



STATE OF NORTH CAROLINA

FAYETTEVILLE STATE UNIVERSITY

FAYETTEVILLE, NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT

FOR THE YEAR ENDED JUNE 30, 2008

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

STATE AUDITOR

FAYETTEVILLE STATE UNIVERSITY

FAYETTEVILLE, NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT

FOR THE YEAR ENDED JUNE 30, 2008

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THE UNIVERSITY OF NORTH CAROLINA

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Beth A. Wood, CPA
State Auditor

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AUDITOR'S TRANSMITTAL

The Honorable Beverly E. Perdue, Governor
The General Assembly of North Carolina
Board of Trustees, Fayetteville State University

We have completed a financial statement audit of Fayetteville State University for the year ended June 30, 2008, 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 Findings and Responses section of this report. The University's response is included following each finding.

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

A handwritten signature in cursive script that reads "Beth A. Wood".

Beth A. Wood, CPA
State Auditor

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Fayetteville State University
Fayetteville, North Carolina

We have audited the accompanying financial statements of Fayetteville State University, a constituent institution of the multi-campus University of North Carolina System, which is a component unit of the State of North Carolina, and its discretely presented component unit, as of and for the year ended June 30, 2008, which collectively comprise the University's basic financial statements as listed in the table of contents. These financial statements are the responsibility of Fayetteville State University's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of Fayetteville State University Foundation, Inc., and Subsidiary, the University's discretely presented component unit. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for those entities, 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 Fayetteville State University Foundation, Inc., and Subsidiary were not audited in accordance with *Government Auditing Standards*. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of Fayetteville State University and its discretely presented component unit as of June 30, 2008, 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.

INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

As discussed in Note 15 to the financial statements, the University implemented Governmental Accounting Standards Board Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, and Statement No. 50, *Pension Disclosures*, during the year ended June 30, 2008.

In accordance with *Government Auditing Standards*, we have also issued our report dated July 15, 2009 on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis, as listed in the table of contents, is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.



Beth A. Wood, CPA
State Auditor

July 15, 2009

FAYETTEVILLE STATE UNIVERSITY MANAGEMENT'S DISCUSSION AND ANALYSIS

Introduction

Fayetteville State University (University) provides this overview and management discussion and analysis to assist in understanding the statements and notes to the financial statements presented herewith for the year ended June 30, 2008, and includes comparative data for the year ended June 30, 2007. The discussion describes important trends and events that have impacted the fiscal health of the University and that may continue to exert influence in future years. This discussion has been prepared by and is the responsibility of the University management along with the financial statements and notes. The report should be read and considered in its entirety.

Using the Annual Report

This annual report consists of a series of financial statements, notes and other information prepared in accordance with the Governmental Accounting Standards Board (GASB). The GASB establishes standards for external financial reporting for public colleges and universities and requires that financial statements be presented on a consolidated basis for the University as a whole. These standards were used in the preparation of this document. The statements 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. Comparative information for the prior fiscal year is also presented in the condensed financial statements.

The Notes to the Financial Statements should be read in conjunction with the financial statements. The Notes to the Financial Statements provide information regarding the significant accounting principles applied in the financial statements, authority for and associated risk of deposits and investments, detailed information on deposits and investments, long-term liabilities, accounts receivable, accounts payable, revenues, and expenses, required information on pension plans, other post employment benefits, insurance against losses, and commitments and contingencies, and if necessary, a discussion of accounting changes, adjustments to prior periods, and events subsequent to the University's financial statement period. Overall, these disclosures provide information to better understand details, risk, and uncertainty associated with amounts reported in the financial statements.

Reporting Entity

The financial statements report information about the University as a whole using accounting methods similar to those used in the private sector. The University's supporting organization, the Fayetteville State University Foundation, Inc., and Subsidiary (Foundation), is a legally separate not-for-profit corporation and is reported as a discretely presented component unit based on the nature and significance of its relationship to the University. Therefore, the results of its operations are not blended with the University's financial statements, but are discretely presented, and are not included in this Management's Discussion and Analysis.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

The Foundation includes as a subsidiary, the University Place Apartments (UPA). These apartments are currently leased to the University under a master lease agreement for use as student housing.

Financial Highlights

The University's financial position, as a whole, remained relatively stable during the fiscal year ended June 30, 2008. The combined net assets for the University increased \$6.77 million in the current year (after restatements), which is an increase of about 6.4 percent.

Summary of Net Assets

The Statement of Net Assets presents the assets, liabilities, and net assets of the University as of the end of the fiscal year. The Statement of Net Assets is a point-in-time financial statement. The purpose of the Statement of Net Assets is to present to the readers of the financial statements a fiscal snapshot of Fayetteville State University. The Statement of Net Assets presents end-of-year data showing assets (property that we own and what we are owed by others); liabilities (what we owe to others and have collected from others in advance of providing the service); and net assets (assets minus liabilities).

From the data presented, readers of the Statement of Net Assets are able to determine the assets available to continue the operations of the University. They are also able to determine how much the University owes to vendors and others and how much is held for future use by the University or others. Finally, the Statement of Net Assets provides a picture of the net assets and their availability for expenditure by the University.

Net assets are divided into categories to show the availability to meet University obligations. The first category, invested in capital assets, net of related debt, provides the University's equity in property, plant, and equipment. The next asset category is restricted net assets, which is divided into two categories, nonexpendable and expendable. Restricted nonexpendable net assets consist primarily of the University's permanent endowment funds and are only available for investment purposes. Expendable restricted net assets are available for use by the University but must be spent for purposes as determined by donors and/or external entities that have placed time or purpose restrictions on the use of the assets. The final category is unrestricted net assets. Unrestricted net assets are available to the University for any lawful purpose of the University. Although unrestricted net assets are not subject to externally imposed stipulations, substantially all of the University's unrestricted net assets have been designated for various academic and research programs and initiatives.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Condensed Summary of Net Assets (in millions)

	2008	2007 (Restated)	Increase/ (Decrease)	Percent Change
Assets:				
Current Assets	\$ 12.62	\$ 14.44	\$ (1.82)	-12.60%
Noncurrent Assets:				
Capital	100.11	95.16	4.95	5.20%
Other	15.50	12.81	2.69	21.00%
Total Assets	128.23	122.41	5.82	4.75%
Liabilities:				
Current Liabilities	4.87	6.71	(1.84)	-27.42%
Noncurrent Liabilities	10.89	10.00	0.89	8.90%
Total Liabilities	15.76	16.71	(0.95)	-5.69%
Net Assets:				
Invested in Capital Assets, Net of Related Debt	93.87	86.35	7.52	8.71%
Restricted:				
Nonexpendable	3.83	3.00	0.83	27.67%
Expendable	8.30	9.84	(1.54)	-15.65%
Unrestricted	6.47	6.51	(0.04)	-0.61%
Total Net Assets	\$ 112.47	\$ 105.70	\$ 6.77	6.40%

Net Assets categories are defined in Note 1.L of the Notes to the Financial Statements. For proper comparison, the 2007 column includes the effect of a \$3.29 million restatement to capitalize assets previously expensed.

As of June 30, 2008, total University assets were \$128.23 million. The University's largest assets are its capital assets of \$100.11 million, representing 78.0 percent of total assets. Current assets decreased by \$1.82 million primarily due to a decrease in cash and cash equivalents of \$1.28 million.

Noncurrent capital assets increased by \$4.95 million primarily due to the renovation of the Science Annex, the Taylor Social Sciences building and the Lilly Gym conversion relating to capital expenditures funded by proceeds from the sale of North Carolina general obligation bonds. Noncurrent other assets increased by \$2.69 million primarily due to an increase in cash and cash equivalents of \$0.95 million.

The University's liabilities totaled \$15.76 million at June 30, 2008. Noncurrent liabilities of \$10.89 million consist mainly of \$4.37 million bonds payable and \$2.86 million compensated absences. Other liabilities include contracts, capital leases and accounts payable, U. S. government grants refundable, and funds held for others. Details of both current and noncurrent liabilities are shown on the Statement of Net Assets and in notes 6 and 7.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

The University's current assets of \$12.62 million covered the current liabilities of \$4.87 million, at a ratio of 2.59 (\$2.59 in current assets for every \$1.00 in current liabilities).

At June 30, the University had outstanding bonds of \$4.96 million, the details of which are shown in the notes. Bonds payable is the University's largest liability, representing 31 percent of total University liabilities. For the fiscal year 2007-08 no new debt for bonds were issued. The University entered into capital leases of \$1.45 million for machinery and equipment and turf.

The \$6.77 million overall increase in net assets was largely attributable to the increase in capital assets of \$4.95 million for construction projects.

