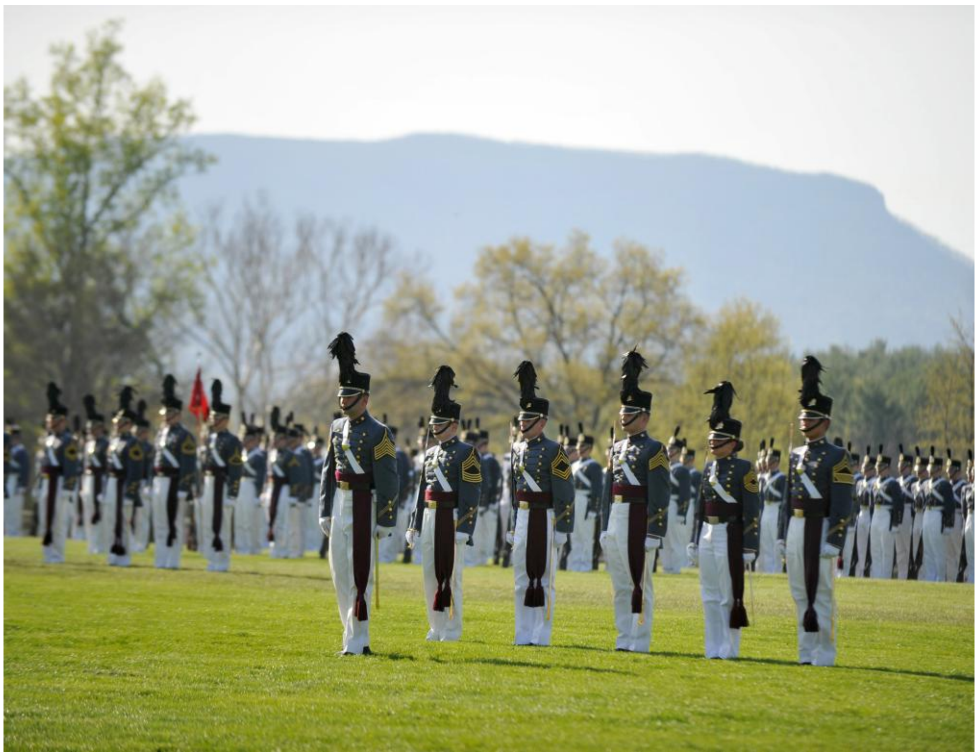
Virginia Military Institute



Financial Statements
For the year ended 30 June 2008

- T A B L E O F C O N T E N T S -

Overview

Virginia Military Institute (VMI) is pleased to present its financial statements for the fiscal year ended 30 June 2008, along with the financial statements of its affiliates as required under Governmental Accounting Standards Board Statement 39. This management discussion and analysis is designed to facilitate the reader's understanding of the accompanying financial statements and to provide an objective, easily readable analysis of the Institute's financial activities based on currently known facts, decisions and conditions. This discussion focuses primarily on VMI's fiscal year 2008 and includes highly summarized data that should be read in conjunction with the accompanying financial statements, notes to the financial statements, and other supplementary information.

VMI's financial statements are prepared in accordance with Governmental Accounting Standards Board (GASB) standards and include three basic statements: the Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; and the Statement of Cash Flows. The affiliates' financial statements are prepared in accordance with Financial Accounting Standards Board (FASB) standards and include the Statement of Financial Condition and the Statement of Activities. The following analysis discusses elements from VMI's statements and provides an overview of the Institute's activities. It also includes a separate section that addresses the financial statements of VMI's affiliates.

Financial Highlights

The financial position of the Institute improved in FY 2008 as net assets increased $13 million after excluding the effect of an extraordinary loss of $37.1 million that was recognized due to a change in the funding source for one of VMI's capital projects. The loss resulted when the State converted funding for VMI's Barracks Expansion and Renovation capital project from general funds to Virginia College Building Authority (VCBA) 21st Century bond proceeds. VMI recognized as revenue in FY 2007 the full amount of State general funds appropriated for this project, but the change to bond financing in FY 2008 requires that this funding be recognized as revenue only as capital project expenditures are incurred or obligated for the project. This change resulted in a loss for accounting purposes, but it does not result in any loss of funding for the project. VMI's net assets (the residual interest in assets after liabilities are deducted) to include this net loss totaled $198.8 million as of 30 June 2008 for a decrease of $24 million from 30 June 2007.

State appropriations for operations totaled $14.6 million in FY 2008 for an increase of $1.0 million or 7.4% more than the previous fiscal year. This increase is net of a $1.0 million State general fund reduction that was ordered by the Governor in October 2007 due to a shortfall in State revenues.

VMI incurred a net investment loss of $.8 million for FY 2008 compared to a net gain of $3.6 million in FY 2007 as a result primarily of a downturn in the stock market.

VMI continued to make substantial progress on three major capital projects during FY 2008 consisting of the expansion and renovation of the Barracks ($63 million), the expansion and renovation of Kilbourne Hall ($24 million), and the construction of the new Center for Leadership and Ethics ($22 million). Kilbourne Hall and the Center for Leadership and Ethics are scheduled to be completed in FY 2009 and the Barracks is scheduled for completion in fall 2010. VMI also completed the North Institute Hill Parking project ($2 million) in FY 2008.

Statement of Net Assets

The Statement of Net Assets presents the financial position of the Institute at the end of the fiscal year and includes all assets and liabilities of the Institute. The difference between total assets and total liabilities—net assets—is one indicator of the current financial condition of the Institute, while the change in net assets is an indicator of whether the overall financial condition has improved or worsened during the year. Readers of the

Statement of Net Assets should be able to determine the assets available to continue the Institute's operations. They should also be able to determine how much the Institute owes vendors, creditors, and others.

Net Assets are divided into three major categories. The first category, "Invested in capital assets, net of related debt," provides the Institute's equity in property, plant, and equipment. The next category is "Restricted" net assets which comprise two subcategories, expendable and nonexpendable. Expendable restricted resources are available for expenditure by the Institute in accordance with stipulation of donors and/or other entities that have placed time or purpose restrictions on the use of the assets. Nonexpendable restricted resources typically represent the corpus of endowments and are available only for investment purposes. The final category is "Unrestricted" net assets which are available for any lawful purpose of the Institute.

Statement of Net Assets

	30 June 2008	30 June 2007	Variance	
Assets:				
Current assets	$ 24,298,428	$ 15,957,175	$ 8,341,253	52.3%
Capital assets, net	185,635,263	150,175,297	35,459,966	23.6%
Other noncurrent assets	22,906,694	86,616,185	(63,709,491)	-73.6%
Total assets	$ 232,840,385	$ 252,748,657	$ (19,908,272)	-7.9%
Liabilities:				
Current liabilities	$ 15,179,674	$ 11,179,418	$ 4,000,256	35.8%
Noncurrent liabilities	18,833,300	18,712,152	121,148	0.6%
Total liabilities	$ 34,012,974	$ 29,891,570	$ 4,121,404	13.8%
Net Assets:				
Invested in capital assets, net of related debt	$ 170,644,678	$ 134,273,630	$ 36,371,048	27.1%
Restricted - expendable	17,565,381	75,974,556	(58,409,175)	-76.9%
Restricted - nonexpendable	1,265,690	4,267,843	(3,002,153)	-70.3%
Unrestricted	9,351,662	8,341,058	1,010,604	12.1%
Total net assets	$ 198,827,411	$ 222,857,087	$ (24,029,676)	-10.8%

VMI's current assets as of 30 June 2008 increased by $8.3 million or 52.3% over 30 June 2007. Cash and cash equivalents increased by $3.4 million and reflect the conversion to cash of $2.8 million of endowment assets designated for the Center for Leadership and Ethics capital project. Receivables from the Commonwealth also increased by $3.6 million and reflect amounts to be reimbursed by the State for expenditures and obligations on bond-funded capital projects. Current assets also increased due to a $1.1 million receivable from the VMI Foundation for support of operations.

Capital assets, net of depreciation, increased by $35.5 million or 23.6% to $185.6 million. This entire increase is attributable to amounts spent during FY 2008 on VMI's three major ongoing capital projects.

Other noncurrent assets decreased by $63.7 million to $22.9 million. This decrease primarily reflects a reduction in appropriations available from the State related to the $37.1 million extraordinary loss explained above and also to appropriations received during FY 2008 for other capital projects. The decrease also reflects a decrease in cash and investments with trustees related to the conversion of $2.8 million of endowment assets for the Center for Leadership and Ethics capital project and to a $1.6 million loss on our investments for the fiscal year.

Current liabilities increased 35.8% or $4 million over the previous year to $15.2 million and primarily reflect an increase in amounts payable to the contractor for the Barracks Expansion and Renovation capital project.

Net assets decreased by $24 million from the previous fiscal year to $198.8 million. As previously explained, net assets actually increased by $13 million or 5.8% over the previous year once we exclude the impact of the extraordinary loss resulting from the change in funding sources for the Barracks Expansion and Renovation capital project.

Statement of Revenues, Expenses, and Changes in Net Assets

Changes in the total net assets as presented on the Statement of Net Assets are based on the activity presented in the Statement of Revenues, Expenses, and Changes in Net Assets. The purpose of this statement is to present the Institute's operating and nonoperating revenues recognized and expenses paid and any other revenues, expenses, gains, and losses received or incurred by the Institute.

Operating revenues are generally recognized when goods and services are provided to cadets and other constituencies of the Institute. Operating expenses are the cost incurred to acquire or produce the goods and services provided and to carry out the Institute's programs and activities.

Nonoperating revenues generally represent income and support for which goods and services are generally not provided. For example, it includes State appropriations for VMI's Educational and General and Unique Military Activities Programs for which goods and services are not directly provided to the State by VMI.

