

**NORTH CAROLINA AGRICULTURAL  
FINANCE AUTHORITY**  
Raleigh, North Carolina

**Financial Statement Audit Report**

Year Ended June 30, 2008

Performed Under Contract With the  
North Carolina Office of the State Auditor

Beth A. Wood, CPA  
State Auditor

**FINANCIAL STATEMENT AUDIT REPORT**

**NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY**

**RALEIGH, NORTH CAROLINA**

**YEAR ENDED JUNE 30, 2008**

**Performed Under Contract With  
The North Carolina Office of the State Auditor  
Beth A. Wood, CPA  
State Auditor**

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**DR. FRANK BORDEAUX, EXECUTIVE DIRECTOR**



**Beth A. Wood, CPA**  
State Auditor

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**AUDITOR'S TRANSMITTAL**

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The Honorable Beverly E. Perdue, Governor  
The General Assembly of North Carolina  
The Board Members, North Carolina Agricultural Finance Authority

This report presents the results of the financial statement audit of North Carolina Agricultural Finance Authority, a component unit of the State of North Carolina, for the year ended June 30, 2008. Thomas & Gibbs, CPAs, PLLC performed this audit under contract with the Office of the State Auditor.

You will note from the independent auditor's report that the auditor determined that the financial statements are presented fairly in all material respects. Consideration of internal control over financial reporting and tests of compliance and other matters resulted in no reportable audit findings.

*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

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
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Year Ended June 30, 2008

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Certified Public Accountants  
and Consultants

## INDEPENDENT AUDITORS' REPORT

To the Board of Directors  
North Carolina Agricultural Finance Authority  
Raleigh, North Carolina

We have audited the accompanying Balance Sheet of the North Carolina Agricultural Finance Authority (the "Authority") as of June 30, 2008 and the related Statement of Revenues, Expenses, Changes in Net Assets and cash flows for the year then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Authority as of June 30, 2008, and the changes in its financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 14 to the financial statements, the Authority implemented Governmental Accounting Standards Board Statement No. 45, *Accounting and Financial Reporting by Employees for Postemployment Benefits Other Than Pensions*, Statement 48, *Sales and Future Revenues*, Statement 50, *Pension Disclosures*, during the year ended June 30, 2008.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 10, 2008 on our consideration of the Authority's internal control over financial reporting and 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 our 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 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. 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.

*James S. Gibbs CPA, PLLC*

Durham, North Carolina  
December 10, 2008

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
Year Ended June 30, 2008

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Management's Discussion and Analysis is intended to give the reader an overview of factors that have affected operations and may affect operations in the future. The Authority is required by the Governmental Accounting Standards Board's (GASB) Statement No. 34 to present three basic financial statements. Those statements are the Balance Sheet, Statement of Revenues, Expenses, and Changes in Net Assets, and the statement of Cash Flows. These statements provide both long-term and short-term financial information for the North Carolina Agricultural Finance Authority.

Since the Management's Discussion and Analysis (MD&A) is designed to focus on the current activities, resulting changes, and currently known facts, please read it in conjunction with the Authority's financial statements.

**2008 Financial Highlights**

- The assets of the Authority exceeded its liabilities at the close of the most recent fiscal year by \$17,856,130 (net assets). This amount is unrestricted and may be used to meet the Authority's ongoing obligations to citizens and creditors.
- The Authority's total net assets increased by \$735,424. This increase is primarily attributable to investment earnings on cash investments.
- Cash and cash equivalents increased by \$6,288,866. This increase is primarily related to collection on and proceeds from the sale of existing loans.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
Year Ended June 30, 2008

**Financial Statements**

Balance Sheet

The Balance Sheet reports all assets and liabilities of the Authority; additionally the Statement classifies those assets and liabilities as current and non-current depending on the availability of the assets or satisfaction of the obligation within twelve months (current) or longer. This statement also reports the net assets, which is the difference between the total assets and total liabilities. The reader may use the net assets to gauge the financial position of the Authority as of June 30, 2008 and 2007.

**Condensed Balance Sheet**

	<u>2008</u>	<u>2007</u>	<u>Variance</u>
Assets			
Current Assets	\$ 12,133,745	\$ 5,930,553	\$ 6,203,192
Capital Assets	29,115	21,643	7,472
Other Noncurrent Assets	5,869,735	11,344,484	(5,474,749)
Total Assets	<u>\$ 18,032,595</u>	<u>\$ 17,296,680</u>	<u>\$ 735,915</u>
Liabilities			
Current Liabilities	\$ 146,924	\$ 149,325	\$ (2,401)
Noncurrent Liabilities	29,541	26,649	2,892
Total Liabilities	<u>176,465</u>	<u>175,974</u>	<u>491</u>
Net Assets			
Invested in Capital Assets, Net of Related Debt	29,115	21,643	\$ 7,472
Unrestricted	17,827,015	17,099,063	727,952
Total Net Assets	<u>\$ 17,856,130</u>	<u>\$ 17,120,706</u>	<u>\$ 735,424</u>

As of June 30, 2008 and 2007, the Authority's total assets were \$18 million and \$17.3 million, respectively, which reflects a \$735,915 increase between these years. Of these totals, \$7.7 million and \$13.1 million were notes receivable from borrowers for the years ended June 30, 2008 and 2007, respectively. The significant decrease in notes receivable is attributable to an increase in collections on notes receivable. Increases in collection activity on notes receivable and sales of existing notes receivable to other entities also impacted cash which increased by \$6,288,866 during the year ended June 30, 2008.

