Tennessee Board of Regents
Tennessee State University

For the Year Ended
June 30, 2002

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FINANCIAL AND COMPLIANCE

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Comptroller of the Treasury, Division of State Audit
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Financial/compliance audits of colleges and universities are available on-line at www.comptroller.state.tn.us/sa/reports/index.html.
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STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY

State Capitol
Nashville, Tennessee 37243-0260
(615) 741-2501

John G. Morgan
Comptroller

March 27, 2003

The Honorable Phil Bredesen, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and
The Honorable Charles W. Manning, Chancellor
Tennessee Board of Regents
1415 Murfreesboro Road, Suite 350
Nashville, Tennessee 37217
and
Dr. James A. Hefner, President
Tennessee State University
3500 John A. Merritt Boulevard
Nashville, Tennessee 37209

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Tennessee Board of Regents, Tennessee State University, for the year ended June 30, 2002. You will note from the independent auditor's report that an unqualified opinion was given on the fairness of the presentation of the financial statements.

Consideration of internal control over financial reporting and tests of compliance disclosed certain deficiencies, which are detailed in the Results of the Audit section of this report. The university's administration has responded to the audit finding; the response is included following the finding. The Division of State Audit will follow up the audit to examine the application of the procedures instituted because of the audit finding.

Sincerely,

John G. Morgan
Comptroller of the Treasury

JGM/cj
02/107

State of Tennessee

Audit Highlights

Comptroller of the Treasury — Division of State Audit

Financial and Compliance Audit
Tennessee State University
For the Year Ended June 30, 2002

AUDIT OBJECTIVES

The objectives of the audit were to consider the university's internal control over financial reporting; to determine compliance with certain provisions of laws, regulations, contracts, and grants; to determine the fairness of the presentation of the financial statements; and to recommend appropriate actions to correct any deficiencies.

COMPLIANCE FINDING

The University Did Not Report Pell Payment Data to the Department of Education (ED) Within the Required Time Frame
For 18 of 20 students whose Pell Payment Data was tested (90%), the university did not report Pell Payment Data to ED within 30 days of disbursement to students. A disbursement record should be submitted no later than 30 days after the disbursment is made (page 7).

OPINION ON THE FINANCIAL STATEMENTS

The opinion on the financial statements is unqualified.

"Audit Highlights" is a summary of the audit report. To obtain the complete audit report, which contains all findings, recommendations, and management comments, please contact

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Audit Report
Tennessee Board of Regents
Tennessee State University
For the Year Ended June 30, 2002

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Tennessee Board of Regents
Tennessee State University
For the Year Ended June 30, 2002

INTRODUCTION

POST-AUDIT AUTHORITY

This is a report on the financial and compliance audit of the Tennessee Board of Regents, Tennessee State University. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which authorizes the Department of Audit to "perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller."

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

BACKGROUND

Tennessee State University was first established as the Agricultural and Industrial State Normal School on June 19, 1912, through an act of the Tennessee General Assembly. In 1922, the institution was raised to the status of a four-year teachers' college and was empowered to grant the bachelor's degree. In August 1951, the State Board of Education granted the institution university status. The university was elevated to a land-grant university by the State Board of Education in August 1958. The land-grant university program established a School of Agriculture and Home Economics, School of Engineering, School of Arts and Sciences, School of Education, Graduate School, Division of Business, Division of Extension and Continuing Education, and Department of Aerospace Studies. The university is supported by state and federal funds, the latter in accordance with the Morrill Act and other federal acts that provide for land-grant institutions.

ORGANIZATION

The governance of Tennessee State University is vested in the Tennessee Board of Regents. The Governor, the Commissioner of Education, the Commissioner of Agriculture, and the Director of the Tennessee Higher Education Commission serve *ex officio* on this board. The chief administrative officer of the university is the president, who is assisted and advised by members of the faculty and administrative staff.

AUDIT SCOPE

The audit was limited to the period July 1, 2001, through June 30, 2002, and was conducted 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. Financial statements are presented for the year ended June 30, 2002. Tennessee State University is an institution of the Tennessee Board of Regents, which is an integral part of state government. As such, the Tennessee Board of Regents has been included as a component unit in the *Tennessee Comprehensive Annual Financial Report.*

OBJECTIVES OF THE AUDIT

The objectives of the audit were

1. to consider the university's internal control over financial reporting to determine auditing procedures for the purpose of expressing an opinion on the financial statements;
2. to determine compliance with certain provisions of laws, regulations, contracts, and grants;
3. to determine the fairness of the presentation of the financial statements; and
4. to recommend appropriate actions to correct any deficiencies.

Although this audit was not intended to serve as an organization-wide audit as described in the Single Audit Act, as amended by the Single Audit Act Amendments of 1996, and Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, it included tests of compliance with applicable federal laws and regulations and consideration of internal control used in administering federal financial assistance programs. This audit is a segment of the organization-wide audit of the State of Tennessee, which is conducted in accordance with the Single Audit Act.

PRIOR AUDIT FINDINGS

Section 8-4-109, *Tennessee Code Annotated*, requires that each state department, agency, or institution report to the Comptroller of the Treasury the action taken to implement the recommendations in the prior audit report. The university filed its report with the Department of Audit on July 17, 2002. A follow-up of the prior audit finding was conducted as part of the current audit.

RESOLVED AUDIT FINDING

The current audit disclosed that the university has corrected the previous audit finding concerning appropriate controls over cash payments and ticket sales.

RESULTS OF THE AUDIT

AUDIT CONCLUSIONS

Internal Control

As part of the audit of the university's financial statements for the year ended June 30, 2002, we considered internal control over financial reporting to determine auditing procedures for the purpose of expressing an opinion on the financial statements, as required by 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. A reportable condition, along with the recommendation and management's response, is detailed in the finding and recommendation. Consideration of internal control over financial reporting disclosed no material weaknesses.

Compliance

The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*. Immaterial instances of noncompliance, along with the recommendation and management's response, are included in the finding and recommendation.

Fairness of Financial Statement Presentation

The Division of State Audit has rendered an unqualified opinion on the university's financial statements.

STATE OF TENNESSEE
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Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*

November 21, 2002

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

We have audited the financial statements of Tennessee State University, an institution of the Tennessee Board of Regents, which is a component unit of the State of Tennessee, as of and for the year ended June 30, 2002, and have issued our report thereon dated November 21, 2002. 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. As discussed in Note 11, the university implemented GASB Statement 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments,* and GASB Statement 35, *Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities*. The university also implemented GASB Statement 37, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments: Omnibus*, and GASB Statement 38, *Certain Financial Statement Note Disclosures*.

Compliance

As part of obtaining reasonable assurance about whether the university's financial statements are free of material misstatement, we performed tests of the university's compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

We did, however, note certain immaterial instances of noncompliance that we have included in the Finding and Recommendation section of this report. We also noted certain other less significant instances of noncompliance, which we have reported to the university's management in a separate letter.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the university's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the university's ability to record, process, summarize, and report financial data consistent with management's assertions in the financial statements.

