West Virginia Higher Education Policy Commission

Financial Statements and Additional Information as of and for the Years Ended June 30, 2005 and 2004 and Independent Auditors' Reports

WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

TABLE OF CONTENTS

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INDEPENDENT AUDITORS' REPORT

To the West Virginia Higher Education
Policy Commission

We have audited the accompanying statements of net assets of the West Virginia Higher Education Policy Commission (the "Commission") as of June 30, 2005 and 2004, and the related statements of revenues, expenses and changes in net assets (deficit) and of cash flows for the years then ended. 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 audits.

We conducted our audits 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Commission's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide 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, 2005 and 2004 and the changes in net assets (deficit) and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages 2 to 11 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 audits were 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 audits of these 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 November 21, 2005, on our consideration of the Commission's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing, 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

November 21, 2005

West Virginia Higher Education Policy Commission

Management Discussion and Analysis
Fiscal Year 2005

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.

The following discussion and analysis of the Commission's financial statements provides an overview of its financial activities for the years ended June 30, 2005 and 2004 with a present focus on the current year 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

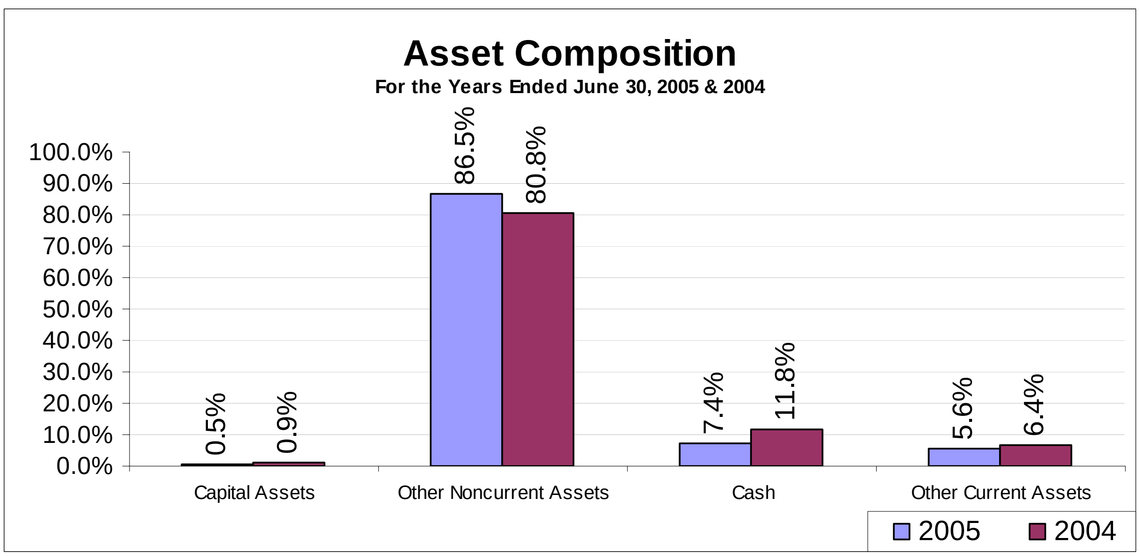
The Statement of Net Assets presents comparative data of the assets, liabilities, and net assets of the Commission as of June 30, 2005 and 2004. The Statement of Net Assets is a point of time financial statement. The purpose of the Statement of Net Assets is to present to the readers of the financial 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).

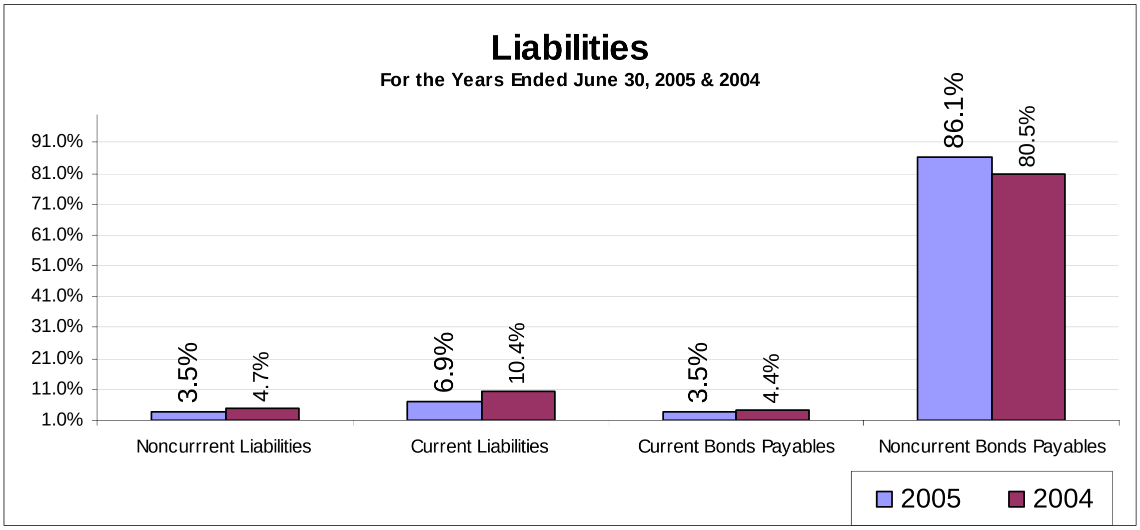
From the data presented, readers of the Statement of Net Assets are able to determine the assets available to continue the operations of the Commission. They are also able to determine how much the Commission owes vendors, employees and lending institutions. Finally, the Statement of Net Assets provides 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 land, 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, 2005 or 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, 2005	June 30, 2004
Assets:		
Current Assets	$ 50,506	$ 43,742
Other Noncurrent Assets	336,348	193,445
Capital Assets, net	1,884	2,158
Total Assets	$ 388,738	$ 239,345
Liabilities		
Current Liabilities	$ 40,708	$ 35,517
Noncurrent Liabilities	350,499	204,034
Total Liabilities	391,207	239,551
Net Assets (Deficit)		
Restricted – expendable	18,496	20,925
Unrestricted	(20,965)	(21,131)
Total Net Assets	(2,469)	(206)
Total Liabilities and Net Assets	$ 388,738	$ 239,345





