

***West Virginia Higher  
Education Policy  
Commission***

*Financial Statements and  
Additional Information for the  
Year Ended June 30, 2004  
and Independent Auditors' Reports*

# WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

## TABLE OF CONTENTS

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	<b>Page</b>
INDEPENDENT AUDITORS' REPORT	1-2
MANAGEMENT'S DISCUSSION AND ANALYSIS (RSI)	3-10
FINANCIAL STATEMENTS FOR THE YEAR ENDED JUNE 30, 2004:	
Statement of Net Assets	11-12
Statement of Revenues, Expenses and Changes in Net Assets (Deficit)	13-14
Statement of Cash Flows	15-16
Notes to Financial Statements	17-29
ADDITIONAL INFORMATION FOR THE YEAR ENDED JUNE 30, 2004:	30
Combining Schedule—Statement of Net Assets Information	31-32
Combining Schedule—Statement of Revenues, Expenses and Changes in Net Assets (Deficit) Information	33-34
INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND COMPLIANCE AND OTHER MATTERS BASED UPON THE AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH <i>GOVERNMENT AUDITING STANDARDS</i>	35-36
SCHEDULE OF FINDINGS AND RESPONSES	37
STATUS OF PRIOR YEAR FINDINGS	38

## INDEPENDENT AUDITORS' REPORT

West Virginia Higher Education  
Policy Commission

We have audited the accompanying financial statements of the West Virginia Higher Education Policy Commission (the "Commission") as of June 30, 2004, and for the year then ended, listed in the foregoing Table of Contents. These financial statements are the responsibility of the management of the Commission. 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 the Commission at June 30, 2004 and the changes in net assets (deficit) 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 1 to the financial statements, the Commission's financial statements include West Virginia Network for Educational Telecommuting.

The Management's Discussion and Analysis on pages 3 to 10 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 the Commission'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.

Our audit was conducted for the purpose of forming an opinion on the basic combined financial statements taken as a whole. The additional information listed in the Table of Contents is presented for the purpose of additional analysis and is not a required part of the basic financial statements. This additional information is the responsibility of the Commission's management. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects when considered in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have issued a report dated January 11, 2005, on our consideration of the Commission's internal control over financial reporting and our tests of its compliance and other matters. The purpose of that report is to describe the scope of our testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

*Deloitte & Touche LLP*

January 11, 2005

**West Virginia Higher Education Policy Commission**  
Management Discussion and Analysis  
Fiscal Year 2004

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

The Governmental Accounting Standards Board (GASB) has issued directives for presentation of college and university financial statements that have been adopted for presentation in Fiscal Year 2002 by the West Virginia Higher Education Policy Commission (Commission). The previous reporting format presented financial balances and activities by fund groups. The current format places emphasis on the overall economic resources of the organization. This is the third fiscal year for this new format.

Comparative statements will not be issued this year due to the inclusion in the Commission statements of the West Virginia Network for Educational Telecomputing (WVNET). WVNET is a division of the Commission located in Morgantown, West Virginia. Separate statements were issued for each office prior to fiscal year 2004.

The following discussion and analysis of the Commission's financial statements provides an overview of its financial activities for the year ended June 30, 2004 and is required supplemental information per GASB No. 35. 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.

**Statement of Net Assets**

The Statement of Net Assets presents the assets, liabilities, and net assets of the Commission as of June 30, 2004. The Statement of Net Assets is a point of time financial statement. The purpose of the Statement of Net Assets is to present to the readers of the financial statements a fiscal snapshot of the Commission. The Statement of Net Assets presents end-of-year data concerning Assets (current and noncurrent), Liabilities (current and noncurrent), and Net Assets (assets minus liabilities).

From the data presented, readers of the Statement of Net Assets are able to determine the assets available to continue the operations of the Commission. They are also able to determine how much the Commission owes vendors, employees, investors and lending institutions. Finally, the Statement of Net Assets provides a picture of the net assets (assets minus liabilities) and their availability for expenditure by the Commission.

Net assets are divided into three major categories. The first category, invested in capital assets, net of related debt, provides the Commission's equity in furniture and equipment owned by the Commission. The next asset category is restricted net assets, which is divided into two categories, nonexpendable and expendable. Nonexpendable restricted net assets are for the Endowment Program where funds are invested and the earnings are

available for expenditure but the original investment is not. The Commission does not have any nonexpendable net assets at June 30, 2004. Expendable restricted net assets are available for expenditure by the Commission but have a specific purpose. The final category is unrestricted net assets. Unrestricted assets are available to be used for any lawful purpose of the Commission.

**Net Assets**

**(In thousands of dollars)**

June 30, 2004

**Assets:**

Current Assets	\$ 43,742
Other Non-Current Assets	193,445
Capital Assets, net	<u>2,158</u>
<b>Total Assets</b>	<b><u>\$ 239,345</u></b>

**Liabilities**

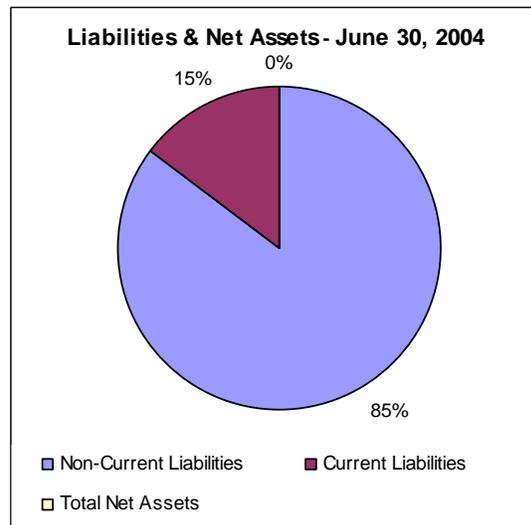
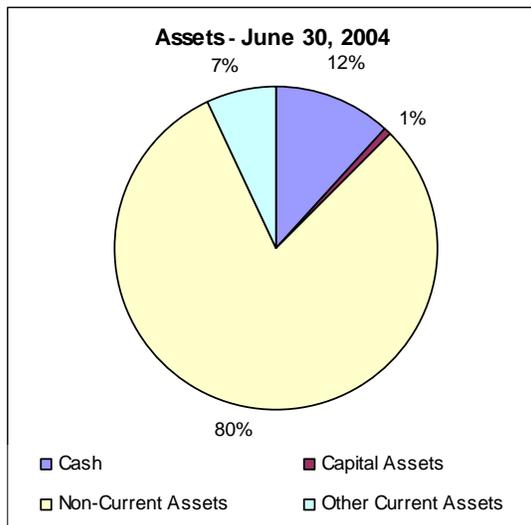
Current Liabilities	\$ 35,391
Non-current Liabilities	<u>204,160</u>
<b>Total Liabilities</b>	<b><u>239,551</u></b>

**Net Assets (Deficit)**

Restricted – expendable	20,925
Unrestricted	<u>(21,131)</u>
<b>Total Net Assets</b>	<b><u>( 206)</u></b>

