

# **Arkansas State University**

**State University, Arkansas**

## **Annual Financial Report Independent Auditor's Report and Other Reports June 30, 2004**

LEGISLATIVE JOINT AUDITING COMMITTEE

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Senate Co-Chair  
Rep. Tommy G. Roebuck  
House Co-Chair  
Sen. Randy Laverty  
Senate Co-Vice Chair  
Rep. David Evans  
House Co-Vice Chair

# Arkansas



Charles L. Robinson, CPA, CFE  
Legislative Auditor

## LEGISLATIVE JOINT AUDITING COMMITTEE DIVISION OF LEGISLATIVE AUDIT

### INDEPENDENT AUDITOR'S REPORT

Arkansas State University  
Legislative Joint Auditing Committee

We have audited the accompanying basic financial statements of Arkansas State University (University), an Institution of Higher Education of the State of Arkansas, as of and for the year ended June 30, 2004 as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the Arkansas State University Foundation, Inc., which represent 100% of the assets, net assets, and revenues of the discretely presented component unit. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it related to the amounts included for the Arkansas State University Foundation, Inc., is 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 the Arkansas State University Foundation, Inc., 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 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 Arkansas State University and of its discretely presented component unit as of June 30, 2004 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.

Management's discussion and analysis is not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consist principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 23, 2004 on our consideration of the University's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

DIVISION OF LEGISLATIVE AUDIT

A handwritten signature in blue ink, appearing to read "Charles L. Robinson".

Charles L. Robinson, CPA, CFE  
Legislative Auditor

Little Rock, Arkansas  
November 23, 2004  
EDHE12504

Sen. Henry "Hank" Wilkins, IV  
Senate Co-Chair  
Rep. Tommy G. Roebuck  
House Co-Chair  
Sen. Randy Laverty  
Senate Co-Vice Chair  
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House Co-Vice Chair

# Arkansas



Charles L. Robinson, CPA, CFE  
Legislative Auditor

## LEGISLATIVE JOINT AUDITING COMMITTEE DIVISION OF LEGISLATIVE AUDIT

### COMBINED REPORT(S) ON COMPLIANCE, INTERNAL CONTROLS AND OTHER MATTERS

Arkansas State University  
Legislative Joint Auditing Committee

The underlying purpose of this letter is to convey certain observations and recommendations regarding state and federal compliance and internal control in conjunction with our audit of Arkansas State University (University). This letter reflects various requirements and pronouncements of the American Institute of Certified Public Accountants (AICPA), the United States General Accounting Office (GAO), and the United States Office of Management and Budget (OMB).

We have audited the financial statements of Arkansas State University, an Institution of Higher Education of the State of Arkansas, as of and for the year ended June 30, 2004, and have issued our report thereon dated November 23, 2004, which included a reference to the report of other auditors. We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. The financial statements of the Arkansas State University Foundation, Inc., were not audited in accordance with *Government Auditing Standards*.

#### Compliance

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 the state constitution, state and federal laws and regulations, and federal contracts and grants, 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 that are required to be reported under *Government Auditing Standards*.

#### Internal Control Over Financial Reporting

In planning and performing our audit, we considered the University's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. Other matters involving compliance and/or internal control were reported to University management in a separate letter.

## AUDIT FINDINGS

As a management service, we would like to bring to your attention the following compliance and/or internal control matter(s) that came to our attention during this audit. The purpose of such comments is to provide constructive feedback and guidance, in an effort to assist management to maintain a satisfactory level of compliance with the state constitution, laws and regulations and achieve adequate internal controls. These matters were discussed previously with University officials during the course of our audit fieldwork and at the exit conference.

1. During our examination of the accounting procedures for capital assets, capitalization and classification errors were detected. Specifically, certain costs pertaining to the construction of the student union had been charged to non-capital accounts. Personnel in the controller's office did not properly analyze these accounts for capital costs until the audit was in progress. University officials subsequently determined costs of \$1,218,314 had not been properly capitalized at year-end. Additionally, a lack of effective communication between the construction and controller's offices regarding the types of items to be charged to the non-capital accounts contributed to this error.

The construction costs of a track facility were entirely capitalized as buildings. However, costs of \$1,941,011 should have been allocated to recreational improvements. Additionally, a real estate acquisition was entirely capitalized as land. However, costs of \$1,963,662 should have been allocated to buildings. Due care must be exercised in the capitalization procedures of all applicable transactions.

University officials prepared the necessary corrections to all accounts during our audit fieldwork.

### **Our audit of the University's data center and Loan Management System (LMS) and Student Information System (SIS) applications revealed the following:**

2. Access Security Controls are not adequate.

The following weaknesses were noted:

- Terminated employee accounts are not being removed in a timely manner.
- Access security privileges assigned to users appear to be excessive in some cases.

#### Recommendation

We recommend the following corrective action for the above-mentioned points as follows:

- Security Administrator establish a process to periodically review all user accounts to ensure that only authorized individuals have the ability to access applications and terminated employee account be removed in a timely manner.
- Develop and implement a formal review process to establish adequate, yet not excessive, security access privilege needs by job role and or specific employee, and a process be established for comparing those needs to actual security access privileges granted.

3. Program Change Controls are not adequate.

The following weaknesses were noted:

- Various deficiencies identified on requests reviewed to include some without Department Head field populated, Priority Category or Priority Justification field populated, Need By (Target Date) field populated, Assigned Date field populated and requests with a "DATE COMPLETED" later than the "NEED BY" date indicated by the user.
- There is no automated system being used to monitor changes to source code. Currently, the Information and Technology Services Department depends on manual procedures to monitor changes to source code but there are no safeguards or controls to ensure that source code is in sync with compiled code or that a copy of source is saved prior to modification.

3. (Continued)

- There are no restrictions in place to prevent Programmers from accessing, modifying and moving source code changes into production.
- Although the Program Change Control process in place does require testing of source code changes and appears to be adequate, the procedure is not documented and there are no documented test results by which to gauge adequacy of source code change tests.

Recommendation

We recommend the following corrective action for the above-mentioned points as follows:

- Emphasis communicated to users of these Request Forms regarding the need to document completely ALL applicable fields and explanations.
- Implement a system to track and monitor source code changes.
- Implement controls to prevent Programmers from accessing source code in the production environment (to include checking out their own version of source code) and from moving their own code modifications into the production environment.
- The Program Change Control process be modified to require standard testing of application source code changes and those tests be documented for proof of diligent and adequate testing efforts.

4. Disaster Recovery or Business Continuity Plans are not adequate.

The following weaknesses were noted:

- There is no formal, documented and approved Disaster Recovery Plan. This situation could cause the University to be without computer-processing abilities for an extended period of time in the event of a disaster or major interruption; no disaster recovery testing has been done, without adequate testing of the plan, there is no way to insure the plan will work as designed.
- There is no formal, documented and approved Business Continuity Plan. Application users have no manual procedures to activate in a disaster situation. Without manual procedures, operations could not continue after a disaster.

Recommendation

We recommend the following corrective action for the above-mentioned points as follows:

- A formal Disaster Recovery Plan be developed, documented, approved by management and tested on a periodic basis. A copy of this plan should also be stored at a secure off-site location. At a minimum, the plan should:
  - a. Identify critical applications that must be restored.
  - b. Identify software and data file backups needed to restore these applications. Backup retention periods and a secure off-site storage location should be identified and utilized.
  - c. Address the acquisition of replacement hardware should it be needed.
  - d. Identify an alternate processing site should it be needed.
  - e. Identify alternate procedures the users can use to cope with the unavailability of the computer application during the recovery period.
- A formal Business Continuity Plan be developed, documented, approved by management and tested on a periodic basis. A copy of this plan should also be stored at a secure off-site location. Each application's user department should develop, test and document manual procedures to be used in lieu of their respective computerized application in the event the application can no longer be utilized.

GENERAL COMMENTS

STUDENT ENROLLMENT DATA - In accordance with Ark. Code Ann. 6-60-209, we performed tests of the student enrollment data for the year ended June 30, 2004, as reported to the State Department of Higher Education, to provide reasonable assurance that the data was properly reported. Our testing was limited to the fall and spring terms of the year. The enrollment data reported was as follows:

	<u>Fall Term 2003</u>	<u>Spring Term 2004</u>
Student Headcount	10,573	9,918
Student Semester Credit Hours	125,181	116,629

During our review, nothing came to our attention that would cause us to believe that the student enrollment data was not substantially correct.

These reports are intended for the information and use of the Legislative Joint Auditing Committee, state executive and oversight management and University management, and is not intended to be and should not be used by anyone other than these specific parties. However, this report is a matter of public record and its distribution is not limited.