The Authority's liabilities totaled \$176,465 and \$175,974 for the years ended June 30, 2008 and 2007, respectively. The total current liabilities of \$146,924 as of June 30, 2008 and \$149,325 as of June 30, 2007, were well covered by current assets of \$12.1 million in 2008 and \$5.9 million in 2007. This indicates the Authority's ability to pay current liabilities as they become due.

The Authority sells a portion of its notes receivable to other entities and continues to act as the collection agent for borrower payments. Current liabilities decreased over the prior year due to a reduction in accrued payroll liability during the year ended June 30, 2008.



NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
Year Ended June 30, 2008

Statement of Revenues, Expenses, and Changes in Net Assets

The Statement of Revenues, Expenses, and Changes in Net Assets reports the revenues earned and expenses incurred during the fiscal year. The increase or decrease of revenues over expenses directly affects (increases/decreases) the total net assets reported on the Balance Sheet. These transactions are classified as operating or non-operating.

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

	<b>2008</b>	<b>2007</b>	<b>% Change</b>
<b>Operating Revenues:</b>			
Interest earnings on notes receivable, net	\$ 776,070	\$ 1,142,132	(32.1)
Sales and services	68,302	118,213	(42.2)
Other Operating revenues	-	1,260	(100.0)
<b>Total Operating Revenues</b>	<b>844,372</b>	<b>1,261,605</b>	<b>(33.1)</b>
<b>Operating Expenses</b>			
Personal services & employee benefits	541,746	531,553	1.9
Rental expense	58,252	48,988	18.9
Contracted personal services	36,215	83,785	(56.8)
Travel	19,878	11,954	66.3
Bad debts	12,515	-	100.0
Maintenance	9,405	825	1,040.0
Communication	7,375	7,005	5.3
Loan registration fees	7,365	3,543	107.9
Equipment	4,533	15,660	(71.1)
Other expenses	3,479	5,344	(34.9)
Supplies and materials	3,281	2,505	31.0
Postage and freight	2,198	2,219	(0.9)
Depreciation	-	1,389	(100.0)
<b>Total Operating Expenses</b>	<b>706,242</b>	<b>714,770</b>	<b>(1.2)</b>
<b>Operating Income</b>	<b>138,130</b>	<b>547,808</b>	<b>(74.8)</b>
<b>Non-operating Revenues</b>			
Investment earnings	580,801	174,395	233.0
Miscellaneous	16,493	16,819	(1.9)
<b>Total Non-operating Revenues</b>	<b>597,294</b>	<b>191,214</b>	<b>212.4</b>
<b>Increase in Net Assets</b>	<b>735,424</b>	<b>738,049</b>	<b>(0.4)</b>
<b>Beginning Net Assets</b>	<b>17,120,706</b>	<b>16,382,657</b>	<b>4.5</b>
<b>Ending Net Assets</b>	<b>\$ 17,856,130</b>	<b>\$ 17,120,706</b>	<b>4.3</b>

Operating revenues primarily consist of interest earnings on notes receivable, net of amounts paid to other entities for sold notes. Operating revenues decreased from the prior year due to Authority's decision to sell a larger portion of its notes receivable portfolio and therefore not retain the interest earnings arrived from these balances.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
Year Ended June 30, 2008

Operating expenses primarily consist of personal services and employer benefit costs, contracted personal services, bad debts, and rental expense. Operating expenses decreased from the previous year primarily due to a large write off of a delinquent loan last year.

Investment earnings on pooled investment accounts and income derived from the sale of the Authority's note receivable portfolio represents the sources of non-operating revenues. Operating grants from the primary government, interest earnings on pooled investment accounts, and federal grants to administer farm pilot projects also represent non-operating revenues. Non-operating revenues increased from the prior year due to increased earnings on pooled investment accounts and greater proceeds from the sale of notes receivable.

Statement of Cash Flows

A very useful measure of financial operations is the Statement of Cash Flows. This statement provides the sources of cash inflows and outflows for three major activities: operating, noncapital financing, and investing activities.

The ending cash and cash equivalents on the Statement of Cash Flows corresponds directly with the sum of the cash and cash equivalents balances on the Balance Sheet.

