AUDIT REPORT

Tennessee Board of Regents
Volunteer State Community College

For the Years Ended
June 30, 2004, and June 30, 2003

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
Department of Audit
Division of State Audit

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STATE OF TENNESSEE

COMPTROLLER OF THE TREASURY

State Capitol
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John G. Morgan
Comptroller

September 22, 2005

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. Warren Nichols, President
Volunteer State Community College
1480 Nashville Pike
Gallatin, Tennessee 37066

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Tennessee Board of Regents, Volunteer State Community College, for the years ended June 30, 2004, and June 30, 2003. You will note from the independent auditor's report that unqualified opinions were given on the fairness of the presentation of the financial statements.

Consideration of internal control over financial reporting and tests of compliance resulted in no audit findings.

Sincerely,

John G. Morgan
Comptroller of the Treasury

JGM/th
05/073

State of Tennessee

Audit Highlights

Comptroller of the Treasury — Division of State Audit

Financial and Compliance Audit
Volunteer State Community College
For the Years Ended June 30, 2004, and June 30, 2003

AUDIT OBJECTIVES

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

AUDIT FINDINGS

The audit report contains no findings.

OPINIONS ON THE FINANCIAL STATEMENTS

The opinions on the financial statements are unqualified.

Audit Report
Tennessee Board of Regents
Volunteer State Community College
For the Years Ended June 30, 2004, and June 30, 2003

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Tennessee Board of Regents
Volunteer State Community College
For the Years Ended June 30, 2004, and June 30, 2003

INTRODUCTION

POST-AUDIT AUTHORITY

This is a report on the financial and compliance audit of the Tennessee Board of Regents, Volunteer State Community College. 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

Volunteer State Community College was approved by the State Board of Education as one of Tennessee's ten community colleges in 1969. The college moved to its present 100-acre campus in 1972. In June 1973, Volunteer State Community College graduated its first class.

In January 1984, Volunteer State Community College became the lead institution for Tennessee Technology Center at Hartsville and Tennessee Technology Center at Livingston. Under the lead institution agreement, Volunteer State Community College performs the accounting and reporting functions for these centers.

The college currently offers the Associate of Arts Degree, the Associate of Science Degree, and the Associate of Applied Science Degree.

ORGANIZATION

The governance of Volunteer State Community College 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 college 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, 2004, 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 years ended June 30, 2004, and June 30, 2003. Volunteer State Community College 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 college's internal control over financial reporting to determine auditing procedures for the purpose of expressing opinions on the financial statements;
2. to determine compliance with certain provisions of laws, regulations, contracts, and grant agreements;
3. to determine the fairness of the presentation of the financial statements; and
4. to recommend appropriate actions to correct any deficiencies.

PRIOR AUDIT FINDINGS

There were no findings in the prior audit report.

OBSERVATIONS AND COMMENTS

FRAUD CONSIDERATIONS

Statement on Auditing Standards No. 99, *Consideration of Fraud in a Financial Statement Audit*, promulgated by the American Institute of Certified Public Accountants, requires auditors to specifically assess the risk of material misstatement of an audited entity's financial statements due to fraud. The standard also restates the obvious premise that management, and not the auditors, is primarily responsible for preventing and detecting fraud in its own entity. Management's responsibility is fulfilled in part when it takes appropriate steps to assess the risk of fraud within the entity and to implement adequate internal controls to address the results of those risk assessments.

During our audit, we discussed these responsibilities with management and how management might approach meeting them. We also increased the breadth and depth of our inquiries of management and others in the entity as we deemed appropriate. We obtained formal assurances from top management that management had reviewed the entity's policies and procedures to ensure that they are properly designed to prevent and detect fraud and that management had made changes to the policies and procedures where appropriate. Top management further assured us that all staff had been advised to promptly alert management of all allegations of fraud, suspected fraud, or detected fraud and to be totally candid in all communications with the auditors. All levels of management assured us there were no known instances or allegations of fraud that were not disclosed to us.

TECHNOLOGY CENTERS

Volunteer State Community College serves as the lead institution under agreements with the Tennessee Technology Center at Hartsville and the Tennessee Technology Center at Livingston. Under these agreements, Volunteer State Community College performs the accounting and reporting functions for the centers. The chief administrative officer of each center is the director, who is assisted and advised by members of the faculty and administrative staff. Each director is responsible to the Chancellor of the Tennessee Board of Regents.

RESULTS OF THE AUDIT

AUDIT CONCLUSIONS

Internal Control

As part of the audit of the college's financial statements for the years ended June 30, 2004, and June 30, 2003, we considered internal control over financial reporting to determine auditing procedures for the purpose of expressing opinions 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*.

Fairness of Financial Statement Presentation

The Division of State Audit has rendered unqualified opinions on the college's financial statements.

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

June 27, 2005

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

Dear Mr. Morgan:

We have audited the financial statements of Volunteer State Community College, an institution of the Tennessee Board of Regents, which is a component unit of the State of Tennessee, and its discretely presented component unit as of and for the years ended June 30, 2004, and June 30, 2003, and have issued our report thereon dated June 27, 2005. 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. During the year ended June 30, 2004, the college implemented GASB Statement 39, *Determining Whether Certain Organizations Are Component Units*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the college's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable 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 caused by error or fraud 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. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

However, we noted certain matters involving the internal control over financial reporting, which we have reported to the college's management in a separate letter.

Compliance and Other Matters

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

We noted certain other less significant instances of noncompliance, which we have reported to the college's management in a separate letter.

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

Sincerely,

Arthur A. Hayes, Jr., CPA
Director

AAH/th

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT
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Independent Auditor's Report

June 27, 2005

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

Dear Mr. Morgan:

We have audited the accompanying basic financial statements of Volunteer State Community College, an institution of the Tennessee Board of Regents, which is a component unit of the State of Tennessee, and its discretely presented component unit as of and for the years ended June 30, 2004, and June 30, 2003, as listed in the table of contents. These financial statements are the responsibility of the college's management. Our responsibility is to express opinions on these financial statements, based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of directors of many agencies, commissions, and component units of the State of Tennessee; managing the state's debt; and making loans to the state's colleges and universities from debt proceeds. Some of the boards of which the Comptroller of the Treasury serves as a member per state statutes include the State Building Commission and the Tennessee Higher Education Commission.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Tennessee Board of Regents, Volunteer State Community College, and its discretely presented component unit as of June 30, 2004, and June 30, 2003, and the respective changes in financial position and cash flows thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

During the year ended June 30, 2004, the college implemented GASB Statement 39, *Determining Whether Certain Organizations Are Component Units*.

The management's discussion and analysis on pages 9 through 26 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.

Our audit was conducted for the purpose of forming opinions on the basic financial statements. The accompanying financial information on page 48 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 27, 2005, on our consideration of the college's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of 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

Volunteer State Community College
Management's Discussion and Analysis
For the Years Ended June 30, 2004, and June 30, 2003

This section of Volunteer State Community College's annual financial report presents a discussion and analysis of the financial performance of the college during the fiscal years ended June 30, 2004, and June 30, 2003. This discussion has been prepared by management along with the financial statements and related footnote 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. Volunteer State College Foundation is a legally separate, tax-exempt organization supporting Volunteer State Community College. The foundation acts primarily as a fund-raising organization to supplement the resources that are available to the college in support of its programs. Although the college does not control the timing or amount of receipts from the foundation, the majority of resources, or income thereon, that the foundation holds and invests are restricted to the activities of the college by the donors. Because these restricted resources held by the foundation can only be used by, or for the benefit of, the college, the foundation is considered a component unit of the college and is discretely presented in the college's financial statements. More detailed information about the Volunteer State College Foundation is presented in note 14 to the financial statements.

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 Volunteer State Community College as a whole and present a long-term view of the college's finances.

The Statement of Net Assets

The Statement of Net Assets presents the financial position of the college at the end of the fiscal year and includes all assets and liabilities of the college. The difference between total assets and total liabilities—net assets—is an indicator of the current financial condition of the college. 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 college's equity in property, plant, and equipment owned by the college. 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 college 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 assets are available to the institution for any lawful purpose of the institution.

Statement of Net Assets (in thousands of dollars)

	College			Component Unit		
	2004	2003	2002	2004	2003	2002
Assets:						
Current assets	$ 9,373	$ 8,400	$ 9,685	$ 536	$ 413	$ 322
Capital assets, net	27,569	27,141	20,141	-	-	-
Other assets	8,676	7,434	6,946	2,905	2,742	2,102
Total assets	45,618	42,975	36,772	3,441	3,155	2,424
Liabilities:						
Current liabilities	6,779	6,380	6,812	-	1	2
Noncurrent liabilities	916	932	591	-	-	-
Total liabilities	7,695	7,312	7,403	-	1	2
Net Assets:						
Invested in capital assets, net of related debt	27,430	26,996	20,141	-	-	-
Restricted - expendable	144	81	91	652	376	362
Restricted - nonexpendable	104	101	97	2,388	2,380	356
Unrestricted	10,245	8,485	9,040	401	398	1,704
Total net assets	$ 37,923	$ 35,663	$ 29,369	$ 3,441	$ 3,154	$ 2,422

- The largest asset in the current assets category of the college is cash in the amount of $8,572,372 at June 30, 2004, and $7,656,542 at June 30, 2003. Included in cash is approximately $3,883,793 at June 30, 2004, and $3,570,524 at June 30, 2003, that Volunteer State is holding as custodian for others such as student organizations, Volunteer State College Foundation, and the Tennessee Technology Centers at Livingston and Hartsville. Also included in cash is approximately $224,737 at June 30, 2004, and $325,560 at June 30, 2003, that has been generated by auxiliary enterprises and presently allocated for auxiliary enterprises. Additionally, about $23,960 at June 30, 2004, and $42,702 at June 30, 2003, of the cash have been designated to pay current liabilities related to the acquisition of plant assets. Most of the increases for each year in current assets are related to the increases in cash. For fiscal year 2004, the cash increase is primarily attributable to some planned expenditures being deferred until later. In fiscal year 2003, the cash increase is primarily attributable to an increase in deposits held in custody for others.

- Capital assets consist of land, buildings, projects in progress, equipment, other improvements, and library holdings. The land has a book value of $1,116,502 at June 30, 2004, and at June 30, 2003. The main campus in Gallatin consists of fourteen primary buildings. The VSCC Center at Livingston consists of one building. The buildings have a net book value of $20,304,512 at June 30, 2004, and $19,775,467 at June 30, 2003.

The equipment has a net book value of $1,542,865 at June 30, 2004, and $1,769,649 at June 30, 2003. Projects in progress have a book value of $75,906 at June 30, 2004, and $1,224,841 at June 30, 2003. Other improvements have a net book value (net of debt and depreciation) of $3,835,362 at June 30, 2004, and $2,689,454 at June 30, 2003. Library holdings have a net book value of $554,523 at June 30, 2004, and $564,927 at June 30, 2003.

