

MOREHEAD STATE UNIVERSITY

**Single Audit Reports Under
OMB Circular A-133**

*As of and for the Years Ended
June 30, 2007 and 2006
with Independent Auditors' Report Thereon*

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MANAGEMENT'S DISCUSSION AND ANALYSIS

Morehead State University's (the University) Management Discussion and Analysis (MD&A) of its financial condition provides an overview of the financial performance of the University for the year ended June 30, 2007. Management has prepared this discussion, along with the financial statements and related footnotes, to provide summary financial information. MD&A should be read in conjunction with the accompanying financial statements and footnotes.

Financial Highlights

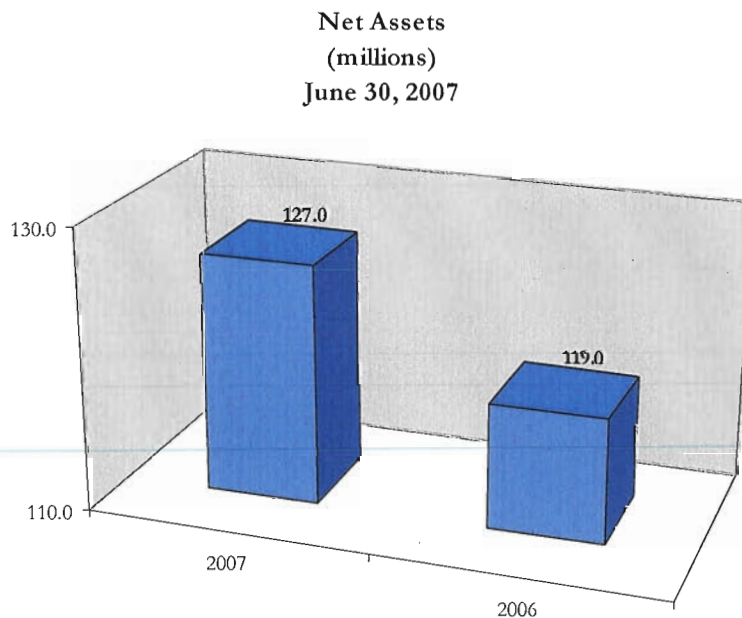
- The financial statements indicate that the University's financial condition remained stable at June 30, 2007. Financial operations were conducted in accordance with the approved budget plan.
- Total assets were \$172 million versus \$168 million at June 30, 2006. Significant components of the assets include \$19 million in cash, \$16 million in investments and \$122 million in capital assets net of depreciation.
- Total liabilities were \$45 million versus \$49 million at June 30, 2006. The significant components of the liabilities were \$29 million in bonds, notes, and capital lease obligations,

MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued

\$8 million in accounts payable and accrued liabilities, \$4 million in refundable grants, and \$4 million in deferred revenue and other liabilities.

- Total net assets were \$127 million at June 30, 2007 and \$119 million at June 30, 2006. Significant components of net assets include \$92 million invested in capital assets, net of depreciation and related debt, \$6 million in expendable restricted net assets, \$12 million of non-expendable restricted net assets, and \$17 million in unrestricted net assets.



- Operating revenues were \$75 million at June 30, 2007 and \$70 million at June 30, 2006. Operating expenses were \$120 million versus \$118 million at June 30, 2006. This created an operating loss of \$45 million versus an operating loss of \$48 million at June 30, 2006.
- Net nonoperating revenues were \$46 million for the year ended June 30, 2007, and \$44 million for the year ended June 30, 2006. Nonoperating revenues were comprised primarily of state appropriations. The combination of the net loss from operations, the net nonoperating revenues, and capital appropriations of \$7 million, resulted in an increase in net assets of \$8.2 million.

MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued

Using the Annual Report

This annual report consists of a series of financial statements, prepared in accordance with Governmental Accounting Standards Board (GASB) Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*. These financial statements focus on the financial condition of the University, the results of operations, and cash flows of the University as a whole.

One of the most important questions asked about University finances is whether the University is better off as a result of the year's activities. The information needed to answer this question can be found in:

- the Statement of Net Assets,
- the Statement of Revenues, Expenses and Changes in Net Assets, and
- the Statement of Cash Flows.



These statements present financial information of the University in a format similar to that used by corporations, and presents a long-term view of the University's finances. To get a full understanding of the University's financial condition these statements should be reviewed as a whole, and not individually. Further important information can be found in the Notes to the Financial Statements, beginning on page 28 of the Financial Statements. The Notes to the Financial Statements contain policies, explanations, and schedules that should be reviewed before, during, and after reviewing the Statements in order to get a complete understanding.

MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued

The Statement of Net Assets

This statement includes all assets and liabilities. It is prepared under the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service, regardless of when cash is exchanged. The University's net assets (the difference between assets and liabilities) are one indicator of the University's financial health. Over time, increases or decreases in net assets can indicate improvement or erosion of the University's financial health. Changes in net assets should be considered in conjunction with non-financial factors such as enrollment levels and conditions of facilities.

The Statement of Revenues, Expenses and Changes in Net Assets

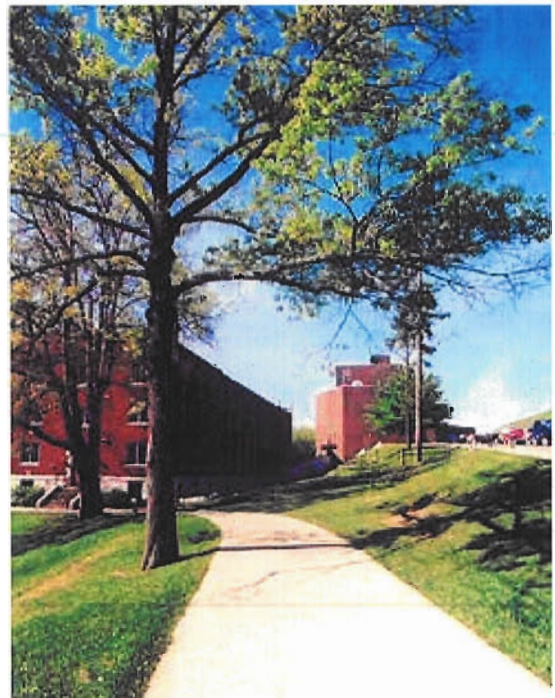
This statement presents the revenues earned and expenses incurred during the year. Activities are reported as either operating or nonoperating. GASB 35 requires State appropriations and gifts to be classified as nonoperating revenues. Accordingly, the University will generate a net operating loss prior to the addition of nonoperating revenues. The utilization of long-lived assets, referred to as Capital Assets, is reflected in the financial statements as depreciation, which amortizes the cost of an asset over its expected useful life.

The Statement of Cash Flows

This statement presents information related to cash inflows and outflows, summarized by operating, non-capital financing, capital financing and investing activities. An important factor to consider when evaluating financial viability is the University's ability to meet financial obligations as they mature.

Reporting Entity

Morehead State University is a component unit of the Commonwealth of Kentucky.



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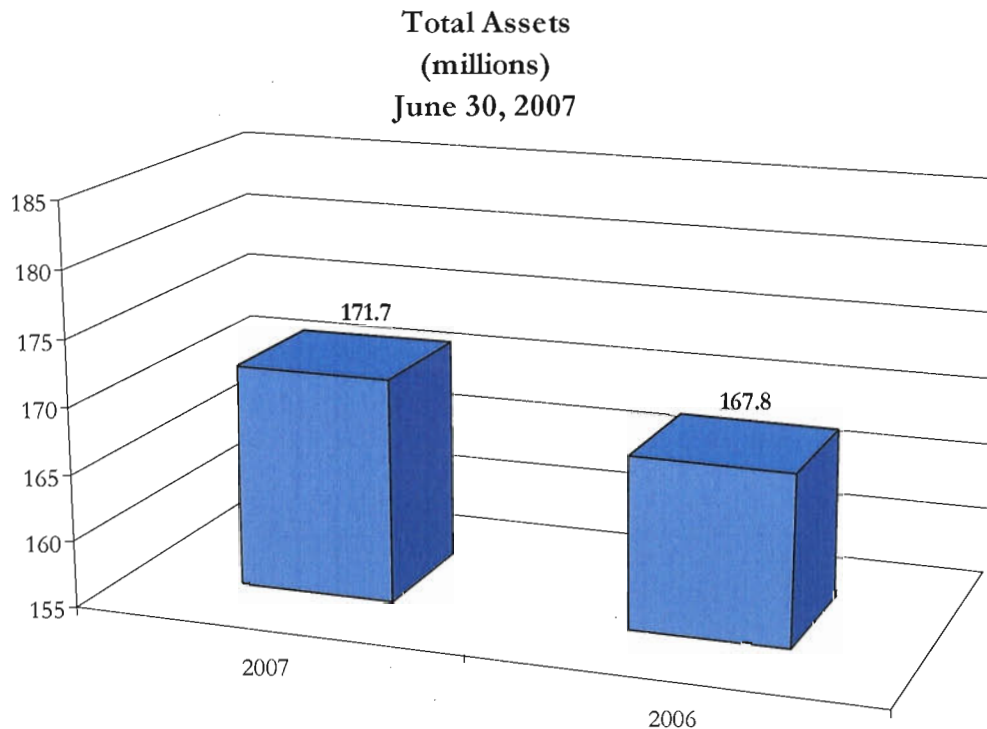
Management's Discussion and Analysis, continued

**Condensed Financial Information
Statement of Net Assets (in thousands)**

	<u>2007</u>	<u>2006</u>
<u>Assets</u>		
Current assets	\$ 30,287	\$ 26,250
Capital assets	121,704	121,166
Other noncurrent assets	<u>19,709</u>	<u>20,425</u>
Total assets	<u>171,700</u>	<u>167,841</u>
<u>Liabilities</u>		
Current liabilities	14,583	15,007
Noncurrent liabilities	<u>30,020</u>	<u>33,942</u>
Total liabilities	<u>44,603</u>	<u>48,949</u>
<u>Net Assets</u>		
Invested in capital assets, net of related debt	92,572	88,653
Restricted, expendable	5,827	6,277
Restricted, nonexpendable	11,756	11,746
Unrestricted	<u>16,942</u>	<u>12,216</u>
Total net assets	<u>\$ 127,097</u>	<u>\$ 118,892</u>

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Management's Discussion and Analysis, continued

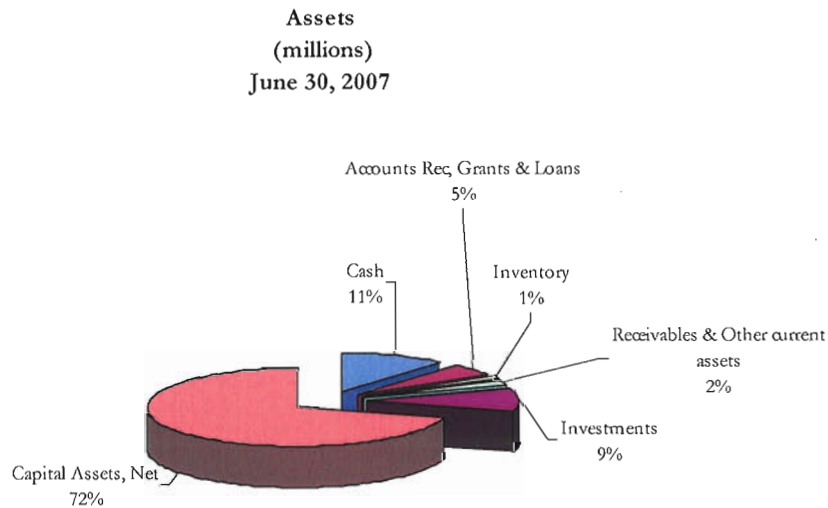


Assets

As of June 30, 2007, the University's total assets amount to approximately \$172 million versus \$168 million at June 30, 2006. Investment in capital assets, net of depreciation, represented the University's largest asset, totaling \$122 million compared to \$121 million at June 30, 2006. Cash and investments, totaling \$36 million at June 30, 2007 and \$37 million at June 30, 2006, were the University's next largest asset.

MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued



Total assets increased by \$3.8 million during the year ended June 30, 2007. The principal areas of change were:

- cash and cash equivalents decreased approximately \$.7 million,
- accounts, grants, and loans receivable, net increased approximately \$4.3 million,
- capital assets, net of accumulated depreciation, increased approximately \$.5 million,
- investments and other receivables decreased approximately \$.3 million.

Liabilities

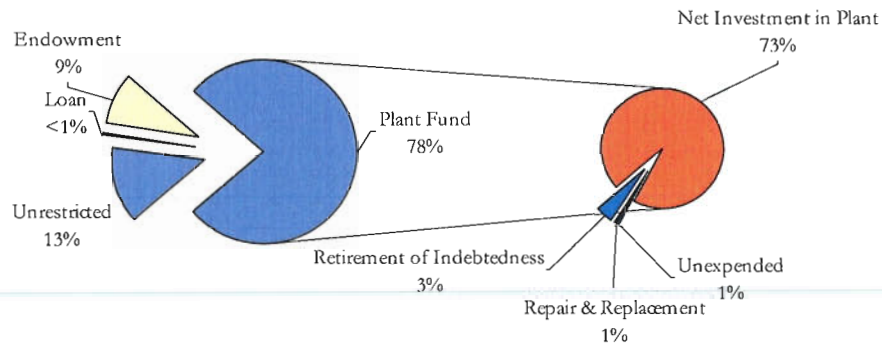
At June 30, 2007, the University's liabilities totaled approximately \$45 million versus \$49 million the previous year. Bonds, notes payable, and capital lease obligations for capital assets represented \$29 million versus \$33 million at June 30, 2006.

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Management's Discussion and Analysis, continued

Total liabilities decreased by \$4.3 million during the year ended June 30, 2007. This decrease was primarily due to a \$.3 million decrease in accounts payable and accrued liabilities, a \$3.4 million decrease in bonds, notes and capital lease obligations, a \$.8 million decrease in advances from federal government for student loans and an increase of \$.2 million in deferred revenue and other liabilities.

Net Assets
June 30, 2007



Net Assets

Net assets at June 30, 2007 totaled approximately \$127 million compared to \$119 million at June 30, 2006. Net assets invested in capital assets, net of related debt, totaled \$92 million versus \$89 million at June 30, 2006. Restricted net assets totaled \$18 million at June 30, 2007 and at June 30, 2006. Unrestricted net assets accounted for \$17 million versus \$12 million at June 30, 2006. Total net assets increased by \$8 million during the year ended June 30, 2007.