DIVISION OF LEGISLATIVE AUDIT

*William R. Baum*

William R. Baum, CPA, CFE  
Deputy Legislative Auditor

Little Rock, Arkansas  
November 23, 2004

# **Arkansas State University – Jonesboro**

## **Management’s Discussion and Analysis**

### **Financial Statement Presentation**

**This section of the Arkansas State University – Jonesboro (The University) annual financial report presents discussion and analysis of the University’s financial performance during the fiscal year ended June 30, 2004. This discussion and analysis is prepared by the University’s financial administrators and is intended to provide information on the financial activities of the University that is both relevant and easily understandable. Information is also provided on the University’s financial position as of June 30, 2004 as further explanation of the results of the year’s financial activities.**

**The statements have been prepared using the format specified in Governmental Accounting Standards Board (GASB) Statements Number 34 and 35. GASB Statement Number 34 requires the presentation of comparative information from the previous fiscal year and a discussion of any significant changes in the University’s financial position or the results of its operations. Accordingly, the University’s annual financial report for the year ended June 30, 2004 includes comparative information for the fiscal year ended June 30, 2003.**

### **Fiscal Year 2004 Highlights**

**The following events or activities of financial significance occurred during the fiscal year ended June 30, 2004.**

- On November 25, 2003 the University executed a \$2,000,000 draw against its established line of credit with the Bank of America. This draw provided funding for the equipping and furnishing of the University’s new student union.**
- The University dedicated and occupied its new student union on March 24, 2004. The related renovation of the Reng Center into a new student services building is ongoing and scheduled for completion in late fall of 2005. Construction costs for this project through June 30, 2004 amounted to \$28,371,030.**
- On March 25, 2004 the University issued student fee revenue refunding and construction bonds and housing system revenue bonds totaling \$45,555,000. The proceeds from these bonds will finance the construction of a new**

residence facility and additional married student housing facilities, the acquisition of land and buildings adjacent to the campus, the construction of a chilled water infrastructure and cooling system, the renovation of existing educational and general facilities, and the refunding of previously issued academic bonds.

- On May 19, 2004 the University acquired for \$5,182,889 from the Arkansas State College Foundation for the Advancement of Higher Education land and residential property contiguous to the campus.

## Statement Discussion

### *Statement of Net Assets*

The Statement of Net Assets is intended to display the financial position of the University. Its purpose is to present to the reader of the financial statements a benchmark from which to analyze the financial stability of the University. It is a “snapshot” of the University’s assets, liabilities, and net assets (assets minus liabilities) as of June 30, 2004, the last day of the fiscal year. Assets and liabilities are presented in two categories: current and noncurrent. Net assets are presented in three categories: capital assets net of related debt, restricted assets, and unrestricted assets. A more detailed explanation of these categories is found in the notes that accompany the financial statements.

Readers of the Statement of Net Assets can determine answers to the following key questions as of June 30, 2004:

**Did the University have sufficient assets available to meet its existing obligations and continue operation?**

**How much did the University owe to external parties including vendors and lending institutions?**

**What resources did the University have available to make future investments and expenditures?**

### Condensed Statement of Net Assets

Assets:	June 30, 2004	June 30, 2003	Percent Change
Current Assets	\$ 26,838,152	\$ 25,170,302	6.63%
Capital Assets, Net	148,811,004	117,710,870	26.42%
Other Noncurrent Assets	<u>69,899,341</u>	<u>55,791,281</u>	<u>25.29%</u>
Total Assets	<u>\$ 245,548,497</u>	<u>\$ 198,672,453</u>	<u>23.59%</u>

Liabilities:

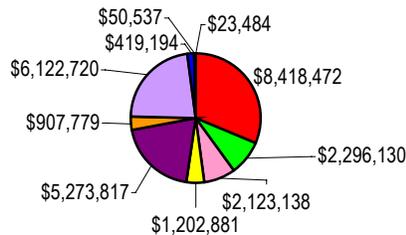
Current Liabilities	\$ 14,366,563	\$ 12,991,955	10.58%
Noncurrent Liabilities	97,874,234	56,420,655	73.47%
<b>Total Liabilities</b>	<b>112,240,797</b>	<b>69,412,610</b>	<b>61.70%</b>

Net Assets:

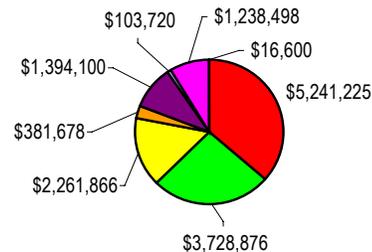
Invested in Capital, Net of Debt	92,900,839	66,270,312	40.18%
Restricted, Nonexpendable	9,017,859	8,246,345	9.36%
Restricted, Expendable	6,972,894	32,793,770	-78.74%
Unrestricted	24,416,108	21,949,416	11.24%
<b>Total Net Assets</b>	<b>133,307,700</b>	<b>129,259,843</b>	<b>3.13%</b>

<b>Total Liabilities and Net Assets</b>	<b>\$ 245,548,497</b>	<b>\$ 198,672,453</b>	<b>23.59%</b>
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**Current Assets**



**Current Liabilities**



- Cash and cash equivalents
- Short-term investments
- Accounts receivable (less allowances of \$307,384)
- Notes and deposits receivable (less allowances of \$110,187)
- Other receivables
- Inventories
- Deposits with trustee
- Accrued interest
- Prepaid expenses
- Other assets

- Accounts payable and accrued liabilities
- Bonds, notes and leases payable
- Compensated absences
- Deferred revenues
- Funds held in trust for others
- Deposits
- Interest payable
- Other liabilities

**The University's current assets increased by \$1,667,850 or 6.63% during the fiscal year ended June 30, 2004 while its net capital assets increased by \$31,100,134 or 26.42%. These changes are attributable to construction activities and the investment of bond and other financing proceeds in capital projects. Overall, the University's total assets increased from \$198,672,453 at June 30, 2003 to \$245,548,497 at June 30, 2004, an increase of 23.59%.**

**The University's total liabilities increased from \$69,412,610 at June 30, 2003 to \$112,240,797 at June 30, 2004 an increase of \$42,828,187 or 61.70% while its total net assets increased from \$129,259,843 to \$133,307,700 during the period, an increase of \$4,047,857 or 3.13%. The substantial increase in the University's liabilities is due in large measure to an increase in bonds, notes, and leases payable of \$42,469,607. The increase in the University's net assets is largely attributable to the net positive affect of these construction and related financing activities.**

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

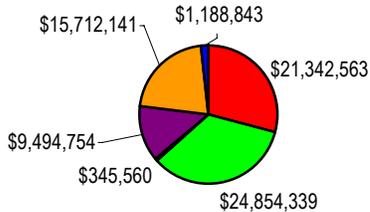
The total net assets as presented on the Statement of Net Assets are based in part on the financial activities that occurred during the fiscal year as presented in the Statement of Revenues, Expenses, and Changes in Net Assets. This statement's purpose is to present the revenues generated and received by the University, both operating and nonoperating, the expenses incurred by the University, both operating and nonoperating, and all other financial gains or losses experienced by the University during the fiscal year ended June 30, 2004.

Generally, revenues from operations are received in exchange for the University providing services or products to students and other constituencies. Operating expenses are those costs paid or incurred in producing those services or products or in carrying out the mission of the University. Nonoperating revenues are financial inflows to the University resulting from nonexchange transactions; that is, the University does not provide a specific service or product in exchange for them. For example, appropriations from the state are considered nonoperating revenue because the legislature does not receive a direct and commensurate benefit from the University in exchange for providing the appropriation.

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

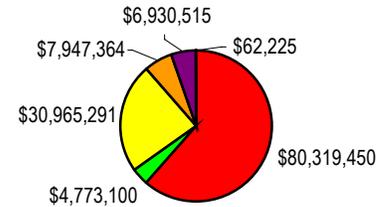
	For the Year Ended June 30, 2004	For the Year Ended June 30, 2003	Percent Change
Operating Revenues	\$ 72,938,200	\$ 68,645,338	6.25%
Operating Expenses	<u>130,997,945</u>	<u>123,602,332</u>	<u>5.98%</u>
Operating Income (Loss)	(58,059,745)	(54,956,994)	5.65%
Nonoperating Revenues (Expenses)	57,003,947	53,317,978	6.91%
Income (Loss) before Other Revenue, Expenses, Gains, or Losses	(1,055,798)	(1,639,016)	-35.58%
Other Revenue (Expenses)	<u>5,103,655</u>	<u>2,008,766</u>	<u>154.07%</u>
Increase in Net Assets	4,047,857	369,750	994.76%
Net Assets at Beginning of the Year, As Originally Reported	129,259,843	136,127,706	
Reclassification of Loan Fund Balance To Noncurrent Liability	<u>0</u>	<u>(7,237,613)</u>	
Net Assets at Beginning of Year, As Restated	<u>129,259,843</u>	<u>128,890,093</u>	
Net Assets at End of Year	\$ 133,307,700	\$ 129,259,843	