**Condensed Statement of Cash Flows**

	<u>June 30, 2008</u>	<u>June 30, 2007</u>	<u>Change</u>	<u>% Change</u>
Net Cash Provided From (Used For):				
Operating activities	\$ 5,691,572	(\$1,071,879)	\$ 6,763,451	-631%
Non-capital Financing Activities	16,493	16,818	(325)	-2%
Investing Activities	580,801	253,672	327,129	129%
Net Increase (Decrease)	<u>6,288,866</u>	<u>(801,389)</u>	<u>7,090,255</u>	<u>-885%</u>
Cash and Cash Equivalents at beginning of year	3,677,026	4,478,415	(801,389)	-18%
Cash and Cash Equivalents at end of year	<u>\$ 9,965,892</u>	<u>\$ 3,677,026</u>	<u>\$ 6,288,866</u>	171%

The net cash provided by operating activities shows net inflow of \$5,691,572 and net outflow of \$1,071,879 for the years ended June 30, 2008 and 2007, respectively. The major outflow was payments to employees and fringe benefits of \$543,618 for the year ended June 30, 2008. The major outflow was payments to borrowers for loan issued of \$1,727,525 during the year ended June 30, 2007. The major source of operating inflow was receipts from collections of notes receivables of \$5.8 million during the year ended June 30, 2008. The major source of operating inflow for the year ended June 30, 2007 was receipts from customers, which was \$1.3 million.

The Authority has cash inflows from investing activities of \$580,801 and \$253,672 for the years ended June 30, 2008 and 2007, respectively. These result from investment income.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
Year Ended June 30, 2008

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**Economic Factors and Future Outlook**

The Authority is affected by both US and North Carolina economic conditions and policies. Federal policy changes such as NAFTA (North American Fair Trade Act) affect the prices farmers receive for their products thereby affecting their ability to repay loans. The Authority attempts to reduce the resultant risk to the loan portfolio by obtaining federal guarantees on loans where possible. Recent volatility in global financial markets could potentially impact the volume of future lending activity.

The rapid development of China's manufacturing economy improves incomes of Chinese consumers which increases export opportunities for United States agriculture. At the same time, their 'trade increases' contribute to an increasing balance of payments deficit in the United States. This trade imbalance weakens the economic strength of the US economy.

Since many countries now compete quite favorably with North Carolina as an agricultural exporter, more attention must be given to finding every opportunity to finance "further processing" or "value added" manufacturing for farmers. This increases the farmer's share of the consumer's dollar and provides additional jobs in rural areas. The Authority's commitment is evidenced by recent loans to the local wineries totaling \$1.3 million to bring on board new income sources in areas severely affected by reductions in tobacco acreage and closing of manufacturing plants.

State policies such as the moratorium on new swine production facilities being constructed by farmers reduce income opportunities for the Authority's farm clientele. The Authority had assisted many farmers to improve their net income by producing swine for the export market. In an attempt to be proactive, the Authority, in cooperation with FPPC (Farm Pilot Project Coordination, Inc.) has used \$12.5 million for innovative projects to eliminate the negative environmental aspects of swine production. This should ultimately return an economic opportunity to North Carolina farmers that can be financed by the Authority.

The trend toward smaller farm numbers will no doubt continue. However, the Authority will continue to promote alternative farm enterprises so that the remaining farmers can continue as economically strong independent producers.

**Request for Information**

The financial report is designed to provide a general overview of the Authority's finances for all those who have an interest in its finances. Questions concerning any of the information presented in this report or requests for additional financial information should be addressed to the Authority's office at P.O. Box 27908, Raleigh, NC 27611-7908.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY

**BALANCE SHEET**

June 30, 2008

**ASSETS**

**Current Assets**

Cash and cash equivalents (Note 3)	\$	9,965,892
Notes receivable, net (Note 4)		1,955,825
Interest receivable		173,101
Other receivable		37,544
Inventories		1,383
<b>Total Current Assets</b>		<b>12,133,745</b>

**Non-current Assets**

Notes receivable, net (Note 4)		5,698,235
Land held for investment (Note 5)		171,500
Capital assets, net (Note 6)		29,115
<b>Total Non-current Assets</b>		<b>5,898,850</b>

**TOTAL ASSETS**

**\$ 18,032,595**

**LIABILITIES AND NET ASSETS**

**Current Liabilities**

Accounts payable		143,355
Accrued payroll		875
Due to primary government		1,080
Accrued vacation leave (Note 7)		1,614
<b>Total Current Liabilities</b>		<b>146,924</b>

**Non-current Liabilities**

Accrued vacation leave (Note 7)		29,541
		<b>29,541</b>

**TOTAL LIABILITIES**

**176,465**

**Net Assets**

Invested in capital assets, net of related debt		29,115
Unrestricted		17,827,015
<b>Total net assets</b>		<b>17,856,130</b>

**TOTAL LIABILITIES AND NET ASSETS**

**\$ 18,032,595**

The accompanying notes are an integral part of these financial statements.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
**STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS**  
Year Ended June 30, 2008

