VIRGINIA COMMONWEALTH UNIVERSITY

RICHMOND, VIRGINIA

REPORT ON AUDIT

FOR THE YEAR ENDED

JUNE 30, 2004

Auditor of Public Accounts

COMMONWEALTH OF VIRGINIA

<u>AUDIT SUMMARY</u>

Our audit of Virginia Commonwealth University for the year ended June 30, 2004, found the following:

- the financial statements are presented fairly, in accordance with generally accepted accounting standards;

- internal control matters that we consider to be a reportable conditions; however, we do not consider these to be material weaknesses;

- no instances of noncompliance or other matters that are required to be reported under <u>Government Auditing Standards</u>; and

- the University has not taken adequate corrective action with respect to the previously reported finding, "Ensure Proper Stewardship and Control Over Fixed Assets." Adequate corrective action was taken with respect to audit findings reported in the prior year that are not repeated in this report.

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INTERNAL CONTROL FINDINGS AND RECOMMENDATIONS

Ensure Proper Stewardship and Control Over Fixed Assets

As reported last year, the University did not adequately maintain and safeguard fixed assets in accordance with the University's fixed asset policies and procedures and the Commonwealth's accounting policies and procedures. Exceptions noted in our testwork included fixed assets not able to be located, assets without identification tags, assets with incorrect location or other description data in the fixed asset system, and assets not appearing on the department's inventory verification listing. These exceptions arose from individual department custodians not following procedures for properly maintaining and tracking fixed assets.

We again recommend that management ensure that each department follows the requirements and guidelines in the University's fixed asset policies and procedures and properly conducts an annual inventory of its fixed assets. Management should establish a uniform procedure of tagging fixed assets, so tags are visible for tracking purposes, and update the policies and procedures to reflect changes caused by the new online fixed asset system. We understand the University has hired a consultant to perform a complete inventory of fixed assets, including making sure all assets have tags and the fixed asset system shows the correct location. We also understand that management plans to strictly enforce departmental compliance with the established policies.

Ensure Cash Reconciling Items are Resolved Timely

The University did not resolve old reconciling items when preparing monthly and year end cash reconciliations. The operating account reconciliation showed reconciling items dating as far back as 1997. Many of the numerous reconciling items were offsetting, so cash is materially correct in the accounting records. However, accounting staff should have posted and cleared these items as part of the reconciliation process. Reconciling items found on the year end cash reconciliation should only pertain to the most recent months.

The University should update its policies and procedures outlining the proper process for preparing monthly and year end cash reconciliations. These policies and procedures should emphasize the importance of posting and clearing reconciling items on a monthly basis.

MANAGEMENT'S DISCUSSION AND ANALYSIS
(unaudited)

Virginia Commonwealth University's Management's Discussion and Analysis provides a discussion and analysis of the University's financial performance during the fiscal year ended June 30, 2004, with comparative information presented for the fiscal year ended June 30, 2003. This discussion does not include the component units of the University other than the Virginia Commonwealth University Intellectual Property Foundation. While maintaining its financial health is crucial to the long-term viability of the University, the primary mission of a public institution of higher education is to provide education, research, and public service. As such, net assets are accumulated only as needed to ensure that there are sufficient reserve funds for future operations and to implement new programs.

This discussion has been prepared by management, along with the financial statements and related note disclosures, and should be read in conjunction with them. The financial statements, notes, and this discussion are the responsibility of management.

Using the Annual Report

This report consists of three basic financial statements: the Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; and the Statement of Cash Flows and provides information on the University as a whole and presents a long-term view of the University's finances.

Statement of Net Assets

The Statement of Net Assets presents the financial position as of the end of the fiscal year and includes all assets and liabilities. The difference between total assets and total liabilities is net assets, which is an indicator of the current financial condition of the University. Assets and liabilities are generally measured using current values, with capital assets as the one notable exception because they are stated at historical cost less an allowance for depreciation.

Net assets are divided into three major categories. The first category is invested in capital assets, net of related debt, which provides the equity in property, plant, and equipment owned by the University. The next asset category is restricted net assets, which is divided into two categories: nonexpendable and expendable. The corpus of nonexpendable restricted resources is available only for investment purposes. Expendable restricted net assets are available for expenditure by the University but must be spent for purposes as determined by donors and/or external entities that have placed time or purpose restrictions on the use of the assets. The final category is unrestricted net assets, which is available to the University for any lawful purpose of the University.

The following table reflects the condensed Statement of Net Assets. For more detailed information, see the accompanying Statement of Net Assets.

	2004	2003
ASSETS		
Current and other assets	$318,194,587	$248,465,841
Capital assets, net	411,457,489	376,935,131
Total assets	729,652,076	625,400,972
LIABILITIES		
Current and other liabilities	93,299,340	107,480,460
Noncurrent liabilities	255,338,248	184,811,064
Total liabilities	348,637,588	292,291,524
NET ASSETS		
Invested in capital assets, net of related debt	255,523,256	238,212,331
Restricted	30,364,843	27,195,431
Unrestricted	95,126,389	67,701,686
Total net assets	$381,014,488	$333,109,448

- The University's assets increased $104.3 million and liabilities increased $56.3 million.

- The University's net assets increased $47.9 million in fiscal year 2004.

Statement of Revenues, Expenses, and Changes in Net Assets

The Statement of Revenues, Expenses, and Changes in Net Assets presents operating results, as well as nonoperating revenues and expenses. State appropriations, while budgeted for operations, are considered nonoperating revenues according to generally accepted accounting principles.

The following is a schedule of the revenues and expenses for the year ended June 30, 2004, with comparative data for the year ended June 30, 2003.

	2004	2003
Operating revenues:		
Student tuition and fees	$ 118,792,030	$ 99,926,510
Grants and contracts	166,507,528	149,370,120
Sales and services of educational departments	14,073,362	7,982,193
Auxiliary enterprises	56,169,201	49,048,955
Hospital services	14,648,597	15,113,012
Other revenues	5,269,812	9,815,379
Total operating revenues	375,460,530	331,256,169
Operating expenses:		
Program activities:		
Instruction	195,305,780	190,419,481
Research	109,968,721	101,496,018
Public service	5,873,696	5,119,446
Supporting services:		
Academic support	28,047,988	29,010,466
Student services	7,075,356	7,351,353
Institutional support	40,522,122	36,302,146
Operation and maintenance of plant	30,981,740	27,723,999
Student aid	14,857,349	14,923,272
Auxiliary enterprises	38,470,582	34,845,952
Hospital services	12,306,939	12,543,335
Depreciation expense	25,845,164	24,927,593
Other expenses	(17,526)	7,073,140
Total operating expenses	509,237,911	491,736,201
Operating loss	(133,777,381)	(160,480,032)
Nonoperating revenues (Expenses):		
State appropriations	154,275,981	164,330,658
Gifts	15,953,944	14,838,938
Investment income, net of investment expense	4,521,221	2,834,409
Interest on capital asset-related debt	(8,797,810)	(8,053,763)
Total nonoperating revenues	165,953,336	173,950,242
Income before other revenues and expenses	32,175,955	13,470,210
Additions to permanent endowments	223,941	336,907
Capital appropriations	15,484,497	2,980,086
Capital gifts	20,647	2,439,181
Change in net assets	47,905,040	19,226,384
Net assets - beginning of year	333,109,448	313,883,064
Net assets - end of year	$ 381,014,488	$ 333,109,448

- Income before other revenues and expenses increased $18.7 million over the prior year.

- Capital appropriations increased $12.5 million over the prior year. This includes $10.1 million for the Massey Cancer Center Addition.

- Student tuition and fees increased $18.9 million as a result of tuition and fee increases of 8.6 percent for residents and 11.3 percent for non-residents over the spring 2003 annualized rates. The increase in operating revenue offset the decrease in state appropriations of $10 million and provided resources for University priorities. Operating expenses increased $17.5 million.

- Grant and contract revenue increased $17.1 million as a result of increased awards.

Statement of Cash Flows

The Statement of Cash Flows provides information about cash receipts and payments during the year. This statement assists users in assessing the University's ability to generate net cash flows and meet its obligations as they come due and its need for external financing.

The following is a summary of the Statement of Cash Flows for the year ended June 30, 2004, with comparative data for the year ended June 30, 2003. For more detailed information, see the accompanying Statement of Cash Flows.

	2004	2003
Cash provided (used) by:		
Operating activities	$(106,790,062)	$(150,256,842)
Noncapital financing activities	172,480,943	185,479,412
Capital financing activities	(4,826,893)	(9,027,180)
Investing activities	(30,767,193)	(5,234,325)
Net increase in cash	30,096,795	20,961,065
Cash and cash equivalents, beginning of year	99,388,189	78,427,124
Cash and cash equivalents, end of year	$ 129,484,984	$ 99,388,189

- The University's operating cash flows increased as a result of tuition revenues, which were used to offset reductions in state appropriations included in noncapital financing activities.

Capital Assets and Debt Administration

Capital Assets

Presented next is the schedule of capital assets, net of depreciation. Depreciation expense totaled $25.8 million for the University.

	2004	2003
Land	$ 27,949,369	$ 26,945,169
Land improvements and infrastructure	5,328,399	4,018,845
Buildings	294,214,164	284,059,975
Equipment	35,390,561	32,205,843
Library books	11,000,072	11,349,492
Construction-in-progress	37,574,924	18,355,807
Total	$411,457,489	$376,935,131

- The University completed construction of the Student Commons Phase III in fiscal year 2004. The Central Dining Facility and Gladding Residence Addition opened for the fall 2004 semester. Capital projects under construction include the Massey Cancer Center Addition, Sanger Hall Research Lab Renovation, Brandt Hall project (Rhoads Hall II), and University Libraries Renovation.

Debt

At June 30, 2004, the University had $220.3 million in debt outstanding.

- The University issued notes payable in the amount of $51.4 million to fund construction of the Academic Parking Deck IV project, Central Dining Facility project, Massey Cancer Center Addition, and Brandt Hall project.

- The University took advantage of a favorable bond market and issued $43.5 million in general revenue pledge refunding bonds to refund, in advance of maturities, the University's outstanding Series 1995, 1996A, and 1996B. By refunding the bonds, the University was able to reduce the cumulative debt service requirements by $4.3 million in future years.

Future Financial Effects

The following are known facts and circumstances that will affect future financial results.

- State appropriations have been increased to $160.5 million for fiscal year 2005.

- University employees will receive an average salary increase of three percent in fiscal year 2005.

- In November 2004, the University issued a note to the Virginia College Building Authority (VCBA) in the amount of $10,855,000. The proceeds of the note will be used to finance the Brandt Hall project.

- The Board of Visitors approved a 5.5 percent increase in resident undergraduate tuition and mandatory fee rates and a 5.1 percent increase for resident graduate tuition and mandatory fee rates for fiscal year 2005. Nonresident tuition and mandatory fees increased by less than one percent.

- The University's Board of Visitors approved VCU 2020, an update to its master site plan, which reflects a 30,000-student capacity and limited geographic growth because of the landlocked nature of the two main campuses. Highlights include:

    - <u>Monroe Park Campus Addition</u> – a $199 million project, east of Belvidere Street and between Main and Canal Streets, that will include a new School of Business building, a second classroom building for the School of Engineering, two residential colleges, a renovation of the historic Central Belting building to house VCU's Adcenter, an executive conference center, an art gallery, and underground parking for 800 vehicles. The Commonwealth has appropriated $25 million towards the construction of the new Schools of Business and Engineering buildings. The remaining $174 million (87 percent of the estimated construction cost) will be funded by private donations and user support.

    - <u>New School of Nursing building</u> – a $14.6 million Nursing Building at 11th and Leigh Streets will help alleviate the Commonwealth's critical nursing shortage. Modern nursing education and research facilities will allow VCU to double the number of undergraduate nursing students and expand research and clinical services. The general obligation bond issue, which was approved by voters in 2002, provides $11.6 million for the construction, with private fundraising providing the remaining $3 million of the project cost.

    - <u>New School of Medicine building</u> – a 500,000 square-foot project is anticipated to be VCU's highest priority for the next state bond bill. The new VCU School of Medicine would replace the obsolete West Hospital and A.D. Williams Clinic, providing modern classroom and laboratory facilities commensurate with being one of the nation's top medical schools.

    - <u>Grace Street "area of interest"</u> – a tract of land east of Belvidere Street and west of Madison Street, bordered by Grace Street and the alley between Grace and Franklin Streets. The master site plan envisions a mix of University and private development.

