



STATE OF NORTH CAROLINA

WINSTON-SALEM STATE UNIVERSITY

WINSTON-SALEM, NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT

FOR THE YEAR ENDED JUNE 30, 2012

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

STATE AUDITOR

WINSTON-SALEM STATE UNIVERSITY

WINSTON-SALEM, NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT

FOR THE YEAR ENDED JUNE 30, 2012

BOARD OF GOVERNORS

THE UNIVERSITY OF NORTH CAROLINA

THOMAS W. ROSS, PRESIDENT

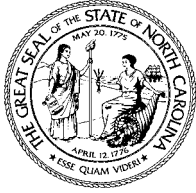
BOARD OF TRUSTEES

DEBRA B. MILLER, CHAIRMAN

ADMINISTRATIVE OFFICERS

DR. DONALD JULIAN REAVES, CHANCELLOR

GERALD E. HUNTER, VICE CHANCELLOR FOR FINANCE AND ADMINISTRATION



Beth A. Wood, CPA
State Auditor

STATE OF NORTH CAROLINA
Office of the State Auditor

2 S. Salisbury Street
20601 Mail Service Center
Raleigh, NC 27699-0601
Telephone: (919) 807-7500
Fax: (919) 807-7647
Internet
<http://www.ncauditor.net>

AUDITOR'S TRANSMITTAL

The Honorable Beverly E. Perdue, Governor
The General Assembly of North Carolina
Board of Trustees, Winston-Salem State University

We have completed a financial statement audit of Winston-Salem State University for the year ended June 30, 2012, and our audit results are included in this report. You will note from the independent auditor's report that we determined that the financial statements are presented fairly in all material respects.

Our consideration of internal control over financial reporting and compliance and other matters based on an audit of the financial statements disclosed certain deficiencies that are detailed in the Audit Findings and Responses section of this report. The University's response is included following each finding.

North Carolina General Statutes require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.

A handwritten signature in cursive script that reads "Beth A. Wood".

Beth A. Wood, CPA
State Auditor

TABLE OF CONTENTS

| | PAGE |
|---|------|
| INDEPENDENT AUDITOR’S REPORT | 1 |
| MANAGEMENT’S DISCUSSION AND ANALYSIS | 3 |
| BASIC FINANCIAL STATEMENTS | |
| University Exhibits | |
| A-1 Statement of Net Assets | 11 |
| A-2 Statement of Revenues, Expenses, and Changes in Net Assets | 13 |
| A-3 Statement of Cash Flows | 14 |
| Component Unit Exhibits | |
| B-1 Consolidated Statement of Financial Position | 16 |
| B-2 Consolidated Statement of Activities | 17 |
| Notes to the Financial Statements | 19 |
| 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 <i>GOVERNMENT AUDITING STANDARDS</i> | 43 |
| AUDIT FINDINGS AND RESPONSES | 45 |
| ORDERING INFORMATION | 47 |



Beth A. Wood, CPA
State Auditor

STATE OF NORTH CAROLINA
Office of the State Auditor

2 S. Salisbury Street
20601 Mail Service Center
Raleigh, NC 27699-0601
Telephone: (919) 807-7500
Fax: (919) 807-7647
Internet
<http://www.ncauditor.net>

INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Winston-Salem State University
Winston-Salem, North Carolina

We have audited the accompanying financial statements of Winston-Salem State University, a constituent institution of the multi-campus University of North Carolina System, which is a component unit of the State of North Carolina, and its discretely presented component unit, as of and for the year ended June 30, 2012, which collectively comprise the University's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of Winston-Salem State University Foundation, Inc. and Subsidiary, the University's discretely presented component unit. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinions, insofar as they relate to the amounts included for the discretely presented component unit, are based on the report 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. The financial statements of Winston-Salem State University Foundation, Inc. and Subsidiary were not audited in accordance with *Government Auditing Standards*. 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 the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinions.

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

INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

In accordance with *Government Auditing Standards*, we have also issued our report dated November 20, 2012 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, 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 considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board, who 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. However, 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.



Beth A. Wood, CPA
State Auditor

November 20, 2012

WINSTON-SALEM STATE UNIVERSITY MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the Winston-Salem State University (the “University”) annual financial report presents our discussion and analysis of the financial performance of the University during the fiscal year ended June 30, 2012. This discussion has been prepared by University management along with the financial statements and notes to the financial statements and should be read in conjunction with, and is qualified in its entirety by, the financial statements and notes. The Management’s Discussion and Analysis has comparative data for the applicable years (past and current) with emphasis on the current year. The financial statements, notes, and this discussion are the responsibility of University management.

Using the Annual Report

This annual report consists of a series of financial statements, prepared in accordance with the Governmental Accounting Standards Board’s (GASB) pronouncements. GASB pronouncements establish standards for external financial reporting for public colleges and universities and require that financial statements be presented on a consolidated basis for the University as a whole, with resources classified for accounting and reporting purposes into four net asset categories. One of the most important questions asked is whether the University as a whole is better or worse off as a result of the year’s activities. The key to understanding this question is provided within the Statement of Net Assets, the Statement of Revenues, Expenses, and Changes in Net Assets, and the Statement of Cash Flows. These statements present financial information in a form similar to that used by corporations. They are prepared under the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service, regardless of when cash is exchanged.

The Statement of Net Assets includes all assets and liabilities. The University’s net assets (the difference between assets and liabilities) are an indicator of the University’s financial health. Over time, increases or decreases in net assets is one indicator of the improvement or erosion of the University’s financial health when considered with nonfinancial facts such as enrollment levels and the condition of the facilities.

The Statement of Revenues, Expenses, and Changes in Net Assets presents the revenues earned and expenses incurred during the year. Activities are reported as either operating or nonoperating. All things being equal, a public University’s dependency on state appropriations and gifts will result in operating deficits, because GASB Statement No. 35 classifies state appropriations, certain grants, and gifts as nonoperating revenues.

The Statement of Cash Flows provides information relative to the University’s sources and uses of cash for operating activities, noncapital financing activities, capital and related financing activities, and investing activities. The statement provides a reconciliation of beginning cash balances and is representative of the activity reported on the Statement of

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Revenues, Expenses, and Changes in Net Assets as adjusted for changes in the beginning and ending balances of noncash accounts on the Statement of Net Assets. For the purpose of this discussion, we will address the Statement of Net Assets and the Statement of Revenues, Expenses, and Changes in Net Assets.

Reporting Entity

The financial statements report information about the University as a whole using accounting methods similar to those used by private-sector companies. The University's supporting organization, the Winston-Salem State University Foundation, Inc. and Subsidiary (the "Foundation"), is an independent nonprofit corporation formed for the exclusive benefit of the University. According to GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units*, the Foundation meets the requirements to be reported discretely in these financial statements.

Financial Highlights

The University's financial position, as a whole, increased during the fiscal year ended June 30, 2012. Its combined net assets increased \$15,024,006.41 or 12.4% from the previous year.

Condensed Financial Information

Statement of Net Assets

The Statement of Net Assets presents the assets (current and noncurrent), liabilities (current and noncurrent), and the net assets (total assets less total liabilities) of the University. This condensed financial statement provides a comparative University fiscal snapshot as of June 30, 2012 and June 30, 2011. This provides the readers of this statement with information on assets available to continue operations.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

| Condensed Statements of Net Assets 6/30/2012 and 6/30/2011 | | | | |
|---|--------------------------|--------------------------|-------------------------|--------|
| | 2012 | 2011 | \$ Change | % Chg |
| Assets | | | | |
| Current Assets | \$ 27,167,384.85 | \$ 21,111,730.23 | \$ 6,055,654.62 | 28.7% |
| Noncurrent Assets | | | | |
| Capital | 170,566,849.97 | 152,200,739.87 | 18,366,110.10 | 12.1% |
| Other | 25,342,386.78 | 25,704,978.72 | (362,591.94) | -1.4% |
| Total Assets | <u>223,076,621.60</u> | <u>199,017,448.82</u> | <u>24,059,172.78</u> | 12.1% |
| Liabilities | | | | |
| Current Liabilities | 12,439,655.74 | 7,977,700.49 | 4,461,955.25 | 55.9% |
| Noncurrent Liabilities | 74,724,241.10 | 70,151,029.98 | 4,573,211.12 | 6.5% |
| Total Liabilities | <u>87,163,896.84</u> | <u>78,128,730.47</u> | <u>9,035,166.37</u> | 11.6% |
| Net Assets* | | | | |
| Invested in Capital Assets, Net of Related Debt | 102,548,873.86 | 85,347,734.14 | 17,201,139.72 | 20.2% |
| Restricted: | | | | |
| Nonexpendable | 16,215,421.37 | 15,661,547.06 | 553,874.31 | 3.5% |
| Expendable | 9,450,549.90 | 13,600,335.84 | (4,149,785.94) | -30.5% |
| Unrestricted | 7,697,879.63 | 6,279,101.31 | 1,418,778.32 | 22.6% |
| Total Net Assets | <u>\$ 135,912,724.76</u> | <u>\$ 120,888,718.35</u> | <u>\$ 15,024,006.41</u> | 12.4% |

*Net Asset categories are defined in Note 1L of the Notes to the Financial Statements.

As of June 30, 2012, total University assets were \$223,076,621.60. The University's largest asset at June 30, 2012 is capital assets totaling \$170,566,849.97, which increased \$18,366,110.10 compared to the prior year's capital assets of \$152,200,739.87. This increase is mainly due to a \$23,487,960.87 increase in construction in progress related to the new Student Activities Center, and a \$1,178,273.48 net increase in depreciable assets offset against a \$6,355,124.25 net increase in accumulated depreciation/amortization. The University's June 30, 2012 current assets of \$27,167,384.85 increased \$6,055,654.62 compared to the prior year's current assets of \$21,111,730.23. This increase is primarily due to an increase in current unrestricted cash of \$1,967,885.62 due to increased housing and dining revenue from increased rates in the 2011-2012 fiscal year along with an increase in current restricted cash of \$3,025,305.46 resulting from the reclassification of approximately \$3,000,000.00 from noncurrent restricted cash to cover current plant liabilities related to the new Student Activities Center.

The \$27,167,384.85 in current assets covered the current liabilities of \$12,439,655.74, as the current ratio was \$2.18 in current assets to every \$1.00 in current liabilities.

University liabilities totaled \$87,163,896.84 at June 30, 2012 compared to \$78,128,730.47 per the prior year, an increase of \$9,035,166.37. This variance is mainly attributed to the issuance of a Guaranteed Energy Savings Notes Payable of \$6,517,358.00 and an increase in accounts payable and retainage of \$2,541,167.99 related to construction of the new Student Activities Center. Bonds payable of \$13,598,861.78, a notes payable of \$6,517,358.00, and capital leases of \$50,810,000.00 were the largest liabilities, representing 81.4% of the total University liabilities. The University had outstanding bonds of \$3,440,000.00, \$1,305,000.00, \$2,015,000.00, and \$6,800,000.00 from 1998, 2002, 2004, and 2008 bond issues, respectively. The notes payable with Siemens Public, Inc. was issued during the

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

2011-2012 fiscal year. Refer to Note 7 of the Notes to the Financial Statements for more detailed information about the University's long-term debt obligations.

