AUDIT REPORT

Tennessee Board of Regents

Walters State Community College

For the Years Ended
June 30, 2013, and June 30, 2012

STATE OF TENNESSEE

COMPTROLLER OF THE TREASURY

Department of Audit

Division of State Audit

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July 31, 2014

The Honorable Bill Haslam, Governor
Members of the General Assembly
The Honorable John G. Morgan, Chancellor
Dr. Wade B. McCamey, President

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Tennessee Board of Regents, Walters State Community College, for the years ended June 30, 2013, and June 30, 2012. You will note from the independent auditor's report that unmodified opinions were given on the fairness of the presentation of the financial statements.

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

Sincerely,

Deborah V. Loveless

Deborah V. Loveless, CPA
Director

14/045

Audit Report
Tennessee Board of Regents
Walters State Community College
For the Years Ended June 30, 2013, and June 30, 2012

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For the Years Ended June 30, 2013, and June 30, 2012

Opinions on the Financial Statements

The opinions on the financial statements are unmodified.

Audit Finding

As Reported in the Previous Three Audits, Management Needs to Improve Financial Statement Preparation and Review Procedures to Prevent Errors in Its Financial Statements*
Walters State Community College's procedures for preparation of its financial statements, including the financial statements of its component unit, Walters State Community College Foundation, should be improved to ensure the accuracy and proper classification of the information presented in its financial statements. This deficiency resulted in several significant reporting errors (page 50).

* This finding is repeated from prior audits.

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Independent Auditor's Report

The Honorable Bill Haslam, Governor
Members of the General Assembly
The Honorable John G. Morgan, Chancellor
Dr. Wade B. McCamey, President

Report on the Financial Statements

We have audited the accompanying financial statements of Walters State Community College, an institution of the Tennessee Board of Regents, which is a component unit of the State of Tennessee, and its discretely presented component unit as of and for the years ended June 30, 2013, and June 30, 2012, and the related notes to the financial statements, which collectively comprise the basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements, based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of Walters State Community College, and its discretely presented component unit as of June 30, 2013, and June 30, 2012, and the respective changes in financial position and, where applicable, cash flows thereof for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

As discussed in Note 1, the financial statements of Walters State Community College, an institution of the Tennessee Board of Regents, are intended to present the financial position, the changes in financial position, and the cash flows of only Walters State Community College. They do not purport to, and do not, present fairly the financial position of the Tennessee Board of Regents, as of June 30, 2013, and June 30, 2012, and the changes in financial position and cash flows thereof for the years then ended, in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

As discussed in Note 1, the college implemented GASB Statement 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, during the year ended June 30, 2013. Our opinion is not modified with respect to this matter.

As discussed in Note 16, the financial statements of Walters State Community College Foundation, a discretely presented component unit of Walters State Community College, include investments valued at $3,014,617.32 at June 30, 2013, (19.6% of net position of the foundation) and $2,069,119.00 at June 30, 2012, (16% of net position of the foundation), whose fair values have been estimated by management in the absence of readily determinable fair values. Management's estimates are based on information provided by the fund managers. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 5 through 19 and the schedule of funding progress on page 46 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the

Governmental Accounting Standards Board, which considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during the audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Supplementary Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the college's basic financial statements. The schedules of cash flows – component unit on page 47 are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The schedules of cash flows – component unit are the responsibility of the college's management and were derived from, and relate directly to, the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedules of cash flows – component unit are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated July 17, 2014, on our consideration of the college's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the college's internal control over financial reporting and compliance.

Deborah V. Loveless

Deborah V. Loveless, CPA
Director
July 17, 2014

Introduction

This section of Walters State Community College's financial report presents a discussion and analysis of the financial performance of the college during the years ended June 30, 2013, and June 30, 2012, with comparative information presented for the year ended June 30, 2011. This discussion has been prepared by management along with the financial statements and related note disclosures and should be read in conjunction with the independent auditor's report, the financial statements, and the notes to the financial statements.

The college has one discretely presented component unit, the Walters State Community College Foundation. More detailed information about the foundation is presented in Note 16 to the financial statements. This discussion and analysis focuses on the college and does not include the foundation.

Overview of the Financial Statements

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

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

The Statement of Net Position

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

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

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

The following table summarizes the college's assets, liabilities, deferred outflows/inflows, and net position at June 30, 2013; June 30, 2012; and June 30, 2011:

Summary of Net Position
(in thousands of dollars)

	2013	2012	2011
Assets:			
Current assets	$16,989	$18,322	$17,295
Capital assets, net	49,535	51,486	54,695
Other assets	7,021	4,979	5,490
Total assets	**73,545**	**74,787**	**77,480**
Deferred outflows of resources:			
Deferred amount on debt refunding	49	-	-
Liabilities:			
Current liabilities	8,287	7,365	7,893
Noncurrent liabilities	4,715	4,775	4,439
Total liabilities	**13,002**	**12,140**	**12,332**
Net position:			
Net investment in capital assets	48,857	50,734	53,875
Restricted – expendable	530	685	336

Unrestricted	11,205	11,228	10,937
Total net position	**$60,592**	**62,647**	**$65,148**

Comparison of Fiscal Year 2013 to Fiscal Year 2012

- Current assets decreased because an amount due from the primary government (Tennessee Department of Transportation-TDOT) at June 30, 2012, for the 25E Highway Renovations project was received by the Tennessee Board of Regents (TBR) and remains on deposit on the college's behalf in noncurrent assets at June 30, 2013.

- Capital assets decreased, in large part due to the demolition of two buildings, a house on North Main Street and the Laughlin Square Building, both located in Greeneville, Tennessee. They were demolished during fiscal year 2013 as a part of the ongoing Greeneville Campus Expansion capital outlay project.

- The increase in other assets included an increase in noncurrent cash because funds due from TDOT for the 25E Highway Renovations project were received at TBR. These funds are on deposit on the college's behalf until the State Building Commission approves a capital outlay project for which the funds can be used. The college has submitted a request to allocate the funds to the Greeneville Campus Expansion project.

- In March 2012, GASB issued Statement 65, *Items Previously Reported as Assets and Liabilities*. This statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities; it also recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. The provisions of this statement are effective for financial statements for periods beginning after December 15, 2012. The college has elected to early implement the provisions of this statement for fiscal year 2013. Hence, deferred outflows of resources increased due to a deferred amount on debt refunding. On August 1, 2012, the state issued $552,807.00 in revenue bonds to advance refund $608,595.00 of outstanding Series 2006A bonds. The advanced refunding resulted in a deferred outflow of $55,034.17 to be amortized over the next nine years.

- Current liabilities increased due to a 2.5% across-the-board cost-of-living increase that affected accrued liabilities in salaries and compensated absences. Also, unearned revenue increased for summer tuition, as well as governmental grants and contracts. Funds were received in fiscal year 2013 for the multi-year Niswonger i3 Grant. The increase in deposits held in custody for others increased as the Tennessee Technology Center at Morristown realized a cash and cash equivalents increase for fiscal year 2013.

- Noncurrent liabilities decreased as to the noncurrent compensated absences liability in fiscal year 2013. The calculation to determine noncurrent compensated absences is based on a three-year average of leave taken.

- Net investment in capital assets decreased, in large part due to the disposal by demolition of two buildings on the Greeneville campus. The house on North Main Street and the Laughlin Square Building were demolished as a part of the Greeneville Campus Expansion project. Additionally, disposals of equipment and library holdings were greater than the additions in fiscal year 2013. See Note 5 to the financial statements to see capital asset activity for the year ended June 30, 2013.

- Restricted expendable-other net position decreased in fiscal year 2013 due to a decrease in funding for the Workforce Investment Act (WIA) federal grant.

- Unrestricted net position decreased in fiscal year 2013 due to expenditures and transfers exceeding current-year revenues.

<u>Comparison of Fiscal Year 2012 to Fiscal Year 2011</u>

- Current assets increased primarily as a result of the college recognizing $1.9 million due from the primary government for the 25E Highway Renovations project. Two Transfer of Jurisdictions between the college and the Tennessee Department of Transportation (TDOT) were negotiated, compensating the college for land, easements, and damages.

- Capital assets decreased due to accumulated depreciation being greater than additions for the year.

- The other assets decreased due to the reduction of noncurrent cash, because expenditures in restricted funds and renewal and replacement funds were greater than additions.

- The current liabilities decreased due to the drop in recognition of unearned revenues related to the Distance Learning Telemedicine Grant and the decline in summer school enrollment. The calculated current compensated absences liability amount also decreased, thus further reducing current liabilities.

- Noncurrent liabilities increased due to an increase in the college's net OPEB obligation. This liability changed as a result of actuarial valuations and the annual required contribution. Additional information regarding the state's postemployment benefit healthcare plan is in Note 10 of the notes to the financial statements. Also, the Banner program PZRLEAV calculated a substantially larger amount of compensated absences as noncurrent, thus increasing noncurrent liabilities.

- The net investment in capital assets decreased due to accumulated depreciation being greater than additions for the year.

- The increase in restricted expendable net position was mainly attributable to a large increase in restricted expendable net position for capital projects – Greeneville/Greene County Campus Expansion, along with nominal increases in instructional department net position funded by Health Information Technology Consortium program income, and other net position funded by student government fees.

- Unrestricted net position increased primarily due to funding in unexpended plant funds for the Greeneville Campus Expansion project and 25E Highway Renovations project.

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

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

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

A summary of the college's revenues, expenses, and changes in net position for the year ended June 30, 2013, and the two previous years follows.

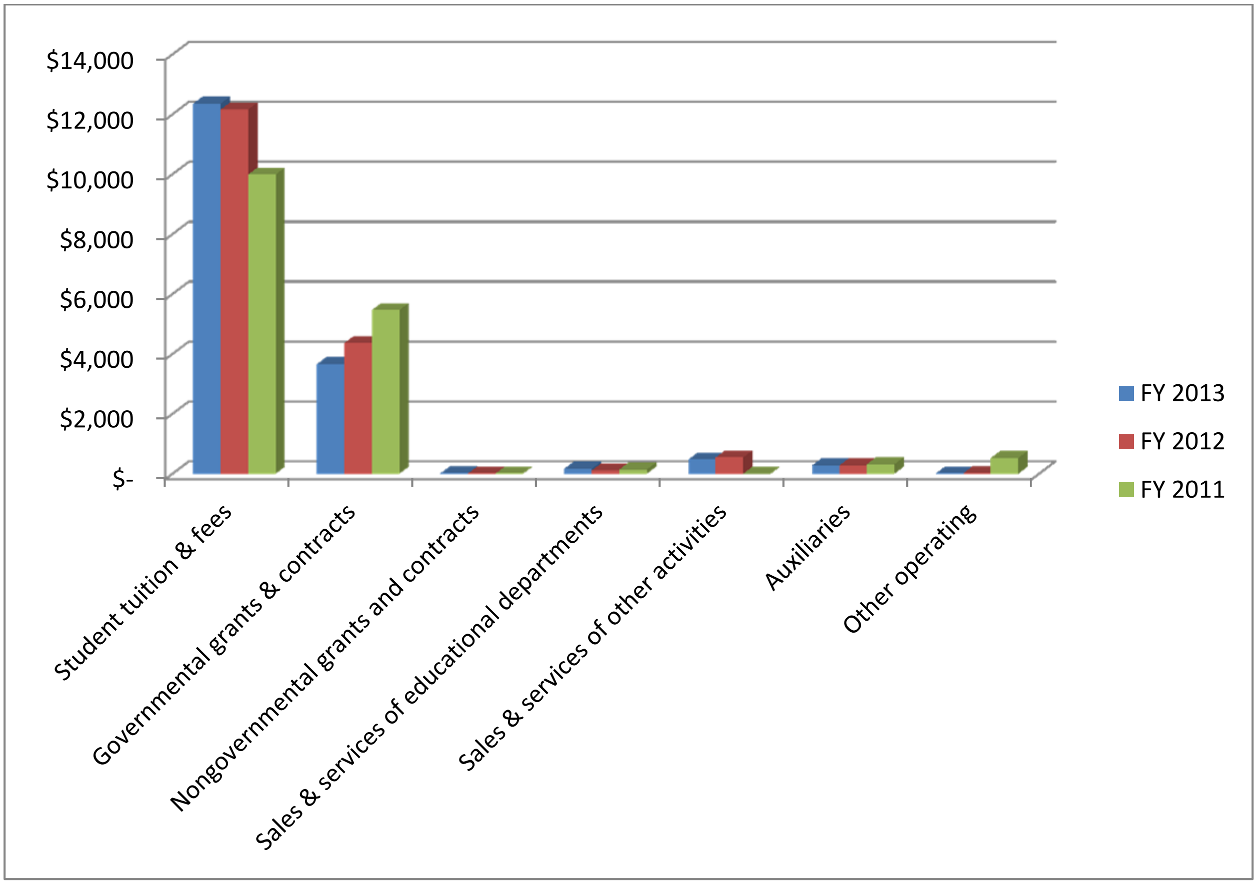
Summary of Revenues, Expenses, and Changes in Net Position
(in thousands of dollars)