VIRGINIA COMMONWEALTH UNIVERSITY
STATEMENT OF NET ASSETS
As of June 30, 2004

	University	VCU Health System Authority
ASSETS		
Current assets:		
Cash and cash equivalents (Note 2)	$ 129,484,984	$ 59,232,115
Short-term investments (Note 2)	54,090,131	49,367,429
Accounts receivable:		
Student, Net of allowance of $2,021,456	5,740,203	-
Sponsors, Net of allowance of $200,000	16,323,044	-
Patient, Net of allowance of $71,045,000	-	90,764,253
Contributions and gifts	-	-
Due from component units	845,896	-
Due from Commonwealth of Virginia	2,027,025	-
Student loans receivable, current portion	4,207,637	-
Other assets	3,110,365	10,025,808
Total current assets	215,829,285	209,389,605
Noncurrent assets:		
Restricted cash and cash equivalents	-	-
Endowment investments (Note 2)	3,337,051	-
Other investments (Note 2)	51,269,938	189,444,115
Contributions and gifts, Net of discount and allowance of $3,102,191	-	-
Student loans receivable, Net of allowance of $3,375,576	20,168,016	-
Loans receivable	-	-
Due from component units	21,517,508	716,173
Other long-term assets	6,072,789	7,572,365
Nondepreciable capital assets (Note 4)	65,524,293	-
Depreciable capital assets, Net (Note 4)	345,933,196	276,727,625
Total noncurrrent assets	513,822,791	474,460,278
Total assets	729,652,076	683,849,883
LIABILITIES		
Current liabilities:		
Accounts payable and accrued liabilities	51,759,716	152,822,631
Deferred revenue	26,464,345	-
Due to component units	-	688,784
Long-term liabilities - current portion (Note 8)	15,075,279	14,659,196
Total current liabilities	93,299,340	168,170,611
Noncurrent liabilities:		
Funds held for others (Note 5)	25,732,605	-
Due to component units	-	2,260,000
Other	-	27,000
Long-term liabilities (Note 8)	229,605,643	99,803,135
Total noncurrent liabilities	255,338,248	102,090,135
Total liabilities	348,637,588	270,260,746

MCV Foundation	VCU Foundation	VCU Real Estate Foundation	VCU School of Engineering Foundation	Eliminations	Total
$ 13,198,000	$ 9,590,979	$ 654,122	$ 595,560	$ -	$ 212,755,760
8,133,000		-	-	-	111,590,560
-	-	-	-	-	5,740,203
-	-	-	-	-	16,323,044
-	-	-	-	-	90,764,253
3,554,770	943,422	210,296	1,240,431	-	5,948,919
-	-	-	-	(845,896)	-
-	-	-	-	-	2,027,025
-	-	-	-	-	4,207,637
-	12,027	1,000	7,843,316	-	20,992,516
24,885,770	10,546,428	865,418	9,679,307	(845,896)	470,349,917
-	-	6,487,618	-	-	6,487,618
113,494,000	29,801,077	-	1,688,600	-	148,320,728
91,660,000	24,074,250	-	21,512,094	(27,081,729)	350,878,668
6,773,230	3,476,592	-	5,717,479	-	15,967,301
-	-	-	-	-	20,168,016
951,000	-	-	-	-	951,000
-	-	1,150,681	-	(23,384,362)	-
52,000	-	732,576	1,294,803	(1,294,803)	14,429,730
-	-	-	-	-	65,524,293
2,103,000	210,962	48,754,425	22,065,267	(20,660,107)	675,134,368
215,033,230	57,562,881	57,125,300	52,278,243	(72,421,001)	1,297,861,722
239,919,000	68,109,309	57,990,718	61,957,550	(73,266,897)	1,768,211,639
3,762,000	-	863,291	40,196	(81,620)	209,166,214
-	-	-	-	-	26,464,345
-	1,150,681	133,000	24,843,475	(26,815,940)	-
-	180,495	1,302,245	10,000	-	31,227,215
3,762,000	1,331,176	2,298,536	24,893,671	(26,897,560)	266,857,774
-	-	-	-	-	25,732,605
4,598,000	22,483,729	19,916,173	14,694,055	(63,951,957)	-
-	160,573	1,212,422	20	-	1,400,015
-	637,811	30,088,516	30,000	-	360,165,105
4,598,000	23,282,113	51,217,111	14,724,075	(63,951,957)	387,297,725
8,360,000	24,613,289	53,515,647	39,617,746	(90,849,517)	654,155,499

VIRGINIA COMMONWEALTH UNIVERSITY
STATEMENT OF NET ASSETS
As of June 30, 2004

	University	VCU Health System Authority
NET ASSETS		
Invested in capital assets, Net of related debt	255,523,256	199,649,869
Restricted for:		
Nonexpendable:		
Scholarships and fellowships	2,816,027	-
Departmental uses	521,024	17,306,738
Expendable:		
Scholarships and fellowships	3,831,587	-
Research	5,302,689	-
Departmental uses	12,849,319	601,047
Loans	4,633,006	-
Capital projects	411,191	-
Unrestricted	95,126,389	196,031,483
Total net assets	$ 381,014,488	$ 413,589,137

The accompanying Notes to Financial Statements are an integral part of this statement.

MCV Foundation	VCU Foundation	VCU Real Estate Foundation	VCU School of Engineering Foundation	Eliminations	Total
-	-	-	-	-	455,173,125
-	-	-	-	-	2,816,027
113,494,000	32,379,977	-	2,249,685	-	165,951,424
-	-	-	-	-	3,831,587
-	-	-	-	-	5,302,689
95,109,000	9,327,493	-	8,828,508	-	126,715,367
-	-	-	-	-	4,633,006
-	-	-	-	-	411,191
22,956,000	1,788,550	4,475,071	11,261,611	17,582,620	349,221,724
$ 231,559,000	$ 43,496,020	$ 4,475,071	$ 22,339,804	$ 17,582,620	$ 1,114,056,140

VIRGINIA COMMONWEALTH UNIVERSITY
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
As of June 30, 2004

	University	VCU Health System Authority
Operating revenues:		
Student tuition and fees, Net of scholarship allowances of $25,942,626	$ 118,792,030	$ -
Federal grants and contracts	135,400,261	-
State grants and contracts	10,395,829	-
Local grants and contracts	686,982	-
Nongovernmental grants and contracts	20,024,456	-
Sales and services of educational departments	14,073,362	-
Contributions and gifts	-	-
Auxiliary enterprises:		
Sales and services	36,800,666	-
Student fees, Net of scholarship allowances of $1,323,291	19,368,535	-
Hospital services	14,648,597	899,203,188
Other revenues	5,269,812	-
Total operating revenues	375,460,530	899,203,188
Operating expenses:		
Instruction	195,305,780	-
Research	109,968,721	-
Public service	5,873,696	-
Supporting services:		
Academic support	28,047,988	-
Student services	7,075,356	-
Institutional support	40,522,122	-
Operations and maintenance of plant	30,981,740	-
Student aid	14,857,349	-
Auxiliary enterprises	38,470,582	-
Hospital services	12,306,939	823,178,972
Depreciation expense	25,845,164	28,310,111
Other expenses	(17,526)	-
Total operating expenses	509,237,911	851,489,083
Operating gain/(loss)	(133,777,381)	47,714,105
Nonoperating revenues (expenses):		
State appropriations	154,275,981	-
Gifts	15,953,944	-
Investment income, Net of investment expense of $814,949	4,521,221	3,832,613
Interest on capital asset-related debt	(8,797,810)	(3,890,090)
Other	-	(10,807,677)
Net nonoperating revenues	165,953,336	(10,865,154)
Income before other revenues and expenses	32,175,955	36,848,951
Other revenues:		
Additions to permanent endowments	223,941	-
Capital appropriations	15,484,497	-
Capital gifts	20,647	118,346
Decrease in beneficial interest in trusts	-	1,645,877
Increase in net assets	47,905,040	38,613,174
Net assets - Beginning of year	333,109,448	374,975,963
Net assets - End of year	$ 381,014,488	$ 413,589,137

The accompanying Notes to Financial Statements are an integral part of this statement

MCV Foundation	VCU Foundation	VCU Real Estate Foundation	VCU School of Engineering Foundation	Eliminations	Total
$ -	$ -	$ -	$ -	$ (427,187)	$ 118,364,843
-	-	-	-	(5,638)	135,394,623
-	-	-	-	-	10,395,829
-	-	-	-	-	686,982
-	-	-	-	(1,390,097)	18,634,359
-	-	-	-	(245,368)	13,827,994
-	-	-	-	-	-
-	-	-	-	(2,076,117)	34,724,549
-	-	-	-	-	19,368,535
-	-	-	-	(1,908,473)	911,943,312
2,217,000	1,056,504	7,506,680	1,365,077	(6,715,413)	10,699,660
2,217,000	1,056,504	7,506,680	1,365,077	(12,768,293)	1,274,040,686
-	475,876	-	-	(61,574)	195,720,082
-	-	-	-	(1,614,578)	108,354,143
-	-	-	-	(31,988)	5,841,708
19,949,000	-	-	-	(13,715,233)	34,281,755
-	-	-	-	(500)	7,074,856
935,000	-	-	-	(2,386)	41,454,736
-	-	2,807,422	40,960	(1,656,129)	32,173,993
1,262,000	-	-	-	-	16,119,349
-	-	-	-	(220,334)	38,250,248
-	-	-	-	(13,069,327)	822,416,584
88,000	-	1,502,314	881,126	-	56,626,715
181,000	3,806,912	375,738	1,942,656	(4,932,755)	1,356,025
22,415,000	4,282,788	4,685,474	2,864,742	(35,304,804)	1,359,670,194
(20,198,000)	(3,226,284)	2,821,206	(1,499,665)	22,536,511	(85,629,508)
-	-	-	-	-	154,275,981
32,170,000	4,198,439	330,000	979,350	(21,519,327)	32,112,406
23,209,000	4,688,753	252,832	3,277,830	(1,525,387)	38,256,862
-	-	(2,022,082)	(1,315,091)	-	(16,025,073)
-	-	-	-	-	(10,807,677)
55,379,000	8,887,192	(1,439,250)	2,942,089	(23,044,714)	197,812,499
35,181,000	5,660,908	1,381,956	1,442,424	(508,203)	112,182,991
5,415,000	1,423,557	-	18,630	-	7,081,128
-	-	-	-	-	15,484,497
-	-	-	-	-	138,993
-	-	-	-	-	1,645,877
40,596,000	7,084,465	1,381,956	1,461,054	(508,203)	136,533,486
190,963,000	36,411,555	3,093,115	20,878,750	18,090,823	977,522,654
$ 231,559,000	$ 43,496,020	$ 4,475,071	$ 22,339,804	$ 17,582,620	$ 1,114,056,140

VIRGINIA COMMONWEALTH UNIVERSITY
STATEMENT OF CASH FLOWS
For the Year Ended June 30, 2004

	University
Cash flows from operating activities:	
Tuition and fees	$ 120,914,136
Grants and contracts	167,577,704
Auxiliary enterprise charges	56,876,570
Hospital services charges	14,648,597
Payments to suppliers	(124,221,114)
Payments to employees	(356,365,991)
Loans issued to students	(5,447,000)
Collection of loans to students	4,356,490
Other receipts	14,870,546
Net cash used by operating activities	(106,790,062)
Cash flows from noncapital financing activities:	
State appropriations	155,698,556
Direct lending receipts	112,659,686
Direct lending disbursements	(112,659,686)
Gifts and contributions	16,177,885
VCU Health System Authority loan repayment received	963,594
Repayment of noncapital long term-debt	(359,092)
Net cash provided by noncapital financing activities	172,480,943
Cash flows from capital financing activities:	
Proceeds from issuance of note payable	99,229,134
State appropriations for capital assets	14,061,922
Gifts for capital assets	20,647
Purchase of capital assets	(60,615,789)
Principal paid on capital-related debt	(48,724,997)
Interest paid on capital-related debt	(8,797,810)
Net cash used by capital financing activities	(4,826,893)
Cash flows from investing activities:	
Proceeds from sales and maturities of investments	104,058,287
Investment income	2,679,888
Purchases of investments	(137,505,368)
Net cash provided by investing activities	(30,767,193)
Net increase in cash	30,096,795
Cash and cash equivalents - Beginning of year, as restated (Note 22)	99,388,189
Cash and cash equivalents - End of year	$ 129,484,984

	University
RECONCILIATION OF NET OPERATING EXPENSES TO NET CASH	
USED BY OPERATING ACTIVITIES:	
Operating loss	$ (133,777,381)
Adjustments to reconcile net gain/(loss) to net cash used by operating activities:	
Depreciation and amortization expense	25,845,164
Loss on asset disposition/sale	491,869
Provision for uncollectible accounts	(45,432)
Changes in assets and liabilities:	
Receivables	1,020,835
Other assets	(6,282,534)
Accounts payable	6,401,966
Deferred revenue	3,023,988
Compensated absences and deferred compensation	(5,278,443)
Deposits	1,809,906
Net cash used by operating activities	$ (106,790,062)

The accompanying Notes to Financial Statements are an integral part of this statement.

