

UNIVERSITY OF GUAM

**FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT
AND REPORT ON
SUPPLEMENTARY INFORMATION**

YEAR ENDED SEPTEMBER 30, 2006

UNIVERSITY OF GUAM

TABLE OF CONTENTS YEAR ENDED SEPTEMBER 30, 2006

	<u>Page No.</u>
INDEPENDENT AUDITORS' REPORT	1
MANAGEMENT'S DISCUSSION AND ANALYSIS	3
FINANCIAL STATEMENTS:	
Statement of Net Assets	14
Statement of Revenues, Expenses and Changes in Net Assets	16
Statement of Cash Flows	18
Notes to Financial Statements	20
ADDITIONAL INFORMATION:	
Schedule of Salaries and Wages	41
Schedule of Expenses by Object Category	42

INDEPENDENT AUDITORS' REPORT

Board of Regents
University of Guam:

We have audited the accompanying financial statements of the University of Guam (the University) (a component unit of the Government of Guam) and its discretely presented component unit as of and for the year ended September 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 an opinion on these financial statements based on our audit.

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 University of Guam Endowment Foundation were audited by other auditors, whose report thereon dated November 3, 2006 expressed an unqualified opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

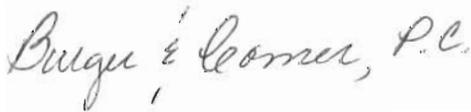
In our opinion, such financial statements present fairly, in all material respects, the respective financial position of the University of Guam and its discretely presented component unit as of September 30, 2006, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 11 to the financial statements, the University is carrying a receivable from the Government of Guam. The Government of Guam is experiencing serious financial difficulty, and has not remitted the balance reflected in the financial statements as of the date of this report. The ultimate collectibility of this receivable cannot presently be determined, but management is of the opinion that the entire balance will be collected before the end of fiscal year 2007 or shortly thereafter. Accordingly, no provision for any loss that may result has been made in the financial statements. Nevertheless, due to uncertainties with the Government of Guam's financial condition, it is at least reasonably possible that management's view of the outcome will change in the near term.

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

The Management's Discussion and Analysis on pages 3 through 13 is not a required part of the basic financial statements but is supplementary information required by 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 taken as a whole. The accompanying schedules on pages 41 through 44 are presented for purposes of additional analysis and are not required part of the basic financial statements. These schedules are the responsibility of the University of Guam's management. Such information 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 statements taken as a whole.



Burger & Comer, P.C.
Tamuning, Guam
April 26, 2007

MANAGEMENT'S DISCUSSION AND ANALYSIS

INTRODUCTION

The University of Guam is the premier institution of higher education in the Western Pacific. It operates under a University Charter and is governed by a Board of Regents. It is a public, U.S. land-grant institution accredited by the Western Association of Schools and Colleges Senior Commission (WASC). Through its mission of instruction, research and service, the University serves the communities of Guam, Micronesia, and the neighboring regions of the Pacific and Asia. The University provides a diverse and multicultural atmosphere, serving approximately 3,200 students, primarily of Asian and Pacific Islander ancestry. As a regional, comprehensive, open admissions institution, the University awards baccalaureate and master's degrees through its three colleges, i.e. Liberal Arts and Social Sciences, Natural and Applied Sciences, and Professional Studies.

The University has four interrelated, strategic initiatives: Enhancement of Academic Quality; Enhancement of Student Success, Enrollment Growth, and Institutional Visibility; Promotion of the Land-Grant Mission; and Strengthening Institutional Effectiveness and Efficiency. These strategic initiatives guide the University in being responsive to student and community needs.

The following is management's discussion and analysis (MD&A) of the University's financial performance during the fiscal year (FY) ended September 30, 2006, as compared to FY2005. It was prepared by University management and should be read in conjunction with the financial statements and related notes that follow.

THE FINANCIAL STATEMENTS

The University's financial report includes three financial statements: the Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; and the Statement of Cash Flows. The referenced financial statements were prepared in accordance with Governmental Accounting Standards Board (GASB) principles.

In FY2002, the University adopted GASB 35 with presentation of the MD&A and the consolidated financial statements; this is in contrast with fund accounting presentation in previous years. In FY2004, the University presented the University of Guam Endowment Foundation financials statements as a component unit, in compliance with GASB 39. In FY2005, the University implemented GASB 40, disclosing fair value of investments with high sensitivity to changes in interest rates.

OVERVIEW OF FY2006 AND FINANCIAL CONDITION

As a critical island resource for economic growth and social development, the University of Guam is focused on its instruction, research and service mission. This audit and the accompanying MD&A address the University's financial stewardship, capacity to deliver its mission, and progress, in the fifth year of its strategic plan, towards achieving the institution's strategic initiatives of academic quality, student success, community engagement, and institutional effectiveness and efficiency.

In evaluating the University's financial health, one of the most important questions is whether the institution is financially better off at the beginning of the year or at the end of the year. In FY2006 the University once again improved its overall financial position, as evidenced by the \$0.6 million increase in net assets from \$82.1 million in the prior year to \$82.7 million during a period of difficult financial conditions associated with the Government of Guam's significant, cumulative General Fund deficit. This is a result of prudent financial management, implementation of austerity measures, implementation of the University's financial management plan¹, and working with government leaders to maintain sustainability of operations.

The University's key financial ratios, as defined by its accrediting body, remained strong. Of particular note are the four-year positive trends in revenues and the returns on total net assets.

Financial management was difficult throughout FY2006. Finances were problematic government-wide, as the government sought to fund the deficit while facing shortfalls in actual versus appropriated revenues, increasing receivables from unpaid taxes, legal mandates to pay cost of living allowances and Earned Income Tax Credits valued at over several hundred million dollars, and the sizeable funding needs of the public school system. These conditions depleted the government's cash and led to delays and shortfalls in payments to the University, which depends upon General Fund appropriations for approximately 40% of its consolidated revenues and over 70% of its general operating revenues. The government's deficit and other financial challenges had a negative spillover impact on the University's financial situation and cash position. The government's withholding a portion of its cash allotment to its agencies evidences the problems. For the University, this meant an agreed 9.2% allotment holdback of \$2.7 million in FY2006. Prior allotment holdbacks were \$0.6 million in FY2005 and \$1.1 million in FY2003. As of fiscal year end, the University's appropriation receivable from the government was \$3.35 million. Faced with various financial problems, government leaders and the University have worked closely and cooperatively together in financial planning and monitoring .

The University's revenues increased for the fourth consecutive year. This was collectively the result of enrollment and tuition increases, an increase in federal grants and contracts reflecting six consecutive years of 12% average growth, the University's growing competitiveness for research funding, and better-than-market returns from the investment portfolio for the fourth consecutive year.

University enrollment is on the upswing. The University remains accessible and affordable, as tuition rates remain approximately 40% less than the average at other U.S. public universities. There were a total of 3,176 students (or 36,408 credit hours) in the Fall 2006 semester. This is a 5% increase in headcount enrollment and 3% increase in credit hour production over the prior year Fall semester. The University welcomed 795 new students for Fall 2006 compared to 713 for Fall 2005. The Nursing Program at the University posted

¹ As in prior years the University's financial management plan collaboratively links its budgets, expenditures and resource allocations to institutional priorities to weather economic instability facing the island and region, while maintaining commitment to its core mission and strategic initiatives. The plan addresses tuition increases, enrollment targets, revenue generation, cost containment, strategic investments and working capital management

record enrollment numbers for Fall 2006. Approximately 450 students enrolled in the pre-nursing and nursing tracks of the program compared to 330 students the prior year.

During FY2006, the Governor identified a first-ever \$1.1 million of Federal Compact Impact funds for critical infrastructure renovation projects at the University. Additionally, federal financial awards increased from \$13 million to \$16 million. New grants successfully obtained during the fiscal year include \$1.3 million (National Institute of Health) for up to four years to be used to encourage students to pursue their PhDs in biomedical research; \$0.238 million (US Department of Education) to the School of Nursing to fund equipment, supplies, for the nursing skills laboratory; and \$0.348 million (Americorps) to establish a student success tutoring/mentoring center.

