AUDIT REPORT

Tennessee Board of Regents
East Tennessee State University

For the Year Ended
June 30, 2012

STATE OF TENNESSEE

COMPTROLLER OF THE TREASURY

Department of Audit

Division of State Audit

Tennessee Comptroller of the Treasury

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November 29, 2012

The Honorable Bill Haslam, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and
The Honorable John G. Morgan, Chancellor
Tennessee Board of Regents
1415 Murfreesboro Road, Suite 340
Nashville, Tennessee 37217
and
Dr. Brian Noland, President
East Tennessee State University
Campus Box 70734
Johnson City, Tennessee 37614-0734

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Tennessee Board of Regents, East Tennessee State University, for the year ended June 30, 2012. You will note from the independent auditor's report that unqualified opinions were given on the fairness of the presentation of the financial statements.

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

Sincerely,

Arthur A. Hayes, Jr.

Arthur A. Hayes, Jr., CPA
Director

AAH/sds
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State of Tennessee

Audit Highlights

Comptroller of the Treasury — Division of State Audit

Financial and Compliance Audit
East Tennessee State University
For the Year Ended June 30, 2012

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.

COMPLIANCE FINDING

Notifications Required by Federal Regulations Were Not Performed for Perkins Loans in Default Status*
The Bursar at East Tennessee State University did not ensure that all notification procedures were performed for Perkins Loans in default status. Required notification letters were not always sent. "Intent to accelerate" letters were not always mailed at least 30 days prior to the effective date of acceleration (page 9).

OPINIONS ON THE FINANCIAL STATEMENTS

The opinions on the financial statements are unqualified.

* This finding is repeated from the prior audit.

Audit Report
Tennessee Board of Regents
East Tennessee State University
For the Year Ended June 30, 2012

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Tennessee Board of Regents
East Tennessee State University
For the Year Ended June 30, 2012

INTRODUCTION

POST-AUDIT AUTHORITY

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

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

BACKGROUND

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

The university has 11 colleges and schools: the College of Arts and Sciences, the College of Business and Technology, the College of Education, the College of Medicine, the College of Nursing, the College of Pharmacy, the College of Public Health, the College of Clinical and Rehabilitative Health Sciences, the Honors College, the School of Continuing Studies and Academic Outreach, and the School of Graduate Studies. East Tennessee State University is officially authorized to grant degrees for 59 bachelor's, 38 master's, one specialist, 11 doctoral, and 2 professional programs.

ORGANIZATION

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

AUDIT SCOPE

The audit was limited to the period July 1, 2011, through June 30, 2012, 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, 2012. East Tennessee State University is an institution of the Tennessee Board of Regents, which is an integral part of state government. As such, the Tennessee Board of Regents has been included as a component unit in the *Tennessee Comprehensive Annual Financial Report.*

OBJECTIVES OF THE AUDIT

The objectives of the audit were

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

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

audit of the State of Tennessee, which is conducted in accordance with the Single Audit Act.

PRIOR AUDIT FINDINGS

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 May 10, 2012. A follow-up of the prior audit findings was conducted as part of the current audit.

RESOLVED AUDIT FINDING

The current audit disclosed that the university has corrected a previous audit finding concerning the failure to document Direct Loan reconciliations.

REPEATED AUDIT FINDING

The prior audit report also contained a finding concerning notifications required by federal regulations to Perkins Loan recipients in default status. 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, 2012, we considered internal control over financial reporting as a basis for designing auditing procedures for the purpose of expressing opinions on the financial statements, as required by auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards. Consideration of internal control over financial reporting disclosed no material weaknesses.

Compliance and Other Matters

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under generally accepted government auditing standards. An immaterial instance of noncompliance, along with a recommendation and management's response, is included in the Finding and Recommendation section.

Fairness of Financial Statement Presentation

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

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

November 16, 2012

The Honorable Bill Haslam, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and
The Honorable John G. Morgan, Chancellor
Tennessee Board of Regents
1415 Murfreesboro Road, Suite 340
Nashville, Tennessee 37217
and
Dr. Brian Noland, President
East Tennessee State University
Campus Box 70734
Johnson City, Tennessee 37614-0734

Ladies and Gentlemen:

We have audited the financial statements of East Tennessee State University, an institution of the Tennessee Board of Regents, which is a component unit of the State of Tennessee, and its discretely presented component units as of and for the year ended June 30, 2012, and have issued our report thereon dated November 16, 2012. Our report was modified to include a reference to other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in generally accepted government auditing standards.

Internal Control Over Financial Reporting

Management of the university is responsible for establishing and maintaining effective 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.

A *deficiency in internal control* 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 and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

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 its 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.

We did, however, note an immaterial instance of noncompliance that we have included in the Finding and Recommendation section of this report.

We noted certain matters that we reported to the management of East Tennessee State University in a separate letter.

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

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

Sincerely,

Arthur A. Hayes, Jr., CPA
Director

AAH/sds

FINDING AND RECOMMENDATION

<u>Notifications required by federal regulations were not performed for Perkins Loans in default status</u>

Finding

East Tennessee State University did not ensure that all notification procedures were performed for Perkins Loans in default status. A similar finding was reported in the previous audit.

According to the *Federal Student Aid Handbook*, volume 6, pages 99-100:

> If a payment is overdue and you have not received a request for forbearance, deferment, or cancellation, you must send the borrower:
>
> - the first overdue notice 15 days after the payment due date;
> - the second overdue notice 30 days after the first overdue notice;
> - the final demand letter 15 days after the second overdue notice.
>
> If [a] borrower does not respond to the final demand letter within 30 days, [the school] must try to contact him or her by telephone before beginning collection procedures. As telephone contact is often very effective in getting the borrower to begin repayment, one call may avoid the more costly procedures of collection.
>
> You should make at least two attempts to reach the borrower on different days and at different times. If the borrower has an unlisted telephone number, you must make reasonable attempts to obtain it by contacting sources such as the borrower's employer or parents. If you are still unsuccessful, you should document the contact attempts in your files.
>
> [The school] may accelerate a loan if the borrower misses a payment or does not file for a deferment, forbearance, or cancellation on time. Acceleration means immediately making payable the entire outstanding balance, including interest and any applicable late charges or collection fees.
>
> Because [loan acceleration] marks a serious stage of default, the borrower should have one last chance to bring his or her account current. For that reason, if the school plans to accelerate the loan, it must send the borrower a written acceleration notice at least 30 days in advance.

For the year ended June 30, 2012, we reviewed the files of 25 students whose Perkins Loans went into default during the fiscal year. We noted the following discrepancies:

- For 11 of 25 students tested (44%), neither the Bursar's Office nor the university's contracted loan servicing agency mailed the final demand letters.

- For 3 of 25 students tested (12%), neither the Bursar's Office nor the university's contracted loan servicing agency made documented additional attempts to contact borrowers with no phone number or an unlisted or invalid phone number. If the student has no additional contact sources (e.g., parents or employers) or additional attempts to contact the student are unsuccessful, this should be documented.

- For 12 of 25 students tested (48%), neither the Bursar's Office nor the university's contracted loan servicing agency mailed the "intent to accelerate" letters at least 30 days prior to the effective date of acceleration. These intent to accelerate letters were mailed, but between 27 and 29 days prior to the acceleration date, rather than the required 30 days.

Based on our discussions with the Bursar, the phone calls and letters described above were the responsibility of the loan servicing agency.

Even though the university uses an outside vendor to perform billing procedures, the responsibility for compliance with federal regulations lies with the university. The *Federal Student Aid Handbook*, volume 6, page 108, states:

> Your school may use a contractor for billing or collection, but it is still responsible for complying with due diligence regulations regarding those activities.

Not ensuring the borrowers were adequately notified before being transferred to a collection agency or before loan acceleration could lead to unnecessary collection costs and/or financial hardship for borrowers in default.

Recommendation

The Bursar should ensure that the university follows due diligence procedures regarding Federal Perkins Loans in default status. Specifically, the Bursar should ensure that the university or its designee mail final demand letters to students in default. The Bursar should ensure that the university or its designee makes the required phone calls to students before referring loans to collections. If the required phone call cannot be made or additional attempts to contact the student are unsuccessful, this should be documented. Finally, the Bursar should ensure that the university or its designee mails the intent to accelerate letters at least 30 days prior to the effective date of the loan acceleration.

The Bursar should ensure that risks such as those noted in this finding are adequately identified and assessed in the university's risk assessment activities. The Bursar should identify specific staff to be responsible for the design and implementation of internal controls to prevent and detect exceptions timely. The Bursar should also identify staff to be responsible for ongoing monitoring for compliance with all requirements and take prompt action should exceptions occur.

Management's Comment

We concur with the finding and recommendation.

In the instances of the borrowers who were not mailed a final demand letter, the loan processing contractor had an error in its electronic loan system that removed 60-day letters from the automatic process for a small subset of schools. This was identified and corrected in September of 2011. This was a one-time issue that has been corrected and has not recurred.

The university determined the missing phone numbers for borrowers were the result of incomplete migration of data from the university to the loan processing contractor at the inception of the contract. The university will obtain a listing from the loan processing contractor of all borrowers in its system with no phone number and will review institutional records to identify a phone number. This review will be documented. Phone numbers that are identified will be forwarded to the loan processing contractor to update the borrower's record in the contractor's system. All phone calls to borrowers and the response received are logged on a report maintained by the loan processing contractor.

The loan processing contractor requested the Department of Education review the contractor's interpretation of the letter of intent to accelerate. The Department of Education provided the contactor with the department's intent of this regulation. Based on that review, the loan processing contractor changed the system logic that triggered the letters. This logic was changed in March of 2012 and the pre-acceleration letters are now sent out at least 30 days prior to the acceleration date.

The university will ensure risks of compliance with loan servicing are included in the university's risk assessment. A staff member in the Bursar's Office has been assigned the responsibility to review compliance and monitor loan servicing by the contractor. The Bursar will review the results of the monitoring on a periodic basis.

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Independent Auditor's Report

November 16, 2012

The Honorable Bill Haslam, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and
The Honorable John G. Morgan, Chancellor
Tennessee Board of Regents
1415 Murfreesboro Road, Suite 340
Nashville, Tennessee 37217
and
Dr. Brian Noland, President
East Tennessee State University
Campus Box 70734
Johnson City, Tennessee 37614-0734

Ladies and Gentlemen:

We have audited the accompanying basic financial statements of East Tennessee State University, an institution of the Tennessee Board of Regents, which is a component unit of the State of Tennessee, as of and for the year ended June 30, 2012, as listed in the table of contents. These financial statements are the responsibility of the university's management. Our responsibility is to express opinions on these financial statements, based on our audit. We did not audit the financial statements of the East Tennessee State University Foundation and the Medical Education Assistance Corporation, discretely presented component units of the university. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the East Tennessee State University Foundation and the Medical Education Assistance Corporation, is based on the reports of the other auditors.