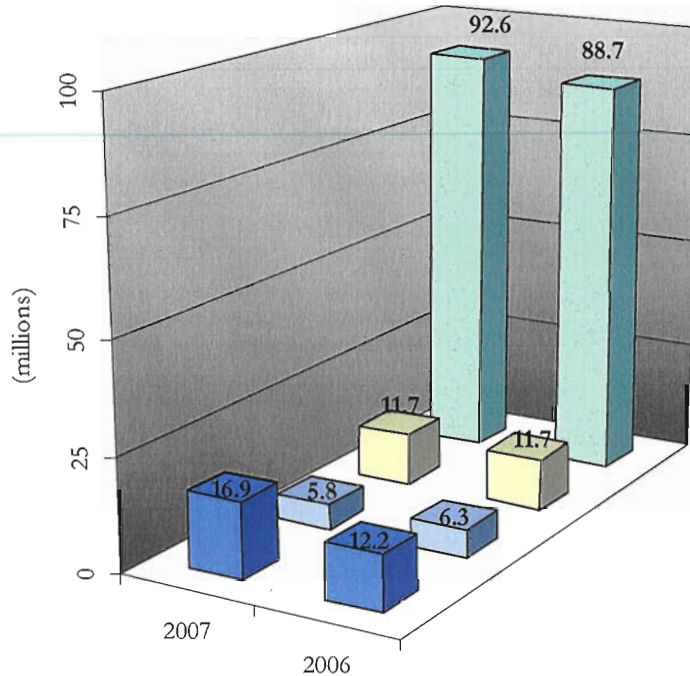
MOREHEAD STATE UNIVERSITY

Management’s Discussion and Analysis, continued

Net Assets Invested in Capital Assets, Net of Related Debt

Net assets invested in capital assets, net of related debt, increased by \$3.9 million. Increases in net assets invested in capital assets were primarily due to a \$2.1 million increase in capital appropriations for buildings versus an increase of \$10.3 million at June 30, 2006, an increase of \$3.8 million for land improvements versus an increase of \$.5 million last year, a decrease of \$2.7 million for capital construction versus a decrease of \$8.6 million last year, and net increases in other capital assets of \$4 million at June 30, 2007 and June 30, 2006. Also \$3.4 million in payments of principal on debt compared to \$3.6 million during fiscal year 2006. Decreases in net assets invested in capital assets (net) were from current year depreciation of \$7.4 million compared to \$6.9 million for the year ended June 30, 2006, as well as disposals and sales of \$.9 million compared to \$.7 million during fiscal year 2006.

**Total Net Assets
June 30, 2007**



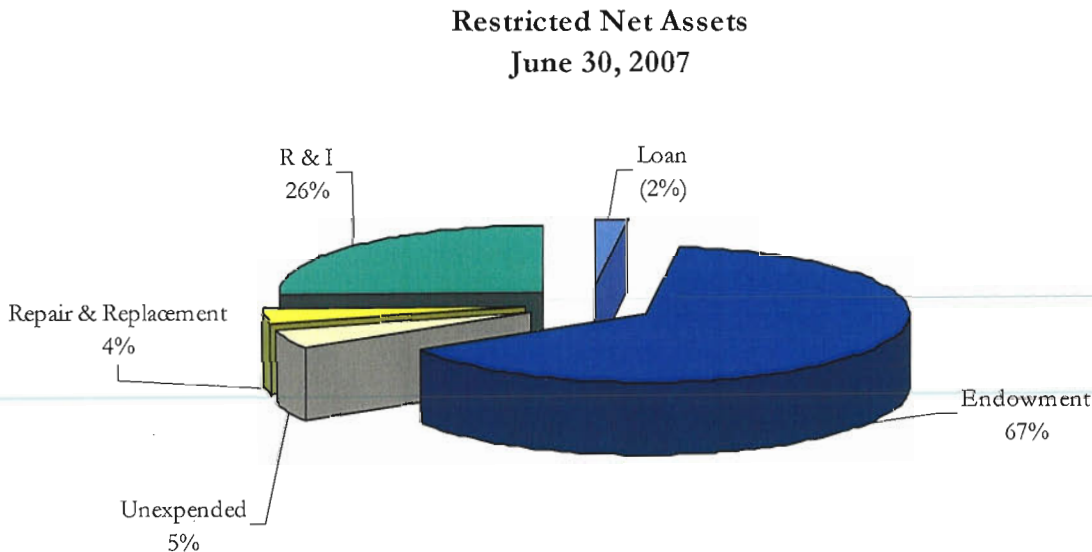
■ Unrestricted □ Expendable □ Non Expendable □ Invested in capital assets, net of related debt

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Management's Discussion and Analysis, continued

Restricted Net Assets

Restricted net assets are subject to stipulations made by entities external to the University that govern the use of these funds. Restricted net assets decreased by \$.4 million from the previous year to \$17.6 million. Major components of the decrease include a \$.8 million decrease in unexpended restricted net assets, and a \$.4 increase in the loan fund net assets.



Unrestricted Net Assets

Unrestricted net assets increased by \$4.7 million from the previous year to \$17 million. Unrestricted net assets are not subject to externally imposed restrictions. However, substantially all of the unrestricted net asset balance has been allocated for the support of academic programs and other initiatives, the completion of capital projects, or working capital requirements. The allocation of unrestricted net assets as of June 30, 2007 is as follows:

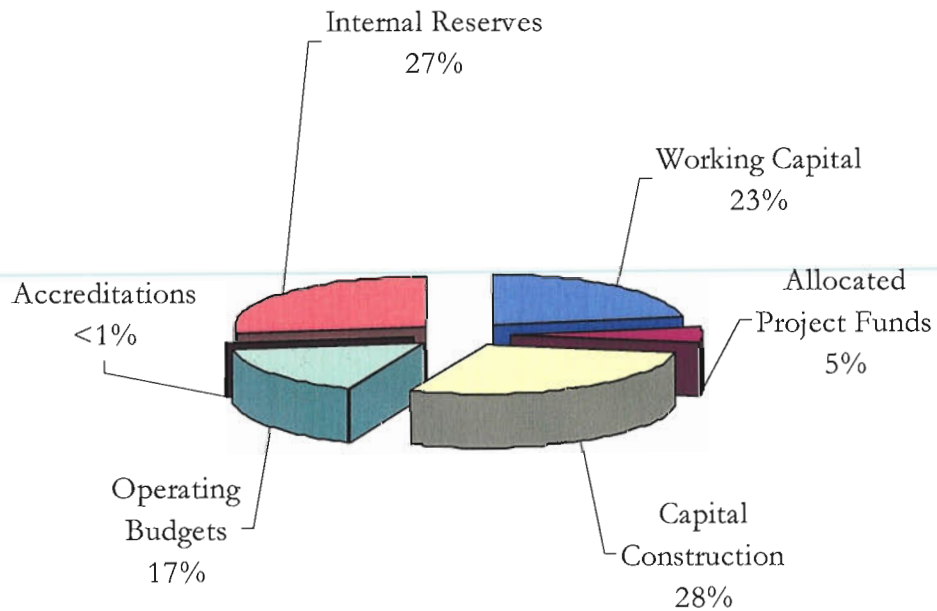
MOREHEAD STATE UNIVERSITY

Management’s Discussion and Analysis, continued

Allocation of Unrestricted Net Assets (in thousands)

	<u>2007</u>	<u>2006</u>
Working capital	\$ 3,835	\$ 7,196
Allocated project funds	887	778
Capital construction	4,847	1,683
Operating budgets	2,800	1,917
Accreditations	11	15
Internal reserves	4,561	627
Unrestricted net assets	<u>\$16,941</u>	<u>\$12,216</u>

**Allocation of Unrestricted Net Assets
June 30, 2007**



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Management's Discussion and Analysis, continued

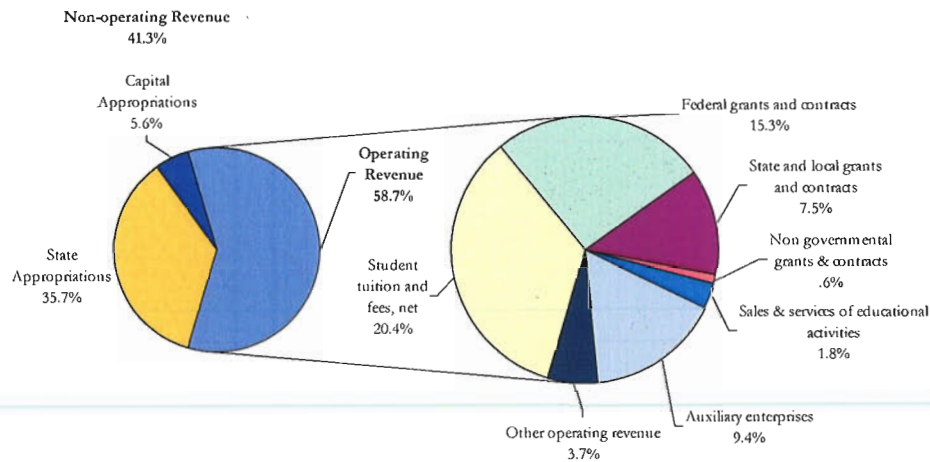
Statement of Revenues, Expenses and Changes in Net Assets (in thousands)

	<u>2007</u>	<u>2006</u>
<u>Operating Revenues</u>		
Student tuition and fees, net	\$ 26,061	\$ 22,326
Federal grants and contracts	19,622	20,714
State and local grants and contracts	9,585	9,882
Nongovernmental grants and contracts	775	902
Sales and services of educational activities	2,303	1,984
Auxiliary enterprises	11,944	11,408
Other operating revenue	<u>4,662</u>	<u>2,680</u>
Total operating revenue	<u>74,952</u>	<u>69,896</u>
<u>Operating Expenses</u>		
Educational and general	101,706	101,269
Auxiliary enterprises	10,628	9,401
Depreciation	7,482	6,939
Other operating expenses	<u>328</u>	<u>89</u>
Total operating expenses	<u>120,144</u>	<u>117,698</u>
Operating loss	<u>(45,192)</u>	<u>(47,802)</u>
<u>Nonoperating Revenues (Expenses)</u>		
State appropriations	45,531	44,902
Investment income, net	2,148	255
Interest on capital assets – debt related	<u>(1,377)</u>	<u>(1,589)</u>
Net nonoperating revenues	<u>46,302</u>	<u>43,568</u>
Income (loss) before other revenues, expenses, gains or losses	1,110	(4,234)
Capital appropriations	<u>7,095</u>	<u>3,579</u>
Increase (decrease) in net assets	8,205	(655)
Net assets, beginning of year	<u>118,892</u>	<u>119,547</u>
Net assets, end of year	<u>\$ 127,097</u>	<u>\$ 118,892</u>

Revenues

Total operating revenues were approximately \$75 million for the year ended June 30, 2007 and approximately \$70 million for the year ended June 30, 2006. The most significant sources of operating revenue for the University are net student fees \$26 million, federal grants and contracts \$20 million, auxiliary enterprises \$11 million, state and local grants \$10 million, and other revenues including, private grants, and sales and services of educational activities, \$8 million.

Sources of Revenue
June 30, 2007

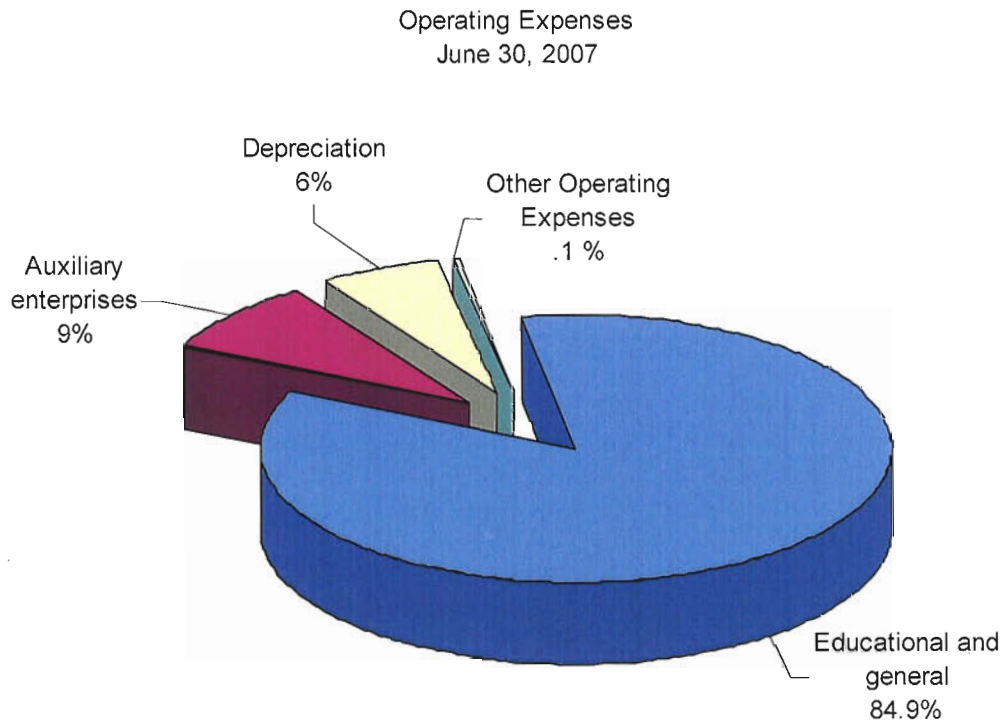


Expenses

Operating expenses totaled approximately \$120 million compared to \$118 million at June 30, 2006. Of this amount, approximately \$102 million was used for educational and general expenses related to functions such as instruction, research, and public service.

MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued



Cash Flows

Another way to assess the financial health of an institution is to look at the Statement of Cash Flows. The primary purpose of the Statement of Cash Flows is to provide information about the cash receipts and cash payments made by the University during the period. The Statement of Cash Flows also helps financial statement readers assess:

- the University's ability to generate future net cash flows
- the University's ability to meet obligations as they become due, and
- the University's need for external financing.



MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued

Statement of Cash Flows (In Thousands) Year ended June 30, 2007

	<u>2007</u>	<u>2006</u>
Cash Provided/Used By:		
Operating activities	\$(42,071)	\$(41,334)
Noncapital financing activities	45,531	44,891
Capital and related financing activities	(6,622)	(6,382)
Investing activities	<u>2,438</u>	<u>132</u>
Net decrease in cash	(724)	(2,693)
Cash, beginning of the year	<u>19,967</u>	<u>22,660</u>
Cash, end of the year	<u>\$ 19,243</u>	<u>\$ 19,967</u>

Major sources of funds included in operating activities are student tuition and fees, \$21.4 million versus \$22.3 million the previous year, and grants and contracts, \$25.6 million compared to \$31.1 million at June 30, 2006. The largest cash payments for operating activities were made to employees \$54.6 million versus \$56.2 million the previous year, and suppliers \$54.7 million compared to \$54.1 million June 30, 2006.



The largest cash receipt in the noncapital financing activities group is the operating appropriation from the Commonwealth of Kentucky of \$45.5 million versus \$44.9 million the previous year and cash used by capital and related financing activities is

primarily expended on the construction and acquisition of capital assets.

