

AUDIT REPORT

Tennessee Board of Regents
East Tennessee State University

For the Year Ended
June 30, 2009



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
DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT**

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February 18, 2010

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. Paul E. Stanton, President
East Tennessee State University
Campus Box 70734
Johnson City, Tennessee 37614-0734

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Tennessee Board of Regents, East Tennessee State University, for the year ended June 30, 2009. 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 disclosed a deficiency, which is detailed in the Results of the Audit section of this report. The university's administration has responded to the audit finding; the response is included following the finding. The Division of State Audit will follow up the audit to examine the application of the procedures instituted because of the audit finding.

Sincerely,

Arthur A. Hayes, Jr., CPA
Director

AAH/sds
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State of Tennessee

Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit
East Tennessee State University
For the Year Ended June 30, 2009

AUDIT OBJECTIVES

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

INTERNAL CONTROL FINDING

The University Needs Improved Review Procedures to Prevent Errors in the Preparation of the University's Financial Statements

The Vice President for Finance and Administration and the Associate Vice President for Financial Services worked together in preparing and reviewing East Tennessee State University's financial statements and related notes to the financial statements. They also relied on information provided by other employees. Our audit found that this arrangement lacked adequate review procedures to ensure the accuracy of the information presented in financial statements and notes. This weakness resulted in three significant reporting errors (page 9).

OPINIONS ON THE FINANCIAL STATEMENTS

The opinions on the financial statements are unqualified.

Audit Report
Tennessee Board of Regents
East Tennessee State University
For the Year Ended June 30, 2009

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**Tennessee Board of Regents
East Tennessee State University
For the Year Ended June 30, 2009**

INTRODUCTION

POST-AUDIT AUTHORITY

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

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

BACKGROUND

East Tennessee State University was established by an act of the General Assembly in 1909 as East Tennessee State Normal School. In 1924, the name was changed to East Tennessee State Teachers College; in 1930, to State Teachers College, Johnson City; and in 1943, to East Tennessee State College. In 1963, by an act of the General Assembly, East Tennessee State College was granted university status, and its name was changed to East Tennessee State University.

The university has 11 colleges and schools: the College of Arts and Sciences, the College of Business and Technology, the College of Education, the College of Medicine, the College of Nursing, the College of Pharmacy, the College of Public Health, the College of Clinical and Rehabilitative Sciences, the Honors College, the School of Continuing Studies, and the School of Graduate Studies. East Tennessee State University is officially authorized to grant 12 undergraduate and 23 graduate degrees.

ORGANIZATION

The governance of East Tennessee State University is vested in the Tennessee Board of Regents. The Governor, the Commissioner of Education, the Commissioner of Agriculture, and the Executive Director of the Tennessee Higher Education Commission serve *ex officio* on this

board. The chief administrative officer of the university is the president, who is assisted and advised by members of the faculty and administrative staff.

AUDIT SCOPE

The audit was limited to the period July 1, 2008, through June 30, 2009, 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 generally accepted government auditing standards. Financial statements are presented for the year ended June 30, 2009. East Tennessee State University is an institution of the Tennessee Board of Regents, which is an integral part of state government. As such, the Tennessee Board of Regents has been included as a component unit in the *Tennessee Comprehensive Annual Financial Report*.

OBJECTIVES OF THE AUDIT

The objectives of the audit were

1. to consider the university's internal control over financial reporting to determine auditing procedures for the purpose of expressing 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.

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

PRIOR AUDIT FINDINGS

There were no findings in the prior audit report.

OBSERVATIONS AND COMMENTS

MANAGEMENT'S RESPONSIBILITY FOR RISK ASSESSMENT

Auditors and management are required to assess the risk of fraud in the operations of the institution. The risk assessment is based on a critical review of operations considering what frauds could be perpetrated in the absence of adequate controls. The auditors' risk assessment is limited to the period during which the audit is conducted and is limited to the transactions that the auditors are able to test during that period. The risk assessment by management is the primary method by which the institution is protected from fraud, waste, and abuse. Since new programs may be established at any time by management or older programs may be discontinued, that assessment is ongoing as part of the daily operations of the institution.

Risks of fraud, waste, and abuse are mitigated by effective internal controls. It is management's responsibility to design, implement, and monitor effective controls in the institution. Although internal and external auditors may include testing of controls as part of their audit procedures, these procedures are not a substitute for the ongoing monitoring required of management. After all, the auditor testing is limited and is usually targeted to test the effectiveness of particular controls. Even if controls appear to be operating effectively during the time of the auditor testing, they may be rendered ineffective the next day by management override or by other circumventions that, if left up to the auditor to detect, will not be noted until the next audit engagement and then only if the auditor tests the same transactions and controls. Furthermore, since staff may be seeking to avoid auditor criticisms, they may comply with the controls during the period that the auditors are on site and revert to ignoring or disregarding the control after the auditors have left the field.

The risk assessments and the actions of management in designing, implementing, and monitoring the controls should be adequately documented to provide an audit trail both for auditors and for management, in the event that there is a change in management or staff, and to maintain a record of areas that are particularly problematic.

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, 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.

RESULTS OF THE AUDIT

AUDIT CONCLUSIONS

Internal Control

As part of the audit of the university's financial statements for the year ended June 30, 2009, we considered internal control over financial reporting as a basis for designing 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 generally accepted government auditing standards. Consideration of internal control over financial reporting disclosed a material weakness.

Compliance and Other Matters

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under generally accepted government auditing standards.

Fairness of Financial Statement Presentation

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



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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***

January 8, 2010

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. Paul E. Stanton, President
East Tennessee State University
Campus Box 70734
Johnson City, Tennessee 37614-0734

Ladies and Gentlemen:

We have audited the financial statements of East Tennessee State University, an institution of the Tennessee Board of Regents, which is a component unit of the State of Tennessee, and its discretely presented component units as of and for the year ended June 30, 2009, and have issued our report thereon dated January 8, 2010. Our report was modified to include a reference to other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the university's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the university's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the university's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified a deficiency in internal control over financial reporting that we consider to be a significant deficiency.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with accounting principles generally accepted in the United States of America such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

We consider the following deficiency to be a significant deficiency in internal control over financial reporting:

- The university needs improved review procedures to prevent errors in the preparation of the university's financial statements.

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

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

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would

not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe the significant deficiency described above is a material weakness.

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

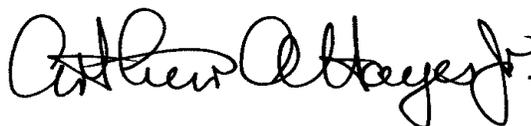
Compliance and Other Matters

As part of obtaining reasonable assurance about whether the university's financial statements are free of material misstatement, we performed tests of the university'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 generally accepted government auditing standards.

East Tennessee State University's response to the finding identified in our audit is included in the Finding and Recommendation section of this report. We did not audit the university's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the General Assembly of the State of Tennessee, the Tennessee Board of Regents, 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,

A handwritten signature in black ink that reads "Arthur A. Hayes, Jr." with a stylized, cursive script.

Arthur A. Hayes, Jr., CPA
Director

AAH/sds

FINDING AND RECOMMENDATION

The university needs improved review procedures to prevent errors in the preparation of the university's financial statements

Finding

The Vice President for Finance and Administration and the Associate Vice President for Financial Services worked together in preparing and reviewing East Tennessee State University's financial statements and related notes to the financial statements. They also relied on information provided by other employees. Our audit found that this arrangement lacked adequate review procedures to ensure the accuracy of the information presented in financial statements and notes. This weakness resulted in three significant reporting errors:

- In note 8 of the financial statements, the Associate Vice President for Financial Services reported the reserve amount for Tennessee State School Bond Authority (TSSBA) bonds as \$21,941.24. The correct amount, according to a TSSBA confirmation, was \$4,093,706.22. No review of this information was performed by another employee. The note was corrected in the audited statements.
- On the statement of revenues, expenses, and changes in net assets, scholarship allowances were understated by \$2,391,961.67. The reported allowances were \$25,361,762.26, whereas the correct amount was \$27,753,723.93. As a result, student tuition and fees were overstated by \$2,343,635.74, residential life revenues were overstated by \$48,325.93, and scholarship expense was overstated by \$2,391,961.67. We discovered that the Bursar made the error in the allowance calculation because she failed to update several items from the prior year's calculation. Inadequate review procedures led to this misstatement, since no review of this important and complex calculation was performed by another employee. The error was corrected on the audited statement.
- On the statement of net assets at June 30, 2009, the Associate Vice President for Financial Services reported \$779,608.79 of unapplied accounts receivable postings as prepaid expenses and deferred charges. The net unapplied balance was the result of problems with the new Banner accounting system. Checks to students were not properly posted to students' accounts receivable, and student and financial aid receipts were not properly posted to students' accounts receivable by year end. As a result, on the statement of net assets, prepaid expenses and deferred charges were overstated by \$779,608.79, and accounts receivable were understated by the same amount. The audited statement was not corrected. The entry was deemed immaterial by the university's Vice President for Finance and Administration.

These reporting errors resulted in significant misstatements in the financial statements. According to the Associate Vice President for Financial Services, these errors were not detected

because she did not have sufficient review time between year-end closing and the final preparation and submission of the financial report to the Tennessee Board of Regents Central Office. The Vice President for Finance and Administration also cited the lack of sufficient resources to provide adequate review due to staff reductions from the university's recent voluntary buyout plan. With an adequate review process, the Vice President or Associate Vice President could have detected and corrected these errors before the financial report was completed.

Recommendation

The Vice President for Finance and Administration should ensure that adequate reviews of the financial information included in the financial report are performed to ensure the accuracy of the financial statements and notes. After preparation, he and the Associate Vice President for Financial Services should perform an additional detailed review to ensure that errors have not been made in the report preparation.

The Vice President for Finance and Administration should ensure that risks associated with report preparation are adequately identified and assessed in the university's risk assessment activities. The Vice President should also implement effective controls to adequately mitigate those assessed risks and take appropriate action.

Management's Comment

We concur with the finding and recommendation. The Vice President for Finance and Administration will assess and refine the review process to ensure the financial statements are accurately prepared. The Associate Vice President for Financial Services will implement additional review processes including additional financial variance analysis to detect misclassification or errors in the financial data that need to be corrected.

The Vice President for Finance and Administration will direct the Financial Services risk assessment team to determine the risks associated with report preparation and take corrective action as deemed necessary.



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Independent Auditor's Report

January 8, 2010

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. Paul E. Stanton, President
East Tennessee State University
Campus Box 70734
Johnson City, Tennessee 37614-0734

Ladies and Gentlemen:

We have audited the accompanying basic financial statements of East Tennessee State University, an institution of the Tennessee Board of Regents, which is a component unit of the State of Tennessee, as of and for the year ended June 30, 2009, as listed in the table of contents. These financial statements are the responsibility of the university's management. Our responsibility is to express opinions on these financial statements, based on our audit. We did not audit the financial statements of the East Tennessee State University Foundation and the Medical Education Assistance Corporation, discretely presented component units of the university. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the East Tennessee State University Foundation and the Medical Education Assistance Corporation, is based on the reports of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. 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.

As discussed in Note 1, the financial statements of East Tennessee State University, an institution of the Tennessee Board of Regents, are intended to present the financial position, the changes in financial position, and the cash flows of only East Tennessee State University. They do not purport to, and do not present fairly the financial position of the Tennessee Board of Regents, as of June 30, 2009, and the changes in its financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, based on our audit and the reports of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Tennessee Board of Regents, East Tennessee State University, and its discretely presented component units as of June 30, 2009, and the respective changes in financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 14 through 33 and the schedule of funding progress on page 68 are not a required part of the basic financial statements but are 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 pages 69 and 70 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 generally accepted government auditing standards, we have also issued our report dated January 8, 2010, on our consideration of the university's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and 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

January 8, 2010
Page Three

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 generally accepted government auditing standards and should be read in conjunction with this report in considering the results of our audit.

Sincerely,

A handwritten signature in black ink that reads "Arthur A. Hayes, Jr." The signature is written in a cursive style with a large initial "A" and a distinct "Jr." at the end.

Arthur A. Hayes, Jr., CPA
Director

AAH/sds

Tennessee Board of Regents East Tennessee State University Management's Discussion and Analysis

This section of East Tennessee State University's annual financial report presents a discussion and analysis of the financial performance of the university during the fiscal year ended June 30, 2009, with comparative information presented for the fiscal year ended June 30, 2008. This discussion has been prepared by management along with the financial statements and related note disclosures and should be read in conjunction with the independent auditor's report and the audited financial statements and accompanying notes. The financial statements, notes, and this discussion are the responsibility of management.