Summary of Revenues, Expenses, and Changes in Net Assets

The Statement of Revenues, Expenses, and Changes in Net Assets presents the revenues earned and expenses incurred during the year. Activities are reported as either operating or nonoperating. A public University's dependency on State aid and gifts will result in operating deficits since the GASB requires that State appropriations and gifts be classified as nonoperating revenues. The utilization of long-lived assets, referred to as capital assets, is reflected in the financial statements as depreciation, which amortizes the cost of an asset over its expected useful life.

The change in total net assets as presented on the Condensed Summary of Net Assets is based on the activity presented in the Statement of Revenues, Expenses, and Changes in Net Assets. The purpose of the statement is to present the revenues received by the University, both operating and nonoperating, the expenses paid by the University, operating and nonoperating, and any other revenues, expenses, gains, and losses received or spent by the University.

Generally speaking, operating revenues are received for providing goods and services to the various customers and constituencies of the University. Operating expenses are those expenses paid to acquire or produce the goods and services provided in return for the operating revenues, and to carry out the mission of the University. Nonoperating revenues are revenues received for which goods and services are not provided. Capital grants are considered neither operating nor nonoperating revenues and are reported after "Loss Before Other Revenues."

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Condensed Summary of Revenues, Expenses, and Changes in Net Assets (in Millions)

	<u>2008</u>	<u>2007 (Restated)</u>	<u>Increase/ (Decrease)</u>	<u>Percent Change</u>
Operating Revenues:				
Student Tuition and Fees, Net	\$ 14.93	\$ 14.14	\$ 0.79	5.59%
Grants and Contracts	12.88	12.65	0.23	1.82%
Sales and Services, Net	8.02	6.32	1.70	26.90%
Other Operating Revenues	0.10	0.30	(0.20)	-66.67%
Total Operating Revenues	35.93	33.41	2.52	7.54%
Operating Expenses:				
Salaries and Benefits	60.88	54.51	6.37	11.69%
Supplies and Materials	9.29	8.28	1.01	12.20%
Services	17.84	15.33	2.51	16.37%
Scholarships and Fellowships	9.56	9.52	0.04	0.42%
Utilities	2.96	2.45	0.51	20.82%
Depreciation	3.35	1.78	1.57	88.20%
Total Operating Expenses	103.88	91.87	12.01	13.07%
Operating Loss	(67.95)	(58.46)	(9.49)	16.23%
Nonoperating Revenues (Expenses):				
State Appropriations	57.07	49.20	7.87	16.00%
Interest and Fees on Debt	(0.30)	(0.28)	(0.02)	7.14%
Other Nonoperating Revenue	9.72	8.11	1.61	19.85%
Net Nonoperating Revenues	66.49	57.03	9.46	16.59%
Loss Before Other Revenues	(1.46)	(1.43)	(0.03)	2.10%
Capital Contributions	7.41	12.93	(5.52)	-42.69%
Permanent Endowment Additions	0.82	0.23	0.59	256.52%
Increase in Net Assets	6.77	11.73	(4.96)	-42.28%
Net Assets:				
Beginning of Year (Restated)	105.70	93.97	11.73	12.48%
End of Year	<u>\$ 112.47</u>	<u>\$ 105.70</u>	<u>\$ 6.77</u>	6.40%

The Condensed Summary of Revenues, Expenses, and Changes in Net Assets shows an increase in net assets of \$6.77 million at the end of the year.

The total operating loss for fiscal year 2008 was \$67.95 million. Since the State of North Carolina appropriation is not included within operating revenue per GASB, the University shows a significant operating loss.

The sources of operating revenue for the University are tuition and fees, grants and contracts, sales and services, and other operating revenues.

The University strives to provide students with the opportunity to obtain a quality education. Future University enrollments may be affected by a number of factors, including any material increase in tuition and other mandatory charges. Changes in appropriation funding from the

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

State of North Carolina may influence costs to students and the ability to continue normal operations. The State appropriations are a critical source of funding for the University.

The State appropriations are received through an allotment and requisition system through the North Carolina Office of State Budget and Management and the North Carolina Office of State Controller. There is no direct connection between the amount of tuition revenues collected by the University and the amount of State funds appropriated in any given year. For the fiscal year beginning July 1, 2007, and ending June 30, 2008, the appropriations from the State for the University were \$57.07 million for operations and \$7.41 million for capital projects. These appropriations were recorded by the University during the fiscal year. State appropriations increased during the fiscal year as a result of funding for enrollment growth, salary and benefit increases, inflationary increases granted as part of the Continuation Budget process, Focused Growth funding for Teacher Education and Nursing, a Summer Term Teacher Education Pilot Program, and funding for the Small Business Technology and Development Center.

Operating revenues include tuition and fees, operating grants and contracts, and sales and services, primarily to students (housing, dining, bookstore, health and other services). The increase in enrollment for the fiscal year was the primary reason for the increase in revenue for tuition and fees and sales and services. The University also had increases in the annual cost of Undergraduate Tuition (\$80), Graduate Tuition (\$526), and Ed Tech Fees (\$38) which were included in tuition and fees. The sales and services also increased due to increases in housing and dining rates and for housing revenue related to the leasing of additional space. The University completed a master lease for the second phase of the University Place Apartments, about 150 additional beds.

Operating expenses, including depreciation of \$3.35 million, totaled \$103.88 million. Of this total, \$48.32 million, or 46.52 percent, was used for instruction and academic support; \$10.42 million, or 10.03 percent, was used for institutional support; \$10.85 million, or 10.44 percent, was used for operations and maintenance of plant; and \$13.39 million, or 12.89 percent, was used for auxiliary enterprises.

There were salary increases of 4% for SPA employees and up to 5% for EPA employees. In addition, employer contributions increased for the State Health Plan by \$329 for the Indemnity Plan and \$198 for the Preferred Provider Plan and retirement contributions increased by .69%. These salary and benefits increases caused most of the increase in the salaries and benefits category for the fiscal year 2008. Also, several key EPA positions were filled in late 06-07 and remained filled for all of 07-08. The increase in operating expenses for services is primarily due to an increase in rent expense for the expanded University Place Apartment lease with Residence Life, discussed with the revenue increase earlier. Other increases were for telephone and data expenses as well as maintenance costs related to software, data and equipment.

One of the University's greatest strengths is the diverse streams of revenues that supplement student tuition and fees, including voluntary private support from individuals, foundations, and corporations, along with government and other sponsored programs, State appropriations, and investment income. The University has in the past and will continue to seek funding

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

aggressively from all possible sources consistent with its mission, to supplement student tuition, and prudently manage the financial resources realized from these efforts to fund its operating activities. During fiscal year 2008 the additions to permanent endowments includes one large gift of \$505,000 to create a new endowed fund named the Tony Rand Distinguished Professorship in Nursing.

Capital Assets

With the successful passage of the higher education bond referendum in November 2000 the University received a \$46 million allocation to enhance campus facilities. Major capital expenditures provided from the bond funding during the year ended June 30, 2008 include, the Lyons Renovation and Additions (\$1.72 million) and the Lilly Building Renovations (\$2.40 million).

Other capital projects for the fiscal year 2008 include repair and renovation expenditures of \$2.21 million. Planning continues on the Nursing Education and Research Center, a \$10 million project, and has started on a new residence hall. The total capital assets, net of accumulated depreciation, at June 30, 2008 were \$100.11 million. For more detailed information about asset holdings, see Note 5 of the Notes to the Financial Statements.

Factors Impacting Future Periods

Management believes that the University is well positioned to continue its strong financial condition and level of excellence in service to students, the community, and governmental agencies. This flexibility, along with the University's ongoing efforts toward revenue diversification and cost containment, will enable the University to provide the necessary resources to support this level of excellence. The University was under interim management for most of the fiscal year 2008. Recent more permanent changes include a new Chancellor and revisions to the management team in the summer of 2008. These changes are not considered to have a significant affect on the continued operations and financial position of FSU.

A crucial element to the University's future will continue to be our relationship with the State of North Carolina, as well as working to manage tuition and stay competitive while providing an outstanding college education for our students. There is a direct relationship between the growth of State support and the University's ability to control tuition growth, as declines in State appropriations generally result in increased tuition levels.

The University continues to execute its long-range plan to modernize and expand its complement of facilities with a balance of new construction. This strategy addresses the University's growth and the continuing effects of technology on teaching methodologies.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONCLUDED)

Private gifts are an important supplement to the fundamental support from the State, student tuition and fees, and other revenue sources. Gifts are a significant factor in the growth and support of academic units and support for student scholarships. Economic pressures affecting donors may affect the future level of support the University receives from corporate and individual giving, including the support received through the FSU Foundation, Inc.

