

***West Virginia Network for  
Educational Telecomputing***

*Financial Statements and Additional Information  
For the Year Ended June 30, 2002 and  
Independent Auditors' Reports*

# WEST VIRGINIA NETWORK FOR EDUCATIONAL TELECOMPUTING

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West Virginia Network for Educational Telecomputing  
Management Discussion and Analysis  
Fiscal Year 2002

**Overview of the Financial Statements and Financial Analysis**

West Virginia Network for Educational Telecomputing (“WVNET”) is pleased to present its financial statements for Fiscal Year 2002. The emphasis of discussions about these statements will be on current year data. There are three financial statements presented: the Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; and, the Statement of Cash Flows. This discussion and analysis of WVNET’s financial statements provides an overview of our financial activities for the year and is required supplemental information.

The Governmental Accounting Standards Board (GASB) issued new directives for presentation of college and university financial statements. WVNET is part of the college and university system of the State of West Virginia. The previous reporting format presented financial balances and activities by fund groups. The new format places emphasis on the overall economic resources of WVNET. This is the first Fiscal Year for this new format. Comparative analysis will be presented in future years.

**Statement of Net Assets**

The Statement of Net Assets presents the assets, liabilities, and net assets of WVNET as of June 30, 2002. The purpose of the Statement of Net Assets is to present to the readers of the financial statements a fiscal snapshot of WVNET. The Statement of Net Assets presents end-of-year data for Assets (current and non-current), Liabilities (current and non-current), and Net Assets (Assets less Liabilities).

From the data presented, readers of the Statement of Net Assets are able to determine the assets available to continue the operations of WVNET. They are also able to determine how much the institution owes vendors and lending institutions.

Finally, the Statement of Net Assets provides a picture of the net assets and their availability for expenditure by WVNET.

Net assets are divided into three major categories. The first category, invested in capital assets, net of debt, reports the equity in property, plant, and equipment owned by WVNET. The next asset category, restricted assets, is divided into two categories – nonexpendable and expendable. As of June 30, 2002, none of WVNET’s net assets were considered restricted. The final category is unrestricted net assets. Unrestricted net assets are available to WVNET for any lawful purpose of WVNET.

Statement of Net Asset Information  
(In thousands of dollars)

June 30, 2002

Assets:	
Current assets	\$2,826
Capital assets, net	<u>2,682</u>
Total Assets	<u>5,508</u>
Liabilities	
Current liabilities	2,273
Non-current liabilities	<u>479</u>
Total Liabilities	<u>2,752</u>
Net Assets	
Invested in capital assets, net	2,508
Unrestricted	<u>248</u>
Total Net Assets	<u>\$2,756</u>

Major items of note in the Statement of Net Assets include:

Total current assets of \$2.8 million exceed current liabilities of \$2.3 million. The two major components of current assets are cash and cash equivalents totaling \$2.1 million and accounts receivable totaling \$0.7 million. The major component of current liabilities is normal accounts payable and accrued liabilities totaling \$1.7 million.

Noncurrent assets consist of \$2.7 million in net book value of equipment. Noncurrent liabilities total only \$0.5 million, primarily related to accruals for compensated absences.

Total net assets are \$2.75 million, of which \$2.5 million is invested in capital assets.

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

Changes in total net assets are based on the activity presented in the Statement of Revenues, Expenses, and Changes in Net Assets. The purpose of the statement is to present the revenues received by the institution, both operating and non-operating, and the expenses paid by WVNET, operating and non-operating, and any other revenues, expenses, gains, and losses received or spent by WVNET.

Operating revenues are received from providing goods and services to the various customers and constituencies of WVNET. 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 WVNET. Revenues received for which goods and services are not provided are reported as non-operating revenues. For example, state appropriations are non-operating because they are

provided by the West Virginia Legislature to WVNET without the Legislature directly receiving commensurate goods and services for those revenues.

**Statement of Revenues, Expenses, and Changes in Net Asset Information**  
**(In thousands of dollars)**

	For the Year Ended June 30, 2002
Operating revenues	\$5,962
Operating expenses	<u>9,918</u>
Operating loss	(3,956)
Non-operating revenues and expenses	<u>2,815</u>
Decrease in Net Assets	<u><u>\$(1,141)</u></u>

A review of individual revenue and expense categories that contribute to the overall change in Net Assets reveals the following:

Operating revenues totaled \$5.96 million. The major sources of operating revenue include \$3.5 million in collections from higher education institutions and \$2.3 million in collections from other entities for data and telecommunication services.