**Total Liabilities and Net Assets**

**\$ 239,345**



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

- Due to the inclusion of WVNET in the Commission's statements, only the current year's Statement of Net Assets is presented. In future years, comparative statements will be presented.
- At June 30, 2004, the Commission's financial statements reflect a receivable from the higher education institutions (an internal obligation) related to principal payments owed by the Commission on system-wide debt obligations. Prior to fiscal year 2003, the system debt had been reflected solely as an obligation of the Commission and the requirement of the institutions to contribute funds to repay this debt was disclosed in a footnote. The internal assignment of this liability was shown as a transfer in the Statement of Revenue, Expenses and Changes in Net Assets during fiscal year 2003. On the Statement of Net Assets as of June 30, 2004, a receivable has been recorded for institutional obligations totaling \$184.4 million out of the total of \$199.1 million in outstanding system-debt. The remaining \$14.7 million continues to be reflected as part of the deficit in the Unrestricted Net Assets and will be allocated to certain institutions on an annual basis over the remaining term of the bonds. This change in reporting results in a more equitable presentation of net assets for both the Commission and the institutions.
- Total current assets of \$43.7 million exceed total current liabilities of \$35.4 million. By the very nature of the Commission, significant funds flow through the operations reported in these financial statements with further distribution to the West Virginia public institutions.
  - Cash balances of \$27.9 million in current assets include \$17.5 million to be returned to the State per Senate Bill 1007 passed on March 21, 2004 by the West Virginia Legislature requiring the Commission to return these prior year appropriated capital funds.
  - Current receivables from the institutions total \$9.1 million, which includes an allocation to the institutions of principal payments to be paid in fiscal year 2005 related to the system-wide bond obligations of \$8.8 million.
  - Current liabilities total \$35.4 million, with \$10.5 million related to the current principal portion of system-wide bond obligations, \$2.1 million in interest payable on the system debt, \$1.6 million in funding deposited for the PROMISE scholarship program and \$17.5 million per Senate Bill 1007 to be returned to the State.
- Non-current assets total \$195.6 million and non-current liabilities total \$204.2 million.
  - The primary non-current asset represents a \$175.3 million receivable from the institutions related to the system-wide bond obligations, \$10.1 million in cash earmarked for capital improvements at the institutions and debt service resulting from the receipt of special lottery funding in 2004.
  - Investment balances total \$3.7 million, which primarily represent revenue received from the State Department of Education for a new scholarship program called West Virginia GEAR UP project to be administered by the

Commission. It will provide students from economically disadvantage counties with financial incentives.

- The other major non-current liability represents the actual system-wide bonds outstanding, as further described in Note 8 to the financial statements.
- Total net assets of the Commission is a deficit of \$.2 million.
  - Net assets invested in capital assets is a deficit of \$14.1 million, primarily reflecting the system debt that is currently not allocated to specific institutions as described above.
  - Funds restricted for scholarship programs total \$6.3 million.
  - Funds restricted for capital projects total \$13.6 million.
  - Unrestricted funds is a deficit \$7.0 million which is a result of \$9.9 million of accreted interest on the Series 2000 A System Bonds that are not set to begin repayment until 2013.

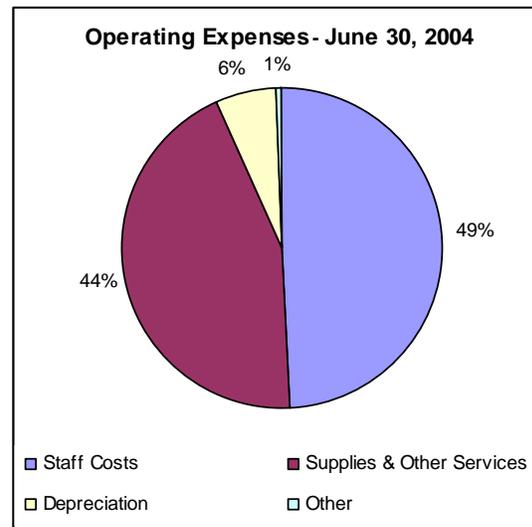
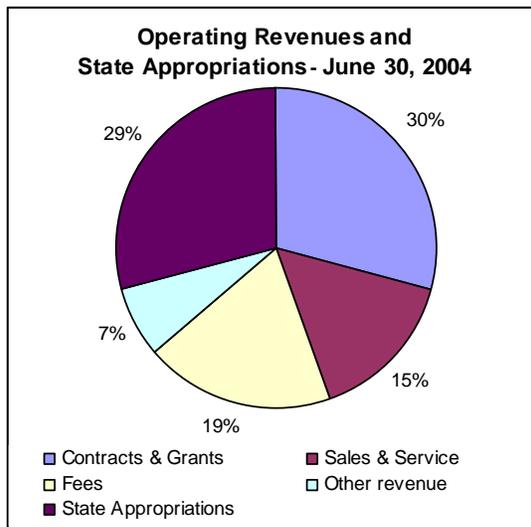
### **Statement of Revenues, Expenses and Changes in Net Assets**

Changes in total net assets as presented on the Statement of 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 of the Commission, both operating and nonoperating, and the expenses of the Commission, operating and nonoperating, and any other revenues, expenses, gains and losses of the Commission.

Operating revenues are fees from the institutions that the Commission by statute can assess them to support the Commission operations and various initiatives. Revenue is also received in the form of federal and State grants. Operating expenses are those expenses incurred in the form of staff salaries, benefits and various goods and services to carry out the mission of the Commission. Revenues for which goods and services are not provided are reported as nonoperating revenues. For example State appropriations are nonoperating because they are provided by the Legislature to the Commission without the Legislature directly receiving commensurate goods and services for those revenues.

**Revenues, Expenses and Changes in Net Assets  
(In thousands of dollars)**

	FY 2004
Operating Revenues	\$ 13,998
Operating Expenses	<u>13,776</u>
Operating Income	222
Net Nonoperating Revenues	<u>2,173</u>
Income Before Other Revenues, Expenses, Gains or Losses	2,395
Other Revenues, Expenses, Gains or Losses	<u>( 7,506)</u>
Decrease in Net Assets	( 5,111)
Net Assets (Deficit) - Beginning of Year	<u>4,905</u>
Net Assets (Deficit) - End of Year	<u><u>\$ ( 206)</u></u>



Major items of note in the Statement of Revenue, Expenses and Change in Net Assets include:

- Due to the inclusion of WVNET in the Commission’s statements, only the current year’s Statement of Revenues, Expenses and Change in Net Assets is presented. In future years, comparative statements will be presented.
- Operating income of the Commission totaled \$14.0 million.
  - Fees collected from higher education institutions for the operations of the Commission and for special projects for higher education totaled \$3.8 million.

- Other state and federal grants totaled \$5.8 million, and represent funding for various programs including the TRIO program, National Science Foundation EPSCoR program, Veterans Administration, Improving Teaching Quality Program and Vocational & Technical Education.
- Operating expenses totaled \$13.8 million.
  - Other operating expenses totaled \$13.8 million, and consist primarily of staff salaries, benefits, and other operating expenses for Commission initiatives and various federal and state funded programs.
- Net non-operating revenue totaled \$2.2 million.
  - State general revenue appropriations totaled \$5.8 million.
  - Lottery funding totaled \$36.0 million, and provides funding for scholarship programs as well as other pass-through funding to the institutions.
  - Pass-through expenditures for scholarships and financial aid totaled \$26.8 million. Funding for these programs comes from the West Virginia Lottery.
  - Payments for interest on indebtedness are offset by payments from the institutions for debt service totaling \$10.3 million
  - Other non-operating expenses totaled \$13.7 million, and primarily represent transfers to the institutions for operations and special projects.
- Capital funds of \$10.0 million were received in 2004 from the State's Excess Lottery Fund to provide funding for debt service on a new 2005 bond issue and a portion to be allocated to the institutions in future capital projects.

