AUDIT REPORT

Tennessee Sports Hall of Fame

For the Year Ended
December 31, 2005

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

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John G. Morgan
Comptroller

January 23, 2007

The Honorable Phil Bredesen, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and
Board of Directors
Tennessee Sports Hall of Fame
Nashville, Tennessee 37203

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Tennessee Sports Hall of Fame for the year ended December 31, 2005. You will note from the independent auditor's report that an unqualified opinion was given on the fairness of the presentation of the financial statements.

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

Sincerely,

John G. Morgan
Comptroller of the Treasury

JGM/th
07/011

State of Tennessee

Audit Highlights

Comptroller of the Treasury — Division of State Audit

Financial and Compliance Audit
Tennessee Sports Hall of Fame
For the Year Ended December 31, 2005

AUDIT OBJECTIVES

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

AUDIT COMMITTEE

On May 19, 2005, the Tennessee General Assembly enacted legislation known as the "State of Tennessee Audit Committee Act of 2005." This legislation requires the creation of audit committees for those entities that have governing boards, councils, commissions, or equivalent bodies that can hire and terminate employees and/or are responsible for the preparation of financial statements. Entities, pursuant to the act, are required to appoint the audit committee and develop an audit committee charter in accordance with the legislation. The ongoing responsibilities of an audit committee include, but are not limited to:

1. overseeing the financial reporting and related disclosures, especially when financial statements are issued;
2. evaluating management's assessment of risk and the agency's system of internal controls;
3. formally reiterating, on a regular basis, to the board, agency management, and staff their responsibility for preventing, detecting, and reporting fraud, waste, and abuse;
4. serving as a facilitator of any audits or investigations of the agency, including advising auditors and investigators of any information it may receive pertinent to audit or investigative matters;

5. informing the Comptroller of the Treasury of the results of assessments and controls to reduce the risk of fraud; and
6. promptly notifying the Comptroller of the Treasury of any indications of fraud.

The Board of Directors of the Tennessee Sports Hall of Fame created a five-person audit committee on February 24, 2006. However, as of August 4, 2006, the audit committee has not met, nor has a charter been created.

In meeting their responsibilities, the audit committee should ensure that management conducts regular periodic risk assessments. The risk assessment to be performed and documented by top management should include risks of fraud, waste, and abuse to the agency.

INTERNAL CONTROL FINDING

Management of the Tennessee Sports Hall of Fame Has Not Completed a Risk Assessment, and the Board Does Not Have a Functioning Audit Committee as Required by State Law
The requirements of the State of Tennessee Audit Committee Act of 2005 include the creation of an audit committee as a standing committee of a state governing board, council, commission, or equivalent body; and the adoption of an audit committee charter addressing the committee's purpose, powers, duties, and mission. The Act also prescribes certain responsibilities of the audit committee which include evaluating management's assessments of the body's system of internal controls. Management has not completed a risk assessment, and the Board of Directors of the Tennessee Sports Hall of Fame does not have a functioning audit committee (page 10).

OPINION ON THE FINANCIAL STATEMENTS

The opinion on the financial statements is unqualified.

Audit Report
Tennessee Sports Hall of Fame
For the Year Ended December 31, 2005

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Tennessee Sports Hall of Fame
For the Year Ended December 31, 2005

INTRODUCTION

POST-AUDIT AUTHORITY

This is a report on the financial and compliance audit of the Tennessee Sports Hall of Fame. The audit was conducted pursuant to Section 4-3-5405, *Tennessee Code Annotated*, which states, "All annual reports and all books of accounts and financial records of the hall of fame shall be subject to audit annually by the comptroller of the treasury."

BACKGROUND

The Tennessee Sports Hall of Fame was created in 1994 by the General Assembly under Section 4-3-5402, *Tennessee Code Annotated*. The purpose of the Hall of Fame is to honor athletes, athletic teams, and other sports personalities of Tennessee.

ORGANIZATION

The Tennessee Sports Hall of Fame is governed by a 25-member board of directors. Eight members are appointed by the Governor, eight by the Lieutenant Governor, and eight by the Speaker of the House of Representatives. The State Treasurer or his designee serves *ex officio*.

AUDIT SCOPE

The audit was limited to the period January 1, 2005, through December 31, 2005, and was conducted in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Financial statements are presented for the year ended December 31, 2005, and for comparative purposes, the year ended December 31, 2004.

OBJECTIVES OF THE AUDIT

The objectives of the audit were

1. to consider the Tennessee Sports Hall of Fame's internal control over financial reporting to determine auditing procedures for the purpose of expressing an opinion on the financial statements;

2. to determine compliance with certain provisions of laws, regulations, contracts, and grant agreements;

3. to determine the fairness of the presentation of the financial statements; and

4. to recommend appropriate actions to correct any deficiencies.