Operating expenses total \$9.9 million. Operating expenses include staff costs of \$3.4 million and \$1.1 million in depreciation expense. Approximately \$0.2 million was expensed for accrual of severance benefits that will result in a reduction of operating expenses in future years.

For the year ended June 30, 2002, there was a net operating loss of \$3.96 million. This loss reflects the reporting of state appropriations of \$2.74 million as nonoperating revenue, and the addition of \$1.1 million in depreciation expense on equipment primarily purchased in previous years.

For the year ended June 30, 2002, there was a decrease in net assets of \$1.1 million, which is reflective of the impact of depreciation expense for the year.

**Statement of Cash Flows**

The final statement presented by WVNET is the Statement of Cash Flows. The Statement of Cash Flows presents detailed information about the cash activity of WVNET during the year. The statement is divided into five parts. The first part deals with operating cash flows and shows the net cash used by the operating activities of WVNET. The second section reflects cash flows from non-capital financing activities. The section reflects the cash received and spent for non-operating, non-investing, and non-capital financing purposes. The third section reflects the cash flows from investing activities and shows the purchases, proceeds, and interest received from investing activities. The fourth section presents cash flows from capital and related financing

activities. This section presents the cash used for the acquisition and construction of capital and related items. The fifth section reconciles the net cash used to the operating income or loss reflected on the Statement of Revenues, Expenses, and Changes in Net Assets. GASB 35 does not require restatement of prior year cash flows in the implementation year.

Statement of Cash Flows Information  
(In thousands of dollars)  
For the year ended June 30, 2002

Cash flows provided (used) by:	
Operating activities	(\$1,656)
Non-operating activities	2,737
Capital and related financing activities	( 721)
Investing activities	<u>92</u>
Net Change in Cash and cash equivalents	452
Cash and cash equivalents– beginning of year	1,654
Cash and cash equivalents– end of year	<u>\$2,106</u>

Although there was a decrease in net assets for the year of \$1.4 million, actual cash and cash equivalents actually increased by \$0.45 million during Fiscal Year 2002. This increase in cash reflects the non-cash nature of depreciation expense, as well as an increase in current accounts payable.

**Capital Asset and Debt Administration**

WVNET added no buildings or major equipment purchases during Fiscal Year 2002, and the only debt obligations relate to \$0.17 million in capital lease obligations as described in Note 8.

**Economic Outlook and Other Factors Impacting WVNET**

The mission of WVNET is to provide telecommunications and computing services within West Virginia, primarily focused upon services for the state public colleges and universities. As such, the operations of WVNET are dependent upon the ability of the higher education institutions and the State of West Virginia to continue to fund these activities. For Fiscal Year 2003 the general revenue funding for virtually all state agencies was reduced by 3%. For Fiscal Year 2004, all state agencies are being requested to submit a general revenue budget with a 10% budget reduction. The strategies for implementing the budget reductions for Fiscal Year 2004 are currently in the process of being evaluated. The economic outlook for the State of West Virginia has in the past and may continue to pose significant challenges. Because of this dynamic environment, WVNET will need to continue its recent positive track record of adjustments to the mix of its products and services in order to maintain its financial viability.

## INDEPENDENT AUDITORS' REPORT

To the West Virginia Higher Education Policy Commission

We have audited the accompanying financial statements of the West Virginia Network for Educational Telecomputing ("WVNET") as of June 30, 2002, and for the year then ended, listed in the foregoing Table of Contents. These financial statements are the responsibility of the management of WVNET. Our responsibility is to express an opinion 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of WVNET at June 30, 2002, and the changes in net assets and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 2 to the financial statements, WVNET changed its financial statement presentation to adopt the provisions of the Governmental Accounting Standards Board ("GASB") Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*, as amended by GASB Statements No. 37, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus*, and No. 38, *Certain Financial Statement Note Disclosures*, as of July 1, 2001.