The University will continue to employ its long-term investment strategy to maximize total returns, at an appropriate level of risk, while utilizing a spending rate policy to insulate the University's operations from temporary market volatility.

While it is not possible to predict the ultimate results, management believes that the University's financial condition is strong enough to weather any economic uncertainties.

Fayetteville State University
Statement of Net Assets
June 30, 2008

Exhibit A-1

ASSETS

Current Assets:

Cash and Cash Equivalents	\$ 5,474,517.29
Restricted Cash and Cash Equivalents	3,889,885.26
Receivables, Net (Note 4)	2,531,921.90
Inventories	220,081.12
Notes Receivable (Note 4)	512,870.54

Total Current Assets	<u>12,629,276.11</u>
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Noncurrent Assets:

Restricted Cash and Cash Equivalents	6,141,009.60
Interest Receivable	5,196.68
Restricted Due from Primary Government	1,682,017.62
Endowment Investments	5,279,398.23
Other Investments	450,178.17
Notes Receivable, Net (Note 4)	1,928,866.93
Capital Assets - Nondepreciable (Note 5)	7,739,335.36
Capital Assets - Depreciable, Net (Note 5)	92,375,422.80

Total Noncurrent Assets	<u>115,601,425.39</u>
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Total Assets	<u>128,230,701.50</u>
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LIABILITIES

Current Liabilities:

Accounts Payable and Accrued Liabilities (Note 6)	2,192,477.39
Due to Primary Government	28,921.40
Unearned Revenue	1,297,854.10
Interest Payable	65,586.10
Long-Term Liabilities - Current Portion (Note 7)	1,280,960.60

Total Current Liabilities	<u>4,865,799.59</u>
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Noncurrent Liabilities:

Funds Held for Others	742,751.31
U. S. Government Grants Refundable	1,900,025.49
Long-Term Liabilities (Note 7)	8,250,089.09

Total Noncurrent Liabilities	<u>10,892,865.89</u>
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Total Liabilities	<u>15,758,665.48</u>
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Fayetteville State University
Statement of Net Assets
June 30, 2008

Exhibit A-1
Page 2

NET ASSETS

Invested in Capital Assets, Net of Related Debt	93,870,583.47
Restricted for:	
Nonexpendable:	
Scholarships and Fellowships	855,911.59
Endowed Professorships	2,392,551.62
Loans	581,503.72
Expendable:	
Scholarships and Fellowships	478,857.66
Endowed Professorships	1,146,478.06
Departmental Uses	863,376.24
Capital Projects	4,804,253.45
Debt Service	1,006,022.90
Unrestricted	6,472,497.31
Total Net Assets	<u><u>\$ 112,472,036.02</u></u>

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

***Fayetteville State University
Statement of Revenues, Expenses, and
Changes in Net Assets
For the Fiscal Year Ended June 30, 2008***

Exhibit A-2

REVENUES

Operating Revenues:	
Student Tuition and Fees, Net (Note 9)	\$ 14,936,776.10
Federal Grants and Contracts	12,877,504.67
Sales and Services, Net (Note 9)	8,015,670.50
Interest Earnings on Loans	1,502.65
Other Operating Revenues	102,557.98
	<hr/>
Total Operating Revenues	35,934,011.90

EXPENSES

Operating Expenses:	
Salaries and Benefits	60,882,928.63
Supplies and Materials	9,295,402.27
Services	17,835,201.10
Scholarships and Fellowships	9,557,935.99
Utilities	2,955,108.03
Depreciation	3,350,748.68
	<hr/>
Total Operating Expenses	103,877,324.70
	<hr/>
Operating Loss	(67,943,312.80)

NONOPERATING REVENUES (EXPENSES)

State Appropriations	57,072,854.89
Noncapital Grants	8,588,739.35
Noncapital Gifts	760,649.68
Investment Income (Net of Investment Expense of \$20,483.02)	356,461.31
Interest and Fees on Debt	(298,489.76)
Other Nonoperating Revenues	5,179.47
	<hr/>
Net Nonoperating Revenues	66,485,394.94
	<hr/>
Loss Before Other Revenues	(1,457,917.86)

Capital Appropriations	1,606,000.00
Capital Grants	5,803,559.83
Additions to Endowments	824,707.09
	<hr/>
Increase in Net Assets	6,776,349.06

NET ASSETS

Net Assets - July 1, 2007, as Restated (Note 16)	<hr/> 105,695,686.96
Net Assets - June 30, 2008	<hr/> <hr/> \$ 112,472,036.02

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

Fayetteville State University
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2008

Exhibit A-3

CASH FLOWS FROM OPERATING ACTIVITIES

Received from Customers	\$ 36,620,674.21
Payments to Employees and Fringe Benefits	(60,952,805.96)
Payments to Vendors and Suppliers	(30,249,594.87)
Payments for Scholarships and Fellowships	(9,557,935.99)
Loans Issued	(462,587.96)
Collection of Loans	269,879.13
Interest Earned on Loans	2,300.89
Other Receipts	56,060.80
	<hr/>
Net Cash Used by Operating Activities	(64,274,009.75)

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

State Appropriations	57,072,854.89
Noncapital Grants	8,588,739.35
Noncapital Gifts	760,649.68
Additions to Endowments	824,707.09
Federal Family Education Loan Receipts	26,202,538.77
Federal Family Education Loan Disbursements	(26,621,834.36)
Related Activity Agency Receipts	412,669.60
	<hr/>
Net Cash Provided by Noncapital Financing Activities	67,240,325.02

CASH FLOWS FROM CAPITAL FINANCING AND RELATED FINANCING ACTIVITIES

State Capital Appropriations	1,606,000.00
Capital Grants	5,516,486.42
Acquisition and Construction of Capital Assets	(8,561,442.01)
Principal Paid on Capital Debt and Leases	(732,293.31)
Interest and Fees Paid on Capital Debt and Leases	(296,910.54)
Other Receipts	5,179.47
	<hr/>
Net Cash Used by Capital Financing and Related Financing Activities	(2,462,979.97)

CASH FLOWS FROM INVESTING ACTIVITIES

Proceeds from Sales and Maturities of Investments	890,000.00
Investment Income	664,166.34
Purchase of Investments and Related Fees	(901,892.35)
	<hr/>
Net Cash Provided by Investing Activities	652,273.99
	<hr/>
Net Increase in Cash and Cash Equivalents	1,155,609.29
Cash and Cash Equivalents - July 1, 2007	14,349,802.86
	<hr/>
Cash and Cash Equivalents - June 30, 2008	\$ 15,505,412.15

Fayetteville State University
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2008

Exhibit A-3

Page 2

**RECONCILIATION OF NET OPERATING EXPENSES
TO NET CASH USED BY OPERATING ACTIVITIES**

Operating Loss	\$ (67,943,312.80)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:	
Depreciation Expense	3,350,748.68
Allowances, Write-Offs, and Amortizations	416,406.00
Changes in Assets and Liabilities:	
Receivables (Net)	92,076.02
Inventories	29,563.41
Accounts Payable and Accrued Liabilities	(263,061.31)
Due to Primary Government	(3,725.87)
U.S. Government Grants Refundable	56,060.80
Unearned Revenue	113,142.15
Compensated Absences	70,802.00
Student Loan Principal Repayments	269,879.13
Student Loans Issued	(462,587.96)
Net Cash Used by Operating Activities	<u><u>\$ (64,274,009.75)</u></u>

RECONCILIATION OF CASH AND CASH EQUIVALENTS

Current Assets:	
Cash and Cash Equivalents	\$ 5,474,517.29
Restricted Cash and Cash Equivalents	3,889,885.26
Noncurrent Assets:	
Restricted Cash and Cash Equivalents	<u>6,141,009.60</u>
Total Cash and Cash Equivalents - June 30, 2008	<u><u>\$ 15,505,412.15</u></u>

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

Assets Acquired through the Assumption of a Liability	\$ 1,451,468.00
Change in Fair Value of Investments	(309,631.10)

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

Fayetteville State University Foundation, Inc., and Subsidiary
Consolidated Statement of Financial Position
June 30, 2008

Exhibit B-1

ASSETS

Current Assets:

Cash in Bank	\$ 2,006,156
Cash in Bank - Housing Foundation	1,408,321
Accounts Receivable	3,300
Investments - Land for Sale	441,122
Investments	2,598,032

Total Current Assets	6,456,931
----------------------	-----------

Property, Plant and Equipment:

Furniture and Equipment	1,100,733
Land and Buildings	12,424,385

	13,525,118
Less: Accumulated Depreciation	2,729,829

Net Property and Equipment	10,795,289
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Total Assets	\$ 17,252,220
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LIABILITIES AND NET ASSETS

Current Liabilities:

Accounts Payable	\$ 13,996
Current Maturities of Long-Term Debt	235,000
Security Deposits	34,439

Total Current Liabilities	283,435
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Long-Term Debt	13,800,000
----------------	------------

Net Assets:

Unrestricted:	
Subsidiary - FSU Housing Foundation	(3,438,681)
Fayetteville State University Foundation	969,651
Temporarily Restricted:	
Subsidiary - FSU Housing Foundation	1,373,882
Fayetteville State University Foundation	1,882,731
Permanently Restricted	2,381,202

Total Net Assets	3,168,785
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Total Liabilities and Net Assets	\$ 17,252,220
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The accompanying notes to the financial statements are an integral part of this statement.

