STATE OF
NORTH CAROLINA

MONTGOMERY COMMUNITY COLLEGE

TROY, 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

MONTGOMERY COMMUNITY COLLEGE

TROY, NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT

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STATE OF NORTH CAROLINA
Office of the State Auditor

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

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AUDITOR'S TRANSMITTAL

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

We have completed a financial statement audit of Montgomery 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 disclosed certain deficiencies that are detailed in the Audit Finding and Response section of this report. The College's response is included following the 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

May 21, 2008

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Montgomery Community College
Troy, North Carolina

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

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 Montgomery 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 the other auditor provide a reasonable basis for our opinions.

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

In accordance with *Government Auditing Standards*, we have also issued our report dated May 7, 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 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

May 7, 2008

Overview of Financial Statements and Financial Analysis

Montgomery Community College would like to present the Management's Discussion and Analysis for the year ended June 30, 2007. The analysis will include a comparison between current year and prior year information.

The College's basic financial statements include: the Statement of Net Assets; Statement of Revenues, Expenses, and Changes in Net Assets; Statement of Cash Flows; and Notes to the Financial Statements. This presentation of the College's financial statements provides an overview of the College's financial activities for the year.

Statement of Net Assets

The Statement of Net Assets presents assets, liabilities and net assets of the College at a point in time for the fiscal year ended June 30, 2007.

From the data presented, readers of the Statement of Net Assets (SNA) are able to determine the assets (current and noncurrent) available to continue the operations of the College along with how much the College owes vendors (current and noncurrent). Ultimately, the SNA provides a snapshot of the net assets (assets minus liabilities) and their availability for expenditures by the College.

Net assets are divided into three major categories. The first category, invested in capital assets, provides the institution's equity in property, plant and equipment owned by the institution. The next asset category is restricted net assets, which is divided into nonexpendable and expendable. Expendable restricted net assets are available for expenditures by the College but must be spent for purposes specified by external entities that have placed restrictions on the use of the assets. With the transfer of past endowments, the College has no restricted nonexpendable assets. The final category is unrestricted net assets, which are available to the College for any lawful purpose of the institution.

Condensed Statement of Net Assets

	June 30, 2007	June 30, 2006	Variance
Assets			
Current Assets	$ 728,645.89	$ 695,722.67	$ 32,923.22
Capital Assets, Net	6,217,136.26	6,349,775.19	(132,638.93)
Other Assets	538,953.52	418,590.58	120,362.94
Total Assets	7,484,735.67	7,464,088.44	20,647.23
Liabilities			
Current Liabilities	347,888.62	238,559.36	109,329.26
Noncurrent Liabilities	324,209.63	332,092.80	(7,883.17)
Total Liabilities	672,098.25	570,652.16	101,446.09
Net Assets:			
Invested in Capital Assets	6,217,136.26	6,349,775.19	(132,638.93)
Restricted	617,357.76	770,615.54	(153,257.78)
Unrestricted	(21,856.60)	(226,954.45)	205,097.85
Total Net Assets	$ 6,812,637.42	$ 6,893,436.28	$ (80,798.86)

Other assets consist solely of receivables due from the County of Montgomery for construction projects. The funds are expected to be used in the coming year to construct additional classroom space. The amount due from the county was significantly higher at June 30, 2007, than what was reported at June 30, 2006, due to an additional allocation of funding by the county during the 2007 fiscal year.

The College did not have any major additions in capital assets this year to offset depreciation cost of $338,506.34. This contributed to the decrease in capital assets. The increase in current liabilities resulted from the year end purchase of a computer server. The server was received by June 30, 2007, but not paid for until July 2007. This resulted in a payable of approximately $100,000 at June 30, 2007.

Statement of Revenues, Expenses, and Changes in Net Assets

Changes in total net assets as presented on the SNA are based on the activity in the Statement of Revenues, Expenses, and Changes in Net Assets (SRECNA). The purpose of the statement is to present the revenues received by the College, including operating and nonoperating, and expenses, both operating and nonoperating.

Generally, operating revenues are received to provide goods and services for the College. Operating expenses are expenses paid to acquire or produce those goods and services that carry out the mission of the College for which we receive operating revenue. Nonoperating revenues are revenues received for which goods and services are not provided. State aid is considered nonoperating because it is provided by the Legislature without the Legislature directly receiving goods and services for that revenue.