The following reportable condition was noted:

- The university did not report Pell Payment Data to the Department of Education within the required time frame.

This condition is described in the Finding and Recommendation section of this report.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we do not believe the reportable condition described above is a material weakness.

We also noted other matters involving the internal control over financial reporting, which we have reported to the university's management in a separate letter.

This report is intended solely for the information and use of the General Assembly of the State of Tennessee and management and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record.

Sincerely,

Arthur A. Hayes, Jr., CPA,
Director

AAH/cj

FINDING AND RECOMMENDATION

The university did not report Pell Payment Data to the Department of Education within the required time frame

Finding

The university did not report Pell Payment Data to the federal government as required. Pell Payment Data is the term used to refer to the electronic or magnetic payment record used to report to the U.S. Department of Education (ED) the Pell payments to students. The record contains various information about each student, including enrollment status and disbursement information. Chapter 3 of the Pell portion of the *Student Financial Aid Handbook* specifies the reporting deadline as follows:

> A disbursement record should be submitted no later than 30 days after the disbursement is made. A school must submit a disbursement record within 30 days of the date the school becomes aware of a Pell change (for example, a new recipient, or an increased award). Schools may do this by reporting once every 30 calendar days (or more frequently), or may set up their own system to ensure that changes are reported in a timely manner.
>
> If a school doesn't report any data for a period of 30 or more calendar days, the Department will consider that the school had no data to report for that period, and any actions (such as changes in authorization levels) will be based only on the data reported up to that time. The 30-day reporting requirement ensures that Federal funds won't remain at a school when its students don't need the funds. Schools that don't submit required records or submit them on time, and schools that submit incomplete records will have their Pell allocations reduced and may be fined.

For 18 of 20 students whose Pell Payment Data was tested (90%), the university did not report Pell Payment Data to ED within 30 days of disbursement to students. Discussions with the Financial Aid Director revealed that the university reported Pell Payment Data past the 30-day deadline due to incorrect information loading from the Student Information System. A program was created, by the Financial Aid Technical Manager and Computer Information Technology staff, that was to be run once. The program automatically updated existing student information into the Student Information System fields needed to report the Pell Payment Data to ED, and from that point, new student information was updated manually. After the information had been updated manually, the program was unintentionally run again replacing the manually updated information. The financial aid counselors had to reenter information that had been changed by the program and manually update any new information. Because of the high volume of students visiting the office during the time period, it was difficult to update the information on a consistent and regular basis. The latest Pell Payment tested was reported 66 days late.

Recommendation

The Financial Aid staff should monitor Pell reporting more closely and report Pell Payment Data within the time frame required. Computer programs should be tested, and updated information should be reviewed for accuracy. Controls should be implemented to ensure computer programs are run only when necessary. Policies and procedures should be reviewed to ensure that proper reporting requirements have been established.

Management's Comment

We concur with the finding and recommendation. A computer program had been developed to improve a manual process. However, the program had a flaw which was not discovered until after the reporting deadline. The program has been corrected, and all data was subsequently reported. In the future, the timely and accurate running of the program and submission of the Pell Payment Data will be closely monitored by the Student Financial Aid Director.

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Independent Auditor's Report

November 21, 2002

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

We have audited the accompanying statement of net assets of Tennessee State University, an institution of the Tennessee Board of Regents, which is a component unit of the State of Tennessee, as of June 30, 2002, and the related statements of revenues, expenses, and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the university's management. Our responsibility is to express an opinion on these financial statements, based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Tennessee Board of Regents, Tennessee State University, as of June 30, 2002, and the revenues, expenses, and changes in net assets and the cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 11, the university implemented GASB Statement 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, and GASB Statement 35, *Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities*. The university also implemented GASB Statement 37, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments: Omnibus*, and GASB Statement 38, *Certain Financial Statement Note Disclosures*.

The management's discussion and analysis on pages 11 through 17 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 21, 2002, on our consideration of the university's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Sincerely,

Arthur A. Hayes, Jr.

Arthur A. Hayes, Jr., CPA,
Director

AAH/cj

TENNESSEE STATE UNIVERSITY
Management's Discussion and Analysis

This section of Tennessee State University's annual financial report presents a discussion and analysis of the financial performance of the university during the fiscal year ended June 30, 2002. This discussion has been prepared by management along with the financial statements and related note disclosures and should be read in conjunction with the financial statements and notes. The financial statements, notes, and this discussion are the responsibility of management.

Since this is a transition year for the new financial reporting format required by the Governmental Accounting Standards Board's Statements No. 34, "Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments" and No. 35, "Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities," only one year of information is presented in the financial statements and this discussion. Comparative information will be presented in future years.

Using This Annual Report

This report consists of three basic financial statements. The Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; and the Statement of Cash Flows provide information on Tennessee State University as a whole and present a long-term view of the university's finances.

The Statement of Net Assets

The Statement of Net Assets presents the financial position of the university at the end of the fiscal year and includes all assets and liabilities of the university. The difference between total assets and total liabilities—net assets—is an indicator of the current financial condition of the university. Assets and liabilities are generally measured using current values. One notable exception is capital assets, which are stated at historical cost less an allowance for depreciation.

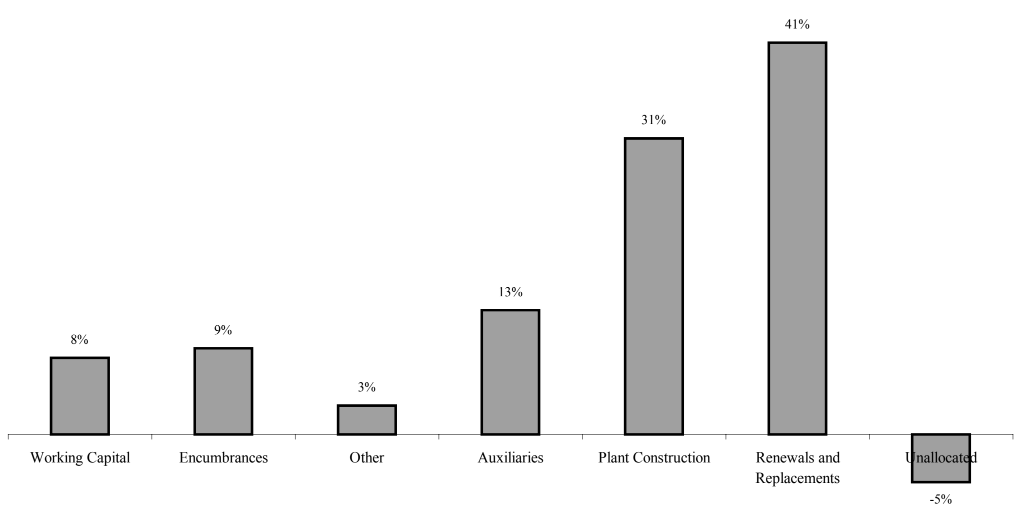
Net assets are divided into three major categories. The first category, invested in capital assets, net of related debt, provides the university's equity in property, plant, and equipment owned by the university. The next asset category is restricted net assets, which is divided into two categories, nonexpendable and expendable. The corpus of nonexpendable restricted resources is only available for investment purposes. Expendable restricted net assets are available for expenditure by the university but must be spent for purposes as determined by donors and/or external entities that have placed time or purpose restrictions on the use of the assets. The final category is unrestricted net assets. Unrestricted net assets are available to the institution for any lawful purpose of the institution.