The university has two discretely presented component units, the East Tennessee State University Foundation and the Medical Education Assistance Corporation (MEAC). More detailed information about the university's component units is presented in Note 20 to the financial statements. Information and analysis regarding the component units is also included in this section.

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 East Tennessee State University as a whole and present a long-term view of the university's finances.

The Statement of Net Assets

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

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

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

**East Tennessee State University
Condensed Statements of Net Assets
(in thousands of dollars)**

	<u>2009</u>	<u>2008</u>
Assets:		
Current assets	\$ 66,900	\$ 52,156
Capital assets, net	253,024	225,128
Other assets	54,458	49,012
Total assets	374,382	326,296
Liabilities:		
Current liabilities	45,291	27,375
Noncurrent liabilities	134,696	99,820
Total liabilities	179,987	127,195
Net assets:		
Invested in capital assets, net of related debt	138,748	141,369
Restricted – nonexpendable	40	40
Restricted – expendable	5,772	6,800
Unrestricted	49,835	50,892
Total net assets	\$194,395	\$199,101

Comparison of fiscal year 2009 to fiscal year 2008

- ◆ Current assets increased from 2008 to 2009 due to the reduction in bond investments and increases in cash deposits with LGIP due to declining market interest rates on bond investments during the fiscal year.
- ◆ In 2009, other assets increased due to increases in LGIP investments for capital projects.
- ◆ Net capital assets increased from 2008 to 2009 as a result of renovations to Carter and Clement Halls, and completion of the softball facility and the Cardiology Clinical Education building.
- ◆ Based upon guidance provided by the Tennessee Recovery Act Management Office, the total allotment of FY 2008-09 State Fiscal Stabilization Funds (\$6,453,200) were drawn down and receipted as of June 30, 2009. It was subsequently determined that institutions would not lose the availability of funds not drawn down at June 30, 2009, and SFSF of

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

\$5,541,038.26 were returned on July 13, 2009, and are included on the statement of net assets as due to primary government.

- ◆ Increases in other current liabilities were primarily due to increased deferred revenue and in the current portion of long-term liabilities related to construction projects completed during the fiscal year 2009.
- ◆ In 2009, noncurrent liabilities increased primarily due to the increased liability for other post-employment benefits (OPEB).
- ◆ Long-term liabilities increased substantially with the debt related to the construction projects for main campus apartments phase II, renovations of dormitories, and the new College of Pharmacy building.
- ◆ Invested in capital assets decreased in 2009 due to depreciation expense.
- ◆ Restricted net assets decreased from 2008 to 2009 due to increases in deferred revenue for Families First and stabilization of nursing revenue clinic collections from the prior year.

**East Tennessee State University Foundation
Condensed Statements of Net Assets
(in thousands of dollars)**

	<u>2009</u>	<u>2008</u>
Assets:		
Current assets	\$ 26	\$ 441
Capital assets, net	251	588
Other assets	56,627	66,870
Total assets	56,904	67,899
Liabilities:		
Current liabilities	59	163
Total liabilities	59	163
Net assets:		
Invested in capital assets, net of related debt	251	589
Restricted – nonexpendable	43,502	52,833
Restricted – expendable	14,855	13,174
Unrestricted	(1,763)	1,140
Total net assets	\$56,845	\$67,736

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

Comparison of fiscal year 2009 to fiscal year 2008

- ◆ Current assets decreased due to market losses.
- ◆ Capital assets and invested in capital assets decreased due to the sale of gift property and transfer of the completed Alumni Walkway to ETSU.
- ◆ Investments decreased due to market conditions.
- ◆ Other assets also decreased due to payments on existing pledges for the College of Pharmacy.
- ◆ Current liabilities decreased due to a reduction in scholarships due to ETSU at June 30.
- ◆ Nonexpendable net assets and unrestricted net assets decreased due to market losses.

**Medical Education Assistance Corporation
Condensed Statements of Net Assets
(in thousands of dollars)**

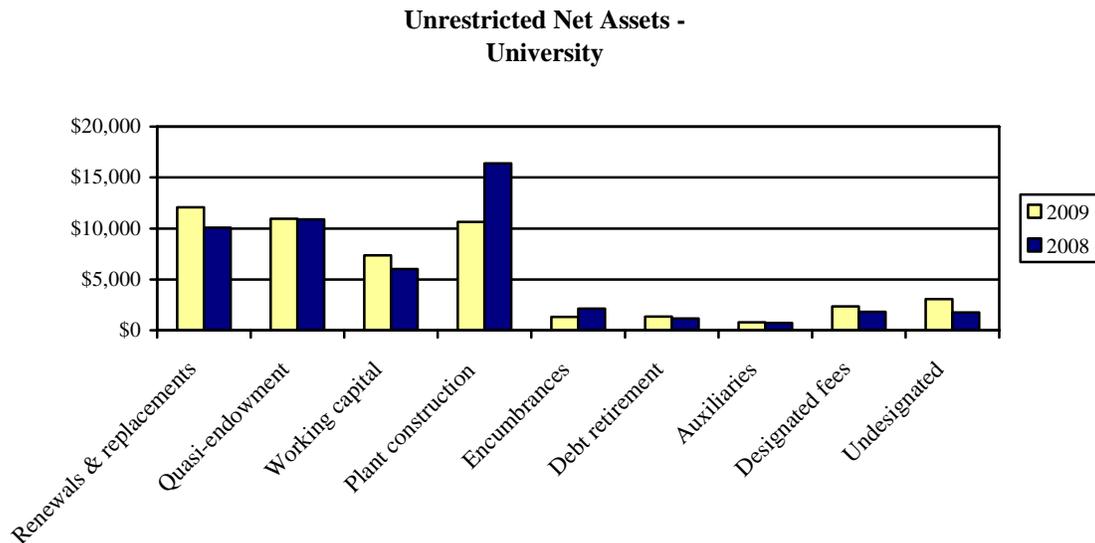
	<u>2009</u>	<u>2008</u>
Assets:		
Current assets	\$15,346	\$18,952
Capital assets, net	2,322	2,336
Other assets	6,015	1,218
Total assets	<u>23,683</u>	<u>22,506</u>
Liabilities:		
Current liabilities	4,456	4,719
Noncurrent liabilities	2,043	2,064
Total liabilities	<u>6,499</u>	<u>6,783</u>
Net assets:		
Invested in capital assets, net of related debt	693	679
Unrestricted	16,491	15,044
Total net assets	<u><u>\$17,184</u></u>	<u><u>\$15,723</u></u>

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

Comparison of fiscal year 2009 to fiscal year 2008

- ◆ Current assets decreased from 2008 to 2009 due to decreases in cash and short-term investments which were used to pay for the new Cardiology Clinical Education Building.
- ◆ Net capital assets decreased slightly from 2008 to 2009 due to more equipment retirements in the current year.
- ◆ Other assets increased as a result of an increase in long-term investments and the addition of a prepaid lease with ETSU for the Cardiology building.
- ◆ In 2009, current liabilities decreased as a result of decreases in other accrued expenses and payables to related parties. There was a slight decrease in noncurrent liabilities due to the decrease in the note payable for the building in Kingsport.

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



**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

Comparison of fiscal year 2009 to fiscal year 2008

- ◆ The allocations for plant construction decreased in 2009 due to the completion of several construction projects including Governor's Hall and the College of Pharmacy building. Other allocations remained relatively unchanged.

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

The statement of revenues, expenses, and changes in net assets presents the operating results of the university, as well as the nonoperating revenues and expenses. Annual state appropriations, while budgeted for operations, are considered nonoperating revenues according to accounting principles generally accepted in the United States of America.

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

**East Tennessee State University
Condensed Statements of Revenues, Expenses, and Changes in Net Assets
(in thousands of dollars)**

	<u>2009</u>	<u>2008</u>
Operating revenues:		
Net tuition and fees	\$ 59,480	\$ 54,093
Grants and contracts	42,005	37,573
Auxiliary	13,825	12,333
Other	25,292	22,990
Total operating revenues	140,602	126,989
Operating expenses	286,904	272,954
Operating income (loss)	(146,302)	(145,965)
Nonoperating revenues and expenses:		
State appropriations	92,402	98,619
Gifts	3,417	4,467
Grants and contracts	40,088	35,498
Investment income	2,327	3,964
Other revenues and expenses	(3,677)	(3,641)
Total nonoperating revenues and expenses	134,557	138,907
Income (loss) before other revenues, expenses, gains, or losses	(11,745)	(7,058)
Other revenues, expenses, gains, or losses:		
Capital appropriations	6,691	5,999
Capital grants and gifts	801	2,226
Other	(453)	-
Total other revenues, expenses, gains, or losses	7,039	8,225
Increase (decrease) in net assets	(4,706)	1,167
Net assets at beginning of year	199,101	197,934
Net assets at end of year	\$194,395	\$199,101

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

**ETSU Foundation
Condensed Statements of Revenues, Expenses, and Changes in Net Assets
(in thousands of dollars)**

	<u>2009</u>	<u>2008</u>
Operating revenues and expenses:		
Operating revenues	\$ 3,939	\$ 6,967
Operating expenses	5,758	7,077
Operating income (loss)	(1,819)	(110)
 Nonoperating revenues and expenses:		
Gifts	872	827
Investment income (loss)	(11,613)	(2,473)
Other revenues and expenses	(345)	-
Total nonoperating revenues and expenses	(11,086)	(1,646)
 Income (loss) before other revenues, expenses, gains, or losses	(12,905)	(1,756)
 Other revenues, expenses, gains, or losses:		
Capital grants and gifts	52	42
Additions to permanent endowments	1,962	1,266
Total other revenues, expenses, gains, or losses	2,014	1,308
 Increase (decrease) in net assets	(10,891)	(448)
 Net assets at beginning of year	67,736	68,184
Net assets at end of year	\$56,845	\$67,736

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

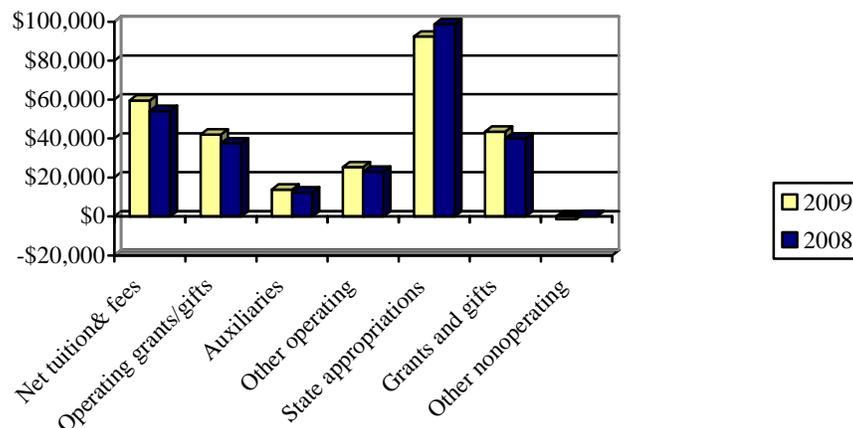
**Medical Education Assistance Corporation
Condensed Statements of Revenues, Expenses, and Changes in Net Assets
(in thousands of dollars)**

	<u>2009</u>	<u>2008</u>
Operating revenues and expenses:		
Operating revenues	\$38,010	\$36,453
Operating expenses	34,511	33,118
Operating income (loss)	<u>3,499</u>	<u>3,335</u>
 Nonoperating revenues and expenses:		
Investment income	387	652
Other revenues and expenses	(2,425)	(2,360)
Total nonoperating revenues and expenses	<u>(2,038)</u>	<u>(1,708)</u>
Increase in net assets	<u>1,461</u>	<u>1,627</u>
 Net assets at beginning of year	15,723	14,096
Net assets at end of year	<u><u>\$17,184</u></u>	<u><u>\$15,723</u></u>

Revenues

The following is a graphic illustration of revenues by source (both operating and nonoperating), which were used to fund the university's operating activities for the years ended June 30, 2009, and June 30, 2008. Amounts are presented in thousands of dollars.