Statement of Revenues, Expenses, and Changes in Net Assets

	30 June 2008	30 June 2007	Variance	
Operating revenues:				
Tuition and fees	$ 12,718,166	$ 12,031,383	$ 686,783	5.7%
Grants and contracts	297,022	947,051	(650,029)	-68.6%
Auxiliary enterprises	11,050,124	10,653,102	397,022	3.7%
Unique military activities	1,614,686	1,482,892	131,794	8.9%
Other sources	1,153,188	1,150,297	2,891	0.3%
Total operating revenues	26,833,186	26,264,725	568,461	2.2%
Operating expenses:				
Educational and general	40,828,927	37,812,377	3,016,550	8.0%
Auxiliary enterprises	$ 16,582,169	$ 16,757,487	(175,318)	-1.0%
Unique military activity	5,848,168	4,840,824	1,007,344	20.8%
Loan cancellations and write-offs	-	17,245	(17,245)	-
Total expenses	63,259,264	59,427,933	3,831,331	6.4%
Operating loss	(36,426,078)	(33,163,208)	(3,262,870)	9.8%

Nonoperating revenues (expenses):				
State appropriations	14,562,865	13,565,769	997,096	7.4%
Gifts and contributions	15,654,780	14,862,389	792,391	5.3%
Investments	(763,176)	3,556,303	(4,319,479)	-121.5%
Other	(215,916)	(1,201,408)	985,492	-82.0%
Net nonoperating revenues	29,238,553	30,783,053	(1,544,500)	-5.0%
Loss before other revenues	(7,187,525)	(2,380,155)	(4,807,370)	202.0%
Other revenues/extraordinary item	(16,842,151)	98,346,204	(115,188,355)	-117.1%
Increase (decrease) in net assets	(24,029,676)	95,966,049	(119,995,725)	-125.0%
Net assets - beginning of year	222,857,087	126,891,038	95,966,049	75.6%
Net assets - end of year	$198,827,411	$222,857,087	$ (24,029,676)	-10.8%

Operating revenues increased by 2.2% or $.6 million to $26.8 million while operating expenses increased by 6.5% or $3.8 million to $63.3 million. Nearly half of the increase in operating expenses is attributed to non-capitalizable costs within capital projects that were classified as operation and maintenance of physical plant current year expenses. An additional $1 million of expenses relate to the Unique Military Activities Program consisting of cadet uniform replacement costs (converting from the Battle Dress Uniform or BDU to the Army Combat Uniform or ACU) and increases in indirect costs payable to the Educational and General Program.

Non-operating revenues total $29.2 million for a decrease of $1.5 million or 5%. This decrease is attributed to a loss on investments for FY 2008 which was offset by some increase in state appropriations and private gifts.

Other revenues and extraordinary items decreased by $115.2 million from $98.3 million in FY 2007 to a loss of $16.8 million in FY 2008. For FY 2007, VMI received $65.8 million in State appropriations for capital projects including $60.8 million for the Barracks Expansion and Renovation capital project. In FY 2008, VMI received only $2.1 million for capital projects. The State also changed the funding source for the Barracks capital project from general funds to VCBA bond funds in FY 2008 that resulted in a $37.1 million extraordinary loss that was required to be recognized for accounting purposes. VMI also received $14.4 million less in FY 2008 from private gifts and State contributions for capital projects due to the completion of Athletic facilities renovations and Mallory Hall renovations.

<u>Statement of Cash Flows</u>

This statement presents detailed information about the Institute’s cash activity during the year. Cash flows from operating activities will always differ from the operating loss on the Statement of Revenues, Expenses and Changes in Net Assets (SRECNA). The SRECNA is prepared on the accrual basis of accounting and includes noncash items such as accounts receivable and accrued liabilities as well as such expenses as depreciation, whereas the Statement of Cash Flows presents cash inflows and outflows without regard to accrual items. The Statement of Cash Flows helps the reader assess the Institute’s ability to generate cash flows sufficient to meet its obligations. It is divided into five parts: operating activities, noncapital financing activities, investing activities, capital and related financing activities, and reconciliation of the net cash used, to the operating income or loss reflected on the SRECNA.

Statement of Cash Flows

	30 June 2008	30 June 2007	Variance	
Net cash used by operating activities	$ (30,805,559)	$ (27,216,018)	$ (3,589,541)	13.2%
Net cash provided by noncapital financing activities	29,148,587	28,458,918	689,669	2.4%
Net cash provided by capital and related financing activities	766,526	(8,970,060)	9,736,586	-108.5%
Net cash provided by investing activities	4,253,301	1,488,158	2,765,143	185.8%
Net increase (decrease) in cash	3,362,855	(6,239,002)	9,601,857	-153.9%
Cash - beginning of year, as restated	9,619,840	15,858,844	(6,239,004)	-39.3%
Cash - end of year	$ 12,982,695	$ 9,619,842	$ 3,362,853	35.0%

Cash provided and/or (used) by operating activities will always result in a net use for the Institute because all state appropriations and private gifts are treated as cash sources for noncapital or capital financing activities rather than sources for operating activities. Tuition and fees ($12.7 million) and auxiliary enterprise revenues ($11.2 million) represent the largest sources of operating cash, while compensation and benefits ($34.9 million) and payments for supplies and services ($22 million) are the most significant uses of operating cash.

Net cash provided by noncapital financing activities consists largely of State appropriations ($14.6 million) and private fund support ($14.3 million) of operations.

Net cash provided by capital and related financing activities consists primarily of state appropriations ($23.9 million) and gifts and contributions from the VMI Development Board and the State ($14.6 million). The purchase and construction of capital assets ($36.3 million) and principal and interest paid on capital debt ($1.6 million) account for the largest uses of cash for capital and related financing activities.

The $4.3 million in net cash provided by investing activities primarily reflects spendable income from VMI's endowment assets that support various programs and activities, as well as the $2.8 million transfer of funds from the Gillis endowment to cash and cash equivalents for the Center for Leadership and Ethics capital project.

Capital Asset and Debt Administration

FY 2008 was the sixth year of implementing VMI's Vision 2039 master plan. Vision 2039 is a leadership plan rather than a construction plan; however, construction of new facilities and the renovations of older buildings on Post are essential components of Vision 2039. During the year, planning and/or renovation and construction continued on a number of academic as well as other mission essential facilities: Kilbourne Hall, Center for Leadership and Ethics, and the Barracks Expansion and Renovation.

The Kilbourne Hall project consists of three components: the construction of a new Physical Plant facility; the renovation and expansion of Kilbourne Hall and the renovation of the old Buildings and Grounds facility; and improvements to storm water lines along Main Street (this storm water project also included additional funding of $1.3 million from a separate storm water project). The new Physical Plant facility was completed in September 2006 and the storm water project was completed in December 2006. The renovation of the old Buildings and Grounds facility and expansion of Kilbourne Hall was completed in March 2008 and the renovation of Kilbourne Hall is scheduled to be completed in October of 2008. The Kilbourne Hall project is funded predominantly by State general funds and some support from private funds.

The Center for Leadership and Ethics project began construction in October 2006 with completion scheduled for December 2008. This project is being financed with bonds issued through the Lexington Industrial Development Authority by the VMI Development Board, Inc.

The VMI Barracks Expansion and Renovation project has been on-going since the 2005 General Assembly appropriated $1.9 million of State funds to begin planning. The 2006 General Assembly appropriated $46.8 million for construction and the 2007 General Assembly appropriated supplemental funding of $14 million. During FY 2008, the State changed the funding source for this project from general funds to Virginia College Building Authority (VCBA) 21st Century bond proceeds. This project provides much needed repairs and upgrades to this historic facility and allows VMI to grow the Corps to 1,500 cadets beginning in Fall 2010. The Barracks expansion is scheduled to be completed in December 2008 and the renovation is scheduled for completion in August 2010.

Capital projects completed during FY 2008 consisted of the following: the renovation of Mallory Hall ($13.8 million), the renovations of Foster Football Stadium and the Gray-Minor Baseball Stadium ($19.6 million), and construction of the North Institute Hill Parking facility ($1.8 million). These projects were all financed with State funds or private funds resulting in no debt obligations for VMI.

The 2008 General Assembly appropriated Virginia College Building Authority (VCBA) bond financing for two new VMI capital projects beginning in FY 2009 consisting of $15.1 million for VMI's Military Leadership and Field Training Grounds project and $816,000 in planning funds to renovate the Science Building. It also appropriated $400,000 of auxiliary funds and $800,000 of private funds to renovate the VMI Commandant's Quarters. Two parking projects totaling $4.8 million were also appropriated for bond financing.

VMI has six capital projects totaling $115 million in progress or in the planning stages at the end of FY 2008. These projects are all financed with State funds or private funds from VMI's alumni agencies resulting in no debt obligations for VMI. Since VMI began its Vision 2039 capital program, it has incurred debt on only the Jackson Memorial Hall, the Cocke Hall Annex, and the Crozet Hall capital projects. The debt on these projects totals approximately $14.9 million with annual debt service payments of $1.3 million, most of which is being funded by the VMI Foundation and VMI Development Board. VMI's Board of Visitors adopted debt guidelines in August 2005 to help ensure sound management and control of debt.

Affiliates' Financial Statements

VMI's affiliates consist of the VMI Alumni Agencies (VMIAA) and the VMI Research Laboratories, Inc. (VMIRL). The VMIAA is comprised of four separate entities: the VMI Alumni Association, the VMI Foundation, Inc., the VMI Development Board, Inc., and the VMI Keydet Club, Inc. These entities share a common purpose of raising funds, investing funds, and performing other activities in support of VMI, and accordingly, present their financial statements on a combined basis. The VMIRL exists to administer grant and contract research, symposia, and other educational programs at VMI.

Total net assets of the VMIAA and the VMIRL amounted to $307.1 million and $.4 million, respectively, as of 30 June 2008 as compared to $348.7 million and $.3 million as of 30 June 2007. VMIAA net assets consist of $26.4 million in unrestricted net assets and $280.7 million in temporarily and permanently restricted net assets. VMIAA revenues totaled $24.1 million for FY 2008 and $24.3 million for FY 2007. The amount the VMIAA remitted directly to or on behalf of VMI for FY 2008 was $31.6 million compared to $39.1 million for FY 2007, a 19.2% decrease. This $7.5 million decrease is attributed to a reduction in funding for capital projects due to the completion of the Foster Football Stadium and Gray-Minor Baseball Stadium.