Statement of Net Assets (in thousands of dollars)

	2002
Assets:	
Current assets	32,627
Capital assets, net	150,775
Other assets	21,748
Total assets	**205,150**
Liabilities:	
Current liabilities	20,843
Noncurrent liabilities	28,347
Total liabilities	**49,190**
Net assets:	
Invested in capital assets, net of related debt	123,908
Restricted – nonexpendable	62
Restricted – expendable	7,697
Unrestricted	24,293
Total net assets	**155,960**

Many of the university's unrestricted net assets have been designated or reserved for specific purposes such as: repairs and replacement of equipment, auxiliary services, encumbrances, and capital projects. The following graph shows the allocations:

UNRESTRICTED NET ASSETS



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

The Statement of Revenues, Expenses, and Changes in Net Assets presents the operating results of the university, as well as the nonoperating revenues and expenses. Annual state appropriations, while budgeted for operations, are considered nonoperating revenues according to generally accepted accounting principles.

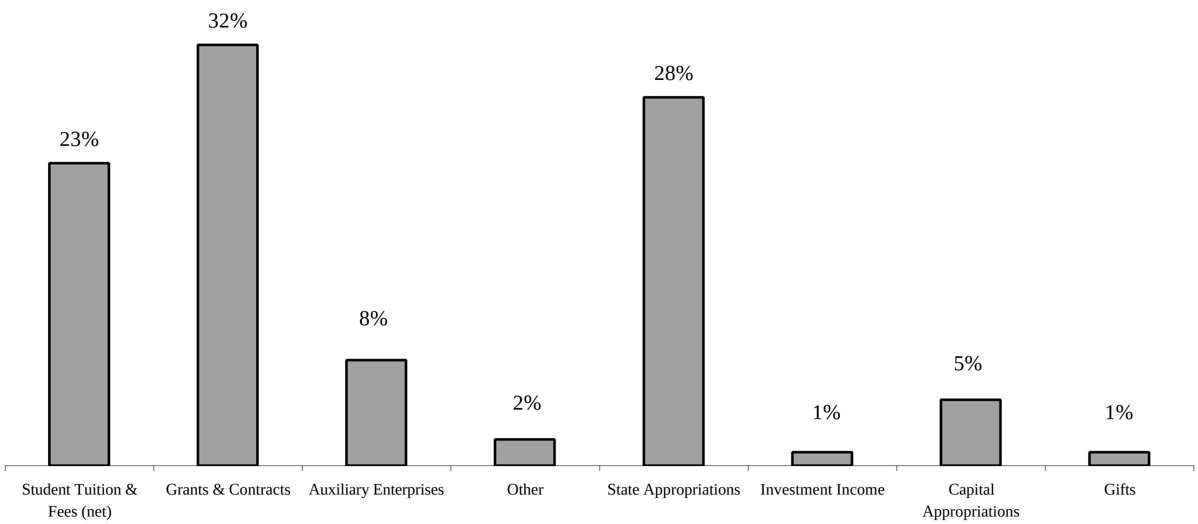
Statement of Revenues, Expenses, and Changes in Net Assets (in thousands of dollars)

	2002
Operating revenues:	
Net tuition and fees	31,318
Grants and contracts	44,555
Auxiliary	11,022
Other	2,105
Total operating revenues	**89,000**
Operating expenses	129,674
Operating loss	**(40,674)**
Nonoperating revenues and expenses:	
State appropriations	38,530
Gifts	1,528
Investment income	1,048
Other revenues and expenses	(30,602)
Total nonoperating revenues and expenses	**10,504**
Loss before other revenues, expenses, gains, or losses	**(30,170)**
Other revenues, expenses, gains, or losses:	
Capital appropriations	6,810
Capital grants and gifts	5
Total other revenues, expenses, gains, or losses	**6,815**
Decrease in net assets	**(23,355)**
Net assets at beginning of year, as originally reported	263,656
Cumulative effect of changes in accounting principle	(84,341)
Net assets at beginning of year, as restated	**179,315**
Net assets at end of year	**155,960**

Revenues

The following is a graphic illustration of revenues by source (both operating and nonoperating), which are used to fund the university's operating activities for the year ended June 30, 2002.

Revenues by Source



- The university received 23% of its funding from student fees and 28% from state appropriations.

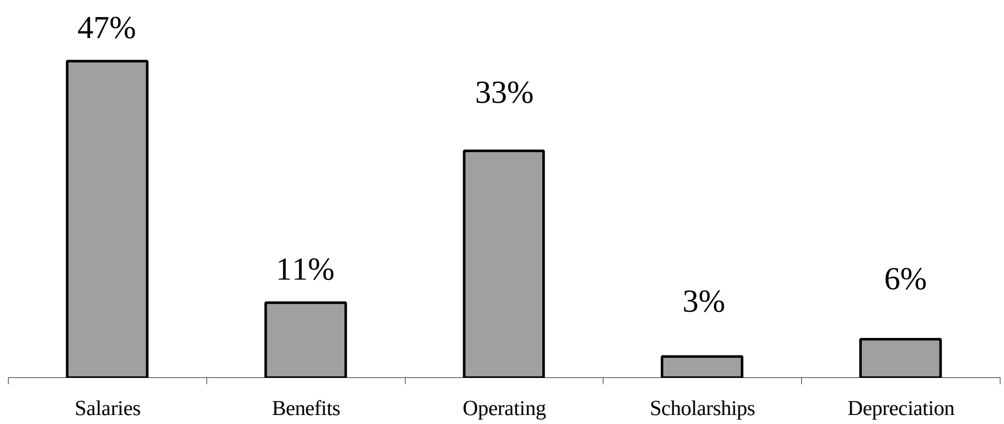
Expenses

Operating expenses can be displayed in two formats, natural classification and program classification. Both formats are displayed below (in thousands of dollars).

