



STATE OF NORTH CAROLINA

**NORTH CAROLINA AGRICULTURAL AND TECHNICAL STATE
UNIVERSITY**

GREENSBORO, NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT

FOR THE YEAR ENDED JUNE 30, 2007

OFFICE OF THE STATE AUDITOR

LESLIE W. MERRITT, JR., CPA, CFP

STATE AUDITOR

**NORTH CAROLINA AGRICULTURAL AND TECHNICAL STATE
UNIVERSITY**

GREENSBORO, NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT

FOR THE YEAR ENDED JUNE 30, 2007

BOARD OF GOVERNORS

THE UNIVERSITY OF NORTH CAROLINA

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STATE OF NORTH CAROLINA
Office of the State Auditor

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

2 S. Salisbury Street
20601 Mail Service Center
Raleigh, NC 27699-0601
Telephone: (919) 807-7500
Fax: (919) 807-7647
Internet
<http://www.ncauditor.net>

AUDITOR'S TRANSMITTAL

The Honorable Michael F. Easley, Governor
The General Assembly of North Carolina
Board of Trustees, North Carolina Agricultural and Technical State University

We have completed a financial statement and compliance audit of North Carolina Agricultural and Technical State University for the year ended June 30, 2007, and our audit results are included in this report. You will note from the independent auditor's report that we determined that the financial statements are presented fairly in all material respects.

Our consideration of internal control over financial reporting and compliance and other matters based on an audit of the financial statements and our consideration of the University's administration of federal programs in accordance with applicable laws, regulations, contracts and grants disclosed certain deficiencies and/or instances of noncompliance that are detailed in the Audit Findings and Responses section of this report. The University's response is included following each finding.

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

Leslie W. Merritt, Jr.

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

May 27, 2008

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
North Carolina Agricultural and Technical State University
Greensboro, North Carolina

We have audited the accompanying financial statements of North Carolina Agricultural and Technical 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, 2007, which collectively comprise the University's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the North Carolina Agricultural and Technical 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 The North Carolina A&T University Foundation, Inc., 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 opinions, insofar as they relate to the amounts included for The North Carolina A&T University Foundation, Inc., are based on the report of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The financial statements of The North Carolina A&T University Foundation, Inc., were not audited in accordance with *Government Auditing Standards*. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our 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 North Carolina Agricultural and Technical State University and its discretely presented component unit as of June 30, 2007, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

In accordance with *Government Auditing Standards*, we have also issued our report dated April 22, 2008, on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

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

Leslie W. Merritt, Jr.

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

April 22, 2008

NORTH CAROLINA AGRICULTURAL AND TECHNICAL STATE UNIVERSITY MANAGEMENT'S DISCUSSION AND ANALYSIS

Management's Discussion and Analysis provides an overview of the financial position and operating activities of North Carolina Agricultural and Technical State University for the year ending June 30, 2007, and includes comparative data for the year ending June 30, 2006. Information contained in this section has been prepared by University staff for the purpose of identifying significant transactions, trends and events that have impacted the fiscal health of the University and that may continue to exert influence in future years. It is recommended that this discussion and analysis be read in conjunction with the related financial statements and notes to the financial statements.

The Financial Statements

The financial statements for North Carolina Agricultural and Technical State University include the Statement of Net Assets, the Statement of Revenues, Expenses, and Changes in Net Assets, and the Statement of Cash Flows. These statements were prepared in accordance with Governmental Accounting Standards Board (GASB) principles and reflect an economic resource measurement focus and the accrual basis of accounting. Management's discussion and analysis will concentrate on the Statement of Net Assets and the Statement of Revenues, Expenses, and Changes in Net Assets, using condensed versions for the purposes of this discussion. In order to enhance comparability, the cash and cash equivalent figures for 2006 have been restated to reflect negative restricted cash borrowed from unrestricted sources.

Statement of Net Assets

The Statement of Net Assets presents the financial position of the University at June 30, 2007, defined by the balances of assets, liabilities and assets net of liabilities. Assets are classified as current or noncurrent and cash is further identified as unrestricted or restricted. Current assets include those resources available to meet current obligations and operating requirements while noncurrent assets are to be held to meet future needs. Capital assets are shown net of depreciation. Assets, net of liabilities, are grouped into three categories: investment in capital assets net of related debt, restricted net assets, and unrestricted net assets. Restricted net assets are further classified as unexpendable or expendable. Endowments and loan funds comprise the nonexpendable net assets, and expendable net assets are made up primarily of contracts, grants, and restricted gifts.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Condensed Statement of Net Assets

	<u>2007</u>	<u>Restated 2006</u>	<u>Change</u>
Assets			
Current Assets	\$ 61,381,418.94	\$ 53,056,431.93	\$ 8,324,987.01
Noncurrent Assets:			
Noncurrent Capital Assets, Net of Accumulated Depreciation	265,544,680.79	250,908,494.90	14,636,185.89
Other Noncurrent Assets	<u>63,196,133.70</u>	<u>24,322,528.18</u>	<u>38,873,605.52</u>
Total Assets	<u>390,122,233.43</u>	<u>328,287,455.01</u>	<u>61,834,778.42</u>
Liabilities			
Current Liabilities	14,486,016.79	19,114,173.04	(4,628,156.25)
Noncurrent Liabilities	<u>26,754,234.08</u>	<u>21,652,236.47</u>	<u>5,101,997.61</u>
Total Liabilities	<u>41,240,250.87</u>	<u>40,766,409.51</u>	<u>473,841.36</u>
Net Assets			
Investment in Capital Assets, Net of Related Debt	247,124,680.79	231,723,039.80	15,401,640.99
Restricted - Nonexpendable	10,845,326.18	9,797,967.65	1,047,358.53
Restricted - Expendable	54,949,178.27	15,873,064.08	39,076,114.19
Unrestricted	<u>35,962,797.32</u>	<u>30,126,973.97</u>	<u>5,835,823.35</u>
Total Net Assets	<u>\$ 348,881,982.56</u>	<u>\$ 287,521,045.50</u>	<u>\$ 61,360,937.06</u>

The increase of \$8,324,987.01 in current assets is primarily due to an increase in cash and cash equivalents totaling \$7,553,262.05. There were increases in unrestricted and restricted cash in the amounts of \$6,109,291.98 and \$1,443,970.07, respectively. These increases were due largely to increases in State appropriations held at year end and lower expenditures in overhead funds for the fiscal year.

Noncurrent assets increased by \$53,509,791.41. The increase in other noncurrent assets of \$38,873,605.52 was primarily driven by an increase of \$34,169,180.20 in the receivable from the State, an amount that represents the difference between the total allotment for construction projects funded by State bonds and the actual funds that were received by year end. In addition, endowment investments increased by \$3,553,041.33, a result of a little over \$1,000,000.00 in reinvested earnings as well as the purchase of additional investments from cash holdings. Noncurrent capital assets increased by \$14,636,185.89 with the largest increases occurring in buildings and construction in progress.

Total current liabilities decreased by \$4,628,156.25 during the year in large part because of the retirement of \$6,168,000.00 in short-term temporary financing used to fund the construction of a 500 car parking deck. Long-term debt was issued to retire that construction note and primarily accounted for the increase of \$5,101,997.61 in noncurrent liabilities.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Restricted expendable net assets experienced a large increase of \$39,076,114.19 due primarily to the increase in assets held to fund large construction projects.

Statement of Revenues, Expenses, and Changes in Net Assets

The Statement of Revenues, Expenses, and Changes in Net Assets reports the activity of the University during the year and is subdivided into four major components: operating revenues, operating expenses, nonoperating revenues (expenses), and other revenues, expenses, gains or losses. Revenues are reported by major source and expenses are reported by natural classification. Intra-departmental sales, services, and transfers are eliminated and depreciation of capital assets is recorded.

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

	<u>2007</u>	<u>2006</u>	<u>Change</u>
Operating Revenues			
Tuition and Fees, Net	\$ 49,424,075.95	\$ 47,929,884.69	\$ 1,494,191.26
Grants and Contracts	37,235,591.50	35,704,055.25	1,531,536.25
Federal Appropriations	4,479,086.69	5,023,260.80	(544,174.11)
Sales and Services, Net	24,251,028.38	24,590,908.73	(339,880.35)
Other Operating Revenues	1,693,827.24	1,519,962.12	173,865.12
Total Operating Revenues	<u>117,083,609.76</u>	<u>114,768,071.59</u>	<u>2,315,538.17</u>
Operating Expenses	<u>218,521,893.65</u>	<u>204,614,715.70</u>	<u>13,907,177.95</u>
Operating Loss	<u>(101,438,283.89)</u>	<u>(89,846,644.11)</u>	<u>(11,591,639.78)</u>
Nonoperating Revenues (Expenses)			
State Appropriations	89,056,885.06	80,441,591.31	8,615,293.75
Noncapital Grants and Gifts	9,711,266.87	14,349,503.38	(4,638,236.51)
Other Nonoperating Expenses	(1,221,051.93)	(1,330,554.06)	109,502.13
Other Nonoperating Revenues	3,835,348.19	2,047,041.20	1,788,306.99
Net Nonoperating Revenues	<u>101,382,448.19</u>	<u>95,507,581.83</u>	<u>5,874,866.36</u>
Income (Loss) Before Other Revenues	<u>(55,835.70)</u>	<u>5,660,937.72</u>	<u>(5,716,773.42)</u>
Capital Appropriations and Grants	60,359,052.22	8,111,084.10	52,247,968.12
Capital Gifts	0.00	70,263.00	(70,263.00)
Additions to Permanent Endowments	1,057,720.54	646,960.10	410,760.44
Total Other Revenues	<u>61,416,772.76</u>	<u>8,828,307.20</u>	<u>52,588,465.56</u>
Total Increase (Decrease) in Net Asset	<u>61,360,937.06</u>	<u>14,489,244.92</u>	<u>46,871,692.14</u>
Net Assets			
Beginning of the Year	<u>287,521,045.50</u>	<u>273,031,800.58</u>	<u>14,489,244.92</u>
End of the Year	<u>\$ 348,881,982.56</u>	<u>\$ 287,521,045.50</u>	<u>\$ 61,360,937.06</u>

During fiscal year 2007, operating revenues contributed 41.65% of total revenues, while nonoperating revenues made up 58.35%. Total University revenues increased by \$60,669,367.96 with the increase in capital appropriations and grants accounting for \$52,247,968.12 of that increase.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Operating revenues increased by \$2,315,538.17. Major operating revenue categories that experienced increases include tuition and fees, and grants and contracts. The \$1,494,191.26 increase in tuition and fees reflects an increase of \$225.00 per student for tuition and fees, while nongovernmental grants and contracts experienced an increase of \$1,338,502.36.