VIRGINIA COMMONWEALTH UNIVERSITY

NOTES TO FINANCIAL STATEMENTS

AS OF JUNE 30, 2004

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

As one of only three Carnegie Doctoral/Research University-Extensive Universities in Virginia, Virginia Commonwealth University plays a significant role in providing a college-trained workforce, high quality health care, and cultural enrichment for the Richmond area and the Commonwealth.

More than 27,000 undergraduate, graduate, and professional students pursue 174 degree programs on the University's two campuses: the Monroe Park Campus, situated in the historic Fan District, and the Medical College of Virginia (MCV) Campus, located two miles east in the commercial and governmental district of downtown Richmond. The University's 16 schools include the School of Engineering, one of the largest School of Arts in the country, as well as the South's oldest School of Social Work. The University is also the site for the VCU Health System Authority (Authority), one of the most comprehensive academic health centers in the nation. In addition, the University operates the VCU School of the Arts in Qatar, located in the capital city of Doha, which provides special educational opportunities in the design professions to the citizens of Qatar.

The University's accounting policies conform with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB), including all applicable GASB pronouncements, as well as applicable Financial Accounting Standards Board (FASB) statements and interpretations, Accounting Principles Board opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

The Authority's accounting policies conform with generally accepted accounting principles as prescribed by GASB, including all FASB statements and interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure issued, unless those pronouncements conflict with or contradict GASB pronouncements.

The accounting policies of the Medical College of Virginia Foundation, VCU Foundation, VCU Real Estate Foundation, and VCU School of Engineering Foundation conform with the generally accepted accounting principles as prescribed by FASB, which are comparable to the GASB accounting principles except for certain disclosures.

The accompanying financial statements are prepared in accordance with generally accepted accounting principles as prescribed by GASB Statement 34 *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments* and GASB Statement 35, *Basic Financial Statements and Management's Discussion and Analysis of Public Colleges and Universities.* Because the University is a component unit of the Commonwealth of Virginia, it is included in the Comprehensive Annual Financial Report of the Commonwealth.

A. <u>Reporting Entity</u>

The accompanying financial statements include the accounts of all organizational units of the University and the VCU Intellectual Property Foundation, a component unit, which is blended (consolidated) with University operations. These statements are presented as stand-alone statements of the University.

In accordance with GASB Statement 39, *Determining Whether Certain Organizations Are Component Units*, the financial statements include the MCV Foundation, VCU Foundation, VCU Real Estate Foundation, and VCU School of Engineering Foundation effective for the fiscal year ending June 30, 2004. GASB Statement 39 provides additional guidance to determine whether certain organizations for which the University is not financially accountable should be reported as component units. Generally, it requires an organization that raises and holds economic resources for the direct benefit of the University be reported as a component unit. As a result, where in the past the University presented summary financial information of certain of its foundations in the Notes to Financial Statements, the University will be required under GASB Statement 39 to include selected foundations in the body of its financial statements**.** The financial statements also continue to include the Authority as a discrete component unit.

The Authority is a public corporate body and political subdivision of the Commonwealth of Virginia created and established by an Act of the General Assembly of the Commonwealth of Virginia during 1996. The Authority is a tax-exempt, not-for-profit organization under the provisions of Internal Revenue Code Section 115. For additional information regarding the Authority, contact the Office of the Chief Financial Officer, P.O. Box 980510; Richmond, VA 23298-0510.

The Authority's principal activity is the operation of the Medical College of Virginia Hospitals (the Hospitals), University Health Services, Inc. and subsidiaries (UHS), and MCV Associated Physicians (MCVAP). The Hospitals, a division of the Authority, is an approximately 900-bed teaching hospital which provides inpatient and outpatient services primarily to patients in the Commonwealth of Virginia. MCVAP, formed in 1991 as a non-stock, not-for-profit charitable educational organization, functions as the group practice plan for those physicians and health care professionals who have faculty appointments in the VCU School of Medicine. Separate financial statements for MCVAP may be obtained from MCVAP's corporate office at 1605 Rhoadmiller Street, Richmond, VA 23220-1100. The Hospitals, UHS, and MCVAP are included in the enterprise funds of the Authority.

UHS, a component unit of the Authority, is a not-for-profit, non-stock, tax-exempt corporation, which supports the educational, scientific, and charitable purposes and activities of the University and, in particular, the activities of the MCV Campus and the Hospitals. These activities include, but are not limited to, activities undertaken pursuant to Section 23-50.16B of the <u>Code of Virginia</u>. UHS is a blended component unit of the Authority due to the significance of the operational and financial relationship between the two entities. Virginia Premier Health Plan, Inc. (VA Premier) is a wholly-owned subsidiary of UHS. VA Premier is a for-profit health maintenance organization (HMO) whose primary purpose is to provide quality health care within a managed care framework.

The MCV Foundation is a not-for-profit corporation organized to aid, strengthen, and extend the work, services and objectives of the MCV Campus of the University. This mission is achieved by receiving contributions, investing and managing funds, disbursing current funds and a portion of the total return on endowment, and providing information about the activities of the MCV Campus and the MCV Foundation. The MCV Foundation is exempt from federal income taxes under Internal Revenue Code Section 501(c)(3). For additional information regarding the Medical College of Virginia Foundation, contact Michael Dowdy, President, P.O. Box 980234; Richmond, VA 23298-0234.

The VCU Foundation is a Virginia corporation, which functions as a nonprofit charitable foundation solely to assist and support the University. The VCU Foundation is exempt from federal income taxes under Internal Revenue Code Section 501(c)(3). The VCU Foundation exists solely to assist, support, and foster the University in all proper ways that may from time to time be approved by the trustees of the Foundation with the guidance of the University. The VCU Foundation manages and distributes current and endowment gifts for all schools, departments, and programs throughout the University with major emphasis on programs for the Monroe Park Campus. For additional information regarding VCU Foundation, contact Thomas C. Burke, Jr., Director, Blanton House, 828 West Franklin Street; P.O. Box 842026; Richmond, VA 23284-2026.

The VCU Real Estate Foundation is a Virginia corporation, which functions as a nonprofit charitable foundation solely to assist and support the University. The VCU Real Estate Foundation is exempt from federal income taxes under Internal Revenue Code Section 501(c)(3). For additional information regarding VCU Real Estate Foundation, contact Real Estate and Foundation Services, 700 West Grace St., Suite 3200; P.O. Box 843075; Richmond, VA 23284-3075.

The VCU Real Estate Foundation's controlled affiliate, Universal Ford Acquisition Corporation, is a Virginia nonstock corporation, which functions as a nonprofit organization solely to support the VCU Real Estate Foundation The Universal Ford Acquisition Corporation is exempt from federal income taxes under Internal Revenue Code Section 501(c)(3).

The VCU School of Engineering Foundation is a Virginia corporation, which functions as a nonprofit charitable foundation solely to assist and support the University. The Foundation is exempt from federal income taxes under Internal Revenue Code Section 501(c)(3). The sole purpose of the VCU School of Engineering Foundation is to provide financial and other support to the VCU School of Engineering for the benefit of the University. For additional information regarding the VCU School of Engineering Foundation, contact Real Estate and Foundation Services, 700 West Grace St., Suite 3200; P.O. Box 843075; Richmond, VA 23284-3075.

The University also benefits from a number of organizations that exist mainly to support the various purposes and activities of the University and Authority. The assets of these affiliated organizations, which are separately incorporated and managed by their own Boards, are not included in these statements. The affiliated organizations are listed below and are described in Note 10:

- Virginia Biotechnology Research Park Authority
- MCV Alumni Association of VCU
- VCU Alumni Association
- MCV/VCU. Dental Faculty Practice Association

B. Basis of Accounting

The financial statements of the University have been prepared on the accrual basis including depreciation expense relating to capitalized fixed assets. Revenues for the summer term are prorated on the basis of student class days occurring before and after June 30.

Pursuant to GASB Statement 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Authority has elected to apply the provisions of all relevant pronouncements of FASB that do not contradict or conflict with GASB pronouncements, including those issued after November 30, 1989. The University applies only those FASB pronouncements issued prior to November 30, 1989.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States 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. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

C. Allowance for Uncollectible Receivables

The allowance for uncollectible receivables is based on management's evaluation of the collectibility of individual receivables. Receivables are charged against the allowance when deemed to be uncollectible. Subsequent recoveries are added to the allowance.

D. Pledges Receivable

Unconditional gifts are recognized when the donor makes a promise to give that is, in substance, unconditional. Unconditional gifts expected to be collected within one year are recorded at their net realizable value. Unconditional gifts expected to be collected in future years are recorded at the net present value of the estimated future cash flows.

Donations or contributions of land, buildings, equipment, and gifts-in-kind, except contributed services, are recorded at fair market value when received or pledged, if earlier.

E. Investments

Investments in open-end mutual funds, debt securities, and equity securities that have readily determinable fair values are carried at fair value. The fair values of marketable equity securities, bonds, and other investments are based on quoted market prices. Investments held in the liquidity fund (securities with a maturity of less than one year) of the University are reported as current assets with the remaining investments reported as noncurrent assets.

F. Inventories

Inventories are valued at the lower of cost (generally determined on the first-in, first-out method) or market.

G. Investment Income

Investment income, including net realized and unrealized gains or losses on investment transactions and investment expense, is recorded as nonoperating revenue.

It is the practice of the VCU Foundation, MCV Foundation, and VCU School of Engineering Foundation to annually distribute a set percentage of each endowment corpus to be utilized for the purpose of the fund as stipulated by the donor and/or established by the Foundation. Any excess net investment income over the distribution percentage is added to the individual endowment fund corpus.

H. Accrued Compensated Absences

University full-time classified, part-time classified and faculty employed on or after January 1, 1999, who are also active members of the Virginia Retirement System (VRS) are covered under the Virginia Sickness and Disability Program (VSDP). The plan provides for sick leave, family and personal leave, short-term disability benefits, and long-term disability benefits. Full-time classified, part-time classified, and faculty employed prior to January 1, 1999, who are active members of VRS, participate in VSDP under one of two options or remain under the traditional sick leave program in which classified employees and 12-month faculty earn five hours of leave each pay period regardless of the length of state service and nine month faculty accrue 48 hours per semester. One VSDP option permitted eligible employees to convert accumulated sick leave balances to short-term disability credits. The other allowed for the conversion of sick leave balances to VRS service credit. The University was not required to currently fund the cost of conversion to VRS service credit. Enrollment in the VSDP is irrevocable and no additional enrollments are planned. Under VSDP, unused VSDP sick leave and family and personal leave balances do not carry forward from one year to the next and employees are not paid for unused balances upon termination. The converted short-term disability credits of classified employees are payable upon termination in accordance with the Commonwealth of Virginia’s sick leave payout policy discussed below. Faculty who converted sick leave balances to short-term disability credits are not compensated for these balances at termination.

Full-time and part-time 12-month faculty and classified employees earn annual leave based upon the number of years of continuous state service. Faculty and classified employees carry forward annual leave balances from one year to the next based on the years of service. Upon termination, the payout of unused annual leave balances is subject to the maximum payout policy for each category of employee.

Employees who are not subject to the overtime provisions of the Fair Labor Standards Act may be eligible to earn compensatory leave. Leave is earned on an hour-for-hour basis for having worked additional hours in a workweek or on holidays or scheduled days off. Compensatory leave may be used for paid time off and is payable upon termination. Accrued compensatory leave lapses within 12 months from the date it is earned and once lapsed may not be used or paid upon termination.

The University records a liability for all unused annual, non-VSDP sick and compensatory leave, and unused short-term disability credits, as well as related fringe benefits. Annual and compensatory leave balances are paid in full upon termination. Non-VSDP sick leave and short-term disability credits are payable upon employment termination and are limited to 25 percent of the value accumulated or $5,000, whichever is less, under the

Commonwealth of Virginia's sick leave pay-out policy for employees with five or more years of service.

The Authority records a liability for all paid time off and related FICA taxes expected to be paid.