Natural Classification

Salaries	60,546
Benefits	14,367
Operating	43,378
Scholarships	4,068
Depreciation	7,316
Total	**129,675**

Expenses by Natural Classification

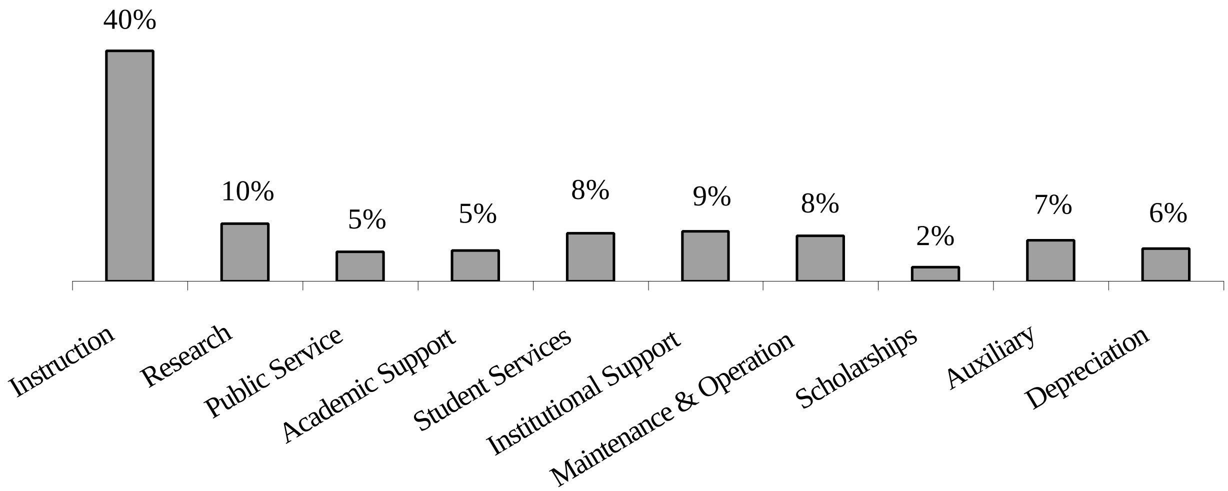


- Fifty-eight percent (58%) of expenses for the university were in salaries and benefits.
- The university employs 1,139 full-time employees: 57 Administrators, 336 Faculty, 367 Professional Support, and 379 Clerical Support.
- Operating expenses included $4.084 million in Utilities, $11.515 million in Professional & Administrative Services, and $7.896 million in Operating Supplies.

Program Classification

Instruction	50,995
Research	12,945
Public service	6,693
Academic support	6,926
Student services	10,811
Institutional support	11,254
Maintenance & operations	10,273
Scholarships	3,172
Auxiliary	9,290
Depreciation	7,316
Total	**129,675**

Expenses by Program Classification



- Sixty percent (60%) of university expenses were in the academic functions (instruction, research, public service, and academic support).

The Statement of Cash Flows

The Statement of Cash Flows provides information about cash receipts and cash payments during the year. This statement also assists users in assessing the university's ability to generate net cash flows, its ability to meet its obligations as they come due, and its need for external financing.

Statement of Cash Flows (in thousands of dollars)

	2002
Cash provided (used) by:	
Operating activities	(35,359)
Noncapital financing activities	40,088
Capital and related financing activities	(3,932)
Investing activities	998
Net increase in cash	**1,795**
Cash, beginning of year	**33,853**
Cash, end of year	**35,648**

- The university's cash and cash equivalents increased approximately $1.8 million from the prior fiscal year.

Capital Assets and Debt Administration

Capital Assets

At June 30, 2002, the university had $150,774,757.73 invested in capital assets, net of accumulated depreciation of $90,722,355.24. Depreciation charges totaled $7,315,610.09 for the current fiscal year. Details of these assets are shown below.

Schedule of Capital Assets, Net of Depreciation (in thousands of dollars)

	2002
Land	9,525
Land improvements & infrastructure	17,927
Buildings	90,004
Equipment	5,124
Library holdings	2,984
Projects in progress	25,211
Total	**150,775**

More detailed information about the university's capital assets is presented in Note 6 to the financial statements.

Debt

At June 30, 2002, the university had $26,866,431.60 in debt outstanding. This debt is in bonds issued through the Tennessee State School Bond Authority (TSSBA). The TSSBA issued $7,309,830.94 in AA-rated bonds for the construction of new student apartments and the north campus project. More detailed information about the university's long-term liabilities is presented in Note 7 to the financial statements.

Economic Factors That Will Affect the Future

The Tennessee Board of Regents approved a 7.5% fee increase for the 2002-03 academic year. The increase in fees has resulted in the cost for students to attend the university exceeding the amount of financial aid available per student. This requires students to result to alternative means of financing the cost of attending the university. The impact this will have on enrollment is unknown. The university's appropriation from the state did not increase from the prior fiscal year. The university does not anticipate any significant increases in state funding. The university is not aware of any other factors that will have a significant effect on the financial position or results of operations.

Exhibit A

TENNESSEE STATE UNIVERSITY
STATEMENT OF NET ASSETS
JUNE 30, 2002

ASSETS		
Current assets:		
Cash and cash equivalents (Notes 2 and 3)	$	17,306,864.04
Short-term investments (Notes 3 and 4)		3,095,490.80
Accounts, notes, and grants receivable (net) (Note 5)		10,824,890.67
Inventories (at lower of cost or market)		39,134.05
Accrued interest receivable		1,331,920.19
Other assets		29,227.00
Total current assets		32,627,526.75
Noncurrent assets:		
Cash and cash equivalents (Notes 2 and 3)		18,272,811.93
Investments (Notes 3 and 4)		1,656,844.30
Accounts, notes, and grants receivable (net) (Note 5)		1,749,622.45
LGIP deposit - capital projects (Note 2)		68,777.82
Capital assets (net) (Note 6)		150,774,757.73
Total noncurrent assets		172,522,814.23
Total assets		205,150,340.98
LIABILITIES		
Current liabilities:		
Accounts payable		1,770,567.30
Accrued liabilities		6,236,161.63
Due to grantors (Note 7)		101,950.26
Student deposits		754,802.91
Deferred revenue		1,955,363.39
Compensated absences (Note 7)		1,681,819.31
Accrued interest payable		284,901.87
Long-term liabilities, current portion (Note 7)		3,103,348.36
Deposits held in custody for others		4,459,411.06
Other liabilities		495,285.50
Total current liabilities		20,843,611.59
Noncurrent liabilities:		
Compensated absences (Note 7)		2,148,925.06
Long-term liabilities (Note 7)		23,763,083.24
Due to grantors (Note 7)		2,434,975.79
Total noncurrent liabilities		28,346,984.09
Total liabilities		49,190,595.68
NET ASSETS		
Invested in capital assets, net of related debt		123,908,326.13
Restricted for:		
Nonexpendable:		
Scholarships and fellowships		61,452.07
Expendable:		
Scholarships and fellowships		42,694.53
Research		719,596.75
Instructional department uses		3,697,326.03
Loans		845,812.03
Other		2,391,530.75
Unrestricted (Note 8)		24,293,007.01
Total net assets	$	155,959,745.30