### **Statement of Cash Flows**

The final statement presented by Commission is the Statement of Cash Flows. The Statement of Cash Flows presents detailed information about the cash activity of the Commission during the year. The statement is divided into five parts. The first section deals with operating cash flows and shows the net cash used by the operating activities of the Commission. The second section reflects cash flows from noncapital financing activities. This section reflects the cash received and spent for nonoperating, noninvesting, and noncapital 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 deals with cash flows from capital and related financing activities. This section deals with the cash used for the acquisition and construction of capital and related items. The fifth part reconciles the net cash used to the operating income or loss reflected on the Statement of Revenues, Expenses, and Changes in Net Assets.

**Cash Flows**  
**(In thousands of dollars)**

FY 2004

Cash Provided (used) by:	
Operating Activities	\$ 803
Noncapital Financing Activities	(548)
Capital and Related Financing Activities	15,411
Investing Activities	<u>(2,840)</u>
Increase in Cash and Cash Equivalents	12,826
Cash and Cash Equivalents, beginning of year	<u>15,119</u>
Cash and Cash Equivalents, end of year	<u>\$ 27,945</u>

Major items of note in the Cash Flow Statement include:

- Due to the inclusion of WVNET in the Commission's statements, only the current year's Statement of Cash Flows is presented. In future years, comparative statements will be presented.
- Net cash provided by operating revenues offset cash expended for operating activities. Major variances from that reported on the Statement of Revenue, Expenses and Changes in Net Assets include depreciation expense and accruals for compensated absences.
- Net cash expended in Noncapital Financing Activities are primarily for excess payments made by the Commission for programs which the Commission provides fiduciary fiscal services.
- Net cash used by Capital Financing Activities is \$15.4 million primarily for Legislative mandate to return \$17.5 million to the State.
- Major activity was to refund and defease all outstanding University and College System Series 1992 Bonds in the amount of \$95.2 million and also to issue the Series 2003 A Bonds. The total cash flow savings for the remaining life of the bonds was approximately \$8.0 million. The economic gain of the refinancing was approximately \$6.8 million.
- Net cash provided from Investing Activities totaled \$2.8 million primarily for revenue invested for the GEAR Up Program as discussed earlier.
- Total cash for FY 2004 year increased by \$12.8 million. This increase primarily relates to return of the previously discussed \$17.5 million to be returned to the State. This amount is offset by increases in payments to institutions and fiduciary entities.

**Other Factors Impacting the Financial Position and Results of Operations of the Commission**

The mission of the Commission is to align the West Virginia Higher Education System to contribute to the long-term growth and diversification of West Virginia's economy as outlined in It All Adds Up: Compact for the Future of West Virginia. (the "Compact")

focuses on goals in the following six major areas: Preparation, Participation, Affordability, Competitive Work Force, Economic Development, and Accountability.

The achievement of the goals for the higher education system as described in the Compact are dependent upon many factors, one of which is adequate resources to implement the strategies necessary to achieve the goals. At the present time the Commission itself maintains a strong financial condition. Although the net asset position of the Commission is reported as a deficit of \$.2 million, this deficit does not include the \$14.7 million in net system bond indebtedness that will be allocated to the institutions as the debt is repaid over the next eight years. The vast majority of the funding which is reported in the financial statements of the Commission is ultimately assigned to the public higher education institutions in the State for capital projects, grants, scholarships and special projects. This funding is critical to the success of the higher education system in meeting the Compact goals.

### **Economic Outlook**

General revenue funding for the Commission's operations was reduced by 23% for fiscal year 2004, as compared to fiscal year 2003, due to budget constraints imposed upon virtually all state agencies. For fiscal year 2005, the General Revenue funding for the Commission's operations was reduced by approximately 5%. For fiscal year 2006, all state agencies are being requested to submit a general revenue budget appropriation request with a 5.5% budget reduction. The strategies for implementing the budget reductions for fiscal year 2006 are currently in the process of being evaluated prior to implementation.

# WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

## STATEMENT OF NET ASSETS

JUNE 30, 2004

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### ASSETS:

#### Current assets:

Cash and cash equivalents	\$ 27,945,024
Investments	360,746
Appropriations due from Primary Government	2,462,386
Accounts receivable—net	3,864,731
Interest receivable	50,225
Receivable from institutions—current portion	<u>9,059,104</u>

Total current assets 43,742,216

#### Noncurrent assets:

Cash and cash equivalents	10,118,153
Investments	3,683,817
Receivable from institutions	175,333,069
Other assets	4,309,938
Investment in capital assets—net	<u>2,158,186</u>

Total noncurrent assets 195,603,163

TOTAL ASSETS \$ 239,345,379

(Continued)

# WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

## STATEMENT OF NET ASSETS JUNE 30, 2004

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### LIABILITIES:

#### Current liabilities:

Accounts payable	\$ 2,223,426
Accrued liabilities	109,124
Unappropriated liability due to State	17,506,041
Deposits	1,836,507
Deferred revenue	306,114
Compensated absences—current portion	518,000
Interest payable	2,112,682
Bonds payable—current portion	10,535,000
Capital lease obligation	<u>244,784</u>

Total current liabilities 35,391,678

#### Noncurrent liabilities:

Compensated absences	983,877
Deferred interest payable	9,879,201
Due to West Virginia University	125,387
Bonds payable	192,835,806
Capital lease obligation	<u>335,753</u>

Total noncurrent liabilities 204,160,024

Total liabilities 239,551,702

### NET ASSETS (DEFICIT):

Invested in capital assets, net of related debt

-

Restricted for—

Expendable:

Scholarships	6,281,484
Sponsored projects	677,106
Capital projects	13,590,426
Debt service	360,746
Other	<u>14,962</u>

Total restricted expendable 20,924,724

Unrestricted (21,131,047)

Total net assets (206,323)

TOTAL LIABILITIES AND NET ASSETS

\$ 239,345,379

See notes to financial statements.

