AUDIT REPORT

Tennessee Board of Regents
Tennessee State University

For the Year Ended
June 30, 2009

STATE OF TENNESSEE

COMPTROLLER OF THE TREASURY

Department of Audit

Division of State Audit

Tennessee Comptroller of the Treasury

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Audit Manager

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In-Charge Auditors

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Gail K. Moses
Tiffany Tanner, CFE
Staff Auditors

Gerry Boaz, CPA
Technical Manager

Amy Brack
Editor

Comptroller of the Treasury, Division of State Audit
1500 James K. Polk Building, Nashville, TN 37243-1402
(615) 401-7897

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STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT
SUITE 1500
JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE (615) 401-7897
FAX (615) 532-2765

March 11, 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. Melvin N. Johnson, President
Tennessee State University
3500 John A. Merritt Boulevard
Nashville, Tennessee 37209

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Tennessee Board of Regents, Tennessee State University, for the year ended June 30, 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 certain deficiencies, which are detailed in the Results of the Audit section of this report. The university's administration has responded to the audit finding; the responses are 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/fd
09/081

State of Tennessee

Audit Highlights

Comptroller of the Treasury   Division of State Audit

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

As Noted in the Prior Audit, Neither the Associate Vice President for Business and Finance nor the Fiscal Accounts Manager for the Foundation Ensured That Amounts Were Properly Reported in the Financial Statements and Accompanying Notes to the Financial Statements*
Our audit of the financial statements of Tennessee State University—including its foundation, which is a discretely presented component unit of the university—discovered numerous reporting errors (page 8).

This finding was considered a material weakness. 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.

*   This finding is repeated from the prior audit.

OPINIONS ON THE FINANCIAL STATEMENTS

The opinions on the financial statements are unqualified.

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

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

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

BACKGROUND

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

ORGANIZATION

The governance of Tennessee State University is vested in the Tennessee Board of Regents. The Governor, the Commissioner of Education, the Commissioner of Agriculture, and the 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. 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.

PRIOR AUDIT FINDING

Section 8-4-109, *Tennessee Code Annotated*, requires that each state department, agency, or institution report to the Comptroller of the Treasury the action taken to implement the recommendations in the prior audit report. The university filed its report with the Department of Audit on January 28, 2010. A follow-up of the prior audit finding was conducted as part of the current audit.

The prior audit report contained a finding concerning improper reporting of the financial statements and the accompanying notes to the financial statements. This finding has not been resolved and is repeated in this 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. A material weakness, along with the recommendation and management's response, is detailed in the Finding and Recommendation section of this report.

Compliance

The results of our tests disclosed no instances of noncompliance 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.

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT
SUITE 1500
JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE (615) 401-7897
FAX (615) 532-2765

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 27, 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. Melvin N. Johnson, President
Tennessee State University
3500 John A. Merritt Boulevard
Nashville, Tennessee 37209

Ladies and Gentlemen:

We have audited the financial statements of Tennessee State University, an institution of the Tennessee Board of Regents, which is a component unit of the State of Tennessee, and its discretely presented component unit as of and for the year ended June 30, 2009, and have issued our report thereon dated January 27, 2010. 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 certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

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.

The following significant deficiency was noted:

As noted in the prior audit, neither the Associate Vice President for Business and Finance nor the Fiscal Accounts Manager for the foundation ensured that amounts were properly reported in the financial statements and accompanying notes to the 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 consider the significant deficiency described above to be 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.

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,

Arthur A. Hayes, Jr., CPA
Director

AAH/fd

FINDING AND RECOMMENDATION

<u>As noted in the prior audit, neither the Associate Vice President of Business and Finance nor the Fiscal Accounts Manager for the foundation ensured that amounts were properly reported in the financial statements and accompanying notes to the financial statements</u>

Finding

Our audit of the financial statements of Tennessee State University—including its foundation, which is a discretely presented component unit of the university—discovered numerous reporting errors. Many of these errors in the financial statements and notes to the financial statements involved the foundation. The responsibility for financial reporting for the foundation is split between the Associate Vice President of Business and Finance and the Fiscal Accounts Manager for the foundation, who is an employee of the university's development office.

As stated in the prior audit report, neither the Associate Vice President of Business and Finance nor the Fiscal Accounts Manager ensured that the financial statements and the accompanying notes to the financial statements were free of material misstatement. Although management did address some of the issues from the prior audit report related to the university's expenses, the foundation's investment reconciliations, and the foundation's statement of cash flows, we still noted several financial reporting errors in the 2009 financial report.

FOUNDATION ACCOUNTING ERRORS

Inaccurate Journal Entries

One journal entry transferred $1,612,247.28 from investments to cash. While the investments portion had been appropriately reduced, cash was improperly affected as investment income should have been reduced rather than increasing cash. Another journal entry for $684,034.72 improperly reduced cash and net assets. These entries were made in an attempt to correct the balance at year-end; however, they were made hurriedly and incorrectly. Adjustments were made to the financial statements to correct these errors.

Errors in the Preparation of the Foundation's Financial Statements and Notes

During our audit, we found that net assets expendable for scholarships and fellowships were overstated by $936,644.73, net assets expendable for research were understated by $2,929.42, net assets expendable for instructional department uses were understated by $132,161.71, and net assets expendable for other purposes were understated by $801,553.60.

According to the Associate Vice President for Business and Finance, a report was run within the financial reporting system to close operating accounts at year-end. In the previous year, all fund balances were moved to unrestricted net assets within the system, and then he manually reclassified them to their appropriate categories. However, for the current year, the report reflected that some fund balances had already been moved to the correct net asset accounts, while others were again moved to unrestricted net assets. Although the Associate Vice

President for Business and Finance realized this had occurred, he only manually reclassified some of the funds appropriately. Adjustments were made to the Statement of Net Assets to correct these errors.

During our audit, we found that on the Statement of Cash Flows, sales and maturities of investments were overstated by $17,994,450.89 and purchases of investments were overstated by $17,056,545.30. Several factors contributed to these errors, including the Fiscal Accounts Manager incorrectly reporting the transfer of investments from a former broker to the current broker as sales and purchases and overlooking a portion of the sales and maturities of investments that occurred during the year. Adjustments were made to the Statement of Cash Flows to correct these errors.

Our audit also found incorrect disclosures in the notes to the financial statements. The Associate Vice President of Business and Finance prepared these notes based on information received from the Fiscal Accounts Manager. U.S. Treasury investments in the amount of $25,462.58 that were scheduled to mature in five to ten years and U.S. Treasury investments in the amount of $26,798.86 that were scheduled to mature in more than ten years were incorrectly reported as scheduled to mature in one to five years. Mortgage-backed securities in the amount of $334,329.52 that were scheduled to mature in more than ten years were incorrectly reported as scheduled to mature in six to ten years.

In the credit risk disclosures, $3,105,275.08 in real estate investment trusts was also inappropriately included in this note. As credit risk applies to debt securities, real estate investment trusts should not be included in this disclosure. The Notes to the Financial Statements were corrected.

ERRORS IN THE PREPARATION OF THE UNIVERSITY'S FINANCIAL STATEMENTS AND NOTES

In addition to the errors involving the foundation, we also noted several inaccuracies within the notes to the financial statements for the university itself. It appears that these errors occurred because the Associate Vice President for Business and Finance and his staff in some instances used inaccurate information to make calculations, and in other instances did not understand what information was or was not included in certain reports used to gather information to be disclosed. According to the Associate Vice President for Business and Finance, he, the Assistant Director of Finance and Accounting, and the Associate Director of Finance and Accounting prepare certain portions of the notes to the financial statements and ask each other to review their work. The errors noted are described below.

The receivables note overstated the Federal Perkins Loan receivables by $15,556,160.48. This amount included loans that had been repaid and loans that had been canceled by the federal government. Both the Perkins loans receivable and the allowance for doubtful accounts for Perkins loans were overstated. The note was corrected.

The additions to and deductions from compensated absences in the long-term liabilities note were reported as $128,441.64 and $174,126.17, respectively. These amounts should have been $2,049,834.28 for additions to compensated absences and $2,095,518.81 for deductions. The note was adjusted accordingly.

The university's contributions to defined contribution plans (which include TIAA-CREF, ING, and VALIC) were overstated by $767,554.87 in the Pension note. The note incorrectly included employee contributions to the 403(b) supplemental plans in the amount reported. The note was corrected.

The amount the university contributed toward the annual cost of other postemployment benefits (OPEB) was reported as $351,870.00 instead of the correct amount of $1,201,032.90. This error also affected the net OPEB obligation on the Statement of Net Assets; the benefits expense on the Statement of Revenues, Expenditures, and Changes in Net Assets; and information in the Expenses note. The affected statements and notes were adjusted.

CONCLUSION

Management has identified within the university's risk assessment the risk of inaccurate financial reporting and the risk that journal entries will not be recorded or classified in accordance with applicable accounting standards. For these items, management's intention is to monitor through supervisory controls, such as reconciliations and journal entry review; and through executional controls, such as journal entry preparation. However, the Associate Vice President of Business and Finance and his staff did not detect the reporting errors noted above during their review.