## Operating Revenues



- Student tuition and fees (net of scholarship allowances of \$17,822,615)
- Grants and contracts
- Sales and services of educational departments
- Self-insurance
- Auxiliary enterprises (net of scholarship allowances of \$3,002,046)
- Other operating revenues

## Operating Expenses



- Personal services
- Scholarships and fellowships
- Supplies and services
- Self-insurance
- Depreciation
- Other

**The Statement of Revenues, Expenses, and Changes in Net Assets for the fiscal year ended June 30, 2004 reflects an increase in the net assets of the University of \$4,047,857 compared with an increase of \$369,750 for the year ended June 30, 2003. Highlights from the information presented in the Statement of Revenues, Expenses, and Changes in Net Assets for the fiscal year ended June 30, 2004 include the following:**

- **Tuition and Fees, Net of Scholarship Allowance** amounted to \$21,342,563 or 29.26% of Total Operating Revenues.
- **Personal Services** expenses totaled \$80,319,450 or 61.31% of Total Operating Expenses.
- **Scholarships and Fellowships** expenses totaled \$4,773,100 or 3.64% of Total Operating Expenses. Scholarships and Fellowships expenses amounted to 22.36% of Tuition and Fees revenue.
- **The University's Self Insurance Program** generated revenues of \$9,494,754 and expenses of \$7,947,364.
- **The University's Loss from Operations** amounted to \$58,059,745. State Appropriations, which are reported as Nonoperating Revenues, amounted to \$56,329,189. Other Nonoperating Revenues amounted to \$3,739,549.

- Total Other Revenues amounted to \$6,456,104. Of this amount, \$2,507,311 was derived from Capital Appropriations, Grants, and Gifts and \$2,097,139 resulted from the recognition of Capitalized Interest related to construction activities.

*Statement of Cash Flows*

The third and final statement presented is the Statement of Cash Flows. This statement presents detailed information about the University's financial activities from the perspective of their effect on cash. The information is presented in five components. The first presents cash inflows and outflows resulting from the University's normal operating activities. The second component presents cash flows from noncapital financing activities, that is, cash received from or spent for activities that do not result from normal operations, capital financing activities, or investing. The third component presents cash inflows and outflows resulting from capital and related financing activities such as debt issuance, lease agreements, and capital appropriations, grants, or gifts. The fourth component presents cash flows resulting from investing activities such as purchases and liquidations of investments and interest, gains, and losses generated by these activities. The fifth component of the Statement of Cash Flows is a reconciliation of the net operating revenues (expenses) for the fiscal year as reported on the Statement of Revenues, Expenses, and Changes in Net Assets to the net cash provided (used) by operating activities as presented in component one of the Statement of Cash Flows.

Cash Flows for the Year Ended June 30, 2004

Cash Provided (Used) by:

Operating Activities	\$ (51,800,446)
Noncapital Financing Activities	58,653,542
Capital and Related Financing Activities	(12,126,355)
Investing Activities	<u>(2,619,226)</u>
Net Increase (Decrease) in Cash	(7,892,485)
Cash - Beginning of the Year	<u>18,657,868</u>
Cash - End of the Year	<u><u>\$ 10,765,383</u></u>

*Capital Assets and Debt Administration*

In November of 2003 the University executed a \$2,000,000 tax-exempt note through its existing \$6,000,000 credit agreement with the Bank of America, N.A. to provide financing for the equipping and furnishing of the new Student Union. The note matures on January 1, 2007 with payment of the principal due in full on that date.

**Under the terms of the note interest is variable and payable quarterly until maturity. The University began making quarterly payments of principal and interest in January of 2004.**

**In March of 2004 the University issued \$45,555,000 in tax-exempt bonds and used \$34,000,000 of the proceeds to finance new residential construction on campus, \$5,200,000 to acquire land and buildings adjacent to the campus, \$2,355,000 to retire outstanding academic bonds, \$2,000,000 to finance a chilled water infrastructure and cooling system, and \$2,000,000 to finance the renovation of existing educational and general facilities. The Series 2004 will mature in thirty years and have an average coupon rate of 4.73% on the Housing System Bonds and 4.27% on the Student Fee Revenue Refunding and Construction Bonds.**

### *Economic Outlook*

**The University increased its Net Assets during the fiscal year ended June 30, 2004 by \$4,047,857 or 3.13% compared with an increase during the fiscal year ended June 30, 2003 of \$369,750. This increase is almost entirely attributable to construction and related capital financing activities. Capital related revenues in the form of Capital Appropriations, Grants, and Gifts and the Recognition of Capitalized Interest amounted to \$4,604,450. Without these revenue sources, the decrease in the University's Net Assets during the fiscal year ended June 30, 2004 would have amounted to \$556,593. If construction and related financing activities are not considered, the University fully expended the financial resources provided to it during the fiscal year ended June 30, 2004 through its operations and other activities.**

**While economic conditions at the state and national level continue to improve the likelihood that significant new resources will be appropriated to the University by the state legislature is remote. Additionally, the ability of the University to raise significant new amounts of revenue through tuition and fee assessment is increasingly constrained by regional and state demographics and competition between Arkansas's institutions of higher education. The current full utilization of the University's existing financial resources coupled with the likelihood of no significant new revenues will require the University to consider budget reductions, resource reallocation, and cost containment measures as necessary means of providing resources for new initiatives, maintaining its financial position and continuing its mission.**

ARKANSAS STATE UNIVERSITY  
COMPARATIVE STATEMENT OF NET ASSETS  
JUNE 30, 2004

Exhibit A

	June 30, 2004	
	2004	2003
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 8,418,472	\$ 7,694,382
Short-term investments	2,296,130	2,807,783
Accounts receivable (less allowances of \$307,384 and \$295,282)	2,123,138	2,354,565
Notes and deposits receivable (less allowances of \$110,187 and \$92,474)	1,202,881	1,044,042
Other receivables	5,273,817	6,340,588
Inventories	907,779	1,056,972
Deposits with trustee	6,122,720	3,318,753
Accrued interest	419,194	388,107
Prepaid expenses	50,537	143,003
Other assets	23,484	22,107
Total Current Assets	26,838,152	25,170,302
Noncurrent Assets:		
Restricted cash and cash equivalents	2,346,911	10,963,486
Endowment investments	9,083,392	7,121,882
Other long-term investments	14,934,409	12,156,333
Notes and deposits receivable (less allowances of \$556,878 and \$509,583)	6,212,305	5,761,223
Deposits with trustee	37,322,324	19,764,317
Investments in real estate		24,040
Capital assets (net of accumulated depreciation of \$123,340,224 and \$118,166,981)	148,811,004	117,710,870
Total Noncurrent Assets	218,710,345	173,502,151
TOTAL ASSETS	<b>245,548,497</b>	<b>198,672,453</b>
<b>LIABILITIES</b>		
Current Liabilities:		
Accounts payable and accrued liabilities	5,241,225	5,503,744
Bonds, notes and leases payable	3,728,876	2,752,326
Compensated absences	2,261,866	2,042,538
Deferred revenues	381,678	550,255
Funds held in trust for others	1,394,100	1,347,564
Deposits	103,720	102,939
Interest payable	1,238,498	629,991
Other liabilities	16,600	62,598
Total Current Liabilities	14,366,563	12,991,955
Noncurrent Liabilities:		
Bonds, notes and leases payable	90,181,289	48,688,232
Compensated absences	380,483	519,100
Deposits	122,718	148,925
Refundable federal advances	7,189,744	7,064,398
Total Noncurrent Liabilities	97,874,234	56,420,655
TOTAL LIABILITIES	112,240,797	69,412,610

ARKANSAS STATE UNIVERSITY  
COMPARATIVE STATEMENT OF NET ASSETS  
JUNE 30, 2004

Exhibit A

	June 30, 2004	
	2004	2003
<b>NET ASSETS</b>		
Invested in capital assets, net of related debt	\$ 92,900,839	\$ 66,270,312
Restricted for:		
Nonexpendable:		
Scholarships and fellowships	5,529,038	5,116,735
Loans	868,136	826,354
Other	2,620,685	2,303,256
Expendable:		
Scholarships and fellowships	401,685	374,178
Research	341,957	139,065
Capital projects	1,237,850	29,432,242
Debt service	2,770,377	207,493
Renewal and replacement	50,594	50,348
Other	2,170,431	2,590,444
Unrestricted	24,416,108	21,949,416
TOTAL NET ASSETS	\$ 133,307,700	\$ 129,259,843

The accompanying notes are an integral part of these financial statements.