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

Exhibit B

TENNESSEE STATE UNIVERSITY
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
FOR THE YEAR ENDED JUNE 30, 2002

REVENUES		
Operating revenues:		
Student tuition and fees (net of scholarship allowances of $11,704,997.54)	$	31,317,880.46
Governmental grants and contracts		44,554,780.70
Sales and services of educational departments		1,756,175.56
Auxiliary enterprises:		
Residential life (net of scholarship allowances of $1,155,565.72; all residential life revenues are used as security for revenue bonds; see Note 7)		6,500,444.01
Bookstore		275,700.75
Food service		3,768,308.22
Other auxiliaries		477,790.34
Other operating revenues		349,088.23
Total operating revenues		89,000,168.27
EXPENSES		
Operating expenses (Note 15):		
Salaries and wages		60,546,310.19
Benefits		14,366,937.43
Utilities, supplies, and other services		43,378,030.92
Scholarships and fellowships		4,067,722.98
Depreciation expense		7,315,610.09
Total operating expenses		129,674,611.61
Operating loss		(40,674,443.34)
NONOPERATING REVENUES (EXPENSES)		
State appropriations		38,530,600.00
Gifts		1,527,936.22
Investment income (net of investment expense of $163,128.03)		1,047,610.79
Interest on capital asset-related debt		(1,123,726.08)
Bond issuance costs		(99,080.90)
Other nonoperating revenues (expenses)		(29,379,586.57)
Net nonoperating revenues		10,503,753.46
Loss before other revenues, expenses, gains, or losses		(30,170,689.88)
Capital appropriations		6,810,708.71
Capital grants and gifts		5,000.00
Total other revenues		6,815,708.71
Decrease in net assets		(23,354,981.17)
NET ASSETS		
Net assets - beginning of year, as originally reported		263,655,537.74
Cumulative effects of changes in accounting principle (Note 11)		
Adoption of capitalization criteria for buildings and additions		(3,855,409.31)
Adoption of depreciation for capital assets		(79,551,335.84)
Deferred revenue recognition		1,337,781.64
Other		(2,271,847.76)
Net assets - beginning of year, as restated		179,314,726.47
Net assets - end of year	$	155,959,745.30

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

Exhibit C

TENNESSEE STATE UNIVERSITY
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2002

CASH FLOWS FROM OPERATING ACTIVITIES		
Tuition and fees	$	31,962,274.63
Grants and contracts		41,301,606.70
Sales and services of educational activities		1,807,000.58
Payments to suppliers and vendors		(43,569,342.11)
Payments to employees		(59,982,659.83)
Payments for benefits		(14,276,769.37)
Payments for scholarships and fellowships		(4,067,722.98)
Loans issued to students and employees		(626,564.75)
Collection of loans from students and employees		613,807.16
Interest earned on loans to students		122,732.59
Auxiliary enterprise charges:		
Residence halls		6,475,805.28
Bookstore		275,700.75
Food services		3,768,308.22
Other auxiliaries		487,896.80
Other receipts (payments)		349,088.23
Net cash used by operating activities		(35,358,838.10)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State appropriations		38,103,800.00
Gifts and grants received for other than capital or endowment purposes		1,554,186.22
Federal student loan receipts		28,497,461.00
Federal student loan disbursements		(29,967,757.00)
Changes in deposits held for others		1,760,524.90
Other noncapital financing receipts (payments)		139,773.71
Net cash provided by noncapital financing activities		40,087,988.83
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from capital debt		7,309,830.94
Capital - state appropriations		6,774,196.28
Purchases of capital assets and construction		(15,290,550.70)
Principal paid on capital debt and lease		(1,487,230.28)
Interest paid on capital debt and lease		(1,081,905.30)
Bond issue costs paid on new debt issue		(99,080.90)
Other capital and related financing receipts (payments)		(57,485.34)
Net cash used by capital and related financing activities		(3,932,225.30)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments		2,559,153.84
Income on investments		776,734.59
Purchases of investments		(2,337,486.97)
Net cash provided by investing activities		998,401.46
Net increase in cash and cash equivalents		1,795,326.89
Cash and cash equivalents - beginning of year		33,853,126.90
Cash and cash equivalents - end of year	$	35,648,453.79

TENNESSEE STATE UNIVERSITY
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2002

Reconciliation of operating loss to net cash used by operating activities:		
Operating loss	$	(40,674,443.34)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation expense		7,315,610.09
Change in assets and liabilities:		
Receivables, net		3,646,549.93
Inventories		1,109.88
Accounts payable		(1,042,289.86)
Accrued liabilities		(351,624.94)
Deferred revenue		322,046.34
Deposits		117,088.71
Compensated absences		192,958.68
Loans to students and employees		(4,885,843.59)
Net cash used by operating activities	$	(35,358,838.10)

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

Tennessee Board of Regents
Tennessee State University
Notes to the Financial Statements
June 30, 2002

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The university is a part of the State University and Community College System of Tennessee (Tennessee Board of Regents). This system is a component unit of the State of Tennessee because the state appoints a majority of the system's governing body and provides financial support; the system is discretely presented in the *Tennessee Comprehensive Annual Financial Report*.

Basis of Presentation

The financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). In June 1999, the GASB issued Statement 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*. This was followed in November 1999 by GASB Statement 35, *Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities*. The financial presentation required by those statements provides a comprehensive, entity-wide perspective of the university's assets, liabilities, net assets, revenues, expenses, changes in net assets, and cash flows, and replaces the fund-group perspective previously required.

Significant accounting changes made in order to comply with the new requirements include (1) adoption of depreciation on capital assets and (2) reporting summer school revenues and expenses between fiscal years rather than in one fiscal year.

Basis of Accounting

For financial statement purposes, the university is considered a special-purpose government engaged only in business-type activities. Accordingly, the financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. All significant interfund transactions have been eliminated.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. The university has the option of following private-sector guidance issued subsequent to November 30, 1989, subject to the above limitation. The university has elected not to follow private-sector guidance issued subsequent to November 30, 1989.

Amounts reported as operating revenues include (1) tuition and fees, net of waivers and discounts; (2) federal, state, local, and private grants and contracts; (3) sales and services of auxiliary enterprises; and (4) other sources of revenue. Operating expenses for the university include (1) salaries and wages; (2) employee benefits; (3) scholarships and fellowships; (4) depreciation; and (5) utilities, supplies, and other services.

All other activity is nonoperating in nature and includes (1) state appropriations for operations; (2) investment income; (3) bond issuance costs; (4) interest on capital asset-related debt; and (5) gifts.

When both restricted and unrestricted resources are available for use, generally it is the university's policy to use the restricted resources first.

LGIP Deposit – Capital Projects

Payments related to the university's capital projects are made by the State of Tennessee's Department of Finance and Administration. The university's estimated local share of the cost of each project is held in a separate Local Government Investment Pool (LGIP) account. As expenses are incurred, funds are withdrawn from the LGIP account by the Tennessee Board of Regents and transferred to the Department of Finance and Administration. The funds in the account are not available to the university for any other purpose until the project is completed and the Tennessee Board of Regents releases any remaining funds.

Inventories

Inventories are valued at the lower of cost or market on an average cost or first-in, first-out basis.

Compensated Absences

The university's employees accrue annual leave at varying rates, depending on length of service or classification. Some employees also earn compensatory time. The amount of these liabilities and their related benefits are reported in the statement of net assets.

Capital Assets

Capital assets, which include property, plant, equipment, and library holdings, are reported in the statement of net assets at historical cost or at fair value at date of donation, less accumulated depreciation. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend the asset's useful life are not capitalized.