Net nonoperating revenues increased by \$5,874,866.36. The University received an increase in State appropriations of \$8,615,293.75 to cover operating budget increases and to fund new programs. The increase in State appropriations was offset by a decrease of \$4,638,236.51 in noncapital, grants and gifts. The University received a large single gift in fiscal year 2006, resulting in a decline in that category in 2007. Investment income increased by \$1,788,306.99 as cash and asset balances in endowment, auxiliary, and unrestricted funds increased during the year.

Capital appropriations and grant funds went up by \$52,247,968.12, primarily the result of increases in funds received in the current year or committed for future years from the State for bond construction projects, as well as increases in State appropriations for repair and replacement of facilities.

The University presents expenditures by natural classification in the Statement of Revenues, Expenses, and Changes in Net Assets. Personnel services accounted for 59.41% of operating expenses, followed by services at 17.37%, supplies and materials at 11.49%, scholarships at 5.09%, depreciation at 4.36%, and utility costs at 2.28%.

The rise in operating costs of \$13,907,177.95 is attributed primarily to increases in payroll charges and expenditures for supplies and materials. Payroll expenditures increased by \$10,325,662.93, as a result of a 5.5% payroll raise granted by the State legislature and the creation of new positions. The increases in payroll and supplies and materials were offset somewhat by a decrease in utilities of \$428,983.00, helped in part by a mild winter, but also due in part to the implementation of the Strategic Energy Management Planning program.

Capital Assets and Debt Administration

The cost of construction projects continued to exert significant influence on the University's financial statements for 2007 and will continue to do so through 2008. Since the passage in



The new 500 vehicle parking deck was completed in August of 2006.

November 2000 of a \$2.5 billion bond package for the improvement and expansion of facilities on the 16 campuses of the University of North Carolina system, the University has received over \$124,989,165.18 in State construction grants financed by the bond proceeds. All twenty-two of the University's bond-funded projects were under design, in the construction phase or completed at June 30, 2007. During 2007 the University completed major renovation projects, totaling \$8,705,458.04, for Harrison Auditorium and Graham Hall and made significant progress on a new classroom building for the School of

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Education. The University also received \$4,988,862.29 in grant funds from the Office of Education to support the construction of the School of Education facility. In addition to the construction projects funded through State bonds, the University completed a parking deck, designed to accommodate 500 vehicles.

Long-term debt totaled \$18,420,000.00 at June 30, 2007. The University retired \$6,168,000.00 in temporary construction financing through the issuance of long-term debt in the amount of \$6,234,366.50, including a premium of \$269,366.50. In addition, the University refunded Dining System bonds, totaling \$7,910,000.00, using \$7,525,000.00 from a new bond issue and funds from other sources in the amount of \$927,660.18. The economic gain to the University is expected to total \$290,470.76.

Highlights

Several promising initiatives began in 2007. North Carolina Agricultural and Technical State University entered into a collaborative partnership with the University of North Carolina at Greensboro that will establish state-of-the-art research facilities. The research facilities will make possible cutting edge work in life and physical sciences, engineering, technology and other applied science areas. The ribbon cutting and ground breaking ceremony that took place on May 16, 2007, marked the start of construction on the South Campus of the Gateway University Research Park. The South Campus is located on 75 acres of the University's farm. The North Campus, located off Highway 29 near Bryan Park, currently has eight buildings that will be renovated to support economic development and University research in the areas of the social sciences.

The University of North Carolina Board of Governors established the Joint School of Nanoscience and Nanoengineering with North Carolina A & T State University and the University of North Carolina at Greensboro. The Nanotechnology School will be located on the Gateway University Research Park.

With the assistance of the North Carolina Biotechnology Center, The School of Agriculture and Environmental Sciences created a company named Provagen. A first for North Carolina Agricultural and Technical State University, the spinoff company will market its patented "Synthetic Protein V" in the multibillion dollar biotechnology industry. Provagen's technology can be used to purify and isolate antibodies that can be used in the diagnosis and treatment of several diseases.

Economic Forecast

The University anticipates that enrollment will remain relatively flat over the next two years and then begin a trend of slow, but steady growth again by the year 2009. The level enrollment figures will result in only small increases in State appropriations during this period. Currently, State revenues remain strong, but if the downturn of the economy affects tax receipts that outlook may change. State economists at present do not expect a significant economic slowdown for the State over the next twelve to eighteen months and that should result in stable funding levels.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONCLUDED)

State appropriations comprise only about 32 percent of the University's annual revenues. The University will continue to look for financial resources to supplement State support and help provide the level of services required by academic support functions, financial aid needs, and research activities. Although the five year capital campaign comes to a close in December 2007, the University will continue to cultivate support through community and national partnerships as well as alumni relationships.

North Carolina Agricultural and Technical State University
Statement of Net Assets
June 30, 2007

Exhibit A-1

ASSETS

Current Assets:

Cash and Cash Equivalents	\$ 37,541,778.04
Restricted Cash and Cash Equivalents	12,654,603.92
Receivables, Net (Note 4)	8,920,500.10
Due from Primary Government	371,000.00
Due from University Component Units	8,506.30
Inventories	1,566,096.13
Notes Receivable, Net (Note 4)	318,934.45
	<hr/>
Total Current Assets	61,381,418.94

Noncurrent Assets:

Restricted Cash and Cash Equivalents	9,331,625.37
Receivables (Note 4)	409,624.89
Restricted Due from Primary Government	39,249,443.29
Endowment Investments	13,124,523.51
Other Investments	2,112.21
Notes Receivable, Net (Note 4)	1,078,804.43
Capital Assets - Nondepreciable (Note 5)	30,341,088.24
Capital Assets - Depreciable, Net (Note 5)	235,203,592.55
	<hr/>
Total Noncurrent Assets	328,740,814.49

Total Assets	<hr/> <hr/> 390,122,233.43
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LIABILITIES

Current Liabilities:

Accounts Payable and Accrued Liabilities (Note 6)	8,483,634.66
Due to Primary Government	66,135.75
Unearned Revenue	4,203,911.14
Interest Payable	233,326.58
Long-Term Liabilities - Current Portion (Note 8)	1,499,008.66
	<hr/>
Total Current Liabilities	14,486,016.79

Noncurrent Liabilities:

Deposits Payable	403,931.78
Funds Held for Others	56,772.92
U. S. Government Grants Refundable	1,310,739.88
Long-Term Liabilities (Note 8)	24,982,789.50
	<hr/>

Total Noncurrent Liabilities	26,754,234.08
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Total Liabilities	<hr/> <hr/> 41,240,250.87
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North Carolina Agricultural and Technical State University
Statement of Net Assets
June 30, 2007

Exhibit A-1
Page 2

NET ASSETS

Invested in Capital Assets, Net of Related Debt	247,124,680.79
Restricted for:	
Nonexpendable:	
Scholarships and Fellowships	5,949,176.46
Endowed Professorships	4,531,992.18
Departmental Uses	73,079.31
Loans	291,078.23
Expendable:	
Scholarships and Fellowships	3,729,565.15
Research	234,735.14
Endowed Professorships	1,693,411.27
Departmental Uses	3,490,780.04
Capital Projects	45,800,686.67
Unrestricted	<u>35,962,797.32</u>
Total Net Assets	<u>\$ 348,881,982.56</u>

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

North Carolina Agricultural and Technical State University
Statement of Revenues, Expenses, and
Changes in Net Assets
For the Fiscal Year Ended June 30, 2007

Exhibit A-2

REVENUES

Operating Revenues:	
Student Tuition and Fees, Net (Note 10)	\$ 49,424,075.95
Federal Appropriations	4,479,086.69
Federal Grants and Contracts	34,118,822.58
State and Local Grants and Contracts	617,327.37
Nongovernmental Grants and Contracts	2,499,441.55
Sales and Services, Net (Note 10)	24,251,028.38
Interest Earnings on Loans	3,428.17
Other Operating Revenues	1,690,399.07
	<hr/>
Total Operating Revenues	117,083,609.76

EXPENSES

Operating Expenses:	
Salaries and Benefits	129,818,336.20
Supplies and Materials	25,103,046.46
Services	37,954,265.12
Scholarships and Fellowships	11,115,584.65
Utilities	4,996,575.53
Depreciation	9,534,085.69
	<hr/>
Total Operating Expenses	218,521,893.65
	<hr/>
Operating Loss	(101,438,283.89)

NONOPERATING REVENUES (EXPENSES)

State Appropriations	89,056,885.06
Noncapital Grants	9,016,786.79
Noncapital Gifts	694,480.08
Investment Income (Net of Investment Expense of \$28,890.63)	3,835,348.19
Interest and Fees on Debt	(1,117,335.47)
Other Nonoperating Expenses	(103,716.46)
	<hr/>
Net Nonoperating Revenues	101,382,448.19
	<hr/>
Income Before Other Revenues	(55,835.70)

Capital Appropriations	7,880,700.00
Capital Grants	52,478,352.22
Additions to Endowments	1,057,720.54
	<hr/>
Increase in Net Assets	61,360,937.06

NET ASSETS

Net Assets - July 1, 2006	<hr/>
	287,521,045.50
	<hr/>
Net Assets - June 30, 2007	\$ 348,881,982.56

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

North Carolina Agricultural and Technical State University
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2007

Exhibit A-3

CASH FLOWS FROM OPERATING ACTIVITIES

Received from Customers	\$ 115,523,476.93
Payments to Employees and Fringe Benefits	(128,297,118.89)
Payments to Vendors and Suppliers	(67,674,132.17)
Payments for Scholarships and Fellowships	(11,115,584.65)
Loans Issued	(433,918.00)
Collection of Loans	542,326.97
Interest Earned on Loans	15,064.06
Other Receipts	1,690,399.07
	<hr/>
Net Cash Used by Operating Activities	(89,749,486.68)

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

State Appropriations	89,056,885.06
Noncapital Grants	8,168,424.38
Noncapital Gifts	526,887.47
Additions Endowments	1,057,720.54
William D. Ford Direct Lending Receipts	47,003,918.00
William D. Ford Direct Lending Disbursements	(47,003,918.00)
Related Activity Agency Receipts	86,057.56
Related Activity Agency Disbursements	(35,276.93)
Other Receipts	11,567.21
	<hr/>
Net Cash Provided by Noncapital Financing Activities	98,872,265.29

