Tennessee Board of Regents
Tennessee State University

For the Year Ended
June 30, 2003

Comptroller of the Treasury, Division of State Audit
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STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
State Capitol
Nashville, Tennessee 37243-0260
(615) 741-2501

John G. Morgan
Comptroller

April 8, 2004

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, 2003. 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 findings; the responses are included following each finding. The Division of State Audit will follow up the audit to examine the application of the procedures instituted because of the audit findings.

Sincerely,

John G. Morgan
Comptroller of the Treasury

JGM/th
04/014

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, 2003

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.

INTERNAL CONTROL FINDINGS

Foundation scholarship accounts were permitted to reach significant negative account balances, ultimately resulting in the foundation as a whole not having adequate resources to fund current operations

In accordance with the foundation's mission statement, scholarships are issued in the name of the foundation to students at the university. The university's President awarded the Foundation Honors Scholarships without input or review by the foundation board or foundation personnel. Over the past few years, foundation and university personnel did not adequately monitor the balances in the Foundation Honor scholarship account, the Academic scholarship account, and the Alumni Scholarship Drive account. As a result, scholarships were awarded to students without funds available in these accounts to cover the scholarships awarded. From June 30, 1998, through June 30, 2003, the overall negative balance in the scholarship accounts grew from ($197,792.50) to ($2,694,238.76). At June 30, 2003, the current cash and cash equivalents negative balance for the foundation as a whole was ($568,790.21) (page 7).

Not all foundation honors scholarship recipients tested were eligible for the aid received, and as a consequence, the foundation was not able to provide scholarships to students who met the criteria for scholarships
The Tennessee State University Foundation does not adequately monitor honors scholarship accounts to ensure that students meet the appropriate criteria. Based on the testwork performed related to foundation honors scholarships, some ineligible students received foundation honors scholarship funds and some students continued to receive foundation honors scholarship funds after they became ineligible. As a result, the foundation was not able to provide scholarships to students who met the criteria for scholarships (page 24).

The Tennessee State University Foundation does not have adequate procedures for recording and reconciling revenues and maintaining documentation
The Tennessee State University (TSU) Foundation does not have adequate procedures for recording and reconciling of revenues. In addition, foundation personnel (TSU employees) could not provide adequate documentation that all funds received had been appropriately deposited through the university Bursar's Office and had been correctly posted to the specified foundation accounts (page 26).

The university President exceeded his authority by improperly entering into an agreement with the Tennessee State University Foundation
The university President improperly entered into an agreement with the Tennessee State University Foundation in order to attempt to remedy negative scholarship account balances and negative current cash and cash equivalent amounts shown on the foundation's accounting records. (See the related finding on negative account balances.) This agreement was authorized by the university President without the approval of the Tennessee Board of Regents, which was in violation of the Board's guidelines (page 29).

The university has not implemented adequate controls over management of computer user accounts
Auditors observed that the university has not implemented adequate controls over management of computer user accounts. The university's policies require the protection of proprietary, personal, privileged, or otherwise sensitive data and resources that may be processed in any manner. Improvements are needed to comply with this policy. Failure to provide such controls increases the risk that unauthorized individuals could access sensitive university systems and information (page 30).

COMPLIANCE FINDING

The university did not submit correct data on the FISAP
The Financial Aid Office did not submit correct data to the U.S. Department of Education on the 2002-2003 Fiscal Operations Report and Application to Participate (FISAP) submitted on October 1, 2003, and the revised 2001-2002 FISAP submitted December 2002. The FISAP, which is for campus-based financial aid, consists of the Application for Participation for the upcoming award year and the Fiscal Operations Report for the previous award year. If the

Financial Aid Office submits incorrect and unverifiable data on the FISAP, the allocation of funds from the Department of Education could be affected (page 31).

OPINION ON THE FINANCIAL STATEMENTS

The opinion on the financial statements is unqualified.

Audit Report
Tennessee Board of Regents
Tennessee State University
For the Year Ended June 30, 2003

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For the Year Ended June 30, 2003

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, 2002, through June 30, 2003, 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, 2003, and for comparative purposes, 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 August 5, 2003. 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 the reporting of Pell Payment Data to the Department of Education within the required time frame.

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, 2003, 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. Reportable conditions, along with recommendations and management's responses, are detailed in the findings and recommendations. 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 recommendations and management's responses, are included in the findings and recommendations.

Fairness of Financial Statement Presentation

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

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT
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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 13, 2003

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, 2003, and have issued our report thereon dated November 13, 2003. 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.

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 Findings and Recommendations 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 conditions were noted:

- Foundation scholarship accounts were permitted to reach significant negative account balances, ultimately resulting in the foundation as a whole not having adequate resources to fund current operations

- Not all foundation honors scholarship recipients tested were eligible for the aid received, and as a consequence, the foundation incurred scholarship costs that could have been avoided if the eligibility criteria had been properly applied

- The Tennessee State University Foundation does not have adequate procedures for recording and reconciling revenues and maintaining documentation

- The university President exceeded his authority by improperly entering into an agreement with the Tennessee State University Foundation

- The university has not implemented adequate controls over management of computer user accounts

- The university did not submit correct data on the FISAP

These conditions are described in the Findings and Recommendations 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 believe none of the reportable conditions 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.

Arthur A. Hayes, Jr., CPA,
Director

AAH/th

FINDINGS AND RECOMMENDATIONS

1. Foundation scholarship accounts were permitted to reach significant negative account balances, ultimately resulting in the foundation as a whole not having adequate resources to fund current operations

Finding

In accordance with the foundation's mission statement, scholarships are issued in the name of the foundation to students at the university. The university's President awarded the Foundation Honors Scholarships without input or review by the foundation board or foundation personnel. Over the past few years, foundation and university personnel did not adequately monitor the balances in the Foundation Honor scholarship account, the Academic scholarship account, and the Alumni Scholarship Drive scholarship account. As a result, scholarships were awarded to students without funds available in these accounts to cover the scholarships awarded.

NEGATIVE SCHOLARSHIP ACCOUNT BALANCES

From June 30, 1998, through June 30, 2003, the overall negative balance in the scholarship accounts grew from ($197,792.50) to ($2,694,238.76), as shown in the following table:

	Academic Scholarship Account	Foundation Honor Scholarship Account	Alumni Scholarship Drive Scholarship Account	Total
June 30, 1998	(253,989.44)	-	56,196.94	(197,792.50)
June 30, 1999	(250,360.80)	(258,930.00)	42,391.92	(466,898.88)
June 30, 2000	(247,773.00)	(720,422.50)	70,235.31	(897,960.19)
June 30, 2001	(247,075.50)	(937,161.50)	32,335.80	(1,151,901.20)
June 30, 2002	(246,777.37)	(932,988.37)	(738,402.84)	(1,918,168.58)
June 30, 2003	(246,580.40)	(948,596.37)	(1,499,061.99)	(2,694,238.76)

At June 30, 2003, the current cash and cash equivalents negative balance for the foundation as a whole was ($568,790.21).

Although these scholarship accounts were already in a deficit status at the end of each fiscal year, the university's President continued to award scholarships. The following table, based on the foundation's accounting records, lists the number of scholarships disbursed for each account for each school year:

School Year	Foundation Honors Scholarships	Alumni Scholarship Drive Scholarships	Total Scholarships
1998 – 1999	73	31	104
1999 – 2000	96	14	110
2000 – 2001	105	35	140
2001 – 2002	-	127	127
2002 – 2003	4	120	124

No funds were disbursed to students from the Foundation Honor scholarship account during the 2001-2002 school year. However, many of the students funded under that account in the prior year received scholarships from the Alumni Scholarship Drive scholarship account in 2001-2002. During the periods listed in the table, no scholarships were awarded from the Academic scholarship account; there were small decreases in the negative balance from year to year because of undesignated revenue that was posted to the account with appropriate approval of foundation management.

FOUNDATION POLICIES, PROCEDURES, AND PRACTICES

Based on a review of the *Tennessee State University Foundation Policy and Procedures Manual*, the foundation does not have policies and procedures that address budgeting for the number of scholarships to be awarded or the source, amounts, and timing of funding for the scholarships. According to the foundation's current and former Executive Directors and chairs of the foundation's board, instead of first raising funds and then awarding scholarships from those funds, the foundation awards the scholarships in the fall, and then tries to raise enough money during the school year to fund the scholarships issued for that year. The funds raised have been inadequate to cover the scholarships awarded as reflected in the account balances noted above.

ROLE OF THE UNIVERSITY'S BUSINESS OFFICE

On July 27, 1989, the foundation entered into an agreement with the university which provided, in part, that the university was to ". . . Maintain the records and accounts of the Foundation in the Business Services area of the University and hold them separate as agency funds from the University's records and accounts." In accordance with the agreement, the university processes all of the foundation's transactions and provides monthly reports to the foundation's management.

During this entire period, the university's Business Office processed the foundation's transactions and prepared accounting records and reports for the foundation. However, the university's Business Office staff took limited action to control and specifically communicate the negative results of foundation operations to foundation personnel. Based on discussions with TSU's Director of Finance and Accounting and the Vice President for Business and Finance, the Business Office staff had concluded that they were only required to make entries in the foundation accounting records to effect transactions initiated by foundation staff and not to manage or control the account activity.

The Business Office only assumed control over the foundation's accounts when the total net current cash position of the foundation's restricted and unrestricted accounts became negative. At that point, Business Office personnel froze spending on all foundation accounts because any additional payments would have come from the university's funds. Business Office personnel stated that it was their opinion that controlling the foundation's negative accounts before obligations for foundation scholarships reached into university funds would have been usurping a foundation management role and would have violated the university's agreement with the foundation and the foundation's separate legal status as a Section 501(c)(3) nonprofit corporation. In this regard, the Business Office did not apply the same care and due diligence to foundation accounts as the Business Office applied to university accounts.

The Business Office staff did not specifically point out the negative account balances to foundation personnel and management. Although this was not an explicit requirement under the terms of the agreement between the university and the foundation, a reasonable practice would have included clear and explicit notification to foundation staff and management of its negative account balances and the university's need to restrict processing of additional payments unless the foundation's board of trustees and/or management approved expenses to negative accounts. At that point, if foundation management continued to approve charges to negative accounts, Business Office staff should have communicated with the university President regarding the situation and should have reevaluated the university's relationship with the foundation and its role as the foundation's bookkeeper.

ROLE OF THE FOUNDATION STAFF

Although foundation staff, who are employees of the university, had adequate information to know the negative status of the scholarship accounts, apparently they failed to comprehend the nature and consequences of these developments. The Business Office provided the foundation staff access to (a) review foundation accounts in an electronic format on the computer in the foundation office, which would have clearly shown negative balances in the scholarship accounts; (b) review the detail of individual accounts through a printed monthly transaction listing, which would also have clearly shown negative balances in the scholarship accounts; and (c) review the foundation's annual financial statements, which would not have shown deficits in the scholarship accounts because of the summary nature of the financial statements. In addition to the information provided in the university's Financial Records System, the foundation staff also had access to the Student Information System, which documents scholarship activity in the students' accounts. Foundation personnel stated they had reviewed this information.

Transactions related to the foundation, including scholarships, were initiated by foundation staff and approved by foundation management. For scholarships, upon notification of scholarship recipients by the President's office, the foundation staff provided a list of students, amounts, and types of scholarships to the Financial Aid Office. The scholarships were then posted to the university's financial records, which included the foundation's accounts. If foundation personnel had been adequately monitoring scholarship awards, the situation of negative account balances would have been apparent to them and corrective action could have been taken.

GEIER CONSENT DECREE

The Business Office staff began to take a more proactive role in the foundation's accounts when it started to process transactions for the foundation's newly established Endowment for Educational Excellence account in January 2002. This endowment was created as a part of the Geier Consent Decree. The Geier case is a federal desegregation case which was filed against the State of Tennessee in 1968, and involved the University of Tennessee (UT) and TSU. Several rulings required the state to submit various desegregation plans, including one that resulted in the merger of UT's Nashville campus with TSU. Several motions and reviews were made by the Desegregation Monitoring Committee (DMC) in an effort to resolve the lawsuit. The DMC is composed of employees and board members of the Tennessee Higher Education Commission, the Tennessee Board of Regents, and UT. In 2000, the result of the mediation was a Consent Decree agreed to by all parties. The Consent Decree was filed on December 20, 2000, and the court entered the related order on January 4, 2001. One of the terms of the Consent Decree was the establishment of an endowment for scholarships. This endowment was to be managed by the TSU Foundation.

The corpus of the endowment comes from three funding sources. The first source is the State of Tennessee, whose funding consists of two components: (1) ten million dollars, which is paid to the endowment at a rate of one million dollars a year for ten years through the Tennessee Higher Education Commission and the Tennessee Board of Regents; and (2) up to an additional ten million dollars, which can be obtained from the state, as a match, if private donations are collected, with a maximum of $1.5 million available in any year, during the same ten-year period. The second source of funding is the Title III Strengthening Historically Black Colleges and Universities Program administered by the U.S. Department of Education, which allows the university to use 20% of its total Title III award for an endowment for scholarships. The third source of funding for the endowment is private donations.