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

As discussed in Note 1, the financial statements of East Tennessee State University, an institution of the Tennessee Board of Regents, are intended to present the financial position, the changes in financial position, and the cash flows of only East Tennessee State University. They do not purport to, and do not, present fairly the financial position of the Tennessee Board of Regents, as of June 30, 2012, and the changes in its financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of East Tennessee State University, and its discretely presented component units as of June 30, 2012, and the respective changes in financial position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 15 through 33 and the schedule of funding progress on page 68 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, which considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during the audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

November 16, 2012
Page Three

Our audit was conducted for the purpose of forming opinions on the basic financial statements as a whole. The accompanying financial information on pages 69 and 70 is presented for purposes of additional analysis and is not a required part of the basic financial statements. This information is the responsibility of the university's management and was derived from, and relates directly to, the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves and other additional procedures, in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information, based on our audit and the reports of the other auditors, 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 November 16, 2012, 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 considered in assessing the results of our audit.

Sincerely,

Arthur A. Hayes, Jr.

Arthur A. Hayes, Jr., CPA
Director

AAH/sds

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

This section of East Tennessee State University's annual financial report presents a discussion and analysis of the financial performance of the university during the fiscal year ended June 30, 2012, with comparative information presented for the fiscal year ended June 30, 2011. This discussion has been prepared by management along with the financial statements and related note disclosures and should be read in conjunction with the independent auditor's report and the audited financial statements and notes. The financial statements, notes, and this discussion are the responsibility of management.

The university has two discretely presented component units, the East Tennessee State University Foundation and the Medical Education Assistance Corporation (MEAC). More detailed discussion about the university's component units is presented in Note 21 in the notes to the financial statements. Information and analysis regarding the component units are also included in this section.

Using This Annual Report

This report consists of three basic financial statements. The statement of net assets; the statement of revenues, expenses, and changes in net assets; and the statement of cash flows provide information on East Tennessee State University as a whole and present a long-term view of the university's finances.

The Statement of Net Assets

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

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

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

	2012	2011
Assets:		
Current assets	$ 38,675	$ 50,773
Capital assets, net	269,329	264,784
Other assets	104,606	94,933
Total assets	**412,610**	**410,490**
Liabilities:		
Current liabilities	33,517	34,665
Noncurrent liabilities	155,782	153,121
Total liabilities	**189,299**	**187,786**
Net assets:		
Invested in capital assets, net of related debt	138,427	135,746
Restricted – expendable	6,615	7,304
Unrestricted	78,269	79,654
Total net assets	**$223,311**	**$222,704**

Comparison of fiscal year 2012 to fiscal year 2011

- Current assets decreased from 2011 to 2012 due to decreases in student accounts receivable because of an early start date for College of Pharmacy summer classes in 2012. In addition, current accounts receivable also decreased because Graduate Medical Education funds were receivable at June 30, 2011, but not at June 30, 2012.

- In 2012, other assets increased due to increases in bond investments.

- Capital assets, net of depreciation, increased from 2011 to 2012 due to the completion of the College of Medicine Student Center, student apartments, transfer of the Valleybrook property from the ETSU Foundation, and several renovation projects, including dormitory renovations, HVAC upgrades, and window replacements.

- Current liabilities decreased from 2011 to 2012 due to the decreases in deferred revenue related to an earlier start date for the College of Pharmacy.

- In 2012, noncurrent liabilities increased due to the prior period adjustment to record bond premiums.

- Invested in capital assets, net of related debt, increased in 2012 due to the completion of the capital projects noted above.

- Unrestricted net assets decreased from 2011 to 2012 due to decreases in working capital for accounts receivable.

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

	2012	2011
Assets:		
Current assets	$ 98	$ 51
Capital assets, net	9	1,661
Other assets	75,999	75,900
Total assets	**76,106**	**77,612**
Liabilities:		
Current liabilities	93	55
Total liabilities	**93**	**55**
Net assets:		
Invested in capital assets, net of related debt	9	1,661
Restricted – nonexpendable	58,089	58,100
Restricted – expendable	17,034	16,526
Unrestricted	881	1,270
Total net assets	**$76,013**	**$77,557**

Comparison of fiscal year 2012 to fiscal year 2011

- Current assets increased due to an increase in investment in the State of Tennessee Local Government Investment Pool (LGIP).

- Capital assets and invested in capital assets decreased due to the transfer of the Valleybrook property to ETSU.

- Current liabilities increased due to an accounts payable accrual increase at June 30.

- Expendable net assets increased due to investment income growth.

- Unrestricted net assets decreased due to unrealized market losses.

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

	2012	2011
Assets:		
Current assets	$18,373	$14,755
Capital assets, net	2,889	3,061
Other assets	4,825	7,623
Total assets	**26,087**	**25,439**
Liabilities:		
Current liabilities	4,688	4,786
Noncurrent liabilities	2,041	2,010
Total liabilities	**6,729**	**6,796**
Net assets:		
Invested in capital assets, net of related debt	1,361	1,497
Unrestricted	17,997	17,146
Total net assets	**$19,358**	**$18,643**

Comparison of fiscal year 2012 to fiscal year 2011

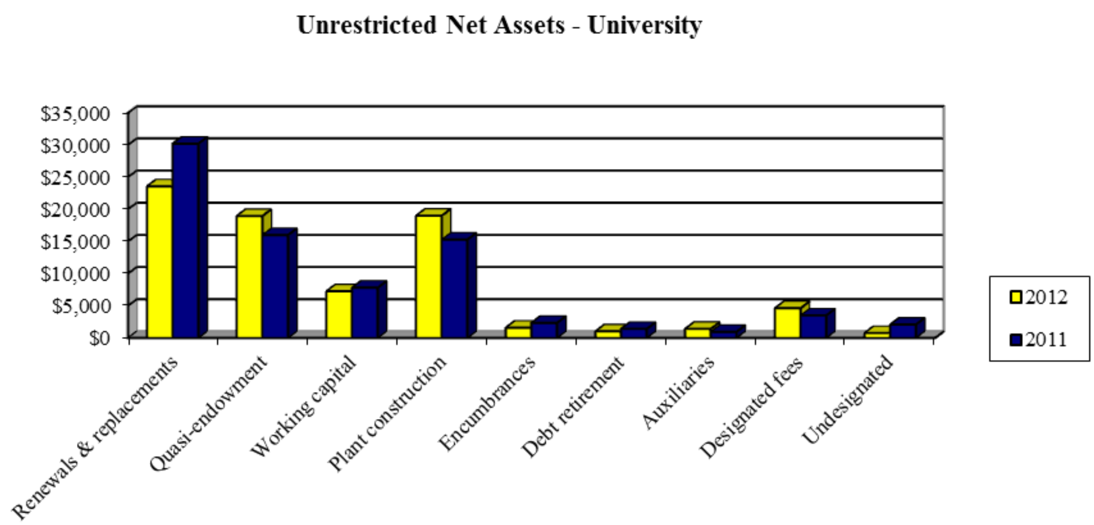
- Current assets increased in fiscal year 2012 as a result of an increase in cash and short-term investments.

- Other assets decreased due to long-term investments maturing into short-term investments.

- Days in accounts receivable were 26 in June 2012 compared to 27 in June 2011.

- Liabilities decreased slightly in fiscal year 2012 due to decreases in accrued compensation and accrued expenses.

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



<u>Comparison of fiscal year 2012 to fiscal year 2011</u>

- The allocations for renewals and replacements decreased due to completion of some renovation projects.
- The allocation for quasi-endowments increased primarily due to a $1.5 million increase in the endowment for College of Medicine Clinical Services.
- The allocation for working capital decreased with the reduction in accounts receivable.
- The allocation for plant construction increased as a result of increases for a student parking garage.
- Other allocations remained relatively unchanged.

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

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

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

	2012	2011
Operating revenues:		
Net tuition and fees	$ 80,653	$ 70,466
Grants and contracts	38,912	38,768
Auxiliary	18,665	17,843
Other	29,204	28,399
Total operating revenues	**167,434**	**155,476**
Operating expenses	309,873	297,594
Operating income (loss)	**(142,439)**	**(142,118)**
Nonoperating revenues and expenses:		
State appropriations	78,140	98,631
Gifts	4,385	3,450
Grants and contracts	55,494	60,287
Investment income	1,390	1,298
Other nonoperating revenues (expenses)	(4,658)	(5,791)
Total nonoperating revenues and expenses	**134,751**	**157,875**
Income (loss) before other revenues, expenses, gains, or losses	**(7,688)**	**15,757**
Other revenues, expenses, gains, or losses:		
Capital appropriations	4,664	1,629
Capital grants and gifts	6,074	3,085
Total other revenues, expenses, gains, or losses	**10,738**	**4,714**
Increase in net assets	**3,050**	**20,471**
Net assets at beginning of year	**222,704**	**202,233**

Prior-period adjustment	**(2,443)**	**-**
Net assets at end of year	**$223,311**	**$222,704**