I. Capital Assets

Capital assets are stated at cost or, if donated, at fair market value on the date of acquisition. Equipment costing $5,000 or more with a useful life of two or more years is capitalized. Infrastructure assets are included in the financial statements and are depreciated. The University and the Authority record depreciation on property, plant, and equipment, including capital leases and excluding land and construction-in-progress, computed over the estimated useful lives of the assets based on the straight-line method. The general range of estimated useful lives is 10 to 40 years for buildings and fixtures and 5 to 20 years for equipment. The estimated useful life of library books is five years. The general range of estimated useful lives is 10 to 25 years for land improvements and infrastructure. Expenditures for construction-in-progress are capitalized as incurred and reflected in net investment in plant. Interest expense relating to construction is capitalized net of interest income earned on resources set aside for this purpose. Capital assets at the time of disposal revert to the Commonwealth of Virginia for disposition.

The VCU School of Engineering Foundation, VCU Foundation, and VCU Real Estate Foundation record the acquisition of real estate at cost or, if donated, at fair market value at the time of donation. Depreciation is provided for properties that are actively rented, using the straight-line method, at rates adequate to amortize the cost of the property over its estimated useful life. The estimated useful lives of these properties are between 10 to 40 years.

The VCU Real Estate Foundation records the acquisition of equipment at cost or, if donated, at fair market value at the time of donation. Depreciation is computed on a straight-line basis over the estimated useful lives of the equipment. The estimated useful lives for equipment are between 5 and 20 years.

The MCV Foundation records property and equipment at cost for purchased items and at fair value for contributed items. Acquisitions of fixed assets with a cost less than $1,000 are expensed as acquired. Depreciation is computed on a straight-line basis over the estimated useful lives of the assets. The estimated useful lives range between 3 and 39 years.

J. Hospital Services

In addition to the services provided by the Authority to patients, the University provides facilities, graduate medical education, clinical support, and administrative support to hospitals. The revenues and expenditures necessary to provide the services are classified as hospital services.

K. Charity Care

The Authority provides care to patients who meet certain criteria under its indigent care policy without charge or at amounts less than its established rates. Because the Authority does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. The costs and expenses incurred in providing these services are included in operating expenses. Charges written off to charity care for the year ended June 30, 2004, measured at established rates, approximated $220,455,000.

L. Net Patient Service Revenue

Net patient service revenue is reported in hospital services at the estimated net realizable amounts from patients, third-party payors, and others for services rendered and includes estimated retroactive adjustments due to future audits, reviews, and investigations.

Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered. Such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, and investigations.

A summary of the payment arrangements with major third-party payors follows:

- Anthem Inpatient acute care services rendered to Anthem subscribers are paid at a per diem or discounted rate. Outpatient services rendered to Anthem subscribers are reimbursed at discounted rates or using applicable fee schedules. The rates are not subject to retroactive adjustment.

- Medicare Inpatient acute care services and defined capital costs rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates may vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Inpatient non-acute services, certain outpatient services, and education related to Medicare beneficiaries are paid based on prospectively determined rates and a discounted cost reimbursement methodology. The Authority is reimbursed for cost-reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Authority and audits thereof by the Medicare fiscal intermediary. The Authority's Medicare cost reports have been audited by the Medicare fiscal intermediary through June 30, 2001.

- Medicaid Inpatient acute care services rendered to Medicaid program beneficiaries are paid at a per diem rate. Outpatient services rendered to Medicaid program beneficiaries are reimbursed on prospectively determined rates and a cost reimbursement methodology. In addition to inpatient and outpatient services provided to Medicaid program beneficiaries, Medicaid reimburses the Authority for services provided to indigent patients up to a certain amount. Total Medicaid and indigent reimbursements to the Authority totaled $207 million in 2004. The

Authority's Medicaid cost reports have been audited by the Medicaid program representative through June 30, 2002.

In accordance with third-party payor agreements, the difference between payment for services and the Authority's standard billing rates results in contractual adjustments. Contractual adjustments are recorded as deductions from patient service revenue in the period in which the related services are rendered. The annual settlements of reimbursement for patients services covered by third parties are determined through cost reports for Medicare (for outpatient and educational costs) and Medicaid. The settlements are subject to audit and retroactive adjustment by these third parties.

Provisions for possible adjustments of cost reports have been estimated and reflected in the accompanying financial statements as considered appropriate. The difference in any year between the originally estimated amount and the final determination is reported in the year of determination as an adjustment to net patient service revenue. Net patient service revenue was decreased by approximately $6.07 million in 2004, as a result of such settlements.

M. Premiums Earned

VA Premier has contracts with the Virginia Department of Medical Assistance Services (DMAS) wherein VA Premier provides health care services to the Aid for Families with Dependent Children (AFDC), the Children's Medical Services Insurance Plan (CMSIP), and Aged, Blind, and Disabled (ABD) residents of Virginia through a health maintenance organization (HMO). VA Premier recognizes premiums received from DMAS for members in the period to which health care coverage relates. All of VA Premier's premiums were earned from contracts with DMAS.

N. Estimated Medical Claims Payable

VA Premier provides for the liability arising from services rendered to HMO members, but unpaid at year-end based upon the experience of VA Premier and cost-per-member trends. Although considerable variability is inherent in such estimates, management believes that the liability is adequate. Any required revisions to these estimates are reflected in operations of the period in which such revisions are determined.

O. Net Assets

GASB Statement 34 requires that the Statement of Net Assets report the difference between assets and liabilities as net assets, not fund balances. Net assets are classified according to external donor restrictions or availability of assets for satisfaction of obligations. Invested in capital assets, net of related debt, represents the net value of capital assets (property, plant, and equipment) less the debt incurred to acquire or construct the asset. Nonexpendable restricted net assets are gifts that have been received for endowment purposes, the corpus of which cannot be expended. Expendable restricted net assets represent gifts that have been received for specific purposes.

The Authority's investment balances include resources restricted for debt service under a bond indenture agreement, resources restricted under malpractice trust agreement, resources restricted by insurance regulations of the Commonwealth of Virginia, and resources restricted under the pension plan agreement.

The Authority's restricted net assets consist principally of beneficial interests in perpetual trust funds established by split interest agreements. Split interest agreements are trust agreements established by donors under which the Authority receives benefits that are shared with other beneficiaries. The trust agreements established by donors provide for a third party to hold the trust assets. These trusts do not permit donors to revoke their charitable contributions. Trust assets of $17,284,000, which are restricted by donors for the Authority in perpetuity, are reported at fair value, which approximates the present value of the future cash receipts from the trust assets.

P. Scholarship Allowances and Student Aid

Financial aid to students is reported in the financial statements under the alternative method as prescribed by the National Association of College and University Business Officers (NACUBO). Certain aid (loans and funds provided to students as awarded by third parties and Federal Direct Lending) is accounted for as third party payments and is credited to the student's account as if the student made the payment. All other aid is reflected in the financial statements as operating expenses or scholarship allowances, which reduce revenues. The amount reported as operating expense represents the portion of aid that was provided to the student in the form of cash. Scholarship allowances represent the portion of aid provided to the student in the form of reduced tuition. Under the alternative method, these amounts are computed on a total university basis by allocating the cash payments to students, excluding payments for services, on the ratio of all aid to the aid not considered to be third party aid.

Q. Intangibles

The Authority's other assets include $4,424,899 of goodwill that is not amortized, but reviewed annually for impairment in accordance with Statement of Financial Accounting Standards (SFAS) No 142, *Goodwill and Other Intangible Assets.*

R. Revenue and Expense Classifications

Operating revenues include activities that have the characteristics of exchange transactions such as: (1) student tuition and fees, net of scholarship discounts and allowances; (2) sales and services of auxiliary enterprises, net of scholarship allowances; and (3) federal, state, and nongovernmental grants and contracts.

Nonoperating revenues include activities that have the characteristics of nonexchange transactions such as gifts and other revenue sources that are defined as nonoperating revenues by GASB Statement 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*, and GASB Statement 34, such as state appropriations and investment and interest income.

Nonoperating expenses include interest on debt related to the purchase of capital assets and losses on the disposal of capital assets. All other expenses are classified as operating expenses.

2. CASH AND INVESTMENTS

Cash

All cash of the University is maintained in accounts collateralized in accordance with the Virginia Security for Public Deposits Act, Section 2.2-4400 et seq. of the Code of Virginia or covered by federal depository insurance.

Investments

The University's non-state funds, other than endowment and funds internally designated to function as an endowment, are managed by professional investment managers. The University's investment objective is to ensure the preservation of asset values with sufficient liquidity to meet cash disbursement requirements. The investment policy of the University is established by the Board of Visitors and is monitored by its Finance, Investment, and Property Committee. Investment managers may invest in the following types of investments: direct obligations of the United States; obligations unconditionally guaranteed by the United States, including collateralized mortgage obligations; obligations of any agency or instrumentality of the United States; repurchase agreements; banker's acceptances; commercial paper issued by domestic corporations; money market funds; corporate notes of domestic corporations; fully hedged debt obligations of sovereign governments and companies;obligations of the Commonwealth of Virginia; asset backed securities with AAA ratings; and negotiable certificates of deposit and negotiable bank notes of domestic banks. The allocation of assets at June 30, 2004, is 8.2 percent high-quality cash equivalents with maturities of less than three months and 91.8 percent high-quality fixed income securities.

In accordance with bond resolutions adopted by its Board of Directors, the Authority can invest assets held with trustees in the following instruments: obligations of federal agencies or those guaranteed by the United States of America; savings accounts; certificates of deposit; time deposits; and obligations of the Commonwealth of Virginia.

The University's investments that are represented by specific identifiable investment securities are classified as to the level of risk assumed at year-end. Category 1 includes investments that are insured or registered or for which the securities are held by the University or its agents in the University's name. Category 2 includes uninsured and unregistered investments for which the securities are held in the broker's or dealer's trust department or safekeeping agent in the University's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the broker or dealer, or by its trust department or safekeeping agent, but not in the University's name. All of the University's investments are categorized as Category 1.

For management purposes, endowment funds and funds internally designated to function as an endowment, are held in the investment pools of the VCU Foundation and the MCV Foundation. These funds remain the property of the University. The investment pools consist of cash equivalents, bonds, preferred and common stocks, and real estate. The University's equity in the investment pools is based on units or shares in the investment pools. Consequently, funds held by the foundations are not categorized as to the level of risk.

Investments are reported at fair value (market). Categorization of investments at June 30, 2004 is as follows:

	Category 1	Fair Value	Cost
University:			
U.S. government and U.S. government agency securities	$ 27,625,562	$ 27,625,562	$ 27,715,044
Corporate bonds	9,408,214	9,408,214	9,461,934
Commercial paper	1,396,991	1,396,991	1,395,842
Municipal bonds	127,619	127,619	111,807
Mutual and money market funds	-	39,763,815	39,763,971
Investments held by the Treasurer of Virginia - Securities loans	-	2,611,591	2,611,591
Investments held by the VCU Intellectual Property Foundation	-	681,599	40,206
Investment pools held by:			
VCU Foundation	-	22,483,729	19,138,988
MCV Foundation	-	4,598,000	3,053,962
Total University	38,558,386	108,697,120	103,293,345
Authority:			
Cash and cash equivalents	55,339,805	55,339,805	55,339,805
Money market instruments	3,388,576	3,388,576	3,388,576
U.S. government and U.S. government agency securities	40,734,906	40,734,906	41,233,026
Corporate obligations	46,418,799	46,418,799	46,538,690
Commercial paper	28,659,506	28,659,506	28,766,638
Interest receivable	783,966	783,966	783,966
Mutual funds	4,765,589	4,765,589	4,758,849
Equity securities	20,785,458	20,785,458	19,344,056
Externally restricted:			
Cash and cash equivalents	14,470,948	14,470,948	14,470,948
U.S. government and U.S. government agency securities	6,157,453	6,157,453	6,173,959
Commercial paper	22,350	22,350	22,350
Beneficial interest in trust	-	17,284,188	17,284,188
Total Authority	221,527,356	238,811,544	238,105,051
MCV Foundation:			
Common Fund Index Fund	-	63,432,000	45,377,000
Corporate stocks	-	27,192,000	19,841,000
Private equity	-	8,231,000	8,183,000
Corporate bonds	-	16,720,000	16,318,000
Common Fund International Equity Fund	-	17,494,000	12,773,000
U.S. government obligations	-	65,006,000	65,631,000
Vanguard Index Fund	-	5,925,000	4,481,000
Temporary cash investments	-	8,133,000	8,133,000
Other	-	1,154,000	1,154,000
Less: Held for the University	-	4,598,000	3,053,962
Total MCV Foundation	-	208,689,000	178,837,038

	Category 1	Fair Value	Cost
VCU Foundation:			
Fixed income instruments	-	9,879,308	9,783,527
Equities	-	43,996,019	42,893,186
Less: Held for the University	-	22,483,729	19,138,988
Total VCU Foundation	-	31,391,598	33,537,725
VCU School of Engineering Foundation:			
Private equity	-	1,802,886	1,438,590
Fundamental Managers Fund, L.P.	-	12,466,302	12,466,302
Private Advisors Small Company Buyout Fund, L.P.	-	507,005	507,005
Private Advisors Hedged Equity Fund, L.P.	-	2,185,411	2,185,411
Private Advisors Stable Value Fund, LTD	-	6,239,090	6,239,090
Total VCU School of Engineering Foundation	-	23,200,694	22,836,398
Total investments	$260,085,742	$610,789,956	$576,609,557

3. JOINT VENTURES AND EQUITY INVESTMENTS

As of June 30, 2004, the Authority sold all investments in joint ventures held as of June 30, 2003, except its investment in 7th and Marshall Corporation in which it has a net investment totaling approximately $387,000 as of June 30, 2004. A disclosure of investments held as of June 30, 2004, is noted below. Individual financial statements for the 7th and Marshall Corporation investment is available from the Authority's corporate office.