On July 11, 2003, at the written request of the Foundation Manager and with the written approval of the university President, the university Business Office transferred $1,007,852.86 of foundation operating funds to a foundation investment account for the Endowment for Educational Excellence. Unfortunately, the immediate but unintended effect of the transfer was that it created a net negative current restricted cash position for the foundation as a whole. In other words, after the transfer, the foundation did not have sufficient current resources to meet current claims on cash. Apparently, this consequence was not clearly understood by university officials.

As noted above, the transfer occurred on July 11, 2003. The first time the Board of Regents staff was notified specifically about negative scholarship account balances was after that date. At that point, the Vice Chancellor contacted the Division of State Audit to apprise the auditors of the foundation's negative scholarship accounts and to request the Division's assistance in looking into the matter.

The propriety of the transfer for the Endowment for Educational Excellence and the legal consequences are under evaluation by the State Attorney General, the Tennessee Higher Education Commission, and the Tennessee Board of Regents.

MINUTES OF FOUNDATION BOARD MEETINGS

Based on a review of the minutes from meetings of the foundation's board of trustees, board members, foundation personnel, and representatives of the President's office were aware of deficiencies in the foundation scholarships at least as early as 1998. In the board minutes for September 17, 1998, concerns related to the issuance of four-year scholarships and funding were noted, and additional information was requested. The concerns were evidenced by the following statements from the then Acting Chairperson:

> The other point of discussion I would like to bring up is that we talked about scholarships for the students. We tell the students that when we give them a scholarship we are going to fund the scholarship for 4 years. But we are only showing funds for the individual yearly. From my standpoint on the balance sheet we should show all of the scholarships that we are obligated to fund for the life of that student while they [are] attending the university. What we are going to find out is that we are going to have a negative net worth.

The minutes of the next board meeting, held on January 21, 1999, refer to discussions related to a foundation balance sheet dated December 31, 1998, showing a net liability of $1.1 million for foundation scholarships and state that " . . . we have granted more scholarships today than we can afford to pay for today." The financial data presented during the meeting, along with the discussion recorded in the board minutes, revealed current and future possible insolvencies in the foundation scholarship accounts. The following statements from various board members quoted in the minutes evidenced the board of trustees' appropriate concerns relative to solvency of the scholarships:

> If we did not grant any scholarships for the next 4 years, we would need to raise $260,000 or $270,000 a year to pay off our obligation every year.
>
> It seems that we have a very basic problem, there are no checks and balances. While we are here raising money and others are spending money and if you are spending the money there are no limits on what they can spend. It seems like the Foundation is going to have to say if we are going to raise money for this many scholarships, here are the criteria. And then we assign the administration what is available.
>
> I think it imperative and it is our <u>fiduciary responsibility</u> [emphasis added] as a foundation that we need to address this issue especially due to the fact that we are trying to keep more of our students active with scholarships. That means that our proposed activities to do so [are] going to be counterproductive to us in the end. The Board really needs to put a limit and set forth some guidelines where this does not occur. Otherwise we are heading into a very strange and very unnecessary financial hazard.
>
> Is it prudent that we continue to offer scholarships when we don't know our solvency? Do we need to take action today to temporarily suspend it until we determine if we are solvent? For instance, what is the number of scholarships that have already been offered for the next year for freshmen? I think it is prudent to set some checks in point so we don't make ourselves less solvent than we already are.
>
> Once I was given the information I just heard that we are actually insolvent to redeem the scholarships that have been awarded, <u>we are liable for this as of this meeting</u> [emphasis added]. We have heard the facts. We know we cannot pay the scholarships that we have promised these kids. Something needs to be done at this particular meeting right now.

The result of this discussion was the creation of a three-person committee to review and evaluate the criteria in place for spending foundation funds and awarding scholarships and to recommend procedural policies for scholarship administration. The committee was also granted authority to place a moratorium on awarding scholarships. However, the minutes then contain a comment from the then Executive Assistant to the TSU President questioning if a moratorium had been placed on scholarships, and the minutes specifically state that no moratorium was currently in place. So, although the foundation board clearly understood that there should be an immediate suspension of new scholarships, the board apparently declined to enforce such an action at that time.

On March 18, 1999, the special committee that had been created reported to the foundation board of trustees. The minutes of that meeting record three recommendations by the committee to eliminate deficit balances on the restricted foundation balance sheet, as follows:

1. Suspension of the Foundation Honors Scholarships until the deficit is replenished from future fund raising efforts.

2. Development of a committee to research and recommend adjustments in the Foundation Scholars Program to improve historical attrition rates.

3. Upon the end of the suspension, change the scholarship awards process, giving the scholarship committee the power to award scholarships. Dr. Hefner will sit on this committee to determine the Foundation Honors Scholars. The Board, based on the financial condition, would determine the number of scholarships awarded annually. The scholarship committee would select the recipients.

The board accepted the report but clarified that the recommendations would not be acted upon until reviewed by the university President. There was no further record in the minutes regarding review of the Foundation Honors Scholarship program or suspension of scholarship awards.

In an interview conducted on January 27, 2004, the university President stated that he and two of the foundation board members on the special ad hoc committee appointed on January 21, 1999, met in the old administration building after the March meeting. The university President also stated that during this meeting it was resolved to continue to award foundation scholarships, on a cautious basis. According to the President, part of the awards from the scholarship accounts would be to deal with the fact that the Tennessee Board of Regents had required him to reduce and temporarily suspend the number of out-of-state tuition waivers being given by him, and he needed to use scholarship funds for this purpose. Both members of the special ad hoc committee who were named by the university President stated that they did not have any recollection of such a meeting and that they did not authorize the President to continue to award scholarships. However, the foundation board chairperson for the three-and-a-half-year period ended June 30, 2003, stated to the auditors that he and other members of the board were aware that the university President was continuing to award foundation scholarships.

FOUNDATION BOARD'S REQUEST FOR AN EXTERNAL AUDIT

The minutes of the foundation's board of trustees meetings, as cited above, record that the foundation's board of trustees, management, and staff, and the university President were all aware of the deficits created by the issuance of scholarships by the foundation and that they recognized their fiduciary responsibility to correct the deficit balances. However, the university President, with the apparent approval or acquiescence of the foundation, continued to award scholarships.

According to the former board chairperson, the board asked foundation staff for account by account information, which would have disclosed the extent of the negative balances in the scholarship accounts. However, foundation staff failed to provide this specific information although they had it. The minutes of board meetings did not contain any record of these requests, the responses, or the reasons the information was not provided. The foundation staff did provide tables of contingency analyses, which showed the current and projected liabilities for scholarships that had been awarded. Foundation staff also provided unaudited financial statement information on an annual basis. These contingency tables, unaudited financial statements, and the related discussions are recorded in board minutes.

The former board chairperson stated that although the board was not provided with detailed information, foundation staff advised them that there were shortages in some scholarship accounts. However, the negative balances were not a concern to the board because the information the board received from foundation staff showed that in aggregate the foundation had sufficient funds to meet its obligations. In fact, this information that the total balance in foundation accounts was positive was correct. In other words, even though the board did not receive the details of account balances, the board had the correct information about the status of foundation accounts overall. However, the board lacked the clear identification of accounts with negative balances and the exact extent of the negative balances.

Because of the concerns over increases in funds related to the Geier Consent Decree and the concerns noted in the 1998–1999 board minutes related to scholarships, the foundation board indicated an interest in an external audit, starting in 2001. (The 1989 agreement between TSU and the foundation requires approval from the Comptroller of the Treasury in order for the foundation to hire an external auditor.)

According to the February 2001 executive committee minutes, the board chair stated that he would recommend to the board at its March 2001 board meeting that the foundation be audited by an outside audit firm in addition to the normal state audit. The board chair further indicated that two audit firms had been contacted for that purpose. According to the board chair, the decision to secure an outside firm was

> . . . to give strong credibility to the Foundation in the ongoing capital campaign, to determine if TSU's Foundation is doing things similar to other institutions, and to see if the Foundation's paperwork [is] in compliance with what it should be doing.

At its March 2001 board meeting, the board addressed the issue of an external audit. According to the March 2001 board minutes, the board chair indicated his desire that the foundation undergo an audit. He reported that an audit firm had been contacted and that the estimated audit costs would be between $15,000 and $20,000. According to the minutes,

> The purpose of the Audit was to determine what we are doing in comparison to other schools who are raising mega dollars. He [the board chair] also stated that we need to determine what we can do better. Although, there may be constraints with TBR, because the Foundation is audited by the State. The Board [TBR] has been contacted to obtain approval.

The next mention of the board's desire for an external audit occurs in the March 2003 board minutes. Discussions among board members resulted in a motion, which was adopted, that the Comptroller's Office be contacted about the foundation conducting an independent external audit. According to the March 2003 board minutes, the board chair stated that the rationale for conducting an audit of the TSU Foundation was to develop "best practices" for the future growth of the foundation. The board chair further stated that, as part of an external audit of the foundation, it was "rational to include a parallel review of the financial books of Tennessee State University . . . Presently, the State of Tennessee, vis-à-vis the Comptroller, is unable to provide the financial records of the University to the TSU foundation." At that time, the board adopted a resolution that a board representative and the foundation's attorney discuss and resolve the matter with the university's President and the foundation's Executive Director.

Prior to its March 2003 meeting, the board provided two draft proposals for audit services from one audit firm to TBR staff with a request for assistance in expediting approval of this review by the Comptroller's Office in time for the first visit by a representative of the audit firm.

The TBR Vice Chancellor for Business and Finance discussed the board's request with the Comptroller. At that time, the Comptroller's office understood the request to pertain to management practices and to an external audit in lieu of audit work that could be performed by State Audit. There was no indication in those discussions that the foundation board was concerned about financial mismanagement or negative accounts. Therefore, consistent with past practices of the Comptroller's office, the Comptroller's office was in agreement with the foundation board's proposal for a review of management practices but did not support an external audit in lieu of the audit work which could be performed by State Audit.

An external audit of the foundation as a legal entity, separate and distinct from the university, would have confirmed the foundation board's understanding of the financial position of the foundation, would have given them the actual numbers for account balances, and also would have confirmed the information they already had in the foundation's unaudited financial statements regarding the net position of the foundation. Clearly, the foundation board was proactive in identifying the gap between the scholarship commitments resulting from the President's actions and the available funding in the current year, as well as estimated fund-raising for future years. The foundation board was also proactive in requesting more detailed financial information from foundation staff. In addition, the foundation board was proactive in seeking an external audit to obtain more information about the foundation's financial position. As evidenced by these actions, the foundation board recognized the problems related to funding scholarships and took appropriate steps to obtain additional intelligence regarding the foundation's overall finances, revenues, expenses, and current and long-term obligations.

AWARDING OF SCHOLARSHIPS BY THE UNIVERSITY PRESIDENT

Not only did the university President know about the serious problems with foundation scholarships as recorded in foundation board meeting minutes, he had additional information about these matters available to him due to his position as TSU President. The university President selected candidates to receive Alumni and Honors scholarships through the TSU Foundation. The university President stated that he made selections based on recommendations from alumni groups, TSU recruiters, and his personal recruiting activities. The President signed each scholarship award letter.

Based on a review of the foundation board minutes and discussions with foundation staff, it appears that the university President never requested information regarding how much money he could award or how many students could be awarded scholarships. It appears the university President's focus was on encouraging honors students to attend TSU, without regard for the costs of the scholarships being offered. He stated that he was relying on foundation staff to provide information related to the funds for the scholarships awarded. However, he never appeared to seek any of this information even though he knew he lacked the information and knew how to obtain it.

In this regard, two instances were noted where the President received information concerning the deficit accounts in the foundation. The first is a memorandum from the then Executive Director of the foundation to the university President dated October 11, 1999. The memorandum contained the statement that the academic scholarship account had a negative balance of $250,070.17. The second is a memorandum from the Vice President for University Relations and Development to the university President dated July 18, 2002. That memorandum included the information that there was approximately $1,361,105 in uncovered scholarship debt. When asked about these memoranda, the university President said he could not recall ever seeing either document.

CRITICAL CONTRIBUTING CONDITIONS

Our analysis disclosed several critical contributing conditions that in combination facilitated the foundation's slide into insolvency and that also worked to prevent full disclosure of the foundation's true financial position. First, the President of the university served in the dual roles of university President, responsible for both the Business Office staff and the foundation staff (who were university employees), and foundation board member. As a board member, the President was a key member of the foundation management team. In addition, the President was the individual who took the initiative to personally award Foundation Honors Scholarships, without the input or review of the foundation board or foundation staff. However, the university President awarded scholarships without regard for available funds and with apparent knowledge of insufficient funding. This was due, to some extent, to a lack of appreciation of the need for budgetary controls on spending, but also to a belief on his part that he was a successful fund-raiser who could solicit enough contributions to offset any negative account balances. Moreover, as cited above, although foundation staff informed the university President in writing about negative balances on two occasions, he did not recall receiving the information, indicating a lack of attention to significant communications which identified serious problems that required his prompt attention. Further, the university President, or his representative, was present at board meetings where deficit scholarship accounts and shortages were discussed, which placed the President on notice regarding problems with funding scholarships.