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

	June 30, 2007	June 30, 2006	Variance
Operating Revenues			
Student Tuition and Fees, Net	$ 527,097.01	$ 511,870.75	$ 15,226.26
Federal Grants and Contracts	1,251,821.35	1,374,296.32	(122,474.97)
State and Local Grants and Contracts	167,646.47	193,601.56	(25,955.09)
Sales and Services	123,592.56	115,880.27	7,712.29
Other Operating Revenues	29,546.90	39,411.22	(9,864.32)
Total Operating Revenues	2,099,704.29	2,235,060.12	(135,355.83)
Nonoperating Revenues			
State Aid	4,917,407.22	4,153,954.46	763,452.76
County Appropriations	847,738.00	792,543.09	55,194.91
Noncapital Grants	87,134.62	269,320.99	(182,186.37)
Noncapital Gifts	71,353.66	52,745.60	18,608.06
Other Nonoperating Revenues	22,828.46	7,435.22	15,393.24
Total Nonoperating Revenues	5,946,461.96	5,275,999.36	670,462.60
Total Revenues	8,046,166.25	7,511,059.48	535,106.77
Operating Expenses	8,805,345.64	8,095,923.85	709,421.79
Capital Appropriations/Grants	678,380.53	378,909.17	299,471.36
Decrease in Net Assets	(80,798.86)	(205,955.20)	125,156.34
Net Assets - Beginning of the Year	6,893,436.28	7,099,391.48	(205,955.20)
Net Assets - End of the Year	$ 6,812,637.42	$ 6,893,436.28	$ (80,798.86)

Montgomery Community College continues to experience steady enrollment growth driven by high unemployment and underemployment throughout the County. The increased enrollment has caused increases in State funding and federal grants. The increase in operating expenses was primarily due to an increase Personal Services. This increase was due to hiring additional employees and salary increases. The increased county funding discussed above contributed to the increase in capital appropriations/grants. A grant related to the dental assisting school ended July 2006. This resulted in the decrease in noncapital grants.

Economic Outlook

The College continues to be fully funded initially with immediate requests for reversions. The upcoming year's reversion should not exceed 1% of our formula funding, approximately $50,000. Cash flow restrictions from previous years have shown significant improvement. Fall curriculum enrollment again has shown growth. We are not aware of any significant effects on the financial position of the College. We are anticipating the upcoming fiscal year will be much like the last and Montgomery Community College will continue to strategically meet its goals and objectives.

Montgomery Community College
Statement of Net Assets
June 30, 2007 ***Exhibit A-1***

ASSETS		
Current Assets:		
Cash and Cash Equivalents	$	462,266.29
Restricted Cash and Cash Equivalents		108,229.29
Receivables, Net (Note 3)		94,259.06
Due from State of North Carolina Component Units		11,606.03
Inventories		52,285.22
Total Current Assets		728,645.89
Noncurrent Assets:		
Receivables (Note 3)		538,953.52
Capital Assets - Nondepreciable (Note 4)		516,930.40
Capital Assets - Depreciable, Net (Note 4)		5,700,205.86
Total Noncurrent Assets		6,756,089.78
Total Assets		7,484,735.67
LIABILITIES		
Current Liabilities:		
Accounts Payable and Accrued Liabilities (Note 5)		191,718.64
Unearned Revenue		61,105.05
Funds Held for Others		33,310.73
Long-Term Liabilities - Current Portion (Note 6)		61,754.20
Total Current Liabilities		347,888.62
Noncurrent Liabilities:		
Long-Term Liabilities (Note 6)		324,209.63
Total Liabilities		672,098.25
NET ASSETS		
Invested in Capital Assets		6,217,136.26
Restricted for:		
Expendable:		
Scholarships and Fellowships		2,311.66
Capital Projects		538,953.52
Other		76,092.58
Unrestricted		(21,856.60)
Total Net Assets	$	6,812,637.42

