VIRGINIA STATE UNIVERSITY

REPORT ON AUDIT

FOR THE YEAR ENDED

JUNE 30, 2006

Auditor of
Public Accounts
COMMONWEALTH OF VIRGINIA

AUDIT SUMMARY

Our audit of Virginia State University for the year ended June 30, 2006, found:

- the financial statements are presented fairly, in all material respects;
- internal control matters that we consider to be reportable conditions; however, we do not consider these matters to be material weaknesses;
- an instance of non-compliance required to be reported; and
- the University has taken adequate corrective action with respect to the audit findings reported in the prior year.

We recommend that the University improve:

- the financial statement preparation process; and
- the information security program.

In this report, we also provide a discussion of the status of Project New Horizons, the University's implementation of the new Banner administrative systems, with updated recommendations.

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

STATUS OF PROJECT NEW HORIZONS

We have continued to monitor Virginia State University's progress in implementing their new Banner administrative systems, Project New Horizons. The University successfully went live with their Finance module in July 2006. The University is still implementing components related to Finance, but these components were not critical for go-live, and all the components are set to be complete in April 2007. The University's main focus is currently on implementing the Student and Financial Aid modules.

The University implemented Banner Financial Aid in January 2007 and plans to fully implement the Banner Student module by July 2007. The Admissions component of the Student module went live in October 2006, with the Admissions Office entering and accepting student applications for Fall 2007. As of March 2007, the University enabled the web admissions and self-service functions which allow prospective freshman students to apply on-line for University admissions.

Below, we provide a discussion of what action the University has taken since our last update and provide updated recommendations. The University has worked hard to address the issues we reported previously and we commend their efforts, but much work remains for the successful implementation of the Student module on schedule.

Address Staffing Issues

The University experienced staffing shortages during the Finance module implementation. To address the shortages, the University restructured the project team. This approach increased productivity and facilitated the successful go-live of the Finance module. The University is taking the same approach for the Financial Aid module, but the need for additional resources still remains.

The Banner Student project recently experienced delays during the conversion of data from the University's current student system for three main Student components, General Person, Admissions, and General Student. During data conversion SunGard and University staff used different conversion methodologies, which neither discovered until after encountering conversions delays.

SunGard and the University provided additional resources to the conversion effort, but these resources have not overcome the delays and are therefore not available to assist on current activities. The University is aware of this situation and has requested SunGard provide additional technical and functional support and also hired a consulting firm to help complete tasks. It is important that the University complete, test, and verify the tasks and conversions before June since they are essential functions to the system integration before the planned go-live in July.

Project Oversight

The University has hired a full-time committed project manager to run the daily management of the project. The project manager ensures the project remains on schedule, scope, and budget. The University also contracts with SunGard project management services and both project managers work collaboratively and share responsibility for project planning, execution, and control.

The Banner project is on their second SunGard project manager. The University is dissatisfied with SunGard's vendor provided services. This problem is not unique to Virginia State University. They should remain assertive in managing SunGard as well as having the ultimate authority over the project.

Maintain Internal Audit Oversight

The Project Charter originally called for the University Internal Auditor's involvement in conducting mid-quarter quality assessments that are essentially abridged versions of a full Independent Verification and Validation (IV&V) review. However, turnover had left the University's Internal Audit department with limited staff, reducing their ability to provide the mid-quarter quality assessments. In August 2006, at the request of the Chief Audit Executive and with concurrence of University management, Virginia Information Technologies Agency (VITA) and others, Internal Audit's mid-quarter quality assessments were waived. VITA and University management believed VITA's level of involvement along with the Independent Verification and Validation (IV&V) process was sufficient and that mid-quarter assessments were not necessary.

The Chief Audit Executive has remained active on the project serving in an advisory role to the Executive Oversight Committee and posing concerns as appropriate. An IT Audit Manager was hired in January 2007 and has continued as an active advisor to the various committees on the project. As a result of these developments, Internal Audit oversight is no longer an issue.

Recommendation

The University plans to use the Banner Student module in July 2007. Before go-live, the University must complete all related project tasks and full system integration testing. However, the schedule includes late tasks and delayed conversion efforts, and there is a significant amount of work scheduled for completion in a short period of time.

Currently, there are risks to the project that the University must continue to closely monitor and manage to achieve success. These risks include: staffing issues, completing tasks on schedule, and performing adequate system testing. The University's Chief Information Officer (CIO) is aware of these risks, is closely monitoring them, and has added an additional testing period to the project schedule and additional resources to bring the project tasks and conversions back on schedule. The CIO needs to continue to monitor these issues quickly or the project may become too far behind schedule to perform adequate system testing.

While the University is confident that the system will go live as scheduled in July, we remain cautious. Project New Horizons is entering another critical stage, and there is still a significant amount of work that requires completion in a short period of time. With no remaining slack in the project schedule to absorb delays, every delay could result in decreased system testing or error resolution. It is important that the University implement a quality review system to ensure thorough testing of the system and allow time to resolve errors and retest before going live.

INTERNAL CONTROL AND COMPLIANCE FINDINGS AND RECOMMENDATIONS

Improve Financial Statement Preparation Process

The current financial statement preparation process puts the University at risk of not meeting the Commonwealth's performance standards for universities. During the past several audits, including the current audit, University financial reporting staff and our auditors identified several accounting issues that required material audit adjustments to the financial statements. Additionally, University financial reporting staff were required to devote significant resources to correct errors and deficiencies to the University's final financial statements that were presented to senior management and the Board of Visitors and were used for the University's submissions for the state's Comprehensive Annual Financial Report.

The American Institute of Certified Public Accountants has adopted new auditing standards effective with the audit for the year ended June 30, 2007, and had we conducted the current audit following these standards, we would have reported a material weakness in internal controls. Having a material weakness in internal controls may result in a significant deficiency that would keep the University from meeting the Commonwealth's performance standards and sharing in financial benefits related to interest on state-held funds and purchase card rebates.

The new auditing standard will require the auditor to review the financial statement preparation process including the gathering of all information from throughout the campus and determining the adequacy of support for all information in the statements and related journal vouchers. The auditor must also determine if a proper segregation of duties exists within the process. Finally, the auditor must determine if the process is sufficiently comprehensive to produce financial statements without the auditor finding any material audit adjustments, which, even if recorded, could result in a material weakness.

We recommend that the University continue to improve its financial preparation process. The University must continue to ensure that financial reporting is fully staffed, responsibilities are cross-trained to other staff to aid in their development, provide separation of duties, and allow for proper succession planning. With continued improvements in the financial statement preparation process, the University would ensure that each year an accurate financial statements process should take less time, continue to meet all applicable deadlines, and allow staff to complete their regular work cycle while preparing the financial statements. If the University does not address this issue, the next audit would result in the University receiving a material weakness in internal controls. University senior management must commit the resources to continue to improve the financial statement preparation process, if it is to avoid risking not meeting the Commonwealth's performance standards.

Improve Information Security Program

In December 2006, we issued a report on the results of a statewide security audit in which we reported that the University had an inadequate security program. University management responded appropriately to our concerns and began to take corrective action in implementing a number of items found during that audit.

A recent incident involving the University's security program indicates that management will need to perform additional review and development of the program. The program has a corrective action component for each of the specific concerns that we identified in our December audit report. However, the recent incident indicates that the management should take a high-level approach to making sure that its overall plan has a mechanism to unify and coordinate the components of the security program, so that it adequately addresses all of the University's business operations. We recommend the University review their security program in the following four areas.

- Determine that the security program includes proper responses to incidents or disasters involving a particular type of technological asset that the University depends on. For example, if the Student Information System is highly dependent on Internet availability, ensure the University's security program includes appropriate risk responses for threats to network and server components.

- Create and maintain awareness and training needs of personnel to effectively execute the program incident response and reporting process. Incident reporting is essential to the timely and effective resolution of a security problem.

- Make sure that the entire University community understands their responsibilities and duties under the individual security program components, and how performing their duties in a timely, cohesive, and coordinated manner will help the entire University's business and academic functions.

- Continue to involve senior management in the review and approval of the University's information security program.

MANAGEMENT'S DISCUSSION AND ANALYSIS
(unaudited)

Introduction

This discussion and analysis provides an overview of the financial position and results of activities of Virginia State University for the year ended June 30, 2006. Comparative information for the fiscal year ended June 30, 2005, has been provided where applicable. The financial statements referred to above were prepared in accordance with applicable pronouncements and statements of the Governmental Accounting Standards Board (GASB).

Effective with fiscal year 2006, the University was required to implement GASB Statement 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recovery.* This statement requires universities to account for and report the impairment of capital assets which currently are written down only through the process of depreciation. Asset impairment is defined as a significant, unexpected decline in the service utility of a capital asset. There were no assets which required reporting under this statement.

Background

The University is one of two land grant institutions in the Commonwealth. As a land grant institution, the University engages in natural resource related research projects and agriculture extension services. The University, founded in 1882, was designated a land grant institution in 1920, and attained University status in 1979. The University offers programs at the doctoral, graduate, and undergraduate levels in science, education, humanities, social sciences, and business. The University is governed by an eleven member Board of Visitors.

The University is a component unit of the Commonwealth of Virginia and is included in the basic financial statements of the Commonwealth. The Commonwealth's Comprehensive Annual Financial Report (CAFR) includes all agencies, boards, commissions, and authorities over which the Commonwealth exercises or has the ability to exercise oversight authority.

Financial Highlights

The University's financial position remained strong at June 30, 2006, with total assets of $169,232,288 and liabilities of $40,168,180 compared to total assets of $156,285,624 and total liabilities of $34,032,635 at June 30, 2005. Total assets grew by 8.3 percent and total liabilities grew by 18.0 percent.

Net assets grew from $122,252,989 at June 30, 2005, to $129,064,108 at June 30, 2006. This is a 5.6 percent increase. The increase in net assets from operating and non operating revenues is summarized below:

Summary of the Increase in Net Assets *

	Year Ended June 30, 2006	Year Ended June 30, 2005	Increase/(Decrease) Amount	Increase/(Decrease) Percent
Total operating revenues	$ 57,803	$ 53,007	$ 4,796	9.0
Total operating expenses	94,883	88,095	6,788	7.7
Operating loss	(37,080)	(35,088)	(1,992)	5.7
Nonoperating revenues	38,559	35,772	2,787	7.8
Other revenue	5,332	7,978	(2,646)	(33.2)
Total	$ 6,811	$ 8,662	$ (1,851)	(21.4)

* in thousands

Comparing fiscal years 2005 and 2006, operating revenues increased by $4.8 million (9.0 percent) while operating expenses increased by $6.8 million (7.7 percent). Nonoperating revenues increased by $2.8 million (7.8 percent). After adding in other revenues, net assets increased by $6.8 million in fiscal year 2006.

