AUDIT REPORT

Tennessee Board of Regents
East Tennessee State University

For the Year Ended
June 30, 2013

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

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December 30, 2013

The Honorable Bill Haslam, Governor
Members of the General Assembly
The Honorable John G. Morgan, Chancellor
Dr. Brian Noland, President

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, 2013. You will note from the independent auditor's report that unmodified opinions were given on the fairness of the presentation of the financial statements.

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

Sincerely,

Deborah V. Loveless

Deborah V. Loveless, CPA
Director

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Tennessee Board of Regents

East Tennessee State University

For the Year Ended June 30, 2013

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For the Year Ended June 30, 2013

Opinions on the Financial Statements

The opinions on the financial statements are unmodified.

Audit Findings

The audit report contains no findings.

STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
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Independent Auditor's Report

The Honorable Bill Haslam, Governor
Members of the General Assembly
The Honorable John G. Morgan, Chancellor
Dr. Brian Noland, President

Report on the Financial Statements

We have audited the accompanying 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, 2013, and the related notes to the financial statements, which collectively comprise the basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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. Those statements were audited by other auditors, whose reports have been furnished to us. Our opinion, insofar as it relates to the amounts included for these institutions, is based solely 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 *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, based on our audit and the reports of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of East Tennessee State University, and its discretely presented component units as of June 30, 2013, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended, in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

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, 2013, and the changes in financial position and cash flows thereof for the year then ended, in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

As discussed in Note 1, the university implemented GASB Statement 65, *Items Previously Reported as Assets and Liabilities*, during the year ended June 30, 2013. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 5 through 14 and the schedule of funding progress on page 43 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.

Supplementary Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the university's basic financial statements. The schedules of cash flows for both East Tennessee State University Foundation and the Medical Education Assistance Corporation on pages 44 and 45 are presented for purposes of additional analysis and are not a required part of the basic financial statements. Both the foundation's schedule of cash flows and the corporation's schedule of cash flows are the responsibility of the university's management and were derived from, and relate directly to, the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied 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 basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America by us and other auditors. In our opinion, based on our audit and the procedures performed as described above, the information is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 27, 2013, on our consideration of the university's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the university's internal control over financial reporting and compliance.

Deborah V. Loveless

Deborah V. Loveless, CPA
Director
November 27, 2013

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, 2013, with comparative information presented for the fiscal year ended June 30, 2012. 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 18 in the notes to the financial statements. This discussion and analysis focuses on the university and does not include the foundation or MEAC.

Overview of the Financial Statements

The financial statements have been prepared in accordance with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB), which establishes standards for external financial reporting for public colleges and universities. The financial statements are presented on a consolidated basis to focus on the university as a whole. The full scope of the university's activities is considered to be a single business-type activity and, accordingly, is reported within a single column in the basic financial statements.

The university's financial report includes the statement of net position; the statement of revenues, expenses, and changes in net position; and the statement of cash flows. Notes to the financial statements are also presented to provide additional information that is essential to a full understanding of the financial statements.

The Statement of Net Position

The statement of net position is a point-in-time financial statement. The statement of net position presents the financial position of the university at the end of the fiscal year. To aid the reader in determining the university's ability to meet immediate and future obligations, the statement includes all assets, liabilities, deferred outflows/inflows, and net position of the university and segregates the assets and liabilities into current and noncurrent components. Current assets are those that are available to satisfy current liabilities, inclusive of assets that will be converted to cash within one year. Current liabilities are those that will be paid within one year. The statement of net position is prepared under the accrual basis of accounting; assets and liabilities are recognized when goods or services are provided or received, despite when cash is actually exchanged.

From the data presented, readers of the statement are able to determine the assets available to continue the operations of the university. They are also able to determine how much the university owes vendors, lenders, and others. Net position represents the difference between the university's assets and liabilities, along with the difference between deferred outflows and deferred inflows of resources, and is one indicator of the university's current financial condition.

The statement of net position also indicates the availability of net position for expenditure by the university. Net position is divided into three major categories. The first category, net investment in capital assets, represents the university's total investment in property, plant, and equipment, net of outstanding debt obligations and deferred outflows/inflows of resources related to these capital assets. To the extent debt or deferred inflows of resources has been incurred but not yet expended for capital assets, such amounts are not included. The next category is restricted net position, which is sub-divided into two categories, nonexpendable and expendable. Nonexpendable restricted net position includes endowment and similar resources whose use is limited by donors or other outside sources and, as a condition of the gift, the principal is to be maintained in perpetuity. Expendable restricted net position is 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 resources. The final category is unrestricted net position. Unrestricted net position is available to the university for any lawful purpose of the university.

Summary of Net Position
(in thousands of dollars)

	2013	2012
Assets:		
Current assets	$ 37,767	$ 38,675
Capital assets, net	295,833	269,329
Other assets	105,145	104,606
Total assets	**438,745**	**412,610**
Deferred outflows of resources		
Deferred loss on debt refunding	410	-
Total deferred outflows	**410**	**-**
Liabilities:		
Current liabilities	35,723	33,517
Noncurrent liabilities	173,681	155,782
Total liabilities	**209,404**	**189,299**
Net position:		
Net investment in capital assets	148,244	138,427
Restricted – nonexpendable	-	-
Restricted – expendable	6,799	6,615
Unrestricted	74,708	78,269
Total net position	**$229,751**	**$223,311**

Comparison of Fiscal Year 2013 to Fiscal Year 2012

- Current assets, primarily in current cash, decreased from 2012 to 2013 due to a later start date and payment deadline for all summer terms.

- In 2013, other assets increased due to increases in Perkins Loan fund lending (noncurrent notes receivable).

- Capital assets, net of depreciation, increased from 2012 to 2013 due to the completion of the Johnson City Community Health Center, the renovation of Reece Museum, the renovation of student apartments, HVAC renovations, and the renovation of Brown Hall.

- In 2013, the Tennessee State School Bond Authority issued revenue bonds to advance refund two prior issues of debt, which resulted in a deferred loss of $445 thousand. The unamortized balance at June 30 was $410 thousand.

- Current liabilities increased from 2012 to 2013 due to increases in the current portion of long-term debt for capital improvements, increases in accrued salaries for summer school, and increases in unearned revenues resulting from the later start dates for summer term classes. These increases were offset with a decrease in accounts payable.

- In 2013, noncurrent liabilities increased due to increases in long-term debt for capital improvements and increases in the net OPEB obligation.

- Invested in capital assets increased in 2013 due to completion of the capital projects noted above.

- Unrestricted net position decreased from 2012 to 2013 due to decreases in net position from designated fees, primarily technology access fees, and decreases in net position for plant construction as many projects were completed.

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

The statement of revenues, expenses, and changes in net position presents the results of operations for the fiscal year. Revenues and expenses are recognized when earned or incurred, regardless of when cash is received. The statement indicates whether the university's financial condition has improved or deteriorated during the fiscal year. The statement presents the revenues received by the university, both operating and nonoperating; the expenses paid by the university, both operating and nonoperating; and any other revenues, expenses, gains, or losses received or spent by the university.