Second, Business Office staff knew about the increasing negative balances in some of the foundation scholarship accounts. However, in their communications with foundation staff, they did not specifically emphasize those negative balances, the possible consequences of even larger negative balances, or the necessity to resolve the negative balances without delay. Moreover, Business Office staff did not communicate their concerns directly to the foundation board; instead, they only provided information to foundation staff.

Third, foundation staff had information available to them that would have disclosed the negative balances, but it is unclear that they fully understood the information or that they grasped the significance and consequences of those negative balances. In fact, foundation staff perceived the negative balances more as fund-raising targets, indicating amounts that needed to be raised through heightened fund-raising activities.

Fourth, the foundation board astutely identified the problem of awarding more scholarships than could be funded with available dollars. The foundation board also determined that the information provided to it, by either foundation staff or the audits of the university, which included the foundation, did not furnish sufficient detail to them as to the foundation's accounts. However, the foundation board tended to focus exclusively on an external audit as the instrument by which to obtain a true picture of the foundation's financial health. By doing so, the foundation board bypassed another more direct and effective avenue for gathering information: requesting that the President of the university direct his staff to provide the foundation board with the necessary information by a certain date. Clearly, the foundation board took one path, and when that path was blocked, the board did not seek other alternatives. Furthermore, the board discussed these issues over a period of approximately three and a half years, as noted in the board minutes cited above, but did not stop the awarding of scholarships by the university President.

Fifth, as regards the issue of an external audit, the urgency and necessity for an external audit as a tool to further examine negative account balances was not communicated to either the staff of the Board of Regents (TBR) or the auditors. The first time sufficient information about the foundation's problems was provided to any organization external to the university and the foundation was not until August 2003, when it was provided to TBR staff. As soon as this information was provided to State Audit by TBR staff, we began an intensive review of the foundation's records.

The foundation board and TBR staff had several conversations over the years 2001-2003 regarding the board's interest in having an external audit performed of the foundation. During these conversations, the TBR staff recall advising the foundation board that although the Comptroller's Office audits the university, which included the foundation, and therefore would be the entity to perform any special financial audits of the foundation, the foundation board could retain a CPA firm to conduct a management (rather than a financial) audit. In early 2003, the foundation board formally presented to TBR staff a request for a "management audit" with the goal of reviewing current procedures against "best practices" in gift account, donor acknowledgement, requisition procedures from accounts payable, board policies and structure, files and records, and general capital campaign readiness.

As a result of this request, there was one conversation between the Comptroller and TBR staff in which the matter of an additional external financial audit of the foundation was discussed. During that conversation, the Comptroller took the position, indicated above, that the Division of State Audit would perform any particular financial audit work needed by the foundation, but the foundation was free to obtain the services of a CPA firm to engage in the type of work that it appeared the foundation board wanted, a management audit. Unfortunately, at no time was there any mention to the Comptroller or the auditors that an audit was being requested to look into problems with the funding of scholarships.

From an audit perspective, the foundation, due to its relatively small size of operations and financial activity in comparison to the university taken as a whole, is not a material element of the university's operations. Consequently, given that the external audit focus is the university taken as a whole, the extent of audit work performed relative to the foundation was limited in nature. The audit scope of the university did not require examining the foundation's accounts in great detail. Auditing to that detail would have disclosed the negative balances in the individual accounts, a condition the board had already discussed and considered serious. Of course, if auditors had found the negative balances, the practice and consequences of maintaining such balances would have been considered a serious problem requiring corrective action.

In addition, as part of the audit process, auditors seek information from top management of the university regarding, among other things, those officials' understanding of the adequacy of the internal controls and their knowledge of any problems that should be particularly addressed. Unfortunately, the detailed information available to top management of the university regarding the foundation's funding was not shared with the auditors. Had it been, either in 2003 or at any time during the preceding five years, specific audit procedures would have been performed on the detailed accounts of the foundation.

REVIEW OF STUDENT INFORMATION SYSTEM AND RECONCILIATION

Foundation personnel stated that for the period 2002-2003, they conducted a daily review of student financial aid awards from the foundation to prevent overawarding of financial assistance. However, they acknowledged that they could not provide documentation of their review of the accounts of scholarship recipients on the university's Student Information System or that they reconciled the amounts awarded with the amounts the students received from the Financial Aid Office. Furthermore, they acknowledged that they did not note if any problems were found in their review. In the *Tennessee State University Foundation Policy and Procedures Manual*, which was in effect for the periods discussed, Section (5), III, C. 1., states:

> The Student Information System (SIS) should be reviewed to determine if the student's charges will be covered by the Foundation awarded scholarship and if any other grants, loans, or scholarships have been applied to their account. If it is found that other scholarships, grants, or loans can cover the student's total charges, then the Foundation award can be adjusted accordingly. In addition, the student refund report can be reviewed to determine any students who have current credit balances.

The reconciliation would have ensured that students did not receive an overaward of funds.

Recommendation

The university President should exercise due care in all activities that can put state and foundation assets at risk. He should reevaluate his and the university's relationship with the foundation in light of the issues noted in this report. He should recognize the inherent conflicts and confusion created when he serves in dual roles with the university and the foundation and should realize that his primary responsibilities are to the university. If he continues to participate in foundation board activities, he should use his position to protect the university from improper situations. If he cannot influence the foundation board to avoid problems for the university, he should dissolve the university's association with the foundation. In recognition of his fiduciary duties, the President should accept his responsibility to ensure that his employees develop policies and procedures to ensure adequate funding is available before issuing scholarships and to properly monitor foundation accounts to avoid issuing scholarships when accounts are in a deficit status. The President should ensure that his employees assigned to foundation duties and in the university's Business Office develop a mechanism for the preparation of timely reconciliations of student accounts. University policies and procedures applicable to transactions of departments should be applied to the foundation's transactions recorded in university records by university employees. The agreement between the university and foundation should be amended to reflect any new procedures established to delineate the responsibilities of each party.

The university President, in consultation with the Tennessee Board of Regents and legal counsel, should establish a proper plan for the reduction of negative account balances. The board should review the actions of the President noted in this report and resolve why the President failed to take more prudent measures to address these issues as they were developing, including providing more candid information to Board of Regents officials.

The Tennessee Board of Regents should be proactive in its advice to TSU and other member schools about their need to not abrogate their responsibilities for foundations and other outside entities under the direct supervision of the school, and the Board of Regents should be proactive in its review and oversight of its member schools' relationship with such entities.

Management's Comment

Tennessee Board of Regents:

We concur with the finding and recommendation. The university president will reevaluate his and the university's relationship with the foundation in order to address the issues noted in this audit report.

The foundation policies and procedures manual currently includes a policy on scholarships. However, procedures and responsibilities for budgeting for scholarship programs and ensuring funds are available before a scholarship is actually awarded to a student are inadequate to ensure scholarships are not awarded from accounts with insufficient funds. Procedures will be developed by June 1, 2004, that address and assign specific responsibilities for ensuring funds are available in foundation scholarship accounts before scholarships are awarded to students. Additionally, the business office has been directed by the TBR Vice Chancellor for Finance to process no disbursements on any foundation account that does not have a sufficient positive balance to cover the requested disbursement.

It has been the practice for a number of years for the TSU president to award foundation scholarships to students with the expectation that the foundation would raise sufficient funds during the academic year to cover those scholarship commitments. This practice has ceased, and the president is no longer involved in the awarding of foundation scholarships. Scholarship commitments will not be made unless funds are already in place to fund the award rather than offering scholarships with the intention of raising the funds later to finance the scholarship commitment.

The failure to adequately monitor foundation accounts by the TSU business office appears to have resulted from varying interpretations of responsibilities as outlined in the July 1989, agreement between the university and the Tennessee State University Foundation. A complete review of this agreement will be accomplished by July 1, 2004, and if the university and foundation decide to continue to have an operating agreement, then any needed revisions or clarifications will be incorporated into a new agreement. Additionally, procedures will be developed to include timely reconciliations of student accounts to ensure foundation scholarships are properly recorded in student accounts.

The financial pressures that the transfer of $1,007,852.86 to the Geier Consent Decree Endowment placed on the foundation resulted from inadequate internal communication at the university concerning available funding. The Tennessee Board of Regents' Central Office will require any future requests for consent decree transfers to include a written certification that privately raised funds are available for that purpose. The certification must be signed by the president, the vice president for university relations and development, the vice president for business and finance, and the president of the foundation (if the funds reside in the foundation).

The university president, in consultation with staff of the Tennessee Board of Regents and the Tennessee State University Foundation Board of Trustees, will develop a plan for eliminating the negative account balances in the foundation scholarship accounts. Additionally, the Board of Regents will be proactive in assisting TSU in resolving the problems cited in this audit as well as providing proper oversight to all TBR institutions relating to foundation operating agreements.

The Tennessee State University president offers the following specific corrective actions that will be undertaken:

- No expenditures will be processed from foundation accounts unless there are sufficient funds available in the accounts. The foundation staff will be responsible for communicating to all parties information regarding the processing procedures for all transactions.

- Separating the foundation's operations from the university's operations will be considered. Representatives from a well-respected public institution which has proven successes in its foundation's separate relationship with its university will be brought in to advise the foundation on the most efficient procedure for the separation of responsibilities.

- A comprehensive evaluation of the university's senior staff will be made to determine what, if any, changes are necessary.

- The president will work in conjunction with the foundation to hold periodic fund-raising events to address the scholarship deficits.

- The president will have regular meetings with the vice president for business and finance to review foundation finances.

- The president will have regular meetings with the vice president for university relations and development to review foundation issues.

- The Tennessee State University Foundation's banking and financial accounts will be separated from the university's bank accounts.

- The business office staff and foundation staff will hold joint training workshops on a periodic basis.

- The business office will make formal financial reports to the foundation board at least quarterly.

- The university's vice president for university relations and development will no longer serve as executive director of the foundation.

- Prior to the completion of the 2003-04 fiscal year, the university’s finance and accounting staff will review all foundation accounts in order to determine if they are properly classified as endowment, unrestricted, or restricted.

- The president will recommend to the foundation that new criteria be established for awarding scholarships and that the president’s role be limited to making recommendations in this process.

- The president will recommend to the foundation that he not serve on the board.

<u>Tennessee State University Foundation Board of Trustees:</u>

The audit (including findings 1-4) contains some statements with which we take issue.

1. The audit findings do not make clear that references to the conduct and procedures of "Foundation personnel" are in fact references to University personnel, as a result of the execution of the 1989 agreement that removed administrative and financial oversight duties and responsibilities from the Foundation and assigned those tasks and responsibilities to the University. In retrospect, this arrangement—which was surely intended as a cost-savings measure—may have been a major cause of the problems now facing the University and the Foundation, but it was part of the landscape when the members of the Board took office. Thus, the audit repeatedly makes reference to "Foundation staff" and "Foundation personnel" who carried out various tasks reviewed by this audit without explaining that these tasks were the contractual responsibility of the University rather than the Foundation. In fact, the Foundation Board had no say-so over the hiring or supervision of those individuals who are the subject of the findings contained in the audit. This observation is not meant to be a negative assessment of those University employees' actions, but rather an attempt to avoid any misconception about who paid their checks and who supervised them.

2. The audit paints the Board as a tunnel-visioned entity that sought an external audit while ignoring other possible avenues for addressing possible problems with scholarship accounts. The Board made known to University officials on several occasions its concerns about scholarship accounts. It formed a committee that made recommendations for improvement. Its leadership met with University leadership to express its concerns. In the end, however, the Board took the position that the fairest and best way to check the financial wellness of the Foundation was to request an audit. While the Board would have welcomed an audit by the Comptroller or a private auditing firm, prior to July 1, 2003 and the enactment of a new law regarding the auditing of university foundations, it was questionable whether the Comptroller had the authority to audit the books of the non-profit foundation. (the Comptroller was clearly of the view that his office lacked such authority during the May 2003 legislative hearings regarding the amendment of T.C.A. § 49-7-107). We note that, unlike audits of Board of Regents colleges during the years we were trying to grapple with this issue, Comptroller's audits this year have included an examination of the foundations. We welcome this scrutiny and wish it had taken place at the time we requested an audit.

3. The audit correctly notes the Board's repeated attempts to raise the issue of Foundation account deficits, but suggests that an audit would have occurred long ago if its concerns had been conveyed in a more direct fashion. We concur that the Board could have been more explicit regarding its concerns in its requests for an audit, even though it had been extremely explicit in its direct communication with the University leadership. But the minutes of our meetings are shared with the Tennessee Board of Regents and presumably are open to any citizen who wishes to review them. Those minutes show the depth of our concern regarding scholarship accounts and our willingness to tackle the issues. Indeed, the previous Chairman of the Foundation Board made three requests for an audit and all were refused by the Chancellor.