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

Montgomery 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 8)	$	527,097.01
Federal Grants and Contracts		1,251,821.35
State and Local Grants and Contracts		167,646.47
Sales and Services		123,592.56
Other Operating Revenues		29,546.90
Total Operating Revenues		2,099,704.29
EXPENSES		
Operating Expenses:		
Personal Services		5,799,214.19
Supplies and Materials		923,991.02
Services		556,860.05
Scholarships and Fellowships		966,685.66
Utilities		220,088.38
Depreciation		338,506.34
Total Operating Expenses		8,805,345.64
Operating Loss		(6,705,641.35)
NONOPERATING REVENUES		
State Aid		4,917,407.22
County Appropriations		847,738.00
Noncapital Grants		87,134.62
Noncapital Gifts		71,353.66
Investment Income		22,828.46
Net Nonoperating Revenues		5,946,461.96
Income Before Other Revenues, Expenses, Gains, and Losses		(759,179.39)
State Capital Aid		403,765.67
County Capital Aid		9,999.99
Capital Grants		264,614.87
Decrease in Net Assets		(80,798.86)
NET ASSETS		
Net Assets, July 1, 2006		6,893,436.28
Net Assets, June 30, 2007	$	6,812,637.42

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

Montgomery Communtiy College
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2007 — *Exhibit A-3*

CASH FLOWS FROM OPERATING ACTIVITIES	
Received from Customers	$ 2,275,353.23
Payments to Employees and Fringe Benefits	(5,776,299.50)
Payments to Vendors and Suppliers	(1,602,549.24)
Payments for Scholarships and Fellowships	(966,685.66)
Other Payments	(5,648.61)
Net Cash Used by Operating Activities	(6,075,829.78)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
State Aid Received	4,917,407.22
County Appropriations	847,738.00
Noncapital Grants Received	56,061.88
Noncapital Gifts Received	71,353.66
Cash Provided by Noncapital Financing Activities	5,892,560.76
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
State Capital Aid Received	548,017.60
County Capital Aid	9,999.99
Acquisition and Construction of Capital Assets	(205,867.41)
Net Cash Provided by Capital and Related Financing Activities	352,150.18
CASH FLOWS FROM INVESTING ACTIVITIES	
Investment Income	22,828.46
Cash Provided by Investing Activities	22,828.46
Net Increase in Cash and Cash Equivalents	191,709.62
Cash and Cash Equivalents, July 1, 2006	378,785.96
Cash and Cash Equivalents, June 30, 2007	$ 570,495.58
RECONCILIATION OF OPERATING LOSS TO NET CASH USED BY OPERATING ACTIVITIES	
Operating Loss	$ (6,705,641.35)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:	
Depreciation Expense	338,506.34
Changes in Assets and Liabilities:	
Receivables, Net	176,071.07
Inventories	(5,678.64)
Accounts Payable and Accrued Liabilities	104,558.63
Unearned Revenue	(422.13)
Funds Held for Others	(5,648.61)
Compensated Absences	22,424.91
Net Cash Used by Operating Activities	$ (6,075,829.78)

RECONCILIATION OF CASH AND CASH EQUIVALENTS

Current Assets:		
Cash and Cash Equivalents	$	462,266.29
Restricted Cash and Cash Equivalents		108,229.29
Total Cash and Cash Equivalents - June 30, 2007	$	570,495.58

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

Increase in Receivables Related to Nonoperating Income	$	276,220.90

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

Montgomery Community College Foundation, Inc.
Statement of Financial Position
June 30, 2007

Exhibit B-1

ASSETS		
Cash and Cash Equivalents	$	292,200
Investments Held by Fiscal Agent		1,498,403
Unconditional Promises		127,372
Total Assets		1,917,975
LIABILITIES		
Accounts Payable		2,795
NET ASSETS		
Unrestricted		607,662
Temporarily Restricted		71,454
Permanently Restricted		1,236,064
Total Net Assets	$	1,915,180

See Note 1 in the Notes to the Financial Statements

Montgomery Community College Foundation, Inc.
Statement of Activities
For the Fiscal Year Ended June 30, 2007 ***Exhibit B-2***

CHANGES IN UNRESTRICTED NET ASSETS	
Revenue and Support	
Contributions	$ 592
Fundraising Events	47,497
Income Earned on Investments	8,684
Net Realized and Unrealized Gains on Investments	219,259
Net Assets Released from Restrictions: Satisfaction of Program Restrictions	141,785
Total Revenue and Support	417,817
Expenses	
Programs	128,092
Management and General	31,287
Fundraising	32,590
Total Expenses	191,969
Increase in Unrestricted Net Assets	225,848
CHANGES IN TEMPORARILY RESTRICTED NET ASSETS	
Revenue and Support	
Contributions	183,422
Income Earned on Investments	40,205
Net Realized and Unrealized Losses on Investments	(88,667)
Net Assets Released from Restrictions: Satisfaction of Program Restrictions	(128,092)
Increase in Temporarily Restricted Net Assets	6,868
CHANGES IN PERMANENTLY RESTRICTED NET ASSETS	
Revenue and Support	
Contributions	104,336
Net Assets Released from Restrictions: Satisfaction of Program Restrictions	(13,693)
Increase in Permanently Restricted Net Assets	90,643
Increase in Net Assets	323,359
Net Assets at Beginning of Year	1,591,821
Net Assets at End of Year	$ 1,915,180