CASH FLOWS FROM CAPITAL FINANCING AND RELATED FINANCING ACTIVITIES

Proceeds from Capital Debt	13,411,507.15
State Capital Appropriations	7,880,700.00
Capital Grants	18,309,172.02
Proceeds from Sale of Capital Assets	69.99
Acquisition and Construction of Capital Assets	(23,960,929.25)
Principal Paid on Capital Debt and Leases	(7,153,000.00)
Interest and Fees Paid on Capital Debt and Leases	(1,094,233.92)
Payment to Bond Escrow Agent	(7,910,000.00)
	<hr/>
Net Cash Used by Capital Financing and Related Financing Activities	(516,714.01)

CASH FLOWS FROM INVESTING ACTIVITIES

Proceeds from Sales and Maturities of Investments	3,898,238.07
Investment Income	3,508,392.18
Purchase of Investments and Related Fees	(6,537,219.27)
	<hr/>
Net Cash Provided by Investing Activities	869,410.98

Net Increase in Cash and Cash Equivalents	9,475,475.58
Cash and Cash Equivalents - July 1, 2006	50,052,531.74
	<hr/>
Cash and Cash Equivalents - June 30, 2007	\$ 59,528,007.32

The North Carolina A&T University Foundation, Inc.
Statement of Financial Position
June 30, 2007

Exhibit B-1

ASSETS

Current Assets

Cash and Cash Equivalents	\$ 638,642
Investments	3,721,211
Unconditional Promises to Give	264,561
Accounts Receivable - NCA&TSU	120,606
Other Current Assets	415,459

Total Current Assets	5,160,479
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Restricted Deposits

Bond Operating Reserve Fund	504,700
Bond Interest Fund	175,526
Bond Surplus Fund	1,014,918
Bond Repair and Replacement Fund	81,291
Bond Taxes and Insurance Fund	67,788
Bond Debt Service Fund	3,198,311
Bond Fund Principal Fund	87,917
Bond Pledged Revenue Fund	92,000

Total Restricted Deposits	5,222,451
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Endowment Investments

Investments	3,683,996
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Property, Furniture and Equipment, at Cost, Net

37,604,374

Long-term Unconditional Promises to Give, Less

Allowance For Uncollectible Promises of \$41,250 for 2007	253,553
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Other Assets	4,107,206
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Total Assets	\$ 56,032,059
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LIABILITIES

Current Liabilities

Current Maturities of Bonds Payable	\$ 1,055,000
Accounts Payable	44,209
Other Liabilities	303,506

Total Current Liabilities	1,402,715
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Long-Term Liabilities

Bonds Payable, Less Current Maturities	46,645,000
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Total Liabilities	48,047,715
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The North Carolina A&T University Foundation, Inc.
Statement of Financial Position
June 30, 2007

Exhibit B-1
Page 2

NET ASSETS

Unrestricted:	
Operating	33,796
Fixed Assets	99,606
	<hr/>
Total Unrestricted	133,402
Temporarily Restricted	3,995,517
Permanently Restricted	3,855,425
	<hr/>
Total Net Assets	7,984,344
	<hr/>
Total Liabilities and Net Assets	\$ 56,032,059
	<hr/> <hr/>

See accompanying notes to the financial statements.

North Carolina A&T University Foundation, Inc.
Statement of Activities
For the Fiscal Year Ended June 30, 2007

Exhibit B-2

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
PUBLIC SUPPORT, REVENUES AND RECLASSIFICATIONS				
Contributions				
Foundations and Corporations	\$ 45,148	\$ 1,200,073	\$ 54,232	\$ 1,299,453
Board of Directors	5,500	2,000	4,400	11,900
Individuals/Friends	2,556	868,044	136,696	1,007,296
Interest and Dividends	403,941	127,206	101,260	632,407
Administrative Fee	93,744			93,744
Miscellaneous	204,171	429,289		633,460
Unrealized Gain from Investments	230,295	312,341		542,636
Net Assets Released From Restrictions:				
Satisfaction of Program Restrictions	3,280,637	(3,280,637)		
Rental Income	6,281,772			6,281,772
Management Fees	264,385			264,385
Fundraising	167,875			167,875
Gain From Sale of Property (Net)	15,000			15,000
Total Public Support, Revenues and Reclassifications	<u>10,995,024</u>	<u>(341,684)</u>	<u>296,588</u>	<u>10,949,928</u>
EXPENSES				
Programs:				
Scholarships:				
Scholarships-Unrestricted	140,047			140,047
Scholarships-Departmental	1,122,696			1,122,696
Total Scholarships	<u>1,262,743</u>			<u>1,262,743</u>
Academic Departmental Programs	2,157,941			2,157,941
Administration	889,954			889,954
Student Housing	6,257,970			6,257,970
Transfer to NCA&TSU and Promises to Give Writeoffs			104,679	104,679
Total Expenses	<u>10,568,608</u>		<u>104,679</u>	<u>10,673,287</u>
Changes in Net Assets	426,416	(341,684)	191,909	276,641
Net Assets as of Beginning of Year	<u>(293,014)</u>	<u>4,337,201</u>	<u>3,663,516</u>	<u>7,707,703</u>
Net Assets as of End of Year	<u>\$ 133,402</u>	<u>\$ 3,995,517</u>	<u>\$ 3,855,425</u>	<u>\$ 7,984,344</u>

See accompanying notes to financial statements.

NORTH CAROLINA AGRICULTURAL AND TECHNICAL STATE UNIVERSITY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2007

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. North Carolina Agricultural and Technical 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 is reported in separate financial statements because of its use of different GAAP reporting models and to emphasize its legal separateness.

Discretely Presented Component Units - The North Carolina A&T University Foundation, Inc., is a legally separate not-for-profit corporation and is reported as a discretely presented component unit based on the nature and significance of its relationship to the University.

The North Carolina A&T University Foundation, Inc., is a legally separate, tax-exempt component unit of the 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 16 elected members. 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 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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

reported in separate financial statements because of the difference in its reporting model, as described below.

The North Carolina A&T University Foundation, Inc., is a private not-for-profit organization that reports its financial results under Financial Accounting Standards Board (FASB) Statements. As such, certain revenue recognition criteria and presentation features are different from 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, 2007, the Foundation distributed \$1,804,046.05 to the University for both restricted and unrestricted purposes. Complete financial statements for the Foundation can be obtained from The North Carolina A&T University Foundation, Inc., located at The Alumni Foundation Events Center, 200 North Benbow Road, Greensboro, North Carolina 27411-0001. The mailing address is P.O. Box 20366, Greensboro, NC 27420.

- 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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

recognized when earned, and expenses are recorded when an obligation has been incurred, regardless of the timing of the cash flows.

Nonexchange transactions, in which the University receives (or gives) value without directly giving (or receiving) equal value in exchange includes State appropriations, certain grants, and donations. Revenues are recognized, net of estimated uncollectible amounts, as soon as all eligibility requirements imposed by the provider have been met, if probable of collection.

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

E. Investments - This classification includes long-term fixed income investments, equity investments, mutual funds, money market funds, real estate investment trusts, and real estate. Except for money market funds and real estate not held by a governmental external investment pool, investments are accounted for at fair value, as determined by quoted market prices, or an amount determined by management if quoted market prices are not available. The net increase in the fair value of investments is recognized as a component of investment income.

Money market funds and real estate not held by a governmental external investment pool are reported at cost, if purchased, or at fair value or appraised value at date of gift, if donated.

F. Receivables - Receivables consist of tuition and fees charged to students and charges for auxiliary enterprises' sales and services. Receivables also include amounts due from the federal government, State and local governments, private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants, and pledges that are verifiable, measurable, and expected to be collected and available for 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 cost using average cost of last invoice price, using first-in, first-out method or, in the case of agricultural supplies inventory, current market

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

value. 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 of more than one year unless part of a collection and are expensed in the year of acquisition.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 10 to 50 years for general infrastructure, 10 to 50 years for buildings, and 5 to 15 years for equipment.

The Heritage Center and Art Gallery collections are capitalized at cost or fair value at the date of donation. These collections are considered inexhaustible and are therefore not depreciated.

- I. Restricted Assets** - Unexpended proceeds of revenue bonds and unexpended capital contributions are classified as restricted assets because their use is limited by applicable bond covenants or donor/grantor agreements. These assets are also classified as noncurrent since they cannot be used for current operations. Certain other assets are classified as restricted because their use is limited by external parties or statute.
- J. Noncurrent Long-Term Liabilities** - Noncurrent long-term liabilities include principal amounts of bonds payable and compensated absences that will not be paid within the next fiscal year.

Bonds payable are reported net of unamortized premiums or discounts and deferred losses on refunds. The University amortizes bond premiums/discounts over the life of the bonds using the straight-line method. The deferred losses on refunds are amortized over the life of the old debt using the straight-line method. Issuance costs 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 for SPA and EPA employees. An employee can be paid up to 30 days upon termination of employment. When classifying compensated absences into current and noncurrent, leave is considered

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 EPA and SPA employees at June 30 equals the leave carried forward at the previous December 31 plus the leave earned, less the leave taken between January 1 and June 30.

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

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

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

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

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

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

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

Restricted and unrestricted resources are tracked using a fund accounting system and are spent in accordance with established fund authorities. Fund authorities provide rules for the fund activity and are separately established for restricted and unrestricted activities. When both restricted

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

and unrestricted funds are available for expenditure, the decision for funding is transactional based within the departmental management system in place at the University. For projects funded by tax-exempt debt proceeds and other sources, the debt proceeds are always used first.

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

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

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

O. Internal Sales Activities - Certain institutional auxiliary operations provide goods and services to University departments, as well as to its

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

customers. These institutional auxiliary operations include activities such as bookstore, motor pool, postal services, and telecommunications. In addition, the University has other miscellaneous sales and service units that operated either on a reimbursement or charge basis. All internal sales activities to University departments from auxiliary operations and sales and service units have been eliminated in the accompanying financial statements. These eliminations are recorded by removing the revenue and expense in the auxiliary operations and sales and service units and, if significant, allocating any residual balances to those departments receiving the goods and services during the year.

NOTE 2 - DEPOSITS AND INVESTMENTS

- A. Deposits** - Unless specifically exempt, the University is required by *North Carolina General Statute 147-77* to deposit moneys received with the State Treasurer or with a depository institution in the name of the State Treasurer. In addition, the University of North Carolina Board of Governors, pursuant to G.S. 116-36.1, requires the University to deposit its institutional trust funds, except for funds received for services rendered by health care professionals, with the State Treasurer. Although specifically exempted, the University may voluntarily deposit endowment funds, special funds, revenue bond proceeds, debt service funds, and funds received for services rendered by health care professionals with the State Treasurer. Special funds consist of moneys for intercollegiate athletics and agency funds held directly by the University.