Revenues by Source - University

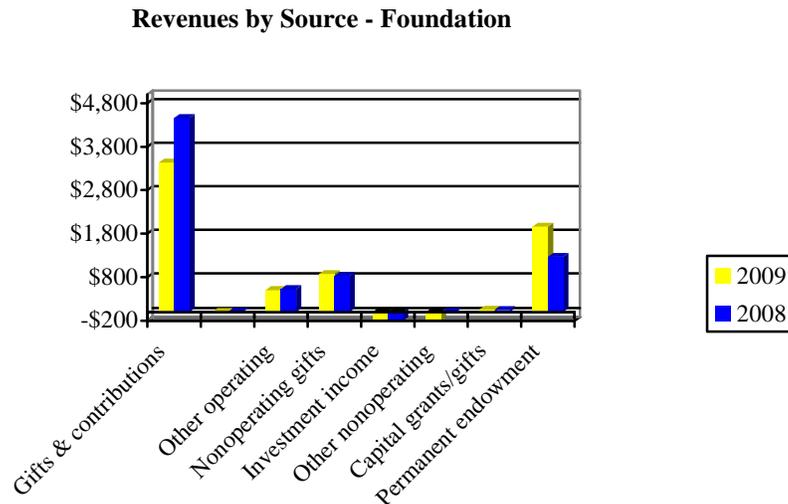


**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

Comparison of fiscal year 2009 to fiscal year 2008

- ◆ Tuition and fees increased in 2009 due to a 6% fee increase and a 3% increase in enrollment.
- ◆ Grants and contracts increased as a result of increased revenue in Family First funding.
- ◆ Auxiliary revenue increased due to an increase in housing revenue with the new Governor's Hall, and increases in commission revenue for bookstore and food service.
- ◆ Noncapital state appropriations decreased by \$6.2 million from 2008 to 2009 as a result of operating reductions and a 3.4% reversion.
- ◆ Nonoperating gifts decreased as no gifts received were needed for the College of Pharmacy from the ETSU Foundation as compared with the prior year.

The following is a graphic illustration of revenues by source (both operating and nonoperating), which were used to fund the foundation's operating activities for the year ended June 30, 2009, and June 30, 2008. Amounts are presented in thousands of dollars.



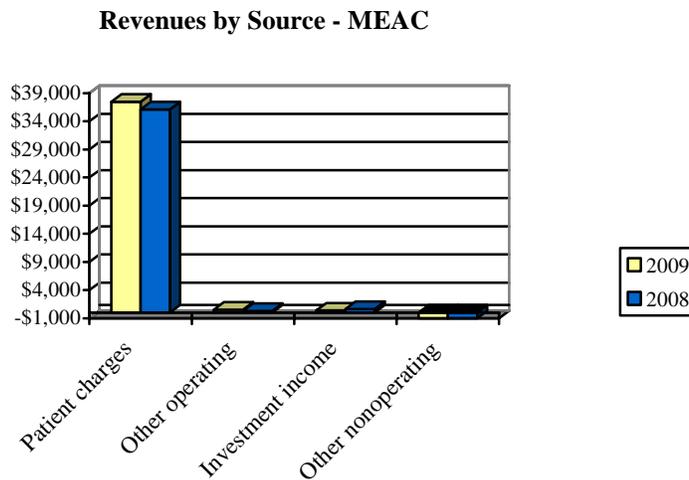
Comparison of fiscal year 2009 to fiscal year 2008

- ◆ Operating revenues decreased due to reductions in cash and in-kind gifts for operating purposes. Gifts decreased due to a worsening economy.

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

- ◆ Investment income decreased due to a reduction of realized capital gains for the year.
- ◆ Unrealized losses increased due to market conditions.
- ◆ Additions to permanent endowment increased due to a major endowment gift during the year.

The following is a graphic illustration of revenues by source (both operating and nonoperating), which were used to fund the MEAC's operating activities for the year ended June 30, 2009, and June 30, 2008. Amounts are presented in thousands of dollars.



Comparison of fiscal year 2009 to fiscal year 2008

- ◆ Net operating revenues increased 4% in fiscal year 2009.
- ◆ Patient service revenue increased in 2009 primarily due to increased productivity.
- ◆ Investment income decreased significantly in 2009 due to lower interest rates.

Expenses

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

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

**University
Natural Classification**

	<u>2009</u>	<u>2008</u>
Salaries	\$145,895	\$ 139,114
Benefits	48,453	48,246
Other operating	59,686	55,911
Scholarships	21,336	18,936
Depreciation	11,534	10,747
Total expenses	\$286,904	\$ 272,954

**Foundation
Natural Classification**

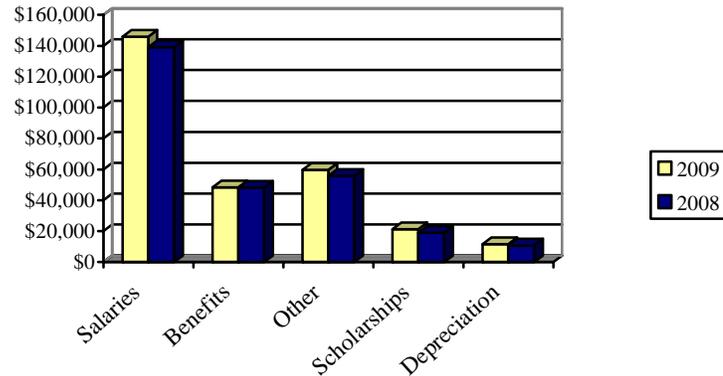
	<u>2009</u>	<u>2008</u>
Other operating	\$ 2,047	\$ 1,979
Scholarships	1,269	977
Depreciation	3	3
Payments to or on behalf of ETSU	2,439	4,118
Total expenses	\$ 5,758	\$ 7,077

**MEAC
Natural Classification**

	<u>2009</u>	<u>2008</u>
Salaries	\$22,643	\$21,701
Benefits	2,098	1,881
Other operating	9,529	9,286
Depreciation	241	250
Total expenses	\$34,511	\$33,118

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

Operating Expenses by Natural Classification - University

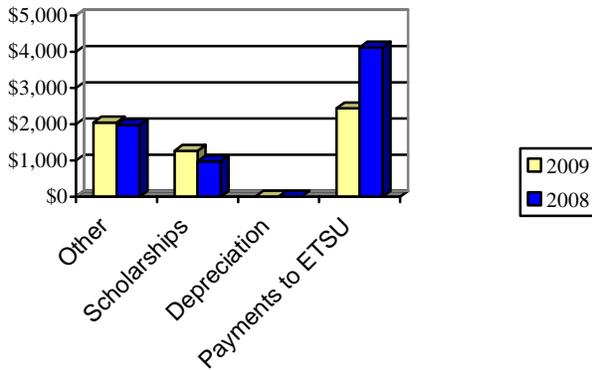


Comparison of fiscal year 2009 to fiscal year 2008

- ◆ Salaries increased due to the voluntary buy-out program of \$3.5 million, equity pay adjustments, and a bonus paid in the fall.
- ◆ Benefits increased as a result of increases in the state health insurance premiums and the recognition of other post employment benefits.
- ◆ Other operating expenses increased primarily due to increases in energy and fuel costs for utilities, and construction costs for the main campus apartments.
- ◆ Scholarships increased along with increased enrollment.
- ◆ Depreciation expense increased from 2008 to 2009 with the completion of construction projects, renovations of dormitories, and the completion of the Cardiology Clinical Education Building.

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

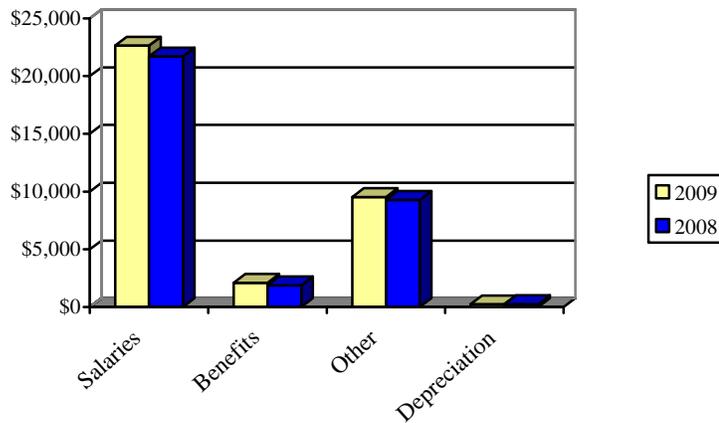
**Operating Expenses by Natural Classification -
Foundation**



Comparison of fiscal year 2009 to fiscal year 2008

- ◆ The decrease in payments to ETSU in fiscal year 2009 is attributed to a reduction in the transfer to ETSU for College of Pharmacy operations.

**Operating Expenses by Natural Classification -
MEAC**



Comparison of fiscal year 2009 to fiscal year 2008

- ◆ In fiscal year 2009, physician compensation increased 4% over the prior year. As a result of increased staffing and salary increases, non-physician compensation increased 3.8% in 2009.

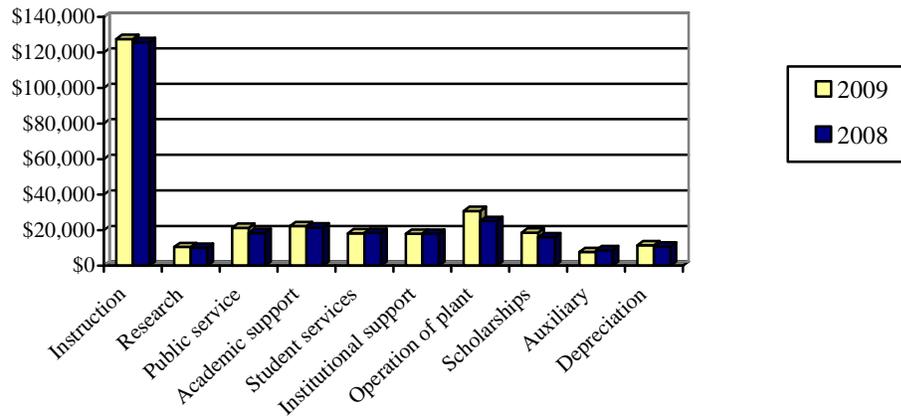
**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

- ◆ Supplies expense increased steadily in 2009, while expenses for malpractice insurance and purchased services remained consistent with the prior year.

**University
Program Classification
(in thousands of dollars)**

	<u>2009</u>	<u>2008</u>
Instruction	\$127,619	\$125,784
Research	10,497	10,037
Public service	21,380	18,466
Academic support	22,327	21,500
Student services	18,343	18,547
Institutional support	18,065	17,984
Operation and maintenance of plant	30,848	25,193
Scholarships	18,630	16,072
Auxiliary	7,661	8,624
Depreciation	11,534	10,747
Total expenses	<u>\$286,904</u>	<u>\$272,954</u>

**Operating Expenses by Program Classification -
University**



**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

Comparison of fiscal year 2009 to fiscal year 2008

- ◆ Instruction is the largest expenditure area for the university. Increases in instruction were due in part to the voluntary buy-out program, equity pay adjustments, and a bonus paid in the fall of 2008.
- ◆ Increases in operation of plant are due primarily because of expenditures for construction of new campus apartments.
- ◆ Increases in public service are due to increased expenditures for Families First.
- ◆ Depreciation expense increased from 2008 to 2009 with the completion of construction projects, renovations of dormitories, and completion of the Cardiology Clinical Education Building.
- ◆ Expenditures in other areas did not change materially from 2008 to 2009.

Capital Assets and Debt Administration

Capital Assets

The university had \$253 million in capital assets, net of accumulated depreciation at June 30, 2009; and \$225.1 million in capital assets, net of accumulated depreciation at June 30, 2008. Depreciation charges totaled \$11.5 million and \$10.7 million for the years ended June 30, 2009, and June 30, 2008, respectively. Details of these assets are shown below. More detailed information about the university's capital assets is presented in Note 5 to the financial statements.

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

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

	<u>2009</u>	<u>2008</u>
Land	\$ 24,571	\$ 24,164
Land improvements & infrastructure	20,397	17,390
Buildings	162,552	151,774
Equipment	9,642	9,642
Library holdings	4,244	4,934
Software	3,017	3,118
Projects in progress	28,601	14,106
Total capital assets, net	<u>\$253,024</u>	<u>\$225,128</u>

Comparison of fiscal year 2009 to fiscal year 2008

- ◆ In 2009, capital assets increased from the capitalization of the new softball stadium, the Cardiology building, and the completion of several renovation projects. Construction in progress continues for a new dormitory, which will be occupied in fall 2009. Software decreased as depreciation expense exceeded additions.

At June 30, 2009, and June 30, 2008, the foundation had \$250,000 and \$588,000, respectively, invested in capital assets, net of accumulated depreciation. Depreciation charges totaled \$3,000 for both fiscal years. Details of these assets are shown below.