(Concluded)

# WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

## STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS (DEFICIT) YEAR ENDED JUNE 30, 2004

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### OPERATING REVENUES:

Fees from higher education institutions	\$ 3,776,718
Institutional collections	1,306,236
Contracts and grants:	
Federal	2,622,496
State	3,143,702
Sales and services of educational activities	3,041,747
Miscellaneous—net	<u>107,030</u>
Total operating revenues	<u>13,997,929</u>

### OPERATING EXPENSES:

Salaries and wages	5,496,009
Benefits	1,319,133
Supplies and other services	6,053,785
Utilities	86,373
Depreciation	<u>821,103</u>
Total operating expenses	<u>13,776,403</u>

OPERATING INCOME	<u>221,526</u>
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(Continued)

# WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

## STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS (DEFICIT) YEAR ENDED JUNE 30, 2004

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NONOPERATING REVENUES (EXPENSES):	
State appropriations	\$ 41,750,649
Investment income	114,601
Institutional debt service payments to Commission:	
Interest	7,308,528
Other	3,012,849
Interest on indebtedness	(9,581,969)
Student financial aid payments to institutions	(26,763,755)
Other payments to institutions	<u>(13,667,513)</u>
Net nonoperating revenues	<u>2,173,390</u>
INCOME BEFORE OTHER REVENUES, EXPENSES, GAINS OR LOSSES	2,394,916
CAPITAL APPROPRIATIONS	10,000,000
UNAPPROPRIATED CAPITAL	<u>(17,506,041)</u>
DECREASE IN NET ASSETS	(5,111,125)
NET ASSETS—Beginning of year	<u>4,904,802</u>
NET ASSETS (DEFICIT)—End of year	<u>\$ (206,323)</u>
See notes to financial statements.	(Concluded)

# WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

## STATEMENT OF CASH FLOWS YEAR ENDED JUNE 30, 2004

CASH FLOWS FROM OPERATING ACTIVITIES:	
Fees and reimbursements from higher education institutions	\$ 6,772,650
Institutional collections	1,183,199
Contracts and grants	5,766,198
Payments to and on behalf of employees	(6,976,611)
Payments to suppliers	(9,014,593)
Payments to utilities	(86,373)
Sales and service of educational activities	3,030,914
Other payments—net	<u>128,165</u>
Net cash provided by operating activities	<u>803,549</u>
CASH FLOWS FROM NONCAPITAL FINANCING:	
State appropriations	42,232,170
Receipts from fiduciary governmental entities	22,264,249
Disbursements to fiduciary governmental entities	(25,954,437)
Payments to institutions	<u>(39,090,011)</u>
Net cash used in noncapital financing activities	<u>(548,029)</u>
CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES:	
Capital appropriations	10,000,000
Proceeds from bond issuance	100,009,292
Payment of bond issuance costs	(4,814,292)
Institutional receipts for debt service	18,570,804
Purchases of capital assets	(128,799)
Principal paid on bonds	(107,850,000)
Interest paid on bonds	(7,354,493)
Principal paid on leases	(161,861)
Interest paid on leases	(23,391)
Capital projects construction bond payments	(181,789)
Capital loans to institutions	(475,000)
Capital loan repayments from institutions	199,500
Decrease in noncurrent cash and cash equivalents	<u>7,621,222</u>
Net cash provided by capital financing activities	<u>15,411,193</u>
CASH FLOWS FROM INVESTING ACTIVITIES:	
Receipts from sale of investments	181,789
Purchases of investments	(3,102,721)
Interest on investments	<u>80,727</u>
Net cash used in investing activities	<u>(2,840,205)</u>
INCREASE IN CASH AND CASH EQUIVALENTS	12,826,508
CASH AND CASH EQUIVALENTS—Beginning of year	<u>15,118,516</u>
CASH AND CASH EQUIVALENTS—End of year	<u>\$ 27,945,024</u>

(Continued)

# WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

## STATEMENT OF CASH FLOWS YEAR ENDED JUNE 30, 2004

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### RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:

Operating income	\$ 221,526
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation expense	821,103
Loss on disposals of assets	20,500
Changes in assets and liabilities:	
Accounts receivables—net	(163,384)
Accounts payable	71,520
Accrued liabilities	(97,285)
Compensated absences	(47,762)
Deferred revenue	<u>(22,669)</u>

NET CASH PROVIDED BY OPERATING ACTIVITIES \$ 803,549

See notes to financial statements.

(Concluded)

# WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

## NOTES TO FINANCIAL STATEMENTS YEAR ENDED JUNE 30, 2004

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### 1. ORGANIZATION

On March 19, 2000, the West Virginia Legislature enacted Senate Bill No. 653 (“S.B. 653”), which restructured public higher education in West Virginia.

S.B. 653 also created the West Virginia Higher Education Policy Commission (the Board of the West Virginia Higher Education Fund that encompasses all West Virginia public higher education), which is responsible for developing, gaining consensus around and overseeing the implementation and development of a higher education public policy agenda. The West Virginia Higher Education Policy Commission (the “Commission”) consists of two parts. One part is the administrative functions of the Commission. The second part is a separate division which was previously not included in these financial statements. The financial statements of the Commission include the accounts of West Virginia Network for Educational Telecommuting (“WVNET”), a division of the Commission, as oversight of WVNET lies with the Commission. WVNET was originally created in 1975 to provide central computing facilities and wide-area network communications services as a resource for the public colleges and universities in the state of West Virginia.

Each Institutional Governing Board (all institutions and the Commission which comprises the West Virginia Higher Education Fund) has certain powers and duties including but not limited to, the power to determine, control, supervise and manage the financial, business and educational policies and affairs of the institution(s) under its jurisdiction, the duty to develop a master plan for the institution, the power to prescribe the specific functions and institution’s budget request, the duty to review, at least every five years, all academic programs offered at the institution, and the power to fix tuition and other fees for the different classes or categories of students enrolled at the institution(s).

During fiscal year 2004, Senate Bill 448 (“S.B. 448”) was passed. S.B. 448 created the Council for Community and Technical Colleges (the “Council”) which has responsibility for all community and technical colleges within the West Virginia Higher Education Fund. For the year ended June 30, 2004, all activities of the Council are included in the Commission. As required by S.B. 448, beginning for the fiscal year ending June 30, 2005, the Council will be separated from the Commission. The transfer of net assets from the Commission to the Council has not yet been determined.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Commission 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 – for 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 the Commission’s assets, liabilities, net assets, revenues, expenses, changes in net assets and cash flows.

The Commission 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**—The Commission is a statutory entity and an operating unit of the West Virginia Higher Education Fund and represents separate funds of the State of West Virginia (the “State”) that are not included in the State’s general fund. The Commission is a separate entity which, along with all State institutions of higher education, 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 direct authority of the Commission. The basic criteria for inclusion in the accompanying financial statements is the exercise of oversight responsibility derived from the Commission’s ability to significantly influence operations and accountability for fiscal matters of related entities.

**Financial Statement Presentation**—During fiscal 2002, the Commission 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 basis to focus on the Commission as a whole. Net assets are classified into four categories according to external donor restrictions or availability of assets for satisfaction of Commission obligations. The Commission’s net assets are classified as follows:

- *Invested in capital assets, net of related debt*—This represents the Commission’s total investment in capital assets, net of outstanding debt obligations related to capital assets, including those on individual institutions’ financial statements. 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 the Commission is legally or contractually obligated to spend resources in accordance with restrictions imposed by external third parties.

The West Virginia Legislature, as a regulatory body outside the reporting entity, has restricted the use of certain funds by Article 10, *Fees and Other Money Collected at State Institutions of Higher Education* of the West Virginia State Code (the “Code”). House Bill 101 passed in March 2004 simplified the tuition and fee restrictions. For 2004, these restrictions are for auxiliaries and capital items. These activities are fundamental to the normal ongoing operations of the related institutions. These restrictions are subject to change by future actions of the West Virginia Legislature. The Commission does not have any such Code-restricted net assets at June 30, 2004.

- *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. There were no nonexpendable net assets as of June 30, 2004.
- *Unrestricted net assets*—Unrestricted net assets represent resources derived from student tuition and fees, state appropriations and sales and services of educational activities. These resources are used for transactions relating to the educational and general operations of the Commission, and may be used at the discretion of the Higher Education Policy Commission to meet current expenses for any purpose.