The Management's Discussion and Analysis on pages 1 to 4 is not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of WVNET's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 11, 2002, on our consideration of WVNET's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

October 11, 2002

# WEST VIRGINIA NETWORK FOR EDUCATIONAL TELECOMPUTING

## STATEMENT OF NET ASSETS JUNE 30, 2002

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### ASSETS:

#### Current assets:

Cash and cash equivalents	\$ 2,106,216
Accounts receivable	706,478
Interest receivable	12,508
Prepaid expenses	<u>923</u>

Total current assets 2,826,125

#### Noncurrent assets:

Investment in capital assets, net	<u>2,681,794</u>
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TOTAL ASSETS \$ 5,507,919

### LIABILITIES:

#### Current liabilities:

Accounts payable and accrued liabilities	\$ 1,693,798
Accrued severance benefits	87,868
Compensated absences	253,300
Deferred revenue	168,066
Capital lease obligation	<u>70,316</u>

Total current liabilities 2,273,348

#### Noncurrent liabilities:

Accrued severance benefits	93,001
Compensated absences	282,350
Capital lease obligation	<u>103,283</u>

Total noncurrent liabilities 478,634

TOTAL LIABILITIES 2,751,982

### NET ASSETS:

Invested in capital assets, net of related debt	2,507,484
Unrestricted	<u>248,453</u>

Total net assets 2,755,937

TOTAL LIABILITIES AND NET ASSETS \$ 5,507,919

See notes to financial statements.

# WEST VIRGINIA NETWORK FOR EDUCATIONAL TELECOMPUTING

## STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS YEAR ENDED JUNE 30, 2002

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### OPERATING REVENUES:

Institutional collections	\$ 3,473,103
Contracts and grants:	
State	41,700
Local	76,298
Sales and services of educational activities	2,251,922
Miscellaneous - net	<u>119,098</u>
 Total operating revenues	 <u>5,962,121</u>

### OPERATING EXPENSES:

Salaries and wages	2,807,249
Benefits	619,953
Supplies and other services	5,102,993
Utilities	112,018
Depreciation	1,095,557
Severance benefit	<u>180,869</u>
 Total operating expenses	 <u>9,918,639</u>

OPERATING LOSS (3,956,518)

### NONOPERATING REVENUES (EXPENSES):

State appropriations	2,736,911
Investment income	98,737
Interest on indebtedness	<u>(20,804)</u>
 Net nonoperating revenues	 <u>2,814,844</u>

DECREASE IN NET ASSETS (1,141,674)

NET ASSETS - BEGINNING OF YEAR (AS RESTATED) 3,897,611

NET ASSETS - END OF YEAR \$ 2,755,937

See notes to financial statements.

# WEST VIRGINIA NETWORK FOR EDUCATIONAL TELECOMPUTING

## STATEMENT OF CASH FLOWS YEAR ENDED JUNE 30, 2002

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CASH FLOWS FROM OPERATING ACTIVITIES:	
Institutional collections	\$ 3,108,216
Contracts and grants	351,626
Payments to and on behalf of employees	(3,176,855)
Payments to suppliers	(4,119,419)
Payments to utilities	(112,018)
Sales and service of educational activities	2,500,289
Other payments - net	<u>(207,951)</u>
Net cash used in operating activities	<u>(1,656,112)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:	
State appropriations	<u>2,736,911</u>
CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES:	
Purchases of capital assets	(46,581)
Principal paid on leases	(650,789)
Interest paid on leases	<u>(23,981)</u>
Net cash used in capital financing activities	<u>(721,351)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:	
Interest on investments	<u>92,480</u>
INCREASE IN CASH AND CASH EQUIVALENTS	451,928
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	<u>1,654,288</u>
CASH AND CASH EQUIVALENTS - END OF YEAR	<u>\$ 2,106,216</u>

(Continued)

## WEST VIRGINIA NETWORK FOR EDUCATIONAL TELECOMPUTING

### STATEMENT OF CASH FLOWS YEAR ENDED JUNE 30, 2002

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#### RECONCILIATION OF NET OPERATING LOSS TO NET CASH USED IN OPERATING ACTIVITIES

Operating loss	\$ (3,956,518)
Adjustments to reconcile net loss to net cash used in operating activities:	
Depreciation expense	1,095,557
Changes in assets and liabilities:	
Accounts receivable	(24,314)
Prepaid expenses	223,056
Accounts payable	807,110
Accrued liabilities	180,869
Compensated absences	34,982
Deferred revenue	<u>(16,854)</u>
NET CASH USED IN OPERATING ACTIVITIES	<u>\$ (1,656,112)</u>
Noncash transactions:	
Equipment purchased on capital lease	<u>\$ 107,712</u>
See notes to financial statements.	(Concluded)

# WEST VIRGINIA NETWORK FOR EDUCATIONAL TELECOMPUTING

## NOTES TO FINANCIAL STATEMENTS YEAR ENDED JUNE 30, 2002

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### 1. ORGANIZATION

West Virginia Network for Educational Telecommuting (“WVNET”) was created in 1975 to provide central computing facilities and wide-area network communications services as a resource for the public college and universities in the state of West Virginia. With the passage of Senate Bill 653, effective July 1, 2000, the governance of WVNET was assigned to the newly created West Virginia Higher Education Policy Commission (the “Commission”). The Commission is responsible for developing, gaining consensus around, and overseeing the implementation and development of a higher education public policy agenda. Prior to the creation of the Commission, WVNET was jointly governed by the Board of Governors of the State College System and the Board of Trustees of the University System.