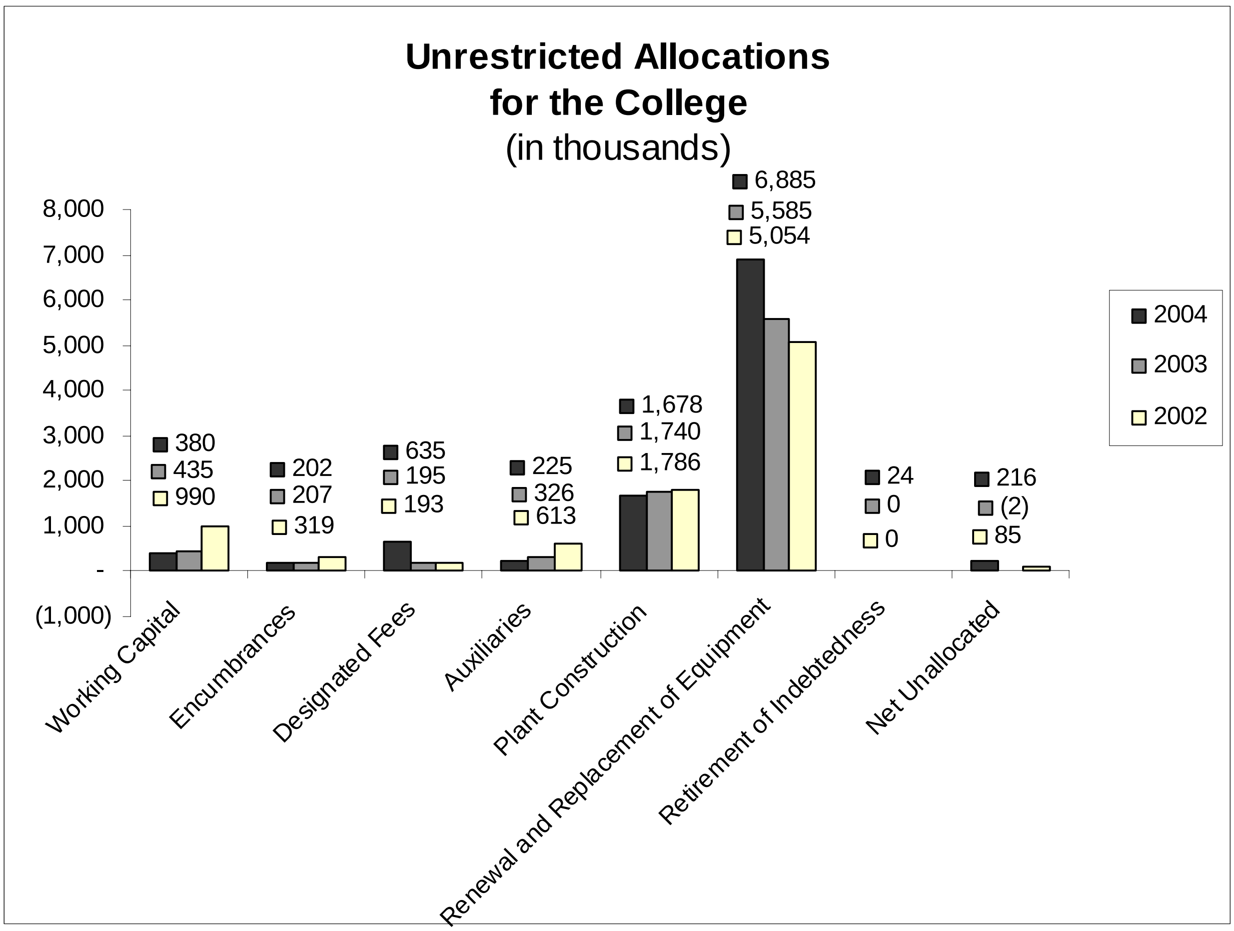
- Other noncurrent assets consist primarily of cash. Approximately $8,563,327 at June 30, 2004, and $7,324,588 at June 30, 2003, of cash has been designated for the future renewal and replacement of equipment and for various capital projects. Increases in current assets were the result of transfers of current asset cash to the other asset category to be used for future capital purchases and improvements. Additionally, $103,626 at June 30, 2004, and $100,483, at June 30, 2003, of cash is for restricted and nonexpendable endowments.

- Current liabilities at June 30, 2004, consist primarily of deposits held in custody for others of $3,883,740, accrued liabilities of $1,587,977, deferred revenue of $752,593, compensated absences of $284,845, and accounts payable of $241,360. Current liabilities at June 30, 2003, consist primarily of deposits held in custody for others of $3,563,738, accrued liabilities of $1,563,018, deferred revenue of $633,802, compensated absences of $272,279, and accounts payable of $326,388. The deposits held in custody for others are from the Volunteer State College Foundation, student organizations, and the Tennessee Technology Centers at Livingston and Hartsville for both fiscal years 2003 and 2004, and in addition, non-institutional scholarship sources for fiscal year 2003. Accrued liabilities consist primarily of accrued salaries, benefits, and other payroll withholdings payable. Most of the accrued salaries are the result of faculty contracts that begin in August and end in May but are paid over a 12-month period. Thus, one month of pay (and related benefits) is accrued at June 30th. Also, most of the compensation for summer school instruction is paid by Volunteer State in July and August. However, a portion of the compensation is earned before June 30th and thus, recorded as an accrued liability at June 30th. Also, summer semester classes normally begin in May and end in August. Revenues that are collected before June 30th but that are earned after June 30th are recorded as deferred revenue. Additionally, employees of the college are permitted to accrue and carry forward vacation time. Based on historical trends, the portion of the accumulated vacation time at June 30th that is estimated to be used during the next fiscal year (and related benefits) is accrued as a current liability. Accounts payable are generated through normal operating activities and are for goods or services received by June 30th but not paid as of June 30th. Increases in current liabilities were primarily from increases in deposits held in custody for others. Accrued liabilities increased due to an overall increase in payroll costs. For fiscal year 2004, deferred revenue increased largely due to increased tuition costs. For fiscal year 2003, accrued liabilities increased due to an overall increase in payroll costs.

- The remaining portion of the accumulated vacation time is accrued as a noncurrent liability and is for the most part the only noncurrent liability of the college. Also, the college has a long-term liability for bonds that was issued to fund a portion of the cost for the chiller replacement project. At June 30, 2003, the amount of the commercial paper liability is $145,000.

- For the component unit, overall the net assets increased by approximately $287,000 in 2004 because of increases in permanent endowments and excess revenues over transfers to the college.

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



- Working capital decreased slightly in 2004 because of a decrease of current unrestricted accounts receivable. Working capital decreased significantly in 2003 because at June 30, 2002, the college was carrying a large receivable for the sale of the bookstore inventory.

The college bookstore was leased to a private management company near the end of the 2002 fiscal year.

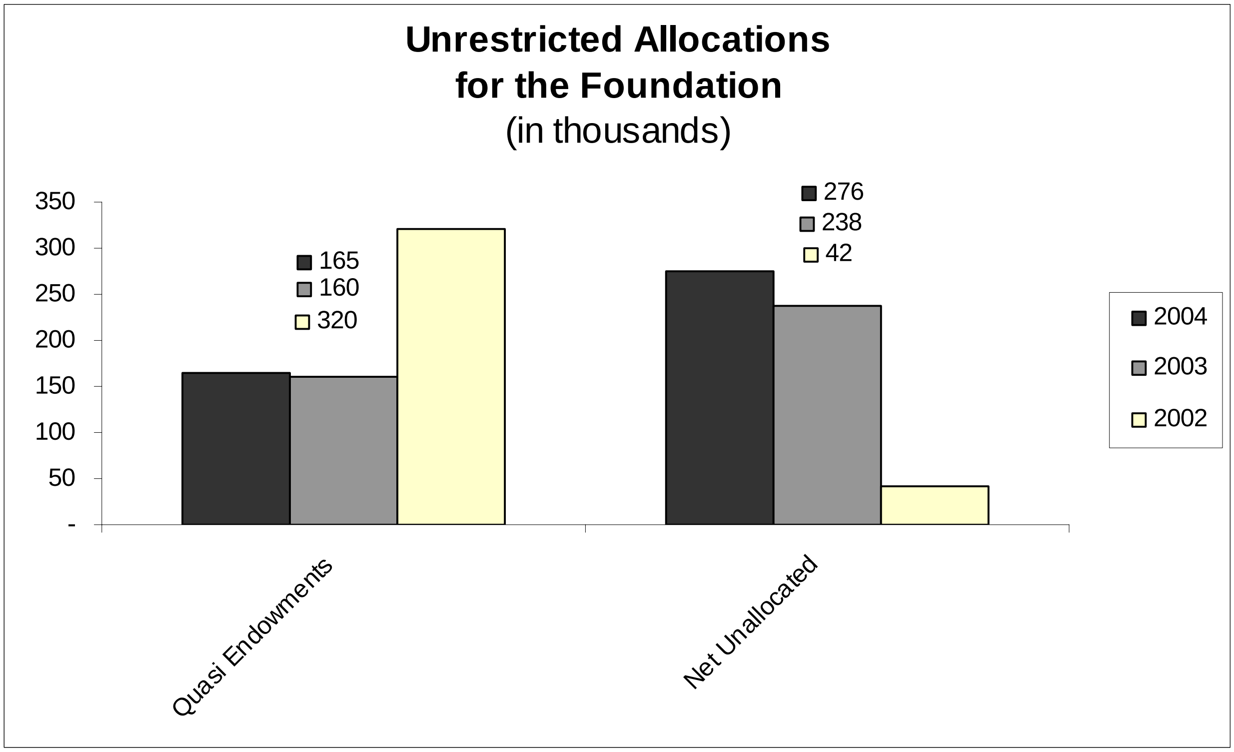
- Encumbrances were lower at June 30, 2003, for no particular unusual reason. The balance in encumbrances at June 30th each year usually relates to the timing of issuing purchase orders. This pattern can vary from year to year based on the spending patterns of the departments. Budget reductions experienced in 2003 could be the reason for the lower outstanding encumbrances.

- Designated fees increased during 2004 due to an increase in unspent technology access fees. There were projects that were planned but not completed during the fiscal year.

- Auxiliaries decreased during the 2004 and 2003 fiscal years due to the transfer of auxiliary fund balances to the plant funds for the future renewal and replacement of various equipment items.

- In 2004, renewal and replacement balances increased in large part because savings from temporarily unfilled positions were transferred to renewal and replacement to fund some large upcoming projects such as roof replacements and parking lots. In 2003, renewal and replacement balances increased in large part because of the auxiliary fund transfers.

- The net unallocated increased during the 2004 fiscal year because of general savings. Expenditures were slowed this year due to discussions of a possible five percent reduction in state appropriations for the following year which helped contribute to an increased ending fund balance. The net unallocated declined during fiscal year 2003 because of the five percent reductions experienced in state appropriations and because of transfers to the renewal and replacement of equipment accounts.



- Quasi endowment allocation for the component unit decreased significantly and net unallocated net assets increased significantly during 2003 because of reclassification between the two.

- Unrestricted net assets for the component unit increased only slightly during 2004. The large majority of the component unit's net assets is not unallocated but instead is restricted for scholarships.