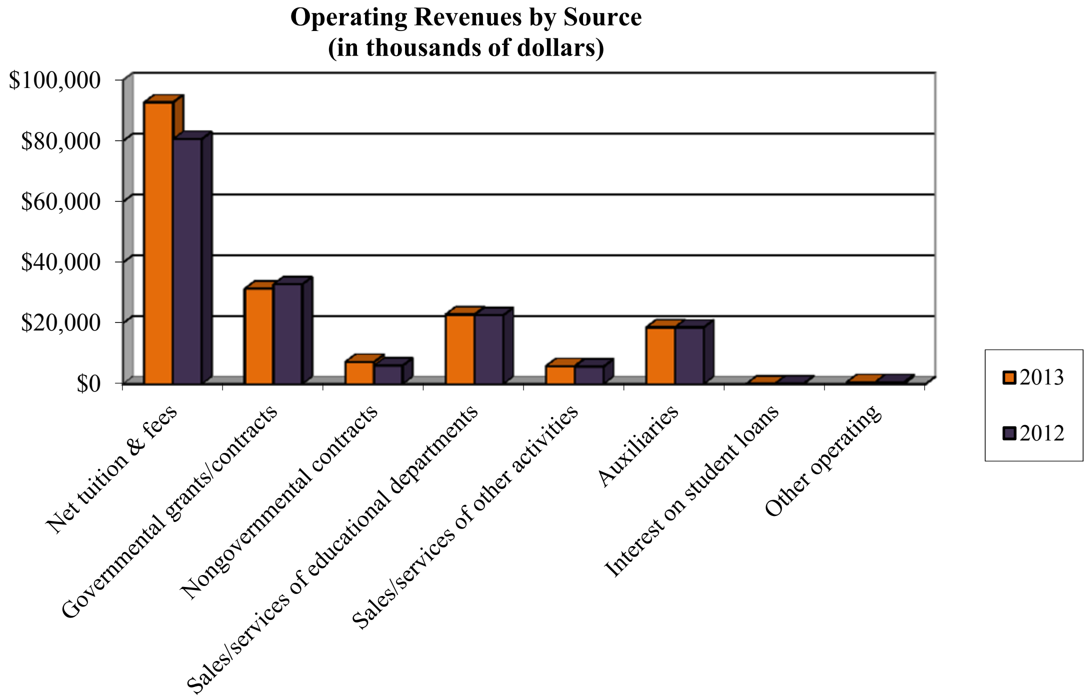
Generally speaking, operating revenues are received for providing goods and services to the various customers and constituencies of the university. Operating expenses are those expenses paid to acquire or produce the goods and services provided in return for the operating revenues, and to carry out the mission of the university. Nonoperating revenues are revenues received for which goods and services are not provided directly to the payor. Although the university is dependent upon state appropriations and gifts to fund educational and general operations, under GASB standards these funding sources are reported as nonoperating revenues, as is investment income. As a result, the university has historically reported an excess of operating expenses over operating revenues, resulting in an operating loss. Therefore, the "increase in net position" is more indicative of overall financial results for the year.

Summary of Revenues, Expenses, and Changes in Net Position
(in thousands of dollars)

	2013	2012
Operating revenues	$ 179,693	$ 167,434
Operating expenses	324,420	309,873
Operating loss	**(144,727)**	**(142,439)**
Nonoperating revenues and expenses	135,113	134,751
Income (loss) before other revenues, expenses, gains, or losses	(9,614)	(7,688)
Other revenues, expenses, gains, or losses	16,054	10,738
Increase in net position	**6,440**	**3,050**
Net position at beginning of year	223,311	222,704
Prior period adjustment	-	(2,443)
Net position at end of year	**$ 229,751**	**$ 223,311**

Operating Revenues

The following summarizes the operating revenues by source that were used to fund operating activities for the last two fiscal years:



Comparison of Fiscal Year 2013 to Fiscal Year 2012

- Tuition and fees increased in 2013 due to an average 8% fee increase and establishment or increases in student fees related to completion, learning support, specialized academic fees, and materials fees.

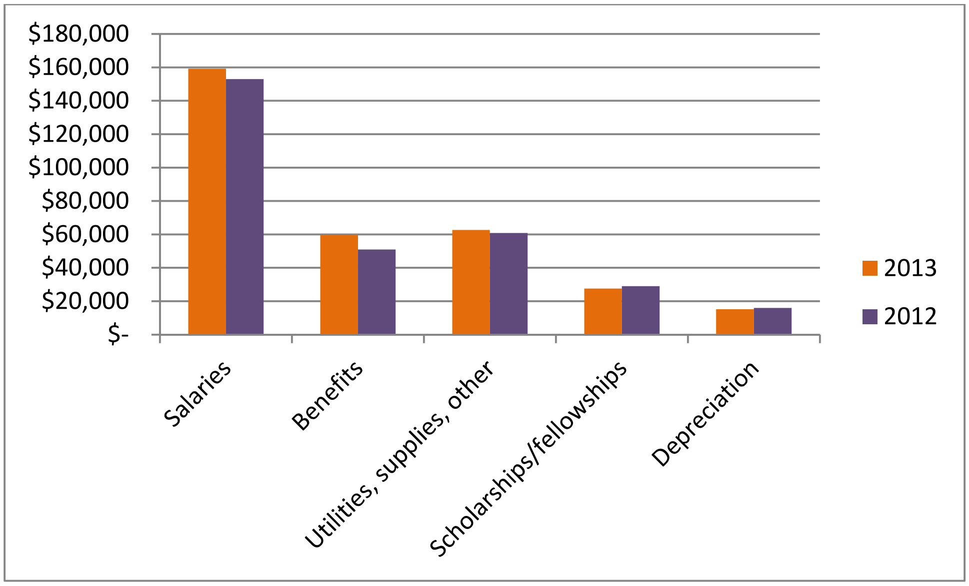
- Governmental grants and contracts decreased due to reductions in funding through federal and state grants and contracts.

- Other categories remained relatively unchanged.

Operating Expenses

Operating expenses may be reported by nature or function. The university has chosen to report the expenses in their natural classification on the statement of revenues, expenses, and changes in net position and has displayed the functional classification in the notes to the financial statements. The following summarizes the operating expenses by natural classifications for the last two fiscal years:

Operating Expenses – Natural Classification
(in thousands of dollars)



Comparison of Fiscal Year 2013 to Fiscal Year 2012

- Salaries increased due to a 3% across-the-board pay increase and an equity pay increase.
- Benefits increased based on the increase in salaries and the inclusion of graduate assistant fee waivers in the benefits expense category.
- Other operating expenses (utilities, supplies, and other services) increased with increases in professional and administrative services for renovation and construction projects.
- Scholarships and fellowships decreased slightly due to the exclusion of graduate assistant fee waivers from the scholarships expense category.
- Depreciation expense remained relatively unchanged.