***Basis of Accounting***—For financial reporting purposes, the Commission is considered a special-purpose government engaged only in business-type activities. Accordingly, the Commission’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, the Commission 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 State Legislature and is subject to oversight by the 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.

***Investments***—The Commission’s investments are on deposit with the Municipal Bond Commission or with external financial institutions. These funds primarily represent unexpended proceeds of bond issuances, and are restricted to expenditures for capital improvements and bond related costs and debt service reserve funds. Funds on deposit with external financial institutions are invested in money market accounts. A portion of these funds are classified as noncurrent due to the restrictions on expenditure or requirement to provide debt service reserve funds. Amounts for restricted expenditures are available for immediate withdrawal. Investments are recorded at fair value.

***Allowance for Doubtful Accounts***—It is the Commission’s policy to provide for future losses on uncollectible accounts, contracts, grants and loans receivable based on an evaluation of the underlying account, contract, grant and loan balances, the historical collectibility experienced by the Commission on such balances and such other factors which, in the Commission’s judgment, require consideration in estimating doubtful accounts.

***Noncurrent Cash and Cash Equivalents***—Cash, that is (1) externally restricted to make debt service payments or to maintain sinking or reserve funds, and (2) to purchase capital or other noncurrent assets, is classified as a noncurrent asset in the statement of net assets.

***Other Assets***—Other assets include bond issuance costs which are amortized over the life of the related bonds.

***Capital Assets***—Capital assets include furniture and equipment. Capital assets are stated at cost at the date of acquisition or construction, 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 furniture and equipment.

***Deferred Revenue***—Cash received for programs or activities to be conducted primarily in the next fiscal year are classified as deferred revenue.

**Compensated Absences**—The Commission 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.

The Commission'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 extends health insurance for one month of single coverage and three days extends 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, the Commission 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 the Commission 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 (deficit).

**Deferred Interest**—Interest on capital accretion bonds are recognized over the life of the related bonds on the interest method.

**Bonds**—Bond premiums or discounts are amortized over the life of the related bonds.

**Risk Management**—The State's Board of Risk and Insurance Management ("BRIM") provides general, property and casualty, and medical malpractice liability coverage to the Commission and its employees. Such coverage may be provided to the Commission 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 the Commission or other participants in BRIM's insurance programs. As a result, management does not expect significant differences between premiums the Commission is currently charged by BRIM and the ultimate cost of that insurance based on the Commission's actual loss experience. In the event such differences arise between estimated premiums currently charged by BRIM to the Commission and the Commission's ultimate actual loss experience, the difference will be recorded, as the change in estimate becomes known.

**Classification of Revenues**—The Commission has classified its revenues as either operating or nonoperating revenues according to the following criteria:

- **Operating revenues**—Operating revenues include activities that have the characteristics of exchange transactions, such as (1) fees from higher education institutions, and (2) most federal,

State, local, and nongovernmental grants and contracts and (3) federal appropriations for land grant institutions.

- *Nonoperating revenues*—Nonoperating revenues include activities that have the characteristics of nonexchange 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 and Federal appropriations and investment income.
- *Unappropriated capital*—Unappropriated capital is amounts which were recognized as revenue in prior years, which were legislatively required to be returned.

***Use of Restricted Net Assets***—The Commission 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, the Commission attempts to utilize restricted funds first when practical.

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

***Government Grants and Contracts***—Government grants and contracts normally provide for the recovery of direct and indirect costs, subject to audit. The Commission 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 five years.

***Interest Expense***—The Commission accounts for interest on debt as an expense of the period in which it is incurred. The Commission does not capitalize interest on debt as part of the cost of the asset.

***Income Taxes***—The Commission 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 expenses 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. 40, *Deposit and Investment Risk Disclosures*. This statement is effective for periods beginning after June 15, 2004. The Commission has not completed the process of evaluating the impact, if any, that will result from adopting GASB Statement No. 40. The statement, when adopted, could result in additional disclosure in the Commission's financial statements regarding custodial credit risk, concentration of credit risk and interest rate risk related to deposits and investments.

The GASB has also issued Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, effective for fiscal years beginning after December 15,

2004. This statement requires the Commission to evaluate prominent events or changes in circumstances affecting capital assets to determine whether impairment of a capital asset has occurred and record impaired assets and impairment losses accordingly. This statement also addresses the appropriate recording of an insurance recovery associated with the events or changes in circumstances resulting in impairment of a capital asset. The Commission has not yet determined the effect that the adoption of GASB Statement No. 42 may have on the financial statements.

The GASB has also issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, effective for fiscal years beginning after December 15, 2006. This statement provides standards for the measurement, recognition and display of other postemployment benefit expenditures, assets, and liabilities, including applicable note disclosures and required supplementary information. The Commission has not yet determined the effect that the adoption of GASB Statement No. 45 may have on the financial statements.

The GASB has also issued Statement No. 46, *Net Assets Restricted by Enabling Legislation* (an amendment of GASB Statement No. 34), effective for fiscal years beginning after June 15, 2005. This statement provides guidance clarifying the meaning of the phrase “legally enforceable” as it applies to restrictions imposed on net asset use by ensuring legislation. The Commission has not yet determined the effect, if any, that the adoption of GASB Statement No. 46 may have on its financial statements.

**3. CASH AND CASH EQUIVALENTS**

The composition of cash and cash equivalents was as follows at June 30, 2004:

Cash on deposit with the State Treasurer:	
Current	\$27,945,024
Noncurrent	<u>10,118,153</u>
	<u>\$38,063,177</u>

Cash on deposit with the State Treasurer is a noncategorized deposit in accordance with GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*.

**4. INVESTMENTS**

The composition of investments was as follows at June 30, 2004:

	<b>Current</b>	<b>Noncurrent</b>	<b>Total</b>
Municipal Bond Commission	<u>\$360,746</u>	<u>\$3,683,817</u>	<u>\$4,044,563</u>

**5. ACCOUNTS RECEIVABLE**

Accounts receivable were as follows at June 30, 2004:

Student receivables—net of allowance for doubtful accounts of \$648,504	\$ 309,576
Grants and contracts receivable	61,712
Due from higher education institutions	2,765,494
Other accounts receivable	<u>727,949</u>
	<u>\$3,864,731</u>

**6. CAPITAL ASSETS**

The following is a summary of capital asset activity for the Commission for the year ended June 30, 2004:

	Beginning Balance	Additions	Reductions	Ending Balance
Capital assets:				
Equipment	\$ 9,479,414	\$ 128,799	\$ (272,527)	\$ 9,335,686
Leased equipment	<u>960,406</u>	<u>202,954</u>	<u>                    </u>	<u>1,163,360</u>
Total capital assets	10,439,820	331,753	(272,527)	10,499,046
Less accumulated depreciation for:				
Equipment	7,560,927	693,522	(252,027)	8,002,422
Leased equipment	<u>210,857</u>	<u>127,581</u>	<u>                    </u>	<u>338,438</u>
Total accumulated depreciation	<u>7,771,784</u>	<u>821,103</u>	<u>(252,027)</u>	<u>8,340,860</u>
Capital assets—net	<u>\$ 2,668,036</u>	<u>\$ (489,350)</u>	<u>\$ (20,500)</u>	<u>\$ 2,158,186</u>

Title to certain real property at the institutions is held by the Commission by virtue of legislative assignment from prior system-wide governing boards. Title can be transferred from the Commission to the Institutional Governing Boards upon mutual agreement. Regardless of title, all real property at the institution is recorded in the institution's financial statements.

