

MOREHEAD STATE UNIVERSITY

Single Audit Reports Under OMB Circular A-133

*As of and for the Years Ended June 30, 2011 and 2010
with Independent Auditors' Report Thereon*

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MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis



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, 2011. 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, 2011. Financial operations were conducted in accordance with the approved budget plan.
- Total assets were \$247 million versus \$243 million at June 30, 2010. Significant components of the assets include \$28 million in cash, \$15 million in accounts, grants and loans receivable, net, \$14 million in investments and \$188 million in capital assets net of depreciation.
- Total liabilities were \$71 million versus \$75 million at June 30, 2010. The significant components of the liabilities were \$54 million in bonds, notes and capital lease obligations, \$8 million in accounts payable

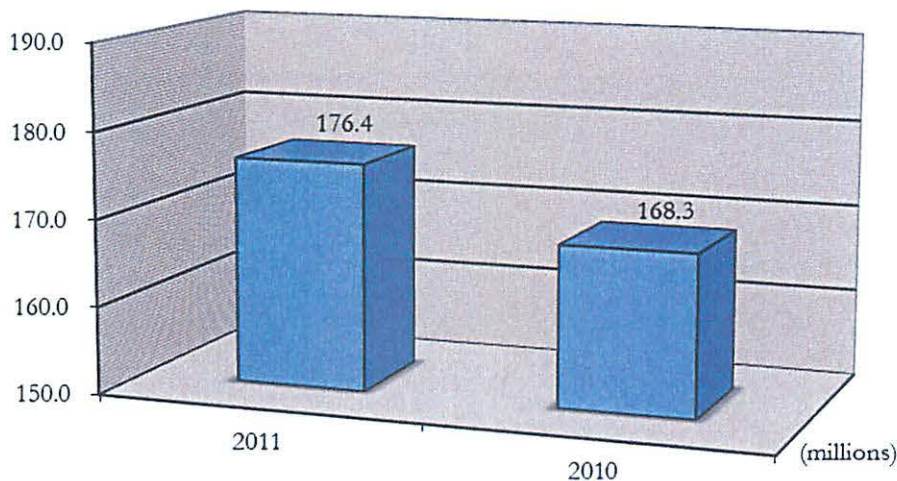
MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued

and accrued liabilities, \$3 million in refundable grants and \$6 million in deferred revenue and other liabilities.

- Total net assets were \$176 million at June 30, 2011 and \$168 million at June 30, 2010. Significant components of net assets include \$135 million invested in capital assets, net of depreciation and related debt, \$10 million in expendable restricted net assets, \$12 million of non-expendable restricted net assets and \$19 million in unrestricted net assets.

**Net Assets
(millions)
June 30, 2011**



- Operating revenues were \$77 million at June 30, 2011 and \$73 million at June 30, 2010. Operating expenses were \$145 million versus \$140 million at June 30, 2010. This created an operating loss of \$68 million at June 30, 2011 and \$67 million at June 30, 2010.
- Net non-operating revenues were \$65 million for the year ended June 30, 2011 and \$62 million for the year ended June 30, 2010. Non-operating revenues were comprised primarily of state appropriations. The combination of the net loss from operations, the net non-operating revenues and capital appropriations of \$11 million, resulted in an increase in net assets of \$8 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:

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

These statements present financial information of the University in a format similar to that used by corporations and present 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

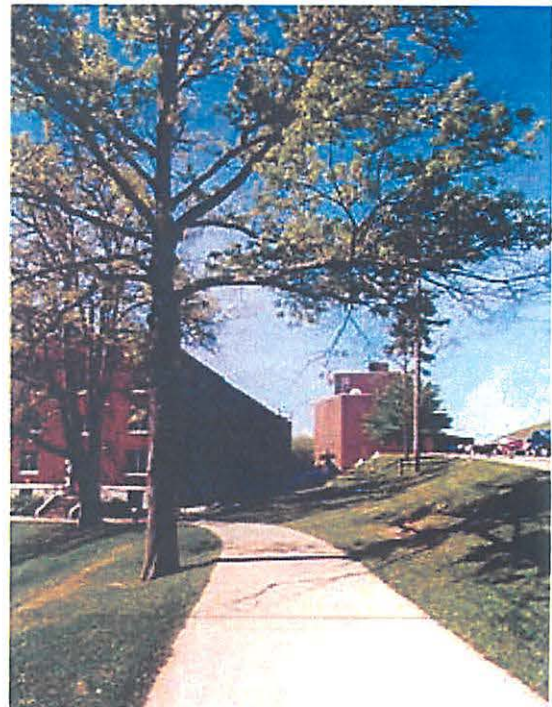
This statement presents the revenues earned and expenses incurred during the year. Activities are reported as either operating or non-operating. GASB 35 requires state appropriations and gifts to be classified as non-operating revenues. Accordingly, the University will generate a net operating loss prior to the addition of non-operating 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.



MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued

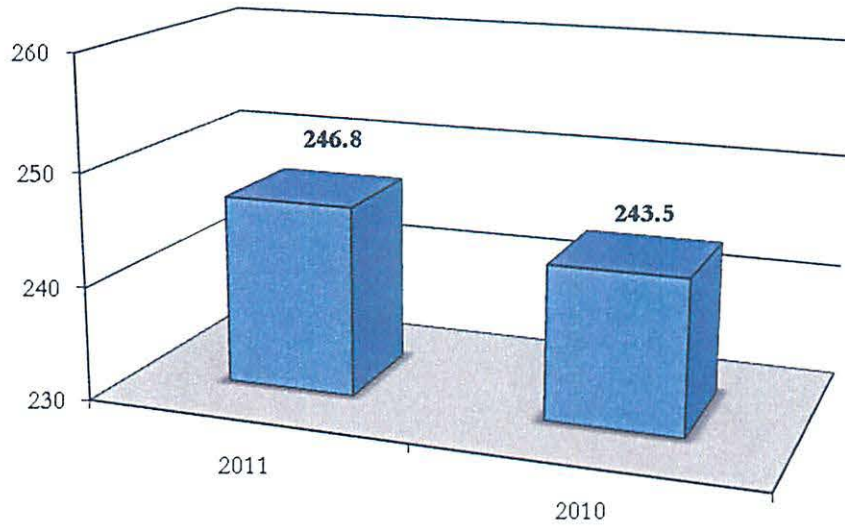
Condensed Financial Information
Statements of Net Assets (in thousands)

	<u>2011</u>	<u>2010</u>
<u>Assets</u>		
Current assets	\$ 41,325	\$ 53,966
Capital assets	187,797	171,964
Other noncurrent assets	<u>17,670</u>	<u>17,531</u>
Total assets	<u>246,792</u>	<u>243,461</u>
<u>Liabilities</u>		
Current liabilities	17,769	17,441
Noncurrent liabilities	<u>52,998</u>	<u>57,658</u>
Total liabilities	<u>70,767</u>	<u>75,099</u>
<u>Net Assets</u>		
Invested in capital assets, net of related debt	134,593	114,660
Restricted, expendable	10,121	24,044
Restricted, nonexpendable	12,427	12,012
Unrestricted	<u>18,884</u>	<u>17,646</u>
Total net assets	<u>\$ 176,025</u>	<u>\$ 168,362</u>

MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued

**Total Assets
(millions)
June 30, 2011**



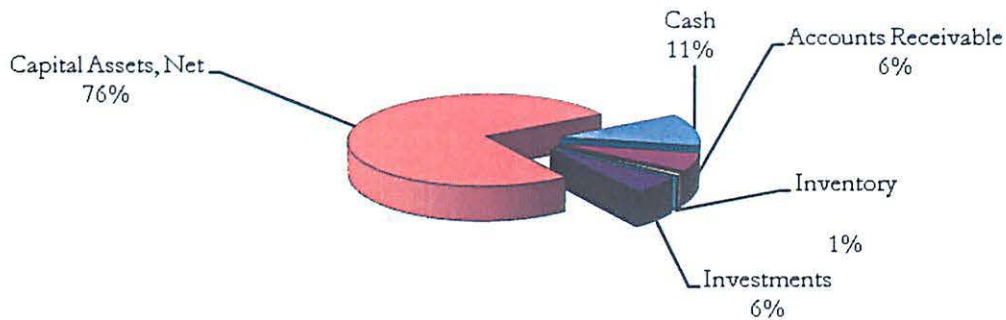
Assets

As of June 30, 2011, the University's total assets amount to approximately \$247 million versus \$243 million at June 30, 2010. Investment in capital assets, net of depreciation, represented the University's largest asset, totaling \$188 million compared to \$172 million at June 30, 2010. Cash and investments, totaling \$42 million at June 30, 2011 and \$51 million at June 30, 2010, were the University's next largest asset.

MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued

**Assets
(millions)
June 30, 2011**



Total assets increased by \$3.3 million during the year ended June 30, 2011. The principal areas of change were:

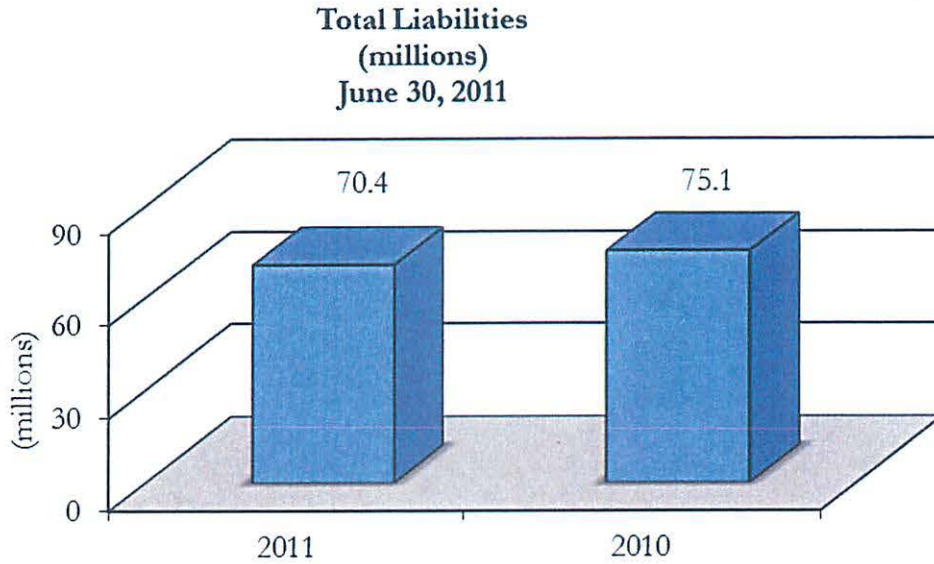
- cash and cash equivalents decreased approximately \$9.6 million,
- accounts, grants and loans receivable, net decreased approximately \$3.3 million,
- capital assets, net of accumulated depreciation, increased approximately \$15.8 million,
- investments and other assets increased approximately \$0.5 million

Liabilities

At June 30, 2011, the University's liabilities totaled approximately \$71 million versus \$75 million the previous year. Bonds, notes payable and capital lease obligations for capital assets represented \$54 million versus \$58 million at June 30, 2010.

MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued



Total liabilities decreased by \$4.3 million during the year ended June 30, 2011. This decrease was primarily due to a \$4.2 million decrease in bonds, notes and capital lease obligations and a decrease of \$0.1 million in deferred revenue and other liabilities.

Net Assets

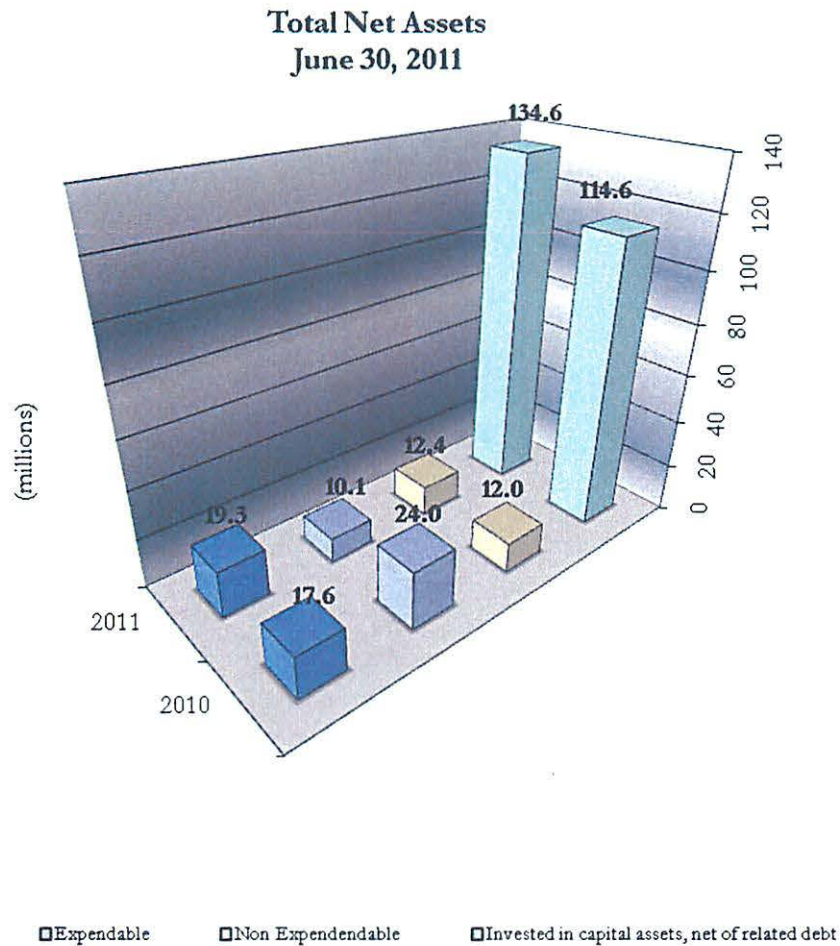
Net assets at June 30, 2011 totaled approximately \$176 million compared to \$168 million at June 30, 2010. Net assets invested in capital assets, net of related debt, totaled \$135 million versus \$115 million at June 30, 2010. Restricted net assets totaled \$22 million compared to \$36 million at June 30, 2010. Unrestricted net assets accounted for \$19 million versus \$18 million at June 30, 2010. Total net assets increased by \$8 million during the year ended June 30, 2011.