In summary, these reporting errors resulted in material misstatements on the foundation's Statement of Net Assets, the foundation's Statement of Cash Flows, and the university and foundation's note disclosures. Management relies on financial information as reported in the financial statements to make critical financial decisions. Management decisions based upon flawed financial reporting may result in negative consequences for the foundation and/or the university. Furthermore, when staff responsible for financial reporting do not properly use appropriate supporting documentation, there is an increased risk for reporting errors and possible mismanagement of funds.

Recommendation

The President, in conjunction with the Vice President of Business and Finance and the Vice President for Development, should consider whether it is feasible to move the accounting for the foundation to the accounting staff in the business office. Journal entries should be prepared with a proper amount of consideration and understanding as to the purpose and the validity of such entries. Each journal entry should be carefully and thoughtfully reviewed by a knowledgeable individual independent of the entry.

The President and Vice President of Business and Finance should ensure that all accounting staff seek technical advice when instructions or tasks are not understood. They should carefully and thoughtfully review the financial statements and related notes. The Vice

President of Business and Finance should ensure that the amounts reported in the financial ledgers are accurate, that all notes to the financial statements are accurate at year-end and in agreement with the respective amounts in the financial statements, and that all financial reporting is done in accordance with generally accepted accounting principles. The President and Vice President of Business and Finance should assign specific staff the responsibility of monitoring the processes for preparing year-end entries and, ultimately, the financial statements and related notes, to mitigate the risk of material misstatement in the financial statements.

The President and Vice President of Business and Finance should ensure that steps are taken to improve coordination among all staff and management involved in requesting, approving, executing, and reviewing accounting entries and transactions. Management should continue to evaluate risks and include them in documented risk assessment activities. Management should ensure that staff who are responsible for the design and implementation of internal controls to adequately mitigate those risks and to prevent and detect exceptions in a timely manner are continually evaluating those controls. Management should ensure that staff who are responsible for ongoing monitoring for compliance with all requirements are indeed monitoring and taking prompt action when exceptions occur. All controls and control activities, including monitoring, should be adequately documented.

Management's Comment

Management concurs with the finding and recommendation.

The fiscal year 2009 year-end closing was unique, in that the fiscal year 2008 audit was still in process during the preparation of the fiscal year 2009 statements. The fiscal year 2008 audit report was released on August 25, 2009, and the fiscal year 2009 financial statements were initially transmitted to the Tennessee Board of Regents on August 28, 2009. The university immediately implemented corrective actions in response to the 2008 audit report.

As noted in the Management's Comment section of fiscal year 2008 audit:

> The President, in conjunction with the Vice President for Business and Finance and the Vice President for Development will ensure that transactions related to the investment assets managed by the TSU Foundation are analyzed and recorded in Banner on a monthly basis. The Fiscal Accounts Manager for the foundation will prepare a monthly reconciliation of the various brokerage statements that will be reviewed and approved by the Executive Director of the foundation. The monthly transactions, supported by the reconciliation, will be initiated by the Fiscal Accounts Manager and approved by the Executive Director of the foundation and the Associate Vice President for Business and Finance. The Fiscal Accounts Manager will ensure Banner reconciles to the brokerage statements monthly.

The above process was implemented for the fiscal year 2010 immediately upon receipt of the prior-year finding. This process will result in a more efficient year-end closing process and reduce the risk of incorrect journal entries. This will also allow for additional time to ensure "sales and maturities" and "purchases of investments" are properly presented on the Statement of Cash Flows and ensure proper note disclosure for the Component Unit. The Associate Vice President for Business and Finance will no longer initiate journal entries, which will allow for an independent review by the Associate Vice President.

The President, Vice President for Business and Finance, and Vice President for University Relations and Development will also consider whether it is feasible to move the accounting function for the foundation under the direct supervision of the Associate Vice President for Business and Finance. An additional position would be required, as the current Fiscal Accounts Manager has other foundation responsibilities. Due to budget reductions, the University has eliminated 137 positions since the beginning of last fiscal year. Title III and other alternative funding sources will be investigated.

The Fiscal Accounts Manager has reviewed the Net Asset classifications for funds currently in the foundation for accuracy. As new funds are requested, the Fiscal Accounts Manager will notify the Associate Vice President for Business and Finance of the proper Net Asset classification.

For fiscal year 2010, the preliminary year-end closing will be conducted by the Finance and Accounting staff to identify potential classification errors. The President and the Vice President for Business and Finance have assigned specific staff with the responsibility of monitoring the year-end process, including preparing the financial statements and related notes. In addition, staff assignments for the year-end closing process will be reviewed for efficiency and effectiveness, and necessary changes to the process will be communicated to the staff.

The Federal Perkins Loan receivables note disclosure has been consistently presented in the university's Unaudited Financial Statements and in the audited financial statements since the 2002 fiscal year. We will report them in the future as recommended by the audit staff.

We recognize that errors may occur during year-end closing and reporting for future periods. Given the limited time available to close the fiscal year and complete the unaudited statements, the possibility of undetected errors and mistakes cannot be completely eliminated. However, everything practicable will be done to ensure that items are displayed properly in the unaudited financial statements.

Management will continue to evaluate risks and include them in documented risk assessment activities. The President, the Vice President for Business and Finance, and the Vice President for University Relations and Development and their staffs are cognizant of the risks involved with financial reporting and remain committed to the establishment of internal controls necessary to minimize any risk.

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT
SUITE 1500
JAMES K. POLK STATE OFFICE BUILDING
NASHVILLE, TENNESSEE 37243-1402
PHONE (615) 401-7897
FAX (615) 532-2765

Independent Auditor's Report

January 27, 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. Melvin N. Johnson, President
Tennessee State University
3500 John A. Merritt Boulevard
Nashville, Tennessee 37209

Ladies and Gentlemen:

We have audited the accompanying basic financial statements of 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 unit 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 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 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 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, the financial statements referred to above present fairly, in all material respects, the respective financial position of Tennessee State University, and its discretely presented component unit as of June 30, 2009, and the respective changes in financial position and cash flows thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 16 through 28 and the schedule of funding progress on page 59 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 page 60 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 27, 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 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,

Arthur A. Hayes, Jr., CPA
Director

AAH/fd

This section of Tennessee State University's 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, the audited financial statements, and the accompanying notes. The financial statements, notes, and this discussion are the responsibility of management.

Using This Annual Report

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

The Statement of Net Assets

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

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

Net Assets (in thousands of dollars)

	INSTITUTION		COMPONENT UNIT	
	2009	2008	2009	2008
Assets:				
Current assets	$ 27,953	$ 25,018	$ 5,307	$ 3,072
Capital assets, net	172,466	176,900	-	-
Other assets	42,806	42,553	27,796	31,275
Total Assets	**243,225**	**244,471**	**33,103**	**34,347**
Liabilities:				
Current liabilities	21,804	17,256	16	20
Noncurrent liabilities	50,130	48,900	-	-
Total Liabilities	**71,934**	**66,156**	**16**	**20**
Net Assets:				
Invested in capital assets, net of related debt	132,527	136,142	-	-
Restricted - Nonexpendable	74	75	28,926	31,254
Restricted - Expendable	7,514	7,350	3,985	2,928
Unrestricted	31,176	34,748	176	145
Total Net Assets	**$ 171,291**	**$ 178,315**	**$ 33,087**	**$ 34,327**

Comparison of FY 2009 to FY 2008 – University

- Current assets increased as a result of budget restrictions.

- The increase in current liabilities is the result of a $4 million liability due to the State of Tennessee. Based upon guidance provided by the Tennessee Recovery Act Management Office, the total allotment of FY 2008-2009 State Fiscal Stabilization Funds (SFSF) was drawn down and receipted as of June 30, 2009, and the entire allotment was returned on July 21, 2009, and is included on the Statement of Net Assets as Due to Primary Government.

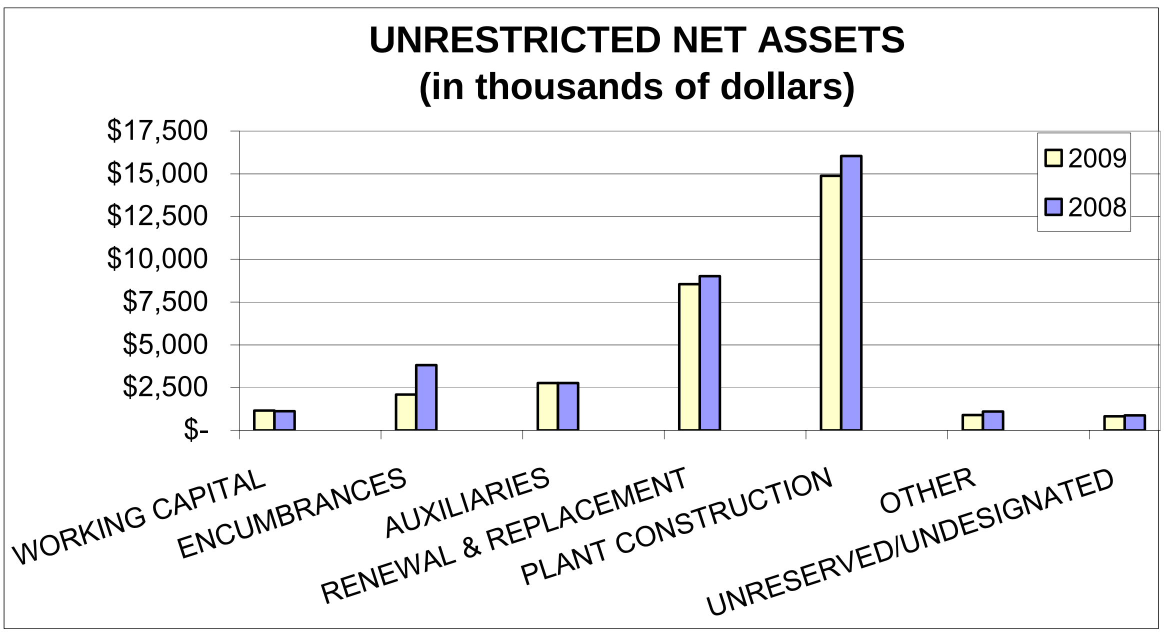
- Noncurrent Liabilities increased over $1.2 million due to the recording of an accrued liability for Postemployment health care.

