



**STATE OF TENNESSEE  
COMPTROLLER OF THE TREASURY**

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**TENNESSEE BOARD OF REGENTS  
EAST TENNESSEE STATE UNIVERSITY**

**Financial and Compliance Audit Report**

For the Year Ended June 30, 2015

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**Justin P. Wilson, Comptroller**



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COMPTROLLER OF THE TREASURY  
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February 26, 2016

The Honorable Bill Haslam, Governor  
Members of the General Assembly  
The Honorable David Gregory, Acting 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, 2015. 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, CPA  
Director

15/077

**Audit Report**  
**Tennessee Board of Regents**  
**East Tennessee State University**  
**For the Year Ended June 30, 2015**

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State of Tennessee

# **A u d i t   H i g h l i g h t s**

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit  
**Tennessee Board of Regents**  
**East Tennessee State University**  
For the Year Ended June 30, 2015

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## **Opinions on the Financial Statements**

The opinions on the financial statements are unmodified.

## **Audit Findings**

The audit report contains no findings.



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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, 2015, 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 university'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, 2015, 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, 2015, and the changes in financial position and cash flows thereof for the year then ended, in accordance 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 18, the university implemented Governmental Accounting Standards Board Statement 68, *Accounting and Financial Reporting for Pensions – an Amendment of GASB Statement No. 27*; and Statement 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*, during the year ended June 30, 2015. Our opinion is not modified with respect to this matter.

As discussed in Note 19, the financial statements of East Tennessee State University Foundation, a discretely presented component unit of East Tennessee State University, include investments valued at \$9,570,599.40 (9.8% of net position of the foundation), whose fair values have been estimated by management in the absence of readily determinable fair values. Management's estimates are based on information provided by the fund managers. 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 6 through 15, the schedule of funding progress on page 52, the schedule of East Tennessee State University's proportionate share of the net pension liability for the Closed State and Higher Education Employee Pension Plan within TCRS on page 53, the schedule of East Tennessee State University's contributions for the Closed State and Higher Education Employee Pension Plan within TCRS on page 54, and the schedule of East Tennessee State University's contributions for the State and Higher Education Employee Retirement Plan within TCRS on page 55 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 56 and 57 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 December 11, 2015, 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, CPA

Director

December 11, 2015

**Tennessee Board of Regents**  
**EAST TENNESSEE STATE UNIVERSITY**  
**Management's Discussion and Analysis**

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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 year ended June 30, 2015, with comparative information presented for the year ended June 30, 2014. This discussion has been prepared by management along with the financial statements and related note disclosures and should be read in conjunction with the independent auditor's report, the financial statements, and the notes to the financial statements.

The university has two discretely presented component units, the East Tennessee State University Foundation and the Medical Education Assistance Corporation (MEAC). More detailed information about the university's component units is presented in Note 19 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 of resources, 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 have been incurred but not yet expended for capital assets, such amounts are not included. The next category is restricted net position, which is subdivided 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.

The following table summarizes the university's assets, liabilities, deferred outflows/inflows of resources, and net position at June 30, 2015, and June 30, 2014.

**Summary of Net Position  
(in thousands of dollars)**

	<u>2015</u>	<u>2014</u>
<b>Assets:</b>		
Current assets	\$ 26,394	\$ 27,269
Capital assets, net	295,798	301,205
Other assets	128,001	115,372
<b>Total assets</b>	<b>450,193</b>	<b>443,846</b>
<b>Deferred outflows of resources</b>		
Deferred amount on debt refunding	7,279	374
Deferred outflows related to pensions	8,213	-
<b>Total deferred outflows</b>	<b>15,492</b>	<b>374</b>
<b>Liabilities:</b>		
Current liabilities	38,881	38,930
Noncurrent liabilities	190,289	172,378
<b>Total liabilities</b>	<b>229,170</b>	<b>211,308</b>

**Deferred inflows of resources**

Deferred inflows related to pensions	20,291	-
<b>Total deferred inflows</b>	<b>20,291</b>	<b>-</b>

**Net position:**

Net investment in capital assets	156,812	152,409
Restricted – expendable	6,552	5,752
Unrestricted	52,860	74,751
<b>Total net position</b>	<b>\$216,224</b>	<b>\$232,912</b>

Comparison of Fiscal Year 2015 to Fiscal Year 2014

- ◆ Current assets decreased from 2014 to 2015 due to reductions primarily in student accounts receivable through increased collection activity and changes in summer school schedules.
- ◆ Capital assets, net of depreciation, decreased from 2014 to 2015 due to depreciation for the year exceeding additions to capital assets for the year.
- ◆ In 2015, other assets increased due to increases in noncurrent cash held in plant funds for fiscal year 2016 projects.
- ◆ Deferred outflows increased during the year due to two major activities. The Tennessee State School Bond Authority issued revenue bonds to advance refund 16 prior issues of debt, which resulted in a deferred loss of \$7.3 million. The unamortized balance at June 30 for all debt refunding was \$7.2 million. Additionally, the university recorded a deferred outflow for pensions equal to the payments made during the year to the Tennessee Consolidated Retirement System with the implementation of GASB Statement 68. The unamortized balance for pensions is \$8.2 million. Further information on the debt refunding may be found in Note 8 and on pensions, in Note 10 of the financial statements.
- ◆ Current liabilities remained relatively unchanged from 2014 to 2015.
- ◆ In 2015, noncurrent liabilities increased primarily due to recording of the net pension liability of \$14 million with the implementation of GASB Statement 68. Further information regarding pensions can be found in Note 10 of the financial statements.
- ◆ Net investment in capital assets increased \$4.4 million due to a decrease in net capital assets of \$5.4 million, a decrease in reported capital debt of \$2.9 million, and an increase in deferred amount on debt refunding of \$6.9 million.
- ◆ Unrestricted net position decreased from 2014 to 2015, primarily due to the cumulative effect of a change in accounting principle related to pensions. The university's new net pension liability is funded by unrestricted net position.

## 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 East Tennessee State 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.

A summary of the university's revenues, expenses, and changes in net position for the years ended June 30, 2015, and June 30, 2014, follows.

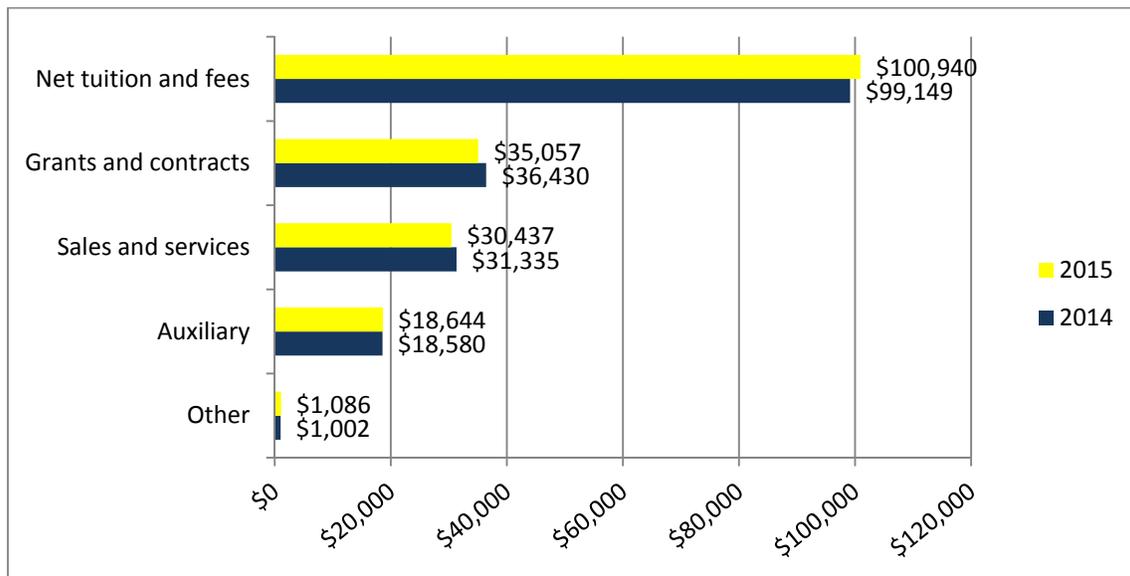
### Summary of Revenues, Expenses, and Changes in Net Position (in thousands of dollars)

	<u>2015</u>	<u>2014</u>
Operating revenues	\$186,164	\$186,495
Operating expenses	313,057	323,549
Operating loss	(126,893)	(137,054)
Nonoperating revenues and expenses	135,784	133,166
Income (loss) before other revenues, expenses, gains, or losses	8,891	(3,888)
Other revenues, expenses, gains, or losses	6,697	6,606
Increase in net position	15,588	2,718
Net position at beginning of year	232,912	229,751
Cumulative effect of change in accounting principle	(32,276)	-
Prior-period adjustment	-	443
Net position at beginning of year - restated	200,636	230,194
Net position at end of year	<b>\$216,224</b>	<b>\$232,912</b>

## Operating Revenues

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

### **Operating Revenues by Source (in thousands of dollars)**



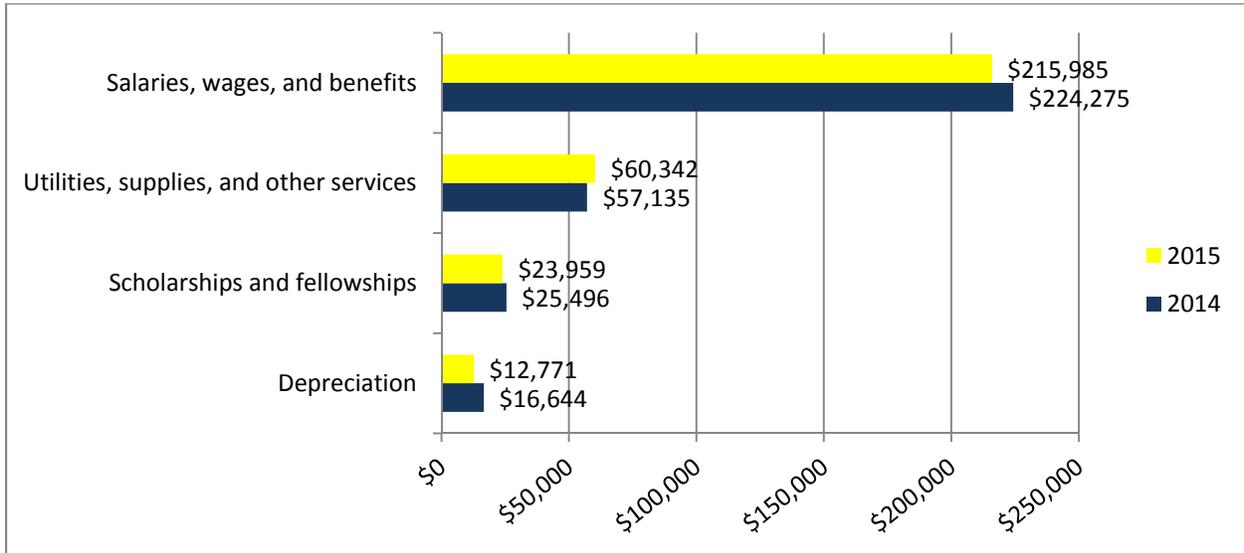
## Comparison of Fiscal Year 2015 to Fiscal Year 2014