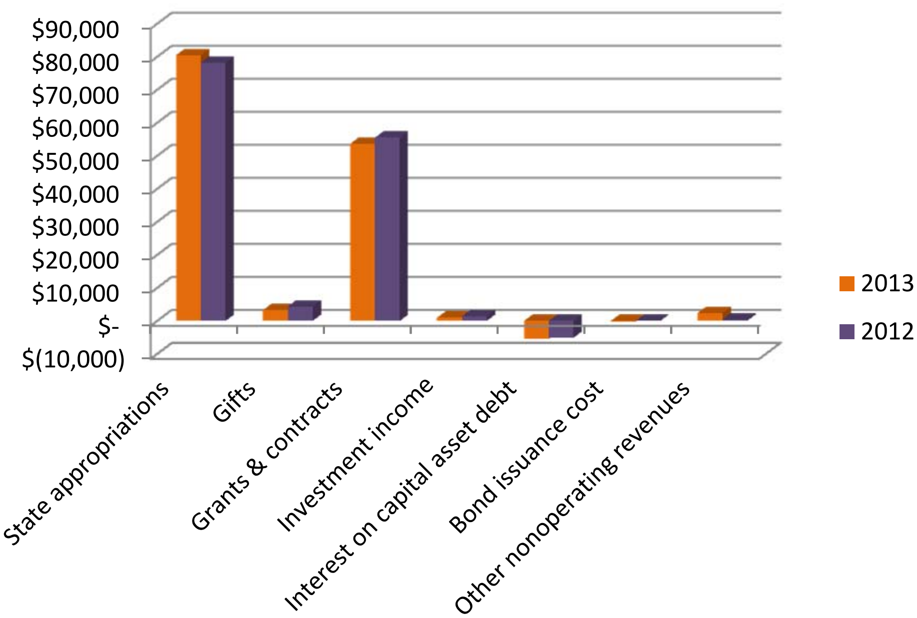
Nonoperating Revenues and Expenses

Certain revenue sources that the university relies on to provide funding for operations, including state noncapital appropriations, certain gifts and grants, and investment income, are defined by the GASB as nonoperating. Nonoperating expenses include capital financing costs and other costs related to capital assets. The following summarizes the university's nonoperating revenues and expenses for the last two fiscal years:

Nonoperating Revenues (Expenses)
(in thousands of dollars)

	2013	2012
State appropriations	$ 80,453	$ 78,140
Gifts	3,263	4,385
Grants and contracts	53,604	55,494
Investment income	970	1,390
Interest on capital asset-related debt	(5,368)	(5,110)
Bond issuance costs	(172)	(22)
Other nonoperating revenues (expenses)	2,363	474
Total nonoperating revenues (expenses)	**$ 135,113**	**$ 134,751**

Nonoperating Revenues/Expenses
(in thousands of dollars)



Comparison of Fiscal Year 2013 to Fiscal Year 2012

- State appropriations increased due to increases in funding from the state.
- Nonoperating gifts decreased due to the prior year gift from the Medical Education Assistance Corporation for the Clinical Education Building.
- Nonoperating grants and gifts decreased as a result of a reduction in revenues from the Tennessee Lottery scholarship and Pell grant funds.

- Investment income decreased due to decreases in interest rates for investments.

- Bond issuance costs increased due to new issues of bonds payable.

- Other nonoperating revenues (expenses) increased due to the income from an IRS refund for medical residents' FICA of $5.2 million and a related payment to the original grantors of $2.9 million, for a net revenue of $2.3 million.

Other Revenues

This category is composed of state appropriations for capital purposes and capital gifts and grants. These amounts were as follows for the last two fiscal years:

Other Revenues (Expenses)
(in thousands of dollars)

	2013	**2012**
Capital appropriations	$ 4,460	$ 4,664
Capital grants and gifts	11,594	6,074
Total other revenues	**$ 16,054**	**$ 10,738**

Comparison of Fiscal Year 2013 to Fiscal Year 2012

- Capital appropriations remained relatively constant from 2012 to 2013.

- Capital gifts and grants increased due to capital grants through the American Recovery and Reinvestment Act for the Johnson City Community Health Center, the College of Medicine Building 119 renovation, and the Brown Hall renovation.

Capital Assets and Debt Administration

Capital Assets

The university had $296 million invested in capital assets, net of accumulated depreciation of $183 million at June 30, 2013; and $269 million invested in capital assets, net of accumulated depreciation of $169 million at June 30, 2012. Depreciation charges totaled $15 and $16 million for the years ended June 30, 2013, and June 30, 2012, respectively.

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

	2013	2012
Land	$ 16,471	$ 16,451
Land improvements & infrastructure	26,190	21,121
Buildings	208,353	203,937
Equipment	14,343	12,222
Library holdings	618	727
Intangible assets	1,379	1,800
Projects in progress	28,479	13,071
Total	**$295,833**	**$269,329**

Significant additions to capital assets occurred in fiscal year 2013. These additions were from completion of tennis courts, a baseball facility, and the Johnson City Community Health Center; housing renovations; renovations to Brown Hall and Reece Museum; and HVAC projects.

At June 30, 2013, outstanding commitments under construction contracts totaled $16 million for various renovations and repairs of buildings and infrastructure. Future state capital outlay appropriations will fund $2.6 million of these costs.

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

Debt

The university had $148 and $131 million in Tennessee State School Bond Authority (TSSBA) debt outstanding at June 30, 2013, and June 30, 2012, respectively. The table below summarizes these amounts by type of debt instrument.

Schedule of Outstanding Debt
(in thousands of dollars)

	2013	2012
Commercial paper	$ 24,833	$ 23,501
Bonds	118,054	105,106
Unamortized bond premiums	5,112	2,295
Total	**$147,999**	**$130,902**

The university is responsible for the debt service of these bonds. The current portion of the $118 million of bonds outstanding at June 30, 2013, is $4.6 million.

The ratings on debt issued by the TSSBA at June 30, 2013, were as follows:

Fitch	AA+
Moody's Investor Service	Aa1
Standard & Poor's	AA

More information about the university's long-term liabilities is presented in Note 8 to the financial statements.

Economic Factors That Will Affect the Future

The economic outlook for the State of Tennessee has improved during fiscal year 2013. For the 2014 fiscal year, the state approved funding for a 1.5% across-the-board salary increase through appropriations and fees. For the first time in 10 years, the state provided increased appropriations for operating expenses other than salaries. 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 1.5% salary equity pool for university employees and board level technological enhancements for data. It is hoped the economy will continue to improve, resulting in increased, or at least more constant, appropriations for the future.

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 during the fiscal year.

Tennessee Board of Regents
EAST TENNESSEE STATE UNIVERSITY
Statement of Net Position
June 30, 2013