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

	<u>2009</u>	<u>2008</u>
Land	\$ 1	\$ 49
Buildings	241	243
Equipment	9	9
Projects in progress	-	287
Total capital assets, net	<u>\$251</u>	<u>\$588</u>

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

Comparison of fiscal year 2009 to fiscal year 2008

- ◆ Land and projects in progress decreased due to the sale of gift property and transfer of the completed Alumni Walkway to ETSU.

MEAC had \$2,322,276 in capital assets, net of accumulated depreciation at June 30, 2009; and \$2,335,928 in capital assets, net of accumulated depreciation at June 30, 2008. Depreciation charges totaled \$241 thousand and \$250 thousand for the years ended June 30, 2009, and June 30, 2008, respectively. Details of these assets are shown below.

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

	<u>2009</u>	<u>2008</u>
Land	\$ 18	\$ 18
Buildings and leasehold improvements	1,800	1,836
Equipment	504	482
Total capital assets, net	\$2,322	\$2,336

Comparison of fiscal year 2009 to fiscal year 2008

- ◆ In 2009, net investment in capital assets remained consistent with the prior year.

Debt

The university had \$114 million and \$84 million in debt outstanding at June 30, 2009, and June 30, 2008, respectively. The table below summarizes these amounts by type of debt instrument.

**University
Outstanding Debt Schedule
(in thousands of dollars)**

	<u>2009</u>	<u>2008</u>
Commercial paper	\$ 2,003	\$19,298
Notes	150	200
Loans	1,549	1,689
Bonds	110,574	62,572
Total debt	\$114,276	\$83,759

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

Comparison of fiscal year 2009 to fiscal year 2008

- ◆ In 2009, bonds increased related to the Phase II apartments, housing renovations, energy performance projects, and the College of Pharmacy building.

The Tennessee State School Bond Authority (TSSBA) must authorize all capital long-term debt on behalf of the university. TSSBA currently is rated as AA by Standard & Poor. More detailed information about the university's long-term liabilities is presented in Note 8 to the financial statements.

The ETSU Foundation had no outstanding debt at June 30, 2009.

**MEAC
Outstanding Debt Schedule
(in thousands of dollars)**

	<u>2009</u>	<u>2008</u>
Notes	\$1,629	\$1,657
Total debt	\$1,629	\$1,657

Comparison of fiscal year 2009 to fiscal year 2008

- ◆ MEAC has one note payable for the Kingsport facility which has a declining balance due.

Economic Factors That Will Affect the Future

The economic outlook for the State of Tennessee remains poor. During fiscal year 2009, the state reduced the university appropriation an additional 19.4%, in addition to the 5.4% that was reduced at the beginning of the year, for a total reduction of 24.8%. The university has received federal stimulus and state maintenance of effort (MOE) dollars that have helped to temporarily avoid these reductions. The university received \$6,453,200 in federal stimulus and state MOE funds in fiscal year 2009 and will receive \$18,030,400 of such funds in both fiscal years 2010 and fiscal year 2011. These funds have allowed the university to make reductions over a two-year period that will enable it to be in a position to operate at the expected reduced level of appropriations beginning with fiscal year 2012.

**Tennessee Board of Regents
East Tennessee State University
Management's Discussion and Analysis (Cont.)**

We are not aware of any other factors, decisions, or conditions that are expected to have a significant impact on financial position or results of operations during future fiscal years.

Requests for Information

This financial report is designed to provide a general overview of the university's finances for all those with an interest in the university's finances. Questions concerning any of the information provided in this report or requests for additional information should be directed to Dr. David Collins, Vice President for Finance and Administration, P.O. Box 70601, Johnson City, TN 37614.

**TENNESSEE BOARD OF REGENTS
EAST TENNESSEE STATE UNIVERSITY
STATEMENT OF NET ASSETS
JUNE 30, 2009**

	Component Units		
	East Tennessee State University	East Tennessee State University Foundation	Medical Education Assistance Corporation
ASSETS			
Current assets:			
Cash and cash equivalents (Notes 2, 3, and 20)	\$ 38,973,387.69	\$ -	\$ 8,341,168.00
Short-term investments (Note 20)	-	-	2,800,000.00
Accounts, notes, and grants receivable (net) (Note 4)	25,386,466.15	7,923.61	3,889,346.00
Pledges receivable (net) (Note 20)	-	18,581.08	-
Inventories	432,807.69	-	-
Prepaid expenses and deferred charges	1,425,524.34	-	315,276.00
Accrued interest receivable	672,779.40	-	-
Other assets	9,691.70	-	-
Total current assets	<u>66,900,656.97</u>	<u>26,504.69</u>	<u>15,345,790.00</u>
Noncurrent assets:			
Cash and cash equivalents (Notes 2, 3, and 20)	31,421,166.93	5,250,117.40	-
Investments (Notes 3 and 20)	16,030,560.00	47,937,395.58	3,000,000.00
Accounts, notes, and grants receivable (net) (Note 4)	7,005,837.97	-	195,575.00
Pledges receivable (net) (Note 20)	-	2,715,985.46	-
Capital assets (net) (Notes 5 and 20)	253,023,782.38	250,686.00	2,322,275.00
Prepaid expenses and deferred charges	-	-	2,819,661.00
Other assets	-	722,807.22	-
Total noncurrent assets	<u>307,481,347.28</u>	<u>56,876,991.66</u>	<u>8,337,511.00</u>
Total assets	<u>374,382,004.25</u>	<u>56,903,496.35</u>	<u>23,683,301.00</u>
LIABILITIES			
Current liabilities:			
Accounts payable (Note 7)	7,092,044.75	58,910.46	707,899.00
Accrued liabilities	7,025,559.39	-	2,873,766.00
Due to primary government	5,541,038.26	-	-
Student deposits	1,000,768.81	-	-
Deferred revenue (Note 8)	15,562,676.30	-	18,470.00
Compensated absences (Notes 8 and 20)	2,581,997.82	-	111,729.00
Accrued interest payable	1,004,214.80	-	-
Long-term liabilities, current portion (Notes 8 and 20)	4,227,403.71	-	33,112.00
Deposits held in custody for others	1,255,244.37	-	361,642.00
Other liabilities	-	-	349,606.00
Total current liabilities	<u>45,290,948.21</u>	<u>58,910.46</u>	<u>4,456,224.00</u>
Noncurrent liabilities:			
Deferred revenue (Note 8)	2,819,661.00	-	-
Compensated absences (Notes 8 and 20)	7,707,715.74	-	446,914.00
Long-term liabilities (Notes 8 and 20)	110,048,621.50	-	1,596,633.00
Due to grantors (Note 8)	7,440,376.64	-	-
Net OPEB obligation (Notes 8 and 13)	6,679,722.02	-	-
Total noncurrent liabilities	<u>134,696,096.90</u>	<u>-</u>	<u>2,043,547.00</u>
Total liabilities	<u>179,987,045.11</u>	<u>58,910.46</u>	<u>6,499,771.00</u>
NET ASSETS			
Invested in capital assets, net of related debt	138,747,757.17	250,686.00	692,531.00
Restricted for:			
Nonexpendable:			
Scholarships and fellowships	40,012.97	34,697,627.95	-
Research	-	547,728.86	-
Instructional department uses	-	4,519,214.17	-
Other	-	3,737,315.07	-
Expendable:			
Scholarships and fellowships	159,904.90	2,451,909.46	-
Research	659,481.54	408,397.43	-
Instructional department uses	68,904.21	2,643,467.91	-
Loans	1,088,786.51	-	-
Capital projects	-	755,394.97	-
Debt service	2,947,824.18	-	-
Other	847,216.34	8,595,876.19	-
Unrestricted (Note 10)	49,835,071.32	(1,763,032.12)	16,490,999.00
Total net assets	<u>\$ 194,394,959.14</u>	<u>\$ 56,844,585.89</u>	<u>\$ 17,183,530.00</u>

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

**TENNESSEE BOARD OF REGENTS
EAST TENNESSEE STATE UNIVERSITY
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
FOR THE YEAR ENDED JUNE 30, 2009**

	Component Units		
	East Tennessee State University	East Tennessee State University Foundation	Medical Education Assistance Corporation
REVENUES			
Operating revenues:			
Student tuition and fees (net of scholarship allowances of \$27,588,773.99)	\$ 59,479,862.19	\$ -	\$ -
Gifts and contributions	-	3,434,062.22	-
Governmental grants and contracts	32,658,854.21	-	-
Nongovernmental grants and contracts	9,346,510.35	-	-
Sales and services of educational departments	23,976,499.73	-	-
Patient charges	-	-	37,473,476.00
Auxiliary enterprises:			
Residential life (net of scholarship allowances of \$164,949.94; all residential life revenues are used as security for revenue bonds; see Note 11)	9,506,604.73	-	-
Bookstore	767,590.84	-	-
Food service	547,858.93	-	-
Wellness facility (all revenues are used as security for revenue bonds; see Note 11)	1,255,221.34	-	-
Other auxiliaries	1,747,325.29	-	-
Interest earned on loans to students	189,117.53	-	-
Other operating revenues	1,126,618.15	504,724.85	536,532.00
Total operating revenues	<u>140,602,063.29</u>	<u>3,938,787.07</u>	<u>38,010,008.00</u>
EXPENSES			
Operating expenses (Note 17):			
Salaries and wages	145,894,521.12	-	22,643,381.00
Benefits	48,452,268.50	-	2,097,390.00
Utilities, supplies, and other services	59,686,692.49	2,046,287.68	9,529,173.00
Scholarships and fellowships	21,336,446.03	1,269,420.41	-
Depreciation expense	11,534,437.34	2,950.00	241,179.00
Payments to or on behalf of East Tennessee State University (Note 20)	-	2,439,113.79	-
Total operating expenses	<u>286,904,365.48</u>	<u>5,757,771.88</u>	<u>34,511,123.00</u>
Operating income (loss)	<u>(146,302,302.19)</u>	<u>(1,818,984.81)</u>	<u>3,498,885.00</u>
NONOPERATING REVENUES (EXPENSES)			
State appropriations	92,401,792.50	-	-
Gifts (university gifts include \$1,808,689.06 from ETSU Foundation and \$1,437,303.00 from MEAC)	3,417,025.03	872,304.00	-
Grants and contracts	40,087,666.99	-	-
Investment income (for the component units, net of investment expense of \$102,249.00)	2,327,460.42	(11,613,292.80)	386,434.00
Interest on capital asset-related debt	(4,136,047.64)	-	(115,460.00)
Payments to or on behalf of East Tennessee State University or East Tennessee State University Foundation (Note 20)	-	-	(2,309,607.00)
Other nonoperating revenues (expenses)	458,871.39	(345,495.15)	-
Net nonoperating revenues (expenses)	<u>134,556,768.69</u>	<u>(11,086,483.95)</u>	<u>(2,038,633.00)</u>
Income (loss) before other revenues, expenses, gains, or losses	<u>(11,745,533.50)</u>	<u>(12,905,468.76)</u>	<u>1,460,252.00</u>
Capital appropriations	6,691,674.63	-	-
Capital gifts and grants (university gifts include \$630,424.73 from ETSU Foundation)	800,880.33	51,676.06	-
Additions to permanent endowments	-	1,962,093.20	-
Other	(453,239.44)	-	-
Total other revenues	<u>7,039,315.52</u>	<u>2,013,769.26</u>	<u>-</u>
Increase (decrease) in net assets	<u>(4,706,217.98)</u>	<u>(10,891,699.50)</u>	<u>1,460,252.00</u>
NET ASSETS			
Net assets - beginning of year	199,101,177.12	67,736,285.39	15,723,278.00
Net assets - end of year	<u>\$ 194,394,959.14</u>	<u>\$ 56,844,585.89</u>	<u>\$ 17,183,530.00</u>