WVNET is also advised by a WVNET Policy Board, which provides a forum for guidance on problem resolution, planning, and policy issues.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of WVNET have been prepared in accordance with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (“GASB”), including Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*, and Statement No. 35, *Basic Financial Statements and Management’s Discussion and Analysis of Public Colleges and Universities* (an Amendment of GASB Statement No. 34). The financial statement presentation required by GASB Statements No. 34 and No. 35 provides a comprehensive, entity-wide perspective of WVNET’s assets, liabilities, net assets, revenues, expenses, changes in net assets and cash flows and replaces the fund-group perspective previously required.

WVNET follows all GASB pronouncements as well as Financial Accounting Standards Board (“FASB”) Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins issued on or before November 30, 1989, and has elected not to apply the FASB Statements and Interpretations issued after November 30, 1989, to its financial statements.

**Reporting Entity**—WVNET is an operating unit of the West Virginia Higher Education Fund and represents separate funds of the State that are not included in the State’s general fund. WVNET is a separate entity which, along with all State institutions of higher education and the Commission, form the Higher Education Fund of the State. The Higher Education Fund is considered a component unit of the State, and its financial statements are discretely presented in the State’s comprehensive annual financial report.

The accompanying financial statements present all funds under the authority of WVNET. The basic criteria for inclusion in the accompanying financial statements is the exercise of oversight responsibility derived from WVNET’s ability to significantly influence operations and accountability for fiscal matters of related entities.

**Description of Business**—WVNET was founded in 1975 to serve West Virginia’s State System of higher education by providing central computing and telecommunication facilities linking the State system of colleges and universities. WVNET’s communications systems provide access to a number of other state networks and systems.

**Financial Statement Presentation**—During fiscal 2002, WVNET adopted GASB Statement No. 35, *Basic Financial Statements—and Management’s Discussion and Analysis –for Public Colleges and Universities*, as amended by GASB Statements No. 37, *Basic Financial Statements and Management’s Discussion and Analysis for State and Local Governments: Omnibus*, and No. 38, *Certain Financial Statement Note Disclosures*. These statements establish standards for external financial reporting for public colleges and universities and require that financial statements be presented on a combined basis to focus on WVNET as a whole. Previously, financial statements focused on the accountability of individual fund groups rather than on WVNET as a whole. GASB Statement No. 35 reports equity as “net assets” rather than “fund balance”. Net assets are classified into four categories according to external donor restrictions or availability of assets for satisfaction of College obligations. WVNET’s net assets are classified as follows:

- *Invested in capital assets, net of related debt*—This represents WVNET’s total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of invested in capital assets, net of related debt.
- *Restricted net assets, expendable*—This includes resources in which WVNET is legally or contractually obligated to spend resources in accordance with restrictions imposed by external third parties. WVNET does not have any restricted expendable net assets at June 30, 2002.
- *Restricted net assets, nonexpendable*—This includes 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 either be expended or added to principal. WVNET does not have any restricted nonexpendable assets at June 30, 2002.
- *Unrestricted net assets*—Unrestricted net assets represent resources derived from institutional collections, state appropriations and sales and services of educational activities. These resources are used for transactions relating to the educational and general operations of WVNET, and may be used at the discretion of the Board of Governors to meet current expenses for any purpose.

GASB Statement No. 35 requires the statements of net assets, revenues, expenses, and changes in net assets, and cash flows to be reported on an entity wide basis. The provisions of GASB Statement No. 35 have been applied to the year presented. Following is a reconciliation of total June 30, 2001 fund balances, as previously reported, to the restated net asset balances for the same date:

	<b>June 30, 2001</b>
Combined fund balances, as previously reported	\$ 11,857,011
Accumulated depreciation	(7,859,438)
Reclassification of grant and contract revenue	<u>(99,962)</u>
Combined fund balances, restated as net assets	<u><u>\$ 3,897,611</u></u>

***Basis of Accounting***—For financial reporting purposes, WVNET is considered a special-purpose government engaged only in business-type activities. Accordingly, WVNET’s financial statements have been prepared on the accrual basis of accounting with a flow of economic resources measurement focus. Revenues are reported when earned and expenditures when materials or services are received. All intercompany accounts and transactions have been eliminated.