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 \$20 million.

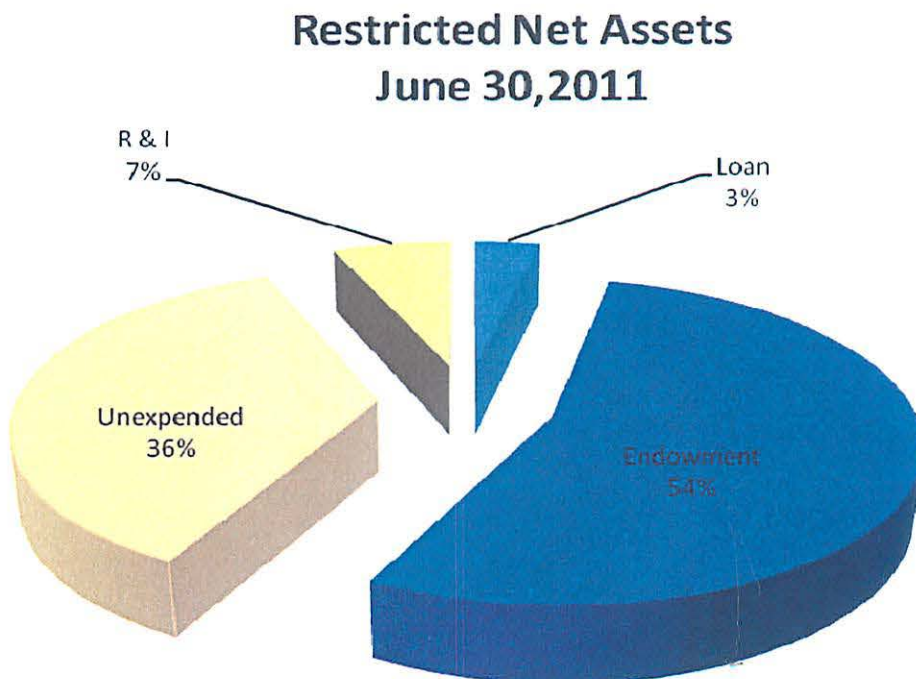


MOREHEAD STATE UNIVERSITY

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 \$14 million from the previous year to \$22 million. This was due to decreases in unexpended restricted net assets.



Unrestricted Net Assets

Unrestricted net assets increased by \$1.2 million from the previous year to \$18.9 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, 2011 is as follows:

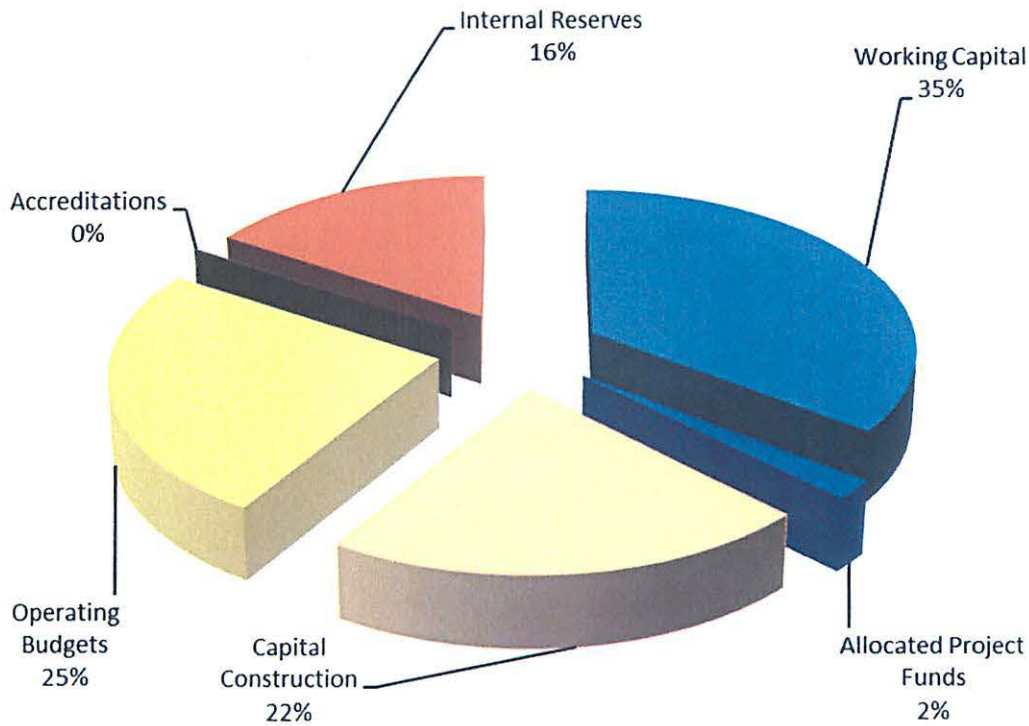
MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued

Allocation of Unrestricted Net Assets (in thousands)

	<u>2011</u>	<u>2010</u>
Working capital	\$ 6,829	\$ 6,962
Allocated project funds	371	821
Capital construction	4,222	2,100
Operating budgets	4,874	7,616
Accreditations	30	80
Internal reserves	<u>2,558</u>	<u>67</u>
Unrestricted net assets	<u>\$ 18,884</u>	<u>\$ 17,646</u>

**Allocation of Unrestricted Net Assets
June 30, 2011**



MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued

Statements of Revenue, Expenses and Changes in Net Assets (in thousands)

	<u>2011</u>	<u>2010</u>
<u>Operating Revenues</u>		
Student tuition and fees, net	\$ 36,597	\$ 33,583
Federal grants and contracts	16,730	17,491
State and local grants and contracts	1,714	1,999
Nongovernmental grants and contracts	610	831
Sales and services of educational activities	2,354	2,663
Auxiliary enterprises	13,269	13,009
Other operating revenue	<u>5,402</u>	<u>3,786</u>
Total operating revenue	<u>76,676</u>	<u>73,362</u>
<u>Operating Expenses</u>		
Educational and general	123,498	118,850
Auxiliary enterprises	12,331	12,710
Depreciation	9,122	8,713
Other operating expenses	<u>98</u>	<u>339</u>
Total operating expenses	<u>145,049</u>	<u>140,612</u>
Operating loss	<u>(68,373)</u>	<u>(67,250)</u>
<u>Non-operating Revenues (Expenses)</u>		
Grants and contracts	22,067	20,954
State appropriations	44,634	43,032
Investment income, net	571	349
Interest on capital assets – debt related	<u>(2,624)</u>	<u>(2,455)</u>
Net non-operating revenues	<u>64,648</u>	<u>61,880</u>
Loss before other revenues, expenses, gains or losses	(3,725)	(5,370)
Capital appropriations	<u>11,389</u>	<u>18,413</u>
Increase in net assets	7,664	13,043
Net assets, beginning of year	<u>168,362</u>	<u>155,319</u>
Net assets, end of year	<u>\$ 176,026</u>	<u>\$ 168,362</u>

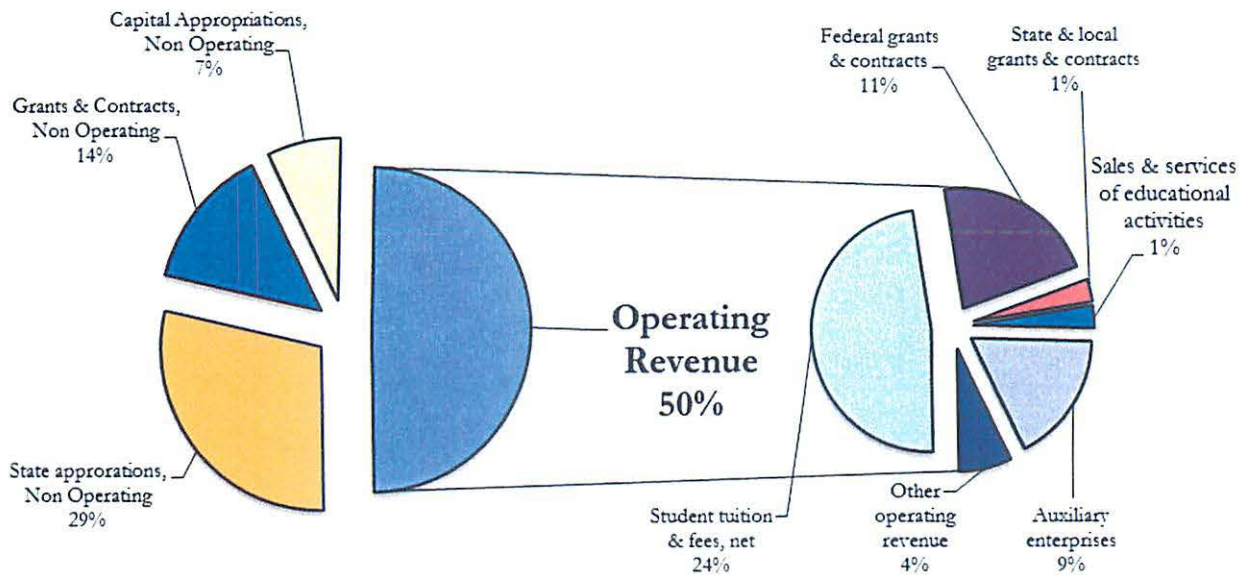
MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued

Revenues

Total operating revenues were approximately \$77 million for the year ended June 30, 2011 and approximately \$73 million for the year ended June 30, 2010. The most significant sources of operating revenue for the University are net student fees \$37 million, federal grants and contracts \$17 million, auxiliary enterprises \$13 million, state and local grants \$2 million and other revenues including, private grants and sales and services of educational activities, \$8 million.

Sources of Revenues
June 30, 2011

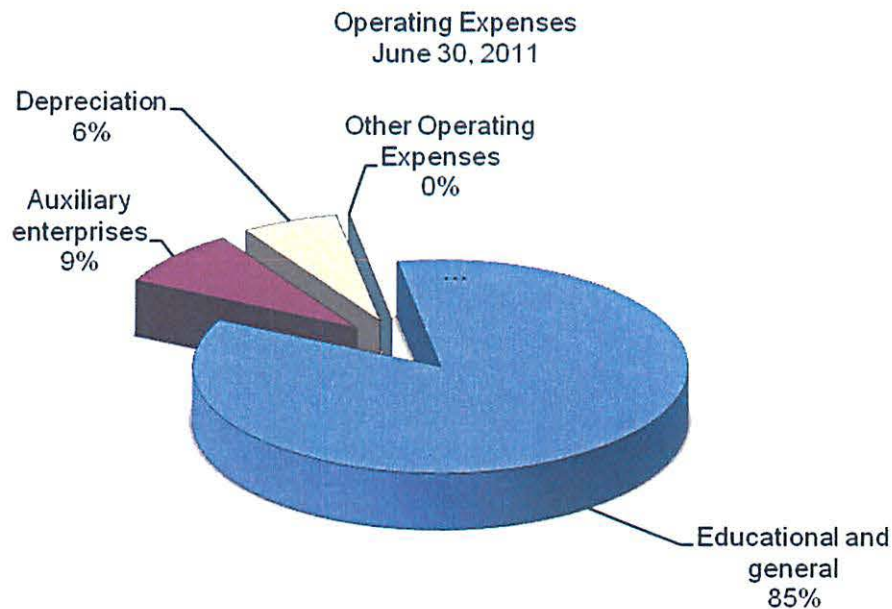


MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, continued

Expenses

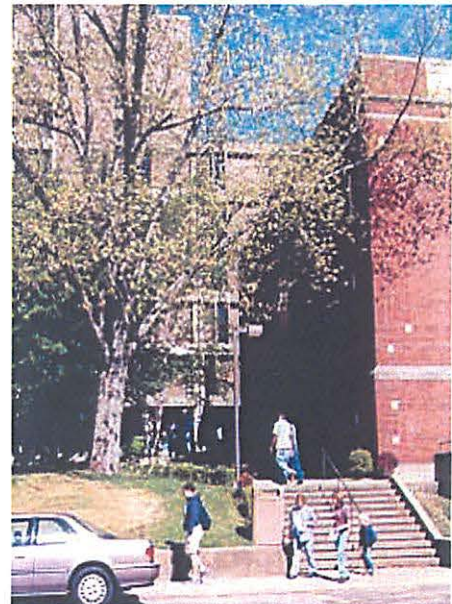
Operating expenses totaled approximately \$145 million compared to \$141 million at June 30, 2010. Of this amount, approximately \$123 million was used for educational and general expenses related to functions such as instruction, research and public service.



Cash Flows

Another way to assess the financial health of an institution is to look at the Statements 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

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

	<u>2011</u>	<u>2010</u>
Cash Provided By (Used In):		
Operating activities	\$ (55,713)	\$ (54,508)
Noncapital financing activities	66,701	63,986
Capital and related financing activities	(20,741)	17,641
Investing activities	<u>179</u>	<u>36</u>
Net (decrease) increase in cash	(9,574)	27,155
Cash, beginning of the year	<u>37,659</u>	<u>10,504</u>
Cash, end of the year	<u>\$ 28,085</u>	<u>\$ 37,659</u>

Major sources of funds included in operating activities are student tuition and fees, \$30.7 million versus \$26.8 million the previous year and grants and contracts, \$19.1 million compared to \$18.7 million the previous year. The largest cash payments for operating activities were made to suppliers \$64.9 million versus \$57.4 million the previous year and employees \$62.0 million compared to \$60.9 million the previous year.