The University's unrestricted net assets were \$7,697,879.63 at June 30, 2012 compared to \$6,279,101.31 in the prior year. This is an increase of \$1,418,778.32 or 22.6% due primarily to increased housing and dining revenue from increased rates.

Statement of Revenues, Expenses, and Changes in Net Assets

The Statement of Revenues, Expenses, and Changes in Net Assets presents the activity that shows the changes in net assets. The activity is represented by the revenues received by the University, both operating and nonoperating, and the expenses paid by the University, operating and nonoperating, as well as any other revenues, expenses, gains and losses received or expended by the University.

Operating revenues are received for providing goods and services to the various customers of the University. Operating expenses are used to acquire goods and services provided in return for the operating revenues, and to carry out the mission of the University. Nonoperating revenues include activities that have the characteristics of nonexchange transactions. Revenues from nonexchange transactions and state appropriations that represent subsidies or gifts to the University, as well as investment income, are considered nonoperating activities since these are either investing, capital, or noncapital financing activities. Nonoperating expenses are expenses other than those involved in the normal operation of the University that can include interest expense.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Condensed Statement of Revenues, Expenses, and Changes in Net Assets 6/30/2012 and 6/30/2011

| | 2012 | 2011 | \$ Change | % Chg |
|--|--------------------------|--------------------------|-------------------------|----------|
| Operating Revenues: | | | | |
| Student Tuition and Fees, Net | \$ 21,147,933.20 | \$ 18,480,202.27 | \$ 2,667,730.93 | 14.4% |
| Sales and Services, Net | 13,958,491.41 | 11,360,546.35 | 2,597,945.06 | 22.9% |
| Other | <u>1,080,918.52</u> | <u>940,775.56</u> | <u>140,142.96</u> | 14.9% |
| Total Operating Revenues | <u>36,187,343.13</u> | <u>30,781,524.18</u> | <u>5,405,818.95</u> | 17.6% |
| Operating Expenses: | | | | |
| Salaries and Benefits | 83,440,618.69 | 83,306,127.73 | 134,490.96 | 0.2% |
| Supplies and Materials | 7,635,246.32 | 10,074,957.91 | (2,439,711.59) | -24.2% |
| Services | 25,160,950.15 | 26,169,661.51 | (1,008,711.36) | -3.9% |
| Scholarships and Fellowships | 12,628,353.20 | 15,546,177.39 | (2,917,824.19) | -18.8% |
| Utilities | 2,740,521.09 | 2,983,978.37 | (243,457.28) | -8.2% |
| Depreciation/ Amortization | <u>6,589,623.19</u> | <u>6,421,857.09</u> | <u>167,766.10</u> | 2.6% |
| Total Operating Expenses | <u>138,195,312.64</u> | <u>144,502,760.00</u> | <u>(6,307,447.36)</u> | -4.4% |
| Operating Loss | (102,007,969.51) | (113,721,235.82) | 11,713,266.31 | -10.3% |
| Nonoperating Revenues (Expenses): | | | | |
| State Appropriations | 67,990,987.56 | 66,298,890.60 | 1,692,096.96 | 2.6% |
| State Aid - Federal Recovery Funds | | 3,827,542.00 | (3,827,542.00) | -100.0% |
| Noncapital Grants | 35,258,298.12 | 40,166,547.00 | (4,908,248.88) | -12.2% |
| Noncapital Gifts | 285,356.73 | 157,113.31 | 128,243.42 | 81.6% |
| Investment Income | 537,043.83 | 2,677,585.79 | (2,140,541.96) | -79.9% |
| Other | <u>(3,330,687.44)</u> | <u>(2,286,103.01)</u> | <u>(1,044,584.43)</u> | 45.7% |
| Net Nonoperating Revenues | <u>100,740,998.80</u> | <u>110,841,575.69</u> | <u>(10,100,576.89)</u> | -9.1% |
| Loss Before Other Revenues | (1,266,970.71) | (2,879,660.13) | 1,612,689.42 | -56.0% |
| Capital Grants | 15,656,827.62 | 1,625,310.11 | 14,031,517.51 | 863.3% |
| Capital Gifts | 100,000.00 | 166,000.00 | (66,000.00) | -39.8% |
| Additions to Endowments | <u>534,149.50</u> | <u>566,024.00</u> | <u>(31,874.50)</u> | -5.6% |
| Total Other Revenues | <u>16,290,977.12</u> | <u>2,357,334.11</u> | <u>13,933,643.01</u> | 591.1% |
| Increase (Decrease) in Net Assets | 15,024,006.41 | (522,326.02) | 15,546,332.43 | -2976.4% |
| Net Assets: | | | | |
| Beginning of Year | <u>120,888,718.35</u> | <u>121,411,044.37</u> | <u>(522,326.02)</u> | -0.4% |
| End of Year | <u>\$ 135,912,724.76</u> | <u>\$ 120,888,718.35</u> | <u>\$ 15,024,006.41</u> | 12.4% |

Total operating loss for fiscal year 2012 was \$102,007,969.51. Since the State of North Carolina appropriation, certain grants, and gifts are not included within operating revenues per GASB Statement No. 35, the University will show a significant operating loss on a continuing basis.

The sources of operating revenues for the University are tuition and fees, auxiliary services, and other educational activities.

The University strives to provide students with the opportunity to obtain a quality education. Future University enrollments may be affected by a number of factors, including any material

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

increase in tuition and other mandatory charges, stemming from any material decrease in appropriation funding from the State of North Carolina.

Operating expenses, including depreciation/amortization of \$6,589,623.19, totaled \$138,195,312.64. Of this total, \$67,629,985.37 or 48.9% was used for instruction and student support. Changes within key operating expenses are identified as follows:

- Salaries and benefits slightly increased by \$134,490.96.
- Supplies and materials decreased by \$2,439,711.59 and services decreased by \$1,008,711.36 due primarily to a decrease in the overall budget for the institution.
- Scholarships and fellowships decreased by \$2,917,824.19 due to a reduction in financial aid awards from federal and state sources during the 2011-2012 fiscal year, with the most significant reductions occurring in the Federal Pell Grant Program and the University of North Carolina Need Based Grant. The reduction in the Federal Pell Grant Program is attributed to year-round funding received in 2010-2011 that was not provided in the 2011-2012 fiscal year.

The University's largest source of nonoperating revenue is the State of North Carolina appropriation. This is received in monthly payments, beginning in July of each year, since the State's fiscal year begins on July 1. There is no direct connection between the amount of tuition revenues collected by the University and the amount of state funds appropriated in any given year. For the fiscal year ended June 30, 2012, the State of North Carolina appropriated to the University \$67,990,987.56 for operations and provided \$15,656,827.62 in capital grants.

Total net revenues were \$153,219,319.05 for fiscal year 2012, compared to \$143,980,433.98 for fiscal year 2011, resulting in a net increase of \$9,238,885.07, which is primarily attributed to the following:

- Student tuition and fees increased \$2,667,730.93 from last year due to increases in tuition and fee rates.
- Sales and services increased \$2,597,945.06 from last year due to increases in housing and dining rates.
- State appropriations reflect a \$1,692,096.96 increase due to increased funding from the State of North Carolina.
- State Aid - Federal Recovery Funds decreased \$3,827,542.00 due to the ending of this federal program.
- Noncapital grants decreased \$4,908,248.88 mainly due to decreased financial aid awards from federal and state sources as previously mentioned in the scholarships and fellowships expense discussion. In addition, there were reductions to other student financial aid revenue due to decreased private funding and the end to federal stimulus funding.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

- Investment income decreased \$2,140,541.96 mainly due to a decrease in returns on endowment investments.
- Capital grants increased by \$14,031,517.51 due to increased state funding for capital projects, in particular the new Student Activities Center.

One of the University's greatest strengths is the diverse streams of revenues which supplement its student tuition and fees, including voluntary private support from individuals, foundations, and corporations, along with government and other sponsored programs, state appropriations and investment income. The University has and will continue to seek funding aggressively from all possible sources consistent with its mission, to supplement student tuition and manage prudently the financial resources realized from these efforts to fund its operating activities.

Capital Assets and Long-Term Debt

Major capital expenses for the year ended June 30, 2012 include the Student Activities Center construction costs of \$17,850,465.43 and Guaranteed Energy Savings implementation costs of \$3,609,114.33. The University's capital assets, net of accumulated depreciation/amortization at June 30, 2012, were \$170,566,849.97. For more information about the University's capital asset holdings, refer to Note 5 of the Notes to the Financial Statements. As stated in the Statement of Net Assets discussion, a notes payable with Siemens Public, Inc. for \$6,517,358.00 was issued during the 2011-2012 fiscal year.

Factors Impacting Future Periods

Management believes that the University is well positioned to continue its strong financial condition and level of excellence in service to students, the community, and governmental agencies. This flexibility, along with the University's ongoing efforts toward revenue diversification and cost containment, will enable the University to provide the necessary resources to support this level of excellence.

A crucial element to the University's future will continue to be our relationship with the State of North Carolina, as we work to manage tuition to make it competitive while providing an outstanding college education for our students. There is a direct relationship between the growth of state support and the University's ability to control tuition growth, as declines in state appropriations generally result in increased tuition levels.

The University continues to execute its long-range plan to modernize and expand its complement of facilities with a balance of new construction. The University has plans to increase the availability of on-campus housing offerings to its students and has entered into an agreement with the Winston-Salem State University Foundation, Inc. and Subsidiary to work collaboratively towards this effort. This strategy addresses the University's growth and the continuing effects of technology on teaching methodologies.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONCLUDED)

Private gifts are an important supplement to the fundamental support from the State and student tuition, and a significant factor in the growth of academic units. Economic pressures affecting donors may also affect the future level of support the University receives from corporate and individual giving.

The University will continue to employ its long-term investment strategy to maximize total returns, at an appropriate level of risk, while utilizing a spending rate policy to insulate the University's operations from temporary market volatility.

While it is not possible to predict the ultimate results, management believes that the University's financial condition is strong enough to weather any economic uncertainties.