	2013	2012	2011
Operating revenues	$16,969	$17,487	$16,460
Operating expenses	56,126	56,584	56,808
Operating loss	(39,157)	(39,097)	(40,348)
Nonoperating revenues and expenses	33,534	35,536	38,335
Income (loss) before other revenues, expenses, gains, or losses	(5,623)	(3,561)	(2,013)
Other revenues, expenses, gains, or losses	3,568	1,131	4,496
Increase (decrease) in net position	(2,055)	(2,430)	2,483
Net position at beginning of year	62,647	65,148	62,665
Prior period adjustment	-	(71)	-
Net position at end of year	$60,592	$62,647	$65,148

Operating Revenues

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

Operating Revenues
(in thousands of dollars)



Comparison of Fiscal Year 2013 to Fiscal Year 2012

- Student tuition and fees increased due to a tuition increase beginning with the fall 2012 semester.
- Government grants and contracts decreased due to reduced federal funding of the Workforce Investment Act (WIA).
- Nongovernmental grants and contracts increased in fiscal year 2013 due to the multi-year Niswonger i3 Grant received in fall 2012.

Comparison of Fiscal Year 2012 to Fiscal Year 2011

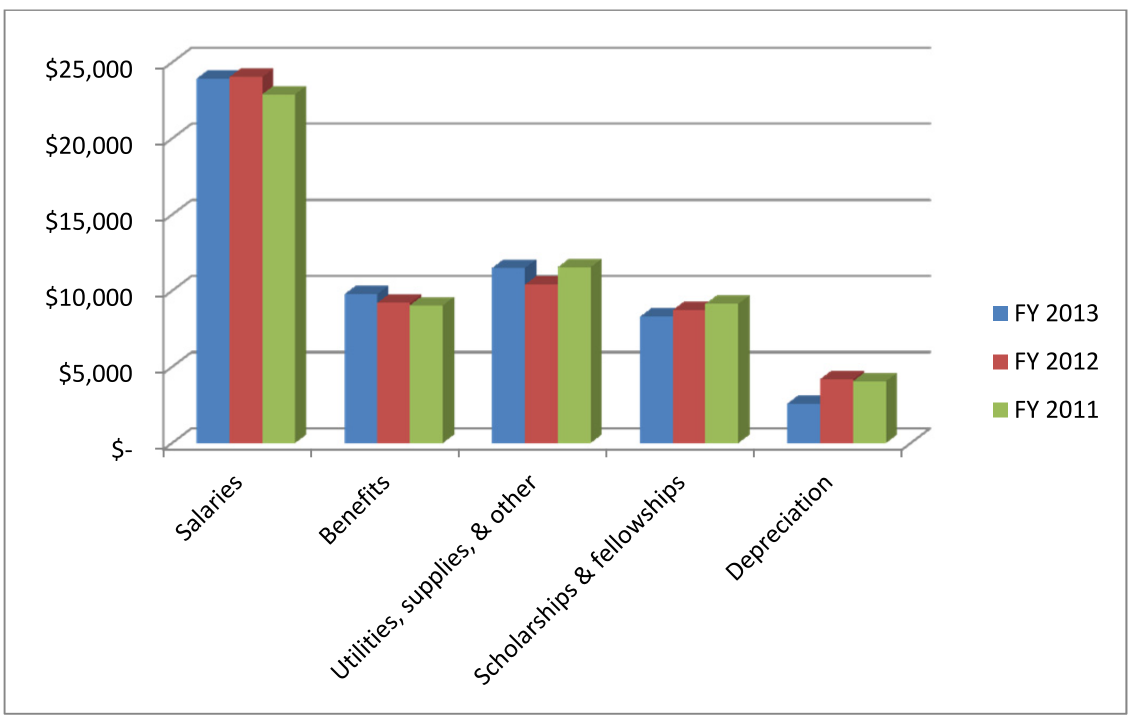
- Operating tuition and fees increased due to the implementation of the new allied health course fee and the new distance education course fee. Also, there was an increase in Regents Online Degree Program (RODP) enrollment and a 9.3% tuition increase. There was also a decrease in scholarship allowances associated with a decrease in Federal Pell grant awards and academic performance scholarships. Information regarding scholarship allowances can be located at the end of Note 1 in the notes to the financial statements.

- Operating grants and contracts decreased because of the continuing decrease in the Workforce Investment Act (WIA) programs and WIA funding from federal sources.

Operating Expenses

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

Operating Expenses – Natural Classification
(in thousands of dollars)



Comparison of Fiscal Year 2013 to Fiscal Year 2012

- A decrease in salaries can be attributed to a one-time service payment to faculty and staff awarded in fiscal year 2012 but not awarded in fiscal year 2013. In addition, the utilization of adjunct faculty decreased due to a decrease in fiscal year 2013 enrollment and the hiring of more full-time faculty.

- Benefits expense increased due to a change in classification of student service scholarships. In the past, the college classified the Academic Performance Scholarship and Academic Service Award Scholarship as scholarship expenses. However, in fiscal year 2013, it was determined service scholarships that create an employment relationship should more appropriately be classified as benefit expenses. In addition, benefits for health insurance increased, along with other postemployment benefit expenses.

- The other operating expense increase (utilities, supplies, and other services) in fiscal year 2013 can be attributed to multiple causes. Travel expenses increased because, for the first time, all five athletic teams participated in national post-season tournaments. Fiscal year 2013 was the second year of existence for the allied health and culinary arts special course fees. At year-end, unspent revenue from these fees is internally designated for use in the next year. Expenses increased in 2013 within these areas, as department deans were more conservative in spending for 2012 to ensure actual revenues were in line with projected revenue. Unexpended plant fund expenses increased for capital maintenance projects related to exterior building repairs funded by appropriations for the Expo Center and Plant Operations Buildings, as well as continued maintenance work on the Claiborne County Campus. In addition, funds remaining from the construction of the Student Services Building were allocated to remodel several areas within the College Center vacated by various student-related offices.

- Scholarship expenses decreased due to a classification change to recognize certain student service scholarships as benefit expenses, instead of scholarships, in fiscal year 2013.

- Depreciation expense decreased in fiscal year 2013, as a result of the College Center Building becoming fully depreciated in fiscal year 2012 and two buildings being demolished on the Greeneville campus, as part of the ongoing Greeneville Campus Expansion capital outlay project.

Comparison of Fiscal Year 2012 to Fiscal Year 2011

- Salaries increased due to a 3% across-the-board pay raise, a one-time service payment in 2012, and faculty and staff promotions.

- Benefits increased due to the increase in FICA and retirement expense associated with the salary increase and due to an increase in group insurance premiums.

- Other operating expense decreased due to the decrease in WIA funding and the reduction of expenditures associated with the Claiborne County Campus and campus improvements.

- Scholarships decreased due to a decrease in the funding for Federal Pell grants and academic performance scholarships.

- During fiscal year 2012, it was determined that periodicals should be more appropriately expensed. The estimated useful life of periodicals was decreased from ten to zero years, resulting in a current-year depreciation expense increase of $60,259.61. Increases in asset balances for land improvements and infrastructure, equipment, and intangible assets also led to increased depreciation expense.

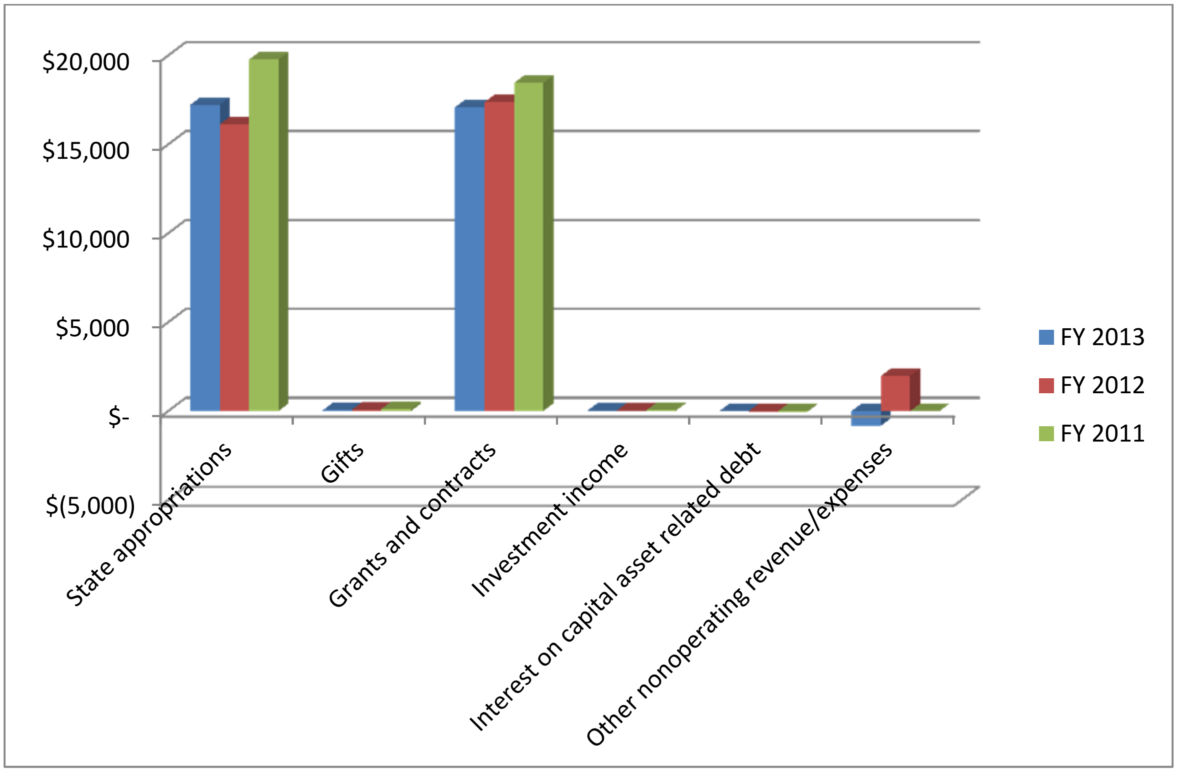
Nonoperating Revenues and Expenses

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

Nonoperating Revenues (Expenses)
(in thousands of dollars)

	2013	2012	2011
State appropriations	$17,227	$16,123	$19,773
Gifts	42	80	119
Grants and contracts	17,090	17,376	18,447
Investment income	22	21	32
Interest on capital asset-related debt	(19)	(34)	(36)
Other nonoperating revenue (expenses)	(828)	1,970	-
Total nonoperating revenues (expenses)	$33,534	$35,536	$38,335

Nonoperating Revenues/Expenses
(in thousands of dollars)



<u>Comparison of Fiscal Year 2013 to Fiscal Year 2012</u>

- State appropriations were increased by the State of Tennessee.

- Gift revenue decreased due to the reduction of private-sector gifts for scholarships, books, and equipment.

- Grants and contracts decreased due to a reduction in Federal Pell and Federal SEOG awards to students.

- On August 1, 2012, the state issued revenue bonds to advance refund $608,595.00 of outstanding Series 2006A bonds, resulting in a deferred outflow on debt refunding of $55,034.17 to be amortized over nine years. Further, the new debt was issued at a premium of $112,580.70 to be amortized over nine years. This debt refunding resulted in a net decrease to interest expense paid on capital debt for fiscal year 2013.