The largest cash receipt in the noncapital financing activities group is the operating appropriation from the Commonwealth of Kentucky of \$44.6 million versus \$43.0 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

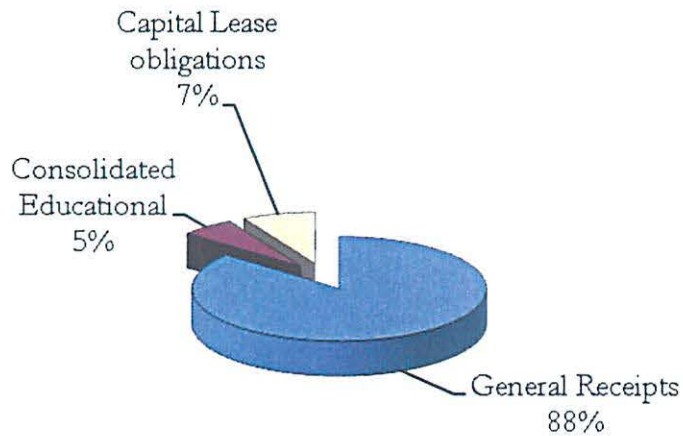
Capital assets, net of accumulated depreciation (but not of related debt), totaled approximately \$187.8 million at June 30, 2011 versus \$172.0 million at June 30, 2010. This represents a net increase of \$15.8 million over June 30, 2010. Significant changes to capital assets during fiscal 2010 - 2011 included:

Buildings and structures	\$ 29.6	million
Library additions, equipment and vehicles	4.8	million
Net change in construction in progress	(10.2)	million
Increase in accumulated depreciation, net	8.4	million

Debt

At year-end, the University had \$53.6 million in outstanding debt versus \$57.8 million the previous year. This includes \$49.8 million in bonds payable compared to \$53.4 million at June 30, 2010. In addition, the University had capital lease obligations of \$3.8 million compared to \$4.4 million the previous year-end.

**Outstanding Debt
June 30, 2011**



MOREHEAD STATE UNIVERSITY

Management's Discussion and Analysis, concluded

Debt, continued

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

	June 30,	
	<u>2011</u>	<u>2010</u>
General Receipts bonds	\$ 47,130	\$ 49,695
Consolidated Educational buildings revenue bonds	2,670	3,660
Capital lease obligations	<u>3,755</u>	<u>4,425</u>
	<u>\$ 53,555</u>	<u>\$ 57,780</u>

Debt outstanding decreased approximately \$4.2 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, 2012 totaling \$135.5 million.
- Under the 2011-12 tuition model, all students will be assessed tuition on a per credit hour basis. The 2011-12 tuition rate includes a 5% increase in the undergraduate resident per credit hour rate with a 60% discount on undergraduate hours enrolled above 12.

DEAN || DORTON || ALLEN || FORD_{PSC}

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, 2011 and the related statement of revenues, expenses, and changes in net assets, and statement of cash flows for the year then ended. 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 audit. The financial statements for the University as of and for the year ended June 30, 2010, were audited by Dean Dorton Ford, PSC, whose report dated September 29, 2010, expressed an unqualified opinion on those statements.

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 statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, 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, 2011 and the respective changes in its net assets and its cash flows for the year 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 7, 2011, 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.

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 audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the University's basic financial statements. The data contained on pages 59 through 60 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 7, 2011
Lexington, Kentucky



MOREHEAD STATE UNIVERSITY

Statement of Net Assets

June 30, 2011 and 2010

	Assets	<u>2011</u>	<u>2010</u>
Current assets:			
Cash and cash equivalents		\$ 28,085,016	\$ 37,659,368
Accounts, grants and loans receivable, net		11,489,241	14,770,254
Prepaid interest		124,649	124,649
Inventories		1,550,106	1,404,776
Other current assets		<u>75,512</u>	<u>6,918</u>
Total current assets		<u>41,324,524</u>	<u>53,965,965</u>
Noncurrent assets:			
Accounts, grants and loans receivable, net		3,681,658	3,809,125
Prepaid interest		226,840	351,488
Investments		13,762,812	13,370,600
Capital assets, net		<u>187,797,068</u>	<u>171,963,970</u>
Total noncurrent assets		<u>205,468,378</u>	<u>189,495,183</u>
Total assets		<u>246,792,902</u>	<u>243,461,148</u>
Liabilities and Net Assets			
Current liabilities:			
Accounts payable and accrued liabilities		7,526,310	8,065,040
Deferred revenue		5,042,812	4,177,568
Other current liabilities		892,637	973,018
Bonds, notes and capital lease obligations, current portion		<u>4,307,643</u>	<u>4,224,982</u>
Total current liabilities		17,769,402	17,440,608
Long-term liabilities:			
Bonds, notes and capital lease obligations, noncurrent portion		49,247,480	53,555,123
Advances from federal government for student loans		3,460,284	3,813,100
Deferred revenue		<u>290,235</u>	<u>290,235</u>
Total long-term liabilities		<u>52,997,999</u>	<u>57,658,458</u>
Total liabilities		<u>70,767,401</u>	<u>75,099,066</u>
Net assets:			
Invested in capital assets, net of related debt		134,593,433	114,660,002
Restricted:			
Expendable		10,120,842	24,043,875
Nonexpendable		12,427,343	12,012,338
Unrestricted		<u>18,883,883</u>	<u>17,645,867</u>
Total net assets		<u>\$ 176,025,501</u>	<u>\$ 168,362,082</u>

See accompanying notes.

MOREHEAD STATE UNIVERSITY FOUNDATION, INC.

Statement of Financial Position

June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Assets		
Current assets:		
Cash	\$ 2,495,337	\$ 561,871
Accounts receivable	1,250	11,748
Accrued interest receivable	7,752	12,488
Current portion of pledges receivable	520,139	297,951
Current portion of net investment in capital leases	<u>62,370</u>	<u>76,097</u>
Total current assets	<u>3,086,848</u>	<u>960,155</u>
Noncurrent assets:		
Investments, at fair value	33,895,166	27,338,067
Cash surrender value – life insurance	108,629	102,299
Property and equipment, net	203,741	218,731
Pledges receivable, net	1,574,990	364,262
Net investment in capital leases	<u>806,540</u>	<u>957,995</u>
Total noncurrent assets	<u>36,589,066</u>	<u>28,981,354</u>
Total assets	<u>\$ 39,675,914</u>	<u>\$ 29,941,509</u>
Liabilities and Net Assets		
Current liabilities:		
Accounts payable	\$ 75,512	\$ -
Annuities payable	175,241	117,581
Due to Morehead State University	<u>-</u>	<u>6,828</u>
Total current liabilities	<u>250,753</u>	<u>124,409</u>
Long-term liabilities:		
Funds held in trust for Morehead State University	12,014,828	11,619,827
Annuities payable	<u>936,770</u>	<u>508,119</u>
Total long-term liabilities	<u>12,951,598</u>	<u>12,127,946</u>
Total liabilities	<u>13,202,351</u>	<u>12,252,355</u>
Net assets:		
Unrestricted	189,514	(155,102)
Temporarily restricted	9,401,972	4,254,520
Permanently restricted	<u>16,882,077</u>	<u>13,589,736</u>
Total net assets	<u>26,473,563</u>	<u>17,689,154</u>
Total liabilities and net assets	<u>\$ 39,675,914</u>	<u>\$ 29,941,509</u>

See accompanying notes.

MOREHEAD STATE UNIVERSITY

Statement of Revenues, Expenses and Changes in Net Assets

Years ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Operating revenues:		
Student tuition and fees (net of scholarship allowances of \$24,551,510 and \$23,463,658)	\$ 36,597,058	\$ 33,583,447
Federal grants and contracts	16,730,415	17,491,129
State and local grants and contracts	1,713,790	1,998,904
Nongovernmental grants and contracts	609,803	831,344
Sales and services of educational activities	2,354,345	2,662,646
Auxiliary enterprises:		
Residence halls (net of scholarship allowances of \$662,367 and \$882,761)	7,479,142	7,300,451
Bookstore	4,421,534	4,406,378
Other auxiliaries	1,367,415	1,301,744
Other operating revenues	<u>5,402,419</u>	<u>3,785,943</u>
Total operating revenues	76,675,921	73,361,986
Operating expenses:		
Education and general:		
Instruction	46,295,191	45,168,444
Research	2,025,681	1,994,360
Public service	6,906,939	7,113,856
Library	3,258,718	3,270,233
Academic support	12,414,159	11,754,564
Student services	15,050,339	13,581,906
Institutional support	15,039,387	14,369,726
Operation and maintenance of plant	9,222,653	8,728,863
Depreciation	9,122,062	8,712,643
Student aid	13,284,719	12,867,825
Auxiliary enterprises:		
Residence Halls	7,350,493	7,741,597
Bookstore	3,691,040	3,819,171
Other auxiliaries	1,289,866	1,149,809
Other operating expenses	<u>97,975</u>	<u>339,436</u>
Total operating expenses	<u>145,049,222</u>	<u>140,612,433</u>
Operating loss	(68,373,301)	(67,250,447)

MOREHEAD STATE UNIVERSITY

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

Years ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Nonoperating revenues (expenses):		
Grants and contracts	22,066,903	20,954,221
State appropriations	44,633,605	43,031,646
Investment income, net	571,172	349,418
Interest on capital asset-related debt	<u>(2,623,868)</u>	<u>(2,454,652)</u>
Net nonoperating revenues	<u>64,647,812</u>	<u>61,880,633</u>
Loss before capital appropriations	(3,725,489)	(5,369,814)
Capital appropriations	<u>11,388,908</u>	<u>18,412,817</u>
Increase in net assets	7,663,419	13,043,003
Net assets, beginning of year	<u>168,362,082</u>	<u>155,319,079</u>
Net assets, end of year	<u>\$ 176,025,501</u>	<u>\$ 168,362,082</u>

See accompanying notes.

MOREHEAD STATE UNIVERSITY FOUNDATION, INC.

Statement of Activities

Year ended June 30, 2011

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Revenues and other support:				
Contributions	\$ 299,697	\$ 3,032,067	\$ 3,292,341	\$ 6,624,105
Other revenue and gains (losses):				
Investment income (loss):				
Interest and dividend income, net	31,999	1,000,690	-	1,032,689
Realized and unrealized losses	47,710	3,347,577	-	3,395,287
In-kind contributed services	97,051	-	-	97,051
Other income	420,637	261,518	-	682,155
Annuities payable adjustment	(301,052)	-	-	(301,052)
Net assets released from restrictions:				
Restrictions satisfied by payments	<u>2,494,400</u>	<u>(2,494,400)</u>	<u>-</u>	<u>-</u>
Total revenues and other support	3,090,442	5,147,452	3,292,341	11,530,235
Expenses:				
Program expenses:				
Contributions to Morehead State				
University for:				
Academic programs	1,293,274	-	-	1,293,274
Athletics	131,960	-	-	131,960
University support:				
Operations and materials	587,922	-	-	587,922
Student financial aid	422,028	-	-	422,028
Athletics	<u>86,176</u>	<u>-</u>	<u>-</u>	<u>86,176</u>
Total program expenses	2,521,360	-	-	2,521,360
General and administrative	180,479	-	-	180,479
Fundraising	<u>43,987</u>	<u>-</u>	<u>-</u>	<u>43,987</u>
Total expenses	<u>2,745,826</u>	<u>-</u>	<u>-</u>	<u>2,745,826</u>
Change in net assets	344,616	5,147,452	3,292,341	8,784,409
Net assets, beginning of year	<u>(155,102)</u>	<u>4,254,520</u>	<u>13,589,736</u>	<u>17,689,154</u>
Net assets, end of year	<u>\$ 189,514</u>	<u>\$ 9,401,972</u>	<u>\$ 16,882,077</u>	<u>\$ 26,473,563</u>

See accompanying notes.

MOREHEAD STATE UNIVERSITY FOUNDATION, INC.

Statement of Activities

Year ended June 30, 2010

	<u>Unrestricted</u>	Temporarily <u>Restricted</u>	Permanently <u>Restricted</u>	<u>Total</u>
Revenues and other support:				
Contributions	\$ 282,273	\$ 2,195,910	\$ 441,984	\$ 2,920,167
Other revenue and gains (losses):				
Investment income:				
Interest and dividend income, net	28,983	781,604	-	810,587
Realized and unrealized gains	22,585	2,901,441	-	2,924,026
In-kind contributed services	101,288	-	-	101,288
Other income	705	471,132	-	471,837
Annuities payable adjustment	(40,016)	-	-	(40,016)
Net assets released from restrictions:				
Restrictions satisfied by payments	<u>2,716,777</u>	<u>(2,716,777)</u>	<u>-</u>	<u>-</u>
Total revenues and other support	3,112,595	3,633,310	441,984	7,187,889
Expenses:				
Program expenses:				
Contributions to Morehead State				
University for:				
Academic programs	1,312,849	-	-	1,312,849
Athletics	294,619	-	-	294,619
University support:				
Operations and materials	808,749	-	-	808,749
Student financial aid	421,789	-	-	421,789
Athletics	<u>57,466</u>	<u>-</u>	<u>-</u>	<u>57,466</u>
Total program expenses	2,895,472	-	-	2,895,472
General and administrative	155,057	-	-	155,057
Fundraising	<u>77,485</u>	<u>-</u>	<u>-</u>	<u>77,485</u>
Total expenses	<u>3,128,014</u>	<u>-</u>	<u>-</u>	<u>3,128,014</u>
Change in net assets	(15,419)	3,633,310	441,984	4,059,875
Net assets, beginning of year	<u>(139,683)</u>	<u>621,210</u>	<u>13,147,752</u>	<u>13,629,279</u>
Net assets, end of year	<u>\$ (155,102)</u>	<u>\$ 4,254,520</u>	<u>\$13,589,736</u>	<u>\$17,689,154</u>

See accompanying notes.