ARKANSAS STATE UNIVERSITY FOUNDATION, INC.  
STATEMENT OF FINANCIAL POSITION  
JUNE 30, 2004

Exhibit A-1

ASSETS	
Cash	\$ 568,626
Repurchase agreements	4,800,000
Unconditional promises to give, net	991,622
Lease purchase receivable	501,996
Accounts receivable, net	23,572
Prepaid expenses	5,798
Short-term investments	253,951
Long-term investments	21,727,440
Property and equipment, net	123,088
Collections	1,055,474
Other assets	<u>13,832</u>
TOTAL ASSETS	<u><u>\$ 30,065,399</u></u>
LIABILITIES	
Accounts payable	\$ 132,406
Notes payable	35,518
Annuities payable	<u>97,027</u>
Total LIABILITIES	<u>264,951</u>
NET ASSETS	
Unrestricted	396,605
Temporarily restricted	6,377,281
Permanently restricted	<u>23,026,562</u>
TOTAL NET ASSETS	<u>29,800,448</u>
TOTAL LIABILITIES AND NET ASSETS	<u><u>\$ 30,065,399</u></u>

ARKANSAS STATE UNIVERSITY  
COMPARATIVE STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS  
FOR THE YEAR ENDED JUNE 30, 2004

Exhibit B

	Year Ended June 30,	
	2004	2003
<b>OPERATING REVENUES</b>		
Student tuition and fees (net of scholarship allowances of \$17,822,615 and \$17,250,736)	\$ 21,342,563	\$ 19,917,029
Grants and contracts	24,854,339	24,666,458
Sales and services of educational departments	345,560	258,931
Self-insurance	9,494,754	8,454,750
Auxiliary enterprises (net of scholarship allowances of \$3,002,046 and \$2,769,341)	15,712,141	14,264,440
Other operating revenues	1,188,843	1,083,730
TOTAL OPERATING REVENUES	<u>72,938,200</u>	<u>68,645,338</u>
<b>OPERATING EXPENSES</b>		
Personal services	80,319,450	75,069,342
Scholarships and fellowships	4,773,100	5,014,729
Supplies and services	30,965,291	29,226,635
Self-insurance	7,947,364	7,672,198
Depreciation	6,930,515	6,554,158
Other	62,225	65,270
TOTAL OPERATING EXPENSES	<u>130,997,945</u>	<u>123,602,332</u>
OPERATING INCOME (LOSS)	<u>(58,059,745)</u>	<u>(54,956,994)</u>
<b>NON-OPERATING REVENUES (EXPENSES)</b>		
State appropriations	56,329,189	53,501,400
Gifts	1,941,131	994,158
Investment income (net of investment expense of \$22,957 and \$22,043)	1,769,306	2,320,549
Interest on capital asset - related debt	(2,995,392)	(3,230,656)
Other revenue	29,112	10,218
Other expense	(69,399)	(277,691)
NET NON-OPERATING REVENUES (EXPENSES)	<u>57,003,947</u>	<u>53,317,978</u>
INCOME BEFORE OTHER REVENUES, EXPENSES, GAINS OR LOSSES	<u>(1,055,798)</u>	<u>(1,639,016)</u>
Capital appropriations	2,061,906	1,988,950
Capital grants and gifts	445,405	303,361
Capitalization of library holdings at rate per volume	103,950	242,795
Gain/(loss) from disposition of capital assets	(191,152)	(68,851)
Capitalization of interest	2,097,139	318,049
Additions to permanent endowments	58,960	91,791
Adjustments to prior year revenues and expenses	(24,285)	(56,187)
Refunds to grantors	(194,656)	(63,385)
Transfer of endowment funds to ASU Indian Club		(833,620)
Accrued interest on bond issue	130,579	
Premium on construction bond issue	896,572	
Net bond issuance costs	(792,791)	
Net payment to escrow agent for advance refunding of bonds	(149,565)	
Other	661,593	85,863
INCREASE (DECREASE) IN NET ASSETS	<u>4,047,857</u>	<u>369,750</u>
NET ASSETS - BEGINNING OF YEAR - AS ORIGINALLY REPORTED	129,259,843	136,127,706
Reclassification - Perkins Loan Program		<u>(7,237,613)</u>
NET ASSETS - BEGINNING OF YEAR - RESTATED	<u>129,259,843</u>	<u>128,890,093</u>
NET ASSETS - END OF YEAR	<u>\$ 133,307,700</u>	<u>\$ 129,259,843</u>

The accompanying notes are an integral part of these financial statements.

ARKANSAS STATE UNIVERSITY FOUNDATION, INC.  
STATEMENT OF ACTIVITIES  
FOR THE YEAR ENDED JUNE 30, 2004

Exhibit B-1

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Support				
Support and Reclassifications				
Contributions	\$ 36,505	\$ 1,768,798	\$ 1,260,184	\$ 3,065,487
Use of contributed facilities	3,400			3,400
Contributed services	140,995			140,995
Contributed supplies	5,315			5,315
Investment return	335,342	82,091	2,975,403	3,392,836
Other income	118,885	224,215	51	343,151
Net assets released from restrictions	2,773,517	(2,394,974)	(378,543)	
Total Support	3,413,959	(319,870)	3,857,095	6,951,184
Expenses and Losses				
Program services:				
Academic activities	811,502			811,502
Administrative	297,141			297,141
Student activities	17,841			17,841
Supporting services:				
Management and general	209,329			209,329
Transfers to Arkansas State University	2,000,466			2,000,466
Total Expenses	3,336,279			3,336,279
Increase (Decrease) in Net Assets	77,680	(319,870)	3,857,095	3,614,905
Net Assets at beginning of year as previously reported	315,851	6,699,251	19,289,212	26,304,314
Prior period adjustments	3,074	(2,100)	(119,745)	(118,771)
Balance at beginning of year, as restated	318,925	6,697,151	19,169,467	26,185,543
Net Assets at end of year	\$ 396,605	\$ 6,377,281	\$ 23,026,562	\$ 29,800,448

ARKANSAS STATE UNIVERSITY  
COMPARATIVE STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED JUNE 30, 2004

Exhibit C

	Year Ended June 30,	
	2004	2003
<b>CASH FLOW FROM OPERATING ACTIVITIES</b>		
Student tuition and fees	\$ 21,418,869	\$ 19,104,533
Grants and contracts	27,645,965	32,207,483
Sales and services of educational departments	345,560	258,931
Auxiliary enterprises revenues	16,214,769	14,059,853
Self-insurance	9,494,754	8,454,750
Collection of principal and interest related to student loans	1,107,412	905,424
Collection of employee travel loans	341,766	570,891
Other receipts	1,401,119	1,241,856
Payments to employees	(62,621,256)	(59,857,660)
Payments for employee benefits	(18,100,512)	(14,964,415)
Payments to suppliers	(31,151,499)	(29,516,124)
Scholarships and fellowships	(4,773,100)	(5,014,729)
Self-insurance	(7,947,364)	(7,672,198)
Loans issued to students	(1,790,401)	(1,790,151)
Travel loans issued to employees	(342,428)	(549,992)
Payments to campuses for financial aid distributions	(3,044,100)	(4,786,069)
Net cash provided (used) by operating activities	(51,800,446)	(47,347,617)
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>		
State appropriations	56,923,088	52,227,583
Private gifts	1,941,131	994,158
Other agency funds - net	(16,021)	445,469
Refunds to grantors	(194,656)	(63,385)
Other		(28,995)
Net cash provided (used) by noncapital financing activities	58,653,542	53,574,830
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Proceeds from capital debt	1,999,000	565,000
Capital appropriations	2,228,058	1,822,798
Capital gift and grants	445,405	104,221
Proceeds from sale of capital assets	22,196	57,010
Received from trustees	23,537,730	22,470,559
Purchases of capital assets	(34,888,235)	(31,267,739)
Principal paid on capital debt and leases	(983,657)	(596,443)
Interest paid on capital debt and leases	(72,090)	(106,710)
Payments to bond trustees	(4,388,104)	(4,275,827)
Other	(26,658)	
Net cash provided (used) by capital and related financing activities	(12,126,355)	(11,227,131)
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Proceeds from sales and maturities of investments	10,108,891	11,303,917
Interest on investments	718,129	1,025,522
Purchases of investments	(13,446,246)	(13,408,347)
Net cash provided (used) by investing activities	(2,619,226)	(1,078,908)
Net increase (decrease) in cash and cash equivalents	(7,892,485)	(6,078,826)
Cash and cash equivalents - beginning of year	18,657,868	24,736,694
Cash and cash equivalents - end of year	\$ 10,765,383	\$ 18,657,868

ARKANSAS STATE UNIVERSITY  
 COMPARATIVE STATEMENT OF CASH FLOWS  
 FOR THE YEAR ENDED JUNE 30, 2004

Exhibit C

	Year Ended June 30,	
	2004	2003
Reconciliation of net operating revenues (expenses) to net cash provided (used) by operating activities:		
Operating income (loss)	\$ (58,059,745)	\$ (54,956,994)
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities:		
Depreciation expense	6,930,515	6,554,158
Change in assets and liabilities:		
Receivables, net	(250,898)	702,150
Inventories	149,193	(64,442)
Prepaid expenses	92,466	(46,032)
Other assets	(344)	(636)
Accounts payable	(330,979)	(348,665)
Deferred revenues	(168,577)	128,939
Deposits	(25,427)	(11,822)
Compensated absences	80,711	55,491
Salaries and withholdings payable	(483,029)	191,776
Accrued interest - Perkins loans	(2,207)	(3,390)
Refundable federal advances	369,975	301,722
Other liabilities	(102,100)	150,128
Net cash provided (used) by operating activities	\$ (51,800,446)	\$ (47,347,617)

The accompanying notes are an integral part of these financial statements.