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

**TENNESSEE BOARD OF REGENTS
EAST TENNESSEE STATE UNIVERSITY
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2009**

CASH FLOWS FROM OPERATING ACTIVITIES	
Tuition and fees	\$ 59,928,886.77
Grants and contracts	44,509,374.03
Sales and services of educational activities	22,801,202.52
Payments to suppliers and vendors	(57,816,331.88)
Payments to employees	(143,257,314.33)
Payments for benefits	(44,931,243.55)
Payments for scholarships and fellowships	(21,327,351.30)
Loans issued to students	(1,656,732.33)
Collection of loans from students	2,677,570.58
Interest earned on loans to students	90,200.91
Auxiliary enterprise charges:	
Residence halls	9,435,436.46
Bookstore	766,487.71
Food services	542,455.35
Wellness facility	1,255,221.34
Other auxiliaries	1,801,482.98
Other receipts	1,102,099.68
Net cash used by operating activities	<u>(124,078,555.06)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
State appropriations	92,344,677.00
Gifts and grants received for other than capital or endowment purposes	45,820,867.39
Federal student loan receipts	41,163,445.79
Federal student loan disbursements	(48,681,403.86)
Changes in deposits held for others	6,950,294.42
Net cash provided by noncapital financing activities	<u>137,597,880.74</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Proceeds from capital debt	81,934,417.75
Capital appropriations	6,691,674.63
Capital grants and gifts received	330,455.60
Purchases of capital assets and construction	(39,067,649.78)
Principal paid on capital debt	(51,417,865.91)
Interest paid on capital debt	(3,731,067.86)
Recovery of bond issue costs paid on new debt issue	805,865.13
Other receipts	2,489,015.03
Net cash used by capital and related financing activities	<u>(1,965,155.41)</u>
CASH FLOWS FROM INVESTING ACTIVITIES	
Proceeds from sales and maturities of investments	16,007,220.00
Income on investments	2,178,335.20
Purchase of investments	(18,002,974.17)
Net cash provided by investing activities	<u>182,581.03</u>
Net increase in cash and cash equivalents	11,736,751.30
Cash - beginning of year	58,657,803.32
Cash - end of year	<u>\$ 70,394,554.62</u>

**TENNESSEE BOARD OF REGENTS
EAST TENNESSEE STATE UNIVERSITY
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2009**

Reconciliation of operating loss to net cash used by operating activities:	
Operating loss	\$ (146,302,302.19)
Adjustments to reconcile operating loss to net cash used by operating activities:	
Depreciation expense	11,534,437.34
Other adjustments	135,361.50
Change in assets and liabilities:	
Receivables, net	(3,379,068.85)
Inventories	37,231.69
Prepaid expenses and deferred charges	(983,960.68)
Other assets	(96,076.62)
Accounts payable	1,443,626.68
Accrued liabilities	2,890,229.29
Net OPEB obligation	3,224,987.02
Deferred revenue	6,160,798.49
Deposits	338,937.30
Compensated absences	(103,594.28)
Loans to students	1,020,838.25
Net cash used by operating activities	<u>\$ (124,078,555.06)</u>
Noncash transactions	
Gifts in-kind	\$ 278,243.96
Gifts of capital assets	\$ 470,424.73
Unrealized gains on investments	\$ 1,409.83
Loss on disposal of capital assets	\$ (68,749.78)

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

**Tennessee Board of Regents
East Tennessee State University
Notes to the Financial Statements
June 30, 2009**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

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

The East Tennessee State University Foundation and the Medical Education Assistance Corporation are considered component units of the university. Although the university does not control the timing or amount of receipts from these organizations, the majority of resources, or income thereon, that these organizations hold and invest are restricted to the activities of the university by the donors. Because these restricted resources held by the foundation and the corporation can only be used by, or for the benefit of, the university, these organizations are considered component units of the university and are discretely presented in the university's financial statements. See Note 20 for more detailed information about the component units and how to obtain their reports.

Basis of Presentation

The financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) applicable to governmental colleges and universities engaged in business-type activities as prescribed by the Governmental Accounting Standards Board (GASB).

Basis of Accounting

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

Tennessee Board of Regents
East Tennessee State University
Notes to the Financial Statements (Cont.)
June 30, 2009

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

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

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; (5) certain grants and contracts; and (6) gifts and nonexchange transactions.

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

Inventories

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

Compensated Absences

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

Capital Assets

Capital assets, which include property, plant, equipment, library holdings, and software, 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.

**Tennessee Board of Regents
East Tennessee State University
Notes to the Financial Statements (Cont.)
June 30, 2009**

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. The capitalization threshold for software is set at \$100,000.

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 university's net assets are classified as follows:

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

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 university is legally or contractually obligated to spend in accordance with restrictions imposed by external third parties.

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

**Tennessee Board of Regents
East Tennessee State University
Notes to the Financial Statements (Cont.)
June 30, 2009**

Scholarship Discounts and Allowances

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

NOTE 2. CASH

At June 30, 2009, cash consists of \$10,160,519.93 in bank accounts, \$35,000.00 of petty cash on hand, \$56,112,395.15 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer, \$4,077,939.54 in LGIP deposits for capital projects, and \$8,700.00 held by the State Treasurer for the benefit of the university.

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

The LGIP's investment policy and required risk disclosures are presented in the *State of Tennessee Treasurer's Report*. That report is available on the state's website at <http://www.tn.gov/treasury/> or by calling (615) 741-2956.

NOTE 3. INVESTMENTS

All investments permitted to be reported at fair value under GASB Statement 31, *Accounting and Financial Reporting for Certain Investments and External Investment*

**Tennessee Board of Regents
East Tennessee State University
Notes to the Financial Statements (Cont.)
June 30, 2009**

Pools, are reported at fair value, including those with a maturity date of one year or less at the time of purchase.

As of June 30, 2009, the university had the following investments and maturities.

<u>Investment Type</u>	<u>Fair Value</u>	<u>Investment Maturities (in Years)</u> 1 to 5
U. S. agency obligations	<u>\$16,030,560.00</u>	<u>\$16,030,560.00</u>

Interest rate risk - Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of a debt investment. The university does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit risk - Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The university is authorized by statute to invest funds in accordance with Tennessee Board of Regents policies. Under the current policy, funds other than endowments may be invested only in obligations of the United States or its agencies backed by the full faith and credit of the United States; repurchase agreements for United States securities; certificates of deposit in banks and savings and loan associations; banker's acceptances; commercial paper; money market mutual funds; and the State of Tennessee Local Government Investment Pool (LGIP). The policy requires that investments of endowments in equity securities be limited to funds from private gifts or other sources external to the university and that endowment investments be prudently diversified. Securities are rated using Standard and Poor's, Moody's, and/or Fitch and are presented below using the Standard and Poor's rating scale. Tennessee Board of Regents policy restricts investments in banker's acceptances and commercial paper. The policy requires that prime banker's acceptances must be issued by domestic banks with a minimum AA rating or foreign banks with a AAA long-term debt rating by a majority of the rating services that have rated the issuer. The policy further requires that commercial paper must be issued by corporations with a minimum rating of A1 or equivalent as provided by the majority of the rating services that rate the issuer. If there is no long-term debt rating, the short-term debt must be rated A1 by all rating services (minimum of two). Commercial paper of a banking institution must not be purchased.

**Tennessee Board of Regents
East Tennessee State University
Notes to the Financial Statements (Cont.)
June 30, 2009**

At June 30, 2009, the university's investments were rated as follows:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Credit Quality Rating</u>	
		<u>AAA</u>	<u>Unrated</u>
LGIP	\$60,190,334.69	\$ -	\$60,190,334.69
U. S. agency obligations	<u>16,030,560.00</u>	<u>16,030,560.00</u>	<u>-</u>
Total	<u>\$76,220,894.69</u>	<u>\$16,030,560.00</u>	<u>\$60,190,334.69</u>

Concentration of credit risk - The Tennessee Board of Regents (TBR) policy restricts investments in banker's acceptances, commercial paper, and money market mutual funds. The policy limits banker's acceptances to not exceed 20% of total investments on the date of acquisition and limits the combined amount of banker's acceptances and commercial paper to not exceed 35% of total investments at the date of acquisition. Additionally, no more than 5% of total investments at the date of acquisition may be invested in the commercial paper of a single issuer. The policy further limits the total holdings of an issuer's commercial paper to not more than 2% of the issuing corporation's total outstanding commercial paper. Tennessee Board of Regents policy limits investments in money market mutual funds to not exceed 10% of total investments on the date of acquisition. More than 5% of the university's investments were invested in the following single issuers:

<u>Issuer</u>	<u>Percentage of Total Investments</u>
	<u>June 30, 2009</u>
Federal Home Loan Mortgage Corporation (FHLM) obligations	87.0%
Federal National Mortgage Association (FNMA) obligations	13.0%

NOTE 4. RECEIVABLES

Receivables included the following:

**Tennessee Board of Regents
East Tennessee State University
Notes to the Financial Statements (Cont.)
June 30, 2009**

	<u>June 30, 2009</u>
Student accounts receivable	\$ 8,199,627.36
Grants receivable	12,999,534.23
Notes receivable	384,925.99
State appropriation receivable	188,731.00
Other receivables	<u>5,999,940.11</u>
Subtotal	27,772,758.69
Less allowance for doubtful accounts	<u>2,124,919.76</u>
Total receivables	<u>\$25,647,838.93</u>

Federal Perkins Loan Program funds included the following:

	<u>June 30, 2009</u>
Perkins loans receivable	\$8,574,092.27
Less allowance for doubtful accounts	<u>1,829,627.08</u>
Total	<u>\$6,744,465.19</u>

NOTE 5. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2009, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Transfers</u>	<u>Reductions</u>	<u>Ending Balance</u>
Land	\$ 24,163,603.13	\$ 407,858.67	\$ -	\$ -	\$ 24,571,461.80
Land improvements and infrastructure	27,637,701.97	-	4,326,730.70	-	31,964,432.67
Buildings	247,893,071.88	-	17,473,528.74	-	265,366,600.62
Equipment	29,218,263.70	1,921,588.76	-	967,027.52	30,172,824.94
Library holdings	11,871,105.26	559,116.63	-	1,931,637.51	10,498,584.38
Software	4,077,642.82	314,394.75	-	-	4,392,037.57
Projects in progress	<u>14,106,030.38</u>	<u>36,295,663.27</u>	<u>(21,800,259.44)</u>	<u>-</u>	<u>28,601,434.21</u>

**Tennessee Board of Regents
East Tennessee State University
Notes to the Financial Statements (Cont.)
June 30, 2009**

Total	<u>358,967,419.14</u>	<u>39,498,622.08</u>	-	<u>2,898,665.03</u>	<u>395,567,376.19</u>
Less accum. depreciation:					
Land improvements and infrastructure	10,247,778.29	1,319,970.45	-	-	11,567,748.74
Buildings	96,118,443.01	6,695,839.45	-	-	102,814,282.46
Equipment	19,576,495.26	1,853,510.02	-	898,277.74	20,531,727.54
Library holdings	6,936,578.59	1,249,412.50	-	1,931,637.51	6,254,353.58
Software	<u>959,776.57</u>	<u>415,704.92</u>	-	-	<u>1,375,481.49</u>
Total accum. depreciation	<u>133,839,071.72</u>	<u>11,534,437.34</u>	-	<u>2,829,915.25</u>	<u>142,543,593.81</u>
Capital assets, net	<u>\$225,128,347.42</u>	<u>\$27,964,184.74</u>	\$ -	<u>\$ 68,749.78</u>	<u>\$253,023,782.38</u>

NOTE 6. CAPITAL LEASES

The university has entered into an Enhanced Use Lease Agreement with the United States Department of Veterans Affairs for certain real property, including land and several buildings, at the Veterans Affairs Medical Center in Johnson City, Tennessee. The lease is for a period of 35 years. In lieu of lease payments, the university has assumed responsibility for all capital and recurring costs of maintaining the property covered by the agreement.

In conjunction with the lease, the university entered into a memorandum of agreement with the Department of Veterans Affairs to construct a new building (the Basic Science Building) with joint funding from the State of Tennessee and the federal government. In accordance with the memorandum of agreement, the state provided \$18 million to the federal government for its share of the total construction costs (\$34,195,153.41). The Basic Science Building is also included under the provisions of the Enhanced Use Lease Agreement.

The university is renovating several other buildings on the VA campus as funds become available. During the 2009 fiscal year, the university completed renovation on Building 2, Building 6, Building 7, and Building 52. The cumulative capitalized cost of these renovations was \$2,144,106.60.

The university's leasing of the Basic Science Building and the other buildings on the VA campus will constitute a capital lease agreement. The lease term is substantially equal to the estimated useful life of the leased property. Accordingly, the university has

**Tennessee Board of Regents
East Tennessee State University
Notes to the Financial Statements (Cont.)
June 30, 2009**

capitalized the cost of the buildings at \$49,779,041.11. At June 30, 2009, the buildings are reported at \$40,071,019.08, net of accumulated depreciation of \$9,708,022.03.