MOREHEAD STATE UNIVERSITY

Statement of Cash Flows

Years ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Cash flows from operating activities:		
Tuition and fees	\$ 30,700,041	\$ 26,839,692
Grants and contracts	19,109,395	18,730,248
Payments to suppliers	(64,889,216)	(57,367,081)
Payments to employees	(62,055,389)	(60,858,247)
Capital appropriations, not yet funded	-	(1,695,799)
Loans issued to students	(236,920)	(669,191)
Collection of loans issued to students	633,276	609,098
Auxiliary enterprises:		
Residence halls	7,479,631	7,688,773
Bookstore	4,419,407	4,466,087
Other auxiliaries	1,370,436	1,299,730
Sales and services of educational activities	2,354,345	2,662,646
Other receipts	<u>5,402,419</u>	<u>3,785,944</u>
Net cash used in operating activities	(55,712,575)	(54,508,100)
Cash flows from noncapital financing activities:		
Nonoperating grants and contracts	22,066,903	20,954,221
State appropriations	<u>44,633,605</u>	<u>43,031,646</u>
Net cash provided by noncapital financing activities	66,700,508	63,985,867
Cash flows from capital and related financing activities:		
Capital appropriations	11,388,908	18,412,817
Purchase of capital assets	(25,053,135)	(29,847,021)
Decrease in advances from federal government for student loan	(352,816)	(35,197)
Issuance of new bonds	-	34,700,000
Principal paid on capital debt and leases	(4,224,982)	(3,259,128)
Interest paid on capital debt and leases	<u>(2,499,220)</u>	<u>(2,330,003)</u>
Net cash (used in) provided by capital and related financing activities	(20,741,245)	17,641,468
Cash flows from investing activities:		
Interest received on investments, net	571,172	349,418
Changes in investments, net	<u>(392,212)</u>	<u>(312,913)</u>
Net cash provided by investing activities	<u>178,960</u>	<u>36,505</u>
Net (decrease) increase in cash and cash equivalents	(9,574,352)	27,155,740
Cash and cash equivalents, beginning of year	<u>37,659,368</u>	<u>10,503,628</u>
Cash and cash equivalents, end of year	<u>\$ 28,085,016</u>	<u>\$ 37,659,368</u>

MOREHEAD STATE UNIVERSITY

Statement of Cash Flows, concluded

Years ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	\$ (68,373,301)	\$ (67,250,447)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation	9,122,062	8,712,643
Loss on disposal of capital assets	97,975	339,436
Bad debt expense	958,747	1,277,212
Changes in assets and liabilities:		
Receivables, net	2,449,733	2,144,793
Inventories	(145,330)	(52,279)
Other current assets	(68,594)	1,528
Accounts payable and accrued liabilities	(538,730)	(333,680)
Deferred revenue	865,244	593,704
Other current liabilities	<u>(80,381)</u>	<u>58,990</u>
Net cash used in operating activities	<u>\$ (55,712,575)</u>	<u>\$ (54,508,100)</u>

See accompanying notes.

MOREHEAD STATE UNIVERSITY

Notes to the 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

University store inventories representing approximately 53% and 50% of total inventories at June 30, 2011 and 2010, respectively, are stated at the lower of cost (retail inventory method) or market. The remainder of the inventories is 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 which increase values or extend useful lives of the respective assets are capitalized. 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
Building improvements	20 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. Deferred revenue also includes tuition billed on or before June 30th for future terms.

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 non-operating 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.

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.

Recent Accounting Pronouncements

In June 2011, the GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. The objective of this statement is to improve financial reporting by standardizing the presentation of deferred outflows of resources and deferred inflows of resources and their effects on net position. It alleviates uncertainty about reporting those financial statement elements by providing guidance where none previously existed. The requirements of this statement are effective for financial statements for periods beginning after December 15, 2011. The University is currently evaluating the effects of this statement on its financial statements.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

1. Organization and Summary of Significant Accounting Policies, continued

Recent Accounting Pronouncements, continued

In December 2010, the GASB issued Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The objective of this statement is to improve financial reporting by contributing to the GASB's efforts to codify all sources of generally accepted accounting principles for state and local governments so that they derive from a single source. It eliminates the need for financial statement preparers to determine which accounting principles apply to state and local governments. The requirements of this statement are effective for financial statements for periods beginning after December 15, 2011. The University does not expect this statement to have a significant impact on its financial statements.

In November 2010, the GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus—an amendment of GASB Statements No. 14 and No. 34*. The objective of this statement is to improve financial reporting for a governmental financial reporting entity. This statement modifies certain requirements for inclusion of component units in the financial reporting entity. This statement also amends the criteria for reporting component units as if they were part of the primary government in certain circumstances. The requirements of this statement are effective for financial statements for periods beginning after June 15, 2012. The University is currently evaluating the effects of this statement on its financial statements.

Subsequent Events

On July 25, 2011, the University sold General Receipts Bonds for \$5,090,000. These bonds will be amortized over twenty years, and will be used to fund the renovation of a residence hall.

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 less than three months.

The state treasurer requires that all state funds be insured by 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 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

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

2. Cash, Cash Equivalents and Investments, continued

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.

At June 30, 2011 and 2010, the University had petty cash funds totaling \$44,576 and \$55,358, respectively and deposits as reflected by bank balances as follows:

	<u>2011</u>	<u>2010</u>
Insured, commercial banks	\$ 265,357	\$ 266,251
Uninsured, commercial banks; collateral held by pledging institution's agent in the University's name	14,432,530	13,139,905
Maintained by Commonwealth of Kentucky	<u>13,342,553</u>	<u>24,197,854</u>
	<u>\$ 28,040,440</u>	<u>\$ 37,604,010</u>

As of June 30, 2011 and 2010, investments consisted of:

	<u>2011</u>	<u>2010</u>
Insured and registered, with securities held by the counterparty or by its trust department or agent, in the University's name:		
Money market funds – restricted for capital purposes	\$ 1,335,469	\$ 1,358,256
Equity mutual funds	303,061	288,241
Money market funds	<u>703</u>	<u>703</u>
	1,639,233	1,647,200
Certificate of deposit	108,751	103,573
Restricted assets held by the Morehead State University Foundation, Inc.	<u>12,014,828</u>	<u>11,619,827</u>
Total investments	<u>\$ 13,762,812</u>	<u>\$ 13,370,600</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 the Foundation are comprised of the Regional University Excellence Trust Fund endowment and other similar endowments (see Note 13). Assets held by the Foundation are invested primarily in an investment pool managed by the Foundation and are carried at fair value.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

2. Cash, Cash Equivalents and Investments, continued

The assets in the Foundation investment pool at June 30, 2011 and 2010, are invested as follows:

	<u>2011</u>	<u>2010</u>
Percentage of pool invested in:		
Registered investment companies fixed income funds	56%	61%
Registered investment companies equity fund	29%	32%
Registered investment companies alternative investments	<u>15%</u>	<u>7%</u>
Total	<u>100%</u>	<u>100%</u>

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.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

3. Accounts, Grants and Loans Receivable

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

	<u>2011</u>	<u>2010</u>
Student tuition and fees	\$ 4,464,797	\$ 3,663,564
Laptop lease	1,455,500	1,324,000
Financing and interest	2,158,415	2,548,977
Capital appropriations	-	1,695,799
Student loans	3,767,496	3,896,386
Grants and contracts	4,253,649	5,125,171
Auxiliary enterprises	387,603	389,066
Other	<u>400,183</u>	<u>251,350</u>
	16,887,643	18,894,313
Allowance for doubtful accounts	<u>(1,716,744)</u>	<u>(314,934)</u>
	15,170,899	18,579,379
Current portion	<u>(11,489,241)</u>	<u>(14,770,254)</u>
Noncurrent portion	<u>\$ 3,681,658</u>	<u>\$ 3,809,125</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

4. Capital Assets, Net

Capital assets as of June 30, 2011, are summarized as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Land and improvements	\$ 18,628,615	\$ 1,005,000	\$ -	\$ 19,633,615
Buildings	218,887,808	28,640,542	-	247,528,350
Library books	22,670,271	1,090,937	-	23,761,208
Vehicles	1,991,753	123,161	154,321	1,960,593
Equipment and livestock	19,923,703	4,406,940	666,833	23,663,810
Datatel	4,197,690	5,800	-	4,203,490
Art collection	824,570	20,635	-	845,205
Construction in progress	<u>10,702,150</u>	<u>17,141,663</u>	<u>27,381,543</u>	<u>462,270</u>
	297,826,560	52,434,678	28,202,697	322,058,541
<u>Accumulated Depreciation</u>				
Land improvements	6,249,247	506,567	-	6,755,814
Buildings	84,297,872	5,028,464	-	89,326,336
Library books	17,746,728	985,403	-	18,732,131
Vehicles	1,704,421	124,912	154,321	1,675,012
Equipment and livestock	11,805,188	2,396,718	568,858	13,633,048
Datatel	<u>4,059,134</u>	<u>79,998</u>	<u>-</u>	<u>4,139,132</u>
	<u>125,862,590</u>	<u>9,122,062</u>	<u>723,179</u>	<u>134,261,473</u>
Capital assets, net	<u>\$ 171,963,970</u>	<u>\$ 43,312,616</u>	<u>\$ 27,479,518</u>	<u>\$ 187,797,068</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

4. Capital Assets, Net, continued

Capital assets as of June 30, 2010, are summarized as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Land and improvements	\$ 18,347,884	\$ 829,864	\$ 549,133	\$ 18,628,615
Buildings	191,320,618	27,567,190	-	218,887,808
Library books	21,530,262	1,140,009	-	22,670,271
Vehicles	2,455,612	44,897	508,756	1,991,753
Equipment and livestock	17,319,469	3,155,517	551,283	19,923,703
Datatel	4,197,690	-	-	4,197,690
Art collection	796,825	27,945	200	824,570
Construction in progress	<u>13,620,551</u>	<u>24,605,459</u>	<u>27,523,860</u>	<u>10,702,150</u>
	269,588,911	57,370,881	29,133,232	297,826,560
<u>Accumulated Depreciation</u>				
Land improvements	6,003,580	507,878	262,211	6,249,247
Buildings	79,938,811	4,359,061	-	84,297,872
Library books	16,776,826	969,902	-	17,746,728
Vehicles	2,072,810	139,210	507,599	1,704,421
Equipment and livestock	10,315,878	1,989,436	500,126	11,805,188
Datatel	<u>3,311,978</u>	<u>747,156</u>	-	<u>4,059,134</u>
	<u>118,419,883</u>	<u>8,712,643</u>	<u>1,269,936</u>	<u>125,862,590</u>
Capital assets, net	<u>\$ 151,169,028</u>	<u>\$ 48,658,238</u>	<u>\$ 27,863,296</u>	<u>\$ 171,963,970</u>

5. Accounts Payable and Accrued Liabilities

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

	<u>2011</u>	<u>2010</u>
Payable to vendors and contractors	\$ 808,124	\$ 1,395,499
Accrued vacation	2,636,694	2,184,052
Accrued salaries and other liabilities	<u>4,081,492</u>	<u>4,485,489</u>
	<u>\$ 7,526,310</u>	<u>\$ 8,065,040</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

6. Long-Term Liabilities

Long-term liabilities at June 30, 2011, 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>
Consolidated Educational Building Revenue Bonds	\$ 3,660,000	\$ -	\$ 990,000	\$ 2,670,000	\$ 1,020,000	\$ 1,650,000
General Receipts Bonds	49,695,000	-	2,565,000	47,130,000	2,585,000	44,545,000
Capital lease obligations	<u>4,425,105</u>	<u>-</u>	<u>669,982</u>	<u>3,755,123</u>	<u>702,643</u>	<u>3,052,480</u>
Total bonds, notes and capital lease obligations	57,780,105	-	4,224,982	53,555,123	4,307,643	49,247,480
Federal refundable grants	<u>3,813,100</u>	<u>-</u>	<u>352,816</u>	<u>3,460,284</u>	<u>-</u>	<u>3,460,284</u>
Total long-term Liabilities	<u>\$ 61,593,205</u>	<u>\$ -</u>	<u>\$ 4,577,798</u>	<u>\$ 57,015,407</u>	<u>\$ 4,307,643</u>	<u>\$ 52,707,764</u>

Long-term liabilities at June 30, 2010, 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>
Consolidated Educational Building Revenue Bonds	\$ 4,610,000	\$ -	\$ 950,000	\$ 3,660,000	\$ 990,000	\$ 2,670,000
General Receipts Bonds	16,665,000	34,700,000	1,670,000	49,695,000	2,565,000	47,130,000
Capital lease obligations	<u>5,064,233</u>	<u>-</u>	<u>639,128</u>	<u>4,425,105</u>	<u>669,982</u>	<u>3,755,123</u>
Total bonds, notes and capital lease obligations	26,339,233	34,700,000	3,259,128	57,780,105	4,224,982	53,555,123
Federal refundable grants	<u>3,848,297</u>	<u>-</u>	<u>35,197</u>	<u>3,813,100</u>	<u>-</u>	<u>3,813,100</u>
Total long-term Liabilities	<u>\$ 30,187,530</u>	<u>\$ 34,700,000</u>	<u>\$ 3,294,325</u>	<u>\$ 61,593,205</u>	<u>\$ 4,224,982</u>	<u>\$ 57,368,223</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 at June 30:

	<u>2011</u>	<u>2010</u>
2.00 – 4.50% Consolidated Educational Building Revenue Bonds, Series L and M repayable in semi-annual installments with the final installment due May, 2024	\$ 2,670,000	\$ 3,660,000
4.00% General Receipts Bonds, 2007 Series A, repayable in semi-annual installments with the final installment due November, 2027	5,365,000	5,740,000
3.00 – 3.80% General Receipts Bonds, 2008 Series A, payable in semi-annual installments with the final installment due November, 2022	8,060,000	8,715,000
4.00 – 4.50% General Receipts Bonds, 2008 Taxable Series B, repayable in semi-annual installments with the final installment due May, 2013	175,000	540,000
2.00 – 6.00% General Receipts Bonds, 2009 Taxable Series A, repayable in semi-annual installments with the final installment due November, 2028	27,760,000	28,930,000
1.27 – 5.75% General Receipts Bonds, 2010 Taxable Series A, repayable in semi-annual installments with the final installment due November, 2029	5,770,000	5,770,000
5.00% Capital lease obligation with the Foundation, repayable in monthly installments with the final installment due February, 2019	120,333	132,901
4.25% Capital lease obligation with the Foundation, repayable in monthly installments with the final installment due May, 2013	230,138	333,388
9.40% Capital lease obligation with the Foundation, repayable in monthly installments with the final installment due March, 2023	364,524	381,015
4.19% Capital lease obligation with a finance corporation in semi-annual payments with final installment due October, 2019	1,169,900	1,282,353
3.58% Capital lease obligation with a finance corporation in semi-annual payments with final installment due June, 2015	1,716,314	2,108,661
4.47% Capital lease obligation with the Foundation, repayable in monthly installments with the final installment due August, 2015	<u>153,914</u>	<u>186,787</u>
	<u>\$ 53,555,123</u>	<u>\$ 57,780,105</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, 2011 and 2010, all reserve requirements have been fully funded (\$1,126,385 reserved both years). The revenue bonds are subject to several non-financial covenants, all of which management has asserted were met as of June 30, 2011 and 2010.