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

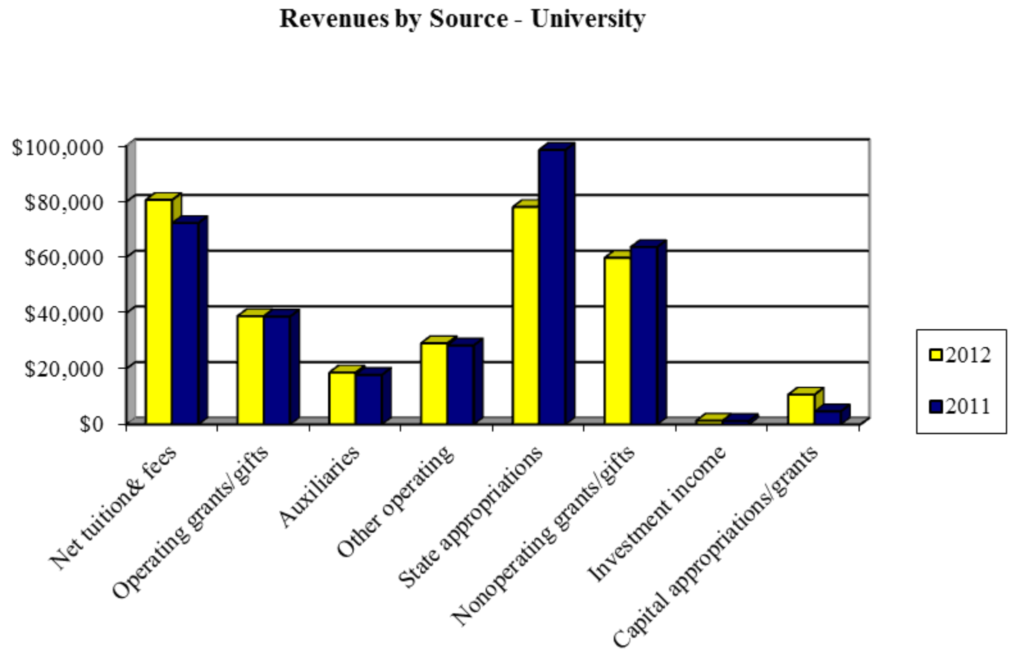
	2012	2011
Operating revenues and expenses:		
Operating revenues	$ 3,848	$ 2,939
Operating expenses	5,331	4,615
Operating income (loss)	**(1,483)**	**(1,676)**
Nonoperating revenues and expenses:		
Investment income (loss)	(598)	11,639
Other nonoperating revenues (expenses)	(1,627)	(741)
Total nonoperating revenues and expenses	**(2,225)**	**10,898**
Income (loss) before other revenues, expenses, gains, or losses	**(3,708)**	**9,222**
Other revenues, expenses, gains, or losses:		
Capital grants and gifts	46	601
Additions to permanent endowments	2,118	2,428
Total other revenues, expenses, gains, or losses	**2,164**	**3,029**
Increase (decrease) in net assets	**(1,544)**	**12,251**
Net assets at beginning of year	**77,557**	**65,306**
Net assets at end of year	**$76,013**	**$77,557**

MEAC
Condensed Statements of Revenues, Expenses, and Changes in Net Assets
(in thousands of dollars)

	2012	2011
Operating revenues and expenses:		
Operating revenues	$37,803	$39,568
Operating expenses	35,463	36,272
Operating income	**2,340**	**3,296**
Nonoperating revenues and expenses:		
Investment income	155	256
Payments to ETSU and ETSU Foundation	(3,413)	(2,520)
Other nonoperating revenues (expenses)	1,633	(91)
Total nonoperating revenues and expenses	**(1,625)**	**(2,355)**
Increase in net assets	**715**	**941**
Net assets at beginning of year	**18,643**	**17,702**
Net assets at end of year	**$19,358**	**$18,643**

Revenues

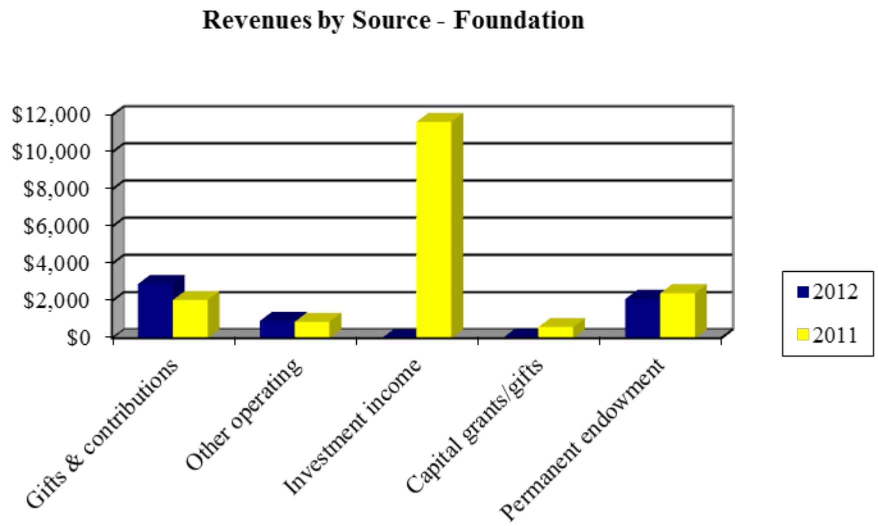
The following is a graphic illustration of ETSU revenues by source (both operating and nonoperating), which were used to fund the university's operating activities for the years ended June 30, 2012, and June 30, 2011. Amounts are presented in thousands of dollars.



Comparison of fiscal year 2012 to fiscal year 2011

- Tuition and fees increased in 2012 due to an average 8% fee increase and increases in enrollment.
- Auxiliary revenue increased due to an increased number of dormitory rooms and increased rates.
- State appropriations decreased due to decreased funding from the state.
- Nonoperating grants and gifts decreased as a result of the termination of American Recovery and Reinvestment Act (ARRA) State Fiscal Stabilization Funds.
- Capital appropriations, gifts, and grants increased primarily due to a capital grant through the American Recovery and Reinvestment Act for the Johnson City Community Health Center Building and transfer of the Valleybrook property from the ETSU Foundation.
- Other categories remained relatively unchanged.

The following is a graphic illustration of foundation revenues by source (both operating and nonoperating), which were used to fund the university's operating activities for the years ended June 30, 2012, and June 30, 2011. Amounts are presented in thousands of dollars.



Comparison of fiscal year 2012 to fiscal year 2011

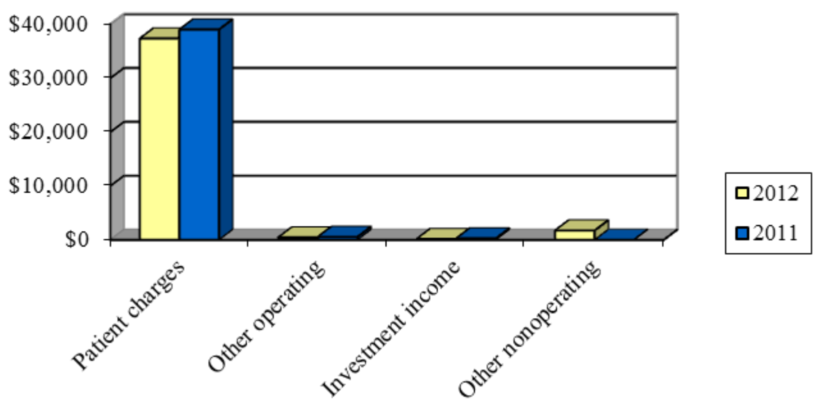
- Operating revenues increased due to new giving for the College of Medicine programs and the Athletics Department and an increased transfer from the Medical Education Assistance Corporation.

- Investment income decreased due to unrealized losses as a result of declining market conditions.

- Capital grants and gifts decreased due to gifts received in fiscal year 2011 for the Baseball Stadium and Quillen College of Medicine Student Study Center.

The following is a graphic illustration of MEAC revenues by source (both operating and nonoperating), which were used to fund the university's operating activities for the years ended June 30, 2012, and June 30, 2011. Amounts are presented in thousands of dollars.

Revenues by Source - MEAC



Comparison of fiscal year 2012 to fiscal year 2011

- Patient service revenue was decreased by 4% primarily due to contractual arrangements with hospital systems that replaced patient service revenue with physician service agreements. The practice saw decreased revenue, but increased net income, from each arrangement.

- Interest income decreased significantly in fiscal year 2012 due to lower rates of return.

Expenses

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

University
Natural Classification

	2012	2011
Salaries	$153,015	$147,213
Benefits	50,983	49,365
Other operating	60,830	58,125
Scholarships	29,028	29,603
Depreciation	16,017	13,288
Total expenses	**$309,873**	**$297,594**

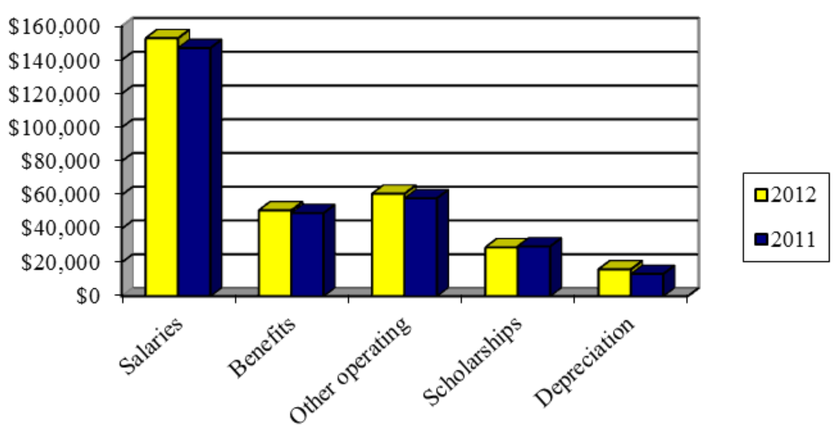
Foundation
Natural Classification

	2012	2011
Other operating	$2,662	$1,511
Scholarships	1,627	1,469
Depreciation	-	33
Payments to or on behalf of ETSU	1,042	1,602
Total expenses	**$5,331**	**$4,615**

MEAC
Natural Classification

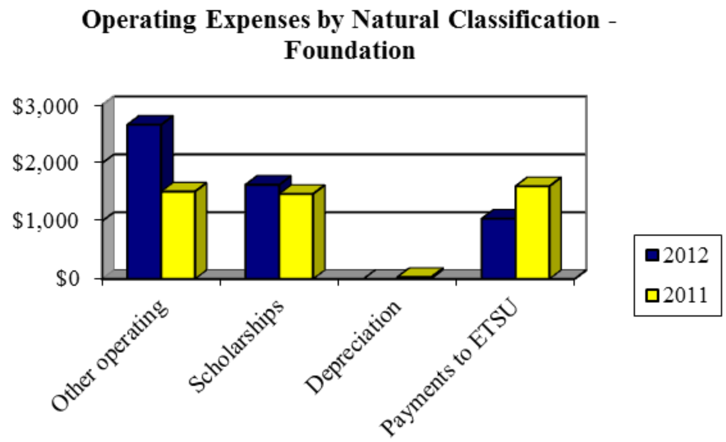
	2012	2011
Salaries	$22,780	$23,732
Benefits	2,122	2,341
Other operating	10,104	9,809
Depreciation	457	390
Total expenses	**$35,463**	**$36,272**