4. Finally, to the extent the audit has concluded that the Foundation lacks standards for the award of its scholarships, that conclusion is incorrect. There are well-settled standards for such awards and, like all administrative functions of the Foundation, the monitoring of compliance with those standards is a contractual obligation of the University.

Thank you for allowing us the opportunity to express these views, and we are confident you will allow them to be reflected in your final report. Our Board is a dedicated group of leaders from this state and community, and we only ask that our efforts to address problems in a responsible way be fully reflected in your final report.

<u>Tennessee Board of Regents' Response to Tennessee State University Board of Trustees' Comments:</u>

We have reviewed the Tennessee State University Foundation Board's response to the draft audit finding regarding the Foundation. We are in agreement that the Foundation had requested approval for an external audit of the Foundation. However, we were informed by your office that approval for a financial audit of the Foundation would not be granted because the annual state audit of the University included the financial records of the Foundation. We were told that the Foundation could have an independent management review of its operations and procedures to identify operating procedures that could be improved. This response was shared with the Foundation Executive Director.

Also, I would like to point out that the central office of the Board of Regents has never received copies of the minutes of the TSU Foundation Board meetings and was unaware of the scholarship funding problems until this past fall semester.

<u>Division of State Audit Response to Tennessee State University Foundation Board of Trustees' Comments:</u>

The Board's response contains four key points.

- The Board states that the execution of the 1989 agreement removed administrative and financial oversight duties and responsibilities from the Foundation and assigned those tasks and responsibilities to the University. In fact, the 1989 agreement does not transfer those duties and responsibilities to the University

- The Board states that the Board had no say-so over the hiring or supervision of " Foundation staff." However, the Foundation staff, who were University employees, had a dual reporting function to both the University President and the Foundation Board. In addition, the University President, who is the Chief Executive Officer of the University, and thus the ultimate supervisor of University employees, was also a Foundation Board member, and not only knew of the problems facing the Foundation but also promised to resolve them. Also, the Foundation accountant was present at Board discussions of deficit accounts.

- The Board states that although the Board could have been more explicit regarding its concerns in its requests for an audit, the minutes of the Board meetings were shared with the Tennessee Board of Regents (TBR). As noted in TBR 's response to the Board's comments, the minutes were not shared with TBR members or staff.

- The Board states that the audit concludes incorrectly that the Foundation lacks standards for the award of its scholarships. In fact, the audit concludes that the Foundation has such standards, but the University President, who awarded scholarships on behalf of the Foundation, did not adhere to those standards in some cases.

2. Not all foundation honors scholarship recipients tested were eligible for the aid received, and as a consequence, the foundation incurred scholarship costs that could have been avoided if the eligibility criteria had been properly applied

Finding

The Tennessee State University Foundation does not adequately monitor honors scholarship accounts to ensure that students meet the appropriate criteria. The foundation issues both honors scholarships and regular scholarships (various types of scholarships other than honors). Based on the testwork performed related to foundation honors scholarships, some ineligible students received foundation honors scholarship funds and some students continued to receive foundation honors scholarship funds after they became ineligible. As a result, the foundation incurred scholarship costs that could have been avoided if the scholarship eligibility criteria had been properly applied.

According to the foundation's website, students who receive foundation honors scholarships are required to have a high school grade point average (GPA) of at least 3.3 and a composite ACT score of at least 21 or a cumulative SAT score of at least 890. Also, as recorded on the audiotape of the foundation board meeting for January 22, 1998, the foundation's then Executive Director stated that foundation honors scholarships required a 3.3 GPA and an ACT of 21. According to the foundation honors scholarship award letters, signed by the university

President, foundation honors scholarship recipients are required to earn at least 12 hours per semester and maintain at least a 3.0 GPA in order to continue receiving their scholarships.

Eligibility was tested for all of the students who received foundation honors scholarship funds for the period July 1, 2000, through December 31, 2003. Based on information provided by the university, 252 students received honors scholarship funds over the 3-1/2 years reviewed. Of the 252 students, six were transfer students. Of the 246 remaining honors scholarship fund recipients, 85 failed to meet the criteria to initially receive the scholarship funds. However, most of these students met at least one of the criteria. Twenty-six students met the GPA requirement of at least a 3.3, but did not meet the test score requirements. An additional 46 met the test score requirements, but did not meet the GPA requirement. Thirteen students did not meet either GPA or test score requirements. Honors scholarship funds paid on behalf of the 85 ineligible students totaled $226,804 for the 3-1/2-year period. In addition, auditors noted several instances where students' earned hours or GPAs dropped below the required levels to continue receiving the scholarship funds, but the students continued to receive the funds.

Based on a limited review of ten foundation honors scholarship award letters prepared by the staff of the President's Office and signed by the President, the high school GPA stated in the letter was incorrect in half of the letters reviewed. In four cases, the actual high school GPA was lower than stated in the letter, and in one case the actual high school GPA was higher when compared to the GPA in the students' official records maintained by the university. However, the ACT and SAT test scores stated in the letters were correct when compared to the scores in the students' records maintained by the university.

Recommendation

Foundation personnel should carefully evaluate the eligibility for each student being considered for a foundation honors scholarship to ensure that each student meets all of the criteria for the scholarship being awarded. Foundation personnel should also carefully evaluate the eligibility of each student to continue receiving the scholarship to ensure that the student meets the criteria for continuation of the scholarship. When foundation personnel identify students who are not eligible for foundation honors scholarships, they should immediately notify the appropriate university staff. Because of the issues identified related to the foundation honors scholarships, foundation personnel should carefully review the status of all other scholarships awarded through the foundation to ensure their compliance with both initial and continuing eligibility criteria. Either the university President should refrain from initiating the scholarship letters or controls should be developed to ensure the President's Office uses correct information in identifying students eligible for scholarships.

Management's Comment

We concur with the finding and recommendation. Foundation personnel will evaluate the eligibility for each student that is being considered for a scholarship to ensure that the student meets all the criteria for the scholarship being awarded. In offering foundation scholarships to students, the president had often made exceptions to the stated criteria based on such things as a student's extra curricular activities or leadership skills. However, the official criteria approved by the foundation did not provide for such exceptions. A review will be made of the criteria for awarding scholarships, and any changes or provisions for exceptions will be included in revised criteria for approval by the foundation board of trustees. Additionally, any changes in criteria will be updated on the foundation's web site.

3. The Tennessee State University Foundation does not have adequate procedures for recording and reconciling revenues and maintaining documentation

Finding

The Tennessee State University (TSU) Foundation does not have adequate procedures for the recording and reconciling of revenues. In addition, foundation personnel (TSU employees) could not provide adequate documentation that all funds received had been appropriately deposited through the university Bursar's Office and had been correctly posted to the specified foundation accounts.

During interviews and the review of accounts related to the other foundation findings, foundation personnel and foundation board members expressed concerns regarding the proper recording of foundation revenue by the university. Therefore, a review of revenue receipting and recording by the foundation and the university was performed. The Foundation Manager and Financial Analyst described the receipting and recording process as follows.

Various funds are received, usually through the mail, by the foundation office and various TSU departments (for example the School of Engineering), which have accounts within the foundation's records. Funds received can include cash or checks; however, most of the funds are in the form of checks. Included in these funds are donations, which can be unrestricted, restricted (based on donor wishes as to how the funds are to be used but not usually in a formal legal restrictive document), or endowed (usually restricted by an endowment agreement). Funds received by the various TSU departments are listed on a Memorandum of Payments Received form by departmental personnel and signed as prepared. The Memorandum of Payments Received form contains columns for the name of the person from whom the funds were received, amount, method of payment, check number, purpose, cash receipt number, date receipted, and account credited. The Memorandum of Payments Received form and the funds received are then taken to the foundation office for processing.

The foundation office also receives funds by mail or walk-in donors. Normally the foundation Secretary would open the mail and collect walk-in revenues, but since that position is vacant, the Foundation Manager currently performs those functions. Since the Secretary position is vacant, he also currently prepares a Memorandum of Payments Received form for the day's receipts, which he signs as the preparer, and collects the Memorandum of Payments Received forms and funds that came in that day from departments. The Foundation Manager then gives the Memorandum of Payments Received forms and the funds to the Financial Analyst. The Financial Analyst stamps the checks for deposit only, reviews the forms, signs as the reviewer on the Memorandum of Payments Received forms, and makes a copy of each check. The Financial Analyst then takes the funds received and the Memorandum of Payments Received forms to the Bursar's Office for receipting and recording in the university's accounting records.

The cashier in the Bursar's Office reviews the deposit and signs each Memorandum of Payments Received form. After reviewing the deposit and signing the form, the cashier records the revenue in the Financial Records System (FRS). FRS generates an Official Cash Receipt with the account number, amount, source of the funds, and the cashier who recorded the transaction. This cash receipt is attached to the Memorandum of Payments Received form and returned to the foundation office. The receipts and forms are usually returned the next time foundation personnel come to the Bursar's Office to make a deposit.

After receiving the receipts and forms from the Bursar's Office, the Financial Analyst posts the revenues to the Alumni Development System (ADS). The ADS does not interface with the university's systems. The Memorandum of Payments Received form and the cash receipt are both multi-copy forms. A copy of the Memorandum of Payments Received form and a copy of the cash receipt are retained by the Bursar's Office for documentation.

The foundation maintains a monthly receipt binder that should contain copies of the checks received, copies of the Memorandum of Payments Received forms, and copies of the Official Cash Receipts obtained from the Bursar's Office. If the foundation receives funds after the deposits for the day have been delivered to the Bursar's Office, the checks or cash are to be kept in the foundation safe. The safe is in a closet in the foundation office.

Based on interviews with the Foundation Manager and the Financial Analyst and a review of the monthly receipt binders, it appears that the procedures described above are not always followed, and the following weaknesses were noted:

- Foundation staff stated that TSU departments sometimes hold checks for multiple days; therefore, the foundation is delayed in getting the funds deposited timely. In addition, based on the review of the supporting receipt documentation and foundation staff interviews, it appears funds may stay in the foundation office for multiple days.

- Foundation staff stated that TSU departments sometimes take deposits directly to the Bursar's Office, which prevents their review of the deposit before it is recorded by the cashier. However, the foundation does subsequently receive a copy of the cash receipt from the Bursar's Office.

- Based on the way funds are handled, checks are not restrictively endorsed as early in the receipting process as possible.

- The Financial Analyst stated that funds are not always placed in the safe before being taken to the Bursar's Office for deposit. He stated that he keeps them in a box in a desk in the foundation office. It was also noted that the door of the closet in which the safe is kept was open and the safe was unlocked during an audit visit to the foundation office.

- It appears that the foundation staff are not reconciling the cash receipts obtained from the Bursar's Office with their documentation to ensure all funds were properly recorded. In addition, the foundation staff does not reconcile the foundation's records with the monthly transaction reports received from the university's Business Office, which show how the revenue was recorded.

The monthly receipt binders were reviewed for the period July 1, 2002, through December 31, 2003, in an attempt to determine that all revenue received by the foundation was recorded properly in the accounting records. The review of the monthly binders showed 1,801 items were included in the binders for the period reviewed. An item would be at least one of the following: a Memorandum of Payments Received form, a TSU Official Cash Receipt, or other supporting documentation such as a copy of a check or a credit card receipt. Due to the incomplete documentation retained by the foundation for many of the items, a full accounting of revenue could not be made. The following discrepancies were noted for 1,035 items out of the 1,800 items examined:

- There was no TSU Official Cash Receipt for the corresponding Memorandum of Payments Received form for 300 of the 1,035 items (28.99%).

- There was no Memorandum of Payments Received form for the corresponding TSU Official Cash Receipt for 627 of the 1,035 items (60.58%).

- There was no Memorandum of Payments Received form or TSU Official Cash Receipt for the corresponding donation by check, cash, or credit card for 97 of the 1,035 items (9.37%).

- There were discrepancies with 11 of the 1,035 items (1.06%) as follows: for 3 items, the account number was not fully shown on the Memorandum of Payments Received form to compare with the cash receipt; 2 items had duplicate receipts; for 3 items, the totals on the Memorandum of Payments Received form did not match the total of the cash receipt; and for 3 items, the account number on the Memorandum of Payments Received form did not match the account number on the cash receipt.

Although the missing documentation does not establish that an error in the accounting records occurred, it does demonstrate the need for foundation staff to reconcile the foundation's records with the information in the university's system on a periodic basis to make sure revenues are being properly recorded. For the transactions for which both a Memorandum of Payments Received form and a matching TSU Official Cash Receipt were present, the university's Business Office properly processed the transaction.

Recommendation

The Foundation Manager should ensure that complete documentation is being maintained for all revenue transactions and that the foundation's records are reconciled with the foundation accounts in the university's system on a timely basis to ensure revenue is recorded properly.