PRIOR AUDIT FINDINGS

Section 8-4-109, *Tennessee Code Annotated*, requires that each state department, agency, or institution report to the Comptroller of the Treasury the action taken to implement the recommendations in the prior audit report. The Tennessee Sports Hall of Fame filed its report with the Department of Audit on June 28, 2006. A follow-up of all prior audit findings was conducted as part of the current audit.

The current audit disclosed that the Tennessee Sports Hall of Fame has corrected all previous audit findings concerning (1) bank reconciliations not being reviewed, (2) revenue reconciliations not always being performed, (3) the credit card policy not always being followed, and (4) disbursements not always being properly approved.

OBSERVATIONS AND COMMENTS

MANAGEMENT'S RESPONSIBILITY FOR RISK ASSESSMENT

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

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

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

FRAUD CONSIDERATIONS

Statement on Auditing Standards No. 99, *Consideration of Fraud in a Financial Statement Audit,* promulgated by the American Institute of Certified Public Accountants requires auditors to specifically assess the risk of material misstatement of an audited entity's financial statements due to fraud. The standard also restates the obvious premise that management, not the auditors, is primarily responsible for preventing and detecting fraud in its own entity. Management's responsibility is fulfilled in part when it takes appropriate steps to assess the risk of fraud within the entity and to implement adequate internal controls to address the results of those risk assessments.

During our audit, we discussed these responsibilities with management and how management might approach meeting them. We also increased the breadth and depth of our inquiries of management and others in the entity as we deemed appropriate. We obtained formal assurances from top management that management had reviewed the entity's policies and procedures to ensure that they are properly designed to prevent and detect fraud and that management had made changes to the policies and procedures where appropriate. Top management further assured us that all staff had been advised to promptly alert management of all allegations of fraud, suspected fraud, or detected fraud and to be totally candid in all communications with the auditors. All levels of management assured us there were no known instances or allegations of fraud that were not disclosed to us.

AUDIT COMMITTEE

As a result of the fraud-related business failures of companies such as Enron and WorldCom in recent years, Congress and the accounting profession have taken aggressive measures to try to detect and prevent future failures related to fraud. These measures have included the signing of the *Sarbanes-Oxley Act of 2002* by the President of the United States and the issuance of Statement on Auditing Standards No. 99 by the American Institute of Certified Public Accountants. This new fraud auditing standard has not only changed the way auditors perform audits but has also provided guidance to management and boards of directors on creating antifraud programs and controls. This guidance has included the need for an independent audit committee.

In the previous audit report, we recommended that the Tennessee Sports Hall of Fame establish an audit committee. The board chair of the Tennessee Sports Hall of Fame appointed a five-member committee in February 2006. However, as of the end of our audit, the audit committee was not fully functional and had no charter. In recognition of the benefits of audit committees for government, the Tennessee General Assembly has enacted legislation known as the "State of Tennessee Audit Committee Act of 2005." This legislation requires the creation of audit committees for those entities that have governing boards, councils, commissions, or equivalent bodies that can hire and terminate employees and/or are responsible for the preparation of financial statements. Applicable entities are required to develop an audit committee charter and appoint the audit committee in accordance with the legislation. The specific activities of any audit committee will depend on, among other things, the mission, nature, structure, and size of each agency. In establishing the audit committee and creating its charter, each board should examine its agency's particular circumstances. Anti-fraud literature notes that there are two categories of fraud: fraudulent financial reporting and misappropriation of assets. The audit committee should consider the risks of fraud in its agency in general as well as the history of its particular agency with regard to prior audit findings, previously disclosed weaknesses in internal control, and compliance issues. The audit committee should consider both the risk of fraudulent financial reporting and the risk of fraud due to misappropriation or abuse of agency assets.

Boards should exercise professional judgment in establishing the duties, responsibilities, and authority of their audit committee. The factors noted below are not intended to be an exhaustive listing of those matters to be considered. The committee should not limit its scope to reacting to a preconceived set of issues and actions but rather should be proactive in its oversight of the agency as it concentrates on the internal control and audit-related activities of the entity. In fact, this individualized approach is one of the main benefits derived from an audit committee.

At a minimum, audit committees should:

1. Develop a written charter that addresses the audit committee's purpose and mission, which should be, at a minimum, to assist the board in its oversight of the agency.

2. Formally reiterate, on a regular basis, to the board, agency management, and staff their responsibilities for preventing, detecting, and reporting fraud, waste, and abuse.