- ◆ Tuition and fees increased in 2015 due to an average 7% fee increase, less an increase in discounts for tuition and fees offered to eligible students and reported as a scholarship allowance in the financial statements.
- ◆ Governmental grants and contracts decreased slightly due to reductions in funding through federal and state grants and contracts.
- ◆ Sales and services declined from 2014 to 2015, as a result of a reduction of 16 medical resident positions funded by local hospitals.
- ◆ Auxiliaries and other operating revenues 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 2015 to Fiscal Year 2014

- ◆ A decrease in benefits due to the recording of \$8 million in pension contributions paid to the Tennessee Consolidated Retirement System as a deferred outflow rather than a retirement expense accounts for most of the change in salaries and benefits from 2014 to 2015.
- ◆ Other operating expenses increased with increases in professional and administrative services related to ongoing construction and renovation projects.
- ◆ Scholarships decreased due to an increase in the institutional discounts provided to eligible students and reported as a scholarship allowance in the financial statements.
- ◆ Depreciation decreased due to a change in accounting estimate. During fiscal year 2015, it was determined that buildings were more appropriately depreciated over a period of from 40 to 60 years, instead of the 40 years previously used. Further information can be found in Note 5.

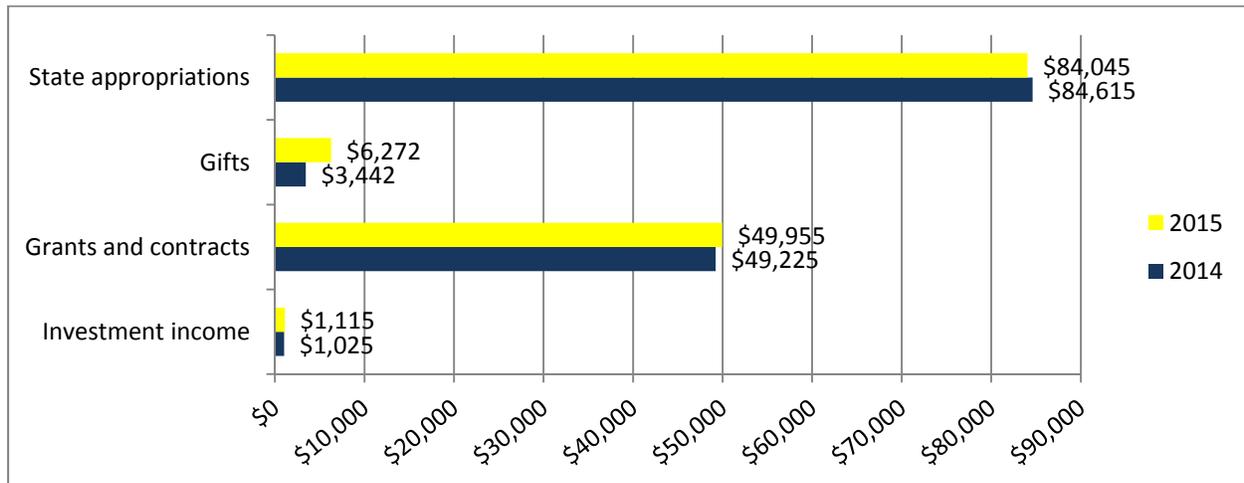
Nonoperating Revenues and Expenses

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)**

	<u>2015</u>	<u>2014</u>
State appropriations	\$ 84,045	\$ 84,615
Gifts	6,272	3,442
Grants and contracts	49,955	49,225
Investment income	1,115	1,025
Interest on capital asset-related debt	(5,303)	(6,090)
Interest on noncapital debt	(17)	-
Bond issuance costs	(158)	(148)
Other nonoperating revenues (expenses)	(125)	1,097
<b>Total nonoperating revenues (expenses)</b>	<b>\$135,784</b>	<b>\$133,166</b>

**Nonoperating Revenues  
(in thousands of dollars)**



Comparison of Fiscal Year 2015 to Fiscal Year 2014

- ◆ State appropriations remained relatively constant.
- ◆ Nonoperating gifts increased due to gifts transferred for the College of Pharmacy.
- ◆ Nonoperating grants and contracts remained relatively constant.
- ◆ Investment income increased slightly due to increased amounts available to invest over the course of the 2015 fiscal year.
- ◆ Interest on capital asset-related debt decreased largely due to lower bond interest rates and bond refunding activities.

- ◆ Bond issuance costs increased slightly with the refunding of 16 bond issues in fiscal year 2015.
- ◆ The other nonoperating revenues (expenses) decrease is a result of a prior year insurance recovery and gain on disposal of land and buildings.

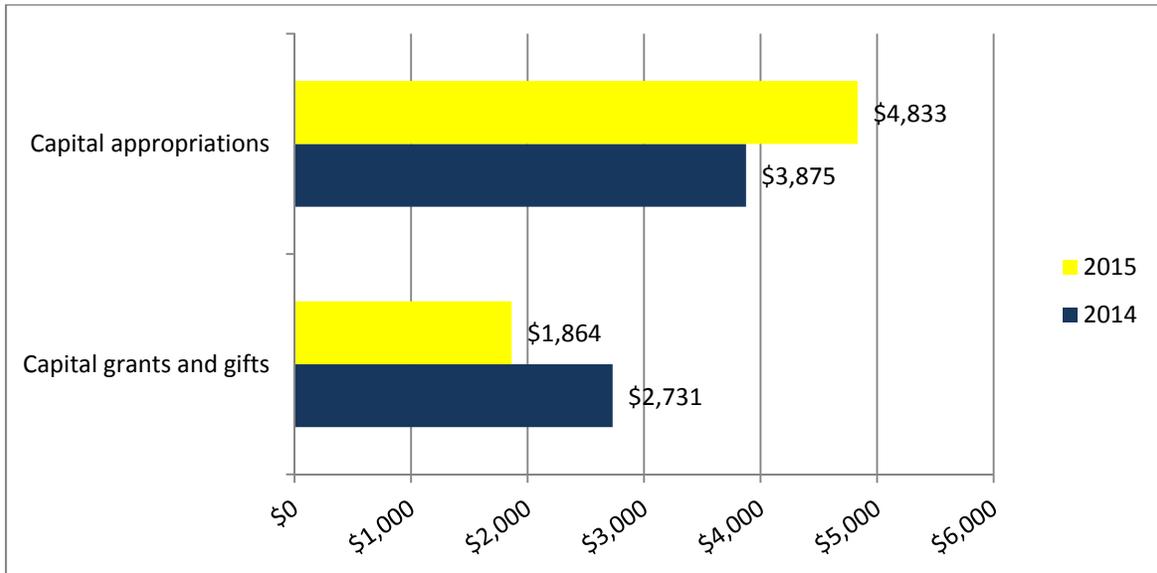
Other Revenues

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

**Other Revenues  
(in thousands of dollars)**

	<u>2015</u>	<u>2014</u>
Capital appropriations	\$4,833	\$3,875
Capital grants and gifts	1,864	2,731
<b>Total other revenues</b>	<b>\$6,697</b>	<b>\$6,606</b>

**Other Revenues  
(in thousands of dollars)**



## Comparison of Fiscal Year 2015 to Fiscal Year 2014

- ◆ Capital appropriations increased from 2014 to 2015 due to an increase in funded expenses for capital projects.
- ◆ Capital gifts and grants decreased due to the comparatively high level of capital grants in fiscal year 2014 through the American Recovery and Reinvestment Act for the Johnson City Community Health Center, College of Medicine Building 119 renovation, and Brown Hall renovations.

## **Capital Assets and Debt Administration**

### Capital Assets

East Tennessee State University had \$295,798,126.05 invested in capital assets, net of accumulated depreciation of \$209,765,691.00 at June 30, 2015; and \$301,205,379.59 invested in capital assets, net of accumulated depreciation of \$198,221,241.33 at June 30, 2014. Depreciation charges totaled \$12,770,811.54 and \$16,643,710.63 for the years ended June 30, 2015, and June 30, 2014, respectively. Depreciation expense decreased by approximately \$4 million due to a change in accounting estimate in which buildings are depreciated over a period of from 40 to 60 years, rather than 40 years.

### **Summary of Capital Assets, Net of Depreciation (in thousands of dollars)**

	<b><u>2015</u></b>	<b><u>2014</u></b>
Land	\$ 16,482	\$ 16,482
Land improvements and infrastructure	25,405	27,665
Buildings	237,183	237,192
Equipment	13,613	14,304
Library holdings	424	514
Intangible assets	538	959
Art and historical collections	24	24
Projects in progress	2,129	4,065
<b>Total</b>	<b>\$295,798</b>	<b>\$301,205</b>

Capital assets, net of depreciation, decreased from 2014 to 2015 due to the depreciation expense taken exceeding capital assets acquired for the year.

At June 30, 2015, outstanding commitments under construction contracts totaled \$5 million for various renovations and repairs of buildings and infrastructure. Future state capital outlay appropriations will fund approximately \$500 thousand 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 \$152,470,683.74 and \$149,170,793.78 in debt outstanding at June 30, 2015, and June 30, 2014, respectively. The table below summarizes these amounts by type of debt instrument.

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

	<u>2015</u>	<u>2014</u>
Revolving credit facility	\$ 2,940	\$ 831
Bonds	132,628	140,979
Unamortized bond premiums	16,903	7,361
<b>Total</b>	<b>\$152,471</b>	<b>\$149,171</b>

The Tennessee State School Bond Authority (TSSBA) issued bonds with interest rates ranging from 0.35% to 5% due serially to 2043 on behalf of East Tennessee State University. The university is responsible for the debt service of these bonds. The current portion of the \$132,627,481.08 of bonds outstanding at June 30, 2015, is \$5,266,086.02.

The ratings on debt issued by the Tennessee State School Bond Authority at June 30, 2015, 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 significantly improved. The university is receiving over \$4.6 million in increased appropriations for the fiscal year ended June 30, 2016, for salary, benefits, and operating increases. This has allowed the university to have the smallest increase in maintenance fees since 2000. In addition, the university is embarking on a major building campaign in which it is expected we will have over \$170 million in construction active over the next several years, which includes new construction or major renovations of a Fine Arts Center, Data Center, Simulation Center, Public Health Building, Student Center, and a football stadium. These projects will fundamentally transform the campus for our students. It is hoped the economy of the state will continue to improve, providing increased funding and opportunities for our students.