Fayetteville State University Foundation, Inc., and Subsidiary
Consolidated Statement of Activities
For the Fiscal Year Ended June 30, 2008

Exhibit B-2

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
SUPPORT				
Gifts and Donations	\$ 107,652	\$ 112,041	\$ 75,281	\$ 294,974
Total Support	107,652	112,041	75,281	294,974
REVENUE				
Interest and Dividend Income	57,054	78,490		135,544
Gain (Loss) on Investments	(1,050)	176,728		175,678
Insurance Recoveries	43,715			43,715
Miscellaneous Income	646			646
Rental Income	1,303,447			1,303,447
Net Mandatory Transfers to and from Debt Service Reserve Accounts	(536,563)	536,563		
Net Assets Released from Restrictions	56,401	(56,401)		
Total Revenue	923,650	735,380		1,659,030
Total Support and Revenue	1,031,302	847,421	75,281	1,954,004
OPERATING EXPENSES				
Program Services	1,881,665			1,881,665
Management and General	9,467			9,467
Fund Raising Expenses	11,683			11,683
Total Operating Expenses	1,902,815			1,902,815
Increase (Decrease) in Net Assets	(871,513)	847,421	75,281	51,189
NET ASSETS				
Beginning of Year	(1,597,517)	2,409,192	2,305,921	3,117,596
End of Year	<u>\$ (2,469,030)</u>	<u>\$ 3,256,613</u>	<u>\$ 2,381,202</u>	<u>\$ 3,168,785</u>

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

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**FAYETTEVILLE STATE UNIVERSITY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2008**

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. Fayetteville State University is a constituent institution of the multi-campus University of North Carolina System, which is a component unit of the State of North Carolina and an integral part of the State's *Comprehensive Annual Financial Report*.

The accompanying financial statements present all funds belonging to the University and its component units. While the Board of Governors of the University of North Carolina System has ultimate responsibility, the Chancellor, the Board of Trustees, and the Board of Trustees of the Endowment Fund have delegated responsibilities for financial accountability of the University's funds. The University's component unit is discretely presented in the University's financial statements. The discretely presented component unit's financial data are reported in separate financial statements because of its use of different GAAP reporting models and to emphasize its legal separateness.

Discretely Presented Component Unit – The Fayetteville State University Foundation, Inc. and Subsidiary (Foundation) is a legally separate, tax-exempt not-for-profit corporation and is reported as a discretely presented component unit based on the nature and significance of its relationship to the University. The Fayetteville State University Housing Foundation, LLC is a wholly owned subsidiary of the Foundation. Its primary purpose is to build, maintain, and manage a student housing facility for students of Fayetteville State University.

The Foundation acts primarily as a fund-raising organization to supplement the resources that are available to the University in support of its programs. The Foundation board consists of 35 directors. Although the University does not control the timing or amount of receipts from the Foundation, the majority of resources, or income thereon, that the Foundation holds and invests, are restricted to the activities of the University by the donors. Because these restricted resources held by the

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Foundation can only be used by, or for the benefit of the University, the Foundation is considered a component unit of the University and is reported in separate financial statements because of the difference in its reporting model, as described below.

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

During the year ended June 30, 2008, the Foundation distributed \$75,901.00 to the University for both restricted and unrestricted purposes. Complete financial statements for the Foundation can be obtained from Fayetteville State University Foundation, Inc., and Subsidiary at (910) 672-1151.

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

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

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

- C. Basis of Accounting** - The financial statements of the University have been prepared using the economic resource measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred, regardless of the timing of the cash flows.

Nonexchange transactions, in which the University receives (or gives) value without directly giving (or receiving) equal value in exchange

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

includes State appropriations, certain grants, and donations. Revenues are recognized, net of estimated uncollectible amounts, as soon as all eligibility requirements imposed by the provider have been met, if probable of collection.

D. Cash and Cash Equivalents – This classification includes undeposited receipts, petty cash, cash on deposit with private bank accounts, money market accounts, cash on deposit with fiscal agents, and deposits held by the State Treasurer in the short-term investment fund. The short-term investment fund maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit and withdraw cash at any time without prior notice or penalty.

E. Investments - Investments generally are reported at fair value, as determined by quoted market prices. The net increase (decrease) in the fair value of investments is recognized as a component of investment income.

Endowment investments include the principal amount of gifts and bequests that, according to donor restrictions, must be held in perpetuity or for a specified period of time, along with any accumulated investment earnings on such amounts. Further, endowment investments also include amounts internally designated by the University for investment in an endowment capacity (i.e. quasi-endowments), along with accumulated investment earnings on such amounts.

F. Receivables – Receivables consist of tuition and fees charged to students and charges for auxiliary enterprises' sales and services. Receivables also include amounts due from the federal government, State and local governments, private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants, that are verifiable, measurable, and expected to be collected and available for expenditures for which the resource provider's conditions have been satisfied. Receivables are recorded net of estimated uncollectible amounts.

G. Inventories – Inventories, consisting of expendable supplies, are valued at last invoice cost. Merchandise for resale is valued 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 value of assets constructed includes all material direct and indirect construction costs. Interest costs incurred are capitalized during the period of construction.

The University capitalizes assets that have a value or cost in excess of \$5,000 at the date of acquisition and an estimated useful life of more than one year. Library books are generally not considered to have a useful life

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 35 to 50 years for general infrastructure, 50 to 75 years for buildings, and 7 to 35 years for equipment.

The University does not capitalize its art collection. This collection adheres to the University's policy to maintain for public exhibition, education or research; protect, keep unencumbered, care for and preserve; and requires proceeds from their sale to be used to acquire other collection items. Accounting principles generally accepted in the United States of America permit collections maintained in this manner to be charged to operations at time of purchase rather than be capitalized.

- I. Restricted Assets** – Certain resources are reported as restricted assets because restrictions on asset use change the nature or normal understanding of the availability of the asset. Resources that are not available for current operations and are reported as restricted include resources restricted or designated for the acquisition or construction of capital assets and resources legally segregated for the payment of principal and interest as required by debt covenants.
- J. Noncurrent Long-Term Liabilities** – Noncurrent long-term liabilities include principal amounts of bonds payable, capital lease obligations, and compensated absences that will not be paid within the next fiscal year.

The University's bond premiums/discounts are considered immaterial and are expensed.

- K. Compensated Absences** - The University's policy is to record the cost of vacation leave when earned. The policy provides for a maximum accumulation of unused vacation leave of 30 days which can be carried forward each January 1 or for which an employee can be paid upon termination of employment. When classifying compensated absences into current and noncurrent, leave is considered taken using a last-in, first-out (LIFO) method. Also, any accumulated vacation leave in excess of 30 days at year-end is converted to sick leave. Under this policy, the accumulated vacation leave for each employee at June 30 equals the leave carried forward at the previous December 31 plus the leave earned, less the leave taken between January 1 and June 30.

In addition to the vacation leave described above, compensated absences include the accumulated unused portion of the special annual leave bonuses awarded by the North Carolina General Assembly. The bonus leave balance on December 31 is retained by employees and transferred into the next calendar year. It is not subject to the limitation on annual

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

leave carried forward described above and is not subject to conversion to sick leave.

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

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

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

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

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

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

Restricted and unrestricted resources are tracked using a fund accounting system and are spent in accordance with established fund authorities. Fund authorities provide rules for the fund activity and are separately established for restricted and unrestricted activities. When both restricted and unrestricted funds are available for expenditure, the decision for funding is transactional based within the departmental management system in place at the University. For projects funded by tax-exempt debt proceeds and other sources, the debt proceeds are always used first.

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

accompanying Statement of Revenues, Expenses, and Changes in Net Assets. To the extent that revenues from these programs are used to satisfy tuition, fees, and other charges, the University has recorded a scholarship discount.