<b>Operating Revenues</b>	
Interest earnings on notes receivable, net	\$ 776,070
Sales and services	68,302
<b>Total Operating Revenues</b>	844,372
 <b>Operating Expenses</b>	
Personal services & employee benefits	541,746
Rental expense	58,252
Contracted personal services	36,215
Travel	19,878
Bad debts	12,515
Maintenance	9,405
Communication	7,375
Loan registration fees	7,365
Equipment	4,533
Other expenses	3,479
Supplies and materials	3,281
Postage and freight	2,198
Depreciation	-
<b>Total Operating Expenses</b>	706,242
<b>Operating Income</b>	138,130
 <b>Non-operating Revenues</b>	
Investment earnings	580,801
Miscellaneous	16,493
<b>Total Non-operating Revenues</b>	597,294
<b>Change in Net Assets</b>	735,424
<b>Beginning Net Assets</b>	17,120,706
<b>Ending Net Assets</b>	\$ 17,856,130

The accompanying notes are an integral part of these financial statements.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
**STATEMENT OF CASH FLOWS**  
Year Ended June 30, 2008

<b>Cash Flows from Operating Activities</b>	
Receipts from customers	\$ 980,839
Receipts from collections of notes receivable	5,827,701
Payments for loan issued	(402,706)
Payments to employees and fringe benefits	(543,618)
Payments to vendors and suppliers	(170,644)
<b>Net cash provided by operating activities</b>	<u>5,691,572</u>
 <b>Cash Flows from Non-capital Financing Activities</b>	
Other receipts	<u>16,493</u>
 <b>Cash Flows from Investing Activities</b>	
Interest on investments	<u>580,801</u>
 <b>Net increase in Cash and Cash Equivalents</b>	 6,288,866
 <b>Cash and Cash Equivalents - July 1</b>	 <u>3,677,026</u>
 <b>Cash and Cash Equivalents - June 30</b>	 <u>\$ 9,965,892</u>
 <b>Reconciliation of Net Operating Income to Net Cash Provided (Used) by Operating Activities</b>	
Operating Income	\$ 138,130
Depreciation expense	-
Adjustments to reconcile operating income to net cash provided by operating activities	
Changes in assets and liabilities	
Notes receivables	5,423,397
Other receivables	137,712
Inventories	559
Intergovernmental payables	486
Accounts payable	1,391
Accrued vacation leave	(2,631)
Change in capital assets	(7,472)
	<u>5,553,442</u>
 <b>Net Cash Provided by Operating Activities</b>	 <u>\$ 5,691,572</u>

The accompanying notes are an integral part of these financial statements.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2008

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**NOTE 1 - THE ORGANIZATION**

The North Carolina Agricultural Finance Authority (the “Authority”) was established in 1986 by the North Carolina Agricultural Finance Act. The Authority was created and empowered to alleviate the severe shortage of capital and credit available at affordable interest rates for investment in agriculture and for the export of agricultural products, commodities and services by providing such capital and credit at interest rates within the financial means of persons and businesses engaged in agriculture and agricultural exports. The Authority is a body politic and corporate created within the North Carolina Department of Agriculture and Consumer Services. The Authority is constituted as a public agency and an instrumentality of the State for the performance of essential public functions as established by the General Assembly (*North Carolina General Statutes* - Chapter 122D).

**NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**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. The North Carolina Agricultural Finance Authority is a component unit of the primary government of the State of North Carolina and is an integral part of the State’s *Comprehensive Annual Financial Report* (CAFR).

As required by General Statute 122D-4, the governing body of the Authority is composed of 10 members. The Commissioner of Agriculture serves ex-officio, with the same rights and privileges, including voting rights, as other members. The remaining nine members are appointed by the Governor of North Carolina (3 members), the General Assembly upon recommendation of the Speaker of the House (3 members), and the General Assembly upon recommendation of the President Pro Tempore of the Senate (3 members).

**Basis of Presentation** - The North Carolina Agricultural Finance Authority is accounted for as a proprietary fund type (enterprise fund) in conformity with the accounting and reporting requirements of the Governmental Accounting Standards Board (GASB). In accordance with GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Authority does not apply Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989 for proprietary activities, unless the GASB amends its pronouncements to specifically adopt FASB pronouncements issued after that date. The measurement focus is upon determination of net income, financial position, and changes in cash flows. The accounting principles used are those generally accepted in the United States of America and applicable to similar businesses in the private sector; thus, the accompanying financial statements have been prepared in accordance with the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized when incurred.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2008

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**NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**Use of Estimates** – The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

The determination of the adequacy of the allowance for loan losses is based on estimates that are particularly susceptible to significant changes in the economic environment and market conditions. In connection with the determination of the estimated losses on loans, management obtains independent appraisals for significant collateral.

While management uses available information to recognize losses on loans, further reductions in the carrying amounts of loans may be necessary based on changes in local, economic conditions. It is reasonably possible that the estimated losses on loans may change materially in the near term. However, the amount of the change that is reasonably possible cannot be estimated.

**Cash and Cash Equivalents** – Cash and cash equivalents include short-term investments with the State Treasurer’s Cash and Investment Pool (a governmental external investment pool). The short-term investment portfolio maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit additional cash at any time and also may withdraw cash at any time without prior notice or penalty.