Operating Expenses by Natural Classification - University



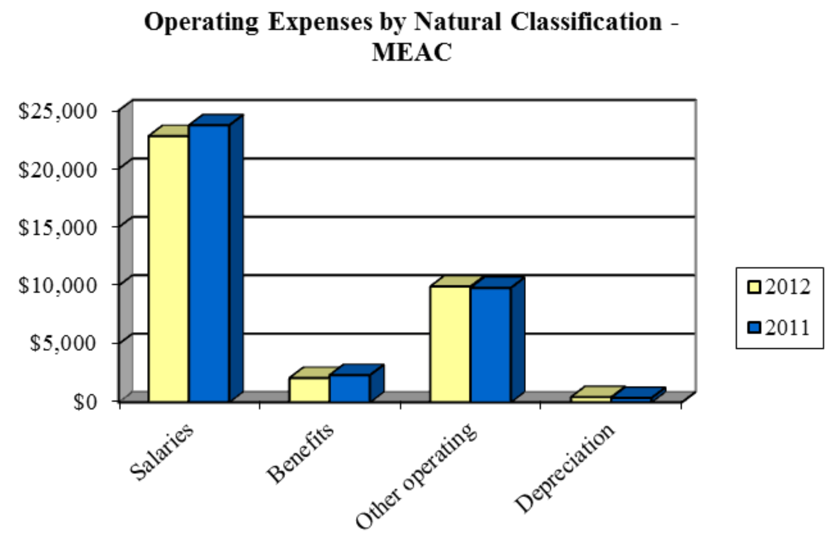
Comparison of fiscal year 2012 to fiscal year 2011

- Salaries increased primarily due to a 3% across-the-board pay increase.
- Benefits increased based on the increase in salaries.
- Other operating expenses increased with increases in professional and administrative services and supplies.
- Scholarships remained at prior-year levels.
- Depreciation expense increased from 2011 to 2012 with the completion of construction projects, most notably the College of Medicine Student Center and student apartments.



Comparison of fiscal year 2012 to fiscal year 2011

- Operating expenses increased due to an increase of restricted in-kind gifts and additional use of funds for supplies and other expenses.
- Scholarships increased due to additional awards from the College of Education, College of Pharmacy, and the Roan Scholars Leadership Program.
- Depreciation decreased due to the transfer of Valleybrook to ETSU.
- Payments to or on behalf of ETSU decreased due to the transfer of the Alumni Plaza Phase II in fiscal year 2011.



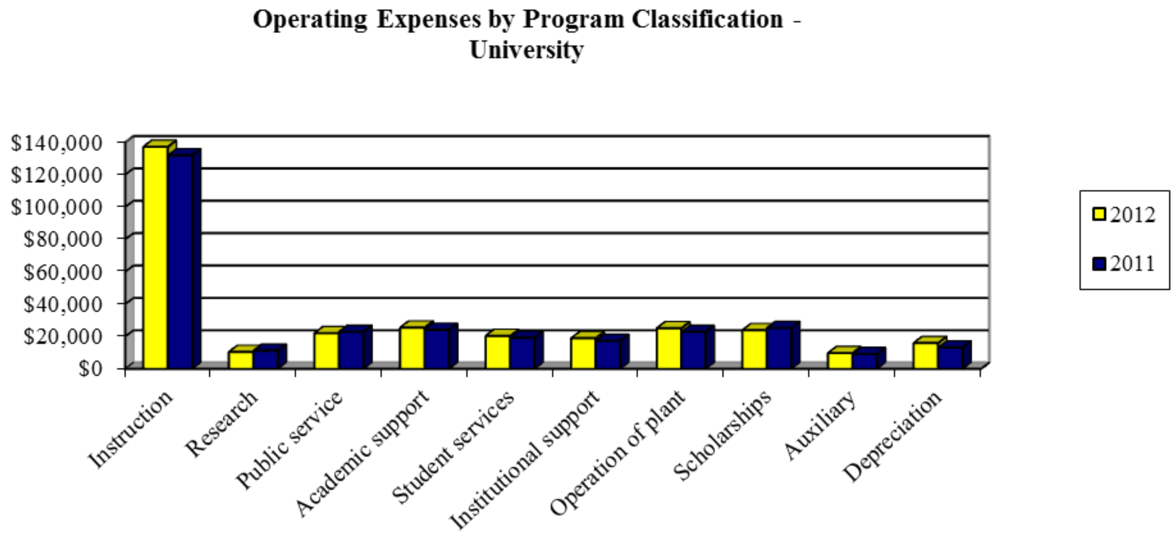
Comparison of fiscal year 2012 to fiscal year 2011

- In fiscal year 2012, physician compensation decreased 7.03% due to decreased patient service revenue.

- The expenses for medical supplies and occupancy remained consistent with the prior year. Professional liability (malpractice) insurance costs decreased by 17% due to rate reductions. Also, other administrative expenses increased.

Program Classification
University
(in thousands)

	2012	2011
Instruction	$137,219	$132,016
Research	10,542	11,238
Public service	22,108	22,859
Academic support	25,523	24,161
Student services	20,424	19,269
Institutional support	19,025	17,325
Operation and maintenance of plant	25,204	22,930
Scholarships	23,976	25,274
Auxiliary	9,835	9,234
Depreciation	16,017	13,288
Total expenses	**$309,873**	**$297,594**



<u>Comparison of fiscal year 2012 to fiscal year 2011</u>

- Instruction is the largest expenditure area for the university. Increases in instruction were largely due to the increases in enrollment and compensation.

- Depreciation increased from 2011 to 2012 with the completion of construction projects, most notably the College of Medicine Student Center and student apartments.

- Expenditures in other areas did not change materially from 2011 to 2012.

Capital Asset and Debt Administration

<u>Capital Assets</u>

The university had $269 million invested in capital assets, net of accumulated depreciation of $169 million at June 30, 2012; and $265 million invested in capital assets, net of accumulated depreciation of $162 million at June 30, 2011. Depreciation charges totaled $16 million and $13 million for the years ended June 30, 2012, and June 30, 2011, respectively. Details of these assets are shown below.

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

	2012	2011
Land	$ 16,451	$ 15,761
Land improvements & infrastructure	21,121	21,301
Buildings	203,937	195,171
Equipment	12,222	11,827
Library holdings	727	3,121
Software	1,800	2,221
Projects in progress	13,071	15,382
Total capital assets, net	**$269,329**	**$264,784**

Comparison of fiscal year 2012 to fiscal year 2011

- In 2012, capital assets increased from the completion of the College of Medicine Student Center, student apartments, and several renovation projects.

At June 30, 2012, and June 30, 2011, the foundation had $9,486 and $1,661,153, respectively, invested in capital assets, net of accumulated depreciation. Depreciation charges totaled $0 for fiscal year 2012 and $33,333 for fiscal year 2011. Details of these assets are shown below.

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

	2012	2011
Land	$ -	$ 685
Buildings	-	967
Equipment	9	9
Total capital assets, net	**$9**	**$1,661**

Comparison of fiscal year 2012 to fiscal year 2011

- Decreases in fiscal year 2012 are due to the transfer of the Valleybrook facility to the university.

MEAC had $2,889,144 in capital assets, net of accumulated depreciation at June 30, 2012; and $3,060,607 in capital assets, net of accumulated depreciation at June 30, 2011. Depreciation charges totaled $457,000 for the current fiscal year and $390,000 for the prior year. Details of these assets are shown below.

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

	2012	2011
Land	$ 18	$ 18
Buildings	1,953	1,918
Equipment	918	1,125
Total capital assets, net	**$2,889**	**$3,061**

- In 2012, net investment in capital assets decreased due to increases in accumulated depreciation exceeding capital asset additions.

See Notes 5 and 21 for additional details on capital assets.

Debt

The university had $131 million and $129 million in debt outstanding at June 30, 2012, and June 30, 2011, respectively. The table below summarizes these amounts by type of debt instrument.

University
Outstanding Debt Schedule
(in thousands of dollars)

	2012	2011
Commercial paper	$ 23,501	$ 18,649
Loans	-	1,238
Bonds	105,106	109,151
Unamortized bond premiums	2,295	-
Total debt	**$130,902**	**$129,038**

Comparison of fiscal year 2012 to fiscal year 2011

- In 2012, commercial paper increased due to construction on the baseball stadium, student apartments, and housing renovations.

- The university recorded unamortized bond premiums greater than $100,000 in 2012, as discussed in Note 17.

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

The ETSU Foundation had no outstanding debt at June 30, 2012.

MEAC
Outstanding Debt Schedule
(in thousands of dollars)

	2012	**2011**
Notes	$1,528	$1,564
Total debt	**$1,528**	**$1,564**

Comparison of fiscal year 2012 to fiscal year 2011

- MEAC has one note payable for the Kingsport facility, and the note has a declining balance due. This note was refinanced during fiscal year 2011 to take advantage of current interest rates.

Economic Factors That Will Affect the Future

The economic outlook for the State of Tennessee has improved during fiscal year 2012. The state approved funding for a 2.5% across-the-board salary increase through appropriations and fee increases. This was the second year for wage increases after a four-year period with no raises. The Tennessee Board of Regents approved an increase in fees by an average of 8.2% for the university. Portions of the fee increase will fund a 3% salary equity pool for university employees and board level technological enhancements for data. It is hoped that state revenues will continue to increase and that no further appropriation reductions will be required.