At June 30, 2007, the amount shown on the Statement of Net Assets as cash and cash equivalents includes \$59,312,761.02 which represents the University's equity position in the State Treasurer's Short-Term Investment Fund. The Short-Term Investment Fund (a portfolio within the State Treasurer's Investment Pool, an external investment pool that is not registered with the Securities and Exchange Commission and does not have a credit rating) had a weighted average maturity of 1.6 years as of June 30, 2007. Assets and shares of the Short-Term Investment Fund are valued at amortized cost, which approximates fair value. Deposit and investment risks associated with the State Treasurer's Investment Pool (which includes the State Treasurer's Short-Term Investment Fund) are included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.ncosc.net/> and clicking on "Financial Reports," or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Cash on hand at June 30, 2007, was \$50,498.31. The carrying amount of the University's deposits not with the State Treasurer was \$164,748.00 and the bank balance was \$159,426.75. 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, 2007, the University's bank balance was exposed to custodial credit risk as follows:

Uninsured and Uncollateralized	<u>\$ 59,383.21</u>
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- B. Investments** - The University is authorized by The University of North Carolina Board of Governors pursuant to G.S. 116-36.2 and Section 600.2.4 of the Policy Manual of the University of North Carolina, to invest its special funds and funds received for services rendered by health care professionals in the same manner as the State Treasurer is required to invest, as discussed below.

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

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

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Investments of the University's component unit, the North Carolina A&T University Foundation, Incorporated, are subject to and restricted by G.S. 36B "Uniform Management of Institutional Funds Act" (UMIFA) and any requirements placed on them by contract or donor agreements.

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

Investments are subject to the following risks.

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

Credit Risk: Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The University's Endowment Board's investment policy addresses credit risk by requiring high quality fixed income instruments, evaluating mutual funds on the basis of their standing on the Lipper 500 Index, and by evaluating stocks on their ability to sustain long-term total returns.

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

Long-Term Investment Pool

Investment Type	Fair Value	Investment Maturities (in Years)		
		Less Than 1	1 to 5	6 to 10
Debt Securities				
U.S. Agencies	\$ 492,094.50	\$ 148,203.50	\$ 195,187.50	\$ 148,703.50
Mutual Bond Funds	1,659,890.97			1,659,890.97
Money Market Mutual Funds	358,253.61	358,253.61		
Domestic Corporate Bonds	616,457.00		616,457.00	
		<u>\$ 506,457.11</u>	<u>\$ 811,644.50</u>	<u>\$ 1,808,594.47</u>
Other Securities				
Other Mutual Funds	6,313,282.01			
Investments in Real Estate	11,690.00			
Real Estate Investment Trust	42,060.63			
Domestic Stocks	3,419,526.54			
Foreign Stocks	211,268.25			
Total Long-Term Investment Pool	<u>\$ 13,124,523.51</u>			

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

	Fair Value	AAA Aaa	AA Aa	A	Unrated
U.S. Agencies	\$ 492,094.50	\$ 492,094.50	\$ 0.00	\$ 0.00	\$ 0.00
Mutual Bond Funds	1,659,890.97		631,809.33	1,028,081.64	
Money Market Mutual Funds	358,253.61				358,253.61
Domestic Corporate Bonds	616,457.00		357,331.00	259,126.00	

Rating Agency: Moody's

Non-Pooled Investments - At year end, the University held a money market fund investment with a fair value of \$675.25 and a maturity of less than one year. The fund is unrated. Also, the University held domestic stocks with a fair value of \$1,436.96.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

	Fair Value
Investment Type	
Debt Securities	
U.S. Agencies	\$ 492,094.50
Mutual Bond Funds	1,659,890.97
Money Market Funds	358,928.86
Domestic Corporate Bonds	616,457.00
Other Securities	
Other Mutual Funds	6,313,282.01
Investments in Real Estate	11,690.00
Real Estate Investment Trust	42,060.63
Domestic Stocks	3,420,963.50
Foreign Stocks	211,268.25
Total Investments	<u>\$ 13,126,635.72</u>

Component Units - Investments of the University's discretely presented component unit, The North Carolina A&T University Foundation, Inc., are subject to and restricted by G.S. 36B "Uniform Management of Institutional Funds Act" (UMIFA) and any requirements placed on them by contract or donor agreements. Because the Foundation reports under the FASB reporting model, disclosures of the various investment risks are not required. The following is an analysis of investments by type: The Foundation's investments include mutual funds administered by Wachovia Bank in the amount of \$7,390,207 and stock in the amount of \$15,000. The total amount of investments for The North Carolina A&T University Foundation, Inc., is \$7,405,207.

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). Annual payouts from the University's endowment funds are based on an adopted spending policy which limits spending to not more than 5% of the endowment principal's market value at December 31 for the past three years. To the extent that the total return for the current year exceeds the payout, the excess is added to principal. If current year earnings do not meet the payout requirements, the University uses accumulated income and appreciation from restricted, expendable net

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

asset endowment balances to make up the difference. At June 30, 2007, net appreciation of \$497,600.00 was available to be spent, all of which was restricted to specific purposes.

NOTE 4 - RECEIVABLES

Receivables at June 30, 2007, were as follows:

	<u>Gross Receivables</u>	<u>Less Allowance for Doubtful Accounts</u>	<u>Net Receivables</u>
Current Receivables:			
Students	\$ 1,623,380.10	\$ 595,839.01	\$ 1,027,541.09
Accounts	1,245,383.29	455,778.62	789,604.67
Intergovernmental	6,065,455.33		6,065,455.33
Pledges	209,286.00		209,286.00
Investment Earnings	381,233.39		381,233.39
Interest on Loans	121,949.23		121,949.23
Other	325,430.39		325,430.39
Total Current Receivables	<u>\$ 9,972,117.73</u>	<u>\$ 1,051,617.63</u>	<u>\$ 8,920,500.10</u>
Noncurrent Receivables:			
Pledges	<u>\$ 409,624.89</u>	<u>\$ 0.00</u>	<u>\$ 409,624.89</u>
Notes Receivable:			
Notes Receivable - Current:			
Federal Loan Programs	<u>\$ 436,950.19</u>	<u>\$ 118,015.74</u>	<u>\$ 318,934.45</u>
Notes Receivable - Noncurrent:			
Federal Loan Programs	<u>\$ 1,478,678.71</u>	<u>\$ 399,874.28</u>	<u>\$ 1,078,804.43</u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 5 - CAPITAL ASSETS

A summary of changes in the capital assets for the year ended June 30, 2007, is presented as follows:

	Balance July 1, 2006	Increases	Decreases	Balance June 30, 2007
Capital Assets, Nondepreciable:				
Land	\$ 8,871,986.09	\$ 0.00	\$ 0.00	\$ 8,871,986.09
Art, Literature, and Artifacts	2,502,077.00			2,502,077.00
Construction in Progress	14,539,996.50	14,749,179.94	10,322,151.29	18,967,025.15
Total Capital Assets, Nondepreciable	25,914,059.59	14,749,179.94	10,322,151.29	30,341,088.24
Capital Assets, Depreciable:				
Buildings	247,294,998.58	16,488,362.00		263,783,360.58
Machinery and Equipment	39,746,338.25	3,358,667.38	738,568.49	42,366,437.14
General Infrastructure	14,775,435.29			14,775,435.29
Total Capital Assets, Depreciable	301,816,772.12	19,847,029.38	738,568.49	320,925,233.01
Less Accumulated Depreciation/Amortization for:				
Buildings	52,080,332.63	5,167,142.01		57,247,474.64
Machinery and Equipment	22,541,706.41	3,922,239.08	634,782.04	25,829,163.45
General Infrastructure	2,200,297.77	444,704.60		2,645,002.37
Total Accumulated Depreciation	76,822,336.81	9,534,085.69	634,782.04	85,721,640.46
Total Capital Assets, Depreciable, Net	224,994,435.31	10,312,943.69	103,786.45	235,203,592.55
Capital Assets, Net	\$ 250,908,494.90	\$ 25,062,123.63	\$ 10,425,937.74	\$ 265,544,680.79

NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

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

	Amount
Accounts Payable	\$ 3,917,790.28
Accrued Payroll	3,179,321.09
Contract Retainage	1,166,909.28
Intergovernmental Payables	219,614.01
Total Accounts Payable and Accrued Liabilities	\$ 8,483,634.66

NOTE 7 - SHORT-TERM DEBT

The University issued a bond anticipation note to secure funds for the construction of a 500 space parking deck. Construction began in the spring of 2006 and was completed in the fall of 2006. The note was paid in full with the issuance of UNC System Pool Revenue Bonds, Series 2006 B, issued in February 2007.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Short-term debt activity for the year ended June 30, 2007, was as follows:

	Balance July 1, 2006	Draws	Repayments	Balance June 30, 2007
Bond Anticipation Notes	\$ 6,168,000.00	\$ 0.00	\$ 6,168,000.00	\$ 0.00

NOTE 8 - LONG-TERM LIABILITIES

A. Changes in Long-Term Liabilities - A summary of changes in the long-term liabilities for the year ended June 30, 2007, is presented as follows:

	Balance July 1, 2006	Additions	Reductions	Balance June 30, 2007	Current Portion
Revenue Bonds Payable	\$ 13,825,000.00	\$ 13,490,000.00	\$ 8,895,000.00	\$ 18,420,000.00	\$ 1,135,000.00
Add/Deduct Premium/Discount	99,587.95	382,240.20	26,451.28	455,376.87	
Deduct Deferred Charge on Refunding	(183,697.75)	(460,733.05)	(42,977.29)	(601,453.51)	
Total Bonds Payable	13,740,890.20	13,411,507.15	8,878,473.99	18,273,923.36	1,135,000.00
Compensated Absences	7,394,032.01	4,344,123.01	3,530,280.22	8,207,874.80	364,008.66
Total Long-Term Liabilities	\$ 21,134,922.21	\$ 17,755,630.16	\$ 12,408,754.21	\$ 26,481,798.16	\$ 1,499,008.66

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

Purpose	Series	Interest Rate/ Ranges	Final Maturity Date	Original Amount of Issue	Principal Paid Through June 30, 2007	Principal Outstanding June 30, 2007
UNC System Pool Revenue Bonds						
Student Union (A)	1998B	3.25-5.25	10/01/2013	\$ 5,860,000.00	\$ 5,040,000.00	\$ 820,000.00
Parking System (A)	1998B	3.25-5.25	10/01/2013	1,465,000.00	660,000.00	805,000.00
Student Union (C)	2005A	3.00-4.89	04/01/2014	2,395,000.00	20,000.00	2,375,000.00
Stadium-Student Fees (B)	2000	5.00-5.25	10/01/2020	1,555,000.00	625,000.00	930,000.00
Parking Deck (D)	2006B	3.75-5.00	10/01/2033	5,965,000.00		5,965,000.00
Dining System Refunding (D)	2006B	3.75-5.00	10/01/2020	7,525,000.00		7,525,000.00
Total UNC System Pool Revenue Bonds				24,765,000.00	6,345,000.00	18,420,000.00
Total Bonds Payable (principal only)				\$ 24,765,000.00	\$ 6,345,000.00	
Less: Unamortized Loss on Refunding						(601,453.51)
Less: Unamortized Discount						(4,525.42)
Plus: Unamortized Premium						459,902.29
Total Bonds Payable						\$ 18,273,923.36