Academically, the University continues to meet accreditation standards. The Capacity and Preparatory Review by the Western Association of Schools and Colleges (WASC) (January 31 – February 2, 2007) noted various accomplishments with respect to educational effectiveness, building organizational structures, and off-site programs among others. WASC highlighted assessment challenges, the need for certain core staff and the precarious financial condition of the University, which hinders its ability to sustain the delivery of effective education. The Capacity and Preparatory Review Team Report is available on the University's website and will be acted on during the June 2007 meeting of the WASC Senior Commission.

The professional schools at the University have received specialized accreditation that speaks to the quality and improvement in their programs. The International Assembly for Collegiate Schools of Business (IACBE) accredits the business program at the School of Business and Public Administration, which is also an accreditation candidate at the prestigious Association to Advance Collegiate Schools of Business (AACSB International). The National League for Nursing (NLN) and Council on Social Work Education (CSWE) accredit programs in the School of Nursing, Social Work and Health Sciences. The National Council for the Accreditation of Teacher Education (NCATE) recently accredited the School of Education. The National Association for Sport and Physical Education also accredits programs within the School of Education.

In September 2006 three new degree programs and one new certificate program were launched at the University including an Associate Degree in Nursing, a Bachelor of Arts in Sociology, a Master of Arts in English, and a Graduate Certificate in Micronesian Studies. The programs respond to community demand for new academic programming in these strategic areas.

The University made a significant institutional investment in the new 57,000 square foot Jesus and Eugenia Leon Guerrero School of Business and Public Administration Building ('Leon Guerrero Building'). The \$14.5 million building project, financed primarily through a \$13.5 million USDA Rural Development Community Facilities Loan, was occupied in July 2006. The project was certified as complete in December 2006.

The University's research, outreach, and academic programs touch the lives of almost every person in Guam's community. From farmers, to individuals caring for elderly relatives, to speech and language pathologists, the University of Guam is connected to its communities and provides the framework for quality of life improvements. The ability to serve the needs

of the region is enabled by the University's leveraging its \$27.5 million Government of Guam appropriation for operations with additional federal monies totaling \$26.1 million to fund programs such as Pell Grants and other student financial assistance; the Cancer Research Center; the Center for Excellence in Developmental Disabilities Education, Research and Service (CEDDERS); Micronesian Health and Aging; coral reef studies; and partnerships for educational improvements in our public schools. The University has requested additional local government appropriations as further leverage for such programs.

While there has been progress in meeting strategic goals, several areas require further improvement. Foremost among these is financial stability, an overriding accreditation concern. While diversifying and fortifying its overall revenues through tuition and enrollment increases, additional federal funding and investment gains, the University remains dependent on Government of Guam appropriations for over 70% of its general operations budget, which is the primary funding source for its teaching and service missions. Student learning and academic quality at the University have, therefore, been particularly susceptible to externally-driven financial problems.

Overall, the University has achieved positive outcomes in challenging financial times. These are due to collaboration and teamwork, the recognition of student learning and academic priorities implemented through a consensus-based strategic plan, the ability to make difficult decisions based on evidence, and the commitment of faculty, staff and administrators. The University continues to focus on strategic priorities, best practices, and accessible and affordable higher education for students in the delivery of its educational mission. The University's strategic focus and measurable progress position it for further growth in FY2007 and beyond.

SUMMARY STATEMENTS OF NET ASSETS (IN 000'S)

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Current assets	\$ 14,316	\$ 14,856	\$14,862
Non-current assets	<u>91,689</u>	<u>85,932</u>	<u>78,763</u>
Total assets	<u>\$ 106,005</u>	<u>\$ 100,788</u>	<u>\$93,625</u>
Current liabilities	\$ 9,194	\$ 9,871	\$8,424
Non-current liabilities	<u>14,095</u>	<u>8,788</u>	4,820
Total Liabilities	<u>\$ 23,289</u>	<u>\$ 18,659</u>	<u>\$13,244</u>
Invested in capital assets, net of related debt	\$ 62,390	\$ 60,297	61,437
Restricted	12,752	11,934	10,758
Unrestricted	<u>7,574</u>	<u>9,898</u>	8,186
Total Net assets	<u>\$ 82,716</u>	<u>\$ 82,129</u>	<u>80,381</u>
Total liabilities and net assets	<u>\$ 106,005</u>	<u>\$ 100,788</u>	<u>93,625</u>

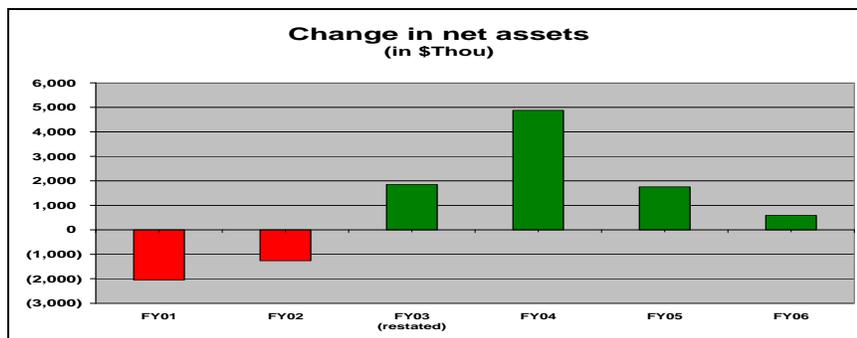
This section presents the overall financial condition of the University at fiscal year-end. Net assets increased by \$0.6 million (or 0.7% over the prior year) to \$82.7 million by end of FY2006, after adjustment for the agreed \$2.7 million allotment holdback. This is compared to the prior year increase of \$1.7 million, also adjusted for an allotment holdback of \$0.6 million.

Assets. Current Assets consist primarily of cash and equivalents (32%) and receivables (tuition 19%, local government appropriations 23%, U.S. government grants and contracts 8%, others 8%). Total current assets cover current liabilities 1.56 times, an indicator of liquidity. Noncurrent Assets consist primarily of restricted cash 4% (Tobacco Settlement Funds, Federal grants, and CIP debt service funds), investments 16% (Endowment Funds, private grants and scholarship, board restricted funds), and capital assets 80%.

Total assets increased by 5% primarily due to the completion of the Leon Guerrero Building (July 2006) and the strong investment returns. The \$14.5 million building project is financed through a \$13.5 million, 40-year, 4.5% USDA Rural Development Community Facilities Loan with debt service funded by a Capital Improvement Fund codified in PL 26-58 §26505, donor commitments from the UOG Endowment Foundation, and earnings from the International Accounting Institute affiliated with the School of Business and Public Administration. The University incurred \$1.2 million expenditures from previous years.

Liabilities. These are composed primarily of accounts payable, deferred tuition revenue, accrued employee annual and sick leave, deposits for others, and long-term debt. The net increase in total liabilities by \$4.6 million (or 25%) is primarily due to the USDA borrowing in connection with the construction of the Leon Guerrero Building.

Net Assets. Net assets represent the residual interest in the University’s assets after liabilities are deducted. The unrestricted component of net assets decreased by \$2.3 million, offset by the \$2.1 million increase in the investment in capital assets for the addition of the Leon Guerrero Building. At the end of FY2006 net assets increased by \$0.6 million marking the fourth year of positive returns, caused by combination of prudent financial management, implementation of the University’s financial management plan and austerity measures, and working with government financial leaders in financial planning and monitoring.