See Note 1 in the Notes to the Financial Statements

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

The accompanying financial statements present all funds of the College and the component unit for which the College's Board of Trustees is financially accountable. The College's component unit is discretely presented in the financial statements. The discretely presented component unit's financial data are reported in separate financial statements because of its use of a different reporting model and to emphasize its legal separateness.

Discretely Presented Component Unit – Montgomery Community College Foundation, Inc., is a legally separate not-for-profit corporation and is reported as a discretely presented component unit based on the nature and significance of its relationship to the College.

The Montgomery Community College Foundation, Inc. is a legally separate, tax-exempt component unit of the College. The Foundation acts primarily as a fund-raising organization to supplement the resources that are available to the College in support of its programs. The Foundation board consists of 20 members. Although the College does not control the timing or amount of receipts from the Foundation, the majority of resources, or income thereon, that the Foundation holds and invests are restricted to the activities of the College by the donors. Because these restricted resources held by the Foundation can only be used by, or for the benefit of, the College, the Foundation is considered a component unit of the College and is reported in separate financial statements because of the difference in its reporting model, as described below.

The Montgomery Community College Foundation, Inc. is a private not-for-profit organization that reports its financial results under Financial

Accounting Standards Board (FASB) Statements. As such, certain revenue recognition criteria and presentation features are different from Governmental Accounting Standards Board (GASB) revenue recognition criteria and presentation features. No modifications have been made to the Foundation's financial information in the College's financial reporting entity for these differences.

During the year ended June 30, 2007, the Foundation distributed $224,982 to the College for both restricted and unrestricted purposes. Complete financial statements for the Foundation can be obtained from Montgomery Community College Business Office.

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

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

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

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

D. **Cash and Cash Equivalents –** This classification includes petty cash, cash on deposit with private bank accounts, 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. **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 and State and local governments. Receivables are recorded net of estimated uncollectible amounts.

F. **Inventories –** Inventories, consisting of expendable supplies, are valued at cost using first-in, first-out method.

G. **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 75 years for general infrastructure, 10 to 50 years for buildings, and 2 to 25 years for equipment.

The pottery collection is capitalized at cost or fair value at the date of donation. This collection is considered inexhaustible and is therefore not depreciated.

H. **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.

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

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

In addition to the vacation leave described above, compensated absences 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.

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

K. **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 – 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.

L. **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.

M. **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.

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

NOTE 2 - DEPOSITS AND INVESTMENTS

A. **Deposits -** All funds of the College are deposited in board-designated official depositories and are required to be collateralized in accordance with *North Carolina General Statute* 115D-58.7. Official depositories may be established with any bank or savings and loan association whose principal office is located in North Carolina. Also, the College may establish time deposit accounts, money market accounts, and certificates of deposit. The amount shown on the Statement of Net Assets as cash and cash equivalents includes cash on hand totaling $400.00, and deposits in private financial institutions with a carrying value of $450,158.73 and a bank balance of $514,751.78.

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.

In addition to these legal limits, the College has formally adopted general investment policies to promote investment safety and return, but the policies do not set forth specific requirements to manage investment risk.

At June 30, 2007, the amount shown on the Statement of Net Assets as cash and cash equivalents includes $119,936.85 which represents the College's equity position in the State Treasurer's Short-Term Investment Fund. The Short-Term Investment Fund (a portfolio within the State Treasurer's Investment Pool, an external investment pool that is not registered with the Securities and Exchange Commission and does not have a credit rating) had a weighted average maturity of 1.6 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.

Foundation's Pooled Investments Held by Fiscal Agent

Investments of the College's component unit, Montgomery 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.