- Other nonoperating expenses increased due to the recognition of a loss on disposal of capital assets. Two buildings, a house on North Main Street and the Laughlin Square Building (both located in Greeneville, Tennessee), were demolished during fiscal year 2013 as a part of the ongoing Greeneville Campus Expansion capital outlay project.

Comparison of Fiscal Year 2012 to Fiscal Year 2011

- The other nonoperating revenues increase is directly attributed to funding related to the 25E Highway Renovations project.

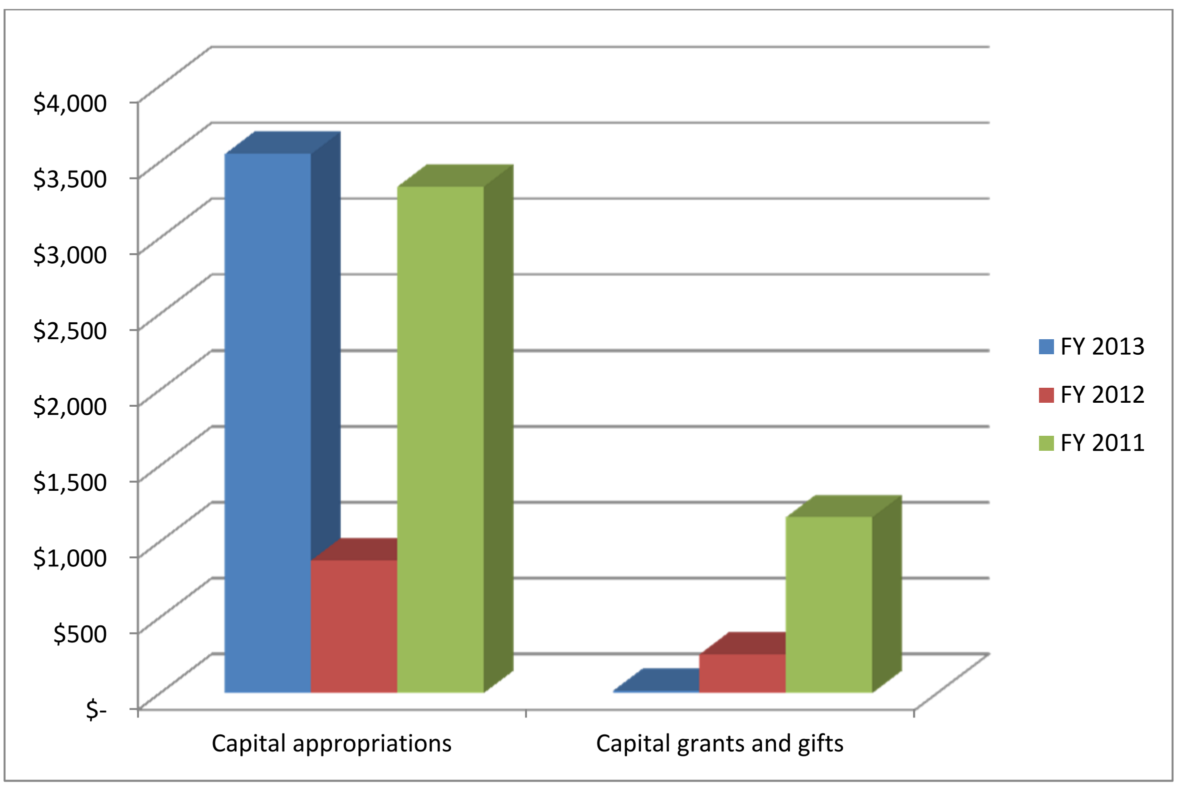
- Nonoperating grants and contracts decreased slightly due to the reduction in American Recovery and Reinvestment Act (ARRA) funding.

- Nonoperating state appropriations decreased due to the completion of one-time nonrecurring appropriations (State Fiscal Stabilization funds and Maintenance of Effort funds) in 2011 and an overall decrease in state appropriations.

Other Revenues

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

Other Revenues
(in thousands of dollars)



Comparison of Fiscal Year 2013 to Fiscal Year 2012

- The increase in capital appropriations for fiscal year 2013 can largely be attributed to the Greeneville Campus Expansion project entering the construction phase.

- In fiscal year 2012, the college received a capital gift of $250,000 from the foundation as matching funds for the Greeneville Campus Expansion project. This level of capital gifts was not sustained in fiscal year 2013.

Comparison of Fiscal Year 2012 to Fiscal Year 2011

- Capital appropriation revenue decreased due to the completion of the Student Services Building project in fiscal year 2011.

- Capital grants and gifts decreased due to the substantial Walters State Community College Foundation gift of the Laughlin Square Building at the Walters State Greeneville Campus that occurred in fiscal year 2011, and no substantial gift was received in fiscal year 2012.

Capital Assets and Debt Administration

Capital Assets

Walters State Community College had $49,534,662 invested in capital assets, net of accumulated depreciation of $42,305,977, at June 30, 2013; and $51,486,366 invested in capital assets, net of accumulated depreciation of $40,744,097 at June 30, 2012. Depreciation charges totaled $2,605,017 and $4,210,258 for the years ended June 30, 2013, and June 30, 2012, respectively.

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

	2013	2012	2011
Land	$ 1,082	$ 884	$ 889
Land improvements & infrastructure	1,723	1,864	1,496
Buildings	42,960	45,885	49,079
Equipment	1,648	1,882	2,026
Library holdings	139	162	245
Intangible assets	472	630	667
Projects in progress	1,511	179	293
Total	$49,535	$51,486	$54,695

Comparison of Fiscal Year 2013 to Fiscal Year 2012

Significant reductions to capital assets occurred in fiscal year 2013. Two buildings located on the Greeneville campus, a house on North Main Street and the Laughlin Square Building, were demolished during fiscal year 2013 as a part of the ongoing Greeneville Campus Expansion capital outlay project. Although an overall reduction in capital assets occurred in fiscal year 2013, the expansion project in Greeneville also attributed to increases in the projects in progress and land asset categories.

At June 30, 2013, outstanding commitments under construction contracts totaled $5,011,693 for the Greeneville Campus Expansion and Greeneville Sewer Corrections projects. Future state capital outlay appropriations will fund $3,027,628 of these costs.

Comparison of Fiscal Year 2012 to Fiscal Year 2011

Land decreased because the State of Tennessee purchased land related to the 25E Highway Renovation project. Land improvements and infrastructure increased due to additions being greater than depreciation. Buildings decreased due to current-year depreciation being greater than additions. Equipment decreased due to current-year depreciation, a prior-period adjustment to depreciation, and any related disposals being greater than additions. The decrease in library holdings is because of a change in accounting estimate. The decrease in intangible assets (software) was due to annual depreciation being greater than additions. The decrease in projects in progress was due to the completion of five projects.

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

Debt

The college had $726,157 and $752,199 in debt outstanding at June 30, 2013, and June 30, 2012, respectively. The table below summarizes these amounts by type of debt instruments.

Schedule of Outstanding Debt

	2013	**2012**	**2011**
Bonds	$626,085	$752,199	$819,689
Unamortized bond premium	100,072	-	-
Total	$726,157	$752,199	$819,689

The Tennessee State School Bond Authority (TSSBA) issued bonds with interest rates ranging from 4% to 5% due serially until 2021 on behalf of Walters State Community College. The college is responsible for the debt service of these bonds. The current portion of the $726,157 outstanding at June 30, 2013, is $73,279.

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

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

More information about the college's long-term liabilities is presented in Note 7 to the financial statements.

Economic Factors That Will Affect the Future

The Tennessee Board of Regents (TBR) approved a 3.0% maintenance fee increase effective for fall 2013. The state legislature approved a 1.5% salary increase for college employees effective July 1, 2013. However, only about two-thirds of the 1.5% was funded by the state. Therefore, the other one-third was to be funded from the maintenance fee increase. The college has an externally prepared compensation pay plan that has been partially paid. The college has funded and been approved to fully implement the final phase of the plan as of October 2013 to be retroactive to July 2013.

Preliminary enrollment data for the fall 2013 semester indicates a downward trend, which will have an adverse effect on revenue sources for the college for 2013-2014. However, the college is poised to manage the effect of the downturn. The college will be entering the fourth year of funding under Tennessee's new funding formula for allocation of state appropriations. With the new emphasis on funding being focused on outcomes such as degree completions and job placements, the college has maintained a favorable position among the funding for community colleges in the TBR system.

Walters State's official three-year cohort default rate relative to student loans is currently 20.3%. As a result of the recent increase in the cohort default rate and the rise of student debt, the college has elected to no longer participate in the William D. Ford Federal Direct Student Loan Program effective with the 2013-2014 award year. Based on guidance from the U.S. Department of Education, the institution did not remove the William D. Ford Federal Direct Student Loan Program from our Program Participation Agreement. However, a notice was provided to the Department of Education to inform the department of the decision for the college to no longer participate in this program. This decision was made in an attempt to help ensure a reduction of the college's cohort default rate to a level that would no longer jeopardize the loss of other Title IV programs. The Financial Aid Office is also working with the Tennessee Student Assistance Corporation (TSAC) to compile a statistical analysis of default patterns and trends. The college does not anticipate the lack of participation in the loan program to affect graduation rates.

The college has begun construction of a new building at the Greeneville campus. Site work has been completed to the point that steel construction has begun. The building is currently on target to be completed by the end of calendar year 2014.

The college is also continuing to implement various aspects of the Complete College Tennessee Act of 2010. Among initiatives currently underway is the implementation of a Business Process Modeling project that is to streamline operations across the TBR institutions with an expectation that institutions will realize savings by utilizing "industry standard" processes. The college may be faced with purchasing additional software systems to implement such processes.

Tennessee Board of Regents
WALTERS STATE COMMUNITY COLLEGE
Statements of Net Position
June 30, 2013, and June 30, 2012

	Walters State Community College		Component Unit - Walters State Community College Foundation	
	June 30, 2013	June 30, 2012	June 30, 2013	June 30, 2012
ASSETS				
Current assets:				
Cash and cash equivalents (Notes 2, 3, and 16)	$ 15,812,084.84	$ 15,181,546.23	$ 2,036,951.71	$ 2,087,024.65
Accounts and grants receivable (net) (Note 4)	1,109,725.04	1,057,034.93	-	14,563.34
Due from primary government	-	1,978,670.00	-	-
Due from the college	-	-	717.50	-
Pledges receivable (net) (Note 16)	-	-	37,378.38	60,027.48
Inventories	27,107.16	21,323.35	-	-
Prepaid expenses	38,163.88	80,720.05	9,241.58	8,105.75
Accrued interest receivable	-	-	-	26.72
Other assets	1,776.09	2,483.59	-	-
Total current assets	16,988,857.01	18,321,778.15	2,084,289.17	2,169,747.94
Noncurrent assets:				
Cash and cash equivalents (Notes 2, 3, and 16)	7,020,917.24	4,978,805.99	1,486,000.00	-
Investments (Note 16)	-	-	10,560,314.50	9,866,294.65
Pledges receivable (net) (Note 16)	-	-	74,914.81	101,454.00
Capital assets (net) (Notes 5 and 16)	49,534,661.63	51,486,366.17	2,383,879.99	1,819,618.32
Other assets	-	-	-	218,257.40
Total noncurrent assets	56,555,578.87	56,465,172.16	14,505,109.30	12,005,624.37
Total assets	73,544,435.88	74,786,950.31	16,589,398.47	14,175,372.31
DEFERRED OUTFLOWS OF RESOURCES				
Deferred amount on debt refunding	48,919.27	-	-	-
Total deferred outflows of resources	48,919.27	-	-	-
LIABILITIES				
Current liabilities:				
Accounts payable (Note 6)	474,480.78	638,602.94	25,246.02	16,607.73
Accrued liabilities	2,016,631.24	2,069,111.33	-	-
Due to component unit	717.50	-	-	-
Unearned revenue	1,253,834.84	884,082.67	8,000.00	8,000.00
Compensated absences (Note 7)	481,027.24	220,607.35	-	-
Accrued interest payable	4,493.04	5,454.48	-	-
Long-term liabilities, current portion (Notes 7 and 16)	73,278.50	70,325.00	108,000.00	96,000.00
Deposits held in custody for others	3,890,247.76	3,404,485.60	-	-
Other liabilities	91,638.39	72,433.88	-	-
Total current liabilities	8,286,349.29	7,365,103.25	141,246.02	120,607.73
Noncurrent liabilities:				
Net OPEB obligation (Note 10)	2,723,233.45	2,518,609.64	-	-
Unearned revenue	-	-	69,142.96	72,000.00
Compensated absences (Note 7)	1,338,894.61	1,574,520.41	-	-
Long-term liabilities (Notes 7 and 16)	652,878.74	681,873.50	921,000.00	1,029,000.00
Other liabilities (Note 16)	-	-	50,000.00	50,000.00
Total noncurrent liabilities	4,715,006.80	4,775,003.55	1,040,142.96	1,151,000.00
Total liabilities	13,001,356.09	12,140,106.80	1,181,388.98	1,271,607.73
NET POSITION				
Net investment in capital assets	48,857,423.66	50,734,167.67	1,354,879.99	694,618.32
Restricted for:				
Nonexpendable:				
Scholarships and fellowships	-	-	8,401,721.97	6,577,592.02
Other	-	-	1,358,556.10	1,357,056.10
Expendable:				
Scholarships and fellowships	33,211.68	45,210.28	1,968,335.97	1,644,784.76
Instructional department uses	88,318.69	75,036.54	-	-
Capital projects	250,000.00	250,000.00	-	-
Other	158,121.07	314,248.86	2,055,603.81	2,329,147.97
Unrestricted	11,204,923.96	11,228,180.16	268,911.65	300,565.41
Total net position	$ 60,591,999.06	$ 62,646,843.51	$ 15,408,009.49	$ 12,903,764.58