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 college, 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.

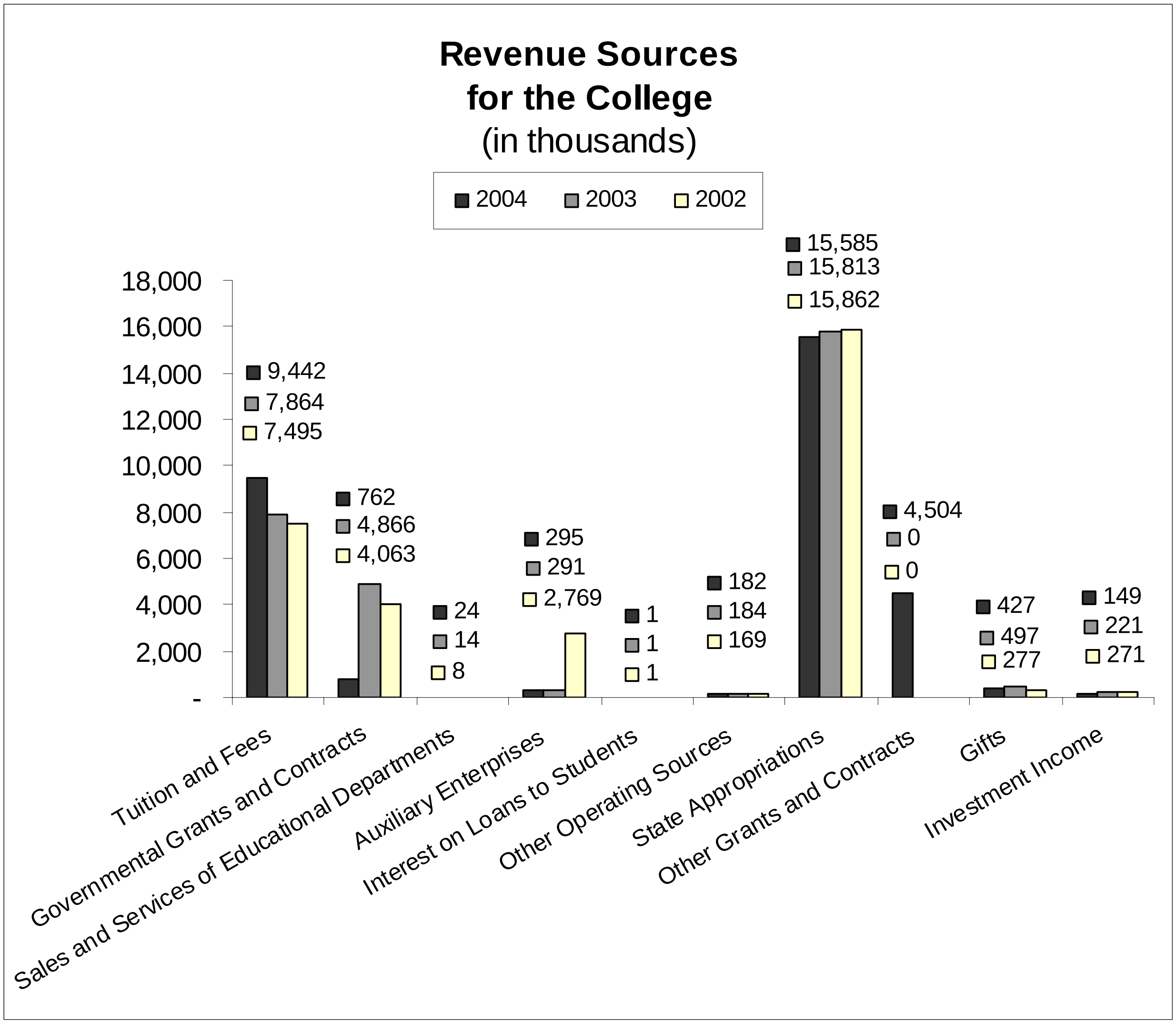
Statement of Revenues, Expenses and Changes in Net Assets (in thousands of dollars)

	College			**Component Unit**		
	2004	**2003**	**2002**	**2004**	**2003**	**2002**
Operating revenues:						
Net tuition and fees	$ 9,442	$ 7,864	$ 7,495	$ -	$ -	$ -
Gifts and contributions	-	-	-	549	286	277
Endowment income (per spending plan)	-	-	-	45	48	14

Auxiliary	295	291	2,769	-	-	-
Grants and contracts	762	4,866	4,064	-	-	-
Other	206	200	177	46	109	38
Total operating revenues	10,705	13,221	14,505	640	443	329
Operating expenses	31,545	32,723	30,598	438	360	318
Operating income (loss)	(20,840)	(19,502)	(16,093)	202	83	11
Nonoperating revenues and expenses:						
State appropriations	15,585	15,813	15,862	-	-	-
Gifts	427	497	277	-	-	-
Grants and contracts	4,504	-	-	-	-	-
Investment income	149	221	271	3	1	1
Other revenues and expenses	-	(1)	-	-	-	-
Total nonoperating revenues and expenses:	20,665	16,530	16,410	3	1	1
Income (loss) before other revenues, expenses, or losses	(175)	(2,972)	317	205	84	12
Other revenues, expenses, gains, or losses						
Capital appropriations	2,432	9,263	5,142	-	-	-
Additions to permanent endowments	3	3	2	82	648	76
Other	-	-	5	-	-	-
Total revenues, expenses, gains, or losses	2,435	9,266	5,149	82	648	76
Increase in net assets	2,260	6,294	5,466	287	732	88
Net assets at beginning of year, as originally reported	35,663	29,369	34,765	3,154	2,422	2,334
Cummulative effect of changes in accounting principle	-	-	(10,862)	-	-	-
Net assets at beginning of year, as restated	35,663	29,369	23,903	3,154	2,422	2,334
Net assets at end of year	$ 37,923	$ 35,663	$ 29,369	$3,441	$3,154	$2,422

Revenues

The following is a graphic illustration of revenues by source (both operating and nonoperating), which are used to fund the college's operating activities.



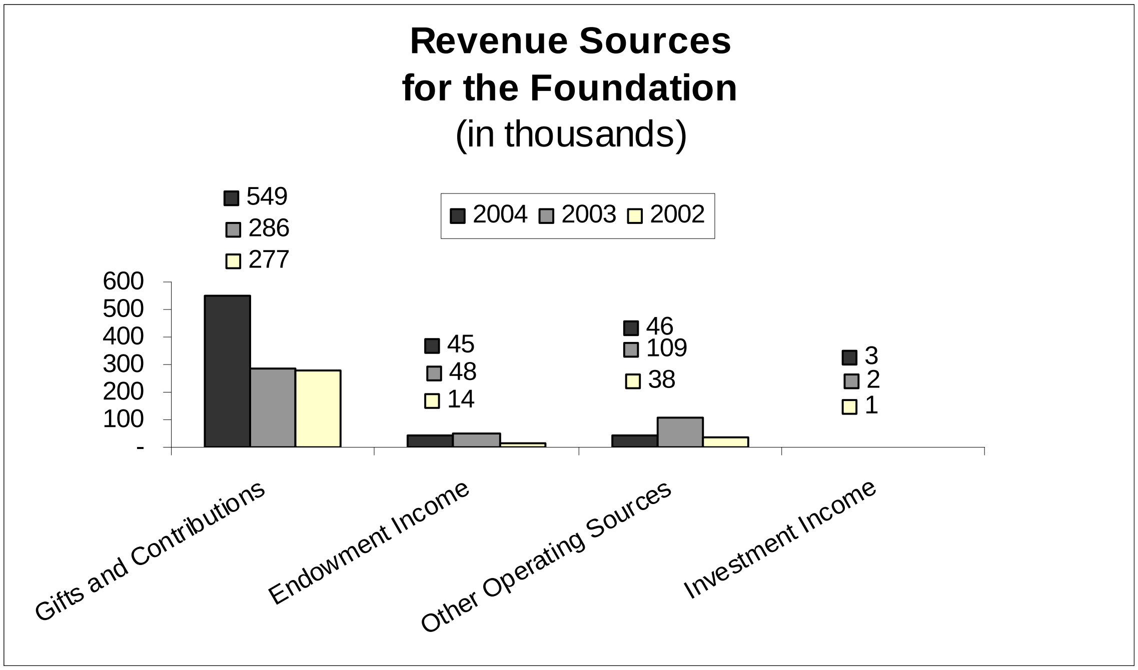
- State appropriations are the largest single source of revenue received by the college. State appropriations are requested by the Tennessee Higher Education Commission based on funding formula calculations. The State of Tennessee General Assembly determines the final state appropriations. The primary source of revenue for the State of Tennessee is sales tax collections. State appropriations account for about 50%, in fiscal year 2004, and 53%, in fiscal year 2003, of the college's total operating and nonoperating revenues. Although it appears that state appropriations only experienced a slight decline in fiscal year 2004 and in fiscal year 2003, the college in fact experienced an effective 9% decline in state appropriations in fiscal year 2004 and experienced a 5% decline in appropriations from the original appropriated amount in fiscal year 2003. For fiscal year 2004, the state appropriation revenues do not reflect a 9% reduction only because the state did appropriate additional funds for state mandated salary increases and increases in benefit costs. For fiscal year 2003, this amounted to an over $800,000 reduction from anticipated appropriations.

- The next largest source of revenue is from student tuition and fees. Tuition and fees, net of scholarship allowances of $2,860,454 at June 30, 2004, and $2,516,087 at June 30, 2003, account for approximately 30% and 26%, respectively, of the college's total operating and nonoperating revenues. Rates for tuition and fees are recommended by the Tennessee Higher Education Commission and approved by the Tennessee Board of Regents. Revenues from tuition and fees may fluctuate depending upon enrollments. During fiscal year 2004, net tuition and fees increased because of a 14% tuition rate increase. During fiscal year 2003, net tuition and fees declined because of an overall increase in scholarships, discounts, and allowances.

- Governmental grants and contracts and other grants and contracts account for approximately 17% in fiscal year 2004, and 16% in fiscal year 2003, of the college's total operating and nonoperating revenues. Approximately 86% in fiscal year 2004 and 85% in fiscal year 2003 of the total grants and contracts revenue are restricted for student aid programs such as Pell grant or SEOG. In fiscal year 2004, governmental grants and contracts decreased significantly while other grants and contracts increased significantly. This was because of a requirement to reclassify revenue from Pell grants and SEOG from governmental grants and contracts to other grants and contracts. In fiscal year 2003, revenues from grants increased in large part due to an increase in Pell grants.

- The college's bookstore operations are leased to Follett Higher Education Group and the college's food service operations are leased to Five Star Food Services. Thus, the revenues for 2004 primarily reflect the commissions paid by these two companies. The bookstore was self-operating until June 2002. For all of the 2003 fiscal year, the college's bookstore operations were leased. Thus, the revenues for 2003 only reflect the commissions paid by Follett whereas, in prior years, the revenues reflected gross sales.