Economic Outlook

State appropriations for operations totaled $14.6 million in FY 2008 and $13.6 million in FY 2007 for an increase of $1.0 million or 7.4%. State appropriations represented 25.7% of VMI's total revenue and support for operations in FY 2008 compared to 23.3% in FY 2007. State appropriations for FY 2008 were reduced approximately $902,000 by the Governor in October 2007 due to a shortfall in State general fund revenues resulting from a sluggish economy. In September 2008, the Governor directed all agencies and institutions to submit plans by 26 September 2008 for additional State budget reductions of five, ten, and fifteen percent to be effective for FY 2009 and FY 2010. VMI's plans reflect State general fund reductions of $701,895, $1,403,789, and $2,105,684, respectively, and consist primarily of deferral of discretionary expenses and reduction in personnel costs to be achieved through vacancy and turnover savings and curtailment of wage employment. The actual reduction in State appropriations is expected to be announced in mid-October 2008 after completion of an updated State revenue forecast and may be revised in December 2008 when the Governor presents his proposed amendments to the 2008-2010 State Budget to the General Assembly money committees.

Gifts and contributions in support of operations totaled $15.7 million in FY 2008 and $14.9 million in FY 2007 for an increase of $0.8 million or 5.3%. This support represented 27.6% of VMI's total revenues and support for operations in FY 2008 compared to 25.5% in FY 2007. Gifts and contributions consist primarily of donations and endowment income from VMI's alumni agencies. This support is projected to increase approximately 9% in FY 2009, but will possibly decrease in FY 2010 due to the effects of the drop in the stock market resulting from the continuing sluggish national economy.

State funding for capital projects totaled $6.0 million in FY 2008 and $76.4 million in FY 2007 and consists of State general funds and bond financing. State funding for FY 2009 is projected to approximate $36.4 million. Private funding for capital projects totaled $14.3 million in FY 2008 and $21.9 million in FY 2007 and consisted primarily of bond financing. Private funding for FY 2009 is projected to total $1.6 million.

VMI increased tuition and fees in FY 2009 by 5.2% for in-state cadets and 5.9% for out-of-state cadets. VMI estimates that increases for FY 2010 will be greater due to additional State general fund reductions and increasing operating costs from rising energy costs and program enhancements mandated by accreditation standards.

VMI enrolled 1,456 cadets in fall 2008 (FY 2009) and 1,408 cadets in fall 2007 (FY 2008) for an increase of 48 cadets or 3.4%. The enrollment consisted of 59.6% in-state cadets in fall 2008 compared to 58.5% in fall 2007. VMI is planning for approximately 1,470 cadets in fall 2009 consisting of 59.0% in-state cadets and is projecting approximately 1,500 cadets by fall 2011 as the completion of the Barracks expansion and renovation capital project allows for a larger Corps. VMI's targeted enrollment mix as approved by the State calls for 55% in-state cadets and 45% out-of-state cadets.

VMI's executive management believes that the Institute is well positioned to continue to provide excellent programs and services to its cadets as it maintains a clear educational focus and a well-established niche in the higher education marketplace. VMI continues to be nationally recognized especially for its engineering programs. Reductions in State support and possibly in private support will impact operations and programs for the near term, but VMI plans to keep its tuition and fees competitive and continue to offer attractive financial assistance packages that will help to sustain and to grow the Corps over the next few years. Growth in the number of cadets who receive Reserve Officers Training Corps (ROTC) scholarships is also helping to bolster the enrollment of out-of-state cadets. A growing enrollment that includes planned increases in the proportion of out-of-state cadets will mitigate some of the impact of reduced State and private funding. VMI will also continue to improve the efficiency and the effectiveness of all its operations and programs through regular assessments in accordance with the mandates of its accrediting body and the State's Agency Risk Management and Internal Control Systems policies.

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FINANCIAL STATEMENTS

VIRGINIA MILITARY INSTITUTE
Statement of Net Assets
As of 30 June 2008

ASSETS	
Current assets	
Cash and cash equivalents (Note 2)	$ 12,029,595
Cash equivalent held by Treasurer of Virginia (Note 2)	359,604
Collateral held for securities lending (Note 2)	1,354,634
Accounts receivable, *Net of allowance for doubtful accounts of $50,374* (Note 3)	1,862,960
Due from the Commonwealth	3,771,588
Prepaid expenditures	842,144
Inventory (Note 4)	3,991,575
Loans receivable	86,328
Total current assets	24,298,428
Noncurrent assets	
Cash and cash equivalents (Note 2)	953,100
Cash equivalent held by Treasurer of Virginia (Note 2)	3,359
Investments held with trustees (Note 2)	15,554,476
Appropriations available\Due from Commonwealth	4,962,057
Accounts receivable (Note 3)	309,694
Loans receivable, *Net of allowance for doubtful accounts of $24,699*	1,124,008
Nondepreciable capital assets (Note 5)	62,822,968
Depreciable capital assets, *Net of accumulated depreciation of $73,486,906* (Note 5)	122,812,295
Total noncurrent assets	208,541,957
Total assets	232,840,385
LIABILITIES	
Current liabilities	
Accounts payable and accrued expenses (Note 6)	10,189,855
Unearned revenue	1,072,652
Obligations under securities lending	1,714,238
Deposits held for others	402,146
Long-term liabilities-current portion: (Note 7)	
Compensated absences	895,609
Bonds payable (Note 8)	400,000
Notes payable (Note 8)	465,000
Capital lease payable (Note 8)	6,001
Installment purchase obligations (Note 8)	34,173
Total current liabilities	15,179,674
Noncurrent liabilities	
Accrued liabilities (Note 6)	516,758
Federal loan program contributions refundable	1,290,773
Retainage payable (Note 10)	2,531,596
Long-term liabilities-noncurrent portion: (Note 7)	
Compensated absences	405,402
Bonds payable (Note 8)	10,269,673
Notes payable (Note 8)	3,755,098
Capital lease payable (Note 8)	14,204
Installment purchase obligations (Note 8)	49,796
Total noncurrent liabilities	18,833,300
Total liabilities	34,012,974
NET ASSETS	
Invested in capital assets, net of related debt	170,644,678
Restricted-nonexpendable	
Endowment	1,265,690
Restricted-expendable	
Scholarships and other	5,527,159
Loan funds	562,950
Quasi-endowment-restricted	11,147,732
Capital projects	327,540
Unrestricted	9,351,662
Total net assets	198,827,411
Total liabilities and net assets	$ 232,840,385

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

COMBINED STATEMENT OF FINANCIAL POSITION
Component Units of Virginia Military Institute
As of 30 June 2008

ASSETS	
Current Assets:	
Cash and cash equivalents	$ 16,263,599
Contributions receivable (Note 19)	4,548,388
Accounts receivable	295,317
Other	400,576
Total current assets	21,507,880
Noncurrent Assets:	
Contributions Receivable (Note 19)	8,455,892
Notes receivable	5,799
Investments held by trustees (Note 19)	307,230,564
Investments, other (Note 19)	17,540,042
Investment securities	110,586
Funds restricted for affiliate	700,102
Cash surrender of life insurance	4,744,377
Property and equipment, net of accumulated depreciation	57,152
Total noncurrent assets	338,844,514
Total assets	360,352,394
LIABILITIES	
Current Liabilities:	
Accounts payable and accrued expenses	1,268,534
Long-term liabilities-current portion:	
Trust and annuity obligations	782,569
Total current liabilities	2,051,103
Noncurrent Liabilities:	
Unearned revenue	18,190
Other liabilities	344,709
Long-term liabilities-noncurrent portion:	
Bonds payable (Note 19)	45,691,022
Trust and annuity obligations	4,745,016
Total noncurrent liabilities	50,798,937
Total liabilities	52,850,040
NET ASSETS	
Unrestricted	26,785,540
Temporarily restricted	176,322,129
Permanently restricted	104,394,685
Total net assets	307,502,354
Total liabilities and net assets	$ 360,352,394

VIRGINIA MILITARY INSTITUTE
Statement of Revenues, Expenses, and Changes in Net Assets
For the Year Ended 30 June 2008

Operating revenues:	
Tuition and fees, *Net of scholarships allowances of $3,840,448*	$ 12,718,166
Federal grants and contracts	266,189
State and private grants and contracts	30,833
Sales and services of educational departments	133,828
Auxiliary enterprise, *Net of scholarship allowances of $3,161,221*	11,050,124
Unique military activities, *Net of scholarships allowances of $503,604*	1,614,686
Other sources:	
Museum programs	530,156
Rents and commissions	222,963
Miscellaneous	266,241
Total operating revenues	26,833,186
Operating expenses:	
Educational and general	
Instruction	17,308,174
Research	355,302
Public service	1,388,747
Academic support	5,585,397
Student services	3,641,176
Institutional support	4,594,202
Operation and maintenance of physical plant	7,062,082
Scholarships and related expense	893,847
Auxiliary enterprises	16,582,169
Unique military activities	5,848,168
Total operating expenses (Note 11)	63,259,264
Net operating loss	(36,426,078)
Nonoperating revenues/(expenses):	
State appropriations (Note 12)	14,562,865
Gifts and contributions	15,654,780
Federal student financial aid (PELL)	472,845
Investment income (loss)	(763,176)
Interest on capital asset - related debt	(661,321)
Loss on disposal of plant assets	(27,440)
Net nonoperating revenues	29,238,553
Loss before other revenues and extraordinary items	(7,187,525)
Other revenues and extraordinary items:	
State appropriations-capital	2,099,738
Grants and contributions-capital	18,109,644
Investment income-capital	3,441
Extraordinary loss-reduction of state appropriations-capital (Note 18)	(37,054,974)
Total other revenues and extraordinary items	(16,842,151)
Increase/(Decrease) in net assets	(24,029,676)
Net assets beginning of the year	222,857,087
Net assets end of year	$ 198,827,411

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

COMBINED STATEMENT OF ACTIVITIES
Component Units of Virginia Military Institute
For the Year Ended 30 June 2008