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

**Tennessee Board of Regents**  
**EAST TENNESSEE STATE UNIVERSITY**  
**Statement of Net Position**  
**June 30, 2015**

	Component Units		
	University	East Tennessee State University Foundation	Medical Education Assistance Corporation
<b>Assets</b>			
<b>Current assets:</b>			
Cash and cash equivalents (Notes 2 and 19)	\$ 8,891,528.21	\$ 635,893.76	\$ 8,605,794.00
Short-term investments (Note 19)	-	-	6,265,000.00
Accounts, notes, and grants receivable (net) (Note 4)	11,812,676.72	-	3,984,493.00
Due from primary government	3,292,121.81	-	-
Due from component units	383,054.57	-	-
Inventories (at lower of cost or market)	280,225.59	-	-
Prepaid expenses	852,584.63	-	279,236.00
Accrued interest receivable	872,164.13	35,574.39	-
Other assets	9,691.70	-	-
<b>Total current assets</b>	<b>26,394,047.36</b>	<b>671,468.15</b>	<b>19,134,523.00</b>
<b>Noncurrent assets:</b>			
Cash and cash equivalents (Notes 2 and 19)	59,233,991.44	1,032,566.95	-
Investments (Notes 3 and 19)	62,788,620.00	90,452,238.40	3,112,115.00
Accounts, notes, and grants receivable (net) (Note 4)	5,978,249.80	-	-
Pledges receivable (Note 19)	-	5,340,290.95	-
Capital assets (net) (Notes 5 and 19)	295,798,126.05	206,066.00	4,496,706.00
Other assets	-	333,528.64	1,516.00
<b>Total noncurrent assets</b>	<b>423,798,987.29</b>	<b>97,364,690.94</b>	<b>7,610,337.00</b>
<b>Total assets</b>	<b>450,193,034.65</b>	<b>98,036,159.09</b>	<b>26,744,860.00</b>
<b>Deferred outflows of resources</b>			
Deferred amount on debt refunding	7,278,912.35	-	-
Deferred outflows related to pensions (Note 10)	8,213,899.59	-	-
<b>Total deferred outflows of resources</b>	<b>15,492,811.94</b>	<b>-</b>	<b>-</b>
<b>Liabilities</b>			
<b>Current liabilities:</b>			
Accounts payable (Note 7)	3,726,038.45	62,509.23	664,160.00
Accrued liabilities	6,837,723.41	-	2,889,979.00
Due to the university	-	24,824.22	358,230.00
Student deposits	509,510.15	-	-
Unearned revenue	16,017,650.22	-	-
Compensated absences (Notes 8 and 19)	3,098,828.05	-	169,528.00
Accrued interest payable	1,024,379.66	-	-
Long-term liabilities, current portion (Note 8)	5,266,086.02	-	-
Deposits held in custody for others	2,401,135.79	-	571,269.00
Other liabilities	-	-	192,201.00
<b>Total current liabilities</b>	<b>38,881,351.75</b>	<b>87,333.45</b>	<b>4,845,367.00</b>
<b>Noncurrent liabilities:</b>			
Net OPEB obligation (Note 11)	13,033,043.15	-	-
Net pension liability (Note 10)	14,082,883.00	-	-
Compensated absences (Notes 8 and 19)	8,273,017.99	-	678,110.00
Long-term liabilities (Note 8)	147,204,597.72	-	-
Due to grantors (Note 8)	7,695,477.13	-	-
<b>Total noncurrent liabilities</b>	<b>190,289,018.99</b>	<b>-</b>	<b>678,110.00</b>
<b>Total liabilities</b>	<b>229,170,370.74</b>	<b>87,333.45</b>	<b>5,523,477.00</b>
<b>Deferred inflows of resources</b>			
Deferred inflows related to pensions (Note 10)	20,291,248.00	-	-
<b>Total deferred inflows of resources</b>	<b>20,291,248.00</b>	<b>-</b>	<b>-</b>
<b>Net position</b>			
Net investment in capital assets	156,812,109.54	206,066.00	4,496,706.00
Restricted for:			
Nonexpendable:			
Scholarships and fellowships	-	41,787,173.01	-
Research	-	714,774.69	-
Instructional department uses	-	5,465,746.63	-
Other	-	4,922,540.31	-
Expendable:			
Scholarships and fellowships	529,397.72	14,113,857.28	-
Research	255,695.50	354,610.57	-
Instructional department uses	231,291.94	4,501,066.41	-
Loans	457,851.75	-	-
Capital projects	-	6,371,865.20	-
Debt service	3,412,204.57	-	-
Other	1,665,806.24	16,313,974.94	-
Unrestricted	52,859,870.59	3,197,150.60	16,724,677.00
<b>Total net position</b>	<b>\$ 216,224,227.85</b>	<b>\$ 97,948,825.64</b>	<b>\$21,221,383.00</b>

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, 2015**

	University	Component Units	
		East Tennessee State University Foundation	Medical Education Assistance Corporation
<b>Revenues</b>			
Operating revenues:			
Student tuition and fees (net of scholarship allowances of \$42,386,882.61)	\$ 100,940,074.50	\$ -	\$ -
Gifts and contributions	-	7,386,263.00	-
Governmental grants and contracts	26,260,024.92	-	617,055.00
Nongovernmental grants and contracts	8,796,515.98	-	-
Sales and services of educational activities	21,477,395.09	-	-
Sales and services of other activities	8,959,869.70	-	-
Net patient revenues	-	-	37,625,591.00
Auxiliary enterprises:			
Residential life (net of scholarship allowances of \$227,633.63; all residential life revenues are used as security for revenue bonds; see Note 9)	14,065,435.64	-	-
Bookstore	327,984.41	-	-
Food service	716,729.85	-	-
Wellness facility	1,422,071.65	-	-
Other auxiliaries	2,111,430.43	-	-
Interest earned on loans to students	201,517.08	-	-
Other operating revenues, foundation revenues including \$395,500.00 from MEAC	884,681.80	1,005,324.37	503,731.00
<b>Total operating revenues</b>	<b>186,163,731.05</b>	<b>8,391,587.37</b>	<b>38,746,377.00</b>
<b>Expenses</b>			
Operating expenses (Note 15):			
Salaries and wages	160,645,420.92	-	24,951,735.00
Benefits	55,340,010.11	-	2,365,556.00
Utilities, supplies, and other services	60,342,436.78	2,839,723.04	7,727,139.00
Scholarships and fellowships	23,958,670.89	1,682,835.98	-
Depreciation expense	12,770,811.54	-	564,476.00
Payments to or on behalf of East Tennessee State University (Note 19)	-	4,808,773.70	-
<b>Total operating expenses</b>	<b>313,057,350.24</b>	<b>9,331,332.72</b>	<b>35,608,906.00</b>
<b>Operating income (loss)</b>	<b>(126,893,619.19)</b>	<b>(939,745.35)</b>	<b>3,137,471.00</b>
<b>Nonoperating revenues (expenses)</b>			
State appropriations	84,045,000.00	-	-
Gifts, including \$3,241,868.64 from ETSU Foundation and \$2,213,772.00 from MEAC	6,272,533.35	-	-
Grants and contracts	49,955,170.19	-	-
Investment income (net of investment expense for the component units of \$129,735.00)	1,115,096.92	(1,354,068.08)	79,948.00
Interest on capital asset-related debt	(5,303,342.21)	-	(34,524.00)
Interest on noncapital debt	(16,710.15)	-	-
Bond issuance costs	(157,737.83)	-	-
Payments to or on behalf of East Tennessee State University or ETSU Foundation (Note 19)	-	-	(2,609,272.00)
Other nonoperating revenues (expenses)	(125,428.19)	16,647.68	2,300.00
<b>Net nonoperating revenues (expenses)</b>	<b>135,784,582.08</b>	<b>(1,337,420.40)</b>	<b>(2,561,548.00)</b>
<b>Income (loss) before other revenues, expenses, gains, or losses</b>	<b>8,890,962.89</b>	<b>(2,277,165.75)</b>	<b>575,923.00</b>
Capital appropriations	4,833,411.89	-	-
Capital grants and gifts, university gifts including \$1,566,905.06 from ETSU Foundation	1,863,859.40	1,122,370.31	-
Additions to permanent endowments	-	1,774,812.29	-
<b>Total other revenues</b>	<b>6,697,271.29</b>	<b>2,897,182.60</b>	<b>-</b>
<b>Increase in net position</b>	<b>15,588,234.18</b>	<b>620,016.85</b>	<b>575,923.00</b>
Net position - beginning of year, as originally reported	232,911,955.67	97,328,808.79	20,645,460.00
Cumulative effect of a change in accounting principle (Note 18)	(32,275,962.00)	-	-
Net position - beginning of year, restated	200,635,993.67	97,328,808.79	20,645,460.00
<b>Net position - end of year</b>	<b>\$ 216,224,227.85</b>	<b>\$ 97,948,825.64</b>	<b>\$ 21,221,383.00</b>

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, 2015**

<b>Cash flows from operating activities</b>	
Tuition and fees	\$ 99,805,582.19
Grants and contracts	35,646,780.67
Sales and services of educational activities	22,606,767.82
Sales and services of other activities	8,959,869.70
Payments to suppliers and vendors	(58,968,805.72)
Payments to employees	(161,262,877.94)
Payments for benefits	(60,526,908.68)
Payments for scholarships and fellowships	(23,974,417.68)
Loans issued to students	(1,502,300.59)
Collection of loans from students	2,016,033.59
Interest earned on loans to students	137,848.53
Auxiliary enterprise charges:	
Residence halls	13,908,118.06
Bookstore	325,306.07
Food services	698,685.18
Wellness facility	1,422,071.65
Other auxiliaries	2,105,759.81
Other receipts (payments)	993,386.80
<b>Net cash used by operating activities</b>	<b>(117,609,100.54)</b>
<b>Cash flows from noncapital financing activities</b>	
State appropriations	84,025,300.00
Gifts and grants received for other than capital or endowment purposes	56,227,703.54
Federal student loan receipts	97,248,527.50
Federal student loan disbursements	(97,082,234.50)
Changes in deposits held for others	(419,931.44)
Principal paid on noncapital debt	(3,465,976.05)
Interest paid on noncapital debt	(265,555.34)
Other noncapital financing receipts (payments)	1,786.44
<b>Net cash provided by noncapital financing activities</b>	<b>136,269,620.15</b>
<b>Cash flows from capital and related financing activities</b>	
Proceeds from capital debt	76,565,230.95
Capital appropriations	4,833,411.89
Capital grants and gifts received	1,793,859.40
Purchases of capital assets and construction	(7,420,772.63)
Principal paid on capital debt	(75,155,647.02)
Interest paid on capital debt	(7,581,820.21)
Bond issue costs paid on new debt issue	(157,737.83)
<b>Net cash used by capital and related financing activities</b>	<b>(7,123,475.45)</b>
<b>Cash flows from investing activities</b>	
Proceeds from sales and maturities of investments	72,007,396.59
Income on investments	1,311,119.73
Purchase of investments	(72,042,880.00)
<b>Net cash provided by investing activities</b>	<b>1,275,636.32</b>
Net increase in cash	12,812,680.48
Cash - beginning of year	55,312,839.17
<b>Cash - end of year</b>	<b>\$ 68,125,519.65</b>