Using the Financial Statements

The University's financial report includes three financial statements: the Statement of Net Assets (SNA); the Statement of Revenues, Expenses, and Changes in Net Assets (SRECNA); and the Statement of Cash Flows (SCF). As stated earlier, these statements are prepared in accordance with GASB principles, which establish standards for external financial reporting for public colleges and universities. Under these principles, revenues and expenses are categorized as either operating or nonoperating. Operating revenues include such items as student tuition and fees, grants and contracts, and sales and services of auxiliary enterprises. Nonoperating revenues include state appropriations and investment income. Consequently, the operating loss of $37,079,772 does not account for the normal nonoperating revenue sources, primarily state appropriations. By adding the nonoperating revenues, the adjusted income is $1,478,913 excluding other revenues (capital appropriations and gifts and additions to permanent endowments). When these revenues are taken into account, this in an overall increase in net assets of $6.8 million.

Statement of Net Assets

The Statement of Net Assets presents the financial position of the University at the end of the fiscal year and includes all assets and liabilities of the University. The difference between the total assets and total liabilities, the net assets, is one indication of the current financial condition of the University, while the change in net assets is an indication of whether the overall financial condition of the University has improved or worsened during the year. Assets and liabilities are generally measured using current values. One notable exception is capital assets, which are stated at historical cost less an allowance for depreciation.

Net assets are classified into four major categories: invested in capital assets, restricted non-expendable net assets, restricted expendable net assets, and unrestricted net assets.

Invested in Capital Assets reflects the University's capital assets net of accumulated depreciation and any debt attributable to their acquisition, construction, or improvement.

Restricted Non-Expendable Assets reflects the University's endowment and similar funds whereby the donor has stipulated that the gift principal is to be maintained and the income from the principal is to be used to support specific programs of the University.

Restricted Expendable Assets reflects the University's endowment and similar funds whereby the donor has stipulated that the gift be used for specific programs of the University.

Unrestricted Assets reflects a broad range of assets available to the University that may be used at the discretion of the Board of Visitors for any lawful purpose in support of the primary mission of education, research, and public service. These assets are derived from student tuition and fees, state appropriations, indirect cost recoveries from grants and contracts, auxiliary services sales, and donations.

A summary of the University's assets, liabilities, and net assets at June 30, 2006 and 2005, follows:

Condensed Statement of Net Assets *

	Year Ended June 30,		Increase/(Decrease)	
	2006	2005	Amount	Percent
Assets:				
Current assets	$ 36,682	$ 36,040	$ 642	1.8
Noncurrent assets:				
Restricted cash and cash equivalents	30,121	31,538	(1,417)	(4.5)
Investments	11,422	10,054	1,368	13.6
Capital assets, net	88,500	76,262	12,238	16.0
Other	2,507	2,391	116	4.9
Total assets	169,232	156,285	12,947	8.3
Liabilities:				
Current liabilities	21,108	18,012	3,096	17.2
Non current liabilities	19,060	16,020	3,040	19.0
Total liabilities	40,168	34,032	6,136	18.0
Net assets:				
Invested in capital assets, net of related debt	77,618	65,769	11,849	18.0
Restricted:				
Nonexpendable	2,183	1,929	254	13.2
Expendable	26,836	36,981	(10,145)	(27.4)
Unrestricted	22,427	17,574	4,853	27.6
Total net assets	$ 129,064	$ 122,253	$ 6,811	5.6

* in thousands

A review of the University's Statement of Net Assets at June 30, 2006 shows that the University continues to build and improve upon its financial condition. This financial condition reflects the prudent use of its financial resources, including budgetary controls, conservative utilization of debt, and maintenance and replacement of the physical plant. The overall increase in net assets of $6.8 million is the result of several factors. Overall, current assets increased by $0.6 million. Current assets are comprised of several different categories, including cash, short term investments, notes and loan receivables, and prepaid expenses. The primary reason for the overall change was an increase in short term investments.

Noncurrent assets increased by $12.3 million. Most of this increase in non-current assets occurred as a result of changes in capital assets. There was a decrease of $8 million in non-depreciable capital assets and an increase in depreciable assets of $20.3 million. The non-depreciable assets were assets in construction in progress which were moved to depreciable capital assets. The largest items were Foster Hall ($4.4 million), Johnston Library ($11.1 million), Rogers Stadium ($1.4 million), and Owens Hall ($6.1 million). These decreases were netted against increases to arrive at the $8.0 million change. The primary increase comes from construction on Gandy Hall and the Engineering and Technology Building.

The increase in depreciable assets of $20.3 million was primarily the result of the construction of the Johnston Library ($10.5 million), Foster Hall ($4.5 million), Rogers Stadium ($1.4 million), and Owens Hall ($6.0 million) and the capitalization of the Banner accounting system ($3.0 million). These amounts do not include depreciation. There were also increases in equipment of $2.5 million and improvements other than buildings of $1.0 million.

On the liability side, current liabilities are up $3.1 million, mainly as a result of an increase in obligations under the Securities Lending Program. Non-current liabilities also increased by $3.0 million, which relates to Rogers Stadium Phase II and Renovation of Student Housing.

Statement of Revenues, Expenses, and Changes in Net Assets

The Statement of Revenues, Expenses, and Changes in Net Assets presents the University's results of operating and nonoperating activities for the fiscal year. It also reflects other revenues (capital appropriations, capital grants and gifts, and additions to permanent endowments). Below is a summarized statement of the University's Revenues, Expenses, and Changes in Net Assets for the years ended June 30, 2006 and 2005.

Condensed Statement of Revenues, Expenses, and Changes in Net Assets *

	Year Ended June 30, 2006	2005	Increase / Decrease Amount	Percent
Operating revenues	$ 57,803	$ 53,007	$ 4,796	9.0
Operating expenses	94,883	88,095	6,788	7.7
Operating loss	(37,080)	(35,088)	(1,992)	5.7
Non operating revenues/(expenses):				
State appropriations	37,012	34,081	2,931	8.6
Other nonoperating revenues and expenses	1,547	1,691	(144)	(8.6)
Net nonoperating revenues and expenses	38,559	35,772	2,787	7.8
Income before other revenues	1,479	684	795	116.1
Capital appropriations	4,614	7,107	(2,493)	(35.1)
Capital grants and gifts	419	568	(149)	(26.2)
Additions to endowments	299	303	(4)	(1.3)
Total other revenues	5,332	7,978	(2,646)	(33.2)
Total increase in net assets	6,811	8,662	(1,851)	(21.4)
Net assets, beginning of year	122,253	113,591	8,662	7.6
Net assets, end of year	$ 129,064	$ 122,253	$ 6,811	5.6

* in thousands

As noted above, operating revenues for the University increased by 9.0 percent from the previous year and operating expenses increased by 7.7 percent. The operating loss for the University actually increased by $2.0 million in fiscal year 2006. This loss was offset by nonoperating revenues of $38.6 million, including state appropriations of $37 million, and other revenues of $5.3 million.

Summary of Revenues

A summary of the University's revenues for the years ended June 30, 2006 and 2005 appears below:

Summary of Revenues *

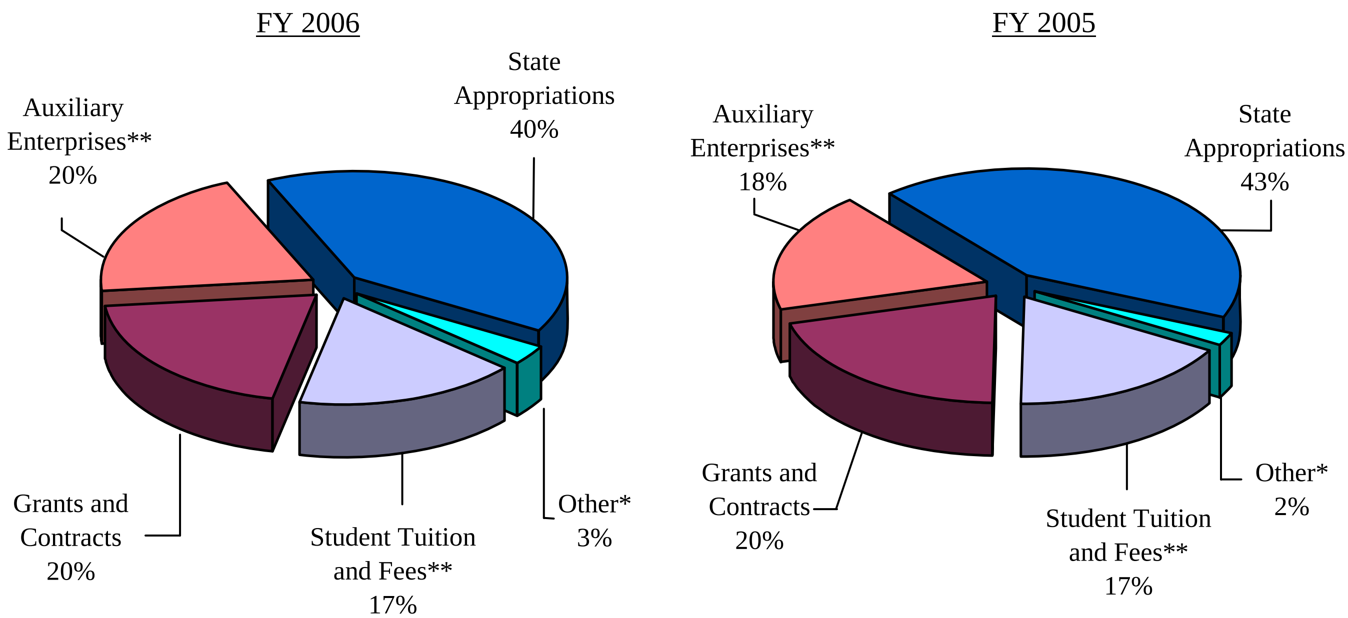
	Year Ended June 30,		Increase/(Decrease)	
	2006	2005	Amount	Percent
Operating revenues:				
Student tuition and fees, net of scholarship allowance	$ 16,833	$ 16,016	$ 817	5.1
Federal, state, and nongovernmental grants and contracts	20,697	19,218	1,479	7.7
Auxiliary enterprises, net of scholarship allowance	20,209	17,633	2,576	14.6
Other operating revenue	64	140	(76)	(54.3)
Total operating revenues	57,803	53,007	4,796	9.0
Nonoperating revenues/(expenses):				
State appropriations	37,012	34,081	2,931	8.6
Gifts	1,206	1,628	(422)	(25.9)
Other non operating revenues	341	63	278	441.3
Total non operating revenues	38,559	35,772	2,787	7.8
Capital revenues and gains:				
Capital appropriations	4,614	7,107	(2,493)	(35.1)
Capital gifts	419	568	(149)	(26.2)
Additions to permanent endowment	299	303	(4)	(1.3)
Total capital revenues	5,332	7,978	(2,646)	(33.2)
Total revenues	$ 101,694	$ 96,757	$ 4,937	5.1

*in thousands

Total operating revenues increased by $4.8 million (9.0 percent) in fiscal year 2006 compared to the previous year. The primary components of operating revenue increases are as follows: Tuition and fees increased by $0.8 million (5.1 percent), which is due to an increase in enrollment and in tuition and fee rates; grants and contracts increased by $1.5 million (7.7 percent) due primarily to an increase in Title III Revenue and the new funding for the Senior Executive Management Development Program; and sales and services of auxiliary enterprises increased by $2.6 million (14.6 percent) due to an increase in student fees. Under nonoperating revenues, state appropriations increased by $2.9 million, an 8.6 percent increase from the previous year.