- Invested in capital assets, net of related debt decreased due to routine depreciation expense (see Note 5).

Comparison of FY 2009 to FY 2008 – TSU Foundation

- Current assets increased due to the receipt of over $2 million from Title III related to the Consent Decree settlement.

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, capital projects, and student loans. The following graph shows the allocations:



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

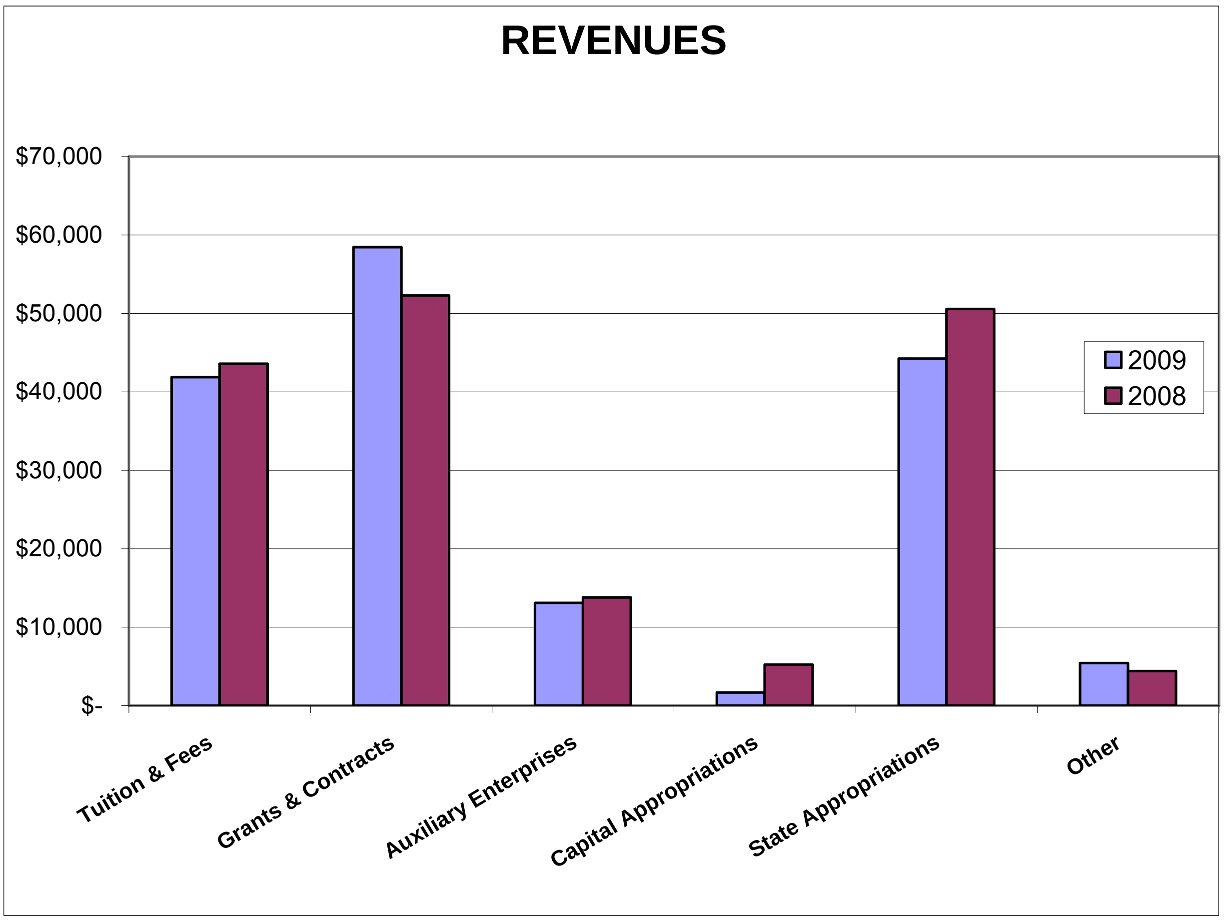
The Statement of Revenues, Expenses, and Changes in Net Assets presents the operating results of the university, as well as the nonoperating revenues and expenses. Annual state appropriations, while budgeted for operations, are considered non-operating revenues according to accounting principles generally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

Changes in Net Assets (in thousands of dollars)

	INSTITUTION		COMPONENT UNIT	
	2009	2008	2009	2008
Operating revenues:				
Net tuition and fees	$ 41,875	$ 43,596	$ -	$ -
Grants and contracts	39,062	31,713	-	-
Auxiliary	13,115	13,808	-	-
Other	3,959	4,397	1,646	1,369
Total operating revenue	98,011	93,514	1,646	1,369
Operating expenses	168,852	167,979	1,409	1,146
Operating loss	(70,841)	(74,465)	237	223
Nonoperating revenues and expenses:				
State appropriations	44,259	50,552	-	-
Gifts	32	85	-	-
Grants and Contracts	18,735	19,341	2,026	-
Investment income	1,419	2,642	(3,579)	172
Other revenues and expenses	(2,522)	(2,001)	-	-
Total nonoperating revenues and expenses	61,923	70,619	(1,553)	172
Income (loss) before other revenues expenses, gains, or losses	(8,918)	(3,846)	(1,316)	395
Other revenues, expenses, gains, or losses				
Capital appropriations	1,692	5,225	-	-
Capital grants and gifts	665	1,216	-	-
Additions to permanent endowments	-	-	76	264
Other	-	(42)	-	-
Total other revenues, expenses, gains, or losses	2,357	6,399	76	264
Increase (decrease) in net assets	(6,561)	2,553	(1,240)	659
Net assets at beginning of period	178,315	175,762	34,327	33,668
Prior Period Adjustment	(463)	-	-	-
Net assets at end of year	$ 171,291	$ 178,315	$ 33,087	$ 34,327

Revenues

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



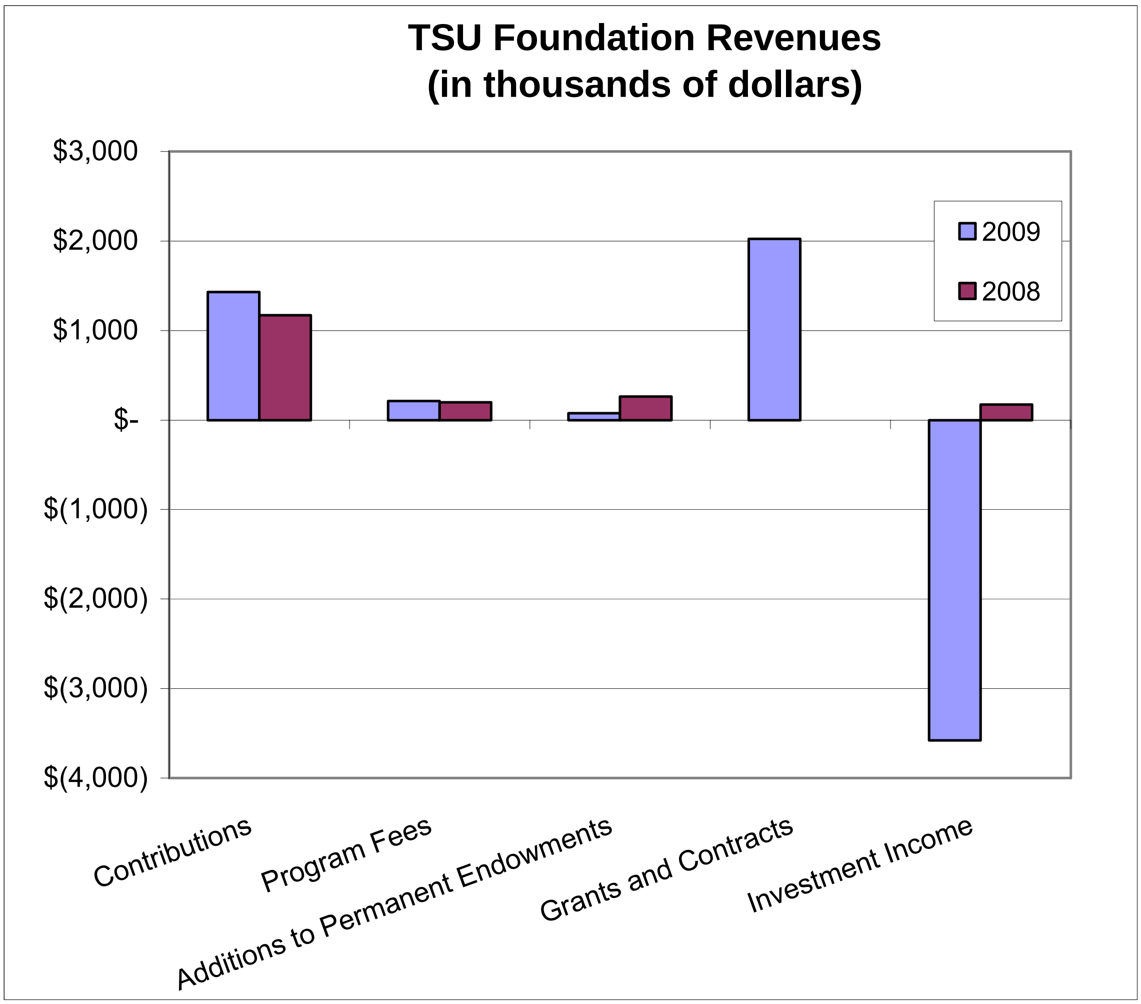
Comparison of FY 2009 to FY 2008 – University

- Net tuition and fees and operating expenses decreased due to a correction in the allocation of the Scholarship Allowance due to an error in the prior year.