MOREHEAD STATE UNIVERSITY

Management’s Discussion and Analysis, continued

Capital Asset and Debt Administration

Capital Assets

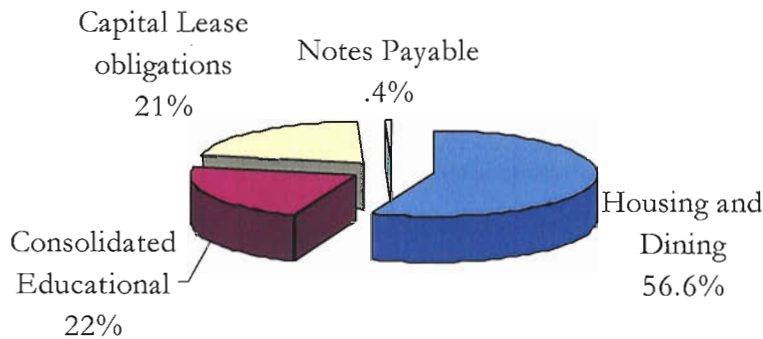
Capital assets, net of accumulated depreciation (but not of related debt), totaled approximately \$121.7 million at June 30, 2007 versus \$121.2 million at June 30, 2006. This represents a net increase of \$.5 million over June 30, 2006. Significant changes to capital assets during fiscal 2006 - 2007 included:

Buildings and structures	\$5.9 million
Library additions, equipment and vehicles	4.1 million
Net change in construction in progress	(2.7) million
Increase in accumulated depreciation, net	(6.8) million

Debt

At year-end, the University had \$29.1 million in outstanding debt versus \$32.5 million the previous year. This includes \$22.8 million in bonds payable compared to \$25.5 million at June 30, 2006. In addition, the University had capital lease obligations of \$6.3 million compared to \$6.8 million the previous year-end. The University had \$.1 million in notes payable at June 30, 2007.

**Outstanding Debt
June 30, 2007**



MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued

The University's debt is summarized by type of debt instrument as follows (in thousands):

	June 30,	
	<u>2007</u>	<u>2006</u>
Housing and Dining System revenue bonds	\$ 16,330	\$ 17,820
Consolidated Educational buildings revenue bonds	6,415	7,665
Capital lease obligations	6,257	6,787
Notes payable	<u>130</u>	<u>240</u>
	<u>\$ 29,132</u>	<u>\$ 32,512</u>

Debt outstanding decreased approximately \$3.3 million from the end of the prior year.

FACTORS IMPACTING FUTURE PERIODS

The following are known facts and circumstances that could affect future financial results:

- The University's Board of Regents has approved an operating budget for the fiscal year ending June 30, 2008 totaling \$119 million.
-
- Tuition rates for FY 2007-08 will increase approximately 8.3% for resident and nonresident undergraduate and graduate students.



Independent Auditors' Report

Members of the Board of Regents and
Dr. Wayne D. Andrews, President
Morehead State University
Morehead, Kentucky

Secretary of Finance and
Administration Cabinet of the
Commonwealth of Kentucky

We have audited the accompanying financial statements of Morehead State University (the "University") and its discretely presented component unit as of June 30, 2007 and 2006, and for the years then ended, which collectively comprise the University's basic financial statements as listed on the table of contents. These financial statements are the responsibility of the University's management. 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the University and its discretely presented component unit as of June 30, 2007 and 2006, and the respective changes in its net assets and, where applicable, its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 26, 2007, on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion 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 considered in assessing the results of our audits.



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in Kentucky

The management's discussion and analysis on pages 1 through 17 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the University's basic financial statements. The supplemental information contained on pages 55 through 58 is presented for purposes of additional analysis and is not a required part of the basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements of the University. The supplemental information and the schedule of expenditures of federal awards have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

November 26, 2007
Lexington, Kentucky

Walter R. Bontney, Jr., R.S.C.

MOREHEAD STATE UNIVERSITY

Statement of Net Assets

June 30, 2007 and 2006

	<u>2007</u>	<u>2006</u>
Assets		
Current assets:		
Cash and cash equivalents	\$ 19,242,952	\$ 19,967,069
Accounts, grants and loans receivable, net	8,996,258	4,290,485
Inventories	1,926,554	1,861,638
Other current assets	<u>121,278</u>	<u>131,278</u>
Total current assets	<u>30,287,042</u>	<u>26,250,470</u>
Noncurrent assets:		
Accounts, grants and loans receivable, net	3,403,180	3,828,058
Investments	16,306,863	16,596,696
Capital assets, net	<u>121,703,879</u>	<u>121,165,679</u>
Total noncurrent assets	<u>141,413,922</u>	<u>141,590,433</u>
Total assets	<u>\$171,700,964</u>	<u>\$167,840,903</u>
Liabilities & Net Assets		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 7,723,602	\$ 8,114,113
Deferred revenue	2,984,786	2,720,271
Other current liabilities	717,700	736,637
Bonds, notes and capital lease obligations, current portion	<u>3,157,368</u>	<u>3,435,914</u>
Total current liabilities	<u>14,583,456</u>	<u>15,006,935</u>
Long-term liabilities:		
Bond, notes and capital lease obligations, noncurrent portion	25,974,194	29,076,275
Advances from federal government for student loans	<u>4,046,260</u>	<u>4,865,694</u>
Total long-term liabilities	<u>30,020,454</u>	<u>33,941,969</u>
Total liabilities	<u>44,603,910</u>	<u>48,948,904</u>
Net Assets:		
Invested in capital assets, net of related debt	92,572,317	88,653,490
Restricted:		
Expendable	5,827,346	6,276,627
Nonexpendable	11,755,936	11,746,002
Unrestricted	<u>16,941,455</u>	<u>12,215,880</u>
Total net assets	<u>\$127,097,054</u>	<u>\$118,891,999</u>

See accompanying notes.

MOREHEAD STATE UNIVERSITY FOUNDATION, INC.

Statement of Financial Position

June 30, 2007 and 2006

	<u>2007</u>	<u>2006</u>
Assets		
Current assets:		
Cash	\$ 507,340	\$ 383,236
Accounts receivable	22,069	-
Accrued interest receivable	14,454	13,871
Pledges receivable, net	650,914	734,304
Lease financing receivable, current	<u>130,342</u>	<u>120,690</u>
Total current assets	<u>1,325,119</u>	<u>1,252,101</u>
Noncurrent assets:		
Investments	29,145,811	26,228,479
Cash surrender value – life insurance	105,235	85,443
Property and equipment, net	267,248	292,334
Pledges receivable, net	519,149	236,987
Lease financing receivable	<u>1,327,653</u>	<u>1,457,995</u>
Total noncurrent assets	<u>31,365,096</u>	<u>28,301,238</u>
Total assets	<u>\$32,690,215</u>	<u>\$29,553,339</u>
Liabilities & Net Assets		
Current liabilities:		
Accounts payable	\$ 6,109	\$ 4,259
Annuities payable	78,681	64,200
Due to Morehead State University	<u>26,900</u>	<u>36,900</u>
Total current liabilities	<u>111,690</u>	<u>105,359</u>
Long-term liabilities:		
Funds held in trust for Morehead State University	11,329,598	11,329,598
Annuities payable	303,752	267,979
Due to Morehead State University	<u>80,700</u>	<u>80,700</u>
Total long-term liabilities	<u>11,714,050</u>	<u>11,678,277</u>
Total liabilities	<u>11,825,740</u>	<u>11,783,636</u>
Net Assets:		
Unrestricted	294,629	593,553
Temporarily restricted	7,618,200	4,641,913
Permanently restricted	<u>12,951,646</u>	<u>12,534,237</u>
Total net assets	<u>20,864,475</u>	<u>17,769,703</u>
Total liabilities and net assets	<u>\$32,690,215</u>	<u>\$29,553,339</u>

See accompanying notes.

MOREHEAD STATE UNIVERSITY

Statement of Revenues, Expenses and Changes in Net Assets

Years ended June 30, 2007 and 2006

	<u>2007</u>	<u>2006</u>
Operating revenues:		
Student tuition and fees (net of scholarship allowances of \$18,436,900 and \$17,045,818)	\$ 26,060,527	\$ 22,326,469
Federal grants and contracts	19,622,279	20,714,214
State and local grants and contracts	9,585,224	9,882,341
Nongovernmental grants and contracts	774,816	901,812
Sales and services of educational activities	2,303,292	1,983,614
Auxiliary enterprises:		
Residence halls (net of scholarship allowances of \$84,088 and \$92,287)	7,252,831	6,903,165
Bookstore	3,895,745	3,831,364
Other auxiliaries	795,130	673,028
Other operating revenues	<u>4,662,631</u>	<u>2,679,744</u>
Total operating revenues	<u>74,952,475</u>	<u>69,895,751</u>
Operating expenses:		
Education and general:		
Instruction	44,626,658	43,057,250
Research	2,340,694	1,727,586
Public service	7,313,882	8,561,048
Library	2,939,303	2,881,181
Academic support	6,990,416	8,219,687
Student services	9,700,861	9,125,819
Institutional support	11,852,915	12,461,158
Operation and maintenance of plant	7,194,940	7,205,714
Depreciation	6,673,767	5,551,621
Student aid	8,745,703	8,029,346
Auxiliary enterprises:		
Residence halls	6,003,612	4,812,739
Bookstore	3,689,317	3,674,966
Other auxiliaries	935,399	913,283
Depreciation	808,661	1,387,905
Other operating expenses	<u>327,865</u>	<u>88,882</u>
Total operating expenses	<u>120,143,993</u>	<u>117,698,185</u>
Operating loss	<u>(45,191,518)</u>	<u>(47,802,434)</u>

MOREHEAD STATE UNIVERSITY

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

Years ended June 30, 2007 and 2006

	<u>2007</u>	<u>2006</u>
Nonoperating revenues (expenses):		
State appropriations	45,531,490	44,901,703
Investment income (net of investment expense of \$7,333 and \$7,177)	2,147,887	255,299
Interest on capital asset - related debt	<u>(1,377,277)</u>	<u>(1,588,821)</u>
Net nonoperating revenues	<u>46,302,100</u>	<u>43,568,181</u>
Income (loss) before capital appropriations	1,110,582	(4,234,253)
Capital appropriations	<u>7,094,473</u>	<u>3,578,706</u>
Increase (decrease) in net assets	8,205,055	(655,547)
Net assets, beginning of year	<u>118,891,999</u>	<u>119,547,546</u>
Net assets, end of year	<u>\$ 127,097,054</u>	<u>\$ 118,891,999</u>

See accompanying notes.

MOREHEAD STATE UNIVERSITY FOUNDATION, INC.

Statement of Activities

Year ended June 30, 2007

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Revenues and other support:				
Contributions	\$ 70,158	\$ 2,367,169	\$ 417,409	\$ 2,854,736
Other revenue and gains (losses):				
Investment income:				
Interest and dividend income, net	44,142	1,330,839	-	1,374,981
Realized and unrealized gains	37,742	2,439,491	-	2,477,233
In-kind contributed services	77,347	-	-	77,347
Other income	158	501,485	-	501,643
Annuities payable adjustment	(43,541)	-	-	(43,541)
Net assets released from restrictions:				
Restrictions satisfied by payments	<u>3,662,697</u>	<u>(3,662,697)</u>	-	-
Total revenues and other support	<u>3,848,703</u>	<u>2,976,287</u>	<u>417,409</u>	<u>7,242,399</u>
Expenses:				
Program expenses:				
Contributions to Morehead State				
University for:				
Academic programs	1,230,772	-	-	1,230,772
Athletics	352,985	-	-	352,985
University support:				
Operations and materials	252,715	-	-	252,715
Student financial aid	451,546	-	-	451,546
Athletics	51,214	-	-	51,214
Eagle Trace Golf Course	<u>1,595,649</u>	-	-	<u>1,595,649</u>
Total program expenses	3,934,881	-	-	3,934,881
General and administrative	140,829	-	-	140,829
Fundraising	<u>71,917</u>	-	-	<u>71,917</u>
Total expenses	<u>4,147,627</u>	-	-	<u>4,147,627</u>
Change in net assets	(298,924)	2,976,287	417,409	3,094,772
Net assets, beginning of year	<u>593,553</u>	<u>4,641,913</u>	<u>12,534,237</u>	<u>17,769,703</u>
Net assets, end of year	<u>\$ 294,629</u>	<u>\$ 7,618,200</u>	<u>\$12,951,646</u>	<u>\$20,864,475</u>

MOREHEAD STATE UNIVERSITY FOUNDATION, INC.

Statement of Activities

Year ended June 30, 2006

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Revenues and other support:				
Contributions	\$ 90,971	\$ 1,266,043	\$ 171,776	\$ 1,528,790
Other revenue and gains (losses):				
Investment income:				
Interest and dividend income, net	25,340	1,224,293	-	1,249,633
Realized and unrealized gains	18,069	757,106	-	775,175
In-kind contributed services	63,628	-	-	63,628
Other income	734	370,289	-	371,023
Annuities payable adjustment	(53,486)	-	-	(53,486)
Net assets released from restrictions:				
Restrictions satisfied by payments	<u>2,011,824</u>	<u>(2,011,824)</u>	<u>-</u>	<u>-</u>
 Total revenues and other support	 <u>2,157,080</u>	 <u>1,605,907</u>	 <u>171,776</u>	 <u>3,934,763</u>
 Expenses:				
Program expenses:				
Contributions to Morehead State				
University for:				
Academic programs	1,322,909	-	-	1,322,909
Athletics	293,846	-	-	293,846
University support:				
Operations and materials	123,698	-	-	123,698
Student financial aid	366,050	-	-	366,050
Athletics	<u>25,837</u>	<u>-</u>	<u>-</u>	<u>25,837</u>
 Total program expenses	 2,132,340	 -	 -	 2,132,340
 General and administrative	 148,238	 -	 -	 148,238
Fundraising	<u>66,043</u>	<u>-</u>	<u>-</u>	<u>66,043</u>
 Total expenses	 <u>2,346,621</u>	 <u>-</u>	 <u>-</u>	 <u>2,346,621</u>
 Change in net assets	 (189,541)	 1,605,907	 171,776	 1,588,142
 Net assets, beginning of year	 <u>783,094</u>	 <u>3,036,006</u>	 <u>12,362,461</u>	 <u>16,181,561</u>
Net assets, end of year	<u>\$ 593,553</u>	<u>\$ 4,641,913</u>	<u>\$12,534,237</u>	<u>\$17,769,703</u>