- The remaining 3% of revenues are from various miscellaneous sources such as gifts, investment income, etc., for both fiscal years 2004 and 2003.



- The foundation's largest source of revenue is from gifts and contributions. Gifts and contributions increased in 2004 largely because before 2004, most gifts were categorized as permanently restricted endowment income. A special event occurred in 2003 honoring the retirement of Volunteer State Community College's president that generated large gifts and pledges to an endowment in his honor. Gifts and contributions increased in 2003 because of the same reason.

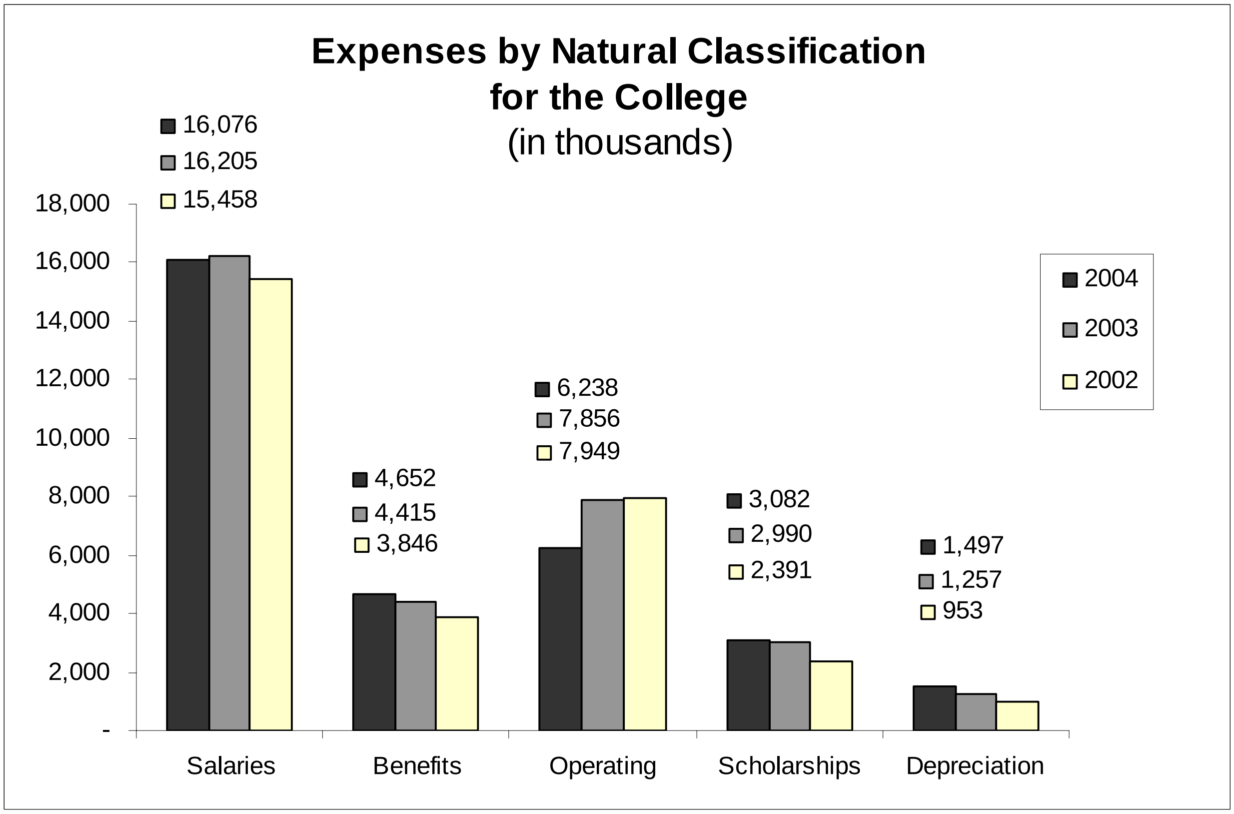
Expenses

Operating expenses can be displayed in two formats, natural classification and program classification. Both formats are displayed below.

Natural Classification

(in thousands of dollars)

	College			Component Unit		
	2004	**2003**	**2003**	**2004**	**2003**	**2003**
Salaries	$ 16,076	$ 16,205	$ 15,459	$ -	$ -	$ -
Benefits	4,652	4,415	3,846	-	-	-
Operating	6,238	7,856	7,949	32	68	22
Scholarships	3,082	2,990	2,391	-	-	-
Depreciation	1,497	1,257	953	-	-	-
Payments to or on behalf of Volunteer State Community College	-	-	-	406	292	296
Total	$ 31,545	$ 32,723	$ 30,598	$ 438	$ 360	$ 318

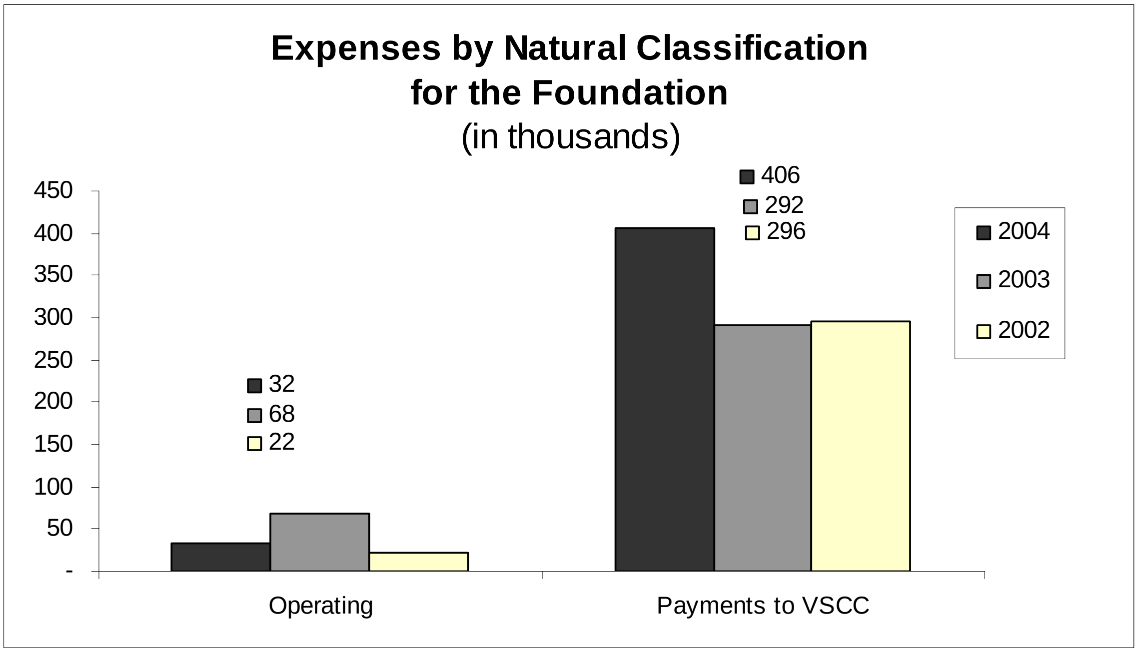


- Salary and related benefits together comprise approximately 66% in fiscal year 2004 and 65% in fiscal year 2003 of the college's expenses. In fiscal year 2004, salary expenses declined because several positions were held unfilled due to possible impending state appropriation reductions. Also in fiscal year 2004, benefits increased largely due to higher benefit costs in areas such as insurance. In fiscal year 2003, salary and benefits increased largely due to an across-the-board salary increase and higher benefit costs.

- Operating expenses, which account for approximately 20% in fiscal year 2004 and 25% in fiscal year 2003 of the total expenses, consist of expenditures for such items as travel, supplies, utilities, communications and shipping, maintenance and repairs, printing, professional and administrative services, rental and insurance, and stores for resale.

- Scholarship expenses are primarily attributable to the federal Pell grant and SEOG programs, TSAA (Tennessee Student Assistance Awards), and private scholarships. Net scholarship expenditures increased slightly in fiscal year 2004. Net scholarship expenditures increased significantly in fiscal year 2003 because of an increase in Pell funds.

- Depreciation expense was recognized for buildings, equipment, other improvements, and library holdings.



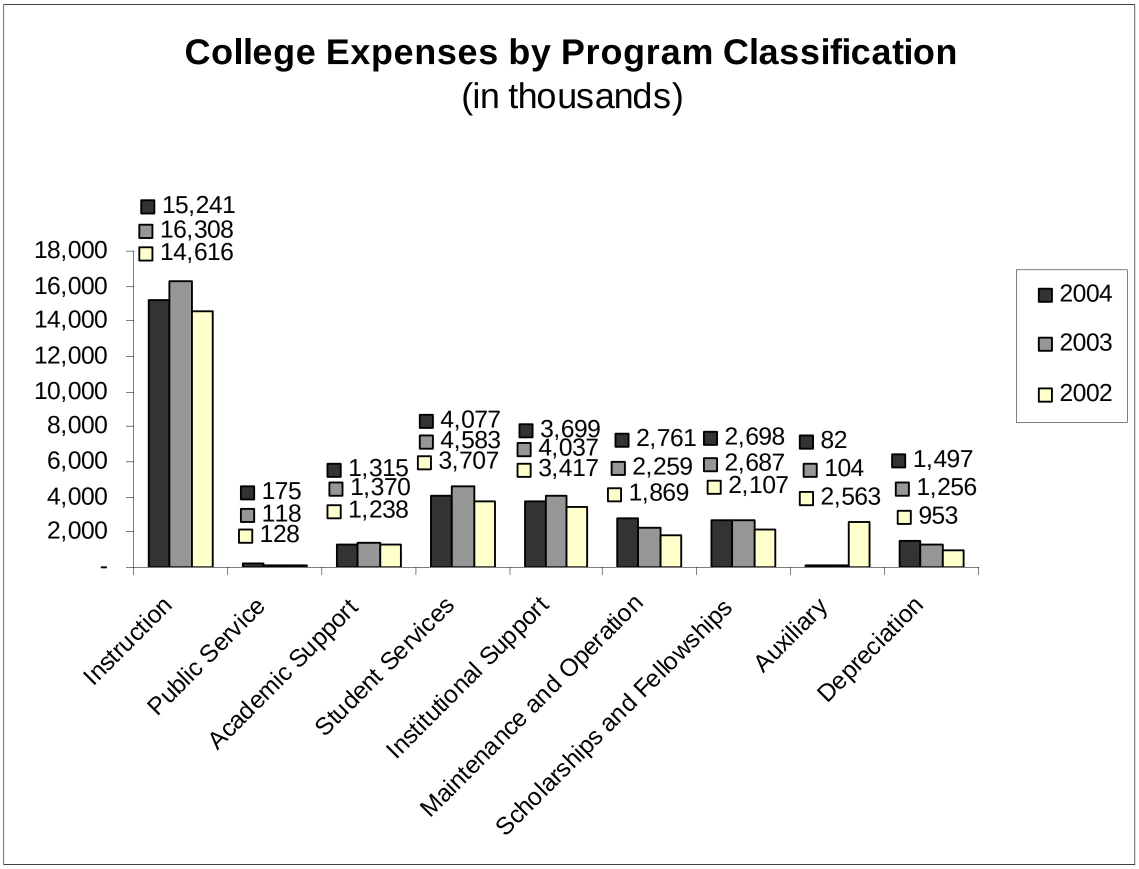
- Operating expenses of the foundation decreased in fiscal year 2004 due to additional costs incurred in fiscal year 2003 for the special fundraising event honoring the retirement of the college's president. This was also the reason for the increase in operating expenses in fiscal year 2003.