Management's Comment

We concur with the finding and recommendation. Although the Tennessee State University Foundation does have a written policy for the solicitation of gifts and donations, the procedures for processing, recording, and reconciling revenues will be strengthened. Foundation staff will reconcile the monthly accounting reports provided by the business office with the foundation office deposit records for that month. Any discrepancies will be investigated and resolved jointly by the foundation and the business office. The reconciliation will be signed by the foundation staff employee preparing the report and will be reviewed and signed as approved by the vice president for university relations and development. The business office will provide any training needed by the foundation staff on reconciling the monthly accounting reports.

4. The university President exceeded his authority by improperly entering into an agreement with the Tennessee State University Foundation

Finding

The university President improperly entered into an agreement with the Tennessee State University Foundation in order to attempt to remedy negative scholarship account balances and negative current cash and cash equivalent amounts shown on the foundation's accounting records. (See the related finding on negative account balances.) This agreement was authorized by the university President without the approval of the Tennessee Board of Regents (TBR), which was in violation of the Board's guidelines.

In a letter dated August 22, 2003, from the foundation Chairman to the university President, the President improperly agreed to extend the university's credit by waiving immediate payment of the foundation's obligations. The letter discussed two draft proposals from the university to the foundation for the payment of foundation obligations to the university. The foundation Chairman indicated the proposals were not suitable for the foundation's needs and made a counterproposal in the letter.

The significant items of the counterproposal included an acknowledgment that the foundation owes a substantial sum to the university for educational services rendered in previous periods to students for whom the foundation had agreed to provide financial assistance and for educational services to be rendered during the 2003-2004 school year. However, the foundation questioned the amount of total scholarships owed to the university, which the university indicated was approximately $2.4 million for prior years and $1.1 million for the 2003-2004 year. In addition, the foundation proposed an immediate payment of cash in the amount of $250,000 (representing approximately one-half of the total that the university purported to be currently due) in partial satisfaction of its obligations. Additionally, the foundation proposed to pay all current semester expenses (fall 2003 semester) after the exact amount was determined and the fall fundraising events had occurred. Also, after an audit of the accounts would be obtained by the foundation, the foundation's obligations to the university would be formally negotiated. Finally, the foundation proposed a graduated payment schedule of the to-be-negotiated amount over the next several years with final payments being made in 2009. The letter was signed as "Accepted and Agreed" by the university President.

Although the letter stated the agreement would have to be approved by the foundation's board of trustees, the President's signed acceptance appeared to attempt to establish a contract between the university and the foundation. The agreement appears to violate TBR Guideline G-030, which requires the approval of the Chancellor or his designee for agreements in excess of $100,000.

Recommendation

The university President should not enter into agreements with outside entities without consultation and review of Tennessee Board of Regents legal counsel and officials. In addition, the terms should be reviewed and negotiated with regard to applicable criteria and the approval required by TBR guidelines should be obtained.

The Tennessee Board of Regents should ensure that its member institutions recognize they cannot enter into such agreements with foundations.

Management's Comment

We concur with the finding and recommendation. Tennessee Board of Regents' staff have advised the university president that board contract policies and guidelines must be followed relative to approval of contracts and agreements. Similar instructions will be conveyed to all TBR presidents reminding them of the requirements for adherence to policies and guidelines for agreements, including any agreements with foundations.

5. The university has not implemented adequate controls over management of computer user accounts

Finding

Auditors observed that the university has not implemented adequate controls over management of computer user accounts. The university's policies require the protection of proprietary, personal, privileged, or otherwise sensitive data and resources that may be processed in any manner. Improvements are needed to comply with this policy. Failure to provide such controls increases the risk that unauthorized individuals could access sensitive university systems and information.

The wording of this finding does not identify specific vulnerabilities that could allow someone to exploit the university's systems. Disclosing those vulnerabilities could present a potential security risk by providing readers with information that might be confidential pursuant to Section 10-7-504 (s), *Tennessee Code Annotated*. We provided the university with detailed information regarding the specific vulnerabilities we identified as well as our recommendations for improvement.

Recommendation

The Office of Communication and Information Technologies should ensure that adequate controls are established. Management should also take all other steps available to establish or improve any compensating controls until these conditions are remedied.

Management's Comment

We concur with the finding and recommendation. The Office of Communication and Information Technologies will establish adequate controls over the management of computer user accounts.

6. <u>The university did not submit correct data on the FISAP</u>

Finding

The Financial Aid Office did not submit correct data to the U.S. Department of Education on the 2002-2003 Fiscal Operations Report and Application to Participate (FISAP) submitted on October 1, 2003, and the revised 2001-2002 FISAP submitted December 2002. The FISAP, which is for campus-based financial aid, consists of the Application for Participation for the upcoming award year and the Fiscal Operations Report for the previous award year. Campus-based financial aid includes Federal Perkins Loans, Federal Supplemental Educational Opportunity Grants, and Federal Work-Study. Volume 4 (Campus-Based Common Provisions), Chapter 1, of the *Student Financial Aid Handbook* and the FISAP Instruction Booklet specify as follows:

> To apply for and receive funds from the Department of Education for one or more of the campus-based programs, a school must submit a FISAP [Fiscal Operations Report and Application to Participate] each award year. . . . The information reported on the FISAP must be accurate and verifiable. . . . **December 15** - all

> corrections to FISAP data and resolution of edits must be submitted to the Department.

The university did not report correct numbers in several sections of the FISAP for the 2002-2003 academic year. The total number of undergraduate and graduate students enrolled was reported inaccurately in Part II, Section D. The number of undergraduate students was overstated by 365, and the number of graduate students was understated by 377. The Dean of Admissions had submitted the correct totals to the Financial Aid Office, but those numbers were not used for the report.

In Part II, Section E of the FISAP, the university did not accurately report total tuition and fees, total Federal Pell Grant expenditures, and total expended for state grants and scholarships made to undergraduates. The total tuition and fees for undergraduates was understated by $4,997, and the total tuition and fees for graduates was overstated by $4,997. The total Federal Pell Grant expenditures was overstated by $10,807, and the total state grants and scholarships made to undergraduates was overstated by $7,935. The *FISAP Technical Reference* instructs universities to:

> Report the total amount expended against your Federal Pell Grant authorization for the period July 1, 2002 through June 30, 2003. This amount should agree with the final cumulative expenditures through June 30, 2003 as entered in the Grants Administration Payment System (GAPS).

Several numbers reported in Part II, Section F of the FISAP, did not agree with the Student Financial Aid Batch Annual (SBA) 680 report. The SBA 680 report is the support for the FISAP that lists financial aid and scholarship information. The information on the report is extracted directly from the Student Information System. In the Dependent section of the FISAP, the number of students reported for item 39 under the (a) column was overstated by 1,383, which also overstated the total for that column. In the Independent section, the number of students reported for item 39 under the (c) column was overstated by 125, the number reported under the (d) column was understated by 1, and the number reported under the (e) column was overstated by 324. These errors also affected the total for each column.

The university also did not report accurate information in Part V, the Federal Work-Study (FWS) section of the FISAP. In Section B, Federal Funds Available for FWS Expenditures, the amount on item 4 was overstated by $109,346, item 5 was overstated by $87,000, and item 7 was understated by $109,346. In Section D, Funds Spent from Federal Share of FWS, item 13 was overstated by $458,070, item 13.a was overstated by $458,070, and item 14 was understated by $144,849. In Section E, Use of FWS Authorization, item 17 was overstated by $7,529, and item 18 was understated by $7,529. These errors were made because the information provided by the Business Office was not used in completing the report. The Director of Financial Aid stated that they had gotten error messages when they attempted to key in some of the information provided by the Business Office. Since they were working on the report very close to the deadline, they did not take time to try and resolve the error messages, but keyed in whatever information would be accepted. In Section F, Information about the Job Location and Development (JLD) Program, the number of students who participated in the JLD Program (item 21) was overstated by 15, and the total earnings of the students (item 22) was understated by $11,807 because Career Services provided estimates when the information was requested by the financial aid office.

The Division of State Audit reviewed the 2001-2002 FISAP as a part of the prior-year audit and discussed the necessary changes with university staff. However, the university did not report the audited totals for the 2001-2002 academic year FISAP report when the revised report was submitted in December 2002. In addition, the university could not provide supporting documentation for the revisions made to the FISAP for tuition and fees, Federal Pell Grant expenditures, state grants and scholarships, and cash on hand. The tables for the Application, Part II, Section F, and the Fiscal Operations Report, Part VI, Section A, were also changed with no support provided. The Director of Finance and Accounting stated that the previous Director of Financial Aid submitted the changes and he is unaware of how she calculated the numbers or which reports were used. No one else reviewed the revised report and reconciled the numbers.

If the Financial Aid Office submits incorrect and unverifiable data on the FISAP, the allocation of funds from the Department of Education could be affected.

Recommendation

The Director of Financial Aid should ensure that information reported on the FISAP is accurate and verifiable, and should properly submit any changes to the FISAP by the deadline and maintain supporting documentation for those changes.

Management's Comment

We concur with the finding and recommendation. September 2003 was the first submission by our new Director of Financial Aid. Corrections were submitted in December 2003. Additional preparation, compilation, and review by the Director will continue to be exercised to ensure the accurate, verifiable, timely, and documented annual submission of the FISAP information.

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT
SUITE 1500
JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-0264
PHONE (615) 401-7897
FAX (615) 532-2765

Independent Auditor's Report

November 13, 2003

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

Dear Mr. Morgan:

We have audited the accompanying statements 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, 2003, and June 30, 2002, and the related statements of revenues, expenses, and changes in net assets and cash flows for the years 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 audits.

We conducted our audits 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 audits provide 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, 2003, and June 30, 2002, and the revenues, expenses, and changes in net assets and the cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 12, 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*. 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 36 through 46 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 13, 2003, 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., CPA,
Director

AAH/th

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, 2003, with comparative information presented for 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.

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)

	2003	2002
Assets:		
Current assets	37,805	32,627
Capital assets, net	153,624	150,775
Other assets	21,647	21,748
Total assets	**213,076**	**205,150**
Liabilities:		
Current liabilities	21,162	20,843
Noncurrent liabilities	35,877	28,347
Total liabilities	**57,039**	**49,190**
Net assets:		
Invested in capital assets, net of related debt	123,734	123,908
Restricted - nonexpendable	62	62
Restricted - expendable	7,721	7697
Unrestricted	24,520	24,293
Total net assets	**156,037**	**155,960**

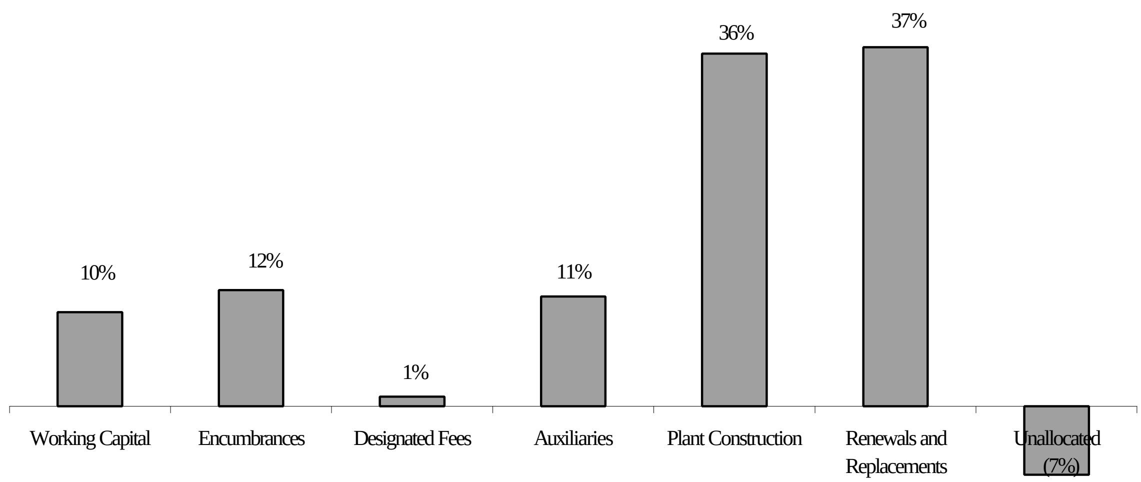
- Current assets increased 16% due to a shift in investments from long-term to short-term due to the decline in interest rates. Investments for the foundation increased $2.5 million as a result of fundraising and state matching funds from the State Consent Decree.

- Current liabilities increased 2% due to the increase in funds held in deposit for the TSU Foundation as a result of fundraising and state matching funds from the State Consent Decree.