MOREHEAD STATE UNIVERSITY

Statement of Cash Flows

Years ended June 30, 2007 and 2006

	<u>2007</u>	<u>2006</u>
Cash flows from operating activities:		
Tuition and fees	\$21,426,147	\$ 22,260,932
Grants and contracts	25,605,391	31,184,058
Payments to suppliers	(54,659,322)	(54,108,690)
Payments to employees	(54,581,842)	(56,230,983)
Loans issued to students	(904,473)	(1,162,429)
Collection of loans issued to students	635,382	655,777
Auxiliary enterprises:		
Residence halls	7,251,936	6,905,033
Bookstore	3,907,463	3,824,298
Other auxiliaries	805,032	674,024
Sales and services of educational activities	2,303,292	1,983,614
Other receipts	<u>6,139,638</u>	<u>2,669,291</u>
Net cash used in operating activities	<u>(42,071,356)</u>	<u>(41,345,075)</u>
Cash flows from noncapital financing activities:		
State appropriations	<u>45,531,490</u>	<u>44,901,703</u>
Net cash provided by noncapital financing activities	<u>45,531,490</u>	<u>44,901,703</u>
Cash flows from capital and related financing activities:		
Capital appropriations	7,094,473	3,578,706
Purchase of capital assets	(8,139,106)	(4,783,637)
Decrease in advances from federal government for student loans	(819,434)	-
Principal paid on capital debt and leases	(3,380,627)	(3,588,634)
Interest paid on capital debt and leases	<u>(1,377,277)</u>	<u>(1,588,821)</u>
Net cash used in capital and related financing activities	<u>(6,621,971)</u>	<u>(6,382,386)</u>
Cash flows from investing activities:		
Interest received on investments, net	2,147,887	255,299
Changes in investments, net	<u>289,833</u>	<u>(122,423)</u>
Net cash provided by investing activities	<u>2,437,720</u>	<u>132,876</u>
Net decrease in cash and cash equivalents	(724,117)	(2,692,882)
Cash and cash equivalents, beginning of year	<u>19,967,069</u>	<u>22,659,951</u>
Cash and cash equivalents, end of year	<u>\$ 19,242,952</u>	<u>\$ 19,967,069</u>

MOREHEAD STATE UNIVERSITY

Statement of Cash Flows, continued

Years ended June 30, 2007 and 2006

	<u>2007</u>	<u>2006</u>
Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	\$ (45,191,518)	\$(47,802,434)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation	7,482,428	6,939,526
Loss on disposal of capital assets	118,478	87,707
Bad debt expense	943,616	630,046
Changes in assets and liabilities:		
Receivables, net	(5,224,511)	1,174,858
Inventories	(64,916)	(25,031)
Other current assets	10,000	(10,000)
Accounts payable and accrued liabilities	(390,511)	(3,085,664)
Deferred revenue	264,515	722,559
Other current liabilities	<u>(18,937)</u>	<u>23,358</u>
 Net cash used in operating activities	 <u>\$ (42,071,356)</u>	 <u>\$(41,345,075)</u>
 Supplemental disclosures of cash flow information:		
Noncash investing and financing transactions:		
Purchase of capital assets with capital lease obligations \$	-	\$ 327,764

See accompanying notes.

MOREHEAD STATE UNIVERSITY

Notes to Financial Statements

1. Organization and Summary of Significant Accounting Policies

Organization

Morehead State University (the University) is a regional, coeducational, public institution of higher education offering general and liberal arts programs and pre-professional and professional training in education and various other fields at both the undergraduate and graduate levels. Located in Morehead, Kentucky, the University has provided educational service to the Commonwealth of Kentucky since 1887.

Reporting Entity

The University is a component unit of the Commonwealth of Kentucky and is included in the general-purpose financial statements of the Commonwealth. The Morehead State University Foundation, Inc. (the Foundation) is a legally separate, tax-exempt organization supporting the University. The Foundation acts primarily as a fund-raising organization to supplement the resources that are available to the University in support of its programs. The Foundation's Board of Directors is self-perpetuating and consists of graduates and friends of the University. Although the University does not control the timing or amount of receipts from the Foundation, the majority of the resources the Foundation holds and invests are restricted by the donors to the activities of the University. Because these restricted resources held by the Foundation can only be used by, or for the benefit of, the University, the Foundation is considered a component unit of the University and is discretely presented in the University's financial statements.

Basis of Presentation

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). The financial statements have been prepared on the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when an obligation has been incurred. In accordance with GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities* (GASB No. 35), and subsequent standards issued by GASB, the University reports as a Business Type Activity (BTA). BTAs are those activities that are financed in whole or in part by fees charged to external parties for goods and services.

GASB No. 35 establishes standards for external financial reporting for public colleges and universities and requires that resources be classified for accounting and reporting purposes into the following net asset categories:

- **Invested in capital assets, net of related debt:** Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

1. Organization and Summary of Significant Accounting Policies, continued

Basis of Presentation, continued

- **Restricted:**

Expendable— Net assets whose use by the University is subject to externally imposed stipulations that can be fulfilled by actions of the University pursuant to those stipulations or that expire by the passage of time.

Nonexpendable— Net assets subject to externally imposed stipulations that they be maintained permanently by the University. Such assets include the University's permanent endowment funds.

- **Unrestricted:** Net assets whose use by the University is not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Regents or may otherwise be limited by contractual agreements with outside parties.

The financial statement presentation required by GASB No. 35 is intended to provide a comprehensive, entity-wide perspective of the University's assets, liabilities, net assets, revenues, expenses, changes in net assets and cash flows.

Pursuant to GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the University has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB) that were issued on or before November 30, 1989, and do not conflict with or contradict GASB pronouncements.

Allowance for Doubtful Accounts

The allowance for doubtful accounts is established through a provision for doubtful accounts charged to expense. The allowance represents an amount which, in management's judgment, will be adequate to absorb probable losses on existing accounts that may become uncollectible.

Inventories

Inventories representing approximately 64% and 61% of total inventories at June 30, 2007 and 2006, respectively, are stated at the lower of cost (retail inventory method) or market. The remainder of the inventories are stated at the lower of moving-average-cost or market.

Investments

The University values investments at fair value based on quoted market prices.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

1. Organization and Summary of Significant Accounting Policies, continued

Investments, continued

Investment income consists of interest and dividend income and the net change for the year in the fair value of investments carried at fair value.

Capital Assets

Capital assets are stated at cost for purchased assets and at fair value at date of donation in the case of gifts. Expenditures of greater than \$1,000 which increase values or extend useful lives of the respective assets are capitalized; whereas expenditures for maintenance and repairs are charged to expense as incurred. Depreciation of assets is computed using the straight-line method over the assets estimated useful lives. The University capitalizes, but does not depreciate, works of art and historical treasures that are held for exhibition, education, research and public service. Estimated lives used for depreciation purposes are as follows:

<u>Classification</u>	<u>Estimated Life</u>
Land improvements	20 years
Buildings	50 years
Vehicles	5-9 years
Equipment	5-15 years
Library books	10 years

Accrued Vacation Pay

Accrued vacation pay is included in accounts payable and accrued liabilities in the statement of net assets and represents earned vacation available to employees at current compensation rates.

Deferred Revenue

Deferred revenue includes amounts received from grant and contract sponsors that have not yet been earned.

Advances from Federal Government for Student Loans

Funds provided by the United States Government under the Federal Perkins Loan program are loaned to qualified students and may be reloaned after collections. These funds are ultimately refundable to the United States Government and, therefore, are recorded as a liability in the accompanying financial statements. Federally funded financial aid programs are subject to special audits. Such audits could result in claims against the resources of the University.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

1. Organization and Summary of Significant Accounting Policies, continued

Restricted Asset Spending Policy

The University's policy is that restrictions on assets cannot be fulfilled by the expenditure of unrestricted funds for similar purposes. The determination on whether restricted or unrestricted funds are expended for a particular purpose is made on a case-by-case basis. Restricted funds remain restricted until spent for the intended purpose.

Operating Activities

The University defines operating activities, as reported on the statement of revenues, expenses and changes in net assets, as those that generally result from exchange transactions, such as payments received for providing goods and services and payments made for services and goods received. Nearly all of the University's expenses are from exchange transactions. Certain significant revenues relied upon for operations, such as state appropriations, gifts and investment income, are recorded as nonoperating revenues, in accordance with GASB No. 35.

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 revenues and expenditures during the reporting period. Actual results could differ from the estimated amounts.

Recent Accounting Pronouncements

In June 2004, the GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. This statement establishes standards for the measurement, recognition, and display of other postemployment benefit expenses/expenditures and related assets/liabilities, note disclosures, and, if applicable, required supplementary information in the financial reports of employers subject to governmental accounting standards. The provisions of this statement are effective for financial statements for fiscal periods beginning after December 15, 2006. The University has not yet evaluated the impact that the adoption of this statement will have on its financial statements.

Income Taxes

As a state institution of higher education, the income of the University is generally exempt from federal and state income taxes under Section 115(1) of the Internal Revenue Code, as amended, and a similar provision of state law. However, the University is subject to federal income tax on any unrelated business taxable income.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

1. Organization and Summary of Significant Accounting Policies, continued

Reclassification

Certain 2006 amounts have been reclassified to conform to 2007 presentation with no effect on total assets, liabilities, net assets, or change in net assets.

2. Cash, Cash Equivalents and Investments

The statement of net assets classification "cash and cash equivalents" includes all readily available sources of cash such as petty cash, demand deposits, deposits with the Commonwealth of Kentucky, certificates of deposit and temporary investments in marketable securities with original maturities of less than three months.

The state treasurer requires that all state funds be insured by the Federal Deposit Insurance Corporation (FDIC), collateralized by securities held by the cognizant Federal Reserve Bank or invested in U.S. Government obligations. The University's deposits with the state treasurer are pooled with funds of other state agencies and then, in accordance with statutory limitations, placed in financial institutions or invested as the state treasurer may determine, in the state's name.

The University requires that balances on deposit with financial institutions be insured by the FDIC or collateralized by securities held by the cognizant Federal Reserve Bank, in the University's name.

Custodial credit risk for deposits is the risk that, in the event of a bank failure, the University's deposits may not be returned to the University. As a means of limiting its exposure to losses from custodial credit risk, the University's deposits and investments are held by the state treasurer, collateralized by securities in the University's name, insured by the FDIC or in the University's name.

As of June 30, 2007 and 2006, the University had petty cash funds totaling \$110,419 and \$116,501, respectively, and deposits as reflected by bank balances as follows:

	<u>2007</u>	<u>2006</u>
Insured, commercial banks	\$ 215,802	\$ 217,326
Uninsured, commercial banks; collateral held by pledging institution's agent in the University's name	17,253,719	15,646,784
Maintained by Commonwealth of Kentucky	<u>1,663,012</u>	<u>3,799,054</u>
	<u>\$ 19,132,533</u>	<u>\$ 19,663,164</u>

The difference in the cash carrying amount per the statement of net assets and the above bank balances represented items in transit.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

2. Cash, Cash Equivalents and Investments, continued

As of June 30, 2007 and 2006, investments consisted of:

	<u>2007</u>	<u>2006</u>
Insured and registered, with securities held by the counter party or by its trust department or agent, in the University's name:		
Money market funds – restricted for capital purposes	\$ 4,550,926	\$ 4,850,695
Equity mutual funds	303,805	296,874
Money market funds	<u>33,106</u>	<u>33,645</u>
	<u>4,887,837</u>	<u>5,181,214</u>
 Certificate of deposit	 89,428	 85,884
 Restricted assets held by the Morehead State University Foundation, Inc.	 <u>11,329,598</u>	 <u>11,329,598</u>
Total investments	<u>\$ 16,306,863</u>	<u>\$ 16,596,696</u>

Restricted investments for capital purposes are comprised of amounts invested for sinking fund and debt service reserves. The University may legally invest in direct obligations of and other obligations guaranteed as to principal by the U.S. Treasury and U.S. agencies and instrumentalities and in bank repurchase agreements. It may also invest to a limited extent in equity securities.

University investments held by MSU Foundation, Inc. (Foundation) are comprised of the Regional University Excellence Trust Fund endowment and other similar endowments (see Note 14). Assets held by the Foundation are invested primarily in an investment pool managed by the Foundation and are carried at fair value.

The assets in the Foundation investment pool as of June 30, 2007 and 2006, are invested as follows:

	<u>2007</u>	<u>2006</u>
Percentage of pool invested in:		
Registered investment companies equity funds	60%	61%
Registered investment companies fixed income funds	<u>40%</u>	<u>39%</u>
Total	<u>100%</u>	<u>100%</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

2. Cash, Cash Equivalents and Investments, continued

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The University does not have a formal policy to specifically limit investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The University does not have a formal policy for concentration of credit risk.

Custodial Credit Risk

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the University will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The University does not have a formal policy for custodial credit risk.

3. Accounts, Grants and Loans Receivable

Accounts, grants and loans receivable consist of the following as of June 30:

	<u>2007</u>	<u>2006</u>
Student tuition and fees	\$ 768,037	\$ 774,594
Financing and interest	488,878	-
Student loans	3,720,029	3,911,375
Grants and contracts	7,197,727	3,044,081
Auxiliary enterprises	899,049	919,775
Other	<u>23,332</u>	<u>131,278</u>
	13,097,052	8,781,103
Allowance for doubtful accounts	<u>(697,614)</u>	<u>(662,560)</u>
	12,399,438	8,118,543
Current portion	<u>(8,996,258)</u>	<u>(4,290,485)</u>
Noncurrent portion	<u>\$ 3,403,180</u>	<u>\$ 3,828,058</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

4. Capital Assets, Net

Capital assets as of June 30, 2007, are summarized as follows:

<u>Cost</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Land and improvements	\$ 13,088,395	\$ 3,816,416	\$ -	\$ 16,904,811
Buildings	168,772,584	2,077,084	-	170,849,668
Library books	18,260,794	1,034,358	-	19,295,152
Vehicles	2,123,170	105,210	52,551	2,175,829
Equipment and livestock	33,373,663	3,690,487	844,683	36,219,467
Datatel	3,864,369	244,815	-	4,109,184
Art collection	66,075	7,816	-	73,891
Construction in progress	<u>4,227,366</u>	<u>2,985,439</u>	<u>5,682,923</u>	<u>1,529,882</u>
	<u>243,776,416</u>	<u>13,961,625</u>	<u>6,580,157</u>	<u>251,157,884</u>
<u>Accumulated Depreciation</u>				
Land improvements	4,582,575	430,245	-	5,012,820
Buildings	74,090,822	3,589,731	-	77,680,553
Library books	14,010,744	893,988	-	14,904,732
Vehicles	1,648,885	181,353	51,531	1,778,707
Datatel	857,167	782,675	-	1,639,842
Equipment and livestock	<u>27,420,544</u>	<u>1,604,436</u>	<u>587,629</u>	<u>28,437,351</u>
	<u>122,610,737</u>	<u>7,482,428</u>	<u>639,160</u>	<u>129,454,005</u>
Capital assets, net	<u>\$ 121,165,679</u>	<u>\$ 6,479,197</u>	<u>\$ 5,940,997</u>	<u>\$ 121,703,879</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