- Payments to the college from the foundation increased in fiscal year 2004 largely due to gifts received and given to the college to fund two faculty positions.

Program Classification

(in thousands of dollars)

	2004	2003	2002
Instruction	$ 15,241	$ 16,308	$ 14,616
Public Service	175	118	128
Academic support	1,315	1,370	1,238
Student services	4,077	4,583	3,707
Institutional support	3,699	4,037	3,417
Maintenance and operations	2,761	2,259	1,869
Scholarships and fellowships	2,698	2,687	2,107
Auxiliary	82	104	2,563
Depreciation	1,497	1,257	953
Total	$ 31,545	$ 32,723	$ 30,598



- The college follows the policies set forth by NACUBO (National Association of College and University Business Officers) for determining functional classifications of expenditures.

- Expenses in direct support of the instructional programs account for approximately 48% of the total expenses for fiscal year 2004 and 51% of total expenses for fiscal year 2003. For fiscal year 2004, most of the decline in expenditures is the result of capital appropriations for instructional building projects being expended in 2003. Appropriations were expended for supplies and equipment. Many of those special projects came to a close in 2003. Additionally, in 2004 there were some unfilled positions due to possible impending state appropriation reductions. In fiscal year 2003, most of the increase in expenditures is the result of general across-the-board increases in cost for such items as salary and benefits and operational items. Additionally, several instructional areas were renovated and equipment purchased during the year.

- Expenses for academic support are approximately 4% of total expenses in both fiscal year 2004 and 2003. The major expenditures in this function are for library services.

- Student services expenses account for about 13% of total expenses in fiscal year 2004 and 14% of total expenses in fiscal year 2003. This primarily includes costs for the administration of the student financial aid programs, admissions and records, counseling/advising services, athletics, and other student services administration. In fiscal year 2004, expenditures declined because of general savings and temporarily unfilled positions. In fiscal year 2003, most of the increases were the result of the across-the-board salary increases, benefit increases, filled positions, and general operating increases.

- Institutional support function expenses amounted to approximately 12% of total expenses in fiscal year 2004 and 13% of total operating expenses in fiscal year 2003. This function includes expenses for such things as executive and fiscal management, public relations and development, safety and security, purchasing, personnel administration, etc. In fiscal year 2004, expense decreases were caused in part by general savings and unfilled positions. Additionally, expenses had been incurred the previous year to develop a marketing plan for the college. In fiscal year 2003, expense increases were caused in part by the increased salary and benefit costs. Also, general operating costs increased because of inflationary increases as well as increased efforts to develop a marketing plan.

- Maintenance and operations costs consist primarily of expenses for the general upkeep of the buildings and grounds. Also, utilities cost is included in this function. Costs for maintenance and operation account for 9% of total expenses in fiscal year 2004 and 7% of total expenses in fiscal year 2003. In both fiscal year 2004 and 2003, maintenance costs increased because of construction and renovation activities occurring on campus. Many of the college's buildings are approaching 30 years of age and are in need of significant repairs and updating.

- Approximately 9% of total expenses in fiscal year 2004 and 5% of total expenses in fiscal year 2003 are for scholarships and grants. A large percentage of those expenditures for scholarships and grants are from restricted sources. In fiscal year 2003, the increase in Pell funding accounts for the net increase in scholarships and fellowships expense.

- Expenses for auxiliary enterprises primarily consist of allocations of institutional support costs and operation and maintenance costs. Operation of both the bookstore and the food service operations are contracted. As noted earlier, in previous years the college owned and operated the bookstore. This resulted in large expenses for cost of goods sold. In fiscal year 2003, the bookstore operations were leased and the college received commissions on sales. Therefore, there was no cost of goods sold in either fiscal year 2004 or 2003.

- Depreciation was previously discussed during the analysis of natural classifications.

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 college'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)

	College			Component Unit		
	2004	**2003**	**2002**	**2004**	**2003**	**2002**
Cash provided (used) by:						
Operating activities	$ (19,374)	$ (17,276)	$ (15,169)	$ 85	$ 96	$ (9)
Noncapital financing activities	20,821	16,936	15,997	75	434	92
Capital and related financing activities	560	1,247	270	-	-	-
Investing activities	150	221	(501)	(34)	(39)	(148)
Net increase (decrease) in cash	2,157	1,128	597	126	491	(65)
Cash, beginning of year	15,082	13,954	13,357	1,626	1,135	1,200
Cash, end of year	$ 17,239	$ 15,082	$ 13,954	$ 1,752	$ 1,626	$ 1,135

- For fiscal year 2004, the major sources of cash flows for operating activities include tuition and fees of $9,539,875, grants and contracts of $661,147, and bookstore commissions of $263,453. For fiscal year 2003, the major sources of cash flows for operating activities include tuition and fees of $7,914,029, grants and contracts of $4,948,997, and bookstore commissions of $696,144. Most of the cash flows from grants and contracts were restricted in nature. In fiscal year 2004, the major uses of cash flows for operating activities include payments for salaries and benefits of $20,687,795, payments to suppliers and vendors for operational items of $6,382,997, and payments for scholarships of $3,086,664. In fiscal year 2003, the major uses of cash flows for operating activities include payments for salaries and benefits of $20,414,379, payments to suppliers and vendors for operational items of $7,698,875, and payments for scholarships of $2,981,201. For fiscal year 2004, generally, the increase of net cash flows used by operating activities was the result of a couple of things. First, tuition and fees increased significantly this year as the result of a 14% tuition increase and a large increase in the technology access fee assessed to students. However, while the fee increases would increase the cash flows for operating activities, there was a reclassification of grants and contracts revenue that significantly reduced cash flows from operating activities. During the 2004 fiscal year the college was required to report revenue from Pell grants and SEOG grants as a noncapital financing activity instead of an operating activity, thus creating a large increase in net cash flows used by operating activities. In fiscal year 2003, generally, the increase of net cash flows used by operating activities was the result of increased payments to employees and payments for benefits and other payments to suppliers and vendors.

- In fiscal year 2004, the primary sources of cash from noncapital financing activities were state appropriations of $15,583,928 and gifts and grants received for other than endowment purposes of $4,918,118. In fiscal year 2003, the primary sources of cash from noncapital financing activities were state appropriations of $15,917,420 and gifts and grants received for other than endowment purposes of $311,878. Cash flows from noncapital financing activities were used to help finance the operating activities of the college. In fiscal year 2004, the increase in cash flows is primarily the result of the reclassification entry discussed above where Pell and SEOG grants were classified as a noncapital financing activity during the 2003-04 fiscal year and were classified as an operating activity during the 2002-03 fiscal year. In fiscal year 2003, the increase in cash flows is the result of the collection of 2002 fiscal year's state appropriations receivable and increases in deposits held for others (college foundation).

- Cash flows from investing activities are from interest income.
- In fiscal year 2004, cash flows provided and used by capital and related financing activities include $2,432,327 received for capital-state appropriations and $1,865,864 used for the purchase of capital assets and construction. In fiscal year 2003, cash flows provided and used by capital and related financing activities include $9,263,388 received for capital-state appropriations and $8,160,574 used for the purchase of capital assets and construction. The General Assembly of the State of Tennessee, in addition to normal state appropriations budgeted for operations, appropriates funds for capital acquisitions and capital maintenance. During the fiscal year 2004, the college received and expended funds for such projects as boiler replacements, infrastructure improvements, and building renovations. Capital appropriations and capital purchases both declined significantly during the 2003-04 fiscal year. In the 2002-03 fiscal year the college neared the completion of several large capital projects funded by the state including the new health sciences building and the renovation of some other buildings. Additionally, funds were received for several infrastructure projects and equipment purchases in fiscal year 2003. Thus, capital projects revenue and expenditures both declined in fiscal year 2004.
- For the fiscal year ended June 30, 2004, and the year June 30, 2003, the liquidity of the college improved. Overall, the cash position of the college increased by $2,157,242 in fiscal year 2004 and $1,128,013 in fiscal year 2003. For fiscal year 2004, the improvement can be attributed to general savings campus wide due to unfilled positions and delayed expenditures. The campus was positioning itself for possible 5% state appropriation reductions during the following year. Additionally, expenditures related to the technology access fee revenue were delayed until the following year. The college has several large maintenance projects planned for the 2004-05 fiscal year such as a new parking lot, roof replacements, fire alarm system upgrades and some general renovations that will use much of the increase in cash generated in 2003-04. For fiscal year 2003, the improvement can be attributed to the increases in funds held for others such as the college foundation and from increases related to capital and related financing activities.

Capital Asset and Debt Administration

Capital Assets

At June 30, 2004, Volunteer State Community College had $27,569,147 invested in capital assets, net of accumulated depreciation of $12,248,279. Depreciation charges totaled $1,497,414 for the 2004 fiscal year. At June 30, 2003, Volunteer State Community College had $27,140,840 invested in capital assets, net of accumulated depreciation of $10,852,336. Depreciation charges totaled $1,256,592 for the 2003 fiscal year. Details of these assets are shown below.

Schedule of Capital Assets, Net of Depreciation

(in thousands of dollars)

	College		
	2004	**2003**	**2002**
Land	$ 1,116	$ 1,116	$ 1,116
Land improvements & infrastructure	3,975	2,689	1,771
Buildings	20,304	19,776	12,030
Equipment	1,543	1,770	1,225
Library holdings	555	565	561
Projects in progress	76	1,225	3,838
Total	$ 27,569	$ 27,141	$ 20,541

During the fiscal years 2004 and 2003, the college completed or had in progress several capital projects. In fiscal year 2004, the college had a new student parking lot project in progress at June 30th. Additionally, projects were completed such as the renovation of a portion of the Warf building, the addition of gas fired boilers to five buildings, additional campus exterior lighting, and various infrastructure improvements to the Annex site. All of the projects were funded by capital state appropriations with the exception of the new student parking lot and the exterior lighting project. In fiscal year 2003, the college had several infrastructure projects in progress at June 30th including a chiller replacement project and a gas fired boiler project. Additionally, projects were completed such as the renovation of a portion of the administration building, the health science's building construction, and the Pickel building renovation. All of the projects were funded by capital state appropriations with the exception of the chiller project which is in part funded by a commercial paper issue of $145,000. In addition to the projects funded by capital state appropriations, a campus lighting project (which was still in progress at June 30, 2003) was funded with college funds allocated for that purpose.

It is expected that all capital projects in progress will be completed during the next fiscal year.

The Foundation has no capital assets.

More detailed information about the college's capital assets is presented in Note 5 to the financial statements.