## 7. LONG-TERM LIABILITIES

The following is a summary of long-term obligation activity for the Commission for the year ended June 30, 2004:

	<b>Beginning Balance</b>	<b>Additions</b>	<b>Reductions</b>	<b>Ending Balance</b>	<b>Current Portion</b>
Bonds payable	\$ 211,715,868	\$ 99,389,938	\$ 107,735,000	\$ 203,370,806	\$ 10,535,000
Capital lease obligations	539,443	202,954	161,860	580,537	<u>\$ 244,784</u>
Other long-term liabilities:					
Accrued compensated absences	1,549,639		47,762	1,501,877	<u>\$ 518,000</u>
Deferred interest payable	7,183,831	2,695,370		9,879,201	
Due to West Virginia University	<u>165,755</u>		<u>40,368</u>	<u>125,387</u>	
Total long-term liabilities	<u>\$ 221,154,536</u>	<u>\$ 102,288,262</u>	<u>\$ 107,984,990</u>	<u>\$ 215,457,808</u>	

## 8. BONDS PAYABLE

The State chartered the former University System of West Virginia and the former State College System of West Virginia with the responsibility to construct or renovate, finance and maintain various academic and other facilities of the State's higher education institutions. Financing for these facilities was provided through revenue bonds issued by the former State Board of Regents, the former College and University System Boards, the Interim Governing Board or the Commission. All bonds payable are administered by the Commission, as successor to the various former governing boards.

The Commission has the authority to assess each institution of the West Virginia Higher Education Fund for payment of debt service on these system bonds. The tuition and registration fees of the institutions are generally pledged as collateral for the Commission's bond indebtedness. Student fees collected by an institution in excess of the debt service allocation are retained by the institution for internal funding of capital projects and maintenance. The bonds remain an obligation of the Commission.

The Series 2003 A University Facility Bonds and the Series 2003 A College Facility Bonds were issued in August 2003 under the provisions of the Code of West Virginia, 1931, as amended, particularly Chapters 13 and 18. These bonds were issued to provide monies which, together with other monies available to the respective boards, were used to (i) refund and defease all outstanding University System of West Virginia Board of Trustees, Series 1992 Bonds and (ii) to provide for the payment of costs of issuing the 2003 Series A Revenue Refunding Bonds. The total cash flow savings for the remaining life of the bonds was approximately \$8 million. The economic gain of the refinancing was approximately \$6.8 million.

Bonds payable consisted of the following at June 30, 2004:

	Maximum Interest Rate	Range of Annual Principal Installment Due		Principal Amount Outstanding
2003 Series A College Facilities Bonds, due through 2012	5.00 %	\$2,325,000	to \$2,690,000	\$ 18,525,000
2003 Series A University Facilities Bonds, due through 2012	5.00	5,740,000	to 7,875,000	53,835,000
Series 1996 University System Bonds, due through 2016	5.75	630,000	to 1,185,000	10,715,000
Series 1997 University System Bonds, due through 2027	5.25	255,000	to 795,000	11,145,000
Series 1998 University System Bonds, due through 2028	5.25	1,065,000	to 3,625,000	51,020,000
Series 2000A University System Bonds, due through 2031	6.26	1,018,912	to 3,263,864	36,590,868
Series 2000B University System Bonds, due through 2025	5.96	210,000	to 670,000	8,475,000
Series 1997 College System Bonds, due through 2027	5.25	200,000	to 625,000	<u>8,755,000</u>
				199,060,868
Add: Bond premium				<u>4,309,938</u>
				<u>\$ 203,370,806</u>

A summary of the annual aggregate payments for years subsequent to June 30, 2004 is as follows:

Year Ending June 30	Principal	Interest	Total
2005	\$ 10,535,000	\$ 8,061,820	\$ 18,596,820
2006	10,945,000	7,613,289	18,558,289
2007	11,355,000	7,163,799	18,518,799
2008	11,780,000	6,704,498	18,484,498
2009	12,295,000	6,155,827	18,450,827
2010-2014	52,931,076	28,851,947	81,783,023
2015-2019	31,574,768	35,021,613	66,596,381
2020-2024	30,787,476	33,312,178	64,099,654
2025-2029	24,754,988	29,697,083	54,452,071
2030-2031	<u>2,102,560</u>	<u>11,497,440</u>	<u>13,600,000</u>
	<u>\$199,060,868</u>	<u>\$174,079,494</u>	<u>\$373,140,362</u>

The higher education institutions' tuition, registration and other specified fees generally are pledged as collateral for the Commission's bond indebtedness, as well as any monies held by the trustees.

## 9. CAPITAL LEASES

Capital lease obligations consisted of the following on June 30, 2004:

	Interest Rate	Principal Amount Outstanding
JP Morgan, Computer Equipment	2.28%	\$ 181,082
JP Morgan, Computer Equipment	3.12%	271,402
JP Morgan, Modem	2.13%	70,374
Document Solutions, Xerox Copiers and Printers	12.50%	23,284
JP Morgan, SP Upgrade	3.97%	<u>34,395</u>
		<u>\$ 580,537</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, 2004 is as follows:

Year Ending June 30	Principal	Interest	Total
2005	\$ 244,784	\$ 12,905	\$ 257,689
2006	186,857	6,016	192,873
2007	128,057	2,039	130,096
2008	20,839	108	<u>20,947</u>
			601,605
Less interest			<u>(21,068)</u>
			<u>\$ 580,537</u>

## 10. COMPENSATED ABSENCES LIABILITY

The composition of the compensated absences liability was as follows at June 30, 2004:

Health and life insurance	\$ 645,648
Accrued vacation liability	657,112
Current retirees' health insurance	<u>199,117</u>
	<u>\$ 1,501,877</u>

The cost of health and life insurance benefits paid by the Commission is based on a combination of years of service and use. For the year ended June 30, 2004, the amount paid by the Commission for extended health or life insurance coverage retirement benefits totaled \$76,893. As of June 30, 2004, there were 12 retirees currently receiving these benefits.

## 11. RETIREMENT PLANS

Substantially all full-time employees of the Commission 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"). Previously, upon full-time employment, all employees were required to make an irrevocable selection between the STRS and 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 the Commission's employees have not been significant to date.

Effective January 1, 2003, higher education employees enrolled in the basic 401(a) retirement plan with TIAA-CREF have an option to switch to the new Educators Money 401(a) basic retirement plan. New hires have the choice of either plan. As of June 30, 2004, no employees were enrolled in the new Educators Money 401(a) basic retirement plan.

The STRS is a cost-sharing, defined benefit public employee retirement system. Employer and employee contribution rates are established annually by the State Legislature. The Commission accrued and paid its contribution to the STRS at a rate of 15% of each enrolled employee's total annual salary for the year ended June 30, 2004. Required employee contributions were at the rate of 6% of total annual salary in 2004. 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 salary out of the last 15 years) multiplied by the number of years of service.