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

- At June 30, 2005, 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 that were issued on behalf of the University and College Systems. Prior to fiscal year 2002, 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 2002. On the Statement of Net Assets as of June 30, 2005, a receivable has been recorded for institutional obligations totaling $174.6 million out of the total amount due from institutions of $175.7 million as compared to $191.9 million in debt including outstanding University and College System Bonds of $179.2 million plus deferred interest of $12.7 million, but not including bond premiums. This shortfall continues to be reflected as part of the deficit in the Net Assets invested in capital assets-net of related debt and will be allocated to certain institutions on an annual basis over the remaining term of the bonds. This allocation of debt to institutions results in a more equitable presentation of net assets for both the Commission and the institutions. As discussed later, the Commission debt for facilities issued in fiscal year 2005 is not allocated to the institutions as the funding will be forthcoming from excess Lottery proceeds.
- Total current assets of $50.5 million exceed total current liabilities of $40.7 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 at June 30, 2005 of $28.7 million compared to cash balances at June 30, 2004 of $28.3 million. This increase of $.4 million is primarily attributed to aggressive collection practices for sales and services of educational activities of outstanding prior year receivables.
    - Current receivables from the institutions total $9.5 million and $9.1 million as of June 30, 2005 and June 30, 2004, respectively. This receivable primarily represents the institutions current obligations for principal payments to be paid on the University and College system-wide bond obligations.
    - Current liabilities total $40.7 million and $35.5 million as of June 30, 2005 and June 30, 2004 respectively. $13.6 million related to the current principal portion of system-wide bond obligations at June 30, 2005 is up $3.1 million due to the sale of the 2004B Series Bonds compared to $10.5 million at June 30, 2004. $4.3 million in interest payable on the system debt at June 30, 2005 is up $2.2 million due to the sale of the 2004B Series Bonds compared to $2.1 million at June 30, 2004. $12.1 million in funding deposited for the PROMISE scholarship program in FY 2005 is up $10.3 million due to the supplemental Lottery transfer described above, compared to $1.8 million at June 30, 2004. The $8.6 million in amounts due to institutions at June 30, 2005 is up $7.8 mainly due to $5.2 million of special project money allocated to the institutions and $2.8 million of bond proceeds due to the institutions compared to $.8 million at June 30, 2004. As mentioned earlier, the unappropriated liability due the State is down $17.5 million at June 30, 2005 as the transfer was a one time legislative mandate to return capital funds.
- As of June 30, 2005 noncurrent assets total $338.2 million and noncurrent liabilities total $350.5 million. As of June 30, 2004, noncurrent assets totaled $195.6 and noncurrent liabilities totaled $204.0 million
    - The primary noncurrent asset is a receivable from the institutions primarily related to the University and College system-wide bond obligations which total $165.4 million at June 30, 2005 compared to $174.5 million at June 30, 2004, a decrease of $9.1 million paid on the principal of outstanding bonds.
    - The other major noncurrent asset is the investment of $156.0 million at June 30, 2005 which did not exist at June 30, 2004, and is attributed to the sale of $167.3 million of new bonds. The majority of the proceeds are still held by the trustee in the investment, and cash of $1.3 million.
    - The primary noncurrent liability represents the actual system-wide bonds outstanding, as further described in Note 8 to the financial statements. At June 30, 2005, noncurrent bonds payable totaled $336.7 million, an increase of $143.9 from $192.8 at June 30, 2004. This is attributed to the sale of $167.3 million of new bonds in FY 2005.

- Total net assets of the Commission were a deficit of $2.5 million as of June 30, 2005, which is a $2.3 million increase in the deficit over the prior year. The major components of net assets as of June 20, 2005 are as follows:
    - Funds restricted for sponsored projects total $5.1 million.
    - Funds restricted for scholarship programs total $8.5 million.
    - Funds restricted for capital projects total $4.4 million.

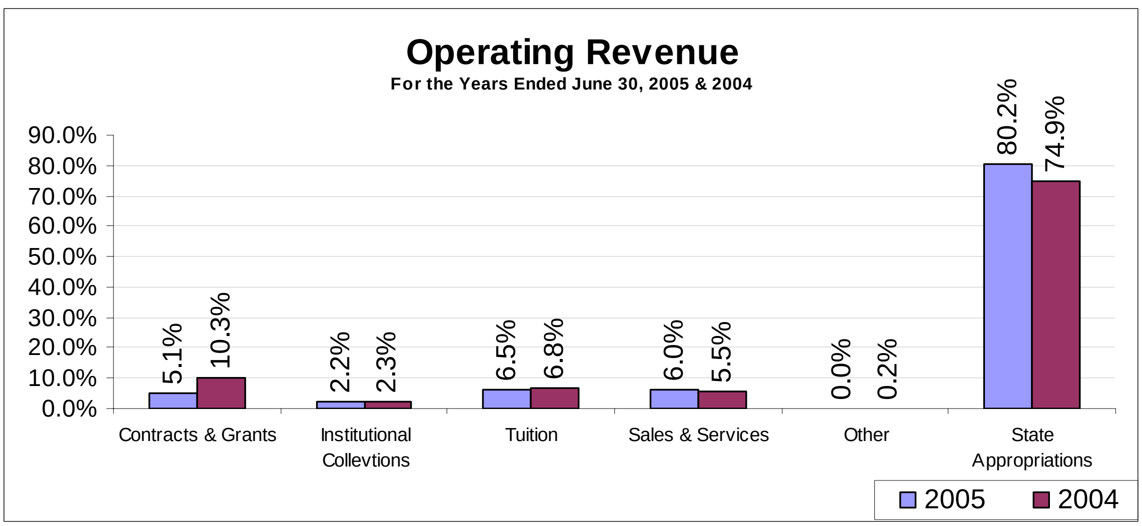
Statement of Revenues, Expenses and Changes in Net Assets

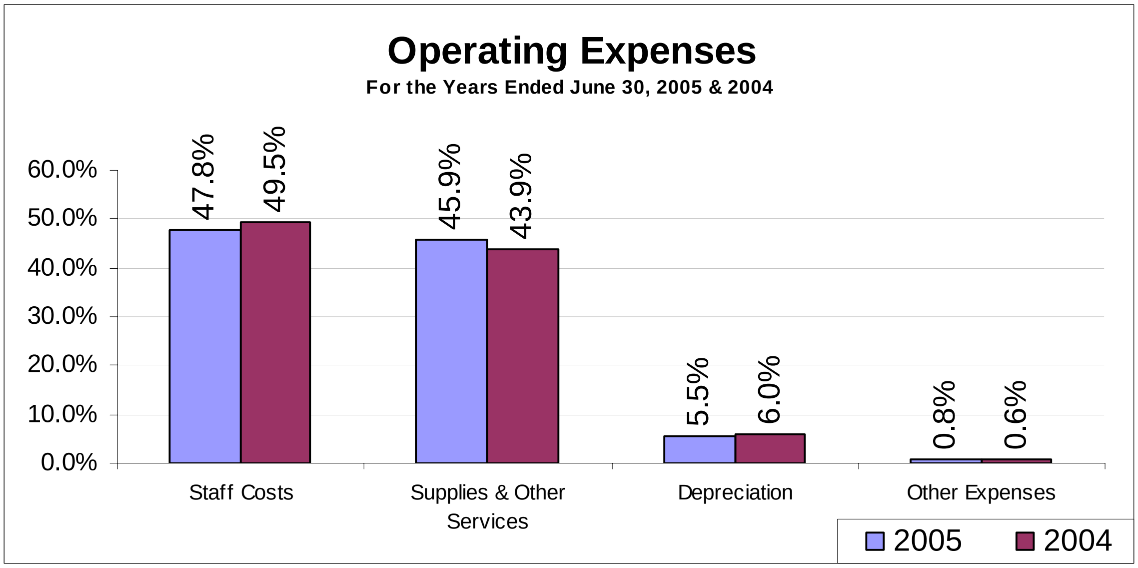
Changes in total net assets as presented on the Statement of Net Assets are based on the activity presented in the Statement of Revenues, Expenses, and Changes in Net Assets. The purpose of the statement is to present the revenues of the Commission, both operating and nonoperating, and the expenses of 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. Additional operating revenue comes from the sale of various services to public and private higher education institutions, public and private K-12, and other state government agencies. 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 2005	FY 2004
Operating Revenues	$ 11,673	$ 14,018
Operating Expenses	13,068	13,776
Operating Income	(1,395)	242
Net Nonoperating Revenues	13,968	2,153
Income Before Other Revenues, Expenses, Gains or Losses	12,573	2,395
Other Revenues, Expenses, Gains or Losses	(14,836)	(7,506)
Decrease in Net Assets	(2,263)	(5,111)
Net Assets (Deficit) - Beginning of Year	(206)	4,905
Net Assets (Deficit) - End of Year	$ (2,469)	$ (206)