Winston-Salem State University
Statement of Net Assets
June 30, 2012

Exhibit A-1
Page 1 of 2

ASSETS

Current Assets:

| | |
|--------------------------------------|------------------|
| Cash and Cash Equivalents | \$ 13,318,069.82 |
| Restricted Cash and Cash Equivalents | 9,218,058.18 |
| Restricted Short-Term Investments | 701,000.02 |
| Receivables, Net (Note 4) | 3,546,930.99 |
| Inventories | 306,776.29 |
| Notes Receivable, Net (Note 4) | 76,549.55 |
| | <hr/> |
| Total Current Assets | 27,167,384.85 |
| | <hr/> |

Noncurrent Assets:

| | |
|--|----------------|
| Restricted Cash and Cash Equivalents | 4,738,091.12 |
| Endowment Investments | 18,684,781.24 |
| Other Investments | 1,341,312.61 |
| Notes Receivable, Net (Note 4) | 578,201.81 |
| Capital Assets - Nondepreciable (Note 5) | 34,322,332.86 |
| Capital Assets - Depreciable, Net (Note 5) | 136,244,517.11 |
| | <hr/> |
| Total Noncurrent Assets | 195,909,236.75 |
| | <hr/> |
| Total Assets | 223,076,621.60 |
| | <hr/> |

LIABILITIES

Current Liabilities:

| | |
|---|---------------|
| Accounts Payable and Accrued Liabilities (Note 6) | 6,681,270.67 |
| Due to Primary Government | 11,141.04 |
| Unearned Revenue | 2,061,066.23 |
| Interest Payable | 472,592.57 |
| Long-Term Liabilities - Current Portion (Note 7) | 3,213,585.23 |
| | <hr/> |
| Total Current Liabilities | 12,439,655.74 |
| | <hr/> |

Noncurrent Liabilities:

| | |
|------------------------------------|---------------|
| Deposits Payable | 336,395.02 |
| Funds Held for Others | 987,165.05 |
| U. S. Government Grants Refundable | 830,513.25 |
| Long-Term Liabilities (Note 7) | 72,570,167.78 |
| | <hr/> |
| Total Noncurrent Liabilities | 74,724,241.10 |
| | <hr/> |
| Total Liabilities | 87,163,896.84 |
| | <hr/> |

Winston-Salem State University
Statement of Net Assets
June 30, 2012

Exhibit A-1
Page 2 of 2

NET ASSETS

| | |
|---|---------------------------------|
| Invested in Capital Assets, Net of Related Debt | 102,548,873.86 |
| Restricted for: | |
| Nonexpendable: | |
| Scholarships and Fellowships | 3,532,623.54 |
| Endowed Professorships | 10,130,500.00 |
| Departmental Uses | 2,462,681.29 |
| Loans | 89,616.54 |
| Expendable: | |
| Scholarships and Fellowships | 1,288,571.92 |
| Professorships | 3,123,127.60 |
| Departmental Uses | 2,935,212.15 |
| Loans | 204,437.37 |
| Capital Projects | 61,124.49 |
| Debt Service | 1,838,076.37 |
| Unrestricted | <u>7,697,879.63</u> |
| Total Net Assets | <u><u>\$ 135,912,724.76</u></u> |

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

Winston-Salem State University
Statement of Revenues, Expenses, and
Changes in Net Assets
For the Fiscal Year Ended June 30, 2012

Exhibit A-2

REVENUES

| | |
|--|------------------|
| Operating Revenues: | |
| Student Tuition and Fees, Net (Note 9) | \$ 21,147,933.20 |
| Sales and Services, Net (Note 9) | 13,958,491.41 |
| Interest Earnings on Loans | 4,296.89 |
| Other Operating Revenues | 1,076,621.63 |
| | <hr/> |
| Total Operating Revenues | 36,187,343.13 |
| | <hr/> |

EXPENSES

| | |
|------------------------------|------------------|
| Operating Expenses: | |
| Salaries and Benefits | 83,440,618.69 |
| Supplies and Materials | 7,635,246.32 |
| Services | 25,160,950.15 |
| Scholarships and Fellowships | 12,628,353.20 |
| Utilities | 2,740,521.09 |
| Depreciation/ Amortization | 6,589,623.19 |
| | <hr/> |
| Total Operating Expenses | 138,195,312.64 |
| | <hr/> |
| Operating Loss | (102,007,969.51) |
| | <hr/> |

NONOPERATING REVENUES (EXPENSES)

| | |
|--|----------------|
| State Appropriations | 67,990,987.56 |
| Noncapital Grants - Student Financial Aid | 22,978,595.23 |
| Other Noncapital Grants | 12,279,702.89 |
| Noncapital Gifts | 285,356.73 |
| Investment Income (Net of Investment Expense of \$90,888.77) | 537,043.83 |
| Interest and Fees on Debt | (3,182,274.25) |
| Other Nonoperating Expenses | (148,413.19) |
| | <hr/> |
| Net Nonoperating Revenues | 100,740,998.80 |
| | <hr/> |
| Loss Before Other Revenues | (1,266,970.71) |
| | <hr/> |
| Capital Grants | 15,656,827.62 |
| Capital Gifts | 100,000.00 |
| Additions to Endowments | 534,149.50 |
| | <hr/> |
| Increase in Net Assets | 15,024,006.41 |
| | <hr/> |

NET ASSETS

| | |
|----------------------------|-------------------|
| Net Assets - July 1, 2011 | 120,888,718.35 |
| | <hr/> |
| Net Assets - June 30, 2012 | \$ 135,912,724.76 |
| | <hr/> <hr/> |

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

Winston-Salem State University
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2012

Exhibit A-3
Page 1 of 2

CASH FLOWS FROM OPERATING ACTIVITIES

| | |
|---|------------------|
| Received from Customers | \$ 35,512,544.17 |
| Payments to Employees and Fringe Benefits | (82,889,063.01) |
| Payments to Vendors and Suppliers | (34,619,092.84) |
| Payments for Scholarships and Fellowships | (12,628,353.20) |
| Loans Issued | (83,000.00) |
| Collection of Loans | 105,229.87 |
| Interest Earned on Loans | 4,296.89 |
| Student Deposits Received | 336,395.02 |
| Student Deposits Returned | (300,266.22) |
| | <hr/> |
| Net Cash Used by Operating Activities | (94,561,309.32) |

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

| | |
|--|-----------------|
| State Appropriations | 67,990,987.56 |
| Noncapital Grants - Student Financial Aid | 23,232,380.46 |
| Other Noncapital Grants | 11,898,387.09 |
| Noncapital Gifts | 285,356.73 |
| Additions to Endowments | 534,149.50 |
| William D. Ford Direct Lending Receipts | 38,442,689.00 |
| William D. Ford Direct Lending Disbursements | (38,442,689.00) |
| Other Receipts | 194,253.91 |
| | <hr/> |
| Net Cash Provided by Noncapital Financing Activities | 104,135,515.25 |

CASH FLOWS FROM CAPITAL FINANCING AND RELATED FINANCING ACTIVITIES

| | |
|---|-----------------|
| Proceeds from Capital Debt | 6,517,358.00 |
| Capital Grants | 15,656,827.62 |
| Acquisition and Construction of Capital Assets | (21,894,146.50) |
| Principal Paid on Capital Debt and Leases | (2,435,000.00) |
| Interest and Fees Paid on Capital Debt and Leases | (3,016,314.67) |
| | <hr/> |
| Net Cash Used by Capital Financing and Related Financing Activities | (5,171,275.55) |

CASH FLOWS FROM INVESTING ACTIVITIES

| | |
|---|------------------|
| Proceeds from Sales and Maturities of Investments | 2,653,886.17 |
| Investment Income | 210,819.90 |
| Purchase of Investments and Related Fees | (2,944,634.97) |
| | <hr/> |
| Net Cash Used by Investing Activities | (79,928.90) |
| | <hr/> |
| Net Increase in Cash and Cash Equivalents | 4,323,001.48 |
| Cash and Cash Equivalents - July 1, 2011 | 22,951,217.64 |
| | <hr/> |
| Cash and Cash Equivalents - June 30, 2012 | \$ 27,274,219.12 |

Winston-Salem State University
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2012

Exhibit A-3
Page 2 of 2

**RECONCILIATION OF NET OPERATING REVENUES (EXPENSES)
TO NET CASH USED BY OPERATING ACTIVITIES**

| | |
|--|---------------------------|
| Operating Loss | \$ (102,007,969.51) |
| Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities: | |
| Depreciation/ Amortization Expense | 6,589,623.19 |
| Allowances, Write-Offs, and Amortizations | 50,177.59 |
| Changes in Assets and Liabilities: | |
| Receivables (Net) | (594,718.11) |
| Inventories | 7,890.47 |
| Notes Receivable (Net) | 36,562.68 |
| Accounts Payable and Accrued Liabilities | 1,023,362.61 |
| Due to Primary Government | (591.50) |
| U.S. Government Grants Refundable | (14,332.81) |
| Unearned Revenue | (75,783.96) |
| Compensated Absences | 388,341.23 |
| Deposits Payable | 36,128.80 |
| | <u>36,128.80</u> |
| Net Cash Used by Operating Activities | <u>\$ (94,561,309.32)</u> |

RECONCILIATION OF CASH AND CASH EQUIVALENTS

| | |
|---|-------------------------|
| Current Assets: | |
| Cash and Cash Equivalents | \$ 13,318,069.82 |
| Restricted Cash and Cash Equivalents | 9,218,058.18 |
| Noncurrent Assets: | |
| Restricted Cash and Cash Equivalents | 4,738,091.12 |
| | <u>4,738,091.12</u> |
| Total Cash and Cash Equivalents - June 30, 2012 | <u>\$ 27,274,219.12</u> |

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

| | |
|-------------------------------------|---------------|
| Assets Acquired through a Gift | \$ 100,000.00 |
| Change in Fair Value of Investments | 384,589.15 |
| Loss on Disposal of Capital Assets | 50,177.59 |

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

**Winston-Salem State University Foundation, Inc.
and Subsidiary
Consolidated Statement of Financial Position
June 30, 2012**

Exhibit B-1

ASSETS

| | | |
|--|----|--------------------------|
| Cash and Cash Equivalents | \$ | 3,251,338 |
| Restricted Cash | | 3,527,191 |
| Certificates of Deposit | | 1,263,913 |
| Accounts Receivable | | 14,344 |
| Lease Obligation Receivable, Net | | 40,957,474 |
| Pledges Receivable, Net | | 1,326,108 |
| Investment Securities | | 8,293,815 |
| Property and Equipment, Net | | 1,721,095 |
| Construction in Progress - Student Housing Project | | 1,042,900 |
| Deferred Financing Costs, Net | | 1,898,284 |
| | | <hr/> |
| Total Assets | \$ | <u><u>63,296,462</u></u> |

LIABILITIES AND NET ASSETS

| | | |
|--|----|-------------------|
| Trade Accounts Payable and Other Accruals | \$ | 408,942 |
| Accounts Payable - Student Housing Project | | 446,333 |
| Line of Credit | | 596,567 |
| Bonds Payable | | 47,930,000 |
| | | <hr/> |
| Total Liabilities | | <u>49,381,842</u> |

NET ASSETS

| | | |
|----------------------------------|----|--------------------------|
| Unrestricted | | 1,216,345 |
| Temporarily Restricted | | 5,826,839 |
| Permanently Restricted | | 6,871,436 |
| | | <hr/> |
| Total Net Assets | | <u>13,914,620</u> |
| | | <hr/> |
| Total Liabilities and Net Assets | \$ | <u><u>63,296,462</u></u> |