**Tennessee Board of Regents**  
**EAST TENNESSEE STATE UNIVERSITY**  
**Statement of Cash Flows (continued)**  
**For the Year Ended June 30, 2015**

<b>Reconciliation of operating loss to net cash used by operating activities:</b>	
Operating loss	\$ (126,893,619.19)
Adjustments to reconcile operating loss to net cash used by operating activities:	
Depreciation expense	12,770,811.54
Pension expense	2,098,169.00
Other adjustments	175,700.00
Change in assets, liabilities, and deferred outflows:	
Receivables, net	863,646.63
Inventories	45,600.06
Prepaid expenses	(617,880.59)
Other assets	(63,668.55)
Accounts payable	1,341,624.10
Accrued liabilities	(244,207.93)
Deferred outflows related to pensions	(8,213,899.59)
Net OPEB obligation	167,461.67
Unearned revenues	136,682.58
Deposits	(3,562.52)
Compensated absences	205,604.25
Due to grantors	108,705.00
Loans to students	513,733.00
<b>Net cash used by operating activities</b>	<b>\$ (117,609,100.54)</b>
<b>Noncash investing, capital, or financing transactions</b>	
Gifts of capital assets	\$ 70,000.00
Unrealized losses on investments	\$ (212,603.41)
Loss on disposal of capital assets	\$ (127,214.62)

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

**Tennessee Board of Regents**  
**EAST TENNESSEE STATE UNIVERSITY**  
**Notes to the Financial Statements**  
**June 30, 2015**

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**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 19 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 accordance 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 of the provider's eligibility requirements have been met. All significant internal activity has been eliminated.

## **Notes to the Financial Statements (Continued)**

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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, net of scholarship discounts and allowances; 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 which to use 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 on length of service or classification. Some employees also earn compensatory time.

The amount of the liabilities for annual leave and compensatory time and their related benefits are reported in the statement of net 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, works of art, historical treasures/collections, 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. The capitalization threshold for art, historical treasures/collections, and similar assets is set at \$5,000.

## **Notes to the Financial Statements (Continued)**

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These assets, with the exception of works of art and historical treasures/collections deemed inexhaustible and land, are depreciated/amortized using the straight-line method over the estimated useful lives, which range from 5 to 60 years.

### **Pensions**

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Closed State and Higher Education Employee Pension Plan and the State and Higher Education Employee Retirement Plan in the Tennessee Consolidated Retirement System (TCRS) and additions to/deductions from the plans' fiduciary net position have been determined on the same basis as they are reported by the TCRS. For this purpose, benefits (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms of the Closed State and Higher Education Employee Pension Plan and the State and Higher Education Employee Retirement Plan. Investments are reported at fair value.

### **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; sales and services of 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.

## Notes to the Financial Statements (Continued)

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### 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.

### Note 2. Cash

This classification includes demand deposits and petty cash on hand. At June 30, 2015, cash consisted of \$2,393,761.29 in bank accounts, \$55,000.00 of petty cash on hand, \$60,712,355.34 in the Local Government Investment Pool (LGIP) administered by the State Treasurer, and \$4,964,403.02 in LGIP deposits for capital projects.

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](http://www.treasury.tn.gov).

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 from the LGIP account and transfers them to the Department of Finance and Administration. The funds in the account are not available to the university for any other purpose until the project is completed and the Tennessee Board of Regents releases any remaining funds.

### Note 3. Investments

In accordance with GASB Statement 31, *Accounting and Financial Reporting for Certain Investments and External Investment Pools*, as amended, investments are reported at fair value, including those with a maturity date of one year or less at the time of purchase, unless otherwise noted.

### 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

## **Notes to the Financial Statements (Continued)**

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maturities as a means of managing its exposure to fair-value losses arising from increasing interest rates.

As of June 30, 2015, the university had the following investments and maturities:

<u>Investment Type</u>	<u>Investment Maturities (In Years)</u>	
	<u>Fair Value</u>	<u>1 to 5</u>
U.S. agency obligations	\$62,788,620	\$62,788,620

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### **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; bankers' 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 bankers' acceptances and commercial paper. The policy requires that prime bankers' 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 bankers' 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.

## Notes to the Financial Statements (Continued)

At June 30, 2015, the university's investments were rated as follows:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Credit Quality Rating</u>	
		<u>AA</u>	<u>Unrated</u>
LGIP	\$ 65,676,758.36	\$ -	\$65,676,758.36
U.S. agency obligations	62,788,620.00	62,788,620.00	-
<b>Total</b>	<b>\$128,465,378.36</b>	<b>\$62,788,620.00</b>	<b>\$65,676,758.36</b>

### 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 bankers' acceptances, commercial paper, and money market mutual funds. The policy limits bankers' acceptances to not exceed 20% of the total investments on the date of acquisition and limits the combined amount of bankers' 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:

<u>Issuer</u>	<u>Percentage of Total Investments</u>
	<u>June 30, 2015</u>
Federal Home Loan Bank (FHLB) obligations	18%
Federal National Mortgage Association (FNMA) obligations	6%
Federal Home Loan Mortgage Corporation (FHLMC) obligations	38%
Federal Farm Credit Bank (FFCB) obligations	38%

## Notes to the Financial Statements (Continued)

### Note 4. Receivables

Receivables at June 30, 2015, included the following:

Student accounts receivable	\$ 7,078,416.54
Grants receivable	3,051,805.20
Notes receivable	465,321.68
Clinic receivables	684,753.98
Medical Resident Participation Agreement receivable	2,456,158.33
Other receivables	1,496,576.69
<hr/>	
Subtotal	15,233,032.42
Less allowance for doubtful accounts	3,084,441.30
<hr/>	
Total receivables	<u>\$12,148,591.12</u>

Federal Perkins Loan Program funds at June 30, 2015, included the following:

Perkins loans receivable	\$7,935,869.32
Less allowance for doubtful accounts	2,293,533.92
<hr/>	
Total	<u>\$5,642,335.40</u>

### Note 5. Capital Assets

Capital asset activity for the year ended June 30, 2015, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Transfers</u>	<u>Reductions</u>	<u>Ending Balance</u>
Land	\$ 16,481,720.07	\$ -	\$ -	\$ -	\$ 16,481,720.07
Land improvements and infrastructure	48,443,615.50	-	-	-	48,443,615.50
Buildings	384,251,169.93	-	7,187,838.91	-	391,439,008.84
Equipment	40,270,707.95	2,196,127.10	-	1,165,795.00	41,301,040.05
Library holdings	1,457,125.44	42,775.46	-	187,781.50	1,312,119.40
Intangible assets	4,433,400.78	-	-	-	4,433,400.78
Art and historical collections	23,500.00	-	-	-	23,500.00
Projects in progress	4,065,381.25	5,251,870.07	(7,187,838.91)	-	2,129,412.41
<hr/>					
Total	499,426,620.92	7,490,772.63	-	1,353,576.50	505,563,817.05
<hr/>					
Less accumulated depreciation/amortization:					
Land improvements and infrastructure	20,779,129.55	2,259,689.40	-	-	23,038,818.95

## Notes to the Financial Statements (Continued)

Buildings	147,058,595.06	7,197,349.33	-	-	154,255,944.39
Equipment	25,966,304.85	2,759,803.78	-	1,038,580.37	27,687,528.26
Library holdings	942,311.00	133,147.02	-	187,781.50	887,676.52
Intangible assets	3,474,900.87	420,822.01	-	-	3,895,722.88
<b>Total</b>	<b>198,221,241.33</b>	<b>12,770,811.54</b>	<b>-</b>	<b>1,226,361.87</b>	<b>209,765,691.00</b>
<b>Capital assets, net</b>	<b>\$301,205,379.59</b>	<b>\$(5,280,038.91)</b>	<b>\$</b>	<b>- \$ 127,214.63</b>	<b>\$295,798,126.05</b>

The decrease in the building depreciation expense for the current period is due to a change in accounting estimate. During fiscal year 2015, it was determined that buildings were more appropriately depreciated over a period of between 40 and 60 years, instead of the 40 years previously used. This change resulted in a reduction in depreciation expense of \$4,099,123.15.

### 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 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 \$64,736,029.26. At June 30, 2015, the buildings are reported at \$44,009,146.49, net of accumulated depreciation of \$20,726,882.77.

### Note 7. Accounts Payable

Accounts payable at June 30, 2015, included the following:

## Notes to the Financial Statements (Continued)

Vendors payable	\$2,946,429.68
Unapplied student payments	583.41
Other payables	779,025.36
<hr/>	
Total accounts payable	\$3,726,038.45

### Note 8. Long-term Liabilities

Long-term liabilities activity for the year ended June 30, 2015, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Current Portion</u>
Payables:					
TSSBA debt:					
Bonds	\$140,978,600.69	\$69,395,200.71	\$77,746,320.32	\$132,627,481.08	\$5,266,086.02
Unamortized bond premium	7,360,907.77	11,965,327.16	2,423,374.96	16,902,859.97	-
Revolving credit facility	831,285.32	2,109,057.37	-	2,940,342.69	-
<hr/>					
Subtotal	149,170,793.78	83,469,585.24	80,169,695.28	152,470,683.74	5,266,086.02
<hr/>					
Other liabilities:					
Compensated absences	11,166,241.79	6,719,927.30	6,514,323.05	11,371,846.04	3,098,828.05
Due to grantors	7,586,772.13	108,705.00	-	7,695,477.13	-
<hr/>					
Subtotal	18,753,013.92	6,828,632.30	6,514,323.05	19,067,323.17	3,098,828.05
<hr/>					
Total long-term liabilities	\$167,923,807.70	\$90,298,217.54	\$86,684,018.33	\$171,538,006.91	\$8,364,914.07

### TSSBA Debt – Bonds

Bonds, with interest rates ranging from 0.35% to 5%, were issued by the Tennessee State School Bond Authority (TSSBA). The bonds are due serially to 2043 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 \$2,326,438.24 at June 30, 2015.