- Grants and Contracts for the University increased due to over $3.2 million in Title III funds for the match of the funds related to the Consent Decree settlement and the receipt of $2 million for Tennessee Early Childhood Training Alliance (TECTA) funding.

- State appropriations decreased due to the decline in the revenue collections for the state.

- Capital appropriations decreased 66% with a $2 million decline in expenses in FY09 for the Avon Williams Campus renovation and $1 million decline in the Windows Replacement project.



Comparison of FY 2009 to FY 2008 – TSU Foundation

- Grants and contracts for the foundation increased due to over $2 million in Title III funds related to the Consent Decree settlement.

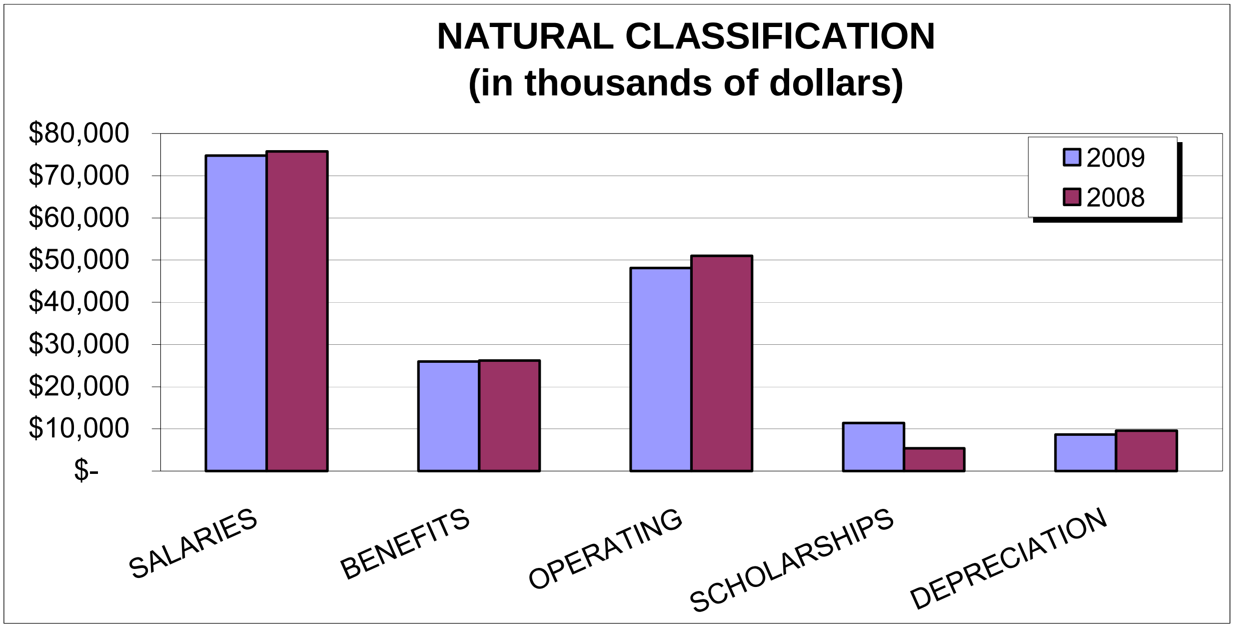
- Investment income decreased due to a $4.7 million unrealized loss for the year caused by a decline in the market and the reallocation of many funds to cash.

Expenses

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

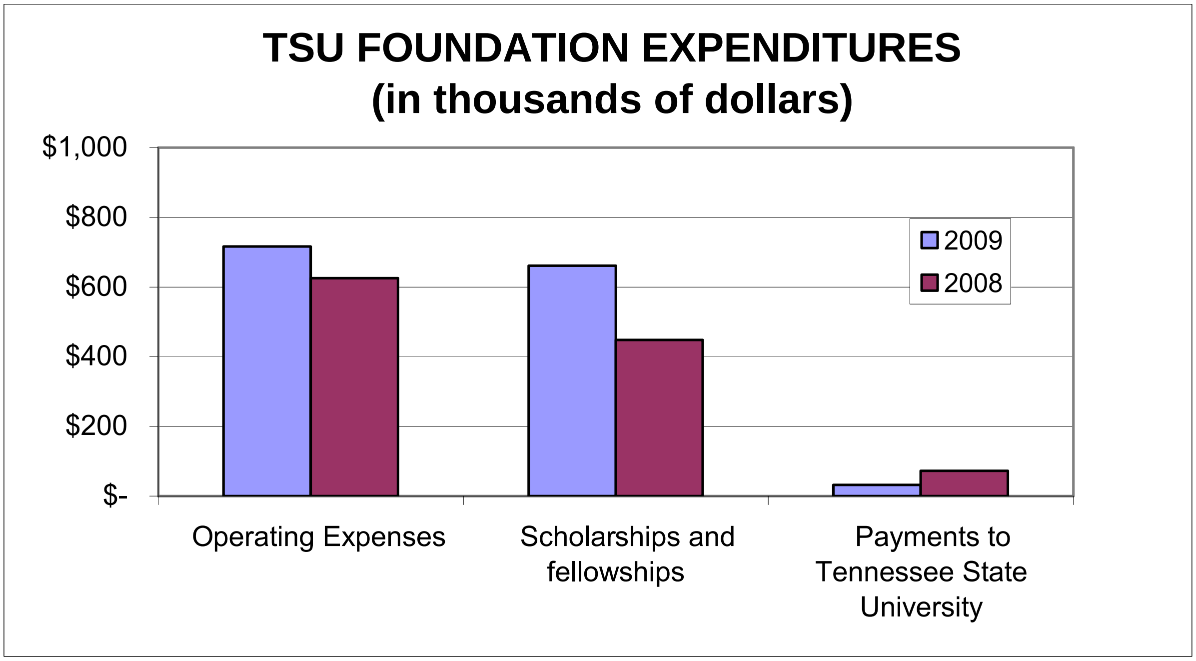
NATURAL CLASSIFICATION
(in thousands of dollars)

	UNIVERSITY		**COMPONENT UNIT**	
	2009	**2008**	**2009**	**2008**
SALARIES	$ 74,731	$ 75,773	$ -	$ -
BENEFITS	25,964	26,214	-	-
OPERATING	48,152	51,000	716	625
SCHOLARSHIPS	11,371	5,406	661	448
PAYMENTS TO TSU	-	-	32	73
DEPRECIATION	8,634	9,586	-	-
TOTAL	**$ 168,852**	**$ 167,979**	**$ 1,409**	**$ 1,146**



Comparison of FY 2009 to FY 2008 – University

- Scholarships increased as a result of a reporting change regarding federal and state financial aid previously included with operating in previous years.