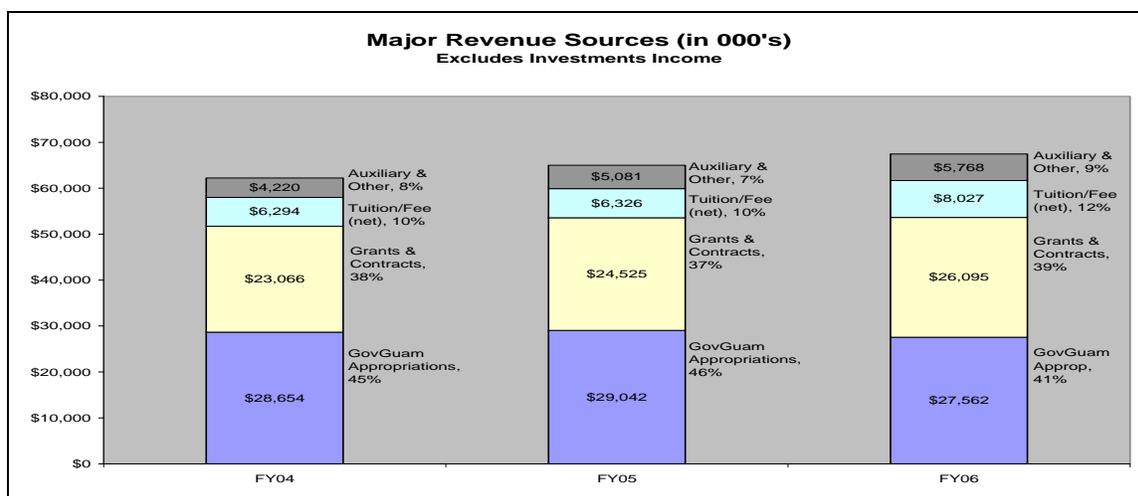
SUMMARY STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS (IN 000’S)

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Operating revenues	\$ 39,891	\$ 35,932	\$33,583
Operating expenses	<u>65,538</u>	<u>62,697</u>	<u>58,850</u>
Operating revenues net of operating expenses	(25,647)	(26,765)	(25,267)
Non-operating revenues	<u>26,234</u>	<u>28,513</u>	<u>30,144</u>
Increase in net assets	587	1,748	4,877
Net assets – beginning of year	<u>82,129</u>	<u>80,381</u>	<u>75,504</u>
Net assets – end of year	<u>\$ 82,716</u>	<u>\$ 82,129</u>	<u>\$80,381</u>

This section provides details of operating and non-operating revenues and expenditures that resulted in the \$0.6 million increase in net assets. Revenues increased while cost control measures kept expenditures within approved limits.

Revenues. The University brought in approximately \$40 million from operations (excluding government appropriations and investments). Tuition and fees, grants and contracts, auxiliary and other revenues contributed to the \$4 million (11%) increase over the prior year operating revenues. These are \$12 million higher than total government appropriations of \$28 million, reflecting continued diversification of revenue streams.

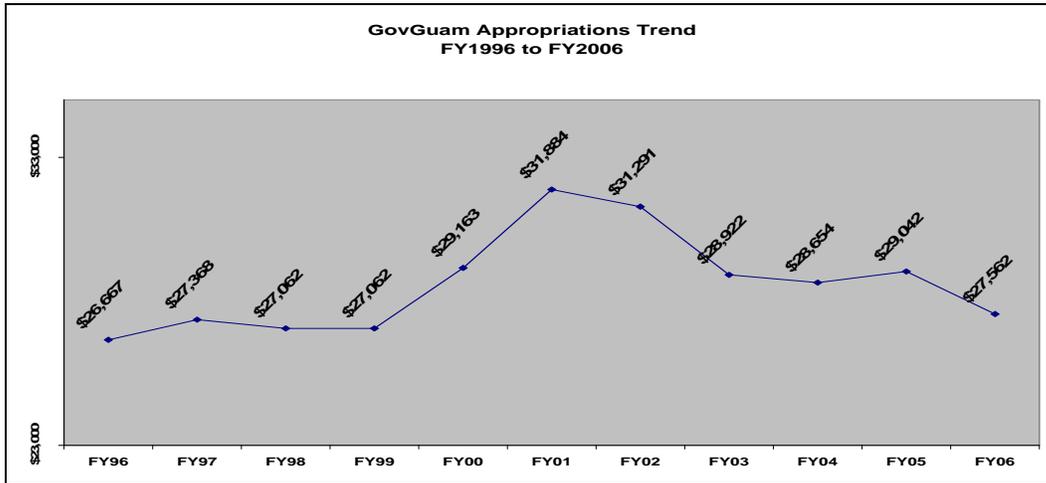
Consolidated revenues from auxiliary funds, tuition, and grant sources comprised 59% of total revenues for operations compared to 55% in FY2005. FY2006 marks the fourth year that internally generated revenues exceeded 50% of total revenues.



Highlights of Major Revenue Sources

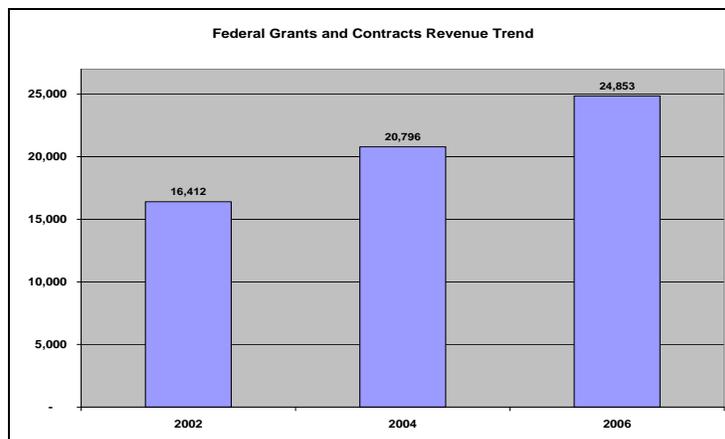
1. Government of Guam Appropriations. FY2006 appropriations totaled \$29.5 million. However, due to economic circumstances and the needs of the public school system and public health, appropriations were reduced by \$2.7 million (to \$27.6 million) in the form of allotment control.

Governments of Guam appropriations to the University topped \$32 million in FY2001 and have declined since then, placing current appropriations at the same level as FY1997. Although other revenue sources have increased, the University still depends on the government appropriations for over 70% of its general operating revenues (excluding federal grants, auxiliary funds, and other non-appropriated funds). Decrease in appropriations have not fully absorbed the increased costs, particularly legally mandated salary increments and retirement fund contributions, utility rate increases, and typhoon insurance coverage. Budget constraints, cash shortages, and allotment holdback on the funds that were appropriated have meant that needed faculty hiring for undermanned programs, student services, plant maintenance and infrastructure support for learning must be deferred or cancelled in order to allocate sufficient funds to higher priority and more immediate academic quality needs, student learning needs and legally mandated increases in operational expenditures.



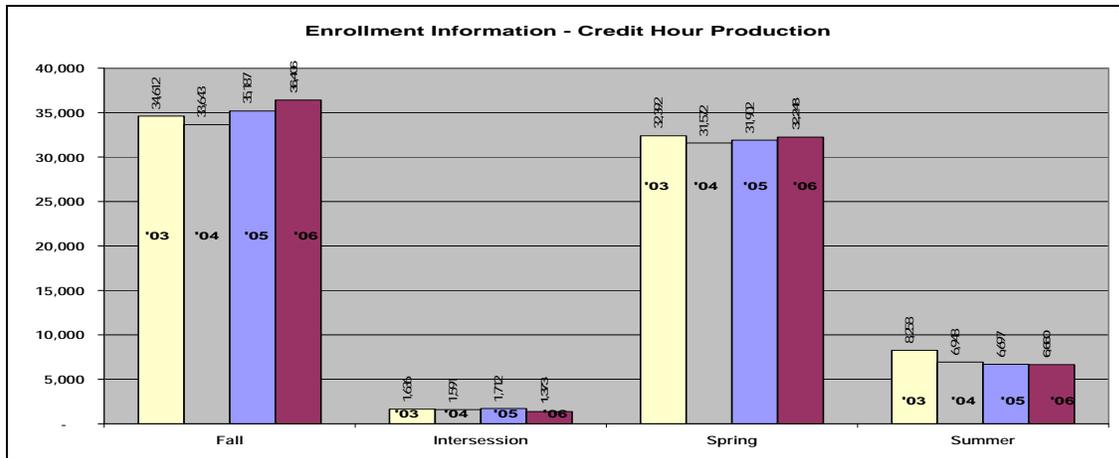
2. Grants and Contracts. Consolidated (Federal, local and private) grant and contract revenues increased by \$1.6 million in 2006, primarily from federal grants. Compared to the prior year, federal grants/contract revenues increased by \$1.5 million (6% over prior year, and an average of 12% over the last six years) to \$25 million. The trend of increased federal grant revenues is evidence that the University has become a competitive research and service institution in the region.