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

**Winston-Salem State University Foundation, Inc.
and Subsidiary**
Consolidated Statement of Activities
For the Year Ended June 30, 2012

Exhibit B-2

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|---------------------------------------|---------------------|-----------------------------------|-----------------------------------|----------------------|
| SUPPORT AND REVENUE | | | | |
| Gifts and Grants | \$ 446,556 | \$ 1,489,691 | \$ 171,428 | \$ 2,107,675 |
| Investment Income | 68,270 | | | 68,270 |
| Unrealized Gains on Investments | 960 | 158,834 | | 159,794 |
| Administrative Fees | 151,187 | | | 151,187 |
| Passport Income | 66,378 | | | 66,378 |
| Lease Income | 2,711,328 | | | 2,711,328 |
| Other | 139,539 | 338,700 | | 478,239 |
| | <u>3,584,218</u> | <u>1,987,225</u> | <u>171,428</u> | <u>5,742,871</u> |
| Net Assets Released from Restrictions | <u>1,698,064</u> | <u>(1,698,064)</u> | | |
| Total Support and Revenue | <u>5,282,282</u> | <u>289,161</u> | <u>171,428</u> | <u>5,742,871</u> |
| EXPENSES | | | | |
| Scholarships | 406,665 | | | 406,665 |
| Special Programs | 1,291,399 | | | 1,291,399 |
| Management and General | 841,767 | | | 841,767 |
| Depreciation and Amortization | 85,283 | | | 85,283 |
| Interest | 2,179,314 | | | 2,179,314 |
| Fundraising Expense | 150,524 | | | 150,524 |
| Total Expenses | <u>4,954,952</u> | | | <u>4,954,952</u> |
| Change in Net Assets | 327,330 | 289,161 | 171,428 | 787,919 |
| NET ASSETS | | | | |
| Net Assets, Beginning | <u>889,015</u> | <u>5,537,678</u> | <u>6,700,008</u> | <u>13,126,701</u> |
| Net Assets, Ending | <u>\$ 1,216,345</u> | <u>\$ 5,826,839</u> | <u>\$ 6,871,436</u> | <u>\$ 13,914,620</u> |

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

[This Page Left Blank Intentionally]

WINSTON-SALEM STATE UNIVERSITY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2012

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

- A. Financial Reporting Entity** - The concept underlying the definition of the financial reporting entity is that elected officials are accountable to their constituents for their actions. As required by accounting principles generally accepted in the United States of America (GAAP), the financial reporting entity includes both the primary government and all of its component units. An organization other than a primary government serves as a nucleus for a reporting entity when it issues separate financial statements. Winston-Salem State University is a constituent institution of the multi-campus University of North Carolina System, which is a component unit of the State of North Carolina and an integral part of the State's *Comprehensive Annual Financial Report*.

The accompanying financial statements present all funds belonging to the University and its component unit. While the Board of Governors of the University of North Carolina System has ultimate responsibility, the Chancellor, the Board of Trustees, and the Board of Trustees of the Endowment Fund have delegated responsibilities for financial accountability of the University's funds. The University's component unit is discretely presented in the University's financial statements. The discretely presented component unit's financial data is reported in separate financial statements because of its use of a different GAAP reporting model and to emphasize its legal separateness.

Discretely Presented Component Unit - The Winston-Salem State University Foundation, Inc. and Subsidiary (Foundation) is a legally separate not-for-profit corporation and is reported as a discretely presented component unit based on the nature and significance of its relationship to the University. The Winston-Salem State University Housing Foundation, LLC, is the wholly owned subsidiary of the Foundation.

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 Foundation board consists of not less than five and not more than 27 elected directors, with the number at any given time being set by the Board of Directors. In addition to the elected directors, the Chancellor and Vice Chancellor for University Advancement of Winston-Salem State University shall be voting members of the Board. Although the University does not control the timing or amount of receipts from the Foundation, the majority of resources, or income thereon, that the

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 reported in separate financial statements because of the difference in its reporting model, as described below.

The Foundation reports its financial results under Financial Accounting Standards Board (FASB) Statements. As such, certain revenue recognition criteria and presentation features are different from the Governmental Accounting Standards Board (GASB) revenue recognition criteria and presentation features. No modifications have been made to the Foundation's financial information in the University's financial reporting entity for these differences.

During the year ended June 30, 2012, the Foundation distributed \$656,665.00 to the University for both restricted and unrestricted purposes. Complete financial statements for the Foundation can be obtained from the Winston-Salem State University Foundation, Inc. and Subsidiary, 304 Blair Hall, 601 Martin Luther King, Jr. Drive, Winston-Salem, NC 27110, or by calling (336) 750-3005.

- B. Basis of Presentation** - The accompanying financial statements are presented in accordance with accounting principles generally accepted in the United States of America as prescribed by the GASB.

Pursuant to the provisions of GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements - and Management's Discussion and Analysis - for Public Colleges and Universities*, 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.

In accordance with GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the University does not apply FASB pronouncements issued after November 30, 1989, unless the GASB amends its pronouncements to specifically adopt FASB pronouncements issued after that date.

- C. Basis of Accounting** - The financial statements of the University have been prepared using the economic resource measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

recognized when earned, and expenses are recorded when an obligation has been incurred, regardless of the timing of the cash flows.

Nonexchange transactions, in which the University receives (or gives) value without directly giving (or receiving) equal value in exchange, include state appropriations, certain grants, and donations. Revenues are recognized, net of estimated uncollectible amounts, as soon as all eligibility requirements imposed by the provider have been met, if probable of collection.

- D. Cash and Cash Equivalents** - This classification includes deposits held by the State Treasurer in the Short-Term Investment Fund. The Short-Term Investment Fund maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit and withdraw cash at any time without prior notice or penalty.
- E. Investments** - This classification includes investments in an external investment pool and money market mutual funds. Investments are reported at fair value, as determined by quoted market prices. The net increase in the fair value of investments is recognized as a component of investment income.

Endowment investments include the principal amount of gifts and bequests that, according to donor restrictions, must be held in perpetuity or for a specified period of time, along with any accumulated investment earnings on such amounts.

- F. Receivables** - Receivables consist of tuition and fees charged to students and charges for auxiliary enterprises' sales and services. Receivables also include amounts due from the federal government, state and local governments, and private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants. Receivables are recorded net of estimated uncollectible amounts.
- G. Inventories** - Inventories of fuel oil held for consumption are valued at cost using the last invoice cost method. Inventories of postage are valued at the retail cost.
- H. Capital Assets** - Capital assets are stated at cost at date of acquisition or fair value at date of donation in the case of gifts. The value of assets constructed includes all material direct and indirect construction costs. Interest costs incurred are capitalized during the period of construction.

The University capitalizes assets that have a value or cost of \$5,000 or greater at the date of acquisition and an estimated useful life of more than one year except for purchased computer software which is capitalized when the value or cost is \$100,000 or greater.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 10 to 50 years for general infrastructure, 20 to 100 years for buildings, 5 to 20 years for equipment, and 2 to 30 years for computer software.

The Diggs Gallery collection is capitalized at cost or fair value at the date of donation. This collection is considered inexhaustible and is therefore not depreciated.

- I. Restricted Assets** - Certain resources are reported as restricted assets because restrictions on asset use change the nature or normal understanding of the availability of the asset. Resources that are not available for current operations and are reported as restricted include resources restricted for the acquisition or construction of capital assets, resources legally segregated for the payment of principal and interest as required by debt covenants, unspent debt proceeds, and endowment and other restricted investments.

- J. Noncurrent Long-Term Liabilities** - Noncurrent long-term liabilities include principal amounts of revenue bonds payable, notes payable, capital lease obligations, and compensated absences that will not be paid within the next fiscal year.

Revenue bonds payable are reported net of unamortized premiums. The University amortizes bond premiums over the life of the bonds using the straight-line method. Issuance costs are expensed.

- K. Compensated Absences** - The University's policy is to record the cost of vacation leave when earned. The policy provides for a maximum accumulation of unused vacation leave of 30 days which can be carried forward each January 1 or for which an employee can be paid upon termination of employment. When classifying compensated absences into current and noncurrent, leave is considered taken using a last-in, first-out (LIFO) method. Also, any accumulated vacation leave in excess of 30 days at year-end is converted to sick leave. Under this policy, the accumulated vacation leave for each employee at June 30 equals the leave carried forward at the previous December 31 plus the leave earned, less the leave taken between January 1 and June 30.

In addition to the vacation leave described above, compensated absences include the accumulated unused portion of the special annual leave bonuses awarded by the North Carolina General Assembly. The bonus leave balance on December 31 is retained by employees and transferred into the next calendar year. It is not subject to the limitation on annual leave carried forward described above and is not subject to conversion to sick leave.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

There is no liability for unpaid accumulated sick leave because the University has no obligation to pay sick leave upon termination or retirement. However, additional service credit for retirement pension benefits is given for accumulated sick leave upon retirement.

L. Net Assets - The University's net assets are classified as follows:

Invested in Capital Assets, Net of Related Debt - This represents the University's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of invested in capital assets, net of related debt.

Restricted Net Assets - Nonexpendable - Nonexpendable restricted net assets include endowments and similar type assets 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.

Restricted Net Assets - Expendable - Expendable restricted net assets include resources for which the University is legally or contractually obligated to spend in accordance with restrictions imposed by external parties.

Unrestricted Net Assets - Unrestricted net assets include resources derived from student tuition and fees, sales and services, unrestricted gifts, royalties, and interest income.

Restricted and unrestricted resources are tracked using a fund accounting system and are spent in accordance with established fund authorities. Fund authorities provide rules for the fund activity and are separately established for restricted and unrestricted activities. When both restricted and unrestricted funds are available for expenditure, the decision for funding is transactional based within the departmental management system in place at the University. For projects funded by tax-exempt debt proceeds and other sources, the debt proceeds are always used first.

M. Scholarship Discounts - Student tuition and fees revenues and certain other revenues from University charges are reported net of scholarship discounts in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. The scholarship discount is the difference between the actual charge for goods and services provided by the University and the amount that is paid by students or by third parties on the students' behalf. Student financial assistance grants, such as Pell grants, and other federal, state, or nongovernmental programs, are recorded as nonoperating revenues in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. To the extent that

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

revenues from these programs are used to satisfy tuition, fees, and other charges, the University has recorded a scholarship discount.

- N. Revenue and Expense Recognition** - The University classifies its revenues and expenses as operating or nonoperating in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the University's principal ongoing operations. Operating revenues include activities that have characteristics of exchange transactions, such as (1) student tuition and fees, (2) sales and services of auxiliary enterprises, (3) certain federal, state, and local grants and contracts that are essentially contracts for services, and (4) interest earned on loans. Operating expenses are all expense transactions incurred other than those related to capital and noncapital financing or investing activities as defined by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*.

Nonoperating revenues include activities that have the characteristics of nonexchange transactions. Revenues from nonexchange transactions and state appropriations that represent subsidies or gifts to the University, as well as investment income, are considered nonoperating since these are either investing, capital, or noncapital financing activities. Capital contributions are presented separately after nonoperating revenues and expenses.