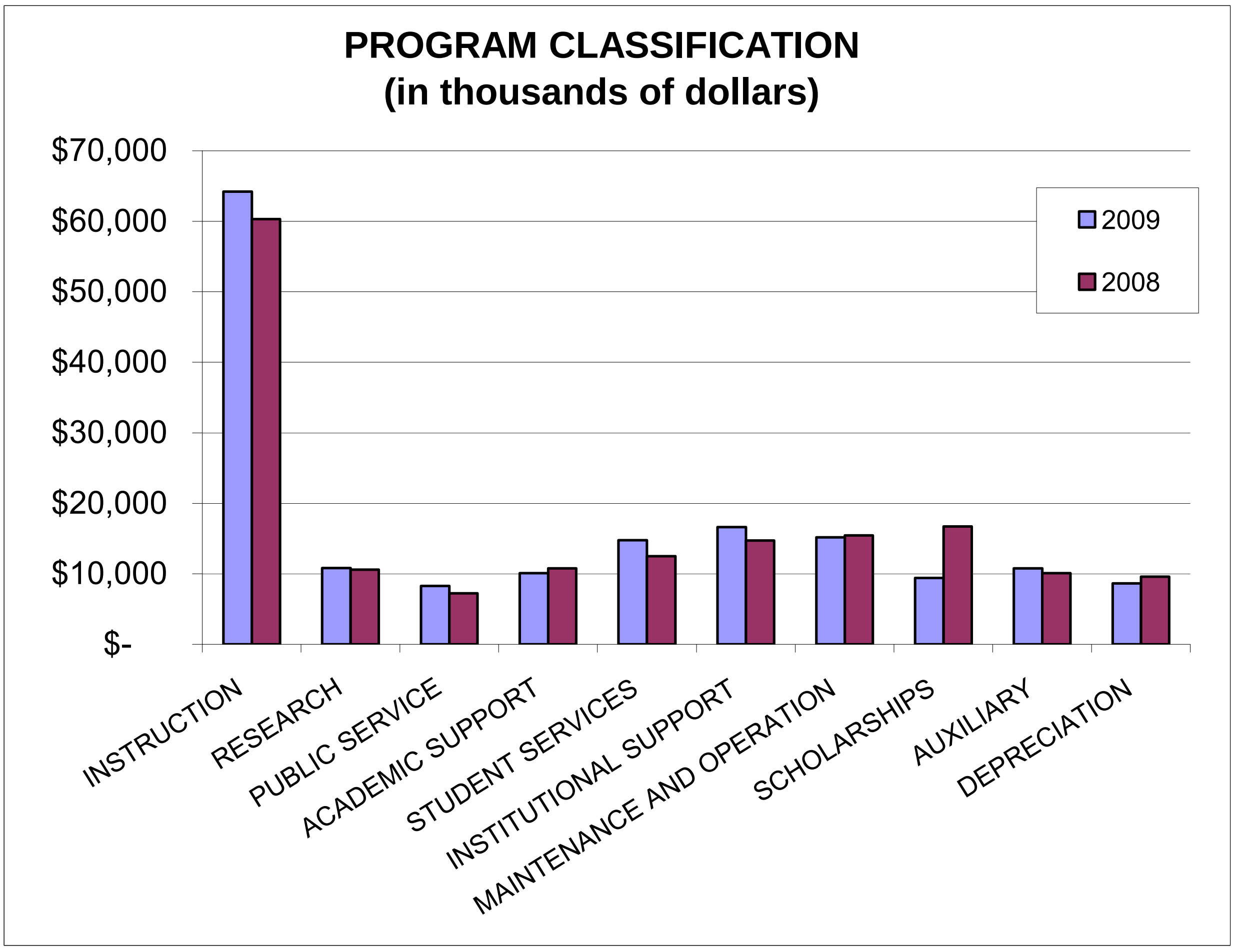
Comparison of FY 2009 to FY 2008 – TSU Foundation

- Scholarship expenditures increased with the continued funding of scholarships following the removal of the hold of issuing new scholarships by the foundation board membership and the additional award of new scholarships.

PROGRAM CLASSIFICATION
(in thousands of dollars)

	UNIVERSITY	
	2009	**2008**
INSTRUCTION	$ 64,219	$ 60,284
RESEARCH	10,811	10,600
PUBLIC SERVICE	8,286	7,236
ACADEMIC SUPPORT	10,109	10,799
STUDENT SERVICES	14,785	12,522
INSTITUTIONAL SUPPORT	16,614	14,711
MAINTENANCE AND OPERATION	15,170	15,429
SCHOLARSHIPS AND FELLOWSHIPS	9,421	16,706

AUXILIARY	10,803	10,107
DEPRECIATION	8,634	9,585
TOTAL	**$ 168,852**	**$ 167,979**



Comparison of FY 2009 to FY 2008 – University

- Public service increased with an additional state appropriation designated for the Cooperative Extension Program.
- Scholarships decreased and instruction increased due to a change to the scholarship allowance allocation in fiscal year 2009.

Capital Assets and Debt Administration

Capital Assets

The university had $172,466,111.56 invested in capital assets, net of accumulated depreciation of $140,136,941.18 at June 30, 2009; and $176,900,454.78 invested in capital assets, net of accumulated depreciation of $132,275,353.17 at June 30, 2008. Depreciation charges totaled $8,633,862.43 and $9,585,634.75 for the years ended June 30, 2009, and June 30, 2008, respectively. Details of these assets are shown below.

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

	2009	2008
Land	$ 9,525	$ 9,525
Land Improvements	9,509	10,731
Buildings	127,398	132,333
Equipment	4,947	5,343
Library Holdings	7,897	7,809
Software	1,907	2,179
Projects In Progress	11,283	8,980
Net Capital Assets	**$ 172,466**	**$ 176,900**

Projects in progress during the fiscal year 2009 included the renovation of the Avon Williams campus, installation of fire sprinkler systems in student housing, energy savings and performance contracting, and window replacements. Work will continue on the fire sprinkler systems and energy savings and performance contracting during fiscal year 2010. These projects are funded by TSSBA. More detailed information about the university's capital assets is presented in Note 5 to the financial statements.

Debt

The university had $39,939,356.68 and $40,758,052.65 in debt outstanding at June 30, 2009, and June 30, 2008, respectively. The table below summarizes these amounts by type of debt instrument.

Schedule of Debt (in thousands of dollars)

	2009	**2008**
TSSBA Bonds	$ 39,890	$ 36,661
TSSBA Commercial Paper	49	4,097
Total	**$ 39,939**	**$ 40,758**

During fiscal year 2008, an additional amount of over $3.94 million was issued in commercial paper for the Research and Sponsored Projects building, the Student Housing Fire Safety upgrade, and the Energy Savings Performance Contract. In 2009, bonds were issued to redeem the commercial paper. More detailed information about the university's long-term liabilities is presented in Note 7 to the financial statements.

The ratings on debt issued by the Tennessee State School Bond Authority at June 30, 2009, were as follows:

Fitch	AA
Moody's Investor Service	Aa2
Standard & Poor's	AA

Economic Factors That Will Affect the Future

The Tennessee Board of Regents approved a 6.0% increase in maintenance and tuition fees for the 2009-10 academic year. The cost for students to attend the university exceeds the amount of financial aid available per student. This requires students to resort to alternative means of financing the cost of attending the university. The enrollment for the Fall 2010 semester is expected to be stable; however, the exact impact is unknown. The impact the economy will have on the level of state support the university will receive is also unknown. The university is not aware of any other factors that will have a significant effect on the financial position or results of operations.

Requests for Information

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

Ms. Cynthia B. Brooks
Vice President for Business and Finance
3500 John A. Merritt Boulevard
Nashville, TN 37209

Exhibit A

TENNESSEE BOARD OF REGENTS
TENNESSEE STATE UNIVERSITY
STATEMENTS OF NET ASSETS
JUNE 30, 2009

	Tennessee State University	Component Unit Tennessee State University Foundation
	June 30, 2009	June 30, 2009
ASSETS		
Current assets:		
Cash and cash equivalents (Notes 2 and 19)	$ 17,026,739.94	$ 5,104,925.88
Short-term investments (Notes 3 and 19)	1,452,866.90	202,143.02
Accounts, notes, and grants receivable (net) (Note 4)	7,673,193.16	-
Inventories	36,011.67	-
Accrued interest receivable	1,764,143.22	-
Total current assets	27,952,954.89	5,307,068.90
Noncurrent assets:		
Cash and cash equivalents (Notes 2 and 19)	27,326,035.44	2,777,487.19
Investments (Notes 3 and 19)	13,305,268.33	25,018,290.86
Accounts, notes, and grants receivable (net) (Note 4)	2,174,793.17	-
Capital assets (net) (Note 5)	172,466,111.56	-
Total noncurrent assets	215,272,208.50	27,795,778.05
Total assets	243,225,163.39	33,102,846.95
LIABILITIES		
Current liabilities:		
Accounts payable (Note 6)	2,150,969.86	16,296.25
Accrued liabilities	6,031,214.29	-
Due to primary government	3,793,100.00	-
Student deposits	1,235,730.21	-
Deferred revenue	5,622,351.73	-
Compensated absences (Note 7)	683,194.15	-
Accrued interest payable	332,310.97	-
Long-term liabilities, current portion (Note 7)	1,756,569.37	-
Deposits held in custody for others	155,390.74	-
Other liabilities	43,556.38	-
Total current liabilities	21,804,387.70	16,296.25
Noncurrent liabilities:		
Net OPEB Obligation (Notes 7 and 12)	3,930,462.13	-
Compensated absences (Note 7)	4,466,818.50	-
Long-term liabilities (Note 7)	38,182,787.31	-
Due to grantors (Note 7)	3,549,346.55	-
Total noncurrent liabilities	50,129,414.49	-
Total liabilities	71,933,802.19	16,296.25
NET ASSETS		
Invested in capital assets, net of related debt	132,526,754.88	-
Restricted for:		
Nonexpendable:		
Scholarships and fellowships	74,022.65	28,926,133.63
Expendable:		
Scholarships and fellowships (Notes 8 and 19)	1,132,272.58	2,815,804.54
Research	1,124,264.53	16,055.72
Instructional department uses (Notes 8 and 19)	3,022,488.62	172,365.15
Loans	924,019.90	-
Other (Note 19)	1,310,931.61	980,939.36
Unrestricted (Note 9)	31,176,606.43	175,252.30
Total net assets	$ 171,291,361.20	$ 33,086,550.70