	East Tennessee State University	Component Units: East Tennessee State University Foundation	Component Units: Medical Education Assistance Corporation
ASSETS			
Current assets:			
Cash and cash equivalents (Notes 2, 3, and 18)	$ 20,635,365.37	$ 46,344.84	$ 5,190,884.00
Short-term investments (Note 18)	-	-	6,324,312.00
Accounts, notes, and grants receivable (net) (Notes 4 and 18)	15,018,465.96	-	4,034,581.00
Due from the university	-	-	105,982.00
Due from component units	688,881.08	-	-
Pledges receivable (net) (Note 18)	-	470.30	-
Inventories	300,498.37	-	-
Prepaid expenses	434,336.72	-	375,626.00
Accrued interest receivable	680,041.96	37,672.34	-
Other assets	9,691.70	-	-
Total current assets	37,767,281.16	84,487.48	16,031,385.00
Noncurrent assets:			
Cash and cash equivalents (Notes 2, 3, and 18)	45,570,589.70	3,547,356.79	-
Investments (Notes 3 and 18)	53,000,480.00	78,425,369.07	4,108,312.00
Accounts, notes, and grants receivable (net) (Notes 4 and 18)	6,573,122.50	-	-
Pledges receivable (net) (Note 18)	-	813,339.86	-
Capital assets (net) (Notes 5 and 18)	295,833,353.89	9,486.00	2,784,881.00
Other assets	-	306,363.89	2,427,360.00
Total noncurrent assets	400,977,546.09	83,101,915.61	9,320,553.00
Total assets	438,744,827.25	83,186,403.09	25,351,938.00
DEFERRED OUTFLOWS OF RESOURCES			
Deferred loss on debt refunding	410,088.26	-	-
Total deferred outflows of resources	410,088.26	-	-
LIABILITIES			
Current liabilities:			
Accounts payable (Note 7)	2,699,730.42	48,447.06	446,041.00
Accrued liabilities	6,601,985.95	-	2,518,341.00
Due to the university	-	358,547.08	330,334.00
Due to component units	105,982.00	-	-
Student deposits	562,555.11	-	-
Unearned revenue (Note 8)	15,328,006.49	-	-
Compensated absences (Notes 8 and 18)	3,057,970.76	-	153,666.00
Accrued interest payable	978,870.36	-	-
Long-term liabilities, current portion (Notes 8 and 18)	4,634,127.58	-	39,209.00
Deposits held in custody for others	1,753,371.77	-	454,893.00
Other liabilities	-	-	119,504.00
Total current liabilities	35,722,600.44	406,994.14	4,061,988.00
Noncurrent liabilities:			
Net OPEB obligation (Note 11)	12,602,678.28	-	-
Unearned revenue (Note 8)	2,427,360.69	-	-
Compensated absences (Notes 8 and 18)	7,819,839.29	-	614,662.00
Long-term liabilities (Notes 8 and 18)	143,364,874.74	-	1,449,569.00
Due to grantors (Note 8)	7,466,388.13	-	-
Total noncurrent liabilities	173,681,141.13	-	2,064,231.00
Total liabilities	209,403,741.57	406,994.14	6,126,219.00
NET POSITION			
Net investment in capital assets	148,244,439.83	9,486.00	1,296,103.00
Restricted for:			
Nonexpendable:			
Scholarships and fellowships	-	40,200,430.32	-
Research	-	606,342.14	-
Instructional department uses	-	5,526,163.39	-
Other	-	4,931,657.87	-
Expendable:			
Scholarships and fellowships	483,649.68	9,364,691.44	-
Research	239,913.48	446,746.59	-
Instructional department uses	255,585.03	3,886,260.62	-
Loans	664,380.80	-	-
Capital projects	-	1,411,587.70	-
Debt service	3,348,812.19	-	-
Other	1,806,645.71	15,221,656.36	-
Unrestricted	74,707,747.22	1,174,386.52	17,929,616.00
Total net position	$ 229,751,173.94	$ 82,779,408.95	$ 19,225,719.00

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

Tennessee Board of Regents
EAST TENNESSEE STATE UNIVERSITY
Statement of Revenues, Expenses, and Changes in Net Position
For the Year Ended June 30, 2013

	East Tennessee State University	Component Units: East Tennessee State University Foundation	Component Units: Medical Education Assistance Corporation
REVENUES			
Operating revenues:			
Student tuition and fees (net of scholarship allowances of $38,122,178.09)	$ 92,743,006.77	$ -	$ -
Gifts and contributions	-	3,094,992.06	-
Governmental grants and contracts	31,397,548.17	-	-
Nongovernmental grants and contracts	7,252,170.15	-	-
Sales and services of educational departments	22,915,640.35	-	-
Sales and services of other activities	5,946,041.14	-	-
Patient charges	-	-	34,446,412.00
Auxiliary enterprises:			
Residential life (net of scholarship allowances of $221,549.24; all residential life revenues are used as security for revenue bonds; see Note 8)	14,329,493.78	-	-
Bookstore	367,050.86	-	-
Food service	675,859.56	-	-
Wellness facility (all revenues are used as security for revenue bonds; see Note 8)	1,448,973.60	-	-
Other auxiliaries	1,867,113.11	-	-
Interest earned on loans to students	121,151.96	-	-
Other operating revenues (foundation revenues include $411,371.00 from MEAC)	628,737.69	1,262,714.39	508,411.00
Total operating revenues	179,692,787.14	4,357,706.45	34,954,823.00
EXPENSES			
Operating expenses (Note 15):			
Salaries and wages	159,245,924.98	-	22,651,246.00
Benefits	59,745,026.65	-	2,220,781.00
Utilities, supplies, and other services	62,659,403.96	2,930,079.32	7,863,622.00
Scholarships and fellowships	27,592,118.96	1,660,169.61	-
Depreciation expense	15,177,378.00	-	587,857.00
Payments to or on behalf of East Tennessee State University (Note 18)	-	1,516,794.67	-
Total operating expenses	324,419,852.55	6,107,043.60	33,323,506.00
Operating income (loss)	(144,727,065.41)	(1,749,337.15)	1,631,317.00
NONOPERATING REVENUES (EXPENSES)			
State appropriations	80,453,089.00	-	-
Gifts (university gifts include $1,123,195.36 from ETSU Foundation and $2,097,719.00 from MEAC)	3,263,348.73	-	-
Grants and contracts	53,603,975.75	-	720,250.00
Investment income (for the component units, net of investment expense of $81,424.00)	970,192.64	6,511,177.11	111,490.00
Interest on capital asset-related debt	(5,368,152.27)	-	(91,728.00)
Payments to or on behalf of East Tennessee State University or East Tennessee State University Foundation (Note 18)	-	-	(2,509,090.00)
Bond issuance costs	(172,643.80)	-	-
Other nonoperating revenues (expenses) (foundation amount includes $98,425.03 of gifts of capital assets to the university)	2,362,960.46	(86,228.65)	5,400.00
Net nonoperating revenues (expenses)	135,112,770.51	6,424,948.46	(1,763,678.00)
Income (loss) before other revenues, expenses, gains, or losses	(9,614,294.90)	4,675,611.31	(132,361.00)
Capital appropriations	4,460,134.45	-	-
Capital gifts and grants (university gifts include $393,599.31 of payments from ETSU Foundation and $98,425.03 of gifts of capital assets from ETSU Foundation)	11,594,114.98	294,301.68	-
Additions to permanent endowments	-	1,796,833.19	-
Total other revenues	16,054,249.43	2,091,134.87	-
Increase (decrease) in net position	6,439,954.53	6,766,746.18	(132,361.00)
NET POSITION			
Net position - beginning of year	223,311,219.41	76,012,662.77	19,358,080.00
Net position - end of year	$ 229,751,173.94	$ 82,779,408.95	$ 19,225,719.00

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

Tennessee Board of Regents
EAST TENNESSEE STATE UNIVERSITY
Statement of Cash Flows
For the Year Ended June 30, 2013