3. Serve as a facilitator of any audits or investigations of the agency, including advising auditors and investigators of any information they may receive or otherwise note regarding risks of fraud or weaknesses in the agency's internal controls; reviewing with the auditors any findings or other matters noted by the auditors during audit engagements; working with the agency management and staff to ensure implementation of audit recommendations; and assisting in the resolution of any problems the auditors may have with cooperation from agency management or staff.

4. Develop a formal process for assessing the risk of fraud at the agency, including documentation of the results of the assessments and assuring that internal controls are in place to adequately mitigate those risks.

5. Develop and communicate to staff of the agency their responsibilities to report allegations of fraud, waste, or abuse at the agency to the committee and the Comptroller of the Treasury's Office as well as a process for immediately reporting such information.

6. Immediately inform the Comptroller's Office when fraud is detected.

7. Develop and communicate to the board, agency management, and staff a written code of conduct reminding those individuals of the public nature of the agency and the need for all to maintain the highest level of integrity with regard to the financial operations and any related financial reporting responsibilities of the agency; to avoid preparing or issuing fraudulent or misleading financial reports or other information; to protect agency assets from fraud, waste, and abuse; to comply with all relevant laws, rules, policies, and procedures; and to avoid engaging in activities which would otherwise bring dishonor to the agency.

The charter of the audit committee should include, at a minimum, the following provisions:

1. The audit committee should be a standing committee of the board.

2. The audit committee should be composed of at least three members. The chair of the audit committee should preferably have some accounting or financial management background. Each member of the audit committee should have an adequate background and education to allow a reasonable understanding of the information

presented in the financial reports of the agency and the comments of auditors with regard to internal control and compliance findings and other issues.

3. The members of the audit committee must be independent from any appearances of other interests that are in conflict with their duties as members of the audit committee.

4. An express recognition that the board, the audit committee, and the management and staff of the agency are responsible for taking all reasonable steps to prevent, detect, and report fraud, waste, and abuse.

5. The audit committee should meet regularly throughout the year. The audit committee can meet by telephone, if that is permissible for other committees. However, the audit committee is strongly urged to meet at least once a year in person. Members of the audit committee may be members of other standing committees of the board, but the audit committee meetings should be separate from the meetings of other committees of the board.

6. The audit committee should record minutes of its meetings.

The Division of State Audit will be available to discuss with the board any questions it might have about the creation of its particular audit committee. There are also other audit committees which have already been established at other state agencies that the board may wish to contact for advice and further information.

RESULTS OF THE AUDIT

AUDIT CONCLUSIONS

Internal Control

As part of the audit of the Tennessee Sports Hall of Fame's financial statements for the year ended December 31, 2005, we considered internal control over financial reporting to determine auditing procedures for the purpose of expressing an opinion on the financial statements, as required by auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. A reportable condition, along with the recommendation and management's response, is detailed in the Finding and Recommendation section of this report. Consideration of internal control over financial reporting disclosed no material weaknesses.

Compliance and Other Matters

The results of our audit tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Fairness of Financial Statement Presentation

The Division of State Audit has rendered an unqualified opinion on the Tennessee Sports Hall of Fame's financial statements.

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

August 25, 2006

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

We have audited the financial statements of the Tennessee Sports Hall of Fame as of and for the year ended December 31, 2005, and have issued our report thereon dated August 25, 2006. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Tennessee Sports Hall of Fame's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Tennessee Sports Hall of Fame's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

The following reportable condition was noted: management of the Tennessee Sports Hall of Fame has not completed a risk assessment, and the board does not have a functioning audit committee as required by state law. This condition is described in the Finding and Recommendation section of this report.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we do not believe that the reportable condition described above is a material weakness.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Tennessee Sports Hall of Fame's financial statements are free of material misstatement, we determined that there were no compliance requirements related to 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. Therefore, we did not test for compliance with laws, regulations, contracts, and grant agreements.

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

Sincerely,

Arthur A. Hayes, Jr., CPA
Director

AAH/th

FINDING AND RECOMMENDATION

Management of the Tennessee Sports Hall of Fame has not completed a risk assessment, and the board does not have a functioning audit committee as required by state law