- O. Internal Sales Activities** - Certain institutional auxiliary operations provide goods and services to University departments, as well as to its customers. These institutional auxiliary operations include activities such as copy centers, motor pool, postal services, telecommunications, and facilities rentals. In addition, the University has other miscellaneous sales and service units that operated either on a reimbursement or charge basis. All internal sales activities to University departments from auxiliary operations and sales and service units have been eliminated in the accompanying financial statements. These eliminations are recorded by removing the revenue and expense in the auxiliary operations and sales and service units and, if significant, allocating any residual balances to those departments receiving the goods and services during the year.

NOTE 2 - DEPOSITS AND INVESTMENTS

- A. Deposits** - Unless specifically exempt, the University is required by *North Carolina General Statute 147-77* to deposit moneys received with the State Treasurer or with a depository institution in the name of the State Treasurer. However, the University of North Carolina Board of

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Governors, pursuant to G.S. 116-36.1, may authorize the University to deposit its institutional trust funds in interest-bearing accounts and other investments authorized by the Board of Governors, without regard to any statute or rule of law relating to the investment of funds by fiduciaries. Although specifically exempted, the University may voluntarily deposit institutional trust funds, endowment funds, special funds, revenue bond proceeds, and debt service funds with the State Treasurer. Special funds consist of moneys for intercollegiate athletics and agency funds held directly by the University.

At June 30, 2012, the amount shown on the Statement of Net Assets as cash and cash equivalents includes \$27,274,219.12 which represents the University's equity position in the State Treasurer's Short-Term Investment Fund. The Short-Term Investment Fund (a portfolio within the State Treasurer's Investment Pool, an external investment pool that is not registered with the Securities and Exchange Commission and does not have a credit rating) had a weighted average maturity of 1.5 years as of June 30, 2012. Assets and shares of the Short-Term Investment Fund are valued at amortized cost, which approximates fair value. Deposit and investment risks associated with the State Treasurer's Investment Pool (which includes the State Treasurer's Short-Term Investment Fund) are included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.nc.gov/> and clicking on "Reports" or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

B. Investments

University - The University is authorized by The University of North Carolina Board of Governors pursuant to G.S. 116-36.2 and Section 600.2.4 of the Policy Manual of the University of North Carolina to invest its special funds in the same manner as the State Treasurer is required to invest, as discussed below.

G.S. 147-69.1(c), applicable to the State's General Fund, and G.S. 147-69.2, applicable to institutional trust funds, authorize the State Treasurer to invest in the following: obligations of or fully guaranteed by the United States; obligations of certain federal agencies; repurchase agreements; obligations of the State of North Carolina; time deposits of specified institutions; prime quality commercial paper; and asset-backed securities with specified ratings. Also, G.S. 147-69.1(c) authorizes the following: specified bills of exchange or time drafts and corporate bonds and notes with specified ratings. G.S. 147-69.2 authorizes the following: general obligations of other states; general obligations of North Carolina

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

local governments; and obligations of certain entities with specified ratings.

In accordance with the bond resolutions, bond proceeds and debt service funds are invested in obligations that will by their terms mature on or before the date funds are expected to be required for expenditure or withdrawal.

G.S. 116-36(e) provides that the trustees of the Endowment Fund shall be responsible for the prudent investment of the Fund in the exercise of their sound discretion, without regard to any statute or rule of law relating to the investment of funds by fiduciaries but in compliance with any lawful condition placed by the donor upon that part of the Endowment Fund to be invested.

Investments of the University's component unit, the Foundation, are subject to and restricted by G.S. 36E "Uniform Prudent Management of Institutional Funds Act" (UPMIFA) and any requirements placed on them by contract or donor agreements.

Investments of various funds may be pooled unless prohibited by statute or by terms of the gift or contract. The University utilizes investment pools to manage investments and distribute investment income.

Investments are subject to the following risks.

Interest Rate Risk: Interest rate risk is the risk the University may face should interest rate variances affect the fair value of investments. The University does not have a formal policy that addresses interest rate risk.

Credit Risk: Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The University does not have a formal policy that addresses credit risk.

UNC Investment Fund, LLC - At June 30, 2012, the University's investments include \$18,684,781.24 which represents the University's equity position in the UNC Investment Fund, LLC (UNC Investment Fund). The UNC Investment Fund is an external investment pool that is not registered with the Securities and Exchange Commission and does not have a credit rating. Asset and ownership interests of the UNC Investment Fund are determined on a market unit valuation basis each month. Investment risks associated with the UNC Investment Fund are included in audited financial statements of the UNC Investment Fund, LLC which may be obtained from UNC Management Company, Inc., 1400 Environ Way, Chapel Hill, NC 27517.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Non-Pooled Investments - The following table presents the fair value of investments by type and investments subject to interest rate risk at June 30, 2012, for the University's non-pooled investments.

Non-Pooled Investments

| | Fair Value | Investment Maturities (in Years) Less Than 1 |
|---------------------------|-----------------|--|
| Investment Type | | |
| Debt Securities | | |
| Money Market Mutual Funds | \$ 2,042,312.63 | \$ 2,042,312.63 |

At June 30, 2012, the Money Market Mutual Funds, with a fair value of \$2,042,312.63, were rated AAAM by Standard and Poor's.

Total Investments - The following table presents the fair value of the total investments at June 30, 2012:

| | Fair Value |
|---------------------------|------------------|
| Investment Type | |
| Debt Securities | |
| Money Market Mutual Funds | \$ 2,042,312.63 |
| Other Securities | |
| UNC Investment Fund | 18,684,781.24 |
| Total Investments | \$ 20,727,093.87 |

Component Unit - Investments of the University's discretely presented component unit, the Foundation, are subject to and restricted by G.S. 36E "Uniform Prudent Management of Institutional Funds Act" (UPMIFA) and any requirements placed on them by contract or donor agreements. Because the Foundation reports under the FASB reporting model, disclosures of the various investment risks are not required. The following is an analysis of investments by type:

| | Fair Value |
|-----------------------------|---------------|
| Investment Type | |
| UNC Investment Fund | \$ 7,281,453 |
| Money Market Fund | 20,258 |
| Mutual Funds | 992,104 |
| Total Investment Securities | \$ 8,293,815 |

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

C. Reconciliation of Deposits and Investments - A reconciliation of deposits and investments for the University as of June 30, 2012, is as follows:

| | | |
|--|-----------|-----------------------------|
| Deposits in the Short-Term Investment Fund | \$ | 27,274,219.12 |
| Investments in the UNC Investment Fund | | 18,684,781.24 |
| Non-Pooled Investments | | <u>2,042,312.63</u> |
| Total Deposits and Investments | \$ | <u>48,001,312.99</u> |
| | | |
| Deposits | | |
| Current: | | |
| Cash and Cash Equivalents | \$ | 13,318,069.82 |
| Restricted Cash and Cash Equivalents | | 9,218,058.18 |
| Noncurrent: | | |
| Restricted Cash and Cash Equivalents | | <u>4,738,091.12</u> |
| Total Deposits | \$ | <u>27,274,219.12</u> |
| | | |
| Investments | | |
| Current: | | |
| Restricted Short-Term Investments | \$ | 701,000.02 |
| Noncurrent: | | |
| Endowment Investments | | 18,684,781.24 |
| Other Investments | | <u>1,341,312.61</u> |
| Total Investments | \$ | <u>20,727,093.87</u> |

NOTE 3 - ENDOWMENT INVESTMENTS

Investments of the University's endowment funds are pooled, unless required to be separately invested by the donor. If a donor has not provided specific instructions, state law permits the Board of Trustees to authorize for expenditure the net appreciation, realized and unrealized, of the investments of the endowment funds. Under the "Uniform Prudent Management of Institutional Funds Act" (UPMIFA), authorized by the North Carolina General Assembly on March 19, 2009, the Board may also appropriate expenditures from eligible nonexpendable balances if deemed prudent and necessary to meet program outcomes and for which such spending is not specifically prohibited by the donor agreements. However, a majority of the University's endowment donor agreements prohibit spending of nonexpendable balances and therefore the related nonexpendable balances are not eligible for expenditure. During the year, the Board did not appropriate expenditures from eligible nonexpendable endowment funds.

Investment return of the University's endowment funds is predicated on the total return concept (yield plus appreciation). The total spending rate is calculated annually by taking the sum of the market value of the endowment investments for the preceding twelve quarters, and dividing the result by twelve. For the fiscal year ending June 30, 2012, the Board of Trustees

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

approved spending from the average value at a rate of five and one-half percent, paid out proportionately on a quarterly basis. To the extent that the total return for the current year exceeds the payout, the excess is added to principal. If current year earnings do not meet the payout requirements, the University uses accumulated income and appreciation from restricted, expendable net asset endowment balances to make up the difference. At June 30, 2012, net appreciation of \$2,558,976.41 was available to be spent, all of which was classified in net assets as restricted: expendable: scholarships and fellowships, professorships, and departmental uses as it is restricted for specific purposes.

NOTE 4 - RECEIVABLES

Receivables at June 30, 2012, were as follows:

| | <u>Gross Receivables</u> | <u>Less Allowance for Doubtful Accounts</u> | <u>Net Receivables</u> |
|--|-------------------------------|---|-------------------------------|
| Current Receivables: | | | |
| Students | \$ 3,131,963.95 | \$ 1,564,916.31 | \$ 1,567,047.64 |
| Accounts | 204,108.94 | | 204,108.94 |
| Intergovernmental | 1,539,238.62 | | 1,539,238.62 |
| Investment Earnings | 11,227.13 | | 11,227.13 |
| Interest on Loans | 205,206.17 | | 205,206.17 |
| Other | 20,102.49 | | 20,102.49 |
| Total Current Receivables | <u>\$ 5,111,847.30</u> | <u>\$ 1,564,916.31</u> | <u>\$ 3,546,930.99</u> |
| Notes Receivable: | | | |
| Notes Receivable - Current: | | | |
| Federal Loan Programs | \$ 133,234.17 | \$ 66,381.05 | \$ 66,853.12 |
| Institutional Student Loan Programs | 13,821.34 | 4,124.91 | 9,696.43 |
| Total Notes Receivable - Current | <u>\$ 147,055.51</u> | <u>\$ 70,505.96</u> | <u>\$ 76,549.55</u> |
| Notes Receivable - Noncurrent: | | | |
| Federal Loan Programs | \$ 1,008,371.90 | \$ 503,932.01 | \$ 504,439.89 |
| Institutional Student Loan Programs | 108,632.76 | 34,870.84 | 73,761.92 |
| Total Notes Receivable - Noncurrent | <u>\$ 1,117,004.66</u> | <u>\$ 538,802.85</u> | <u>\$ 578,201.81</u> |