All investments are valued in the financial statements at fair value based on publicly available trading values. The fair value of the investments held by the fiscal agent at June 30, 2007, was as follows:

	Cost	Fair Value	Carrying Value
First Citizens Equity Fund	$ 692,791	$ 847,057	$ 847,057
First Citizens Fixed Income Fund	592,067	576,548	576,548
First Citizens Cash & Equivalents Fund	74,798	74,798	74,798
Total Investments	$ 1,359,656	$ 1,498,403	$ 1,498,403

The following schedule summarizes the investment return and its classification in the statement of activities.

	Unrestricted	Temporarily Restricted	Total
Interest and Dividends	$ 8,684	$ 40,205	$ 48,889
Net Realized and Unrealized Gains (Losses) on Investments	219,259	(88,667)	130,592
Total Investments	$ 227,943	$ (48,462)	$ 179,481

Reconciliation of College's Deposits and Investments

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

Cash on Hand	$	400.00
Carrying Amount of Deposits with Private Financial Institutions		450,158.73
Investments in the Short-Term Investment Fund		119,936.85
Total Deposits and Investments	$	570,495.58
Current:		
Cash and Cash Equivalents	$	462,266.29
Restricted Cash and Cash Equivalents		108,229.29
Total	$	570,495.58

NOTE 3 - RECEIVABLES

Receivables at June 30, 2007, were as follows:

	Gross Receivables	Allowance for Doubtful Accounts	Net Receivables
Current Receivables:			
Students	$ 81,684.97	$ 6,534.80	$ 75,150.17
Accounts	5,674.00		5,674.00
Intergovernmental	1,242.43		1,242.43
Other	12,192.46		12,192.46
Total Current Receivables	$ 100,793.86	$ 6,534.80	$ 94,259.06
Noncurrent Receivables:			
Intergovernmental	$ 538,953.52	$ 0.00	$ 538,953.52

NOTE 4 - 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 and Land Improvements	$ 442,186.24	$ 0.00	$ 0.00	$ 442,186.24
Art, Literature, and Artifacts	74,744.16			74,744.16
Total Capital Assets, Nondepreciable	516,930.40			516,930.40
Capital Assets, Depreciable:				
Buildings	8,407,579.43			8,407,579.43
Machinery and Equipment	1,487,365.41	157,129.31	99,063.39	1,545,431.33
General Infrastructure	161,795.93	48,738.10		210,534.03
Total Capital Assets, Depreciable	10,056,740.77	205,867.41	99,063.39	10,163,544.79
Less Accumulated Depreciation:				
Buildings	3,066,673.62	221,687.04		3,288,360.66
Machinery and Equipment	1,057,690.24	107,523.58	99,063.39	1,066,150.43
General Infrastructure	99,532.12	9,295.72		108,827.84
Total Accumulated Depreciation	4,223,895.98	338,506.34	99,063.39	4,463,338.93
Total Capital Assets, Depreciable, Net	5,832,844.79	(132,638.93)		5,700,205.86
Capital Assets, Net	$ 6,349,775.19	$ (132,638.93)	$ 0.00	$ 6,217,136.26

NOTE 5 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

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

	Amount
Accounts Payable	$ 154,913.39
Accrued Payroll	36,805.25
Total Accounts Payable and Accrued Liabilities	$ 191,718.64

NOTE 6 - 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	$ 363,538.92	$ 205,465.25	$ 183,040.34	$ 385,963.83	$ 61,754.20

NOTE 7 - OPERATING LEASE OBLIGATIONS

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

Fiscal Year	Amount
2008	$ 12,000.00
2009	3,000.00
Total Minimum Lease Payments	$ 15,000.00

Rental expense for all operating leases during the year was $13,467.30.

NOTE 8 - REVENUES

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

	Gross Revenues	Less Scholarship Discounts	Less Allowance for Uncollectibles	Net Revenues
Operating Revenues:				
Student Tuition and Fees	$ 903,329.93	$ 369,698.12	$ 6,534.80	$ 527,097.01