Finding

Management of the Tennessee Sports Hall of Fame (TSHF) has not completed a risk assessment, and the Board of Directors of the TSHF does not have a functioning audit committee as required by the "State of Tennessee Audit Committee Act of 2005," Section 4-35-101 et seq., *Tennessee Code Annotated*. The requirements of the State of Tennessee Audit Committee Act of 2005 include the creation of an audit committee as a standing committee of a state governing board, council, commission, or equivalent body; and the adoption of an audit committee charter addressing the committee's purpose, powers, duties, and mission. The Act also prescribes certain responsibilities of the audit committee which include:

a. overseeing the financial reporting and related disclosures, especially when financial statements are issued;
b. evaluating management's assessments of the body's system of internal controls;
c. formally reiterating, on a regular basis, to the governing board and management their responsibility for preventing, detecting, and reporting fraud, waste, and abuse;
d. serving as a facilitator of any audits or investigations of the entity, including advising auditors and investigators of any information it may receive pertinent to audit or investigative matters;
e. informing the Comptroller of the Treasury of the results of risk assessments and controls to reduce the risk of fraud;
f. promptly notifying the Comptroller of the Treasury of any indications of fraud; and
g. . . . establish[ing] a process by which employee . . . or . . . citizens may confidentially report suspected illegal, improper, wasteful, or fraudulent activity.

Furthermore, the Act requires the Comptroller of the Treasury to establish guidelines for the creation of an audit committee charter. Those guidelines require the creation or review by the audit committee of a code of conduct and conflict-of-interest policy for the entity.

The Board of Directors of the TSHF did create a five-person audit committee on February 24, 2006. However, as of August 4, 2006, there have been no further actions taken. The audit committee has not met, nor has a charter been created. As a result, the Board of Directors of the TSHF is operating in violation of state law.

As previously stated, one of the audit committee's responsibilities is to evaluate management's assessment of internal controls. This responsibility is of paramount importance, as is the responsibility of management to perform this assessment. However, as of August 4, 2006, management of the TSHF has not performed and documented a risk assessment.

All organizations, regardless of their size or nature, are vulnerable to fraud, waste, and abuse. And so, in all organizations, not just those subject to the Audit Committee Act, management is required by basic tenets of internal control to assess the risk of fraud in the operations of the entity. The risk assessment is based on a critical review of operations considering what fraud could be perpetrated in the absence of adequate controls. The risk assessment by management is the primary method by which the entity is protected from fraud, waste, and abuse. Consideration should be given to the fact that risks of fraud do not just originate at the beginning or end of an entity's fiscal year. Since the operating environment is dynamic, management's assessment should be an ongoing part of the daily operations of the entity.

Risks of fraud, waste, and abuse are mitigated by effective internal controls. It is management's responsibility to design, implement, and monitor effective controls in the entity. This too should be an ongoing process.

Recommendation

Management should conduct regular periodic risk assessments. Each assessment should be well documented, complete, and clear. The process should involve the active participation of staff; however, management is ultimately responsible for the results of the assessment.

The risk assessment should include consideration of the risks of fraud, waste, and abuse related to the TSHF. Management should begin with prior audit findings, ensuring that corrective actions recommended by the auditors have been fully implemented. Management should also think about the general types of problems that can occur, such as conflicts of interest in the procurement processes, overbillings, and theft of funds. The relative materiality of the risks should be considered as well. The results of the risk assessment should be used by management to design appropriate internal controls to mitigate the identified risks. As such, the risks should be prioritized, so that management can focus initially on the greatest risks.

The audit committee should meet and create a charter based on guidelines from the Comptroller of the Treasury. Once completed, the charter should be submitted to the Comptroller for review and approval.

The audit committee should review, evaluate, and approve management's risk assessment and internal controls. In doing so, the audit committee should take whatever steps necessary, including meeting with management, to obtain a sufficient understanding of the assessment. The committee should independently determine that the risk assessment is adequate and appropriate.

Members of the committee should formally sign off on the documentation, acknowledging their approval of the assessment. In addition, they should document both their discussion with management and their comments about the risk assessment.

During the next audit, the auditors will review the risk assessment documentation prepared by management and approved by the audit committee. The results of this review will be part of the basis of the auditors' conclusions about the control environment of the entity.

Management's Comment

Management concurs with the finding above. Management will conduct a risk assessment of the TSHF to be reviewed and approved by the acting audit committee of the TSHF. This assessment will be conducted on a periodic basis to provide the audit committee an opportunity to review and evaluate the operations of the TSHF. To date, an audit committee charter has been drafted and is awaiting approval and acceptance by the audit committee and the Board of Directors. This charter was created based on guidelines provided by the Comptroller of the Treasury in conformance with *Tennessee Code Annotated*.

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

August 25, 2006

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

We have audited the accompanying statements of net assets of the Tennessee Sports Hall of Fame as of December 31, 2005, and December 31, 2004, and the related statements of revenues, expenses, and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Tennessee Sports Hall of Fame's management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Tennessee Sports Hall of Fame, as of December 31, 2005, and December 31, 2004, and the changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 15 through 19 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 25, 2006, on our consideration of the Tennessee Sports Hall of Fame'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* and should be read in conjunction with this report in considering the results of our audit.