- N. Revenue and Expense Recognition** – The University classifies its revenues and expenses as operating or nonoperating in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the University's principal ongoing operations. Operating revenues include activities that have characteristics of exchange transactions, such as (1) student tuition and fees, (2) sales and services of auxiliary enterprises, (3) certain federal, State and local grants and contracts that are essentially contracts for services, and (4) interest earned on loans. Operating expenses are all expense transactions incurred other than those related to capital and noncapital financing or investing activities as defined by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*.

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

- O. Internal Sales Activities** – Certain institutional auxiliary operations provide goods and services to University departments, as well as to its customers. These institutional auxiliary operations include activities such as central stores and printing. In addition, the University has other miscellaneous sales and service units that operated either on a reimbursement or charge basis. All internal sales activities to University departments from auxiliary operations and sales and service units have been eliminated in the accompanying financial statements. These eliminations are recorded by removing the revenue and expense in the auxiliary operations and sales and service units and, if significant, allocating any residual balances to those departments receiving the goods and services during the year.

NOTE 2 - DEPOSITS AND INVESTMENTS

- A. Deposits** – Unless specifically exempt, the University is required by *North Carolina General Statute 147-77* to deposit moneys received with

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

At June 30, 2008, the amount shown on the Statement of Net Assets as cash and cash equivalents includes \$15,332,200.78 which represents the University's equity position in the State Treasurer's Short-Term Investment Fund. The Short-Term Investment Fund (a portfolio within the State Treasurer's Investment Pool, an external investment pool that is not registered with the Securities and Exchange Commission and does not have a credit rating) had a weighted average maturity of 2.9 years as of June 30, 2008. Assets and shares of the Short-Term Investment Fund are valued at amortized cost, which approximates fair value. Deposit and investment risks associated with the State Treasurer's Investment Pool (which includes the State Treasurer's Short-Term Investment Fund) are included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.ncosc.net/> and clicking on "Financial Reports," or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

Cash on hand at June 30, 2008 was \$9,500.00. The carrying amount of the University's deposits not with the State Treasurer was \$163,711.37 and the bank balance was \$161,478.81. Custodial credit risk is the risk that in the event of a bank failure, the University's deposits may not be returned to it. Pursuant to G.S. 116-36.1, funds received for health care services not deposited with the State Treasurer shall be fully secured in the manner as prescribed by the State Treasurer for the security of public deposits. The University does not have a deposit policy for custodial credit risk. As of June 30, 2008, the University's bank balance was covered by federal depository insurance except \$59,779.71 which was exposed to custodial credit risk and held as uninsured and uncollateralized by the bank per bond covenants.

- B. Investments - University** - The University is authorized by The University of North Carolina Board of Governors pursuant to G.S. 116-36.2 and Section 600.2.4 of the Policy Manual of the University of North Carolina, to invest its special funds and funds received for

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

services rendered by health care professionals in the same manner as the State Treasurer is required to invest, as discussed below.

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

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

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

Investments of the University's component unit, The Fayetteville State University Foundation, Inc., and Subsidiary 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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Investments are subject to the following risks.

Interest Rate Risk: Interest rate risk is the risk the University may face should interest rate variances affect the fair value of investments. The University does not have a formal policy that addresses interest rate risk.

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

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

The following table presents the fair value of investments by type and investments subject to interest rate risk at June 30, 2008.

Investments			
Investment Type	Fair Value	Investment Maturities (in Years)	
		Less Than 1	1 to 5
Debt Securities:			
U.S. Treasuries	\$ 450,178.17	\$ 450,178.17	\$ 0.00
Mutual Bond Funds	1,779,935.54		1,779,935.54
		<u>\$ 450,178.17</u>	<u>\$ 1,779,935.54</u>
Other Securities			
Other Mutual Funds	<u>3,499,462.69</u>		
Total Investment	<u>\$ 5,729,576.40</u>		

The University's mutual bond funds held at June 30, 2008, were unrated.

Component Unit - Investments of the University's discretely presented component unit, the Fayetteville State University Foundation, Inc. and Subsidiary, are subject to and restricted by G.S. 36B "Uniform Management of Institutional Funds Act" (UMIFA) and any requirements placed on them by contract or donor agreements. Because the Foundation report is under the FASB reporting model, disclosures of the various investment risks are not required. The following is an analysis of investments by type:

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Fayetteville State University Foundation, Inc. and Subsidiary

Investments are presented in the financial statements at fair market value. Investments earned \$13,446 during the year ended June 30, 2008, and incurred management fees of \$14,593. Investments within the account are composed of the following:

	<u>Cost</u>	<u>Market</u>	<u>Unrealized Appreciation</u>
UNC Investment Fund	<u>\$ 2,559,375</u>	<u>\$ 2,598,032</u>	<u>\$ 38,657</u>

Investments also include donated land which is available for sale. At June 30, 2008 land value totaled \$441,122.

NOTE 3 - ENDOWMENT INVESTMENTS

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

Investment return of the University's endowment funds is predicated on the total return concept (yield plus appreciation). The University's endowment spending policy governs the rate at which funds are released to the operating budget from the endowment. The University uses a disciplined spending rate with a long-term spending rule. The target rate for spending is set between 4% and 6% of the endowment's three-year average year end market value. In order to preserve the purchasing power of the endowment, the portfolio is invested with the expectation of generating a long-term rate of return at least equal to the payout plus the rate of inflation. At June 30, 2008, net appreciation of \$4,271,786.96 was available to be spent, of which \$1,386,256.46 was restricted to specific purposes.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 4 - RECEIVABLES

Receivables at June 30, 2008, were as follows:

	Gross Receivables	Less Allowance for Doubtful Accounts	Net Receivables
Current Receivables:			
Students	\$ 1,519,707.75	\$ 760,912.33	\$ 758,795.42
Accounts	187,451.97		187,451.97
Intergovernmental	1,473,867.63	93,794.20	1,380,073.43
Investment Earnings	35,820.10		35,820.10
Interest on Loans	39,901.00		39,901.00
Other	257,545.97	127,665.99	129,879.98
Total Current Receivables	<u>\$ 3,514,294.42</u>	<u>\$ 982,372.52</u>	<u>\$ 2,531,921.90</u>
Notes Receivable:			
Notes Receivable - Current:			
Federal Loan Programs	\$ 475,969.15	\$ 0.00	\$ 475,969.15
Institutional Student Loan Programs	36,901.39		36,901.39
Total Notes Receivable - Current	<u>\$ 512,870.54</u>	<u>\$ 0.00</u>	<u>\$ 512,870.54</u>
Notes Receivable - Noncurrent:			
Federal Loan Programs	<u>\$ 2,357,133.75</u>	<u>\$ 428,266.82</u>	<u>\$ 1,928,866.93</u>

NOTE 5 - CAPITAL ASSETS

A summary of changes in the capital assets for the year ended June 30, 2008, is presented as follows:

	Balance July 1, 2007 (as restated)	Increases	Decreases	Balance June 30, 2008
Capital Assets, Nondepreciable:				
Land	\$ 963,243.22	\$ 0.00	\$ 0.00	\$ 963,243.22
Construction in Progress	23,807,163.12	5,884,263.70	22,915,334.68	6,776,092.14
Total Capital Assets, Nondepreciable	<u>24,770,406.34</u>	<u>5,884,263.70</u>	<u>22,915,334.68</u>	<u>7,739,335.36</u>
Capital Assets, Depreciable:				
Buildings	85,552,974.13	22,915,334.68		108,468,308.81
Machinery and Equipment	6,773,470.83	1,745,143.32	169,509.10	8,349,105.05
General Infrastructure	2,786,625.27	685,994.00		3,472,619.27
Total Capital Assets, Depreciable	<u>95,113,070.23</u>	<u>25,346,472.00</u>	<u>169,509.10</u>	<u>120,290,033.13</u>
Less Accumulated Depreciation/Amortization for:				
Buildings	20,139,465.12	2,294,579.28		22,434,044.40
Machinery and Equipment	3,144,123.07	924,056.74	161,967.94	3,906,211.87
General Infrastructure	1,442,241.40	132,112.66		1,574,354.06
Total Accumulated Depreciation	<u>24,725,829.59</u>	<u>3,350,748.68</u>	<u>161,967.94</u>	<u>27,914,610.33</u>
Total Capital Assets, Depreciable, Net	<u>70,387,240.64</u>	<u>21,995,723.32</u>	<u>7,541.16</u>	<u>92,375,422.80</u>
Capital Assets, Net	<u>\$ 95,157,646.98</u>	<u>\$ 27,879,987.02</u>	<u>\$ 22,922,875.84</u>	<u>\$ 100,114,758.16</u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2008, were as follows:

	Amount
Accounts Payable	\$ 852,276.53
Accrued Payroll	1,013,938.15
Contract Retainage	326,262.71
Total Accounts Payable and Accrued Liabilities	\$ 2,192,477.39

NOTE 7 - LONG-TERM LIABILITIES

A. Changes in Long-Term Liabilities - A summary of changes in the long-term liabilities for the year ended June 30, 2008, is presented as follows:

	Balance July 1, 2007	Additions	Reductions	Balance June 30, 2008	Current Portion
Revenue Bonds Payable	\$ 5,525,000.00	\$ 0.00	\$ 570,000.00	\$ 4,955,000.00	\$ 590,000.00
Capital Leases Payable		1,451,468.00	162,293.31	1,289,174.69	267,604.60
Compensated Absences	3,216,073.00	1,643,793.00	1,572,991.00	3,286,875.00	423,356.00
Total Long-Term Liabilities	\$ 8,741,073.00	\$ 3,095,261.00	\$ 2,305,284.31	\$ 9,531,049.69	\$ 1,280,960.60

Additional information regarding capital lease obligations is included in Note 8.