4. Capital Assets, Net, continued

Capital assets as of June 30, 2006, are summarized as follows:

<u>Cost</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Land and improvements	\$ 12,541,402	\$ 546,993	\$ -	\$ 13,088,395
Buildings	158,395,223	10,377,361	-	168,772,584
Library books	17,245,514	1,015,280	-	18,260,794
Vehicles	2,068,682	121,463	66,975	2,123,170
Equipment and livestock	32,397,054	1,596,718	620,109	33,373,663
Datatel	3,817,294	47,075	-	3,864,369
Art collection	66,075	-	-	66,075
Construction in progress	<u>12,820,855</u>	<u>2,608,948</u>	<u>11,202,437</u>	<u>4,227,366</u>
	<u>239,352,099</u>	<u>16,313,838</u>	<u>11,889,521</u>	<u>243,776,416</u>
<u>Accumulated Depreciation</u>				
Land improvements	4,291,738	290,837	-	4,582,575
Buildings	70,573,253	3,517,569	-	74,090,822
Library books	13,172,768	837,976	-	14,010,744
Vehicles	1,517,631	174,675	43,421	1,648,885
Datatel	91,903	765,264	-	857,167
Equipment and livestock	<u>26,623,295</u>	<u>1,353,205</u>	<u>555,956</u>	<u>27,420,544</u>
	<u>116,270,588</u>	<u>6,939,526</u>	<u>599,377</u>	<u>122,610,737</u>
Capital assets, net	<u>\$ 123,081,511</u>	<u>\$ 9,374,312</u>	<u>\$ 11,290,144</u>	<u>\$ 121,165,679</u>

5. Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities as of June 30, are as follows:

	<u>2007</u>	<u>2006</u>
Payable to vendors and contractors	\$ 3,311,443	\$ 2,433,031
Accrued vacation	1,955,432	1,787,101
Accrued salaries and other liabilities	<u>2,456,727</u>	<u>3,893,981</u>
	<u>\$ 7,723,602</u>	<u>\$ 8,114,113</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

6. Long-Term Liabilities

Long-term liabilities as of June 30, 2007, are summarized as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Current Portion</u>	<u>Long-term Portion</u>
Housing and Dining System Revenue Bonds	\$ 17,820,000	\$ -	\$ 1,490,000	\$ 16,330,000	\$ 1,560,000	\$ 14,770,000
Consolidated Educational Building Revenue Bonds	7,665,000	-	1,250,000	6,415,000	885,000	5,530,000
Capital lease obligations	6,787,189	-	530,627	6,256,562	582,368	5,674,194
Notes payable	<u>240,000</u>	<u>-</u>	<u>110,000</u>	<u>130,000</u>	<u>130,000</u>	<u>-</u>
Total bonds, notes and capital lease obligations	32,512,189	-	3,380,627	29,131,562	3,157,368	25,974,194
Federal refundable grants	<u>4,865,694</u>	<u>-</u>	<u>819,434</u>	<u>4,046,260</u>	<u>-</u>	<u>4,046,260</u>
Total long-term Liabilities	<u>\$ 37,377,883</u>	<u>\$ -</u>	<u>\$ 4,200,061</u>	<u>\$ 33,177,822</u>	<u>\$ 3,157,368</u>	<u>\$ 30,020,454</u>

Long-term liabilities as of June 30, 2006, are summarized as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Current Portion</u>	<u>Long-term Portion</u>
Housing and Dining System Revenue Bonds	\$ 19,430,000	\$ -	\$ 1,610,000	\$ 17,820,000	\$ 1,490,000	\$ 16,330,000
Consolidated Educational Building Revenue Bonds	8,875,000	-	1,210,000	7,665,000	1,250,000	6,415,000
Capital lease obligations	7,118,059	327,764	658,634	6,787,189	585,914	6,201,275
Notes payable	<u>350,000</u>	<u>-</u>	<u>110,000</u>	<u>240,000</u>	<u>110,000</u>	<u>130,000</u>
Total bonds, notes and capital lease obligations	35,773,059	327,764	3,588,634	32,512,189	3,435,914	29,076,275
Federal refundable grants	<u>4,865,694</u>	<u>-</u>	<u>-</u>	<u>4,865,694</u>	<u>-</u>	<u>4,865,694</u>
Total long-term Liabilities	<u>\$ 40,638,753</u>	<u>\$ 327,764</u>	<u>\$ 3,588,634</u>	<u>\$ 37,377,883</u>	<u>\$ 3,435,914</u>	<u>\$ 33,941,969</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

6. Long-Term Liabilities, continued

The following is a summary of bonds, capital lease obligations and notes payable as of June 30:

	<u>2007</u>	<u>2006</u>
2.75 – 5.75% Housing and Dining System Revenue Bonds, Series N, O, P, Q, and R repayable in annual installments with the final installment due May, 2020	\$ 16,330,000	\$ 17,820,000
2.00 – 5.75% Consolidated Educational Building Revenue Bonds, Series L and M repayable in annual installments with the final installment due May, 2024	6,415,000	7,665,000
5.00% Capital lease obligation with the Foundation, repayable in monthly installments with the final installment due February, 2019	167,053	178,642
5.04% Capital lease obligation with a finance corporation	-	1,190
9.50% Note payable to an individual, repayable in annual installments with the final installment due January, 2008	100,000	200,000
9.50% Note payable to an individual, repayable in annual installments with the final installment due January, 2008	30,000	40,000
5.75% Capital lease obligation with the Foundation, repayable in monthly installments with the final installment due February, 2012	591,735	635,049
9.40% Capital lease obligation with the Foundation, repayable in monthly installments with the final installment due March, 2023	422,157	433,496
4.19% Capital lease obligation with a finance corporation in semi-annual payments with final installment due October, 2019	1,593,042	1,688,308
3.58% Capital lease obligation with a finance corporation in semi-annual payments with final installment due June, 2015	3,205,527	3,545,955
4.47% Capital lease obligation with the Foundation, repayable in monthly installments with the final installment due August, 2015	<u>277,048</u>	<u>304,549</u>
	<u>\$ 29,131,562</u>	<u>\$ 32,512,189</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

6. Long-Term Liabilities, continued

In order to retire the revenue bonds, the University is required to make deposits to sinking funds in annual amounts sufficient to meet the principal and interest payments due within the next twelve months. As of June 30, 2007 and 2006, the reserve requirements have been fully funded. The revenue bonds are subject to several non-financial covenants, all of which management has asserted were met as of June 30, 2007 and 2006.

The revenue bonds are collateralized by various buildings. The revenues derived from student registration fees and residence hall rental fees are pledged as collateral on the revenue bond issues.

The capital leases consist of leases of real estate and equipment. The leased equipment includes items related to an energy savings project and a new computer system.

The following equipment is held under capital lease obligations as of June 30:

	<u>2007</u>	<u>2006</u>
Equipment	\$ 7,722,742	\$ 7,722,742
Less: accumulated depreciation	<u>1,857,386</u>	<u>975,193</u>
	<u>\$ 5,865,356</u>	<u>\$ 6,747,549</u>

The following is a schedule by years of future minimum payments required for the capital lease obligations as of June 30, 2007:

Year ending June 30,		
2008		\$ 870,653
2009		870,653
2010		870,653
2011		870,653
2012		870,653
Thereafter		<u>3,561,210</u>
Total minimum lease payments		7,914,475
Less: amounts representing interest		<u>(1,657,913)</u>
Present value of minimum lease payments		<u>\$ 6,256,562</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

6. Long-Term Liabilities, continued

The principal and interest repayment requirements relating to the outstanding bonds and notes payable as of June 30, 2007, are as follows:

Year ending June 30,	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2008	\$ 2,575,000	\$ 925,067	\$ 3,500,067
2009	2,555,000	819,046	3,374,046
2010	2,655,000	718,570	3,373,570
2011	2,420,000	620,240	3,040,240
2012	2,210,000	532,611	2,742,611
2013-2024	<u>10,460,000</u>	<u>2,278,673</u>	<u>12,738,673</u>
	<u>\$ 22,875,000</u>	<u>\$ 5,894,207</u>	<u>\$ 28,769,207</u>

7. Pension Plan

Kentucky Teachers Retirement System

All faculty and exempt employees required to hold a degree and occupying full-time positions, defined as seven-tenths (7/10) of normal full-time service on a daily or weekly basis, are required by state law to participate in the Kentucky Teachers Retirement System (KTRS). KTRS, a cost sharing, multiple-employer, public employee retirement system, provides retirement benefits based on an employee's final average salary and number of years service. Benefits are subject to certain reductions if the employee retires before reaching age sixty, unless the employee has twenty-seven or more years of participation in the plan. The plan also provides for disability retirement, death and survivor benefits, and medical insurance.

The Kentucky Teachers Retirement System issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to Kentucky Teachers Retirement System, 479 Versailles Road, Frankfort, Kentucky 40601-3868 or by calling (502) 573-5120.

Funding for the plan is provided from eligible employees who contribute 6.16% of their salary through payroll deductions and the Commonwealth of Kentucky, which also indirectly contributes 13.84% of currently eligible employees' salaries to the KTRS through appropriations to the University. Contribution requirements of the plan members and the University are established by Kentucky Revised Statute and the KTRS Board of Trustees. The University's contributions to KTRS for the years ending June 30, 2007 and 2006 were \$4,087,232 and \$4,033,605 respectively, equal to the required contributions for each year.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

7. Pension Plan, continued

Kentucky Employee Retirement System

Substantially all other full-time University employees are required by law to participate in the Kentucky Employees Retirement System (KERS), a cost sharing multiple-employer, public employee retirement system. KERS provides retirement benefits based on an employee's final average salary and number of years of service. Benefits are subject to certain reductions if the employee retires before reaching age sixty-five, or less than twenty-seven years of service. The plan also provides for disability retirement, death and survivor benefits and medical insurance.

The Kentucky Employees Retirement System issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to Kentucky Employees Retirement System, 1260 Louisville Road, Perimeter Park West, Frankfort, Kentucky 40601 or by calling (502) 564-4646.

Funding for the plan is provided from eligible hazardous and non-hazardous employees who contribute 8.00% and 5.00%, respectively of their salary through payroll deductions and the Commonwealth of Kentucky, which also indirectly contributes 22.00% and 7.75%, respectively of current eligible hazardous and non-hazardous employees' salaries to the KERS through appropriations to the University. University contribution rates are determined by the Kentucky Revised Statute and the Board of Trustees of the Kentucky Retirement Systems each biennium. The University's contributions to KERS for the years ending June 30, 2007, and 2006 were \$946,117 and \$724,921 respectively, equal to the required contributions for each year.

Optional Retirement Plans

Optional retirement plans (ORP's) are available to employees hired on or after January 1, 1997, who would otherwise be participants in the Kentucky Teachers' Retirement System. The ORP is established as a 403(b) defined contribution plan under the Internal Revenue Code guidelines. The providers of the University's ORP's are the Teachers Insurance and Annuity Association-College Retirement Equities Fund, Variable Annuity Life Insurance Company and International Netherlands Group. Under these plans the employee's contribution is 6.16% of their gross salary and the University's contribution is 4.41% to the retirement company and 9.43% to Kentucky Teachers Retirement System. The University's contributions under these plans to Kentucky Teachers Retirement System for the years ending June 30, 2007 and 2006 were \$860,697 and \$694,125 respectively, equal to the required contributions for each year.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

8. Operating Leases

The University has operating lease agreements for use of equipment and various parcels of real estate cancelable annually with the option to renew. The University recognizes the expenditures related to those obligations as lease payments are made. Total rent expenses under operating type leases were approximately \$588,000 and \$356,000 in 2007 and 2006, respectively.

9. Contingencies and Commitments

The University is a defendant in two lawsuits; however, University management is of the opinion, based on advice of legal counsel, that the ultimate resolution of these litigation matters will not have a material effect on the future operations or financial position of the University.

The University receives financial assistance from federal and state agencies in the form of grants and awards. The expenditure of funds received under these programs generally requires compliance with terms and conditions specified in the grant agreements and are subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become a liability of the applicable fund. The University had no disallowed claims in the past. In the opinion of management, such potential disallowed claims, if any, would not have a material adverse effect on the overall financial position of the University at June 30, 2007.

The University has made certain commitments related to the completion of various construction projects in progress totaling approximately \$22,200,000. Such construction is principally financed by appropriations from the Commonwealth of Kentucky and proceeds from bonds.

10. Self-Insurance Program

The University maintains a self-insurance program for employees' dental insurance. The University funds the plan at the single rate for all permanent full-time employees with the employees paying the difference between the single plan and the family plan, if applicable. Expenses incurred to cover claims paid by the University under the plan for fiscal year ending June 30, 2007 and 2006 totaled \$291,411 and \$281,078, respectively.

Beginning January 1, 2006, the University switched from a self-insured health plan to a fully insured health plan. The University pays a sliding percentage of premiums for all permanent full-time employees. Depending on the level of coverage, this amount ranges from a low of \$248 per month to a high of \$562 per month. Payments for employee health insurance for both plans for fiscal years ending June 30, 2007 and 2006 were \$4,784,039 and \$4,424,812, respectively.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

11. Risk Management

The University is exposed to various risks of loss from torts; theft of, damage to, destruction of assets; business interruption; employee injuries and illnesses; natural disasters; and employee health and accident benefits. Commercial insurance coverage is purchased for claims arising from theft of, damage to, destruction of assets; business interruption; employee injuries and illnesses; natural disasters; and employee health and accident benefits. Settled claims have not exceeded this commercial coverage in any of the three preceding years. As a sovereign entity of the Commonwealth of Kentucky, the Kentucky Board of Claims handles tort claims on behalf of the University.

The Commonwealth of Kentucky operates a public entity risk pool operating as a common risk management and insurance program for its members. The University pays an annual premium to the pool for its workers' compensation insurance coverage. The pool's governing agreement specifies that the pool will be self-sustaining through member premiums and will reinsure through commercial carriers for claims in excess of specified stop loss amounts.

12. Friends of Kentucky Folk Art Center, Inc.

The Friends of Kentucky Folk Art Center, Inc. (KFAC) provides educational opportunities, benefits and programs to the public to enhance the awareness of and foster an appreciation and understanding of contemporary folk art. Under an operating agreement, the University provides office space and certain administrative services to the KFAC at no charge. As a result of the 1998 General Assembly's legislative decision to appropriate \$200,000 annually to KFAC as an affiliate of the University, the KFAC became an affiliated corporation in accordance with the provisions of KRS 164A.610. The financial statements of this affiliated corporation are reported upon separately. However, the assets, liabilities and net assets of KFAC have been included in the University's financial statements.