Federal financial awards increased from \$13 million to \$16 million in academic year 2005-2006. New grants received during FY2006 include \$1.1 million of Federal Compact Impact funds identified by the Governor’s Office for critical infrastructure renovation projects; \$1.3 million National Institute of Health funding of up to four years to encourage students to pursue their PhDs in biomedical research; \$0.238 million US Department of Education grant to the School of Nursing to fund equipment, supplies, for the nursing skills laboratory; and \$0.348 million Americorps grant to establish a student success tutoring/mentoring center.

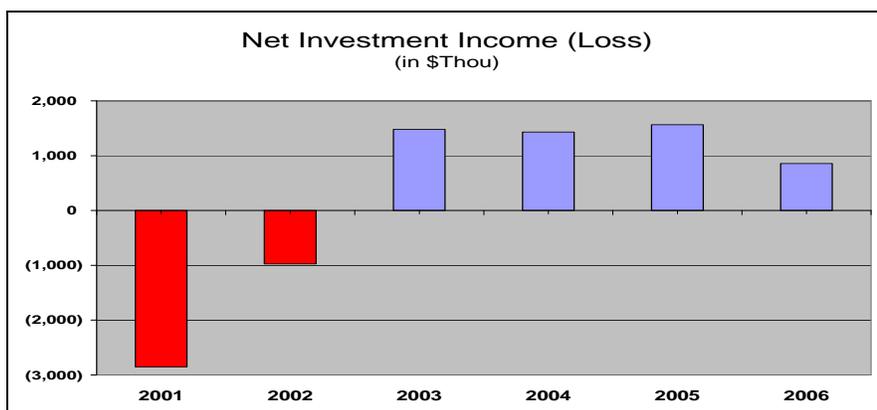


3. Tuition and Fees. Gross student tuition and fee revenues increased by \$1.3 million primarily due to increased enrollment and a 10% annual increase in tuition rates starting Fall 2005. Even with tuition rate increases, the University remains affordable and competitive with students’ paying approximately 40% less than those attending other U.S. public universities.

The University has focused on student recruitment and retention efforts. After a period of decline associated with accreditation concerns, student headcount and credit hour production are increasing. Encouraging signs are apparent in the overall increase in enrollment, in addition to the increase of new undergraduate student enrollment. There were a total of 3,176 students (or 36,408 credit hours) in the Fall 2006 semester. This is a 5% increase in headcount enrollment and 3% increase in credit hour production over the prior year Fall semester. The University welcomed 795 new students for Fall 2006 compared to 713 for Fall 2005. The Nursing Program at the University posted record enrollment numbers for Fall 2006. Approximately 450 students enrolled in the pre-nursing and nursing tracks of the program compared to 330 students the prior year.



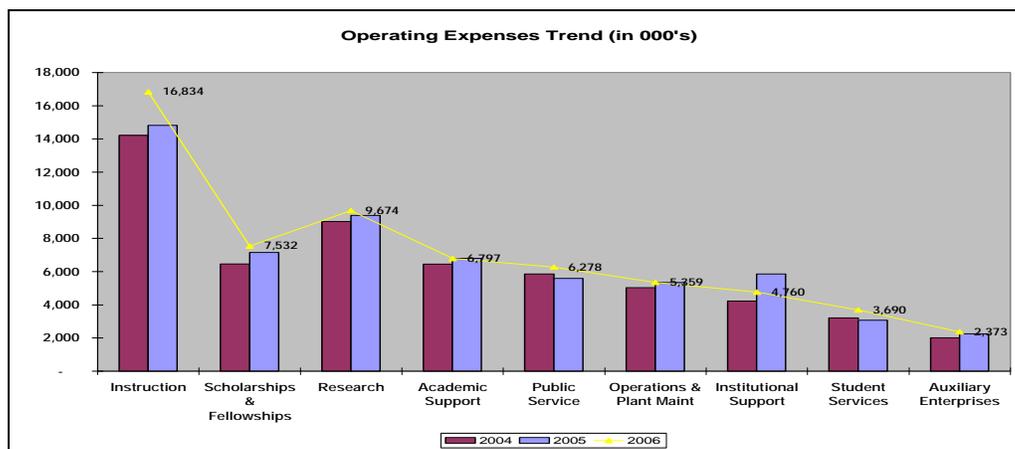
Other Revenues. Net investment income in FY2006 was \$0.9 million from the University's restricted long-term endowment and quasi-endowment investments. This is primarily the result of an increase in market value of the investments portfolio, marking the fourth year of investment gains that bettered market benchmarks. This result reflects a rebound in the equity and bond markets from losses in 2001 and 2002, as well as continued discipline to reinvest investment earnings.



Expenses. FY2006 total operating expenses were \$65.5 million, an increase of \$2.8 million primarily in Instructional and Public Service expenses. Increases were primarily associated with the growth in new grants, merit-based salary increases, and increased enrollment. The University spent \$32.8 million on its core mission. Of that total, 51% went to instruction, 30% to research, and 19% to public service. In addition, the University spent \$15.2 million

on libraries and technology, and student, academic and administrative support; \$12.5 million on student aid; and \$5.3 million on campus maintenance. Other expenses incurred by the University are \$2.3 million in depreciation and \$2.1 million in debt service payments for dormitories and various academic buildings.

As of fiscal year end, total encumbrances (recorded obligations) were recorded at \$4.8 million, a decrease of \$4.4 from prior year amount of \$9.2 million. This decrease is a result of austerity measures implemented in response to government allotment shortfalls.



Net Assets. As discussed earlier, FY2006 marked the fourth year of a positive return on net assets. (Note: Although there was an increase in net assets, the total of operating revenues net of operating expense (“operating net”) was negative because local government appropriations are reported as non-operating revenues rather than operating revenues under GASB 35. As long as the University’s single largest revenue source is local government appropriations, this will be the case at the current level of tuition, fees, grants and contracts.)

STATEMENTS OF CASH FLOWS (IN 000'S)

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Cash provided by (used in):			
Operating activities	\$ (25,470)	\$ (23,980)	(24,240)
Noncapital financing activities	29,157	26,487	33,003
Capital and financing activities	(3,186)	(5,819)	(6,625)
Investing activities	<u>(72)</u>	<u>1,390</u>	<u>(1,700)</u>
Net change in cash and cash equivalents	429	(1,922)	438
Cash and equivalents – beginning of year	<u>4,172</u>	<u>6,094</u>	<u>5,656</u>
Cash and equivalents – end of year	<u>\$ 4,601</u>	<u>\$ 4,172</u>	<u>6,094</u>

This statement provides information about the University’s ability to generate the cash flows needed to meet financial obligations and the extent to which external financing is being used to fund University operations. The University’s cash position increased by \$0.4 million at the end of FY2006, primarily due to \$3.8 million appropriation received on September 29, 2006, and tuition payments. Typically, the University’s cash position at the end of fiscal year is higher than its normal cash position during the balance of the year. This is because fall semester tuition payments are booked at the end of the fiscal year and the government makes catch-up allotment payments close to fiscal year-end. These tuition payments are

subsequently allocated for academic expenses during the remainder of the academic year (which overlap the fiscal year) and for operational expenses, which are normally due at the beginning of the following fiscal year. Financial planning requires that there be an adequate amount of cash on hand at the start of the new fiscal year to pay for prior year encumbrances, insurance premiums, continuing infrastructure restoration and institutional needs.