Total contributions to the STRS for the year ended June 30, 2004 were \$80,946 which consisted of \$57,819 from the Commission and \$23,127 from covered employees. Total contributions to the STRS for the year ended June 30, 2003 were \$93,090, which consisted of \$66,493 from the Commission and \$26,597 from covered employees. Total contributions to the STRS for the year ended June 30, 2002 were \$104,501, which consisted of \$74,644 from the Commission and \$29,857 from covered employees.

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

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. The Commission matches the employees' 6% contribution. Contributions are immediately and fully vested. In addition, employees may elect to make additional contributions to TIAA-CREF which are not matched by the Commission.

Total contributions to the TIAA-CREF for the year ended June 30, 2004 were \$606,462 which consisted of \$303,231 from the Commission and \$303,231 from covered employees. Total contributions to the TIAA-CREF for the year ended June 30, 2003 were \$665,776 which consisted of \$332,888 from the Commission and \$332,888 from covered employees. Total contributions to the TIAA-CREF for the year ended June 30, 2002 were \$667,860, which consisted of \$333,930 from the Commission and \$333,930 from covered employees.

The Commission's total payroll for the years ended June 30, 2004 was \$5,817,650; total covered employees' salaries in the STRS and TIAA-CREF were \$385,462 and \$5,289,416, respectively, in 2004.

During fiscal years 2003 and 2002, the Commission offered staff severance benefit plans to certain eligible employees at WVNET. Two and four employees during fiscal years 2003 and 2002, respectively, accepted the plans and will receive severance benefits over a 24-month period.

## 12. OPERATING LEASES

Future annual minimum lease payments on operating leases for years subsequent to June 30, 2004 are as follows:

<b>Year Ending June 30</b>	
2005	\$ 383,883
2006	<u>386,469</u>
	<u>\$ 770,352</u>

Total rent expense for the year ended June 30, 2004 was \$384,905.

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 the Commission's statement of revenues, expenses, and changes in net assets.

## 13. CONTINGENCIES

The nature of the educational industry is such that, from time-to-time, claims will be presented against the Commission 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 the Commission would not impact seriously on the financial status of the Commission.

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. The Commission's management believes disallowances, if any, will not have a significant impact on the Commission'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 operation with the asbestos in a safe condition.

#### 14. REIMBURSED EXPENDITURES

The Commission, through 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, the Commission, through WVNET, provides purchasing services regarding computer equipment purchases. In fiscal year 2004 approximately \$3,000,000 was reimbursed by the schools and other state agencies to WVNET. The Commission treats these items as reimbursed expenditures so as not to distort total revenues and expenditures.

#### 15. SUBSEQUENT EVENT

During August 2004, the Commission issued \$167,260,000 of Series B Bonds with varying interest rates up to 5.0% per annum, maturing in installments through 2034. Approximately, \$159,500,000 has been allocated to special institutions.

#### 16. NATURAL CLASSIFICATIONS WITH FUNCTIONAL CLASSIFICATIONS

For the year ended June 30, 2004, the following table represents operating expenses within both natural and functional classifications:

	Salaries and Wages	Benefits	Supplies and Other Services	Utilities	Depreciation	Total
General institutional support	\$ 5,496,009	\$ 1,319,133	\$ 6,053,785	\$ -	\$ -	\$ 12,868,927
Administration, operations and maintenance of plant				86,373		86,373
Depreciation					821,103	821,103
Total	<u>\$ 5,496,009</u>	<u>\$ 1,319,133</u>	<u>\$ 6,053,785</u>	<u>\$ 86,373</u>	<u>\$ 821,103</u>	<u>\$ 13,776,403</u>

\* \* \* \* \*

## **ADDITIONAL INFORMATION**

# WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

## COMBINING SCHEDULE—STATEMENT OF NET ASSETS INFORMATION JUNE 30, 2004

	HEPC Division	WVNET Division	Eliminations	Combined
<b>ASSETS:</b>				
Current assets:				
Cash and cash equivalents	\$ 25,386,394	\$ 2,558,630	\$ -	\$ 27,945,024
Investments	360,746			360,746
Appropriations due from Primary Government	2,462,386			2,462,386
Accounts receivable—net	2,596,610	1,269,224	(1,103) (A)	3,864,731
Interest receivable	49,080	1,145		50,225
Receivable from institutions—current portion	<u>9,059,104</u>	<u>                    </u>	<u>                    </u>	<u>9,059,104</u>
Total current assets	<u>39,914,320</u>	<u>3,828,999</u>	<u>(1,103)</u>	<u>43,742,216</u>
Noncurrent assets:				
Cash and cash equivalents	10,118,153			10,118,153
Investments	3,683,817			3,683,817
Receivable from institutions	175,333,069			175,333,069
Other assets	4,309,938			4,309,938
Investment in capital assets—net	<u>172,900</u>	<u>1,985,286</u>	<u>                    </u>	<u>2,158,186</u>
Total noncurrent assets	<u>193,617,877</u>	<u>1,985,286</u>	<u>-</u>	<u>195,603,163</u>
<b>TOTAL ASSETS</b>	<u>\$ 233,532,197</u>	<u>\$ 5,814,285</u>	<u>\$ (1,103)</u>	<u>\$ 239,345,379</u>

(Continued)

# WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

## COMBINING SCHEDULE—STATEMENT OF NET ASSETS INFORMATION JUNE 30, 2004

	HEPC Division	WVNET Division	Eliminations	Combined
<b>LIABILITIES:</b>				
Current liabilities:				
Accounts payable	\$ 1,080,937	\$ 1,143,592	\$ (1,103) (A)	\$ 2,223,426
Accrued liabilities	71,963	37,161		109,124
Unappropriated liability due to State	17,506,041			17,506,041
Deposits	1,836,507			1,836,507
Deferred revenue	245,576	60,538		306,114
Compensated absences—current portion	275,412	242,588		518,000
Interest payable	2,112,682			2,112,682
Bonds payable—current portion	10,535,000			10,535,000
Capital lease obligation		244,784		244,784
Total current liabilities	<u>33,664,118</u>	<u>1,728,663</u>	<u>(1,103)</u>	<u>35,391,678</u>
Noncurrent liabilities:				
Compensated absences	580,306	403,571		983,877
Deferred interest payable	9,879,201			9,879,201
Due to West Virginia University	125,387			125,387
Bonds payable	192,835,806			192,835,806
Capital lease obligation		335,753		335,753
Total noncurrent liabilities	<u>203,420,700</u>	<u>739,324</u>	<u>-</u>	<u>204,160,024</u>
Total liabilities	<u>237,084,818</u>	<u>2,467,987</u>	<u>(1,103)</u>	<u>239,551,702</u>
<b>NET ASSETS (DEFICIT):</b>				
Invested in capital assets	(15,531,296)	1,404,749	14,126,547 (C)	-
Restricted for:				
Expendable:				
Scholarships	6,281,484		(C)	6,281,484
Sponsored projects	677,106			677,106
Capital projects	13,590,426			13,590,426
Debt service	360,746			360,746
Other	14,962			14,962
Total restricted expendable	20,924,724	-	-	20,924,724
Unrestricted	(8,946,049)	1,941,549	(14,126,547)	(21,131,047)
Total net assets	<u>(3,552,621)</u>	<u>3,346,298</u>	<u>-</u>	<u>(206,323)</u>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<u>\$ 233,532,197</u>	<u>\$ 5,814,285</u>	<u>\$ (1,103)</u>	<u>\$ 239,345,379</u>