CASH FLOWS FROM OPERATING ACTIVITIES	
Tuition and fees	$ 92,968,124.29
Grants and contracts	42,287,793.89
Sales and services of educational activities	21,928,806.89
Sales and services of other activities	6,021,201.71
Payments to suppliers and vendors	(63,613,942.18)
Payments to employees	(158,094,163.03)
Payments for benefits	(58,538,299.88)
Payments for scholarships and fellowships	(27,587,562.93)
Loans issued to students	(1,725,336.25)
Collection of loans from students	1,456,119.99
Interest earned on loans to students	122,764.41
Auxiliary enterprise charges:	
Residence halls	14,363,348.22
Bookstore	360,705.72
Food services	664,671.50
Wellness facility	1,448,973.60
Other auxiliaries	1,844,485.16
Other receipts	646,954.48
Net cash used by operating activities	(125,445,354.41)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
State appropriations	80,497,400.00
Gifts and grants received for other than capital or endowment purposes	56,867,324.48
Federal student loan receipts	95,675,908.00
Federal student loan disbursements	(96,689,319.91)
Changes in deposits held for others	48,180.19
Other noncapital financing receipts	2,036,137.34
Net cash provided by noncapital financing activities	138,435,630.10
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Proceeds from capital debt	48,976,008.54
Capital appropriations	4,460,134.45
Capital grants and gifts received	10,916,425.77
Purchases of capital assets and construction	(41,041,906.57)
Principal paid on capital debt	(31,984,320.92)
Interest paid on capital debt	(5,599,648.85)
Bond issue costs paid on new debt issue	(172,643.80)
Net cash used by capital and related financing activities	(14,445,951.38)
CASH FLOWS FROM INVESTING ACTIVITIES	
Proceeds from sales and maturities of investments	12,996,916.67
Income on investments	1,155,916.45
Purchases of investments	(13,000,000.00)
Net cash provided by investing activities	1,152,833.12
Net decrease in cash	(302,842.57)
Cash - beginning of year	66,508,797.64
Cash - end of year	$ 66,205,955.07

Tennessee Board of Regents
EAST TENNESSEE STATE UNIVERSITY
Statement of Cash Flows (Continued)
For the Year Ended June 30, 2013

Reconciliation of operating loss to net cash used by operating activities:		
Operating loss	$	(144,727,065.41)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation expense		15,177,378.00
Other adjustments		132,289.00
Change in assets and liabilities:		
Receivables, net		(67,306.97)
Inventories		5,859.90
Prepaid expenses		42,846.85
Other assets		1,612.45
Accounts payable		(1,230,531.92)
Accrued liabilities		689,999.62
Net OPEB obligation		894,111.68
Unearned revenue		3,380,612.60
Deposits		(133,134.30)
Compensated absences		638,973.56
Due to grantors		18,216.79
Loans to students		(269,216.26)
Net cash used by operating activities	$	(125,445,354.41)

Noncash investing, capital, or financing transactions		
Gifts of capital assets	$	677,689.21
Unrealized losses on investments	$	(175,683.33)
Loss on disposal of capital assets	$	(32,171.60)

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 18 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 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.

The university has classified its revenues and expenses as either operating or nonoperating according to the following criteria: Operating revenues and expenses are those that have the characteristics of exchange transactions. Operating revenues include (1) tuition and fees, net of scholarship discounts and allowances; (2) certain federal, state, local, and private grants and contracts; (3) sales and services of auxiliary enterprises; and (4) interest on institutional loans. Operating expenses include (1) salaries and wages; (2) employee benefits, (3) utilities, supplies, and other services; (4) scholarships and fellowships; and (5) depreciation.

Nonoperating revenues and expenses include activities that have the characteristics of nonexchange transactions, such as gifts and contributions, and other activities that are defined as nonoperating by GASB Statement 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities that Use Proprietary Fund Accounting*, and GASB Statement 34, such as state appropriations and investment income.

When both restricted and unrestricted resources are available for use, it is the university's policy to determine whether to use restricted or unrestricted resources first, depending upon existing facts and circumstances.

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 upon 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 position. 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 position 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 Position

The university's net position is classified as follows:

Net investment in capital assets — This represents the university's total investment in capital assets, net of accumulated depreciation and net of outstanding debt obligations and deferred outflows/inflows of resources 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 net investment in capital assets.

Nonexpendable restricted net position — Nonexpendable restricted net position consists 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 position — Expendable restricted net position includes resources that the university is legally or contractually obligated to spend in accordance with restrictions imposed by external third parties.

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

Accounting Change

The university implemented GASB Statement 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position,* during the year ended June 30,

2013. The effect on the university was the renaming of the residual of all other elements in the statement of financial position as net position, rather than net assets.

Early Implementation of Accounting Pronouncement

In March 2012, GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities; it also recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. The provisions of this statement are effective for financial statements for periods beginning after December 15, 2012. However, the university has elected to early implement the provisions of this statement for fiscal year 2013.

Note 2. Cash

This classification includes demand deposits and petty cash on hand. At June 30, 2013, cash consists of $817,233.06 in bank accounts, $41,000 of petty cash on hand, $57,543,444.46 in the State of Tennessee Local Government Investment Pool (LGIP) administered by the State Treasurer, $7,795,577.55 in LGIP deposits for capital projects, and $8,700 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, the Tennessee Board of Regents withdraws funds and transfers them from the LGIP account 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, 2013, 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	$53,000,480.00	$4,022,720.00	$48,977,760.00

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. Securities are rated by Standard and Poor's, Moody's Investors Service, and/or Fitch Ratings 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 that are under contract of sale or are 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, 2013, the university's investments were rated as follows:

Investment Type	Fair Value	Credit Quality Rating AA	Unrated
LGIP	$ 65,339,022.01	$ -	$65,339,022.01
U.S. agency obligations	53,000,480.00	53,000,480.00	-
Total	$118,339,502.01	$53,000,480.00	$65,339,022.01

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, 2013
Federal Home Loan Bank (FHLB) obligations	24%
Federal National Mortgage Association (FNMA) obligations	34%
Federal Home Loan Mortgage Corporation (FHLMC) obligations	42%

Note 4. Receivables

Receivables included the following:

	June 30, 2013
Student accounts receivable	$ 5,714,861.25
Grants receivable	5,300,973.13
Notes receivable	253,696.17
Other receivables	6,765,024.87
Subtotal	18,034,555.42
Less allowance for doubtful accounts	2,794,584.67
Total	$15,239,970.75

Federal Perkins Loan Program funds included the following:

	June 30, 2013
Perkins loans receivable	$8,296,217.58
Less allowance for doubtful accounts	1,944,599.87
Total	$6,351,617.71

Note 5. Capital Assets

Capital asset activity for the year ended June 30, 2013, was as follows:

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$ 16,450,770.07	$ 20,700.00	$ -	$ -	$ 16,471,470.07
Land improvements and infrastructure	37,516,472.85	98,425.03	7,069,500.36	-	44,684,398.24
Buildings	331,390,345.30	-	14,296,678.06	510,580.00	345,176,443.36
Equipment	34,041,661.19	4,760,511.99	-	992,909.87	37,809,263.31
Library holdings	1,765,140.62	59,838.27	-	158,774.97	1,666,203.92
Intangible assets	4,433,400.78	-	-	-	4,433,400.78
Projects in progress	13,070,726.74	36,774,837.20	(21,366,178.42)	-	28,479,385.52
Total	438,668,517.55	41,714,312.49	-	1,662,264.84	478,720,565.20
Less accum. deprecia-tion/amortization:					
Land improvements and infrastructure	16,395,275.66	2,099,038.97	-	-	18,494,314.63
Buildings	127,453,661.73	9,880,770.54	-	510,580.00	136,823,852.27
Equipment	21,819,448.81	2,607,980.23	-	960,738.27	23,466,690.77
Library holdings	1,038,283.50	168,766.25	-	158,774.97	1,048,274.78

Intangible assets	2,633,256.85	420,822.01	-	-	3,054,078.86
Total	169,339,926.55	15,177,378.00	-	1,630,093.24	182,887,211.31
Capital assets, net	$269,328,591.00	$26,536,934.49	$ -	$ 32,171.60	$295,833,353.89

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 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 $52,861,654.57. At June 30, 2013, the buildings are reported at $36,319,198.90, net of accumulated depreciation of $16,542,455.67.