The Consolidated Educational Building Revenue Bonds are collateralized by various buildings. The revenues derived from student registration fees are pledged as collateral on the Consolidated Educational Building 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 at June 30:

	<u>2011</u>	<u>2010</u>
Equipment	\$ 7,722,742	\$ 7,722,742
Less: accumulated depreciation	<u>(4,579,705)</u>	<u>(4,472,416)</u>
	<u>\$ 3,143,037</u>	<u>\$ 3,250,326</u>

The following is a schedule by years of future minimum payments required for the capital lease obligations as of June 30, 2011:

Year ending June 30,	
2012	\$ 870,653
2013	863,403
2014	740,869
2015	740,869
2016	242,718
Thereafter	<u>973,790</u>
Total minimum lease payments	4,432,302
Less: amounts representing interest	<u>(677,179)</u>
Present value of minimum lease payments	<u>\$ 3,755,123</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 at June 30, 2011, are as follows:

Year ending June 30,	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2012	3,605,000	2,226,549	5,831,549
2013	3,210,000	2,112,740	5,322,740
2014	3,015,000	2,010,293	5,025,293
2015	2,530,000	1,903,585	4,433,585
2016	2,610,000	1,807,589	4,417,589
2017-2030	<u>34,830,000</u>	<u>12,111,166</u>	<u>46,941,166</u>
	<u>\$ 49,800,000</u>	<u>\$ 22,171,922</u>	<u>\$ 71,971,922</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 7.16% of their salary through payroll deductions and the Commonwealth of Kentucky, which also indirectly contributes 14.84% 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, 2011 and 2010 were \$4,521,516 and \$4,369,477, respectively, equal to the required contributions for each year.

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

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

7. Pension Plan, continued

Kentucky Employee Retirement System, continued

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 has 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 26.12% and 16.98%, 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 System each biennium.

The University's contributions to KERS for the years ending June 30, 2011 and 2010 were \$1,966,670 and \$1,481,704 respectively, equal to the required contributions for each year.

Optional Retirement Plans

Optional retirement plans (ORPs) 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 ORPs 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 6.33% of their gross salary and the University's contribution is 8.74% to the retirement providers. The University's contributions under these plans for the years ended June 30, 2011 and 2010 were \$1,364,273 and \$918,782 respectively, equal to the required contributions for each year.

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 \$696,000 and \$687,000 in 2011 and 2010, respectively.

9. Contingencies and Commitments

The University is a defendant in various 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.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

9. Contingencies and Commitments, continued

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 has 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, 2011.

The University has made certain commitments related to the completion of various construction projects in progress totaling \$12,970,798. 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, 2011 and 2010 totaled \$317,955 and \$305,908, respectively.

The University maintains 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 \$362 per month to a high of \$804. Payments for employee health insurance for fiscal years ended June 30, 2011 and 2010 were \$6,987,264 and \$6,743,482 respectively.

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; 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 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.

The University operates a self-insurance program for worker's compensation for its employees. The University purchases reinsurance through commercial carriers for claims in excess of specified stop loss amounts.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

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. 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 Foundation also holds endowment investments for the University which are associated with the Technology Endowment Program. The University will provide matching funds of at least one dollar for every dollar of grant funds. At the end of twenty years, both the principal and the income derived will be used to upgrade and/or replace software/hardware of the University's Information Management System.

The fair market value of Morehead State University endowment funds held by the Foundation as of June 30, 2011 and 2010 was \$34,305,649 and \$27,492,673, respectively. The portion of the endowments representing the value of the funding received from the Kentucky General Assembly was \$11,724,599 and \$11,329,599 for the years ended June 30, 2011 and 2010, and is included in investments held by the Foundation. The portion of the endowments representing the value of the funding received from the Technology Endowment Program was approximately \$290,000 for both 2011 and 2010 and is included in investments held by the Foundation. The portion of the endowments representing the value of the funding received from the Comprehensive University Excellence Trust Fund was \$395,000 for the year ended June 30, 2011, and is included in investments held by the Foundation.

14. 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.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

14. Related Parties, continued

Related party transactions and funds held by the Foundation on behalf of the University are as follows during 2011 and 2010:

	<u>2011</u>	<u>2010</u>
Funds disbursed by the University on behalf of the Foundation for employee salaries and benefits	\$ 97,051	\$ 101,288
Funds held by the Foundation on behalf or for the benefit of the University	12,014,828	11,619,827
Funds due to the University by the Foundation	75,512	6,828

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 an annual rate determined mutually by the two entities, \$79,908 for the years ended June 30, 2011 and 2010. Amounts disclosed above as funds disbursed by the University on behalf of the Foundation for employee salaries and benefits are net of the annual rate for the fiscal years ended June 30, 2011 and 2010.

The University has also entered into several direct financing capital leases of real estate with the Foundation as disclosed in Note 15I.

15. 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.

B. Summary of Significant Accounting Policies

The financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) which require management to make estimates and assumptions that affect the reported amounts and disclosures in the financial statements. Actual results could differ from those estimates. The following is a summary of the significant accounting policies consistently followed by the Foundation in the preparation of its financial statements.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

15. Morehead State University Foundation, Inc, continued

B. Summary of Significant Accounting Policies, continued

Basis of Presentation

The Foundation's financial statements are presented in accordance with GAAP. 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.

Cash

The Foundation maintains its cash balances in financial institutions located in Kentucky. Some of the balances are insured by the Federal Deposit Insurance Corporation (FDIC). On July 21, 2010, U.S. Congress passed legislation that permanently increases FDIC coverage from \$100,000 to \$250,000 for each depositor. As of December 31, 2010, all noninterest bearing deposit accounts are fully insured until December 31, 2012 due to new legislation passed by Congress. As of June 30, 2011 and 2010, the Foundation's uninsured cash balances totaled \$2,746,232 and \$850,588, respectively.

Revenue Recognition

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions on net assets are reported as reclassifications between the applicable classes of net assets.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

15. 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 1.76% and 1.79% for the years ended June 30, 2011 and 2010, 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.

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, 2011 and 2010 were \$148,723 and \$113,563, respectively.

The June 30, 2011 and 2010 annuity liability balances of \$1,112,011 and \$625,700, respectively 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 1.34% to 4.39%. The estimated remaining life expectancies of the annuitants ranged from 5.2 to 21.0 years and 5.1 to 15.1 years for the years ended June 30, 2011 and 2010, respectively.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

15. Morehead State University Foundation, Inc, continued

B. Summary of Significant Accounting Policies, continued

Due to Morehead State University

A gift was pledged to the Foundation that the donor stipulated was specifically for the University. In accordance with GAAP, the gift has been included as a liability on the Foundation's statements of financial Position.

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, 2011 and 2010, the Foundation held \$12,014,828 and \$11,619,827 respectively, for the University's investment purposes.

Income Taxes

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.

The Foundation has evaluated the tax positions taken on all income tax returns that remain open to examination by the respective taxing authorities (those returns filed for the years 2008 through 2010) and does not believe there are any uncertain positions on those returns that should impact the financial statements.

Contributions

Gifts of cash and other assets received without donor stipulations are reported as unrestricted revenue and net assets. Gifts received with donor stipulations that limit 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 statements 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

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

15. Morehead State University Foundation, Inc, continued

B. Summary of Significant Accounting Policies, continued

Contributions, continued

resulting in the reclassification of temporarily restricted net assets to unrestricted net assets are reported when the long-lived assets are placed in service.

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 statements of activities for the years ended June 30, 2011 and 2010 include in-kind contributions of \$351,423 and \$529,477, 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.

Subsequent Events

Management has evaluated subsequent events for accounting and disclosure requirements through September 30, 2011, the date the financial statements were available to be issued.

C. Investments

Investments held as of June 30, 2011 and 2010 are summarized as follows:

	<u>2011</u>	<u>2010</u>
Certificates of deposit	\$ 989,871	\$ 1,051,941
Mutual funds	32,725,809	26,121,606
Corporate bonds and stocks	48,340	35,314
Annuity investment	<u>131,146</u>	<u>129,206</u>
Total investments at fair value	<u>\$ 33,895,166</u>	<u>\$ 27,338,067</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

15. Morehead State University Foundation, Inc, continued

C. Investments, continued

Investment management fees were approximately \$43,000 and \$55,000 during the years ended June 30, 2011 and 2010, respectively.

D. Fair Value Measurements

The Foundation has determined the fair value of certain assets and liabilities through application of GAAP.

June 30, 2011	Fair Value	Fair Value Measurements at Reporting Date Using		
		Quoted Prices in Active Markets for Identical Assets/Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Certificates of deposit	\$ 989,871	\$ 989,871	\$ -	\$ -
Mutual funds:				
Equity				
U.S. Large Cap	4,856,854	4,856,854	-	-
U.S. Small Cap	1,221,790	1,221,790	-	-
International	2,809,893	2,809,893	-	-
Global	1,063,411	1,063,411	-	-
Fixed income and cash				
Cash	653,059	653,059	-	-
Core	12,861,917	12,861,917	-	-
Non-core/tactical	4,256,648	4,256,648	-	-
Alternative investments				
Hedge funds	1,705,058	-	-	1,705,058
Real assets	3,297,179	-	-	3,297,179
Corporate bonds and stocks	48,340	48,340	-	-
Annuity investment	131,146	131,146	-	-
Total assets	\$33,895,166	\$ 28,892,929	\$ -	\$ 5,002,237

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

15. Morehead State University Foundation, Inc, continued

D. Fair Value Measurements, continued

<u>June 30, 2010</u>	<u>Fair Value</u>	<u>Fair Value Measurements at Reporting Date Using</u>		
		<u>Quoted Prices in Active Markets for Identical Assets/Liabilities (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>
Certificates of deposit	\$ 1,051,941	\$ 1,051,941	\$ -	\$ -
Mutual funds	26,121,606	26,121,606	-	-
Corporate bonds and stocks	35,314	35,314	-	-
Annuity investment	129,206	129,206	-	-
 Total assets	 <u>\$ 27,338,067</u>	 <u>\$ 27,338,067</u>	 <u>\$ -</u>	 <u>\$ -</u>

Financial assets and liabilities valued using level 1 inputs are based on unadjusted quoted market prices within active markets. Financial assets and liabilities valued using level 2 inputs are based primarily on quoted prices for similar assets or liabilities in active or inactive markets. Financial assets and liabilities valued using level 3 inputs are primarily valued using management's assumptions about the assumptions market participants would utilize in pricing the assets or liabilities. All assets have been valued using a market approach.

Donor-Designated Endowments

The Foundation has adopted the Uniform Prudent Management of Institutional Funds Act (UPMIFA). The Foundation follows UPMIFA and its own governing documents. The Foundation has interpreted UPMIFA as maintaining historical dollar value and to retain in endowment funds a portion of the investment return to support the increasing cost of benefits in the future, absent explicit donor stipulations to the contrary. As a result of this interpretation, the Foundation classifies as permanently restricted net assets (1) the original value of gifts donated to the permanent endowment, (2) the original value of subsequent gifts to the permanent endowment, and (3) accumulations made pursuant to an applicable gift agreement. The Foundation has determined that the balance of its endowments includes funds that require that the income and net appreciation be restricted to certain uses for the benefit of participants.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

15. Morehead State University Foundation, Inc., continued

D. Fair Value Measurements, continued

Donor-Designated Endowments, continued

The Foundation, on the advice of legal counsel, has determined that the majority of contributions are subject to the terms of its governing documents. Certain contributions are received subject to other gift instruments, or are subject to specific agreements with the Foundation. Under the terms of the Foundation's governing documents, the Foundation has the ability to distribute as much of the original principal of any trust or separate gift, devise, bequest, or fund as the Foundation in its sole discretion shall determine. As a result of the ability to distribute the original principal, all contributions not classified as temporarily restricted or permanently restricted are classified as unrestricted net assets for financial statement purposes.

The Foundation has established a financial management and investment policy for endowment assets that provides general guidelines for the prudent investment management of the endowment fund assets. The investment policy is established with the objective to preserve the real purchasing power of endowment assets as well as generate capital appreciation, after accounting for endowment spending, inflation, and costs of the portfolio and fund management, both internal and external.

The current financial management and investment policy establishes an annual maximum approved spending goal for distributions of up to 3.5% of endowment assets, a management fee used to support the annual operating budget which shall not exceed 1%, the costs of managing the portfolio shall not be greater than 1% of the portfolio value, and therefore the long-term target minimum annual return shall be 5.5%. In order to achieve a prudent level of portfolio diversification, the securities of any one company should not exceed more than 10% of total, and no more than 25% of total should be invested in any one sector.