Sincerely,

Arthur A. Hayes, Jr., CPA
Director

AAH/th

MANAGEMENT'S DISCUSSION AND ANALYSIS

The management of the Tennessee Sports Hall of Fame, Inc. (TSHF) provides this discussion and analysis as an overview of the TSHF's financial activities for the fiscal years ended December 31, 2005, and December 31, 2004.

FINANCIAL HIGHLIGHTS

- At December 31, 2005, the TSHF had current assets of $799,163, an increase of $30,522, or 4.0%, from $768,641 at December 31, 2004.
- Net investment income for the year ended December 31, 2005, totaled $19,347, an increase of $8,892, or 85.0%, from $10,455 for the year ended December 31, 2004. The continued improvement in market conditions has resulted in a weighted average return to the TSHF portfolio of 1.89% during fiscal year 2005.
- An operating loss of $68,785 was recognized for the year ended December 31, 2005. This was a decrease of $28,688, or 29.4%, from a $97,473 loss for the year ended December 31, 2004.
- Operating expenses for the year ended December 31, 2005, totaled $287,197 versus $323,191 for the year ended December 31, 2004. This is a decrease of 11.1%, or $35,994, compared to the Consumer Price Index of 3.4% for the 12 months ended December 31, 2005.

OVERVIEW OF THE FINANCIAL STATEMENTS

The TSHF's financial statements consist of the *Statements of Net Assets*, the *Statements of Revenues, Expenses, and Changes in Net Assets*, the *Statements of Cash Flows*, and the *Notes to the Financial Statements*. In addition, this *Management's Discussion and Analysis* is included as *Required Supplementary Information*.

The *Statements of Net Assets* and the *Statements of Revenues, Expenses, and Changes in Net Assets* report information about the TSHF's net assets (total assets in excess of total liabilities) as of the end of the fiscal year and the changes in those net assets during the fiscal year. These statements include all assets and liabilities using the accrual basis of accounting. Under the accrual basis of accounting, the current year's revenues and expenses are included in the financial activity, regardless of when cash is received or paid. The difference between the total assets and total liabilities on the *Statements of Net Assets* provides a measurement of the financial position of the TSHF as of the end of the fiscal year. The *Statements of Revenues, Expenses, and Changes in Net Assets* provide information on the activities that caused the financial position to change during the fiscal year. Over time, increases or decreases in the net assets of the TSHF are one indicator of whether the TSHF's financial health is improving or deteriorating. The *Statements of Cash Flows* provide an overall indication of the amount and sources of cash received and how it was used during the fiscal years. The *Notes to the Financial Statements* are also important to the reader's understanding of the financial statements and provide additional information regarding the TSHF, such as the general composition of the Board of Directors and information about the accounting principles used in the recording of financial transactions and in the preparation of these financial statements.

ANALYSIS OF ASSETS, LIABILITIES, AND NET ASSETS

At December 31, 2005, the TSHF had net assets (total assets in excess of total liabilities) of $1,643,765, a decrease of $49,438, or 2.9%, from $1,693,203 at December 31, 2004. Net assets at December 31, 2004, represented a decrease of $87,018, or 5%, from $1,780,221 at December 31, 2003. The assets of the TSHF consist primarily of short-term investments and museum exhibits. During fiscal year 2005, the investments in certificates of deposit garnered over $19,000 in investment income while museum exhibits depreciated over $71,000. During fiscal year 2004, the investments in certificates of deposit garnered over $10,000 in investment income while museum exhibits depreciated over $98,000. More detailed information about the TSHF's capital assets is presented in Note 3 to the financial statements.

Liabilities at December 31, 2005, consist primarily of deferred revenue. Liabilities at December 31, 2004, and December 31, 2003, consist primarily of accounts payable for payroll taxes due at December 31.

Condensed financial information comparing the TSHF's assets, liabilities, and net assets for the past three fiscal years follows.