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

Tennessee Board of Regents
WALTERS STATE COMMUNITY COLLEGE
Statements of Revenues, Expenses, and Changes in Net Position
For the Years Ended June 30, 2013, and June 30, 2012

	Walters State Community College		Component Unit - Walters State Community College Foundation	
	Year Ended June 30, 2013	Year Ended June 30, 2012	Year Ended June 30, 2013	Year Ended June 30, 2012
REVENUES				
Operating revenues:				
Student tuition and fees (net of scholarship allowances of $9,726,905.18 for the year ended June 30, 2013, and $9,773,147.63 for the year ended June 30, 2012)	$ 12,356,803.13	$ 12,156,392.21	$ -	$ -
Gifts and contributions	-	-	219,464.13	501,274.39
Governmental grants and contracts	3,659,782.37	4,361,553.01	-	-
Nongovernmental grants and contracts	18,183.20	11,195.46	-	-
Sales and services of educational departments	173,889.95	114,240.24	-	-
Sales and services of other activities	472,661.17	543,538.67	-	-
Auxiliary enterprises:				
Bookstore	256,707.52	263,069.79	-	-
Food service	10,886.49	8,664.17	-	-
Other auxiliaries	9,737.56	10,366.56	-	-
Other operating revenues	10,029.13	18,398.17	152,961.15	121,844.50
Total operating revenues	16,968,680.52	17,487,418.28	372,425.28	623,118.89
EXPENSES				
Operating expenses (Note 13):				
Salaries and wages	23,946,234.08	24,042,713.26	-	-
Benefits	9,778,171.95	9,198,457.54	-	-
Utilities, supplies, and other services	11,504,735.70	10,402,462.10	119,526.46	112,291.32
Scholarships and fellowships	8,291,002.49	8,730,663.36	407,973.62	359,791.71
Depreciation expense	2,605,016.61	4,210,258.07	62,562.27	44,332.50
Payments to or on behalf of Walters State Community College (Note 16)	-	-	33,701.49	256,980.36
Total operating expenses	56,125,160.83	56,584,554.33	623,763.84	773,395.89
Operating loss	(39,156,480.31)	(39,097,136.05)	(251,338.56)	(150,277.00)
NONOPERATING REVENUES (EXPENSES)				
State appropriations	17,227,301.50	16,123,158.44	-	-
Gifts (college gifts include $17,201.49 from component unit in 2013 and $6,980.36 in 2012)	42,362.39	79,994.46	-	-
Grants and contracts	17,089,992.50	17,375,605.61	-	-
Investment income (for component unit, net of investment expense of $44,077.42 in 2013 and $43,965.89 in 2012)	21,821.25	21,399.78	651,182.71	(167,132.33)
Interest on capital asset-related debt	(19,118.91)	(33,790.55)	-	-
Bond issuance costs	(1,758.53)	-	-	-
Other nonoperating revenues (expenses)	(827,041.23)	1,969,555.34	(166,662.93)	3,444.60
Net nonoperating revenues (expenses)	33,533,558.97	35,535,923.08	484,519.78	(163,687.73)
Income (loss) before other revenues, expenses, gains, or losses	(5,622,921.34)	(3,561,212.97)	233,181.22	(313,964.73)
Capital appropriations	3,551,476.75	874,776.74	-	-
Capital grants and gifts (college gifts include $16,500.00 from component unit in 2013 and $250,000.00 in 2012)	16,600.14	255,891.51	365,720.04	575,708.22
Additions to permanent endowments	-	-	1,905,343.65	287,239.46
Total other revenues	3,568,076.89	1,130,668.25	2,271,063.69	862,947.68
Increase (decrease) in net position	(2,054,844.45)	(2,430,544.72)	2,504,244.91	548,982.95
NET POSITION				
Net position - beginning of year	62,646,843.51	65,148,318.07	12,903,764.58	12,354,781.63
Prior period adjustment (Note 14)	-	(70,929.84)	-	-
Net position - end of year	$ 60,591,999.06	$ 62,646,843.51	$ 15,408,009.49	$ 12,903,764.58

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

Tennessee Board of Regents
WALTERS STATE COMMUNITY COLLEGE
Statements of Cash Flows
For the Years Ended June 30, 2013, and June 30, 2012

	Year Ended June 30, 2013	Year Ended June 30, 2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Tuition and fees	$ 12,482,069.07	$ 12,264,765.85
Grants and contracts	3,913,130.69	3,758,936.40
Sales and services of educational activities	174,554.95	114,240.24
Sales and services of other activities	472,661.17	552,214.67
Payments to suppliers and vendors	(11,574,704.65)	(10,304,899.87)
Payments to employees	(23,882,712.95)	(24,015,810.91)
Payments for benefits	(9,641,038.26)	(8,988,396.36)
Payments for scholarships and fellowships	(8,291,002.49)	(8,729,171.53)
Auxiliary enterprise charges:		
Bookstore	261,984.46	299,090.55
Food services	9,130.15	9,617.71
Other	9,737.56	10,366.56
Other receipts	10,029.13	18,398.17
Net cash used by operating activities	(36,056,161.17)	(35,010,648.52)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State appropriations	17,237,700.00	16,098,800.00
Gifts and grants received for other than capital or endowment purposes	17,126,245.19	17,480,050.36
Federal student loan receipts	3,720,715.00	3,753,818.00
Federal student loan disbursements	(3,775,518.00)	(3,761,707.00)
Changes in deposits held for others	501,329.66	(142,726.86)
Other noncapital financing receipts	268,978.50	56,330.00
Net cash provided by noncapital financing activities	35,079,450.35	33,484,564.50
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Capital appropriations	3,530,300.64	875,776.74
Proceeds from sale of capital assets	1,956,686.52	5,439.75
Capital grants and gifts	-	250,000.00
Purchases of capital assets and construction	(1,762,648.32)	(1,108,122.36)
Principal paid on capital debt	(70,325.00)	(67,490.50)
Interest paid on capital debt	(26,474.41)	(34,258.26)
Net cash provided (used) by capital and related financing activities	3,627,539.43	(78,654.63)
CASH FLOWS FROM INVESTING ACTIVITIES		
Income on investments	21,821.25	21,399.78
Net cash provided by investing activities	21,821.25	21,399.78
Net increase (decrease) in cash	2,672,649.86	(1,583,338.87)
Cash at beginning of year	20,160,352.22	21,743,691.09
Cash at end of year	$ 22,833,002.08	$ 20,160,352.22

Tennessee Board of Regents
WALTERS STATE COMMUNITY COLLEGE
Statements of Cash Flows (Continued)
For the Years Ended June 30, 2013, and June 30, 2012

	Year Ended June 30, 2013	Year Ended June 30, 2012
Reconciliation of operating loss to net cash used by operating activities:		
Operating loss	$ (39,156,480.31)	$ (39,097,136.05)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation expense	2,605,016.61	4,210,258.07
Gifts in-kind	34,506.34	42,848.60
Other adjustments	24,901.50	24,858.44
Change in assets and liabilities:		
Receivables, net	9,444.00	(190,998.45)
Inventories	(5,783.81)	(1,557.90)
Prepaid items	42,556.17	(20,216.96)
Other assets	707.50	389.75
Accounts payable	(161,454.16)	103,548.40
Accrued liabilities	(52,480.09)	54,812.36
Net OPEB obligation	204,623.81	157,942.51
Unearned revenues	371,065.17	(294,948.51)
Compensated absences	24,794.09	3,404.07
Other	2,422.01	(3,852.85)
Net cash used by operating activities	$ (36,056,161.17)	$ (35,010,648.52)
Noncash investing, capital, or financing transactions		
Gifts of capital assets	$ 16,500.00	$ 5,891.51
Gain (loss) on disposal of capital assets	$ (1,154,970.68)	$ 254,061.79
Trade-in allowance	$ -	$ 19,340.85

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

Note 1. Summary of Significant Accounting Policies

Reporting Entity

The college is a part of the State University and Community College System of Tennessee (Tennessee Board of Regents). This system is a component unit of the State of Tennessee because the state appoints a majority of the system's governing body and provides significant financial support; the system is discretely presented in the *Tennessee Comprehensive Annual Financial Report*.

The financial statements present only that portion of the Tennessee Board of Regents' activities that is attributable to the transactions of Walters State Community College.

The Walters State Community College Foundation is considered a component unit of the college. Although the college 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 college by its donors. Because these restricted resources held by the foundation can only be used by, or for the benefit of, the college, the foundation is considered a component unit of the college and is discretely presented in the college's financial statements. See Note 16 for more detailed information about the component unit and how to obtain the report.

Basis of Presentation

The college and the foundation's financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America applicable to governmental colleges and universities engaged in business-type activities as prescribed by the Governmental Accounting Standards Board (GASB).

Basis of Accounting

For financial statement purposes, the college is considered a special-purpose government engaged only in business-type activities. Accordingly, the financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all of the provider's eligibility requirements have been met. All significant interfund transactions have been eliminated.

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

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

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

Inventories

Inventories are valued at the lower of cost or market on an average cost or first-in, first-out basis.

Cash Equivalents

This classification included instruments that are readily convertible to known amounts of cash and have original maturities of three months or less.

Compensated Absences

The college's employees accrue annual and sick leave at varying rates, depending on length of service or classification. Some employees also earn compensatory time.

The amount of the liabilities for annual leave and compensatory time and their related benefits are reported in the statement of net position. There is no liability for unpaid accumulated sick leave since the college's policy is to pay this only if the employee dies or is absent because of illness, injury, or related family death.

Capital Assets

Capital assets, which include property, plant, equipment, library holdings, and intangible assets, are reported in the statement of net position at historical cost or at fair value at date of donation, less accumulated depreciation/amortization. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend the asset's useful life are not capitalized.

A capitalization threshold of $100,000 is used for buildings, and $50,000 is used for infrastructure. Equipment is capitalized when the unit acquisition cost is $5,000 or greater. The capitalization threshold for additions and improvements to buildings and land is set at $50,000. The capitalization threshold for intangible assets is set at $100,000.

These assets, with the exception of land, are depreciated/amortized using the straight-line method over the estimated useful lives, which range from 5 to 40 years.

Under a contract with the Tennessee Department of Labor and Workforce Development, the college is the administrative entity and grant recipient for the Local Workforce Investment Area in Workforce Investment Area 2 of the State of Tennessee. The title to all the equipment purchased by Walters State Community College under the provisions of the Workforce Investment Act resides with the U.S. government. Therefore, this equipment is not included in the college's capital assets.