During the year, cash flows were negatively influenced by the government's deficit, which led to irregular allotment payments and cash shortfalls.

ECONOMIC OUTLOOK AND OVERALL CONCLUSION

Guam's economic outlook continues to show signs of recovery. Increased tourist arrivals and the announced buildup in the U.S. military presence are indicative of a rebound. However, there are continuing threats to the government's financial and cash position on the horizon, such as the cumulative Government of Guam General Fund deficit; continuation of federal income tax cuts; unpaid Earned Income Tax Credit obligations; significant unmet needs in high priority government services such as education and health; and supplemental benefits for Government of Guam retirees. The Office of the Governor has recently initiated a short-term financial recovery plan for consideration by the 29th Guam Legislature to address the approximately \$530 million General Fund deficit, growing structural deficit, and threat of a bond credit rating reduction. In May 2007 the Legislature transmitted Bill 74 to the Governor for approval. The Bill substantially revises and re-balances the executive, legislative and judicial branch FY07 revenues and appropriations with increased fees, additional revenues from a tax amnesty program, reduced business tax credits, and reduced appropriations. The University's net appropriation has been cut approximately \$2.7 million or 8.9%, generally in line with other government-wide cutbacks except for a few exempt areas. These reductions will impact the University's general operations, financial aid and special appropriations. In addition, the \$2 million capital outlay appropriation from the proposed 1993 bond refinancing proceeds has been repealed. While the short-term measures are being considered, the Government is working on a longer-term deficit elimination and economic recovery plan.

The University remains focused on its strategic initiatives and continual improvement, while mindful of the difficult economic conditions and limited resources available. Academic quality and student learning remain the highest priorities. In addition to more sophisticated financial, cash and risk management procedures, there are efforts underway to generate additional revenues through enrollment management and entrepreneurial opportunities, stabilize finances through better planning and closer work with government policy makers and fiscal teams, to secure additional federal grant funding, to expand outreach associated with the University's mission, and to improve institutional efficiency through business process redesign and the application of technology. In April 2007 President Allen established an Institutional Improvement & Sustainability Taskforce with representatives from key constituencies. Its purpose is to address the recommendations of the WASC Capacity and Preparatory Review Team Report with the intent of formulating proposals that strengthen academic quality and student learning, better align structures with strategic objectives, and positioning the University to sustain educational effectiveness in an environment of scarce resources. The Taskforce will release its initial recommendations in May 2007.

Clearly, the University's most challenging problem is sustaining a predictable and reliable cash flow that provides a basis for long-range institutional planning and the ability to make investments in additional core faculty, institutional research and assessment, and information technology that will ensure institutional sustainability and mission focus. And yet, despite the financial challenges, the University has made progress by reordering strategic priorities to address the most critical needs; by strengthening internal communications and governance relationships to produce an engaged community of learners and scholars; and by working closely with all stakeholders to ensure that student learning is not compromised.

Despite the challenging financial conditions, the University remains focused on demonstrating student learning outcomes, educational effectiveness, and will continue to work in a collaborative environment to build and sustain support for the University's core mission.

For further news and up-to-date information concerning the University of Guam, please visit the website at www.uog.edu. The University's annual report and other publications are also available.

UNIVERSITY OF GUAM
Statement of Net Assets
September 30, 2006
(With Comparative Figures for 2005)

<u>ASSETS</u>	<u>2006</u>	<u>2005</u>
Current assets:		
Cash and cash equivalents	\$ 4,600,872	4,172,010
Short-term investments	111,643	110,251
Due from Government of Guam	3,350,000	4,945,723
Tuition receivable, net of allowance of \$4,215,818	2,759,869	2,398,489
Due from U.S. Federal government	1,131,511	1,208,342
Other receivables	1,187,500	986,152
Inventories	614,431	493,005
Other current assets	559,718	541,593
Total current assets	<u>14,315,544</u>	<u>14,855,565</u>
Noncurrent assets:		
Restricted cash and cash equivalents	3,795,261	4,862,292
Investments	6,241,437	5,824,248
Endowment investments	8,248,097	7,736,477
Capital assets, net of accumulated depreciation	73,404,534	67,509,706
Total non current assets	<u>91,689,329</u>	<u>85,932,723</u>
Total assets	<u>\$ 106,004,873</u>	<u>100,788,288</u>
<u>LIABILITIES AND NET ASSETS</u>		
Current liabilities:		
Accounts payable and accrued liabilities:	4,507,367	4,591,274
Current portion of long-term debt	385,000	294,304
Deferred revenue	4,301,124	4,986,070
Total current liabilities	<u>9,193,491</u>	<u>9,871,648</u>
Noncurrent liabilities:		
Deposits held on behalf of others	1,583,892	2,389,690
Accrued annual leave	729,310	647,991
DCRS sick leave liability	917,552	863,155
Long-term debt, net of current portion	10,864,519	4,887,149
Total noncurrent liabilities	<u>14,095,273</u>	<u>8,787,985</u>
Total liabilities	<u>23,288,764</u>	<u>18,659,633</u>
Net assets:		
Invested in capital assets, net of related debt	62,389,854	60,296,558
Restricted:		
Nonexpendable	5,015,944	5,013,399
Expendable	7,736,139	6,920,471
Unrestricted	7,574,172	9,898,227
Total net assets	<u>82,716,109</u>	<u>82,128,655</u>
Total liabilities and net assets	<u>\$ 106,004,873</u>	<u>100,788,288</u>

See accompanying notes to financial statements.

UNIVERSITY OF GUAM ENDOWMENT FOUNDATION, INC.

Statements of Financial Position

December 31, 2005 and 2004

	<u>ASSETS</u>	<u>2005</u>	<u>2004</u>
Cash and cash equivalents		\$ 21,574	30,594
Pledges receivable, net of an allowance for doubtful accounts of \$100,000 at December 31, 2005 and 2004		548,982	482,526
Accounts receivable		23,538	14,403
Advances		-	13,100
Equipment, net		8,822	7,198
Investment in Bank of Guam stock		157,942	157,942
Investment in Citizens Security Bank stock		203,544	203,544
Investment in securities		6,487,977	6,760,516
Other		<u>3,010</u>	<u>9,001</u>
		\$ <u>7,455,389</u>	<u>7,678,824</u>
	<u>LIABILITIES AND NET ASSETS</u>		
Liabilities:			
Accounts payable		35,193	222
Accrued expenses		21,353	8,701
Due to University of Guam		<u>6,457</u>	<u>5,935</u>
Total liabilities		<u>63,003</u>	<u>14,858</u>
Net assets:			
Unrestricted		815,686	1,135,790
Temporarily restricted		6,328,835	6,280,311
Permanently restricted		<u>247,865</u>	<u>247,865</u>
Total net assets		<u>7,392,386</u>	<u>7,663,966</u>
		\$ <u>7,455,389</u>	<u>7,678,824</u>

See accompanying notes to financial statements.