Net Assets

	December 31, 2005	December 31, 2004	Percent Change FY 05-FY 04	December 31, 2003	Percent Change FY 04-FY 03
Assets					
Current assets					
Cash and cash equivalents	$ 42,536	$ 71,086	-40%	$ 73,264	-3%
Investments	750,897	694,691	8%	685,496	1%
Receivable	5,730	2,864	100%	2,130	34%
Total current assets	799,163	768,641	4%	760,890	1%
Noncurrent assets					
Capital assets	855,857	927,804	-8%	1,026,237	-10%
Total assets	1,655,020	1,696,445	-2%	1,787,127	-5%
Liabilities					
Current liabilities					
Accounts payable	3,805	2,592	47%	6,906	-62%
Deferred revenue	7,450	650	1046%	-	-
Total liabilities	11,255	3,242	247%	6,906	-53%
Net assets					
Invested in capital assets	855,857	927,804	-8%	1,026,237	-10%
Unrestricted	787,908	765,399	3%	753,984	2%
Total net assets	$ 1,643,765	$ 1,693,203	-3%	$ 1,780,221	-5%

ANALYSIS OF REVENUES AND EXPENSES

Revenues consist of contributions, program revenue, fundraising revenue, and investment income. Contributions for fiscal year 2005 decreased by $8,535, or 6.8%, over contributions for fiscal year 2004, due chiefly to the loss of a corporate partnership with American General, Inc., who chose not to renew their sponsorship following a five-year commitment. Contributions for fiscal year 2004 decreased by $11,478, or 8%, over contributions for fiscal year 2003. Contributions consist of corporate sponsorships and other donations. Contributions and donations can fluctuate on an annual basis depending on market and economic cycles. Program revenues from membership rose $725 from fiscal year 2004, and fiscal year 2004 program revenues were up slightly from fiscal year 2003 as a result of a membership campaign. Banquet and museum ticket sales were up by $9,794, or 17.2%, from fiscal year 2004. Fiscal year 2004 banquet revenues were up by $16,534 from fiscal year 2003, but museum ticket sales for fiscal year 2004 were down $2,818 from fiscal year 2003. Fund raising efforts from our annual golf tournament were down $9,290, or 25.8%, following the loss of our tournament title sponsor Gaylord Springhouse Golf club in 2005. Golf tournament revenues for fiscal year 2004 were down $1,475 from fiscal year 2003. Investment income for the year ended December 31, 2005, totaled $19,347, an increase of $8,892 versus fiscal year 2004. Investment income for the year ended December 31, 2004, totaled $10,455, an increase of $1,072 versus fiscal year 2003.

Total operating expenses for fiscal year ending December 31, 2005, were $287,197, a decrease of $35,994, or 11.1%, over fiscal year 2004. The decrease in expenses is a result of reductions in all program areas including the museum and the golf tournament fundraiser. Total operating expenses for fiscal year ending December 31, 2004, were $323,191, an increase of 10% over fiscal year 2003. This can be attributed to the increases in maintenance and upgrading of the museum, an increase to the cost per attendee at the banquet, and to the increase in expenses as a result of the membership campaign. The chief expense items in total operating expenses for the fiscal years ending December 31, 2005, and December 31, 2004, include the depreciation expense relating to museum exhibits of $71,947 and $98,433, respectively, and salary expense of $98,250 for each year.

Condensed financial information comparing the TSHF's revenues and expenses for the past three fiscal years follows.

Changes in Net Assets

	Year Ended December 31, 2005	Year Ended December 31, 2004	Percent Change FY 05-FY 04	Year Ended December 31, 2003	Percent Change FY 04-FY 03
Operating revenues					
Membership dues	$ 6,925	$ 6,200	12%	$ 4,950	25%
Banquet revenues	58,445	49,525	18%	32,991	50%
Golf tournament	26,680	35,970	-26%	37,445	-4%
Contributions	117,965	126,500	-7%	137,978	-8%
Museum ticket sales	8,397	7,523	12%	10,341	-27%
Total operating revenues	218,412	225,718	-3%	223,705	1%

Operating expenses					
Membership	2,303	3,426	-33%	1,974	74%
Banquet	66,831	67,766	-1%	45,862	48%
General and administrative	118,941	116,186	2%	112,773	3%
Golf tournament	10,128	20,496	-51%	19,479	5%
Hall of fame museum	88,994	115,317	-23%	113,999	1%
Total operating expenses	287,197	323,191	-11%	294,087	10%
Operating income (loss)	(68,785)	(97,473)	29%	(70,382)	-38%
Nonoperating revenues					
Interest income	19,347	10,455	85%	9,383	11%
Increase (decrease) in net assets	(49,438)	(87,018)	43%	(60,999)	-43%
Total net assets, January 1	1,693,203	1,780,221	-5%	1,841,220	-3%
Total net assets, December 31	$ 1,643,765	$ 1,693,203	-3%	$ 1,780,221	-5%

ECONOMIC FACTORS, FUNDING, AND OVERALL OUTLOOK

The continued rise in the interest rate has benefited the TSHF's investment portfolio, which is comprised 100% of certificates of deposit (CDs). In the past year, interest rates for CD's have fluctuated from 1.65% to 3.25% and are expected to remain steady or increase over the next 6-12 months. This should mean increased investment revenue for the $750,000 portfolio. Projections for investment income are expected to meet and exceed the budgeted $10,000 in investment earnings.