Net Position

The college's net position is classified as follows:

<u>Net investment in capital assets</u> – This represents the college's total investment in capital assets, net of accumulated depreciation and net of outstanding debt obligations and deferred outflows/inflows of resources related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of net investment in capital assets.

<u>Nonexpendable restricted net position</u> – Nonexpendable restricted net position consists of endowment and similar type funds in which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may be expendable or added to principal.

<u>Expendable restricted net position</u> – Expendable restricted net position includes resources that the college is legally or contractually obligated to spend in accordance with restrictions imposed by external third parties.

<u>Unrestricted net position</u> – Unrestricted net position represents resources derived from student tuition and fees; state appropriations; sales and services of educational departments and other activities; and auxiliary enterprises. These resources are used for transactions relating to the educational and general operations of the college and may be used at the college's discretion to meet current expenses for any purpose. The auxiliary enterprises are substantially self-supporting activities that provide services for students, faculty, and staff.

Scholarship Discounts and Allowances

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

Accounting Change

The college implemented GASB Statement 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, during the year ended June 30, 2013. The effect on the college was the renaming of the residual of all other elements in the statement of financial position as net position, rather than net assets. Amounts on the statement of net position and statement of revenues, expenses, and changes in net position have been restated for comparative purposes for the year ended June 30, 2012.

Early Implementation of Accounting Pronouncement

In March 2012, GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities; it also recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. The provisions of this statement are effective for financial statements for periods beginning after December 15, 2012. However, the college has elected to implement the provisions of this statement for fiscal year 2013. Amounts on the statement of net position and statement of revenues, expenses, and changes in net position have been restated for comparative purposes for the year ended June 30, 2012.

Note 2. Cash

This classification includes demand deposits and petty cash on hand. At June 30, 2013, cash consisted of $2,537,654.29 in bank accounts, $4,290.00 of petty cash on hand, $18,088,402.79 in the State of Tennessee Local Government Investment Pool (LGIP) administered by the State Treasurer, $250,000.00 in LGIP deposits for capital projects, and $1,952,655.00 on deposit with the Tennessee Board of Regents. At June 30, 2012, cash consisted of $2,957,298.85 in bank accounts, $4,290.00 of petty cash on hand, $16,948,736.65 in the State of Tennessee Local Government Investment Pool (LGIP) administered by the State Treasurer, and $250,026.72 in LGIP deposits for capital projects.

The college has deposits in the LGIP, which is administered by the State Treasurer. The LGIP is part of the State Pooled Investment Fund. The fund's required risk disclosures are presented in the *State of Tennessee Treasurer's Report*. That report is available on the state's website at www.treasury.tn.gov.

LGIP deposits for capital projects – Payments related to the college's capital projects are made by the State of Tennessee's Department of Finance and Administration. The college's estimated local share of the cost of each project is held in a separate LGIP account. As expenses are incurred, the Tennessee Board of Regents withdraws funds from the LGIP account and transfers them to the Department of Finance and Administration. The funds in the account are not available to the college for any other purpose until the project is completed and the Tennessee Board of Regents releases any remaining funds.

Note 3. Investments

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The college is authorized by statute to invest funds in accordance with Tennessee Board of Regents policies. Under the current policy, funds other than endowments may be invested only in obligations of the United States or its agencies which are backed by the full faith and credit of the United States; repurchase agreements for United States securities; certificates of deposit in banks and savings and loan associations; bankers' acceptances; commercial paper; money market mutual funds; and the State of Tennessee Local Government Investment Pool.

Tennessee Board of Regents policy restricts investments in bankers' acceptances and commercial paper. The policy requires that prime bankers' acceptances must be issued by domestic banks with a minimum AA rating or foreign banks with a AAA long-term debt rating by a majority of the rating services that have rated the issuer. Prime bankers' acceptances are required to be eligible for purchase by the Federal Reserve System. To be eligible, the original maturity must not be more than 270 days, and it must 1) arise out of the current shipment of goods between countries or with the United States, or 2) arise out of storage within the United States of goods that are under contract of sale or are expected to move into the channel of trade within a reasonable time and that are secured throughout their life by a warehouse receipt or similar document conveying title to the underlying goods.

Tennessee Board of Regents policy requires that prime commercial paper shall be limited to that of corporations that meet the following criteria: 1) Senior long-term debt, if any, should have a minimum rating of A1 or equivalent, and short-term debt should have a minimum rating of A1 or equivalent, as provided by a majority of the rating services that rate the issuer. If there is no long-term debt rating, the short-term debt rating must be A1 by all rating services (minimum of two). 2) The rating should be based on the merits of the issuer or guarantee by a nonbank. 3) A financial review should be made to ascertain the issuer's financial strength to cover the debt. 4) Commercial paper of a banking institution should not be purchased. Prime commercial paper shall not have a maturity that exceeds 270 days.

As of June 30, 2013, and June 30, 2012, the college's investments consisted entirely of investments in the Local Government Investment Pool. The fair value of these investments was $18,338,402.79 at June 30, 2013, and $17,198,763.37 at June 30, 2012. LGIP investments are not rated by nationally recognized statistical ratings organizations. The LGIP is part of the State Pooled Investment Fund. The fund's required risk disclosures are presented in the *State of Tennessee Treasurer's Report*. That report is available on the state's website at www.treasury.tn.gov.

Note 4. Receivables

Receivables included the following:

	June 30, 2013	June 30, 2012
Student accounts receivable	$1,103,337.51	$ 987,180.65
Grants receivable	541,597.71	669,075.15
Other receivables	160,672.97	114,237.73
Subtotal	1,805,608.19	1,770,493.53
Less allowance for doubtful accounts	695,883.15	713,458.60
Total receivables	$1,109,725.04	$1,057,034.93

Note 5. Capital Assets

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

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$ 884,281.81	$ 198,120.00	$ -	$ -	$ 1,082,401.81
Land improvements and infrastructure	3,048,657.27	-	-	-	3,048,657.27
Buildings	79,006,754.52	-	-	1,210,134.33	77,796,620.19
Equipment	7,259,361.99	264,362.16	-	940,248.59	6,583,475.56
Library holdings	436,574.99	13,303.51	-	47,724.65	402,153.85
Intangible assets	1,416,286.39	-	-	-	1,416,286.39
Projects in progress	178,546.47	1,332,497.08	-	-	1,511,043.55
Total	92,230,463.44	1,808,282.75	-	2,198,107.57	91,840,638.62
Less accumulated depreciation/amortization:					
Land improvements and infrastructure	1,184,010.62	142,289.80	-	-	1,326,300.42
Buildings	33,121,503.70	1,775,878.90	-	60,451.90	34,836,930.70
Equipment	5,377,375.23	492,897.71	-	934,960.34	4,935,312.60
Library holdings	274,588.11	36,533.51	-	47,724.65	263,396.97
Intangible assets	786,619.61	157,416.69	-	-	944,036.30
Total	40,744,097.27	2,605,016.61	-	1,043,136.89	42,305,976.99
Capital assets, net	$51,486,366.17	$ (796,733.86)	$ -	$1,154,970.68	$49,534,661.63

Capital asset activity for the year ended June 30, 2012, was as follows:

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$ 889,230.75	$ -	$ -	$ 4,948.94	$ 884,281.81
Land improvements and infrastructure	2,537,829.27	-	510,828.00	-	3,048,657.27
Buildings	78,987,522.92	19,231.60	-	-	79,006,754.52
Equipment	6,933,554.15	550,915.91	-	225,108.07	7,259,361.99
Library holdings	575,882.25	19,084.01	-	158,391.27	436,574.99
Intangible assets	1,296,536.44	-	119,749.95	-	1,416,286.39
Projects in progress	284,342.07	524,782.35	(630,577.95)	-	178,546.47
Total	91,504,897.85	1,114,013.87	-	388,448.28	92,230,463.44
Less accumulated depreciation/amortization:					
Land improvements and infrastructure	1,041,720.93	142,289.69	-	-	1,184,010.62
Buildings	29,908,337.64	3,213,166.06	-	-	33,121,503.70
Equipment	4,976,027.83	595,820.00	-	194,472.60	5,377,375.23
Library holdings	331,413.75	101,565.63	-	158,391.27	274,588.11
Intangible assets	629,202.92	157,416.69	-	-	786,619.61
Total	36,886,703.07	4,210,258.07	-	352,863.87	40,744,097.27
Capital assets, net	$54,618,194.78	$(3,096,244.20)	$ -	$ 35,584.41	$51,486,366.17

The fiscal year 2012 decrease in library holdings is partly due to a change in accounting estimate. During fiscal year 2012, it was determined that periodicals should be more appropriately expensed. The estimated useful life of periodicals was decreased from ten years to zero years, resulting in a current-year adjustment of $85,724.41.

Note 6. Accounts Payable

Accounts payable included the following:

	June 30, 2013	June 30, 2012
Vendors payable	$195,271.60	$260,288.29
Other payables	279,209.18	378,314.65
Total accounts payable	$474,480.78	$638,602.94

Note 7. Long-term Liabilities

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

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Payables:					
TSSBA debt:					
Bonds	$ 752,198.50	$ 552,807.00	$ 678,920.00	$ 626,085.50	$ 73,278.50
Unamortized bond premium	-	112,580.70	12,508.96	100,071.74	-
Subtotal	752,198.50	665,387.70	691,428.96	726,157.24	73,278.50
Other liabilities:					
Compensated absences	1,795,127.76	1,335,477.59	1,310,683.50	1,819,921.85	481,027.24
Subtotal	1,795,127.76	1,335,477.59	1,310,683.50	1,819,921.85	481,027.24
Total long-term liabilities	$2,547,326.26	$2,000,865.29	$2,002,112.46	$2,546,079.09	$554,305.74

Long-term liabilities activity for the year ended June 30, 2012, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Payables:					
TSSBA debt:					
Bonds	$ 819,689.00	$ -	$ 67,490.50	$ 752,198.50	$ 70,325.00
Subtotal	819,689.00	-	67,490.50	752,198.50	70,325.00
Other liabilities:					
Compensated absences	1,791,723.69	1,341,587.41	1,338,183.34	1,795,127.76	220,607.35
Subtotal	1,791,723.69	1,341,587.41	1,338,183.34	1,795,127.76	220,607.35
Total long-term liabilities	$2,611,412.69	$1,341,587.41	$1,405,673.84	$2,547,326.26	$290,932.35

TSSBA Debt – Bonds

Bonds, with interest rates ranging from 4% to 5%, were issued by the Tennessee State School Bond Authority (TSSBA). The bonds are due serially to 2021 and are secured by pledges of the facilities' revenues to which they relate and certain other revenues and fees of the college, including state appropriations; see Note 8 for further details.

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

Year Ending June 30	Principal	Interest	Total
2014	$ 73,278.50	$ 30,571.50	$103,850.00
2015	67,337.00	26,798.66	94,135.66
2016	70,889.00	23,387.40	94,276.40
2017	74,627.00	19,796.23	94,423.23
2018	78,561.00	16,015.68	94,576.68

2019 – 2021	261,393.00	23,318.85	284,711.85
Total	$626,085.50	$139,888.32	$765,973.82

Refunding of Debt

On August 1, 2012, the state issued $552,807.00 in revenue bonds with an average interest rate of 5% to advance refund $608,595.00 of outstanding Series 2006A bonds with an average interest rate of 4.23%. The net proceeds of $663,629.17 (including a premium of $112,580.70 and after payment of $1,758.53 in underwriter's fees and issuance costs) were deposited with an escrow agent to provide for all future debt service payments on the 2006A bonds. As a result, the Series 2006A bonds are considered to be defeased, and the liability for those bonds has been removed from the college's long-term liabilities.

Although the advance refunding resulted in the recognition of a deferred outflow of $55,034.17 to be amortized over the next nine years, the college in effect reduced its aggregate debt service payments by $59,772.53 over the next nine years and obtained an economic gain (difference between the present values of the old and new debt service payments) of $48,385.18.