Note 7. Accounts Payable

Accounts payable included the following:

	June 30, 2013
Vendors payable	$2,182,291.66
Unapplied student payments	93,762.09
Other payables	423,676.67
Total	$2,699,730.42

Note 8. Long-term Liabilities

Long-term liabilities activity for the year ended June 30, 2013, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Payables:					
TSSBA debt:					
Bonds	$105,105,597.49	$24,985,295.00	$12,036,847.96	$118,054,044.53	$4,634,127.58
Unamortized bond premium	2,294,687.52	3,122,296.27	304,530.18	5,112,453.61	-
Commercial paper	23,501,471.61	21,278,505.53	19,947,472.96	24,832,504.18	-
Subtotal	130,901,756.62	49,386,096.80	32,288,851.10	147,999,002.32	4,634,127.58
Other liabilities:					
Unearned revenue	14,733,749.30	15,131,856.49	12,110,238.61	17,755,367.18	15,328,006.49
Compensated absences	10,238,836.49	6,894,051.78	6,255,078.22	10,877,810.05	3,057,970.76
Due to grantors	7,448,171.34	20,094.00	1,877.21	7,466,388.13	-
Subtotal	32,420,757.13	22,046,002.27	18,367,194.04	36,099,565.36	18,385,977.25
Total long-term liabilities	$163,322,513.75	$71,432,099.07	$50,656,045.14	$184,098,567.68	$23,020,104.83

TSSBA Debt - Bonds

Bonds, with interest rates ranging from 2% to 5%, were issued by the Tennessee State School Bond Authority (TSSBA). The bonds are due serially to 2042 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 9 for further details. The bonded indebtedness with the Tennessee State School Bond Authority included in long-term liabilities on the statement of net position 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, 2013.

Debt service requirements to maturity for the university's portion of TSSBA bonds at June 30, 2013, are as follows:

Year Ending June 30	Principal	Interest	Total
2014	$ 4,634,127.58	$ 5,609,013.68	$ 10,243,141.26
2015	4,738,988.50	5,439,112.27	10,178,100.77
2016	4,696,666.91	5,237,405.24	9,934,072.15
2017	4,927,423.51	5,015,131.91	9,942,555.42
2018	5,157,484.21	4,805,356.89	9,962,841.10
2019-2023	28,950,627.39	20,221,172.64	49,171,800.03
2024-2028	26,058,805.90	13,435,956.54	39,494,762.44
2029-2033	18,999,376.91	7,720,740.35	26,720,117.26
2034-2038	16,666,347.70	3,435,486.98	20,101,834.68

2039-2042	3,224,195.92	394,987.09	3,619,183.01
Total	$118,054,044.53	$71,314,363.59	$189,368,408.12

TSSBA Debt - Commercial Paper

The TSSBA issues commercial paper to finance the costs of various capital projects during the construction phase. When projects are placed in service, TSSBA issues long-term, fixed-rate debt to finance the project over its useful payback period and redeems the commercial paper. The amount issued for projects at the university was $24,832,504.18 at June 30, 2013.

For the commercial paper program, TSSBA 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.

Refunding of Debt

On August 1, 2012, the TSSBA issued $7,139,298 in revenue bonds with an average interest rate of 4.24% to advance refund $7,630,546.69 of outstanding Series 2004B and Series 2006A bonds with an average interest rate of 4.34%. The net proceeds of $8,076,183.16 (after payment of $23,524.36 in underwriter's fees and issuance costs) were deposited with an escrow agent to provide for all future debt service payments on the Series 2004B and Series 2006A bonds. As a result, the Series 2004B and Series 2006A bonds are considered to be defeased, and the liability for those bonds has been removed from the university's long-term liabilities.

Although the advance refunding resulted in the recognition of a deferred loss of $445,618.47 to be amortized over the next 22 years, the university in effect reduced its aggregate debt service payments by $1,136,508.00 over the next 22 years and obtained an economic gain (difference between the present values of the old and new debt service payments) of $852,240.31.

Note 9. Pledged Revenues

The university has pledged certain revenues and fees, including state appropriations, to repay $118,054,044.53 in revenue bonds issued from June 2005 to August 2012. Proceeds from the bonds provided financing for construction and renovation projects. The bonds are payable through 2042. Annual principal and interest payments on the bonds are expected to require 3.59% of available revenues. The total principal and interest remaining to be paid on the bonds is $189,368,408.12. Principal and interest paid for the current year and total available revenues were $9,749,017.20 and $271,914,959.37, respectively.

Note 10. Pension Plans

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.treasury.tn.gov/tcrs.

Funding Policy — Plan members are noncontributory. The university is required to contribute at an actuarially determined rate. The current rate is 15.03% 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 ending June 30, 2013; June 30, 2012; and June 30, 2011, were $8,044,873.15, $7,674,153.32, and $7,186,330.71, respectively. Contributions met the requirements for each year.

Defined Contribution Plans

Optional Retirement Plans

Plan Description – The university contributes to three defined contribution plans: Teachers Insurance and Annuity Association–College Retirement Equities Fund, ING Life Insurance and Annuity Company, and Variable Annuity Life Insurance Company. 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 $8,357,420.17 for the year ended June 30, 2013, and $7,998,091.16 for the year ended June 30, 2012. Contributions met the requirements for each year.

Note 11. Other Postemployment Benefits

Health care 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 plan for health care 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 17. The plans are reported in the *Tennessee Comprehensive Annual Financial Report* (CAFR). The CAFR is available on the state's website at www.tn.gov/finance/act/cafr.shtml.

Special Funding Situation

The State of Tennessee is legally responsible for contributions to the Medicare Supplement Plan, which covers the retirees of other governmental entities, including East Tennessee State University. The state is the sole contributor for the university retirees who 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. The plan's claims liabilities are periodically computed using actuarial and statistical techniques to establish premium rates. The plan's administrative costs 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, adjusted for years of service, as active employees. 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)	$ 3,483,000.00
Interest on the net OPEB obligation	468,342.67
Adjustment to the ARC	(497,136.83)
Annual OPEB cost	3,454,205.84
Amount of contribution	(2,560,094.16)
Increase in net OPEB obligation	894,111.68
Net OPEB obligation – beginning of year	11,708,566.60
Net OPEB obligation – end of year	$12,602,678.28

Year-end	Plan	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation at Year-end
June 30, 2013	State Employee Group Plan	$3,454,205.84	74.1%	$12,602,678.28
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

Funded Status and Funding Progress

The funded status of the 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% investment rate of return (net of administrative expenses) and an annual health care cost trend rate of 9.25% initially. The rate decreased to 8.75% in fiscal year 2013, and then reduces by decrements to an ultimate rate of 5% in fiscal year 2021. All rates include a 2.5% inflation assumption, which also represents the projected salary increase. 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 12. Chairs of Excellence

The university had $23,489,022.56 on deposit at June 30, 2013, with the State Treasurer for its Chairs of Excellence program. These funds are held in trust by the state and are not included in the financial statements.