**Notes Receivable and Allowance for Doubtful Accounts** - The Authority provides the following direct loan programs:

*Farm Loan Programs* – Loans made for the purpose of buying, improving, or enlarging farms. This category comprises the majority of loans made by the Authority. Loan rates are variable based on the Prime Rate as published in the *Wall Street Journal* plus an additional percentage. Loan terms and limits vary depending on the type of loan; however, all are secured by liens on the real estate owned or purchased, improvements made with the loan funds, and any other additional security that might be required on an individual loan basis.

*Agribusiness Loan Program* – Loans are made to assist agribusinesses in obtaining capital to start-up, increase, or make changes to their business. Agribusiness loans are designed to provide capital to acquire and build facilities. Loan rates are variable based on the Prime Rate as published in the *Wall Street Journal*.

*Agricultural Facilities Disaster Loans* – Loans are made to assist agricultural property owners who have suffered property damage due to natural disasters to repair or replace structures and to return to normal work routines as quickly as possible. These loans are designed to provide for damages to farm facilities (structures) not fully covered for replacement costs or covered by federal disaster funds. Interest rates are fixed for the life of the loan and established on criteria tied to the Prime Rate. Maximum length of the loan cannot exceed 10 years.



NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2008

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**NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

*Cotton Gin Air Quality Loan Program* – Loans are made to assist modern day cotton gins in complying with changes in the dust emissions regulations. Eligible cotton gins must have been in operation at least one year prior to application and the financed improvements must comply with state and federal air quality standards. Each loan program has specified eligibility that must be met. These loans are normally secured by a first lien on collateral. The loan committee determines the interest rate on the loans and the interest accrues from the original date that the loan is closed.

Principal payments can be made either annually, quarterly, or monthly. The loans are repaid over various term lengths, generally with a maximum of 20 years. Application fees and loan processing fees vary by loan type.

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

In the normal course of business, the Authority sells notes receivable to other entities and continues to act as the collection agent for the borrower payments. Notes receivable are reported net of notes sold to other entities.

**Inventories** - Inventories held by the Authority are priced at the lower of cost or market value using the first-in, first-out method. The inventories consist of expendable supplies and postage.

**Capital Assets** – It is the policy of the Authority to capitalize all capital assets costing more than \$5,000 with an estimated useful life of two or more years. In addition, other items that are purchased and used in large quantities are capitalized. The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized. The Authority uses the straight line method to depreciate assets over estimated useful lives as follows:

Machinery and Equipment	5 -10 years
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NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2008

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**NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**Lease Obligations** – Operating lease payments are recorded as expenses when incurred. All leases of the Authority contain appropriation clauses indicating that continuation of the lease is subject to continued funding by the Legislature.

**Compensated Absences** - Employees of the Authority are permitted to accumulate earned but unused vacation pay benefits. The Authority's policy is to record the cost of vacation leave when earned. The policy provides for the maximum accumulation of unused vacation leave of 30 days which can be carried forward each January 1st or for which an employee can be paid upon termination of employment. When determining the vacation pay liability due within one year, leave is considered taken on a last in, first out (LIFO) basis. Any accumulated vacation leave in excess of 30 days at December 31<sup>st</sup> is converted to sick leave. Under this policy, the accumulated vacation leave for each employee at June 30<sup>th</sup> equals the leave carried forward at the previous December 31<sup>st</sup> plus the leave earned, less the leave taken between January 1<sup>st</sup> and June 30<sup>th</sup>.

The Authority has the policy of recording the cost of sick leave when taken and paid rather than when the leave is earned. The policy provides for unlimited accumulation of sick leave, but the employee cannot be compensated for any unused sick leave upon termination of employment.

Full-time permanent, probationary and trainee employees earn vacation leave ranging from .98 to 2.15 days per month, depending upon years of service. Part-time employees earn the same range of leave on a pro-rata amount based on the number of hours a week they work. At termination, employees are paid for any accumulated vacation leave. Full-time permanent, probationary and trainee employees earn sick leave at the rate of one day per month with an unlimited accumulation. Part-time employees earn a percentage of the total of 8 hours per month based on the number of hours a week they work. While payment for accumulated sick leave upon termination is not allowed, additional service credit for retirement pension benefits is given for accumulated sick leave upon retirement.

In addition to vacation leave describe 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 part of the 30 day maximum applicable to regular vacation leave and is not subject to conversion to sick leave.

**Net Assets** – The Authority's net assets are classified as follows:

*Invested in Capital Assets* – This represents the Authority's total investment in capital assets.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
**NOTES TO FINANCIAL STATEMENTS**  
 June 30, 2008

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**NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

*Unrestricted Net Assets* – Unrestricted net assets are all those not invested in capital assets.

**Revenue and Expense Recognition** – The Authority presents its revenues and expenses as operating or non-operating based on recognition definitions from GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*. Operating activities are those activities that are necessary and essential to the mission of the Authority. Investment income is considered non-operating since it is either investing, capital or non-capital financing activities. Operating expenses are all expense transactions incurred other than those related to investing, capital or non-capital financing activities.

**NOTE 3 - DEPOSITS**

At June 30, 2008, the \$9,965,892 shown on the Balance Sheet as cash and cash equivalents represents the Authority’s equity position in the Short Term Investment Fund managed by the North Carolina State Treasurer (a portfolio within the State Treasurer’s investment Pool, and external investment pool that is not registered with the Securities and Exchange Commission and does not have a credit rating). The Short-Term Investment Fund 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.

