above are considered to be material weaknesses.

We noted certain matters that we reported to management of the College in a separate letter dated February 19, 2008.

The College'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 College's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management of the College, the Board of Trustees, the State Board of Community Colleges, 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

February 26, 2008

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.

DEFICIENCIES IN FINANCIAL REPORTING

The financial statements prepared by McDowell Technical Community College contained several misstatements and could be misleading to readers:

a) The College did not properly report construction in progress or buildings in the capital assets note. Construction on a new building was completed and the College should have reported $2,853,600.40 as buildings instead of construction in progress. Also, depreciation on the building of $63,061.31 should have been recorded.

b) The College's buildings were overstated $1,034,581.58 because the useful lives of these assets were not reasonably stated.

c) Current unrestricted cash was overstated $321,369.84 and restricted cash was understated. The College did not record the effect of borrowing unrestricted cash to cover deficit balances in restricted funds.

Recommendation: The College should place greater emphasis on the year end financial reporting process and implement effective internal controls to ensure the completeness and accuracy of the financial statements.

College's Response: The College acknowledges that its financial statements contained misstatements involving the misclassification and useful lives of capital assets. College officials mistakenly assumed that construction on a new building was still in progress because contingency funds had not been depleted as of June 30. Moreover, the approved copy of the final inspection certification had not been received by the College as of June 30. The college also mistakenly overlooked the need for the extension of the useful life of assets that were still in use. To avoid these problems, the college will ensure that the staff involved in the year-end closing has adequate training and experience related to these matters in advance of the next fiscal year closing.

We further acknowledge the misclassification of some cash balances by restriction. Upon review, we discovered that our automated financial statement processor was mistakenly configured to aggregate cash accounts on our balance sheets. In addressing this problem, we have modified the financial statement processor to ensure that cash asset accounts are properly disaggregated and reported.

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