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

Exhibit B

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

	Tennessee State University	Component Unit Tennessee State University Foundation
	Year Ended June 30, 2009	Year Ended June 30, 2009
REVENUES		
Operating revenues:		
Student tuition and fees (net of scholarship allowances of $16,306,145.30)	$ 41,875,196.87	$ -
Gifts and contributions	-	1,432,373.10
Governmental grants and contracts	38,207,151.05	-
Nongovernmental grants and contracts	854,873.69	-
Sales and services of educational departments	3,702,096.05	-
Auxiliary enterprises:		
Residential life (net of scholarship allowances of $1,001,606.03; all residential life revenues are used as security for revenue bonds; see Note 7)	7,383,812.68	-
Bookstore	350,770.92	-
Food service	4,612,131.46	-
Other auxiliaries	768,490.54	-
Other operating revenues	256,448.23	213,210.90
Total operating revenues	98,010,971.49	1,645,584.00
EXPENSES		
Operating expenses (Note 16):		
Salaries and wages	74,730,730.22	-
Benefits	25,963,944.13	-
Utilities, supplies, and other services	48,151,973.17	715,890.08
Scholarships and fellowships	11,370,975.20	661,600.45
Depreciation expense	8,633,862.43	-
Payments to or on behalf of Tennessee State University	-	31,886.59
Total operating expenses	168,851,485.15	1,409,377.12
Operating income (loss)	(70,840,513.66)	236,206.88

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

	Tennessee State University	Component Unit Tennessee State University Foundation
	Year Ended June 30, 2009	Year Ended June 30, 2009
NONOPERATING REVENUES (EXPENSES)		
State appropriations	44,259,635.00	-
Gifts from component unit	31,886.59	-
Grants and contracts	18,734,772.90	2,026,136.00
Investment income	1,418,891.97	(3,578,736.25)
Interest on capital asset-related debt	(1,926,154.05)	-
Bond issuance costs	(348,056.02)	-
Other nonoperating revenues (expenses)	(248,017.15)	-
Net nonoperating revenues (expenses)	61,922,959.24	(1,552,600.25)
Loss before other revenues, expenses, gains, or losses	(8,917,554.42)	(1,316,393.37)
Capital appropriations	1,691,569.46	-
Capital grants and gifts	664,863.03	-
Additions to permanent endowments	-	76,157.70
Total other revenues	2,356,432.49	76,157.70
Decrease in net assets	(6,561,121.93)	(1,240,235.67)
NET ASSETS		
Net assets - beginning of year	178,315,170.93	34,326,786.37
Prior period adjustment (Note 17)	(462,687.80)	-
Net assets - beginning of year, restated	177,852,483.13	34,326,786.37
Net assets - end of year	$ 171,291,361.20	$ 33,086,550.70

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

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

	Year Ended June 30, 2009
CASH FLOWS FROM OPERATING ACTIVITIES	
Tuition and fees	$ 41,383,323.69
Grants and contracts	44,023,182.41
Sales and services of educational activities	3,701,540.82
Payments to suppliers and vendors	(48,172,680.43)
Payments to employees	(75,155,018.39)
Payments for benefits	(24,072,573.51)
Payments for scholarships and fellowships	(11,370,975.20)
Loans issued to students	(139,301.19)
Collection of loans from students	550,089.28
Interest earned on loans to students	75,740.09
Auxiliary enterprise charges:	
Residence halls	7,447,647.84
Bookstore	350,770.92
Food services	4,612,131.46
Other auxiliaries	867,891.62
Other receipts (payments)	256,448.23
Net cash used by operating activities	(55,641,782.36)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
State appropriations	44,231,700.00
Gifts and grants received for other than capital or endowment purposes, including $31,886.59 from Tennessee State University Foundation for the year ended June 30, 2009	18,766,659.49
Changes in deposits held for others	7,817.29
Net cash provided by noncapital financing activities	63,006,176.78
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Proceeds from capital debt	6,170,005.78
Capital appropriations	1,725,413.01
Capital grants and gifts received	1,497,958.51
Purchase of capital assets and construction	(4,199,979.21)
Principal paid on capital debt and lease	(6,950,115.87)
Interest paid on capital debt and lease	(1,899,646.76)
Bond issue costs paid on new debt issue	(466,778.14)
Net cash used by capital and related financing activities	(4,123,142.68)
CASH FLOWS FROM INVESTING ACTIVITIES	
Proceeds from sales and maturities of investments	9,848,989.36
Income on investments	1,271,128.77
Purchase of investments	(11,855,588.37)
Net cash used by investing activities	(735,470.24)
Net increase in cash and cash equivalents	2,505,781.50
Cash and cash equivalents - beginning of year	41,846,993.88
Cash and cash equivalents - end of year	$ 44,352,775.38

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

		Year Ended June 30, 2009
Reconciliation of operating loss to net cash used by operating activities:		
Operating loss	$	(70,840,513.66)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation expense		8,633,862.43
Other adjustments		55,135.00
Change in assets and liabilities:		
Receivables, net		(50,730.48)
Prepaid/deferred items		150.00
Accounts payable		27,011.06
Accrued liabilities		1,471,838.44
Deferred revenue		1,188,018.55
Deposits		(3,264.20)
Compensated absences		(45,684.53)
Due to grantors		3,922,395.03
Net cash used by operating activities	$	(55,641,782.36)
Noncash transactions		
Unrealized gains/losses on investments	$	61,760.92
Loss on disposal of capital assets		(787,526.54)
Bad debt expense		(84,343.90)

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

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 significant 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 Tennessee State University.

The Tennessee State University Foundation is considered a component unit 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. See Note 19 for more detailed information about the component unit and how to obtain the report.

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.

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.

Cash Equivalents

This classification includes instruments that are readily convertible to known amounts of cash and have original maturities of three months or less.

Inventories

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

Compensated Absences

The 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.

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/amortized 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.

Scholarship Discounts and Allowances

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

NOTE 2. CASH

At June 30, 2009, cash consisted of $3,129,556.65 in bank accounts, $4,850.00 of petty cash on hand, $39,793,391.32 in the State of Tennessee Local Government Investment Pool (LGIP) administered by the State Treasurer, and $1,424,977.41 in LGIP deposits for capital projects.

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 account. As expenses are incurred, funds are withdrawn from the LGIP account by the Tennessee Board of Regents and transferred to the Department of Finance and Administration. The funds in the account are not available to the university for any other purpose until the project is completed and the Tennessee Board of Regents releases any remaining funds.

NOTE 3. INVESTMENTS

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

Pools, 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 university had the following investments and maturities.

		Investment Maturities (in Years)			
Investment Type	Fair Value	Less than 1	1 to 5	6 to 10	More than 10
U. S. agencies	$ 14,371,142.44	$ 1,065,874.11	$ 9,957,098.98	$ 2,064,155.64	$ 1,284,013.71
Certificates of deposit	386,992.79	386,992.79	-	-	-
Total	$ 14,758,135.23	$ 1,452,866.90	$ 9,957,098.98	$ 2,064,155.64	$ 1,284,013.71

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 ratings 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 a 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.

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

		Credit Quality Rating	
Investment Type	Fair Value	AAA	Unrated
LGIP	$ 41,218,368.73	$ -	$ 41,218,368.73
US Agencies	14,371,142.44	14,371,142.44	-
Total	$ 55,589,511.17	$ 14,371,142.44	$ 41,218,368.73

Concentration of Credit Risk

Tennessee Board of Regents 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 the total investments on the date of acquisition and limits the combined amount of banker's acceptances and commercial paper to not exceed 35% of the 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:

Issuer	Percentage of Total Investments
Federal National Mortgage Assn.	28%
Federal Home Loan Mortgage Co.	23%
Federal Home Loan Mortgage Assn.	10%
Federal Home Loan Bank	22%
Federal Farm Credit Banks	14%

NOTE 4. RECEIVABLES

Receivables included the following:

	June 30, 2009
Student accounts receivable	$ 3,533,901.43
Grants receivable	5,422,457.27
Notes receivable	23,927.97
State appropriation receivable	221,554.58
Other receivables	451,023.11
Subtotal	9,652,864.36
Less allowance for doubtful accounts	(1,965,173.86)
Total receivables	$ 7,687,690.50

Federal Perkins Loan Program funds included the following:

	June 30, 2009
Perkins loans receivable	$ 2,832,672.25
Less allowance for doubtful accounts	(672,376.42)
Total	$ 2,160,295.83

NOTE 5. CAPITAL ASSETS

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

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$ 9,525,009.24	$ -	$ -	$ -	$ 9,525,009.24
Land improvements and infrastructure	39,043,809.26	-	-	-	39,043,809.26
Buildings	209,416,195.86	-	-	-	209,416,195.86
Equipment	25,406,037.02	1,017,307.47	-	934,618.42	25,488,726.07
Library holdings	14,124,906.31	1,667,289.71	-	625,182.64	15,167,013.38