Student tuition and fee revenue is shown net of tuition discounts and scholarship allowances. The tuition discounts and scholarship allowance are the difference between the stated charge for goods and services provided by the University and the amount that is paid by students and/or third parties on their behalf. Gross student tuition and fees were $22,210,558 and the auxiliary enterprise revenue was $26,396,592. The tuition discount and scholarship allowances totaling $11,565,188 is divided between tuition and fees ($5,377,721) and auxiliary enterprise ($6,187,467).

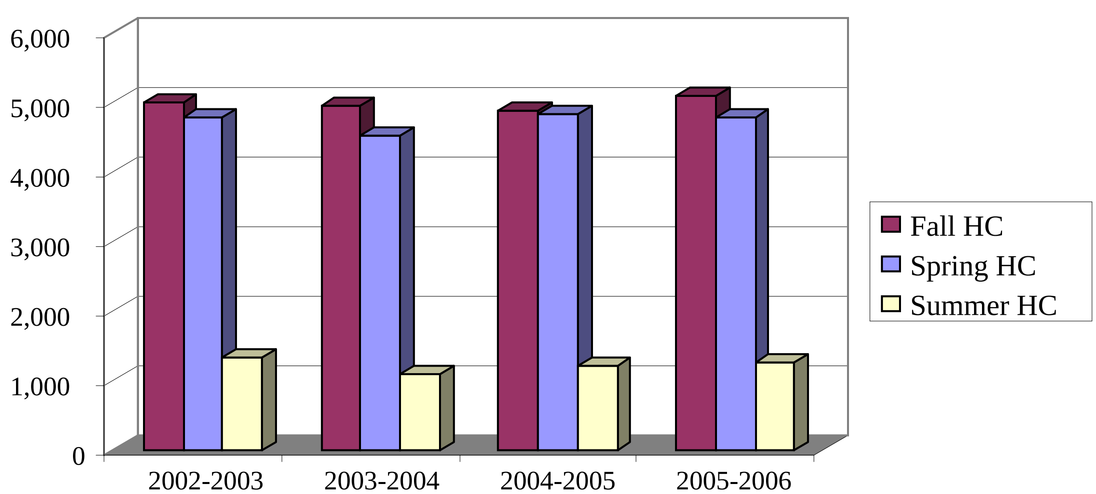
Summary of Revenues



*Other includes: – Gifts, Other Operating Revenue, and Other Nonoperating Revenue
**net of scholarship allowance

As demonstrated on the following chart, student headcount enrollment is shown for current fiscal year and the previous three fiscal years.

Student Enrollment
Fiscal Years 2004 - 2007
Student Course Enrollment Headcount



Overall student headcount has remained fairly steady over the last four fiscal years. Headcount is defined as "A student enrolled for more than zero credit hours in courses offered for degrees or certificate credit, or a student who meets the criteria for classification as a remedial student". Fall headcount rebounded in 2005-06 from the dip in the previous year, increasing from 4,867 to 5,089. This was partially offset by a dip in spring enrollment dropping from 4,822 in 2004-05 to 4,783 in 2005-06. Summer enrollment was up slightly, going from 1,195 in 2005 to 1,256 in 2006. This enrollment data would suggest that students continue to believe that Virginia State University is a good place to receive an education.

Summary of Expenses

A summary of the University's operating expenses for the years ended June 30, 2006 and 2005 appears below. Total operating expenses increased by $6.8 million in fiscal year 2006 compared to the previous fiscal year. This represents a 7.7 percent increase from the previous year. Auxiliary enterprise expenses increased by $2.3 million (15.0 percent) in 2006. Operation and maintenance of plant expenses increased by $2.3 million (20.0 percent) and depreciation expenses increased by $2.2 million (29.9 percent) as new facilities became operational.

Summary of Expenses *

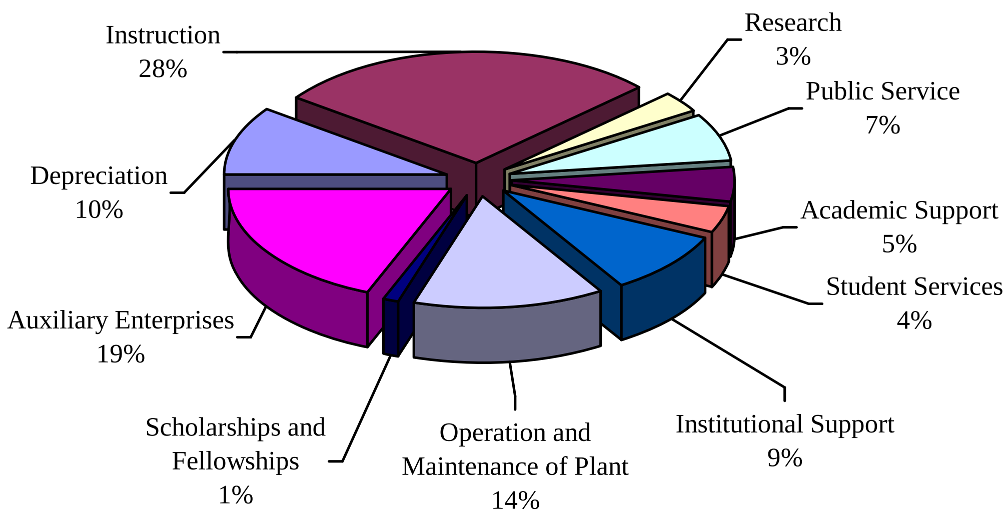
			Increase/(Decrease)	
	2006	2005	Amount	Percent
Operating expenses:				
Instruction	$ 25,822	$ 25,93	$ (109)	(0.4)
Research	3,006	2,84	157	5.5
Public service	6,328	5,56	762	13.7
Academic support	4,950	6,08	(1,135)	(18.7)
Student services	4,003	3,70	303	8.2
Institutional support	8,382	8,42	(42)	(0.5)
Operation and maintenance of plant	13,610	11,337	2,273	20.0
Scholarships and fellowships	1,309	1,326	(17)	(1.3)
Auxiliary enterprises	17,802	15,476	2,326	15.0
Other operating expenses	57	-	57	100.0
Depreciation	9,614	7,401	2,213	29.9
Total operating expenses	$ 94,883	$ 88,095	$ 6,788	7.7

* in thousands

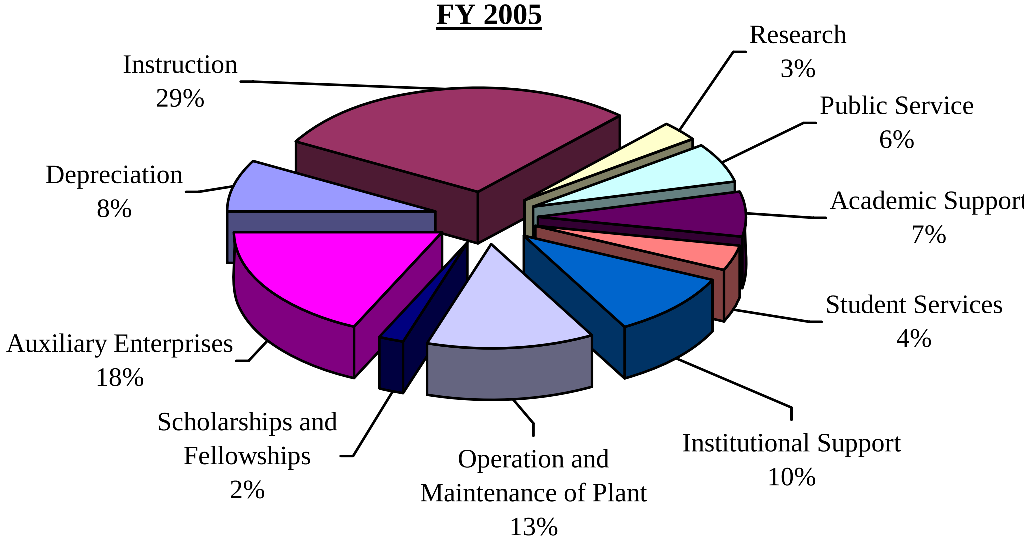
When expenses are reviewed on a natural classification basis, (see item 9 in Footnotes), salaries and wages increased $4.1 million (12.5 percent), from $33 million in fiscal year 2005 to $37.1 million in fiscal year 2006. Fringe benefits increased $1.8 million (19.6 percent), from $9.4 million in fiscal year 2005 to $11.2 million in fiscal year 2006. The increase in salaries and wages and related fringe benefits was due to an increase in faculty and support staffing in fiscal year 2006. Services and supplies expenses decreased $1.2 million (3.8 percent), from $29.8 million in fiscal year 2005 to $28.6 million in fiscal year 2006. The primary reason for the change was the capitalization of the Banner project. Depreciation expenses increased $2.2 million (29.9 percent) due to new facilities coming on line, from $7.4 million in fiscal year 2005 to $9.6 million in fiscal year 2006.

Summary of Expenses

FY 2006



FY 2005



Statement of Cash Flows

The Statement of Cash Flows provides additional information about the University's financial results by reporting the major sources and uses of cash. GASB principles define four major categories of cash flows: cash flows from operating activities, cash flows from noncapital financing activities, cash flows from capital and related financing activities, and cash flows from investing activities.

This statement provides a slightly different perspective from the Statement of Revenues, Expenses, and Changes in Net Assets. On the latter statement, state appropriations and gifts are considered nonoperating revenue. However, on the Statement of Cash Flows, these revenues are reflected under noncapital financing activities, while investment income is shown under investing activities. These cash flows are crucial to funding the operation of the University.

Statement of Cash Flows *

	Year Ended June 30,		Increase/(Decrease)	
	2006	2005	Amount	Percent
Cash flows from:				
Operating activities	$ (25,082)	$ (29,095)	$ 4,013	(13.8)
Noncapital financing activities	38,628	37,151	1,477	4.0
Capital and related financing activities	(14,347)	(5,593)	(8,754)	156.5
Investing activities	(910)	3,649	(4,559)	(124.9)
Net increase/(decrease) in cash and cash equivalents	(1,711)	6,112	(7,823)	(128.0)
Cash and cash equivalents, beginning of year-restated	56,114	54,168	1,946	3.6
Cash and cash equivalents, end of year	$ 54,403	$ 60,280	$ (5,877)	(9.8)

* in thousands
Cash and cash equivalents as of July 1, 2005 does not include certain amounts previously included in the Statement of Cash Flows.