Financial statements and disclosures for the State Treasurer’s Investment Pool 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.osc.state.nc.us/> and clicking on “Financial Reports” or by calling the State Controller’s Financial Reporting Section at (919) 981-5454.

**NOTE 4 - NOTES RECEIVABLE, NET**

A summary of notes receivable is presented as follows:

Notes receivable from borrowers	\$ 17,814,818
Notes payable to holders	(9,960,758)
	7,854,060
Less allowance	(200,000)
Notes receivable, net	7,654,060
Current portion	(1,955,825)
Non-current portion	\$ 5,698,235

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
**NOTES TO FINANCIAL STATEMENTS**  
 June 30, 2008

**NOTE 5 - LAND HELD FOR INVESTMENT**

Land held for investment of \$171,500 at June 30, 2008 was acquired as part of a loan foreclosure and is valued at the acquisition value on the date of foreclosure.

**NOTE 6 - CAPITAL ASSETS**

A summary of changes in capital assets for the year ended June 30, 2008 is presented below.

	Balance July 1, 2006 (as restated)	Additions	Deductions	Balance June 30, 2007
<b>Capital Assets, depreciable:</b>				
Machinery and equipment	\$ 25,989	\$ 7,472	\$ -	\$ 33,461
Total capital assets, depreciable	<u>25,989</u>	<u>7,472</u>	<u>-</u>	<u>33,461</u>
<b>Less accumulated depreciation for:</b>				
Machinery and equipment	(4,346)	-	-	(4,346)
Total accumulated depreciation	<u>(4,346)</u>	<u>-</u>	<u>-</u>	<u>(4,346)</u>
Capital assets, net	<u>\$ 21,643</u>	<u>\$ 7,472</u>	<u>\$ -</u>	<u>\$ 29,115</u>

**NOTE 7 - CHANGES IN NON-CURRENT LIABILITIES**

A summary of changes in accrued vacation leave for the year ended June 30, 2008 is presented as follows:

	Balance July 1, 2007	Additions	Reductions	Balance June 30, 2008	Current Portion
Accrued Vacation Leave	<u>\$ 28,524</u>	<u>\$ 24,400</u>	<u>\$ (21,769)</u>	<u>\$ 31,155</u>	<u>\$ 1,614</u>

**NOTE 8 - OPERATING LEASES**

The Authority leases its office space. Rental expense was \$58,252 for the year ended June 30, 2008. On September 1, 2007, the Authority entered into an operating lease agreement with Alton B. Smith Trust for a term of five years, which includes payments ranging from \$5,000 per month to \$5,519 per month.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2008

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**NOTE 8 - OPERATING LEASES (continued)**

Future minimum lease payments under the lease are as follows at June 30:

2009	\$	61,250
2010		62,781
2011		64,351
2012		65,960
2013		<u>11,038</u>
Total minimum lease payments	\$	<u>265,380</u>

**NOTE 9 - NON-OPERATING REVENUES**

**North Carolina State University Agreement** - The Authority administers funds on behalf of the North Carolina State University College of Natural Resources (the University) for approved projects that rehabilitate or educate the people of rural North Carolina. The funds originated from proceeds of a sale of federal forestland held by the North Carolina Rural Rehabilitation Corporation. These funds are invested with the State Treasurer's Cash and Investment Pool.

**Farm Pilot Project** - The enactment of the Agricultural, Rural Development, Food and Drug Administration and Related Agencies Appropriation Act of Fiscal Years 2002 (the Act) appropriated funds to the United States Department of Agriculture Natural Resources Conservation Service (NRCS) for pilot projects demonstrating innovative treatment technologies which result in at least a 75% reduction in the nutrient content of wastewater discharged by animal feeding operations. The Act identified the Authority and a Florida not-for-profit corporation, as entities authorized to create and implement the pilot project. For its services, the Authority receives cash payments to cover project and administrative costs.

The Authority received \$9,169 in service fees to administer these projects during the year ended June 30, 2008. This amount is included in miscellaneous revenues.

**NOTE 10 - PENSION PLANS**

**Retirement Plans** - Each permanent full-time employee, as a condition of employment, is a member of the Teacher's and State Employees' Retirement System (TSERS), a cost-sharing multiple-employer defined benefit pension plan administered by the State of North Carolina. Benefit and contribution provisions of the Teacher's and State Employees' Retirement System are established by *North Carolina General Assembly Statutes* 135-5 and 135-8 and may be amended by the North Carolina General Assembly.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2008

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**NOTE 10 - PENSION PLANS (continued)**

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 Authority had a total payroll of \$541,745, of which \$437,965 was covered under the Teacher's and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were \$25,839 and \$13,358, respectively. 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 Authority made 100% of its annual required contributions for the years ended June 30, 2008, 2007, and 2006, which were \$13,358, \$11,336, and \$10,452, respectively.