B. Revenue Bonds Payable - The University was indebted for revenue bonds payable for the purposes shown in the following table:

Purpose	Series	Interest Rate/ Ranges	Final Maturity Date	Original Amount of Issue	Principal Paid Through June 30, 2008	Principal Outstanding June 30, 2008
Dormitory System						
Dormitory System Revenue Bond	1975B	8.0%-10.0%	10/01/2009	\$ 1,750,000.00	\$ 1,500,000.00	\$ 250,000.00 (1)
The University of North Carolina System Pool Revenue Bonds						
Refunding of U.S. Department of Education Notes Payable	2002B	3.5%-5.375%	04/01/2022	1,245,000.00	250,000.00	995,000.00
Stadium Renovation	2002B	3.5%-5.0%	04/01/2012	2,735,000.00	1,445,000.00	1,290,000.00
Dining	2005B	3.5%-4.5%	04/01/2023	2,770,000.00	350,000.00	2,420,000.00
Total The University of North Carolina System Pool Revenue Bonds				6,750,000.00	2,045,000.00	4,705,000.00
Total Bonds Payable (principal only)				\$ 8,500,000.00	\$ 3,545,000.00	\$ 4,955,000.00

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The University has pledged future revenues, net of specific operating expenses, to repay revenue bonds as shown in the table below:

Ref	Revenue Source	Total Future Revenues Pledged	Current Year Revenues Net of Expenses	Current Year Principal & Interest	Estimate of % of Revenues Pledged
(1)	Housing Revenues	\$ 270,910.00	\$ 513,481.08	\$ 135,010.00	26%

- C. Annual Requirements** - The annual requirements to pay principal and interest on the long-term obligations at June 30, 2008, are as follows:

	Annual Requirements	
	Bonds Payable	
Fiscal Year	Principal	Interest
2009	\$ 590,000.00	\$ 225,737.50
2010	625,000.00	197,887.50
2011	515,000.00	169,057.50
2012	545,000.00	145,257.50
2013	200,000.00	120,107.50
2014-2018	1,150,000.00	463,125.02
2019-2023	1,330,000.00	177,850.02
Total Requirements	<u>\$ 4,955,000.00</u>	<u>\$ 1,499,022.54</u>

- D.** The University has extinguished long-term obligations by the issuance of new long-term debt instruments as follows:

Prior Year Bond Defeasance - During prior years, the University defeased certain bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the University's financial statements. At June 30, 2008, the outstanding balance of prior year defeased bonds was \$2,260,000.00.

E. Component Unit – Long-Term Debt

Fayetteville State University Foundation, Inc., and Subsidiary

Long-term debt at June 30, 2008 consisted of a North Carolina Student Housing Facilities Revenue Bond with a balance of \$14,035,000, secured by real property. The Foundation has entered into an interest rate swap agreement to lock in the interest rate on 90% of the bond at 3.45%. The remainder of the bond is at a variable interest rate based on the BMA

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

index. The buildings are used as housing for students of Fayetteville State University.

Maturities of long term debt are as follows:

<u>Fiscal Year</u>	<u>Amount</u>
2009	\$ 235,000.00
2010	245,000.00
2011	260,000.00
2012	275,000.00
2013	290,000.00
2014-2018	<u>\$ 12,730,000.00</u>
Total Foundation Long-Term Debt	<u><u>\$ 14,035,000.00</u></u>

NOTE 8 - LEASE OBLIGATIONS

A. Capital Lease Obligations - Capital lease obligations relating to synthetic turf for the athletic field and computer networking equipment are recorded at the present value of the minimum lease payments. Future minimum lease payments under capital lease obligations consist of the following at June 30, 2008:

<u>Fiscal Year</u>	<u>Amount</u>
2009	\$ 349,874.12
2010	349,874.12
2011	349,874.12
2012	188,958.44
2013	120,358.80
2014-2018	<u>150,448.50</u>
Total Minimum Lease Payments	1,509,388.10
Amount Representing Interest (Imputed Interest Rates range from 5.46% to 8.95%)	<u>220,213.41</u>
Present Value of Future Lease Payments	<u><u>\$ 1,289,174.69</u></u>

Machinery and equipment acquired under capital lease amounted to \$765,474.00 and landscaping assets (turf) amounted to \$685,994.00 at June 30, 2008. Depreciation on these assets at June 30, 2008 amounted to \$118,550.72.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

B. Operating Lease Obligations – The University entered into operating leases for 341 beds at University Place Apartments, space at Bronco Square (for the University Bookstore), modular buildings, computer networking equipment and printers (including hardware and service). Future minimum lease payments under noncancelable operating leases consist of the following at June 30, 2008:

<u>Fiscal Year</u>	<u>Amount</u>
2009	\$ 2,426,128.62
2010	2,421,437.42
2011	2,409,657.88
2012	816,661.80
2013	781,119.30
Total Minimum Lease Payments	<u>\$ 8,855,005.02</u>

Rental expense for all operating leases during the year was \$1,834,860.93.

NOTE 9 - REVENUES

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

	<u>Gross Revenues</u>	<u>Internal Sales Eliminations</u>	<u>Less Scholarship Discounts</u>	<u>Less Allowance for Uncollectibles</u>	<u>Net Revenues</u>
Operating Revenues:					
Student Tuition and Fees	<u>\$ 21,476,818.00</u>	<u>\$ 0.00</u>	<u>\$ 5,691,717.85</u>	<u>\$ 848,324.05</u>	<u>\$ 14,936,776.10</u>
Sales and Services:					
Sales and Services of Auxiliary Enterprises:					
Residential Life	\$ 5,375,130.63	\$ 0.00	\$ 1,333,079.68	\$ 49,961.33	\$ 3,992,089.62
Dining	3,502,546.55		912,950.12	63,228.20	2,526,368.23
Bookstore	133,526.93				133,526.93
Other	1,905,778.20	926,467.04		20,858.93	958,452.23
Sales and Services of Education and Related Activities	<u>405,233.49</u>				<u>405,233.49</u>
Total Sales and Services	<u>\$ 11,322,215.80</u>	<u>\$ 926,467.04</u>	<u>\$ 2,246,029.80</u>	<u>\$ 134,048.46</u>	<u>\$ 8,015,670.50</u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 10 - OPERATING EXPENSES BY FUNCTION

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

	Salaries and Benefits	Supplies and Materials	Services	Scholarships and Fellowships	Utilities	Depreciation	Total
Instruction	\$ 33,834,824.82	\$ 1,534,813.03	\$ 1,855,132.67	\$ 0.00	\$ 0.00	\$ 0.00	\$ 37,224,770.52
Research	528,802.53	295,410.62	112,147.84				936,360.99
Public Service	1,914,693.19	212,749.37	840,910.10				2,968,352.66
Academic Support	5,763,113.83	2,952,118.99	2,383,900.61				11,099,133.43
Student Services	3,020,865.29	210,511.69	510,145.50				3,741,522.48
Institutional Support	6,511,895.69	360,116.82	3,543,630.97				10,415,643.48
Operations and Maintenance of Plant	5,047,045.19	2,457,259.97	1,163,914.02		2,185,060.72		10,853,279.90
Student Financial Aid	321,661.70	11,600.12	4,545.51	9,557,935.99			9,895,743.32
Auxiliary Enterprises	3,940,026.39	1,260,821.66	7,420,873.88		770,047.31		13,391,769.24
Depreciation						3,350,748.68	3,350,748.68
Total Operating Expenses	\$ 60,882,928.63	\$ 9,295,402.27	\$ 17,835,201.10	\$ 9,557,935.99	\$ 2,955,108.03	\$ 3,350,748.68	\$ 103,877,324.70

NOTE 11 - PENSION PLANS

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

The Teachers' and State Employees' Retirement System is a cost sharing multiple-employer defined benefit pension plan established by the State to provide pension benefits for employees of the State, its component units and local boards of education. The plan is administered by the North Carolina State Treasurer.