***Cash and Cash Equivalents***—For purposes of the statement of net assets, WVNET considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

Cash and cash equivalents balances on deposit with the State of West Virginia Treasurer’s Office (the “State Treasurer”) are pooled by the State Treasurer with other available funds of the State for investment purposes by the West Virginia Investment Management Board (the “IMB”). These funds are transferred to the IMB and the IMB is directed by the State Treasurer to invest the funds in specific external investment pools. Balances in the investment pools are recorded at fair value, which is determined by a third-party pricing service based on asset portfolio pricing models and other sources, in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments for External Investment Pools*. The IMB was established by the West Virginia State Legislature and is subject to oversight by the West Virginia State Legislature. Fair value and investment income are allocated to participants in the pools based upon the funds that have been invested. The amounts on deposit with the State Treasurer are available for immediate withdrawal and, accordingly, are presented as cash and cash equivalents in the accompanying financial statements.

***Allowance for Doubtful Accounts***—It is WVNET’s policy to provide for future losses on uncollectible accounts, contracts and grants receivable based on an evaluation of the underlying account, contract and grant balances, the historical collectibility experienced by WVNET on such balances and such other factors which, in WVNET’s judgment, require consideration in estimating doubtful accounts. At June 30, 2002, no allowance was necessary.

***Capital Assets***—Capital assets includes primarily equipment. Capital assets are stated at cost at the date of acquisition, or fair market value at the date of donation in the case of gifts. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 3 to 10 years for equipment. Ownership of capital leased assets is transferred to WVNET at the end of the lease term.

***Deferred Revenue***—Revenues for services and activities to be conducted primarily in the next fiscal year are classified as deferred revenue and include internet access subscription fees and contract and grant monies.

***Compensated Absences***—WVNET accounts for compensated absences in accordance with the provisions of GASB Statement No. 16, *Accounting for Compensated Absences*. This statement requires entities to accrue for employees’ rights to receive compensation for vacation leave, or payments in lieu of accrued vacation or sick leave, as such benefits are earned and payment becomes probable.

WVNET's full-time employees earn up to two vacation leave days for each month of service and are entitled to compensation for accumulated, unpaid vacation leave upon termination. Full-time employees also earn 1-1/2 sick leave days for each month of service and are entitled to extend their health or life insurance coverage upon retirement in lieu of accumulated, unpaid sick leave. Generally, two days of accrued sick leave extend health insurance for one month of single coverage and three days extend health insurance for one month of family coverage. For employees hired after 1988, the employee shares in the cost of the extended benefit coverage to the extent of 50% of the premium required for the extended coverage. Employees hired July 1, 2001 or later will no longer receive sick leave credit toward insurance premiums when they retire.

The estimate of the liability for the extended health or life insurance benefit has been calculated using the vesting method in accordance with the provisions of GASB Statement No. 16. Under that method, WVNET has identified the accrued sick leave benefit earned to date by each employee, determined the cost of that benefit by reference to the benefit provisions and the current cost experienced by WVNET for such coverage, and estimated the probability of the payment of that benefit to employees upon retirement.

The estimated expense and expense incurred for the vacation leave, sick leave or extended health or life insurance benefits are recorded as a component of benefits expense on the statement of revenues, expenses and changes in net assets.

**Risk Management**—The State's Board of Risk and Insurance Management ("BRIM") provides general, property and casualty, and medical malpractice liability coverage to WVNET and its employees. Such coverage may be provided to WVNET by BRIM through self-insurance programs maintained by BRIM or policies underwritten by BRIM that may involve experience-related premiums or adjustments to BRIM.

BRIM engages an independent actuary to assist in the determination of its premiums so as to minimize the likelihood of premium adjustments to WVNET or other participants in BRIM's insurance programs. As a result, management does not expect significant differences between the premiums WVNET is currently charged by BRIM and the ultimate cost of that insurance based on WVNET's actual loss experience. In the event such differences arise between estimated premiums currently charged by BRIM to WVNET and WVNET's ultimate actual loss experience, the difference will be recorded, as the change in estimate becomes known.