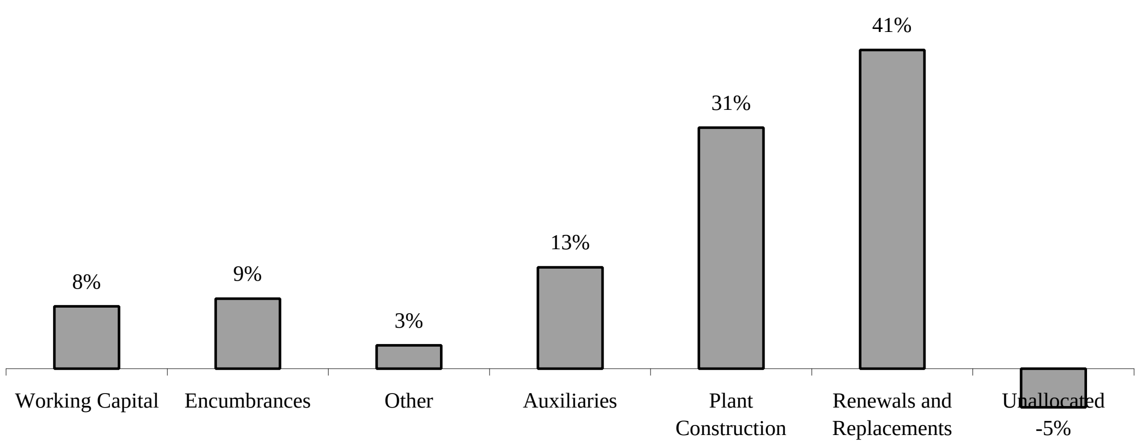
- Noncurrent liabilities increased 27% due in part to a $3 million dollar increase in bonds payable that included funds for North Campus Improvements and TSU Housing Phase II. The current portion of long-term liabilities decreased $2.4 million. The compensated absences liability increased $1.1 million due to a change in reports used to calculate the balance.

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

Urestricted Net Assets 2003



Unrestricted Net Assets 2002



- University purchases were delayed due to the uncertainty of the funding for the next fiscal year. The purchases were initiated later in the fiscal year which increased the encumbrances at June 30, 2003.

- The reserve for plant construction increased due to a transfer of $1.7 million from debt reserves.

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

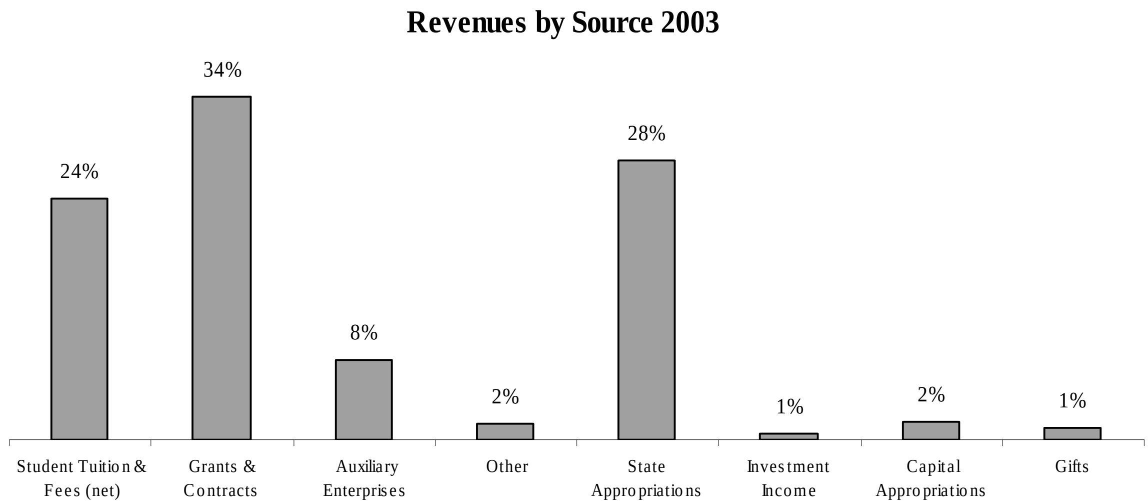
The Statement of Revenues, Expenses, and Changes in Net Assets presents the operating results of the university, as well as the nonoperating revenues and expenses. Annual state appropriations, while budgeted for operations, are considered nonoperating revenues according to generally accepted accounting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

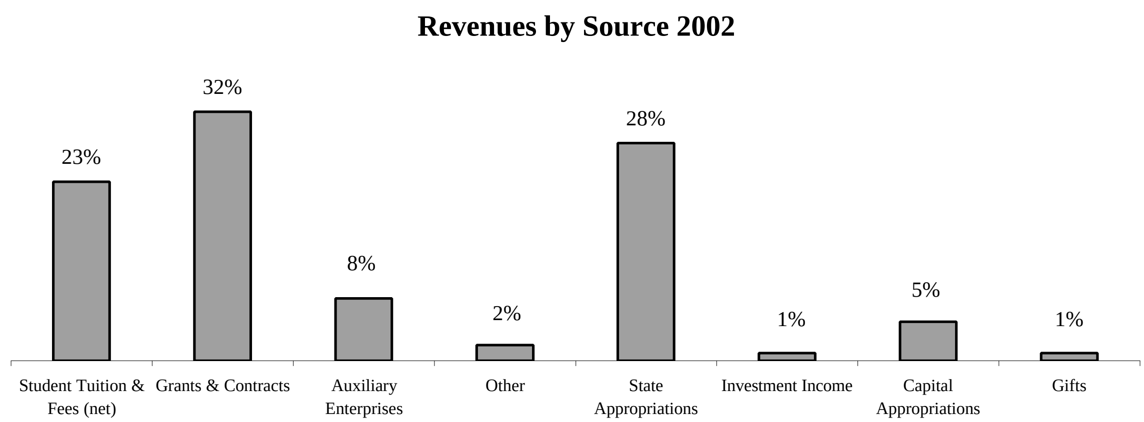
Statement of Revenues, Expenses, and Changes in Net Assets
(in thousands of dollars)

	2003	2002
Operating revenues:		
Net tuition and fees	34,591	31,318
Grants and contracts	47,997	44,555
Auxiliary	12,065	11,022
Other	2,326	2,105
Total operating revenues	**96,979**	**89,000**
Operating expenses	138,049	129,674
Operating loss	**(41,070)**	**(40,674)**
Nonoperating revenues and expenses:		
State appropriations	39,040	38,530
Gifts	1,146	1,528
Investment income	897	1,048
Other revenues and expenses	(2,985)	(30,602)
Total nonoperating revenues and expenses	**38,098**	**10,504**
Loss before other revenues, expenses, gains, or losses	**(2,972)**	**(30,170)**
Other revenues, expenses, gains, or losses:		
Capital appropriations	2,607	6,810
Capital grants and gifts	442	5
Total other revenues, expenses, gains, or losses	**3,049**	**6,815**
Increase (decrease) in net assets	77	(23,355)
Net assets at beginning of year, as originally reported	155,960	263,656
Cumulative effect of changes in accounting principle	-	(84,341)
Net assets at beginning of year, as restated	**155,960**	**179,315**
Net assets at end of year	**156,037**	**155,960**

Revenues

The following is a graphic illustration of revenues by source (both operating and nonoperating), which were used to fund the university's operating activities for the years ended June 30, 2003, and June 30, 2002.





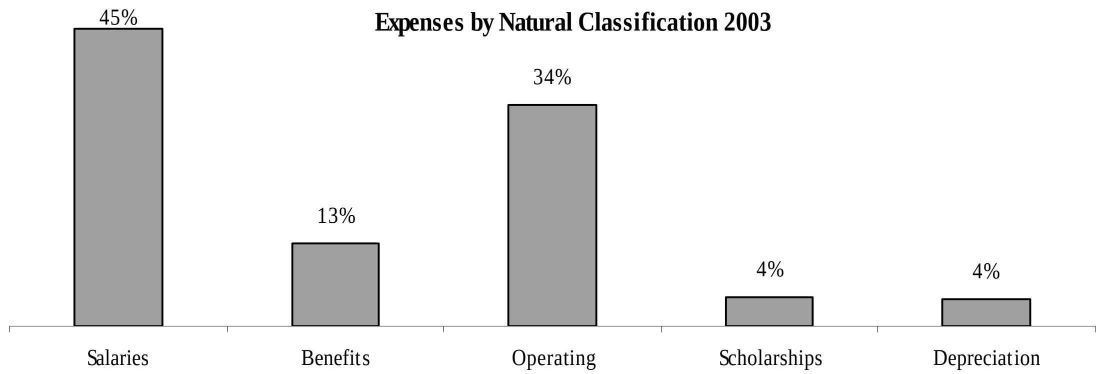
- The revenue from capital appropriations decreased $4 million due to a change in the adjustment for unexpended state appropriations for capital projects.

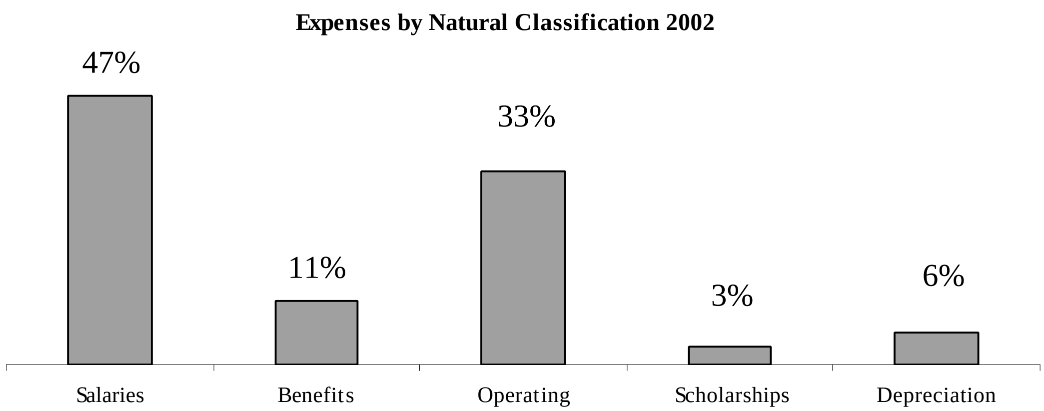
Expenses

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

Natural Classification

	2003	2002
Salaries	62,567	60,546
Benefits	17,405	14,367
Operating	46,350	43,378
Scholarships	5,964	4,068
Depreciation	5,763	7,316
Total	**138,049**	**129,675**





- The percentage for benefits increased as a result of an increase in the liability for compensated absences and health care premiums.

- The percentage of expenses for depreciation decreased with the audit adjustment of the useful life for certain categories of equipment, buildings, and improvements other than buildings.

Program Classification

	2003	2002
Instruction	55,729	50,995
Research	13,259	12,945
Public service	6,940	6,693
Academic support	9,441	6,926
Student services	12,566	10,811
Institutional support	12,650	11,254
Maintenance and operation	8,110	10,273
Scholarships	2,805	3,172
Auxiliary	10,786	9,290
Depreciation	5,763	7,316
Total	**138,049**	**129,675**

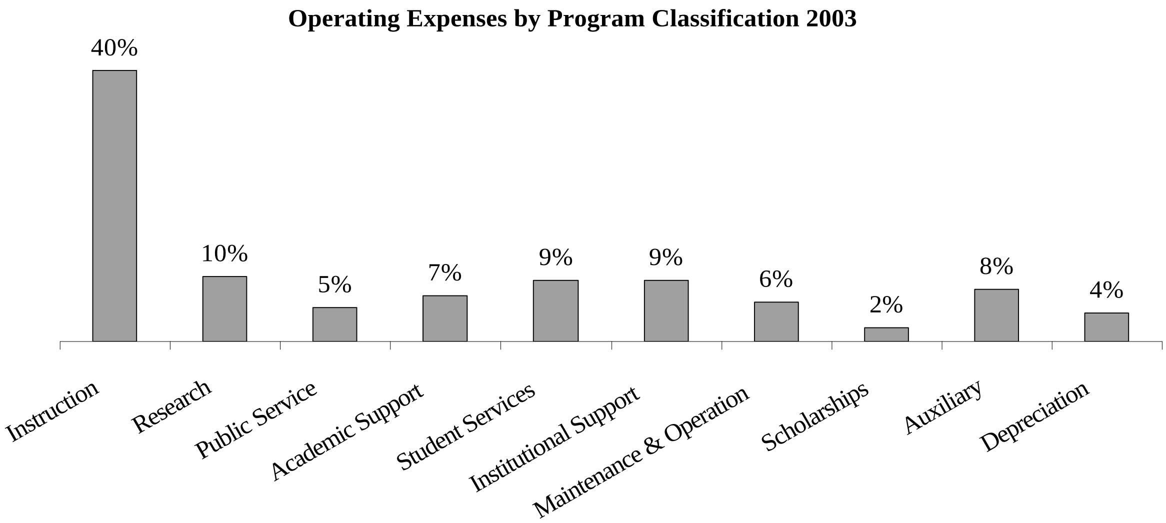
- The percentage of increase in academic support is a result of increased expenses for the library and academic computing and an increase in compensated absences.