Note 13. 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 earthquake 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, 2013, is presented in the *Tennessee Comprehensive Annual Financial Report* (CAFR). 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, 2013, the Risk Management Fund held $108.5 million in cash designated for payment of claims.

At June 30, 2013, the scheduled coverage for the university was $870,734,300 for buildings and $172,452,300 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 costs of claims that have been reported but not settled and of claims that have been incurred but not reported. Employees and providers have 13 months to file medical claims.

Note 14. Commitments and Contingencies

Sick Leave

The university records the cost of sick leave when paid. The dollar amount of unused sick leave was $55,754,009.31 at June 30, 2013.

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 $457,750.46 for the year ended June 30, 2013. All operating leases are cancelable at the lessee's option.

Construction in Progress

At June 30, 2013, outstanding commitments under construction contracts totaled $16,363,725.24 for a student parking garage, lab renovations at the College of Medicine, expansion of the student recreation facility, accessibility and code corrections, and various other projects, of which $2,685,555.46 will be funded by future state capital outlay appropriations.

Litigation

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

Note 15. Natural Classification With Functional Classifications

The university's operating expenses for the year ended June 30, 2013, are as follows:

	Natural Classification					
Functional Classification	Salaries	Benefits	Other Operating	Scholarships	Depreciation	Total
Instruction	$ 95,348,313.00	$33,273,607.87	$17,092,596.78	$ 1,055,889.14	$ -	$146,770,406.79
Research	5,487,498.05	1,600,375.48	3,939,181.55	3,686.15	-	11,030,741.23
Public service	11,949,208.42	4,385,563.29	6,163,773.02	93,906.42	-	22,592,451.15
Academic support	15,641,132.64	6,653,872.88	4,446,098.66	187,585.93	-	26,928,690.11
Student services	10,071,614.39	4,379,879.49	5,787,628.80	1,906,215.82	-	22,145,338.50
Institutional support	12,715,205.48	5,285,281.26	1,993,361.29	114,894.23	-	20,108,742.26
Operation & maintenance of plant	6,169,811.11	3,496,372.54	14,285,378.85	-	-	23,951,562.50
Scholarships & fellowships	-	-	577,313.10	24,082,371.24	-	24,659,684.34
Auxiliary	1,863,141.89	670,073.84	8,374,071.91	147,570.03	-	11,054,857.67
Depreciation	-	-	-	-	15,177,378.00	15,177,378.00
Total	$159,245,924.98	$59,745,026.65	$62,659,403.96	$27,592,118.96	$15,177,378.00	$324,419,852.55

Note 16. 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 foundation's most recently audited financial report, at June 30, 2013, the assets of the foundation totaled $2,271,008.00, liabilities were $177,195.00, and the net position amounted to $2,093.813.00.

Note 17. On-behalf Payments

During the year ended June 30, 2013, the State of Tennessee made payments of $132,289.00 on behalf of the university for retirees participating in the Medicare Supplement Plan. The Medicare Supplement Plan is a postemployment benefit health care plan and is discussed further in Note 11. The plan is reported in the *Tennessee Comprehensive Annual Financial Report*. That report is available on the state's website at www.tn.gov/finance/act/cafr.shtml.

Note 18. 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, 2013, the foundation made distributions of $1,516,794.67 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 that are readily convertible to known amounts of cash and that have original maturities of three months or less. At June 30, 2013, cash and cash equivalents consists of $165,161.05 in bank accounts, $3,133,827.27 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer, and $294,713.31 in cash held by others.

The Local Government Investment Pool is part of the State 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, 2013, 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	$ 5,041,995.99	$2,065,881.37	$2,976,114.62	$ -	$ -	$ -
Bond mutual funds	16,595,885.20	1,967,878.02	6,309,017.47	4,110,085.30	4,208,904.41	-
Equity mutual funds	56,787,487.88	-	-	-		56,787,487.88
Total	$78,425,369.07	$4,033,759.39	$9,285,132.09	$4,110,085.30	$4,208,904.41	$56,787,487.88

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 the 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 Investor Service, and/or Fitch Ratings and are presented below using the Standard and Poor's rating scale. The foundation's 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, 2013, the foundation's investments were rated as follows:

		Credit Quality Rating				
Investment Type	Fair Value	AAA	AA	A	BBB or Less	Unrated
LGIP	$ 3,133,827.27	$ -	$ -	$ -	$ -	$3,133,827.27
Corporate bonds	5,041,995.99	-	2,621,837.91	2,420,158.08	-	-
Bond mutual funds	16,595,885.20	10,543,899.13	1,027,779.47	2,379,985.68	2,644,220.92	-
Total	$24,771,708.46	$10,543,899.13	$3,649,617.38	$4,800,143.76	$2,644,220.92	$3,133,827.27

Investments of endowment and similar funds are composed of the following:

	June 30, 2013
Mutual funds	$57,654,039.83
Corporate bonds	5,041,995.99
Cash held by others	294,713.31
Total	$62,990,749.13

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. Of the total units at June 30, 2013, each having a fair value of $1.1400842819, 55,992,078.14 units were owned by endowments, and 429,870.76 units were owned by quasi-endowments.

The following tabulation summarizes changes in relationships between cost and fair values of the pooled assets for the year ended June 30, 2013:

	Pooled Assets			Fair
			Net Gains	Value
	Fair Value	Cost	(Losses)	Per Unit
End of year	$78,425,369.07	$75,872,206.94	$2,553,162.13	$1.1400842819
Beginning of year	$69,342,039.49	$68,722,577.97	619,461.52	$1.0952771929
Unrealized net gains			1,933,700.61	
Realized net gains			2,622,048.69	
Total net gains			$4,555,749.30	

The average annual earnings per unit, exclusive of net gains, were $0.027 for the year ended June 30, 2013.

Pledges Receivable

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

	June 30, 2013
Current pledges	$327,464.23
Pledges due in one to five years	501,853.38
Subtotal	829,317.61
Less discounts to net present value	15,507.45
Total pledges receivable, net	$813,810.16

Capital Assets

Capital asset activity for the year ended June 30, 2013, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance
Buildings	$59,000.00	$ -	$ -	$59,000.00
Equipment	9,486.00	-	-	9,486.00
Projects in progress	-	98,425.03	98,425.03	-
Total	68,486.00	98,425.03	98,425.03	68,486.00
Less accumulated depreciation:				
Buildings	59,000.00	-	-	59,000.00
Capital assets, net	$ 9,486.00	$98,425.03	$98,425.03	$ 9,486.00

Endowments

The ETSU Foundation's endowment consists of 488 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 position 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 nonexpendable restricted net position (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 position (total net position less reserves). The remaining portion of the donor-restricted endowment fund that is not classified in nonexpendable restricted net position is classified as expendable restricted net position until those amounts are appropriated for expenditure by the foundation in a manner consistent with the standard of prudence prescribed by the Act. In accordance with the Act, the foundation considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. the duration and preservation of the fund,
2. the purposes of the foundation and the endowment fund,
3. general economic conditions,
4. the possible effect of inflation or deflation,

5. the expected total return from income and the appreciation of investments,
6. other resources of the foundation, and
7. the investment policies of the foundation.