Software	2,679,599.36	-	-	-	2,679,599.36
Projects in progress	8,980,250.90	2,302,448.67	-	-	11,282,699.57
Total	309,175,807.95	4,987,045.85	-	1,559,801.06	312,603,052.74
Less accumulated depreciation:					
Land improvements and infrastructure	28,312,709.88	1,221,758.22	-	-	29,534,468.10
Buildings	77,083,556.67	4,934,216.82	-	-	82,017,773.49
Equipment	20,062,998.58	1,352,481.76	-	873,353.03	20,542,127.31
Library holdings	6,316,066.61	1,579,219.64	-	625,182.64	7,270,103.61
Software	500,021.43	272,447.24	-	-	772,468.67
Total accumulated depreciation	132,275,353.17	9,360,123.68	-	1,498,535.67	140,136,941.18
Capital assets, net	$176,900,454.78	$ (4,373,077.83)	$ -	$ 61,265.39	$172,466,111.56

NOTE 6. ACCOUNTS PAYABLE

Accounts payable included the following:

	June 30, 2009
Vendors payable	$1,760,982.41
Other payables	389,987.45
Total accounts payable	$2,150,969.86

NOTE 7. LONG-TERM LIABILITIES

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

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Payables:					
TSSBA debt:					
Bonds	$ 36,660,849.96	$ 5,046,255.58	$ 1,817,073.86	$ 39,890,031.68	$ 1,756,569.37
Commercial paper	4,097,202.69	1,148,590.17	5,196,467.86	49,325.00	-
Subtotal	40,758,052.65	6,194,845.75	7,013,541.72	39,939,356.68	1,756,569.37
Other liabilities:					
Compensated absences	5,195,697.18	2,049,834.28	2,095,518.81	5,150,012.65	683,194.15
Due to grantors	3,420,051.52	137,622.29	8,327.26	3,549,346.55	-
Net OPEB obligation	2,001,090.08	1,929,372.05	-	3,930,462.13	-
Subtotal	10,616,838.78	4,116,828.62	2,103,846.07	12,629,821.33	638,194.15
Total long-term liabilities	$ 51,374,891.43	$ 10,311,674.37	$ 9,117,387.79	$ 52,569,178.01	$ 2,439,763.52

TSSBA Debt - Bonds

Bonds, with interest rates ranging from 3.25% to 5.13%, were issued by the Tennessee State School Bond Authority (TSSBA). The bonds are due serially to 2032 and are secured by pledges of the facilities' revenues to which they relate and certain other revenues and fees of the university, including state appropriations, see Note 10 for further details. 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 $805,473.56 at June 30, 2009. Unexpended debt proceeds were $44,262.21 at June 30, 2009.

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

Year Ending June 30	Principal	Interest	Total
2010	$ 1,756,569.37	$ 1,965,358.65	$ 3,721,928.02
2011	2,191,104.09	1,869,448.74	4,060,552.83
2012	2,296,833.44	1,774,019.77	4,070,853.21
2013	2,378,345.14	1,678,048.66	4,056,393.80

2014	2,484,823.22	1,565,070.01	4,049,893.23
2015 – 2019	11,891,348.04	6,136,813.17	18,028,161.21
2020 – 2024	9,474,635.88	3,347,916.73	12,822,552.61
2025 – 2029	6,003,477.00	1,117,340.36	7,120,817.36
2030 - 2032	1,412,895.50	143,675.48	1,556,570.98
Total	$ 39,890,031.68	$ 19,597,691.57	$ 59,487,723.25

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 $49,325.00 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://tn.gov/comptroller/bf/tssbacafr.htm.

NOTE 8. ENDOWMENTS

If a donor has not provided specific instructions to the university, state law permits the university to authorize for expenditure the net appreciation (realized and unrealized) of the investments of endowment funds. When administering its power to spend net appreciation, 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 net appreciation spent is required to be spent for the purposes for which the endowment was established.

The university chooses to spend only a portion of the investment income (including changes in the value of investments) each year. At June 30, 2009, net appreciation of $41,821.81 is available to be spent, of which $1,596.70 is included in restricted net assets expendable for scholarships and fellowships, and $40,225.11 is included in restricted net assets expendable for instructional department uses.

NOTE 9. UNRESTRICTED NET ASSETS

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

	June 30, 2009
Working capital	$ 1,153,647.92
Encumbrances	2,091,228.25
Designated fees	902,067.79
Auxiliaries	2,772,956.73
Plant construction	14,880,018.74
Renewal and replacement of equipment	8,551,881.45
Undesignated	824,805.55
Total	$31,176,606.43

NOTE 10. PLEDGED REVENUES

The university has pledged certain revenues and fees, including state appropriations, to repay $39,890,031.68 in revenue bonds issued from December 1989 to November 2008. Proceeds from the bonds provided financing for dormitory renovations, student housing and apartments, North Campus improvements, chiller replacement, research and sponsored programs building, student housing fire suppression, energy savings performance contracting, and Avon Williams Campus. The bonds are payable through 2032. Annual principal and interest payments on the bonds are expected to require 3% of available revenues. The total principal and interest remaining to be paid on the bonds is $59,487,723.25. Principal and interest paid for the current year and total available revenues were $3,671,714.08 and $118,100,724.23, respectively.

NOTE 11. PENSION PLANS

A. Defined Benefit Plans

1. Tennessee Consolidated Retirement System

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

The TCRS issues a publicly available financial report that includes financial statements and required supplementary information for SETHEEPP. That report is available on the state's website at http://www.state.tn.us/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 $3,926,390.23, $4,089,428.71, and $3,928,524.36. Contributions met the requirements for each year.

2. Federal Retirement Program

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

Retirement Programs. For both systems, benefit provisions are established in federal statutes. Federal statutes are amended by the U.S. Congress. All of the university's extension employees currently participate in CSRS.

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

Funding Policy - Participating employees and the university are required to contribute to the CSRS plan. Contribution requirements are established and may be amended by federal statutes. The university was required to contribute 7% of covered payroll to the CSRS plan, and employees were required to contribute 7% of covered payroll. Contributions to CSRS for the year ended June 30, 2009, were $52,581.80, which consisted of $26,290.90 from the university and $26,290.90 from the employees. Contributions for the year ended June 30, 2008, were $57,048.80, which consisted of $28,524.40 from the university and $28,524.40 from the employees. Contributions for the year ended June 30, 2007, were $55,393.80, which consisted of $27,696.90 from the university and $27,696.90 from the employees. Contributions met the requirements for each year.

B. Defined Contribution Plans

Optional Retirement Plans (ORP)

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

Funding Policy - Plan members are noncontributory. The university contributes an amount equal to 10% of the employee's base salary up to the social security wage base and 11% above the social security wage base. Contribution requirements are established and amended by state statute. The contribution made by the university to the plans was $3,825,435.74 for the year ended June 30, 2009, and $4,777,916.81 for the year ended June 30, 2008. Contributions met the requirements for each year.

NOTE 12. OTHER POSTEMPLOYMENT 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 Section 8-27-201, *Tennessee Code Annotated*, for the State Employee Group Plan and Section 8-27-701, *Tennessee Code Annotated*, 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 18. The plans are reported in the *Tennessee Comprehensive Annual Financial Report*. That report is available on the state's website at http://tennessee.gov/finance/act/cafr.html, or by calling (615) 741-2140.

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 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.

University's Annual OPEB Cost and Net OPEB Obligation
State Employee Group Plan

Annual required contribution (ARC)	$3,128,000.00
Interest on the net OPEB obligation	90,049.05
Adjustment to the ARC	(87,644.10)
Annual OPEB cost	3,130,404.95
Amount of contribution	(1,201,032.90)
Increase in net OPEB obligation	1,929,372.05
Net OPEB obligation – beginning of year	2,001,090.08
Net OPEB obligation – end of year	$3,930,462.13

Year-end	Plan	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation at Year-end
June 30, 2009	State Employee Group Plan	$3,130,404.95	38.4%	$3,930,462.13

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)	$26,258,000.00
Actuarial value of plan assets	-
Unfunded actuarial accrued liability (UAAL)	$26,258,000.00
Actuarial value of assets as a percentage of the AAL	0.00%
Covered payroll (active plan members)	$92,730,202.17
UAAL as percentage of covered payroll	28.3%

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 Required Supplementary Information 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.

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 13. 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 amounts of settlements have not exceeded insurance coverage for each of the three past 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://tennessee.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 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 $127.0 million in cash and cash equivalents designated for payment of claims.

At June 30, 2009, the scheduled coverage for the university was $422,658,400.00 for buildings and $84,475,500.00 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 that have been reported but not settled and of claims that have been incurred but not reported. Employees and providers have 13 months to file medical claims.

NOTE 14. COMMITMENTS AND CONTINGENCIES

Sick Leave

The university records the cost of sick leave when paid. Generally, since sick leave (earned one day per month with unlimited accumulation) is paid only when an employee dies or is absent because of illness, injury, or related family death, there is no liability for sick leave at June 30. The dollar amount of unused sick leave was $31,775,893.57 at June 30, 2009.

Operating Leases

The university has entered into various operating leases for buildings and equipment. Such leases will probably continue to be required. Expenses under operating leases for real property were $201,167.07 and for personal property were $115,854.87 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 $3,493,330.29 for ADA improvements, Avon Williams campus improvements, power plant mechanical upgrade, Agricultural Extension Center, Clement Hall Allied Health, Elliott Hall Exhibition, Student Housing Fire Suppression, Several Buildings Window and Water, Gentry Drainage Correction, Hankle Hall Renovation, Infrastructure Repairs, Roof Repair or Replacement, NBIC Roof Repairs, Network Infrastructure Improvements, Wilson Hall Interiors Upgrade, Center for AG Biotechnology, and Performing Arts/Radio Station, of which $1,247,304.64 will be funded by future state capital outlay appropriations.