Overall, there was a $5.9 million decrease in cash in fiscal year 2006 compared to 2005. Cash outflows from operating activities increased by $4.0 million from the prior year. The primary reason for the increase was the capitalization of the Banner project. There were also increases in cash from certain revenue lines such as Tuition and Fees and offsetting decreases in cash from expenses such as payments to employees. Cash flows from non capital financing activities went up by $1.5 million from the previous fiscal year. The primary reason for this change was an increase in State Appropriations.

Cash outflows from capital financing activities increased by $8.8 million from fiscal year 2005. The reason for this increase was due primarily to the capitalization of the Banner project, as well as, a decrease in Capital Appropriations and an increase in the purchase of capital assets. Lastly, there was an outflow of cash from investing activities of $.9 million compared to an increase of $3.6 million in fiscal year 2005. This was the result of proceeds from the sale of investments decreasing in fiscal year 2006 compared to fiscal year 2005 and a increase in the purchase of investments in fiscal year 2006.

Capital and Debt Activities

The renewal and replacement of the University's capital assets is crucial to sustaining the quality of its academic and research programs and residential life. The University continues to invest in capital assets in accordance with its long range plan, modernizing its older facilities, balanced with new construction.

Capital assets, net of depreciation increased by $12.2 million going from $76.3 million to $88.5 million, a 16.0 percent increase. Projects that were completed during fiscal year 2006 include the Johnston

Memorial Library renovation and dormitory upgrades and repairs. The University also capitalized the Banner project in fiscal year 2006.

Projects that were in progress at June 30, 2006, include repairs to Sanitation and Sewer System, Rogers Stadium Renovation, construction of the new Engineering and Technology Building, improvement to Handicap Access, and the Gandy Hall Renovation.

Proper management of University resources requires the prudent use of debt to finance capital projects. University bonds are issued pursuant to Section 9(c) of Article X of the Constitution of Virginia. Most of the bonds at the University are Section 9(c) bonds and are backed by the full faith, credit and taxing power of the Commonwealth.

Statement of Auxiliary Enterprise Revenue, Expenditures and Change in Fund Balances

Overall, the fund balance of the Auxiliary Enterprise units increased by $6.0 million from the prior year. Most of the increase occurred in three areas, Food Services ($0.6 million), Residential Services ($2.0 million), and Reserves ($2.1 million.). The increase in the Food Services, Residential Services, and Reserves balances was due primarily to the increase in student fees applicable to these areas.

These fund balances will be partially used to fund new on-campus residential housing and a new dining facility. These projects are essential to the future of the University by keeping it competitive. Funds generated by the University's Auxiliary Enterprise functions are also used to cover current and future debt service.

Looking to the Future

In Fall 2004, the University's Board of Visitors approved the 20/20 Vision Plan – a long-range plan for the University. This plan is intended to guide the course of the University for approximately 16 years – through the year 2020. The plan contains Goals and Objectives and Action Items in nine different areas. The plan contains short, mid, and long range goals and objectives, many of which have been accomplished and work is continuing on the remainder. The University is also reviewing the current Goals and Objectives and Action Items to ensure that they are all in accordance with the current and future environment. This will continue throughout this process.

In order to remain competitive, the University must continue to enhance, renew and replace its physical plant. During fiscal year 2007, the new Engineering and Technology Building will be completed. Renovations are also underway for Gandy Hall, Rogers Stadium, and several other buildings. In October 2006, the University started the Gateway I project, a new residence hall and dining facility. This project is expected to be completed in the summer of 2007. Requests are being made in 2007 for the funding of Gateway II, a 500 bed project (the replacement of Student Village) and the replacement of the existing Howard Hall, a 464 bed project. These housing offerings will allow the University to remain competitive with other Universities and will address a critical need for on-campus suite style housing.

In the fall of 2007, the University will begin the process for re-accreditation by the Southern Association of Colleges and Schools. The off-site review will occur in October 2007 and the on-site review is scheduled in early 2008. The entire campus is mobilized for a successful conclusion of this review.

Future Economic Outlook

The Executive Management of Virginia State University believes that the University is well positioned to maintain and strengthen its financial position, and to continue to provide excellent services and programs to its students and other constituents. Part of this optimism stems from the continuing strength in its financial performance as evidenced by the accompanying financial statements.

A major factor in the University's overall financial health and future expectations is the result of the relationship with the Commonwealth of Virginia and the financial support it provides through the State Appropriations. Almost all State Universities operate at a loss prior to the recognition of State General Fund dollars. In Virginia State University's case, the University had an operating loss of $37.1 million. State general fund support has increased from $34.1 million in fiscal year 2005 to $37.0 million in fiscal year 2006. The University is very thankful for the continued support from the Commonwealth and is hopeful that the Governor and General Assembly will continue to provide needed state support.

FINANCIAL STATEMENTS

VIRGINIA STATE UNIVERSITY
STATEMENT OF NET ASSETS
As of June 30, 2006

		Component Units	
	University	VSUF	VSUREF
ASSETS			
Current assets:			
Cash and cash equivalents (Note 2)	$ 24,281,445	$ 508,098	$ 1,588,084
Cash and cash equivalents - Securities lending (Note 2)	3,792,812	-	-
Short-term investments (Note 2)	3,753,423	5,321,096	49,667
Accounts and loans receivable, net of allowance (Note 3)	2,181,476	-	143,607
Due from the Commonwealth (Note 3)	418,773	-	-
Due from affiliates	-	119,652	-
Prepaid expenses	2,171,741	-	278
Notes and mortgages receivable net of allowance, (Note 3)	82,161	-	-
Total current assets	36,681,831	5,948,846	1,781,636
Noncurrent assets:			
Restricted cash and cash equivalents (Note 2)	30,121,423	-	1,058,020
Restricted investments (Note 2)	161,077	-	-
Endowment investments (Note 2)	10,390,896	-	-
Notes and mortgages receivable, net of allowance (Note 3)	2,468,841	-	-
Other long-term investments (Note 2)	869,311	-	-
Unamortized issuance cost	36,081	-	578,694
Gain on advance refunding	2,322	-	-
Nondepreciable capital assets (Note 4)	22,032,521	-	542,828
Depreciable capital assets, net (Note 4)	66,467,985	-	13,628,979
Total noncurrent assets	132,550,457		15,808,521
Total assets	169,232,288	5,948,846	17,590,157
LIABILITIES			
Current liabilities:			
Accounts payable and accrued liabilities (Note 5)	5,539,066	61,246	88,577
Due to affiliates	-	-	214,279
Deferred revenue	3,786,316	-	16,803
Retainage payable	572,596	-	-
Obligations under securities lending (Note 2)	7,546,235	-	-
Deposits held in custody for others	1,133,716	-	178,553
Long-term liabilities - current portion (Notes 6 and 7)	2,460,719	-	265,000
Other current liabilities	69,886	-	998,209
Total current liabilities	21,108,534	61,246	1,761,421
Non-current liabilities:			
Long-term liabilities - noncurrent (Notes 6 and7)	19,059,646	-	18,693,497
Total liabilities	40,168,180	61,246	20,454,918

VIRGINIA STATE UNIVERSITY
STATEMENT OF NET ASSETS
As of June 30, 2006

		Component Units	
	University	VSUF	VSUREF
NET ASSETS			
Invested in capital assets (net of related debt)	77,618,521	-	-
Restricted for:			
Nonexpendable:			
Scholarships and fellowships	1,549,899	-	-
Instructional	440,609	-	-
Other	192,437	3,723,946	-
Expendable:			
Scholarships and fellowships	8,422,313	-	-
Instruction	194,495	-	-
Loans	755,601	-	-
Capital projects	16,678,738	-	-
Other	784,790	497,092	-
Unrestricted	22,426,705	1,666,562	(2,864,761)
Total net assets	$ 129,064,108	$ 5,887,600	$ (2,864,761)

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

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VIRGINIA STATE UNIVERSITY
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
For the Year Ended June 30, 2006

	University	Component Units VSUF	Component Units VSUREF
Operating revenues:			
Student tuition and fees, net of scholarship allowances of $5,377,721	$ 16,832,837	$ -	$ -
Federal grants and contracts	20,038,082	-	-
State and local grants and contracts	658,646	-	-
Sales and services - educational departments	20,387	-	-
Sales and service - auxiliary enterprises, net of scholarship			-
allowance of $6,187,467	20,209,125	-	-
Other operating revenues	44,174	-	2,358,151
Total operating revenues	57,803,251	-	2,358,151
Operating expenses: (Note 9)			
Education and general:			
Instruction	25,822,188	-	-
Research	3,005,792	49,133	-
Public service	6,327,739	-	-
Academic support	4,949,646	-	-
Student services	4,003,021	-	-
Institutional support	8,381,693	248,619	1,013,875
Operation and maintenance of plant	13,610,409	-	-
Scholarships and fellowships	1,309,358	301,423	-
Auxiliary enterprises	17,801,762	-	-
Other Operating Expense	56,969	-	
Depreciation	9,614,446	-	785,631
Total operating expenses	94,883,023	599,175	1,799,506
Operating income/(loss)	(37,079,772)	(599,175)	558,645
Nonoperating revenues/(expenses):			
State appropriations (Note 8)	37,011,649	-	-
Gifts	1,206,470	265,159	-
Investment income	456,894	156,670	49,556
Interest on capital asset-related debt	(698,821)	-	-
Interest on indebtness	(20,840)	-	295,427
Loss on disposal of assets	(6,385)	-	-
Other nonoperating revenues	828,001	-	138,705
Other nonoperating expenses	(218,283)	(61,630)	-
Net nonoperating revenue	38,558,685	360,199	483,688
Income before other revenues	1,478,913	(238,976)	1,042,333
Capital appropriations	4,614,000	-	-
Capital grants and gifts	418,773	-	-
Additions to permanent endowments	299,433	568,203	-
Total other revenues	5,332,206	568,203	-
Increase in net assets	6,811,119	329,227	1,042,333
Net assets, beginning of year	122,252,989	5,558,373	(3,907,094)
Net assets, end of year	$ 129,064,108	$ 5,887,600	$ (2,864,761)

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

VIRGINIA STATE UNIVERSITY
STATEMENT OF CASH FLOWS
For the Year Ended June 30, 2006