The Teacher's and State Employees' Retirement System's financial information is included the State of North Carolina's *Comprehensive Annual Financial Report* (CAFR). 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 "Financial Reports," or by calling the State Controller's Financial Report Section at (919) 981-5454.

**NOTE 11 - OTHER POSTEMPLOYMENT BENEFITS**

**Health Benefits** – The Authority participates in the Comprehensive Major Medical Plan (the Plan), a cost sharing, multiple-employer 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 (DIPNC) and retirees of the Teachers' and State Employees' Retirement System (TSERS). Coverage eligibility varies depending on years of contributory 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, or 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 the 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 employees 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.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2008

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**NOTE 11 - OTHER POSTEMPLOYMENT BENEFITS (continued)**

For the current fiscal year the Authority contributed 4.1% of the covered payroll under the Teachers' and State Employees' Retirement System to the Fund. Required contribution rates for the year's ended June 30, 2007 and 2006, were 3.8% and 3.8%, respectively.

The Authority made 100% of its annual required contributions to the Plan for the years ended June 30, 2008, 2007, and 2006, which were \$17,957, \$16,195, and \$16,973, respectively. The Authority assumes no liability for retiree health care benefits provided by the programs other than the required contribution.

Additional detailed information about these programs can be located in the State of North Carolina's *Comprehensive Annual Financial Report* (CAFR). 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 "Financial Reports," or by calling the State Controller's Financial Report Section at (919) 981-5454.

**Disability Income** - The Authority 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. 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 Authority made a statutory contribution of .52% of covered payroll under the Teachers' and State Employees' Retirement System to the DIPNC. Required contribution rates for the years ended June 30, 2007, and 2006, were .52% and .52%, respectively. The Authority made 100% of its annual required contributions to the DIPNC for the years ended June 30, 2008, 2007, and 2006, which were \$2,277, \$2,216, and \$2,323, respectively. The Authority assumes no liability for long-term disability benefits under the Plan other than its contribution.

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

**NOTE 12 - RISK MANAGEMENT**

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and the destruction of assets; errors and omissions; injuries to employees; and natural disasters.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2008

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**NOTE 12 - RISK MANAGEMENT(continued)**

These exposures to loss are handled by a combination of methods, including participation in various State-administered risk pools, 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 from the previous year and settled claims have not exceeded coverage in any of the past three fiscal years.

**Public Officers' and Employees' Liability Insurance** – In accordance with Chapter 58, Article 32, Part 15, of the General Statutes, public officers' and employees' liability insurance is provided by private insurers for all employees of the State and participating component units. The policy provides \$5,000,000 excess insurance over the \$500,000 statutory limit payable for any one claim under the State Tort Claims Act. The first \$150,000 of an award against a State agency is the responsibility of the state agency's general fund budget code or up to \$500,000 if a non-general fund budget code.

For general fund budget codes, any award greater than \$150,000 but less than \$500,000 is funded by proportionate shares of estimated lapse salaries from all agencies general fund budget codes. Since State agencies and component units are responsible for funding any tort claims of \$500,000 or less from their budget and/or lapse salaries, total claims liabilities are not measurable.

Employers are charged a premium for the excess insurance based on a composite rate. The employers pay the premiums directly to the private insurer. Settled claims have not exceeded coverage in any of the past three fiscal years.

**Comprehensive Major Medical Plan** – In accordance with Chapter 135, Article 3, Part 3, of the General Statutes, the State of North Carolina provides comprehensive major medical care for employees and retirees of the State and its participating component units, as well as their dependents. Coverage is self-funded by contributions to the State Health Plan (the Plan).

Contributions for employee and retiree coverage are made by the State while employees and retirees make contributions for dependent coverage. Coverage is also extended to certain individuals as another post-employment benefit. The Plan is administered by a third party contractor who is responsible for the processing of claims and administration of cost containment. The Plan pays most expenses that are medically necessary and eligible for coverage based on usual, customary and reasonable allowances. Claims are subject to specified annual deductible and co-payment requirements. The plan disallows claims in excess of a lifetime maximum of \$5 million.

**Statewide Workers' Compensation Program** - The Workers' Compensation Program (the Program) was created by Chapter 97, Article 1, of the General Statutes to provide benefits to workers injured on the job and includes all employees of the State and its component units.



NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2008

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**NOTE 12 - RISK MANAGEMENT (continued)**

An injury is covered under workers' compensation if it is caused by an accident that arose out of and in the course of employment. Also, certain occupational diseases specifically designated in the North Carolina Workers' Compensation Act are compensable.

Losses payable by the Program include medical claims, loss of wages, disability, and death benefits. The State and its component units are self-insured for workers' compensation. State agencies and participating component units contribute to a fund administered by the Office of the State Controller to cover their workers' compensation claims. A third-party administrator handles workers' compensation claims, receives a per case administration fee, and draws down State funds to make medical and indemnity payments on behalf of the State in accordance with the North Carolina Workers' Compensation Act.