Return objectives and risk parameters — The foundation has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity or for 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% 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% 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% 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, 2013, net appreciation of $11,181,216.56 is available to be spent, of which $5,816,222.48 is included in restricted net position expendable for scholarships and fellowships, $87,639.56 is included in restricted net position expendable for research, $727,335.92 is included in restricted net position expendable for instructional departmental uses, and $4,550,018.60 is included in restricted net position expendable for other purposes.

Prior Period Restatement

In prior years, endowment net appreciation was included in restricted nonexpendable net position. It was determined that the net appreciation should be included in restricted expendable net position. As a result of this error, net position has been restated as of June 30, 2012.

	As Previously Stated	As Restated	Effect of Correction
Statement of net position at June 30, 2012:			
Restricted for nonexpendable:			
Scholarships and fellowships	$43,568,747	$38,764,339	$(4,804,408)
Research	655,512	582,304	(73,208)
Instructional departmental uses	5,679,472	5,092,777	(586,695)
Other	8,185,000	4,837,891	(3,347,109)
Expendable:			
Scholarships and fellowships	3,253,983	8,058,390	4,804,407
Research	287,821	361,030	73,209
Instructional departmental uses	3,179,181	3,765,877	586,696
Other	10,089,318	13,436,427	3,347,109

MEDICAL EDUCATION ASSISTANCE CORPORATION

The 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, 2013, MEAC made distributions of $2,509,090 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, 2013, cash consisted of $5,103,803 in bank accounts, $2,350 of petty cash on hand, and $84,731 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer.

The Local Government Investment Pool is part of the State 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, 2013, 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, 2013, MEAC had no rated investments, as deposits in LGIP are unrated.

Receivables

Receivables included the following:

	June 30, 2013
Patient accounts receivable, net	$2,645,318
Other receivables	1,389,263
Total	$4,034,581

Capital Assets

Capital asset activity for the year ended June 30, 2013, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance
Land	$ 18,150	$ -	$ -	$ 18,150
Buildings	1,960,233	-	-	1,960,233
Leasehold improvements	645,171	6,872	-	652,043
Equipment	3,992,959	476,722	179,382	4,290,299
Total	6,616,513	483,594	179,382	6,920,725
Less accumulated depreciation:				
Buildings	263,396	52,276	-	315,672
Leasehold improvements	388,558	58,839	-	447,397
Equipment	3,075,415	476,742	179,382	3,372,775
Total accumulated depreciation	3,727,369	587,857	179,382	4,135,844
Capital assets, net	$2,889,144	$(104,263)	$ -	$2,784,881

Long-term liabilities

Long-term liabilities activity for the year ended June 30, 2013, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Note payable	$1,527,853	$ -	$39,075	$1,488,778	$ 39,209
Compensated absences	687,966	80,362	-	768,328	153,666
Total long-term liabilities	$2,215,819	$80,362	$39,075	$2,257,106	$192,875

Notes 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 lower interest rates. 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 $1,488,778 at June 30, 2013.

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

Year Ending June 30	Principal	Interest	Total
2014	$ 39,209	$ 91,051	$ 130,260
2015	41,706	88,554	130,260
2016	1,407,863	46,997	1,454,860
Total	$1,488,778	$226,602	$1,715,380

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	28.03%
July 1, 2010	State Employee Group Plan	$ -	$39,835,000.00	$39,835,000.00	0%	$97,197,256.00	40.98%
July 1, 2009	State Employee Group Plan	$ -	$44,411,000.00	$44,411,000.00	0%	$99,072,828.00	44.83%

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, 2013

CASH FLOWS FROM OPERATING ACTIVITIES		
Gifts and contributions	$	2,783,137.02
Payments to suppliers and vendors		(2,318,875.64)
Payments for scholarships and fellowships		(1,416,799.12)
Payments to or on behalf of East Tennessee State University		(1,516,794.67)
Other receipts		1,262,714.39
Net cash used by operating activities		(1,206,618.02)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Private gifts for endowment purposes		1,796,833.19
Net cash provided by noncapital financing activities		1,796,833.19
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Capital grants and gifts received		294,301.68
Purchase of capital assets and construction		(98,425.03)
Net cash provided by capital and related financing activities		195,876.65
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments		23,737,181.16
Income on investments		4,605,948.69
Purchases of investments		(30,924,735.92)
Net cash used by investing activities		(2,581,606.07)
Net decrease in cash and cash equivalents		(1,795,514.25)
Cash and cash equivalents - beginning of year		5,389,215.88
Cash and cash equivalents - end of year	$	3,593,701.63
Reconciliation of operating loss to net cash used by operating activities:		
Operating loss	$	(1,749,337.15)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Change in assets and liabilities:		
Receivables, net		228,817.84
Accounts payable		313,901.29
Net cash used by operating activities	$	(1,206,618.02)
Noncash investing, capital, or financing transactions		
Unrealized gains on investments	$	1,933,700.61
Transfer of capital assets to the university	$	(98,425.03)

Tennessee Board of Regents
EAST TENNESSEE STATE UNIVERSITY
Supplementary Information
Schedule of Cash Flows - Medical Education Assistance Corporation
For the Year Ended June 30, 2013

CASH FLOWS FROM OPERATING ACTIVITIES	
Collections from patient charges	$ 34,541,919.00
Payments to suppliers and vendors	(8,200,933.00)
Payments to employees	(22,638,060.00)
Payments for benefits	(2,220,781.00)
Other receipts	61,596.00
Net cash provided by operating activities	1,543,741.00
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
Gifts and grants	720,250.00
Payments to or on behalf of East Tennessee State University or East Tennessee State University Foundation	(2,509,090.00)
Net cash used by noncapital financing activities	(1,788,840.00)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Proceeds from sale of capital assets	1,000.00
Purchase of capital assets and construction	(483,594.00)
Principal paid on capital debt	(39,075.00)
Interest paid on capital debt	(91,728.00)
Net cash used by capital and related financing activities	(613,397.00)
CASH FLOWS FROM INVESTING ACTIVITIES	
Income on investments	111,491.00
Proceeds from sales and maturities of investments	8,047,507.00
Purchases of investments	(8,132,896.00)
Other investing receipts	4,400.00
Net cash provided by investing activities	30,502.00
Net decrease in cash	(827,994.00)
Cash - beginning of year	6,018,878.00
Cash - end of year	$ 5,190,884.00
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	$ 1,631,317.00
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation expense	587,857.00
Change in assets and liabilities:	
Receivables, net	(351,306.00)
Prepaid expenses	341,136.00
Accounts payable	(145,098.00)
Accrued liabilities	(67,176.00)
Compensated absences	80,363.00
Due to the university	(434,488.00)
Other liabilities	(98,864.00)
Net cash provided by operating activities	$ 1,543,741.00

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

The Honorable Bill Haslam, Governor
Members of the General Assembly
The Honorable John G. Morgan, Chancellor
Dr. Brian Noland, President

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, 2013, and the related notes to the financial statements, which collectively comprise the university's basic financial statements, and have issued our report thereon dated November 27, 2013. We conducted our audit in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Our report includes a reference to other auditors who audited the financial statements of the East Tennessee State University Foundation and the Medical Education Assistance Corporation, as described in our report on East Tennessee State University's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the university's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances 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. Accordingly, we do not express an opinion on the effectiveness of the university's internal control.

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. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the university's financial statements are free from 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 *Government Auditing Standards*.

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Deborah V. Loveless

Deborah V. Loveless, CPA
Director
November 27, 2013