Investment in 7th and Marshall Corporation

Included in other long-term assets on the accompanying Statement of Net Assets is a capital contribution to 7th and Marshall Corporation of $500,000. UHS and Hospital Hospitality House, Inc., are the sole members of the 7th and Marshall Corporation, a not-for-profit corporation formed to support the charitable, educational, and scientific activities of UHS and Hospital Hospitality House, Inc. The 50 percent investment in 7th and Marshall Corporation is accounted for under the equity method of accounting. The investment is carried at $387,000.

4. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2004 follows:

	Beginning Balance	Additions	Reductions	Ending Balance
University:				
Land	$ 26,945,169	$ 1,004,200	$ -	$ 27,949,369
Land improvements and infrastructure	11,614,780	1,966,069	10,883	13,569,966
Buildings	440,547,864*	23,016,696	1,068,917	462,495,643
Equipment	98,741,169	11,004,985	12,058,353	97,687,801
Library books	79,429,632	4,648,324	-	84,077,956
Construction-in-progress	18,355,807	44,824,849	25,605,732	37,574,924
Total cost of capital assets	675,634,421	86,465,123	38,743,885	723,355,659
Less accumulated depreciation for:				
Land improvements and infrastructure	7,595,935	656,515	10,883	8,241,567
Buildings	156,487,889	12,669,881	876,291	168,281,479
Equipment	66,535,326	7,521,024	11,759,110	62,297,240
Library books	68,080,140	4,997,744	-	73,077,884
Total accumulated depreciation	298,699,290	25,845,164	12,646,284	311,898,170
Total capital assets, net	$376,935,131	$ 60,619,959	$26,097,601	$411,457,489
Authority:				
Land	$ 2,683,248	$ -	$ -	$ 2,683,248
Buildings	265,750,994	29,509,190	-	295,260,184
Equipment	196,652,875	58,467,867	1,370,589	253,750,153
Construction-in-progress	35,993,041	32,057,179	63,588,479	4,461,741
Total cost of capital assets	501,080,158	120,034,236	64,959,068	556,155,326
Less accumulated depreciation for:				
Buildings	101,143,173	11,374,629	-	112,517,802
Equipment	151,294,145	16,886,158	1,270,404	166,909,899
Total accumulated depreciation	252,437,318	28,260,787	1,270,404	279,427,701
Total capital assets, net	$248,642,840	$ 91,773,449	$63,688,664	$276,727,625
MCV Foundation:				
Property and equipment, net depreciation	$ 752,000	$ 1,439,000	$ 88,000	$ 2,103,000
VCU Foundation:				
Land and building – not depreciated	$ 210,962	$ -	$ -	$ 210,962

	Beginning Balance	Additions	Reductions	Ending Balance
VCU Real Estate Foundation:				
Land and buildings	$ 35,342,272	$ 18,989,062	$ 951,019	$ 53,380,315
Construction-in-progress	14,351,433	-	14,351,433	-
Total cost of capital assets	49,693,705	18,989,062	15,302,452	53,380,315
Less: Accumulated depreciation	3,149,967	1,475,923	-	4,625,890
Total capital assets, net	$ 46,543,738	$ 17,513,139	$15,302,452	$ 48,754,425
VCU School of Engineering Foundation:				
Land and buildings	$ 28,010,521	$ -	$ 1,015,662	$ 26,994,859
Construction-in-progress	172,513	52,714	-	225,227
Total cost of capital assets	28,183,034	52,714	1,015,662	27,220,086
Less: Accumulated depreciation	4,283,583	871,236	-	5,154,819
Total before eliminations	23,899,451	(818,522)	1,015,662	22,065,267
Less: Included on University	21,531,343	(871,236)	-	20,660,107
Total capital assets, net	$ 2,368,108	$ 52,714	$ 1,015,662	$ 1,405,160

* Buildings' beginning balance was adjusted for a building that was not recorded until the current year, but was owned in the prior year.

5. FUNDS HELD FOR OTHERS

At June 30, 2004, the University held deposits for others, which are composed of the following:

Federal loan programs	$22,955,759
Student organizations and others	2,776,846
Total	$25,732,605

6. VCU FACULTY EARLY RETIREMENT INCENTIVE PLAN

The University established the VCU Faculty Early Retirement Incentive Plan (Plan) to provide a financial early retirement incentive for certain tenured faculty that will facilitate the release of tenured faculty resources for budget reallocation or reduction in accordance with the University Strategic Plan goals, changes in enrollment, and other University needs. Tenure is a permanent appointment granted to associate professors and professors, which continues until the faculty member leaves the University, is dismissed for cause, or is terminated due to a financial crisis.

The Plan provides an annuity for five years from the date of retirement equal to 20 percent of the average University salary of the faculty members eligible to participate in the Plan, not to exceed 30 percent of the participant's base annual salary from University resources at the time the agreement was signed. In addition, the University provides a health care benefit supplement until the participant becomes Medicare eligible (currently age 65) if the participant retires or up to 18 months of COBRA benefits if the participant does not retire.

As of June 30, 2004, 50 faculty members were enrolled in the Plan. Payments during fiscal year 2004 were $872,153. The present value of future Plan payments schedule follows:

Fiscal Year	Plan Obligations
2005	$ 842,509
2006	690,227
2007	492,742
2008	383,706
2009	117,155
2010-2014	16,403
Total	$2,542,742

7. FACULTY ALTERNATIVE SEVERANCE OPTION

The University established a Faculty Alternative Severance Option Policy (FASO) whereby certain University faculty are eligible to receive defined severance benefits or, in some instances, enhanced retirement benefits (VRS employees only) upon their resignation or retirement from the University. Participating academic and administrative units must develop business plans designed to achieve strategic budget reductions, program modifications, and/or the elimination of positions. Faculty who hold certain teaching, research, administrative, and/or professional faculty positions in areas that are targeted in the business plans for modification or reduction and meet the eligibility criteria defined in the policy are eligible. FASO is not an early retirement program.

Under FASO, severance benefits include severance pay for up to 36 weeks of University salary depending on years of continuous service and employer contributions for health and life insurance coverage for up to 12 months. Enhanced retirement benefits are available through the VRS Defined Benefit Retirement Program with retirement income based on average salary, age, and length of service. In lieu of the severance benefits, eligible faculty may elect to have the University purchase additional years of age or service credit, thereby enhancing their overall VRS retirement income.

As of June 30, 2004, 111 faculty members participated. Payments during fiscal year 2004 were $6,320,838. Future payments due in 2005 are $1,556,801.

8. LONG-TERM LIABILITIES

Long-term liabilities consist of bonds, notes payable, capital leases, installment purchases, deferred compensation, compensated absences, and estimated losses on malpractice claims.

Bonds Payable

The Commonwealth of Virginia issues bonds for agencies and institutions of the Commonwealth. The University has received a portion of the proceeds to fund capital construction. The University recognizes a liability associated with its share of the bonds and remits principal and interest payments related to this liability to the Treasurer of Virginia. The general revenue pledge bonds (Section 9d Bonds) carry interest rates of 4.25 to 5.75 percent and are due through 2033. The Commonwealth of Virginia revenue bonds (Section 9c bonds) carry interest rates of 2.5 to 6 percent and are payable through 2017. Included in the total general revenue pledge bonds are outstanding bonds payable in the amount of $19.2 million, which will be repaid by the VCU Real Estate Foundation as described in Note 15. Of the total Commonwealth of Virginia revenue bonds, outstanding bonds payable in the amount of $2,674,784 will be repaid by the Authority as described in Note 15.

Virginia College Building Authority

The Virginia College Building Authority (VCBA) issues Educational Facilities Revenue Bonds (Public Higher Education Financing Program). As a participating institution in this program, the University issued a note payable to the VCBA. This note, along with the notes of other institutions, is held by the VCBA as security for the Educational Facilities Revenue Bonds. For accounting purposes, the financing arrangement is considered to represent a note payable. The notes have interest rates of three to six percent.

Virginia Public Building Authority

The University participates in a financing arrangement with the Virginia Public Building Authority to construct a steam plant adjacent to the MCV Campus. The University considers this financing arrangement to be a capital lease with imputed interest rates of 2.25 to 5.85 percent.

Virginia Biotechnology Research Park Authority

As more fully described in Note 10, the University occupies space owned by the Virginia Biotechnology Research Park Authority. For accounting purposes, this arrangement is considered to be a capital lease with an imputed interest rate of nine percent.

Defeasance of Debt

In the current year, the University issued $22.8 million of 2004A Series general revenue pledge bonds with an average interest rate of 4.03 percent to advance refund $21.4 million of 1996A Series bonds with an average interest rate of 5.65 percent. The University also issued $20.6 million of 2004B Series general revenue bonds with an average interest rate of 3.63 percent to advance refund $12.4 million of 1996B Series bonds with an average interest rate of 5.52 percent, and $7.1 million of 1995 Series bonds with an average interest rate of 5.70 percent. The net proceeds of $45.5 million, plus an additional $760,512, were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the 1995, 1996A, and 1996B Series bonds. As a result, the bonds are considered to be defeased and the liability for those bonds has been removed from the Statement of Net Assets.

The advance refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of $5 million. The University completed the advance refunding to reduce its total debt service payments over the next 17 years by $4.3 million and to obtain an economic gain of $3.5 million.

The 2004A and 2004B Series general revenue bonds were issued at a premium of $2 million in excess of the face value of the bonds. That premium is reported in the long-term debt section of the financial statements.

In prior fiscal years, a portion of the Commonwealth of Virginia revenue bonds, of which the University has a share, has been defeased. Details relating to the prior years' defeasances are reported in the Comprehensive Annual Financial Report of the Commonwealth.

The changes in long-term liabilities are as shown below:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
University:					
Bonds payable:					
General revenue pledge bonds	$ 66,455,000	$ 43,460,005	$43,170,005	$ 66,745,000	$ 3,150,000
Commonwealth of Virginia revenue bonds	25,940,831	-	2,936,524	23,004,307	2,003,436
Total bonds payable	92,395,831	43,460,005	46,106,529	89,749,307	5,153,436
Notes payable:					
Virginia College Building Authority	58,842,345	55,769,129	1,638,867	112,972,607	2,560,000
Capital leases:					
Virginia Public Building Authority	12,742,269	-	840,444	11,901,825	885,306
Virginia Biotechnology Research Park Authority	5,175,991*	243,602	228,751	5,190,842	261,361
Total capital leases	17,918,260	243,602	1,069,195	17,092,667	1,146,667
Installment purchases	730,222	-	269,498	460,724	231,844
Total long-term debt	169,886,658	99,472,736	49,084,089	220,275,305	9,091,947
Compensated absences	20,478,414	15,714,052	15,886,392	20,306,074	3,584,022
Deferred compensation	9,205,646	2,086,887	7,192,990	4,099,543	2,399,310
Total	$199,570,718	$117,273,675	$72,163,471	$244,680,922	$15,075,279
Authority:					
Bonds payable:					
General revenue pledge bonds	$ 71,095,000	$ -	$6,015,000	$ 65,080,000	$ 1,995,000
Capital leases	279,788	2,466,966	476,508	2,270,246	498,826
Installment purchases	947,787	7,798,808	1,667,689	7,078,906	2,086,990
Total long-term debt	72,322,575	10,265,774	8,159,197	74,429,152	4,580,816

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Estimated losses on malpractice claims	28,437,301	208,831	3,738,190	24,907,942	1,000,000
Compensated absences	14,215,636	2,391,113	1,481,512	15,125,237	9,078,380
Total	$114,975,512	$ 12,865,718	$13,378,899	$114,462,331	$14,659,196
VCU Foundation:					
Notes payable	$ 1,000,000	$ -	$ 181,694	$ 818,306	$ 180,495
VCU Real Estate Foundation:					
Tax exempt bonds payable	$ 15,810,000	$ -	$ 270,000	$ 15,540,000	$ 280,000
Notes payable	16,087,113	1,739,872	1,976,224	15,850,761	1,022,245
Total	$ 31,897,113	$ 1,739,872	$ 2,246,224	$ 31,390,761	$ 1,302,245
VCU School of Engineering Foundation:					
Notes payable	$ 50,000	$ -	$ 10,000	$ 40,000	$ 10,000

* Capital Leases - Virginia Biotechnology Research Park Authority's beginning balance was adjusted for a capital lease that was not recorded until the current year, but was acquired in the prior year.