**Death Benefit Plan of North Carolina** - Term life insurance (death benefits) is provided through the Death Benefit Plan to all members of the Teachers' and State Employees' Retirement System who have completed at least 12 consecutive months of membership in the System. Lump sum death benefit payments to beneficiaries are equal to the employee's highest 12 month salary in a row during the 24 months prior to his/her death, with a minimum benefit of \$25,000 and a maximum of \$50,000.

Death benefits are funded by actuarially based employer contributions that are established in the biennial appropriation bill by the General Assembly. The benefits are established by Chapter 135, Article 3, Part 3, of the General Statutes and may be amended only by the North Carolina General Assembly. The plan requires the Authority to contribute .16% of covered payroll which amounted to \$682 for the year ended June 30, 2007.

**Employee Dishonesty and Computer Fraud** – Blanket public employee dishonesty and computer fraud insurance is provided for agencies of the State and its component units with a limit of \$5 million per occurrence, subject to a \$50,000 deductible and a 10% participation in each loss above the deductible. The coverage is placed with a private insurance company and is handled by the North Carolina Department of Insurance. Agencies of the State and its component units are charged premiums by the private insurance company. Settled claims have not exceeded coverage in any of the past three fiscal years.

**Automobile, Fire and Other Property Losses** – The State of North Carolina is required by Chapter 58, Article 31, Part 50, of the General Statutes to provide liability insurance on every state-owned motor vehicle. The State is self-insured for the first \$500,000 of any loss through a retrospective rated plan. The plan purchases excess insurance through a private insurer to cover losses greater than \$500,000.

The liability limits for losses incurring in-state are \$500,000 per claimant and \$5 million per occurrence. For losses incurring out-of-state, the limits are \$1 million per claimant and \$5 million per occurrence.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2008

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**NOTE 12 - RISK MANAGEMENT (continued)**

Users of the state cars are charged premiums to cover the cost of the excess insurance and to pay for those losses falling under the self-insured retention. Premiums charged are also based on the projected losses to be incurred.

The private insurer processes all claims, establishes a reserve for amounts expected to be paid for claims, and pays claims after they are approved by the Attorney General's Office. Settled claims have not exceeded coverage in any of the past three fiscal years.

The State Property Fire Insurance Fund (the Fund) was also created by Chapter 58, Article 31, of the General Statutes. The Fund insures State owned buildings and contents for fire, extended coverage, and other property losses. Coverage for fire losses is free for all operations that are supported by the State's General Fund. Those operations that are not supported by the State's General Fund are charged for fire coverage.

Extended coverage and other property coverage such as sprinkler leakage, business interruption, vandalism, theft, and "all risk" for buildings and contents can be purchased through the Fund at premiums discounted from industry manual rates.

The fund insures losses up to \$2.5 million per occurrence. All losses covered by the Fund are subject to a \$500 per occurrence deductible except for theft, which carries a \$1,000 per occurrence deductible. The Fund purchases excess insurance from a private insurer to cover losses over the amounts insured by the Fund. Settled claims have not exceeded coverage in any of the past three fiscal years.

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 13 - COMMITMENTS AND CONTINGENCIES**

**No Commitment Debt** - Since 1995, the Authority has issued Agricultural Development Revenue Bonds to provide financial assistance to North Carolina farmers and agribusinesses for the acquisition, construction, and equipping of various agricultural projects deemed to be in furtherance of the Authority's purpose. The bonds are secured by an Indenture of Trust and a Letter of Credit and are payable solely from payments received on the underlying loan obligations. Neither the Authority nor the State of North Carolina is obligated in any manner for repayment of the bonds. Accordingly, the bonds are not reported as liabilities in the accompanying financial statements.

As of June 30, 2008, there were four series of Agricultural Development Revenue Bonds outstanding with an aggregate principal amount payable of \$11,810,000.

NORTH CAROLINA AGRICULTURAL FINANCE AUTHORITY  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2008

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**NOTE 14 - CHANGES IN FINANCIAL ACCOUNTING AND REPORTING**

For the fiscal year ended June 30, 2008, the Authority 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 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 be 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 contributions rates are established.

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INDEPENDENT AUDITORS' 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*

To the Board of Directors  
North Carolina Agricultural Finance Authority  
Raleigh, North Carolina

We have audited the financial statements of the North Carolina Agricultural Finance Authority (the "Authority") as of and for the year ended June 30, 2008, and have issued our report thereon dated December 10, 2008.

As discussed in Note 14 to the financial statements, the Authority implemented Governmental Accounting Standards Board Statement No. 45, *Accounting and Financial Reporting by Employees for Postemployment Benefits Other Than Pensions*, Statement 48, *Sales and Future Revenues*, 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.

**Internal Control Over Financial Reporting**

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

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 Authority'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 Authority's financial statements that is more than inconsequential will not be prevented or detected by the Authority's internal control.

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 Authority'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 internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

### **Compliance and Other Matters**

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

This report is intended solely for the information and use of the management of the Authority, the Governor, the Office of State Budget and Management, the Office of the State Controller and the General Assembly and is not intended to be, and should not be, used by anyone other than these specified parties.



Durham, North Carolina  
December 10, 2008

## ORDERING INFORMATION

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