13. Segment Information

A segment is an identifiable activity reported as a stand-alone entity for which one or more revenue bonds are outstanding. A segment has a specifically identifiable revenue stream pledged in support of revenue bonds and has related expenses, gains and losses, assets, and liabilities, that are required by an external party to be accounted for separately. The University has one segment that meets the reporting requirements of GASB No. 35, which is the University Housing and Dining System.

The Housing and Dining System is an organizational unit of the University that manages the University's student dormitory housing units. The gross revenues from the dormitory housing units are pledged for retirement of the Housing and Dining System Revenue Bonds.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

13. Segment Information, continued

Condensed Statement of Net Assets as of June 30:

	2007	2006
	<u>Housing</u>	<u>Housing</u>
	<u>and Dining</u>	<u>and Dining</u>
Assets		
Current assets	\$ 875,457	\$ 665,394
Noncurrent assets	2,979,108	3,267,828
Accounts receivable	927,621	-
Capital assets, net	<u>23,245,863</u>	<u>23,925,146</u>
Total assets	<u>28,028,049</u>	<u>27,858,368</u>
Liabilities		
Current liabilities	1,560,000	1,490,000
Noncurrent liabilities	<u>14,770,000</u>	<u>16,330,000</u>
Total liabilities	<u>16,330,000</u>	<u>17,820,000</u>
Net assets		
Invested in capital, net of related debt	6,915,863	6,105,146
Restricted, expendable	<u>4,782,186</u>	<u>3,933,222</u>
Total net assets	<u>\$11,698,049</u>	<u>\$10,038,368</u>

Condensed Statement of Revenues, Expenses and Changes in Net Assets for the years ended June 30:

	2007	2006
	<u>Housing</u>	<u>Housing</u>
	<u>and Dining</u>	<u>and Dining</u>
Operating revenues	\$ 7,144,698	\$ 6,815,320
Operating expenses	(6,087,700)	(4,905,026)
Depreciation expense	<u>(808,661)</u>	<u>(1,687,861)</u>
Operating income	248,337	222,433
Nonoperating revenue	192,221	180,131
Nonoperating expenses	<u>(744,266)</u>	<u>(804,724)</u>
Deficiency of revenues over expenses	(303,708)	(402,160)
Transfer from MSU operating account	<u>1,963,389</u>	-
Change in net assets	1,659,681	(402,160)
Net assets, beginning of year	<u>10,038,368</u>	<u>10,440,528</u>
Net assets, end of year	<u>\$11,698,049</u>	<u>\$10,038,368</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

13. Segment Information, continued

Condensed Statement of Cash Flows for the years ended June 30:

	2007	2006
	<u>Housing and Dining</u>	<u>Housing and Dining</u>
Net cash flows from operating activities	\$129,377	\$1,910,294
Net cash flows from investing activities	480,941	839,785
Net cash flows from capital and related financing activities	<u>(400,255)</u>	<u>(3,262,776)</u>
Net increase (decrease) in cash and cash equivalents	210,063	(512,697)
Cash and cash equivalents, beginning of year	<u>665,394</u>	<u>1,178,091</u>
Cash and cash equivalents, end of year	<u>\$ 875,457</u>	<u>\$ 665,394</u>

14. Endowment Trust Funds

The Foundation holds endowment investments for the University, the majority of which are associated with the Regional University Excellence Trust Fund (RUETF). The RUETF was created by the Kentucky General Assembly with the passage of the Postsecondary Education Improvement Act of 1997 ("House Bill 1"). The RUETF Endowment Match Program, also known as "Bucks for Brains", provides state funds on a dollar-for-dollar basis. Funds are endowed for the purposes of supporting endowed chairs and professorships.

The fair market value of Morehead State University endowment funds held by the Foundation as of June 30, 2007 and 2006 was \$23,398,371 and \$20,857,833, respectively. The portion of the endowments representing the value of the funding received from the Kentucky General Assembly was \$11,329,598 for both the years ended June 30, 2007 and 2006, and is included in investments held by the Foundation.

15. Related Parties

The University and the Foundation are related parties. The Foundation's purpose is to assist in the development, growth, expansion and progress of the student programs of Morehead State University. The University authorizes the Foundation to solicit contributions on its behalf. In the absence of donor restrictions, the Foundation has discretionary control over the amounts and timing of its distributions to the University.

Related party transactions and funds held by the Foundation on behalf of the University are as follows during 2007 and 2006:

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

15. Related Parties, continued

	<u>2007</u>	<u>2006</u>
Funds disbursed by the University on behalf of the Foundation for employee salaries and benefits	\$ 77,347	\$ 63,628
Funds held by the Foundation on behalf or for the Benefit of the University as of June 30	\$11,329,598	\$11,329,598
Funds due to the University by the Foundation	\$ 107,600	\$ 117,600

The University entered into an agreement with the Foundation where the University will provide personnel, office space, support equipment and other services that may be necessary to the operation of the Foundation. The Foundation reimburses the University for these services at a rate determined mutually by the two entities of \$30,000 per year. Amounts disclosed above as funds disbursed by the University on behalf of the Foundation for employee salaries and benefits are net of the \$30,000 per year.

The University has also entered into several direct financing capital leases of real estate with the Foundation as disclosed in Note 17H.

16. Subsequent Event

On August 13, 2007 the University sold General Receipts Bonds for \$6,445,000. These bonds will be amortized over twenty years, and will be used to fund the renovation of a residence hall and an expansion of the wellness center.

17. Morehead State University Foundation, Inc.

A. Description of Organization

The Morehead State University Foundation, Inc. (the Foundation) is a corporation formed for educational, charitable and public purposes in accordance with the provisions of KRS 273.0010. The Foundation is a component unit of Morehead State University (the University). Specifically, it was founded to cooperate with the University and its Board of Regents in the promotion of the educational, civic and charitable purposes of the University in any lawful manner deemed appropriate by the Foundation's Board of Trustees. This purpose includes the encouragement of scholarship and research and the promotion of the prestige, expansion and development of the University's physical plant and faculty and the assistance of its students and alumni.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

17. Morehead State University Foundation, Inc., continued

B. Summary of Significant Accounting Policies

The preparation of financial statements prepared in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from these estimates. The following is a summary of the significant accounting policies consistently followed by the Foundation in the preparation of its financial statements.

Basis of Presentation

The Foundation's financial statements are presented in accordance with Statement of Financial Accounting Standards (SFAS) No. 117, *Financial Statements of Not-for-Profit Organizations*. Under these standards net assets and revenues, expenses, gains and losses are classified based upon the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Foundation and changes therein are classified and reported as follows:

Unrestricted net assets: Net assets that are not subject to donor-imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of the Board of Trustees.

Temporarily restricted net assets: Net assets whose use by the Foundation is subject to donor-imposed stipulations that can be fulfilled by actions of the Foundation pursuant to those stipulations or that expire by the passage of time.

Permanently restricted net assets: Net assets subject to donor-imposed stipulations that neither expire by the passage of time nor can be fulfilled or otherwise removed. Generally, donors of these assets permit the Foundation to use all or part of the income earned on related investments for general or specific purposes.

Pledges Receivable

Pledges receivable of amounts greater than \$500, less an appropriate allowance amount, are recorded at the net present value of estimated future cash flows using a discount rate commensurate with the risks involved. Net present value was computed using a discount rate of 5.25 percent for both years ended June 30, 2007 and 2006, respectively.

The allowance for doubtful accounts is established through a provision for doubtful accounts charged to expense. The allowance represents an amount, which, in management's judgment, will be adequate to absorb probable losses on existing pledges that may become uncollectible.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

17. Morehead State University Foundation, Inc., continued

B. Summary of Significant Accounting Policies, continued

Pledges Receivable

Pledges receivable of amounts greater than \$500, less an appropriate allowance amount, are recorded at the net present value of estimated future cash flows using a discount rate commensurate with the risks involved. Net present value was computed using a discount rate of 5.25 percent for both years ended June 30, 2007 and 2006, respectively.

The allowance for doubtful accounts is established through a provision for doubtful accounts charged to expense. The allowance represents an amount, which, in management's judgment, will be adequate to absorb probable losses on existing pledges that may become uncollectible.

Investments

Investments in equity securities having a readily determinable fair value and all debt securities are carried at fair value. Investment returns include dividend, interest and other investment income and realized and unrealized gains and losses on investments carried at fair value. Investment returns that are initially restricted by donor stipulation and for which the restriction will be satisfied in the same year are included as unrestricted net assets. Other investment returns are reflected in the statement of activities as unrestricted, temporarily restricted or permanently restricted based upon the existence and nature of any donor or legally imposed restrictions.

Property and Equipment

Property and equipment is stated at cost at the date of acquisition or fair value at date of donation. Expenditures with a cost greater than \$1,000, which increase values or extend useful lives of the respective assets, are capitalized, whereas expenditures for maintenance and repairs are charged to expense as incurred. Depreciation of assets is computed using the straight-line method over the estimated useful lives of the respective assets.

Funds Held in Trust for Morehead State University

The Foundation is the custodian of funds owned by the University for the purpose of establishing certain endowment funds as authorized by the Kentucky Council on Postsecondary Education and the Kentucky General Assembly. The Foundation invests the principal with a portion of the income derived from the principal to be remitted annually to the University. For the years ended June 30, 2007 and 2006, the Foundation held \$11,329,598 for the University's investment purposes.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

17. Morehead State University Foundation, Inc., continued

B. Summary of Significant Accounting Policies, continued

Annuities Payable

The Foundation pays stipulated amounts periodically to individuals (annuitants) who have given to the Foundation certain assets and who have entered into agreements that such payments cease at the death of the annuitant. Total annuity payments for the years ended June 30, 2007 and 2006 were \$66,387 and \$63,807, respectively.

The June 30, 2007 and 2006 annuity liabilities balances of \$382,433 and \$332,179 are the present values of the monthly, quarterly, or semiannual payments to the annuitants based on the life expectancies of the annuitants and interest rates ranging from 7.8% to 9.9%. The estimated remaining life expectancies of the annuitants range from 6.0 to 9.6 years and 7.1 to 10.1 years for the years ended June 30, 2007 and 2006, respectively.

Due to Morehead State University

A gift was pledged to the Foundation that the donor stipulated was specifically for the University. In accordance with SFAS No. 136, *Transfers of Assets to a Not-for-Profit Organization or Charitable Trust That Raises or Holds Contributions for Others*, the gift has been included as a liability on the Foundation's Statement of Financial Position.

Contributions

Gifts of cash and other assets received without donor stipulations are reported as unrestricted revenue and net assets. Gifts received with a donor stipulation that limits their use are reported as temporarily or permanently restricted revenue and net assets. When a donor-stipulated time restriction ends or the purpose of the restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. Gifts and investment income that are originally restricted by the donor and for which the restriction is met in the same time period are included in unrestricted net assets.

Gifts of land, buildings, equipment, and other long-lived assets are reported as unrestricted revenue and net assets unless explicit donor stipulations specify how such assets must be used, in which case the gifts are reported as temporarily or permanently restricted revenue and net assets. Absent explicit donor stipulations for the time long-lived assets must be held, expirations of restrictions resulting in the reclassification of temporarily restricted net assets to unrestricted net assets are reported when the long-lived assets are placed in service.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

17. Morehead State University Foundation, Inc., continued

B. Summary of Significant Accounting Policies, continued

Unconditional gifts expected to be collected within one year are reported at their net realizable value. Unconditional gifts expected to be collected in future years are recorded at the present value of estimated future cash flows. The resulting discount is computed using risk-free interest applicable to the years in which the promises are received. Amortization using the level-yield method is included in contribution revenue. Conditional gifts are not included as support until the conditions are substantially met.

Donated Materials and Property

Donated materials and property are recorded at their estimated fair value when received. The Statement of Activities for the years ended June 30, 2007 and 2006 includes in-kind contributions of \$387,445 and \$583,130, respectively.

Functional Allocation of Expenses

The costs of supporting the various programs and other activities have been summarized on a functional basis in the Statements of Activities. Certain costs have been allocated among the functional categories based on their relationship to various direct costs in those functions.

Tax Exempt Status

The Foundation is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code, except for tax on any unrelated business income activities. No provision for income taxes has been made.

C. Investments

Investments held as of June 30, 2007 and 2006 are summarized as follows:

	<u>2007</u>	<u>2006</u>
Money market funds	\$ -	\$ 515,845
Certificates of deposit	1,068,343	1,059,386
Mutual funds	27,922,610	24,503,653
Corporate bonds and stocks	37,875	36,394
Annuity investment	<u>116,983</u>	<u>113,201</u>
Total investments at fair value	<u>\$29,145,811</u>	<u>\$26,228,479</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

17. Morehead State University Foundation, Inc., continued

C. Investments, continued

Investment management fees were approximately \$65,000 and \$43,000 during the years ended June 30, 2007 and 2006, respectively.

D. Pledges Receivable

Pledges receivable have been designated to be paid by donors as follows:

Year ended June 30		
2008	\$	713,674
2009		243,866
2010		185,614
2011		177,444
2012		64,550
Thereafter		<u>70,350</u>
		1,455,498
Less: present value discount		(139,885)
Less: allowance for uncollectible pledges		<u>(145,550)</u>
Pledges receivable, net		1,170,063
Less: current pledges receivable		<u>(650,914)</u>
Noncurrent pledges receivable	\$	<u>519,149</u>

E. Property and Equipment

Property and equipment as of June 30, 2007 and 2006 consist of the following:

	<u>2007</u>	<u>2006</u>
Land	\$ 53,000	\$ 53,000
Furniture and equipment	134,819	133,223
Buildings	<u>175,000</u>	<u>175,000</u>
	362,819	361,223
Less: accumulated depreciation	<u>(95,571)</u>	<u>(68,889)</u>
	<u>\$ 267,248</u>	<u>\$ 292,334</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

17. Morehead State University Foundation, Inc., continued

F. Deferred Giving Program

The Foundation established a life insurance deferred giving program during 1983. The program consists of donors designating the Foundation as the owner and beneficiary of life insurance policies. There are twenty deferred giving programs with life insurance in effect totaling \$640,000 for the years ended June 30, 2007 and 2006. The cash surrender value of these policies as of June 30, 2007 and 2006 is \$105,235 and \$85,443, respectively.

G. Support for Morehead State University

The Foundation's purpose is to assist in the development, growth, expansion and progress of the student programs of Morehead State University. All support to the University has been disclosed separately on the Statement of Activities as "University support".