**Classification of Revenues**—WVNET has classified its revenues as either operating or non-operating revenues according to the following criteria:

- *Operating revenues*—Operating revenues include activities that have the characteristics of exchange transactions, such as (1) institutional collections, (2) most state, local, and nongovernmental grants and contracts, and (3) sales and services of educational activities.
- *Nonoperating revenues*—Nonoperating revenues include activities that have the characteristics of non-exchange transactions, such as gifts and contributions, and other revenues that are defined as nonoperating revenues by GASB No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting* and GASB No. 34, such as state appropriations and investment income.

**Use of Restricted Net Assets**—WVNET has not adopted a formal policy regarding whether to first apply restricted or unrestricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available. Generally, WVNET attempts to utilize restricted net assets first when practicable.

**Institutional Collections**—Institutional collections represent revenues earned from colleges and universities throughout the State for the use of central site computing services which are provided by WVNET.

**Government Grants and Contracts**—Government grants and contracts normally provide for the recovery of direct and indirect costs, subject to audit. WVNET recognizes revenue associated with direct costs as the related costs are incurred. Recovery of related indirect costs is generally recorded at fixed rates negotiated for a period of one to three years.

**Income Taxes**—WVNET is exempt from income taxes, except for unrelated business income, as a nonprofit organization under federal income tax laws and regulations of the Internal Revenue Service.

**Cash Flows**—Any cash and cash equivalents escrowed, restricted for noncurrent assets or in funded reserves have not been included as cash and cash equivalents for the purpose of the statement of cash flows.

**Use of Estimates**—The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

**Recent Statements Issued by the Government Accounting Standards Board**—The GASB issued Statement No. 39, *Determining Whether Certain Organizations are Component Units*, an amendment of GASB Statement No. 14. This statement is effective for periods beginning after June 15, 2003. WVNET has not completed the process of evaluating the impact, if any, that will result from adopting GASB Statement No. 39. This statement, when adopted, could result in additional entities being included in WVNET's financial statements.

### 3. CASH AND CASH EQUIVALENTS

The composition of cash and cash equivalents was as follows at June 30, 2002:

Cash on deposit with the State Treasurer	<u>\$ 2,106,216</u>
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No cash held by the State Treasurer is restricted for any purpose. Cash on deposit with the State Treasurer is a noncategorized deposit in accordance with GASB Statement No. 3, *Deposits with Financial Institutions, Investments (Including Receivable Agreements), and Reverse Repurchase Agreements*.

**4. ACCOUNTS RECEIVABLE**

Accounts receivable were as follows at June 30, 2002:

Institutional collections	\$ 504,542
Due from other State agencies	182,388
Other	<u>19,548</u>
	<u>\$ 706,478</u>

**5. ACCOUNTS PAYABLE**

Accounts payable were comprised of the following at June 30, 2002:

Institutional - State of West Virginia	\$ 318,505
Other	<u>1,375,293</u>
	<u>\$1,693,798</u>

**6. CAPITAL ASSETS**

The following is a summation of capital assets transactions for WVNET for the year ended June 30, 2002:

	Beginning Balance	Additions	Reductions	Other	Ending Balance
Capital assets:					
Equipment	\$ 9,033,363	\$ 46,581	\$ (88,235)	\$ 2,102,710	\$ 11,094,419
Leased equipment	<u>2,449,133</u>	<u>107,712</u>	<u>          </u>	<u>(2,102,710)</u>	<u>454,135</u>
Total capital assets	11,482,496	154,293	(88,235)	-	11,548,554
Less accumulated depreciation for:					
Equipment	5,977,484	770,183	(88,235)	2,102,710	8,762,142
Leased equipment	<u>1,881,954</u>	<u>325,374</u>	<u>          </u>	<u>(2,102,710)</u>	<u>104,618</u>
Total accumulated depreciation	<u>7,859,438</u>	<u>1,095,557</u>	<u>(88,235)</u>	<u>          </u>	<u>8,866,760</u>
Capital assets, net	<u>\$ 3,623,058</u>	<u>\$ (941,264)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,681,794</u>

WVNET has no capital assets that are not being depreciated. Amounts included in "Other" represent equipment with lease terms that expired during the year and title transferred to WVNET.

## 7. CHANGES IN LONG-TERM LIABILITIES

The following is a summary of long-term obligation transactions for WVNET for the year ended June 30, 2002:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Capital lease obligations	\$ 716,676	\$ 107,712	\$ 650,789	\$ 173,599	\$ 70,316
Other long-term liabilities:					
Accrued severance benefits		180,869		180,869	87,868
Compensated absences	<u>500,668</u>	<u>34,982</u>	<u>          </u>	<u>535,650</u>	<u>253,300</u>
Total long-term liabilities	<u>\$ 1,217,344</u>	<u>\$ 323,563</u>	<u>\$ 650,789</u>	<u>\$ 890,118</u>	<u>\$ 411,484</u>

Additional information regarding lease obligations is included in Note 8.