(Concluded)

## WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

### COMBINING SCHEDULE—STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS (DEFICIT) INFORMATION YEAR ENDED JUNE 30, 2004

	HEPC Division	WVNET Division	Eliminations	Combined
OPERATING REVENUES:				
Fees from higher education institutions	\$3,776,718	\$ -	\$ -	\$ 3,776,718
Institutional collections		1,306,236		1,306,236
Contracts and grants:				
Federal	2,622,496			2,622,496
State	3,143,702			3,143,702
Sales and services of educational activities		3,091,589	(49,842) (B)	3,041,747
Miscellaneous—net	<u>7,364</u>	<u>99,666</u>	<u>          </u>	<u>107,030</u>
Total operating revenues	<u>9,550,280</u>	<u>4,497,491</u>	<u>(49,842)</u>	<u>13,997,929</u>
OPERATING EXPENSES:				
Salaries and wages	3,271,644	2,274,207	(49,842) (B)	5,496,009
Benefits	736,015	583,118		1,319,133
Supplies and other services	3,210,314	2,843,471		6,053,785
Utilities		86,373		86,373
Depreciation	<u>169,336</u>	<u>651,767</u>	<u>          </u>	<u>821,103</u>
Total operating expenses	<u>7,387,309</u>	<u>6,438,936</u>	<u>(49,842)</u>	<u>13,776,403</u>
OPERATING INCOME (LOSS)	<u>2,162,971</u>	<u>(1,941,445)</u>	<u>-</u>	<u>221,526</u>

(Continued)

## WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

### COMBINING SCHEDULE—STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS (DEFICIT) INFORMATION YEAR ENDED JUNE 30, 2004

	HEPC Division	WVNET Division	Eliminations	Combined
NONOPERATING REVENUES (EXPENSES):				
State appropriations	\$ 39,679,630	\$ 2,071,019	\$ -	\$41,750,649
Investment income	96,827	17,774		114,601
Institutional debt service payments to Commission:				
Interest	7,308,528			7,308,528
Other	3,012,849			3,012,849
Interest on indebtedness	(9,558,578)	(23,391)		(9,581,969)
Student financial aid payments to institutions	(26,763,755)			(26,763,755)
Other payments to institutions	<u>(13,667,513)</u>			<u>(13,667,513)</u>
Net nonoperating revenues (expenses)	<u>107,988</u>	<u>2,065,402</u>	<u>-</u>	<u>2,173,390</u>
INCOME BEFORE OTHER REVENUES, EXPENSES, GAINS OR LOSSES	2,270,959	123,957		2,394,916
CAPITAL APPROPRIATIONS	10,000,000			10,000,000
UNAPPROPRIATED CAPITAL	<u>(17,506,041)</u>			<u>(17,506,041)</u>
(DECREASE) INCREASE IN NET ASSETS	(5,235,082)	123,957		(5,111,125)
NET ASSETS—Beginning of year	<u>1,682,461</u>	<u>3,222,341</u>		<u>4,904,802</u>
NET ASSETS (DEFICIT)—End of year	<u>\$ (3,552,621)</u>	<u>\$ 3,346,298</u>	<u>\$ -</u>	<u>\$ (206,323)</u>

(A) To eliminate inter-division receivables/payables

(B) To eliminate inter-division income/expense

(C) To reclass negative net assets invested in capital assets, net of related debt

(Concluded)

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

West Virginia Higher Education  
Policy Commission

We have audited the financial statements of the West Virginia Higher Education Policy Commission (the "Commission") as of and for the year ended June 30, 2004, and have issued our report thereon dated January 11, 2005, which contains a consistency paragraph for the change in reporting entity. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

### **Internal Control Over Financial Reporting**

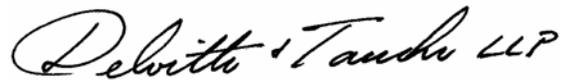
In planning and performing our audit, we considered the Commission's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the Commission's internal control over financial reporting and its operations that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operations of the internal control over financial reporting that, in our judgment, could adversely affect the Commission's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying schedule of findings and questioned costs as items 04-01 and 04-02.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe the reportable conditions items 04-01 and 04-02 described above are material weaknesses.

## Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Commission'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 or other matters that are required to be reported under *Government Auditing Standards*.

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

The image shows a handwritten signature in black ink that reads "Deloitte & Touche LLP". The signature is written in a cursive, flowing style.

January 11, 2005

# WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

## SCHEDULE OF FINDINGS AND RESPONSES YEAR ENDED JUNE 30, 2004

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Reference Number		Finding
04-01	<b>Criteria:</b>	The accounts payable detailed ledger of WVNET should agree to the accounts payable balance reported in the trial balance.
	<b>Condition:</b>	The accounts payable balance as reported in the detailed ledger of WVNET differed by a substantial amount when compared to the accounts payable balance reported in the trial balance at June 30, 2004.
	<b>Cause:</b>	A timely process to prevent or detect an out-of-balance condition between the accounts payable detailed ledger and the accounts payable balance reported in the trial balance does not exist.
	<b>Effect:</b>	The accounts payable balance reported in the trial balance was not supported by the accounts payable detailed ledger.
	<b>Recommendation:</b>	The Commission should revisit the established automated and manual reconciliation procedures between the accounts payable detailed ledger and the trial balance at WVNET.
	<b>Corrective Action Plan:</b>	The Commission will institute procedures and reviews, thereof, to correct this situation prior to June 30, 2005.
04-02	<b>Criteria:</b>	A reconciliation of the accounts receivable ledger of WVNET for payments received should occur timely.
	<b>Condition:</b>	The accounts receivable detailed ledger of WVNET included numerous invoices as unpaid that had actually already been paid.
	<b>Cause:</b>	A timely reconciliation of the accounts receivable ledger for payments received was not performed.
	<b>Effect:</b>	The accounts receivable detailed ledger included numerous invoices as unpaid that had actually been paid.
	<b>Recommendation:</b>	The Commission should revisit the established automated and manual reconciliation procedures between the accounts receivable detailed ledger and payments received at WVNET.
	<b>Corrective Action Plan:</b>	The Commission will institute procedures and reviews, thereof, to correct this situation prior to June 30, 2005.

# WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

## STATUS OF PRIOR YEAR FINDINGS YEAR ENDED JUNE 30, 2004

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**Finding 03-01:** The accounts receivable balance of WVNET as reported in the detailed ledger differed by a substantial amount when compared to the accounts receivable balance reported in the trial balance at June 30, 2003.

**Status:** The accounts receivable balance of WVNET as reported in the detailed ledger agreed to the accounts receivable balance reported in the trial balance at June 30, 2004.

**Finding 03-02:** The accounts receivable detailed ledger of WVNET included numerous invoices reported as being cancelled invoices that should not have been included in the detail.

**Status:** The accounts receivable detailed ledger of WVNET did not include numerous invoices reported as being cancelled, however, there were other errors which are reported on Finding 04-02.