H. Net Investment in Capital Leases

The Foundation's net investment in direct financing capital leases of real estate as of June 30, 2007 and 2006 is as follows:

	<u>2007</u>	<u>2006</u>
Total minimum lease payments to be received	\$2,137,341	\$2,378,620
Less: unearned income	<u>(679,346)</u>	<u>(799,935)</u>
Net investment in capital leases	<u>\$1,457,995</u>	<u>\$1,578,685</u>

The following is a schedule of future minimum lease payments due from direct financing capital leases as of June 30:

2008	\$ 241,279
2009	241,279
2010	241,279
2011	241,279
2012	241,279
Thereafter	<u>930,946</u>
	<u>\$2,137,341</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

17. Morehead State University Foundation, Inc., continued

I. Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are available at June 30, 2007 and 2006 for the following purposes:

	<u>2007</u>	<u>2006</u>
Funds restricted for specific purposes	\$5,115,438	\$ 2,686,272
Scholarships	1,347,754	1,182,546
Athletics	<u>1,155,008</u>	<u>773,095</u>
	<u>\$7,618,200</u>	<u>\$ 4,641,913</u>

Permanently restricted net assets at June 30, 2007 and 2006 consist of endowment funds.

Temporarily restricted net assets consist of the following as of June 30:

	<u>2007</u>	<u>2006</u>
Pledges receivable	\$ 451,554	\$ 166,493
Investments	<u>7,166,646</u>	<u>4,475,420</u>
	<u>\$ 7,618,200</u>	<u>\$ 4,641,913</u>

Permanently restricted net assets consist of the following as of June 30:

	<u>2007</u>	<u>2006</u>
Pledges receivable	\$ 658,054	\$ 760,145
Investments	<u>12,293,592</u>	<u>11,774,092</u>
	<u>\$12,951,646</u>	<u>\$ 12,534,237</u>

J. Related-Party Transactions

The University entered into an agreement with the Foundation where the University will provide personnel, office space, support equipment and other services that may be necessary to the operation of the Foundation. The Foundation reimburses the University for these services at a rate determined mutually by the two entities of \$30,000 per year.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

17. Morehead State University Foundation, Inc., continued

J. Related-Party Transactions, continued

SFAS No. 116, *Accounting for Contributions Received and Contributions Made*, requires recognition of professional services received if those services (a) create long-lived assets or (b) require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation. Those services in excess of \$30,000 per year are considered in-kind contributed services and are treated as both revenue and expense to the Foundation.

Transactions with the University include direct financing capital leases and support for the University as disclosed in Notes 7 and 8.

K. Concentration of Credit Risk

The Foundation has a concentration of credit risk in that it maintains cash deposits in financial institutions which, at times, exceed federally insured limits. Cash deposits in excess of the federally insured limits total \$1,149,246 and \$965,049 as of June 30, 2007 and 2006, respectively. The Foundation has not experienced any losses in such accounts and does not believe it is exposed to any significant credit risk related to the accounts.

SUPPLEMENTAL INFORMATION

MOREHEAD STATE UNIVERSITY

Schedule of Bonds, Notes and Capital Lease Obligations

June 30, 2007

	<u>Issue Date</u>	<u>Net Amount of Issue</u>	<u>Interest Cost</u>	<u>Outstanding June 30, 2006</u>	<u>Retired Bonds 2006-07</u>	<u>New Issues</u>	<u>Outstanding June 30, 2007</u>	<u>Interest Paid 2006-07</u>	<u>Debt Service Requirements 2007-08</u>	
									<u>Principal</u>	<u>Interest</u>
Housing and Dining System Revenue Bonds:										
Series I	11/01/66	3,920,000	3.00	-	-	-	-	-	-	-
Series N	06/01/00	4,790,000	5.0-5.75	4,010,000	180,000	-	3,830,000	215,891	190,000	206,364
Series O	06/01/00	4,625,000	5.0-5.25	2,540,000	515,000	-	2,025,000	118,032	545,000	91,002
Series P	07/01/01	5,125,000	2.75-4.9	4,175,000	200,000	-	3,975,000	181,410	210,000	173,515
Series Q	04/16/03	4,485,000	3.25	3,320,000	425,000	-	2,895,000	98,400	440,000	85,425
Series R	06/01/03	4,270,000	3.682	3,775,000	170,000	-	3,605,000	130,532	175,000	126,864
Total housing and dining system		<u>27,215,000</u>		<u>17,820,000</u>	<u>1,490,000</u>	-	<u>16,330,000</u>	<u>744,265</u>	<u>1,560,000</u>	<u>683,170</u>
Consolidated Educational Building Revenue Bonds:										
Series L	12/01/01	4,875,000	5.5-5.75	2,930,000	770,000	-	2,160,000	120,763	390,000	90,925
Series M	01/01/04	5,620,000	2.0-3.3625	4,735,000	480,000	-	4,255,000	149,423	495,000	138,622
Total educational buildings		<u>10,495,000</u>		<u>7,665,000</u>	<u>1,250,000</u>	-	<u>6,415,000</u>	<u>270,186</u>	<u>885,000</u>	<u>229,547</u>
Lease Purchase Agreements:										
G.E. Capital	01/26/01	457,000	5.04	1,190	1,190	-	-	-	-	-
MSU Foundation, Inc.	03/01/99	240,000	5.0	178,642	11,589	-	167,053	7,340	10,821	8,107
MSU Foundation, Inc.	07/15/02	990,000	5.75	635,049	43,314	-	591,735	86,470	78,313	51,470
MSU Foundation, Inc.	10/21/02	466,457	9.4	433,496	11,339	-	422,157	40,674	12,452	39,561
Citi Mortgage, Inc.	03/31/05	1,824,000	4.19	1,688,308	95,266	-	1,593,042	69,753	99,299	65,719
Suntrust Bank, Inc.	06/15/05	3,874,522	3.58	3,545,955	340,428	-	3,205,527	122,735	352,728	111,628
MSU Foundation, Inc.	09/01/05	327,764	4.47	304,549	27,501	-	277,048	13,054	28,755	11,800
Total lease purchase agreements		<u>8,179,743</u>		<u>6,787,189</u>	<u>530,627</u>	-	<u>6,256,562</u>	<u>340,026</u>	<u>582,368</u>	<u>288,285</u>

MOREHEAD STATE UNIVERSITY

Schedule of Bonds, Notes and Capital Lease Obligations, continued

June 30, 2007

	<u>Issue Date</u>	<u>Net Amount of Issue</u>	<u>Interest Cost</u>	<u>Outstanding June 30, 2006</u>	<u>Retired Bonds 2006-07</u>	<u>New Issues</u>	<u>Outstanding June 30, 2007</u>	<u>Interest Paid 2006-07</u>	<u>Debt Service Requirements 2007-08</u>	
									<u>Principal</u>	<u>Interest</u>
Notes Payable:										
Fred White	06/01/01	\$700,000	9.5	\$200,000	\$100,000	-	\$100,000	\$19,000	\$100,000	\$9,500
Freddie White	06/01/01	90,000	9.5	40,000	10,000	-	30,000	3,800	30,000	2,850
Total notes payable		<u>790,000</u>		<u>240,000</u>	<u>110,000</u>	-	<u>130,000</u>	<u>22,800</u>	<u>130,000</u>	<u>12,350</u>
Total		<u>\$46,679,743</u>		<u>\$32,512,189</u>	<u>\$3,380,627</u>	-	<u>\$29,131,562</u>	<u>\$1,377,277</u>	<u>\$3,157,368</u>	<u>\$1,213,352</u>

MOREHEAD STATE UNIVERSITY

Schedules of Housing System Revenues and Expenditures

Year ended June 30, 2007

Revenues:	
Housing fees	\$ 7,144,698
Interest income	<u>192,221</u>
	<u>7,336,919</u>
Operating expenditures:	
Residence hall grants	84,088
Maintenance and IT allocations	3,243,045
Residence hall services	1,313,325
Student housing	675,707
Residence hall building services	355,544
Telephone	298,144
Married student housing	<u>117,847</u>
	<u>6,087,700</u>
Revenues in excess of operating expenditures	<u>1,249,219</u>
Debt service expenditures:	
Principal	1,490,000
Interest	<u>744,266</u>
	<u>2,234,266</u>
Deficiency of revenues over expenditures	<u>\$ (985,047)</u>

MOREHEAD STATE UNIVERSITY

Schedule of Bond Reserves

June 30, 2007

	Sinking Fund	Housing and Dining System Debt Service Reserve Fund	Repair Fund	Consolidated Educational Building Bonds	Totals
Balances, beginning of year	\$ 135,699	\$2,515,534	\$ 591,203	\$1,996,246	\$5,238,682
Receipts and other additions:					
Transfers, net	1,382,045	-	99,412	-	1,481,457
Income from investments	<u>2,677</u>	<u>107,137</u>	<u>29,313</u>	<u>92,751</u>	<u>231,878</u>
Total available funds	<u>1,384,722</u>	<u>107,137</u>	<u>128,725</u>	<u>92,751</u>	<u>1,713,335</u>
Disbursements and other deductions:					
Transfers, net	-	370,290	-	-	370,290
Redemption of bonds	1,250,000	-	-	-	1,250,000
Payment of interest	270,185	-	-	-	270,185
Administrative fees	<u>225</u>	<u>-</u>	<u>-</u>	<u>7,108</u>	<u>7,333</u>
Total disbursements and other deductions	<u>1,520,410</u>	<u>370,290</u>	<u>-</u>	<u>7,108</u>	<u>1,897,808</u>
Balances, end of year	<u>\$ 11</u>	<u>\$2,252,381</u>	<u>\$ 719,928</u>	<u>\$2,081,889</u>	<u>\$5,054,209</u>

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2007

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
U.S. Department of Education:			
Direct Programs:			
Student Financial Aid Cluster:			
National Science and Mathematics Access to Retain Talent Grant Program		84.375	\$ 281,326
Academic Competitiveness Grant Program		84.376	173,139
Federal Work Study Program		84.033	551,940
Federal Pell Grant Program		84.063	9,925,950
Federal Supplemental Educational Opportunity Grants Program		84.007	449,844
Federal Perkins Loan Program		84.038	3,695,503
Federal Direct Loans Program		84.268	27,405,021
			<hr/> 42,482,723
Trio Cluster:			
CEOC - NE 04-07		84.066	451,127
CEOC - SE 02-07		84.066	217,019
Student Support Services 01-06		84.042	72,470
Student Support Services 06-07		84.042	262,957
Talent Search 02-06		84.044	464,310
Talent Search II 02-06		84.044	252,600
Upward Bound Central 05-06		84.047	504,513
Upward Bound Math/Science 04-06		84.047	212,056
Upward Bound East 03-06		84.047	255,556
			<hr/> 2,692,608
Gear-up IRAPP 00-05		84.334	771,237
Mandzy-Fulbright 06		84.019	59,015
Hail-IFIR 05-07		84.116	203,605
Hail-IRC 05-07		84.116	232,140
Patrick-SI 05-06		84.031	298,640
			<hr/> 46,739,968

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2007

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
Passed through Council on Postsecondary Education:			
Kentucky Gear-up 05-06	M-05508393	84.334	45,416
Kentucky Gear-up 06-07	M-05508393	84.334	163,657
Gunn - CPE 07-08	P0241506400047151	84.367	9,321
			<u>218,394</u>
Passed through Kentucky Department of Education:			
TE 01 AHS 06-07	RCG 05-082	84.048	2,633
TE 01 IS 06-07	RCG 05-082	84.048	3,066
TE 01 IET 06-07	RCG 05-082	84.048	5,468
Spangler - KDE06	M-06084525	84.048	6,844
Cleveland KDE 06-07	M-06126813	84.298	21,513
First Coach 06-07	M-06091930	84.357	236,484
			<u>276,008</u>
Passed through Western Kentucky University:			
Teacher Quality 05-06	WKURF 543604-05-38	84.336	28,338
Passed through Department of Vocational Rehabilitation:			
CDP Rehab 06-08	M-06189260	84.126	557,785

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2007

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
Passed through Kentucky Workforce Development Cabinet:			
TE 02 IET 06-07	RCG 05-081	84.048	3,029
TE 02 Carryfwd 06-07	TE-02	84.048	7,321
Title 1c IS 06-07	M-06157071	84.048	8,948
Title 1c IET 06-07	M-06157071	84.048	45,482
Title 1c RS 06-07	M-06157071	84.048	54,242
Title 1c NAHS 06-07	M-06157071	84.048	54,487
Title 1c AHS 06-07	M-06157071	84.048	58,411
Fiscal Agent 06-07	M-06190288	84.048	108,857
			<u>340,777</u>
Passed through National Writing Project Corp.:			
NWP#13 05-06	94-KY07 (#13)	84.928	58,394
Passed through Office of Career & Technical Education:			
Math/CTE Tech Ed 06-07	P02531060000097011	84.019	148,866
Total U. S. Department of Education			<u>48,368,530</u>
United States Department of Health and Human Services - National Institute of Health:			
Direct Programs:			
Prefont Cortex 03-06		93.242	3,839

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2007

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
Passed through University of Louisville Research Foundation:			
INBRE - Fultz 06-07	5T20RR016481-06	93.385	13,459
INBRE - DeMoss 07-08	OGMB040388C	93.385	17,599
INBRE - Mattingly 07-08	2P20RR016481-07	93.385	21,644
INBRE - White 07-08	2P20RR016481-07	93.385	28,382
INBRE - Mattingly 06-07	2P20RR016481-06	93.385	44,086
INBRE - White 06-07	2P20RR016481-06	93.385	116,019
INBRE - DeMoss 06-07	2P20RR016481-06	93.385	124,720
			<u>365,909</u>
Passed through Kentucky Families And Children:			
STEPS 06-08	M-06069677	93.558	41,201
Passed through Eastern Kentucky University:			
PCWCP - Pburg 06-07	P0273606000002621	93.648	6,039
PCWCP - Ashland 06-07	P0273606000002621	93.648	7,720
PCWCP - Morehead 06-07	P0273606000002621	93.648	9,198
MSU Training 06-07	P0273670600002621	93.658	97,958
			<u>120,915</u>
Passed through University of Kentucky Research Foundation:			
Nurse Practitioner 04-05	UKRF 4-63922-01-284	93.247	56,470
Passed through Johns Hopkins University:			
White-JHU 05-06	8512-47647-X	93.848	9,945

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2007

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
Passed through Kentucky Seniors Saving Medicare:			
KY Medicare 06-07	RCG 05-158	93.048	37,595
KY Medicare 07-08	90AM313302	93.048	3,300
			<u>40,895</u>
Total U.S. Department of Health and Human Services - National Institute of Health			<u>639,174</u>
Corporation for National and Community Service:			
Direct Programs:			
RSVP 03-06		94.002	101,190
Passed through Kentucky Cabinet for Families and Children:			
Promise Corps 05-06	M-04185843	94.006	66,455
Total Corporation for National and Community Service			<u>167,645</u>
National Science Foundation			
Direct Programs:			
CSMS 03-07		47.076	2,105
NSF-Jerde 04-07		47.050	16,012
			<u>18,117</u>