Debt

At June 30, 2004, the college had $139,476 in debt outstanding. At June 30, 2003, the college had $145,000 in debt outstanding. The table below summarizes these amounts by type of debt instrument.

Debt Summary

2004

Debt Instrument	Beginning Balance	Additions	Reductions	Ending Balance
Commercial Paper	$ 145,000	$ -	$ 145,000	$ -
Bonds	-	145,000	5,524	139,476
Totals	$ 145,000	$ 145,000	$ 150,524	$ 139,476

2003

Debt Instrument	Beginning Balance	Additions	Reductions	Ending Balance
Commercial Paper	$ -	$ 145,000	$ -	$ 145,000

The debt issued was for the college's chiller replacement project. Commercial paper was used to fund the project during construction. However, at the end of construction bonds were issued for the long-term financing of the project and commercial paper debt was retired. State appropriations funded the majority of the cost of the project. However, the college was required to assume $139,476 in bond debt. More detailed information about the college's long-term liabilities is presented in Note 6 to the financial statements.

Economic Factors That Will Affect the Future

A 7% tuition increase was approved for the next fiscal year. There will be no increases or decreases to state appropriations other than to help cover state mandated salary and benefit increases.

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 college's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be directed to:

Ms. Elizabeth C. Cooksey, C.P.A.
Vice President of Business and Finance
Volunteer State Community College
1480 Nashville Pike
Gallatin, TN 37066-3188
(615) 230-3560

Exhibit A

TENNESSEE BOARD OF REGENTS
VOLUNTEER STATE COMMUNITY COLLEGE
STATEMENTS OF NET ASSETS
JUNE 30, 2004, AND JUNE 30, 2003

	College		Component Unit Volunteer State College Foundation	
	June 30, 2004	June 30, 2003	June 30, 2004	June 30, 2003
ASSETS				
Current assets:				
Cash (Notes 2 and 3)	$ 8,572,371.94	$ 7,656,542.23	$ -	$ -
Deposits with college (Note 14)	-	-	438,304.07	352,878.98
Accounts, notes, and grants receivable (net) (Note 4)	792,080.25	728,772.52	-	-
Pledges receivable (net) (Note 14)	-	-	97,923.10	60,002.35
Inventories (at lower of cost or market)	1,373.62	3,177.62	-	-
Prepaid expenses and deferred charges	7,171.70	9,793.65	-	-
Accrued interest receivable	497.82	1,588.40	-	-
Total current assets	9,373,495.33	8,399,874.42	536,227.17	412,881.33
Noncurrent assets:				
Cash (Notes 2 and 3)	8,666,953.37	7,425,541.23	-	-
Investments (Note 14)	-	-	1,333,526.30	1,300,314.65
Deposits with college (Note 14)	-	-	1,313,655.97	1,273,328.78
Pledges receivable (net) (Note 14)	-	-	240,110.88	152,032.60
Capital assets (net) (Note 5)	27,569,146.73	27,140,839.92	-	-
Other assets	8,628.95	8,496.16	17,367.44	16,101.25
Total noncurrent assets	36,244,729.05	34,574,877.31	2,904,660.59	2,741,777.28
Total assets	45,618,224.38	42,974,751.73	3,440,887.76	3,154,658.61
LIABILITIES				
Current liabilities:				
Accounts payable	241,360.29	326,388.41	53.00	413.80
Accrued liabilities	1,587,977.47	1,563,017.51	-	-
Deferred revenue	752,592.74	633,801.68	-	-
Compensated absences (Note 6)	284,844.53	272,278.61	-	-
Accrued interest payable	1,025.53	167.74	-	-
Long-term liabilities, current portion (Note 6)	11,828.96	-	-	-
Deposits held in custody for others	3,883,739.87	3,563,738.25	-	-
Other liabilities	15,941.88	21,027.80	-	-
Total current liabilities	6,779,311.27	6,380,420.00	53.00	413.80
Noncurrent liabilities:				
Compensated absences (Note 6)	788,265.69	786,290.00	-	-
Long-term liabilities (Note 6)	127,647.47	145,000.00	-	-
Due to grantors (Note 6)	391.19	-	-	-
U.S. Government grants refundable (Note 6)	-	391.19	-	-
Total noncurrent liabilities	916,304.35	931,681.19	-	-
Total liabilities	7,695,615.62	7,312,101.19	53.00	413.80
NET ASSETS				
Invested in capital assets, net of related debt	27,429,670.30	26,995,839.92	-	-
Restricted for:				
Nonexpendable:				
Scholarships and fellowships	103,626.10	100,482.90	2,388,480.90	2,379,676.83
Expendable:				
Scholarships and fellowships	24,628.34	27,353.48	648,983.17	374,423.31
Instructional department uses	72,882.14	7,282.67	570.00	570.00
Loans	371.48	335.25	-	-
Other	46,772.74	46,291.62	1,849.36	1,830.26
Unrestricted (Note 8)	10,244,657.66	8,485,064.70	400,951.33	397,744.41
Total net assets	$ 37,922,608.76	$ 35,662,650.54	$ 3,440,834.76	$ 3,154,244.81

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

TENNESSEE BOARD OF REGENTS
VOLUNTEER STATE COMMUNITY COLLEGE
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED JUNE 30, 2004, AND JUNE 30, 2003

	College		Component Unit Volunteer State College Foundation	
	Year Ended June 30, 2004	Year Ended June 30, 2003	Year Ended June 30, 2004	Year Ended June 30, 2003
REVENUES				
Operating revenues:				
Student tuition and fees (net of scholarship allowances of $2,860,453.84 for the year ended June 30, 2004, and $2,516,087.49 for the year ended June 30, 2003)	$ 9,442,150.51	$ 7,863,672.37	$ -	$ -
Gifts and contributions	-	-	548,594.90	286,235.86
Endowment income (per spending plan)	-	-	45,517.41	48,145.10
Governmental grants and contracts	761,937.59	4,866,288.99	-	-
Sales and services of educational departments	23,792.95	13,580.00	-	-
Auxiliary enterprises:				
Bookstore	275,048.00	245,818.31	-	-
Food service	20,279.84	45,041.87	-	-
Interest earned on loans to students	537.83	788.76	-	-
Other operating revenues	181,871.28	185,494.95	45,724.38	109,222.12
Total operating revenues	10,705,618.00	13,220,685.25	639,836.69	443,603.08
EXPENSES				
Operating expenses (Note 13):				
Salaries and wages	16,075,462.36	16,204,733.72	-	-
Benefits	4,651,817.94	4,415,595.06	-	-
Utilities, supplies, and other services	6,238,369.48	7,856,774.83	31,652.46	68,205.29
Scholarships and fellowships	3,082,105.21	2,989,628.87	-	-
Depreciation expense	1,497,414.36	1,256,592.00	-	-
Payments to or on behalf of Volunteer State Community College	-	-	406,426.51	292,496.62
Total operating expenses	31,545,169.35	32,723,324.48	438,078.97	360,701.91
Operating income (loss)	(20,839,551.35)	(19,502,639.23)	201,757.72	82,901.17
NONOPERATING REVENUES (EXPENSES)				
State appropriations	15,584,800.00	15,813,120.00	-	-
Gifts, including $406,426.51 from component unit in the year ended June 30, 2004, and $292,496.62 from component unit in the year ended June 30, 2003	426,609.41	497,238.08	-	-
Grants and contracts	4,504,019.68	-	-	-
Investment income (net of investment expense for the institution of $0.00 for the year ended June 30, 2004, and $0.00 for the year ended June 30, 2003; and for the component unit of $2,861.86 for the year ended June 30, 2004, and $0.00 for the year ended June 30, 2003)	149,142.57	220,948.72	3,067.97	1,501.46
Interest on capital asset-related debt	(1,898.23)	(652.40)	-	-
Other nonoperating revenues (expenses)	1,866.82	-	-	-
Net nonoperating revenues	20,664,540.25	16,530,654.40	3,067.97	1,501.46
Income (loss) before other revenues, expenses, gains, or losses	(175,011.10)	(2,971,984.83)	204,825.69	84,402.63
Capital appropriations	2,432,327.32	9,263,388.27	-	-
Additions to permanent endowments	2,642.00	2,495.50	81,764.26	648,018.94
Total other revenues	2,434,969.32	9,265,883.77	81,764.26	648,018.94
Increase in net assets	2,259,958.22	6,293,898.94	286,589.95	732,421.57
NET ASSETS				
Net assets - beginning of year	35,662,650.54	29,368,751.60	3,154,244.81	2,421,823.24
Net assets - end of year	$ 37,922,608.76	$ 35,662,650.54	$ 3,440,834.76	$ 3,154,244.81

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

Exhibit C

TENNESSEE BOARD OF REGENTS
VOLUNTEER STATE COMMUNITY COLLEGE
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2004, AND JUNE 30, 2003

	FY 2004	FY 2003
CASH FLOWS FROM OPERATING ACTIVITIES		
Tuition and fees	$ 9,539,874.69	$ 7,914,021.49
Grants and contracts	661,146.56	4,948,997.37
Sales and services of educational activities	23,792.95	13,580.00
Payments to suppliers and vendors	(6,382,996.64)	(7,698,875.03)
Payments to employees	(16,057,766.06)	(16,111,577.31)
Payment for benefits	(4,630,029.64)	(4,302,801.84)
Payments for scholarships and fellowships	(3,086,663.76)	(2,981,201.46)
Interest earned on loans to students	537.83	788.76
Bookstore	263,453.00	696,143.79
Food services	38,977.05	37,454.78
Other receipts (payments)	255,313.12	207,059.59
Net cash flows used by operating activities	(19,374,360.90)	(17,276,409.86)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State appropriations	15,583,928.10	15,917,420.00
Gifts and grants received for other than capital or endowment purposes (including $406,426.51 from the component unit for the year ended June 30, 2004, and $292,496.62 for the year ended June 30, 2003)	4,918,117.84	311,878.08
Private gifts for endowment purposes	2,642.00	2,495.50
Federal student loan receipts	3,634,056.07	2,667,258.68
Federal student loan disbursements	(3,633,295.98)	(2,662,319.56)
Changes in deposits held for others	319,241.53	691,336.61
Other noncapital financing receipts (payments)	(3,219.10)	8,481.27
Net cash flows provided by noncapital financing activities	20,821,470.46	16,936,550.58
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from capital debt	-	145,000.00
Capital - state appropriations	2,432,327.32	9,263,388.27
Purchase of capital assets and construction	(1,865,864.37)	(8,160,573.65)
Interest paid on capital debt and lease	(1,040.44)	(484.66)
Other capital and related financing receipts (payments)	(5,523.57)	(646.70)
Net cash flows provided by capital and related financing activities	559,898.94	1,246,683.26
CASH FLOWS FROM INVESTING ACTIVITIES		
Income on investments	150,233.35	221,189.26
Net cash provided by investing activities	150,233.35	221,189.26
Net increase in cash	2,157,241.85	1,128,013.24
Cash - beginning of year	15,082,083.46	13,954,070.22
Cash - end of year (Note 2)	$ 17,239,325.31	$ 15,082,083.46

TENNESSEE BOARD OF REGENTS
VOLUNTEER STATE COMMUNITY COLLEGE
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2004, AND JUNE 30, 2003

	FY 2004	FY 2003
RECONCILIATION OF OPERATING LOSS TO NET CASH USED BY OPERATING ACTIVITIES		
Operating loss	$ (20,839,551.35)	$ (19,502,639.23)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation expense	1,497,414.36	1,256,592.00
Gifts in-kind	12,511.25	25,325.00
Change in assets and liabilities:		
Receivables, net	(110,234.95)	603,182.30
Inventories	1,804.00	621.69
Prepaid/deferred items	2,621.95	(9,006.95)
Other assets	(132.79)	(195.63)
Accounts payable	(97,086.00)	87,884.42
Accrued liabilities	24,959.96	173,901.49
Deferred revenues	118,791.06	57,534.25
Deposits	-	(144.00)
Compensated absences	14,541.61	30,534.80
Net cash used by operating activities	$ (19,374,360.90)	$ (17,276,409.86)

	FY 2004	FY 2003
Non-cash transactions		
Gifts in-kind	$ 12,511.25	$ 25,325.00
Gifts in-kind - capital		$ 160,035.00

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

Tennessee Board of Regents
Volunteer State Community College
Notes to the Financial Statements
June 30, 2004, and June 30, 2003

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The college 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* and in May 2002, by GASB Statement 39, *Determining Whether Certain Organizations Are Component Units*. The financial statement presentation required by those statements provides a comprehensive, entity-wide perspective of the college's, including component units, assets, liabilities, net assets, revenues, expenses, changes in net assets, and cash flows.