Long-term debt matures as follows:

	Fiscal Year	Revenue Bonds	Notes Payable	Capital Leases	Installment Purchases	Total
University:						
	2005	$ 5,153,436	$ 2,560,000	$ 2,248,800	$ 231,844	$ 10,194,080
	2006	5,124,300	3,240,000	2,247,713	227,446	10,839,459
	2007	5,351,029	3,950,000	2,246,869	1,434	11,549,332
	2008	5,506,518	4,100,000	2,245,505	-	11,852,023
	2009	5,666,750	4,315,000	2,244,255	-	12,226,005
	2010-2014	29,040,878	24,790,000	10,592,645	-	64,423,523
	2015-2019	17,991,396	31,730,000	2,285,160	-	52,006,556
	2020-2024	7,285,000	28,485,000	-	-	35,770,000
	2025-2029	4,350,000	3,685,000	-	-	8,035,000
	2030-2034	4,280,000	-	-	-	4,280,000
Add:	Unamortized Premium	-	6,117,607	-	-	6,117,607
Less:	Interest	-	-	(7,018,280)	-	(7,018,280)
	Total	$89,749,307	$112,972,607	$ 17,092,667	$ 460,724	$220,275,305

	Fiscal Year	Revenue Bonds	Notes Payable	Capital Leases	Installment Purchases	Total
Authority:						
	2005	$1,995,000	$ -	$ 553,518	$2,086,990	$ 4,635,508
	2006	2,080,000	-	459,974	2,001,837	4,541,811
	2007	2,175,000	-	459,974	1,032,803	3,667,777
	2008	2,270,000	-	459,974	578,799	3,308,773
	2009	2,385,000	-	497,005	556,886	3,438,891
	2010-2014	13,805,000	-	-	575,172	14,380,172
	2015-2019	17,670,000	-	-	246,419	17,916,419
	2020-2024	22,700,000	-	-	-	22,700,000
	Less: Interest	-	-	(160,199)	-	(160,199)
	Total	$65,080,000	$ -	$ 2,270,246	$7,078,906	$ 74,429,152
VCU Foundation:						
	2005	$ -	$ 180,495	$ -	$ -	$ 180,495
	2006	-	185,182	-	-	185,182
	2007	-	190,051	-	-	190,051
	2008	-	262,578	-	-	262,578
	Total	$ -	$ 818,306	$ -	$ -	$ 813,306
VCU Real Estate Foundation:						
	2005	$ 280,000	$ 1,022,245	$ -	$ -	$ 1,302,245
	2006	295,000	2,262,557	-	-	2,557,557
	2007	305,000	907,824	-	-	1,212,824
	2008	320,000	11,560,847	-	-	11,880,847
	2009	335,000	9,177	-	-	344,177
	Thereafter	14,005,000	88,111	-	-	14,093,111
	Total	$ 15,540,000	$ 15,850,761	$ -	$ -	$ 31,390,761
VCU School of Engineering Foundation:						
	2005	$ -	$ 10,000	$ -	$ -	$ 10,000
	2006	-	10,000	-	-	10,000
	2007	-	10,000	-	-	10,000
	2008	-	10,000	-	-	10,000
	Total	$ -	$ 40,000	$ -	$ -	$ 40,000

A summary of future interest requirements is as follows:

	Fiscal Year	Revenue Bonds	Notes Payable	Total
University:				
	2005	$ 3,581,078	$ 5,081,215	$ 8,662,293
	2006	3,351,605	4,973,524	8,325,129
	2007	3,143,668	4,832,631	7,976,299
	2008	2,985,025	4,652,001	7,637,026
	2009	2,825,697	4,465,439	7,291,136
	2009-2014	11,261,235	18,920,782	30,182,017
	2014-2019	5,694,326	11,828,144	17,522,470
	2019-2024	2,768,569	3,957,081	6,725,650
	2024-2029	1,655,375	151,147	1,806,522
	2029-2034	520,125	-	520,125
	Total	$37,786,703	$58,861,964	$96,648,667
Authority:				
	2005	$ 3,178,941	$ -	$ 3,178,941
	2006	3,087,421	-	3,087,421
	2007	2,991,721	-	2,991,721
	2008	2,878,221	-	2,878,221
	2009	2,758,971	-	2,758,971
	2010-2014	11,812,695	-	11,812,695
	2015-2019	7,723,976	-	7,723,976
	2020-2024	2,443,087	-	2,443,087
	Total	$36,875,033	$ -	$36,875,033

9. RETIREMENT, PENSION PLANS, AND POST EMPLOYMENT BENEFITS OTHER THAN PENSION BENEFITS

University

Substantially all full-time, classified, salaried and certain full-time faculty employees of the University participate in the defined benefit retirement plan administered by the Virginia Retirement System (VRS). The VRS is an agent multiple-employer public employee retirement system (PERS) that acts as a common investment and administrative agency for the Commonwealth of Virginia and its political subdivisions.

The long-term disability benefit provided by the Virginia Sickness and Disability Program (VSDP) is administered by VRS. Funding for this benefit has been incorporated into the VRS contribution shown below.

The University’s payroll costs, excluding accrued payroll, for employees covered by the VRS for the year ended June 30, 2004 were $222,559,148. The University’s total payroll costs for the year were $283,245,474.

Information regarding types of employees covered, benefit provisions, employee eligibility requirements including eligibility for vesting, and the authority under which benefit provisions, as well as employer and employee obligations to contribute is established and disclosed in the Comprehensive Annual Financial Report of the Commonwealth of Virginia.

The University's total VRS contributions were $11,448,004 for the year ended June 30, 2004, which included the five percent employee contribution assumed by the employer. These contributions represent 17 percent of covered payroll for law enforcement employees and five percent of covered payroll for employees covered by VRS.

The VRS does not measure assets and pension benefit obligations separately for individual state institutions. The Comprehensive Annual Financial Report of the Commonwealth of Virginia provides disclosure of the Commonwealth's unfunded pension benefit obligation at June 30, 2004. The same report contains historical trend information showing VRS's progress in accumulating sufficient assets to pay benefits when due.

Full-time faculty and certain administrative staff are eligible to participate in other retirement plans. These are fixed-contribution programs where the retirement benefits received are based upon the employer (5.4 percent) and employee (5 percent) contributions (all of which are paid by the University) plus interest and dividends.

Individual contracts issued under the plans provide for full and immediate vesting of both the University's and the employee's contributions. Contributions to other retirement plans were calculated using the base salary $100,086,037 in fiscal year 2004. Total pension costs under these plans were $10,408,948 in fiscal year 2004.

The state participates in the VRS-administered statewide group life insurance program, which provides post employment life insurance benefits to eligible retired and terminated employees. The state also provides health care credits against the monthly health insurance premiums of its retirees who have at least 15 years of state service and participate in the state health plan. Information related to these plans is available at the statewide level in the Comprehensive Annual Financial Report of the Commonwealth.

The Deferred Compensation Plan (DCP) gives eligible participants (full- and part-time faculty and staff who contribute at least $10 each pay period through the TDA Program) a matching contribution of 50 percent up to a maximum of $20 each pay period of the amount faculty and staff contribute through the TDA Program.

Authority

Prior to July 1, 1997, employees of the Authority were employees of the Commonwealth of Virginia. These employees are eligible to participate in a defined benefit pension plan administered by the VRS. The VRS also administers life insurance and health-related plans for retired employees. Information relating to these plans is available at the statewide level only in the Commonwealth of Virginia's Comprehensive Annual Financial Report. The Commonwealth, not the Authority, has overall responsibility for these plans. Total pension costs for the year were approximately $4,645,000.

Effective July 1, 1997, the Authority established the Virginia Commonwealth University Health System Authority Defined Contribution Plan (the Plan). All employees working at least 35 hours of service per week are eligible to participate in the Plan. Per the Plan document, as approved by the Authority's Board of Directors, the Authority contributes up to eight percent of the participant's salary to the Plan, up to a maximum of $30,000. Total contributions to the Plan for the year were approximately $8,831,000. The Authority shall have the right at anytime, and without the consent of any party, to terminate the Plan in its entirety. The Authority's Board of Directors must approve in writing any changes to the provisions of the Plan, including the contribution requirements.

The Authority has also established the Virginia Commonwealth University Health System Authority Health Care Providers Defined Contribution Plan (the HCP Plan). All persons hired as a health care provider on or after July 1, 1993 and prior to July 1, 1997 and working at least 35 hours of service per week are eligible to participate in the HCP Plan. All significant provisions of the HCP Plan, including the contribution requirements, are similar to the Plan. Total contributions to the HCP Plan for the year were approximately $19,000.

The Plan and the HCP Plan use the accrual basis of accounting and the Plan assets, which consist of mutual funds, are carried at fair market value. The fair market values of the mutual funds are based on quoted market prices. Individual organizations that hold five percent or more of the assets are:

	2004
Fidelity Investments	$25,089,058
TIAA/CREF	18,827,947
VALLIC	9,390,871
Net assets available for plan benefits	$53,307,876

MCVAP sponsors the MCVAP 401(a) Retirement Plan, a noncontributory, defined contribution plan which covers substantially all full-time clinical provider employees of MCVAP. Contributions to the 401(a) Plan by MCVAP, as determined annually at the discretion of the Board of Directors, were approximately $4,906,000 for the year.

MCVAP sponsors the VCUHS 401(a) Retirement Plan, a defined contribution plan, which covers all non-medical employees of MCVP and the VCUHS 457(b) Retirement Plan, a salary reduction plan that represents employee contributions. These plans became effective on January 1, 2002 and replaced the MCVAP 403(b) plan for all non-medical staff. The 401(a) Plan contributions are a function of the employee's age plus years of service per the table below. MCVAP employees may contribute to the VCUHS 457(b) Plan. Employees may also receive a two percent matching contribution in their VCUHS 401(a) Plan based on their VCUHS 457(b) salary reduction contribution.

Age + Years of Service	401(a) Plan Employer Contribution
65+	10%
55 – 65	8
45 – 55	6
35 – 45	4
<35	2

The contributions to the VCUHS 401(a) Plan and the VCUHS 457(b) Plan were $3,160,000.

Effective August 1, 1999, VA Premier adopted a 401(k) plan sponsored by Prudential Mutual Fund Management, Inc. Employees may enter into the plan on the first day of the month coinciding with or following the date on which the employee begins employment. There is no minimum service or age requirement to be in the 401(k) plan. Employees may contribute 1 to 15 percent of their compensation. VA Premier will match 50 percent of the employees' contributions up to four percent of the employees' compensation. Matching will occur based on the bi-weekly pay periods. In addition, VA Premier contributes three percent of the employee's compensation after each bi-weekly payroll effective when the employee begins employment. Employees are fully vested after four years of service in which the employees have at least 1,000 hours of service each year. The total expense to VA Premier was approximately $313,000.

10. RELATED PARTIES

The financial statements do not include the assets, liabilities, or fund balances of affiliated organizations. All of these organizations are separately incorporated entities managed by their own boards and audited by other independent certified public accounting firms or the Auditor of Public Accounts. Each organization is described below.

Virginia Biotechnology Research Park Authority

The primary purpose of the Virginia Biotechnology Research Park Authority is to expand knowledge pertaining to scientific and technological research and development among public and private entities and promote the economic and industrial development of the City of Richmond and the Commonwealth of Virginia. The University currently occupies 34,439 square feet of Biotech One under a capital lease as shown in Note 8. In addition, the University is committed to a 20-year master lease with the Authority, which guarantees monthly rent equal to the principal and interest necessary to amortize the outstanding debt associated with the construction of the facilities and any additional rent required. The maximum amount payable under this lease for space not occupied by the University is $543,235 annually during the first ten years of the lease and $1,278,200 annually for the remainder of the lease term.

MCV Alumni Association of VCU

The purpose of the MCV Alumni Association of VCU is to organize alumni activities for the University. The University provided funding of $237,289 in 2004 as the principal source of funding for the Association's operation.