ARKANSAS STATE UNIVERSITY  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2004

NOTE 1: Reporting Entity

Arkansas State University ("the University"), a component unit of the State of Arkansas, developed from one of four (4) State agricultural schools established in 1909 by an act of the Arkansas General Assembly.

The University opened as a vocational high school in 1910 and was reorganized as a junior college in 1918. The name was changed to State Agricultural and Mechanical College by an act of the Legislature in 1925. Authority to extend the curriculum, offer senior college work, and grant degrees were granted in 1931. In 1933, the Legislature changed the name of the College to Arkansas State College. In January 1967, the Arkansas State Legislature passed an act authorizing a change in the name of Arkansas State College to Arkansas State University, effective July 1, 1967.

A branch campus at Beebe, Arkansas was added to Arkansas State College by an act of the General Assembly of the State of Arkansas in 1955. The branch campus was designated as Arkansas State College – Beebe Branch. Under the provisions of Ark. Code Ann. 6-53-405, White River Technical College was consolidated with Arkansas State University – Beebe campus effective July 1, 1992. Act 90 of 2001 eliminated the word "branch" from the references to campuses of Arkansas State University. Subsequently, the Newport campus separated itself from Beebe and became Arkansas State University – Newport.

Effective July 1, 1992, Arkansas State University began administrative operations at a Mountain Home campus. On October 19, 1993, the voters of Baxter County authorized the levy of a two (2) mill tax to support operations at the Mountain Home campus.

Effective July 1, 2001, Delta Technical Institute was merged to the University to become the Arkansas State University Technical Center.

The governing body of the University is the Board of Trustees comprised of five (5) members.

The Arkansas State University Foundation, Inc. (the Foundation) is a legally separate, tax-exempt component unit of Arkansas State University (the University). The Foundation acts primarily as a fund-raising and asset management organization to develop and supplement the resources that are available to the University in support of its mission and programs. The thirty-three (33) member board of the Foundation is self-perpetuating and consists of graduates and friends of the University. Although the University does not control the timing or amount of receipts from the Foundation, the majority of resources, or income thereon, that the Foundation holds and invests are restricted to the activities of the University by donors. Because these restricted resources held by the Foundation may only be used by, or for the benefit of, the University, the Foundation is considered a component unit of the University under the guidelines established by Governmental Accounting Standards Board Statement Number 39, *Determining Whether Certain Organizations Are Component Units*. Accordingly, the financial statements of the Foundation are discretely presented in the University's financial statements in accordance with the provisions of GASB Statement Number 39.

While the activities and resources of the Foundation benefit all of the campuses of Arkansas State University the University has elected to discretely present the financial statements of the Foundation within the financial statements of Arkansas State University - Jonesboro for the fiscal year ended June 30, 2004. During the year ended June 30, 2004 the Foundation distributed \$851,088 to the University for both restricted and unrestricted purposes. Complete financial statements for the Foundation may be obtained from the Foundation at P. O. Box 1990, State University, AR 72467-1990.

The Foundation reports under FASB standards, including FASB Statement No. 117, *Financial Reporting for Not-for-Profit Organizations*. As such, certain revenue recognition criteria and presentation features are different from GASB revenue recognition criteria and presentation features. No modifications have been made to the Foundation's financial information in the University's financial statements.

ARKANSAS STATE UNIVERSITY  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2004

NOTE 2: Summary of Significant Accounting Policies

Financial Statement Presentation

In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*. GASB Statement No. 35, *Basic Financial Statements - and Management's Discussion and Analysis - for Public Colleges and Universities*, followed in November 1999. The financial statement presentation required by GASB No. 34 and No. 35 provides a comprehensive, entity-wide perspective of the University's assets, liabilities, net assets, revenues, expenses, changes in net assets and cash flows.

Measurement Focus and Basis of Accounting

For financial reporting purposes, the University is considered a special-purpose government engaged only in business-type activities. Accordingly, the University's financial statements have been presented using the economic resources focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation is incurred. All significant intra-agency transactions have been eliminated.

The University may choose whether to apply pronouncements of the Financial Accounting Standards Board (FASB) issued after November 30, 1989 unless those pronouncements conflict with pronouncements of the Governmental Accounting Standards Board. The University has elected to not apply pronouncements of the FASB issued after November 30, 1989.

Capital Assets and Depreciation

Land, buildings, improvements and infrastructure, equipment, audiovisual holdings and construction in progress are recorded at cost at the date of acquisition or fair market value at the date of donation in the case of gifts. Livestock held for educational purposes is recorded at estimated fair value. Library holdings are recorded at a stated rate per volume. Library holdings that are capitalized do not include periodicals, microfilm, microfiche and government documents. The University's capitalization policy for equipment is to record, as assets, any items with a unit cost of more than \$2,500 and an estimated useful life greater than one year. Improvements to buildings, infrastructure, and land that significantly increase the value or extend the useful life of the asset are capitalized. Routine repairs and maintenance are charged to operating expense when incurred.

Depreciation is calculated using the straight-line method over the estimated useful life of the asset. Estimated useful lives, for the computation of depreciation, are 15 to 30 years for buildings, 15 years for improvements and infrastructure, 10 years for library and audiovisual holdings and 3 to 20 years for equipment. Capital assets are presented net of accumulated depreciation where applicable.

Operating and Nonoperating Revenues

Revenues of the University are classified as either operating or nonoperating according to the following criteria:

**Operating Revenues:** Operating revenues result from activities that have characteristics of exchange transactions; that is, the University receives payment in exchange for providing services or products to students or other constituencies. Student tuition and fees, net of scholarship discounts and allowances, sales and services of auxiliary operations, net of scholarship discounts and allowances, and most federal, state, local and private grants are the main categories of operating revenues for the University.

**Nonoperating Revenues:** Nonoperating revenues are those revenues that result from nonexchange transactions or from activities specifically defined as nonoperating by the Governmental Accounting Standards Board. Appropriations from the state are considered nonoperating under the definitions set forth by the GASB because the University does not provide a direct and commensurate benefit to the legislature in exchange for them.

ARKANSAS STATE UNIVERSITY  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2004

NOTE 2: Summary of Significant Accounting Policies (Continued)

Cash Equivalents

For purposes of the statement of cash flows, the University considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

Accounts Receivable

Accounts receivable consists of assets the University is legally entitled to, but for which payment has not been received as of the close of the fiscal year at June 30, 2004. The various sources of the University's receivables are detailed in a subsequent note. Receivables are presented net of any estimated uncollectible amounts in accordance with generally accepted accounting principles.

Investments

The University accounts for its investments, except for nonparticipating contracts, at fair value in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. Changes in unrealized gain (loss) on the carrying value of investments are reported as a component of investment income in the Statement of Revenues, Expenses and Changes in Net Assets. Nonparticipating contracts are reported at cost.

It is the University's policy to report all endowment funds, administered by other parties for investment purposes, as investments in the financial statements.

Inventories

Inventories are valued at cost with cost being generally determined on a first-in, first-out or average basis.

Noncurrent Cash and Investments

Cash and investments that are externally restricted for endowment scholarships and other purposes or to purchase or construct capital assets, are classified as noncurrent assets in the Statement of Net Assets. Additionally, this classification includes other long-term investments with original maturity dates greater than one year.

Deferred Revenues

Deferred revenues consist primarily of amounts received prior to the end of the fiscal year for tuition and fees and certain auxiliary activities that relate to a subsequent accounting period. For example, payments for tuition and fees for the second summer semester or season football tickets for the upcoming fall season received prior to June 30, 2004 are treated as deferred revenues. They are considered liabilities of the University until earned.

Compensated Absences Payable

Employee vacation pay earned, but not paid, and related matching costs are recorded as a liability and expense on the University's financial statements as required by generally accepted accounting principles. An estimate is made to allocate this liability between its current and noncurrent components.

Deposits with Trustees

Deposits with Trustees are externally restricted and held by various banks for the University. They are maintained in order to make debt service payments, to maintain sinking or reserve funds as required by bond covenants, or to purchase or construct capital assets.

ARKANSAS STATE UNIVERSITY  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2004

NOTE 2: Summary of Significant Accounting Policies (Continued)

Noncurrent Liabilities

Noncurrent liabilities include (1) principal amounts of bonds payable, notes payable and capital lease obligations with contractual maturities greater than one year; (2) estimated amounts for accrued compensated absences and related matching costs and other liabilities that will not be paid within the next fiscal year; and (3) the refundable federal portion of the Perkins Loan Program.