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 5 - CAPITAL ASSETS

A summary of changes in the capital assets for the year ended June 30, 2012, is presented as follows:

| | Balance July 1, 2011 | Increases | Decreases | Balance June 30, 2012 |
|--|--------------------------|-------------------------|---------------------|--------------------------|
| Capital Assets, Nondepreciable: | | | | |
| Land | \$ 5,231,051.56 | \$ 0.00 | \$ 0.00 | \$ 5,231,051.56 |
| Art, Literature, and Artifacts | 898,772.00 | 55,000.00 | | 953,772.00 |
| Construction in Progress | 4,649,548.43 | 23,487,960.87 | | 28,137,509.30 |
| Total Capital Assets, Nondepreciable | <u>10,779,371.99</u> | <u>23,542,960.87</u> | | <u>34,322,332.86</u> |
| Capital Assets, Depreciable: | | | | |
| Buildings | 176,333,899.25 | | | 176,333,899.25 |
| Machinery and Equipment | 14,767,161.43 | 1,361,199.01 | 284,676.53 | 15,843,683.91 |
| General Infrastructure | 13,320,778.61 | | | 13,320,778.61 |
| Computer Software | 291,207.38 | 101,751.00 | | 392,958.38 |
| Total Capital Assets, Depreciable | <u>204,713,046.67</u> | <u>1,462,950.01</u> | <u>284,676.53</u> | <u>205,891,320.15</u> |
| Less Accumulated Depreciation/Amortization for: | | | | |
| Buildings | 52,096,913.87 | 4,646,993.51 | | 56,743,907.38 |
| Machinery and Equipment | 7,671,102.79 | 1,329,960.50 | 234,498.94 | 8,766,564.35 |
| General Infrastructure | 3,494,541.39 | 541,708.82 | | 4,036,250.21 |
| Computer Software | 29,120.74 | 70,960.36 | | 100,081.10 |
| Total Accumulated Depreciation/Amortization | <u>63,291,678.79</u> | <u>6,589,623.19</u> | <u>234,498.94</u> | <u>69,646,803.04</u> |
| Total Capital Assets, Depreciable, Net | <u>141,421,367.88</u> | <u>(5,126,673.18)</u> | <u>50,177.59</u> | <u>136,244,517.11</u> |
| Capital Assets, Net | <u>\$ 152,200,739.87</u> | <u>\$ 18,416,287.69</u> | <u>\$ 50,177.59</u> | <u>\$ 170,566,849.97</u> |

NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2012, were as follows:

| | Amount |
|---|------------------------|
| Accounts Payable | \$ 4,754,263.87 |
| Accrued Payroll | 698,226.65 |
| Contract Retainage | 1,228,780.15 |
| Total Accounts Payable and Accrued Liabilities | <u>\$ 6,681,270.67</u> |

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 7 - LONG-TERM LIABILITIES

UNIVERSITY

A. Changes in Long-Term Liabilities - A summary of changes in the long-term liabilities for the year ended June 30, 2012, is presented as follows:

| | Balance July 1, 2011 | Additions | Reductions | Balance June 30, 2012 | Current Portion |
|------------------------------------|-------------------------|-------------------------|------------------------|--------------------------|------------------------|
| Revenue Bonds Payable | \$ 14,695,000.00 | \$ 0.00 | \$ 1,135,000.00 | \$ 13,560,000.00 | \$ 1,200,000.00 |
| Add Premium | 48,005.73 | | 9,143.95 | 38,861.78 | |
| Total Revenue Bonds Payable | <u>14,743,005.73</u> | | <u>1,144,143.95</u> | <u>13,598,861.78</u> | <u>1,200,000.00</u> |
| Notes Payable | 82,073.48 | 6,517,358.00 | 82,073.48 | 6,517,358.00 | |
| Capital Leases Payable | 52,110,000.00 | | 1,300,000.00 | 50,810,000.00 | 1,350,000.00 |
| Compensated Absences | 4,469,192.00 | 3,583,338.00 | 3,194,996.77 | 4,857,533.23 | 663,585.23 |
| Total Long-Term Liabilities | <u>\$ 71,404,271.21</u> | <u>\$ 10,100,696.00</u> | <u>\$ 5,721,214.20</u> | <u>\$ 75,783,753.01</u> | <u>\$ 3,213,585.23</u> |

Additional information regarding capital lease obligations is included in Note 8.

B. Revenue Bonds Payable - The University was indebted for revenue bonds payable for the purposes shown in the following table:

| Purpose | Series | Interest Rate/ Ranges | Final Maturity Date | Original Amount of Issue | Principal Paid Through June 30, 2012 | Principal Outstanding June 30, 2012 | See Table Below |
|---|--------|-----------------------------|---------------------------|--------------------------------|--|---|-----------------------|
| Housing and Dining System | | | | | | | |
| UNC System Pool Revenue Bonds | 2008A | 3.00%-5.00% | 10/01/2033 | \$ 4,591,004.21 | \$ 323,221.77 | \$ 4,267,782.44 | |
| UNC System Pool Revenue Bonds | 2002B | 3.50%-5.37% | 04/01/2017 | 3,090,000.00 | 1,785,000.00 | 1,305,000.00 | |
| Revenue Refunding Bonds | 1998B | 3.70%-5.00% | 01/01/2017 | <u>8,430,000.00</u> | <u>4,990,000.00</u> | <u>3,440,000.00</u> | (1) |
| Total Housing and Dining System | | | | <u>16,111,004.21</u> | <u>7,098,221.77</u> | <u>9,012,782.44</u> | |
| Student Services System | | | | | | | |
| UNC System Pool Revenue Bonds | 2008A | 3.00%-5.00% | 10/01/2033 | 2,723,995.79 | 191,778.23 | 2,532,217.56 | |
| UNC System Pool Revenue Bonds | 2004B | 3.00%-5.00% | 04/01/2022 | <u>2,925,000.00</u> | <u>910,000.00</u> | <u>2,015,000.00</u> | |
| Total Student Services System | | | | <u>5,648,995.79</u> | <u>1,101,778.23</u> | <u>4,547,217.56</u> | |
| Total Revenue Bonds Payable (principal only) | | | | <u>\$ 21,760,000.00</u> | <u>\$ 8,200,000.00</u> | 13,560,000.00 | |
| Plus: Unamortized Premium | | | | | | <u>38,861.78</u> | |
| Total Revenue Bonds Payable | | | | | | <u>\$ 13,598,861.78</u> | |

The University has pledged future revenues, net of specific operating expenses, to repay revenue bonds as shown in the table below:

| Ref | Revenue Source | Total Future Revenues Pledged | Current Year | | | Estimate of % of Revenues Pledged |
|-----|-----------------------------|----------------------------------|-----------------------------|----------------------|----------------------|--------------------------------------|
| | | | Revenues Net of Expenses | Principal | Interest | |
| (1) | Housing and Dining Revenues | <u>\$ 3,974,250.00</u> | <u>\$ 2,695,221.35</u> | <u>\$ 580,000.00</u> | <u>\$ 186,210.00</u> | 41% |

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

C. Annual Requirements - The annual requirements to pay principal and interest on the long-term obligations at June 30, 2012, are as follows:

| Fiscal Year | Annual Requirements | | | |
|---------------------------|-------------------------|------------------------|------------------------|------------------------|
| | Revenue Bonds Payable | | Notes Payable | |
| | Principal | Interest | Principal | Interest |
| 2013 | \$ 1,200,000.00 | \$ 626,332.50 | \$ 0.00 | \$ 435,159.92 |
| 2014 | 1,255,000.00 | 571,200.00 | 211,089.17 | 258,669.12 |
| 2015 | 1,325,000.00 | 509,931.26 | 259,493.44 | 236,672.87 |
| 2016 | 1,395,000.00 | 444,331.26 | 283,425.39 | 226,416.37 |
| 2017 | 1,460,000.00 | 373,475.00 | 290,578.47 | 215,442.81 |
| 2018-2022 | 2,385,000.00 | 1,383,228.14 | 2,183,669.57 | 858,579.18 |
| 2023-2027 | 1,585,000.00 | 919,075.06 | 3,109,369.39 | 360,256.92 |
| 2028-2032 | 2,005,000.00 | 495,515.63 | 179,732.57 | 1,712.03 |
| 2033-2034 | 950,000.00 | 48,000.00 | | |
| Total Requirements | \$ 13,560,000.00 | \$ 5,371,088.85 | \$ 6,517,358.00 | \$ 2,592,909.22 |

D. Notes Payable - The University was indebted for notes payable for the purpose shown in the following table:

| Purpose | Financial Institution | Interest Rate | Final Maturity Date | Original Amount of Issue | Principal Paid Through June 30, 2012 | Principal Outstanding June 30, 2012 |
|-----------------------------|-----------------------|---------------|---------------------|--------------------------|--------------------------------------|-------------------------------------|
| Energy Performance Contract | Siemens Public, Inc. | 3.81% | 09/30/2027 | \$ 6,517,358.00 | \$ 0.00 | \$ 6,517,358.00 |

On September 15, 2011, the University entered into an installment financing contract with Siemens Public, Inc. for \$6,517,358.00 resulting in a Guaranteed Energy Savings Notes Payable with an interest rate of 3.81% per annum fixed, maturing on September 30, 2027. The University shall pay the purchase price plus interest to Siemens Public, Inc. in quarterly installments consisting solely of interest commencing on September 15, 2012, and then in quarterly installments consisting of principal and interest commencing on September 30, 2013.

COMPONENT UNIT

Bonds Payable - Three student housing facilities have been financed through the issuance of bonds. In December 2001, \$17,665,000.00 of Series 2001 bonds were issued by the North Carolina Facilities Finance Agency to fund the construction of Rams Commons. The bonds were scheduled to mature at various intervals through 2031.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

In September 2004, \$35,900,000.00 of Series 2004 bonds were issued. The proceeds of this issuance were used to retire the Series 2001 bonds, and to finance the construction of Gleason-Hairston Terrace. These bonds mature at various intervals through 2036, and bear interest at fixed rates ranging from 3% to 5%.