VCU Alumni Association

The Association was formed for educational purposes to further the best interests of the University, alumni, and students. The University provided funding of $132,248 in 2004 as the principal source of funding for the Association's operation.

MCV/VCU Dental Faculty Practice Association

The Association was established to support the education, research, service, and patient care mission of the School of Dentistry (School) of VCU. The Association promotes and coordinates the delivery of superior patient care at the School.

11. FUNDS HELD IN TRUST BY OTHERS

Under the provisions of the wills of certain benefactors, the University's portion of principal sums with market values of $14,856,200 at June 30, 2004, was held in trust by others. These assets are not included in the University's statement of net assets.

12. COMMITMENTS

The University and the Authority are party to various construction commitments. At June 30, 2004, the remaining commitments were $37,851,520 for the University and approximately $7.9 million for the Authority.

The University is also committed under various operating leases such as for buildings, computer equipment, and business equipment. The University has renewal options on the leased assets for another similar term. In most cases, the University expects that, in the normal course of business, these leases will be replaced by similar leases. Rental expense for the fiscal year ended June 30, 2004, was $3,550,008 for the University and $5,869,000 for the Authority. In addition, the University reimburses the Commonwealth of Virginia $141,735 annually for the use of space in a facility owned by the Commonwealth.

The University has, as of June 30, 2004, the following total future minimum rental payments due under the above leases.

Fiscal Year	University	Authority
2005	$3,374,064	$ 7,561,554
2006	2,082,265	4,880,716
2007	1,462,915	4,660,826
2008	783,512	3,912,941
2009	434,033	573,361
2010-2014	408,711	-
2015-2019	224,206	-
Total future minimum rental payments	$8,769,706	$21,589,398

13. LITIGATION

The University and Authority have been named as a defendant in a number of lawsuits. The final outcome of any of these lawsuits cannot be determined at this time. However, management is of the opinion that any ultimate liability to which the University and Authority may be exposed will not have a material effect upon the entity's financial position.

14. INDEMNIFICATIONS

As permitted or required under Virginia law, the MCV Foundation has certain obligations to indemnify its current and former officers and directors for certain events or occurrences while the officer or director is, or was serving, at the Foundation's request in such capacities. The maximum liability under these obligations is unlimited; however, the Foundation believes that the estimated fair value of these indemnification obligations is minimal.

15. TRANSACTIONS BETWEEN COMPONENT UNITS

The University and its component units provide services and support to each other so as to avoid duplication of efforts as much as possible.

The VCU Foundation and the MCV Foundation hold the University's investments that function as endowments, both true and quasi. The assets are reflected as investments in the University and the component unit's financial statements. These investments are eliminated from the Foundations.

The VCU School of Engineering Foundation constructed a building using the proceeds of debt issued by the University. The building is leased to the University for $1 per year. The VCU School of Engineering Foundation transfers sufficient funds to the University annually to fund the debt service. The University reports the building and the liability for the outstanding debt on the Statement of Net Assets. The annual transfer is recorded by the University as a gift received. The VCU School of Engineering Foundation reports the building, deferred bond issuance costs, prepaid bond interest, a liability to the University, and accrued contribution to the University on its financial statements, all of which are eliminated in the Statement of Net Assets.

The MCV Foundation, VCU Foundation and VCU School of Engineering Foundation solicit funds to benefit the University and transfer a portion of those funds to the University to support programs. These transactions have been eliminated from the Statement of Revenues, Expenses, and Changes in Net Assets from gift revenue and supporting services.

MCVAP, a component of the VCU Health System, transfers a portion of its patient revenues to the University to support the academic and research missions. Those transfers are eliminated from hospital services expenses and gift revenues.

The VCU Real Estate Foundation acquires facilities and rents them to the University and VCU Health System. Those rental expenses are eliminated from operations and maintenance expenses and other revenues. On February 1, 2003, the VCU Real Estate Foundation entered into a financing and support agreement with the University for the Broad and Belvidere student housing facility. Under the terms of the agreement, the Foundation agreed to develop and construct the project and provide for payment of debt service. In return, the University issued $19.2 million of its tax-exempt general revenue pledge bonds, as shown in Note 8, to fund construction and agreed to operate the facility as part of its student housing system. The University reports the bonds as long-term liabilities on the Statement of Net Assets and the Foundation reports the bonds as a Due to the University on its financial statements. The Due to the University is eliminated from the Foundation's financial statements.

The University and VCU Health System support each other through the sharing of capabilities and resources. Reimbursements of costs are made between the entities to ensure that each entity bears its proper portion of costs. Those transactions are eliminated between the revenue recorded and the expense category, so that the expense is included in the expense category that reflects the service delivered to the student or public. In conjunction with a transfer agreement associated with the formation of the Authority, the University transferred parking deck E to the Authority. The Authority assumed responsibility for the payments on the associated construction debt. Debt is payable to the University in installments beginning 2003 through 2016. The parking deck and its related debt are reported on the Authority's financial statements. The related debt for the parking deck is recorded on the University's financial statements. The liability associated with the related debt is eliminated from the University's Statement of Net Assets.

16. SUBSEQUENT EVENT

In November 2004, the University issued a note to the Virginia College Building Authority (VCBA) in the amount of $10,850,000. The proceeds of the note will be used to finance the Rhoads Hall 4 project. The note bears interest at rates ranging from 2.5 to 5.0 percent payable in the years 2005 through 2025.

17. CONTINGENCIES

Through June 30, 1990, the Hospitals were insured under a claims-made policy with respect to institutional and professional liability, each with liability limits of $1 million per incident and an aggregate annual liability limit of $3 million in each policy year. Either the PHICO Insurance Company or the Virginia Insurance Reciprocal provided insurance.

Effective July 1, 1990 and through June 30, 1998, the Hospitals and the Authority were insured under a risk management plan for the Commonwealth of Virginia. This plan was also claims-made with institutional and professional liability limits of $1 million per incident, but with no aggregate limit.

Effective July 1, 1998, the Authority insured itself under a self-insured professional liability, self-administered plan. This plan is claims-made with professional liability limits of $1 million per incident and $3 million in aggregate with excess insurance coverage up to $10 million, which is provided by the Reciprocal of America (the Reciprocal), a multiprovider reciprocal insurance company. A revocable trust has been established and is funded based on actuarially determined reserves. At June 30, 2004, the medical malpractice trust fund includes approximately $7.07 million for claims and related legal expenses for reported and unreported incidents occurring since July 1, 1998. There have been malpractice claims asserted against the Authority by various claimants. The claims are in various stages of processing and some may ultimately be brought to trial. There are also known incidents that have occurred through June 30, 2004 that may result in the assertion of additional claims. In addition, there may be other claims from unreported incidents arising from services provided to patients through June 30, 2004. At June 30, 2004, the Authority's management accrued professional liability losses to the extent they fall within the limits of the Authority's self-insurance program or exceed the limits of the excess insurance coverage. The liability for medical malpractice at June 30, 2004, includes approximately $5,598,000 for claims and related legal expenses for reported and unreported incidents occurring since July 1, 1998. The liability was actuarially determined combining industry data and the Authority's historical experience.

MCVAP's professional liability coverage is provided through a claims-made policy obtained from Universal Re-Insurance Company (URIC), a Bermuda insurance corporation. At June 30, 2001, the policy provided coverage of $1.65 million per occurrence and $8 million in the aggregate. Premiums paid by MCVAP to URIC are recorded as expense by MCVAP and deposited in an irrevocable trust fund administered by SunTrust Bank. Under the terms of the agreement with URIC, no risk has been transferred by MCVAP to URIC. As a result, the irrevocable trust, totaling $9.3 million has been recorded as a deposit in assets with an offsetting liability for estimated losses for malpractice claims (discounted at five percent). There were no premiums paid during 2004.

Through June 30, 2002, an excess professional liability policy was written by the Reciprocal. This policy covers losses in excess of the URIC limits for an additional aggregate amount of $10 million.

Effective July 1, 2002, an excess professional liability policy was written by Columbia Casualty Group of the CNA Insurance Group. This policy covers losses in excess of the URIC limits for an additional aggregate amount of $5 million. This amount was increased to $10 million effective July 1, 2003.

In addition, MCVAP insures itself under a self-insured liability self-administered plan for any claims in excess of its insurance coverage. The Board sets aside funds to be used to fund estimated losses based on actuarially determined reserves. At June 30, 2004, assets whose use is limited includes approximately $9,979,000 that has been designated by the Board to fund malpractice claims. In addition, MCVAP's management accrued estimated losses on malpractice claims (discounted at five percent) includes approximately $9,979,000 in addition to the amount recorded under the URIC agreement.

Funding levels are based on factors such as actual claims history and the percentage of certainty that actual losses will not exceed the funds set aside to cover these losses. During the fiscal year ended June 30, 2004, the funding level was calculated based on an assumption of 90 percent certainty (90 percent confidence level) that the actual losses related to professional liability would not exceed the available funds. During the year ended June 30, 2004, due to changes in malpractice estimates, management reduced the accrual for malpractice insurance funding by approximately $6,382,000, which resulted in a credit for malpractice insurance funding in the Statement of Revenues, Expenses, and Changes in Net Assets.

VA Premier maintains general and professional liability policies. The general liability policy in force is occurrence-based. The coverage under the professional liability policy is made on a claims-made basis and must be renewed or replaced with the equivalent insurance if claims incurred during its terms, but asserted after its expiration, are to be insured. Coverage limits for the general liability policy are $1 million per occurrence and $3 million annual aggregate. The coverage limits for the professional liability policy are $5 million per medical incident and $5 million annual aggregate.

In management's opinion, the claims-made insurance coverage is adequate to cover the estimated ultimate liability which could result upon settlement of claims currently asserted against the Authority and the ultimate liability for medical incidents of which the Authority has knowledge, but for which no claim has been asserted against the Authority. Based upon current historical data, management is of the opinion that the liability, if any, for unreported medical incidents would not have a material effect on the Authority's financial position.

During fiscal 1996, the Department of Health and Human Services (HHS) announced its intention to audit Medicare billings submitted by teaching physicians at all of the major teaching hospitals in the United States. During fiscal 1998, MCVAP received notification from the Department of Justice (DOJ) stating that it was the subject of investigations relating to CHAMPUS and Medicare billing practices. MCVAP has cooperated fully with this notification from the DOJ. At the present time, management does not have sufficient information to determine if MCVAP will have any liability related to these issues or what the potential liability, if any, might be.

18. STOP-LOSS COVERAGE

VA Premier has a stop-loss arrangement to limit its losses on individual claims. This contract provides stop-loss coverage for all VA Premier enrollee claims. This contract provides coverage for 100 percent of certain hospital claims in excess of $100,000 subject to certain limitations and an annual limit of $1 million per enrollee and a lifetime limit of $2 million per enrollee. Reinsurance recoveries, net of stop-loss premiums of approximately $352,000 are included as a reduction in medical claims expense in the year.

19. NET PATIENT SERVICE REVENUE

The Authority's patient service revenue is as follows for the year ended June 30, 2004:

Gross patient revenue:	
Inpatient:	
Routine services	$ 160,437,477
Ancillary services	714,013,357
Outpatient:	
Emergency	51,928,467
Special medical	378,425,473
Total gross patient service revenue	1,304,804,774
Provision for indigent care and contractual adjustments	(682,571,200)
Provision for bad debts	(77,381,018)
Net patient service revenue (Hospitals)	544,852,556
MCVAP's net patient service revenue	97,003,254
Net patient service revenue (Authority)	$ 641,855,810

20. ESTIMATED MEDICAL CLAIMS PAYABLE

Claims expenses and liabilities arising from services rendered to VA Premier's HMO members are reported when it is probable that services have been provided and the amount of the claim can be reasonably estimated. The claims payable includes an estimate of claims that have been incurred, but not reported. At June 30, the amount of these liabilities included in accounts payable and accrued liabilities was $27,546,796. This liability is VA Premier's best estimate based on available information.

21. STATE APPROPRIATIONS – UNRESTRICTED FUNDS

The University receives state appropriations from the General Fund of the Commonwealth. The Appropriation Act specifies that such unexpended appropriations shall revert at the end of the biennium, as specifically provided by the General Assembly, unless the University meets management standards.

The following is a summary of state appropriations by the University for the year ended June 30, 2004, including all reversions.