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

- Operating revenues of the Commission totaled $11.7 in FY 2005 compared to $14.0 million in FY 2004. This is a decrease of $2.3 million that primarily is attributed to the reduction of Federal and State Grants caused by the separate reporting of the West Virginia Council for Community and Technical College Education beginning with the year ended June 30, 2005.
    - Fees collected from higher education institutions for the operations of the Commission and for special projects for higher education totaled $3.8 million at June 30, 2005 basically unchanged from June 30, 2004.
    - Other state, federal and local grants totaled $3.0 million in FY 2005 compared to $5.8 million in FY 2004. A decrease of $2.8 million is attributed as mentioned above to the separate reporting of the West Virginia Council for Community and Technical College Education. Various programs administered by the Commission include the TRIO program, National Science Foundation EPSCoR program, Veterans Administration, Improving Teaching Quality program.
- Operating expenses totaled $13.1 million in FY 2005 compared to $13.8 in FY 2004. The decrease of $.7 million is primarily attributed to the separate reporting of the West Virginia Council for Community and Technical College Education. Operating expenses consist primarily of staff salaries, benefits, and other operating expenses for Commission initiatives and various federal and state funded programs.
- Net nonoperating revenue totaled $14.0 million in FY 2005 compared to $2.2 million in FY 2004. The increase of $11.8 million is primarily attributed to lottery receipts for the 2004 Series B Bonds and additional state general revenue appropriations primarily for special projects, partially offset by additional interest expense.

  - State general revenue and lottery appropriations totaled $47.4 in FY 2005 compared to $41.8 million in FY 2004. An increase of $5.6 million. This increase is attributed to supplemental appropriations in FY 2005 of $5.6 million of Special Project dollars for various Commission institutional initiatives.
  - Pass-through expenditures for scholarships and financial aid totaled $26.9 million in FY 2005 compared to $26.8 million in FY 2004. Funding for these programs primarily comes from the West Virginia Lottery.
  - Payments for interest on indebtedness are offset by payments from the institutions for debt service totaling $10.6 million in FY 2005. This is compared to $10.3 million in FY 2004. A slight increase of .3 million is attributed to higher interest rates.
  - Investment income totaled $4.1 million in FY 2005 compared to $0.1 million in FY 2004. The increase of $4.0 million is attributed to investment earnings of the unexpended bond proceeds from the 2004 Series Bonds.
  - Other non-operating expenses totaled $4.4 million in FY 2005 compared to $13.7 million in FY 2004. The decrease of $9.3 million primarily is from the $5.6 million of Special Project state general revenue dollars that represent additional transfers to the institutions for special projects.
- There were no Capital Appropriations from State in FY 2005 compared to $10.0 million in FY 2004. The decrease of $10.0 million is attributed to the sale $167.3 million of the 2004 Series Bonds by the Commission. The Commission will receive $10.0 million per year commencing in FY 2005 through year 2034 of excess lottery revenues from the West Virginia Lottery Commission for payment of debt service.
- Capital Appropriations to Institutions totaled $7.0 million in FY 2005 as the Commission began funding various capital projects at the institutions in FY 2005 from the $10.0 million Capital allocation from the Legislature in FY 2004. The additional $3.0 million was retained by the Commission for debt service reserves.
- Transfer to the West Virginia Council for Community and Technical College Education. This is a result of Senate Bill 448 passed by the West Virginia Legislature effective July 1, 2004. Senate Bill 448 separated the community and technical college education responsibility from the Commission to the newly created Council. The transfer of $.8 million represented the assets and liabilities at June 30, 2004 allocated to the Council from the Commission.

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 2005	FY 2004
Cash Provided (Used In):		
Operating Activities	909	$ 803
Noncapital Financing Activities	26,528	(548)
Capital and Related Financing Activities	126,430	11,727
Investing Activities	(153,480)	1,204
Increase in Cash and Cash Equivalents	387	13,186
Cash and Cash Equivalents, beginning of year	28,305	15,119
Cash and Cash Equivalents, end of year	28,692	$ 28,305

Major items of note in the Cash Flow Statement include:

- Net Cash provided by operating activities in both FY 2005 and FY 2004 were comparable. Major variances from that reported on the Statement of Revenue, Expenses and Changes in Net Assets include depreciation expense, accruals for compensated absences and fluctuations in accounts payable and receivables.
- 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. As mentioned earlier, the Commission received supplemental state and lottery appropriations of $5.6 million of Special Project dollars and $10.9 million of Promise Scholarship dollars for expenditure in FY 2006.
- Net cash provided by Capital Financing Activities totaled $126.4 million in FY 2005 primarily due to the sale of the 2004 Series Bonds. Additional activity was the refunding and defeasance of outstanding University Series 1996 Bonds in the amount of $9.4 million with the proceed of the 2004 Series Bonds. The refinancing of the Series 1996 Bonds with a reduced interest rate will provide a savings of $.7 million to the State of West Virginia.
- Net cash used in Investing Activities totaled $153.5 million in FY 2005 compared to net cash provided by investing activities of $1.2 million in FY 2004. The increase of $154.7 million is primarily related to the 2004 Series Bond proceeds invested with FSA Capital Management Services LLC, the trustee at 2.83%.
- Total cash for FY 2005 year increased by $.4 million which is less then the FY 2004 increase of $13.2 million, but the overall cash position increased to a total of $28.7 million.

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 $.8 million, this deficit includes the $14.0 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 from the State for the Commission's operations was relatively the same in FY 2005 at $4.0 million compared to $4.1 million in FY 2004. Mandated State budget reductions account for the decrease of $0.1 million. For fiscal year 2006, fees from the institutions for the funding of Commission's operations was approximately $3.8 million and substantially unchanged from 2004. The decrease of $.2 million from FY 2005 is also from mandated State budget reductions. Departmental expenditure reductions in certain areas and the utilization of operational reserve funds have offset the budget reductions. For fiscal year 2007, all state agencies have being requested to submit a general revenue budget appropriation request at the current level as FY 2006. No budget reductions are anticipated. The Commission has submitted a number of improvement level requests to restore prior years lost funding that will be addressed in the calendar year 2007 Legislature.

WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

STATEMENTS OF NET ASSETS
AS OF JUNE 30, 2005 AND 2004

ASSETS	2005	2004
CURRENT ASSETS:		
Cash and cash equivalents	$ 28,692,823	$ 27,945,024
Investments		360,746
Appropriations due from Primary Government	9,036,705	2,462,386
Accounts receivable—net	1,501,684	3,864,731
Interest receivable	1,741,775	50,225
Prepaid expense	3,187	
Receivable from institutions—current portion	9,530,115	9,059,104
Total current assets	50,506,289	43,742,216
NONCURRENT ASSETS:		
Cash and cash equivalents	4,594,888	10,118,153
Investments	155,938,732	3,683,817
Receivable from institutions	166,202,954	175,333,069
Other assets	9,611,266	4,309,938
Investment in capital assets—net	1,883,886	2,158,186
Total noncurrent assets	338,231,726	195,603,163
TOTAL	$ 388,738,015	$ 239,345,379

(Continued)

WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

STATEMENTS OF NET ASSETS
AS OF JUNE 30, 2005 AND 2004

LIABILITIES AND NET ASSETS	2005	2004
CURRENT LIABILITIES:		
Accounts payable	$ 1,220,754	$ 1,560,963
Amounts due to institutions	8,646,604	787,850
Accrued liabilities	83,668	109,124
Unappropriated liability due to State		17,506,041
Deposits	12,124,798	1,836,507
Deferred revenue	58,035	306,114
Compensated absences—current portion	453,565	518,000
Interest payable	4,284,402	2,112,682
Bonds payable—current portion	13,625,000	10,535,000
Capital lease obligations	211,714	244,784
Total current liabilities	40,708,540	35,517,065
NONCURRENT LIABILITIES:		
Compensated absences	890,462	983,877
Deferred interest payable	12,740,535	9,879,201
Bonds payable	336,697,134	192,835,806
Capital lease obligations	170,584	335,753
Total noncurrent liabilities	350,498,715	204,034,637
Total liabilities	391,207,255	239,551,702
NET ASSETS (DEFICIT):		
Invested in capital assets—net of related debt		
Restricted for—		
Expendable:		
Scholarships	8,534,044	6,281,484
Sponsored projects	5,062,968	677,106
Capital projects	4,407,960	13,590,426
Debt service	335,513	360,746
Other	155,015	14,962
Total restricted expendable	18,495,500	20,924,724
Unrestricted	(20,964,740)	(21,131,047)
Total net assets (deficit)	(2,469,240)	(206,323)
TOTAL	$ 388,738,015	$ 239,345,379

See notes to financial statements. (Concluded)

WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS (DEFICIT) FOR THE YEARS ENDED JUNE 30, 2005 AND 2004

	2005	2004
OPERATING REVENUES:		
Fees from higher education institutions	$ 3,814,292	$ 3,776,718
Institutional collections	1,312,639	1,306,236
Contracts and grants:		
Federal	1,927,475	2,622,496
State	910,574	3,143,702
Local	153,332	
Sales and services of educational activities	3,556,015	3,041,747
Miscellaneous—net	(1,399)	127,530
Total operating revenues	11,672,928	14,018,429
OPERATING EXPENSES:		
Salaries and wages	5,162,194	5,496,009
Benefits	1,090,024	1,319,133
Supplies and other services	5,999,011	6,053,785
Utilities	101,065	86,373
Depreciation	715,476	821,103
Total operating expenses	13,067,770	13,776,403
OPERATING INCOME (LOSS)	$ (1,394,842)	$ 242,026

(Continued)

WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS (DEFICIT) FOR THE YEARS ENDED JUNE 30, 2005 AND 2004

	2005	2004
NONOPERATING REVENUES (EXPENSES):		
State appropriations	$ 47,383,042	$ 41,750,649
Investment income	4,149,933	114,601
Institutional debt service payments to Commission:		
Interest	7,783,498	7,308,528
Other	2,829,248	3,012,849
Interest on indebtedness	(16,876,245)	(9,581,969)
Student financial aid payments to institutions	(26,858,152)	(26,763,755)
Other payments to institutions	(4,438,796)	(13,667,513)
Other nonoperating expenses—net	(4,554)	(20,500)
Net nonoperating revenues	13,967,974	2,152,890
INCOME BEFORE OTHER REVENUES, EXPENSES, GAINS, OR LOSSES	12,573,132	2,394,916
CAPITAL APPROPRIATIONS FROM STATE		10,000,000
CAPITAL APPROPRIATIONS TO INSTITUTIONS	(7,012,000)	
UNAPPROPRIATED CAPITAL		(17,506,041)
BOND PROCEEDS TO INSTITUTIONS	(6,983,346)	
TRANSFER TO THE WEST VIRGINIA COUNCIL FOR COMMUNITY AND TECHNICAL COLLEGE EDUCATION	(840,703)	
DECREASE IN NET ASSETS	(2,262,917)	(5,111,125)
NET ASSETS (DEFICIT)—Beginning of year	(206,323)	4,904,802
NET DEFICIT—End of year	$ (2,469,240)	$ (206,323)

See notes to financial statements.

(Concluded)

WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2005 AND 2004

	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES:		
Fees and reimbursements from higher education institutions	$ 5,679,868	$ 6,772,650
Institutional collections	1,810,002	1,183,199
Contracts and grants	2,991,381	5,766,198
Payments to and on behalf of employees	(6,695,480)	(6,976,611)
Payments to suppliers	(6,387,730)	(9,014,593)
Payments to utilities	(101,065)	(86,373)
Sales and service of educational activities	3,613,322	3,030,914
Other payments—net	(1,399)	128,165
Net cash provided by operating activities	908,899	803,549
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:		
State appropriations	40,808,723	42,232,170
Receipts from fudiciary governmental entities	43,609,231	22,264,249
Disbursements to fudiciary governmental entities	(33,320,940)	(25,954,437)
Payments to institutions	(23,728,193)	(39,090,011)
Transfer of assets to West Virginia Council for Community and Technical College Education	(840,703)	
Net cash provided by (used in) noncapital financing activities	26,528,118	(548,029)
CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES:		
Capital appropriations (unappropriations)	(17,506,041)	10,000,000
Capital projects proceeds to institutions	(7,012,000)	
Proceeds from bond issuance—net	173,278,720	100,009,292
Payment of bond issuance costs	(6,018,720)	(4,814,292)
Institutional receipts for debt service	19,649,850	18,570,804
Purchases of capital assets	(109,579)	(128,799)
Principal paid on bonds	(16,245,000)	(107,850,000)
Principal paid on defeased bonds	(9,365,000)	
Interest paid on bonds	(11,828,742)	(7,354,493)
Principal paid on leases	(244,390)	(161,861)
Interest paid on leases	(14,448)	(23,391)
Capital projects construction bond payments	(7,233,346)	(181,789)
Capital loans to institutions	(375,000)	(475,000)
Capital loan repayments from institutions	247,000	199,500
Decrease in noncurrent cash and cash equivalents	9,207,082	7,621,222
Net cash provided by capital financing activities	126,430,386	15,411,193
CASH FLOWS FROM INVESTING ACTIVITIES:		
Receipts from investment income and sales	2,819,128	262,516
Purchases of investments	(155,938,732)	(3,102,721)
Net cash provided by (used in) investing activities	(153,119,604)	(2,840,205)
INCREASE IN CASH AND CASH EQUIVALENTS	747,799	12,826,508
CASH AND CASH EQUIVALENTS—Beginning of year	27,945,024	15,118,516
CASH AND CASH EQUIVALENTS—End of year	$ 28,692,823	$ 27,945,024

(Continued)

WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2005 AND 2004

	2005	2004
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating income (loss)	$ (1,394,842)	$ 242,026
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation expense	715,476	821,103
Changes in assets and liabilities:		
Accounts receivables—net	2,362,939	(163,384)
Prepaid expenses	(3,187)	
Accounts payable	(340,102)	71,520
Accrued liabilities	(25,456)	(97,285)
Compensated absences	(157,850)	(47,762)
Deferred revenue	(248,079)	(22,669)
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 908,899	$ 803,549

See notes to financial statements. (Concluded)

WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

NOTES TO FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED JUNE 30, 2005 AND 2004

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 encompassed all West Virginia public higher education prior to Senate Bill No. 448 ("S.B. 448")), 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 includes the accounts of West Virginia Network for Educational Telecommuting ("WVNET"). 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, the Commission, and the West Virginia Council for Community and Technical College Education (the "Council") comprise 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, S.B. 448 was passed. S.B. 448 created 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, effective July 1, 2004, the Council was separated from the Commission with a transfer of $840,703 of net assets.