Cash flows from operating activities:		
Tuition and fees	$	17,260,007
Grants and contracts		22,146,175
Auxiliary enterprises		20,129,038
Other revenues		259,260
Payments to employees		(51,210,002)
Payments to suppliers		(25,376,387)
Payments for utilities		(5,348,676)
Payments for scholarships and fellowships		(3,008,596)
Loans issued to students		(421,609)
Collection of loans from students		292,622
Other payments		195,669
Net cash used by operating activities		(25,082,499)
Cash flows from noncapital financing activities:		
State appropriations		37,011,649
Gifts		1,505,903
Other nonoperating revenue		609,718
Loss on disposal of assets		(6,385)
Funds held in custody for others - receipts		9,973,271
Funds held in custody for others - disbursements		(9,939,458)
Federal direct lending program receipts		21,511,537
Federal direct lending program disbursements		(22,038,230)
Net cash provided by noncapital financing activities		38,628,005
Cash flows from capital financing activities:		
Capital appropriations		4,614,000
Capital gifts and grants		418,773
Interest paid on capital debt, leases, and installments		(681,876)
Principal paid on capital debt, leases, and installments		(1,280,390)
Principal received on capital debt, leases, and installments		4,315,010
Purchase of capital assets		(21,732,234)
Net cash used by capital financing activities		(14,346,717)
Cash flows from investing activities:		
Investment income		456,894
Proceeds from sales and maturities of investments		176,074
Purchase of investments		(1,542,993)
Net cash used by investing activities		(910,025)
Net decrease in cash		(1,711,236)
Cash and cash equivalents - beginning of the year		56,114,104
Cash and cash equivalents - end of the year	$	54,402,868

VIRGINIA STATE UNIVERSITY
STATEMENT OF CASH FLOWS
For the Year Ended June 30, 2006

Reconciliation of net operating loss to net cash used by operating activities		
Operating loss	$	(37,079,772)
Adjustments to reconcile net cash used by operating activities:		
Depreciation expense		9,614,446
Changes in assets and liabilities:		
Receivables, net		1,159,356
Inventory		440,336
Prepaid expenses		(13,172)
Other assets		(14,722)
Accounts payable		(64,467)
Interest payable		(37,781)
Deferred revenue		831,873
Other liabilities		210,391
Net loans		(128,987)
Net cash used by operating activities	$	(25,082,499)
Noncash investing, capital, and financing activities:		
Loss on disposal of assets	$	(6,385)
Change in fair value of investments recognized as a component of income	$	168,885
Principal and interest on capital debt paid by state agency on behalf of the University	$	540,053

The accompanying Notes to Financial Statements are in intergral part of this statement.

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NOTES TO FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

Virginia State University (the University), founded in 1882, is one of two land grant universities in the state, having been so designated in 1920. As a land grant institution, the University engages in natural resource related research projects and agricultural extension services. The institution attained university status in 1979. The University offers programs at the doctoral, graduate, and undergraduate levels in science, education, humanities, social sciences, and business. The University's stated mission is to prepare students to advance intellectually, socially, economically, and politically, so they and the University will make significant contributions to the enhancement of society.

The University is a component unit of the Commonwealth of Virginia and is included in the Comprehensive Annual Financial Report (CAFR) of the Commonwealth. These basic financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB) applicable to colleges and universities. They are prepared for and at the direction of the Commonwealth of Virginia for inclusion in the Commonwealth's CAFR, which includes all agencies, boards, commissions, and authorities associated with the Commonwealth over which the Commonwealth exercises or has the ability to exercise oversight authority.

The Virginia State University Foundation (VSUF) is a legally separate component unit of the University and was organized as a tax-exempt charitable and educational organization in 1968. The purpose of this foundation is to accept contributions from individual donors and to safeguard, invest, and distribute the funds as designated by the donors or the Foundation's Board of Trustees for the benefit of the University, its students, alumni, and educational community in support of the University's mission.

The Virginia State University Real Estate Foundation (VSUREF) is a legally separate component unit of the University and was organized as a tax-exempt charitable and educational organization in 2002. Operations began in August 2003. The purpose of the Foundation is to construct and manage the University Apartments at Ettrick (UAE), a 504-bedroom dormitory facility for the University, in support of the University's mission.

Although the University does not control the timing or amount of receipts from either the VSUF or the VSUREF, the majority of the resources or income thereof that both foundations hold and invest is restricted to the activities of the University by the donors. Because these restricted resources held by the foundation can only be used by, or for the benefit of, the University, the VSUF and the VSUREF are considered component units of the University and are discretely presented in the University's financial statements.

During the year ended June 30, 2006, the VSUF distributed $535,933 to the University for both restricted and unrestricted purposes. Separate financial statements for the VSUF can be obtained by writing Virginia State University Foundation c/o Larry Saunders & Associates, CPAs, 2902 Chamberlayne Avenue, Richmond, VA 23222. Separate financial statements for the VSUREF can be obtained by writing Virginia State University Real Estate Foundation c/o Vice President of Development, Storum Hall, P.O. Box 9027, Petersburg, VA 23806.

B. Basis of Presentation

The University's accounting policies conform with generally accepted accounting principles as prescribed by GASB, including all applicable GASB pronouncements, as well as applicable Financial Accounting Standards Board (FASB) statements and interpretations, Accounting Principles Board opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. The financial statements have been prepared in accordance with GASB Statement 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, and GASB Statement 35, *Basic Financial Statements and Management's Discussion and Analysis of Public Colleges and Universities.*

The VSUF and the VSUREF 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 and presentation features. No modifications have been made to the foundations' information in the University's financial reporting entity for these differences.

C. Basis of Accounting

The University's financial statements have been prepared 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 a liability has been incurred, regardless of the timing of related cash flows. All significant intra-agency transactions have been eliminated.

Effective with fiscal year 2006, the University was required to implement GASB Statement 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recovery*. This statement requires universities to account for and report the impairment of capital assets which currently are written down only through the process of depreciation. Asset impairment is defined as a significant, unexpected decline in the service utility of a capital asset. The University does not have any assets which needed to be written down as a result of this new standard during fiscal year 2006.

D. Cash Equivalents

The University considers all highly liquid investments with an original maturity of 90 days or less to be cash equivalents. Funds invested through the State Non-Arbitrage Program (SNAP) and portions of the funds invested in the State Securities Lending Program are considered cash equivalents.

E. Investments

In accordance with GASB Statement 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, investments are recorded at fair market value at June 30, 2006. 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.

F. Prepaid Expenses

The University capitalized periodical subscriptions, membership dues, and conference registrations for fiscal year 2007, that were paid in advance as of June 30, 2006.

G. Capital Assets

Capital assets consisting of land, buildings, equipment, infrastructure assets, improvements other than buildings, inexhaustible works of art, and construction-in-progress are stated at appraised historical cost or actual cost, where determinable. Purchased or constructed capital assets are reported at actual cost or estimated historical cost. Donated capital assets are reported at fair value on the date of acquisition. Library materials are valued using purchase price for library acquisitions. Equipment is capitalized when the acquisition cost is $5,000 or greater and the estimated useful life is two years or more. Expenses for construction-in-progress are capitalized as incurred. Interest expense of $161,668 relating to construction was capitalized, net of interest income earned on resources set aside for this purpose, for the year ended June 30, 2006. Infrastructure assets are recorded at cost. Depreciation is calculated using the straight-line method over the estimated useful live as follows:

Buildings	40-50 years
Infrastructure assets	15-20 years
Equipment	2-10 years
Banner administrative systems	5 years
Library books	5 years
Other improvements	20 years

H. Restricted and Unrestricted Net Assets

Resources restricted by outside sources are distinguished from unrestricted resources allocated for specific purposes by action of the Board of Visitors. Externally-restricted resources may be utilized only in accordance with the purposes established by the source of such resources and are in contrast with unrestricted resources, of which the governing board retains full control to use in achieving the institutional purpose.

Restricted net assets can be expendable or nonexpendable. Nonexpendable restricted net assets are endowments and similar type funds where the donor(s) or some other outside source has stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to principal. Expendable restricted net assets are resources which the University is legally or contractually obligated to spend in accordance with the restrictions imposed by external parties.

Unrestricted net assets are resources derived primarily from state appropriations, sales and services of educational departments, student tuition and fees, auxiliary enterprises fees and revenues, and gifts. Auxiliary enterprises are self-supporting activities that provide services for students, faculty, and staff. These unrestricted resources are used for transactions relating to the educational and general operations of the University and at the discretion of the governing board to meet current expenses.

When an expense has been incurred that can be paid using either restricted or unrestricted resources, the University's policy is first to apply the expense toward restricted resources and then toward unrestricted. Restricted funds remain classified as such until restrictions have been satisfied.

I. Deferred Revenue

Deferred revenue represents revenues collected, but not earned as of June 30, 2006. This consists primarily of student tuition and fees received in advance of the academic term and advance payments from grant and contract sponsors.

J. Accrued Compensated Absences

The amount of leave earned, but not taken by 12-month faculty and salaried employees is recorded as a liability on the Statement of Net Assets. The amount reflects all unused vacation leave, overtime leave, compensatory leave, and the amount payable upon termination under the Commonwealth of Virginia's sick leave payout policy as of June 30, 2006. The applicable share of employer-related taxes payable on eventual termination payments is also included.

K. Revenue and Expense Classifications

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

Nonoperating revenues include activities that have the characteristics of nonexchange transactions such as gifts and other revenue sources that are defined as non operating revenues by GASB Statement 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting,* and GASB Statement 34, *Basic Financial Statements – and Management's Discussion and Analysis*, such as state appropriations and investment and interest income.

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

L. Discounts, Premiums, and Bond Issuance Costs

Bonds payable on the Statement of Net Assets are reported net of related discount and premiums, which are expensed over the life of the bond. Bond issuance costs are expensed as incurred.

M. Scholarship Allowances

Student tuition and fee revenues, and certain other revenues from students, are reported net of scholarship allowance in the Statement of Revenues, Expenses, and Change in Net Assets. Scholarship allowance is the difference between the stated charge for goods and services provided by the University and the amount paid by students and/or third parties making payments on the students' behalf. Financial aid to students is reported using the alternative method as recommended by the National Association of College and University Business Officer (NACUBO). The alternative method is a simple proportionality algorithm that computes scholarships allowance on a University-wide basis by allocating the amounts applied to student's accounts and the cash payment to students, excluding payments for services, on the ratio of total aid to the aid not considered to be third-party aid.

N. Federal Financial Assistance Programs

The University participates in federally funded programs such as Pell Grants, Supplemental Educational Opportunity Grants, Federal Work-Study, and the Perkins Loan 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.*

2. CASH AND CASH EQUIVALENTS AND INVESTMENTS

A. Cash and Cash Equivalents

Pursuant to Section 2.2-1800, et seq., Code of Virginia (1950) as amended, all state funds of the University are held by the Treasurer of Virginia, who is responsible for the collection, disbursement, custody, and investment of state funds. Cash deposits held by the University are maintained in accounts that are covered by federal depository insurance or collateralized in accordance with the Virginia Security for Public Deposits Act, Section 2.2-4400 of the Code of Virginia. In accordance with the GASB Statement 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds,* definition of cash and cash equivalents, cash represents cash with the Treasurer of Virginia, cash on hand, and cash deposits including certificates of deposit and temporary investments with original maturities of three months or less. At June 30, 2006, the carrying amount of cash and cash equivalents was $58,195,680.