Original legislative appropriation per Chapter 1042:	
Educational and general programs	$133,329,525
Higher education student financial assistance	11,008,638
Supplemental adjustments:	
Financial assistance for educational and general services	1,200,000
Virginia Department of Health appropriation transfer	300,000
Reappropriation of financial assistance for educational and general services	361,407
Return of pre-payment of fiscal year 2003	1,800,000
General Fund central transfers	2,908,473
Steam plant debt service	602,623
Higher Education Equipment Trust Fund	4,118,027
Higher Education Equipment Trust Fund Non-General Fund payment	(214,930)
Transfers from Higher Education Operating Fund	(1,119,921)
Reversion to the General Fund of the Commonwealth	(17,861)
Adjusted appropriation	$154,275,981

22. RESTATEMENT OF BEGINNING CASH AND CASH EQUIVALENTS

Beginning cash and cash equivalents originally reported in the University's financial statements as of June 30, 2003, have been restated to reflect further evaluation of assets.

Cash and cash equivalents as previously reported June 30, 2003	$93,909,645
Beginning balance adjustments:	
To correct for appropriations receivable previously recorded as a separate line item on the financial statements	5,478,544
Cash and cash equivalents balance at July 1, 2003	$99,388,189

VIRGINIA COMMONWEALTH UNIVERSITY
SCHEDULE OF AUXILIARY ENTERPRISES - REVENUE AND EXPENDITURES
For The Year Ended June 30, 2004

	Athletics	Siegel Center	Food Services	Gyms	Larrick Student Center	Parking and Transportation
Revenue:						
Student fees	$ -	$ -	$ 7,762,036	$ -	$ -	$ -
University fee	6,308,590	2,085,483	-	2,665,724	209,137	1,809,517
Sales and services	1,552,219	1,384,143	1,395,700	296,487	-	6,950,833
Total revenue	7,860,809	3,469,626	9,157,736	2,962,211	209,137	8,760,350
Cost of sales	-	-	-	-	-	-
Net revenue	7,860,809	3,469,626	9,157,736	2,962,211	209,137	8,760,350
Expenditures:						
Personal services	2,511,390	365,617	213,804	1,050,381	130,486	1,470,830
Employee benefits	614,823	82,651	72,027	173,274	34,716	368,824
Contractual services	1,270,533	913,930	4,462,786	219,916	25,324	1,332,044
Supplies and materials	60,489	10,508	(79,103)	146,538	1,524	13,826
Equipment	60,795	119,894	100,687	127,389	728	275,181
Current charges and obligations	3,184,878	927,482	171,924	401,522	44,493	2,290,105
Miscellaneous	204,830	(23,082)	91,937	80,187	6,960	326,912
Operating expenditures	7,907,738	2,397,000	5,034,062	2,199,207	244,231	6,077,722
Interdepartmental recoveries and charges	(6,871)	-	(7,608)	(445)	-	(3,187)
Net operating expenditures	7,900,867	2,397,000	5,026,454	2,198,762	244,231	6,074,535
Excess (deficiency) of revenues over (under) operating expenses before transfers	(40,058)	1,072,626	4,131,282	763,449	(35,094)	2,685,815
Transfers (in) out:						
Mandatory	237,881	1,605,502	142,947	471,041	-	2,695,289
Nonmandatory	(1,502)	(803,648)	2,811,999	1,684,560	-	(688,994)
Excess (deficiency) of revenues over (under) expenditures and transfers	(276,437)	270,772	1,176,336	(1,392,152)	(35,094)	679,520
Beginning fund balance	(258,296)	1,597,339	1,334,411	3,158,635	(35,426)	3,537,994
Ending fund balance	$(534,733)	$ 1,868,111	$ 2,510,747	$ 1,766,483	$(70,520)	$ 4,217,514

Note: This schedule is prepared on the modified accrual basis of accounting and does not support the basic financial statements.

Residence Halls	Stores and Shops	Student Commons	Student Health	Business Services Administration	Development Programs	Unassigned	Steam Plant	Total
$ 11,015,583	$ -	$ -	$ 2,696,466	$ -	$ -	$ 20,104,178	$ -	$ 41,578,263
-	-	2,999,524	1,027,035	-	152,231	(17,257,241)	-	-
1,361,270	2,786,657	99,224	629,614	27,742	8,960	302,810	3,159,153	19,954,812
12,376,853	2,786,657	3,098,748	4,353,115	27,742	161,191	3,149,747	3,159,153	61,533,075
-	1,478,376	-	-	-	-	-	-	1,478,376
12,376,853	1,308,281	3,098,748	4,353,115	27,742	161,191	3,149,747	3,159,153	60,054,699
2,998,780	150,046	986,518	2,389,659	384,810	181,137	10,230	526,016	13,369,704
658,296	40,188	213,562	550,932	102,478	47,730	852	154,083	3,114,436
1,816,544	232,747	152,000	354,637	39,362	15,458	1,771,768	408,690	13,015,739
(81,667)	(70,374)	109,448	446,421	(290,995)	16,321	171,078	415,519	869,533
244,243	15,572	10,167	58,634	19,541	207	-	-	1,033,038
3,090,585	81,815	479,905	135,111	463,991	17,860	(1,229,360)	1,339,903	11,400,214
334,108	39,043	90,162	167,040	9,343	3,528	188,679	398	1,520,045
9,060,889	489,037	2,041,762	4,102,434	728,530	282,241	913,247	2,844,609	44,322,709
(23,499)	-	(37,284)	-	(604,117)	(160,872)	-	-	(843,883)
9,037,390	489,037	2,004,478	4,102,434	124,413	121,369	913,247	2,844,609	43,478,826
3,339,463	819,244	1,094,270	250,681	(96,671)	39,822	2,236,500	314,544	16,575,873
2,409,062	-	695,421	126,418	-	-	224,111	-	8,607,672
(340,377)	464,443	649,667	20,064	(228,226)	-	1,116,376	-	4,684,362
1,270,778	354,801	(250,818)	104,199	131,555	39,822	896,013	314,544	3,283,839
(499,961)	1,288,886	1,337,156	841,697	366,703	46,576	5,961,856	(207,964)	18,469,606
$ 770,817	$ 1,643,687	$ 1,086,338	$ 945,896	$ 498,258	$ 86,398	$ 6,857,869	$ 106,580	$ 21,753,445

Commonwealth of Virginia

Auditor of Public Accounts
P.O. Box 1295
Richmond, Virginia 23218

Walter J. Kucharski, Auditor

December 22, 2004

The Honorable Mark R. Warner
Governor of Virginia

The Honorable Lacey E. Putney
Chairman, Joint Legislative Audit
and Review Commission

Board of Visitors
Virginia Commonwealth University

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

We have audited the accompanying basic financial statements of **Virginia Commonwealth University**, a component unit of the Commonwealth of Virginia, and its aggregate discretely presented component units as of and for the year ended June 30, 2004, as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the financial statements of the component units of the University, which are discussed in Note 1A. Those financial statements were audited by other auditors whose reports thereon have been furnished to us and our opinion, insofar as it relates the amounts included for the component units of the University, is based on the reports of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The financial statements of the component units of the University that were audited by other auditors upon whose reports we are relying were audited in accordance with auditing standards generally accepted in the United States of America, but not in accordance with Government Auditing Standards. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of the University and of its aggregate discretely presented component units as of June 30, 2004, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

As described in the notes to the financial statements, the University has implemented the provisions of GASB Statement 39, *Determining Whether Certain Organizations are Component Units,* which addresses the conditions under which institutions should include associated foundations as component units and how such component units should be displayed in the financial statements.

The management's discussion and analysis on pages three through eight is not a required part of the basic financial statements, but is supplementary information required by the accounting principles generally accepted in the United States of America. 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 opinions on the basic financial statements of the University. The Schedule of Auxiliary Enterprises – Revenue and Expenditures is presented for the purpose of additional analysis and is not a required part of the basic financial statements. The information in the schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statement taken as a whole.

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS

In planning and performing our audit of the financial statements of the University as of and for the year ended June 30, 2004, we considered internal controls over financial reporting and tested compliance with certain provisions of laws, regulations, contracts, and grant agreements 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. We did not consider internal controls over financial reporting or test compliance with certain provisions of laws, regulations, contracts, and grants for the financial statements of the component units of the University, which were audited by other auditors.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the University's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the University's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions, entitled "Ensure Proper Stewardship and Control Over Fixed Assets" and "Ensure Cash Reconciling Items are Resolved Timely" are described in the section titled "Internal Control Findings and Recommendations."

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that none of the reportable conditions described above is a material weakness.

Compliance and Other Matters

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

Status of Prior Findings

The University has not taken adequate corrective action with respect to the previously reported finding "Ensure Proper Stewardship and Control Over Fixed Assets." Accordingly, we included this finding in the section entitled "Internal Control and Recommendations." The University has taken adequate corrective action with respect to audit findings reported in the prior year that are not repeated in this report.

The Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters is intended solely for the information and use of the Governor and General Assembly of Virginia, the Board of Visitors, and management, and is not intended to be and should not be used by anyone, other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

EXIT CONFERENCE

We discussed this report with management at an exit conference held on January 11, 2005.

AUDITOR OF PUBLIC ACCOUNTS

MSM/kva
kva:

VCU
Academic Campus
Virginia Commonwealth University

Office of the Senior Vice President for Finance and Administration

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January 26, 2005

David A. Von Moll
State Comptroller
Virginia Department of Accounts
P.O. Box 1971
Richmond, VA 23218

Dear Mr. Von Moll:

In compliance with the Commonwealth Accounting Policies and Procedures (CAPP) Manual, Section 10200, Financial Management, Virginia Commonwealth University (VCU) is submitting its response to the "Internal Control Findings and Recommendations" of the Auditor of Public Accounts' Report on Audit for the Year Ended June 30, 2004.

Should you have any questions or require additional information, please contact me at 828-6116.

Sincerely,

Paul W. Timmreck

Paul W. Timmreck
Senior Vice President for Finance and Administration

Enclosure

cc: The Honorable Belle S. Wheelan
Walter J. Kucharski, Auditor of Public Accounts
Richard D. Brown, Department of Planning and Budget

During Virginia Commonwealth University's (VCU) annual audit, the Auditor of Public Accounts routinely considers internal controls to determine financial statement auditing procedures. Although the Auditor provides no assurance about internal controls, no material weaknesses were identified during the audit; two reportable conditions are noted in his report.

The following internal control recommendations are included in the VCU Report on Audit for the year ended June 30, 2004:

1. Ensure Proper Stewardship and Control Over Fixed Assets
2. Ensure Cash Reconciling Items are Resolved Timely

Although the Auditor's findings indicate conditions requiring management's attention, the conditions do not have a material effect on the financial statements.

Findings of the Auditor:

1. Ensure Proper Stewardship and Control Over Fixed Assets

   As reported last year, the University did not adequately maintain and safeguard fixed assets in accordance with the University's fixed asset policies and procedures and the Commonwealth's Accounting Policies and Procedures. Exceptions noted in our test work included being unable to locate fixed assets, assets without identification tags, assets with incorrect location or other description data in the fixed asset system, and assets not appearing on the department's inventory verification listing. These exceptions arose from individual department custodians not following procedures for properly maintaining and tracking fixed assets.

   We again recommend that management ensure that each department follows the requirements and guidelines in the University's fixed asset policies and procedures and properly conducts an annual inventory of its fixed assets. Management should establish a uniform procedure of tagging fixed assets so tags are visible for tracking purposes, and update the policies and procedures to reflect changes caused by the new online fixed asset system. We understand the University has hired a consultant to perform a complete inventory of fixed assets, including making sure all assets have tags and the fixed asset system shows the correct location. We also understand that management plans to strictly enforce departmental compliance with the established policies.

   VCU Response

   The University has initiated a comprehensive physical inventory of moveable equipment. Once completed, the University will institute financial penalties for departments that fail to properly maintain fixed assets records. Property management will explore procedures for the uniform tagging of future fixed assets. The fixed asset on-line system is being modified to improve the asset location identifier data, and our policies and procedures will be updated to reflect these changes.

2. Ensure Cash Reconciling Items are Resolved Timely

The University did not resolve old reconciling items when preparing monthly and year-end cash reconciliations. The operating account reconciliation showed reconciling items dating as far back as 1997. Many of the numerous reconciling items were offsetting, so cash is materially correct in the accounting records. However, accounting staff should have posted and cleared these items as part of the reconciliation process. Reconciling items found on the year-end cash reconciliation should only pertain to the most recent months.

The University should develop updated policies and procedures outlining the proper process for preparing monthly and year-end cash reconciliations. These policies and procedures should emphasize the importance of posting and clearing reconciling items on a monthly basis.

VCU Response

The University identified the timeliness of reconciliations as a problem and established a new Assistant Controller position to strengthen staffing in this area. The reconciliation process has been under review since filling this position in November 2003. Procedures have been reviewed and changes are being instituted to ensure that all reconciling items are resolved on a timely basis. All old items on the cash reconciliation will be removed no later than June 30, 2005.