The Foundation's investments include endowment investments for the University associated with the Technology Endowment Program and RUETF Endowment Match Program, also known as "Bucks for Brains". Funds held for the Technology Endowment Program are matched by the University of at least one dollar for every dollar of grant funds. As of both June 30, 2011 and 2010, the amount of funds included in the Foundation's investments held for the Technology Endowment Program was \$290,229. Funds held for the RUETF Endowment Match Program are endowed for the purposes of supporting endowed chairs and professorships, scholarships, fellowships, research funds, and mission support funds. As of June 30, 2011 and 2010, the amount of funds included in the Foundation's investments held for the RUETF Endowment Match Program were \$11,724,599 and \$11,329,598, respectively. These amounts are shown as funds held in trust for Morehead State University on the statements of financial position and are therefore not included in donor-designated endowment net assets.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

15. Morehead State University Foundation, Inc., continued

D. Fair Value Measurements, continued

Donor-Designated Endowments, continued

Endowment net asset composition by fund type and changes in endowment net assets by fund type as of June 30, 2011 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowment Assets</u>
Endowment net assets,				
beginning of year	\$ -	\$ 2,283,110	\$ 13,589,736	\$ 15,872,846
Contributions	-	25,277	3,292,341	3,317,618
Interest and dividend income	-	999,816	-	999,816
Amounts appropriated for expenditure	-	(1,247,036)	-	(1,247,036)
Net appreciation	-	3,347,577	-	3,347,577
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Endowment net assets, end of year	<u>\$ -</u>	<u>\$ 5,408,744</u>	<u>\$ 16,882,077</u>	<u>\$ 22,290,821</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

15. Morehead State University Foundation, Inc., continued

D. Fair Value Measurements, continued

Donor-Designated Endowments, continued

Endowment net asset composition by fund type and changes in endowment net assets by fund type as of June 30, 2011 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowment Assets</u>
Endowment net assets, beginning of year	\$ -	\$ (672,707)	\$ 13,147,752	\$ 12,475,045
Contributions	-	-	441,984	441,984
Interest and dividend income	-	781,604	-	781,604
Net appreciation	-	2,901,441	-	2,901,441
Amounts appropriated for expenditure	-	(727,228)	-	(727,228)
Endowment net assets, end of year	<u>\$ -</u>	<u>\$ 2,283,110</u>	<u>\$ 13,589,736</u>	<u>\$ 15,872,846</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

15. Morehead State University Foundation, Inc., continued

E. Pledges Receivable

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

Year ended June 30,		
2012	\$	776,801
2013		590,499
2014		576,758
2015		561,929
2016		37,065
Thereafter		<u>70,050</u>
		2,613,102
Less: present value discount		(256,662)
Less: allowance for uncollectible pledges		<u>(261,311)</u>
Pledges receivable, net		2,095,129
Less: current pledges receivable		<u>(520,139)</u>
Noncurrent pledges receivable	\$	<u><u>1,574,990</u></u>

F. Property and Equipment

Property and equipment as of June 30, 2011 and 2010 consists of the following:

	<u>2011</u>	<u>2010</u>
Land	\$ 53,000	\$ 53,000
Furniture and equipment	122,538	154,579
Buildings	<u>175,000</u>	<u>175,000</u>
	350,538	382,579
Less: accumulated depreciation	<u>(146,797)</u>	<u>(163,848)</u>
	<u>\$ 203,741</u>	<u>\$ 218,731</u>

Depreciation expense was \$13,589 and \$21,964 for the years ended June 30, 2011 and 2010, respectively.

G. 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 \$685,000 for both years ending June 30, 2011 and 2010, respectively. The cash surrender value of these policies as of June 30, 2011 and 2010 is \$108,629 and \$102,299, respectively.

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

15. Morehead State University Foundation, Inc., continued

H. 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 statements of activities as University support.

I. Net Investment in Capital Leases

The Foundation's net investment in direct financing capital leases of real estate with the University as of June 30, 2011 and 2010 is as follows:

	<u>2011</u>	<u>2010</u>
Total minimum lease payments to be received	\$ 1,172,225	\$ 1,413,504
Less: unearned income	<u>(303,315)</u>	<u>(379,412)</u>
 Net investment in capital leases	 <u>\$ 868,910</u>	 <u>\$ 1,034,092</u>

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

2012	\$ 241,279
2013	234,030
2014	111,495
2015	111,495
2016	77,700
Thereafter	<u>396,226</u>
	 <u>\$ 1,172,225</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

15. Morehead State University Foundation, Inc., continued

J. Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are available at June 30, 2011 and 2010 for the following purposes:

	<u>2011</u>	<u>2010</u>
Funds restricted for specific purposes	\$ 9,278,618	\$ 4,107,547
Scholarships	87,429	110,384
Athletics	<u>35,925</u>	<u>36,589</u>
	<u>\$ 9,401,972</u>	<u>\$ 4,254,520</u>

Permanently restricted net assets at June 30, 2011 and 2010 consist of endowment funds.

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

	<u>2011</u>	<u>2010</u>
Cash	\$ 600,000	\$ -
Pledges receivable	1,861,705	374,455
Investments	6,158,744	3,033,109
Buildings	142,752	146,252
Net investment in capital leases	<u>638,771</u>	<u>700,704</u>
	<u>\$ 9,401,972</u>	<u>\$ 4,254,520</u>

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

	<u>2011</u>	<u>2010</u>
Pledges receivable	\$ 192,114	\$ 227,989
Investments	16,406,824	12,975,359
Land	53,000	53,000
Net investment in capital leases	<u>230,139</u>	<u>333,388</u>
	<u>\$ 16,882,077</u>	<u>\$ 13,589,736</u>

MOREHEAD STATE UNIVERSITY

Notes to the Financial Statements, continued

15. Morehead State University Foundation, Inc., continued

K. 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 \$79,908 per year. GAAP 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 \$79,908 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 15 H and 15 I.

SUPPLEMENTAL INFORMATION

MOREHEAD STATE UNIVERSITY

Schedule of Bonds, Notes and Capital Lease Obligations

June 30, 2011

	<u>Issue Date</u>	<u>Net Amount of Issue</u>	<u>Interest Cost</u>	<u>Outstanding June 30, 2010</u>	<u>Payments 2010-11</u>	<u>New Issues</u>	<u>Outstanding June 30, 2011</u>	<u>Interest Paid 2010-11</u>	<u>Debt Service Requirements 2011-12</u>	
									<u>Principal</u>	<u>Interest</u>
Consolidated Educational										
Building Revenue Bonds:										
Series L	12/01/01	\$ 4,875,000	2.25-4.30	\$ 930,000	\$ 455,000	\$ -	\$ 475,000	\$ 39,763	\$ 475,000	\$ 20,425
Series M	01/01/04	<u>5,620,000</u>	2.00-4.50	<u>2,730,000</u>	<u>535,000</u>	<u>-</u>	<u>2,195,000</u>	<u>96,622</u>	<u>545,000</u>	<u>80,572</u>
Total educational buildings		10,495,000		3,660,000	990,000	-	2,670,000	136,385	1,020,000	100,997
General Receipts:										
2007 Series A Bonds	08/14/07	6,445,000	4.00	5,740,000	375,000	-	5,365,000	222,100	390,000	206,800
2008 Series A Bonds	06/10/08	10,000,000	3.00-3.80	8,715,000	655,000	-	8,060,000	285,323	675,000	265,373
2008 Series B Bonds	06/10/08	1,875,000	4.00-4.50	540,000	365,000	-	175,000	22,475	85,000	7,875
2009 Series A Bonds	07/29/09	28,930,000	2.00-6.00	28,930,000	1,170,000	-	27,760,000	1,423,059	1,190,000	1,397,674
2010 Series A Bonds	06/29/10	<u>5,770,000</u>	1.27-5.75	<u>5,770,000</u>	<u>-</u>	<u>-</u>	<u>5,770,000</u>	<u>209,207</u>	<u>245,000</u>	<u>247,830</u>
Total General Receipts		53,020,000		49,695,000	2,565,000	-	47,130,000	2,162,164	2,585,000	2,125,552

MOREHEAD STATE UNIVERSITY

Schedule of Bonds, Notes and Capital Lease Obligations, concluded

June 30, 2011

	<u>Issue Date</u>	<u>Net Amount of Issue</u>	<u>Interest Cost</u>	<u>Outstanding June 30, 2010</u>	<u>Payments 2010-11</u>	<u>New Issues</u>	<u>Outstanding June 30, 2011</u>	<u>Interest Paid 2010-11</u>	<u>Debt Service Requirements 2011-12</u>	
									<u>Principal</u>	<u>Interest</u>
Lease Purchase Agreements:										
MSU Foundation, Inc.	03/01/99	240,000	5.00	132,901	12,568	-	120,333	6,360	13,211	5,717
MSU Foundation, Inc.	07/15/02	990,000	4.25	333,388	103,250	-	230,138	26,534	113,216	16,568
MSU Foundation, Inc.	10/21/02	466,457	9.40	381,015	16,491	-	364,524	35,522	18,109	33,903
Citi Mortgage, Inc.	03/31/05	1,824,000	4.19	1,282,353	112,453	-	1,169,900	52,565	117,215	47,804
Suntrust Bank, Inc	06/15/05	3,874,522	3.58	2,108,661	392,347	-	1,716,314	72,009	406,519	57,838
MSU Foundation, Inc.	09/01/05	<u>327,764</u>	4.47	<u>186,787</u>	<u>32,873</u>	<u>-</u>	<u>153,914</u>	<u>7,681</u>	<u>34,373</u>	<u>6,180</u>
Total lease purchase		<u>7,722,743</u>		<u>4,425,105</u>	<u>669,982</u>	<u>-</u>	<u>3,755,123</u>	<u>200,671</u>	<u>702,643</u>	<u>168,010</u>
Total		<u>\$ 71,237,743</u>		<u>\$ 57,780,105</u>	<u>\$ 4,224,982</u>	<u>\$ -</u>	<u>\$ 53,555,123</u>	<u>\$ 2,499,220</u>	<u>\$ 4,307,643</u>	<u>\$ 2,394,560</u>

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2011

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>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	\$258,301
ACADEMIC COMPETITIVENESS GRANT PROGRAM		84.376	167,974
FEDERAL WORK STUDY		84.033	839,726
FEDERAL PELL GRANT PROGRAM		84.063	15,299,796
FEDERAL SUPPLEMENTAL EDUCATIONAL OPPORTUNITY GRANT PROGRAM		84.007	333,685
FEDERAL PERKINS LOAN PROGRAM		84.038	458,175
FEDERAL DIRECT LOAN PROGRAM		84.268	41,362,729
TEACHER EDUCATION ASSISTANCE FOR COLLEGE AND HIGHER EDUCATION GRANT		84.379	<u>122,750</u>
			58,843,136
TRIO Cluster:			
CEOC - SE 07-10		84.066	187,132
CEOC-NE 09/14	PO66090058	84.066	424,962
STUDENT SUPPORT SERVICES 06-07		84.042	144,135
STUDENT SUPPORT SERVICES 10.15		84.042	252,431
TALENT SEARCH 07-11		84.044	449,999
TALENT SEARCH II 07-11		84.044	233,698
UPWARD BOUND MATH-SCIENCE 08-12		84.047	244,757
UPWARD BOUND EAST 07-11		84.047	274,550
UPWARD BOUND CENTRAL 09/10		84.047	<u>526,471</u>
			2,738,135
GEAR-UP IRAPP 08-14	P334A080059	84.334	1,762,415
KY GEAR UP II 09/10	PO2 415 0800019454 2	84.334	156,277
KY GEAR UP II 10/11	PO2 415 1100000130 1	83.334	29,323
ODDIS-MAGNETS 09/10		84.116	28,930
RATLIFF-SHOWCASE-CEE 10		84.215	1,889
RATLIFF-ENTREPRENEUR-CEE 10/11		84.215	3,176
RATLIFF-ECONOMICS-CEE 10/11		84.215	5,226
PATRICK-SI 05-06		84.031	<u>200,689</u>
			2,187,925

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2011

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>CFDA Number</u>	<u>Federal Expenditures</u>
Passed through Kentucky Education and Workforce Development Cabinet - Department for Workforce Investment:			
DEMOSS-CTE-RESERVE 10/11	PON2 531 1000003770 1	84.048	17,322
DEMOSS-KDE-TEACH PREP 10/11	PON2 531 1000003837 1	84.051	19,484
DEMOSS-KDE-PRF DEV 10/11	PON2 531 1000003837 1	84.051	7,177
PLATT-FOOD-KEC 10	P02 531 1000004169 1	84.048	738
STUBBS-TITLE 1C AS 10/11	P02 531 1000006165 1	84.048	31,364
STUBBS-TITLE 1C NAHS 09/10	P02 531 0900024691 1	84.048	147
STUBBS-TITLE 1C NAHS 10/11	P02 531 1000006165 1	84.048	30,860
STUBBS-TITLE 1C IS 10/11	P02 531 0900024691 1	84.048	21,609
STUBBS-TITLE 1C DEAN 10/11	P02 531 0900024691 1	84.048	4,433
MATTINGLY-CDP REHAB 08/10	PO2 531 0800016952 1	84.346	720,978
MICULINICH-USED-TEACH 11	PON2 531 1100001984 1	84.243A	718
PRATER-USED-WORKSHOP 11	PON2 531 1100001984 1	84.243A	1,472
WILLIS-FIRST COACH 09/10	PO2 540 0900023727 1	84.357A	<u>71,826</u>
			928,128
Passed through Kentucky Education and Workforce Development Cabinet - Department of Education:			
DEMOSS-MSP CAP 09/10	PO2 540 0900024282 1	84.366	9,501
PRICE-KDE-CTL MATH/SCI 10/11	PO2 540 0900012560 1	84.366	<u>3,306</u>
			12,807
Passed through Kentucky Council on Postsecondary Education:			
GUNN-CPE-MATH & SCIENCE II 10/11		84.367	76,877
GUNN-CPE-MATH & SCIENCE 09/10	PO2 415 09000223101	84.367	33,461
BARTON-USED-CPE-MATH 11/12	PO2 415 1100002589 1	84.367	31,326
BARTON-USED-CPE-READINESS 10/11		84.367	93,744
BARTON-USED-CPE-READINESS 11/12	PO2 415 1100002583 1	84.367	19,071
ACKERMAN-ADULT ED ACAD 10/11		84.002	217,001
CONNELL-POWELL ADULT LC 10/11		84.002	129,222
CONNELL-POWELL ADULT LC RESULTS		84.002	4,469
TOBIN-WL ADULT LC-CPE 10/11		84.002	167,361
TOBIN-WL ADULT LC-RESULTS		84.002	510
HARR-CPE-FISCAL AGENT 10/11	PO2 415 1000005928 1	84.002	84,120
HENDERSON-MSU ADULT LC RESULTS		84.002	500
HENDERSON-MSU ADULT LC 10/11		84.002	<u>148,025</u>
			1,005,687