NOTE 9 - OPERATING EXPENSES BY FUNCTION

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

	Personal Services	Supplies and Materials	Services	Scholarships and Fellowships	Utilities	Depreciation	Total
Instruction	$ 3,601,892.75	$ 416,333.62	$ 115,817.13	$ 0.00	$ 0.00	$ 0.00	$ 4,134,043.50
Academic Support	397,851.37	53,920.88	20,170.33				471,942.58
Student Services	390,405.45	36,128.99	36,842.33				463,376.77
Institutional Support	1,042,968.88	94,519.72	247,640.31				1,385,128.91
Operations and Maintenance of Plant	305,543.71	321,711.67	112,353.27		220,088.38		959,697.03
Student Financial Aid	60,552.03	1,376.14	950.20	966,685.66			1,029,564.03
Auxillary Enterprise			23,086.48				23,086.48
Depreciation						338,506.34	338,506.34
Total Operating Expenses	$ 5,799,214.19	$ 923,991.02	$ 556,860.05	$ 966,685.66	$ 220,088.38	$ 338,506.34	$ 8,805,345.64

NOTE 10 - PENSION PLANS

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

Benefit and contribution provisions for the Teachers' and State Employees' Retirement System are established by *North Carolina General Statutes* 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contribution rates are set each year by the North Carolina General Assembly based on annual actuarial valuations. For the year ended June 30, 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 $4,876,965.61, of which $4,001,410.60 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were $240,084.64 and $106,437.52, respectively. The College made 100% of its annual required contributions for the years ended June 30, 2007, 2006, and 2005, which were $106,437.52, $84,120.25, and $72,500.66, 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 $26,779.00 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 $16,050.00 for the year ended June 30, 2007.

NOTE 11 - OTHER POSTEMPLOYMENT BENEFITS

A. Health Care for Long-Term Disability Beneficiaries and Retirees – The College participates in State-administered programs which provide postemployment health insurance to eligible former employees. Eligible former employees include long-term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers' and State Employees' Retirement System. These benefits were established by Chapter 135, Article 3, Part 3, of the General Statutes and may be amended only by the North Carolina General Assembly. Funding for the health care benefit for long-term disability beneficiaries and retirees is financed on a pay-as-you-go basis. The College contributed 3.8% 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 $152,053.61. 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 $20,807.34. The College assumes no liability for long-term disability benefits under the Plan other than its contribution. Additional detailed information about the DIPNC is disclosed in the State of North Carolina's *Comprehensive Annual Financial Report.*

NOTE 12 - RISK MANAGEMENT

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

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

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

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

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

The College also purchased a general liability policy with an aggregate of $2,000,000.

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.

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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
Montgomery Community College
Troy, North Carolina

We have audited the financial statements of Montgomery Community College, a component unit of the State of North Carolina, and its discretely presented component unit, as of and for the year ended June 30, 2007, which collectively comprise the College's basic financial statements and have issued our report thereon dated May 7, 2008. Our report was modified to include a reference to other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Other auditors audited the financial statements of the discretely presented component unit, as described in our report on the College's financial statements. The financial statements of the discretely presented component unit were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the 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. 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 deficiency described in the finding in the Audit Finding and Response section of this report to be a significant deficiency in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the 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, we believe that the significant deficiency described above is not a material weakness.

Compliance and Other Matters

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

The College's response to the finding identified in our audit is described in the Audit Finding and Response 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 State Controller, and the General Assembly, 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

May 7, 2008

AUDIT FINDING AND RESPONSE

Matters Related to Financial Reporting Objectives

The following finding and recommendation was identified during the current audit and discusses conditions that represent deficiencies in internal control.

DEFICIENCIES IN FINANCIAL REPORTING

The financial statements prepared by Montgomery Community College contained misstatements that were corrected as a result of our audit. Without these corrections, the financial statements could have been misleading to readers.

Misstatements noted in our audit included:

- The College misclassified $313,329 of capital grants and State capital aid, resulting in an overstatement of operating revenues and an understatement of non-operating revenues.
- The College did not properly determine student accounts receivable and unearned revenue at June 30, 2007. This resulted in a $70,853 overstatement of revenues, a $47,587 overstatement of accounts receivable, and a $23,266 understatement of unearned revenue.
- As a result of a keying error while preparing the financial statements, the College reported non-current long-term liabilities inaccurately. As a result, the Statement of Net Assets did not balance and the noncurrent long-term liabilities were understated by $61,754.
- Various other misstatements were made in the financial statements and in the notes to the financial statements.

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 continues to implement stronger internal controls in the year-end process and the preparation of the financial statements, including developing a year-end close-out calendar and check-off list, templates for routine year-end adjusting and reversing entries, and spreadsheets to support fixed asset inventory. We will also conduct a thorough review of the general ledger classifications and ensure that they are consistent with the financial statement classifications.

ORDERING INFORMATION

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