Debt service requirements to maturity for the university's portion of TSSBA bonds at June 30, 2015, are as follows:

<u>Year Ending June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2016	\$ 5,266,086.02	\$ 6,172,564.67	\$ 11,438,650.69
2017	5,498,190.31	5,976,390.23	11,474,580.54
2018	4,726,316.76	5,791,758.17	10,518,074.93
2019	4,606,290.88	5,525,339.26	10,131,630.14

## Notes to the Financial Statements (Continued)

2020	6,038,950.53	5,234,006.77	11,272,957.30
2021-2025	31,644,623.65	21,946,527.18	53,591,150.83
2026-2030	27,682,273.28	14,740,342.42	42,422,615.70
2031-2035	22,811,012.53	8,592,762.44	31,403,774.97
2036-2040	17,606,859.12	3,529,460.51	21,136,319.63
2041-2043	6,746,878.00	609,971.47	7,356,849.47
<b>Total</b>	<b>\$132,627,481.08</b>	<b>\$78,119,123.12</b>	<b>\$210,746,604.20</b>

### TSSBA Debt – Revolving Credit Facility

The Tennessee State School Bond Authority (TSSBA) receives loans from the revolving credit facility 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 repays the revolving credit facility debt. The total outstanding loans from the revolving credit facility for the university were \$2,940,342.69 at June 30, 2015.

More detailed information regarding the bonds and revolving credit facility can be found in the notes to the financial statements in the financial report for the TSSBA. That report is available on the state's website at [www.comptroller.tn.gov/tssba/cafr.asp](http://www.comptroller.tn.gov/tssba/cafr.asp).

### Refunding of Debt

On August 7, 2014, the state issued \$41,128,324.17 in revenue bonds with interest rates ranging from 0.35% to 5% to advance refund \$44,344,074.90 of outstanding 2005A, 2008A, 2008B, and 2009A Series bonds with interest rates ranging from 3.75% to 5%. The net proceeds of \$49,345,522.11 (after payment of \$102,540.64 in underwriter's fees and issuance costs) were deposited with an escrow agent to provide for all future debt service payments on the bonds. As a result, the 2005A, 2008A, 2008B, and 2009A Series bonds which were refunded 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 \$4,143,963.02 to be amortized over the next 2 to 18 years, the university in effect reduced its aggregate debt service payments by \$4,482,121.25 over the next 18 years and obtained an economic gain (difference between the present values of the old and new debt service payments) of \$3,254,497.06.

On April 9, 2015, the state issued \$28,266,876.54 in revenue bonds with interest rates ranging from 0.67% to 5% to advance refund \$30,039,025.08 of outstanding 2007C, 2008A, and 2009A Series bonds with interest rates ranging from 4.5% to 5%. The net proceeds of \$33,751,576.15 (after payment of \$62,995.74 in underwriter's fees and issuance costs) were deposited with an escrow agent to provide for all future debt service payments on the bonds. As a result, the 2007C, 2008A, and 2009A Series bonds which were refunded are considered to be defeased, and the liability for those bonds has been removed from the university's long-term liabilities.

## **Notes to the Financial Statements (Continued)**

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Although the advance refunding resulted in the recognition of a deferred loss of \$3,205,909.06 to be amortized over the next 8 to 24 years, the university in effect reduced its aggregate debt service payments by \$3,732,225.22 over the next 24 years and obtained an economic gain (difference between the present values of the old and new debt service payments) of \$1,956,657.22.

### **Note 9. Pledged Revenues**

The university has pledged certain revenues and fees, including state appropriations, to repay \$132,627,481.08 in revenue bonds issued from June 2005 to April 2015 (see Note 8 for further detail). Proceeds from the bonds provided financing for construction and renovation projects. The bonds are payable through 2043. Annual principal and interest payments on the bonds are expected to require 3.95% of available revenues. The total principal and interest remaining to be paid on the bonds is \$210,746,604.20. Principal and interest paid for the current year and total available revenues were \$11,199,110.44 and \$283,795,493.92, respectively. The amount of principal and interest paid for the current year does not include debt of \$74,383,099.98 defeased through bond refunding in fiscal year 2015.

### **Note 10. Pension Plans**

#### **Defined Benefit Plans**

##### **Closed State and Higher Education Employee Pension Plan**

###### *General Information about the Pension Plan*

Plan description – State employees and higher education employees with membership in the Tennessee Consolidated Retirement System (TCRS) before July 1, 2014, are provided with pensions through the Closed State and Higher Education Employee Pension Plan. This plan is a component of the Public Employee Retirement Plan, an agent, multiple-employer defined benefit pension plan. The Closed State and Higher Education Employee Pension Plan stopped accepting new membership on June 30, 2014, but will continue providing benefits to existing members and retirees. Beginning July 1, 2014, a new agent defined benefit retirement plan, the State and Higher Education Employee Retirement Plan, became effective for state employees and higher education employees hired on or after July 1, 2014.

The TCRS was created by state statute under Title 8, Chapters 34-37, *Tennessee Code Annotated*. The TCRS Board of Trustees is responsible for the proper operation and administration of all employer pension plans in the TCRS. The Tennessee Treasury Department, an agency in the legislative branch of state government, administers the plans of the TCRS. The TCRS issues a publicly available financial report that can be obtained at [www.treasury.tn.gov/tcrs](http://www.treasury.tn.gov/tcrs).

## Notes to the Financial Statements (Continued)

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Benefits provided – Title 8, Chapters 34-37, *Tennessee Code Annotated*, establishes the benefit terms and can be amended only by the Tennessee General Assembly. Members of the Closed State and Higher Education Employee Pension Plan are eligible to retire with an unreduced benefit at age 60 with 5 years of service credit or after 30 years of service credit regardless of age. Benefits are determined using the following formula:

$$\begin{array}{l} \text{Average of member's highest} \\ \text{compensation for 5} \\ \text{consecutive years (up to Social} \\ \text{Security integration level)} \end{array} \times 1.50\% \times \begin{array}{l} \text{Years of Service} \\ \text{Credit} \end{array} \times 105\%$$

Plus:

$$\begin{array}{l} \text{Average of member's highest} \\ \text{compensation for 5} \\ \text{consecutive years (over the} \\ \text{Social Security integration} \\ \text{level)} \end{array} \times 1.75\% \times \begin{array}{l} \text{Years of Service} \\ \text{Credit} \end{array} \times 105\%$$

A reduced early retirement benefit is available at age 55 and vested. Members are vested with five years of service credit. Service-related disability benefits are provided regardless of length of service. Five years of service is required for non-service-related disability eligibility. The service-related and non-service-related disability benefits are determined in the same manner as a service retirement benefit but are reduced 10% and include projected service credits. A variety of death benefits are available under various eligibility criteria. Member and beneficiary annuitants are entitled to automatic cost of living adjustments (COLAs) after retirement. A COLA is granted each July for annuitants retired prior to the 2<sup>nd</sup> of July of the previous year. The COLA is based on the change in the consumer price index (CPI) during the prior calendar year, capped at 3%, and applied to the current benefit. No COLA is granted if the change in the CPI is less than 0.5%. A 1% COLA is granted if the CPI change is between 0.5% and 1%. A member who leaves employment may withdraw employee contributions, plus any accumulated interest.

Contributions – Contributions for state employees and higher education employees are established in the statutes governing the TCRS and may only be changed by the Tennessee General Assembly. The university's employees are non-contributory, as are most members in the Closed State and Higher Education Employee Pension Plan. State and higher education agencies make employer contributions at the rate set by the Board of Trustees as determined by an actuarial valuation. By law, employer contributions for the Closed State and Higher Education Employee Pension Plan are required to be paid. Employer contributions by the university for the year ended June 30, 2015, to the Closed State and Higher Education Employee Pension Plan were \$8,121,766.75, which is 15.03% of covered payroll. The employer rate is expected to finance the costs of benefits earned by members during the year and the cost of administration, as well as an amortized portion of any unfunded liability.

## Notes to the Financial Statements (Continued)

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### *Pension Liabilities (Assets), Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions*

Pension liability – At June 30, 2015, the university reported a liability of \$14,082,883 for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2014, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The university's proportion of the net pension liability was based on a projection of the university's contributions during the year ended June 30, 2014, to the pension plan relative to the contributions of all participating state and higher education agencies. At the June 30, 2014, measurement date, the university's proportion was 2.041149%, representing the first-time presentation of this proportion.

Pension expense – For the year ended June 30, 2015, the university recognized a pension expense of \$2,098,169.00.

Deferred outflows of resources and deferred inflows of resources – For the year ended June 30, 2015, the university reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Differences between expected and actual experience	\$ -	\$ 3,038,068.00
Net difference between projected and actual earnings on pension plan investments	-	17,253,180.00
University's contributions subsequent to the measurement date of June 30, 2014	8,121,766.75	-
Total	\$8,121,766.75	\$20,291,248.00

Deferred outflows of resources, resulting from the university's employer contributions of \$8,121,766.75 subsequent to the measurement date will be recognized as a decrease in net pension liability in the year ended June 30, 2016. Other amounts reported as deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year Ended June 30	
2016	\$(5,072,812)
2017	(5,072,812)
2018	(5,072,812)
2019	(5,072,812)

In the table above, positive amounts will increase pension expense, while negative amounts will decrease pension expense.

## Notes to the Financial Statements (Continued)

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Actuarial assumptions – The total pension liability as of the June 30, 2014, actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.0%
Salary increases	Graded salary ranges from 8.97% to 3.71% based on age, including inflation, averaging 4.25%
Investment rate of return	7.5%, net of pension plan investment expenses, including inflation
Cost-of-living adjustment	2.5%

Mortality rates were based on actual experience from the June 30, 2012, actuarial experience study adjusted for some of the expected future improvement in life expectancy.

The actuarial assumptions used in the June 30, 2014, actuarial valuation were based on the results of an actuarial experience study performed for the period July 1, 2008, through June 30, 2012. The demographic assumptions were adjusted to more closely reflect actual and expected future experience.

The long-term expected rate of return on pension plan investments was established by the TCRS Board of Trustees in conjunction with the June 30, 2012, actuarial experience study by considering the following three techniques: (1) the 25-year historical return of the TCRS at June 30, 2012, (2) the historical market returns of asset classes from 1926 to 2012 using the TCRS investment policy asset allocation, and (3) capital market projections that were utilized as a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. Four sources of capital market projections were blended and utilized in the third technique. The blended capital market projection established the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding inflation of 3%. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

<u>Asset Class</u>	<u>Long-term Expected Real Rate of Return</u>	<u>Target Allocation</u>
U.S. equity	6.46%	33%
Developed market international equity	6.26%	17%
Emerging market international equity	6.40%	5%
Private equity and strategic lending	4.61%	8%
U.S. fixed income	0.98%	29%
Real estate	4.73%	7%

## Notes to the Financial Statements (Continued)

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Short-term securities	0.00%	1%
		100%

The long-term expected rate of return on pension plan investments was established by the TCRS Board of Trustees as 7.5% based on a blending of the three factors described above.