(A) The University of North Carolina System Pool Revenue Bonds, Series 1998B
(B) The University of North Carolina System Pool Revenue Bonds, Series 2000
(C) The University of North Carolina System Pool Revenue Bonds, Series 2005A
(D) The University of North Carolina System Pool Revenue Bonds, Series 2006B

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

- C. Annual Requirements** - The annual requirements to pay principal and interest on the long-term obligations at June 30, 2007, are as follows:

Fiscal Year	Annual Requirements	
	Revenue Bonds Payable	
	Principal	Interest
2008	\$ 1,135,000.00	\$ 909,831.28
2009	1,200,000.00	801,353.15
2010	1,240,000.00	698,900.02
2011	1,285,000.00	648,446.89
2012	1,345,000.00	590,031.26
2013-2017	4,745,000.00	2,157,112.55
2018-2022	3,380,000.00	1,320,650.05
2023-2027	1,025,000.00	878,071.88
2028-2032	2,075,000.00	506,581.25
2033-2037	990,000.00	49,100.00
Total Requirements	\$ 18,420,000.00	\$ 8,560,078.33

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

On November 30, 2006, the University issued \$7,525,000.00 in The University of North Carolina System Pool Revenue Bond Series 2006B refunding bonds with an average interest rate of 4.23%. The bonds were issued to advance refund \$7,910,000.00 of outstanding University of North Carolina System Pool Revenue Bonds, Series 2000, with an average interest rate of 5.35%. The net proceeds of the refunding bonds were used to purchase U.S. government securities. These securities were deposited into an irrevocable trust to provide for all future debt service payments on the refunded bonds. As a result, the refunded bonds are considered to be defeased and the liability has been removed from the University's Statement of Net Assets. This advance refunding was undertaken to reduce total debt service payments by \$1,437,699.10 over the next 15 years and resulted in an economic gain of \$290,470.76. At June 30, 2007, the outstanding balance was \$7,910,000.00 for the defeased University of North Carolina System Pool Revenue Bonds, Series 2000.

Prior Year Defeasances - 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, 2007, the outstanding balance of prior year defeased bonds was \$2,390,000.00.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

E. Component Units - The North Carolina A&T University Foundation, Inc., issued bonds to finance the construction of student housing. Bonds payable for the Foundation at June 30, 2007 were \$47,700,000.00.

NOTE 9 - LEASE OBLIGATIONS

Operating Lease Obligations - The University entered into operating leases for rental of equipment and real estate. Future minimum lease payments under noncancelable operating leases consist of the following at June 30, 2007:

<u>Fiscal Year</u>	<u>Amount</u>
2008	\$ 286,478.95
2009	66,947.40
2010	15,631.80
Total Minimum Lease Payments	<u>\$ 369,058.15</u>

Rental expense for all operating leases during the year was \$421,978.50.

NOTE 10 - REVENUES

A summary of eliminations and allowances by revenue classification and revenues pledged as security for revenue bonds 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>	<u>Revenues Pledged as Security for Debt</u>
Operating Revenues:						
Student Tuition and Fees	\$ 62,650,984.16	\$ 0.00	\$ 12,602,525.72	\$ 624,382.49	\$ 49,424,075.95	\$ 1,598,713.76 (A)
Sales and Services:						
Sales and Services of Auxiliary Enterprises:						
Residential Life	\$ 9,571,045.49	\$ 0.00	\$ 1,846,974.29	\$ 92,782.37	\$ 7,631,288.83	\$ 0.00
Dining	8,963,486.11		1,776,063.66	88,650.32	7,098,772.13	7,098,772.13 (B)
Student Union Services	46,178.56				46,178.56	
Health, Physical Education, and Recreation Services	1,240.80				1,240.80	
Bookstore	6,249,610.88	66,026.14		88.89	6,183,495.85	
Parking	886,609.24			17.67	886,591.57	886,591.57 (C)
Athletic	1,802,422.06				1,802,422.06	
Recreational Services	75,219.41				75,219.41	
Other	380,657.23			3,157.26	377,499.97	
Sales and Services of Education and Related Activities	2,166,066.54	2,017,747.34			148,319.20	
Total Sales and Services	<u>\$ 30,142,536.32</u>	<u>\$ 2,083,773.48</u>	<u>\$ 3,623,037.95</u>	<u>\$ 184,696.51</u>	<u>\$ 24,251,028.38</u>	<u>\$ 7,985,363.70</u>

Revenue Bonds Secured by Pledged Revenues:

- (A) Student Union, Stadium, and Parking System Bonds
- (B) Dining System Bonds
- (C) Parking System Bonds

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 11 - 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	\$ 61,346,604.43	\$ 1,493,116.17	\$ 1,873,565.67	\$ 824,585.29	\$ 0.00	\$ 0.00	\$ 65,537,871.56
Research	13,843,725.21	1,989,535.74	4,236,771.03	1,078,566.67			21,148,598.65
Public Service	4,580,480.29	367,634.52	1,047,831.95	130,893.43	234.69		6,127,074.88
Academic Support	13,268,325.73	6,917,737.57	4,917,298.56	1,534,764.97	1,321.87		26,639,448.70
Student Services	5,430,405.32	323,079.20	1,216,243.77	80,655.65			7,050,383.94
Institutional Support	13,309,365.00	1,198,104.92	5,073,601.82	14,537.17	4,196.09		19,599,805.00
Operations and Maintenance of Plant	8,190,798.47	6,997,773.11	5,000,109.45		3,354,087.83		23,542,768.86
Student Financial Aid	158,835.18	42,301.23	667,303.42	5,184,253.83			6,052,693.66
Auxiliary Enterprises	9,689,796.57	5,773,764.00	13,921,539.45	2,267,327.64	1,636,735.05		33,289,162.71
Depreciation						9,534,085.69	9,534,085.69
Total Operating Expenses	\$ 129,818,336.20	\$ 25,103,046.46	\$ 37,954,265.12	\$ 11,115,584.65	\$ 4,996,575.53	\$ 9,534,085.69	\$ 218,521,893.65

NOTE 12 - PENSION PLANS

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

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

Benefit and contribution provisions for the Teachers' and State Employees' Retirement System are established by *North Carolina General Statutes* 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contribution rates are set each year by the North Carolina General Assembly based on annual actuarial valuations. For the year ended June 30, 2007, these rates were set at 2.66% of covered payroll for employers and 6% of covered payroll for members.

For the year ended June 30, 2007, the University had a total payroll of \$107,255,804.60, of which \$59,456,776.53 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were \$3,567,406.59 and \$1,581,550.26, respectively. The University made

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

100% of its annual required contributions for the years ended June 30, 2007, 2006, and 2005, which were \$1,581,550.26, \$1,265,048.44, and \$1,086,916.00, respectively.

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

The Optional Retirement Program (Program) is a defined contribution retirement plan that provides retirement benefits with options for payments to beneficiaries in the event of the participant's death. Administrators and eligible faculty of the University may join the Program instead of the Teachers' and State Employees' Retirement System. The Board of Governors of The University of North Carolina is responsible for the administration of the Program and designates the companies authorized to offer investment products. The Board has authorized the following carriers: Teachers' Insurance and Annuity Association - College Retirement Equities Fund (TIAA-CREF), Lincoln Life Insurance Company, Variable Annuity Life Insurance Company (VALIC), and Fidelity Investments. Participants may elect to allocate their contributions and the University contributions to the carrier of their choice. Each carrier offers a variety of investment funds, including both fixed and variable account investment options and mutual funds.

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

Participant eligibility and contributory requirements are established by General Statute 135-5.1. Employer and member contribution rates are set each year by the North Carolina General Assembly. For the year ended June 30, 2007, these rates were set at 6.84% of covered payroll for employers and 6% of covered payroll for members. The University assumes no liability other than its contribution.

For the year ended June 30, 2007, the University had a total payroll of \$107,255,804.60, of which \$30,905,971.24 was covered under the Optional Retirement Program. Total employee and employer contributions for pension benefits for the year were \$1,854,358.27 and \$2,113,968.43, respectively.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The Federal Retirement System is a multiple-employer system. University extension employees participate in the Civil Service Retirement System (CSRS), a program for participants employed prior to January 1, 1987. Participants contributed approximately 7.0% of their salary to CSRS and the University match was approximately 7.23%. For the year ended June 30, 2007, covered payroll was \$1,089,069.14 and the total employee and employer contributions were \$76,234.84 and \$78,724.10, 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 \$236,224.51 for the year ended June 30, 2007.

IRC Section 401(k) Plan - All members of the Teachers' and State Employees' Retirement System and the Optional Retirement Program are eligible to enroll in the Supplemental Retirement Income Plan, a defined contribution plan, created under Internal Revenue Code Section 401(k). All costs of administering the Plan are the responsibility of the Plan participants. No costs are incurred by the University except for a 5% employer contribution for the University's law enforcement officers, which is mandated under General Statute 143-166.30(e). Total employer contributions on behalf of University law enforcement officers for the year ended June 30, 2007, were \$54,772.85. The voluntary contributions by employees amounted to \$403,010.00 for the year ended June 30, 2007.

IRC Section 403(b) and 403(b)(7) Plans - Eligible University employees can participate in tax sheltered annuity plans created under Internal Revenue Code Sections 403(b) and 403(b)(7). The employee's eligible contributions, made through salary reduction agreements, are exempt from federal and State income taxes until the annuity is received or the

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 \$1,495,047.57 for the year ended June 30, 2007.