Benefit and contribution provisions for the Teachers' and State Employees' Retirement System are established by *North Carolina General Statutes* 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contribution rates are set each year by the North Carolina General Assembly based on annual actuarial valuations. For the year ended June 30, 2008, these rates were set at 3.05% of covered payroll for employers and 6% of covered payroll for members.

For the current fiscal year, the University had a total payroll of \$49,583,567.46, of which \$29,675,589.18 was covered under the Teachers' and State Employees' Retirement System. Total employer and employee contributions for pension benefits for the year were \$905,105.47 and \$1,780,535.35, respectively.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Required employer contribution rates for the years ended June 30, 2007, and 2006, were 2.66% and 2.34%, respectively, while employee contributions were 6% each year. The University made 100% of its annual required contributions for the years ended June 30, 2008, 2007, and 2006, which were \$905,105.47, \$712,913.53, and \$568,392.83, respectively.

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

The Optional Retirement Program (Program) is a defined contribution retirement plan that provides retirement benefits with options for payments to beneficiaries in the event of the participant's death. Administrators and eligible faculty of the University may join the Program instead of the Teachers' and State Employees' Retirement System. The Board of Governors of The University of North Carolina is responsible for the administration of the Program and designates the companies authorized to offer investment products or the trustee responsible for the investment of contributions under the Program and approves the form and contents of the contracts and trust agreements.

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

Participant eligibility and contributory requirements are established by General Statute 135-5.1. Employer and member contribution rates are set each year by the North Carolina General Assembly. For the year ended June 30, 2008, these rates were set at 6.84% of covered payroll for employers and 6% of covered payroll for members. The University assumes no liability other than its contribution.

For the current fiscal year, the University had a total payroll of \$49,583,567.46, of which \$14,748,733.10 was covered under the Optional Retirement Program. Total employer and employee contributions for pension benefits for the year were \$1,008,813.34 and \$884,923.99, respectively.

B. Deferred Compensation and Supplemental Retirement Income Plans - IRC Section 457 Plan - The State of North Carolina offers its permanent employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457 through the North Carolina Public Employee Deferred Compensation Plan (the Plan). The Plan permits each participating employee to defer a portion of his or her salary until future years. The deferred compensation is available to employees upon separation from service, death, disability, retirement, or financial hardships if approved by the Board of Trustees of the Plan. The Board, a part of the North Carolina Department of Administration, maintains a separate fund for the exclusive benefit of the participating employees and their beneficiaries, *the North Carolina Public Employee Deferred Compensation Trust Fund*. The Board also contracts with an external third party to perform certain administrative requirements and to manage the trust fund's assets. All costs of administering and funding the Plan are the responsibility of the Plan participants. No costs are incurred by the University. The voluntary contributions by employees amounted to \$124,804.32 for the year ended June 30, 2008.

IRC Section 401(k) Plan - All members of the Teachers' and State Employees' Retirement System and the Optional Retirement Program are eligible to enroll in the Supplemental Retirement Income Plan, a defined contribution plan, created under Internal Revenue Code Section 401(k). All costs of administering the Plan are the responsibility of the Plan participants. No costs are incurred by the University except for a 5% employer contribution for the University's law enforcement officers, which is mandated under General Statute 143-166.30(e). Total employer contributions on behalf of University law enforcement officers for the year ended June 30, 2008, were \$33,270.49. The voluntary contributions by employees amounted to \$198,544.00 for the year ended June 30, 2008.

IRC Section 403(b) and 403(b)(7) Plans - Eligible University employees can participate in tax sheltered annuity plans created under Internal Revenue Code Sections 403(b) and 403(b)(7). The employee's eligible contributions, made through salary reduction agreements, are exempt from federal and State income taxes until the annuity is received or the contributions are withdrawn. These plans are exclusively for employees of universities and certain charitable and other nonprofit institutions. All costs of administering and funding these plans are the responsibility of the Plan participants. No costs are incurred by the University. The voluntary contributions by employees amounted to \$627,938.60 for the year ended June 30, 2008.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 12 - OTHER POSTEMPLOYMENT BENEFITS

- A. Health Benefits** - The University participates in the Comprehensive Major Medical Plan (the Plan), a cost-sharing, multiple-employer defined benefit health care plan that provides postemployment health insurance to eligible former employees. Eligible former employees include long-term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers' and State Employees' Retirement System or the Optional Retirement Program. Coverage eligibility varies depending on years of contributory membership service in their retirement system prior to disability or retirement.

The Plan's benefit and contribution provisions are established by Chapter 135-7, Article 1, and Chapter 135, Article 3, of the General Statutes and may be amended only by the North Carolina General Assembly. The Plan does not provide for automatic post-retirement benefit increases.

By General Statute, a Retiree Health Benefit Fund (the Fund) has been established as a fund in which accumulated contributions from employers and any earnings on those contributions shall be used to provide health benefits to retired and disabled employees and applicable beneficiaries. By statute, the Fund is administered by the Board of Trustees of the Teachers' and State Employees' Retirement System and contributions to the fund are irrevocable. Also by law, Fund assets are dedicated to providing benefits to retired and disabled employees and applicable beneficiaries and are not subject to the claims of creditors of the employers making contributions to the Fund. Contribution rates to the Fund, which are intended to finance benefits and administrative expenses on a pay-as-you-go basis, are determined by the General Assembly in the Appropriations Bill.

For the current fiscal year the University contributed 4.1% of the covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the Fund. Required contribution rates for the years ended June 30, 2007, and 2006, were 3.8% and 3.8%, respectively. The University made 100% of its annual required contributions to the Plan for the years ended June 30, 2008, 2007, and 2006, which were \$1,821,397.21, \$1,512,574.38, and \$1,343,337.21, respectively. The University assumes no liability for retiree health care benefits provided by the programs other than its required contribution.

Additional detailed information about these programs can be located in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

<http://www.ncosc.net/> and clicking on “Financial Reports,” or by calling the State Controller’s Financial Reporting Section at (919) 981-5454.

- B. Disability Income** - The University participates in the Disability Income Plan of North Carolina (DIPNC), a cost-sharing, multiple-employer defined benefit plan, to provide short-term and long-term disability benefits to eligible members of the Teachers’ and State Employees’ Retirement System and the Optional Retirement Program. Benefit and contribution provisions are established by Chapter 135, Article 6, of the General Statutes, and may be amended only by the North Carolina General Assembly. The plan does not provide for automatic post-retirement benefit increases.

Disability income benefits are funded by actuarially determined employer contributions that are established in the Appropriations Bill by the General Assembly. For the fiscal year ended June 30, 2008, the University made a statutory contribution of .52% of covered payroll under the Teachers’ and State Employees’ Retirement System and the Optional Retirement Program to the DIPNC. Required contribution rates for the years ended June 30, 2007, and 2006, were .52% and .52%, respectively. The University made 100% of its annual required contributions to the DIPNC for the years ended June 30, 2008, 2007, and 2006, which were \$231,006.48, \$206,983.86, and \$183,825.09, respectively. The University assumes no liability for long-term disability benefits under the Plan other than its contribution.

Additional detailed information about the DIPNC is disclosed in the State of North Carolina’s *Comprehensive Annual Financial Report*.

NOTE 13 - RISK MANAGEMENT

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

Tort claims of up to \$1,000,000 are self-insured under the authority of the State Tort Claims Act. In addition, the State provides excess public officers’ and employees’ liability insurance up to \$5,000,000 via contract with a private insurance company. The University pays the premium, based on a composite rate, directly to the private insurer.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The University is required to maintain fire and lightning coverage on all State-owned buildings and contents through the State Property Fire Insurance Fund (Fund), an internal service fund of the State. Such coverage is provided at no cost to the University for operations supported by the State's General Fund. Other operations not supported by the State's General Fund are charged for the coverage. Losses covered by the Fund are subject to a \$500 per occurrence deductible, except theft losses are subject to a \$1,000 per occurrence deductible. The University also purchased through the Fund extended coverage for sprinkler leakage, business interruption, vandalism, theft, and "all risks" for all buildings and contents that carries a \$25,000 per occurrence deductible.