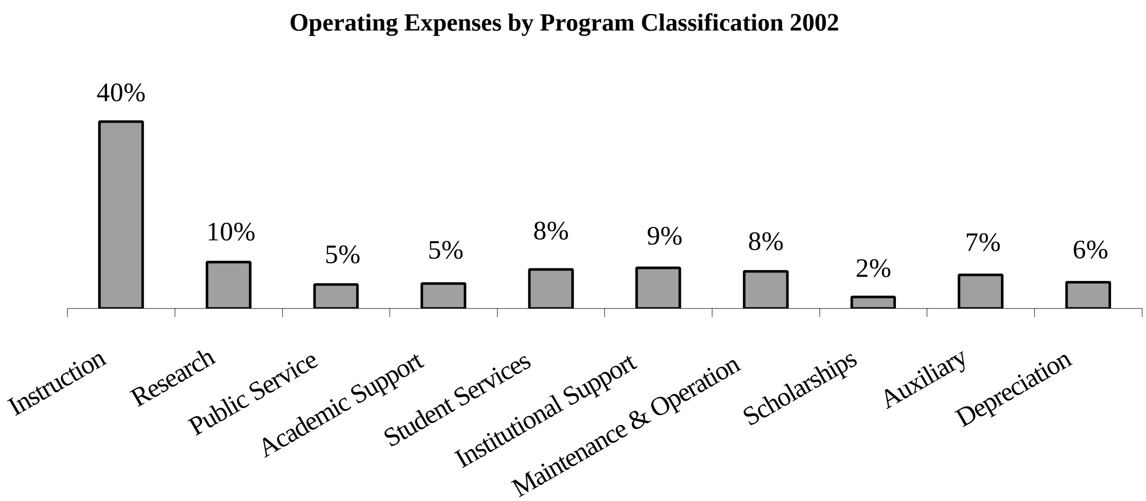
- Student services expenses increased for athletics, and compensated absences increased.

- Expenses for the write off of uncollectible student receivables and the police department and an increase in compensated absences make up the increase in institutional support.

- Noncapital improvements to the campus facilities decreased in 2003 resulting in a decrease in maintenance and operation expenses.

- An increase in expenses for the food service and telecommunications and an increase in compensated absences resulted in an increase for auxiliary operations for 2003.





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)

	2003	2002
Cash provided (used) by:		
Operating activities	(34,469)	(35,359)
Noncapital financing activities	43,343	40,088
Capital and related financing activities	(5,228)	(3,932)
Investing activities	(633)	998
Net increase in cash	**3,013**	**1,795**
Cash, beginning of year	**35,648**	**33,853**
Cash, end of year	**38,661**	**35,648**

- The university's cash and cash equivalents increased approximately $3 million from the prior fiscal year improving the university's liquidity.

- The cash used by operating activities was offset with the increase in tuition and fees and the increase in operating grants and contracts.

- The cash used by capital and related financing activities reduced the debt for the TSU Housing Phase II project bond issue by $1.9 million.

- Cash used for investing activities increased $2.5 million as a result of fundraising and state matching funds from the State Consent Decree.

Capital Assets and Debt Administration

Capital Assets

At June 30, 2003, the university had $153,624,257.71 invested in capital assets, net of accumulated depreciation of $96,485,257.84. Depreciation charges totaled $5,762,902.60 for the current fiscal year. Details of these assets are shown below.

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

	2003	2002
Land	9,525	9,525
Land improvements and infrastructure	16,618	17,927
Buildings	86,527	90,004
Equipment	5,276	5,124
Library holdings	4,362	2,984
Projects in progress	31,316	25,211
Net capital assets	**153,624**	**150,775**

- During the fiscal year, no projects in progress additions were transferred to buildings; however, depreciation expense for buildings totaled $3.5 million.

- During the fiscal year, $164,000 for current fund additions was transferred to land improvements; however, depreciation expense for land improvements totaled $1.5 million.

- The library is fully automated with the purchase of on-line databases, which constituted the 46% increase from 2002.

- Two projects, which were begun in 2002, had increased expenses. The projects are the Performing Arts Building and North Campus Improvements, Phase III.

- During the next fiscal year, the Performing Arts Building and North Campus Improvements projects will be near completion. The Performing Arts Building is being funded by state appropriations. The North Campus Improvements are being funded through Tennessee State School Bond Authority bonds.

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

Debt

At June 30, 2003, the university had $29,890,449.09 in debt outstanding. The total debt outstanding as of June 30, 2002, was $26,866,431.60. This debt is in bonds issued through the Tennessee State School Bond Authority. More detailed information about the university's long-term liabilities is presented in Note 7 to the financial statements.

- There was a supplemental agreement in 2003 which reduced the debt for the TSU Housing Phase II project by $1.9 million.

Economic Factors That Will Affect the Future

The Tennessee Board of Regents approved a 14% increase in maintenance and tuition fees for the 2003-04 academic year. The cost for students to attend the university exceeds the amount of financial aid available per student. This requires students to resort to alternative means of financing the cost of attending the university. The impact that will have on enrollment is unknown. The State of Tennessee budget included a nine percent reduction in base funding for most state agencies and departments, including the university. The university is not aware of any other factors that will have a significant affect on the financial position or results of operations.

Requests for Information

This financial report is designed to provide a general overview of the institution's finances for all those with an interest in the university's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be directed to:

Mr. H. Clay Harkleroad
Vice President for Business and Finance
3500 John A. Merritt Boulevard
Nashville, Tennessee 37209

Exhibit A

TENNESSEE BOARD OF REGENTS
TENNESSEE STATE UNIVERSITY
STATEMENTS OF NET ASSETS
JUNE 30, 2003, AND JUNE 30, 2002

	June 30, 2003	June 30, 2002
ASSETS		
Current assets:		
Cash and cash equivalents (Notes 2 and 3)	$ 19,824,195.28	$ 17,306,864.04
Short-term investments (Notes 3 and 4)	5,266,119.28	3,095,490.80
Accounts, notes, and grants receivable (net) (Note 5)	11,302,266.75	10,824,890.67
Inventories (at lower of cost or market)	39,574.93	39,134.05
Accrued interest receivable	1,353,745.74	1,331,920.19
Other assets	18,982.18	29,227.00
Total current assets	37,804,884.16	32,627,526.75
Noncurrent assets:		
Cash and cash equivalents (Notes 2 and 3)	18,836,910.61	18,341,589.75
Investments (Notes 3 and 4)	994,907.00	1,656,844.30
Accounts, notes, and grants receivable (net) (Note 5)	1,814,957.90	1,749,622.45
Capital assets (net) (Note 6)	153,624,257.71	150,774,757.73
Total noncurrent assets	175,271,033.22	172,522,814.23
Total assets	213,075,917.38	205,150,340.98
LIABILITIES		
Current liabilities:		
Accounts payable	2,187,802.77	1,770,567.30
Accrued liabilities	6,374,360.44	6,236,161.63
Due to grantors (Note 7)	60,482.01	101,950.26
Student deposits	867,007.91	754,802.91
Deferred revenue	2,214,858.28	1,955,363.39
Compensated absences (Note 7)	820,338.29	1,681,819.31
Accrued interest payable	255,728.81	284,901.87
Long-term liabilities, current portion (Note 7)	671,603.60	3,103,348.36
Deposits held in custody for others	7,362,913.18	4,459,411.06
Other liabilities	346,519.97	495,285.50
Total current liabilities	21,161,615.26	20,843,611.59
Noncurrent liabilities:		
Compensated absences (Note 7)	4,098,056.74	2,148,925.06
Long-term liabilities (Note 7)	29,218,845.49	23,763,083.24
Due to grantors (Note 7)	2,560,130.99	2,434,975.79
Total noncurrent liabilities	35,877,033.22	28,346,984.09
Total liabilities	57,038,648.48	49,190,595.68
NET ASSETS		
Invested in capital assets, net of related debt	123,733,808.62	123,908,326.13
Restricted for:		
Nonexpendable:		
Scholarships and fellowships	61,671.53	61,452.07
Expendable:		
Scholarships and fellowships	39,019.81	42,694.53
Research	708,751.60	719,596.75
Instructional department uses	3,722,392.24	3,697,326.03
Loans	844,052.42	845,812.03
Other	2,407,331.17	2,391,530.75
Unrestricted (Note 8)	24,520,241.51	24,293,007.01
Total net assets	$ 156,037,268.90	$ 155,959,745.30

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

Exhibit B

TENNESSEE BOARD OF REGENTS
TENNESSEE STATE UNIVERSITY
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2003, AND JUNE 30, 2002

	Year Ended June 30, 2003	Year Ended June 30, 2002
REVENUES		
Operating revenues:		
Student tuition and fees (net of scholarship allowances of $12,735,090.24 for the year ended June 30, 2003, and $11,704,997.54 for the year ended June 30, 2002)	$ 34,590,616.61	$ 31,317,880.46
Governmental grants and contracts	47,997,041.67	44,554,780.70
Sales and services of educational departments	2,051,953.93	1,756,175.56
Auxiliary enterprises:		
Residential life (net of scholarship allowances of $936,582.46 for the year ended June 30, 2003, and $1,155,565.72 for the year ended June 30, 2002; all residential life revenues are used as security for revenue bonds; see Note 7)	7,001,533.19	6,500,444.01
Bookstore (all bookstore revenues are used as security for revenue bonds; see Note 7)	435,322.12	275,700.75
Food service	3,879,263.74	3,768,308.22
Other auxiliaries	748,477.16	477,790.34
Other operating revenues	274,466.09	349,088.23
Total operating revenues	96,978,674.51	89,000,168.27
EXPENSES		
Operating expenses (Note 16):		
Salaries and wages	62,566,781.52	60,546,310.19
Benefits	17,405,098.22	14,366,937.43
Utilities, supplies, and other services	46,350,458.58	43,378,030.92
Scholarships and fellowships	5,964,214.02	4,067,722.98
Depreciation expense	5,762,902.60	7,315,610.09
Total operating expenses	138,049,454.94	129,674,611.61
Operating loss	(41,070,780.43)	(40,674,443.34)
NONOPERATING REVENUES (EXPENSES)		
State appropriations	39,040,110.00	38,530,600.00
Gifts	1,146,282.79	1,527,936.22
Investment income (net of investment expense of $163,128.03 for the year ended June 30, 2002)	897,244.58	1,047,610.79
Interest on capital asset-related debt	(1,654,702.69)	(1,123,726.08)
Bond issuance costs	-	(99,080.90)
Other nonoperating revenues (expenses)	(1,330,435.92)	(29,379,586.57)
Net nonoperating revenues	38,098,498.76	10,503,753.46
Loss before other revenues, expenses, gains, or losses	(2,972,281.67)	(30,170,689.88)
Capital appropriations	2,607,250.02	6,810,708.71
Capital grants and gifts	442,555.25	5,000.00
Total other revenues	3,049,805.27	6,815,708.71
Increase (decrease) in net assets	77,523.60	(23,354,981.17)
NET ASSETS		
Net assets - beginning of year, as originally reported	155,959,745.30	263,655,537.74
Cumulative effects of changes in accounting principle (Note 12)		
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	155,959,745.30	179,314,726.47
Net assets - end of year	$ 156,037,268.90	$ 155,959,745.30

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

Exhibit C

TENNESSEE BOARD OF REGENTS
TENNESSEE STATE UNIVERSITY
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2003, AND JUNE 30, 2002

	Year Ended June 30, 2003	Year Ended June 30, 2002
CASH FLOWS FROM OPERATING ACTIVITIES		
Tuition and fees	$ 34,291,244.12	$ 31,962,274.63
Grants and contracts	48,028,441.80	41,301,606.70
Sales and services of educational activities	1,872,438.24	1,807,000.58
Payments to suppliers and vendors	(46,247,436.76)	(43,569,342.11)
Payments to employees	(61,654,635.60)	(59,982,659.83)
Payments for benefits	(17,231,356.14)	(14,276,769.37)
Payments for scholarships and fellowships	(5,964,214.02)	(4,067,722.98)
Loans issued to students and employees	(424,934.95)	(626,564.75)
Collection of loans from students and employees	483,085.13	613,807.16
Interest earned on loans to students	112,299.78	122,732.59
Auxiliary enterprise charges:		
Residence halls	6,928,366.19	6,475,805.28
Bookstore	435,322.12	275,700.75
Food services	3,879,263.74	3,768,308.22
Other auxiliaries	748,369.18	487,896.80
Other receipts (payments)	274,466.09	349,088.23
Net cash used by operating activities	(34,469,281.08)	(35,358,838.10)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State appropriations	39,305,710.00	38,103,800.00
Gifts and grants received for other than capital or endowment purposes	183,429.93	1,554,186.22
Federal student loan receipts	37,311,877.00	28,497,461.00
Federal student loan disbursements	(35,966,252.00)	(29,967,757.00)
Changes in deposits held for others	2,903,502.12	1,760,524.90
Other noncapital financing receipts (payments)	(395,091.24)	139,773.71
Net cash provided by noncapital financing activities	43,343,175.81	40,087,988.83
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from capital debt	6,224,656.73	7,309,830.94
Capital - state appropriations	2,607,250.02	6,774,196.28
Capital grants and gifts received	442,555.25	-
Purchases of capital assets and construction	(9,496,655.85)	(15,290,550.70)
Principal paid on capital debt and lease	(1,422,760.80)	(1,487,230.28)
Interest paid on capital debt and lease	(1,683,875.75)	(1,081,905.30)
Bond issue costs paid on new debt issue	-	(99,080.90)
Other capital and related financing receipts (payments)	(1,899,140.08)	(57,485.34)
Net cash used by capital and related financing activities	(5,227,970.48)	(3,932,225.30)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments	4,363,339.41	2,559,153.84
Income on investments	875,419.03	776,734.59
Purchases of investments	(5,872,030.59)	(2,337,486.97)
Net cash provided (used) by investing activities	(633,272.15)	998,401.46
Net increase in cash and cash equivalents	3,012,652.10	1,795,326.89
Cash and cash equivalents - beginning of year	35,648,453.79	33,853,126.90
Cash and cash equivalents - end of year	$ 38,661,105.89	$ 35,648,453.79

TENNESSEE BOARD OF REGENTS
TENNESSEE STATE UNIVERSITY
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2003, AND JUNE 30, 2002

	Year Ended June 30, 2003	Year Ended June 30, 2002
Reconciliation of operating loss to net cash used by operating activities:		
Operating loss	$ (41,070,780.43)	$ (40,674,443.34)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation expense	5,762,902.60	7,315,610.09
Change in assets and liabilities:		
Receivables, net	(1,122,883.86)	3,646,549.93
Inventories	(440.88)	1,109.88
Accounts payable	420,646.65	(1,042,289.86)
Accrued liabilities	81,924.29	(351,624.94)
Deferred revenue	259,494.89	322,046.34
Deposits	112,205.00	117,088.71
Compensated absences	1,087,650.66	192,958.68
Loans to students and employees	-	(4,885,843.59)
Net cash used by operating activities	$ (34,469,281.08)	$ (35,358,838.10)
Noncash transactions		
Unrealized gain/loss on investments	$ 661,542.23	$ -

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, 2003, and 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.