Note 8. Pledged Revenues

The college has pledged certain revenues and fees, including state appropriations, to repay $626,085.50 in revenue bonds issued from June 26, 2006, to August 1, 2012 (see Note 7 for further detail). Proceeds from the bonds provided financing for an Energy Savings and Performance Contract. The bonds are payable through 2021. Annual principal and interest payments on the bonds are expected to require .24% of available revenues. The total principal and interest remaining to be paid on the bonds at June 30, 2013, is $765,973.82. Principal and interest paid for fiscal year 2013 and total available revenues were $95,837.97 and $40,288,644.81, respectively. Principal and interest paid for fiscal year 2012 and total available revenues were $106,735.53 and $39,111,813.13, respectively.

Note 9. Pension Plans

<u>Defined Benefit Plans</u>

Tennessee Consolidated Retirement System

<u>Plan Description</u> – The college contributes to the State Employees, Teachers, and Higher Education Employees Pension Plan (SETHEEPP), a cost-sharing, multiple-employer, defined benefit pension plan administered by the Tennessee Consolidated Retirement System (TCRS). TCRS provides retirement, death, and disability benefits, as well as annual cost-of-living adjustments to plan members and their beneficiaries. Title 8, Chapters 34-37, *Tennessee Code Annotated*, establishes benefit provisions. State statutes are amended by the Tennessee General Assembly.

The TCRS issues a publicly available financial report that includes financial statements and required supplementary information for SETHEEPP. That report is available on the state's website at www.treasury.tn.gov/tcrs.

Funding Policy – Plan members are noncontributory. The college is required to contribute an actuarially determined rate. The current rate is 15.03% of annual covered payroll. Contribution requirements for the college are established and may be amended by the TCRS' Board of Trustees. The college's contributions to TCRS for the years ended June 30, 2013; June 30, 2012; and June 30, 2011, were $2,425,254.14, $2,408,725.07, and $2,275,007.87, respectively. Contributions met the requirements for each year.

Defined Contribution Plans

Optional Retirement Plans

Plan Description – The college contributes to three defined contribution plans: Teachers Insurance and Annuity Association–College Retirement Equities Fund, ING Life Insurance and Annuity Company, and Variable Annuity Life Insurance Company. These plans are administered by the Tennessee Department of the Treasury. Each plan provides retirement benefits to faculty and staff who are exempt from the overtime provisions of the Fair Labor Standards Act and who waive membership in the TCRS. Benefits depend solely on amounts contributed to the plan plus investment earnings. Plan provisions are established by state statute in Title 8, Chapter 35, Part 4, *Tennessee Code Annotated*. State statutes are amended by the Tennessee General Assembly.

Funding Policy – Plan members are noncontributory. The college contributes an amount equal to 10% of the employee's base salary up to the social security wage base and 11% above the social security wage base. Contribution requirements are established and amended by state statute. The contributions made by the college to the plans were $486,208.91 for the year ended June 30, 2013, and $486,182.36 for the year ended June 30, 2012. Contributions met the requirements for each year.

Note 10. Other Postemployment Benefits

Health care is the only "other postemployment benefit" (OPEB) provided to employees. The State of Tennessee administers a group health insurance program which provides postemployment health insurance benefits to eligible college retirees. This program includes two plans available to higher education employees—the State Employee Group Plan and the Medicare Supplement Plan. For accounting purposes, the plans are agent multiple-employer defined benefit OPEB plans. Benefits are established and amended by an insurance committee created by Section 8-27-101, *Tennessee Code Annotated*. Prior to reaching age 65, all members have the option of choosing between the standard or partnership preferred provider organization plan for health care benefits. Subsequent to age 65, members who are also in the state's retirement system may participate in a state-administered Medicare supplement that does not include pharmacy. The state makes on-behalf payments to the Medicare Supplement Plan for the college's eligible retirees; see Note 15. The plans are reported in the *Tennessee Comprehensive Annual Financial Report* (CAFR). The CAFR is available on the state's website at www.tn.gov/finance/act/cafr.shtml.

Special Funding Situation

The State of Tennessee is legally responsible for contributions to the Medicare Supplement Plan, which covers the retirees of other governmental entities, including Walters State Community College. The state is the sole contributor for the college retirees who participate in the Medicare Supplement Plan and, therefore, is acting as the employer.

Funding Policy

The premium requirements of members of the State Employee Group Plan are established and may be amended by the insurance committee. The plan is self-insured and financed on a pay-as-you-go basis with the risk shared equally among the participants. The plan's claims liabilities are periodically computed using actuarial and statistical techniques to establish premium rates. The plan's administrative costs are allocated to plan participants. In accordance with Section 8-27-205(b), *Tennessee Code Annotated*, retirees in the State Employee Group Plan pay the same base premium, adjusted for years of service, as active employees. Retirees with 30 years of service are subsidized 80%; retirees with 20 years of service but less than 30 years of service, 70%; and retirees with less than 20 years of service, 60%. Retirees in the Medicare Supplement Plan have flat-rate premium subsidies based on years of service. Retirees with 30 years of service receive $50 per month; retirees with 20 years of service but less than 30 years of service, $37.50; and retirees with 15 years of service but less than 20 years of service, $25.

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

	2013	2012
Annual required contribution (ARC)	$ 710,000.00	$ 703,000.00
Interest on the net OPEB obligation	100,744.39	94,426.69
Adjustment to the ARC	(106,938.25)	(100,232.13)
Annual OPEB cost	703,806.14	697,194.56
Amount of contribution	(499,182.33)	(539,252.05)
Increase in net OPEB obligation	204,623.81	157,942.51
Net OPEB obligation – beginning of year	2,518,609.64	2,360,667.13
Net OPEB obligation – end of year	$2,723,233.45	$2,518,609.64

Year-end	Plan	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation at Year-end
June 30, 2013	State Employee Group Plan	$703,806.14	70.9%	$2,723,233.45

June 30, 2012	State Employee Group Plan	$697,194.56	77.3%	$2,518,609.64
June 30, 2011	State Employee Group Plan	$772,900.68	61.4%	$2,360,667.13

Funded Status and Funding Progress

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

	State Employee Group Plan
Actuarial valuation date	July 1, 2011
Actuarial accrued liability (AAL)	$5,978,000.00
Actuarial value of plan assets	-
Unfunded actuarial accrued liability (UAAL)	$5,978,000.00
Actuarial value of assets as a percentage of the AAL	0.00%
Covered payroll (active plan members)	$19,857,614.24
UAAL as percentage of covered payroll	30.1%

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future, and actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. The schedule of funding progress, presented as Required Supplementary Information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

Actuarial Methods and Assumptions

Calculations are based on the types of benefits provided under the terms of the substantive plan at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point. Actuarial calculations reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

In the July 1, 2011, actuarial valuation, the Projected Unit Credit actuarial cost method was used. The actuarial assumptions included a 4% investment rate of return (net of administrative expenses) and an annual health care cost trend rate of 9.25% initially. The rate decreased to 8.75% in fiscal year 2013 and then reduces by decrements to an ultimate rate of 5% in fiscal year 2021. All rates include a 2.5% inflation assumption, which also represents the projected salary increase. The unfunded actuarial accrued liability is being amortized as a level percentage of payroll on a closed basis over a 30-year period beginning with July 1, 2007.

Note 11. Insurance-related Activities

It is the policy of the state not to purchase commercial insurance for the risks associated with casualty losses for general liability, automobile liability, professional medical malpractice, and workers' compensation. The state's management believes it is more economical to manage these risks internally and set aside assets for claim settlement in its internal service fund, the Risk Management Fund. The state purchases commercial insurance for real property, builder's risk (for construction projects starting prior to July 1, 2012), and crime and fidelity coverage on the state's officials and employees. The contractor is responsible for acquiring builder's risk insurance for all construction projects after June 30, 2012; thus, builder's risk is no longer covered by the Risk Management Fund. For property coverage, the deductible for an individual state agency is the first \$25,000 of losses. The Risk Management Fund is responsible for property losses for the annual aggregate deductible of \$10 million for perils other than earthquakes and flood. Purchased insurance coverage is responsible for losses exceeding the \$10 million annual aggregate deductible. For earthquake and flood, there is a deductible of \$10 million per occurrence. The maximum insurance coverage is \$750 million per year for perils other than earthquake and flood. The maximum flood insurance coverage is \$50 million per occurrence, except there is only \$25 million of coverage in flood zones A and V. The maximum earthquake insurance coverage is \$50 million per occurrence. The amounts of settlements have not exceeded insurance coverage for each of the three past fiscal years.

The college participates in the Risk Management Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the college based on a percentage of the college's expected loss costs, which include both experience and exposures. This charge considers recent trends in actual claims experience of the state as a whole. An actuarial valuation is performed as of fiscal year-end to determine the fund liability and premium allocation. Information regarding the determination of the claims liabilities and the changes in the balances of the claims liabilities for the year ended June 30, 2013, is presented in the *Tennessee Comprehensive Annual Financial Report* (CAFR). The CAFR is available on the state's website at www.tn.gov/finance/act/cafr.shtml. Since the college participates in the Risk Management Fund, it is subject to the liability limitations under the provisions of the Tennessee Claims Commission Act, *Tennessee Code Annotated*, Section 9-8-101 et seq. Liability for negligence of the college for bodily injury and property damage is limited to \$300,000 per person and \$1,000,000 per occurrence. The limits of liability under workers' compensation are set forth in *Tennessee Code Annotated,* Section 50-6-101 et seq. Claims are paid through the state's Risk Management Fund. At June 30, 2013, the Risk Management Fund held \$108.5 million in cash designated for payment of claims. At June 30, 2012, the Risk Management Fund held \$97.2 million in cash designated for payment of claims.

At June 30, 2013, the scheduled coverage for the college was \$144,527,900 for buildings and \$25,627,200 for contents. At June 30, 2012, the scheduled coverage for the college was \$144,527,900 for buildings and \$25,405,900 for contents.

The state has also set aside assets in the Employee Group Insurance Fund, an internal service fund, to provide a program of health insurance coverage for the employees of the state, with the risk retained by the state. The college participates in the Employee Group Insurance Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the college based on estimates of the ultimate cost of claims, including the cost of claims that have been reported but not settled and of claims that have been incurred but not reported. Employees and providers have 13 months to file medical claims.

Note 12. Commitments and Contingencies

Sick Leave

The college records the cost of sick leave when paid. The dollar amount of unused sick leave was $8,100,961.77 at June 30, 2013, and $7,851,972.28 at June 30, 2012.

Operating Leases

The college has entered into various operating leases for buildings and equipment. Such leases will probably continue to be required. Expenses under operating leases for real property were $117,380.05 and expenses for personal property were $51,187.40 for the year ended June 30, 2013. The amounts for the year ended June 30, 2012, were $87,380.00 and $49,908.46. All operating leases are cancelable at the lessee's option.

Construction in Progress

At June 30, 2013, outstanding commitments under construction contracts totaled $5,011,692.75 for the Greeneville/Greene County Campus Expansion and Greeneville Campus Sewer Correction projects, of which $3,027,627.92 will be funded by future state capital outlay appropriations.