Basis of Accounting

For financial statement purposes, the college 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 college has the option of following private-sector guidance issued subsequent to November 30, 1989, subject to the above limitation. The college 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 college 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 college's policy to use the restricted resources first.

Inventories

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

Compensated Absences

The college'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.

Net Assets

The college's net assets are classified as follows:

Invested in capital assets, net of related debt – This represents the college'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.

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

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

Unrestricted net assets – Unrestricted net assets represent resources derived from student tuition and fees, state appropriations, and sales and services of educational departments and auxiliary enterprises. These resources are used for transactions relating to the educational and general operations of the college, and may be used at the discretion of the college 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 college 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 college's financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees and other student charges, the college has recorded a scholarship discount and allowance.

NOTE 2. CASH

This classification includes demand deposits and petty cash on hand. At June 30, 2004, cash consisted of $2,935,865.03 in bank accounts, $5,000.00 of petty cash on hand, $14,003,272.30 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer, and $295,187.98 in LGIP deposits for capital projects. At June 30, 2003, cash consisted of $3,370,352.37 in bank accounts, $5,000.00 of petty cash on hand, and $11,706,731.09 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer.

LGIP deposits for capital projects - Payments related to the college's capital projects are made by the State of Tennessee's Department of Finance and Administration. The college'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 college 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 college'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, 2004, the carrying amount of the college's deposits in financial institutions participating in the collateral pool was $2,869,315.49, and the bank balance including accrued interest was $3,488,657.10. The bank balance was insured. At June 30, 2003, the carrying amount of the college's deposits in financial institutions participating in the collateral pool was $3,351,414.02, and the bank balance including accrued interest was $3,906,839.41. 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 college. Category 1 consists of deposits that are insured or collateralized with securities held by the college or by its agent in the college's name.

At June 30, 2004, the carrying amount of the college's deposits was $2,935,865.03, and the bank balance including accrued interest was $3,555,206.65. Of the bank balance, $3,555,206.65 was category 1. During the year ended June 30, 2004, the college had uncollateralized deposits ranging from $523.39 to $5,234.10 for four days in January 2004.

At June 30, 2003, the carrying amount of the college's deposits was $3,370,352.37, and the bank balance including accrued interest was $3,924,815.02. Of the bank balance, $3,924,815.02 was category 1. During the year ended June 30, 2003, the college had uncollateralized deposits ranging from $171.92 to $16,439.29 for five days in July 2002, and $418.35 to $11,986.67 for 18 days in October 2002.

The college 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. RECEIVABLES

Receivables included the following:

	June 30, 2004	June 30, 2003
Student accounts receivable	$ 506,952.18	$ 450,568.76
Grants receivable	242,271.27	125,860.42
State appropriation receivable	50,700.00	52,800.00
Other receivables	325,257.92	361,961.73
Subtotal	1,125,181.37	991,190.91
Less allowance for doubtful accounts	(333,101.12)	(262,418.39)
Total receivables	$ 792,080.25	$ 728,772.52

Federal Perkins Loan Program funds included the following:

	June 30, 2004	June 30, 2003
Perkins loans receivable	$ 24,361.57	$ 23,858.19
Less allowance for doubtful accounts	(24,361.57)	(23,858.19)
Total	$ -	$ -

NOTE 5. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2004, was as follows:

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$ 1,116,501.86	$ -	$ -	$ -	$ 1,116,501.86
Land improvements and infrastructure	3,692,828.10	734,612.03	808,353.13	-	5,235,793.26
Buildings	26,987,805.14	856,205.81	406,974.78	-	28,250,985.73
Equipment	3,858,622.74	156,450.05	-	-	4,015,072.79
Library holdings	1,112,577.29	112,059.70	-	101,470.87	1,123,166.12
Projects in progress	1,224,840.51	66,393.58	(1,215,327.91)	-	75,906.18

Total	37,993,175.64	1,925,721.17	-	101,470.87	39,817,425.94
Less accum. depreciation:					
Land improvements and infrastructure	1,003,373.76	257,581.56	-	-	1,260,955.32
Buildings	7,212,337.72	734,135.41	-	-	7,946,473.13
Equipment	2,088,973.74	383,233.70	-	-	2,472,207.44
Library holdings	547,650.50	122,463.69	-	101,470.87	568,643.32
Total accum. depreciation	10,852,335.72	1,497,414.36	-	101,470.87	12,248,279.21
Capital assets, net	$27,140,839.92	$ 428,306.81	$ -	$ -	$27,569,146.73

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

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$ 1,116,501.86	$ -	$ -	$ -	$ 1,116,501.86
Land improvements and infrastructure	2,593,675.40	436,304.47	662,848.23	-	3,692,828.10
Buildings	18,602,715.99	50,578.93	8,334,510.22	-	26,987,805.14
Equipment	2,995,698.75	862,923.99	-	-	3,858,622.74
Library holdings	1,061,760.60	122,424.84	-	71,608.15	1,112,577.29
Projects in progress	3,438,019.39	6,784,179.57	(8,997,358.45)	-	1,224,840.51
Total	29,808,371.99	8,256,411.80	-	71,608.15	37,993,175.64
Less accum. depreciation:					
Land improvements and infrastructure	822,940.47	180,433.29	-		1,003,373.76
Buildings	6,572,412.59	639,925.13	-		7,212,337.72
Equipment	1,771,158.69	317,815.05	-		2,088,973.74
Library holdings	500,840.12	118,418.53	-	71,608.15	547,650.50
Total accum. depreciation	9,667,351.87	1,256,592.00	-	71,608.15	10,852,335.72
Capital assets, net	$20,141,020.12	$6,999,819.80	$ -	$ -	$27,140,839.92

NOTE 6. LONG-TERM LIABILITIES

Long-term liabilities activity for the year ended June 30, 2004, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Payables:					
Bonds	$ -	$ 145,000.00	$ 5,523.57	$ 139,476.43	$ 11,828.96
Commercial paper	145,000.00	-	145,000.00	-	-
Subtotal	145,000.00	145,000.00	150,523.57	139,476.43	11,828.96
Other liabilities:					
Compensated absences	1,058,568.61	576,896.51	562,354.90	1,073,110.22	284,844.53
Due to grantors	-	391.19	-	391.19	-
U.S. Government grants refundable	391.19	-	391.19	-	-
Subtotal	1,058,959.80	577,287.70	562,746.09	1,073,501.41	284,844.53
Total long-term liabilities	$ 1,203,959.80	$ 722,287.70	$ 713,269.66	$ 1,212,977.84	$ 296,673.49

Long-term liabilities activity for the year ended June 30, 2003, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Payables:					
Commercial paper	$ -	$ 145,000.00	$ -	$ 145,000.00	$ -
Subtotal	-	145,000.00	-	145,000.00	-
Other liabilities:					
Compensated absences	1,028,033.81	578,189.48	547,654.68	1,058,568.61	272,278.61
U.S. Government grants refundable	391.19	-	-	391.19	-
Subtotal	1,028,425.00	578,189.48	547,654.68	1,058,959.80	272,278.61
Total long-term liabilities	$ 1,028,425.00	$ 723,189.48	$ 547,654.68	$ 1,203,959.80	$ 272,278.61

Bonds Payable

Bond issues, with interest rates ranging from 2.0% to 4.5% for Tennessee State School Bond Authority bonds, are due serially to 2014 and are secured by pledges of the facilities' revenues to which they relate and certain other revenues and fees of the college, 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 and unexpended debt proceeds amounts had zero balances at June 30, 2004, and June 30, 2003.

Debt service requirements to maturity for bonds payable at June 30, 2004, are as follows:

Year Ending June 30	Principal	Interest	Total
2005	$ 11,828.96	$ 4,963.70	$ 16,792.66
2006	12,568.33	4,275.88	16,844.21
2007	12,876.26	3,993.08	16,869.34
2008	13,191.73	3,703.36	16,895.09
2009	13,514.93	3,406.56	16,921.49
2010-2014	75,496.22	9,736.39	85,232.61
	$ 139,476.43	$ 30,078.97	$ 169,555.40

Commercial Paper

The Tennessee State School Bond Authority also authorized the issuance of commercial paper to finance the costs of various capital projects. The amount issued for projects at the college was $145,000.00 at June 30, 2003.

For the commercial paper program, the Tennessee State School Bond Authority maintains an interest rate reserve fund. The college contributes amounts to the reserve fund based on the amounts drawn. The principal of the reserve will be contributed to pay off notes or credited back to the college when the notes are converted to bonds. The interest earned on the reserve is used to pay interest due during the month.

NOTE 7. ENDOWMENTS

If a donor has not provided specific instructions to the college, state law permits the college to authorize for expenditure the earnings of the investments of endowment funds. When administering its power to spend the earnings, the college is required to consider the college’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 college chooses to spend only a portion of the investment income each year. Under the spending plan established by the college, 100% of current year earnings has been authorized for expenditure. The remaining amount, if any, is retained to be used in future years. At June 30, 2004, investment income of $575.11 is available to be spent, of which $575.11 is included in restricted net assets expendable for scholarships and fellowships. At June 30, 2003, investment income of $866.60 is available to be spent, of which $866.60 is included in restricted net assets expendable for scholarships and fellowships.