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

Requests for Information

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

TENNESSEE BOARD OF REGENTS
EAST TENNESSEE STATE UNIVERSITY
STATEMENTS OF NET ASSETS
JUNE 30, 2012

		Component Units	
	East Tennessee State University	East Tennessee State University Foundation	Medical Education Assistance Corporation
ASSETS			
Current assets:			
Cash and cash equivalents (Notes 2, 3, and 21)	$ 21,333,411.66	$ 69,385.56	$ 6,018,878.00
Short-term investments (Note 21)	-	-	8,047,507.00
Accounts, notes, and grants receivable (net) (Note 4)	15,684,850.87	-	3,687,480.00
Due from primary government	176,600.00	-	-
Pledges receivable (net) (Note 21)	-	470.30	-
Inventories	306,358.27	-	-
Prepaid expenses and deferred charges	471,900.28	-	618,687.00
Accrued interest receivable	691,694.89	28,218.74	-
Other assets	9,691.70	-	-
Total current assets	38,674,507.67	98,074.60	18,372,552.00
Noncurrent assets:			
Cash and cash equivalents (Notes 2, 3, and 21)	45,175,385.98	5,319,830.32	-
Investments (Notes 3 and 21)	53,173,080.00	69,342,039.49	2,299,728.00
Accounts, notes, and grants receivable (net) (Note 4)	6,259,095.44	-	-
Pledges receivable (net) (Note 21)	-	1,042,157.70	-
Capital assets (net) (Notes 5 and 21)	269,328,591.00	9,486.00	2,889,144.00
Other assets	-	294,167.51	2,525,435.00
Total noncurrent assets	373,936,152.42	76,007,681.02	7,714,307.00
Total assets	412,610,660.09	76,105,755.62	26,086,859.00
LIABILITIES			
Current liabilities:			
Accounts payable (Note 7)	4,036,244.34	93,092.85	591,139.00
Accrued liabilities	5,911,986.33	-	2,585,517.00
Student deposits	695,689.41	-	-
Deferred revenue (Note 8)	12,208,313.77	-	-
Compensated absences (Notes 8 and 21)	2,942,233.51	-	137,593.00
Accrued interest payable	905,836.76	-	-
Long-term liabilities, current portion (Notes 8 and 21)	4,098,626.03	-	37,006.00
Deposits held in custody for others	2,718,603.49	-	459,098.00
Other liabilities	-	-	877,206.00
Total current liabilities	33,517,533.64	93,092.85	4,687,559.00
Noncurrent liabilities:			
Deferred revenue (Note 8)	2,525,435.53	-	-
Compensated absences (Notes 8 and 21)	7,296,602.98	-	550,373.00
Long-term liabilities (Notes 8 and 21)	126,803,130.59	-	1,490,847.00
Due to grantors (Note 8)	7,448,171.34	-	-
Net OPEB obligation (Note 12)	11,708,566.60	-	-
Total noncurrent liabilities	155,781,907.04	-	2,041,220.00
Total liabilities	189,299,440.68	93,092.85	6,728,779.00
NET ASSETS			
Invested in capital assets, net of related debt	138,426,834.38	9,486.00	1,361,291.00
Restricted for:			
Nonexpendable:			
Scholarships and fellowships	-	43,568,746.74	-
Research	-	655,511.80	-
Instructional department uses	-	5,679,472.35	-
Other	-	8,185,000.20	-
Expendable:			
Scholarships and fellowships	375,253.50	3,253,982.82	-
Research	155,781.67	287,821.39	-
Instructional department uses	320,456.76	3,179,181.41	-
Loans	945,925.55	-	-
Capital projects	-	223,270.16	-
Debt service	2,904,086.61	-	-
Other	1,913,406.71	10,089,317.89	-
Unrestricted (Note 9)	78,269,474.23	880,872.01	17,996,789.00
Total net assets	$ 223,311,219.41	$ 76,012,662.77	$ 19,358,080.00

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

TENNESSEE BOARD OF REGENTS
EAST TENNESSEE STATE UNIVERSITY
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
FOR THE YEAR ENDED JUNE 30, 2012

		Component Units	
	East Tennessee State University	East Tennessee State University Foundation	Medical Education Assistance Corporation
REVENUES			
Operating revenues:			
Student tuition and fees (net of scholarship allowances of $41,268,258.38)	$ 80,653,509.64	$ -	$ -
Gifts and contributions	-	2,917,501.81	-
Governmental grants and contracts	32,821,942.48	-	-
Nongovernmental grants and contracts	6,090,109.21	-	-
Sales and services of educational departments	22,627,947.89	-	-
Sales and services of other activities	5,742,887.34	-	-
Patient charges	-	-	37,366,586.00
Auxiliary enterprises:			
Residential life (net of scholarship allowances of $207,580.07; all residential life revenues are used as security for revenue bonds; see Note 8)	14,653,367.55	-	-
Bookstore	250,929.68	-	-
Food service	649,045.01	-	-
Wellness facility (all revenues are used as security for revenue bonds; see Note 8)	1,299,265.88	-	-
Other auxiliaries	1,812,470.42	-	-
Interest earned on loans to students	176,798.35	-	-
Other operating revenues (foundation revenues include $574,034.03 from MEAC)	655,368.00	930,909.93	437,193.00
Total operating revenues	167,433,641.45	3,848,411.74	37,803,779.00
EXPENSES			
Operating expenses (Note 16):			
Salaries and wages	153,014,999.57	-	22,780,074.00
Benefits	50,983,451.35	-	2,122,480.00
Utilities, supplies, and other services	60,830,160.51	2,663,115.36	10,103,661.00
Scholarships and fellowships	29,027,894.41	1,626,561.60	-
Depreciation expense	16,016,902.64	-	457,236.00
Payments to or on behalf of East Tennessee State University (Note 21)	-	1,041,824.38	-
Total operating expenses	309,873,408.48	5,331,501.34	35,463,451.00
Operating income (loss)	(142,439,767.03)	(1,483,089.60)	2,340,328.00
NONOPERATING REVENUES (EXPENSES)			
State appropriations	78,140,008.02	-	-
Gifts (university gifts include $994,839.57 from ETSU Foundation and $2,839,375.97 from MEAC)	4,385,241.06	-	-
Grants and contracts	55,493,780.00	-	1,721,250.00
Investment income (for the component units, net of investment expense of $93,505.00)	1,389,960.44	(598,136.07)	155,741.00
Interest on capital asset-related debt	(5,110,138.38)	-	(94,234.00)
Payments to or on behalf of East Tennessee State University or East Tennessee State University Foundation (Note 21)	-	-	(3,413,410.00)
Bond issuance costs	(21,713.96)	-	-
Other nonoperating revenues (expenses) (foundation amount includes $1,651,666.67 of capital gifts to the university)	474,316.71	(1,627,344.76)	5,700.00
Net nonoperating revenues (expenses)	134,751,453.89	(2,225,480.83)	(1,624,953.00)
Income (loss) before other revenues, expenses, gains, or losses	(7,688,313.14)	(3,708,570.43)	715,375.00
Capital appropriations	4,663,803.80	-	-
Capital gifts and grants (university gifts include $46,984.81 of payments from ETSU Foundation and $1,651,666.67 of gifts of capital assets)	6,074,428.62	46,590.21	-
Additions to permanent endowments	-	2,117,677.90	-
Total other revenues	10,738,232.42	2,164,268.11	-
Increase (decrease) in net assets	3,049,919.28	(1,544,302.32)	715,375.00
NET ASSETS			
Net assets - beginning of year	222,704,511.36	77,556,965.09	18,642,705.00
Prior-period adjustment (Note 17)	(2,443,211.23)	-	-
Net assets - end of year	$ 223,311,219.41	$ 76,012,662.77	$ 19,358,080.00

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

Exhibit C

TENNESSEE BOARD OF REGENTS
EAST TENNESSEE STATE UNIVERSITY
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2012

CASH FLOWS FROM OPERATING ACTIVITIES		
Tuition and fees	$	82,210,988.18
Grants and contracts		41,317,341.33
Sales and services of educational activities		22,367,153.66
Sales and services of other activities		5,749,044.06
Payments to suppliers and vendors		(60,227,557.75)
Payments to employees		(152,787,414.33)
Payments for benefits		(49,991,730.20)
Payments for scholarships and fellowships		(29,046,279.94)
Loans issued to students		(1,480,852.25)
Collection of loans from students		1,370,950.38
Interest earned on loans to students		138,107.83
Auxiliary enterprise charges:		
Residence halls		14,225,114.01
Bookstore		240,614.03
Food services		652,448.24
Wellness facility		1,299,265.88
Other auxiliaries		1,749,742.39
Other receipts		681,253.00
Net cash used by operating activities		(121,531,811.48)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State appropriations		77,980,748.37
Gifts and grants received for other than capital or endowment purposes		60,000,937.33
Federal student loan receipts		96,840,783.00
Federal student loan disbursements		(96,719,900.09)
Changes in deposits held for others		(100,890.96)
Other noncapital financing receipts		162,844.72
Net cash provided by noncapital financing activities		138,164,522.37
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from capital debt		8,695,324.02
Capital appropriations		4,663,803.80
Capital grants and gifts received		4,355,490.76
Purchases of capital assets and construction		(18,920,101.52)
Proceeds from sale of capital assets		381,000.00
Principal paid on capital debt		(9,126,368.85)
Interest paid on capital debt		(5,304,863.81)
Bond issue costs paid on new debt issue		(21,713.96)
Other capital and related financing receipts		178,628.39
Net cash used by capital and related financing activities		(15,098,801.17)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments		53,000,000.00
Income on investments		1,356,400.84
Purchases of investments		(63,005,794.92)
Net cash used by investing activities		(8,649,394.08)
Net decrease in cash		(7,115,484.36)
Cash - beginning of year		73,624,282.00
Cash - end of year	$	66,508,797.64

Exhibit C (cont.)

TENNESSEE BOARD OF REGENTS
EAST TENNESSEE STATE UNIVERSITY
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2012

Reconciliation of operating loss to net cash used by operating activities:		
Operating loss	$	(142,439,767.03)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation expense		16,016,902.64
Other adjustments		164,859.65
Change in assets and liabilities:		
Receivables, net		5,241,058.35
Inventories		74,296.72
Prepaid expenses and deferred charges		45,639.90
Other assets		(38,690.52)
Accounts payable		634,430.51
Accrued liabilities		154,602.74
Net OPEB obligation		682,451.84
Deferred revenue		(2,189,296.57)
Deposits		(27,305.89)
Compensated absences		233,023.05
Due to grantors		25,885.00
Loans to students		(109,901.87)
Net cash used by operating activities	$	(121,531,811.48)
Noncash investing, capital, or financing transactions		
Gifts of capital assets	$	1,718,937.86
Unrealized gains on investments	$	56,105.08
Loss on disposal of capital assets	$	(53,060.07)

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 East Tennessee State University.

The East Tennessee State University Foundation and the Medical Education Assistance Corporation are considered component units of the university. Although the university does not control the timing or amount of receipts from these organizations, the majority of resources, or income thereon, that these organizations hold and invest are restricted to the activities of the university by the donors. Because these restricted resources held by the foundation and the corporation can only be used by, or for the benefit of, the university, these organizations are considered component units of the university and are discretely presented in the university's financial statements. See Note 21 for more detailed information about the component units and how to obtain their reports.

Basis of Presentation

The university and its component units' 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.

Inventories

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

Compensated Absences

The university's employees accrue annual and sick leave at varying rates, depending on length of service or classification. Some employees also earn compensatory time. The amount of the liabilities for annual leave and compensatory time and their related benefits are reported in the statement of net assets. There is no liability for unpaid accumulated sick leave since the university's policy is to pay this only if the employee dies or is absent because of illness, injury, or related family death.