## 8. CAPITAL LEASES

Capital lease obligations consisted of the following at June 30, 2002:

	Interest Rate	Principal Amount Outstanding
Environmental Managers, due in varying principal amounts through October 4, 2002	5.76 %	\$ 19,919
CISCO, due in varying principal amounts through August 5, 2002	5.41 %	10,085
SP Upgrade, due in varying principal amounts through May 7, 2005	3.97 %	102,064
Xerox Copier Equipment, due in varying principal amounts through June 11, 2006	12.5 %	<u>41,531</u>
		<u>\$ 173,599</u>

The obligations above represent financing for office and communication equipment as well as research and education equipment.

A summary of the annual aggregate principal payments for capital leases for years subsequent to June 30, 2002 is as follows:

<b>Year Ending June 30</b>	<b>Principal</b>	<b>Interest</b>	<b>Total</b>
2003	\$ 70,316	\$ 8,895	\$ 79,211
2004	45,667	5,724	51,391
2005	45,224	2,988	48,212
2006	12,392	855	<u>13,247</u>
			192,061
Less interest			<u>18,462</u>
			<u><u>\$ 173,599</u></u>

## **9. COMPENSATED ABSENCES LIABILITY**

The composition of the compensated absences liability was as follows at June 30, 2002:

Health or life insurance benefits	\$ 202,953
Accrued vacation leave	323,877
Current retirees health insurance	<u>8,820</u>
	<u><u>\$ 535,650</u></u>

The cost of health and life insurance benefits paid by WVNET is based on a combination of years of service and age. For the year ended June 30, 2002, the amount paid by WVNET for extended health or life insurance coverage retirement benefits totaled approximately \$1,807. As of June 30, 2002, there was one retiree currently eligible for these benefits.

## **10. RETIREMENT PLANS**

Substantially all full-time employees of WVNET participate in either the West Virginia Teachers' Retirement System (the "STRS") or the Teachers' Insurance and Annuities Association - College Retirement Equities Fund (the "TIAA-CREF"). Effective July 1, 1991, the STRS was closed to new participants. Current participants in the STRS are permitted to make a one-time election to cease their participation in that plan and commence contributions to the West Virginia Teachers' Defined Contribution Plan. Contributions to and participation in the West Virginia Teachers' Defined Contribution Plan by WVNET employees have not been significant to date.

The STRS is a cost sharing, defined benefit public employee retirement system. Employer and employee contribution rates are established annually by the West Virginia State Legislature. WVNET accrued and paid its contribution to the STRS at the rate of 15% of each enrolled employee's total annual salary for the year ended June 30, 2002. Required employee contributions were at the rate of 6% of total annual salary for the year ended June 30, 2002. Participants in the STRS may retire with full benefits upon reaching age 60 with five years of service, age 55 with 30 years of service, or any age with 35 years of service. Lump-sum withdrawal of employee contributions is available upon termination of employment. Pension benefits are based upon 2% of final average salary (the highest five years' salaries out of the last 15 years) multiplied by the number of years of service.

The TIAA-CREF is a defined contribution benefit plan in which benefits are based solely upon amounts contributed plus investment earnings. Employees who elect to participate in this plan are required to make a contribution equal to 6% of total annual compensation. WVNET matches the employees' 6% contribution. Contributions are immediately and fully vested.

Total contributions to the STRS for the years ended June 30, 2002, 2001 and 2000, were \$25,890, \$25,158 and \$23,136, respectively, which consisted of \$18,493, \$17,970 and \$16,526 from WVNET in 2002, 2001 and 2000, respectively, and \$7,397, \$7,188 and \$6,610 from the covered employees in 2002, 2001 and 2000, respectively.

The contribution rate is set by the West Virginia State Legislature on an overall basis, and the STRS does not perform a calculation of the contribution requirement for individual employers, such as WVNET. Historical trend and net pension obligation information is available from the annual financial report of the Consolidated Public Retirement Board, Building 5, Room 1000, Charleston, WV 25305.

Total contributions to the TIAA-CREF for the years ended June 30, 2002, 2001 and 2000, were \$320,868, \$337,576 and \$308,210, respectively, which consisted of contributions of \$160,434, \$168,788 and \$154,105 from WVNET and \$160,434, \$168,788 and \$154,105 from the covered employees in 2002, 2001 and 2000, respectively.