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2011

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>CFDA Number</u>	<u>Federal Expenditures</u>
Passed through National Writing Project Corporation: NWP #13 05-06	94-KY07	84.928	<u>37,531</u>
 Total U.S. Department of Education			 <u>65,753,349</u>
 U.S Department of Health and Human Services:			
Direct Programs:			
BLUNT-HHS-RURAL HEALTH 08/11		93.912	136,426
REGAN-HHS-RURAL HEALTH 09/10		93.912	31,097
LILES-SCHOLARSHIP-HHS 10/11		93.925	34,729
LILES-SCHOLARSHIP-HHS ARRA 11		93.407	22,693
HARDMAN-MARTIN COUNTY-HRSA 09/10		93.888	71,370
MAGNER-MARTIN COUNTY-HRSA 10/12		93.888	9,833
SEELIG-MARTIN COUNTY HHS 10/12		93.888	<u>87,501</u>
			393,649
 Passed through Eastern Kentucky University:			
SLOAN-TRAINING RESOURCE 10/11	452129-11-165	93.658	92,107
HESTERBERG-PCWCP-PRESTON 10/11		93.648	6,670
PCWCP-ASHLAND 09/10		93.648	6,790
GEURIN-PCWCP-MOREHEAD 10/11		93.658	5,997
GEURIN-PCWCP-MT. STERLING 10/11		93.648	<u>5,978</u>
			117,542
 Passed through Louisville Metro Community Action Project:			
WILLIAMS-CAPACITY BUILDING 10/11		93.048	1,601
WILLIAMS-KY NEDUCARE 10/11	90AM3133/05	93.048	<u>20,716</u>
			22,317
 Passed through Volunteers of America of Los Angeles:			
SHANNON-HHS-ADULT 10/11		93.243	17,281
SHANNON-HHS-VETERANS 10/11		93.243	10,857
		93.243	<u>5,362</u>
			33,500

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2011

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>CFDA Number</u>	<u>Federal Expenditures</u>
Passed through Administration Office of Courts:			
SHANNON-HHS-DAVIESS 10/11	PON2-025-11*1372	93.243	10,882
SHANNON-HHS-CHRISTIAN 10/11	3048 106655-11-303	93.243	3,391
SHANNON-HHS FLOYD PERRY 10/11	3048 105484-11-302	93.243	4,151
SHANNON-HHS-FAYETTE 10/11	PON2-025-11*1371	93.243	<u>30,395</u>
			48,819
Passed through KY Cabinet for Health and Family Services:			
MCBRIDE-STEPS-CHFS 10/11	PON 2736 1000036271	93.558	<u>35,366</u>
Total U.S. Department of Health and Human Services			<u>651,193</u>
U.S. Department of Homeland Security:			
Direct Programs:			
LANGE-NIHS STUIDY 10/11		97.000	<u>300,025</u>
Total U.S. Department of Homeland Security			<u>300,025</u>
U.S. Department of Defense			
Direct Programs			
MALPHRUS DOD 10/11		12.000	<u>340,342</u>
Total Department of Defense			<u>340,342</u>
U.S Department of Commerce:			
Direct Programs:			
SLOAN-HEIGHT MOD NOAA 08/09		11.400	<u>13,920</u>
Total U.S Department of Commerce			<u>13,920</u>

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2011

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>CFDA Number</u>	<u>Federal Expenditures</u>
National Science Foundation:			
Direct Programs:			
Xu-NFS-MRI 09/11		47.041	1,657
DENNIS-NSF-MSP 08/09		47.076	<u>27,008</u>
			28,665
Passed through University of Kentucky Research Foundation			
GRISE-NSF-UKRF 09/10	3048105113-09-184	47.07	<u>7,081</u>
Total National Science Foundation			<u>35,746</u>
Corporation for National and Community Service			
Direct Programs:			
WILLIAMS-RSVP 09/12		94.002	<u>102,405</u>
			102,405
Passed through Kentucky Campus Compact Foundation			
COOPER-CNCS-PAY IT FORWARD 10/11		94.005	<u>15,655</u>
			15,655
Passed through Western Kentucky University Research Foundation			
HAIGHT-KUPEE 09/12	528101-10-001	94.005	<u>61,893</u>
			61,893
Passed through CNCS			
MSU CORP CNCS 10/11	PO2 703 1000003914	94.006	469,123
MSU CORP2 MONTH CNCS-1-	PO2 730 08000014292 3	94.006	<u>34,663</u>
			503,786
Total Corporation for National and Community Service			<u>683,739</u>

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2011

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>CFDA Number</u>	<u>Federal Expenditures</u>
Corporation for Public Broadcasting			
Direct Programs:			
HITCHCOCK-CPB 09/11		11.550	122,226
HITCHCOCK-CPB 11/12		11.550	36,214
HITCHCOCK-CPB-ARRA 10		11.550	9,453
HITCHCOCK-CPB BONUS 10/11		11.550	<u>19,717</u>
Total Corporation for Public Broadcasting			<u>187,610</u>
Small Business Administration:			
Passed through University of Kentucky Research Foundation:			
SBDC Federal UKRF 10/11	1-603001-Z-0018-30	59.037	110,867
SBDC Federal UKRF 09/10		59.037	<u>29,028</u>
Total Small Business Administration			<u>139,895</u>
U.S. Department of Justice:			
Passed through Kentucky State Police:			
WILBURN-DOJ-RESPONSE 10	VAWA-2010-MOREHEAD-00141	16.588	28,636
WEBB-KSP-JUSTICE 10/12	2010-AH-FX-0093-MS	16.727	<u>12,942</u>
Total U.S. Department of Justice			<u>41,578</u>
Appalachian Regional Commission:			
Direct Programs:			
KY-AHED-Duvall 04-09		23.001	440,117
WALKER-AHED-ARC-IEL 09/10		23.001	7,149
DEMOSS-ARC 09		23.001	<u>749,917</u>
			1,197,183

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2011

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>CFDA Number</u>	<u>Federal Expenditures</u>
Passed through East Tennessee State			
MCMICHAEL-ARC-ETS-ATP 10/11	220010-05	23.001	<u>4,000</u>
Total Appalachian Regional Commission			<u>1,201,183</u>
U.S. Department of Labor			
Passed Through U.S. Department of Housing and Urbana Development			
SLOAN-HUD YOUTHBUILD 07-08	YB16868YAO	17.274	131,285
SLOAN-YOUTHBUILD-DOL-HUD 09/12	YB-18972-09-60-A21	17.274	273,959
SLOAN-YOUTHBUILD-DOL-HUD II 09/12	YB-18972-09-60-A21	17.274	<u>168,476</u>
			573,720
Passed through Buffalo Trace Area Development District:			
REYNOLDS-TODAY'S YOUTH 09/10	FY 11-5245	17.259	<u>118,406</u>
Total U.S. Department of Labor			<u>692,126</u>
National Aeronautics and Space Administration:			
Passed through Western Kentucky University:			
MALPHRUS-NASA-WKU-LUNAR 09/10	WKU 516171-10-160	43.001	4,033
THOMAS-NASA-WKU 09/10	WKU 516171-10-164	43.001	1,888
THOMAS-NASA-KSG-STEM 11	3048107336-11-190	43.010	2,268
MALPHRUS-COURSE-NASA-KSGC 09/10	WKU 516171-09-142	43.001	7,503
MALPHRUS-FELLOW-KSGC-NASA 10		43.001	4,000
MALPHRUS—NASA-KSGC Sband 11	3048107336-11-158	43.001	1,881
OKEEFE-NASA-WKU 09/10	WKU 516171-10-161	43.001	1,196
PANNUTI-NASA-WKY-Bluegrass 09/10	WKU 516171-09-137	43.001	3,944
PANNUTI-NASA-WKY-Bluegrass 09/10	WKU 516171-09-137	43.001	4,404
PANNUTI-NASA-WKY-Nuclei & Blaz	WKU 516171-09-139	43.001	<u>3,232</u>
Total National Aeronautics and Space Administration			<u>34,349</u>

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2011

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>CFDA Number</u>	<u>Federal Expenditures</u>
U.S. Department of Agriculture:			
Direct Programs:			
CADY-SUMMER FOOD 10		10.558	20,542
CADY-SUMMER FOOD 11		10.558	6,031
MORLEY-ENERGY AUDIT 10/12		10.769	32,741
MORLEY-USDA 08/10		10.769	<u>130,791</u>
Total U.S. Department of Agriculture			<u>190,105</u>
National Endowment for the Arts:			
Direct Programs:			
TOWELL-NEA-SOUTHERN ARTS		45.024	4,250
COLLINSWORTH-NEA-WILLIAMS 09/10		45.024	<u>13,096</u>
Total National Endowment for the Arts			<u>17,346</u>
National Endowment for the Humanities:			
Direct Programs:			
DAVIDSON-QUESTIONS-NEH 10/12		45.163	<u>13,604</u>
Total National Endowment for the Humanities			<u>13,604</u>
U.S. Environmental Protection Agency:			
Passed through Kentucky Environmental and Public Protection Cabinet :			
WRIGHT-LABORATORY CRT 10.12		66.468	64,354
WRIGHT-PRINCIPAL LAB 10/12		66.468	<u>30,666</u>
			95,020
Passed through Kentucky Division of Water:			
HAIGHT-TRIPLETT CREEK 08/09	C9994861-08	66.460	<u>62,217</u>
Total U.S. Environmental Protection Agency			<u>157,237</u>

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2011

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>CFDA Number</u>	<u>Federal Expenditures</u>
National Institute of Health:			
Direct Programs:			
DENNIS-NIH-BIOGENESIS 08/10		93.859	48,525
DENNIS-NIH-ARRA 09/10		93.701	16,204
HARE-NIH 09/12		93.859	63,713
WHITE- NIH AMP 07/10		93.279	<u>45,933</u>
			174,375
Passed through University of Louisville Research Foundation:			
KBRIN-INBRE-WHITE 10/11	2P20RR016481-09	93.389	29,777
KBRIN-INBRE-HARE 10/11	2P20RR016481-09	93.389	54,612
KBRIN-INBRE-HARE 11/12		93.389	13,596
KBRIN-INBRE-T HARE 11/12		93.389	10,275
KBRIN-INBRE-DENNIS 09/10	2P20RR016481-09	93.389	58,836
KBRIN-INBRE-DENNIS 11/12		93.389	8,289
KBRIN-INBRE-DENNIS FELLOW 10/11	2P20RR016481-09	93.389	31,625
KBRIN-INBRE-DENNIS FELLOW 11.12		93.389	4,312
KBRIN-INBRE-MATTINGLY 11/12		93.389	12,414
KBRIN-INBRE MATTINGLY 10/11	2P20RR016481-09	93.389	<u>233,890</u>
			457,626
Total National Institute of Health			<u>632,001</u>
U.S. Geological Survey:			
Direct Programs:			
O'KEEFE USGS 10/11		15.808	7,811
PARKANSKY-USGS 07/11		15.808	<u>107,359</u>
			115,170
Passed through America View, Inc.			
MCMICHAEL-USGS-AMVIEW		15.815	7,902
MCMICHAEL-USGS-America View 09/10	AV08-KY01	15.808	<u>16,316</u>
			24,218
Total U.S. Geological Survey			<u>139,388</u>

MOREHEAD STATE UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2011

<u>Federal Grantor/Pass Through Grantor/Program or Cluster Title</u>	<u>Pass Through Number</u>	<u>CFDA Number</u>	<u>Federal Expenditures</u>
National Highway Traffic Safety Administration: Passed through Kentucky Transportation Cabinet JAMES-NTSA-POSTED 10/11	AL-11-28	20.600	<u>7,706</u>
Total National Highway Traffic Safety Administration			<u>7,706</u>
U.S. Department of Energy: Direct Programs: PHILLIPS-US ENERGY 10/11		81.087	<u>152,587</u>
Total U.S. Department of Energy			<u>152,587</u>
Passed through Kentucky Office of Governor ARRA-SFSF ARRA 2010	84.394A	84.394	<u>2,542,000</u>
Total Expenditures of Federal Awards			<u><u>\$73,927,029</u></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, 2011 are summarized as follows:

Federal Perkins Loan Program:		
Loans disbursed	\$	458,175
Federal Direct Loan Program:		
Federal Unsubsidized Loans	\$	20,268,553
Federal Subsidized Loans		18,915,944
Federal Plus Loans		2,178,232

As of June 30, 2011, the University had loans outstanding, in the amount of \$3,526,695 with an allowance for doubtful accounts of \$85,838 under the Federal Perkins Loan Program.

DEAN || DORTON || ALLEN || FORD_{PLC}**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 the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of Morehead State University (the University) as of and for the year ended June 30, 2011 which collectively comprise the University's basic financial statements and have issued our report thereon dated November 7, 2011. 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 as a basis for designing 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.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the University's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in the internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and questioned costs that we consider to be significant deficiencies in internal control over financial reporting, item 11-01. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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*.

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 7, 2011
Lexington, Kentucky



DEAN || DORTON || ALLEN || FORD_{LLC}

Report on Compliance with Requirements that Could Have a Direct and Material Effect on Each Major Program and 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 Morehead State University's (the "University") compliance 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, 2011. 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 referred to above 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 identified in the accompanying schedule of findings and questioned costs 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 of the University's compliance with those requirements.