The slow but steady improvements in financial conditions for the 2005 and 2006 fiscal years have resulted in an improved outlook for the TSHF. Though the losses of three corporate partnerships (FedEx, Eastman Chemical Co., American General Inc.) were substantial, executive management in conjunction with the Board of Directors is encouraged by potential new partnerships in the corporate community. Beginning in 2006, Vanderbilt University committed to a three-year sponsorship of the annual golf tournament fundraiser. Renewals of the corporate partnerships, including First Tennessee, Pilot Oil, and Bellsouth also serve to encourage the continued support of the TSHF by corporations throughout the state. In fiscal year 2006, we have already begun to see increased participation in all our program and fundraising efforts.

The prospects for continued funding from corporate partners are good, and management has kept expenses to a very moderate growth rate while reducing expenses in some areas. In addition, the reserves of the TSHF are adequate to sustain the current expense rates for several years.

CONTACTING THE TSHF

This report is designed to provide a financial overview of the TSHF to state legislators, members of the Board of Directors of the TSHF, state officials, and any other interested parties. Questions or requests for additional information regarding the financial information presented in this report may be addressed in writing to the Tennessee Sports Hall of Fame, State Treasurer’s Office, 500 Charlotte Ave., Nashville, TN 37243.

Exhibit A

TENNESSEE SPORTS HALL OF FAME
STATEMENTS OF NET ASSETS
DECEMBER 31, 2005, AND DECEMBER 31, 2004

	2005	2004
ASSETS		
Current assets		
Cash and cash equivalents (Note 2)	$ 42,536	$ 71,086
Investments (Note 2)	750,897	694,691
Interest receivable	5,730	2,864
Total current assets	799,163	768,641
Noncurrent assets		
Capital assets (Note 3)		
Museum exhibits	1,419,969	1,419,969
Less accumulated depreciation	(564,112)	(492,165)
Total noncurrent assets	855,857	927,804
Total assets	1,655,020	1,696,445
LIABILITIES		
Current liabilities		
Accounts payable	3,805	2,592
Deferred revenue	7,450	650
Total liabilities	11,255	3,242
NET ASSETS		
Invested in capital assets	855,857	927,804
Unrestricted	787,908	765,399
Total net assets	$ 1,643,765	$ 1,693,203

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

Exhibit B

TENNESSEE SPORTS HALL OF FAME
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2005, AND DECEMBER 31, 2004

	2005	2004
OPERATING REVENUES		
Membership dues	$ 6,925	$ 6,200
Banquet revenue	58,445	49,525
Golf tournament	26,680	35,970
Contributions	117,965	126,500
Museum ticket sales	8,397	7,523
Total operating revenues	218,412	225,718
OPERATING EXPENSES		
Membership	2,303	3,426
Banquet	66,831	67,766
General and administrative	118,941	116,186
Golf tournament	10,128	20,496
Hall of fame museum	88,994	115,317
Total operating expenses	287,197	323,191
Operating loss	(68,785)	(97,473)
NONOPERATING REVENUES		
Interest income	19,347	10,455
Decrease in net assets	(49,438)	(87,018)
Total net assets, January 1	1,693,203	1,780,221
Total net assets, December 31	$ 1,643,765	$ 1,693,203

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

Exhibit C

TENNESSEE SPORTS HALL OF FAME
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2005, AND DECEMBER 31, 2004

	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers	$ 207,367	$ 203,218
Payments to suppliers	(95,934)	(105,792)
Payments to employees	(100,258)	(100,130)
Net cash provided (used) by operating activities	11,175	(2,704)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest received	16,480	9,721
Investment purchases	(1,491,947)	(1,384,949)
Proceeds from maturities of investments	1,435,742	1,375,754
Net cash provided (used) by investing activities	(39,725)	526
Net decrease in cash and cash equivalents	(28,550)	(2,178)
Cash and cash equivalents, January 1	71,086	73,264
Cash and cash equivalents, December 31	$ 42,536	$ 71,086
RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES		
Operating loss	$ (68,785)	$ (97,473)
Adjustments to reconcile operating loss to net cash provided (used) by operating activities		
Depreciation expense	71,947	98,433
Increase (decrease) in accounts payable	1,213	(4,314)
Increase in deferred revenue	6,800	650
Net cash provided (used) by operating activities	$ 11,175	$ (2,704)

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

Tennessee Sports Hall of Fame
Notes to the Financial Statements
December 31, 2005, and December 31, 2004

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The Tennessee Sports Hall of Fame is a nonprofit corporation founded in the 1960s to honor the outstanding achievements of Tennesseans in the realm of sports. With Title 4, Chapter 3, *Tennessee Code Annotated*, the General Assembly passed the Tennessee Sports Hall of Fame Act of 1994 (Act) to officially create a Tennessee Sports Hall of Fame to honor, preserve, and perpetuate the names and accomplishments of outstanding Tennessee athletes, athletic teams, and other sports personalities; to establish, erect, and maintain a permanent archive for the collection and display of memorabilia related to the lives and careers of individuals, teams, and sports events chosen for induction by the hall of fame; and to promote the spirit of sportsmanship and genteel competition both inside and outside the arena of athletic competition.