Capital Assets

Capital assets, which include property, plant, equipment, library holdings, and intangible assets, are reported in the statement of net assets at historical cost or at fair value at date of donation, less accumulated depreciation/amortization. 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 intangible assets 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 students' behalf. Certain governmental grants, such as Pell grants, and other federal, state, or nongovernmental programs are recorded as either operating or nonoperating revenues in the university's financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees and other student charges, the university has recorded a scholarship discount and allowance.

NOTE 2. CASH

This classification includes demand deposits and petty cash on hand. At June 30, 2012, cash consists of $4,314,593.27 in bank accounts, $41,000.00 of petty cash on hand, $52,104,187.81 in the State of Tennessee Local Government Investment Pool (LGIP) administered by the State Treasurer, $10,040,316.56 in LGIP deposits for capital projects, and $8,700.00 held by the State Treasurer for the benefit of the university.

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

The LGIP is part of the State Pooled Investment Fund. The fund's required risk disclosures are presented in the *State of Tennessee Treasurer's Report*. That report is available on the state's website at www.treasury.tn.gov.

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* (as amended), are reported at fair value, including those with a maturity date of one year or less at the time of purchase.

As of June 30, 2012, the university had the following investments and maturities.

		Investment Maturities (in Years)	
Investment Type	Fair Value	Less than 1	1 to 5
U. S. agency obligations	$53,173,080.00	$2,013,940.00	$51,159,140.00

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. 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. Prime banker's acceptances are required to be eligible for purchase by the Federal Reserve System. To be eligible, the original maturity must not be more than 270 days, and it must 1) arise out of the current shipment of goods between countries or with the United States, or 2) arise out of storage within the United States of goods under contract of sale or expected to move into the channel of trade within a reasonable time and that are secured throughout their life by a warehouse receipt or similar document conveying title to the underlying goods.

The policy requires that prime commercial paper shall be limited to that of corporations that meet the following criteria: 1) Senior long-term debt, if any, should have a minimum rating of A1 or equivalent, and short-term debt should have 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 rating must be A1 by all rating services (minimum of two). 2) The rating should be based on the merits of the issuer or guarantee by a nonbank. 3) A financial review should be made to ascertain the issuer's financial strength to cover the debt. 4) Commercial paper of a banking institution should not be purchased. Prime commercial paper shall not have a maturity that exceeds 270 days.

At June 30, 2012, the university's investments were rated as follows:

		Credit Quality Rating		
Investment Type	Fair Value	AAA	AA	Unrated
LGIP	$ 62,144,504.37	$ -	$ -	$62,144,504.37
U.S. agency obligations	53,173,080.00	6,063,300.00	47,109,780.00	-
Total	$115,317,584.37	$6,063,300.00	$47,109,780.00	$62,144,504.37

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of the university's investment in a single issuer. 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. The amount invested in any one bank shall not exceed 5% of total investments on 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
	June 30, 2012
Federal Home Loan Bank (FHLB) obligations	25%
Federal National Mortgage Association (FNMA) obligations	34%
Federal Home Loan Mortgage Corporation (FHLMC) obligations	41%

NOTE 4. RECEIVABLES

Receivables included the following:

	June 30, 2012
Student accounts receivable	$5,731,172.78
Grants receivable	7,305,144.57
Notes receivable	166,870.56
Other receivables	5,526,539.16

Subtotal	18,729,727.07
Less allowance for doubtful accounts	2,937,607.71
Total receivables	$15,792,119.36

Federal Perkins Loan Program funds included the following:

	June 30, 2012
Perkins Loans receivable	$7,941,039.71
Less allowance for doubtful accounts	1,789,212.76
Total	$6,151,826.95

NOTE 5. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2012, was as follows:

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$ 15,761,006.80	$ 692,356.38	$ -	$ 2,593.11	$ 16,450,770.07
Land improvements and infrastructure	35,952,288.62	-	1,564,184.23	-	37,516,472.85
Buildings	313,520,964.16	966,666.67	16,902,714.47	-	331,390,345.30
Equipment	32,612,940.42	2,669,552.12	-	1,240,831.35	34,041,661.19
Library holdings	8,997,527.91	132,655.18	-	7,365,042.47	1,765,140.62
Intangible assets	4,433,400.78	-	-	-	4,433,400.78
Projects in progress	15,381,456.33	16,156,169.11	(18,466,898.70)	-	13,070,726.74
Total	426,659,585.02	20,617,399.46	-	8,608,466.93	438,668,517.55
Less accum. depreciation/amortization:					
Land improvements and infrastructure	14,651,395.42	1,743,880.24	-	-	16,395,275.66
Buildings	118,350,067.70	9,103,594.03	-	-	127,453,661.73
Equipment	20,785,674.84	2,221,545.25	-	1,187,771.28	21,819,448.81
Library holdings	5,876,264.86	2,527,061.11	-	7,365,042.47	1,038,283.50
Intangible assets	2,212,434.84	420,822.01	-	-	2,633,256.85

Total	161,875,837.66	16,016,902.64	-	8,552,813.75	169,339,926.55
Capital assets, net	$264,783,747.36	$ 4,600,496.82	$ -	$ 55,653.18	$269,328,591.00

The increase in accumulated depreciation for library holdings is due to a change in accounting estimate. During fiscal year 2012, it was determined that periodicals are more appropriately expensed. The estimated useful life of periodicals was decreased from 10 years to 0 years, resulting in a current-year adjustment of $2,348,266.63.

NOTE 6. CAPITAL LEASES

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

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

The university's leasing of the Basic Science Building and the other buildings on the VA campus will constitute a capital lease agreement. The lease term is substantially equal to the estimated useful life of the leased property. Accordingly, the university has capitalized the cost of the buildings at $52,853,604.57. At June 30, 2012, the buildings are reported at $38,021,227.30, net of accumulated depreciation of $14,832,377.27.

NOTE 7. ACCOUNTS PAYABLE

Accounts payable included the following:

	June 30, 2012
Vendors payable	$3,782,742.63
Unapplied student payments	5,406.61
Other payables	248,095.10
Total accounts payable	$4,036,244.34

NOTE 8. LONG-TERM LIABILITIES

Long-term liabilities activity for the year ended June 30, 2012, was as follows:

	Beginning Balance, as Restated	Additions	Reductions	Ending Balance	Current Portion
Payables:					
Loan	$ 1,237,945.80	$ -	$ 1,237,945.80	$ -	$ -
TSSBA debt:					
Bonds	109,150,693.33	-	4,045,095.84	105,105,597.49	4,098,626.03
Unamortized bond premium/discount	2,443,211.23	-	148,523.71	2,294,687.52	-
Commercial paper	18,649,474.80	8,695,324.02	3,843,327.21	23,501,471.61	-
Subtotal	131,481,325.16	8,695,324.02	9,274,892.56	130,901,756.62	4,098,626.03
Other liabilities:					
Deferred revenue	16,760,201.15	12,110,238.61	14,136,690.46	14,733,749.30	12,208,313.77
Compensated absences	10,005,813.44	5,885,815.22	5,652,792.17	10,238,836.49	2,942,233.51
Due to grantors	7,422,286.34	25,885.00	-	7,448,171.34	-
Subtotal	34,188,300.93	18,021,938.83	19,789,482.63	32,420,757.13	15,150,547.28
Total long-term liabilities	$165,669,626.09	$26,717,262.85	$29,064,375.19	$163,322,513.75	$19,249,173.31

Loan Payable

The Tennessee General Assembly earmarked in Section 41, Item 41, of Chapter 563 of the Public Acts of 1989 the amount of $3,000,000 from the funds appropriated in Section 1, Title 111-25, of Chapter 563 of the Public Acts of 1989 for the East Tennessee State University Clinical Education Facility. These funds were intended to be an interest-bearing loan from the General Fund to the Tennessee Board of Regents on behalf of East Tennessee State University. The loan had an interest rate of 7.15%, a principal amount of $3,000,000.00, a minimum annual debt service of $260,919.72, and a due date of January 1, 2017. The balance owed by the university was paid off on February 28, 2012.

TSSBA Debt - Bonds

Bonds, with interest rates ranging from 2.0% to 5.0%, were issued by the Tennessee State School Bond Authority (TSSBA). The bonds are due serially until 2039 and are secured by pledges of the facilities' revenues to which they relate and certain other revenues and fees of the university, including state appropriations; 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 $4,228,545.00 at June 30, 2012.

Debt service requirements to maturity for the university's portion of TSSBA bonds at June 30, 2012, are as follows:

Year Ending June 30	Principal	Interest	Total
2013	$ 4,098,626.03	$ 5,043,169.14	$ 9,141,795.17
2014	4,270,445.95	4,859,498.80	9,129,944.75
2015	4,412,992.62	4,695,971.91	9,108,964.53
2016	4,349,850.68	4,515,167.24	8,865,017.92
2017	4,558,550.26	4,315,038.32	8,873,588.58
2018-2022	25,722,384.35	18,374,188.67	44,096,573.02
2023-2027	25,795,246.28	12,175,331.54	37,970,577.82
2028-2032	15,603,598.33	6,850,048.83	22,453,647.16
2033-2037	14,259,551.07	3,088,604.34	17,348,155.41
2038-2039	2,034,351.92	300,250.02	2,334,601.94

Total	$105,105,597.49	$64,217,268.81	$169,322,866.30

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 $23,501,471.61 at June 30, 2012.

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 www.comptroller.tn.gov/tssba/cafr.asp.

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, 2012
Working capital	$ 7,267,014.72
Encumbrances	1,602,667.42
Designated fees	4,631,024.95
Auxiliaries	1,419,348.66
Quasi-endowment	18,962,069.27
Plant construction	19,005,061.70
Renewal and replacement of equipment	23,575,752.50
Debt retirement	1,036,726.47

Undesignated	769,808.54
Total	$78,269,474.23

NOTE 10. PLEDGED REVENUES

The university has pledged certain revenues and fees, including state appropriations, to repay $105,105,597.49 in revenue bonds issued from March 25, 2004, to September 15, 2010. Proceeds from the bonds provided financing for construction and renovation projects. The bonds are payable through 2039. Annual principal and interest payments on the bonds are expected to require 3.55% of available revenues. The total principal and interest remaining to be paid on the bonds is $169,322,866.30. Principal and interest paid for the current year and total available revenues were $9,052,979.05 and $254,955,639.92, respectively.