In our opinion, Morehead State University complied, in all material respects, with the compliance requirements referred to above that are applicable to each of its major federal programs identified in the accompanying schedule of findings and questioned costs for the year ended June 30, 2011. However, the results of our auditing procedures disclosed instances of noncompliance with those compliance requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 11-02 and 11-03.

We did not audit the University's compliance with requirements governing the maintaining contact with and billing borrowers and processing deferment and cancellation requests and payments for the Perkins Loan Program. Those requirements govern functions that are performed by University Accounting Service, LLC (UAS). Since we did not apply auditing procedures to satisfy ourselves as to compliance with those requirements, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on compliance with those requirements. UAS's compliance with the requirements governing the functions that it performs for the University was examined by other accountants whose report has been furnished to us. The report of the other accountants indicates that compliance with those requirements was examined in accordance with the Department of Education's Audit Guide, *Compliance Audits (Attestation Engagements) of Federal Student Financial Assistance Programs at Participating Institutions and Institution Servicers*. Based on our review of the service organization accountant's report, we have determined that all of the compliance requirements included in the *Compliance Supplement* that are applicable to the major program in which the University participates are addressed in either our report or the report of the service organization accountants. Further, based on our review of the service organization accountant's report, we have determined that it does not contain any findings of noncompliance that would have a direct and material effect on the University's major program.

Internal Control Over Compliance

Management of Morehead State University is responsible for establishing and maintaining effective internal control over compliance with the compliance requirements referred to above. In planning and performing our audit, we considered the University's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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 of the University's internal control over compliance.

Requirements governing the maintaining contact with and billing borrowers and processing deferment and cancellation requests and payments for the Federal Perkins Loan Program are performed by UAS. Internal control over compliance relating to such functions was reported on by other accountants in accordance with the U.S. Department of Education's Audit Guide, *Compliance Audits (Attestation Engagements) of Federal Student Financial Assistance Programs at Participating Institutions and Institution Servicers*. A copy of the service organization accountant's report has been furnished to us. However, the scope of our work did not extend to internal control maintained at UAS.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be deficiencies, significant deficiencies, or material weaknesses in internal control over compliance. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies as described in the accompanying schedule of findings and questioned cost as items 11-02 and 11-03. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

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

This report is intended solely for the information and use of management, the Board of Regents, others within the entity, audit committee, 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 7, 2011
Lexington, Kentucky



MOREHEAD STATE UNIVERSITY

Schedule of Findings and Questioned Costs

Year ended June 30, 2011

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. Internal control over financial reporting:
 - Material weaknesses: **No**
 - 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. Internal control over major programs:
 - Material weaknesses: **No**
 - Significant deficiencies identified that are not considered to be material weaknesses: **Yes**
- 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: **Yes**
- g. Major programs:
 - Student Financial Aid Custer:**
 - Federal Pell Grant, CFDA 84.063
 - Federal Work Study, CFDA 84.033
 - Federal Supplemental Educational Opportunity Grant, CFDA 84.007
 - Federal Perkins Loan, CFDA 84.038
 - Federal Direct Loan Program, CFDA 84.268
 - Academic Competitiveness Grant, CFDA 84.376
 - National Science and Mathematics Access to Retain Talent Grant, CFDA 84.375
 - Teacher Education Assistance for College and Higher Education Grant, CFDA 84.379
 - Liles Scholarship, CFDA 93.925
 - ARRA -Liles Scholarship, CFDA 93.407
 - ARRA -State Fiscal Stabilization Fund, CFDA 84.394
 - Adult Education grant, CFDA 84.002
 - Appalachian Regional Development, CFDA 23.001
 - AmeriCorps, CFDA 94.006
 - National Center for Research Resources - INBRE, CFDA 93.389
 - Carl D. Perkins Vocational Training Center, CFDA 84.346

MOREHEAD STATE UNIVERSITY

Schedule of Findings and Questioned Costs, continued

Year ended June 30, 2011

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

- h. Dollar threshold used to distinguish between Type A and Type B programs: \$450,794
- i. Auditee qualified as a low-risk auditee: Yes

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*:
11-01

Condition:

During our audit, we noted that Morehead State University modified its employee vacation policy but did not properly account for the modification. This condition resulted in the accrued vacation account being understated at year end.

Effect:

An adjusting journal entry was required to correct the vacation accrual on the financial statements for the year ending June 30, 2011.

Recommendation:

We recommend that the University review the accounting for the vacation accrual on a regular basis to ensure that it is being calculated accurately and according to policy.

Management’s Response:

Following a review of the University’s employee vacation accrual policy by the Office of Human Resources in February 2011, the University modified its interpretation of the policy. The change in the interpretation was applied to all current employee vacation accrual calculation tables, resulting in additional vacation leave time being available to those current employees. Although the University had recorded a liability for accrued vacation leave as of June 30, 2011, the net effect of the change in interpretation of the policy had not been quantified at that time, and therefore could not be booked accurately. Once that additional amount was determined in September 2011, the net financial effect of the change was booked in a subsequent adjusting entry to the University’s June 30, 2011 financial statements. Future accrual adjustments for vacation leave time will be determined in accordance with the new interpretation.

MOREHEAD STATE UNIVERSITY

Schedule of Findings and Questioned Costs, continued

Year ended June 30, 2011

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: 11-02, 11-03

Finding 11-02:

Federal Program: U.S. Department of Education
Federal Pell Grant, CFDA 84.063

Condition:

During our testing of the verification requirement, we noted 3 students (out of the sample of 45) for which the verification process was not completed properly. For these 3 students the income tax return section of the Institutional Student Information Record (ISIR) was not properly reconciled to the income tax return provided by the student. The differences related primarily to “untaxed income and benefits” not being properly accounted for on the student’s application for federal aid. Due to the errors noted in our original sample, we requested that MSU examine all verifications performed in the current to determine the full magnitude of this issue. MSU pulled the verification records for 2,672 students and noted that 45 of those students had similar issues regarding the untaxed income reported on the ISIR not being properly reconciled to the income tax return.

Criteria:

Per 34 CRF 668.55, schools are required to perform verification procedures to ensure that the data used to award aid to students is accurate, based on source documentation. Per 34 CRF 668.56 and 668.57, dictate the types of items that are required to be verified including untaxed income and benefits as well as what source documentation is acceptable.

Cause:

There is no internal control in place to provide a review of the verification process prior to the disbursement of the students' awards to ensure that all supporting documentation agrees to the ISIR.

Effect:

The University failed to properly verify the untaxed income for 48 students. Using the incorrect income resulted in an incorrect calculation of the expected family contribution (EFC). The incorrect EFC impacted the amount of aid that was awarded to students. Specifically, 47 students were awarded too much Pell (\$31,275) and 1 student was not awarded enough Pell (\$1,500). The net Pell overaward of \$29,775 is required to be returned to the federal government. The \$29,775 was returned on October 24, 2011.

MOREHEAD STATE UNIVERSITY

Schedule of Findings and Questioned Costs, continued

Year ended June 30, 2011

Finding 11-02, continued:

Recommendation:

We recommend that MSU put a control in place to properly monitor the verification process that is being conducted as well as ensure that any changes that are being put into place for the year being verified are properly communicated to all members involved in the verification process.

Management Response:

The required verification data items vary from one year to the next, most often regarding untaxed income. Due to the changes, we believe some items were overlooked during times when two years overlapped. We have developed a check sheet that will be updated each year that contains all required data items to be verified. This will ensure each data item is checked. When years overlap and we are verifying two years at the same time, we now have a process in place to work on the years separately to prevent any conflicting issues. Verifications completed will be spot checked throughout the year to ensure compliance with current year requirements.

Our verification processor has participated in two Webinars and one federal training regarding verification processes in the last two months, with continued training planned. We will ensure training continues and that the director of financial aid communicates more with the verification processor regarding the processes.

Finding 11-03:

Federal Program: U.S. Department of Education
Federal Pell Grant, CFDA 84.063
Federal Direct Loan Program, CFDA 84.268

Condition:

During our audit, we encountered an error in the return of Title IV funds calculation. The error primarily related to the calculation of the Pell money that should be returned. The computer system, Datatel, was not using the actual amount of Pell that was disbursed in the return calculation. This error primarily related to students that enrolled at full time and then dropped to part time before withdrawing completely and therefore resulting in a return calculation. In four separate cases, the Datatel withdrawal calculation was not reviewed and incorrect amounts were calculated for the amount of aid earned and the amount of aid to be returned.

MOREHEAD STATE UNIVERSITY

Schedule of Findings and Questioned Costs, continued

Year ended June 30, 2011

Finding 11-03, continued:

Criteria:

Per 34 CFR 668.22, the amount of Title IV grant or loan assistance that is earned by the student is calculated by: (1) determining the percentage of Title IV grant or loan assistance that has been earned by the student and (2) applying this percentage to the total amount of Title IV grant or loan assistance that was disbursed for the payment period or period of enrollment as of the student's withdrawal date.

Cause:

There is no internal control in place to provide a review of the return of Title IV aid calculation to ensure that all funds are being returned timely and in the appropriate amounts.

Effect:

In all cases noted above, the amount of aid earned by the student was incorrectly calculated. As a result, in two of these cases, both the institution and the student returned more Title IV aid than was required.

Recommendation:

We recommend that an internal control be implemented to ensure that all return of Title IV aid calculations are being reviewed to ensure that the Datatel system is working properly and correct amounts of aid are being returned in a timely manner.

Management Response:

The Assistant Director for Student Services is now reviewing all Return of Title IV Fund Calculations to ensure that the Datatel system is working properly and correct amounts of aid are being returned in a timely manner.

MOREHEAD STATE UNIVERSITY

Summary Schedule of Prior Audit Findings

Year ended June 30, 2011

Finding 10-01:

Federal Program: U.S. Department of Education
Federal Direct Loan Program, CFDA 84.268
Federal Pell Grant Program, CFDA 84.063

Condition:

During the audit, we noted several students who were determined to be unofficially withdrawn from the University had incorrect return calculations of Title IV funds. The University had used the midterm date as the 50% point in the semester for both Spring and Fall semesters rather than using the midpoint date, which takes the actual number of days in the semester divided by two. This resulted in a percentage of Title IV aid earned being slightly higher than 50 percent. When the University recalculated all unofficial withdrawal calculations, they needed to return additional Title IV funds to the federal government, which had exceeded the 45 day requirement period for returning funds. Per management, this affected 376 students and resulted in \$11,402 of Direct Loan and Pell Grant funds being returned outside the 45 day required period.

Criteria:

The University must comply with the provisions of § 668.22.

Cause:

The University misinterpreted the regulations and used the midterm date as the 50% point in the semester rather than using the midpoint date, which takes the actual number of days in the semester divided by two.

Effect:

Several Return of Title IV Funds calculations were incorrect in the current year due to the University using the midterm date instead of the midpoint date for unofficial withdrawals. This has caused some federal funds to not be returned timely.

Recommendation:

We recommend that the University establish an internal control to verify that the dates input into the system are properly calculating to 50% for unofficial withdrawals.

MOREHEAD STATE UNIVERSITY

Summary Schedule of Prior Audit Findings

Year ended June 30, 2011

Finding 10-01, Continued:

Management's Response:

We misinterpreted the regulations and used the midterm date as the 50% point in the semester rather than using the midpoint date, which takes the actual number of days in the semester divided by two. This resulted in percentages of Title IV aid earned being slightly higher than 50% (50.9% for Fall 2009 and 52.8% for Spring 2010). The University recalculated all unofficial withdrawals and returned the additional Title IV funds to the federal government. This was caught early enough to avoid this from repeating in the next fiscal year.

Current Status:

No instances of this compliance issue repeated in current year.

Finding 10-02:

Federal Program: U.S. Department of Education
TRIO Cluster
Talent Search Program
Federal CFDA 84.044

Condition:

We were notified by Management during the financial statement audit in August 2010 that an employee in the Talent Search program of the TRIO cluster had reported excessive hours on her timesheets. The University's Internal Auditor conducted an investigation and determined amounts exceeding \$11,000 to be unreasonable costs to the program, as the program received no benefit from those expenditures.

Criteria:

Per the OMB Circular A-133, auditors are required to report questioned costs. Unreasonable costs are defined as:

Unreasonable Costs – These are costs incurred that may not be consistent with the actions that a prudent person would take in the circumstances.

MOREHEAD STATE UNIVERSITY

Summary Schedule of Prior Audit Findings

Year ended June 30, 2011

Finding 10-02, continued

Cause:

The control in place that calls for review of the employee's weekly timesheets by a supervisor was not being properly performed as designed. Since the control was not effective, the irregularities were not identified and stopped in a timely fashion.

Effect:

The grant was charged for salary and fringe expenditures that were not supported by actual time devoted to the grant as a result of incorrect timecards being submitted and approved.

Perspective Information:

The issue regarding the Talent Search program within the TRIO cluster was identified by the University, investigated internally, and brought to our attention during the financial statement audit. The TRIO cluster was not audited as a major program for the year ended June 30, 2011. However we did obtain supporting documents from the investigation performed by the University's Internal Auditor and performed certain procedures on those documents. We found that investigation to be very thorough. We also performed procedures to determine that this issue was isolated to the one employee in question. Due to the results of these procedures, we did not consider it necessary to audit the entire TRIO cluster. We audited the TRIO cluster as a major program in the 2010 audit and noted no instances of fraud within our testwork.

Recommendation:

We recommend that the supervisor of the Talent Search program ensure that the control around timecard approval be performed as intended. It appears that this issue could have been identified more timely if the control was being properly observed.

Management's Response:

We concur that the actual time devoted to the grant did not agree to the time submitted on the time sheet. The amount of questioned costs will be reduced from future payment requests from the Department of Education. All Trio Program overtime must now be approved by the Assistant VP for Adult Education and College Access.

Current Status:

No instances of this compliance issue repeated in current year.