NOTE 7. ACCOUNTS PAYABLE

Accounts payable included the following:

	<u>June 30, 2009</u>
Vendors payable	\$6,585,344.77
Unapplied student payments	1,781.35
Other payables	<u>504,918.63</u>
Total	<u>\$7,092,044.75</u>

NOTE 8. LONG-TERM LIABILITIES

Long-term liabilities activity for the year ended June 30, 2009, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Current Portion</u>
Payables:					
Note	\$ 199,999.84	\$ -	\$ 49,999.84	\$ 150,000.00	\$ 50,000.00
Loan	1,689,158.05	-	140,144.91	1,549,013.14	150,165.27
TSSBA debt:					
Bonds	62,572,471.55	55,152,886.25	7,151,488.18	110,573,869.62	4,027,238.44
Commercial paper	<u>19,297,843.93</u>	<u>26,781,531.50</u>	<u>44,076,232.98</u>	<u>2,003,142.45</u>	<u>-</u>
Subtotal	<u>83,759,473.37</u>	<u>81,934,417.75</u>	<u>51,417,865.91</u>	<u>114,276,025.21</u>	<u>4,227,403.71</u>
Other liabilities:					
Deferred revenue	9,279,284.34	18,406,855.77	9,303,802.81	18,382,337.30	15,562,676.30
Compensated absences	10,393,307.84	5,435,607.39	5,539,201.67	10,289,713.56	2,581,997.82
Due to grantor	7,440,376.64	-	-	7,440,376.64	-
Net OPEB obligation	<u>3,454,735.00</u>	<u>3,224,987.02</u>	<u>-</u>	<u>6,679,722.02</u>	<u>-</u>
Subtotal	<u>30,567,703.82</u>	<u>27,067,450.18</u>	<u>14,843,004.48</u>	<u>42,792,149.52</u>	<u>18,144,674.12</u>
Total long-term liabilities	<u>\$114,327,177.19</u>	<u>\$109,001,867.93</u>	<u>\$66,260,870.39</u>	<u>\$157,068,174.73</u>	<u>\$22,372,077.83</u>

**Tennessee Board of Regents
East Tennessee State University
Notes to the Financial Statements (Cont.)
June 30, 2009**

Note Payable

The Tennessee Board of Regents, on behalf of the university, borrowed funds for the renovation of the Memorial Athletic Medical Center (“BucSports”). The note bears an annually adjusted interest rate equal to the average Local Government Investment Pool rate for the previous year, a face amount of \$500,000.00, a minimum annual debt service of \$50,000.00 plus interest with payments due annually to 2012. The balance owed by the university was \$150,000.00 at June 30, 2009.

Debt service requirements to maturity for the note payable at June 30, 2009, are as follows:

Year Ending <u>June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2010	\$ 50,000.00	\$8,120.00	\$ 58,120.00
2011	50,000.00	6,090.00	56,090.00
2012	<u>50,000.00</u>	<u>4,060.00</u>	<u>54,060.00</u>
	<u>\$150,000.00</u>	<u>\$18,270.00</u>	<u>\$168,270.00</u>

Loan Payable

The Tennessee General Assembly earmarked in Section 41, Item 41 of Chapter 563 of the Public Acts of 1989 the amount of \$3,000,000 from the funds appropriated in Section 1, Title 111-25 of Chapter 563 of the Public Acts of 1989 for the East Tennessee State University Clinical Education Facility. These funds were intended to be an interest-bearing loan from the General Fund to the Tennessee Board of Regents on behalf of East Tennessee State University. The loan bears an interest rate of 7.15% and has a principal amount of \$3,000,000.00, a minimum annual debt service of \$260,919.73, and a due date of January 1, 2017. The balance owed by the university was \$1,549,013.14 at June 30, 2009.

**Tennessee Board of Regents
East Tennessee State University
Notes to the Financial Statements (Cont.)
June 30, 2009**

Debt service requirements to maturity for the loan payable at June 30, 2009, are as follows:

Year Ending <u>June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2010	\$ 150,165.27	\$110,754.46	\$ 260,919.73
2011	160,902.09	100,017.64	260,919.73
2012	172,406.59	88,513.14	260,919.73
2013	184,733.66	76,186.07	260,919.73
2014	197,942.11	62,977.61	260,919.72
2015 - 2017	<u>682,863.42</u>	<u>99,895.59</u>	<u>782,759.01</u>
	<u>\$1,549,013.14</u>	<u>\$538,344.51</u>	<u>\$2,087,357.65</u>

TSSBA Debt - Bonds

Bonds, with interest rates ranging from 2.0% to 5.125%, were issued by the Tennessee State School Bond Authority (TSSBA). The bonds are due serially until 2039 and are secured by pledges of the facilities' revenues to which they relate and certain other revenues and fees of the university, including state appropriations. The bonded indebtedness with the Tennessee State School Bond Authority included in long-term liabilities on the statement of net assets is shown net of assets held by the authority in the debt service reserve and unexpended debt proceeds. The reserve amount was \$4,093,706.22 at June 30, 2009. Unexpended debt proceeds were \$4,011,527.77 at June 30, 2009, and were restricted for capital projects.

Debt service requirements to maturity for the university's portion of TSSBA bonds at June 30, 2009, are as follows:

Year Ending <u>June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2010	\$ 4,027,238.44	\$ 5,474,498.42	\$ 9,501,736.86
2011	3,841,960.05	5,246,736.49	9,088,696.54
2012	3,962,328.24	5,106,121.94	9,068,450.18
2013	4,014,203.03	4,967,175.99	8,981,379.02
2014	4,184,334.55	4,785,194.10	8,969,528.65

**Tennessee Board of Regents
East Tennessee State University
Notes to the Financial Statements (Cont.)
June 30, 2009**

2015-2019	22,595,364.46	21,234,928.65	43,830,293.11
2020-2024	25,874,334.23	15,662,714.33	41,537,048.56
2025-2029	20,659,129.56	9,681,265.41	30,340,394.97
2030-2034	15,237,326.46	5,261,135.74	20,498,462.20
2035-2039	<u>6,177,650.60</u>	<u>1,741,252.90</u>	<u>7,918,903.50</u>
	<u>\$110,573,869.62</u>	<u>\$79,161,023.97</u>	<u>\$189,734,893.59</u>

TSSBA Debt - Commercial Paper

The Tennessee State School Bond Authority issues commercial paper to finance the costs of various capital projects during their construction phase. When projects are placed in service, long-term, fixed-rate debt is issued by TSSBA to finance the project over its useful payback period and the commercial paper is redeemed. The amount issued for projects at the university was \$2,003,142.45 at June 30, 2009.

For the commercial paper program, the Tennessee State School Bond Authority maintains an interest rate reserve fund. The university 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 university when the notes are converted to bonds. The interest earned on the reserve is used to pay interest due during the month.

More detailed information regarding the bonds and commercial paper can be found in the notes to the financial statements in the financial report for the Tennessee State School Bond Authority. That report is available on the state's website at <http://www.tn.gov/comptroller/bf/tssbacafr.htm>.

NOTE 9. ENDOWMENTS

If a donor has not provided specific instructions to the university, state law permits the university to authorize for expenditure the earnings of the investments of endowment funds. When administering its power to spend these earnings, the university is required to consider the university's long-term and short-term needs, present and anticipated financial requirements, expected total 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.

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The university's donor-restricted endowments are invested to produce only interest income. Under the spending plan established by the university, the total income has been authorized for expenditure. However, based on the university's needs for scholarship funding, the university chooses to spend only a portion of the interest income each year. The remaining amount, if any, is retained to be used in future years.

At June 30, 2009, net appreciation of \$13,336.70 is available to be spent, all of which is included in restricted net assets expendable for scholarships and fellowships.

NOTE 10. UNRESTRICTED NET ASSETS

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

	<u>June 30, 2009</u>
Working capital	\$ 7,379,246.82
Encumbrances	1,314,023.96
Designated fees	2,331,269.10
Auxiliaries	783,809.03
Quasi-endowment	10,946,136.49
Plant construction	10,624,556.59
Renewal and replacement of equipment	12,071,651.47
Debt retirement	1,337,138.53
Undesignated	<u>3,047,239.33</u>
 Total	 <u>\$49,835,071.32</u>

NOTE 11. PLEDGED REVENUES

The university has pledged certain revenues and fees, including state appropriations, to repay \$110,573,869.62 in revenue bonds issued from June 16, 1976, to April 15, 2009. Proceeds from the bonds provided financing for construction and renovation projects. The bonds are payable through 2039. Annual principal and interest payments on the

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bonds are expected to require 2.69% of available revenues. The total principal and interest remaining to be paid on the bonds is \$189,734,893.59. Principal and interest paid for the current year and total available revenues were \$6,152,791.34 and \$229,062,207.36, respectively.

NOTE 12. PENSION PLANS

A. Defined Benefit Plan

Tennessee Consolidated Retirement System

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

The TCRS issues a publicly available financial report that includes financial statements and required supplementary information for SETHEEPP. That report is available on the state's website at <http://www.tn.gov/treasury/tcrs/index.html>.

Funding Policy - Plan members are noncontributory. The university is required to contribute an actuarially determined rate. The current rate is 13.02% of annual covered payroll. Contribution requirements for the university are established and may be amended by the TCRS' Board of Trustees. The university's contributions to TCRS for the years ended June 30, 2009, 2008, and 2007, were \$6,187,232.82, \$6,372,126.18, and \$6,067,796.51. Contributions met the requirements for each year.

B. Defined Contribution Plans

Optional Retirement Plans (ORP)

Plan Description - The university contributes to three defined contribution plans: Teachers Insurance and Annuity Association-College Retirement

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

Funding Policy - Plan members are noncontributory. The university contributes an amount equal to 10% of the employee's base salary up to the social security wage base and 11% above the social security wage base. Contribution requirements are established and amended by state statute. The contribution made by the university to the plans was \$6,767,617.57 for the year ended June 30, 2009, and \$6,819,497.22 for the year ended June 30, 2008. Contributions met the requirements for each year.

NOTE 13. OTHER POST-EMPLOYMENT BENEFITS

Healthcare is the only "other postemployment benefit" (OPEB) provided to employees. The State of Tennessee administers a group health insurance program which provides postemployment health insurance benefits to eligible university retirees. This program includes two plans – the State Employee Group Plan and the Medicare Supplement Plan. For accounting purposes, the plans are agent multiple-employer defined benefit OPEB plans. Benefits are established and amended by an insurance committee created by *Tennessee Code Annotated (TCA)* Section 8-27-201 for the state plan and *TCA* 8-27-701 for the Medicare Supplement Plan. Prior to reaching age 65, retirees may participate in the State Employee Group Plan. Members of this plan have the option of choosing a preferred provider organization (PPO), point of service (POS), or health maintenance organization (HMO) plan for healthcare benefits. Subsequent to age 65, retirees who are also in the state's retirement system may participate in the Medicare Supplement Plan that does not include pharmacy. The state makes on-behalf payments to the Medicare Supplement Plan for the university's eligible retirees; see Note 19. The plans are reported in the *Tennessee Comprehensive Annual Financial Report*. That report is available on the state's website at <http://www.tn.gov/finance/act/cafr.html>, or by calling (615) 741-2140.

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Special Funding Situation

The State of Tennessee is legally responsible for contributions to the Medicare Supplement Plan that covers the retirees of other governmental entities, including East Tennessee State University. The state is the sole contributor for the university retirees that participate in the Medicare Supplement Plan and, therefore, is acting as the employer.

Funding Policy

The premium requirements of members of the State Employee Group Plan are established and may be amended by the insurance committee. The plan is self-insured and financed on a pay-as-you-go basis with the risk shared equally among the participants. Claims liabilities of the plan are periodically computed using actuarial and statistical techniques to establish premium rates. Administrative costs of the plan are allocated to participants. Retirees in the State Employee Group Plan pay the same base premium as active employees in the plan adjusted for years of service. Retirees with 30 years of service pay 20% of the total premium. Retirees with 20 but less than 30 years of service pay 30% of the total premium. Retirees with less than 20 years of service pay 40% of the total premium.