NOTE 11. PENSION PLANS

A. Defined Benefit Plan

Tennessee Consolidated Retirement System

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

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

Funding Policy - Plan members are noncontributory. The university is required to contribute an actuarially determined rate. The current rate is 14.91% 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, 2012, 2011, and 2010, were $7,674,153.32, $7,186,330.71, and $6,074,138.11, respectively. 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 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 contributions made by the university to the plans were $7,998,091.16 for the year ended June 30, 2012, and $7,834,914.78 for the year ended June 30, 2011. 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 available to higher education employees—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 8-27-101, *Tennessee Code Annotated.* Prior to reaching age 65, all members have the option of choosing between the standard or partnership preferred provider organization (PPO) plan for healthcare benefits. Subsequent to age 65, members who are also in the state's retirement system may participate in a state-administered Medicare supplement that does not include pharmacy. The state makes on-behalf payments to the Medicare supplement plan for the university's eligible retirees; see Note 20. The plans are reported in the State of Tennessee's *Comprehensive Annual Financial Report* (CAFR). The CAFR is available on the state's website at http://tn.gov/finance/act/cafr.shtml.

Special Funding Situation

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

Funding Policy

The premium requirements of members of the State Employee Group Plan are established and may be amended by the insurance committee. The plan is self-insured and financed on a pay-as-you-go basis with the risk shared equally among the participants. Claims liabilities of the plan are periodically computed using actuarial and statistical techniques to establish premium rates. Administrative costs of the plan are allocated to plan participants. In accordance with Section 8-27-205(b), *Tennessee Code Annotated*, 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 are subsidized 80%; retirees with 20 years of service but less than 30 years of service, 70%; and retirees with less than 20 years of service, 60%.

Retirees in the Medicare Supplement Plan have flat-rate premium subsidies based on years of service. Retirees with 30 years of service receive $50 per month; retirees with 20 years of service but less than 30 years of service, $37.50; and retirees with 15 years of service but less than 20 years of service, $25.

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

Annual required contribution (ARC)	$ 3,449,000.00
Interest on the net OPEB obligation	441,044.59
Adjustment to the ARC	(468,160.44)
Annual OPEB cost	3,421,884.15
Amount of contribution	(2,739,432.31)
Increase in net OPEB obligation	682,451.84
Net OPEB obligation – beginning of year	11,026,114.76
Net OPEB obligation – end of year	$11,708,566.60

Year-end	Plan	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation at Year-end
June 30, 2012	State Employee Group Plan	$3,421,884.15	80.1%	$11,708,566.60
June 30, 2011	State Employee Group Plan	$4,092,091.82	57.8%	$11,026,114.76
June 30, 2010	State Employee Group Plan	$4,501,871.50	41.8%	$9,297,631.48

Funded Status and Funding Progress

The funded status of the university's portion of the State Employee Group Plan as of July 1, 2011, was as follows:

Actuarial valuation date	July 1, 2011
Actuarial accrued liability (AAL)	$28,137,000.00
Actuarial value of plan assets	-
Unfunded actuarial accrued liability (UAAL)	$28,137,000.00
Actuarial value of assets as a percentage of the AAL	0%
Covered payroll (active plan members)	$100,388,162.00
UAAL as percentage of covered payroll	28.0%

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, 2011, actuarial valuation, the Projected Unit Credit actuarial cost method was used. The actuarial assumptions included a 4 percent investment rate of return (net of administrative expenses) and an annual healthcare cost trend rate of 9.25 percent in fiscal year 2012. The rate decreases to 8.75 percent in fiscal year 2013, and then reduces by decrements to an ultimate rate of 5 percent in fiscal year 2021. All rates include a 2.5 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. CHAIRS OF EXCELLENCE

The university had $22,293,300.04 on deposit at June 30, 2012, with the State Treasurer for its Chairs of Excellence program. These funds are held in trust by the state and are not included in these financial statements.

NOTE 14. INSURANCE-RELATED ACTIVITIES

It is the policy of the state not to purchase commercial insurance for the risks associated with casualty losses for general liability, automobile liability, professional medical 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, builder's risk (for construction projects starting prior to July 1, 2012) and crime and fidelity coverage on the state's officials and employees. The contractor is responsible for acquiring builder's risk insurance for all construction projects after June 30, 2012; thus, builder's risk is no longer covered by the Risk Management Fund. For property coverage, the deductible for an individual state agency is the first $25,000 of losses. The Risk Management Fund is responsible for property losses for the annual aggregate deductible of $10 million for perils other than earthquakes and flood. Purchased insurance coverage is responsible for losses exceeding the $10 million annual aggregate deductible. For earthquake and flood, there is a deductible of $10 million per occurrence. The maximum insurance coverage is $750 million per year for perils other than earthquake and flood. The maximum flood insurance coverage is $50 million per occurrence, except there is only $25 million of coverage in flood zones A and V. The maximum earthquake insurance coverage is $50 million per occurrence. The amounts of settlements have not exceeded insurance coverage for each of the three past fiscal years.

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 year ended June 30, 2012, are presented in the *Tennessee Comprehensive Annual Financial Report*. The CAFR is available on the state's website at www.tn.gov/finance/act/cafr.shtml. 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, 2012, the Risk Management Fund held $97.2 million in cash and cash equivalents designated for payment of claims.

At June 30, 2012, the scheduled coverage for the university was $861,883,200 for buildings and $171,662,300 for contents.

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

NOTE 15. COMMITMENTS AND CONTINGENCIES

Sick Leave

The university records the cost of sick leave when paid. The dollar amount of unused sick leave was $51,899,698.14 at June 30, 2012.

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 $480,298.12 for the year ended June 30, 2012. All operating leases are cancelable at the lessee's option.

Construction in Progress

At June 30, 2012, outstanding commitments under construction contracts totaled $19,994,002.59 for housing renovations, a baseball stadium, the College of Medicine Student Center, a new parking garage, and various other projects, of which $2,626,637.47 will be funded by future state capital outlay appropriations.

Litigation

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

NOTE 16. NATURAL CLASSIFICATIONS WITH FUNCTIONAL CLASSIFICATIONS

The university's operating expenses for the year ended June 30, 2012, are as follows:

	Natural Classification					
Functional Classification	Salaries	Benefits	Other Operating	Scholarships	Depreciation	Total
Instruction	$ 91,253,620.60	$27,945,638.27	$15,668,086.36	$2,351,301.05	$ -	$137,218,646.28
Research	5,871,959.06	196,261.16	4,358,499.49	115,449.21	-	10,542,168.92
Public service	11,675,468.68	4,720,314.19	5,605,104.61	107,317.15	-	22,108,204.63
Academic support	14,876,186.34	5,796,235.11	4,497,144.73	353,221.69	-	25,522,787.87
Student services	9,663,500.22	3,446,061.14	5,148,953.83	2,166,083.69	-	20,424,598.88
Institutional support	12,018,172.84	4,904,694.10	1,967,551.19	134,681.74	-	19,025,099.87
Operation & maintenance of plant	5,839,658.03	3,415,062.84	15,949,429.25	-	-	25,204,150.12
Scholarships & fellowships	-	-	385,792.00	23,590,267.75	-	23,976,059.75
Auxiliary	1,816,433.80	559,184.54	7,249,599.05	209,572.13	-	9,834,789.52
Depreciation	-	-	-	-	16,016,902.64	16,016,902.64
Total	$153,014,999.57	$50,983,451.35	$60,830,160.51	$29,027,894.41	$16,016,902.64	$309,873,408.48

NOTE 17. PRIOR-PERIOD ADJUSTMENT

In the year ended June 30, 2012, the university began amortizing TSSBA bond premiums and discounts greater than $100,000 over the life of the bonds. Prior issuances were reviewed for materiality. The university identified 11 projects with bond premiums exceeding the $100,000 threshold. Unamortized premiums of $2,443,211.23 at June 30, 2011, were recorded. As a result, net assets invested in capital assets, net of related debt, was reduced by $2,443,211.23 at June 30, 2011.

NOTE 18. AFFILIATED ENTITY NOT INCLUDED

The East Tennessee State University Research Foundation is a private, nonprofit foundation with the university as the sole beneficiary. The Research Foundation is controlled by a board independent of the university. The financial records, investments, and other financial transactions are handled external to the university and these amounts are not included in the university's financial report. As reported in the most recently audited financial report, at June 30, 2012, the assets of the Research Foundation totaled $2,493,530.98, liabilities were $365,369.43, and the net assets amounted to $2,128,161.55.

NOTE 19. INSURANCE RECOVERIES

The university sustained damage to the VA Building 35 Theater during a tornado on April 9, 2011. The impairment of the asset was temporary, and no impairment loss was recognized. An insurance recovery for the damage in the amount of $177,503.39 was received in fiscal year 2012. The insurance recovery is classified as other nonoperating revenue in the statement of revenues, expenses, and changes in net assets.

NOTE 20. ON-BEHALF PAYMENTS

During the year ended June 30, 2012, the State of Tennessee made payments of $164,859.65 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.shtml.

NOTE 21. COMPONENT UNITS

EAST TENNESSEE STATE UNIVERSITY FOUNDATION

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

During the year ended June 30, 2012, the foundation made distributions of $1,041,824.38 to or on behalf of the university for both restricted and unrestricted purposes. Complete financial statements for the foundation can be obtained from Dr. David D. Collins, Vice President for Finance and Administration, P.O. Box 70601, Johnson City, TN 37614.

Cash and Cash Equivalents

In addition to demand deposits and petty cash on hand, this classification includes instruments which are readily convertible to known amounts of cash and which have original maturities of three months or less. At June 30, 2012, cash and cash equivalents consisted of $133,443.29 in bank accounts, $4,487,583.49 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer, and $768,189.10 in cash held by others.

The Local Government Investment Pool is part of the Pooled Investment Fund. The fund's required risks disclosures are presented in the *State of Tennessee's Treasurer's Report.* That report is available on the state's website at www.treasury.tn.gov.

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, 2012, 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
Corporate bonds	$ 4,018,628.38	$1,050,054.38	$2,968,574.00	$ -	$ -	$ -
Bond mutual funds	17,532,265.61	1,706,286.52	3,745,901.40	3,950,727.42	8,129,350.27	-
Equity mutual funds	47,791,145.50	-	-	-	-	47,791,145.50
Total	$69,342,039.49	$2,756,340.90	$6,714,475.40	$3,950,727.42	$8,129,350.27	$47,791,145.50

Interest rate risk - Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of a debt investment. In order to reduce its exposure to interest rate risk, the foundation will set limits regarding the weighted average maturity for each direct investment pool. In the case of federal securities, the weighted average of all investments should be less than three years.