Under the act, a new Board of Directors was founded composed of 25 Tennessee citizens: 8 appointed by the Governor, 8 by the Lieutenant Governor, and 8 by the Speaker of the House. The State Treasurer or his designee serves as an *ex officio* member of the board.

The Tennessee Sports Hall of Fame has been classified as a related organization of the State of Tennessee and is discussed in a note to the financial statements in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor William R. Snodgrass Tennessee Tower, 312 Eighth Avenue North, Nashville, Tennessee 37243-0298.

Basis of Presentation

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The Tennessee Sports Hall of Fame follows all applicable GASB pronouncements, as well as applicable private-sector pronouncements issued on or before November 30, 1989, to the extent that those standards do not conflict with or contradict guidance of the GASB. The Tennessee Sports Hall of Fame has the option of following subsequent private-sector guidance subject to the same limitation, but has elected not to follow subsequent private-sector guidance.

Measurement Focus and Basis of Accounting

The accompanying financial statements of the Tennessee Sports Hall of Fame have been prepared using the flow of economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded at the time liabilities are incurred.

The Tennessee Sports Hall of Fame distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services in connection with principal ongoing operations. The principal operating revenues are contributions and revenue from fund-raising events. Operating expenses include general and administrative, hall of fame museum, and fund-raising expenses. Any revenues and expenses not meeting this definition would be reported as nonoperating revenues and expenses.

Cash Equivalents

Cash equivalents are defined as short-term, highly liquid investments that are both readily convertible to known amounts of cash and so near to their maturity that they present insignificant risk of changes in value because of changes in interest rates.

Capital Assets

Capital assets are comprised of museum exhibits which are reported net of accumulated depreciation and include any improvements costing in excess of $5,000. Costs of maintenance and repairs are charged to expense. Depreciation is calculated by the straight-line method to allocate the cost of the assets over their estimated useful lives. The general range of useful lives is 5 to 10 years for interactive, audio-visual, and multi-media assets and 20 to 30 years for all other exhibit assets.

NOTE 2. DEPOSITS AND INVESTMENTS

Cash and cash equivalents include demand deposits, savings deposits in banks, and certificates of deposit with maturities of 90 days or less. Investments include certificates of deposit with maturities of more than 90 days and are reported at cost. Investments at December 31, 2005, had maturities ranging from 182 to 183 days and ranges of return from 3% to 3.75%. Investments at December 31, 2004, had maturities ranging from 181 to 184 days and ranges of return from 1.65% to 2.10%.

The bank balances of deposits and investments, including accrued interest, are in financial institutions which participate in the bank collateral pool administered by the

Treasurer of the State of Tennessee. The securities pledged to protect these deposits and investments are pledged in the aggregate rather than against each individual account. The members of the pool may be required by agreement to pay an assessment to cover any deficiency. Under this additional assessment agreement, public fund accounts covered by the pool are considered to be insured for purposes of credit risk disclosure.

NOTE 3. CAPITAL ASSETS

Capital asset activity for the year ended December 31, 2005, was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Museum exhibits	$ 1,419,969	$ -	$ -	$ 1,419,969
Less accumulated depreciation	(492,165)	(71,947)	-	(564,112)
Total capital assets, net of depreciation	$ 927,804	$ (71,947)	$ -	$ 855,857

Capital asset activity for the year ended December 31, 2004, was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Museum exhibits	$ 1,419,969	$ -	$ -	$ 1,419,969
Less accumulated depreciation	(393,732)	(98,433)	-	(492,165)
Total capital assets, net of depreciation	$ 1,026,237	$ (98,433)	$ -	$ 927,804

NOTE 4. RISK MANAGEMENT

The Tennessee Sports Hall of Fame is exposed to various risks of loss related to general liability; flood, fire, and other disasters, including terrorist acts, with respect to its office and museum space; and errors and omissions. The Tennessee Sports Hall of Fame has purchased commercial insurance for these risks. There have been no claims filed with the commercial insurer in the past three years.