WVNET's total payroll for the year ended June 30, 2002 was \$2,798,084; total covered employees' salaries in the TIAA-CREF and STRS were \$2,674,797 and \$123,287, respectively, in 2002.

From June 1, 2002 to June 30, 2002, WVNET offered a staff severance benefit plan to certain eligible employees. Four employees were accepted under the plan and will receive severance benefits over a 24 month period commencing August 1, 2002. WVNET recorded the present value of the benefits for these employees amounting to \$180,869 during the year ended June 30, 2002.

## **11. CONTINGENCIES**

The nature of the educational industry is such that, from time-to-time, claims will be presented against WVNET on account of alleged negligence, acts of discrimination, breach of contract or disagreements arising from the interpretation of laws or regulations. While some of these claims may be for substantial amounts, they are not unusual in the ordinary course of providing educational services in a higher education system.

In the opinion of management, all known claims are covered by insurance or are such that an award against WVNET would not seriously impact the financial status of the institution.

Under the terms of federal grants, periodic audits are required and certain costs may be questioned as not being appropriate expenditures under the terms of the grants. Such audits could lead to reimbursement to the grantor agencies. WVNET's management believes disallowances, if any, will not have a significant financial impact on WVNET's financial position.

WVNET occupies a building which is known to contain asbestos. WVNET is not required by Federal, State or Local Law to remove the asbestos from the building. WVNET is required by Federal Environmental, Health and Safety Regulations to manage the presence of asbestos in the building in a safe condition. WVNET addresses its responsibility to manage the presence of asbestos in the building. Significant problems of dangerous asbestos conditions are abated as the condition becomes known. WVNET also addresses the presence of asbestos as building renovation or demolition projects are undertaken and through asbestos operation and maintenance programs directed at containing, managing or operating with the asbestos in a safe condition.

## **12. REIMBURSED EXPENDITURES**

WVNET acts as purchasing agent for the public higher education institutions of West Virginia and other state agencies to obtain bulk-pricing discounts for maintenance and equipment purchases. In addition, WVNET provides purchasing services regarding computer equipment purchases. In fiscal year 2002 \$3,891,271 was reimbursed by the schools and other state agencies to WVNET. WVNET treats these items as reimbursed expenditures so as to not distort total revenues and expenditures.

## **13. RELATED PARTY TRANSACTION**

The primary operations of WVNET are conducted at property located on Chestnut Ridge Road in Morgantown. This property is owned or titled by other units of the West Virginia Higher Education Fund and WVNET is not charged any rent for the use of the property. WVNET is responsible for all physical plant services, utilities, renovations, insurance, and other operating costs for this property. These operating costs are recorded in WVNET's Statement of Revenues, Expenses, and Changes in Net Assets.

**14. NATURAL CLASSIFICATIONS WITH FUNCTIONAL CLASSIFICATIONS**

For the year ended June 30, 2002, the following table represents operating expenses within both natural and functional classifications:

	<b>Salaries and Wages</b>	<b>Benefits</b>	<b>Supplies and Other Services</b>	<b>Utilities</b>	<b>Depreciation</b>	<b>Severance Benefit</b>	<b>Total</b>
General institutional support	\$2,587,701	\$ 567,469	\$ 5,059,034	\$ -	\$ -	\$ 180,869	\$8,395,073
Administration	219,548	52,484					272,032
Operations and maintenance of plant			43,959	112,018			155,977
Depreciation					<u>1,095,557</u>		<u>1,095,557</u>
Total	<u>\$2,807,249</u>	<u>\$ 619,953</u>	<u>\$ 5,102,993</u>	<u>\$ 112,018</u>	<u>\$1,095,557</u>	<u>\$ 180,869</u>	<u>\$9,918,639</u>

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**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the West Virginia Higher Education Policy Commission

We have audited the financial statements of West Virginia Network for Educational Telecomputing ("WVNET") as of and for the year ended June 30, 2002, and have issued our report thereon dated October 11, 2002, which contains a paragraph addressing its financial statement presentation to adopt the provisions of Governmental Accounting Standards Board Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*. 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.

**Compliance**

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

**Internal Control Over Financial Reporting**

In planning and performing our audit, we considered WVNET's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to the management of WVNET in a separate letter dated October 11, 2002.

This report is intended solely for the information and use of the Policy Commission, management of WVNET, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

October 11, 2002