Net Assets

The University's net assets are classified as follows:

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

**Restricted Net Assets:** Within this classification there are two categories of net assets:

**Restricted, expendable:** Restricted expendable net assets include resources for which the University is legally or contractually obligated to spend only in accordance with restrictions imposed by external parties.

**Restricted, nonexpendable:** Nonexpendable restricted net assets consist of endowment and similar type funds for which donors or other external parties have stipulated that the principal or corpus is to be maintained inviolate and in perpetuity and invested only for the purpose of producing income which may either be expended in accordance with the donors' or external parties' stipulations or added to the principal.

**Unrestricted Net Assets:** Unrestricted net assets represent resources of the University that are unrelated to capital items and not externally restricted. These resources may be expended at the discretion of the University's governing board in the educational and general operations of the University and in furtherance of its mission.

Restricted/Unrestricted Resources

The University has no formal policy addressing which resources to use when both restricted and unrestricted net assets are available for the same purpose. University personnel decide which resources to use at the time expenses are incurred.

Scholarship Discounts and Allowances

Student tuition and fees, and certain other revenues received from students are reported net of scholarship discounts and allowances in the Statement of Revenues, Expenses and Changes in Net Assets. Scholarship discounts and allowances are the difference between the University's stated rates and charges and the amount actually paid by students and/or third parties making payments on behalf of the students. Under this approach, scholarships awarded by the University are considered as reductions in tuition and fee revenues rather than as expenses. Additionally, certain governmental grants, such as Pell grants, and payments from other federal, state or nongovernmental programs, are required to be recorded as either operating or nonoperating revenues in the University's financial statements. To the extent that revenues from such programs are applied to tuition, fees, and other student charges, the University has reported a corresponding scholarship discount or allowance.

ARKANSAS STATE UNIVERSITY  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2004

NOTE 2: Summary of Significant Accounting Policies (Continued)

Student Financial Assistance Programs

The program participation agreement approved by the U. S. Department of Education covers all student financial assistance programs for all of the University's campuses. Therefore, the University initially receives all applicable federal funds pertaining to these programs. The University then distributes the appropriate funds to its individual campuses. The amount received and subsequently distributed has been eliminated from the accompanying Statement of Revenues, Expenses and Changes in Net Assets (Exhibit B) to allow each campus to properly report the scholarship allowances.

NOTE 3: Public Fund Deposits and Investments

Cash deposits are carried at cost. The University's cash deposits at year-end are shown below:

	Carrying Amount	Bank Balance
Insured (FDIC)	\$ 208,904	\$ 208,904
Uninsured, Collateralized	3,113,625	4,434,778
Total Deposits	\$ 3,322,529	\$ 4,643,682

The above deposits do not include cash on deposit in the state treasury, cash on hand maintained by the University and cash equivalents in the amounts of \$3,833,448, \$80,159 and \$3,529,247 for the year ended June 30, 2004, respectively. Cash equivalents consisted entirely of the short-term Common Fund account.

Investments, except for nonparticipating contracts, are reported at fair value. Fair value for reporting purposes is market value if a market price or quote is readily available. Investments that do not have readily available market prices or quotes are reported at estimated fair value. The University's investments at year-end are shown below by category to give an indication of the level of risk assumed. Category 1 includes investments that are insured or registered or for which the securities are held by Arkansas State University or its agent in the University's name. Category 2 includes uninsured and unregistered investments for which the securities are held by the broker's or dealer's trust department or agent in the University's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the broker or dealer, or by its trust department or agent but not in the University's name.

Type of Investment	Category			Carrying Amount	Market Value
	1	2	3		
Certificates of deposit	\$ 2,715,073			\$ 2,715,073	\$ 2,715,073
U. S. Government obligations	2,500,000		\$ 7,457,474	9,957,474	9,957,474
Common stock			67,500	67,500	67,500
Bonds			4,954,199	4,954,199	4,954,199
Mutual funds			3,443,038	3,443,038	3,443,038
Common Fund - intermediate			3,991,843	3,991,843	3,991,843
Other managed investments			1,184,804	1,184,804	1,184,804
Totals	\$ 5,215,073	\$ 0	\$ 21,098,858	\$ 26,313,931	\$ 26,313,931

ARKANSAS STATE UNIVERSITY  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2004

NOTE 3: Public Fund Deposits and Investments (Continued)

Of the above investments in Category 1, \$90,000 was uninsured and uncollateralized at June 30, 2004.

The above investments include \$5,650,850 of University endowment funds pooled with funds maintained by the Arkansas State University Foundation, Inc. The pool is administered by the Arkansas State University Foundation, Inc. The above investments also include endowment funds of \$3,432,542 administered by a third party.

NOTE 4: Income Taxes

The University is tax exempt under Internal Revenue Service code. It is also exempt from state income taxes under Arkansas law. Accordingly, no provision for income taxes is made in the financial statements.

NOTE 5: Capital Assets

Following are the changes in capital assets for the year ended June 30, 2004:

	Balance July 1, 2003	Additions	Transfers	Retirements	Balance June 30, 2004
Capital assets not being depreciated					
Land	\$ 2,720,553	\$ 3,423,097			\$ 6,143,650
Livestock for educational purposes	33,510	4,445			37,955
Construction in progress	31,010,759	28,898,517	\$ (7,366,103)		52,543,173
Total capital assets not being depreciated	<u>\$ 33,764,822</u>	<u>\$ 32,326,059</u>	<u>\$ (7,366,103)</u>		<u>\$ 58,724,778</u>
Other capital assets					
Improvements and infrastructure	\$ 11,516,407	\$ 246,942	\$ 2,113,734		\$ 13,877,083
Buildings	153,566,035	3,397,974	5,252,369	\$ (323,829)	161,892,549
Equipment	25,616,551	2,185,072		(1,313,493)	26,488,130
House Trailers	349,296			(349,296)	
Library/audiovisual holdings	11,064,740	103,950		(2)	11,168,688
Total other capital assets	<u>202,113,029</u>	<u>5,933,938</u>	<u>7,366,103</u>	<u>(1,986,620)</u>	<u>213,426,450</u>
Less accumulated depreciation for					
Improvements and infrastructure	4,234,133	737,827			4,971,960
Buildings	89,352,178	3,267,469		(224,279)	92,395,368
Equipment	14,623,081	2,556,934		(1,183,695)	15,996,320
House Trailers	349,296			(349,296)	
Library/audiovisual holdings	9,608,293	368,285		(2)	9,976,576
Total accumulated depreciation	<u>118,166,981</u>	<u>6,930,515</u>		<u>(1,757,272)</u>	<u>123,340,224</u>
Other capital assets, net	<u>\$ 83,946,048</u>	<u>\$ (996,577)</u>	<u>\$ 7,366,103</u>	<u>\$ (229,348)</u>	<u>\$ 90,086,226</u>
Capital Asset Summary:					
Capital assets not being depreciated	\$ 33,764,822	\$ 32,326,059	\$ (7,366,103)		\$ 58,724,778
Other capital assets, at cost	202,113,029	5,933,938	7,366,103	\$ (1,986,620)	213,426,450
Total cost of capital assets	235,877,851	38,259,997		(1,986,620)	272,151,228
Less accumulated depreciation	118,166,981	6,930,515		(1,757,272)	123,340,224
Capital Assets, net	<u>\$ 117,710,870</u>	<u>\$ 31,329,482</u>	<u>\$ 0</u>	<u>\$ (229,348)</u>	<u>\$ 148,811,004</u>

ARKANSAS STATE UNIVERSITY  
NOTES TO FINANCIAL STATEMENTS  
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NOTE 6: Long-Term Liabilities

Debt payments on bonds amounted to \$4,394,795 for the fiscal year ended June 30, 2004. The amount of \$1,055,747 was expended for debt payments on notes payable and major capital leases.

A summary of long-term debt is as follows:

<u>Date of Issue</u>	<u>Date of Final Maturity</u>	<u>Rate of Interest</u>	<u>Amount Authorized and Issued</u>	<u>Debt Outstanding June 30, 2004</u>	<u>Maturities To June 30, 2004</u>
10/1/69	10/1/09	4.5%	\$ 2,250,000	\$ 655,000	\$ 1,595,000
2/1/96	11/1/05	3.8 - 4.75%	5,380,000	1,325,000	4,055,000
3/1/99	3/1/24	3.4 - 5.05%	9,460,000	8,470,000	990,000
5/1/99	4/1/24	3.4 - 5.1%	17,000,000	14,835,000	2,165,000
4/1/00	4/1/25	4.5 - 6.125%	5,500,000	5,030,000	470,000
3/1/01	3/1/31	3.6 - 5.25%	7,000,000	6,625,000	375,000
3/1/01	3/1/31	3.6 - 5.25%	3,000,000	2,840,000	160,000
4/5/02	5/5/05	Variable	1,500,000	502,401	997,599
8/23/02	7/1/04	5.65%	110,552	56,798	53,754
11/15/02	12/1/27	1.6 - 5%	6,105,000	5,915,000	190,000
8/11/03	9/1/08	7%	507,000	434,299	72,701
11/25/03	1/1/07	Variable	2,000,000	1,666,667	333,333
3/1/04	3/1/34	3 - 5%	34,000,000	34,000,000	
3/1/04	3/1/34	2 - 4.6%	11,555,000	11,555,000	
Totals			<u>\$ 105,367,552</u>	<u>\$ 93,910,165</u>	<u>\$ 11,457,387</u>

The lenders calculate the interest rates on the two (2) notes above at periodic intervals. Such calculations are based on the lenders' changes in the index determined by the Prime Rate or the LIBOR Rate. Each note is subject to a maximum rate of interest that can be assessed.