UNIVERSITY OF GUAM
Statement of Revenues, Expenses and Changes in Net Assets
Year ended September 30, 2006
(With Comparative Figures for 2005)

	<u>2006</u>	<u>2005</u>
Operating revenues:		
Student tuition and fees	\$ 12,958,734	11,598,490
Less: Scholarship discounts and allowances	<u>(4,931,545)</u>	<u>(5,272,668)</u>
	8,027,189	6,325,822
Federal grants and contracts	24,834,075	22,346,410
FEMA disaster recoveries	18,727	226,044
Tobacco settlement funds	-	768,335
Government of Guam grants and contracts	525,087	425,828
Private grants and contracts	717,454	758,454
Sales and services of education department	501,237	396,381
Auxiliary enterprises	2,225,286	2,080,035
Other revenues	<u>3,042,424</u>	<u>2,604,749</u>
Total operating revenues	39,891,479	35,932,058
Operating expenses:		
Instruction	16,834,230	14,817,636
Research	9,673,858	9,391,835
Public service	6,278,184	5,590,951
Academic support	6,796,839	6,798,532
Student services	3,689,970	3,081,109
Institutional support	4,760,240	5,857,633
Operations and maintenance, plant	5,359,090	5,347,390
Depreciation	2,241,174	2,405,825
Scholarships and fellowships	7,531,803	7,150,948
Auxiliary enterprises	<u>2,373,044</u>	<u>2,255,383</u>
Total operating expenses	<u>65,538,432</u>	<u>62,697,242</u>
Operating revenues net of operating expenses	(25,646,953)	(26,765,184)
Nonoperating revenues (expenses):		
Government of Guam appropriations:		
Operations	23,698,666	26,030,648
Student financial aid program	2,762,672	2,511,000
Capital expenditure loan repayment	500,000	-
Transfer from Yamashita Education Corporation	600,000	500,000
Net investment income	857,761	1,565,514
Interest on capital assets - debt related	(157,390)	(66,906)
Debt service - DOA bond	<u>(2,027,302)</u>	<u>(2,027,291)</u>
Net nonoperating revenues	<u>26,234,407</u>	<u>28,512,965</u>
Net increase in net assets	587,454	1,747,781
Net assets:		
Net assets at beginning of year	<u>82,128,655</u>	<u>80,380,874</u>
Net assets at end of year	<u>\$ 82,716,109</u>	<u>82,128,655</u>

See accompanying notes to financial statements.

UNIVERSITY OF GUAM ENDOWMENT FOUNDATION, INC.

Statement of Activities and Changes in Net Assets

Year Ended December 31, 2005

	<u>Unrestricted</u>	Temporarily <u>Restricted</u>	Permanently <u>Restricted</u>	<u>Total</u>
Revenues, gains and other income:				
Net investment earnings	\$ 448,681	-	-	448,681
Contributions	79,407	87,298	-	166,705
In kind donations	229,089	-	-	229,089
Fundraising activities	360,497	-	-	360,497
Fundraising – Guam Medical Society	-	126,237	-	126,237
Net assets released from restrictions:				
Satisfaction of program restrictions	<u>165,011</u>	<u>(165,011)</u>	<u>-</u>	<u>-</u>
Total revenues	<u>1,282,685</u>	<u>48,524</u>	<u>-</u>	<u>1,331,209</u>
Program services:				
Contributions to University of Guam programs	47,831	-	-	47,831
Scholarships	15,500	-	-	15,500
Fundraising – Guam Medical Society	<u>101,680</u>	<u>-</u>	<u>-</u>	<u>101,680</u>
Total program services	<u>165,011</u>	<u>-</u>	<u>-</u>	<u>165,011</u>
Support services:				
Management and general	711,656	-	-	711,656
Fundraising activities	<u>726,122</u>	<u>-</u>	<u>-</u>	<u>726,122</u>
Total support services	<u>1,437,778</u>	<u>-</u>	<u>-</u>	<u>1,437,778</u>
Total expenses	<u>1,602,789</u>	<u>-</u>	<u>-</u>	1,602,789
Change in net assets	(320,104)	48,527	-	(271,580)
Net assets at beginning of year	<u>1,135,790</u>	<u>6,280,311</u>	<u>247,865</u>	<u>7,663,966</u>
Net assets at end of year	\$ <u>815,686</u>	<u>6,328,835</u>	<u>247,865</u>	<u>7,392,386</u>

See accompanying notes to financial statements.

UNIVERSITY OF GUAM
Statement of Cash Flows
Year ended September 30, 2006
(With Comparative Figures for 2005)

	<u>2006</u>	<u>2005</u>
Cash flows from operating activities:		
Student tuition and fees, net	\$ 7,665,809	6,930,509
Grants and contracts	27,749,170	24,069,388
Sales and services of education department	299,889	163,011
Auxiliary services	(147,758)	(175,348)
Other receipts	3,042,424	2,604,749
Payments to employees for salaries and benefits	(35,568,438)	(33,467,700)
Payments to suppliers and others	(20,979,455)	(16,953,953)
Payments to students for financial aid	(7,531,803)	(7,150,948)
Net cash used in operating activities	<u>(25,470,162)</u>	<u>(23,980,292)</u>
Cash flows from noncapital financing activities:		
Government of Guam appropriations	<u>29,157,061</u>	<u>26,486,679</u>
Cash flows from capital and related financing activities:		
Interest paid on capital debt	(157,390)	(66,906)
Purchases of capital assets	(8,136,002)	(6,360,243)
Principal paid on capital debt	(2,262,142)	(2,252,823)
Proceeds from issuance of debt	6,302,906	4,485,122
Changes in restricted cash	1,067,031	(1,623,908)
Net cash used in capital and related financing activities	<u>(3,185,597)</u>	<u>(5,818,758)</u>
Cash flows from investing activities:		
Investment income	857,761	1,565,514
Net (purchases) sales of investments	(930,201)	(175,047)
Net cash provided by (used in) investing activities	<u>(72,440)</u>	<u>1,390,467</u>
Net change in cash and cash equivalents	428,862	(1,921,904)
Cash and cash equivalents at beginning of year	4,172,010	6,093,914
Cash and cash equivalents at end of year	<u>\$ 4,600,872</u>	<u>4,172,010</u>
Reconciliation of operating income to net cash used in operating activities:		
Operating revenues net of operating expenses	(25,646,953)	(26,765,184)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation	2,241,174	2,405,825
Loss on disposal of fixed assets	-	89,592
Changes in assets and liabilities:		
Accounts receivable, net	(485,897)	(932,915)
Inventory	(121,426)	189,789
Other assets	(18,125)	(123,102)
Accounts payable and accrued liabilities	(2,588)	199,813
Deferred revenue	(684,946)	848,549
DCRS sick leave	54,397	141,484
Deposits held on behalf of others	(805,798)	(34,143)
Net cash used in operating activities	<u>\$ (25,470,162)</u>	<u>(23,980,292)</u>

See accompanying notes to financial statements.

UNIVERSITY OF GUAM ENDOWMENT FOUNDATION, INC.

Statements of Cash Flows

Years Ended December 31, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Cash flows from operating activities:		
Change in net assets	\$ (271,580)	371,148
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Interest and dividend income reinvested	(180,429)	(154,623)
Unrealized investment gains	(268,252)	(819,017)
(Increase) decrease in receivables	(69,600)	490,726
Decrease in prepaid expenses	13,100	9,001
Increase (decrease) in accounts payable and accrued expenses	47,623	(7,646)
Increase in due to University of Guam	<u>522</u>	<u>-</u>
Net cash used in operating activities	<u>(728,616)</u>	<u>(110,411)</u>
Cash flows from investing activities:		
Sale of investments	644,546	486,222
Purchase of investments	-	(500,000)
Acquisition of Bank of Guam stock	-	(41,242)
Investment fees	76,674	80,761
Purchase of equipment	<u>(1,624)</u>	<u>(86)</u>
Net cash provided by investing activities	<u>719,596</u>	<u>25,655</u>
Decrease in cash and cash equivalents	(9,020)	(84,756)
Cash and cash equivalents at beginning of year	<u>30,594</u>	<u>115,350</u>
Cash and cash equivalents at end of year	\$ <u>21,574</u>	<u>30,594</u>

See accompanying notes to financial statements.

UNIVERSITY OF GUAM

Notes to Financial Statements September 30, 2006 (with comparative information for 2005)

1. Organization

Administrative autonomy was granted to the University of Guam (the University) with the enactment of Public Law No. 13-194, "The Higher Education Act of 1976," which became effective on November 3, 1976. The Act, with subsequent amendments, established the University as a non-membership, not-for-profit corporation of the Government of Guam, under the control and operation of a nine-member Board of Regents appointed by the Governor with the advice and consent of the Legislature. The University is a component unit of the Government of Guam.

2. Basis of Presentation

- A. Financial Statement Presentation. In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*. This was followed in November 1999 by GASB Statement No. 35, *Basic Financial Statements and Management's Discussion and Analysis for Public Colleges and Universities*. The financial statement presentation required by GASB No. 34 and 35 provides a comprehensive, entity-wide perspective of the University's assets, liabilities, net assets, revenues, expenses, changes in net assets, and cash flows, and replaces the fund-group perspective previously required.