Note 13. Natural Classification With Functional Classifications

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

	Natural Classification					
Functional Classification	Salaries	Benefits	Other Operating	Scholarships	Depreciation	Total
Instruction	$13,964,765.38	$4,928,291.18	$ 3,273,541.41	$ 103,178.00	$ -	$22,269,775.97
Public service	1,285,567.54	554,385.80	1,615,723.55	152,077.00	-	3,607,753.89
Academic support	1,889,833.55	773,996.20	(374,897.15)	-	-	2,288,932.60
Student services	2,530,161.02	1,571,445.50	1,352,988.95	342,456.55	-	5,797,052.02
Institutional support	2,600,721.56	1,099,291.12	879,439.46	-	-	4,579,452.14
Maintenance & operation	1,675,185.03	850,762.15	4,728,633.66	-	-	7,254,580.84
Scholarships & fellowships	-	-	-	7,693,290.94	-	7,693,290.94
Auxiliary	-	-	29,305.82	-	-	29,305.82
Depreciation	-	-	-	-	2,605,016.61	2,605,016.61
Total	$23,946,234.08	$9,778,171.95	$11,504,735.70	$8,291,002.49	$2,605,016.61	$56,125,160.83

The college's operating expenses for the year ended June 30, 2012, are as follows:

Functional Classification	Natural Classification Salaries	Benefits	Other Operating	Scholarships	Depreciation	Total
Instruction	$14,061,354.24	$4,839,522.31	$ 3,492,959.65	$ 48,587.00	$ -	$22,442,423.20
Public service	1,322,656.46	601,313.50	1,982,132.67	147,158.00	-	4,053,260.63
Academic support	1,918,119.02	792,784.38	(321,394.86)	-	-	2,389,508.54
Student services	2,458,216.00	1,014,735.47	1,208,304.90	354,264.74	-	5,035,521.11
Institutional support	2,570,493.24	1,068,352.41	882,241.96	-	-	4,521,087.61
Maintenance & operation	1,711,874.30	881,749.47	3,127,414.11	-	-	5,721,037.88
Scholarships & fellowships	-	-	1,351.76	8,180,653.62	-	8,182,005.38
Auxiliary	-	-	29,451.91	-	-	29,451.91
Depreciation	-	-	-	-	4,210,258.07	4,210,258.07
Total	$24,042,713.26	$9,198,457.54	$10,402,462.10	$8,730,663.36	$4,210,258.07	$56,584,554.33

Expenses initially incurred by the academic support function as a result of providing internal services to the other functional classifications were allocated to the other functional areas by reducing the academic support function's operating expenses by the total amount of salaries, benefits, and operating expenses incurred in the provision of these services, and allocating this amount to the other functional areas' operating expenses on the basis of usage. As a result of this process, expenses totaling $1,759,306.56 for the year ended June 30, 2013, and $1,813,021.45 for the year ended June 30, 2012, were reallocated from academic support to the other functional areas and caused academic support operating expenses to appear as a negative amount in the schedule above.

Note 14. Prior-year Adjustment

A prior-period adjustment of $70,929.84 was necessary to correct three errors:

- Due to calculation errors, depreciation expense for equipment was understated by $68,654.63 during the 2008, 2009, 2010, and 2011 fiscal years.
- An adjustment of $8,231.40 was recorded to expense projects in progress incorrectly capitalized at June 30, 2011.
- Accrued salaries and benefits were overstated by $5,956.19 at June 30, 2011.

Note 15. On-behalf Payments

During the year ended June 30, 2013, the State of Tennessee made payments of $24,901.50 on behalf of the college for retirees participating in the Medicare Supplement Plan. The amount for the year ended June 30, 2012, was $24,858.44. The Medicare Supplement Plan is a postemployment benefit health care plan and is discussed further in Note 10. The plan is reported in the *Tennessee Comprehensive Annual Financial Report*. That report is available on the state's website at www.tn.gov/finance/act/cafr.shtml.

Note 16. Component Unit

The Walters State Community College Foundation is a legally separate, tax-exempt organization supporting Walters State Community College. The foundation acts primarily as a fund-raising organization to supplement the resources that are available to the college in support of its programs. The 151-member board of the foundation is self-perpetuating and consists of graduates and friends of the college. Although the college 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 college by the donors. Because these restricted resources held by the foundation can only be used by, or for the benefit of, the college, the foundation is considered a component unit of the college and is discretely presented in the college's financial statements.

During the year ended June 30, 2013, the foundation made distributions of $33,701.49 to or on behalf of the college for both restricted and unrestricted purposes. During the year ended June 30, 2012, the foundation made distributions of $256,980.36 to or on behalf of the college for both restricted and unrestricted purposes. Complete financial statements for the foundation can be obtained from Dr. Mark A. Hurst, Walters State Community College Foundation, P. O. Box 1508, Morristown, TN 37816-1508.

Cash and Cash Equivalents

In addition to demand deposits and petty cash on hand, this classification includes instruments that are readily convertible to known amounts of cash and that have original maturities of three months or less. At June 30, 2013, cash and cash equivalents consisted of $235,275.22 in bank accounts, $500.00 of petty cash on hand, $1,720,149.54 in the Local Government Investment Pool (LGIP) administered by the State Treasurer, and $1,567,026.95 in money market mutual funds. At June 30, 2012, cash and cash equivalents consisted of $213,305.33 in bank accounts, $500.00 of petty cash on hand, $1,767,565.53 in the LGIP, and $105,653.79 in money market mutual funds.

Deposits

At June 30, 2013, and June 30, 2012, the foundation's bank balances were $650,275.22 and $628,305.33, respectively. Of those amounts, $35,275.22 and $13,305.13 were uninsured and uncollateralized at June 30, 2013, and June 30, 2012, respectively.

The foundation also had deposits in the Local Government Investment Pool (LGIP) administered by the State Treasurer. The LGIP is part of the State Pooled Investment Fund. The fund's required risks disclosures are presented in the State of Tennessee Treasurer's Report. That report is available on the state's website at www.treasury.tn.gov.

Investments

The foundation is authorized to invest funds in accordance with its board of directors' policies. All investments permitted to be reported at fair value under GASB Statement 31, as amended, are reported at fair value, including those with a maturity date of one year or less at the time of purchase.

At June 30, 2013, the foundation had the following investments and maturities:

		Investment Maturities (in Years)				
Investment Type	Fair Value	Less than 1	1 to 5	6 to 10	More than 10	No Maturity Date
Corporate bonds	$ 129,190.25	$ 50,448.50	$ 78,741.75	$ -	$ -	$ -
Mutual funds-bonds	1,249,650.01	-	562,846.71	686,803.30	-	-
Money market funds	1,567,026.95	1,567,026.95	-	-	-	-
Corporate stocks	26,162.72	-	-	-	-	26,162.72
Mutual funds-equity	5,642,963.93	-	-	-	-	5,642,963.93
Certificates of deposit	415,000.00	-	-	-	-	415,000.00
Hedge fund	2,214,617.32	-	-	-	-	2,214,617.32
Private equity fund	800,000.00	-	-	-	-	800,000.00
Cash surrender value of life insurance	82,730.27	-	-	-	-	82,730.27
Total investments and cash equivalents	12,127,341.45	1,617,475.45	641,588.46	686,803.30	-	9,181,474.24
Less cash equivalents	1,567,026.95	1,567,026.95	-	-	-	-
Total investments	$10,560,314.50	$ 50,448.50	$641,588.46	$686,803.30	$ -	$9,181,474.24

At June 30, 2012, the foundation had the following investments and maturities:

		Investment Maturities (in Years)				
Investment Type	Fair Value	Less than 1	1 to 5	6 to 10	More than 10	No Maturity Date
Corporate bonds	$ 182,946.00	$ 50,348.00	$132,598.00	$ -	$ -	$ -
Mutual funds-bonds	1,140,447.27	-	58,186.56	1,082,260.71	-	-
Money market funds	105,653.79	105,653.79	-	-	-	-
Corporate stocks	26,336.56	-	-	-	-	26,336.56
Mutual funds-equity	5,945,143.64	-	-	-	-	5,945,143.64
Certificates of deposit	415,000.00	-	-	-	-	415,000.00
Hedge fund	2,069,119.00	-	-	-	-	2,069,119.00
Cash surrender value of life insurance	87,302.18	-	-	-	-	87,302.18
Total investments and cash equivalents	9,971,948.44	156,001.79	190,784.56	1,082,260.71	-	8,542,901.38
Less cash equivalents	105,653.79	105,653.79	-	-	-	-
Total investments	$9,866,294.65	$ 50,348.00	$190,784.56	$1,082,260.71	$ -	$8,542,901.38

<u>Interest rate risk</u> – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of a debt investment. The foundation does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair-value losses arising from increasing interest rates.

Credit risk – Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Securities are rated using Standard and Poor's, Moody's Investors Service, and/or Fitch Ratings and are presented below using the Standard and Poor's rating scale. The foundation has no investment policy limiting its investment choices based on ratings issued by nationally recognized statistical rating organizations.

At June 30, 2013, the foundation's investments were rated as follows:

		Credit Quality Rating	
Investment Type	Fair Value	BBB	Unrated
LGIP	$1,720,149.54	$ -	$1,720,149.54
Corporate bonds	129,190.25	129,190.25	-
Mutual funds-bonds	1,249,650.01	-	1,249,650.01
Money market funds	1,567,026.95	-	1,567,026.95
Total	$4,666,016.75	$129,190.25	$4,536,826.50

At June 30, 2012, the foundation's investments were rated as follows:

		Credit Quality Rating		
Investment Type	Fair Value	A	BBB	Unrated
LGIP	$1,767,565.53	$ -	$ -	$1,767,565.53
Corporate bonds	182,946.00	50,348.00	132,598.00	-
Mutual funds-bonds	1,140,447.27	-	-	1,140,447.27
Money market funds	105,653.79	-	-	105,653.79
Total	$3,196,612.59	$50,348.00	$132,598.00	$3,013,666.59

Custodial credit risk – For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the foundation will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The foundation does not have a policy for custodial credit risk. At June 30, 2013, the foundation had $129,190.25 of uninsured and unregistered investments for which the securities are held by the counterparty. At June 30, 2012, the foundation had $182,946.00 of uninsured and unregistered investments for which the securities are held by the counterparty.

Foreign currency risk – Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. The foundation places no limit on the amount it may invest in foreign currency.

At June 30, 2013, the foundation's exposure to foreign currency risk is as follows:

Investment	Currency	Maturity	Fair Value
Corporate bonds	Various	9/17/13	$50,448.50
Mutual funds-equity	Various	-	$9,959.16

At June 30, 2012, the foundation's exposure to foreign currency risk is as follows:

Investment	Currency	Maturity	Fair Value
Corporate bonds	Various	9/17/13	$51,470.50
Mutual funds-equity	Various	-	$9,121.54

Alternative Investments

The foundation has investments in a hedge fund and private equity fund at June 30, 2013. The foundation had an investment in the hedge fund at June 30, 2012. The estimated fair value of these assets is $3,014,617.32 at June 30, 2013, and $2,069,119.00 at June 30, 2012.

The hedge fund is a "fund of funds," a hedge fund which invests in other hedge funds. The private equity fund invests in class B, B+, and select class A multifamily communities in major secondary markets across the United States.

The foundation believes that the carrying amount of its alternative investments is a reasonable estimate of fair value as of June 30, 2013, and June 30, 2012. Because these investments are not readily marketable, the estimated value is subject to uncertainty and, therefore, may differ from the value that would have been used had a ready market for the investments existed, and such differences could be material. These investments are made in accordance with the foundation's investment policy. These investments are designed to enhance diversification and provide reductions in overall portfolio volatility. These fair values are estimated using various valuation techniques.

The fair values for the hedge fund of funds are estimated using an industry-recognized pricing service. At June 30, 2013, the hedge "fund of funds" fund was valued at the net asset value as determined by the portfolio manager. The fund issues audited financial statements on a calendar year basis. Using those audited fair values, valuations are adjusted mainly by Level 2 inputs as established in the fair value hierarchy by U.S. GAAP. Level 2 inputs are derived principally from observable market data by correlation or other means.

The fair value for the private equity fund investment is determined by the fund managers using various methodologies as applicable under Generally Accepted Accounting Principles. These valuations are audited on an annual basis by independent accounting firms engaged by the private equity fund managers.