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

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

The University purchased Intercollegiate Sports Accident Insurance from a private insurance company through the North Carolina Department of Insurance. This policy covers medical expenses incurred for the treatment of injury to covered persons, with an excess medical limit of \$75,000, an accidental death and specific loss limit of \$25,000 and a deductible of \$25,000.

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

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

Term life insurance (death benefits) of \$25,000 to \$50,000 is provided to eligible workers. This Death Benefit Plan is administered by the State

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Treasurer and funded via employer contributions. The employer contribution rate was .16% for the current fiscal year.

Additional details on the State-administered risk management programs are disclosed in the State's *Comprehensive Annual Financial Report*, issued by the Office of the State Controller.

NOTE 14 - COMMITMENTS AND CONTINGENCIES

- A. Commitments** - The University has established an encumbrance system to track its outstanding commitments on construction projects and other purchases. Outstanding commitments on construction contracts were \$1,709,598.83 and on other purchases were \$2,024,212.40 at June 30, 2008.
- B. Pending Litigation and Claims** – The University is a party to litigation and claims in the ordinary course of its operations. Since it is not possible to predict the ultimate outcome of these matters, no provision for any liability has been made in the financial statements. University management is of the opinion that the liability, if any, for any of these matters will not have a material adverse effect on the financial position of the University.

NOTE 15 - CHANGES IN FINANCIAL ACCOUNTING AND REPORTING

For the fiscal year ended June 30, 2008, the University implemented the following pronouncements issued by the Governmental Accounting Standards Board (GASB):

GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*.

GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*.

GASB Statement No. 50, *Pension Disclosures*.

GASB Statement No. 45, requires cost-sharing employers to recognize OPEB expense for their contractually required contributions to the plan generally

NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)

consistent with the approach adopted in GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, with modifications to reflect differences between pension benefits and OPEB.

GASB Statement No. 48, requires disclosures pertaining to future revenues that have been pledged in order to disclose information about which revenues will be unavailable for other purposes and how long they will continue to do so.

GASB Statement No. 50, aligns the financial reporting requirements for pensions with those of other postemployment benefits, to conform with GASB Statement No. 45. This Statement amends GASB Statement No. 27 to require note disclosure of the employer contribution rates and percentage of the amount contributed for the current and preceding two years and to disclose how the required contribution rates are established.

NOTE 16 - NET ASSET RESTATEMENT

As of July 1, 2007, net assets as previously reported was restated as follows:

	<u>Amount</u>
July 1, 2007 Net Assets as Previously Reported	\$ 102,406,271.67
Restatement: To Revise Construction in Progress for Assets Previously Expensed	<u>3,289,415.29</u>
July 1, 2007 Net Assets as Restated	<u>\$ 105,695,686.96</u>

NOTE 17 - SUBSEQUENT EVENTS

Economic events subsequent to June 30, 2008 have negatively impacted the University's investments. Both the U.S. and international financial markets have experienced severe downturns in recent months.

Endowment Investments

According to the most recent information available at March 31, 2009, the value of the University's endowment investments was \$3,802,858.23, representing a decline of \$1,476,540.00 or 28.0%, from the value of \$5,279,398.23 as reported at June 30, 2008.

Other Investments

Other investments of the University valued at \$450,178.17 at June 30, 2008 have not experienced a decline in value. These investments were valued at \$450,178.17 at February 28, 2009 and were comprised of United States Treasury Bonds with a market value equivalent to investment cost.

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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
Fayetteville State University
Fayetteville, North Carolina

We have audited the financial statements of Fayetteville State University, a constituent institution of the multi-campus University of North Carolina System, which is a component unit of the State of North Carolina, and its discretely presented component unit, as of and for the year ended June 30, 2008, which collectively comprise the University's basic financial statements and have issued our report thereon dated July 15, 2009. Our report was modified to include a reference to other auditors.

As discussed in Note 15 to the financial statements, the University implemented Governmental Accounting Standards Board Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, Statement 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, and Statement 50, *Pension Disclosures*, during the year ended June 30, 2008.

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

Internal Control Over Financial Reporting

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

**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 (CONTINUED)**

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

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

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider Findings 1 and 2 to be material weaknesses.

Compliance and Other Matters

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

**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)**

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

This report is intended solely for the information and use of management of the University, the Board of Governors, the Board of Trustees, the Audit Committee, others within the entity, 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.



Beth A. Wood, CPA
State Auditor

July 15, 2009

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AUDIT FINDINGS AND RESPONSES

Matters Related to Financial Reporting

The following audit findings were identified during the current audit and describe conditions that represent significant deficiencies in internal control. Finding numbers 2 and 3 were also reported in the prior year.

1. DEFICIENCIES IN FINANCIAL REPORTING

The financial statements and related notes prepared by the University contained a number of misstatements that were corrected as a result of our audit. Without these corrections, the financial statements could have been misleading to readers.

Misstatements noted during our audit included:

- a. The University reported cash held for its discretely presented component unit on both the University's and the component unit's financial statements. The cash should only have been reported on the component unit's statement of net assets. As a result, the University's cash and funds held for others accounts were overstated by \$1,944,524.11.
- b. The University did not properly classify cash on the statement of net assets. As a result, current unrestricted cash and cash equivalents was overstated by \$2,345,090.81, current restricted cash and cash equivalents was understated by \$2,893,420.06, and noncurrent restricted cash and cash equivalents was overstated by \$548,329.25.
- c. The University did not properly record a restatement for prior year construction costs. This caused supplies and materials to be overstated by \$818,708.01.
- d. The University did not capitalize the cost of two renovation projects. This caused construction-in-progress to be understated by \$1,295,685.39 and supplies and materials to be overstated by the same amount.
- e. The University used the wrong useful lives in its calculation of depreciation expense. This caused depreciation to be understated by \$1,047,277.67 and accumulated depreciation to be understated by the same amount.

Recommendation: The University 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.

University Response: FSU agrees with the importance of accurately presenting the financial statements, including the notes. We are working diligently to put procedures in place to accurately reflect financial activity. For future statements, we will remove the cash held in the University STIF account for the Fayetteville State University Foundation; report restricted cash based on Banner fund, rather than GASB fund, as previously

AUDIT FINDINGS AND RESPONSES (CONTINUED)

reported; and more thoroughly review capital expenditures. The University will continue to place emphasis on the year-end financial reporting process and be diligent in the review of financial statement information.

2. INFORMATION SYSTEM ACCESS RIGHTS INCONSISTENT WITH JOB DUTIES

The University has granted information system access rights that are inconsistent with prudent internal control principles. As a result, there is an increased risk of error and fraud.

Inappropriate access rights included the following:

- The data owner and security manager are not reviewing assigned access rights on a regular basis to ensure that they are appropriate and support proper segregation of duties.
- We identified accounting personnel with access rights that were inconsistent with their job duties. Personnel should only be granted the minimum access rights needed to perform their job.
- Various security classes contain forms that should not be together in the same security class. This allows personnel the access to forms that do not support proper segregation of duties.

Recommendation: The University should take appropriate steps to strengthen internal controls to limit employees' access rights to those that are only necessary to perform their jobs. Security classes should also be evaluated to maintain adequate segregation of duties in employees' access to the system. System access rights should be reviewed on a regular basis.

University Response: University staff has worked consistently to review and correct inconsistencies in system access rights. The specific items listed in the prior year audit were corrected and other changes were made during the audit period, including ensuring separation of duties for data entry and approval of journal entries and requisitions. Review of security classes will continue and an extensive audit and reassignment project is underway.

3. MONITORING OF CASH COLLECTED OUTSIDE OF MAIN CASHIERING OFFICE IS INADEQUATE

During the audit year, cash collected outside of the University's main cashiering office was not adequately monitored. Management did not ensure that all of the cash collected was turned in to the University's main cashiers. As a result, the University significantly increased its risk for error or fraud.

The University's student purchasing cards are called Bronco One cards. Students use the cards to pay for a variety of services. University employees in the Bronco One Card Office collect cash from students on a daily basis and are responsible for updating

AUDIT FINDINGS AND RESPONSES (CONCLUDED)

students' Bronco One accounts for the funds collected. In the 2008 fiscal year, Bronco One Card Office employees submitted cash collections to the University's main cashier's office for deposit in the University's account; however, no reconciliation was prepared between the amount of cash collected and credited to students' Bronco One accounts and the amount of cash submitted by the Bronco One Card Office for deposit.

Sound internal controls require that all cash be deposited promptly and a reconciliation between cash collected and credited to students' accounts and cash submitted to the main cashiering office for deposit.

This finding has been resolved: The University corrected the deficiencies as of April 2008.

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