ETSU Annual OPEB Cost and Net OPEB Obligation

State Employee
Group Plan

Annual required contribution (ARC)	\$5,355,848.03
Interest on the net OPEB obligation	155,463.08
Adjustment to the ARC	<u>(151,311.09)</u>
Annual OPEB cost	5,360,000.02
Amount of contribution	<u>(2,135,013.00)</u>
Increase (decrease) in net OPEB obligation	3,224,987.02
Net OPEB obligation – beginning of year	<u>3,454,735.00</u>
Net OPEB obligation – end of year	<u>\$6,679,722.02</u>

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<u>Year-End</u>	<u>Plan</u>	<u>Annual OPEB Cost</u>	<u>Percentage of Annual OPEB Cost Contributed</u>	<u>Net OPEB Obligation at Year-end</u>
June 30, 2009	State Employee Group Plan	\$5,360,000.02	39.8%	\$6,679,722.02
June 30, 2008	State Employee Group Plan	\$526,000.00	33.0%	\$352,424.56

Funded Status and Funding Progress

The funded status of the university's portion of the State Employee Group Plan as of July 1, 2007, was as follows:

Actuarial valuation date	July 1, 2007
Actuarial accrued liability (AAL)	\$47,831,000.00
Actuarial value of plan assets	-
Unfunded actuarial accrued liability (UAAL)	\$47,831,000.00
Actuarial value of assets as a % of the AAL	0%
Covered payroll (active plan members)	\$97,727,873.49
UAAL as percentage of covered payroll	48.9%

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future, and actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. The schedule of funding progress, presented as RSI following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Actuarial Methods and Assumptions

Calculations are based on the types of benefits provided under the terms of the substantive plan at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point. Actuarial calculations reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

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In the July 1, 2007, actuarial valuation, the Projected Unit Credit actuarial cost method was used. The actuarial assumptions included a 4.5 percent investment rate of return (net of administrative expenses) and an annual healthcare cost trend rate of 7 percent initially, increased to 11 percent in the second year and then reduced by decrements to an ultimate rate of 5 percent after 12 years. Both rates include a 3 percent inflation assumption. The unfunded actuarial accrued liability is being amortized as a level percentage of payroll on a closed basis over a 30-year period beginning with July 1, 2007.

NOTE 14. 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 amount of settlements have not exceeded insurance coverage for each of the past three fiscal years. The Risk Management Fund is also responsible for claims for damages 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 \$5 million.

The university participates in the Risk Management Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the university based on a percentage of the university's expected loss costs, which include both experience and exposures. This charge considers recent trends in actual claims experience of the state as a whole. An actuarial valuation is performed as of fiscal year-end to determine the fund liability and premium allocation. Information regarding the determination of the claims liabilities and the changes in the balances of the claims liabilities for the years ended June 30, 2009, and June 30, 2008, are presented in the *Tennessee Comprehensive Annual Financial Report*. The CAFR is available on the state's website at <http://www.tn.gov/finance/act/cafr.html>. Since the university 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 university for

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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, 2009, the Risk Management Fund held \$127 million in cash and cash equivalents designated for payment of claims.

At June 30, 2009, the scheduled coverage for the university was \$634,478,000 for buildings and \$161,390,900 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 university participates in the Employee Group Insurance Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the university based on estimates of the ultimate cost of claims, including the 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 15. COMMITMENTS AND CONTINGENCIES

Sick Leave

The university records the cost of sick leave when paid. Generally, since sick leave (earned one day per month with unlimited accumulation) is paid only when an employee dies or is absent because of illness, injury, or related family death, there is no liability for sick leave at June 30. The dollar amount of unused sick leave was \$45,780,220.44 at June 30, 2009.

Operating Leases

The university has entered into various operating leases for buildings. Such leases will probably continue to be required. Expenses under operating leases for real property were \$330,516.51 for the year ended June 30, 2009. All operating leases are cancelable at the lessee's option.

Construction in Progress

At June 30, 2009, outstanding commitments under construction contracts totaled \$11,474,452.87 for the Surface Parking project, the Housing Renovations project, the

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Coal Boiler Safety project, the Electrical Upgrades project, and various other projects, of which \$1,775,422.00 will be funded by future state capital outlay appropriations.

Litigation

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

NOTE 16. CHAIRS OF EXCELLENCE

The university had \$18,174,804.66 on deposit at June 30, 2009, with the State Treasurer for the university's Chairs of Excellence program. These funds are held in trust by the state and are not included in these financial statements.

NOTE 17. NATURAL CLASSIFICATIONS WITH FUNCTIONAL CLASSIFICATIONS

The university's operating expenses by functional classification for the year ended June 30, 2009, are as follows:

Functional Classification	Natural Classification					Total
	Salaries	Benefits	Other Operating	Scholarships	Depreciation	
Instruction	\$ 86,116,377.66	\$25,802,282.61	\$13,568,278.06	\$2,131,628.20	\$ -	\$127,618,566.53
Research	4,588,082.91	1,788,958.67	4,049,223.09	70,477.17	-	10,496,741.84
Public service	11,884,639.55	4,158,046.58	5,252,519.32	85,295.84	-	21,380,501.29
Academic support	13,384,309.23	4,808,286.92	3,779,910.76	354,080.03	-	22,326,586.94
Student services	9,183,049.31	3,269,673.97	4,285,766.76	1,604,899.09	-	18,343,389.13
Institutional support	12,783,459.77	4,887,607.62	302,113.87	91,932.89	-	18,065,114.15
Operation & maintenance of plant	6,095,583.22	3,149,786.38	21,602,471.98	-	-	30,847,841.58
Scholarships & fellowships	25,943.00	-	1,773,851.39	16,830,308.78	-	18,630,103.17
Auxiliary	1,833,076.47	587,625.75	5,072,557.26	167,824.03	-	7,661,083.51
Depreciation	-	-	-	-	11,534,437.34	11,534,437.34
Total	<u>\$145,894,521.12</u>	<u>\$48,452,268.50</u>	<u>\$59,686,692.49</u>	<u>\$21,336,446.03</u>	<u>\$11,534,437.34</u>	<u>\$286,904,365.48</u>

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NOTE 18. AFFILIATED ENTITY NOT INCLUDED

The East Tennessee State University Research Foundation is a private, nonprofit foundation with the university as the sole beneficiary. The foundation's financial transactions are not included in the university's financial report. As reported in the Research Foundation's most recently audited financial report, at June 30, 2009, the assets of the Research Foundation totaled \$840,474.36, liabilities were \$575,756.67, and the net assets amounted to \$264,717.69.

NOTE 19. ON-BEHALF PAYMENTS

During the year ended June 30, 2009, the State of Tennessee made payments of \$135,361.50 on behalf of the university for retirees participating in the Medicare Supplement Plan. The Medicare Supplement Plan is a postemployment benefit healthcare plan and is discussed further in Note 13. The plan is reported in the *Tennessee Comprehensive Annual Financial Report*. That report is available on the state's website at <http://www.tn.gov/finance/act/cafr.html>.

NOTE 20. COMPONENT UNITS

East Tennessee State University Foundation

The East Tennessee State University Foundation is a legally separate, tax-exempt organization supporting East Tennessee State University. The foundation acts primarily as a fund-raising organization to supplement the resources that are available to the university in support of its programs. The 30-member board of the foundation is self-perpetuating and consists of graduates and friends of the university. Although the university does not control the timing or amount of receipts from the foundation, the majority of resources, or income thereon, that the foundation holds and invests are restricted to the activities of the university by the donors. Because these restricted resources held by the foundation can only be used by, or for the benefit of, the university, the foundation is considered a component unit of the university and is discretely presented in the university's financial statements.

During the year ended June 30, 2009, the foundation made distributions of \$2,439,113.79 to or on behalf of the university for both restricted and unrestricted

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purposes. Complete financial statements for the foundation can be obtained from Dr. David D. Collins, Vice President for Finance and Administration, P. O. Box 70601, Johnson City, TN 37614.

Cash and Cash Equivalents

In addition to demand deposits and petty cash on hand, this classification includes instruments which are readily convertible to known amounts of cash and which have original maturities of three months or less. At June 30, 2009, cash and cash equivalents consisted of \$120,178.98 in bank accounts, \$4,895,291.76 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer, and \$234,646.66 in cash held by others.

As described above, the foundation has deposits in the Local Government Investment Pool (LGIP) administered by the State Treasurer. The LGIP is part of the State Pooled Investment Fund. The fund's investment policy and required risk disclosures are presented in the *State of Tennessee Treasurer's Report*. That report is available on the state's website at <http://www.tn.gov/treasury> or by calling (615) 741-2956.

Investments

The foundation is authorized to invest funds in accordance with its board of directors' policies. All investments permitted to be reported at fair value under GASB Statement 31 are reported at fair value, including those with a maturity date of one year or less at the time of purchase.

At June 30, 2009, the foundation had the following investments and maturities.

<u>Investment Type</u>	<u>Fair Value</u>	<u>Investment Maturities (in Years)</u>				<u>No Maturity Date</u>
		<u>Less than 1</u>	<u>1 to 5</u>	<u>6 to 10</u>	<u>More than 10</u>	
U. S. agency obligations	\$ 2,494,370.00	\$ -	\$2,494,370.00	\$ -	\$ -	\$ -
Bond mutual funds	13,548,593.63	224,204.00	7,158,734.63	2,899,195.00	3,266,460.00	-
Equity mutual funds	<u>31,894,431.95</u>	-	-	-	-	<u>31,894,431.95</u>
Total	<u>\$47,937,395.58</u>	<u>\$224,204.00</u>	<u>\$9,653,104.63</u>	<u>\$2,899,195.00</u>	<u>\$3,266,460.00</u>	<u>\$31,894,431.95</u>

Interest rate risk - Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of a debt investment. In order to reduce its exposure to

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interest rate risk, the foundation will set limits regarding the weighted average maturity for each direct investment pool. In the case of U.S. federal securities, the weighted average of all investments should be less than three years.

Credit risk - Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Securities are rated using Standard and Poor's, Moody's, and/or Fitch and are presented below using the Standard and Poor's rating scale. The foundation policy is to limit all direct investments to securities with an investment rating of no less than Aaa as rated by Moody's and AAA as rated by Standard and Poor's.

At June 30, 2009, the foundation's investments were rated as follows:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Credit Quality Rating</u>				
		<u>AAA</u>	<u>AA</u>	<u>A</u>	<u>BBB or Less</u>	<u>Unrated</u>
LGIP	\$ 4,895,291.76	\$ -	\$ -	\$ -	\$ -	\$ 4,895,291.76
U. S. agency obligations	2,494,370.00	2,494,370.00	-	-	-	-
Bond mutual funds	<u>13,548,593.63</u>	<u>9,363,372.63</u>	<u>977,070.00</u>	<u>1,723,326.00</u>	<u>1,484,825.00</u>	<u>-</u>
Total	<u>\$20,938,255.39</u>	<u>\$11,857,742.63</u>	<u>\$977,070.00</u>	<u>\$ 1,723,326.00</u>	<u>\$1,484,825.00</u>	<u>\$ 4,895,291.76</u>

Investments of the foundation's endowment and similar funds are composed of the following:

	<u>Carrying Value June 30, 2009</u>
LGIP	\$ 234,646.66
U.S. agency obligations	2,494,370.00
Mutual funds	<u>40,868,275.67</u>
	<u>\$43,597,292.33</u>

Assets of endowment funds are pooled on a fair value basis, with each individual fund subscribing to or disposing of units on the basis of the fair value per unit at the beginning of the calendar quarter within which the transaction takes place. The units at June 30, 2009, had a fair value of \$0.7073797138 each. A total of 52,891,741 units were owned by endowments, and 760,731 units were owned by quasi-endowments.

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The following tabulations summarize changes in relationships between cost and fair values of the pooled assets:

FY 2009

	Pooled Assets		Net Gains (Losses)	Fair Value Per Unit
	Fair Value	Cost		
End of year	\$47,937,395.58	\$61,211,687.38	(\$13,274,291.80)	\$0.7073797138
Beginning of year	\$59,124,061.16	\$59,173,674.99	<u>(49,613.83)</u>	\$1.1136779515
Unrealized net losses			(13,323,905.63)	
Realized net losses			<u>(107,385.09)</u>	
Total net losses			<u>(\$13,431,290.72)</u>	

The average annual earnings per unit, exclusive of net gains, were \$.028 for the year ended June 30, 2009.