Discount rate – The discount rate used to measure the total pension liability was 7.5%. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the current rate and that contributions from all state and higher education agencies will be made at the actuarially determined contribution rate in accordance with the funding policy of the TCRS Board of Trustees and as required to be paid by state statute. Based on those assumptions, the pension plan’s fiduciary net position was projected to be available to make projected future benefit payments of current active and inactive members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the net pension liability (asset) to changes in the discount rate – The following presents the university’s proportionate share of the net pension liability (asset) calculated using the discount rate of 7.5%, as well as what the university’s proportionate share of the net pension liability (asset) would be if it were calculated using a discount rate that is 1 percentage point lower (6.5%) or 1 percentage point higher (8.5%) than the current rate:

	1% Decrease	Current Discount Rate	1% Increase
	<u>(6.5%)</u>	<u>(7.5%)</u>	<u>(8.5%)</u>
University’s net pension liability (asset)	\$48,302,662	\$14,082,883	\$(14,721,244)

Pension plan fiduciary net position – Detailed information about the pension plan’s fiduciary net position is available in a separately issued TCRS financial report at [www.treasury.tn.gov/tcrs](http://www.treasury.tn.gov/tcrs).

### *Payable to the Pension Plan*

At June 30, 2015, the university had no payable to report for the outstanding amount of contributions to the pension plan required for the year ended June 30, 2015.

### **State and Higher Education Employee Retirement Plan**

#### *General Information about the Pension Plan*

Plan description – State employees and higher education employees with membership in the Tennessee Consolidated Retirement System (TCRS) before July 1, 2014, are provided with pensions through the Closed State and Higher Education Employee Pension Plan, an agent plan within the Public Employee Retirement Plan administered by the TCRS. TCRS is a multiple-employer pension plan. The Closed State and Higher Education Employee Pension Plan was

## **Notes to the Financial Statements (Continued)**

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closed effective June 30, 2014, and covers employees hired before July 1, 2014. Employees hired after June 30, 2014, are provided with pensions through a legally separate plan referred to as the State and Higher Education Employee Retirement Plan, an agent plan within the Public Employee Retirement Plan administered by the TCRS. The TCRS was created by state statute under Title 8, Chapters 34-37, *Tennessee Code Annotated*.

Benefits provided – Title 8, Chapters 34-37, *Tennessee Code Annotated*, establishes the benefit terms and can be amended only by the Tennessee General Assembly. Members of the State and Higher Education Employee Retirement Plan are eligible to retire at age 65 with 5 years of service credit or pursuant to the rule of 90 in which the member's age and service credit total 90. Members are entitled to receive unreduced service retirement benefits, which are determined by a formula using the member's highest five consecutive year average compensation and the member's years of service credit. Service-related disability benefits are provided regardless of length of service. Five years of service is required for non-service-related disability eligibility. The service-related and non-service-related disability benefits are determined in the same manner as a service retirement benefit but are reduced 10% and include projected service credits. A variety of death benefits are available under various eligibility criteria. Member and beneficiary annuitants are entitled to automatic cost of living adjustments (COLAs) after retirement. A COLA is granted each July for annuitants retired prior to July 2 of the previous year. The COLA is based on the change in the consumer price index (CPI) during the prior calendar year, capped at 3%, and applied to the current benefit. No COLA is granted if the change in the CPI is less than 0.5%. A 1% COLA is granted if the CPI change is between 0.5% and 1%. A member who leaves employment may withdraw employee contributions, plus any accumulated interest. Under the State and Higher Education Employee Retirement Plan, benefit terms and conditions, including COLA, can be adjusted on a prospective basis. Moreover, there are defined cost controls and unfunded liability controls that provide for the adjustment of benefit terms and conditions on an automatic basis.

Contributions – Contributions for state and higher education employees are established in the statutes governing the TCRS and may only be changed by the Tennessee General Assembly. Employees contribute 5% of their salary. The higher education institutions make employer contributions at the rate set by the Board of Trustees as determined by an actuarial valuation. Per the statutory provisions governing the TCRS, the employer contribution rate cannot be less than 4% for all aggregate employee groups, except in years when the maximum funded level, approved by the TCRS Board of Trustees, is reached. By law, employer contributions for the State and Higher Education Employee Retirement Plan are required to be paid. Employer contributions by the university for the year ended June 30, 2015, to the State and Higher Education Employee Retirement Plan were \$92,132.84, which is 3.87% of covered payroll. The employer rate, when combined with member contributions, is expected to finance the costs of benefits earned by members during the year and the cost of administration, as well as an amortized portion of any unfunded liability.

## **Notes to the Financial Statements (Continued)**

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*Pension Liabilities (Assets), Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions*

Pension liabilities – Since the measurement date is June 30, 2014, which is prior to the July 1, 2014, inception of the State and Higher Education Employee Retirement Plan, there is not a net pension liability to report at June 30, 2015.

Pension expense – Since the measurement date is June 30, 2014, the university did not recognize a pension expense at June 30, 2015.

Deferred outflows of resources and deferred inflows of resources – For the year ended June 30, 2015, the university reported deferred outflows of resources related to pensions from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
University's contributions subsequent to the measurement date of June 30, 2014	\$92,132.84	\$ -

The university's employer contributions of \$92,132.84 reported as pension related deferred outflows of resources, subsequent to the measurement date, will be recognized as a reduction in net pension liability in the year ended June 30, 2016.

### *Payable to the Pension Plan*

At June 30, 2015, the university had no payable to report for the outstanding amount of legally required contributions to the pension plan required for the year ended June 30, 2015.

### **Defined Contribution Plans**

#### **Optional Retirement Plans**

Plan description – The university contributes to the Optional Retirement Plan (ORP). The ORP, administered by the Tennessee Treasury Department, is a defined contribution plan. The ORP was established by state statute in Title 8, Chapter 35, Part 4, of *Tennessee Code Annotated*. This statute also sets out the plan provisions. The plan provisions are amended by the Tennessee General Assembly. The ORP was designed to provide benefits at retirement to faculty and staff who are exempt from the overtime provision of the Fair Labor Standards Act and who waive membership in the TCRS. In a defined contribution plan, benefits depend solely on amounts contributed to the plan plus investment earnings.

Funding policy – For employees employed prior to July 1, 2014, 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. For employees hired after June 30, 2014, plan members will contribute 5% to the ORP and the

## **Notes to the Financial Statements (Continued)**

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university will contribute 9% of the employee's base salary. Pension expense equaled the required contributions made to the ORP of \$7,605,476.87 for the year ended June 30, 2015, and \$7,798,162.13 for the year ended June 30, 2014. Contributions met the requirements for each year.

Members are immediately 100% vested in the employer contributions made pursuant to the ORP. The Treasury Department has selected three investment vendors who offer a variety of investment products in which members are responsible for selecting how the contributions are invested. Each member makes the decision when to reallocate future contributions or when to transfer funds from one investment product to another. Funds are held by the investment vendor in the name of the member, not in the name of the State of Tennessee. The State of Tennessee has no discretion over these funds other than to make the initial contributions. Accordingly, the State of Tennessee is not acting in a trustee capacity, nor does it have a fiduciary responsibility for the funds held by the investment vendors.

### **Deferred Compensation Plans**

Employees are offered three deferred compensation plans. The university, through the State of Tennessee, provides two plans, one established pursuant to IRC, Section 457 and the other pursuant to IRC, Section 401(k). The third plan is administered by the university and was established in accordance with IRC, Section 403(b). The plans are outsourced to third-party vendors and the administrative costs assessed by the vendors of these plans are the responsibility of plan participants. Section 401(k), Section 403(b), and Section 457 plan assets remain the property of the contributing employees; therefore, they are not presented in the accompanying financial statements. IRC Sections 401(k), 403(b), and 457 establish participation, contribution, and withdrawal provisions for the plans. Participation in the 403(b) and the 457 plans are voluntary for employees. The university provides up to a \$50 monthly employer match for employees who participate in the state's 401(k) plan. Employees hired before July 1, 2014, voluntarily participate in the state's 401(k) plan. Pursuant to Public Chapter No. 259 of *Public Acts of 2013*, employees hired after June 30, 2014, are automatically enrolled in the state's 401(k) plan and contribute 2% of their salary, with the employer contributing an additional non-matching 5%. Employees may opt out of the 2% auto enrollment. Such contribution rates may only be amended by the Tennessee General Assembly. There are certain automatic cost controls and unfunded liability controls in the defined benefit plan where the employees participate that may impact the non-matching 5% employer contribution to the 401(k) plan.

Employees are immediately vested in both the employee and employer contributions in all plans. The IRC establishes maximum limits that an employee can contribute to these plans. The employee may increase, decrease, or stop contributions at any time for all three plans.

During the year ended June 30, 2015, contributions totaling \$2,829,199.23 were made by employees participating in the plan, and the university recognized pension expense of \$1,012,878.59 for employer contributions. During the year ended June 30, 2014, contributions totaling \$2,663,478.93 were made by employees participating in the plan, with contributions of \$881,199.99 made by the university.

## Notes to the Financial Statements (Continued)

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### Note 11. Other Postemployment Benefits

Healthcare is the only “other postemployment benefit” (OPEB) provided to employees. The State of Tennessee administers a group health insurance program that 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 8-27-201, *Tennessee Code Annotated*, for the State Employee Group Plan and Section 8-27-701, *Tennessee Code Annotated*, for the Medicare Supplement Plan. Prior to reaching age 65, all members have the option of choosing between the standard or partnership preferred provider organization plan for healthcare benefits. Subsequent to age 65, members who are also in the state’s retirement system may participate in a state-administered Medicare supplement that does not include pharmacy. The state makes on-behalf payments to the Medicare Supplement Plan for the university’s eligible retirees; see Note 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](http://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. 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.

## Notes to the Financial Statements (Continued)

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

Annual Required Contribution (ARC)	\$ 2,917,000.00
Interest on the net OPEB obligation	514,623.25
Adjustment to the ARC	(501,367.11)
<hr/>	
Annual OPEB cost	2,930,256.14
Amount of contribution	(2,762,794.47)
<hr/>	
Increase in net OPEB obligation	167,461.67
Net OPEB obligation – beginning of year	12,865,581.48
<hr/>	
Net OPEB obligation – end of year	\$13,033,043.15

<u>Year-end</u>	<u>Plan</u>	<u>Annual OPEB Cost</u>	<u>Percentage of Annual OPEB Cost Contributed</u>	<u>Net OPEB Obligation at Year-end</u>
June 30, 2015	State Employee Group Plan	\$2,930,256.14	94.3%	\$13,033,043.15
June 30, 2014	State Employee Group Plan	\$2,827,985.26	90.7%	\$12,865,581.48
June 30, 2013	State Employee Group Plan	\$3,454,205.84	74.1%	\$12,602,678.28

### Funded Status and Funding Progress

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

Actuarial valuation date	July 1, 2013
Actuarial accrued liability (AAL)	\$22,189,000.00
Actuarial value of plan assets	-
<hr/>	
Unfunded actuarial accrued liability (UAAL)	\$22,189,000.00
Actuarial value of assets as a percentage of the AAL	0%
Covered payroll (active plan members)	\$108,619,569.26
UAAL as percentage of covered payroll	20.4%

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.