B. Investments - Credit Risk, Custodial Credit Risk, and Interest Rate Risk

The University evaluates common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. The following disclosures are made in accordance with GASB Statement 40, *Deposit and Investment Risk Disclosures*. As an element of interest rate risk, this statement requires certain disclosures of investments with fair values that are highly sensitive to changes in interest rates. Deposit and investment policies related to the risks identified in this statement must be disclosed. GASB Statement 40 also modifies disclosures required by GASB Statement 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*.

In June 2006, the University transferred its primary endowment holding from Smith Barney Citigroup to the University of Richmond Spider Management Group in accordance with Board of Visitors actions. The endowment allocation policy currently provides for the break down and percentage allocations reflected below. The Spider Management Group utilizes a different allocation basis. The University's Board of Visitors is making changes in the Endowment Allocation policy to bring it in line with the University of Richmond policy.

As of June 30, 2006, the University had the following investments:

Investments	
Spider Management Group	$ 11,079,016
Wachovia	342,268
Securities lending	7,546,235
Total investments	$ 18,967,519

Investments held by the Treasurer of Virginia include the University's allocated share of securities totaling $7,546,235 received for securities lending transactions and 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 CAFR.

C. Interest Rate Risk

The following information is provided with respect to the credit risk associated with the University's cash and cash equivalents and investments at June 30, 2006. Interest rate risk is the risk that changes in interest rates will adversely affect the fair market value of an investment. The University's policy for investment of endowment fund assets requires that the investments be allocated as follows:

Allocation of Investments	
U.S. large cap stocks	45 - 55%
U.S. small cap stocks	0 - 15%
International stocks	0 - 15%
Fixed income	20 - 40%
Cash and short-term investments	0 - 30%

This asset allocation helps limit the University's exposure to interest rate risk.

D. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation. Statutes authorize the investment of local funds held by the University in obligations of the Commonwealth; federal government; other states or political subdivisions thereof; Virginia political subdivisions; the International Bank for Reconstruction and Development; the Asian Development Bank; and the African Development Bank. In addition, the University may invest in prime quality commercial paper rated Prime 1 by Moody's Investment Service or A-1 by Standard and Poor's, Incorporated. The University may also invest in overnight term or open repurchase agreements and money market funds.

E. Custodial Credit Risk

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty, the endowment funds will not be able to recover the value of the investments that are in possession of an outside party. The University does not have a formal investment policy for custodial arrangements. At June 30, 2006, the University endowment funds were held at the custodial banks, the Spider Management Group and Wachovia.

F. Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government or university in a single issuer. The University does not have a formal policy to reduce concentration of credit risk; however, all of the University's investments were held in various instruments and stocks and were not exposed to this risk.

G. VSUF – Cash and Investments

The investments of the VSUF consist primarily of equity securities and mutual funds. All investments are stated at fair value as reported by investment managers and reflect readily determinable market prices. All investments are considered available for sale. Realized gains are calculated based on the difference between the costs and selling price of the security. The amount of cash and short term investments held by the Foundation at June 30, 2006, was $5,829,194.

H. VSUREF - Cash and Investments

The investments of the VSUREF consist primarily of U.S. government money market funds. All investments are stated at fair value as reported by investment managers and reflect readily determinable market prices. All investments are considered available for sale. Realized gains are calculated based on the difference between the costs and selling price of the security. Cost is determined based on the initial purchase price of each individual investment. The amount of cash and short term investments held by the Foundation at June 30, 2006, was $1,637,751.

3. ACCOUNTS RECEIVABLE AND NOTES RECEIVABLE

A. Accounts Receivable

Accounts receivable is shown net of allowance for doubtful accounts in the accompanying Statement of Net Assets.

At June 30, 2006, accounts receivable consisted of the following:

Student tuition and fees	$ 391,583
Federal, state and private grants and contracts	1,130,520
Auxiliary enterprises	111,563
Pledges	199,990
University apartments at Ettrick	175,280
Third party receivables - students	138,492
Non sufficient fund checks	84,875
Other receivables	48,929
Due from VSUREF	76,041
Due from VSUF	2,520
Total	2,359,793
Less: allowance for doubtful accounts	(178,317)
Net accounts receivable	$ 2,181,476

Pledges receivable represent pledges of financial support from corporations, foundations, and individuals. Pledges are recorded as gifts and certain pledges are recorded at present value using a discount rate of five percent. Allowance for doubtful accounts includes an allowance on pledges receivable amounting to $45,647.

B. Due from the Commonwealth

Receivables due from the Commonwealth represent reimbursements due for equipment purchases made by the University under the Equipment Trust Fund Program. On a reimbursement basis, this program provides state-supported institutions of higher education with bond proceeds for financing the acquisition and replacement of instructional and research equipment. Due from the Commonwealth shown on the Statement of Net Assets at June 30, 2006, is $418,773.

C. Notes Receivable

Notes receivable are shown net of allowance for doubtful accounts in the accompanying Statement of Net Assets.

At June 30, 2006, notes receivable consisted of the following:

Current notes receivable:	
Federal student loans	$ 87,391
Less: Allowance for doubtful accounts	5,230
Net current notes receivable	82,161
Noncurrent notes receivables:	
Federal student loans	1,784,337
Less: Allowance for doubtful accounts	178,452
Net federal student loans	1,605,885
JPI Apartment Development, LLP	25,000
VSU Real Estate Foundation	837,956
Total noncurrent notes receivables	2,468,841
Total notes receivable	$ 2,551,002

4. CAPITAL ASSETS

A summary of changes in the various capital asset categories for the year ending June 30, 2006, is presented as follows:

	Beginning Balance	Increase	Decrease	Ending Balance
Nondepreciable capital assets:				
Land	$ 267,084	$ -	$ -	$ 267,084
Inexhaustible works of art and/ or historical treasures	354,645	-	-	354,645
Construction in progress	29,454,847	15,505,360	(23,549,415)	21,410,792
Total nondepreciable capital assets	30,076,576	15,505,360	(23,549,415)	22,032,521
Depreciable capital assets:				
Buildings	96,442,305	22,827,543	(27,364)	119,242,484
Equipment	23,837,574	3,175,964	(68,055)	26,945,483
Banner administrative systems	-	2,216,884	-	2,216,884
Infrastructure assets	8,786,152	-	-	8,786,152
Improvements other than buildings	3,929,821	1,026,530	-	4,956,351
Library books	17,166,774	656,205	-	17,822,979
Total depreciable capital assets	150,162,626	29,903,126	(95,419)	179,970,333

Less accumulated depreciation for:				
Building	65,640,935	6,168,209	(20,979)	71,788,165
Equipment	16,132,770	1,967,461	(68,055)	18,032,176
Infrastructure assets	6,249,768	301,352	-	6,551,120
Improvements other than buildings	1,569,243	234,028	-	1,803,271
Library books	14,384,220	943,396	-	15,327,616
Total accumulated depreciation	103,976,936	9,614,446	(89,034)	113,502,348
Depreciable capital assets, net	46,185,690	20,288,680	(6,385)	66,467,985
Total capital assets, net	$ 76,262,266	$ 35,794,040	$(23,555,800)	$ 88,500,506

Net capital assets of the VSUREF consist of $542,828 for Land and $13,628,979 (net of accumulated depreciation of $1,642,794) for Buildings, Land Improvements, and Equipment as of June 30, 2006.

5. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities consist of the following at June 30, 2006:

Employee salaries, wages, and fringe benefits payable	$ 638,526
Matured interest payable	168,539
Vendor and supplies accounts payable	4,732,001
Total	$ 5,539,066

6. LONG-TERM LIABILITIES

The University's noncurrent liabilities consist of long-term debt (further described in Note 7) and other noncurrent liabilities. A summary of changes in non-current liabilities for the year ending June 30, 2006, is presented as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion	Noncurrent
Long-term debt:						
General obligation revenue bonds	$ 5,596,994	$ 255,000	$ (990,000)	$ 4,861,994	$ 775,682	$ 4,086,312
Notes payable	8,270,183	4,060,010	(270,430)	12,059,763	475,588	11,584,175
Installment purchases	114,696	-	(19,960)	94,736	20,647	74,089
Total long-term debt	13,981,873	4,315,010	(1,280,390)	17,016,493	1,271,917	15,744,576
Other noncurrent liabilities:						
Accrued compensated absences	2,852,258	1,536,034	(1,357,980)	3,030,312	1,188,802	1,841,510
Federal Perkins Loan contributions	1,453,900	19,660	-	1,473,560	-	1,473,560
Total long-term liabilities	$18,288,031	$5,870,704	$(2,638,370)	$ 21,520,365	$2,460,719	$19,059,646

7. LONG-TERM INDEBTEDNESS

A. Bonds Payable

The University's bonds are issued pursuant to Section 9 of Article X of the Constitution of Virginia. All of the bonds at the University are Section 9(c) bonds. These bonds are backed by the full faith, credit and taxing power of the Commonwealth, and are issued to finance capital projects which, when completed, will generate revenue to repay the debt.

The University had a total of $4,861,994 in bonds outstanding at June 30, 2006. Aggregate annual maturities of bonds payable for fiscal years after 2006 are:

	Interest Rate	Maturity	Total
General obligation revenue bonds:			
Jones Dining Hall Project, Series 2006R	4% - 5%	2008	$ 255,000
Foster Hall Project, Series 1995	4% - 5%	2010	185,000
Langston Hall Project, Series 1995	4% - 5%	2010	205,000
Dorm Renovation Project, Series 1995	4% - 5%	2010	215,000
Foster Hall Project, Series 2002R	4% - 5%	2010	592,102
Langston Hall Project, Series 2002R	4% - 5%	2010	660,832
Dorm Renovation Project, Series 2002R	4% - 5%	2010	690,169
Jones Dining Hall Project, Series 2002R	4% - 5%	2016	1,357,553
Jones Dining Hall Project, Series 1998	4% - 5%	2018	95,000
Jones Dining Hall Project, Series 2004R	4% - 5%	2018	606,338
Total bonds payable			$ 4,861,994

Aggregate annual maturities of bonds payable for fiscal years after 2006 are:

Maturity	Principal	Interest	Total
2007	$ 775,682	$ 226,818	$ 1,002,500
2008	777,842	190,339	968,181
2009	852,694	154,666	1,007,360
2010	891,521	120,102	1,011,623
2011	206,191	75,525	281,716
2012 - 2016	1,213,121	210,357	1,423,478
2017 - 2018	144,943	9,402	154,345
Total	$ 4,861,994	$ 987,209	$ 5,849,203

B. Prior Year Defeasance of Debt

In prior years, the Commonwealth of Virginia, on behalf of the University issued refunding general obligation bonds to pay off earlier debit. Proceeds were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the refunded bonds. As a result, the bonds refunded are considered defeased and are not reflected in the University's financial statements. At June 30, 2006, $4,190,000 of bonds that were considered defeased were still outstanding.