Litigation

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

NOTE 15. CHAIRS OF EXCELLENCE

The university had $3,781,056.47 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 the financial statements.

NOTE 16. 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	Salaries	Benefits	Other Operating	Scholarships	Depreciation	Total
	Natural Classification					
Instruction	$ 37,002,887.83	$ 11,777,997.37	$ 14,629,278.44	$ 808,812.52	$ -	$ 64,218,976.16
Research	5,637,526.53	1,584,544.15	3,409,661.55	179,329.30	-	10,811,061.53
Public service	4,593,795.76	1,925,003.48	1,762,734.93	4,062.74	-	8,285,596.91
Academic support	5,873,453.70	2,169,701.73	2,043,021.84	23,254.43	-	10,109,431.70
Student services	7,191,112.40	2,421,131.87	4,261,077.47	911,145.94	-	14,784,467.68
Institutional support	9,510,273.65	3,820,425.47	3,283,260.30	118.42	-	16,614,077.84
Operation & maintenance	3,161,452.61	1,633,098.65	10,376,475.01	(570.05)	-	15,170,456.22
Scholarships & fellowships	5,679.86	2,348.88	121,495.01	9,291,038.40	-	9,420,562.15
Auxiliary	1,754,547.88	629,692.53	8,264,968.62	153,783.50	-	10,802,992.53
Depreciation	-	-	-	-	8,633,862.43	8,633,862.43
Total	$ 74,730,730.22	$ 25,963,944.13	$ 48,151,973.17	$ 11,370,975.20	$ 8,633,862.43	$ 168,851,485.15

NOTE 17. PRIOR-YEAR ADJUSTMENT

A prior year adjustment of $462,687.80 was made to accounts receivable. During fiscal year 2008, funds were received for a federally funded capital project. However, the receivable was not reduced. As a result, accounts receivable was overstated by this amount at June 30, 2008.

NOTE 18. ON-BEHALF PAYMENTS

During the year ended June 30, 2009, the State of Tennessee made payments of $55,135.00 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 12. The plan is reported in the *Tennessee Comprehensive Annual Financial Report*. That report is available on the state's website at http://tennessee.gov/finance/act/cafr.html.

NOTE 19. COMPONENT UNIT

The Tennessee State University Foundation is a legally separate, tax-exempt organization supporting 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 18-member board of the foundation is self-perpetuating and consists of graduates and friends of the university. The size of the board shall be determined by the majority votes of its members, any vacancy in its membership shall be filled in the same way. The entire membership of the Board of Trustees shall not exceed twenty-five (25) in number and a minimum of eight (8). All trustees shall serve until the expiration of their respective terms and until their respective successors are selected and qualified. 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 $31,886.59 to or on behalf of the university for both restricted and unrestricted purposes. Complete financial statements for the foundation can be obtained from Mr. Shereitte Stokes, Vice President for University Relations and Development, 3500 John A. Merritt Boulevard, Nashville, TN 37209.

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 $5,319,842.04 in bank accounts, and $2,562,571.03 in money market accounts.

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.

		Investment Maturities (in Years)				
Investment Type	Fair Value	Less than 1	1 to 5	6 to 10	More than 10	No Maturity Date
U. S. Treasury	$ 353,950.01	$ 202,143.02	$ -	$ 104,811.33	$ 46,995.66	$ -
U. S. Agencies	272,540.86	-	272,540.86	-	-	-
Corporate stocks	689,235.90	-	-	-	-	689,235.90
Corporate bonds	884,570.44	-	423,782.86	374,094.15	86,693.43	-
Mutual bond funds	8,557,176.54	-	-	-	-	8,557,176.54
Mutual equity funds and exchange traded funds	10,488,760.23	-	-	-	-	10,488,760.23
Other:						
Mortgage backed securities	868,924.82	-	-	82,951.73	785,973.09	-
REITs	3,105,275.08	-	-	-	-	3,105,275.08
Money market accounts	2,562,571.03	-	-	-	-	2,562,571.03
Savings account	3,108.95	-	-	-	-	3,108.95
Less cash and cash equivalents:						
Money market accounts	(2,562,571.03)	-	-	-	-	(2,562,571.03)
Savings account	(3,108.95)	-	-	-	-	(3,108.95)
Total	$ 25,220,433.88	$ 202,143.02	$ 696,323.72	$ 561,857.21	$ 919,662.18	$ 22,840,447.75

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 foundation 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. 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 has no investment policy limiting its investment choices based on ratings issued by nationally recognized statistical rating organizations.

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

		Credit Quality Rating				
Investment Type	Fair Value	AAA	AA	A	BBB	Unrated
US Agencies	$ 272,540.86	$ 272,540.86	$ -	$ -	$ -	$ -
Corporate bond	884,570.44	-	121,834.14	674,868.94	87,867.36	-
Mutual bond funds	8,557,176.54	-	-	-	-	8,557,176.54
Mortgage backed securities	868,924.82	-	-	-	-	868,924.82
Total	$ 10,583,212.66	$ 272,540.86	$ 121,834.14	$ 674,868.94	$ 87,867.36	$ 9,426,101.36

Alternative investments - The foundation has investments in Real Estate Investment Trusts (REITs). The estimated fair value of these assets is $3,105,275.08 at June 30, 2009.

The foundation believes that the carrying amount of its alternative investments is a reasonable estimate of fair value as of June 30, 2009. Because these investments are not readily marketable, the estimated value is subject to uncertainty and, therefore, may differ from the value that would have been used had a ready market for the investments existed, and such differences could be material. These investments are made in accordance with the foundation's investment policy that approves the allocation of funds to various asset classes in order to ensure the proper level of diversification. These investments are designed to enhance diversification and provide reductions in overall portfolio volatility. These fair values are estimated using various valuation techniques.

The value of shares is estimated to be the offering price of $10 per share (ignoring purchase price discounts for certain categories of purchasers), provided, however, that if the company has sold property and has made one or more special distributions to its stockholders of all or a portion of the net proceeds per share will be equal to $10 per share distributed to stockholders prior to the valuation date.

Endowments

The Tennessee State University Foundation's endowment consists of 79 individual funds established for a variety of purposes. Its endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. As required by GAAP, net assets associated with endowment funds, including funds designated by the Board of Trustees 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 Trustees of the Tennessee State University Foundation has interpreted the Uniform Prudent Management of Institutional Funds Act (the Act) as adopted by Tennessee and their intention is to abide by all applicable laws as it relates to financial obligations, annual giving, and portfolio management and oversight. As a result of this interpretation, the Tennessee State University Foundation classifies as permanently restricted net assets (1) the original value of gifts donated to the permanent endowment; (2) the original value of subsequent gifts to the permanent endowment; and (3) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted 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 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; and (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 board is willing to expose the investments of the foundation to a risk level of conservative to moderate in nature. The foundation expects its endowment funds, over time, to provide an average rate of return of approximately 7%, or 4% plus inflation as measured by the Consumer Price Index 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.

<u>Spending policy and how the investment objectives relate</u> - The foundation has a policy of appropriating for distribution each year, an amount equal to 40% of the 3-year average interest and dividend income rate. 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 2-3 percent annually. This is consistent with the foundation's objective to 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 $1,319,645.03 is available to be spent, of which $1,222,746.20 is included in restricted net assets expendable for scholarships and fellowships, $5,747.63 is included in restricted net assets expendable for instructional departmental uses, and $91,151.20 is included in restricted net assets expendable for other.

Tennessee Board of Regents
Tennessee State University
Required Supplementary Information
OPEB 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	$ 0.00	$26,258,000	$26,258,000	0.0%	$92,730,202	28.3%

TENNESSEE BOARD OF REGENTS
TENNESSEE STATE UNIVERSITY
SUPPLEMENTARY SCHEDULE OF CASH FLOWS - COMPONENT UNIT
FOR THE YEAR ENDED JUNE 30, 2009

		Year Ended June 30, 2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Gifts and contributions	$	1,432,373.10
Payments to suppliers and vendors		(719,705.36)
Payments for scholarships and fellowships		(661,600.45)
Payments to Tennessee State University		(31,886.59)
Other receipts (payments)		213,210.90
Net cash provided by operating activities		232,391.60
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Gifts and grants received for other than capital or endowment purposes		2,026,136.00
Private gifts for endowment purposes		76,157.70
Net cash provided by noncapital financing activities		2,102,293.70
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments		10,237,811.53
Income on investments		1,003,448.24
Purchases of investments		(10,710,604.33)
Net cash provided (used) by investing activities		530,655.44
Net decrease in cash and cash equivalents		2,865,340.74
Cash and cash equivalents - beginning of year		5,017,072.33
Cash and cash equivalents - end of year	$	7,882,413.07
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	$	236,206.88
Adjustments to reconcile operating income to net cash provided by operating activities:		
Accounts payable		(3,815.28)
Net cash provided by operating activities	$	232,391.60
Noncash transactions		
Unrealized losses on investments	$	(4,780,576.17)