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
REVENUES				
Amounts raised on behalf of VMI	$ 8,210,407	$ 6,933,063	$ 4,444,038	$ 19,587,508
Grants, contributions and contracts	545,187	20,000	-	565,187
Event sponsorships, registrations and fees	487,486	-	-	487,486
Investment income	5,025,977	422	-	5,026,399
Actuarial gain/(loss) on trust and annuity obligations	(325,464)	350,401	(47,729)	(22,792)
Unrealized loss on swap contract	-	(503,186)	-	(503,186)
Administrative fees	36,386	-	-	36,386
Other Income	120,391	-	-	120,391
Net assets released from restrictions and reclassifications	7,902,653	(7,902,653)	-	-
Total revenues	22,003,023	(1,101,953)	4,396,309	25,297,379
EXPENSES				
Amounts remitted directly to or on behalf of VMI:				
Unrestricted	22,818,235	-	-	22,818,235
Designated	8,752,408	-	-	8,752,408
Cost of operations	5,665,093	-	-	5,665,093
Conference, research and education	963,206	-	-	963,206
Total expenses	38,198,942	-	-	38,198,942
Change in net assets before net realized and unrealized gain/(loss) on investments	(16,195,919)	(1,101,953)	4,396,309	(12,901,563)
NET REALIZED AND UNREALIZED GAINS/(LOSS) ON INVESTMENTS	(8,366,727)	(20,213,001)	-	(28,579,728)
Change in net assets	(24,562,646)	(21,314,954)	4,396,309	(41,481,291)
NET ASSETS				
Beginning	51,348,186	197,637,083	99,998,376	348,983,645
Ending	$ 26,785,540	$ 176,322,129	$ 104,394,685	$ 307,502,354

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

VIRGINIA MILITARY INSTITUTE

Statement of Cash Flows
For the Year Ended 30 June 2008

Cash provided/(used) by operating activities:	
Tuition and fees	$ 12,718,904
Federal grants and contracts	287,764
State and private grants and contracts	30,833
Sales and services-educational and general	135,604
Auxiliary charges	11,184,445
Unique military activity charges	1,609,922
Other operating receipts	982,055
Payments to employees for salaries and benefits	(34,921,371)
Payments for supplies and services	(21,953,155)
Payments for scholarships and fellowships	(893,847)
Loans issued to students	(258,496)
Collections of loans from students	271,783
Net cash provided/(used) by operating activities	(30,805,559)
Cash provided/(used) by noncapital financing activities:	
State appropriations	14,562,865
Nonoperating grants and contracts	472,846
Gifts and contributions for other than capital purposes	14,289,513
Federal Direct Lending Program-receipts	3,372,228
Federal Direct Lending Program-disbursements	(3,372,228)
Agency receipts	3,507,961
Agency disbursements	(3,684,598)
Net cash provided/(used) by noncapital financing activities	29,148,587
Cash provided/(used) by capital and related financing activities:	
Capital appropriations	23,939,971
Capital gifts and contributions	14,638,400
Proceeds from sale of capital assets	37,093
Purchase and construction of capital assets	(36,287,745)
Principal paid on capital debt, leases and installments	(866,767)
Interest paid on capital debt, leases and installments	(698,118)
Investment income-capital	3,692
Net cash provided/(used) by capital and relating financing activities	766,526
Cash provided/(used) by investing activities:	
Interest on investments	341,656
Investment/Endowment income	372,882
Sale of investments	3,561,263
Purchase of investments	(22,500)
Net cash provided/(used) by investing activities	4,253,301
Net increase/(decrease) in cash	3,362,855
Cash-beginning of year, as restated (Note 1)	9,619,840
Cash-end of year	$ 12,982,695

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

VIRGINIA MILITARY INSTITUTE
Statement of Cash Flows
For the Year Ended 30 June 2008

Reconciliation of net operating expenses to net cash used by operating activities:

Net operating expenses	$	(36,426,078)
Adjustments to reconcile net operating expenses to cash used by operating activities:		
Depreciation expense		5,314,267
Changes in assets and liabilities:		
Accounts receivable		16,152
Inventories		(823)
Prepaid expenditures		(68,324)
Due from Commonwealth		(82,059)
Loans receivable		16,203
Notes receivable		210,000
Accounts payable and accrued liabilities		112,458
Deposits held in custody for others-security deposits		14,458
Unearned revenue		145,574
Compensated absences		(54,471)
Federal loan program contributions refundable		(2,916)
Net cash used in operating activities	$	(30,805,559)

Noncash investing, noncapital financing, and capital related financing transactions:

Capital assets acquired by donation		1,234,398
Change in fair value of investments recognized as a component of investment income/(loss)		(2,222,465)
	$	(988,067)

Reconciliation of cash and cash equivalents to the Statement of Net Assets:

Cash and cash equivalents classified as current assets		12,029,595
Cash and cash equivalents classified as noncurrent assets		953,100
	$	12,982,695

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

- NOTES TO FINANCIAL STATEMENTS -

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of Virginia Military Institute (VMI) have been prepared in accordance with generally accepted accounting principles for colleges and universities. The significant accounting policies followed by the Institute are as follows:

A. Reporting Entity

The Virginia Military Institute believes that the measure of a college lies in the quality and performance of its graduates and their contributions to society. Therefore, it is the mission of the Virginia Military Institute to produce educated, honorable men and women prepared for the varied work of civil life, imbued with love of learning, confident in the functions and attitudes of leadership, possessing a high sense of public service, advocates of the American Democracy and free enterprise system, and ready as citizen-soldiers to defend their country in time of national peril.

To accomplish this result, Virginia Military Institute shall provide to qualified young men and women undergraduate education of highest quality – embracing engineering, science, and the arts – conducted in, and facilitated by, the unique VMI system of military discipline.

Virginia Military Institute is part of the Commonwealth of Virginia's statewide system of public higher education. The Board of Visitors, appointed by the Governor, is responsible for overseeing the Institute's governance. A separate report is prepared for the Commonwealth of Virginia which includes all agencies, boards, commissions, and authorities over which the Commonwealth exercises or has the ability to exercise oversight authority. The Institute is a component unit of the Commonwealth of Virginia and is included in the general purpose financial statements of the Commonwealth.

The Governmental Accounting Standards Board (GASB) Statement 39, *Determining Whether Certain Organizations Are Component Units*, became effective for the fiscal year ended 30 June 2004. GASB Statement 39 provides guidance to determine whether certain organizations for which the Institute is not financially accountable should be reported as component units. Generally, it requires reporting as a component unit, an organization that raises and holds economic resources for the direct benefit of the Institute.

The VMI Alumni Agencies is a legally separate, tax-exempt entity whose purpose is to organize the alumni of the Institute and to aid in the promotion of its welfare and the successful prosecution of its educational purposes. It accomplishes this through fund-raising to supplement the support VMI receives from the Commonwealth of Virginia and the tuition and fees charged to cadets. Because the VMI Alumni Agencies' resources are held almost entirely for the benefit of the Institute and these resources are considered significant to the Institute, we have determined that the Alumni Agencies should be included as a component unit.

The VMI Research Laboratories (VMIRL) is a legally separate, tax-exempt entity whose purpose is to administer contract and grant research at the Institute. Because of the VMIRL's close relationship to the Institute, we believe in our professional judgment, it should be included as a component unit in our financial statements. Both the VMI Alumni Agencies and the VMIRL have been discretely presented in these statements.

Because the VMI Alumni Agencies and the VMIRL report under a different reporting model, the Financial Accounting Standards Board (FASB) standards, the VMI Board of Visitors and the administration of the Institute believe the Institute's financial statements should be presented on a page separate from the Institute's component units as allowed by GASB Statement 39. Separate financial statements for the VMI Alumni Agencies may be obtained by writing the Chief Financial Officer, VMI Foundation, Inc., P.O. Box 932, Lexington, Virginia 24450. Separate financial statements for the VMI Research Laboratories, Inc., may be obtained by writing the Treasurer, VMI Research Laboratories, Inc., Virginia Military Institute, Lexington, Virginia 24450.

B. Financial Statement Presentation

The Institute's accounting policies conform with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (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 Procedures issued on or before 30 November 1989, unless those pronouncements conflict with or contradict GASB pronouncements. The financial statements have been prepared in accordance with GASB Statement 34, *Basic Financial Statements and Management Discussion and Analysis for State and Local Governments*, and GASB Statement 35, *Basic Financial Statements and Management's Discussion and Analysis for Public Colleges and Universities.*

The VMI Alumni Agencies and the VMI Research Laboratories, Inc. are private, nonprofit organizations that report under FASB standards including FASB Statement 117, *Financial Reporting for Not-for-Profit Organizations*. As such, certain revenue recognition criteria and presentation features are different from GASB revenue recognition criteria and presentation features. No modifications have been made to the VMI Alumni Agencies' or the VMI Research Laboratories' financial information in the Institute's financial report for these differences.

C. Basis of Accounting

For financial statement purposes, the Institute is considered a special-purpose government engaged only in business-type activities. Accordingly, the Institute's financial statements have been presented using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. All significant intra-agency transactions have been eliminated.

D. Investments

In accordance with GASB Statement 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, purchased investments, interest-bearing temporary investments classified with cash, and investments received as gifts are recorded at fair value. All investment income, including changes in the fair value of investments (unrealized gains and losses), is reported as nonoperating revenue in the Statement of Revenues, Expenses, and Changes in Net Assets.

E. Capital Assets

Capital assets include land, buildings and other improvements, library materials, equipment and infrastructure assets such as sidewalks, steam tunnels, and electrical and computer network cabling systems. Capital assets are generally defined by the Institute as assets with an initial cost of $5,000 or more and an estimated useful life in excess of two years. Buildings and equipment are stated at appraised value or actual cost where determinable. Land is stated at cost. Library materials are valued using published average prices for library acquisitions. Expenses for major capital assets and improvements are capitalized (construction in progress) as projects are constructed. Operating expenditures of $10,000 or greater for renewals and replacement are capitalized only to the extent that such expenditures represent long-term improvement to properties. Interest expense relating to construction is capitalized net of interest income earned on resources set aside for this purpose. The costs of normal maintenance and repairs that do not add to an asset's value or materially extend its useful life are not capitalized.

Depreciation is computed using the straight-line method over the estimated useful life of the asset. Useful lives by asset categories are listed below:

Buildings	50 years
Other improvements	10-30 years
Equipment	5-25 years
Library materials	10 years

The Institute does not capitalize works of art, historical treasures and similar assets. Such items are held for public exhibition, education or research in the furtherance of public service rather than financial gain. Institute collections may be sold but the proceeds must be used for the acquisition of similar type Institute collections. Exceptions to this requirement must be pre-approved by the Deputy Superintendent for Finance, Administration and Support.