In October 2006, \$18,835,000.00 of Series 2006 bonds were issued. The proceeds of this issuance were used to finance the construction of Foundation Heights. These bonds mature at various intervals through 2038, and bear interest at fixed rates from 3% to 5%.

| Fiscal Year | Bonds Payable |
|--------------------|---------------|
| 2013 | \$ 1,255,000 |
| 2014 | 1,295,000 |
| 2015 | 1,340,000 |
| 2016 | 1,395,000 |
| 2017 | 1,455,000 |
| Thereafter | 41,190,000 |
| Total Requirements | \$ 47,930,000 |

NOTE 8 - LEASE OBLIGATIONS

A. Capital Lease Obligations - Capital lease obligations relating to University student housing and athletic facilities are recorded at the present value of the minimum lease payments. Future minimum lease payments under capital lease obligations consist of the following at June 30, 2012:

| Fiscal Year | Amount |
|--|-------------------------|
| 2013 | \$ 3,626,473.02 |
| 2014 | 3,620,391.02 |
| 2015 | 3,618,637.26 |
| 2016 | 3,623,336.76 |
| 2017 | 3,629,602.02 |
| 2018-2022 | 18,130,964.54 |
| 2023-2027 | 18,110,817.32 |
| 2028-2032 | 17,891,487.52 |
| 2033-2036 | 11,289,793.76 |
| Total Minimum Lease Payments | 83,541,503.22 |
| Amount Representing Interest (3.00% - 5.00% Rate of Interest) | 32,731,503.22 |
| Present Value of Future Lease Payments | \$ 50,810,000.00 |

Buildings acquired under capital lease amounted to \$58,035,000.00 at June 30, 2012. Depreciation for the capital assets associated with capital leases is included in depreciation expense.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

B. Operating Lease Obligations - The University entered into operating leases for athletic fields, office space, and parking. Future minimum lease payments under noncancelable operating leases consist of the following at June 30, 2012:

| Fiscal Year | Amount |
|-------------------------------------|----------------------|
| 2013 | \$ 348,547.41 |
| 2014 | 27,839.12 |
| 2015 | 24,903.21 |
| 2016 | 25,100.83 |
| 2017 | 25,304.37 |
| 2018-2022 | 90,110.56 |
| 2023-2027 | 44,301.90 |
| 2028-2032 | 51,358.05 |
| 2033-2037 | 59,538.09 |
| 2038-2039 | 26,390.83 |
| Total Minimum Lease Payments | \$ 723,394.37 |

Rental expense for all operating leases during the year was \$1,317,679.07.

NOTE 9 - REVENUES

A summary of eliminations and allowances by revenue classification is presented as follows:

| | Gross Revenues | Internal Sales Eliminations | Less Scholarship Discounts | Less Allowance for Uncollectibles | Net Revenues |
|--|-------------------------|-----------------------------------|----------------------------------|---|-------------------------|
| Operating Revenues: | | | | | |
| Student Tuition and Fees | \$ 31,989,710.38 | \$ 0.00 | \$ 10,621,397.88 | \$ 220,379.30 | \$ 21,147,933.20 |
| Sales and Services: | | | | | |
| Sales and Services of Auxiliary Enterprises: | | | | | |
| Residential Life | \$ 12,242,836.92 | \$ 0.00 | \$ 4,321,756.20 | \$ 84,688.09 | \$ 7,836,392.63 |
| Dining | 5,295,710.34 | | 1,612,926.96 | 38,988.98 | 3,643,794.40 |
| Student Union Services | 1,094,065.62 | | | 2,547.75 | 1,091,517.87 |
| Health, Physical Education, and Recreation Services | 97,612.64 | | | | 97,612.64 |
| Parking | 837,684.79 | | | 1,306.30 | 836,378.49 |
| Athletic | 217,970.00 | | | | 217,970.00 |
| Telecommunications | 1,214,518.74 | 1,197,927.25 | | | 16,591.49 |
| Print Shop | 122,873.36 | 122,873.36 | | | |
| Transport Services | 317,113.29 | 317,113.29 | | | |
| Other | 218,233.89 | | | | 218,233.89 |
| Total Sales and Services | \$ 21,658,619.59 | \$ 1,637,913.90 | \$ 5,934,683.16 | \$ 127,531.12 | \$ 13,958,491.41 |

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 10 - OPERATING EXPENSES BY FUNCTION

The University's operating expenses by functional classification are presented as follows:

| | Salaries and Benefits | Supplies and Materials | Services | Scholarships and Fellowships | Utilities | Depreciation/ Amortization | Total |
|-------------------------------------|-----------------------------|------------------------------|-------------------------|------------------------------------|------------------------|-------------------------------|--------------------------|
| Instruction | \$ 46,575,333.64 | \$ 1,455,509.73 | \$ 3,917,689.03 | \$ 918,007.06 | \$ 0.00 | \$ 0.00 | \$ 52,866,539.46 |
| Research | 908,310.05 | 287,408.60 | 500,962.93 | 15,010.00 | | | 1,711,691.58 |
| Public Service | 781,141.18 | 386,077.73 | 481,533.45 | 12,750.00 | | | 1,661,502.36 |
| Academic Support | 6,055,505.45 | 2,353,919.30 | 1,735,940.20 | 5,000.00 | | | 10,150,364.95 |
| Student Services | 3,790,408.10 | 187,739.79 | 623,359.07 | 11,574.00 | | | 4,613,080.96 |
| Institutional Support | 11,493,133.80 | 959,739.88 | 3,385,447.40 | | | | 15,838,321.08 |
| Operations and Maintenance of Plant | 6,735,008.77 | 1,247,027.07 | 3,854,708.33 | | 1,583,889.90 | | 13,420,634.07 |
| Student Financial Aid | 401,038.08 | | 2,959.13 | 10,279,787.09 | | | 10,683,784.30 |
| Auxiliary Enterprises | 6,700,739.62 | 757,824.22 | 10,658,350.61 | 1,386,225.05 | 1,156,631.19 | | 20,659,770.69 |
| Depreciation/ Amortization | | | | | | 6,589,623.19 | 6,589,623.19 |
| Total Operating Expenses | \$ 83,440,618.69 | \$ 7,635,246.32 | \$ 25,160,950.15 | \$ 12,628,353.20 | \$ 2,740,521.09 | \$ 6,589,623.19 | \$ 138,195,312.64 |

NOTE 11 - PENSION PLANS

A. Retirement Plans - Each permanent full-time employee, as a condition of employment, is a member of either the Teachers' and State Employees' Retirement System or the Optional Retirement Program. Eligible employees can elect to participate in the Optional Retirement Program at the time of employment, otherwise they are automatically enrolled in the Teachers' and State Employees' Retirement System.

The Teachers' and State Employees' Retirement System (Plan) is a cost-sharing multiple-employer defined benefit pension plan established by the State to provide pension benefits for employees of the State, its component units, and local boards of education. The Plan is administered by the North Carolina State Treasurer.

Benefit and contribution provisions for the Teachers' and State Employees' Retirement System are established by *North Carolina General Statutes* 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contribution rates are set each year by the North Carolina General Assembly based on annual actuarial valuations. For the year ended June 30, 2012, these rates were set at 7.44% of covered payroll for employers and 6% of covered payroll for members.

For the current fiscal year, the University had a total payroll of \$65,342,262.91, of which \$35,827,356.81 was covered under the Teachers' and State Employees' Retirement System. Total employer and employee contributions for pension benefits for the year were \$2,665,555.35 and \$2,149,641.41, respectively.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Required employer contribution rates for the years ended June 30, 2011, and 2010, were 4.93% and 3.57%, respectively, while employee contributions were 6% each year. The University made 100% of its annual required contributions for the years ended June 30, 2012, 2011, and 2010, which were \$2,665,555.35, \$1,729,323.28, and \$1,228,010.43, respectively.

The Teachers' and State Employees' Retirement System's financial information is included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.nc.gov/> and clicking on "Reports" or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

The Optional Retirement Program (Program) is a defined contribution retirement plan that provides retirement benefits with options for payments to beneficiaries in the event of the participant's death. Administrators and eligible faculty of the University may join the Program instead of the Teachers' and State Employees' Retirement System. The Board of Governors of The University of North Carolina is responsible for the administration of the Program and designates the companies authorized to offer investment products or the trustee responsible for the investment of contributions under the Program and approves the form and contents of the contracts and trust agreements.

Participants in the Program are immediately vested in the value of employee contributions. The value of employer contributions is vested after five years of participation in the Program. Participants become eligible to receive distributions when they terminate employment or retire.

Participant eligibility and contributory requirements are established by General Statute 135-5.1. Employer and member contribution rates are set each year by the North Carolina General Assembly. For the year ended June 30, 2012, these rates were set at 6.84% of covered payroll for employers and 6% of covered payroll for members. The University assumes no liability other than its contribution.

For the current fiscal year, the University had a total payroll of \$65,342,262.91, of which \$21,566,306.88 was covered under the Optional Retirement Program. Total employer and employee contributions for pension benefits for the year were \$1,475,135.39 and \$1,293,978.41, respectively.

B. Deferred Compensation and Supplemental Retirement Income Plans - Internal Revenue Code Section 457 Plan - The State of North

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Carolina offers its permanent employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457 through the North Carolina Public Employee Deferred Compensation Plan (the Plan). The Plan permits each participating employee to defer a portion of his or her salary until future years. The deferred compensation is available to employees upon separation from service, death, disability, retirement, or financial hardships if approved by the Board of Trustees of the Plan. The Board, a part of the North Carolina Department of Administration, maintains a separate fund for the exclusive benefit of the participating employees and their beneficiaries, *the North Carolina Public Employee Deferred Compensation Trust Fund*. The Board also contracts with an external third party to perform certain administrative requirements and to manage the trust fund's assets. All costs of administering and funding the Plan are the responsibility of the Plan participants. No costs are incurred by the University. The voluntary contributions by employees amounted to \$175,027.00 for the year ended June 30, 2012.

Internal Revenue Code Section 401(k) Plan - All members of the Teachers' and State Employees' Retirement System and the Optional Retirement Program are eligible to enroll in the Supplemental Retirement Income Plan, a defined contribution plan, created under Internal Revenue Code Section 401(k). All costs of administering the Plan are the responsibility of the Plan participants. No costs are incurred by the University except for a 5% employer contribution for the University's law enforcement officers, which is mandated under General Statute 143-166.30(e). Total employer contributions on behalf of University law enforcement officers for the year ended June 30, 2012, were \$39,453.57. The voluntary contributions by employees amounted to \$273,146.57 for the year ended June 30, 2012.

Internal Revenue Code Section 403(b) and 403(b)(7) Plans - Eligible University employees can participate in tax sheltered annuity plans created under Internal Revenue Code Sections 403(b) and 403(b)(7). The employee's eligible contributions, made through salary reduction agreements, are exempt from federal and state income taxes until the annuity is received or the contributions are withdrawn. These plans are exclusively for employees of universities and certain charitable and other nonprofit institutions. All costs of administering and funding these plans are the responsibility of the Plan participants. The plan administrators are Fidelity and TIAA-CREF. No costs are incurred by the University. The voluntary contributions by employees amounted to \$704,168.02 for the year ended June 30, 2012.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 12 - OTHER POSTEMPLOYMENT BENEFITS

- A. **Health Benefits** - The University participates in the Comprehensive Major Medical Plan (the Plan), a cost-sharing, multiple-employer defined benefit health care plan that provides postemployment health insurance to eligible former employees. Eligible former employees include long-term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers' and State Employees' Retirement System or the Optional Retirement Program. Coverage eligibility varies depending on years of contributory membership service in their retirement system prior to disability or retirement.

The Plan's benefit and contribution provisions are established by the State Treasurer and the Board of Trustees of the State Health Plan for Teachers and State Employees as authorized by Chapter 135, Article 3B, of the General Statutes. The Plan does not provide for automatic post-retirement benefit increases.