## **Notes to the Financial Statements (Continued)**

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### **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, 2013, 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 healthcare cost trend rate of 7.5% initially. The rate decreased to 7% in fiscal year 2015 and then reduces by decrements to an ultimate rate of 4.19% in fiscal year 2044. All rates include a 2.5% inflation assumption. The unfunded actuarial accrued liability is being amortized as a level percentage of payroll on a closed basis over a 30-year period beginning with July 1, 2007. Payroll is assumed to grow at a rate of 3%.

### **Note 12. Chairs of Excellence**

The university had \$25,929,211.67 on deposit at June 30, 2015, 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 (RMF). 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 RMF. For property coverage, the deductible for an individual state agency is the first \$25,000 of losses. The RMF 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.

## **Notes to the Financial Statements (Continued)**

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The university participates in the RMF. 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, 2015, 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](http://www.tn.gov/finance/act/cafr.shtml). Since the university participates in the RMF, it is subject to the liability limitations established by statute. The maximum liability for general liability, automobile liability, and medical malpractice liability is \$300,000 per person and \$1,000,000 per occurrence. Claims are paid through the state's RMF. At June 30, 2015, the RMF held \$127.9 million in cash designated for payment of claims.

At June 30, 2015, the scheduled coverage for the university was \$849,658,497 for buildings and \$175,351,500 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 \$57,781,585.44 at June 30, 2015.

#### **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 \$572,631.36 for the year ended June 30, 2015. All operating leases are cancelable at the lessee's option.

#### **Construction in Progress**

At June 30, 2015, outstanding commitments under construction contracts totaled \$4,945,169.59 for construction and renovation projects, of which \$520,164.30 will be funded by future state capital outlay appropriations.

## Notes to the Financial Statements (Continued)

### 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, 2015, are as follows:

Functional Classification	Natural Classification					Total
	Salaries	Benefits	Other Operating	Scholarships	Depreciation	
Instruction	\$ 95,497,422.24	\$31,552,301.79	\$15,143,194.74	\$ 953,990.28	\$ -	\$143,146,909.05
Research	4,409,982.82	1,254,789.70	3,144,333.01	7,529.20	-	8,816,634.73
Public service	12,155,092.89	3,924,086.76	6,222,200.53	45,451.69	-	22,346,831.87
Academic support	16,232,673.86	5,960,144.94	4,891,288.53	193,164.35	-	27,277,271.68
Student services	11,577,658.29	4,673,231.88	7,003,140.67	1,511,574.83	-	24,765,605.67
Institutional support	13,003,719.12	4,626,901.76	1,544,387.02	88,119.00	-	19,263,126.90
Maintenance & operation	5,904,999.58	2,740,697.65	15,037,673.91	-	-	23,683,371.14
Scholarships & fellowships	-	-	481,401.86	21,037,500.64	-	21,518,902.50
Auxiliary	1,863,872.12	607,855.63	6,874,816.51	121,340.90	-	9,467,885.16
Depreciation	-	-	-	-	12,770,811.54	12,770,811.54
<b>Total</b>	<b>\$160,645,420.92</b>	<b>\$55,340,010.11</b>	<b>\$60,342,436.78</b>	<b>\$23,958,670.89</b>	<b>\$12,770,811.54</b>	<b>\$313,057,350.24</b>

### 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, 2015, the assets of the foundation totaled \$395,843, liabilities were \$2,356, and the net position amounted to \$393,487.

### Note 17. On-behalf Payments

During the year ended June 30, 2015, the State of Tennessee made payments of \$175,700 on behalf of the university for retirees participating in the Medicare Supplement Plan. The Medicare Supplement Plan is a postemployment benefit healthcare plan and is discussed further in Note 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](http://www.tn.gov/finance/act/cafr.shtml).

## **Notes to the Financial Statements (Continued)**

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### **Note 18. Cumulative Effect of a Change in Accounting Principle**

During fiscal year 2015, the university implemented GASB Statement 68, *Accounting and Financial Reporting for Pensions*, and GASB Statement 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*. These statements establish standards for the measurement, recognition, and display of the net pension liability and related expenses, deferred outflows of resources, deferred inflows of resources, note disclosures, and required supplementary information. The implementation of these statements resulted in a cumulative adjustment to beginning net position of \$(32,275,962). This cumulative adjustment does not include related deferred outflows and deferred inflows of resources.

### **Note 19. 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, 2015, the foundation made distributions of \$4,808,773.70 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, 2015, cash and cash equivalents consisted of \$82,342.51 in bank accounts, \$993,462.76 in the Local Government Investment Pool administered by the State Treasurer, and \$592,655.44 in cash held by others.

The Local Government Investment Pool 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](http://www.treasury.tn.gov).

## Notes to the Financial Statements (Continued)

### Investments

The foundation is authorized to invest funds in accordance with its board of directors' policies. In accordance with GASB Statement 31, *Accounting and Financial Reporting for Certain Investments and External Investment Pools*, as amended, investments are reported at fair value, including those with a maturity date of one year or less at the time of purchase, unless otherwise noted.

**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.

At June 30, 2015, the foundation had the following investments and maturities:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Investment Maturities (in Years)</u>			
		<u>Less than 1</u>	<u>1 to 5</u>	<u>6 to 10</u>	<u>More than 10</u>
Corporate bonds	\$ 3,786,753.00	\$562,873.00	\$3,223,880.00	\$ -	\$ -
Bond mutual funds	18,073,244.00	144,219.00	4,420,301.00	4,389,606.00	9,119,118.00
Certificates of deposit	2,500,803.00				
Equity mutual funds	56,520,839.00				
Hedge fund	9,119,015.40				
Alternative investment	451,584.00				
<b>Total</b>	<b>\$90,452,238.40</b>				

**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, 2015, the foundation's investments were rated as follows:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Credit Quality Rating</u>				
		<u>AAA</u>	<u>AA</u>	<u>A</u>	<u>BBB or Less</u>	<u>Unrated</u>
LGIP	\$ 993,462.76	\$ -	\$ -	\$ -	\$ -	\$993,462.76
Corporate bonds	3,786,753.00	-	310,514.00	3,476,239.00	-	-
Bond mutual funds	18,073,244.00	9,556,685.00	1,355,051.00	2,751,879.00	4,409,629.00	-
<b>Total</b>	<b>\$22,853,459.76</b>	<b>\$9,556,685.00</b>	<b>\$1,665,565.00</b>	<b>\$6,228,118.00</b>	<b>\$4,409,629.00</b>	<b>\$993,462.76</b>

## Notes to the Financial Statements (Continued)

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

	<u>June 30, 2015</u>
Mutual funds	\$68,292,767.00
Corporate bonds	3,786,753.00
Cash held by others	13,651.00
Certificates of deposit	250,630.00
<hr/>	
Total	\$72,343,801.00

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, 2015, each having a fair value of \$1.1417575585, 64,418,563.23 units were owned by endowments, and 265,922.45 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, 2015:

	<u>Pooled Assets</u>		Net Gains <u>(Losses)</u>	Fair Value <u>Per Unit</u>
	<u>Fair Value</u>	<u>Cost</u>		
End of year	\$90,452,238.00	\$85,275,845.00	\$ 5,176,393.00	\$1.1417575585
Beginning of year	\$93,183,257.00	\$82,384,911.00	<u>10,798,346.00</u>	\$1.1300189213
Unrealized net losses			(5,621,953.00)	
Realized net gains			<u>2,045,761.00</u>	
Total net losses			<u>\$(3,576,192.00)</u>	

The average annual earnings per unit, exclusive of net gains, were \$0.027 for the year ended June 30, 2015.

### Pledges Receivable

Pledges receivable at June 30, 2015, are summarized below, net of the allowance for doubtful accounts:

## Notes to the Financial Statements (Continued)

Current pledges	\$1,090,935.00
Pledges due in one to five years	3,406,109.00
Pledges due after five years	1,149,050.00
Subtotal	5,646,094.00
Less allowance for doubtful accounts	84,939.00
Less discounts to net present value	220,864.05
Total pledges receivable, net	\$5,340,290.95

### Capital Assets

Capital asset activity for the year ended June 30, 2015, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Land	\$196,580.00	\$ -	\$ -	\$196,580.00
Buildings	59,000.00	-	-	59,000.00
Equipment	9,486.00	-	-	9,486.00
Total	265,066.00	-	-	265,066.00
Less accumulated depreciation:				
Buildings	59,000.00	-	-	59,000.00
Capital assets, net	\$206,066.00	\$ -	\$ -	\$206,066.00

### Endowments

The ETSU Foundation's endowment consists of 510 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, and (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. 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

## **Notes to the Financial Statements (Continued)**

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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, 2015, net appreciation of \$14,654,251.00 is available to be spent, of which \$6,826,518.00 is included in restricted net position expendable for scholarships and fellowships, \$103,346.00 is included in restricted net position expendable for research, \$891,688.00 is

## **Notes to the Financial Statements (Continued)**

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included in restricted net position expendable for instructional departmental uses, and \$6,832,699.00 is included in restricted net position expendable for other purposes.

### **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, 2015, MEAC made distributions of \$2,609,272 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, 2015, cash consisted of \$8,518,763 in bank accounts, \$2,150 of petty cash on hand, and \$84,881 in the 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 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](http://www.treasury.tn.gov).

### **Investments**

The corporation is authorized to invest funds in accordance with its board of directors' policies. In accordance with GASB Statement 31, *Accounting and Financial Reporting for Certain Investments and External Investment Pools*, as amended, investments are reported at fair value, including those with a maturity date of one year or less at the time of purchase, unless otherwise noted. The corporation's investments at June 30, 2015, consisted of bonds and certificates of deposit with original maturities of greater than three months.

**Interest Rate Risk** – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of a debt investment. MEAC 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.