F. Inventories

Inventory cost values for the museum, post hospital and physical plant are determined by using the weighted average method. The military store inventory is valued at cost using the first-in first-out method.

G. Unearned Revenue

Unearned revenue represents revenues collected but not earned as of 30 June 2008. This is primarily composed of revenue for student tuition and fees received in advance of the next semester or term.

H. Interest Capitalization

Interest expense incurred during the construction of capital assets is capitalized, if material, net of interest income earned on resources set aside for this purpose. The Institute incurred interest expense totaling $661,321 for the fiscal year ended 30 June 2008, of which none was capitalized as construction period interest.

I. Accrued Compensated Absences

Nonfaculty salaried employee's attendance and leave regulations make provisions for the granting of a specified number of days of leave with pay each year. Instructional personnel do not earn leave. The amount of leave earned but not taken as of 30 June 2008 is recorded as a liability on the Statement of Net Assets. The liability reflects all earned vacation, compensatory and overtime leave not taken as well as the amount payable under the Commonwealth of Virginia's sick leave payout policy upon termination which is the lesser of 25% of sick leave not taken or $5,000 per employee with five or more years of service. Also included is an estimation of sick leave for those employees who, while not currently vested, will probably attain the 5 years of service required to vest. The last element reflected in the liability is Social Security and Medicaid taxes to be paid by the Institute on all accrued compensated absences.

J. Federal Financial Assistance Programs

The Institute participates in federally funded Pell Grants, Supplemental Educational Opportunity Grants, Federal Work-Study and Perkins Loans programs. Federal programs are audited in accordance with the Single Audit Act Amendments of 1996, the Office of Management and Budget Revised Circular A-133, *Audit of States, Local Governments and Non-Profit Organizations,* and the Compliance Supplement.

K. 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.

The Institute's net assets are classified as follows:

Invested in capital assets, net of related debt: This represents the Institute's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of invested in capital assets, net of related debt.

Restricted net assets – nonexpendable: Nonexpendable restricted net assets consist of endowment funds in which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to the principal.

Restricted net assets – expendable: Restricted expendable net assets include resources in which the Institute is legally or contractually obligated to spend in accordance with restrictions imposed by external third parties.

Unrestricted net assets: Unrestricted net assets represent resources derived from student tuition and fees, state appropriations, and sales and services of educational departments and auxiliary enterprises. These resources are used for transactions relating to the educational and general operations of the Institute, and may be used at the discretion of the governing board to meet current expenses for any purpose. These resources also include auxiliary enterprises, which are substantially self-supporting activities that provide services for students, faculty and staff. Also included in unrestricted net assets are funds that have been set aside by the Board of Visitors as quasi-endowments. These funds are treated the same as true endowment funds; however, unlike true endowments they may be expended.

The Institute has no policy regarding flow assumption to determine which assets (restricted or unrestricted) are being used when both restricted and unrestricted assets are available for the same purpose. Our practice is to allow Department Heads to make this determination and they typically spend unrestricted assets prior to spending restricted resources.

L. Classification of Revenues

The Institute has classified its revenues as either operating or nonoperating revenues according to the following criteria:

Operating revenues: Operating revenues include activities that have the characteristics of exchange transactions, such as (1) student tuition and fees, net of scholarship discounts and allowances, (2) sales and services of auxiliary enterprises, net of scholarship discounts and allowances, (3) most federal, state and local grants and contracts, and (4) interest on student loans.

Nonoperating revenues: Nonoperating revenues include activities that have the characteristics of nonexchange transactions, such as gifts and contributions, 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, GASB Statement 33 *Accounting and Financial Reporting for Nonexchange Transactions,* and GASB Statement 34, such as state appropriations and investment income.

Scholarship Discounts and Allowances: Student tuition and fee revenues are reported net of scholarship discounts and allowances in the statements of revenues, expenses, and changes in net assets. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by the Institute, and the amount that is paid by students and/or third parties making payments on the students' behalf. Certain governmental grants, such as Pell grants, and other federal, state or nongovernmental programs, are recorded as either operating or nonoperating revenues in the Institute's financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees, the Institute has recorded a scholarship discount and allowance.

M. Reclassification

An adjustment to the beginning balance amount of cash and cash equivalents has been made on the Statement of Cash Flows. The prior year ending balance included funds for appropriations available for capital projects. Based on guidance from the Virginia Department of Accounts appropriations available amounts will now be reflected on a separate line item "Appropriation available/Due from Commonwealth" and will no longer be reflected as cash. The following adjustment has been made to the ending cash and cash equivalent balance for fiscal year 2007:

Cash and cash equivalents at 30 June 2007	$ 73,477,104
Reporting change Virginia Department of Accounts	(63,857,264)
Cash and cash equivalents, as restated – Statement of Cash Flows	$ 9,619,840

NOTE 2: CASH AND CASH EQUIVALENTS AND INVESTMENTS

The following information is provided with respect to the Institute's cash, cash equivalents, and investments as of 30 June 2008. The following risk disclosures are required by GASB Statement 40, Deposit and Investment Risk Disclosures.

Custodial credit risk (Category 3 deposits and investments) – The custodial risk for deposits is the risk that, in the event of a failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in possession of an outside party. The Institute had no category 3 deposits or investments for fiscal year 2008.

Credit risk – The risk that an issuer or other counterparty to an investment will not fulfill its obligations. GASB Statement 40 requires the disclosure of the credit quality ratings of all investments subject to credit risk.

Concentration of credit risk – The risk of loss attributed to the magnitude of a government's investment in a single issuer is referred to as a credit risk. GASB Statement 40 requires disclosure of any issuer with more than five percent of total investments.

Interest rate risk - This is the risk that interest rate changes will adversely affect the fair value of an investment. GASB Statement 40 requires disclosure of maturities for any investments subject to interest rate risk. The Institute does not have an interest rate risk policy.

Foreign currency risk – This risk refers to the possibility that changes in exchange rates will adversely affect the fair value of an investment or a deposit.

The Institute's credit risk, concentration of credit risk, interest rate risk, and foreign currency risk are described in the Investments Note below.

Cash and Cash Equivalents

Pursuant to Section 2.2-1800, et seq., Code of Virginia, all state funds of VMI are maintained by the Treasurer of Virginia, who is responsible for the collection, disbursement, custody, and investment of state funds. Cash deposits held by VMI are maintained in accounts that are collateralized in accordance with the Virginia Security for Public Deposits Act, Section 2.2-4400, et seq., Code of Virginia. In accordance with the GASB Statement 9 *Definition of Cash and Cash Equivalents*, cash represents cash with the Treasurer, cash on hand, and cash deposits including certificate of deposits, and temporary investments with original maturities of three months or less.

Cash and cash equivalents consist of the following balances as of 30 June 2008:

Cash with Treasurer of Virginia	$ 6,864,383
SunTrust NOW checking	6,082,242
State Non-Arbitrage Program (SNAP)*	2,959
Bank of New York Bond Fund Interest	400
Securities under securities lending	359,604
Petty cash	8,070
Wachovia Bank time deposit	28,000
Total cash and cash equivalents	$ 13,345,658

*Rated as 'AAAm' by Standard and Poor

Investments

Investments include endowment and similar funds pooled and invested with VMI affiliates and retirement fund investments for selected employees. It also includes VMI's allocated share of securities held for security lending transactions conducted by the Commonwealth. Investments consist of the following balances as of 30 June 2008:

Investments with the Treasurer of Virginia:	
Securities under Securities Lending	$ 1,354,634
Investments with Trustees:	
Investments pooled with VMI Affiliates	15,052,718
Mutual fund investments (retirement accounts)	501,758
Total with Trustees	15,554,476
Total investments	$ 16,909,110

VMI's endowment, loan and similar funds are pooled for investment purposes with the endowment funds of the VMI Alumni Agencies (the VMI Foundation, Inc., the VMI Development Board, Inc., the VMI Keydet Club, and the VMI Alumni Association) and the George C. Marshall Foundation. VMI owns units in the pooled fund that operates similar to a mutual fund. The Board of Trustees of the VMI Foundation, Inc. is responsible for the management of these endowment funds (the Fund) and has appointed an Investment Committee to supervise the Fund's assets. The Committee is responsible for setting and implementing the investment policies and guidelines adopted by the Committee. Authorized investments are set forth in the Uniform Management of Institutional Funds Act, Section 55-268 et seq. of the Code of Virginia and include cash equivalents, preferred and common stocks, bonds, and real estate.

The market value of the Fund as of 30 June 2008 was $330.1 million, of which, VMI owned $15.1 million or 4.57 percent of the Fund assets. The Fund held $43 million in debt securities with an average maturity of 7.48 years. The average quality rating was AA+ (Moodys). Bonds must be rated above investment grade by two of the following rating agencies: Moody's, Fitch Rating, and Standard and Poors at the time of purchase and cannot be more than 20 percent of the total assets invested in bonds (at market). No stock may be in excess of five percent of the equity portfolio at cost or ten percent at market. No more than 25 percent of the equity portfolio at market value may be invested in any one general industry as defined by the S&P 500 industry classifications. No more than three percent of the outstanding shares of any company may be owned in the equity portfolio. The Fund held $75.3 million in international equities denominated primarily in the Euro, the Pound, and the Yen. The custodians for the Fund are independently audited annually.

Securities Lending Transactions

Collateral held for securities lending and the securities lending transactions reported on the financial statements represent the Institute's allocated share of securities received for securities lending transactions held in the General Account of the Commonwealth. Information related to the credit risk of these investments and securities lending transactions held in the General Account is available on a statewide level in the Commonwealth of Virginia's *Comprehensive Annual Financial Report.* The Commonwealth's policy is to record unrealized gains and losses in the General Fund in the Commonwealth's basic financial statements. When gains or losses are realized, the actual gains and losses are recorded by the affected agencies.

Funds Held In Trust By Others

Assets of funds held by trustees for the benefit of the Institute are not reflected in the accompanying Statement of Net Assets. The Institute has irrevocable rights to all or a portion of the income of these funds. However, assets of the funds are not under the management discretion of the Institute according to the trust agreements. Income from funds held by trustees for the benefit of the Institute totaled $119,167 and is included in the endowment income.