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 and the Council, 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—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* 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 to 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, 2005 and 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, 2005 and 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"). The State Treasurer's Office is permitted by West Virginia Code 12-1-12A to invest up to $125 million in overnight repurchase agreements. 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 in accordance with West Virginia Code, policies set by the IMB, provisions of bond indentures, and the trust agreements when applicable. 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.

The IMB maintains the Consolidated Fund investment fund which consists of five investment pools and participant directed accounts, in which the state and local governmental agencies invest. The IMB also manages other investment pools which include amounts invested by pension funds of the State, as well as certain operating funds of the Workers' Compensation Fund and other funds. These pools have been structured as multiparticipant variable net asset funds to reduce risk and offer investment liquidity diversification to the Fund participants. Funds not required to meet immediate disbursement needs are invested for longer periods. A more detailed discussion of the IMB's investment operations pool can be found in the IMB's annual report. A copy of the IMB's annual report can be obtained from the following address: 500 Virginia Street East, Suite 200, Charleston, WV 25301 or http://www.wvimb.org.

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. 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.

Permissible investments for all agencies include those guaranteed by the United States of America, its agencies and instrumentalities (U.S. Government obligations); equities; corporate debt obligations, including commercial paper, which meet certain ratings; certain money market funds; investment agreements with certain financial institutions; repurchase agreements; state and local government securities (SLGS); and other investments. Other investments consist primarily of single family mortgage loans and collateralized mortgage obligations. SLGS are direct obligations of the U.S. Government, issued to state and local government entities to provide those governments with required cash flows at yields which do not exceed IRS arbitrage limits.

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 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 percent 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 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.

- *Other revenues*—Other revenues consist primarily of capital grants and gifts.

- *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.

Risk and Uncertainties—Investments are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain securities, it is reasonably possible that changes in risk and values will occur in the near term and that such changes could materially affect the amounts reported in the financial statements.

Recent Statements Issued by the Government Accounting Standards Board—The GASB has 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.

The GASB has also issued Statement No. 47, *Accounting for Termination Benefits*, effective for fiscal years beginning after June 15, 2005. However, for termination benefits that affect defined benefit postemployment benefits other than pensions, GASB Statement No. 47 should be implemented simultaneously with GASB Statement No. 45. This statement provides recognition and measurement guidance related to benefits provided to employees that are terminated. The Commission has not yet determined the effect, if any, that the adoption of GASB Statement No. 47 may have on its financial statements.

Reclassifications—Certain items in the prior year financial statements have been reclassified to conform with the current year classifications.

3. CASH AND CASH EQUIVALENTS

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

	2005		
	Current	**Noncurrent**	**Total**
Cash on deposit with the State Treasurer	$28,601,077	$ 3,000,000	$31,601,077
Cash on deposit with Municipal Bond Commission	91,746	335,513	427,259
Cash on deposit with Trustee		1,259,375	1,259,375
	$28,692,823	$ 4,594,888	$33,287,711

	2004		
	Current	**Noncurrent**	**Total**
Cash on deposit with the State Treasurer	$27,945,024	$10,118,153	$38,063,177

Cash shown above as held by the Municipal Bond Commission or Trustee represents various project revenue, debt service, and other repair and replacement reserve funds required to be escrowed by various bond trust indentures.

Cash on deposit with the State Treasurer as of June 30, 2005 is comprised of the following investment pools.

Cash Liquidity

Credit risk

The IMB limits the exposure to credit risk in the Cash Liquidity pool by requiring all corporate bonds to be rated AA or higher. Commercial paper must be rated A1 by Standard & Poor's and P1 by Moody's. Additionally, the pool must have at least 15% of its assets in United States Treasury issues.

The following table provides information on the weighted average credit ratings of the Cash Liquidity pool's investments.

Security Type	Moody's	S&P	Carrying Value	Percent of Assets
Commercial paper	P1	A-1	$ 598,241,394	37.9%
U. S. Treasury bills	Aaa	AAA	259,397,648	16.4%
Corporate notes	Aaa	AAA	155,559,323	9.9%
Certificates of deposit	P1	A-1	152,998,937	9.7%
Agency bonds	Aaa	AAA	147,955,465	9.4%
Agency discount notes	P1	A-1	119,564,248	7.6%
Money market funds	Aaa	AAA	4,241,278	0.3%
Total rated investments			$1,437,998,293	91.2%

Unrated securities include repurchase agreements of $141,050,000. Acceptable collateral for the repurchase agreements include U. S. Treasury and government agency securities, all of which carry the highest credit rating.

The West Virginia Higher Education Policy Commission ownership represents 1.17% of these amounts held by IMB.

Concentration of credit risk

West Virginia statutes prohibit the Cash Liquidity pool from investing more than 5% of its assets in securities issued by a single private corporation or association. At June 30, 2005, the pool did not have investments in any one private corporation or association that represented more than 5% of assets.

Custodial credit risk

At June 30, 2005, the Cash Liquidity pool held no securities that were subject to custodial credit risk. Repurchase agreements are collateralized at 102% and the collateral is held in the name of the IMB. Securities lending collateral that is reported in the Statement of Assets and Liabilities is invested in the lending agent's money market fund.

Interest rate risk

The weighted average maturity of the investments of the Cash Liquidity pool cannot exceed 60 days. The maturity of floating rate notes is assumed to be the next interest rate reset date. The following table provides the weighted average maturities (WAM) for the various asset types in the Cash Liquidity pool.

Security Type	Carrying Value	WAM
Commercial paper	$ 598,241,394	49
U. S. Treasury bills	259,397,648	30
Corporate notes	155,559,323	53
Certificates of deposit	152,998,937	42
Agency bonds	147,955,465	88
Repurchase agreements	141,050,000	1
Agency discount notes	119,564,248	52
Money market funds	4,241,278	1
Total assets	$ 1,579,008,293	45

Foreign currency risk

The Cash Liquidity pool has no securities that are subject to foreign currency risk.

<u>Government Money Market</u>

Credit risk

The IMB limits the exposure to credit risk in the Government Money Market pool by limiting the pool to U. S. Treasury issues, U. S. government agency issues, money market funds investing in U. S. Treasury issues and U. S. government agency issues, and repurchase agreements collateralized by U. S. Treasury issues and U. S. government agency issues. None of the government agency issues held by the pool have the explicit guarantee of the U. S. Treasury; however, they are all rated Aaa by Moody's and AAA by Standard & Poor's. Agency discount notes held by the pool are rated P1 by Moody's and A-1 by Standard & Poor's.

The West Virginia Higher Education Policy Commission ownership represents .39% of these amounts held by IMB.

Concentration of credit risk

West Virginia statutes prohibit the Government Money Market pool from investing more than 5% of its assets in securities issued by a single private corporation or association. At June 30, 2005, the pool did not have investments in any one private corporation or association that represented more than 5% of assets.

Custodial credit risk

At June 30, 2005, the Government Money Market pool held no securities that were subject to custodial credit risk. Repurchase agreements are collateralized at 102% and the collateral is held in the name of the IMB. Securities lending collateral that is reported in the Statement of Assets and Liabilities is invested in the lending agent's money market fund.

Interest rate risk

The weighted average maturity of the investments of the Government Money Market pool cannot exceed 60 days. The maturity of floating rate notes is assumed to be the next interest rate reset date. The following table provides the weighted average maturities (WAM) for the various asset types in the Government Money Market pool.