A capitalization threshold of $100,000 is used for buildings, $50,000 for additions and improvements to land, buildings, or infrastructure, and $5,000 for equipment.

These assets, with the exception of land, are depreciated using the straight-line method over the estimated useful lives, which range from 5 to 40 years.

Tennessee State University Foundation

The university is the sole beneficiary of the Tennessee State University Foundation. A board independent of the university controls this private, nonprofit foundation. The university handles the financial records, investments, and other financial transactions, and the assets and liabilities of the foundation are included on the university's statement of net assets.

Net Assets

The university's net assets are classified as follows:

<u>Invested in capital assets, net of related debt</u> – 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.

<u>Nonexpendable restricted net assets</u> – Nonexpendable restricted net assets consist of endowment and similar type funds in which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may be expendable or added to principal.

Expendable restricted net assets – Expendable restricted net assets include resources which the university is legally or contractually obligated to spend in accordance with restrictions imposed by external third parties.

Unrestricted net assets – Unrestricted net assets represent resources derived from student tuition and fees, state appropriations, and sales and services of educational departments and auxiliary enterprises. These resources are used for transactions relating to the educational and general operations of the university, and may be used at the discretion of the university to meet current expenses for any purpose. The auxiliary enterprises are substantially self-supporting activities that provide services for students, faculty, and staff.

Scholarship Discounts and Allowances

Student tuition and fee revenues, and certain other revenues from students, are reported net of scholarship discounts and allowances in the statement of revenues, expenses, and changes in net assets. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by the university and the amount that is paid by the student and/or third parties making payments on the student's behalf. Certain governmental grants, such as Pell grants, and other federal, state, or nongovernmental programs, are recorded as either operating or nonoperating revenues in the university's financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees and other student charges, the university has recorded a scholarship discount and allowance.

Comparative Data

Comparative financial statements are not presented as the university implemented GASB Statements 34, 35, 37, and 38, and comparative statements are not required. Certain amounts presented in prior years' data have been reclassified to be consistent with the current year's presentation.

NOTE 2. CASH AND CASH EQUIVALENTS

In addition to demand deposits and petty cash on hand, this classification includes instruments which are readily convertible to known amounts of cash and which have original maturities of three months or less. At June 30, 2002, cash and cash equivalents consisted of $7,482,025.90 in bank accounts, $4,050.00 of petty cash on hand, $27,366,406.23 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer, and $727,193.84 in capital management account money funds.

For purposes of the statement of cash flows, the university considers the LGIP deposit - capital projects to be a part of cash and cash equivalents.

NOTE 3. DEPOSITS

Some of the university's deposits are in financial institutions that participate in the bank collateral pool administered by the State Treasurer. The securities pledged to protect these accounts are pledged in the aggregate rather than against each individual account. The members of the pool may be required by agreement to pay an assessment to cover any deficiency. Under this additional assessment agreement, public fund accounts covered by the pool are considered to be insured for purposes of credit risk disclosure.

At June 30, 2002, the carrying amount of the university's deposits in financial institutions participating in the collateral pool was $7,492,750.93, and the bank balance including accrued interest was $9,874,914.59. The bank balance was insured.

The laws of the State of Tennessee require that collateral be pledged to secure all uninsured deposits. Tennessee Board of Regents policies require that the market value of collateral pledged equal 115%, 100%, or 90% of the uninsured deposits at financial institutions participating in the collateral pool and 105% of the uninsured deposits at all other financial institutions. The pledge level for financial institutions participating in the collateral pool is based on financial criteria set by the Collateral Pool Board with the financially strongest institutions being eligible for the lowest pledge level.

Deposits with financial institutions are required to be categorized to indicate the level of risk assumed by the university. Category 1 consists of deposits that are insured or collateralized with securities held by the university or by its agent in the university's name. Category 2 consists of deposits collateralized with securities held by the pledging financial institution's trust department or agent in the university's name. Category 3 deposits are uncollateralized. This category includes any bank balance that is collateralized with securities held by the pledging financial institution or by its trust department or agent but not in the university's name.

At June 30, 2002, the carrying amount of the university's deposits was $7,818,526.71, and the bank balance including accrued interest was $10,204,209.41. Of the bank balance, $9,974,914.59 was category 1, and $229,294.82 was category 2.

The university also has deposits in the Local Government Investment Pool (LGIP) administered by the State Treasurer. The LGIP is part of the Pooled Investment Fund. The fund's investment policy and custodial credit risk are presented in the *Tennessee Comprehensive Annual Financial Report.* That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Eighth Avenue North, Nashville, Tennessee 37243-0298, or by calling (615) 741-2140.

NOTE 4. INVESTMENTS

The university is authorized by statute to invest funds in accordance with Tennessee Board of Regents policies. Under the current policy, funds other than endowments may be invested only in obligations of the United States or its agencies backed by the full faith and credit of the United States; repurchase agreements for United States securities; certificates of deposit in banks and savings and loan associations; bankers' acceptances; commercial paper; money market mutual funds; and the State of Tennessee Local Government Investment Pool. The policy requires that investments of endowments in equity securities be limited to funds from private gifts or other sources external to the university and that endowment investments be prudently diversified. The Tennessee State University Foundation is authorized to invest funds in accordance with its board of directors' policies.

All investments permitted to be reported at fair value under GASB Statement 31 are reported at fair value, including those with a maturity date of one year or less at the time of purchase. Certificates of deposit have been included with other deposits in Note 3 to determine the adequacy of collateral security pledged.

The university's/foundation's investments are categorized below to indicate the level of risk assumed by the university/foundation at year-end. Category 2 consists of uninsured and registered investments for which the securities are held by the counterparties' trust department or agent in the university's/foundation's name.

Category 2:	
University:	
U.S. government securities	$ 1,595,392.23
Foundation:	
Corporate bonds	1,167,414.64
Corporate stocks	513,898.75
U.S. government securities	350,699.80
Investments not susceptible to credit risk categorization:	
Mutual funds	788,428.87
Certificates of deposit classified as investments	336,500.81
Total investments on the statement of net assets	$4,752,335.10

NOTE 5. RECEIVABLES

Receivables at June 30, 2002, included the following:

Student accounts receivable	$ 2,830,721.25
Grants receivable	7,955,934.83
Notes receivable	464,645.23
Pledges receivable	78,000.00
Other receivables	1,066,474.35
Subtotal	12,395,775.66
Less allowance for doubtful accounts	1,539,695.92
Total receivables	$10,856,079.74

Pledges receivable are promises of private donations that are reported as accounts receivable and revenue. At June 30, 2002, all were considered to be collectible.