NOTE 3: ACCOUNTS RECEIVABLE

Accounts receivable consisted of the following at 30 June 2008:

Current:		
Student tuition and fees	$	320,165
Other educational and general		30,118
Auxiliary enterprises		19,807
Unique military activity		8,989
Federal grants		2,547
State grants		725
Private gifts		1,115,269
Agency funds		267,438
Other operating		72,905
Retirement of indebtedness		75,371
	$	1,913,334
Less: Allowance for doubtful accounts		(50,374)
Total current accounts receivable, net	$	1,862,960
Noncurrent:		
Private gifts	$	250,000
Other operating		59,694
Total noncurrent accounts receivable	$	309,694
Total accounts receivable	$	2,172,654

NOTE 4: INVENTORIES

Inventories consisted of the following at 30 June 2008:

Physical Plant	$ 386,623
Military Store	3,446,777
Museums	141,313
VMI Hospital	16,862
Total	$ 3,991,575

NOTE 5: CAPITAL ASSETS

A summary of changes in the various capital asset categories is presented as follows:

	Beginning Balance 1 July 2007	Additions	Reductions	Ending Balance 30 June 2008
Nondepreciable capital assets:				
Land	$ 1,935,720	$ 587,756	$ -	$ 2,523,476
Construction in progress	35,977,086	40,102,927	(15,780,521)	60,299,492
Total nondepreciable capital assets	37,912,806	40,690,683	(15,780,521)	62,822,968
Depreciable capital assets:				
Buildings	146,542,371	12,765,990	-	159,308,361
Improvements other than buildings	11,501,118	2,183,473	(33,639)	13,650,952
Equipment	12,460,351	765,412	(618,477)	12,607,286
Library books	10,563,890	213,732	(45,020)	10,732,602
Total depreciable capital assets	181,067,730	15,928,607	(697,136)	196,299,201
Less accumulated depreciation for:				
Buildings	50,827,500	3,220,181	-	54,047,681
Improvements other than buildings	1,959,864	567,028	(33,639)	2,493,253
Equipment	7,040,700	1,230,156	(553,942)	7,716,914
Library books	8,977,175	296,903	(45,020)	9,229,058
Total accumulated depreciation	68,805,239	5,314,268	(632,601)	73,486,906
Depreciable capital assets	112,262,491	10,614,339	(64,535)	122,812,295
Total capital assets, net	$ 150,175,297	$ 51,305,022	$ (15,845,056)	$ 185,635,263

NOTE 6: ACCOUNTS PAYABLE AND ACCRUED EXPENSES

Accounts payable and accrued expenses consisted of the following at 30 June 2008:

Current liabilities:		
Employee salaries, wages and benefits payable	$	3,331,996
Vendors and supplies accounts payable		6,733,878
Accrued interest payable		101,941
Other accrued liabilities		22,040
Total current-accounts payable and accrued expenses	$	10,189,855

Noncurrent liabilities:		
Retirement annuities	$	501,758
Other		15,000
Total noncurrent-accrued liabilities	$	516,758

NOTE 7: LONG-TERM LIABILITIES SUMMARY

The Institute's long-term liabilities primarily consist of long-term debt (further described in Note 8) and accrued compensated absences. A summary of changes in long-term liabilities for the year ending 30 June 2008 is presented as follows:

	Beginning Balance 1 July 2007	Additions	Reductions	Ending Balance 30 June 2008	Current Portion 30 June 2008
Long-term debt:					
Bonds payable	$ 11,082,153	-	(412,480)	$ 10,669,673	$ 400,000
Notes payable	4,659,658	33,721	(473,281)	4,220,098	465,000
Capital leases	25,731	-	(5,526)	20,205	6,001
Installment purchases	106,409	18,800	(41,240)	83,969	34,173
Total long-term debt	$ 15,873,951	$ 52,521	$ (932,527)	$ 14,993,945	$ 905,174
Accrued compensated absences	1,355,482	975,118	(1,029,589)	1,301,011	895,609
Total long-term liabilities	$ 17,229,433	$ 1,027,639	$ (1,962,116)	$ 16,294,956	$ 1,800,783

NOTE 8: LONG-TERM INDEBTEDNESS DETAIL

Bonds payable:

In August 2004, pursuant to Section 9(c) of Article X of the Constitution of Virginia, $11,240,000 of revenue bonds, Series 2004A, were issued by the Department of Treasury for the Commonwealth of Virginia, on behalf of the Institute for renovation and expansion of Crozet Hall, the Institute dining facility, and parking. The bonds bear interest at an average coupon rate of 4.8% and are payable over 20 years through June 2025. Net proceeds after the cost of issuance total $11,889,591 and included a premium realized on the sale. The revenue bonds are secured by the net revenues of the facility which is comprised primarily of cadet fees.

Bonds Payable:	Interest Rates (%)	Maturity	Balance 30 June 2008
Crozet Hall, Series 2004A, issued $11,240,000	4.63 - 5.00	2025	$ 10,669,673

Notes payable:

Notes payable are debt obligations between the Virginia College Building Authority (VCBA) and the Institute. The VCBA issues bonds through the Pooled Bond Program and uses the proceeds to purchase debt obligations (notes) of the Institute. The Barracks Wiring and JM Hall Renovation notes are secured by funds paid by the VMI Foundation, Inc. on a year-to-year basis as a gift to the Institute. Should the gift be discontinued, repayment will be made from the general revenues of the Institute. The Cocke Hall Annex note will be paid from auxiliary reserve funds which consist predominantly of cadet fees.

Notes Payable:	Interest Rates (%)	Maturity	Balance 30 June 2008
Barracks Wiring, Series 1998A, issued $1,790,000	3.70 - 4.10	2009	$ 285,000
Cocke Hall Annex:			
Series 2002A, issued $2,025,000 - partial refunding *	4.00 - 5.25	2022	1,052,007
Series 2007B, issued $735,000 - refunding Series 2002A *	4.00 - 4.50	2020	776,264
Jackson Memorial Hall Renovation:			
Series 2002A, issued $2,335,000 - partial refunding *	4.00 - 5.25	2022	1,209,144
Series 2007B, issued $850,000 - refunding Series 2002A *	4.00 - 4.50	2020	897,683
			$ 4,220,098

* See Note 9 Bond Defeasance - current year

Maturities on notes and bonds payable for years succeeding 30 June 2008 are as follows:

Year	Bonds Payable	Notes Payable	Total
2009	$ 400,000	$ 465,000	$ 865,000
2010	415,000	185,000	600,000
2011	440,000	200,000	640,000
2012	455,000	210,000	665,000
2013	475,000	220,000	695,000
2014-2018	2,770,000	1,255,000	4,025,000
2019-2023	3,535,000	1,560,000	5,095,000
2024-2025	1,660,000	-	1,660,000
Unamortized premium	519,673	132,973	652,646
Deferral on debt defeasance	-	(7,875)	(7,875)
Total future principal requirements	$ 10,669,673	$ 4,220,098	$ 14,889,771

A summary of future interest commitments for fiscal years subsequent to 30 June 2008 is presented as follows:

Year	Bonds Payable	Notes Payable	Total
2009	$ 490,856	$ 181,743	$ 672,599
2010	470,856	166,825	637,681
2011	450,106	157,275	607,381
2012	433,606	147,125	580,731
2013	410,856	136,475	547,331
2014-2018	1,672,281	518,556	2,190,837
2019-2023	907,031	206,306	1,113,337
2024-2025	114,838	-	114,838
Total future interest requirements	$ 4,950,430	$ 1,514,305	$ 6,464,735

Installment Purchase Obligations

The Institute has future obligations under installment purchase agreements. The book value of the assets capitalized under these installment purchase agreements is $176,468 with no interest. A summary of future obligations under these agreements as of 30 June 2008 follows:

Year Ending 30 June	Principal
2009	34,173
2010	31,974
2011	14,889
2012	2,200
2013	733
Total	$ 83,969

Capital Leases Payable

VMI is the lessee of equipment under capital leases expiring in 2012. The assets acquired under capital leases are recorded as property, plant, and equipment at the lower of the net present value of the minimum lease payments during the lease term or the fair market value of the asset.

For all capital leases, the minimum lease payments together with the present value of the net minimum lease payments as of 30 June 2008 are as follows:

Year Ending 30 June	Other Capital Leases
2009	$ 9,925
2010	9,925
2011	9,925
2012	828
Total Minimum lease payments	30,603
Less: Executory costs	(7,650)
Less: Interest	(2,748)
Present value of net minimum lease payments	$ 20,205

Equipment Trust Fund

The Equipment Trust Fund (ETF) program was established to provide state-supported institutions of higher education bond proceeds for financing the acquisition and replacement of instructional and research equipment. The Virginia College Building Authority (VCBA) manages the program. The VCBA issues bonds and uses the proceeds to reimburse the Institute and other institutions of higher education for equipment purchased. For fiscal years prior to 1999, the VCBA purchased the equipment and leased it to the Institute. For fiscal years 1999 and following, financing agreements for ETF were changed so that the Institute now owns the equipment from the date of purchase.

The Statement of Net Assets line “Due from the Commonwealth” includes $57,085 representing equipment purchased by the Institute that was not reimbursed by the VCBA as of 30 June 2008.

Operating Leases

VMI is committed under various operating leases for equipment. Operating leases do not give rise to property rights or lease obligations, and therefore the results of the lease agreements are not reflected in the Institute’s Statement of Net Assets. In general, the leases are for a three year term and the Institute has renewal options. In most cases, the Institute expects these leases will be replaced by similar leases in the normal course of business. Rental expense was approximately $103,943 for the year ended 30 June 2008. Rental expense commitments for subsequent fiscal years are as follows:

Year Ending 30 June	Amount
2009	82,457
2010	57,091
2011	45,330
2012	29,166
2013	8,254
Total	$ 222,298

Capital Improvement Commitments

As of 30 June 2008, the Institute had outstanding construction contract commitments of $32,190,923. This amount represents the value of obligations remaining on capital improvement project contracts. These obligations are for future efforts and as such have not been accrued as expenses or liabilities on the Institute's financial statements.