Security Type	Carrying Value	WAM (days)
Agency discount notes	$ 46,409,362	32
Agency bonds	42,571,144	75
Repurchase agreements	39,950,000	1
U. S. Treasury bills	24,903,836	48
Money market funds	985,190	1
Total assets	$ 154,819,532	38

Foreign currency risk

The Government Money Market pool has no securities that are subject to foreign currency risk.

<u>Enhanced Yield</u>

Credit risk

The IMB limits the exposure to credit risk in the Enhanced Yield pool by requiring all corporate bonds to be rated A or higher. Commercial paper must be rated A1 by Standard & Poor's and P1 by Moody's. Additionally, the pool must have at least 15% of its assets in United States Treasury issues.

The following table provides information on the weighted average credit ratings of the Enhanced Yield pool's investments.

Security Type	Moody's	S&P	Fair Value	Percent of Assets
Corporate notes	A	AA	$ 81,631,581	30.0%
Agency bonds	Aaa	AAA	69,203,277	25.5%
U. S. Treasury notes	Aaa	AAA	66,466,539	24.5%
Corporate asset backed securities	Aaa	AAA	49,990,408	18.4%
Total rated investments			$ 267,291,805	98.4%

Unrated securities include repurchase agreements of $4,362,262. Acceptable collateral for the repurchase agreements include U. S. Treasury and government agency securities, all of which carry the highest credit rating.

The West Virginia Higher Education Policy Commission ownership represents 1.83% of these amounts held by IMB.

Concentration of credit risk

West Virginia statutes prohibit the Enhanced Yield pool from investing more than 5% of its assets in securities issued by a single private corporation or association. At June 30, 2005, the pool did not have investments in any one private corporation or association that represented more than 5% of assets.

Custodial credit risk

At June 30, 2005, the Enhanced Yield pool held no securities that were subject to custodial credit risk. Repurchase agreements are collateralized at 102% and the collateral is held in the name of the IMB. Securities lending collateral that is reported in the Statement of Assets and Liabilities is invested in the lending agent's money market fund.

Interest rate risk

The weighted average maturity of the investments of the Enhanced Yield pool cannot exceed two years. The maturity of floating rate notes is assumed to be the next interest rate reset date. The following table provides the weighted average maturities (WAM) for the various asset types in the Enhanced Yield pool.

Security Type	Fair Value	WAM (years)
Corporate notes	$ 81,631,581	1.7
Agency bonds	69,203,277	1.9
U. S. Treasury notes	66,466,539	2.3
Corporate asset backed securities	49,990,408	1.1
Repurchase agreement	4,362,262	0.0
Total assets	$ 271,654,067	1.7

Foreign currency risk

The Enhanced Yield pool has no securities that are subject to foreign currency risk.

<u>Cash in Bank with Trustee</u>

J.P. Morgan Trust Company

Cash and cash equivalents invested with J.P Morgan Trust Company are invested in a US Government Money Market Fund and a US Treasury Securities Money Market Fund. The US Government Money Market Fund invests in US Government Agencies, US Treasuries, and Repurchases Agreements. This fund is rated AAAm by Standard and Poor's and Aaa by Moody's. The carrying value at June 30, 2005 is $1,128,369. The US Treasury Securities Money Market Fund invests in US Treasuries. This fund is rated AAAm-G by Standard and Poor's and Aaa by Moody's. The carrying value at June 30, 2005 is $131,006. These funds have no significant custodial credit risk or interest rate risk. These funds are not exposed to a concentration of credit risk nor any foreign currency risk.

FSA Capital Management Services LLC

A concentration of credit risk exists as this fund represents greater then 5% of total investments.

4. INVESTMENTS

The composition of investments was as follows at June 30, 2005:

	Noncurrent
Guaranteed Investment Contract	$155,938,732

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

	Current	Noncurrent	Total
Municipal Bond Commission	$ 360,746	$3,683,817	$4,044,563

Investments with FSA Capital Management Services LLC, a subsidiary of FSA Incorporated have a rating of AAA by Standard and Poor's and Aaa by Moody's. HEPC has an FSA Guaranteed Investment Contract ("GIC") with a fixed rate of interest of 2.83%. The carrying value of this investment at June 30, 2005 is $155,938,732 and is restricted by the bond indenture. This fund has no significant custodial risk or interest rate risk and is not exposed to any foreign currency risk.

5. ACCOUNTS RECEIVABLE

Accounts receivable were as follows at June 30:

	2005	2004
Student receivables—net of allowance for doubtful accounts of $1,383,560 and $648,504	$ 355,572	$ 309,576
Grants and contracts receivable	67,347	61,712
Due from higher education institutions	509,010	2,765,494
Other accounts receivable	569,755	727,949
	$1,501,684	$3,864,731

6. CAPITAL ASSETS

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

2005	Beginning Balance	CTC Transfers	Additions	Reductions	Ending Balance
Capital assets not being depreciated—					
Land	$ -	$ -	$ 290,000	$ -	$ 290,000
Total capital assets not being depreciated	$ -	$ -	$ 290,000	$ -	$ 290,000
Other capital assets:					
Buildings	$ -	$ -	$ 35,000	$ -	$ 35,000
Equipment	9,335,686	(38,393)	74,579	(3,327)	9,368,545
Leased equipment	1,163,360		46,151		1,209,511
Total other capital assets	10,499,046	(38,393)	155,730	(3,327)	10,613,056
Less accumulated depreciation for:					
Buildings			8,050		8,050
Equipment	8,002,422	(34,865)	707,426	(2,301)	8,672,682
Leased equipment	338,438				338,438
Total accumulated depreciation	8,340,860	(34,865)	715,476	(2,301)	9,019,170
Other capital assets—net	$ 2,158,186	$ (3,528)	$(559,746)	$ (1,026)	$ 1,593,886
Capital asset summary:					
Capital assets not being depreciated	$ -	$ -	$ 290,000	$ -	$ 290,000
Other capital assets	10,499,046	(38,393)	155,730	(3,327)	10,613,056
Total cost of capital assets	10,499,046	(38,393)	445,730	(3,327)	10,903,056
Less accumulated depreciation	8,340,860	(34,865)	715,476	(2,301)	9,019,170
Capital assets—net	$ 2,158,186	$ (3,528)	$(269,746)	$ (1,026)	$ 1,883,886

2004	Beginning Balance	Additions	Reductions	Ending Balance
Capital assets:				
Equipment	$ 9,479,414	$ 128,799	$(272,527)	$ 9,335,686
Leased equipment	960,406	202,954		1,163,360
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	210,857	127,581		338,438
Total accumulated depreciation	7,771,784	821,103	(252,027)	8,340,860
Capital assets—net	$ 2,668,036	$(489,350)	$ (20,500)	$ 2,158,186

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 years ended June 30:

2005	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Bonds payable	$203,370,806	$173,278,720	$ (26,327,392)	$350,322,134	$13,625,000
Capital lease obligations	580,537	46,151	(244,390)	382,298	211,714
Other long-term liabilities:					
Accrued compensated absences	1,501,877		(157,850)	1,344,027	453,565
Deferred interest payable	9,879,201	2,861,334		12,740,535	
Total long-term liabilities	$215,332,421	$176,186,205	$ (26,729,632)	$364,788,994	

2004	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
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	244,784
Other long-term liabilities:					
Accrued compensated absences	1,549,639		(47,762)	1,501,877	518,000
Deferred interest payable	7,183,831	2,695,370		9,879,201	
Total long-term liabilities	$220,988,781	$102,288,262	$(107,944,622)	$215,332,421	

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 2004 Series B Higher Education Facilities Bonds were issued in August 2004 under the provisions of the Code of West Virginia, 1931, as amended, particularly Chapters 13 and 18. These bonds were issued to provide funds for capital improvements at institutions of higher education throughout the State's universities and colleges. In addition the 2004 Series B Bonds provided funding for a refinancing of a portion of the Series 1996 Bonds outstanding principal amount of $9,365,000. The amount refinanced was $9,615,000 and with the reduced interest rates will provide a total cash savings of $738,550. The economic gain of the refinancing was $574,486.