Pledges Receivable

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

	June 30, 2013	June 30, 2012
Current pledges	$ 41,138.85	$ 65,557.91
Pledges due in one to five years	71,994.34	97,069.57
Subtotal	113,133.19	162,627.48
Less discount to net present value	(840.00)	(1,146.00)
Total pledges receivable, net	$112,293.19	$161,481.48

Capital Assets

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

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$ 26,700.00	$ 9,314.00	$ -	$ -	$ 36,014.00
Buildings	1,773,300.00	649,977.44	107,450.82	33,300.00	2,497,428.26
Projects in progress	107,450.82	-	(107,450.82)	-	-
Total	1,907,450.82	659,291.44	-	33,300.00	2,533,442.26
Less accumulated depreciation:					
Buildings	87,832.50	62,562.27	-	832.50	149,562.27
Total	87,832.50	62,562.27	-	832.50	149,562.27
Capital assets, net	$1,819,618.32	$596,729.17	$ -	$32,467.50	$2,383,879.99

Capital asset activity for the year ended June 30, 2012, was as follows:

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	$ -	$ 26,700.00	$ -	$ -	$ 26,700.00
Buildings	1,740,000.00	33,300.00	-	-	1,773,300.00
Projects in progress	-	107,450.82	-	-	107,450.82
Total	1,740,000.00	167,450.82	-	-	1,907,450.82
Less accumulated depreciation:					
Buildings	43,500.00	44,332.50	-	-	87,832.50
Total	43,500.00	44,332.50	-	-	87,832.50
Capital assets, net	$1,696,500.00	$123,118.32	$ -	$ -	$1,819,618.32

Long-term Liabilities

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

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Payables:					
Capital lease obligation	$1,125,000.00	$ -	$96,000.00	$1,029,000.00	$108,000.00
Subtotal	1,125,000.00	-	96,000.00	1,029,000.00	108,000.00
Other liabilities:					
Split interest trust	50,000.00	-	-	50,000.00	-
Subtotal	50,000.00	-	-	50,000.00	-
Total long-term liabilities	$1,175,000.00	$ -	$96,000.00	$1,079,000.00	$108,000.00

Long-term liabilities activity for the year ended June 30, 2012, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Payables:					
Capital lease obligation	$1,685,000.00	$ -	$560,000.00	$1,125,000.00	$96,000.00
Subtotal	1,685,000.00	-	560,000.00	1,125,000.00	96,000.00
Other liabilities:					
Split interest trust	-	50,000.00	-	50,000.00	-
Subtotal	-	50,000.00	-	50,000.00	-
Total long-term liabilities	$1,685,000.00	$50,000.00	$560,000.00	$1,175,000.00	$96,000.00

Capital Lease

The foundation has a capital lease agreement with the Claiborne County Industrial Development Board for the former Claiborne County High School Building. This agreement began in August 2010 and ends on the earlier of January 30, 2023, or upon the retirement of the indebtedness incurred by the Claiborne County Industrial Development Board to purchase and renovate the building. There is no imputed interest rate. The asset balance at June 30, 2013, was $2,347,865.99, net of accumulated depreciation of $149,562.27. The foundation is renting the space to Walters State Community College to serve as its Claiborne County campus. The following is a schedule by years of future minimum lease payments under the capital lease together with the present value of the net minimum lease payments at June 30, 2013:

Year Ending June 30	
2014	$ 108,000.00
2015	108,000.00
2016	108,000.00
2017	108,000.00
2018	108,000.00
2019 - 2023	489,000.00
Total minimum lease payments	1,029,000.00
Less amount representing interest	-
Present value of net minimum lease payments	$1,029,000.00

Endowments

If a donor has not provided specific instructions to the foundation, the foundation's policies and procedures permit the foundation to authorize for expenditure the net appreciation (realized and unrealized) of the investments of endowment funds. When administering its power to spend net appreciation, the foundation is required to consider its long-term and short-term needs; present and anticipated financial requirements; expected total return on its investments; price-level trends; and general economic conditions. Any net appreciation that is spent is required to be spent for the purposes for which the endowment was established.

The foundation chooses to spend only a portion of the investment income (including changes in the value of investments) each year. Under the spending plan established by the foundation, 4.5% of a rolling five-year average of the endowment market value has been authorized for expenditure. The remaining amount, if any, is retained to be used in future years when the amount computed using the spending plan exceeds the investment income. At June 30, 2013, net appreciation of $1,136,300.95 is available to be spent, of which $986,545.98 is included in restricted net position expendable for scholarships and fellowships; $59,640.38 is included in restricted net position expendable for other purposes; and $90,114.59 is included in unrestricted net position. At June 30, 2012, net appreciation of $836,062.02 is available to be spent, of which $700,781.50 is included in restricted net position expendable for scholarships and fellowships; $53,626.58 is included in restricted net position expendable for other purposes; and $81,653.94 is included in unrestricted net position.

Tennessee Board of Regents
Walters State Community College
Required Supplementary Information
OPEB Schedule of Funding Progress

Actuarial Valuation Date	Plan	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll [(b-a)/c)]
July 1, 2011	State Employee Group Plan	$ -	$5,978,000.00	$5,978,000.00	0%	$19,857,614.00	30.10%
July 1, 2010	State Employee Group Plan	$ -	$7,536,000.00	$7,536,000.00	0%	$14,807,428.00	50.89%
July 1, 2009	State Employee Group Plan	$ -	$8,408,000.00	$8,408,000.00	0%	$14,791,924.00	56.84%

The amount reported here for covered payroll relates to the fiscal year in which the valuations were performed.

Tennessee Board of Regents
WALTERS STATE COMMUNITY COLLEGE
Supplementary Information
Schedules of Cash Flows - Component Unit
For the Years Ended June 30, 2013, and June 30, 2012

	Year Ended June 30, 2013	Year Ended June 30, 2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Gifts and contributions	$ 268,652.42	$ 525,647.45
Payments to suppliers and vendors	(135,727.80)	(128,358.58)
Payments for scholarships and fellowships	(407,973.62)	(359,791.71)
Payments to Walters State Community College	(9,997.69)	(256,980.36)
Other receipts	163,949.95	194,562.83
Net cash used by operating activities	(121,096.74)	(24,920.37)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Private gifts for endowment purposes	772,010.65	287,239.46
Other noncapital financing receipts (payments)	(1,962.43)	3,444.60
Net cash provided by noncapital financing activities	770,048.22	290,684.06
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from sale of capital assets	1,000,000.00	-
Purchases of capital assets and construction	(74,214.00)	(60,000.00)
Principal paid on capital lease	(96,000.00)	(60,000.00)
Other capital and related financing payments	-	(250,000.00)
Net cash provided (used) by capital and related financing activities	829,786.00	(370,000.00)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments	1,669,042.91	2,414,294.68
Income on investments	280,830.76	250,832.98
Purchases of investments	(1,992,684.09)	(2,512,929.62)
Net cash provided by investing activities	(42,810.42)	152,198.04
Net increase in cash and cash equivalents	1,435,927.06	47,961.73
Cash and cash equivalents at beginning of year	2,087,024.65	2,039,062.92
Cash and cash equivalents at end of year	$ 3,522,951.71	$ 2,087,024.65
Reconciliation of operating loss to net cash used by operating activities:		
Operating loss	$ (251,338.56)	$ (150,277.00)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Change in assets and liabilities:		
Depreciation expense	62,562.27	44,332.50
Receivables, net	63,034.13	17,091.39
Prepaid expenses	(1,135.83)	4,763.18
Accounts payable	8,638.29	(20,830.44)
Unearned revenues	(2,857.04)	80,000.00
Net cash used by operating activities	$ (121,096.74)	$ (24,920.37)
Noncash investing, capital, or financing transactions		
Gifts of capital assets	$ 1,499,053.04	$ 575,708.22
Unrealized gains (losses) on investments	$ 286,937.52	$ (366,694.21)

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

The Honorable Bill Haslam, Governor
Members of the General Assembly
The Honorable John G. Morgan, Chancellor
Dr. Wade B. McCamey, President

We have audited the financial statements of Walters State Community College, an institution of the Tennessee Board of Regents, which is a component unit of the State of Tennessee, and its discretely presented component unit as of and for the years ended June 30, 2013, and June 30, 2012, and the related notes to the financial statements, which collectively comprise the college's basic financial statements, and have issued our report thereon dated July 17, 2014. We conducted our audit in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies, and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, we identified the following deficiency in internal control that we consider to be a material weakness:

- As reported in the previous three audits, management needs to improve financial statement preparation and review procedures to prevent errors in its financial statements.

This deficiency is described in the Finding and Recommendation section of this report.

Compliance and Other Matters

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

Walters State Community College's Response to Finding

The college's response to the finding identified in our audit is included in the Finding and Recommendation section of this report. The college's response was not subjected to the auditing procedures applied in the audit of the financial statements, and, accordingly, we express no opinion on it.

Purpose of This Report

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

Deborah V. Loveless

Deborah V. Loveless, CPA
Director
July 17, 2014

Finding and Recommendation

<u>As reported in the previous three audits, management needs to improve financial statement preparation and review procedures to prevent errors in its financial statements</u>

Finding

Walters State Community College's procedures for preparation of its financial statements, including the financial statements of its component unit, Walters State Community College Foundation, should be improved to ensure the accuracy and proper classification of information presented in its financial statements. Similar findings were reported in the previous three audits. The current weakness resulted in the following significant reporting errors:

The Vice President for College Advancement, who is responsible for the oversight of the day-to-day accounting for foundation transactions, misclassified certain transactions when entering them into the accounting system. These errors did not have an impact on total revenues, expenses, or net position, but affected certain line items on the financial statements as follows:

- On the foundation's 2013 statement of revenues, expenses, and changes in net position, the donation of a capital asset valued at $1,133,333 was misclassified as a capital gift rather than as an addition to permanent endowments. The donor had specified that the asset was to be sold and the proceeds used to create a permanent endowment. In addition, another $43,875 of additions to permanent endowments was misclassified as gifts and contributions. The audited statement was corrected.

- On the foundation's statement of net position at June 30, 2013, $1,486,000 of cash received as an addition to a nonexpendable endowment was misclassified as a current asset. (The cash was $1,000,000 from the sale of the capital asset described above plus an additional $486,000 in cash from the same donor.) The cash should have instead been classified as a noncurrent asset, since it could not be expended to meet current obligations due to donor restrictions. The audited statement was corrected.

- On the foundation's 2013 schedule of cash flows, net cash provided by capital and related financing activities was understated by $218,257.40, and net cash provided by investing activities was overstated by $218,257.40. The schedule in the audit report was corrected.

- On the foundation's 2013 and 2012 schedules of cash flows, included as supplementary information accompanying the college's 2013 and 2012 financial statements, unrealized gains on investments were misstated. For 2013, under noncash investing transactions, unrealized gains were reported at $935,527.40, rather than $286,937.52. For 2012, under noncash investing transactions, unrealized losses were reported at ($143,801.04), rather than ($366,694.21). The Vice President for College Advancement made errors in calculating each year's amount. The schedules in the audit report were corrected.

The component unit's statements are prepared by the college's Vice President for College Advancement using foundation information in the college's Banner accounting system. That information is entered and accounted for by foundation personnel, who are college employees.

Based on our discussions with the college's Vice President for College Advancement concerning the first three items, he had never encountered these situations and used his best judgment concerning how to account for these transactions. As for the last item, he misunderstood how to calculate unrealized gains on investments.

The results of our current audit of the financial statements have indicated that, despite overall improvement and management's assurances in prior audits, the controls over financial reporting for the foundation have not operated effectively.

Recommendation

The Vice President for Business Affairs should ensure that staff members accounting for foundation transactions and preparing and/or reviewing the foundation's financial statements have adequate knowledge of accounting and reporting requirements to properly perform their responsibilities. Foundation staff, including the college's Vice President for College Advancement, should seek the counsel of the college's accounting staff when new or unusual transactions occur. The Vice President for Business Affairs and the college's accounting staff should have a detailed understanding of the foundation's operations and accounting transactions to properly oversee the foundation's accounting and financial reporting functions. Capital assets donated to the college, which are to be used to establish an endowment, should be reported as additions to permanent endowments, rather than capital gifts. Cash and cash equivalents held in endowment funds should be classified as noncurrent because they will not be used in current operations. The foundation's schedules of cash flows should be properly prepared, with amounts properly classified. Under noncash investing transactions on those schedules, unrealized gains for the respective year should be accurately calculated.

Management's Comment

Management concurs with the finding. To address this finding, for the next two fiscal years, the foundation will contract with an external accounting firm to oversee preparation of its financial statements and the classification of its transactions. Taking this additional step of using outside expertise will ensure this problem does not reoccur. The college also plans to continue pursuing appropriate training for College Advancement/Foundation staff relative to foundation accounting transaction classifications.

Observations and Comments

College of Applied Technology

Walters State Community College serves as the lead institution under an agreement with the Tennessee College of Applied Technology at Morristown. Under this agreement, Walters State Community College performs the accounting and reporting functions for the college. The chief administrative officer of each college is the director, who is assisted and advised by members of the faculty and administrative staff. The director is responsible to the Chancellor of the Tennessee Board of Regents. Prior to July 1, 2013, these workforce training schools were named Tennessee Technology Centers.