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, 2004	June 30, 2003
Working capital	$ 380,071.68	$ 435,056.65
Encumbrances	202,035.30	206,689.19
Designated fees	634,652.69	195,130.72
Auxiliaries	224,737.37	325,559.62
Plant construction	1,678,482.65	1,739,544.13
Renewal and replacement of equipment	6,884,844.62	5,585,043.89
Debt retirement	23,580.73	478.96
Unreserved/undesignated	216,252.62	(2,438.46)
Total	$ 10,244,657.66	$ 8,485,064.70

NOTE 9. PENSION PLANS

A. Defined Benefit Plan

Tennessee Consolidated Retirement System

Plan Description - The college 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 college is required to contribute an actuarially determined rate. The current rate is 7.3% of annual covered payroll. Contribution requirements for the college are established and may be amended by the TCRS' Board of Trustees. The college's contributions to TCRS for the years ended June 30, 2004, 2003, and 2002 were $555,619.72, $576,109.87, and $478,341.65. Contributions met the requirements for each year.

B. Defined Contribution Plans

Optional Retirement Plans (ORP)

Plan Description - The college 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 college 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 college to the plans was $620,587.33 for the year ended June 30, 2004, and $585,558.83 for the year ended June 30, 2003. Contributions met the requirements for each year.

NOTE 10. OTHER POST-EMPLOYMENT BENEFITS

The State of Tennessee administers a group health insurance program which provides post-employment health insurance benefits to eligible college retirees. This benefit is provided and administered by the State of Tennessee. The college assumes no liability for retiree health care programs. Information related to this plan is available at the statewide level in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Eighth Avenue North, Nashville, Tennessee 37243-0298, or by calling (615) 741-2140.

NOTE 11. INSURANCE-RELATED ACTIVITIES

It is the policy of the state not to purchase commercial insurance for the risks of losses for general liability, automobile liability, professional malpractice, and workers' compensation. The state's management believes it is more economical to manage these risks internally and set aside assets for claim settlement in its internal service fund, the Risk Management Fund. The state purchases commercial insurance for real property, flood, earthquake, and builder's risk losses and surety bond coverage on the state's officials and employees. The Risk Management Fund is also responsible for claims for damage to state owned property up to the amount of the property insurance aggregate deductible amount. The insurance policy deductibles vary from $25,000 per occurrence, depending on the type of coverage, to an aggregate of $7.5 million.

The college participates in the Risk Management Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the college based on a percentage of the college'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 college participates in the Risk Management 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 college 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 Risk Management Fund. At June 30, 2004, the Risk Management Fund held $101.1 million in cash designated for payment of claims.

During the year ended June 30, 2003, the state incurred 13 property claims which exceeded the per occurrence deductible. The gross amount of claims for the period was approximately $7.2 million, of which the state's property insurance carrier will ultimately assume approximately $2.2 million.

At June 30, 2004, the scheduled coverage for the college was $37,539,900 for buildings and $18,408,800 for contents. At June 30, 2003, the scheduled coverage for the college was $36,895,700 for buildings and $14,570,800 for contents.

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 college 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 college 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 12. COMMITMENTS AND CONTINGENCIES

Sick Leave - The college 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 $5,471,890.57 at June 30, 2004, and $5,225,554.96 at June 30, 2003.

Operating Leases - The college has entered into various operating leases for buildings and equipment. Such leases will probably continue to be required. Expenses under operating leases for personal property were $117,340.48 and $111,308.09 for the years ended June 30, 2004, and June 30, 2003, respectively. All operating leases are cancelable at the lessee's option.

Construction in Progress - At June 30, 2004, outstanding commitments under construction contracts totaled $1,137,711.11 for administration building renovation, renovation of science facilities, parking lot additions, roof replacements, and fire alarm improvements, of which $866,060.00 will be funded by future state capital outlay appropriations.

Litigation - The college is involved in one lawsuit, which is not expected to have a material effect on the accompanying financial statements.

NOTE 13. NATURAL CLASSIFICATIONS WITH FUNCTIONAL CLASSIFICATIONS

The college's operating expenses by functional classification for the year ended June 30, 2004, are as follows:

	Natural Classification					
Functional Classification	Salaries	Benefits	Other Operating	Scholarships	Depreciation	Total
Instruction	$ 9,607,848.13	$2,625,028.78	$ 2,910,038.99	$ 97,912.59	$ -	$ 15,240,828.49
Public service	88,726.98	23,447.36	58,089.27	4,730.00	-	174,993.61
Academic support	1,464,044.79	433,586.82	(608,006.52)	24,952.32	-	1,314,577.41
Student services	1,898,621.60	642,033.96	1,321,493.96	214,729.33	-	4,076,878.85
Institutional support	2,200,671.87	642,621.06	814,824.52	41,443.11	-	3,699,560.56
Operation & maint.	815,548.99	285,099.96	1,660,074.86	164.95	-	2,760,888.76
Scholar. & fellow.	-	-	-	2,698,172.91	-	2,698,172.91
Auxiliary	-	-	81,854.40	-	-	81,854.40
Depreciation	-	-	-	-	1,497,414.36	1,497,414.36
Total	$ 16,075,462.36	$4,651,817.94	$ 6,238,369.48	$3,082,105.21	$ 1,497,414.36	$ 31,545,169.35

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

Functional Classification	Natural Classification Salaries	Benefits	Other Operating	Scholarships	Depreciation	Total
Instruction	$ 9,611,206.76	$2,464,071.55	$ 4,158,186.26	$ 74,888.80	$ -	$ 16,308,353.37
Public service	56,845.12	17,662.70	39,335.78	4,082.00	-	117,925.60
Academic support	1,485,296.80	425,205.82	(553,363.26)	12,482.45	-	1,369,621.81
Student services	1,920,259.10	605,104.39	1,884,867.87	173,163.00	-	4,583,394.36
Institutional support	2,274,277.89	615,604.69	1,111,775.36	35,738.76	-	4,037,396.70
Operation & maint.	844,794.45	301,153.42	1,110,809.44	2,547.00	-	2,259,304.31
Scholar. & fellow.	-	-	-	2,686,726.86	-	2,686,726.86
Auxiliary	12,053.60	(13,207.51)	105,163.38	-	-	104,009.47
Depreciation	-	-	-	-	1,256,592.00	1,256,592.00
Total	$ 16,204,733.72	$4,415,595.06	$ 7,856,774.83	$ 2,989,628.87	$ 1,256,592.00	$ 32,723,324.48

NOTE 14. COMPONENT UNIT

The Volunteer State College Foundation is a legally separate, tax-exempt organization supporting Volunteer State Community College. The foundation acts primarily as a fund-raising organization to supplement the resources that are available to the college in support of its programs. The 73-member board of the foundation is self-perpetuating and consists of graduates and friends of the college. Although the college does not control the timing or amount of receipts from the foundation, the majority of resources, or income thereon, that the foundation holds and invests are restricted to the activities of the college by the donors. Because these restricted resources held by the foundation can only be used by, or for the benefit of, the college, the foundation is considered a component unit of the college and is discretely presented in the college's financial statements.

The foundation is a nonprofit organization that reports under Financial Accounting Standards Board (FASB) standards, including FASB Statement 117, *Financial Statements of Not-for-Profit Organizations*. As such, certain revenue recognition criteria and presentation features are different from GASB revenue recognition criteria and presentation features. With the exception of necessary presentation reformatting, no modifications have been made to the foundation's financial information in the college's financial statements for these differences.

During the year ended June 30, 2004, the foundation made distributions of $406,426.51 to or on behalf of the college for both restricted and unrestricted purposes. During the year ended June 30, 2003, the foundation made distributions of $292,496.62 to or on behalf of the college for both restricted and unrestricted purposes. Complete financial statements for the foundation can be obtained from Volunteer State College Foundation Office, 1480 Nashville Pike, Gallatin, TN 37066.

Deposits with college - Deposits with college consists of certain assets of the foundation that are held and managed by the college for the foundation. At June 30, 2004, these assets include $1,751,960.04 in cash. At June 30, 2003, these assets include $1,626,207.76 in cash. These assets have been reported by the college and included in the college's applicable note disclosures above.

Investments - Investments are recorded on the date of contribution and are stated at market value. Unrealized gains and losses are determined by the difference between market values at the beginning and end of the year.

Investments held at June 30, 2004, were as follows:

	Cost	Market Value
Equities	$ 663,586.67	$ 589,273.50
Bonds	533,441.46	477,254.93
Mutual funds	300,668.93	266,997.87
Total	$ 1,497,697.06	$ 1,333,526.30

Investments held at June 30, 2003, were as follows:

	Cost	Market Value
Equities	$ 63,344.36	$ 56,240.06
Bonds	475,504.04	422,174.55
Mutual funds	925,723.24	821,900.04
Total	$ 1,464,571.64	$ 1,300,314.65

Pledges Receivable - Pledges receivable are summarized below net of the allowance for doubtful accounts.

	June 30, 2004	June 30, 2003
Current pledges	$ 101,059.25	$ 61,473.23
Pledges due in one to five years	245,416.11	157,235.78
Pledges due after five years	-	-
Subtotal	346,475.36	218,709.01
Less discounts to net present value	(8,441.38)	(6,674.06)
Total pledges receivable, net	$ 338,033.98	$ 212,034.95

SUPPLEMENTARY INFORMATION
TENNESSEE BOARD OF REGENTS
VOLUNTEER STATE COMMUNITY COLLEGE
STATEMENTS OF CASH FLOWS - COMPONENT UNIT
FOR THE YEARS ENDED JUNE 30, 2004, AND JUNE 30, 2003

		FY 2004		FY 2003
CASH FLOWS FROM OPERATING ACTIVITIES				
Gifts and contributions	$	428,303.46	$	286,235.86
Endowment income per spending plan		49,514.08		62,149.80
Payments to suppliers and vendors		(32,013.26)		(69,556.21)
Payments to Volunteer State Community College		(406,426.51)		(292,496.62)
Other receipts (payments)		45,724.38		109,222.12
Net cash flows provided by operating activities		85,102.15		95,554.95
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
Private gifts for endowment purposes		76,056.67		435,983.99
Other noncapital financing receipts (payments)		(1,266.19)		(1,476.84)
Net cash flows provided by noncapital financing activities		74,790.48		434,507.15
CASH FLOWS FROM INVESTING ACTIVITIES				
Income on investments		3,067.97		1,501.46
Purchase of investments		(37,208.32)		(40,329.43)
Net cash used by investing activities		(34,140.35)		(38,827.97)
Net increase in cash and cash equivalents		125,752.28		491,234.13
Cash - beginning of year		1,626,207.76		1,134,973.63
Cash - end of year	$	1,751,960.04	$	1,626,207.76
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES				
Operating income	$	201,757.72	$	82,901.17
Adjustments to reconcile operating loss to net cash provided (used) by operating activities:				
Other adjustments		3,996.67		14,004.70
Change in assets and liabilities				
Receivables, net		(120,291.44)		-
Accounts payable		(360.80)		(1,350.92)
Net cash provided (used) by operating activities	$	85,102.15	$	95,554.95
Non-cash transactions				
Pledges	$	125,999.03	$	212,034.95
Unrealized loss on investments	$	(3,996.67)	$	(14,004.70)