Bonds payable consisted of the following at June 30:

	Maximum Interest Rate	Original Range of Annual Principal Installment Due	Principal Amount Outstanding	
			2005	2004
2004 Series B Higher Ed Facilities Bonds, due through 2034	6.00%	$ 2,680,000 to 9,520,000	$ 161,550,000	$ -
2003 Series A College Facilities Bonds, due through 2012	5.00%	2,325,000 to 2,690,000	16,200,000	18,525,000
2003 Series A University Facilities Bonds, due through 2012	5.00%	5,740,000 to 7,875,000	48,095,000	53,835,000
Series 1996 University System Bonds, due through 2006	5.75%	630,000 to 1,185,000	690,000	10,715,000
Series 1997 University System Bonds, due through 2027	5.25%	255,000 to 795,000	10,875,000	11,145,000
Series 1998 University System Bonds, due through 2028	5.25%	1,065,000 to 3,625,000	49,910,000	51,020,000
Series 2000A University System Bonds, due through 2031	6.26%	Zero to 3,263,864	36,590,868	36,590,868
Series 2000B University System Bonds, due through 2025	5.96%	210,000 to 625,000	8,255,000	8,475,000
Series 1997 College System Bonds, due through 2027	5.25%	200,000 to 625,000	8,545,000	8,755,000
			340,710,868	199,060,868
Add Bond premium			9,611,266	4,309,938
			$ 350,322,134	$ 203,370,806

A summary of the annual aggregate payments for years subsequent to June 30, 2005 is as follows:

Year Ending June 30	Principal	Interest	Total
2006	$ 13,625,000	$ 14,870,900	$ 28,495,900
2007	14,165,000	14,287,410	28,452,410
2008	14,630,000	13,791,573	28,421,573
2009	15,285,000	13,103,462	28,388,462
2010	15,930,000	12,418,595	28,348,595
2011–2015	64,066,360	63,049,813	127,116,173
2016–2020	52,360,672	62,902,996	115,263,668
2021–2025	59,281,816	54,800,849	114,082,665
2026–2030	54,898,108	43,523,982	98,422,090
2031–2034	36,468,912	10,320,338	46,789,250
	$340,710,868	$303,069,918	$643,780,786

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:

	Interest Rate	Principal Amount Outstanding 2005	Principal Amount Outstanding 2004
JP Morgan, Computer Equipment	2.28%	$ 114,462	$ 181,082
JP Morgan, Computer Equipment	3.12%	181,830	271,402
JP Morgan, Modem	2.13%	27,082	70,374
Document Solutions, Xerox Copiers and Printers	9.25–12.50%	58,924	23,284
JP Morgan, SP Upgrade	3.97%		34,395
		$ 382,298	$ 580,537

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, 2005 is a follows:

Year Ending June 30	Principal	Interest	Total
2006	$ 211,714	$ 9,798	$ 221,512
2007	145,189	3,280	148,469
2008	25,395	126	25,521
			395,502
Less interest			(13,204)
			$ 382,298

10. COMPENSATED ABSENCES LIABILITY

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

	2005	2004
Health and life insurance	$ 506,426	$ 645,648
Accrued vacation liability	605,594	657,112
Current retirees' health insurance	232,007	199,117
	$ 1,344,027	$ 1,501,877

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 years ended June 30, 2005 and 2004, the amount paid by the Commission for extended health or life insurance coverage retirement benefits totaled $24,364 and $76,893. As of June 30, 2005 and 2004, there were 5 and 12 retirees, respectively, currently receiving these benefits.

11. UNRESTRICTED NET ASSETS

The Commission did not have any designated net assets as of June 30, 2005 or 2004.

12. 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, 2005, one employee was enrolled in the new Educators Money 401(a) basic retirement plan and no employees were enrolled as of June 30, 2004.

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 percent of each enrolled employee's total annual salary for the years ended June 30, 2005 and 2004. Required employee contributions were at the rate of 6 percent of total annual salary in both 2005 and 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 percent 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, 2005 were $66,166, which consisted of $47,261 from the Commission and $18,904 from covered employees. 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 years ended June 30, 2003 were $93,090, which consisted of $66,493 from the Commission and $26,597 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 and Educators Money are defined contribution benefit plans in which benefits are based solely upon amounts contributed plus investment earnings. Employees who elect to participate in these plans are required to make a contribution equal to 6 percent of total annual compensation. The Commission matches the employees' 6 percent contribution. Contributions are immediately and fully vested. In addition, employees may elect to make additional contributions to TIAA-CREF and Educators Money which are not matched by the Commission.

Total contributions to the TIAA-CREF for the years ended June 30, 2005 were $560,800 which consisted of $280,400 from the Commission and $280,400, from covered employees. Total contributions to the TIAA-CREF for the years 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 Educators Money for the year ended June 30, 2005 were $8,422 which consisted of $4,211 from the Commission and $4,211 from covered employees.

The Commission's total payroll for the years ended June 30, 2005 and 2004 was $5,109,267 and $5,817,650, respectively. Total covered employees' salaries in the STRS, TIAA-CREF and Educators Money were $315,076 and $385,462, $4,672,340, and $5,289,416, $70,178, and $0, respectively, in 2005 and 2004, respectively.

13. OPERATING LEASES

Future annual minimum lease payments on operating leases for years subsequent to June 30, 2005 are as follows:

Year Ending June 30	
2006	$ 357,062
2007	362,770
2008	367,301
2009	371,841
2010	124,452
	$ 1,583,426

Total rent expense for the years ended June 30, 2005 and 2004 was $353,204 and $384,905, respectively.

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.

14. 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.

15. 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 years 2005 and 2004, approximately $3,400,000 and $3,000,000, respectively, 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.

16. NATURAL CLASSIFICATIONS WITH FUNCTIONAL CLASSIFICATIONS

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

2005	Salaries and Wages	Benefits	Supplies and Other Services	Utilities	Depreciation	Total
General institutional support	$5,162,194	$1,090,024	$5,999,011	$ -	$ -	$12,251,229
Administration, operations and maintenance of plant				101,065		101,065
Depreciation					715,476	715,476
Total	$5,162,194	$1,090,024	$5,999,011	$101,065	$715,476	$13,067,770

2004	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	$5,496,009	$1,319,133	$6,053,785	$ 86,373	$821,103	$13,776,403

* * * * * *

ADDITIONAL INFORMATION

WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

COMBINING SCHEDULE—STATEMENT OF NET ASSETS INFORMATION
AS OF JUNE 30, 2005 (WITH COMPARATIVE TOTALS FOR 2004)