C. Notes Payable

The University entered into a loan agreement with the Department of Housing and Urban Development (HUD) in 1989 and closed the agreement in 1992 to borrow funds to repair seven dormitories. The loan is to be repaid over 30 years at three percent interest and is secured by a lien on the net revenues from the ownership, operation, and use of the seven dormitories under repair. In prior years and in fiscal year 2006, the University participated in the Virginia College Building Authority (VCBA) Pooled Bond Program to fund the renovation of Rogers Stadium and the Student Village Housing Renovation Project (the "2005A Project"). The 2005A bonds have a last maturity date of September 9, 2025 with a true interest cost of 4.27 percent. The bonds were sold at a premium resulting in combined available funds of $4,060,010. The par amount is $3,840,000 with a net premium of $499,024. At June 30, 2006, the outstanding balances were $2,270,685 for the HUD loan and $9,290,054 for the VCBA notes payable.

A summary of future principal and interest requirements of the HUD loan and VCBA notes payable as of June 30, 2006, are as follows:

Maturity	Principal	Interest	Total
2007	$ 475,588	$ 559,928	$ 1,035,516
2008	459,573	507,569	967,142
2009	478,036	487,418	965,454
2010	501,604	466,194	967,798
2011	525,279	443,863	969,142
2012 – 2016	2,990,537	1,829,886	4,820,423
2017 - 2021	3,890,122	1,048,728	4,938,850
2022 - 2026	2,240,000	213,253	2,453,253
Add: Unamortized Premium	499,024	-	499,024
Total	$ 12,059,763	$ 5,556,839	$ 17,616,602

D. Installment Purchases

In November 2003, the University entered into a seven-year lease purchase agreement with Koch Financial Corporation to provide financing of buses. The interest rate for this financing is 3.39 percent. As of June 30, 2006, there is only one bus with remaining outstanding debt.

Principal and interest payment commitments as of June 30, 2006, are as follows:

	Principal	Interest	Total
2007	$ 20,647	$ 2,889	$ 23,536
2008	21,357	2,179	23,536
2009	22,091	1,445	23,536
2010	22,851	685	23,536
2011	7,790	55	7,845
Total	$ 94,736	$ 7,253	$ 101,989

E. Foundation Debt

The VSUREF has an unsecured line of credit in the amount of $1 million. The interest consists of the London Inter Bank Offered Rate plus two percent (7.33 percent at June 30, 2006), that expires on November 30, 2006. The VSUF guarantees the credit line.

To fund construction of the University Apartments at Ettrick, the VSUREF received proceeds from Industrial Development Authority Bonds issued by Chesterfield County. The bonds consist of a Series 2002A for $17,710,000 and a Series 2002B for $480,000. The bonds were issued on November 19, 2002, and amended September 1, 2004. The bonds are collateralized by the rental property and equipment. Also, the VSUREF is required to maintain a debt service reserve. The contractual interest rates are variable (1.07 percent for Series 2002A and 1.25 percent for Series 2002B at June 30, 2006). The 2002A series matures on July 1, 2029, and the 2002B series matures on July 1, 2006. The VSUREF has agreed to prepayment terms of the principal to the Trustee with payments due on July 1 as follows:

Payments Due July 1,	Principal
2007	$ 265,000
2008	300,000
2009	340,000
2010	395,000
2011	450,000
thereafter	16,225,000
Total	$ 17,975,000

The VSUREF has entered into an interest rate swap agreement as part of the provisions of the bond agreement. Per the terms of the swap agreement, the VSUREF pays a fixed rate of interest of 3.905 percent. The interest rate swap agreements qualify as derivative financial instruments and are used to mitigate the effect of interest rate fluctuations. The Foundation accounts for the interest rate swaps as fair value hedges whereby the fair value of these contracts is reflected in other liabilities in the accompanying statement of financial position with the offsets recorded as expenses. The fair value of these contracts was a negative $213,345 at June 30, 2006. This is the amount the Foundation would have to pay to settle the interest rate swaps as of these respective dates.

In conjunction with the bond issuance, the University signed a support agreement with the VSUREF stating that the University Apartments at Ettrick Project will be an equal part of the Student Housing Program, the University will provide preferential treatment to assign 95 percent occupancy if the debt service coverage ratio is less than 1.2 to 1, and the University will limit additional housing projects.

8. STATE APPROPRIATIONS

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

The following is a summary of state appropriations received by the University for the year ended June 30, 2006:

Virginia State University:	
Original legislative appropriation:	
Education and general programs	$ 28,148,500
Higher education student financial assistance	3,108,907
Supplemental adjustments:	
Central fund appropriation transfers	401,256
Additional appropriation for change in June 24, 2006 payroll timing	651,078
State grants	31,847
Military Tuition Waiver	56,683
Banner project	250,000
Appropriation carryforward	32,711
Total University	32,680,982
VSU Cooperative Extension and Agricultural Research Services:	
Original legislative appropriation:	
Education and general programs	4,143,322
Supplemental adjustments:	
Central fund appropriation transfers	149,309
Additional appropriation for change in June 24, 2006 payroll timing	38,036
Total Extension Service	4,330,667
Total state appropriations	$ 37,011,649

9. EXPENSES BY NATURAL CLASSIFICATION

The following table shows a classification of expenses both by function, as listed in the Statement of Revenues, Expenses, and Changes in Net Assets and by natural classification, which is the basis for amounts shown in the Statement of Cash Flows.

	Salaries and Wages	Fringe Benefits	Services and Supplies	Scholarship and Fellowships	Utilities	Depreciation	Total
Instruction	$18,133,195	$ 4,862,659	$ 2,576,597	$ 103,112	$ 146,625	$ -	$25,822,188
Research	1,625,401	451,833	892,391	5,962	30,205	-	3,005,792
Public Service	2,653,260	673,501	2,783,152	34,816	183,010	-	6,327,739
Academic Support	2,989,126	714,991	1,134,233	73,574	37,722	-	4,949,646
Student Services	2,375,172	784,133	755,873	37,074	50,769	-	4,003,021
Institutional Support	5,407,925	2,012,322	807,931	10,587	142,928	-	8,381,693
Operation and Maintenance of Plant	606,525	239,812	9,977,104		2,786,968	-	13,610,409
Scholarships and Fellowships	4,214	178	62,169	1,242,797	-	-	1,309,358
Auxiliary Enterprises	3,296,698	1,448,905	9,585,036	1,500,674	1,970,449	-	17,801,762
Other	-	-	56,969	-	-	-	56,969
Depreciation	-	-	-	-	-	9,614,446	9,614,446
Total	$37,091,516	$ 11,188,334	$ 28,631,455	$ 3,008,596	$ 5,348,676	$ 9,614,446	$94,883,023

10. COMMITMENTS

As of June 30, 2006, the University was a party to construction contracts totaling approximately $34,879,415 of which $24,792,926 was incurred as of June 30, 2006.

11. RETIREMENT PLANS

A. Virginia Retirement System

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

The VRS does not measure assets and pension benefit obligations separately for individual state institutions. Therefore, all information relating to this plan is available at the statewide level in the Commonwealth's Comprehensive Annual Financial Report. The Commonwealth, not the University, has the overall responsibility for contributions to this plan. The CAFR discloses the unfunded pension benefit obligation at June 30, 2006, as well as the ten-year historical trend information showing VRS's progress in accumulating sufficient assets to pay benefits when due.

The University's total VRS contributions were $2,257,546 for the year ended June 30, 2006, which included the five percent employee contribution assumed by the employer. These contributions represent 10.5 percent of covered payroll for the year. The University's payroll costs for employees covered by the VRS for the year ended June 30, 2006, were $21,543,554. The University's total payroll costs for the year ended was $37,091,516.

B. Optional Retirement Plans

Full-time faculty and certain administrative staff may participate in two other retirement plans: 1) Fidelity Investments Institutional Services and 2) Teacher Insurance and Annuity Association/College Retirement Equity Fund. These are fixed-contribution programs where the retirement benefits received are based upon the employer and employee contributions totaling 10.4 percent, plus interest and dividends.

Individual contracts issued under these plans provide full and immediate vesting of both the University and the participants' contributions. Total pension costs under these plans were approximately $1,121,465 for the year ended June 30, 2006. Contributions to the optional retirement programs were calculated using the base salary amount of approximately $10,783,317.

C. Deferred Compensation

University employees 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 matched dollar amount 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. The University expense for contributions under the Deferred Compensation Plan, which is an amount assessed by the Commonwealth, was $170,739 for fiscal year 2006.

12. POST-EMPLOYMENT BENEFITS

The Commonwealth participates in the VRS administered statewide group life insurance programs, which provides post-employment life insurance benefits to eligible retired and terminated employees. The Commonwealth also provides health care credits against the monthly health insurance premiums for its retirees who have at least 15 years of state service and participate in the State's health plan. Information relating to these plans is available at the statewide level in the Commonwealth of Virginia's CAFR.

13. CONTINGENCIES

The University 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 University.

In addition, the University is required to comply with various regulations issued by the Office of Management and Budget. Failure to comply with these regulations may result in questions concerning the allow-ability of related direct and indirect charges pursuant to such agreements. As of June 30, 2006, the University estimates that no material liabilities will result from such audits or questions.

The University has been a defendant in several legal actions. The final outcome can not be determined at this time, but management is of the opinion that the liability, if any, for these legal actions will not have a material effect on the University's financial position.

14. RISK MANAGEMENT

The University 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 University 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 University 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 CAFR.

15. SUBSEQUENT EVENTS

In November 2006, the University issued $21,110,000 of revenue bonds, Series 2006B, to construct a new residence and dining hall. The bonds were issued through the Virginia College Building Authority Pubic Higher Education Financing Pooled Bonds Program. The bonds were issued with interest rates varying from 4 to 5 percent and will mature in 2026.

In July 2006, the University finalized an Energy Performance contract with Johnson Controls, Inc., to install improvements, upgrades and modifications to electrical, air and water management systems. The total equipment cost of this project is $2,729,129 with an interest rate of 4.32 percent and is being financed through a Master Equipment Lease Agreement. Payments on this lease agreement will begin in Fiscal Year 2008, and continue through Fiscal Year 2022.

On December 1, 2006, the Virginia State University Real Estate Foundation, repaid to the University outstanding debt of $864,279 related to the construction and operation of the University Apartments. The funding to repay this debt was obtained by issuing IDA bonds through Chesterfield County and repaying the outstanding bonds of $17,710,000 at June 30, 2006.