Other GASB Statements are required to be implemented in conjunction with GASB Statements No. 34 and 35. Therefore, the Government of Guam and Guam public colleges and universities have also implemented Statement No. 36, *Recipient Reporting for Certain Shared Nonexchange Revenues*, Statement No. 37, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus* and Statement No. 38, *Certain Financial Statement Note Disclosures*.

- B. Basis of Accounting. For financial statement purposes, the University is considered a special-purpose government engaged only in business-type activities. Accordingly, the University's financial statements have been presented using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. All significant intra-university transactions have been eliminated. The University reports as a business-type activity, as defined by GASB Statement No. 35. Business-type activities are those that are financed in whole or in part by fees charged to external parties for goods or services.

UNIVERSITY OF GUAM

Notes to Financial Statements
September 30, 2006
(with comparative information for 2005)

2. Basis of Presentation, continued

The University has the option to apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless FASB conflicts with GASB. The University has elected to not apply FASB pronouncements issued after the applicable date.

- C. Reporting Entity. Effective October 1, 2003, the University adopted GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units*. The University of Guam Endowment Foundation (the Foundation) is a legally separate, tax-exempt entity which meets the criteria set forth for component units under GASB Statement No. 39. The Foundation provides financial support for the objectives, purposes and programs of the University. Although the University does not control the timing, purpose, or amount of receipts from the Foundation, the resources (and income thereon) which the Foundation holds and invests are restricted to the activities of the University. Because the resources held by the Foundation can only be used by, or for the benefit of, the University, the Foundation is considered a component unit of the University and its Statements of Financial Position and Statements of Activities and Changes in Net Assets are separately presented in the University's financial statements. In addition, the Foundation's significant notes are summarized in Note W.

The Foundation is a private organization that reports under FASB standards, including FASB Statement No. 117, *Financial Reporting for Not-for-Profit Organizations*. As such, certain revenue recognition criteria and presentation features are different from GASB revenue recognition criteria and presentation features. No modifications have been made to the Foundation's financial information in the University's financial reporting entity for these differences.

The Foundation's fiscal year end is as of December 31.

3. Summary of Significant Accounting Policies

- A. Cash and Cash Equivalents. Cash and cash equivalents include cash on hand, cash in banks, money market accounts and time certificates of deposit with original maturities of three months or less.

At September 30, 2006 and 2005 the University has cash balances of \$8,396,133 and \$9,034,302, respectively, with corresponding bank balances of \$6,291,242 and \$9,794,882, respectively, of which \$6,147,758 and \$6,272,046, respectively, are insured by the Federal Deposit Insurance Corporation, or collateralized by securities held by a trustee in the name of the financial institution. The remaining balances are uninsured and uncollateralized. Accordingly, these deposits are exposed to custodial credit risk.

UNIVERSITY OF GUAM

Notes to Financial Statements
September 30, 2006
(with comparative information for 2005)

3. Summary of Significant Accounting Policies, continued

- B. Restricted Cash and Cash Equivalents. Cash and cash equivalents that are restricted to make debt service payments and purchases or enhance learning resources materials and technology are classified as noncurrent assets in the Statement of Net Assets.

At September 30, 2006 and 2005, the University recorded \$1,934,492 and \$1,860,944, respectively, from a tobacco settlement agreement entered into by the Government of Guam to be expended by the University for enhancement of learning resources and technology. The fund may only be expended in accordance with purposes set forth by the Guam Economic Development and Commerce Authority, a component unit of the Government of Guam. During the years ended September 30, 2006 and 2005, the fund earned interest of \$73,548 and \$40,560, respectively.

- C. Short-term Investments. Short-term investments include time certificates of deposits with original maturities of more than three months.
- D. Investments. The University accounts for its investments at fair value in accordance with GASB Statement No. 31, *Accounting for Financial Reporting for Certain Investments and for External Investment Pools*. Unrealized gains and losses on the carrying value of investments are reported as a part of net investment income in the Statement Revenues, Expenses and Changes in Net Assets.
- E. Due from Government of Guam. Due from Government of Guam consists of the remaining balance of legislative annual appropriations and scholarships, which have not been received at September 30, 2006 and 2005.
- F. Accounts Receivable – U.S. Government. Accounts receivable from the U.S. Government consist of amounts due from the federal government in connection with reimbursement of allowable expenditures made pursuant to the University's grants and contracts.
- G. Other Receivables. Other receivables consist primarily of auxiliary enterprise services provided to students, faculty and staff, and other departments within the University to the public. Other receivables also include amounts due from the local government or private sources in relation to the performance of grants and contracts.
- H. Inventory Method. Inventory is stated at the lower of cost or market with cost being determined using the first-in, first-out method of valuation.

UNIVERSITY OF GUAM

Notes to Financial Statements September 30, 2006 (with comparative information for 2005)

3. Summary of Significant Accounting Policies, continued

- I. Capital Assets. Depreciation is calculated using the straight-line method over estimated useful lives of 5 – 50 years for buildings and improvements and 5 – 15 years for equipment and land improvements. The University's capitalization policy requires acquisitions greater than \$5,000 to be capitalized and depreciated over the estimated useful lives. The assets are carried at cost, except for land and buildings transferred to the University, which were recorded at management's estimate of fair market value at the date of acquisition. These additions have since been adjusted to fair market value as determined by independent appraisals completed during fiscal year 1988.
- J. Deferred Revenues. Deferred revenues include amounts received for tuition and fees and certain auxiliary activities prior to the end of the fiscal year but relate to the subsequent accounting period. Deferred revenues also include amounts received from grant and contract sponsors that have not yet been earned.
- K. Compensated Absences. Employee vacation leave is accrued at year end for financial statement purposes. Included in accounts payable and accrued liabilities at September 30, 2006 and 2005 is \$1,660,137 and \$1,504,785, respectively, related to compensated absences earned but unused. The change in accrued employee leave is also included as a component of operating expense in the Statement of Revenues, Expenses, and Changes in Net Assets.
- L. Grants-in-Aid. Tuition and fees revenue include grants-in-aid for senior citizens, faculty, staff and their dependents charged to scholarships and fellowships expense. The total of these grants for 2006 and 2005 was \$146,330 and \$161,910, respectively.
- M. Noncurrent Liabilities. Noncurrent liabilities include (1) principal amounts of revenue bonds payable, notes payable, and capital lease obligations with contractual maturities greater than one year, and (2) estimated amounts for accrued compensated absences and other liabilities that will not be paid within the next fiscal year.
- N. Net Assets. The University's net assets are classified as follows:

Invested in Capital Assets, Net of Related Debt – This represents the University's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included in this section.

UNIVERSITY OF GUAM

Notes to Financial Statements
September 30, 2006
(with comparative information for 2005)

3. Summary of Significant Accounting Policies, continued

Restricted Net Assets – Expendable – Restricted expendable net assets include resources that the University is legally or contractually obligated to spend in accordance with restrictions imposed by external third parties.

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

Unrestricted Net Assets – Unrestricted net assets represent resources derived from student tuition and fees, state appropriations, and sales and services of educational departments and auxiliary enterprises. These resources are used for transactions relating to the educational and general operations of the University, and may be used at the discretion of the governing board to meet current expenses for any purpose. These resources also include auxiliary enterprises, which are substantially self-supporting activities that provide services for student, facility and staff.

- O. Classification of Revenues. The University has classified its revenues as either operating or nonoperating according to the following criteria:

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

Nonoperating Revenues – Nonoperating revenues include activities that have the characteristics of nonexchange transactions, such as gifts and contributions, and other revenue sources that are defined as nonoperating revenues by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities that Use Proprietary Fund Accounting*, and GASB Statement No. 34, such as state appropriations and investment income.

- P. Scholarship Discounts and Allowances. Student tuition and fee revenues, and certain other revenues from students, are reported net of scholarship discounts and allowances in the Statement of Revenues, Expenses and Changes in Net Assets. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by the University, and the amount that is paid by students and/or third parties making payments on the students' behalf.