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2007

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
Passed through University of Kentucky			
Research Foundation:			
AMSP 02-05	4-66358-03-191	47.076	235,523
Tuerk - EPSCoR	304688440007416	47.076	1,387
Chatham - EPSCoR	2006-07-084	47.076	8,257
Remillard-UKRF 06/07	304688440006407	47.076	9,812
Hare-KY NSF EPS 06-07	RCG-05-073	47.076	15,166
			<hr/> 270,145
Passed through Kentucky NSF:			
Symbiotic Star	RCG 2003-04-006	47.076	231
Cetiner-KYNSF 05-06	3046901800-05-49	47.076	3,727
Feria-KYNSF 05-06	4-69018-05-496	47.076	13,214
			<hr/> 17,172
Total National Science Foundation			<hr/> <hr/> 305,434
Small Business Administration:			
Passed through University of Kentucky:			
SBDC Federal 06-07	04-60301-20018-25	59.037	102,247
SBDC Federal 05-06	04-60301-20018-25	59.037	35,580
			<hr/> 137,827
Total Small Business Administration			<hr/> <hr/> 137,827
U.S. Department of Agriculture:			
Direct Programs:			
USDA 05-07		10.769	56,596

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2007

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
Passed through Kentucky Department of Education:			
Up Bound Food 06	103-X30-999-SU	10.558	15,038
McMichael-KDF 06-07	P0259506000015171	10.558	<u>2,823</u>
			17,861
			<u>74,457</u>
Total U.S. Department of Agriculture			
U.S. Department of Labor:			
Passed through TENCO Workforce Investment Board:			
Today's Youth 06-07	FY07-5245	17.250	<u>80,505</u>
National Oceanic and Atmospheric Administration:			
Passed through Eastern Kentucky Pride:			
Pride 05/07	RSG 2005-06-054	11.469	<u>203,660</u>
U.S. Department of Housing/Urban Development:			
Direct Programs:			
COPC 02-05		14.551	3,579
Hail-ACRP 04-06		14.243	119,807
Kenney-HUD 06-07		14.246	<u>117,499</u>
			<u>240,885</u>
Total U.S. Department of Housing/ Urban Development			

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2007

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
Appalachian Regional Commission:			
Direct Programs:			
KY AHED Duvall 04-07		23.001	164,772
ARC-Nursing Lab 06-07		23.002	107,965
			<u>272,737</u>
Passed through East Tennessee State University:			
Bortolot ETSU 05-06	5-30773-4	23.011	<u>1,578</u>
Total Appalachian Regional Commission			<u>274,315</u>
U.S. Department of Justice:			
Passed through UNITE:			
Krug-UNITE 06	06MH02 - 4	16.580	14,120
Krug-UNITE 07	07MH01	16.580	5,292
			<u>19,412</u>
Passed through University of Kentucky Research Foundation			
Hail-Hometown Security 05-08	304691600-06-428	16.560	<u>10,709</u>
Total U.S. Department of Justice			<u>30,121</u>
U.S. Department of the Interior:			
Direct Programs:			
Parkansky-USGS 05-09		15.808	<u>41,664</u>

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2007

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
U.S. Environmental Protection Agency: Passed through University of Louisville Research Foundation:			
Reeder-ULRF 05-06	ULRF G03-1016-07	66.460	16,988
Passed through Shaw Environment:			
Smith-Shaw 06-07	EPC04034	66.439	<u>6,235</u>
Total U.S. Environmental Protection Agency			<u>23,223</u>
National Aeronautics and Space Administration: Passed through Western Kentucky University:			
Boram - KSGC 05-06	WKU 516171-06-14	43.001	6,647
Doyle - NASA EPS 05-06	WKU 516171-06-15	43.001	1,736
NASA Travel 05-06	WKU 516171-06-21	43.001	8,000
Malphrus-KYSP 06	WKU 516171-06-36	43.001	10,400
Malphrus-Scholar 06	WKU 516171-06-38	43.001	2,400
Malphrus-WKU-Intern	WKU 516171-07-01	43.001	8,906
NASA Travel 06-07	WKU 516171-07-02	43.001	1,500
Malphrus-Carter 06-07	WKU 516171-07-46	43.001	15,000
Malphrus-Atwood 06-07	WKU 516171-07-58	43.001	<u>3,930</u>
Total National Aeronautics and Space Administration			<u>58,519</u>

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2007

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
National Highway Transportation Safety Board: Passed through Kentucky State Police: Krug-HRD 06-07	2005-AH-FX-0003	20.601	<u>41,328</u>
U.S. Department of Transportation: Passed through University of Kentucky Research Foundation: Blanken-UKRF	3046962300-06-286	16.560	6,425
Passed through Governor's Highway Safety Program: Krug-HRD 06-08	2006-50062-KY-AH	16.727	<u>22,894</u>
Total U.S.Department of Transportation			<u>29,319</u>
National Endowment for the Humanities: Direct Programs: Collinwor-NEA 06-08	06-4448-7108	45.024	14,246
Passed through Kentucky Humanities Council : Little-KHC 05-06	XT2006-002	45.129	<u>123</u>
Total National Endowment for the Humanities			<u>14,369</u>
National Endowment for the Arts: Passed through Southern Arts Foundation: Towell-SAF 06-07	SAF-2818	45.025	<u>5,050</u>

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2007

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
U.S. Department of Commerce: Direct Programs:			
Hail-NOAA 05-06		11.400	<u>390,847</u>
 Total Expenditures of Federal Awards			 <u>\$ 51,126,872</u>

MOREHEAD STATE UNIVERSITY

Notes to Schedule of Expenditures of Federal Awards

1. Basis of Presentation

The accompanying schedule of expenditures of federal awards includes the federal grant activity of Morehead State University (the "University") and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments and Non-profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

2. Federal Student Loan Programs

Loans made by the University to eligible students under the Federal Perkins Loan Program and federal student loans issued by the Federal Direct Loan Program during the year ended June 30, 2007 are summarized as follows:

Federal Perkins Loan Program:	
Loans disbursed	\$ 707,055
Federal Direct Loan Program:	
Federal Subsidized Stafford Loans	\$ 13,718,959
Federal Unsubsidized Stafford Loans	11,684,780
Federal Plus Loans	2,001,282

As of June 30, 2007, the University had loans outstanding, in the amount of \$3,695,503 with an allowance for doubtful accounts of \$107,465 under the Federal Perkins Loan Program.



Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Members of the Board of Regents and
Dr. Wayne D. Andrews, President
Morehead State University
Morehead, Kentucky

We have audited the financial statements of Morehead State University (the University) as of and for the years ended June 30, 2007 and 2006, and have issued our report thereon dated November 26, 2007. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the University's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the University's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified a certain deficiency in internal control over financial reporting that we consider to be a significant deficiency.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the University's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the University's financial statements that is more than inconsequential will not be prevented or detected by the University's internal control. We consider the deficiencies described in the accompanying schedule of findings and questioned costs to be significant deficiencies in internal control over financial reporting, items 07-1 and 07-2.



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A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the University's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider item 07-1 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the University's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of 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.

We noted certain other matters that we reported to management of the University in a separate letter dated November 26, 2007.

The University's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit the University's response and, accordingly, we express no opinion on it.

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

November 26, 2007
Lexington, Kentucky





Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133

Members of the Board of Regents and
 Dr. Wayne D. Andrews, President
 Morehead State University
 Morehead, Kentucky

Compliance

We have audited the compliance of Morehead State University (the “University”) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2007. The University’s major federal programs are identified in the summary of auditors’ results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the University’s management. Our responsibility is to express an opinion on the University’s compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the University’s compliance with those requirements and performing such other procedures, as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the University’s compliance with those requirements.

In our opinion, Morehead State University complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2007.

Internal Control Over Compliance

The management of Morehead State University is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the University’s internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the



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purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness if the University's internal control over compliance.

A control deficiency in a University's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the University's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the University's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the University's internal control.

Our consideration of the internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

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

November 26, 2007
Lexington, Kentucky

Wheeler, Winton + Jones, P.C.

MOREHEAD STATE UNIVERSITY

Schedule of Findings and Questioned Costs

Year ended June 30, 2007

Section I – Summary of Auditors’ Results (under Section .505(d)(1) of OMB Circular A-133):

Financial Statements:

- a. The type of report issued on the financial statements: **Unqualified Opinion**
- b. Material weaknesses in internal control over financial reporting: **Yes**
Significant deficiencies identified that are not considered to be material weaknesses: **Yes**
- c. Non-compliance which is material to the financial statements: **No**

Federal Award:

- d. Material weaknesses in internal control over major programs: **No**
Significant deficiencies identified that are not considered to be material weaknesses: **No**
- e. The type of report issued on compliance for major programs: **Unqualified Opinion**
- f. Any audit findings which are required to be reported under Section .510(a) of OMB Circular A-133: **No**
- g. Major programs:
 - Student Financial Aid Custer:**
 - Federal Pell Grants, CFDA 84.063**
 - Federal Work Study, CFDA 84.033**
 - Federal Supplemental Educational Opportunity Grants, CFDA 84.007**
 - Federal Perkins Loans, CFDA 84.038**
 - Federal Direct Loan Program, CFDA 84.268**
 - Academic Competitiveness Grant, CFDA 84.375**
 - National Science and Mathematics Access to Retain Talent Grant, CFDA 84.268**
- h. Dollar threshold used to distinguish between Type A and Type B programs: **\$512,000**
- i. Auditee qualified as a low-risk auditee: **Yes**

MOREHEAD STATE UNIVERSITY

Schedule of Findings and Questioned Costs, continued

Year ended June 30, 2007

Section II – Financial Statement Findings (under Section .505(d)(2) of OMB Circular A-133):

Findings Relating to the Financial Statements Reported in Accordance with
Government Auditing Standards: 07-01 and 07-02.

Finding 07-1:

Condition:

Our audit procedures revealed that after the departure of the Assistant Director of Accounting & Budgetary Control in March 2007 there was no systematic method of ensuring that timely and complete monthly reconciliation and closing procedures were taking place. However, a Statement of Revenues, Expenses and Changes in Net Assets was produced on a quarterly basis for the first three quarters of fiscal year ended June 30, 2007. A complete set of internal financial statements, which would include a Statement of Net Assets, was not produced during the year.

Effect:

This situation results in a delay in getting transactions and journal entries posted to the accounting system in a timely manner. Not having transactions posted in a timely manner can affect the financial statement information that is available for making informed business decisions and supervision of operations. This weakness in accounting infrastructure increases the risk of errors in the financial records and is less likely to detect irregularities, including fraud, on a timely basis.

Recommendation:

This situation should be corrected as soon as possible with the establishment of a system of consistent monthly reconciliations and closing procedures. Consistent application of established procedures is dependent upon adequate staffing to ensure that systems will continue to operate in the event of turnover or extended absences in senior level accounting positions. In that respect, it is recommended that an appropriate number of senior level accounting staff be added.

MOREHEAD STATE UNIVERSITY

Schedule of Findings and Questioned Costs, continued

Year ended June 30, 2007

Finding 07-1, continued:

Management's Response:

Datatel Colleague was brought up "Live" on July 1, 2006.

While Statements of Net Assets (Balance Sheets) were not being produced on FRx, the report writer that was purchased to accompany Datatel Colleague, we were able to produce Statements of Revenues, Expenditures and Changes in Net Assets (SRECNA) throughout the fiscal year. These statements were provided to the Board of Regents on a quarterly basis. In order to provide accurate SRECNA information, all current funds assets and liabilities were adjusted, which for the most part would flow to the SRECNA.

Additionally, viewing of budgets has been available (and used) throughout the fiscal year by units, divisions and offices across campus. This was done through WebAdvisor, a tool by which personnel across campus track their budgets and the charges against them. It has been our experience that personnel who are charged with overseeing budgets have done so and question any discrepancies that they have found.

We have recently hired three additional full time personnel to work in the Research and Sponsored Programs and bank reconciliation areas of Accounting and Budgetary Control. Full time personnel will enable us to catch up on processes and procedures that have gotten behind due to major turnover in personnel and the new computer system. Also, we have hired an Assistant Director for Accounting and Reporting.

We agree that these areas should be corrected as soon as possible, and intend to do so by putting the personnel, processes and technology together to accomplish that goal.

Finding 07-2:

Condition:

There is no formalized process or procedure in place for the University's system changes. Based on interviews with the Information Technology (IT) department heads, there are verbal policies being used. These policies do not appear to be consistent across the IT organization. Also, there is limited technical documentation of changes made to critical systems. Furthermore, there is no formal policy that prohibits testing of new functionality in the production environment.

MOREHEAD STATE UNIVERSITY

Schedule of Findings and Questioned Costs, continued

Year ended June 30, 2007

Finding 07-2, continued:

Effect:

This could cause undesirable stability and functionality issues.

Recommendation:

The University should develop a written change control process that provides proper documentation and testing for system changes. The process should include individuals allowed to request system changes, testing requirements, contingency planning and exception handling.

Management's Response:

This recommendation is recognized as a critical need and is partially complete with remaining work in progress. Currently in place are documented procedures for scheduling, preparing, and testing all official patches and updates received from Datatel for the new Colleague system, as well as, the specific steps that are performed by the Systems Administrator to perform the actual install patch or update. Written logs are maintained by the Associate Director of Administrative Computing which includes official signoff from each functional unit lead to indicate their completion of the review and test process before each patch or update was moved into production.

Work is currently in process by the staff in Administrative Computer Applications to create comparable set up procedures that will outline how requests for in-house-driven customizations will be handled on the new system including who can request a customization, process for review and approval of the request, customization planning processes, testing procedures when customizations have been completed, suggested alternative processes to customization request, potential impact and exception handling. This work is scheduled to be complete in the first quarter of 2008 which is the timeframe that we anticipate in-house customizations can begin to be considered. Based on the audit recommendation, we will also initiate work to develop a written policy that prohibits staff from testing new functionality in the production environment and complete that policy in the first quarter of 2008.

Section III – Federal Award Findings and Questioned Costs (under Section .505(d)(3) of OMB Circular A-133):

Findings and Questioned Costs relating to Federal Awards: **None**

MOREHEAD STATE UNIVERSITY

Summary Schedule of Prior Audit Findings

Year ended June 30, 2007

Finding 06-01:

Condition:

During our audit, we noted that several cash accounts had not been reconciled to the general ledger and reviewed in a timely manner.

Recommendation:

We recommend that the University establish more effective reconciliation and review procedures as a customary part of the accounting process. This would involve timely reconciliations of all accounts and performing more frequent reviews of the general ledger throughout the year, including making necessary adjustments.

Current Status:

We noted that this issue still existed for the 2007 audit. See Finding 07-1 for further details.

Finding 06-02:

Condition:

During our audit, we noted that a detail grant schedule was being maintained, but the totals did not agree to the financial statements.

Recommendation:

We recommend that a system be implemented such that the detail schedule of grant activity is reconciled to the financial statements on a quarterly basis.

Current Status:

We noted that the schedule agreed to the financial statements for the 2007 audit.