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SUPPLEMENTARY INFORMATION

VIRGINIA STATE UNIVERSITY
SCHEDULE OF AUXILIARY ENTERPRISES-REVENUES AND EXPENDITURES
For the Year Ended June 30, 2006

	Food Service	Bookstore	Residential Services	Parking and Transportation
Revenues:				
Student fees	$ 5,733,775	$ -	$ 8,216,522	$ -
Sales and Sservices	31,403	273,873	113,995	174,599
Interest	-	-	-	-
Miscellaneous revenue	-	(16,239)	26,776	222,594
Rental fees	-	-	197,595	-
Total revenues	5,765,178	257,634	8,554,888	397,193
Operating Expenditures:				
Personal services	-	-	905,456	56,821
Employee benefits	-	-	225,223	46,549
Total personal services and benefits	-	-	1,130,679	103,370
Other than personal services:				
Contractual services	3,731,278	7,680	1,357,125	19,639
Supplies and materials	28,173	-	123,235	(19,854)
Equipment	13,117	-	89,525	-
Current charges and obligations	(12,948)	360	577,347	(5,671)
Scholarships	-	-	523,580	-
Transfer payments	-	-	3,524	-
Indirect cost	895,146	1,824	737,383	24,409
Total other than personal services	4,654,766	9,864	3,411,719	18,523
Total operating expenditures	4,654,766	9,864	4,542,398	121,893
Excess (deficiency) of revenues over (under) operating expenditures before transfers	1,110,412	247,770	4,012,490	275,300
Transfers to other funds:				
Mandatory transfers-debt service	-	-	-	(23,535)
Nonmandatory Transfers	(511,330)	(143,212)	(1,965,579)	-
Net increase/ (decrease)	599,082	104,558	2,046,911	251,765
Fund Balance, July 1, 2005 as restated	2,129,402	212,494	3,200,474	501,250
Fund Balance, June 30, 2006	$ 2,728,484	$ 317,052	$ 5,247,385	$ 753,015

This schedule is prepared on the modified accrual basis of accounting. Purchases of capital assets are recorded as expenses and depreciation is not recorded. Management uses this method of accounting to monitor individual auxiliary enterprises and set rates.
Beginning fund balances were restated to correct for prior year errors in computing these amounts.
Other auxiliary functions includes general auxiliary administration, undistributed auxiliary fees, VSU 1Card, radio station, children's center, copy center, and other enterprises.

Tele-Communication	Student Health Services	Student Unions / Recreational Facilities	Other Auxiliary Functions	Intercollegiate Athletics	Reserves	Total
$ -	$ 25,234	$ -	$ 9,327,770	$ -	$ 735,597	$ 24,038,898
33	-	997	65,105	213,490	-	873,495
-	-	-	771,989	-	-	771,989
21,655	-	40,173	51,317	59,543	-	405,819
-	-	-	108,796	-	-	306,391
21,688	25,234	41,170	10,324,977	273,033	735,597	26,396,592
93,010	379,434	437,496	919,513	819,255	-	3,610,985
36,656	101,339	119,711	312,256	214,520	-	1,056,254
129,666	480,773	557,207	1,231,769	1,033,775	-	4,667,239
(241,995)	83,206	153,108	656,767	356,327	-	6,123,135
17,881	52,681	33,469	389,112	191,728	-	816,425
41,359	15,736	14,457	149,032	30,284	-	353,510
3,926	8,989	(43,675)	1,057,381	(30,645)	359	1,555,423
-	-	13,368	325,403	637,923	-	1,500,274
-	-	12,925	-	6,759	-	23,208
-	148,581	181,229	665,539	356,113	-	3,010,224
(178,829)	309,193	364,881	3,243,234	1,548,489	359	13,382,199
(49,163)	789,966	922,088	4,475,003	2,582,264	359	18,049,438
70,851	(764,732)	(880,919)	5,849,974	(2,309,231)	735,238	8,347,154
-	-	-	-	-	(1,410,395)	(1,433,930)
(68,844)	767,772	1,384,966	(5,479,912)	2,356,835	2,791,805	(867,499)
2,007	3,040	504,048	370,062	47,604	2,116,648	6,045,725
169,636	(46,565)	(80,503)	2,079,453	53,415	5,618,670	13,837,726
$ 171,643	$ (43,525)	$ 423,545	$ 2,449,515	$ 101,019	$ 7,735,318	$ 19,883,451

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Commonwealth of Virginia

Walter J. Kucharski, Auditor

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

April 4, 2007

The Honorable Timothy M. Kaine
Governor of Virginia

The Honorable Thomas K. Norment, Jr.
Chairman, Joint Legislative Audit
and Review Commission

Board of Visitors
Virginia State University

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

We have audited the accompanying basic financial statements of **Virginia State University**, a component unit of the Commonwealth of Virginia, and its discretely presented component units as of and for the year ended June 30, 2006, as listed in the table of contents. These financial statements are the responsibility of the University'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 University, 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 the amounts included for the component units of the University is based on the reports of the other auditors.

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

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of University and of its discretely presented component units as of June 30. 2006, 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 on pages five through 16 is not a required part of the basic financial statements, but is supplementary information required by the accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements of the University. The accompanying Schedule of Auxiliary Enterprises – Revenues and Expenditures is presented for the purpose of additional analysis and is not a required part of the basic financial statements. The Schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statement taken as a whole.

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

Internal Control over Financial Reporting

In planning and performing our audit, we considered the University's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion in the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the University's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions, entitled "Improve Financial Statement Preparation Process," and "Improve Information Security Program" are described in the section titled "Internal Control and Compliance Findings and Recommendations."

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable conditions described above are not material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the University's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance that is required to be reported under Government Auditing Standards. The instance of noncompliance, entitled "Improve Information Security Program" is described in the section titled “Internal Control and Compliance Findings and Recommendations.” There were no other matters that are required to be reported.

Status of Prior Findings

The University has taken adequate corrective action with respect to the audit findings reported in the prior year.

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

Exit Conference

We discussed this report with management at an exit conference held on April 5, 2007.

AUDITOR OF PUBLIC ACCOUNTS

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Vice President for Administration & Finance

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April 20, 2007

Mr. Walter Kucharski
Auditor of Public Accounts
P.O. Box 1295
Richmond, Virginia 23218-1295

Subject: Response to FY 2006 Audit Comments

Dear Mr. Kucharski:

Virginia State University thanks you for the opportunity to respond to the Internal Control and Compliance Findings and Recommendations related to your fiscal year 2006 audit. In accordance with Government Auditing Standards, we are providing the following response for inclusion in your published report.

Status of Project New Horizons

- Staffing: The University acknowledges that it has experienced staffing shortages during the Banner Student module implementation. As noted in the report, the University continues to add and hire additional functional and technical resources to address late data conversions using the SunGard proven conversion methodology. With additional resources, we have successfully completed the three data conversions in January. We have made significant progress with one late data conversion in a short period of time, and we are on schedule with another planned data conversion. To fully and thoroughly test the system, we have added an additional mock registration test, are planning for full AR testing, and are preparing to complete all project tasks leading up to the upcoming system integration testing in June. We have committed and dedicated resources that have and will continue to work extremely hard to complete all work scheduled.

- Project Oversight: The University has a committed Project Manager to provide project management oversight and also has contracted with SunGard Project Management for project implementation services. The University continues to manage and monitor SunGard's service delivery, contract performance, project risks, and issues to ensure that the project remains on schedule, within scope and budget.

The University appreciates the APA's acknowledgement of the progress made to-date on this project. We are well aware of the numerous risks related to any major system implementation and are committed to dedicating the resources required for a successful implementation of Project New Horizons.

Improve Financial Statement Process

The Auditor of Public Accounts (APA) reported to University Officials that this comment was issued because the University made three adjusting journal entries (AJEs), and if the new auditing standard (SAS 112) which becomes effective next Fiscal Year 2007 (FY 07) had applied they would have reported a material weakness in internal controls. The University agrees that during the Fiscal Year 2006 (FY 06) audit that three AJEs were made after the initial statements were completed and released. However, the University has concerns about the application of the new standard to FY 06 year to yield a written comment. The three AJEs involved one transaction that did not meet the Department of Accounts materiality threshold, one capital asset recognition item with which APA was involved in ongoing discussions and of which APA was aware that it had not been recorded, and one other transaction related to the highly unusual statewide change in recording of the payroll at June 30, 2006.

The University places great emphasis and the highest priority on Financial Reporting and the statement preparation process. The University Controller personally devotes a large part of his time to the statement preparation and review process and served as the University's lead audit coordinator. Both Assistant Controllers devote significant energy and time to ensure a successful audit as well as the production of an accurate and timely set of financial statements. Aggressive efforts are underway to fill all Financial Reporting vacant positions. A new Manager of Financial Reporting was recently hired and offers are in process for two reporting analysts.

The University has a strong succession plan in place which had the following impact on the financial reporting office this year: 1) The plan allowed for the successful promotion of an internal candidate who is responsible for financial reporting; 2) The plan allowed us to transfer one of our "double fill" accounting manager positions to the financial reporting area; and 3) The plan allowed us to hire an accounting professional from a temporary agency to support the financial reporting area.

We do not believe that separation of duties is an issue in the Financial Reporting area or any of the Controller's units. APA has not made us aware of any problems related to this. We will continue to diligently monitor our procedures and staffing levels to ensure that a proper separation of duties is maintained.

Cross training is important; we will expose newly hired staff as well as existing staff to the training program in place. We are also currently focused on writing and documenting desk procedures and other policies and procedures for all of the accounting areas.

As noted above the University is committed and will continue to focus efforts on improving the Financial Reporting area.

Incomplete Information Security Program

The University acknowledges that the Auditors rated our Information Security Program as inadequate in the December 2006 report. We have taken appropriate corrective actions to improve and strengthen our Information Security Program. In November 2006, we successfully completed an Information Technology Disaster Recovery test drill to ensure University IT systems could be fully restored and University mission critical business operations could resume normal business operations in a reasonable time period. As a result of this test drill, our IT Disaster Recovery and Business Continuity plans are comprehensive, unified, and coordinate all components of the Information Security Program. The University senior management were involved and apprised of the test drill results, recommendations, and lessons learned.

Recently, the University's web site was hacked. Although the University's data was not compromised or disclosed to the public and the University network or server components were not affected, we immediately took the appropriate actions to respond. We executed our Incident Response plan and timely notified the appropriate individuals including the CIO. To ensure business continuity of operations and availability of mission critical web-operations like Student Information System and other systems, we quickly provided the University community with alternate Internet sites while the web site was becoming fully restored and operational. We believe that our plans are appropriate and worked successfully in this situation. We will, however, continue to monitor and assess the plan on an ongoing basis to determine if improvements can be made.

The University remains committed to addressing all of these findings appropriately. We would like to thank you and your staff for their continued collaboration and support in improving the University and we look forward to next year's audit.

Sincerely,

Clementine S. Cone

Clementine S. Cone
Vice President for Administration and Finance

cc: Dr. Eddie N. Moore, Jr., President
Mr. David A. Von Moll, State Comptroller
The Honorable Dr. Thomas R. Morris, Secretary of Education
Mr. Richard D. Brown, Director of Planning and Budget

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Petersburg, Virginia

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