Federal Perkins Loan Program funds at June 30, 2002, included the following:

Perkins loans receivable	$14,392,326.34
Less allowance for doubtful accounts	12,673,892.96
Total	$ 1,718,433.38

NOTE 6. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2002, was as follows:

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$ 9,525,009.24	$ -	$ -	$ -	$ 9,525,009.24
Land improvements and infrastructure	47,803,341.91	-	(5,598,696.79)	2,983,778.87	39,220,866.25
Buildings	133,237,557.51	-	9,918,336.15	534,675.11	142,621,218.55
Equipment	18,957,890.16	1,393,871.45	-	953,388.91	19,398,372.70
Library holdings	28,854,587.00	1,278,134.49	-	24,612,338.70	5,520,382.79
Projects in progress	16,875,658.04	12,655,244.76	(4,319,639.36)	-	25,211,263.44
Total	255,254,043.86	15,327,250.70	-	29,084,181.59	241,497,112.97
Less accum. depreciation:					
Land improvements and infrastructure	19,670,520.05	1,623,322.11	-	-	21,293,842.16
Buildings	49,140,181.73	3,476,976.74	-	-	52,617,158.47
Equipment	13,377,487.45	1,610,235.93	-	713,383.58	14,274,339.80
Library holdings	1,931,939.50	605,075.31	-	-	2,537,014.81
Total accum. depreciation	84,120,128.73	7,315,610.09	-	713,383.58	90,722,355.24
			-		
Capital assets, net	$171,133,915.13	$8,011,640.61	$ -	$28,370,798.01	$150,774,757.73

NOTE 7. LONG-TERM LIABILITIES

Long-term liabilities activity for the year ended June 30, 2002, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Payables:					
Notes	$ 65,936.93	$ -	$ 65,936.93	$ -	$ -
Bonds	20,599,538.42	7,309,830.94	1,042,937.76	26,866,431.60	3,103,348.36
Commercial paper	378,355.59	-	378,355.59	-	-
Subtotal	21,043,830.94	7,309,830.94	1,487,230.28	26,866,431.60	3,103,348.36

Other liabilities:					
Compensated absences	3,637,785.69	1,874,777.99	1,681,819.31	3,830,744.37	1,681,819.31
Due to grantors	1,077,462.97	73,323,174.04	71,863,710.96	2,536,926.05	101,950.26
Subtotal	4,715,248.66	75,197,952.03	73,545,530.27	6,367,670.42	1,783,769.57
Total long-term liabilities	$ 25,759,079.60	$82,507,782.97	$75,032,760.55	$33,234,102.02	$4,887,117.93

Bonds Payable

Bond issues, with interest rates ranging from 4.00% to 6.90% for Tennessee State School Bond Authority bonds, are due serially to 2032 and are secured by pledges of the facilities' revenues to which they relate and certain other revenues and fees of the university, including state appropriations. The bonded indebtedness with the Tennessee State School Bond Authority reported on the statement of net assets is shown net of assets held by the authority in the debt service reserve and unexpended debt proceeds. The reserve amount was $996,680.00 at June 30, 2002, and unexpended debt proceeds were $7,012,054.86

Debt service requirements to maturity for bonds payable at June 30, 2002, are as follows:

Year Ending June 30	Principal	Interest	Total
2003	$ 1,407,996.05	$ 1,728,976.57	$ 3,136,972.62
2004	1,471,963.88	1,663,984.56	3,135,948.44
2005	1,451,878.55	1,619,755.19	3,071,633.74
2006	1,005,939.97	1,573,165.08	2,579,105.05
2007	1,062,254.62	1,523,337.04	2,585,591.66
2008-2012	6,154,919.19	6,874,204.40	13,029,123.59
2013-2017	3,804,274.90	4,832,581.27	8,636,856.17
2018-2022	4,901,361.92	3,012,622.05	7,913,983.97
2023-2027	5,164,931.47	1,723,716.47	6,888,647.94
2028-2032	440,911.05	494,730.62	935,641.67
	$26,866,431.60	$25,047,073.25	$51,913,504.85

NOTE 8. UNRESTRICTED NET ASSETS

Unrestricted net assets include funds that have been designated or reserved for specific purposes. These purposes include the following:

	Amount
Working capital	$ 1,966,587.25
Encumbrances	2,138,783.83
Auxiliaries	3,110,055.51
Plant construction	7,498,380.90
Renewal and replacement of equipment	9,920,888.88
Debt retirement	777,249.33
Total	$25,411,945.70

NOTE 9. PENSION PLANS

A. Defined Benefit Plans

1. Tennessee Consolidated Retirement System

Plan Description - The university contributes to the State Employees, Teachers, and Higher Education Employees Pension Plan (SETHEEPP), a cost-sharing, multiple-employer, defined benefit pension plan administered by the Tennessee Consolidated Retirement System (TCRS). TCRS provides retirement, death, and disability benefits as well as annual cost-of-living adjustments to plan members and their beneficiaries. Title 8, Chapters 34-37, *Tennessee Code Annotated*, establishes benefit provisions. State statutes are amended by the Tennessee General Assembly.

The TCRS issues a publicly available financial report that includes financial statements and required supplementary information for SETHEEPP. That report may be obtained by writing to the Tennessee Department of the Treasury, Consolidated Retirement System, 10th Floor Andrew Jackson Building, Nashville, Tennessee 37243-0230, or by calling (615) 741-8202.

Funding Policy - Plan members are noncontributory. The university is required to contribute an actuarially determined rate. The current rate is

6.19% of annual covered payroll. Contribution requirements for the university are established and may be amended by the TCRS' Board of Trustees. The university's contributions to TCRS for the years ended June 30, 2002, 2001, and 2000, were $1,543,054.62, $1,503,727.42, and $1,284,482.71. Contributions met the requirements for each year.

2. Federal Retirement Program

Plan Description - The university contributes to the Federal Retirement Program, a cost-sharing, multiple-employer, defined benefit pension plan administered by the Civil Service Retirement System (CSRS) for participants employed prior to January 1, 1984, and the Federal Employees Retirement System (FERS) for participants employed after December 31, 1983. Both systems provide retirement, death, and disability benefits as well as annual cost-of-living adjustments to plan members and their beneficiaries. All regular full-time employees of the Tennessee State University Agricultural Extension Service who hold federal appointments for 51% or more of their time are required to participate in either one of the two Federal Retirement Programs. For both systems, benefit provisions are established in federal statutes. Federal statutes are amended by the U.S. Congress. All the university's extension employees currently participate in CSRS.

The CSRS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to the Office of Personnel Management, Retirement Information Office, P. O. Box 45, Boyers, Pennsylvania 16017-0045, or by calling (202) 606-0500.

Funding Policy - Participating employees and the university are required to contribute to the CSRS plan. Contribution requirements are established and may be amended by federal statutes. The university is required to contribute 8.51% of covered payroll to the CSRS plan, and employees are required to contribute 7% of covered payroll. Contributions to CSRS for the year ended June 30, 2002, were $74,028.73, which consisted of $40,626.62 from the university and $33,402.11 from the employees. Contributions for the year ended June 30, 2001, were $73,143.65, which consisted of $39,657.62 from the university and $33,486.03 from the employees. Contributions for the year ended June 30, 2000, were $63,996.69, which consisted of $34,393.43

from the university and $29,603.26 from the employees. Contributions met the requirements for each year.