By General Statute, a Retiree Health Benefit Fund (the Fund) has been established as a fund in which accumulated contributions from employers and any earnings on those contributions shall be used to provide health benefits to retired and disabled employees and applicable beneficiaries. By statute, the Fund is administered by the Board of Trustees of the Teachers' and State Employees' Retirement System and contributions to the fund are irrevocable. Also by law, Fund assets are dedicated to providing benefits to retired and disabled employees and applicable beneficiaries and are not subject to the claims of creditors of the employers making contributions to the Fund. Contribution rates to the Fund, which are intended to finance benefits and administrative expenses on a pay-as-you-go basis, are determined by the State Treasurer and the Board of Trustees of the State Health Plan for Teachers and State Employees.

For the current fiscal year the University contributed 5.0% of the covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the Fund. Required contribution rates for the years ended June 30, 2011, and 2010, were 4.9% and 4.5%, respectively. The University made 100% of its annual required contributions to the Plan for the years ended June 30, 2012, 2011, and 2010, which were \$2,869,683.18, \$2,782,760.77, and \$2,507,221.48, respectively. The University assumes no liability for retiree health care benefits provided by the programs other than its required contribution.

Additional detailed information about these programs can be located in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Carolina Office of the State Controller's Internet home page <http://www.osc.nc.gov/> and clicking on "Reports" or by calling the State Controller's Financial Reporting Section at (919) 707-0500.

- B. Disability Income** - The University participates in the Disability Income Plan of North Carolina (DIPNC), a cost-sharing, multiple-employer defined benefit plan, to provide short-term and long-term disability benefits to eligible members of the Teachers' and State Employees' Retirement System and the Optional Retirement Program. Benefit and contribution provisions are established by Chapter 135, Article 6, of the General Statutes, and may be amended only by the North Carolina General Assembly. The Plan does not provide for automatic post-retirement benefit increases.

Disability income benefits are funded by actuarially determined employer contributions that are established by the General Assembly. For the fiscal year ended June 30, 2012, the University made a statutory contribution of .52% of covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the DIPNC. The required contribution rate for the years ended June 30, 2011 and 2010 was .52% for both years. The University made 100% of its annual required contributions to the DIPNC for the years ended June 30, 2012, 2011, and 2010, which were \$298,447.06, \$295,313.39, and \$289,723.37, respectively. The University assumes no liability for long-term disability benefits under the Plan other than its contribution.

Additional detailed information about the DIPNC is disclosed in the State of North Carolina's *Comprehensive Annual Financial Report*.

NOTE 13 - RISK MANAGEMENT

The University is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These exposures to loss are handled via a combination of methods, including participation in state-administered insurance programs, purchase of commercial insurance, and self-retention of certain risks. There have been no significant reductions in insurance coverage from the previous year and settled claims have not exceeded coverage in any of the past three fiscal years.

The risk of tort claims of up to \$1,000,000 per claimant is retained under the authority of the State Tort Claims Act. In addition, the State provides excess public officers' and employees' liability insurance up to \$10,000,000 via contract with a private insurance company. The University pays the premium, based on a composite rate, directly to the private insurer.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The University is required to maintain fire and lightning coverage on all state-owned buildings and contents through the State Property Fire Insurance Fund (Fund), an internal service fund of the State. Such coverage is provided at no cost to the University for operations supported by the State's General Fund. Other operations not supported by the State's General Fund are charged for the coverage. Losses covered by the Fund are subject to a \$5,000 per occurrence deductible. However, some agencies have chosen a higher deductible for a reduction in premium. The University also purchased through the Fund extended coverage against losses caused by windstorm or hail, explosion, smoke, aircraft or vehicles, and riot or civil commotion on certain buildings and contents. In addition, the University purchased "all risk" coverage through the Fund for a particular tower and various buildings.

All state-owned vehicles are covered by liability insurance through a private insurance company and handled by the North Carolina Department of Insurance. The liability limits for losses are \$1,000,000 per claim and \$10,000,000 per occurrence. The University pays premiums to the North Carolina Department of Insurance for the coverage.

The University is protected for losses from employee dishonesty and computer fraud. This coverage is with a private insurance company and is handled by the North Carolina Department of Insurance. Universities are charged a premium by the private insurance company. Coverage limit is \$5,000,000 per occurrence. The private insurance company pays 90% of each loss less a \$75,000 deductible.

University employees and retirees are provided comprehensive major medical care benefits. Coverage is funded by contributions to the State Health Plan (Plan), a discretely presented component unit of the State of North Carolina. The Plan has contracted with third parties to process claims.

The North Carolina Workers' Compensation Program provides benefits to workers injured on the job. All employees of the State and its component units are included in the program. When an employee is injured, the University's primary responsibility is to arrange for and provide the necessary treatment for work related injury. The University is responsible for paying medical benefits and compensation in accordance with the North Carolina Workers' Compensation Act. The University retains the risk for workers' compensation.

Term life insurance (death benefits) of \$25,000 to \$50,000 is provided to eligible workers. This Death Benefit Plan is administered by the State Treasurer and funded via employer contributions. The employer contribution rate was .16% for the current fiscal year.

NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)

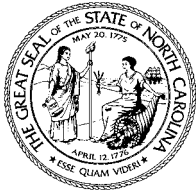
Additional details on the state-administered risk management programs are disclosed in the State's *Comprehensive Annual Financial Report*, issued by the Office of the State Controller.

NOTE 14 - COMMITMENTS AND CONTINGENCIES

- A. **Commitments** - The University has established an encumbrance system to track its outstanding commitments on construction projects and other purchases. Outstanding commitments on construction contracts were \$17,123,326.56 and on other purchases were \$2,070,069.74 at June 30, 2012.

- B. **Pending Litigation and Claims** - The University is a party to litigation and claims in the ordinary course of its operations. Since it is not possible to predict the ultimate outcome of these matters, no provision for any liability has been made in the financial statements. University management is of the opinion that the liability, if any, for any of these matters will not have a material adverse effect on the financial position of the University.

[This Page Left Blank Intentionally]



Beth A. Wood, CPA
State Auditor

STATE OF NORTH CAROLINA
Office of the State Auditor

2 S. Salisbury Street
20601 Mail Service Center
Raleigh, NC 27699-0601
Telephone: (919) 807-7500
Fax: (919) 807-7647
Internet
<http://www.ncauditor.net>

**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**

Board of Trustees
Winston-Salem State University
Winston-Salem, North Carolina

We have audited the financial statements of Winston-Salem State University, a constituent institution of the multi-campus University of North Carolina System, which is a component unit of the State of North Carolina, and its discretely presented component unit, as of and for the year ended June 30, 2012, which collectively comprise the University's basic financial statements and have issued our report thereon dated November 20, 2012. Our report includes a reference to other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Other auditors audited the financial statements of the discretely presented component unit, as described in our report on the University's financial statements. The financial statements of the discretely presented component unit were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

The University's management is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the University's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the University's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the University's financial statements will not be prevented, or detected and corrected on a timely basis.

**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 (CONCLUDED)**


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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the University's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The University's response to the finding identified in our audit is described in the Audit Findings and Responses section of this report. We did not audit the University's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management of the University, the Board of Governors, the Board of Trustees, the Audit Committee, others within the entity, the Governor, the General Assembly, and the State Controller, and is not intended to be and should not be used by anyone other than these specified parties.



Beth A. Wood, CPA
State Auditor

November 20, 2012

AUDIT FINDINGS AND RESPONSES

Matters Related to Financial Reporting

The following audit finding was identified during the current audit and describes a condition that represents a deficiency in internal control.

PAYROLL DEFICIENCIES IN INFORMATION SYSTEM ACCESS AND TIME ENTRY APPROVALS

We identified payroll-related deficiencies in the University's information system access and time entry approvals for hourly employees. As a result, there is an increased risk of error, misappropriation, and improper payroll disbursements, without timely detection.

During our review of the information system access and time entry approvals for payroll, we identified the following deficiencies:

- A human resources office employee had access rights that were inconsistent with her job duties. This employee could create new employees; modify pay rates of existing employees; including her own; process payroll; set up direct deposit information; and make changes to bank account numbers associated with direct deposits. Employees should be granted the minimum access rights needed to perform their job, and the duties should be segregated such that one employee cannot process a transaction from beginning to end.
- Payroll time entries for hourly employees were not always approved by the designated supervisor prior to payroll disbursements.

During the audit year, 487 timesheets for hourly employees were approved in the Banner payroll system by the payroll manager or the payroll specialist, who were not the supervisors designated to perform this approval function. The payroll personnel have been granted access in the Banner payroll system to electronically approve employee timesheets, and they do so when the supervisor does not perform these approvals in the payroll system. However, such payroll personnel approvals should occur only upon authorization from the supervisor verifying the hours worked by the employee. We examined 49 of the 487 timesheets approved by the payroll personnel for evidence of manual approval of hours worked by the employee's supervisor and found that 22 of the 49 timesheets were manually approved by the supervisor. The remaining 27 timesheets or 55% did not contain evidence of supervisory approval of hours worked.

Recommendation: The University should strengthen internal controls over its information system access and time entry approvals for payroll by limiting employees' access rights to those that are only necessary to perform their job duties. Assignment of employees' access and security classes should be evaluated to ensure adequate segregation of duties. In addition, the University should ensure that time entered into the payroll system is properly verified by the employee's supervisor or his designee prior to payroll disbursements. Electronic time

AUDIT FINDINGS AND RESPONSES (CONCLUDED)

entry approvals by payroll personnel should be supported by authorization from the employee's supervisor verifying the hours worked.

University's Response: We concur. A thorough review of the security class assigned to the employee in question and appropriate modifications to the access granted have been made. Specifically, many of the Payroll and Budget application forms previously granted with 'M'odify access has been changed to 'Q'uary access, including the GXADIRD form which would allow the employee to set up direct deposit accounts whereby payroll payments could be inappropriately routed.

We concur. The university has limited employees' access rights to three employees within Payroll and Human Resources that need time entry approval to perform their job duties. Employees' access and security classes are evaluated annually to ensure adequate segregation of duties. Time entry will only be approved by written approval from the supervisor or department (when supervisor is not available). During the audit period the university took the stand to not have any employees who keyed their time into the time entry system to not be penalized by not receiving their paycheck on time due to supervisors not approving their employees' timesheets, especially during the holiday periods. We have now put the responsibility back into the hands of the approver to make sure their employees time have been approved during the pay cycle or the employee's payment will be delayed until the approver has sent written approval.

ORDERING INFORMATION

Audit reports issued by the Office of the State Auditor can be obtained from the web site at www.ncauditor.net. Also, parties may register on the web site to receive automatic email notification whenever reports of interest are issued. Otherwise, copies of audit reports may be obtained by contacting the:

Office of the State Auditor
State of North Carolina
2 South Salisbury Street
20601 Mail Service Center
Raleigh, North Carolina 27699-0601

Telephone: 919/807-7500

Facsimile: 919/807-7647

This audit required 1,099 audit hours at an approximate cost of \$79,128. The cost represents .04% of the University's total assets and .06% of total expenses subjected to audit.