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, and $50,000 is used for infrastructure. Equipment is capitalized when the unit acquisition cost is $5,000 or greater. The capitalization threshold for additions and improvements to buildings and land is set at $50,000.

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.

<u>Expendable restricted net assets</u> – 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.

<u>Unrestricted net assets</u> – 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.

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, 2003, cash and cash equivalents consisted of $8,932,551.57 in bank accounts, $4,050.00 of petty cash on hand, a $269,529.09 certificate of deposit, $28,982,494.39 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer, $68,777.82 in LGIP deposits for capital projects, and $403,703.02 in capital management account money funds. 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, $27,633,406.23 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer, $68,777.82 in LGIP deposits for capital projects, and $727,193.84 in capital management account money funds.

LGIP deposits for 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.

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, 2003, the carrying amount of the university's deposits in financial institutions participating in the collateral pool was $8,993,608.57, and the bank balance including accrued interest was $11,778,716.37. The bank balance was insured. 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.

At June 30, 2003, the carrying amount of the university's deposits was $9,263,137.66, and the bank balance including accrued interest was $12,048,410.17. Of the bank balance, $11,878,716.37 was category 1, and $169,693.80 was category 2.

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 unregistered investments for which the securities are held by the counterparties' trust department or agent in the university's/foundation's name.

	June 30, 2003	June 30, 2002
Category 2:		
University:		
U.S. government securities	$ 933,850.00	$1,595,392.23
Foundation:		
U.S. government securities	963,770.62	350,699.80
Corporate bonds	1,264,773.50	1,167,414.64
Corporate stocks	1,922,764.12	513,898.75
Mortgage backed securities	160,175.60	-
Investments not susceptible to credit risk categorization:		
Foundation mutual funds	954,635.44	788,428.87
University certificates of deposit classified as investments	61,057.00	336, 500. 81
Total	$ 6,261,026.28	$ 4,752,335.10

NOTE 5. RECEIVABLES

Receivables included the following:

	June 30, 2003	June 30, 2002
Student accounts receivable	$ 3,943,936.67	$ 2,830,721.25
Grants receivable	6,820,936.30	7,955,934.83
Notes receivable	457,319.02	464,645.23
Pledges receivable	33,000.00	78,000.00
State appropriation receivable	197,712.43	-
Other receivables	1,852,199.79	1,066,474.35
Subtotal	13,305,104.21	12,395,775.66
Less allowance for doubtful accounts	1,987,179.52	1,539,695.92
Total receivables	$11,317,924.69	$10,856,079.74

Pledges receivable are promises of private donations that are reported as accounts receivable and revenue. At June 30, 2003, and June 30, 2002, all were considered to be collectible.

Federal Perkins Loan Program funds included the following:

	June 30, 2003	June 30, 2002
Perkins loans receivable	$14,813,680.34	$14,392,326.34
Less allowance for doubtful accounts	13,014,380.38	12,673,892.96
Total	$ 1,799,299.96	$ 1,718,433.38

NOTE 6. CAPITAL ASSETS

Capital asset activity for the university for the year ended June 30, 2003, was as follows:

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$ 9,525,009.24	$ -	$ -	$ -	$ 9,525,009.24
Land improvements and infrastructure	39,220,866.25	164,327.67	-	-	39,385,193.92
Buildings	142,621,218.55	-	-	-	142,621,218.55
Equipment	19,398,372.70	1,663,721.87	-	706,148.95	20,355,945.62
Library holdings	5,520,382.79	1,571,879.70	-	186,504.32	6,905,758.17
Projects in progress	25,211,263.44	6,105,126.61	-	-	31,316,390.05
Total	241,497,112.97	9,505,055.85	-	892,653.27	250,109,515.55
Less accum. depreciation:					
Land improvements and infrastructure	21,293,842.16	1,473,105.80	-	-	22,766,947.96
Buildings	52,617,158.47	3,476,976.71	-	-	56,094,135.18
Equipment	14,274,339.80	805,897.04	-	-	15,080,236.84
Library holdings	2,537,014.81	6,923.05	-	-	2,543,937.86
Total accum. depreciation	90,722,355.24	5,762,902.60	-	-	96,485,257.84
Capital assets, net	$150,774,757.73	$3,742,153.25	$ -	$892,653.27	$153,624,257.71

Capital asset activity for the university 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, 2003, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Payables:					
Bonds	$26,866,431.60	$ 6,337,114.31	$3,313,096.82	$29,890,449.09	$671,603.60
Other liabilities:					
Compensated absences	3,830,744.37	1,985,980.66	898,330.00	4,918,395.03	820,338.29
Due to grantors	2,536,926.05	153,852.66	70,165.71	2,620,613.00	60,482.01
Subtotal	6,367,670.42	2,139,833.32	968,495.71	7,539,008.03	880,820.30
Total long-term liabilities	$33,234,102.02	$8,476,947.63	$4,281,592.53	$37,429,457.12	$1,552,423.90

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 3.65% to 7.00% 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, 2003, and $996,680.00 at June 30, 2002. Unexpended debt proceeds were $787,398.11 at June 30, 2003, and $7,012,054.86 at June 30, 2002.

Debt service requirements to maturity for bonds payable at June 30, 2003, are as follows:

Year Ending June 30	Principal	Interest	Total
2004	$ 671,603.60	$ 1,551,168.95	$ 2,222,772.55
2005	1,436,577.18	1,509,219.20	2,945,796.38
2006	988,244.73	1,464,960.87	2,453,205.60
2007	1,041,985.46	1,417,641.76	2,459,627.22

2008	1,052,922.50	1,394,921.68	2,447,844.18
2009-2013	6,363,174.75	6,057,419.32	12,420,594.07
2014-2018	7,148,168.80	4,067,364.70	11,215,533.50
2019-2023	4,341,143.27	2,438,636.99	6,779,780.26
2024-2028	4,986,361.85	1,271,361.86	6,257,723.71
2029-2032	1,860,266.95	250,633.28	2,110,900.23
	$29,890,449.09	$21,423,328.61	$51,313,777.70

NOTE 8. UNRESTRICTED NET ASSETS

Unrestricted net assets include funds that have been designated or reserved for specific purposes. The unrestricted net assets are composed of the following:

	June 30, 2003	June 30, 2002
Working capital	$ 2,373,545.95	$ 1,966,587.25
Encumbrances	2,929,548.67	2,138,783.83
Designated fees	239,487.00	-
Auxiliaries	2,766,203.68	3,110,055.51
Plant construction	8,890,914.26	7,498,380.90
Renewal and replacement of equipment	9,049,597.19	9,920,888.88
Debt retirement	-	777,249.33
Unreserved/undesignated	(1,729,055.24)	(1,118,938.69)
Total	$24,520,241.51	$24,293,007.01

NOTE 9. ENDOWMENTS

If a donor has not provided specific instructions to the university, state law permits the university to authorize for expenditure the earnings, of the investments of endowment funds. When administering its power to spend these earnings, the university is required to consider the university's long-term and short-term needs, present and anticipated financial requirements, expected return on its investments, price-level trends, and general economic conditions. Any earnings spent are required to be spent for the purposes for which the endowment was established.

The university chooses to spend only a portion of the investment income each year. Under the spending plan established by the university, a scholarship is awarded to a student whose residence is in the county specified by the donor, if it has been authorized for expenditure. The remaining amount, if any, is retained to be used in future years when the amount computed using the spending plan exceeds the investment income. At June 30, 2003, investment income of $1,148.50 is available to be spent. This amount is included in restricted net assets expendable for instructional department uses.

NOTE 10. 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 7.29% 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, 2003, 2002, and 2001 were $1,875,558.81, $1,543,054.62, and $1,503,727.42. 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 currently required to contribute 7% 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, 2003, were $70,842.67, which consisted of $37,126.04 from the university and $33,716.63 from the employees. Contributions 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 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 $3,088,789.29 for the year ended June 30, 2003, and $2,825,202.04 for the year ended June 30, 2002. Contributions met the requirements for each year.

NOTE 11. 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 12. 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 13. 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 had no claims filed with the commercial insurer. A designation for casualty losses in the amount of $3.271 million for incurred losses at June 30, 2003, was established in the state's general fund to provide for any property losses not covered by the commercial insurance.

At June 30, 2003, the scheduled coverage for the university was $243,374,100 for buildings and $48,017,100 for contents. 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 14. 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 $27,335,430.02 at June 30, 2003, and $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 $691,328.56 and for personal property were $80,573.07 for the year ended June 30, 2003. Comparative amounts for the year ended June 30, 2002, were $437,703.17 and $232,064.21. All operating leases are cancelable at the lessee's option.

Construction in Progress - At June 30, 2003, outstanding commitments under construction contracts totaled $1,202,765.42 for the following projects: Boyd Hall renovation, new Performing Arts Building, ADA improvements, utility systems and tunnel renovation, Agriculture Extension I.T., Power Plant Bag House replacement, Avon Williams campus improvements, Elliott Hall preservation, and 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 15. CHAIRS OF EXCELLENCE

The university had $3,069,617.94 on deposit at June 30, 2003, and $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 16. NATURAL CLASSIFICATIONS WITH FUNCTIONAL CLASSIFICATIONS

The university's operating expenses by functional classification for the year ended June 30, 2003, are as follows:

	Natural Classification					
Functional Classification	Salaries	Benefits	Other Operating	Scholarships	Depreciation	Total
Instruction	$30,868,442.90	$ 7,698,603.10	$15,185,628.59	$ 1,976,087.81	$ -	$ 55,728,762.40
Research	5,812,998.70	1,522,860.07	5,003,157.35	920,162.51	-	13,259,178.63
Public service	3,951,316.06	1,334,277.93	1,531,363.51	122,918.55	-	6,939,876.05
Academic support	4,497,198.78	1,285,843.96	3,639,022.70	19,333.20	-	9,441,398.64
Student services	5,217,791.74	1,567,606.38	4,169,982.76	1,610,684.95	-	12,566,065.83
Institutional support	7,722,972.71	2,546,152.69	2,362,865.89	17,928.00	-	12,649,919.29
Operation & maint.	2,697,140.21	972,393.58	4,440,327.36	-	-	8,109,861.15
Scholar. & fellow.	19,219.40	(24,241.25)	1,722,476.83	1,087,687.72	-	2,805,142.70
Auxiliary	1,779,701.02	501,601.76	8,295,633.59	209,411.28	-	10,786,347.65
Depreciation	-	-	-	-	5,762,902.60	5,762,902.60
Total	$62,566,781.52	$17,405,098.22	$46,350,458.58	$ 5,964,214.02	$5,762,902.60	$ 138,049,454.94

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

Functional Classification	Salaries	Benefits	Natural Classification Other 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	,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

NOTE 17. PRIOR-YEAR RESTATEMENT

Due to changes in presentation made by the university for the year ended June 30, 2003, some reclassifications were made in the prior-year financial statements for comparative purposes. The LGIP deposit – capital projects was reclassified as noncurrent cash and cash equivalents. Also, the note disclosure for unrestricted net assets was changed to show all of the components rather than just the designated amounts.