B. Defined Contribution Plans

Optional Retirement Plans (ORP)

Plan Description - The university contributes to three defined contribution plans: Teachers Insurance and Annuity Association–College Retirement Equities Fund (TIAA-CREF), Aetna Life Insurance and Annuity Company, and Variable Annuity Life Insurance Company (VALIC). These plans are administered by the Tennessee Department of the Treasury. Each plan provides retirement benefits to faculty and staff who are exempt from the overtime provisions of the Fair Labor Standards Act and who waive membership in the TCRS. Benefits depend solely on amounts contributed to the plan plus investment earnings. Plan provisions are established by state statute in Title 8, Chapter 35, Part 4, *Tennessee Code Annotated.* State statutes are amended by the Tennessee General Assembly.

Funding Policy - Plan members are noncontributory. The university contributes an amount equal to 10% of the employee’s base salary up to the social security wage base and 11% above the social security wage base. Contribution requirements are established and amended by state statute. The contribution made by the university to the plans was $2,825,202.04 for the year ended June 30, 2002, and $2,580,282.25 for the year ended June 30, 2001. Contributions met the requirements for each year.

NOTE 10. OTHER POST-EMPLOYMENT BENEFITS

The State of Tennessee administers a group health insurance program which provides post-employment health insurance benefits to eligible university retirees. This benefit is provided and administered by the State of Tennessee. The university assumes no liability for retiree health care programs. Information related to this plan is available at the statewide level in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee

Tower, 312 Eighth Avenue North, Nashville, Tennessee 37243-0298, or by calling (615) 741-2140.

NOTE 11. CUMULATIVE EFFECTS OF CHANGES IN ACCOUNTING PRINCIPLE

During the year ended June 30, 2002, the university implemented GASB Statement 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, and GASB Statement 35, *Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities*. As a result of this implementation, the university was required to make changes in certain accounting principles, specifically the (1) adoption of capitalization criteria of $100,000 and $50,000 for buildings and additions, respectively; (2) adoption of depreciation on capital assets; (3) recording of certain summer semester revenues between fiscal years rather than in the fiscal year in which the semester was predominantly conducted; and (4) reclassification of the U.S. government grants refundable amount as a liability. The cumulative effects of these changes on net assets are shown below:

Adoption of capitalization criteria for buildings and additions	$ (3,855,409.31)
Adoption of depreciation on capital assets	$(79,551,335.84)
Deferred revenue recognition	$ 1,337,781.64
Reclassification of U.S. government grants refundable	$ (2,271,847.76)

NOTE 12. INSURANCE-RELATED ACTIVITIES

The state purchases commercial insurance for real property losses above $5 million per year and surety bond coverage on the state's officials and employees. In the past three fiscal years, the state has not had any claims filed with the commercial insurer. Designations for casualty losses in the amount of $5 million for deductibles and $1.356 million for incurred losses at June 30, 2002, were established in the state's general fund to provide for any property losses not covered by the commercial insurance.

At June 30, 2002, the scheduled coverage for the university was $178,557,000 for buildings and $42,371,100 for contents.

The state has set aside assets for claim settlement in an internal service fund, the Claims Award Fund. This fund services all claims for risk of loss to which the state is exposed, including general liability, automobile liability, professional malpractice, and workers' compensation. The university participates in the Claims Award Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the university based on a percentage of the university's expected loss costs, which include both experience and exposures. This charge considers recent trends in actual claims experience of the state as a whole. An actuarial valuation is performed as of fiscal year-end to determine the fund liability and premium allocation. Since the university participates in the Claims Award Fund, it is subject to the liability limitations under the provisions of the Tennessee Claims Commission Act, *Tennessee Code Annotated*, Section 9-8-101 et seq. Liability for negligence of the university for bodily injury and property damage is limited to $300,000 per person and $1,000,000 per occurrence. The limits of liability under workers' compensation are set forth in *Tennessee Code Annotated*, Section 50-6-101 et seq. Claims are paid through the state's Claims Award Fund.

The state has also set aside assets in the Employee Group Insurance Fund, an internal service fund, to provide a program of health insurance coverage for the employees of the state with the risk retained by the state. The university participates in the Employee Group Insurance Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the university based on estimates of the ultimate cost of claims that have been reported but not settled and of claims that have been incurred but not reported. Employees and providers have 13 months to file medical claims.

NOTE 13. COMMITMENTS AND CONTINGENCIES

Sick Leave - The university records the cost of sick leave when paid. Generally, since sick leave (earned one day per month with unlimited accumulation) is paid only when an employee dies or is absent because of illness, injury, or related family death, there is no liability for sick leave at June 30. The dollar amount of unused sick leave was $25,924,004.47 at June 30, 2002.

Operating Leases - The university has entered into various operating leases for buildings and equipment. Such leases will probably continue to be required. Expenses under operating leases for real property were $437,703.17 and for personal property were $232,064.21 for the year ended June 30, 2002. All operating leases are cancelable at the lessee's option.

Construction in Progress - At June 30, 2002, outstanding commitments under construction contracts totaled $1,660,940.76 for the following projects: repair and upgrade of various buildings, Boyd Hall renovation, new Performing Arts Building, ADA improvements, utility systems and tunnel renovation, Agricultural I.T. Center, Power Plant Bag House replacement, and roof repair of several buildings, which will be funded by future state capital outlay appropriations.

Litigation - The university is involved in several lawsuits, none of which are expected to have a material effect on the accompanying financial statements.

NOTE 14. CHAIRS OF EXCELLENCE

The university had $2,609,998.95 on deposit at June 30, 2002, with the State Treasurer for the university's Chairs of Excellence program. These funds are held in trust by the state and are not included in the financial statements.

NOTE 15. NATURAL CLASSIFICATIONS WITH FUNCTIONAL CLASSIFICATIONS

The university's operating expenses by functional classification for the year ended June 30, 2002, are as follows:

	Natural Classification					
Functional Classification	Salaries	Benefits	Operating	Scholarships	Depreciation	Total
Instruction	$29,808,814.99	$6,629,679.62	$12,692,015.23	$1,864,063.97	$ -	$50,994,573.81
Research	5,854,375.76	1,268,484.61	4,760,590.22	1,061,863.75	-	12,945,314.34
Public service	3,748,850.57	1,063,187.92	1,663,483.99	217,421.29	-	6,692,943.77
Academic support	4,500,200.73	1,080,149.98	1,344,475.30	1,034.59	-	6,925,860.60
Student services	5,180,144.03	1,238,231.80	3,766,362.39	626,569.37	-	10,811,307.59
Institutional support	7,090,562.43	1,926,585.57	2,211,056.46	25,754.89	-	11,253,959.35
Operation & maint.	2,638,278.07	780,212.35	6,854,225.34	-	-	10,272,715.76
Scholar. & fellow.	12,267.17	(30,818.59)	3,083,109.66	107,544.23	-	3,172,102.47
Auxiliary	1,712,816.44	411,224.17	7,002,712.33	163,470.89	-	9,290,223.83
Depreciation	-	-	-	-	7,315,610.09	7,315,610.09
Total	$60,546,310.19	$14,366,937.43	$43,378,030.92	$4,067,722.98	$7,315,610.09	$129,674,611.61