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

At June 30, 2012, the foundation's investments were rated as follows:

			Credit Quality Rating			
Investment Type	Fair Value	AAA	AA	A	BBB or Less	Unrated
LGIP	$ 4,487,583.49	$ -	$ -	$ -	$ -	$4,487,583.49
Corporate bonds	4,018,628.38	-	-	4,018,628.38	-	-
Bond mutual funds	17,532,265.61	11,749,962.22	1,158,222.12	2,516,310.51	2,107,770.76	-
Total	$26,038,477.48	$11,749,962.22	$1,158,222.12	$6,534,938.89	$2,107,770.76	$4,487,583.49

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

	June 30, 2012
Cash held by others	$ 768,189.10
Corporate bonds	4,018,628.38
Mutual funds	54,057,426.38
	$58,844,243.86

Assets of endowment funds are pooled on a fair value basis, with each individual fund subscribing to or disposing of units on the basis of the fair value per unit at the beginning of the calendar quarter within which the transaction takes place. The units at June 30, 2012, had a fair value of $1.0952771929 each. A total of 53,844,321.79 units were owned by endowments, and 724,355.93 units were owned by quasi-endowments.

The following tabulation summarizes changes in relationships between cost and fair values of the pooled assets:

FY 2012

	Pooled Assets		Net Gains	Fair Value
	Fair Value	Cost	(Losses)	Per Unit
End of year	$69,342,039.49	$68,722,577.97	$ 619,461.52	$1.0952771929
Beginning of year	$69,995,009.50	$66,052,783.03	3,942,226.47	$1.0877576324
Unrealized net losses			(3,322,764.95)	
Realized net gains			952,038.95	
Total net losses			($2,370,726.00)	

The average annual earnings per unit, exclusive of net gains, were $.026 for the year ended June 30, 2012.

Pledges Receivable

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

	June 30, 2012
Current pledges	$ 310,939.60
Pledges due in one to five years	756,568.02
Subtotal	1,067,507.62
Less discounts to net present value	(24,879.62)
Total pledges receivable, net	$1,042,628.00

Capital Assets

Capital asset activity for the year ended June 30, 2012, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance
Land	$ 685,000.00	$ -	$ 685,000.00	$ -
Buildings	1,059,000.00	-	1,000,000.00	59,000.00
Equipment	9,486.00	-	-	9,486.00
Total	1,753,486.00	-	1,685,000.00	68,486.00
Less accum. depreciation:				
Buildings	92,333.33	-	33,333.33	59,000.00
Total accum. depreciation	92,333.33	-	33,333.33	59,000.00
Capital assets, net	$1,661,152.67	$ -	$1,651,666.67	$ 9,486.00

Endowments

The ETSU Foundation's endowment consists of 472 individual funds established for a variety of purposes. Its endowment includes both donor-restricted endowment funds and funds designated by the board of directors to function as endowments. As required by GAAP, net assets associated with endowment funds, including funds designated by the board of directors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

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

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

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

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

Spending policy and how the investment objectives relate - The foundation has a policy of appropriating for distribution each year 2 to 4 percent of the average quarterly balance for the three preceding calendar years depending on the amount of reserve for each endowment. In establishing this policy, the foundation considered the long-term expected return on its endowment. Accordingly, over the long-term, the foundation expects the current spending policy to allow its endowment to grow at an average of 3 percent annually. This is consistent with the foundation's objective to 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, 2012, net appreciation of $8,845,751.33 is available to be spent, of which $4,770,943.94 is included in restricted net assets expendable for scholarships and fellowships, $72,608.20 is included in restricted net assets expendable for research, $581,886.72 is included in restricted net assets expendable for instructional departmental uses, and $3,420,312.47 is included in restricted net assets expendable for other purposes.

MEDICAL EDUCATION ASSISTANCE CORPORATION

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

During the year ended June 30, 2012, MEAC made distributions of $3,413,410, to or on behalf of ETSU or the ETSU Foundation for both restricted and unrestricted purposes. Complete financial statements for MEAC can be obtained from Russell Lewis, Executive Director, P.O. Box 699, Mountain Home, TN 37684.

Cash

At June 30, 2012, cash consisted of $5,931,760 in bank accounts, $2,500 of petty cash on hand, and $84,618 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer.

The Local Government Investment Pool is part of the Pooled Investment Fund. The fund's required risks disclosures are presented in the *State of Tennessee's Treasurer's Report.* That report is available on the state's website at www.treasury.tn.gov.

Investments

The corporation is authorized to invest funds in accordance with its board of directors' policies. The corporation's investments at June 30, 2012, consisted of certificates of deposit with original maturities greater than three months.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. MEAC has no investment policy limiting its investment choices based on ratings issued by nationally recognized statistical rating organizations. At June 30, 2012, MEAC had no rated investments, as deposits in LGIP are unrated.

Capital Assets

Capital asset activity for the year ended June 30, 2012, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance
Land	$ 18,150	$ -	$ -	$ 18,150
Leasehold improvements	536,225	108,946	-	645,171
Buildings	1,933,483	26,750	-	1,960,233
Equipment	3,885,048	150,077	42,166	3,992,959
Total	6,372,906	285,773	42,166	6,616,513
Less accumulated depreciation:				
Leasehold improvements	341,298	47,260	-	388,558
Buildings	211,121	52,275	-	263,396
Equipment	2,759,880	357,701	42,166	3,075,415
Total accumulated depreciation	3,312,299	457,236	42,166	3,727,369
Capital assets, net	$3,060,607	$(171,463)	$ -	$2,889,144

Long-term Liabilities

Long-term liabilities activity for the year ended June 30, 2012, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Note payable	$1,563,878	$ -	$36,025	$1,527,853	$ 37,006
Compensated absences	638,404	49,562	-	687,966	137,593
Total long-term liabilities	$2,202,282	$49,562	$36,025	$2,215,819	$174,599

Note Payable

MEAC borrowed funds in 2007 to purchase medical office space located in Kingsport, Tennessee. The original note was refinanced through a note modification agreement in 2011 to take advantage of the current interest rate environment. The note bears a fixed interest rate of 5.99% for five years. The payment is due in full on January 28, 2016. The balance owed was $1,527,853 at June 30, 2012.

Debt service requirements associated with the note payable are as follows:

Year Ending June 30	Principal	Interest	Total
2013	$ 37,006	$ 93,254	$ 130,260
2014	39,093	91,167	130,260
2015	41,583	88,677	130,260
2016	1,410,171	46,798	1,456,969
Total	$1,527,853	$319,896	$1,847,749

Tennessee Board of Regents
East 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, 2011	State Employee Group Plan	$ -	$28,137,000.00	$28,137,000.00	0%	$100,388,162.00	28.0%
July 1, 2010	State Employee Group Plan	$ -	$39,835,000.00	$39,835,000.00	0%	$99,072,828.00	40.2%
July 1, 2009	State Employee Group Plan	$ -	$44,411,000.00	$44,411,000.00	0%	$97,727,873.00	45.5%

The amount reported here for covered payroll relates to the fiscal year in which the valuations were performed.

TENNESSEE BOARD OF REGENTS
EAST TENNESSEE STATE UNIVERSITY
SUPPLEMENTARY INFORMATION
SCHEDULE OF CASH FLOWS - EAST TENNESSEE STATE UNIVERSITY FOUNDATION
FOR THE YEAR ENDED JUNE 30, 2012

CASH FLOWS FROM OPERATING ACTIVITIES		
Gifts and contributions	$	2,629,140.12
Payments to suppliers and vendors		(2,196,095.26)
Payments for scholarships and fellowships		(1,626,561.60)
Payments to or on behalf of East Tennessee State University		(1,041,824.38)
Other receipts		930,909.93
Net cash used by operating activities		(1,304,431.19)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Private gifts for endowment purposes		2,117,677.90
Net cash provided by noncapital financing activities		2,117,677.90
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Capital grants and gifts received		46,590.21
Net cash provided by capital and related financing activities		46,590.21
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments		5,602,646.41
Income on investments		2,749,469.82
Purchases of investments		(8,306,939.93)
Net cash provided by investing activities		45,176.30
Net increase in cash and cash equivalents		905,013.22
Cash and cash equivalents - beginning of year		4,484,202.66
Cash and cash equivalents - end of year	$	5,389,215.88
Reconciliation of operating loss to net cash used by operating activities:		
Operating loss	$	(1,483,089.60)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Change in assets and liabilities:		
Receivables, net		140,847.90
Accounts payable		37,810.51
Net cash used by operating activities	$	(1,304,431.19)
Noncash investing, capital, or financing transactions		
Gifts of capital assets	$	12,930.00
Unrealized losses on investments	$	(3,322,764.95)
Transfer of capital asset to institution	$	(1,651,666.67)

TENNESSEE BOARD OF REGENTS
EAST TENNESSEE STATE UNIVERSITY
SUPPLEMENTARY INFORMATION
SCHEDULE OF CASH FLOWS - MEDICAL EDUCATION ASSISTANCE CORPORATION
FOR THE YEAR ENDED JUNE 30, 2012

CASH FLOWS FROM OPERATING ACTIVITIES	
Collections from patient charges	$ 35,513,681.00
Payments to suppliers and vendors	(8,301,462.00)
Payments to employees	(23,048,165.00)
Payments for benefits	(2,122,480.00)
Other receipts	586,796.00
Net cash provided by operating activities	2,628,370.00
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
Gifts and grants	1,721,250.00
Payments to or on behalf of East Tennessee State University or East Tennessee State University Foundation	(3,413,410.00)
Net cash used by noncapital financing activities	(1,692,160.00)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Proceeds from sale of capital assets	900.00
Purchase of capital assets and construction	(285,773.00)
Principal paid on capital debt	(36,026.00)
Interest paid on capital debt	(94,234.00)
Net cash used by capital and related financing activities	(415,133.00)
CASH FLOWS FROM INVESTING ACTIVITIES	
Income on investments	155,741.00
Proceeds from sales and maturities of investments	4,285,019.00
Purchases of investments	(4,347,233.00)
Other investing receipts	4,800.00
Net cash provided by investing activities	98,327.00
Net increase in cash	619,404.00
Cash - beginning of year	5,399,474.00
Cash - end of year	$ 6,018,878.00
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	$ 2,340,328.00
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation expense	457,236.00
Bad debt expense	2,083,805.00
Change in assets and liabilities:	
Receivables, net	(2,065,636.00)
Prepaid expenses and deferred charges	(156,124.00)
Accounts payable	(178,733.00)
Accrued liabilities	(264,403.00)
Compensated absences	49,563.00
Deposits held in custody for others	(3,143.00)
Other liabilities	365,477.00
Net cash provided by operating activities	$ 2,628,370.00