The changes in long-term liabilities are as follows:

	<u>Balance July 1, 2003</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance June 30, 2004</u>	<u>Amounts Due Within One Year</u>
Bonds payable	\$ 49,950,000	\$ 45,555,000	\$ 4,255,000	\$ 91,250,000	\$ 2,410,000
Notes payable	1,007,989	2,000,000	838,921	2,169,068	1,169,068
Capital leases	482,569	507,000	498,472	491,097	149,808
Compensated absences	2,561,638	2,573,965	2,493,254	2,642,349	2,261,866
Totals	<u>\$ 54,002,196</u>	<u>\$ 50,635,965</u>	<u>\$ 8,085,647</u>	<u>* \$ 96,552,514</u>	<u>\$ 5,990,742</u>

\*Includes \$2,528,736 retired or refinanced before maturity date. See Note 17.

ARKANSAS STATE UNIVERSITY  
NOTES TO FINANCIAL STATEMENTS  
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NOTE 6: Long-Term Liabilities (Continued)

Total future long-term debt principal and interest payments are as follows:

Year ended June 30,	Principal	Interest	Total
2005	\$ 3,728,876	\$ 4,198,475 *	\$ 7,927,351
2006	3,421,400	4,076,126	7,497,526
2007	3,230,277	3,965,658	7,195,935
2008	2,994,675	3,867,226	6,861,901
2009	2,994,937	3,762,101	6,757,038
2010-2014	15,910,000	17,031,896	32,941,896
2015-2019	16,400,000	13,591,586	29,991,586
2020-2024	19,645,000	9,327,971	28,972,971
2025-2029	12,560,000	5,031,238	17,591,238
2030-2034	13,025,000	1,906,835	14,931,835
Totals	<u>\$ 93,910,165</u>	<u>\$ 66,759,112</u>	<u>\$ 160,669,277</u>

\*Includes interest payable of \$1,238,498 recorded as a current liability at June 30, 2004.

NOTE 7: Capital Leases

The University has acquired certain equipment under various capital leases.

Type of Equipment	Asset Amount
Print shop equipment	\$ 730,791
Sports pro video equipment	306,503
Total	<u>\$ 1,037,294</u>

The following is a schedule of future minimum lease payments under capital leases, together with the present value of the net minimum lease payments, as of June 30, 2004:

Fiscal Year Ending June 30,	
2005	\$ 180,754
2006	120,471
2007	120,471
2008	120,471
2009	20,113
Total Minimum Lease Payments	<u>562,280</u>
Less: Amount Representing Interest	<u>71,183</u>
Total Present Value of Net Minimum Lease Payments	<u>\$ 491,097</u>

ARKANSAS STATE UNIVERSITY  
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NOTE 8: Commitments

The University was contractually obligated for the following at June 30, 2004:

A. Construction Contracts

<u>Project Name</u>	<u>Estimated Completion Date</u>	<u>Contract Balance</u>
Student Union	January 2005	\$ 6,838,694
Lakeport	June 2006	170,738
Lab Science/Kays/Nursing/Benton Center	August 2004	44,809
Museum - Tyrnza	August 2004	87,241
Residence Hall	To be determined	611,162
Kays Field Parking Lot	September 2004	101,089
Hard Wired Café	October 2004	59,149
College of Business	To be determined	99,727
Biosciences/Biotech Research	September 2004	1,944,079
Caraway Road Project	To be determined	407,991
Family Housing - Phase I	December 2004	110,332
Family Housing - Phase II	August 2005	6,089,209
Liberal Arts Building	To be determined	172,951
Reng Center Asbestos Abatement	December 2004	38,364

B. Operating Leases (Noncapital leases with initial or remaining noncancellable lease terms in excess of 1 year).

Various leases for copiers and other office equipment with terms ranging from 24 to 60 months, four (4) real estate leases with terms of 24 to 60 months and items of heavy equipment with terms of 24 to 60 months.

- (a) Future minimum rental payments (aggregate) at June 30, 2004: \$1,002,913
- (b) A lease of 1500 square feet of office space contains a three percent (3%) annual increase clause.
- (c) Future minimum rental payments for the succeeding fiscal years:

<u>Year Ended June 30,</u>	<u>Amount</u>
2005	\$ 537,707
2006	296,572
2007	142,417
2008	26,217

Rental payments for the above operating leases, for the year ended June 30, 2004, were approximately \$519,663.

ARKANSAS STATE UNIVERSITY  
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NOTE 9: Retirement Plans

Teachers Insurance and Annuity Association/College Retirement Equities Fund (TIAA/CREF)

Plan Description. The University participates in TIAA/CREF, a defined contribution plan. The plan is a 403(b) program as defined by Internal Revenue Service Code of 1986 as amended, and is administered by TIAA/CREF. TIAA is an insurance company offering participants a traditional annuity with guaranteed principle and a specific interest rate plus the opportunity for additional growth through dividends. CREF is an investment company which offers a variable annuity. Arkansas law authorizes participation in the plan.

Funding Policy. TIAA/CREF has contributory and non-contributory plans. Contributory members select the percentage of their gross salaries to contribute based on current regulations. The University contributes 10% of earnings for all applicable employees. The University's and participants' contributions for the year ended June 30, 2004 were \$4,332,557 and \$3,897,252, respectively.

Arkansas Teacher Retirement System

Plan Description. The University contributes to the Arkansas Teacher Retirement System (ATRS), a cost-sharing multiple-employer defined benefit pension plan for employees who do not elect a qualified alternative retirement plan. ATRS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit and contribution provisions are established by State law and can be amended only by the Arkansas General Assembly. The Arkansas Teacher Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for ATRS. That report may be obtained by writing to Arkansas Teacher Retirement System, 1400 West Third Street, Little Rock, Arkansas 72201 or by calling 1-800-666-2877.

Funding Policy. ATRS has contributory and non-contributory plans. Contributory members are required by law to contribute 6% of their salaries. Each participating employer is required by law to contribute at a rate established by the Arkansas General Assembly. The current employer rate is 13%. The University's contributions to ATRS for the years ended June 30, 2004, 2003 and 2002 were \$266,311, \$240,651 and \$233,289, respectively, equal to the required contributions for each year.

Arkansas Public Employees Retirement System

Plan Description. The University contributes to the Arkansas Public Employees Retirement System (APERS), a cost-sharing multiple-employer defined benefit pension plan. Employees may elect coverage under APERS as a qualified retirement system. APERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit and contribution provisions are established by State law and can be amended only by the Arkansas General Assembly. The Arkansas Public Employees Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for APERS. That report may be obtained by writing to Arkansas Public Employees Retirement System, One Union National Plaza, 124 W. Capitol, Little Rock, Arkansas 72201 or by calling 1-800-682-7377.

Funding Policy. APERS has contributory and non-contributory plans. Contributory members are required by law to contribute 6% of their salaries. Each participating employer is required by law to contribute at a rate established by the Arkansas General Assembly. The current statutory employer rate is 10% of annual covered payroll. The University's contributions to APERS for the years ended June 30, 2004, 2003 and 2002 were \$582,367, \$584,055 and \$614,796, respectively, equal to the required contributions for each year.

ARKANSAS STATE UNIVERSITY  
NOTES TO FINANCIAL STATEMENTS  
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NOTE 9: Retirement Plans (Continued)

Variable Annuity Life Insurance Company (VALIC)

Plan Description. The University contributes to VALIC, a defined contribution plan. The plan is a 403(b) program as defined by Internal Revenue Service Code of 1986 as amended, and is administered by VALIC. VALIC provides insurance policies that become the property of the participant when issued. Arkansas law authorizes participation in the plan.

Funding Policy. VALIC has contributory and non-contributory plans. Employees select the percentage of their gross salaries to contribute based on current regulations. The University's contributory rate is 10% for all applicable employees. Vesting occurs for all participants immediately. The participants' and the University's contributions for the year ended June 30, 2004 were \$263,308 and \$319,537, respectively.