Pledges Receivable

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

	<u>June 30, 2009</u>
Current pledges	\$ 842,602.57
Pledges due in one to five years	1,807,910.03
Pledges due after five years	<u>164,682.50</u>
Subtotal	2,815,195.10
Less discounts to net present value	<u>(80,628.56)</u>
Total pledges receivable, net	<u>\$2,734,566.54</u>

Capital assets - Capital asset activity for the year ended June 30, 2009, was as follows:

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	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Land	\$ 49,200.00	\$ -	\$ 48,000.00	\$ 1,200.00
Buildings	299,000.00	-	-	299,000.00
Equipment	9,486.00	-	-	9,486.00
Projects in progress	<u>286,883.38</u>	<u>63,607.81</u>	<u>350,491.19</u>	<u>-</u>
Total	<u>644,569.38</u>	<u>63,607.81</u>	<u>398,491.19</u>	<u>309,686.00</u>
Less accum. depreciation:				
Buildings	<u>56,050.00</u>	<u>2,950.00</u>	<u>-</u>	<u>59,000.00</u>
Total accum. depreciation	<u>56,050.00</u>	<u>2,950.00</u>	<u>-</u>	<u>59,000.00</u>
Capital assets, net	<u>\$588,519.38</u>	<u>\$60,657.81</u>	<u>\$398,491.19</u>	<u>\$250,686.00</u>

Endowments

The ETSU Foundation's endowment consists of 410 individual funds established for a variety of purposes. Its endowment includes both donor-restricted endowment funds and funds designated by the Board of Directors to function as endowments. As required by GAAP, net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of relevant law - The Board of Directors of the ETSU Foundation has interpreted the Uniform Prudent Management of Institutional Funds Act (the Act) as adopted by Tennessee as preservation of the historical dollar value of the original gift. As a result of this interpretation, the ETSU Foundation classifies as restricted nonexpendable net assets (a) the original value of gifts donated to the nonexpendable endowment, (b) the original value of subsequent gifts to the nonexpendable endowment, (c) accumulations to the nonexpendable endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund, and (d) funds added should funds in the reserve account at June 30 exceed 20% of the nonexpendable net assets (total net assets less reserves). The remaining portion of the donor-restricted endowment fund that is not classified in restricted nonexpendable net assets is classified as restricted expendable net assets until those amounts are appropriated for expenditure by the foundation in a manner consistent with the standard of prudence prescribed by the Act. In accordance with

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the Act, the foundation considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. The duration and preservation of the fund
2. The purposes of the foundation and the endowment fund
3. General economic conditions
4. The possible effect of inflation or deflation
5. The expected total return from income and the appreciation of investments
6. Other resources of the foundation
7. The investment policies of the foundation

Return objectives and risk parameters - The foundation has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity or for a donor-specified period(s) as well as board-designated funds. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce results that over the long term, will achieve a total return equivalent to or greater than the foundation's financial requirements over the time horizon. The foundation expects its endowment funds, over time, to provide an average rate of return of approximately 7 percent annually. Actual returns in any given year may vary from this amount.

Strategies employed for achieving objectives - To satisfy its long-term rate-of-return objectives, the foundation relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The foundation targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk restraints.

Spending policy and how the investment objectives relate - The foundation has a policy of appropriating for distribution each year 3 to 5 percent of the average quarterly balance for the three preceding calendar years depending on the amount of reserve for each endowment. In establishing this policy, the foundation considered the long-term expected return on its endowment. Accordingly, over the long-term, the foundation expects the current spending policy to allow its endowment to grow at an average of 3 percent annually. This is consistent with the foundation's objective to

**Tennessee Board of Regents
East Tennessee State University
Notes to the Financial Statements (Cont.)
June 30, 2009**

maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

At June 30, 2009, net appreciation of \$7,267,807.84 is available to be spent, of which \$5,836,118.07 is included in restricted net assets expendable for scholarships and fellowships, \$92,151.68 is included in restricted net assets expendable for research, \$731,673.08 is included in restricted net assets expendable for instructional departmental uses, and \$607,865.01 is included in restricted net assets expendable for other purposes.

Medical Education Assistance Corporation

Medical Education Assistance Corporation (MEAC) is a legally separate, tax-exempt organization supporting East Tennessee State University. MEAC acts primarily as a physicians' practice group to supplement the resources that are available to the university in support of its medical programs. The 15-member board of MEAC is self-perpetuating and consists of the departmental chairs from Quillen College of Medicine, a representative from East Tennessee State University's Business and Finance Department, a representative from the Tennessee Board of Regents, and at-large faculty from the Quillen College of Medicine. Although the university does not control the timing or amount of receipts from MEAC, the residual income that MEAC earns is restricted to supporting medical education. Because these restricted resources held by MEAC can only be used by, or for the benefit of, the university, MEAC is considered a component unit of the university and is discretely presented in the university's financial statements.

During the year ended June 30, 2009, MEAC made distributions of \$1,437,303.00 to or on behalf of the university for both restricted and unrestricted purposes. Complete financial statements for MEAC can be obtained from Russell Lewis, Executive Director, P.O. Box 699, Mountain Home, Tennessee 37684.

Cash

At June 30, 2009, cash consisted of \$1,481,928.00 in bank accounts, \$2,135.00 of petty cash on hand, and \$6,857,105.00 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer.

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Notes to the Financial Statements (Cont.)
June 30, 2009**

As described above, the corporation has deposits in the Local Government Investment Pool (LGIP) administered by the State Treasurer. The LGIP is part of the State Pooled Investment Fund. The fund's investment policy and required risk disclosures are presented in the *State of Tennessee Treasurer's Report*. That report is available on the state's website at <http://www.tn.gov/treasury/> or by calling (615) 741-2956.

Investments

The corporation is authorized to invest funds in accordance with its board of directors' policies. The corporation's investments at June 30, 2009, consisted of certificates of deposit with original maturities greater than three months.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. MEAC has no investment policy limiting its investment choices based on ratings issued by nationally recognized statistical rating organizations. At June 30, 2009, MEAC had no rated investments, as deposits in LGIP are unrated.

Capital Assets

Capital asset activity for the year ended June 30, 2009, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Land	\$ 18,150	\$ -	\$ -	\$ 18,150
Leasehold improvements	307,564	-	4,707	302,857
Buildings	1,891,946	16,800	-	1,908,746
Equipment	<u>2,893,251</u>	<u>210,727</u>	<u>241,291</u>	<u>2,862,687</u>
Total	<u>5,110,911</u>	<u>227,527</u>	<u>245,998</u>	<u>5,092,440</u>
Less accumulated depreciation:				
Leasehold improvements	297,753	3,924	4,707	296,970
Buildings	65,649	48,845	-	114,494
Equipment	<u>2,411,581</u>	<u>188,411</u>	<u>241,291</u>	<u>2,358,701</u>
Total accumulated depreciation	<u>2,774,983</u>	<u>241,180</u>	<u>245,998</u>	<u>2,770,165</u>
Capital assets, net	<u>\$2,335,928</u>	<u>(\$13,653)</u>	<u>\$ -</u>	<u>\$2,322,275</u>

**Tennessee Board of Regents
East Tennessee State University
Notes to the Financial Statements (Cont.)
June 30, 2009**

Long-term Liabilities

Long-term liabilities activity for the year ended June 30, 2009, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Current Portion</u>
Note payable	\$1,657,189	\$ -	\$27,444	\$1,629,745	\$ 33,112
Compensated absences	<u>544,565</u>	<u>14,078</u>	<u>-</u>	<u>558,643</u>	<u>111,729</u>
Total long-term liabilities	<u>\$2,201,754</u>	<u>\$14,078</u>	<u>\$27,444</u>	<u>\$2,188,388</u>	<u>\$144,841</u>

NOTE 21. VOLUNTARY BUYOUT PROGRAM

The university implemented a Voluntary Buyout Plan in fiscal year 2009 as a strategy to assist the university in addressing budgetary constraints due to state appropriation reversions and potential budget reductions in the forthcoming fiscal year. One hundred twenty-two participated in the Voluntary Buyout Plan with 103 terminating by June 30, 2009, and 19 terminating by August 30, 2009.

Severance pay was payable the month following the employee separation date, between July and September 2009. Severance pay included:

- Base severance payment equal to three times the employee's monthly rate of pay in effect on March 30, 2009.
- Service payment of \$500 for each full or partial year of university service as of June 30, 2009, or the separation date.
- Amount equivalent to the employee's next longevity payment based on their years of creditable state service.
- Amount equivalent to six months of the university's portion of the monthly health insurance premium.

Severance benefits included:

- Tuition assistance of \$10,800 over two years at technology centers, community colleges, and state universities in Tennessee.
- Membership in the university wellness center for one year.
- Faculty/staff rates for university athletic events for one year.
- University-provided e-mail account for one year.

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Notes to the Financial Statements (Cont.)
June 30, 2009**

In addition, the university offered an incentive of \$500 per year of service, up to a maximum of \$15,000, to faculty to participate in the Post-Retirement Service Program as authorized by Tennessee Board of Regents Guideline P-160. Four faculty chose the Post-Retirement option with one terminating by June 30, 2009, and three terminating by August 30, 2009.

As of June 30, 2009, expenditures for payout of accrued annual leave, compensatory time, or worked holidays for the Voluntary Buyout Plan and Post-Retirement Service Program were \$907,637.52. Accrued expenses for severance pay were \$2,946,618.93 at June 30, 2009.

**Tennessee Board of Regents
 East Tennessee State University
 Required Supplementary Information
 Schedule of Funding Progress
 Unaudited**

Actuarial Valuation Date	Plan	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll [(b-a)/c]
July 1, 2007	State Employee Group Plan	\$ -	\$47,831,000.00	\$47,831,000.00	0%	\$97,727,873.49	48.9%

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SUPPLEMENTARY INFORMATION
SCHEDULE OF CASH FLOWS - EAST TENNESSEE STATE UNIVERSITY FOUNDATION
FOR THE YEAR ENDED JUNE 30, 2009**

CASH FLOWS FROM OPERATING ACTIVITIES

Gifts and contributions	\$ 3,890,172.93
Payments to suppliers and vendors	(1,828,305.62)
Payments for scholarships and fellowships	(1,368,320.41)
Payments to or on behalf of East Tennessee State University	(2,032,911.61)
Other receipts	504,724.85
Net cash used by operating activities	<u>(834,639.86)</u>

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

Gifts and grants received for other than capital or endowment purposes	872,304.00
Private gifts for endowment purposes	1,962,093.20
Other noncapital financing receipts	39,501.92
Net cash provided by noncapital financing activities	<u>2,873,899.12</u>

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES

Capital grants and gifts received	51,676.06
Purchases of capital assets and construction	(63,607.81)
Net cash used by capital and related financing activities	<u>(11,931.75)</u>

CASH FLOWS FROM INVESTING ACTIVITIES

Proceeds from sales and maturities of investments	4,394,244.54
Income on investments	1,608,857.39
Purchases of investments	(6,432,256.93)
Net cash used by investing activities	<u>(429,155.00)</u>

Net increase in cash and cash equivalents	1,598,172.51
Cash and cash equivalents - beginning of year	3,651,944.89
Cash and cash equivalents - end of year	<u>\$ 5,250,117.40</u>

Reconciliation of operating loss to net cash used by operating activities:

Operating loss	\$ (1,818,984.81)
Adjustments to reconcile operating loss to net cash used by operating activities:	
Depreciation expense	2,950.00
Change in assets and liabilities:	
Receivables, net	1,085,017.51
Accounts payable	(103,622.56)
Net cash used by operating activities	<u>\$ (834,639.86)</u>

Noncash transactions

Gifts in-kind	\$ 628,906.80
Unrealized losses on investments	\$ (13,224,677.97)
Loss on disposal of capital assets	\$ (398,491.19)

**TENNESSEE BOARD OF REGENTS
EAST TENNESSEE STATE UNIVERSITY
SUPPLEMENTARY INFORMATION
SCHEDULE OF CASH FLOWS - MEDICAL EDUCATION ASSISTANCE CORPORATION
FOR THE YEAR ENDED JUNE 30, 2009**

CASH FLOWS FROM OPERATING ACTIVITIES

Collections from patient charges	\$ 35,293,444.00
Payments to suppliers and vendors	(10,185,275.00)
Payments to employees	(22,670,400.00)
Payments for benefits	(2,097,389.00)
Other receipts	716,094.00
Net cash provided by operating activities	<u>1,056,474.00</u>

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

Other noncapital financing payments	(2,309,607.00)
Net cash used by noncapital financing activities	<u>(2,309,607.00)</u>

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES

Purchase of capital assets and construction	(227,527.00)
Principal paid on capital debt	(27,445.00)
Interest paid on capital debt	(115,460.00)
Net cash used by capital and related financing activities	<u>(370,432.00)</u>

CASH FLOWS FROM INVESTING ACTIVITIES

Proceeds from sales and maturities of investments	1,200,000.00
Income on investments	386,434.00
Other investing receipts	22,372.00
Net cash provided by investing activities	<u>1,608,806.00</u>

Net decrease in cash	(14,759.00)
Cash - beginning of year	8,355,927.00
Cash - end of year	<u>\$ 8,341,168.00</u>

Reconciliation of operating income to net cash provided by operating activities:

Operating income	\$ 3,498,885.00
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation expense	241,179.00
Change in assets and liabilities:	
Receivables, net	393,918.00
Prepaid expenses and deferred charges	(2,739,612.00)
Accounts payable	96,593.00
Deferred revenues	(46,458.00)
Compensated absences	(27,020.00)
Other	(361,011.00)
Net cash provided by operating activities	<u>\$ 1,056,474.00</u>