NOTE 13 - OTHER POSTEMPLOYMENT BENEFITS

- A. Health Care for Long-Term Disability Beneficiaries and Retirees -** The University participates in State-administered programs that provide postemployment health insurance to eligible former employees. Eligible former employees include long-term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers' and State Employees' Retirement System or the Optional Retirement Program. These benefits were established by Chapter 135, Article 3, Part 3, of the General Statutes and may be amended only by the North Carolina General Assembly. Funding for the health care benefit for long-term disability beneficiaries and retirees is financed on a pay-as-you-go basis. The University contributed 3.8% of the covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program for these health care benefits. For the fiscal year ended June 30, 2007, the University's total contribution to the Plan was \$3,433,784.42. The University assumes no liability for retiree health care benefits provided by the programs other than its required contribution. Additional detailed information about these programs can be located in the State of North Carolina's *Comprehensive Annual Financial Report*.
- B. Disability Income -** The University participates in the Disability Income Plan of North Carolina (DIPNC). Established by Chapter 135, Article 6, of the General Statutes, DIPNC provides short-term and long-term disability benefits to eligible members of the Teachers' and State Employees' Retirement System and the Optional Retirement Program. Long-term disability income benefits are advance funded on an actuarially determined basis using the one-year term cost method. The University contributes .52% of covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the DIPNC. For the year ended June 30, 2007, the University's total contribution to the DIPNC was \$469,886.29. 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*.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 14 - RISK MANAGEMENT

The University is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These exposures to loss are handled via a combination of methods, including participation in State-administered insurance programs, purchase of commercial insurance, and self-retention of certain risks. There have been no significant reductions in insurance coverage from the previous year and settled claims have not exceeded coverage in any of the past three fiscal years. Tort claims of up to \$500,000 are self-insured under the authority of the State Tort Claims Act. In addition, the State provides excess public officers' and employees' liability insurance up to \$5,000,000 via contract with a private insurance company. The University pays the premium, based on a composite rate, directly to the private insurer.

The University is required to maintain fire and lightning coverage on all State-owned buildings and contents through the State Property Fire Insurance Fund (Fund), an internal service fund of the State. Such coverage is provided at no cost to the University for operations supported by the State's General Fund. Other operations not supported by the State's General Fund are charged for the coverage. Losses covered by the Fund are subject to a \$500 per occurrence deductible. All State-owned vehicles are covered by liability insurance through a private insurance company and handled by the North Carolina Department of Insurance. The liability limits for losses occurring in-State are \$500,000 per claim and \$5,000,000 per occurrence and out-of-State are \$1,000,000 per claim and \$5,000,000 per occurrence. The University pays premiums to the North Carolina Department of Insurance for the coverage.

The University is protected for losses from employee dishonesty and computer fraud. This coverage is with a private insurance company and is handled by the North Carolina Department of Insurance. Universities are charged a premium by the private insurance company. Coverage limit is \$5,000,000 per occurrence with a \$75,000 deductible and a 10% participation in each loss above the deductible. University employees and retirees are provided comprehensive major medical care benefits. Coverage is funded by contributions to the State Health Plan (Plan), a pension and other employee benefit trust fund of the State of North Carolina. The Plan has contracted with third parties to process claims.

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

NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)

and compensation in accordance with the North Carolina Workers' Compensation Act. The University is self-insured for workers' compensation.

Term life insurance (death benefits) of \$25,000 to \$50,000 is provided to eligible workers. This Death Benefit Plan is administered by the State Treasurer and funded via employer contributions. The employer contribution rate was .16% for the current fiscal year.

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

NOTE 15 - 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 \$10,866,545.42 and on other purchases were \$6,199,234.75 at June 30, 2007.
- B. Pending Litigation and Claims** - The University is a party to litigation and claims in the ordinary course of its operations. Since it is not possible to predict the ultimate outcome of these matters, no provision for any liability has been made in the financial statements. University management is of the opinion that the liability, if any, for any of these matters will not have a material adverse effect on the financial position of the University.
- C. Other Contingent Receivables** - The University has received notification of other gifts and grants for which funds have not been disbursed by the resource provider and for which conditions attached to the gift or grant have not been satisfied or, in the case of permanent endowments, cannot begin to be satisfied. In accordance with accounting principles generally accepted in the United States of America, these amounts have not been recorded on the accompanying financial statements. The purpose and amount of other contingent receivables at year end is as follows:

Purpose	Amount
Pledge to Endowed Scholarships	\$ 274,000.00



STATE OF NORTH CAROLINA
Office of the State Auditor

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

2 S. Salisbury Street
20601 Mail Service Center
Raleigh, NC 27699-0601
Telephone: (919) 807-7500
Fax: (919) 807-7647
Internet
<http://www.ncauditor.net>

**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
North Carolina Agricultural and Technical State University
Greensboro, North Carolina

We have audited the financial statements of North Carolina Agricultural and Technical 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, 2007, which collectively comprise the University's basic financial statements and have issued our report thereon dated April 22, 2008. Our report was modified to include a reference to other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Other auditors audited the financial statements of The North Carolina A&T University Foundation, Inc., as described in our report on the University's financial statements. The financial statements of The North Carolina A&T University Foundation, Inc., 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.

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

**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)**

weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the University’s ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the University’s financial statements that is more than inconsequential will not be prevented or detected by the University’s internal control. We consider the all deficiencies described in findings 1 thru 9 and 13 in the Audit Findings and Responses section of this report to be significant deficiencies in internal control over financial reporting.

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that none of the significant deficiencies described above is a material weakness.

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 instances of noncompliance or other matters which are required to be reported under *Government Auditing Standards* and are described in finding number 9 in the Audit Findings and Responses section of this report.

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

This report is intended solely for the information and use of management of the University,

**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 Board of Governors, the Board of Trustees, the Audit Committee, the Governor, the General Assembly, and the State Controller, and is not intended to be and should not be used by anyone other than these specified parties.

Leslie W. Merritt, Jr.

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

April 22, 2008

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AUDIT FINDINGS AND RESPONSES

Matters Related to Financial Reporting or Federal Compliance Objectives

The following findings and recommendations were identified during the current audit and discuss conditions that represent deficiencies in internal control and/or noncompliance with laws, regulations, contracts or grants. Finding number 8 was also reported in the prior audit.

1. QUESTIONABLE SCHOLARSHIP AWARDS

We noted a number of questionable scholarship awards and deficiencies in documentation supporting awards. Most of the questionable awards were made to relatives of University employees.

Bookstore Scholarship Fund

Relatives of University employees appear to have received a disproportionate share of financial aid paid from the Bookstore Scholarship Fund. As a result, students with greater need may have gone without assistance.

We examined 13 of the 47 awards made during 2006-07 from the University Bookstore Scholarship Fund. This examination covered \$18,466 of the \$42,435 paid from the fund during the year. We determined that three of the 13 awards examined, totaling \$5,300, were given to relatives of employees working in the office of a Vice Chancellor.

There was no formal policy defining eligibility requirements or the awarding process for the University Bookstore Scholarship Fund. A draft policy stated that the University Treasurer's Office was to make the award and the above-mentioned Vice Chancellor was to approve the awards. Treasurer's Office personnel stated that the scholarship was to assist students with significant financial need.

We determined that none of the 13 awards examined were approved by the Vice Chancellor. According to the students' files, two of employees' relatives who received the scholarships did not have financial need that was not met by other funding sources, and the documentation for the other employee's relative did not clearly demonstrate need. Furthermore, the forms authorizing awards totaling \$4,300 for one of the recipients could not be located. This award was the largest bookstore scholarship given in the 2006-07 year.

In addition to the awards made to employees' relatives, we also noted that two awards were made to a student solely at the direction of a University administrative official. These two awards totaled \$6,092.

The three awards made to employees' relatives combined with those selected by

AUDIT FINDINGS AND RESPONSES (CONTINUED)

University administrative officials accounted for 27% of the total scholarships awarded for the year from the Bookstore Scholarship Fund. Our discussions with personnel in the Treasurer's Office and Financial Aid Office revealed that if these administrative officials or other such persons of authority requested an award be made, it would not be questioned.

Other Scholarships Awarded to Employees' Children

We examined other scholarships paid to employees' relatives and noted that one was awarded a \$5,000 scholarship when the average award for this type of scholarship was only \$1,528. The award for the Spring semester was authorized solely with the Financial Aid Director's signature stamp. Since the Director of Enrollment Services approved the Fall Award, employees may have assumed it was appropriate to continue the award in the Spring. This student also received a \$1,500 scholarship award for which the authorization could not be located.

Authorization was also not located for a \$600 Chancellor's Scholarship awarded to the relative of an employee in an administrative office or for a \$1,500 UNC Campus Scholarship awarded to the relative of an Associate Vice Chancellor. We examined a total of 81 awards to relatives of employees over the past two years. The University was unable to locate authorizations for 25 (31%) of these awards

Recommendation: All scholarship funds should have written eligibility, application and processing procedures. All awards should be properly authorized and documentation maintained by the authorizing department and the Financial Aid Office. To maintain segregation of duties, the office that disburses financial aid should not award financial aid. Therefore, the responsibility for awarding bookstore scholarships should be removed from the Treasurer's office. Scholarships having an element of need should be administered by the Financial Aid Office since that is where documentation of financial need resides. Employees should not be allowed to award scholarships to themselves or immediate family members.

Response:

Bookstore Scholarship Fund

We concur with the recommendations that the disbursement of Bookstore Scholarships (i.e., posting awards to the student accounts) should be coordinated with the Financial Aid Office, that award documentation should be consistently maintained in the financial aid office, and that criteria for the scholarship should be developed. While the greatest number of scholarships awarded from this fund, generally ranging from \$500 to \$1,000, is for the purchase of books and supplies, emergency awards also come from this fund. The Bookstore Scholarship Fund is not intended to be a need based award, and the disbursement of these funds did not result in an over award of financial aid. A further review of this matter has led us to believe that the \$4,300 award mentioned in the above finding may have been erroneously charged to this fund rather than to the University scholarship funds responsible for the student's support.

AUDIT FINDINGS AND RESPONSES (CONTINUED)

Other Scholarships Awarded to Employees' Children

The Financial Aid Director has retrieved all signature stamps. Staff members must indicate their signature on the scholarship award forms. A review will be performed each semester to ensure that all scholarship award forms are in place and the award corresponds with the financial aid system.

The Student Financial Aid Office is developing criteria and procedures for scholarships without written documentation. All scholarship award forms must be properly authorized before the award is keyed in the financial aid system. All forms will be keyed and authorized by personnel in the Scholarship area.

2. DEFICIENCIES IN MANAGEMENT OF STUDENT ACCOUNTS

The University made errors in the way it managed students' accounts. As a result, accounts receivable were overstated, accounts were not collected, and invalid disbursements were made.