NOTE 9: BOND DEFEASANCE

On 2 October 2007, the Virginia College Building Authority (VCBA), on behalf of the Institute, issued $1,669,454 of Section 9(d) revenue bonds to advance-refund $1,660,863 of section 9(d) debt in fiscal year 2008. The advance refunding reduced the aggregate debt service by $92,780, representing a net present-value savings of $77,941.

NOTE 10: RETAINAGE PAYABLE

At 30 June 2008, $2,531,596 was held by the Institute as retainage on various contracts for work, which had been performed. The retainage will be remitted to the various contractors upon satisfactory completion of the projects.

NOTE 11: EXPENSES BY NATURAL CLASSIFICATIONS

The Institute's operating expenses by natural classification were as follows for the year ended 30 June 2008:

Program	Personal Services	Supplies	Contractual Services	Equipment	Utilities	Student Aid	Other Operating Expenses	Depreciation Expense	TOTAL
Instruction	$ 14,441,079	$ 184,394	$ 619,446	$ 323,884	$ -	$ -	$ 39,319	$ 1,700,052	$ 17,308,174
Research	188,515	24,254	74,222	367	-	-	30,417	37,527	355,302
Public service	682,291	174,997	296,604	15,228	-	-	58,677	160,950	1,388,747
Academic support	3,426,017	119,680	1,026,194	213,336	-	-	94,227	705,943	5,585,397
Student services	1,882,613	106,990	1,159,814	163,888	-	-	107,304	220,567	3,641,176
Institutional support	3,101,651	194,825	1,006,943	33,620	4,712	-	134,218	118,233	4,594,202
Operation and maintenance of plant	2,539,704	1,141,644	646,458	1,108,060	717,453	-	382,905	525,858	7,062,082
Student aid	4,423	4,859	43,060	7,729	-	833,776	-	-	893,847
Auxiliary enterprises	5,108,476	535,206	5,305,802	338,568	223,965	10,175	3,474,465	1,585,512	16,582,169
Unique military activities	3,697,606	1,324,683	132,739	37,153	-	-	396,362	259,625	5,848,168
Total operating expenditures	$ 35,072,375	$ 3,811,532	$ 10,311,282	$ 2,241,833	$ 946,130	$ 843,951	$ 4,717,894	$ 5,314,267	$ 63,259,264

NOTE 12: STATE APPROPRIATIONS

Virginia Military Institute receives state appropriations from the General Fund of the Commonwealth of Virginia. The Appropriation Act specifies that such unexpended appropriations shall revert, as specifically provided by the General Assembly, at the end of the biennium. For years ending at the middle of the biennium, unexpended appropriations that have not been approved for reappropriation in the next year by the Governor become part of the General Fund of the Commonwealth and are, therefore, no longer available to VMI for disbursement. Fiscal year 2008 ends the biennium.

During the fiscal year ended 30 June 2008, the Institute received the following supplemental appropriations and reversions in accordance with the Appropriation Act:

Originial legislative appropriation:	
Educational and general programs	$ 10,857,901
Unique military activity	4,931,037
Student financial assistance	716,768

Adjustments:	
Compensation adjustments	484,049
Tuition incentive	131,281
ETF lease payment - NGF portion	(88,844)
Student financial assistance	2,250
Interest on E&G cash balances	15,052
Debt service fee - Non-Virginia cadets	(65,262)
Appropriations transfers:	
Authorized FY 08 transfer - E&G	34,000
SCHEV programs	25,377
VMI budget reduction	(901,946)
Virginia Tech Corps of Cadets	(1,499,382)
Virginia Tech budget reduction	(70,442)
Mary Baldwin budget reduction	(8,974)
Adjusted appropriations	$ 14,562,865

NOTE 13: RETIREMENT AND PENSION SYSTEMS

Employees of the Institute are employees of the Commonwealth of Virginia. Most full-time classified salaried employees of the Institute participate in the defined benefit retirement plan administered by the Virginia Retirement System (VRS). The Institute Post Police officers participate in the Virginia Law Officers Retirement System, (VaLORS), instead of VRS. Both VRS and VaLORS are agent multiple-employer public employee retirement systems (PERS) that acts as a common investment and administrative agency for the Commonwealth of Virginia and its political subdivisions.

The Institute's payroll costs for employees covered by VRS totaled $13,891,419 for the year ended 30 June 2008. The Institute's total payroll costs were $28,501,998 for the year ended 30 June 2008.

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 are established, can be found in the Commonwealth's Comprehensive Annual Financial Report (CAFR).

The Institute's total VRS contribution was $1,823,133 for the year ended 30 June 2008, which included the 5% employee contribution assumed by the employer. These contributions represent 13.15% of covered payrolls for 2008.

The Institute's payroll cost for employees covered by VaLORS was $278,335 for the year ended 30 June 2008. The Institute's total VaLORS contribution was $63,502 for the year ended 30 June 2008, which represents 22.86% of the covered payroll for the 2008 fiscal year.

The VRS does not measure assets and pension benefit obligations separately for individual state institutions. The CAFR provides disclosure of the Commonwealth's unfunded pension benefit obligation at 30 June 2008. The same report contains historical trend information showing VRS's progress in accumulating sufficient assets to pay benefits when due.

TIAA/CREF Insurance Company Optional Retirement Plan (ORP)

Some full-time faculty and contracted administrative staff participate in a retirement annuity program through TIAA/CREF Insurance Companies rather than the VRS. This is a fixed-contribution program where the retirement benefits received are based entirely upon the employer's (10.4%) contributions, plus interest and dividends, with the employer assuming the employee's contribution share.

Individual contracts issued under the plan provide for full and immediate vesting of both the Institute's and the employees' contributions. Total pension costs under this plan were approximately $898,426 year ended 30 June 2008. Contributions to the TIAA/CREF Insurance Companies were calculated using the base salary amount of approximately $8,638,715 for fiscal year 2008.

Fidelity Investments

The Institute also contributed to one other defined contribution pension plan, which is insignificant in relation to VRS and TIAA/CREF. Full-time faculty, certain administrative staff that hold academic rank, and athletic coaches are eligible to participate in this program (ORP) other than VRS and TIAA/CREF. Retirement benefits received are based entirely upon the employer's (10.4%) contributions, plus interest and dividends, with the employer assuming the employee's contribution share.

Amounts contributed to Fidelity Investments were calculated using the base salary amount of approximately $1,225,116 for fiscal year ended 30 June 2008. Total pension costs under this plan were approximately $127,412 for fiscal year 2008.

Deferred Compensation Plan

Employees of the Commonwealth may participate in the Commonwealth's Deferred Compensation Plan. Participating employees can contribute to the plan each pay period with the Commonwealth matching up to $20 per pay period. The dollar amount match can change depending on the funding available in the Commonwealth's budget. The Deferred Compensation Plan is a qualified defined contribution plan under Section 401(a) of the Internal Revenue Code. Employer contributions under the Deferred Compensation Plan were approximately $110,815 for the fiscal year 2008.

NOTE 14: POST-EMPLOYMENT BENEFITS

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

NOTE 15: RISK MANAGEMENT

The Institute is exposed to various risks of loss related to torts; theft or, damage to, and destruction of assets; errors and omissions; non-performance of duty; injuries to employees; and natural disasters. The Institute participates in insurance plans maintained by the Commonwealth of Virginia. The state employee health care and worker's compensation plans are administered by the Department of Human Resource Management and the risk management insurance plans are administered by the Department of Treasury, Division of Risk Management. Risk management insurance includes property, general liability, medical malpractice, faithful performance of duty bond, automobile, and air and watercraft plans. The Institute pays premiums to each of these Departments for its insurance coverage. Information relating to the Commonwealth's insurance plans is available at the statewide level in the Commonwealth of Virginia's Comprehensive Annual Financial Report.

NOTE 16: CONTINGENCIES

The Institute has received federal grants for specific purposes that are subject to review and audit by the grantor agencies. Claims against these resources are generally conditional upon compliance with the terms and conditions of grant agreements and applicable federal regulations, including the expenditure of resources for allowable purposes. Any disallowance resulting from a federal audit may become a liability of the Institute.

In addition, the Institute is required to comply with various federal regulations issued by the Office of Management and Budget. Failure to comply with certain systems requirements of these regulations may result in questions concerning the allowability of related direct and indirect charges pursuant to such agreements. As of 30 June 2008 the Institute estimates that no material liabilities will result from such audits or questions.

In October 2003, VMI entered into a contract modification with ARAMARK Educational Services, VMI's contracted dining services vendor. Under this agreement, ARAMARK provided \$1,200,000 to VMI to support the expansion and renovation of the Crozet Hall dining facility. The agreement requires ARAMARK to amortize this cost on a straight-line basis over a ten-year period. In the event that VMI or ARAMARK terminates the contract, VMI must re-pay any unamortized balance to ARAMARK within 90 days of termination.

In August 2007, the Institute entered into a five year contract (with the option of one additional renewal term of five years) with ARAMARK to provide dining services to cadets. Under this agreement, ARAMARK agreed to provide a $750,000 financial commitment for food service facility renovations and for the purchase and installation of food service equipment, area treatment, signage and marketing materials and other costs associated with the Campus Food Service Program on our premises. During the first year of this contract (fiscal year 2008), the Institute received $500,000 of this commitment with the remaining balance ($250,000) to be paid during the fourth year (fiscal year 2011). In accordance with the agreement, ARAMARK agrees to amortize this commitment on a straight-line basis over a ten year period through 2017. Upon expiration or termination of this agreement by either party prior to 2017, VMI agrees to pay ARAMARK the unamortized balance plus all accrued but unbilled interest (prime rate plus two percentage points per annum, compounded monthly) within 30 days.

NOTE 17: LITIGATION

The renovation of Crozet Hall project was substantially completed on 27 July 2006, 270 days after the original contracted completion date. On 23 May 2007, the contractor filed a claim in Rockbridge County Court, suing the Institute for damages in the amount of $430,242 as a result of these delays. On 26 July 2007, the Institute paid the contractor $99,646, the amount to which the Institute believes the contractor is entitled, leaving an outstanding claim against the Institute of $330,596. On 1 May 2008, the trial court granted final judgment in favor of VMI. The contractor has filed a Petition for Appeal in the Supreme Court of Virginia. VMI, in conjunction with the Office of the Attorney General, has prepared and submitted a Brief in Opposition.