	2005					2004
ASSETS	**HEPC Division**	**WVNET Division**	**Eliminations**		**Combined**	**Total**
CURRENT ASSETS:						
Cash and cash equivalents	$ 25,091,939	$ 3,600,884	$ -		$ 28,692,823	$ 28,305,769
Appropriations due from Primary Government	9,036,705				9,036,705	2,462,386
Accounts receivable—net	731,034	771,861	(1,211)	(A)	1,501,684	3,864,731
Interest receivable	1,732,904	8,871			1,741,775	50,225
Prepaid expense		3,187			3,187	
Receivable from institutions—current portion	9,530,115				9,530,115	9,059,104
Total current assets	46,122,697	4,384,803	(1,211)		50,506,289	43,742,215
NONCURRENT ASSETS:						
Cash and cash equivalents	4,594,888				4,594,888	13,801,970
Investments	155,938,732				155,938,732	
Receivable from institutions	166,202,954				166,202,954	175,333,070
Other assets	9,611,266				9,611,266	4,309,938
Investment in capital assets—net	418,951	1,464,935			1,883,886	2,158,186
Total noncurrent assets	336,766,791	1,464,935	-		338,231,726	195,603,164
TOTAL	$ 382,889,488	$ 5,849,738	$ (1,211)		$ 388,738,015	$ 239,345,379

(Continued)

WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

COMBINING SCHEDULE—STATEMENT OF NET ASSETS INFORMATION
AS OF JUNE 30, 2005 (WITH COMPARATIVE TOTALS FOR 2004)

	2005					2004
LIABILITIES	**HEPC Division**	**WVNET Division**	**Eliminations**		**Combined**	**Total**
CURRENT LIABILITIES:						
Accounts payable	$ 417,349	$ 804,616	$ (1,211)	(A)	$ 1,220,754	$ 1,560,963
Amounts due to institutions	8,646,604				8,646,604	787,850
Accrued liabilities	83,158	510			83,668	109,124
Unappropriated liability due to State						17,506,041
Deposits	12,124,798				12,124,798	1,836,507
Deferred revenue		58,035			58,035	306,114
Compensated absences—current portion	240,661	212,904			453,565	518,000
Interest payable	4,284,402				4,284,402	2,112,682
Bonds payable—current portion	13,625,000				13,625,000	10,535,000
Capital lease obligation		211,714			211,714	244,784
Total current liabilities	39,421,972	1,287,779	(1,211)		40,708,540	35,517,065
NONCURRENT LIABILITIES:						
Compensated absences	504,513	385,949			890,462	983,877
Deferred interest payable	12,740,535				12,740,535	9,879,201
Bonds payable	336,697,134				336,697,134	192,835,806
Capital lease obligation		170,584			170,584	335,753
Total noncurrent liabilities	349,942,182	556,533	-		350,498,715	204,034,637
Total liabilities	389,364,154	1,844,312	(1,211)		391,207,255	239,551,702
NET ASSETS (DEFICIT):						
Invested in capital assets	(21,248,554)	1,082,637	20,165,917	(C)		
Restricted for—						
Expendable:						
Scholarships	8,534,044				8,534,044	6,281,484
Sponsored projects	5,062,968				5,062,968	677,106
Capital projects	4,407,960				4,407,960	13,590,426
Debt service	335,513				335,513	360,746
Other	155,015				155,015	14,962
Total restricted expendable	18,495,500	-	-		18,495,500	20,924,724
Unrestricted	(3,721,612)	2,922,789	(20,165,917)	(C)	(20,964,740)	(21,131,047)
Total net assets (deficit)	(6,474,666)	4,005,426	-		(2,469,240)	(206,323)
TOTAL	$ 382,889,488	$ 5,849,738	$ (1,211)		$ 388,738,015	$ 239,345,379

(Concluded)

(A) To eliminate inter-division receivables/payables

(C) To reclass negative net assets invested in capital assets net of related debt to unrestricted net assets (deficit)

WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

COMBINING SCHEDULE—STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS (DEFICIT) INFORMATION
FOR THE YEAR ENDED JUNE 30, 2005 (WITH COMPARATIVE TOTALS FOR 2004)

	2005					2004
	HEPC Division	WVNET Division	Eliminations		Combined	Total
OPERATING REVENUES:						
Fees from higher education institutions	$3,814,292	$ -	$ -		$ 3,814,292	$ 3,776,718
Institutional collections		1,312,639			1,312,639	1,306,236
Contracts and grants:						
Federal	1,927,475				1,927,475	2,622,496
State	910,574				910,574	3,143,702
Local		153,332			153,332	
Sales and services of educational activities		3,615,825	(59,810)	(B)	3,556,015	3,041,747
Miscellaneous—net	(101,065)	99,666			(1,399)	127,530
Total operating revenues	6,551,276	5,181,462	(59,810)		11,672,928	14,018,429
OPERATING EXPENSES:						
Salaries and wages	2,956,150	2,206,044		(B)	5,162,194	5,496,009
Benefits	540,148	549,876			1,090,024	1,319,133
Supplies and other services	3,039,848	3,018,973	(59,810)		5,999,011	6,053,785
Utilities		101,065			101,065	86,373
Depreciation	78,807	636,669			715,476	821,103
Total operating expenses	6,614,953	6,512,627	(59,810)		13,067,770	13,776,403
OPERATING INCOME (LOSS)	(63,677)	(1,331,165)	-		(1,394,842)	242,026

(Continued)

WEST VIRGINIA HIGHER EDUCATION POLICY COMMISSION

COMBINING SCHEDULE—STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS (DEFICIT) INFORMATION FOR THE YEAR ENDED JUNE 30, 2005 (WITH COMPARATIVE TOTALS FOR 2004)

	2005				2004
	HEPC Division	WVNET Division	Eliminations	Combined	Total
NONOPERATING REVENUES (EXPENSES):					
State appropriations	$ 45,430,380	$ 1,952,662	$ -	$ 47,383,042	$ 41,750,649
Investment income	4,097,853	52,080		4,149,933	114,601
Institutional debt service payments to Commission:					
Interest	7,783,498			7,783,498	7,308,528
Other	2,829,248			2,829,248	3,012,849
Interest on indebtedness	(16,861,796)	(14,449)		(16,876,245)	(9,581,969)
Student financial aid payments to institutions	(26,858,152)			(26,858,152)	(26,763,755)
Other payments to institutions	(4,438,796)			(4,438,796)	(13,667,513)
Other nonoperating revenues	(4,554)			(4,554)	(20,500)
Net nonoperating revenues (expenses)	11,977,681	1,990,293	-	13,967,974	2,152,890
INCOME BEFORE OTHER REVENUES, EXPENSES, GAINS, OR LOSSES	11,914,004	659,128		12,573,132	2,394,916
CAPITAL APPROPRIATIONS	(7,012,000)			(7,012,000)	10,000,000
BOND PROCEEDS TO INSTITUTIONS	(6,983,346)			(6,983,346)	
TRANSFER TO WV COUNCIL FOR COMMUNITY & TECHNICAL COLLEGE EDUCATION	(840,703)			(840,703)	
UNAPPROPRIATED CAPITAL					(17,506,041)
(DECREASE) INCREASE IN NET ASSETS	(2,922,045)	659,128		(2,262,917)	(5,111,125)
NET ASSETS—Beginning of year	(3,552,621)	3,346,298		(206,323)	4,904,802
NET ASSETS (DEFICIT)—End of year	$ (6,474,666)	$ 4,005,426	$ -	$ (2,469,240)	$ (206,323)

(B) To eliminate inter-division revenue/expense.

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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*

To the 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, 2005, and have issued our report thereon dated November 21, 2005. 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. Our consideration of the internal control over financial reporting would not necessarily disclosure all matters in the internal control over financial reporting that might be material weaknesses. 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. We noted no matters involving the internal control over financial reporting and its operation that we consider to be 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 grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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.

Deloitte & Touche LLP

November 21, 2005