We examined a sample of 59 student accounts receivable balances at June 30, 2007, and noted the following issues:

- a. Thirteen accounts were overstated by \$24,967. One reason for the overstatement was failure to reduce charges for housing and meal plans when students withdrew. Apparently, the University's Treasurer's Office did not consistently receive notice when students withdrew or stopped attending the University. In some cases, the University even paid the meal plan vendor for a student who withdrew or stopped attending. Another reason for the overstatement was charges to students participating in a partnership program whereby students who pay for classes at the student's home university can attend classes at another university without additional charges.
- b. Eleven accounts had outstanding balances of \$39,296 because the University erroneously posted student financial aid awards to the students' accounts and then later had to cancel the award. Financial aid was awarded to the students at the beginning of Fall semester 2006 based on preliminary data supplied to the Financial Aid Office. Later these financial aid awards were cancelled when the student failed to submit requested documentation to the Financial Aid Office or was determined to be otherwise ineligible for aid. The students did not pay the costs directly and were not dropped from classes. Financial aid should not be posted to a student account until eligibility has been determined. A student is not eligible to receive financial aid until they have met all documentation requirements.
- c. One student's account was credited with a scholarship because the Summer School office erroneously sent a document to the Treasurer's Office stating that a

AUDIT FINDINGS AND RESPONSES (CONTINUED)

department would pay the bill for the student. After the credit was posted, the scholarship was cancelled and collection from the student was not pursued.

- d. The University used a student's Fall 2006 financial aid to pay off a prior year debt owed by the student. The prior year debt was created when the University erroneously issued PLUS loan payments to both the student and the parent and did not pursue reimbursement. Current year financial aid awards should only be used to satisfy current year charges.
- e. A student that was not enrolled for classes in Spring 2007 had financial aid posted to their account and received a \$6,501 student aid disbursement. The student had preregistered for the Spring in a graduate program and was awarded financial aid. After reviewing grades for Fall 2006, the graduate school academically dismissed the student, but charges for the Spring were not taken off until after financial aid was posted and a disbursement generated.
- f. There were other instances where student accounts had significant balances due to lack of controls over registration and payment of student accounts. Residency status was changed in the Graduate School without supporting documentation. Two students were allowed to register without making payment or having pending financial aid. Two students defaulted on tuition payment plans. Four students added classes or housing and meal charges for which they did not have pending financial aid. These students did not pay for the additional charges. One student made payment with an insufficient funds check and the student's classes were not dropped for the non-payment.

Recommendation: The University should strengthen internal controls over student accounts to ensure that accounts receivable balances are valid, amounts owed are collected, and all disbursements are appropriate. Communication between all areas that affect student accounts should be enhanced so that timely and appropriate changes to accounts can occur.

Response: We concur with the recommendations. The University will perform a detailed analysis of all student receivable accounts. Additionally, the following processes have been and/or are being implemented to enhance controls over the University's 11,000 student accounts:

- a. The Office of Housing & Residence Life has requested a program from our Information Technology staff that will purge housing assignments for non-enrolled students. The current process requires Housing & Residence Life staff to manually perform this process.

Also, the Treasurer's Office and the Registrar's Office will perform a second-level review of consortium student registrations to ensure that they are properly coded, which should prevent the erroneous assessment of charges.

- b. The Student Financial Aid Office has developed procedures to ensure that files are reviewed correctly before an award is made. The Counseling staff has attended in-

AUDIT FINDINGS AND RESPONSES (CONTINUED)

house training on verification. Final review of the files will still occur for 100% accuracy. Procedures will be reviewed to determine appropriate changes in processes.

- c. Scholarship notifications will only be acknowledged if posted in Banner by the Student Financial Aid Office. Students will no longer be validated from documents sent to the Treasurer's Office from internal departments.

3. UNALLOWABLE COSTS PAID FROM STATE APPROPRIATIONS

The University charged costs to state funds that are not allowable under State Budget Manual rules. We identified a total of \$99,458 in unallowable costs.

At year end, the University's Office of Budget and Planning reallocates costs initially charged to overhead receipts accounts to state funds. This prevents excess state appropriations from reverting back to the State. The charges are not reviewed to ensure that they are allowable costs as defined by the State Budget Manual.

For the year ended June 30, 2007, a total of \$3,436,700 was reallocated from overhead receipts to state funds. We examined 102 of the reallocated charges, totaling \$259,492, and determined that \$68,714 was unallowable. The expenditures in question included purchases for theater tickets, flowers, coffee services, catering, housing scholarships, awards/plaques, and travel expenses for a marching band retreat.

We also noted that \$12,178 of travel and contracted services expenditures for the band were paid without typical departmental approval or documentation required by University policy. The band director initially asked budget personnel in Auxiliary Services to approve the travel, which is standard practice. When the travel authorization was denied based on a lack of funds, the band director paid for the trip using a University credit card and then sought and received retroactive approval from the Office of Budget and Planning Director. The Office of Budget and Planning Director initiated an agreement for services on behalf of the band director. There was no documentation to define the duties required in the agreement and the Office of Budget and Planning Director provided the sole approval.

We also examined \$200,350 of expenditures charged to food service accounts for items other than student meal plans. We identified \$30,744 of these expenditures that were not allowed to be paid with state funds according to the State Budget Manual. Unallowable charges included catering, refreshments, and other food related items. Of the \$30,744 identified as unallowable, \$16,165 was for food provided to students at various events. The University had misinterpreted State budget policy and operated under the assumption that if students comprised more than 50% of the attendees at any given event, then State funds could be used to pay for food, refreshments or catering.

Recommendation: The University should strengthen internal control to ensure that charges to state funds are allowable and that University policy is followed.

AUDIT FINDINGS AND RESPONSES (CONTINUED)

Response: We concur with the finding. Our current practice at year end is to move appropriate charges from overhead to state funds if funding is available. We moved transactions associated with the account code. In the future we will review expenditures at the transactional level. This will ensure that each transaction is appropriate for transfer to state funds.

For the band travel, this was an obligation of the University. Three offices met and reviewed the transaction before approval was granted for payment. In the future we will ensure that appropriate procedures are followed so as not to put the University in the position of approving an after-the-fact transaction. We will communicate with all departments that if prior approval has not been granted, the transaction should not take place. We have identified funding to create an administrative support associate position for the University Band Office. The position will be created effective July 1, 2008. This position will be responsible for handling the paperwork from the Band and the Office of Budget and Planning will not have to initiate paperwork on their behalf.

In April 2007, the Division of Business and Finance realized that we were operating under an incorrect assumption relative to the use of state funding for payment of food and catering items when there was demonstrated student participation. After reviewing the information with OSBM, we amended our policy to reflect the appropriate regulation. We communicated the new and revised policy to the entire campus, updated the web information and created a desk reference for administrative staff across the University. The final policy was updated and implemented effective May 2007.

4. INAPPROPRIATE TRAVEL REIMBURSEMENTS PAID

During our audit, we found two instances where travel costs were paid without proper approvals and supporting documentation and 12 instances where employees were paid excessive mileage reimbursements. Questionable charges totaled \$4,769.

When examining expenditures charged to the discretionary account of a Vice Chancellor, we identified two travel expenditures that were not properly approved. One was approved by a subordinate of the Vice Chancellor rather than a designee in the Chancellor's office, which was standard practice. One reimbursement request was signed on behalf of the Chancellor by an undetermined party. The travel assistant did not recognize the initials. Reimbursements for the hotel accommodations were supported by an online confirmation rather than a hotel receipt, and justification for the trips was not documented. Further, the hotel costs of \$329 and \$259 per night appear to be unreasonable compared to the price of other available hotels in the area. The total paid for the two trips was \$4,019, including airfare.

We examined a sample 23 travel expenditures charged to federal grants and found two instances where excessive mileage was approved and reimbursed. Since both excessive mileage amounts were approved by the same supervisor, we examined an additional ten transactions approved by the supervisor. We determined that all ten had excessive

AUDIT FINDINGS AND RESPONSES (CONTINUED)

mileage charges. The supervisor stated that he realized the travel was excessive, but that these employees chose to drive an unusual route. University travel expenditures are reviewed by a travel accountant who stated that mileage is verified through an online mapping service. Mileage for each of the trips examined was in excess of the mileage shown on the mapping service by at least 110 miles, but the mileage reimbursement request was not returned to the department for further review.

Recommendation: all travel expenditures should be made in compliance with university travel policy. All travel expenditures should be authorized in advance and approved by the employee's supervisor. Justification for reimbursement that exceeds state approved subsistence rates should be documented.

Response: We concur that all travel expenditures should be properly authorized and reviewed. The management oversight of the travel accountants has been transferred from the Purchasing Department to the Accounts Payable Department. The travel staff will receive additional training in which we will stress the importance of reviewing travel expenditures for advance approvals in accordance with the University travel policy. The Accounting Office will adhere strictly to the current procedure of requiring justification for reimbursement that exceeds state approved subsistence rates. Additionally, all travel related to senior administrative staff is being reviewed and approved by the Chancellor.

The instance related to excess mileage reimbursement was isolated to three individuals. The department in question has been notified of these instances and a memorandum has subsequently been issued reemphasizing the travel reimbursement policy. Our review of travel expenditures indicates that the instance related to improper travel approval and justification may be isolated in nature. The review of travel reimbursements for proper approval and documentation has been reemphasized to the travel accounting staff.

5. DEFICIENCIES IN FINANCIAL REPORTING

The financial statements and notes to the financial statements prepared by the University had numerous misstatements and could have been misleading to readers without our audit adjustments. Misstatements noted in our audit included:

Current Unrestricted Cash was overstated \$6,419,486 and Restricted Cash and Cash Equivalents was understated by the same amount. The University did not record the effect of interfund borrowing of unrestricted cash to cover deficit balances in restricted funds.

Student Tuition and Fees Revenue and Insurance and Bonding Expense were overstated by \$2,448,010. The University acts as an agent for student health insurance, and thus, the funds billed, collected and remitted to the insurance company are not revenue or expense to the University. In addition, Student Tuition and Fees were overstated \$54,475 when the administrative fee received from the insurance company was recorded as Student Tuition and Fees instead of Other Operating Revenue.

AUDIT FINDINGS AND RESPONSES (CONTINUED)

- a. The Net Assets Restricted for Expendable Debt Service disclosed a deficit balance of \$84,937. For proper financial reporting a reclassification should have been made from Unrestricted Net Assets to eliminate the deficit.
- b. Several of the notes to the financial statements were incomplete or contained errors.

Management is responsible for the fair presentation of its financial statements and notes in accordance with accounting principals generally accepted in the United States of America and the policies of the Office of the State Controller. To meet this responsibility, management must maintain internal controls over financial reporting to prevent or detect and correct material misstatements.

Recommendation: The University should implement effective internal controls to ensure the accuracy of the financial statements and related notes. The process for review of the financial statements and notes should be strengthened to ensure that misstatements and presentation errors are corrected prior to the submission of the statements and notes to the Office of the State Controller and the Office of the State Auditor.