NOTE 10: Natural Classifications with Functional Classifications

The University's operating expenses by functional classifications were as follows:

	Personal Services	Scholarships and Fellowships	Supplies and Services	Self - Insurance	Depreciation	Other	Total
Instruction	\$ 35,196,881	\$ 46,738	\$ 3,708,670				\$ 38,952,289
Research	3,913,735	86,465	1,787,636				5,787,836
Public service	5,567,550	120,562	3,855,369				9,543,481
Academic support	8,106,211	84,381	3,732,104				11,922,696
Student services	4,227,741	145,689	1,412,948				5,786,378
Institutional support	12,120,165		3,633,042				15,753,207
Scholarships and fellowships	1,228	2,119,099	11,498				2,131,825
Operations and maintenance of plant	5,123,028		5,985,534				11,108,562
Auxiliary enterprises	6,062,911	2,170,166	6,838,490				15,071,567
Self-insurance				\$ 7,947,364			7,947,364
Depreciation					\$ 6,930,515		6,930,515
Other						\$ 62,225	62,225
<b>Totals</b>	<b>\$ 80,319,450</b>	<b>\$ 4,773,100</b>	<b>\$ 30,965,291</b>	<b>\$ 7,947,364</b>	<b>\$ 6,930,515</b>	<b>\$ 62,225</b>	<b>\$ 130,997,945</b>

NOTE 11: Disaggregation of Receivable and Payable Balances

Accounts receivable from students was \$2,430,522 at June 30, 2004. This amount was reduced by an allowance for doubtful accounts of \$307,384.

Notes receivable pertains to loans awarded to students through the Federal Perkins Loan Program. Notes receivable were \$7,949,251 at June 30, 2004. This amount was reduced by an allowance for doubtful accounts of \$667,065. Deposits receivable was \$133,000 at June 30, 2004.

Other receivables of \$5,273,817 at June 30, 2004 primarily consisted of reimbursements of \$1,543,578 from various agencies for grants and contracts, \$2,550,693 due from various state treasury accounts and auxiliary enterprises receivables of \$269,212. Other receivables also consisted of \$447,734 due from the U. S. Department of Education for cancellations pertaining to the Federal Perkins Loan Program and miscellaneous items of \$462,600.

The accounts payable and accrued liabilities of \$5,241,225 at June 30, 2004 consisted of \$4,453,176 due to various vendors, \$749,858 for salaries and benefits and other items of \$38,191.

ARKANSAS STATE UNIVERSITY  
NOTES TO FINANCIAL STATEMENTS  
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NOTE 12: Museum Collection

The financial statements do not include the University's museum collection, which consists of numerous historical relics, artifacts, displays and memorabilia. The total value of this collection has not been established.

NOTE 13: Early Retirement Incentive Program

The University contributes to health and life insurance premiums (individual or family coverage) for all employees who retire between the ages of 60 and 65 with at least 10 years of service. These contributions are paid until the retiree is 65 years of age. The University also contributes to health and life insurance premiums for one year for those employees who are determined to be eligible for disability. At June 30, 2004, the number of retirees who were eligible for these benefits totaled 97. The University also pays life insurance premiums for certain retirees under a plan no longer utilized by the University. These premiums are paid until the retiree's death. At June 30, 2004, the number of retirees eligible for these benefits totaled 8. All premiums for these benefits described above were paid monthly and financed on a pay-as-you-go basis. These premiums, paid by the University and the retirees, totaled \$463,494 for the year ended June 30, 2004. Of this amount, the University's contribution was \$327,671.

NOTE 14: Arkansas Services Center

On October 8, 1968, an agreement was signed by Arkansas State University, Arkansas State Hospital, Arkansas Department of Public Welfare, Arkansas State Board of Vocational Education and Craighead County, Arkansas to raise money for the construction of the Arkansas Services Center. This project was financed from the proceeds of a bond issue by Arkansas State University, grants and legislative appropriations by the agencies. With the exception of Craighead County, Arkansas, the participants signed lease agreements for 40 years (the bond term) with rentals and revenues thereof, sufficient to maintain the facility and retire the bonds.

Arkansas State University maintains the financial records of the Arkansas Services Center. Operating revenues are derived solely from agency rentals and vending income. All financial activity relating to the Arkansas Services Center is reflected in the accompanying financial statements as auxiliary enterprises.

NOTE 15: Self-insurance Program

Beginning July 1, 1994, Arkansas State University established a self-funded health benefit plan for employees and their eligible dependents. All campuses of the University participate in the program, which is administered by USABLE and NOVA administrators.

There are three plans available to employees. These include: USABLE Classic I, USABLE Point of Service and NOVA Classic I. At June 30, 2004, approximately 3,584 active employees, their dependents, former employees and retirees were participating in the program. For those participating in the USABLE Classic and the NOVA Classic I plans, the University pays 94% of the total premium for full-time employees and early retirees, and 72% of the total premium for dependents, while former employees, through COBRA, may participate on a fully contributory basis. For those participating in the USABLE Point of Service plan, the University pays 80% of the total premium for full-time employees and early retirees, and 72% of the total premium for dependents, while former employees, through COBRA, may participate on a fully contributory basis.

The University estimates its unpaid health claims liability beyond the experience period to be \$773,929 with USABLE. This is equal to approximately 16.11% of the previous twelve months claims paid.

The University purchases specific and aggregate reinsurance to reduce its exposure to large claims. Reliance National Company of Philadelphia, Pennsylvania was chosen as the reinsurance carrier. Under the specific arrangement, the reinsurance carrier pays for claims for covered employees that exceed \$125,000.

ARKANSAS STATE UNIVERSITY  
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NOTE 16: Endowment Funds

The University has donor-restricted endowment funds. Investment income on the amount endowed is restricted for scholarships and other purposes. All endowment funds are maintained as investments. Investments, reported at fair value, include U. S. Government obligations, common stock, mutual funds, Common Fund – Intermediate and other managed investments. The endowment net assets at June 30, 2004 were \$8,533,741. Of this amount, \$8,149,723 was nonexpendable and the remaining \$384,018 was expendable.

State law allows a governing board to expend a portion of the net appreciation in the fair value of the assets over the historic dollar value of the fund unless the applicable gift document states otherwise. State law stipulates that such expenses are to be for the purpose for which the endowment funds were established.

It is the University's policy for annual expenses from the endowment funds not to exceed 4.5% of the five (5) year average market value as determined at December 31. In periods with no market value appreciation, the University limits the spending to actual income generated by the endowment fund assets.

NOTE 17: Early Retirement of Debt

On March 1, 2004, the University issued bonds of \$11,555,000 with interest rates of 2 to 4.6 percent. Net bond proceeds of \$2,324,565 were deposited with an escrow agent to advance refund \$2,175,000 outstanding bonds dated April 1, 1992 with interest rates of 5.75 to 7.5 percent. The bond proceeds were also used to pay a four percent (4%) call premium and related interest and fees. These bonds were called on May 1, 2004.

The remaining proceeds of \$8,976,207 (after payment of \$254,228 net bond issuance costs) will be utilized for construction.

The University also refinanced a capital lease with the Arkansas State University Foundation, Inc., for equipment on August 11, 2003. The outstanding principal of the original lease, dated April 26, 2001, of \$324,129 was refinanced. The capital lease was also increased by \$182,871 for additional equipment financed by the Foundation for a total debt agreement of \$507,000. Additionally, the University paid \$29,607 before maturity date to complete the retirement of the original lease.

NOTE 18: Subsequent Events

- (a) On August 28, 2004, the University executed a capital lease with Key Government Finance, Inc., for the procurement of telecommunication networking equipment. The principal amount of the lease is \$1,565,782. Payments of \$173,258 representing principal and interest are due semi-annually commencing on August 28, 2004 and concluding on February 28, 2009.
- (b) On August 30, 2004, the University executed contractual agreements with Sungard SCT, Inc., and Oracle Corporation to begin implementation of a new campus-wide enterprise computing solution. Migration to the new hardware and software platforms began in October of 2004 and is scheduled for completion in August of 2007. The current estimated cost of this project is from \$8,600,000 to \$10,000,000.
- (c) On October 5, 2004, the University executed a twenty (20) year promissory note payable to the Arkansas State University Foundation, Inc., for the principal sum of \$465,000. Interest on the note accrues at a rate of six percent (6%) annually. Payments of principal and interest of \$3,332 are due monthly with a final payment to be made on or before October 1, 2024. The proceeds from the note were used to fund the University's portion of the construction costs of the new campus health center.
- (d) On October 19, 2004 and October 21, 2004, respectively, the University executed two (2) capital leases with UniversityLease, a division of California First National Bank for the procurement of computer hardware and software to be used in support of campus parking operations. The principal amount of the first lease is \$49,655. Monthly payments of \$1,521 are required over the thirty-six (36) month term of the lease. The second lease has a principal amount of \$138,178 with required monthly payments over its forty-eight (48) month term of \$3,305.