NOTE 18: EXTRAORDINARY ITEM

Chapter 847 of the 2008 Virginia Acts of Assembly (as amended), authorized the issuance of bonds to replace or supplant the fund source for certain capital projects from general fund cash to bonds. As a result, $37,054,974 of cash and cash equivalents reflected during fiscal year 2007 for the Expansion and Renovation of Barracks capital project, was supplanted with bond proceeds from the Virginia College Building Authority, and is reflected as an extraordinary loss in our 2008 Statement of Revenues, Expenses and Changes in Net Assets.

NOTE 19: VMI ALUMNI AGENCIES

The VMI Alumni Agencies (the “Agencies”) are comprised of four organizations that share the common purpose of raising funds, investing funds, and performing other activities on behalf of VMI alumni and other donors in support of Virginia Military Institute (“VMI”). Significant sources of revenue consist of contributions and investment return. Due to their shared purpose, the Agencies have elected to present their financial statements on a combined basis. All significant interagency accounts and transactions have been eliminated in combination. The individual organizations comprising the Agencies and their purposes are as follows:

The VMI Alumni Association
The purpose of The VMI Alumni Association is to organize the alumni of VMI into one general body.

VMI Foundation, Incorporated
The purposes of the VMI Foundation, Incorporated are to solicit and to accept various funds and to disburse such funds, or income earned from those funds, for the advancement of VMI and the Alumni Association.

VMI Development Board, Incorporated
The purposes of the VMI Development Board, Incorporated are to support VMI by coordinating development and fundraising efforts conducted on behalf of VMI Alumni and other donors.

VMI Keydet Club, Incorporated
The purposes of the VMI Keydet Club, Incorporated are to support, strengthen, and develop the intercollegiate athletic program at VMI.

Contributions receivable

Contributions receivable consist of the following:

	2008
Unconditional promises to give	$ 12,822,873
Charitable trust held by others	181,407
	13,004,280
Less: current portion	(4,548,388)
	$ 8,455,892
Gross amounts expected to be collected in:	
Less than one year	$ 5,053,764
One to five years	9,440,465
More than five years	1,566,651
	16,060,880
Less:	
Discount net present value at 3% - 6%	$ (1,468,653)
Allowance for uncollectible contributions	$ (1,587,947)
	$ 13,004,280

The ownership of contributions receivable for each class of net assets as of 30 June is as follows:

Temporarily restricted	$ 11,148,635
Permanently restricted	1,855,645
	$ 13,004,280

At 30 June 2008, the Agencies had also received bequest and other intentions of approximately $82.7 million. These intentions to give are not recognized as assets and, if they are received, they will generally be restricted for specific purposes stipulated by the donors.

For the year ended 30 June 2008, approximately 28% of the contributions receivable balance was from three donors.

Investments held by trustees

The Agencies participate in a combined investment fund (the "Fund") controlled by the VMI Investment Committee, a committee comprised of representatives from each agency. Mellon Trust of Boston, N.A. serves as custodian for the Fund's assets. The Fund's investments consist of the following:

	2008	
Equities/Hedge Fund	$ 259,663,097	84.1%
Fixed income bond	40,049,465	12.5%
Cash and cash equivalent	9,007,925	3.4%
	308,720,487	100.0%
Less: Amount payable for securities purchased, net	(1,489,923)	
	$ 307,230,564	

These investments, which comprise the majority of the Agencies' assets, are subject to market risk. However, the Agencies' investment funds are managed by a number of investment managers, which limits the amount of risk in any one fund. The Agencies' Investment Committee establishes investment guidelines and performance standards which further reduce its exposure to market risk.

Investments held by trustees activity is reflected in the table below:

Investments held by trustees	2008
Investments, beginning	$ 333,392,423
Investments returns:	
Dividends and interest	5,814,961
Net realized and unrealized gains (losses)	(28,607,993)
Less: investment fees	(2,203,063)
	(24,996,095)
Net receipts (disbursements) from Mellon account used to fund operations	(1,165,764)
Investment, ending	$ 307,230,564

The Agencies employ a total return spending policy that establishes the amount of investment return that is available to support current needs and restricted purposes. This policy is designed to insulate program spending from capital market fluctuations and increase the amount of return that is reinvested in the corpus of the fund in order to enhance its long-term value. For the year ended 30 June 2008, the Board-approved spending formula for the endowment provided for an annual spending rate of 4.7% of the average of the prior twelve quarters' December 31 market values adjusting these market values upward to reflect subsequent receipt of gifts, or downward to reflect extraordinary withdrawals. If cash yield (interest and dividends) is less than the spending rate, realized gains can be used to make up the deficiency. Any income in excess of the spending rate is to be reinvested in the endowment.

Investments, Other

Investments, other, consist of the following:

	2008			
	Held by Agent	Held by Foundation	Held in Irrevocable Trusts*	Total at Fair Value**
Equities	$ 2,984,594	$ 9	$ 8,345,212	$ 11,329,815
Fixed income	35,275	5,891	4,590,836	4,632,002
Real estate	-	1,100,049	-	1,100,049
Cash and cash equivalents	37,469	783	422,574	460,826
Limited partnerships	222	17,128	-	17,350
	$ 3,057,560	$ 1,123,860	$ 13,358,622	$ 17,540,042

*Investments held in irrevocable trusts are not available for use until the occurrence of a future event as noted in the applicable trust agreements.

**For certain components of these investments, primarily real estate, limited partnerships, and common stocks of closely held companies, where fair values were not readily determinable, cost was used.

Bonds Payable

Bonds payable consists of the following:

	2008
Variable Rate Educational Facilities Revenue Bonds, Series 2006, payable in varying installments from $1,080,000 to $2,770,000, commencing 2012 through 2036. Interest payments commenced August 2006, rate is variable and ranged from 1.24% to 3.95% during the year ended June 30, 2008. Interest is subject to an interest rate swap agreement which requires a fixed rate payment by the Agencies of 3.42% (3.92780% through March 31, 2008) on $30,000,000 of the debt. Collateralized by a $45.4 million letter of credit. Unexpended proceeds at June 30, 2008 are included in funds restricted for affiliate in the combined statement of financial position.	45,000,000
Mark-to-market estimate of bank swap transaction related to Industrial Development Authority Bonds	691,022
	$ 45,691,022
Less: current maturities	-
	$ 45,691,022

Year ending 30 June:	
2009-2011	$ -
2012	1,080,000
2013	1,125,000
Thereafter	42,795,000
Mark-to-market on interest rate swap	691,022
	$ 45,691,022

The Agencies entered into an interest rate swap agreement in May 2006. The swap agreement has a notational amount of $30,000,000 that effectively converts the variable rate based payments on $30,000,000 of bond debt to a fixed rate interest payment at 3.92780%. This swap was effective beginning 1 August 2006 and expires 1 August 2013. Terms of the swap were revised effective 1 April 2008 including a change in the fixed rate payment to 3.42%.

NOTE 20: COMPONENT UNITS

Condensed financial statements for the component units of the Institute are as follows:

CONDENSED STATEMENTS OF NET ASSETS As of 30 June 2008	VMI Research Laboratories Inc.	VMI Alumni Agencies	TOTAL
Assets:			
Current assets	$ 463,650	$ 21,044,230	$ 21,507,880
Noncurrent assets	110,586	338,733,928	338,844,514
Total assets	574,236	359,778,158	360,352,394
Liabilities:			
Current liabilities	81,270	1,969,833	2,051,103
Noncurrent liabilities	77,884	50,721,053	50,798,937
Total liabilities	159,154	52,690,886	52,850,040
Net Assets:			
Unrestricted	352,672	26,432,868	26,785,540
Temporarily restricted	52,410	176,269,719	176,322,129
Permanently restricted	10,000	104,384,685	104,394,685
Total net assets	415,082	307,087,272	307,502,354
Total net assets and liabilities	$ 574,236	$ 359,778,158	$ 360,352,394

CONDENSED STATEMENTS OF REVENUES EXPENSES AND CHANGES IN NET ASSETS As of 30 June 2008	VMI Research Laboratories Inc.	VMI Alumni Agencies	TOTAL
Total revenues	$ 1,179,349	$ 24,118,030	$ 25,297,379
Total expenses	(1,044,480)	(37,154,462)	(38,198,942)
Total net realized and unrealized losses on investments	(10,918)	(28,568,810)	(28,579,728)
Total change in net assets	123,951	(41,605,242)	(41,481,291)
Total beginning net assets	291,131	348,692,514	348,983,645
Total ending net assets	$ 415,082	$ 307,087,272	$ 307,502,354

NOTE 21: SUBSEQUENT EVENTS

Since 30 June 2008, the significant drop in the stock market due to the financial market crisis and the recession has resulted in a major reduction in the market value of VMI and the VMI Foundation's endowment investments. VMI's endowment investments dropped in value from $15.6 million as of 30 June 2008 to $8.9 million as of 28 February 2009 due primarily to a 37% reduction in the market value of the investments. The VMI Foundation's endowment investments dropped from $307.2 million as of 30 June 2008 to $193.4 million as of 28 February 2009 due also to a 37% decrease in market value.

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Commonwealth of Virginia

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

Walter J. Kucharski, Auditor

April 13, 2009

The Honorable Timothy M. Kaine
Governor of Virginia
State Capital
Richmond, VA

The Honorable M. Kirkland Cox
Chairman, Joint Legislative Audit
and Review Commission

Board of Visitors
Virginia Military Institute

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

We have audited the accompanying financial statements of the business-type activities and aggregate discretely presented component units of the **Virginia Military Institute**, a component unit of the Commonwealth of Virginia, as of and for the year ended June 30, 2008, which collectively comprise the Institute's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Institute's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the component units of the Institute, which are discussed in Note 1. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the component units of the Institute 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 Institute 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 business-type activities and discretely presented component units of the Institute as of June 30 2008, 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.

The management's discussion and analysis 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.

In accordance with Government Auditing Standards, we have also issued our report dated April 13, 2009 on our consideration of the Virginia Military Institute's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

AUDITOR OF PUBLIC ACCOUNTS

JLN/alh