Response: We concur with the recommendation. A financial statement review committee has been created to insure a more consistent and formal approach to the review of the financial statement exhibits and notes. With the implementation of new audit reporting standards, the University understands the importance of submitting comprehensive financial statements and footnote disclosures for audit review.

6. INTERNAL CONTROLS OVER PURCHASING CIRCUMVENTED

University employees circumvented established internal controls over purchasing by using a purchase order line item normally reserved for incidental charges such as shipping and handling to buy additional items. As a result, there was an increased risk of error or fraud.

The University uses automated purchase orders, and the system has built-in procurement controls to identify transactions requiring price quotes or change orders. However, the automated form has a nondescript line normally used for incidental charges associated with the purchase that can be used to avoid the controls.

We determined that the total amount paid through the additional line on purchase orders during the fiscal year was \$78,959. We examined 16 of the transactions with a total dollar value of \$22,527, and we identified 11 instances totaling \$18,927 where charges other than shipping and handling were added. Change orders would have been required on 10 of these transactions, and in one instance, price quotes would have been required.

AUDIT FINDINGS AND RESPONSES (CONTINUED)

Recommendation: The University should place controls over the use of the additional line on the purchase order to prevent unauthorized purchases. University policies and procedures should be followed regarding obtaining price quotes and change orders.

Response: We concur. This was a training issue with the implementation of Banner accounts payable. We have put policies in place that require that the additional line field would be used only for charges such as freight, shipping & handling. All other additional charges would be handled in accordance with purchasing guidelines. The accounts payable staff has received additional training in this area.

7. STUDENTS NOT BILLED FOR COST OF MEDICAL INSURANCE

The University made medical insurance payments on behalf of students without charging the students for the costs. As a result, the University incurred \$46,945 in costs that should have been reimbursed by students.

The University purchases group medical insurance for students who need coverage and charges the cost of premiums to the students' accounts. However, internal control was not in place to ensure that the total amount paid to the insurance company was in fact charged to students. We determined that 205 students were not billed for their medical insurance premiums.

Recommendation: Internal controls, such as a reconciliation of insurance payments to student charges, should be established to ensure that total insurance payments made are billed to students.

Response: We concur. A system report has been written to identify students who are eligible to receive health insurance and a reconciliation process has been developed. A project team is currently exploring ways to make this a more efficient process.

8. DEFICIENCIES IN ACCOUNTING FOR GRANTS

The accounting records for federal and state grants indicate that the University does not adequately account for individual program activities. As a result, expenditures may be charged for unallowable activities, cash in excess of need may be drawn, and/or the University may fail to request funds earned.

The University had 189 federal and state grant accounts with no activity during the fiscal year ended June 30, 2007, which may indicate that the grants were closed. There were 69 inactive accounts with deficit cash balances totaling \$241,227, and the remaining 120 accounts had total positive cash balances of \$711,115. The deficit balances may indicate that the University used other funds for grant purposes, while the excess positive balances may indicate that excess cash was drawn down from the funding agency. On the other hand, the balances could have resulted from accounting errors.

AUDIT FINDINGS AND RESPONSES (CONTINUED)

The accounting records are designed to ensure that various funding sources are used in accordance with grant restrictions and those revenues are drawn down to support allowable charges. Failure to maintain accurate records on a timely basis increases the risk of errors or fraud.

Recommendation: The University should evaluate its accounting procedures for grant funds and make changes to ensure that receipts are properly applied and that over-expenditures are prevented.

Response: We concur. The accounting procedures for grant funds are currently being evaluated to ensure timely billing, reconciliation of expenditures, receipts and receivables. The University continues to review and analyze remaining cash balances related to closed grants.

9. FAILURE TO RETURN UNEARNED STUDENT FINANCIAL AID FUNDS

The University did not compute or return unearned student financial aid funds to the federal government in accordance with program regulations. When students withdraw, unofficially withdraw, or drop courses, the University is required to compute the amount of unearned student financial aid credited to the students' accounts for tuition and fees and return it to the federal government. Regulations require that the calculation be done within 30 days of the end of the payment period or semester for students who unofficially withdraw, that is, simply stop attending class. Unearned funds are required to be returned to the federal government no later than 45 days after the date that it is determined the student had withdrawn.

The University computed unearned revenue of \$8,512 for the Fall 2006 semester related to unofficial withdrawals; however, the calculation was not done until January 2008, eight months after the end of the academic year. Unearned revenue of \$87,771 related to unofficial withdrawals for the Spring 2007 semester was calculated in July 2007, two months after the end of the academic year. The Fall 2006 amounts were finally paid back to the federal government in March 2008, while the Spring 2007 amounts were paid back July 17, 2007.

In addition to noncompliance with federal regulations, the University also failed to report a liability in the financial statements for the amount owed.

Recommendation: The University should establish policies and procedures to comply with federal regulations regarding the timely identification of unofficial withdrawals and the return of unearned funds.

Response: We concur that the University should adhere to established policies and procedures for all withdrawals. The students mentioned above were all unofficial withdrawals. Additional procedures are being developed to facilitate compliance.

AUDIT FINDINGS AND RESPONSES (CONTINUED)

10. LACK OF CONTROLS OVER FEDERAL DEBARMENT VERIFICATION

The University did not have controls in place to ensure that covered transactions (contracts and procurements in excess of \$25,000 and subawards) were made only to vendors or subrecipients that were eligible to participate in federal programs. The lack of controls increase the risk that the University may contract with, or provide funds to, suspended or debarred parties.

Title 2 CFR sections 180.220 and 180.300 require verification for covered transactions to ensure that the recipients of federal funds are not suspended or debarred. This verification may be accomplished by checking the Excluded Parties List System maintained by the General Services Administration, collecting a certification from the entity, or adding a clause or condition to the covered transaction with that entity.

Recommendation: The University should establish and implement procedures to ensure compliance with federal suspension and debarment regulations.

Response: The control procedure under which the University operates requires the Sponsored Programs Office to review the Federal Debarment List to assure that any potential subcontractor has not been debarred. Additionally, the University Purchasing Office reviews the State of North Carolina Debarment List before issuing purchase orders for procurements. However, we concur that having the Purchasing Office review both the Federal and State list provides stronger assurance that the University is in compliance with federal suspension and debarment regulations. Consequently, the Purchasing Office has now implemented that procedure.

11. NONCOMPLIANCE WITH PERSONNEL TIME AND EFFORT DOCUMENTATION

The University did not consistently maintain documentation to support payroll charges to Research and Development grants. As a result, there is an increased risk of unallowable costs being charged to the grants.

Auditors reviewed nineteen payroll transactions charged to Research and Development grants to determine if the cost was allowable. The University had failed to maintain documentation required by federal cost principles (OMB Circular A-21, J.10) to support personnel charges to federal programs in six of these transactions. Auditors also reviewed eight Research and Development grants with matching requirements. In two of these grants, the University failed to maintain records to support the personnel charges for the required match. The University subsequently obtained after-the-fact time and effort certifications; therefore, no costs are questioned.

Recommendation: We recommend the University strengthen internal controls to ensure compliance with federal cost principles and with its policy concerning time and effort reporting.

AUDIT FINDINGS AND RESPONSES (CONTINUED)

Response: We concur with this finding. As previously noted, the time and effort certifications were subsequently obtained. During the 2007 fiscal year, the University implemented new time and effort reporting policies and procedures. We are continuing to review and strengthen the process to ensure full compliance with cost principles.

12. LACK OF MONITORING GRANT ACTIVITY

The University does not have sufficient internal controls in place to monitor transactions initiated and approved by principal investigators. As a result, there is an increased risk that unallowable transactions may occur without detection.

The A-102 Common Rule and OMB Circular A-110 (2 CFR part 215) require that non-Federal entities receiving Federal awards establish and maintain internal control designed to reasonably ensure compliance with Federal laws, regulations, and program compliance requirements. In a decentralized environment with many people authorizing transactions, having strong monitoring controls is imperative. The University does not have a person with specific knowledge of the grant requirements independently monitoring transactions authorized by principal investigators. Principal investigators may also be responsible for receiving their own procurements, which increases the risk of fraud.

Recommendation: The University should enhance internal controls to include an independent monitoring effort over costs charged to grants.

Response: The University recognizes that strong internal controls are essential to detecting and preventing unallowable transactions. We agree that our current controls may not be at an optimum level. Our plans to enhance controls include the following:

- A position is being established in Contracts and Grants dedicated to training and compliance issues.
- The Contracts and Grants staff is increasing their reviewing and monitoring processes to ensure compliance.
- As resources become available, the University will install departmental research administrators in major research departments to independently monitor transactions authorized by principal investigators.
- The Sponsored Programs and Contracts and Grants Offices are conducting training sessions with principal investigators and administrative staff to review federal allowable cost directives.

AUDIT FINDINGS AND RESPONSES (CONCLUDED)

13. DEFICIENCIES IDENTIFIED BY UNIVERSITY OFFICE OF INTERNAL AUDIT

The University discovered and the Office of Internal Audit (OIA) investigated two situations that resulted in findings relevant to our audit objectives:

- a. The OIA investigated two allegations of possible conflicts of interest involving faculty members. The OIA determined that there were conflicts present for two College of Engineering faculty members. One faculty member who was the principal investigator on five grants was also a principal owner of the vendor paid \$184,000 to perform the grant work. The professor's relationship with the vendor was disclosed on the annual conflict of interest disclosure, but the department chairperson took no action to mitigate the risk of a conflict on interest.
- b. The OIA investigated misuse of a University procurement card that was issued to the Principal Investigator (PI) of a grant. The OIA concluded that lack of management review and oversight allowed the PI to use the procurement card to purchase items for personal use and to purchase items not authorized by the grant. The University Purchasing Department failed to suspend the card when the required monthly reconciliation was not turned in by the PI. There was at least \$20,000 in personal purchases for which the PI has been charged with embezzlement. The PI also failed to perform work necessary to produce results required by the grant or failed to document the work performed.

Recommendation: The University should initiate actions considered necessary to resolve and eliminate the conflict of interest between faculty members employment with the University and any outside business interests. Appropriate University personnel should review conflict of interest disclosures, identify potential conflicts of interest, and take action to mitigate the University's associated risk. Supervisory personnel should review and approve subordinates work periodically to ensure adherence to University policies and procedures. All procurement cards should be placed on suspension when cardholder's reconciliations are not received by the due date.

Response: We concur with the recommendations. The University has taken actions to resolve conflict of interest issues with the faculty member. Additionally, the University is currently reviewing and revising the conflict of interest policy.

The University has enhanced controls over procurement card transactions. The management of the procurement card processor has been transferred to the accounts payable department. Additionally, a confirmation process has been implemented requiring a response from the bank to the University validating all card suspensions and cancellations.

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