## Notes to the Financial Statements (Continued)

At June 30, 2015, MEAC had the following investments and maturities:

<u>Investment Type</u>	<u>Investment Maturities (In Years)</u>		
	<u>Fair Value</u>	<u>Less than 1</u>	<u>1 to 5</u>
U.S. agency obligations	\$3,000,000.00	\$1,000,000.00	\$2,000,000.00
Certificates of deposit	6,377,115.00		
<b>Total</b>	<b>\$9,377,115.00</b>		

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

At June 30, 2015, the corporation’s investments were rated as follows:

<u>Investment Type</u>	<u>Credit Quality Rating</u>		
	<u>Fair Value</u>	<u>AA</u>	<u>Unrated</u>
LGIP	\$ 84,881.00	\$ -	\$84,881.00
U.S. agency obligations	3,000,000.00	3,000,000.00	-
<b>Total</b>	<b>\$3,084,881.00</b>	<b>\$3,000,000.00</b>	<b>\$84,881.00</b>

### Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of the corporation’s investment in a single issuer. The corporation places no limit on the amount it may invest in any one issuer.

At June 30, 2015, more than 5% of the corporation’s investments were invested in the following single issuers:

<u>Issuer</u>	<u>Percentage of Total Investments</u>
	<u>June 30, 2015</u>
Federal Home Loan Bank (FHLB) obligations	22%
Federal National Mortgage Association (FNMA) obligations	11%

## Notes to the Financial Statements (Continued)

### Receivables

Receivables at June 30, 2015, included the following:

Patient accounts receivable, net	\$2,841,456
Other receivables	1,143,037
<hr/>	
Total	\$3,984,493

### Capital Assets

Capital asset activity for the year ended June 30, 2015, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Land	\$ 18,150	\$ -	\$ -	\$ 18,150
Buildings	4,902,488	-	-	4,902,488
Leasehold improvements	679,409	43,347	12,678	710,078
Equipment	4,302,616	128,141	64,104	4,366,653
<hr/>				
Total	9,902,663	171,488	76,782	9,997,369
<hr/>				
Less accumulated depreciation:				
Buildings	882,843	150,352	-	1,033,195
Leasehold improvements	509,660	68,066	12,678	565,048
Equipment	3,620,466	346,058	64,104	3,902,420
<hr/>				
Total	5,012,969	564,476	76,782	5,500,663
<hr/>				
Capital assets, net	\$4,889,694	(\$392,988)	\$ -	\$4,496,706

### Long-term Liabilities

Long-term liabilities activity for the year ended June 30, 2015, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Current Portion</u>
Note payable	\$1,447,791	\$ -	\$1,447,791	\$ -	\$ -
Compensated absences	816,640	30,998	-	847,638	169,528
<hr/>					
Total long-term liabilities	\$2,264,431	\$30,998	\$1,447,791	\$847,638	\$169,528

### Note Payable

MEAC had an obligation with Bank of Tennessee collateralized by 4 Sheridan Square, Unit 2, Kingsport, TN 37660. The note was paid in full in November 2014.

## **Notes to the Financial Statements (Continued)**

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### **Capital Lease Between MEAC and the University**

In 2008, MEAC entered into an agreement to lease a clinical education building from the university for 30 years at a rate equivalent to the cost of construction of the building, which was \$2,942,255. The entire lease obligation was paid in 2009 upon the completion of construction. The agreement is currently being treated as a capital lease. Because there is no remaining obligation, no capital lease obligation has been reported by MEAC, and no capital lease receivable has been reported by the university.

### **Note 20. Prior-period Reclassification**

At June 30, 2014, in calculating net investment in capital assets, the university incorrectly netted noncapital debt related to energy savings projects against net investment in capital assets. The debt should have been netted against unrestricted net position. Therefore, at June 30, 2014, net investment in capital assets was understated by \$6,510,479.15, and unrestricted net position was overstated by \$6,510,479.15. Total net assets on the statement of net position were correctly reported. The error was corrected in the university's June 30, 2015, financial statements.

**Tennessee Board of Regents  
EAST TENNESSEE STATE UNIVERSITY  
Required Supplementary Information  
OPEB Schedule of Funding Progress**

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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, 2013	State Employee Group Plan	\$ -	\$22,189,000	\$22,189,000	0%	\$108,619,569	20.43%
July 1, 2011	State Employee Group Plan	\$ -	\$28,137,000	\$28,137,000	0%	\$100,388,162	28.03%
July 1, 2010	State Employee Group Plan	\$ -	\$39,835,000	\$39,835,000	0%	\$97,197,256	40.98%

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**  
**Required Supplementary Information**  
**Schedule of East Tennessee State University's Proportionate Share**  
**of the Net Pension Liability**  
**Closed State and Higher Education Employee Pension Plan within TCRS**

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	2014
University's proportion of the net pension liability	2.041149%
University's proportionate share of the net pension liability	\$14,082,883
University's covered-employee payroll	\$55,762,565
University's proportionate share of the net pension liability as a percentage of its covered-employee payroll	25.26%
Plan fiduciary net position as a percentage of the total pension liability	95.11%

- 1) To correspond with the measurement date, the amounts presented were determined as of June 30 of the prior fiscal year.
  
- 2) This is a ten-year schedule; however, the information in this schedule is not required to be presented retroactively. Years will be added to this schedule in future years until ten years of information is available.

**Tennessee Board of Regents**  
**East Tennessee State University**  
**Required Supplementary Information**  
**Schedule of East Tennessee State University's Contributions**  
**Closed State and Higher Education Employee Pension Plan within TCRS**

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	2014	2015
Contractually determined contribution	\$ 8,381,113	\$ 8,121,767
Contributions in relation to the contractually determined contribution	8,381,113	8,121,767
Contribution deficiency (excess)	\$ -	\$ -
Covered-employee payroll	\$55,762,565	\$54,038,562
Contributions as a percentage of covered-employee payroll	15.03%	15.03%

This is a ten-year schedule; however, the information in this schedule is not required to be presented retroactively. Years will be added to this schedule in future fiscal years until ten years of information is available.

**Tennessee Board of Regents**  
**East Tennessee State University**  
**Required Supplementary Information**  
**Schedule of East Tennessee State University's Contributions**  
**State and Higher Education Employee Retirement Plan within TCRS**

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	2015
Contractually determined contribution	\$ 92,133
Contributions in relation to the contractually determined contribution	92,133
Contribution deficiency (excess)	\$ -
Covered-employee payroll	\$2,379,157
Contributions as a percentage of covered-employee payroll	3.87%

This is a ten-year schedule; however, the information in this schedule is not required to be presented retroactively. Years will be added to this schedule in future fiscal years until ten years of information is available.

**Tennessee Board of Regents**  
**EAST TENNESSEE STATE UNIVERSITY**  
**Supplementary Schedule of Cash Flows - East Tennessee State University Foundation**  
**For the Year Ended June 30, 2015**

<b>Cash flows from operating activities</b>	
Gifts and contributions	\$ 2,458,331.30
Payments to suppliers and vendors	(2,625,018.04)
Payments for scholarships and fellowships	(1,682,835.98)
Payments to or on behalf of ETSU	(4,808,773.70)
Other receipts (payments)	1,005,324.37
<b>Net cash used by operating activities</b>	<b>(5,652,972.05)</b>
<b>Cash flows from noncapital financing activities</b>	
Private gifts for endowment purposes	1,774,812.29
<b>Net cash provided by noncapital financing activities</b>	<b>1,774,812.29</b>
<b>Cash flows from capital and related financing activities</b>	
Capital grants and gifts received	1,122,370.31
<b>Net cash provided by capital and related financing activities</b>	<b>1,122,370.31</b>
<b>Cash flows from investing activities</b>	
Proceeds from sales and maturities of investments	12,530,277.60
Income on investments	4,338,812.49
Purchases of investments	(15,479,921.15)
<b>Net cash provided by investing activities</b>	<b>1,389,168.94</b>
Net decrease in cash and cash equivalents	(1,366,620.51)
Cash and cash equivalents - beginning of year	3,035,081.22
<b>Cash and cash equivalents - end of year</b>	<b>\$ 1,668,460.71</b>
<b>Reconciliation of operating loss to net cash used by operating activities:</b>	
Operating loss	\$ (939,745.35)
Adjustments to reconcile operating loss to net cash used by operating activities:	
Change in assets and liabilities:	
Receivables	(4,705,976.01)
Accounts payable	(7,250.69)
<b>Net cash used by operating activities</b>	<b>\$ (5,652,972.05)</b>
<b>Noncash investing, capital, or financing transactions</b>	
Unrealized losses on investments	\$ (5,621,952.86)

**Tennessee Board of Regents**  
**EAST TENNESSEE STATE UNIVERSITY**  
**Supplementary Schedule of Cash Flows - Medical Education Assistance Corporation**  
**For the Year Ended June 30, 2015**

<b>Cash flows from operating activities</b>	
Collections from patient charges	\$ 37,415,437.00
Grants and contracts	617,055.00
Payments to employees	(24,654,272.00)
Payments for benefits	(2,365,556.00)
Payments to suppliers and vendors	(7,546,403.00)
Other receipts (payments)	292,210.00
<b>Net cash provided by operating activities</b>	<b>3,758,471.00</b>
<b>Cash flows from noncapital financing activities</b>	
Payments to or on behalf of ETSU or ETSU Foundation	(2,609,272.00)
<b>Net cash used by noncapital financing activities</b>	<b>(2,609,272.00)</b>
<b>Cash flows from capital and related financing activities</b>	
Proceeds from sale of capital assets	500.00
Purchases of capital assets and construction	(171,488.00)
Principal paid on note payable	(1,447,790.00)
Interest paid on note payable	(34,524.00)
<b>Net cash used by capital and related financing activities</b>	<b>(1,653,302.00)</b>
<b>Cash flows from investing activities</b>	
Proceeds from sales and maturities of investments	9,313,536.00
Income on investments	79,948.00
Purchases of investments	(8,112,115.00)
Other investing receipts (payments)	1,800.00
<b>Net cash provided by investing activities</b>	<b>1,283,169.00</b>
Net increase in cash	779,066.00
Cash - beginning of year	7,826,728.00
<b>Cash - end of year</b>	<b>\$ 8,605,794.00</b>

<b>Reconciliation of operating gain to net cash provided by operating activities:</b>	
Operating gain	\$ 3,137,471.00
Adjustments to reconcile operating gain to net cash provided by operating activities:	
Depreciation expense	564,476.00
Changes in assets and liabilities:	
Receivables	(308,146.00)
Due from the university	70,437.00
Prepaid expenses	59,948.00
Other assets	1,234.00
Accounts payable	116,437.00
Accrued liabilities	269,581.00
Due to the university	(247,871.00)
Compensated absences	30,998.00
Deposits	63,906.00
<b>Net cash provided by operating activities</b>	<b>\$ 3,758,471.00</b>



STATE OF TENNESSEE  
COMPTROLLER OF THE TREASURY  
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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, 2015, and the related notes to the financial statements, which collectively comprise the university's basic financial statements, and have issued our report thereon dated December 11, 2015. 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 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, CPA  
Director  
December 11, 2015