UNIVERSITY OF GUAM

Notes to Financial Statements September 30, 2006 (with comparative information for 2005)

3. Summary of Significant Accounting Policies, continued

Certain governmental grants, such as Pell grants, and other federal, state or nongovernmental programs, are recorded as either operating or nonoperating revenues in the University's financial statements. To the extent that revenues from such programs are useful to satisfy tuition and fees and other student charges, the University has recorded to scholarship discount and allowance.

- Q. New Accounting Standards. In fiscal year 2005, the University implemented GASB Statement No. 40, *Deposit and Investment Risk Disclosures* (an amendment of GASB Statement No. 3), which addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. As an element of interest risk, GASB Statement No. 40 requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates.

In November 2003, GASB issued Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. The provisions of the Statement are effective for periods beginning after December 15, 2004. The University does not believe that the implementation of this Statement will have a material effect on its financial statements.

In April 2004, GASB issued Statement No. 43, *Financial Reporting for Postemployment Benefits Plans Other than Pension Plans*. GASB Statement No. 43 establishes uniform financial reporting for other postemployment benefit plans by state and local governments. The provisions of this Statement are effective for periods beginning after December 15, 2007. The University does not believe that the implementation of this Statement will have a material effect on the financial statements.

In May 2004, GASB issued Statement No. 44, *Economic Condition Reporting: The Statistical Section*, an amendment to NCGA Statement 1. GASB Statement No. 44 improves the understandability and usefulness of statistical section information and adds information from the new financial reporting model for state and local governments required by GASB Statement No. 34. The provisions of this Statement are effective for periods beginning after June 15, 2005. The University does not believe the implementation of this Statement will have a material effect on its financial statements.

UNIVERSITY OF GUAM

Notes to Financial Statements
September 30, 2006
(with comparative information for 2005)

3. Summary of Significant Accounting Policies, continued

In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. GASB Statement No. 45 establishes standards for the measurement, recognition, and display of other postemployment benefits expense/expenditures and related liabilities, note disclosures, and, if applicable, required supplementary information in the financial reports of state and local governmental employers. The provisions of this Statement are effective for periods beginning after December 15, 2008. The University does not believe the implementation of this Statement will have a material effect on its financial statements.

In June 2005, GASB issued Statement No. 47, *Accounting for Termination Benefits*. GASB Statement No. 47 establishes guidance for state and local governmental employers on accounting and financial reporting for termination benefits. These benefits include incentives for voluntary terminations (e.g. early retirement window programs) and severance payments with respect to involuntary terminations. The provisions of this Statement are effective for periods beginning after June 15, 2005. The University does not believe that the implementation of this Statement will have a material effect on its financial statements.

- R. Employees' Retirement Plan. Employees of the University hired before October 1, 1995, are under the Government of Guam Employees' Retirement System (a defined benefit, contributory pension plan). Employees hired after September 30, 1995, are members of the Defined Contribution Retirement System (DCRS). Until December 31, 1999 and periodically thereafter, those employees who were members of the Defined Benefit Plan with less than 20 years of service at September 30, 1995, had the option to switch to the Defined Contribution Retirement System.

The Defined Benefit Plan and the DCRS are administered by the Government of Guam Retirement Fund, to which the University contributes based upon a fixed percentage of the payroll for those employees who are members of the Plan.

As a result of actuarial valuations performed as of September 30, 2005, 2004 and 2003, contribution rates for the years ended September 30, 2007, 2006 and 2005, respectively, have been determined as follows:

UNIVERSITY OF GUAM

Notes to Financial Statements
September 30, 2006
(with comparative information for 2005)

3. Summary of Significant Accounting Policies, continued

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Normal costs (% of DB Plan payroll)	18.21%	17.83%	18.30%
Unfunded liability costs (% of total payroll)	<u>20.66%</u>	<u>21.36%</u>	<u>19.93%</u>
	38.87%	39.19%	38.23%
Employee contributions (DB Plan employees)	<u>9.50%</u>	<u>9.50%</u>	<u>9.50%</u>
	29.37%	29.69%	28.73%
Agency specific adjustments-	<u>- %</u>	<u>- %</u>	<u>- %</u>
Government contribution as a % of DB Plan Payroll	29.37%	29.69%	28.73%
Government contributions as a % of total payroll	27.48%	28.21%	24.89%

The plan utilized the actuarial cost method termed “entry age normal”. Significant actuarial assumptions are as follows:

	<u>2005</u> <u>Actuarial Valuation</u>	<u>2004</u> <u>Actuarial Valuation</u>
Interest rate and rate of return	7.0%	7.0%
Payroll increases	3.5%	3.5%
Salary increases	4.0 – 8.5%	4.0 – 8.5%

The actuarial valuation performed as of September 30, 2005, did not provide a breakdown of actuarial present value of vested and non-vested accumulated plan benefits by sponsor or net assets available for benefits by sponsor.

Statutory contribution rates for employer and employee contributions were 20.81% and 9.5%, respectively, of qualifying payroll for both of the years ended September 30, 2006 and 2005.

Contributions into the DCRS by members are based on an automatic deduction of 5% of the member’s regular base pay. The contribution is periodically deposited into an individual annuity account within the DCRS. Employees are afforded the opportunity to select from different annuity accounts available under the DCRS.

Statutory employer contributions into the DCRS for the years ended September 30, 2006 and 2005 are determined using the same rates as the DB plan. Of the amount contributed by the employer, only 5% of the member’s regular base pay is deposited into the member’s individual annuity account. The remaining amount is contributed towards the unfunded liability of the defined benefit plan. Members of the DCRS who have completed five years of government service have a vested balance of 100% of both member and employer contributions plus any earnings thereon.

UNIVERSITY OF GUAM

Notes to Financial Statements
September 30, 2006
(with comparative information for 2005)

3. Summary of Significant Accounting Policies, continued

Public Law 26-86 allows members of the DCRS to receive a lump sum payment of one-half of their accumulated sick leave upon retirement. The University has accrued an estimated liability of \$917,552 and \$863,155 at September 30, 2006 and 2005, respectively, for potential future sick leave payments as a result of this law. However, this amount is an estimate and actual payout may be materially different than estimated.

Retirement contributions for the years ended September 30, 2006 and 2005 are as follows:

	<u>2006</u>	<u>2005</u>
Defined benefit plan	\$ 2,822,239	2,855,424
DCRS	2,156,566	1,899,579

As a result of Public Law No. 21-03, the University has no further responsibility to pay for its share of the unfunded retirement costs. This responsibility now rests with the General Fund of the Government of Guam. Rather, the University's responsibility is to pay the statutorily imposed retirement rate. As of September 30, 2006 and 2005, the General Fund has accrued approximately \$6,540,519 and \$5,361,724, respectively, for the University's cumulative unfunded retirement liability.

- S. Financial Assistance Revenue. Government of Guam appropriations designated for student financial assistance programs are made annually for the period from October 1 to September 30. As certain restrictions are placed on these funds, revenue is realized only to the extent that such funds are expended for current purposes.
- T. Estimates. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the statement of net assets and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.
- U. Risk Management. The University purchases insurance to cover its risk of losses due to typhoons, liability and other risks normal to operating an institution of higher learning. For fiscal year 2006, the University has a \$50,000 deductible for each and every loss. Additionally, the University has a two percent (2%) deductible (with a minimum of \$150,000) for each and every loss from windstorm, typhoon, flood, tidal wave and earthquake

UNIVERSITY OF GUAM

Notes to Financial Statements September 30, 2006 (with comparative information for 2005)

3. Summary of Significant Accounting Policies, continued

V. Reclassification. Certain account balances in 2005 have been reclassified to conform to the 2006 financial statement presentation.

W. UOG Endowment Foundation Pledges Receivable and Investments

UOG Endowment Foundation Pledges Receivable

Pledges receivable consist of donations pledged to the UOG Endowment Foundation, but not yet received as of December 31, 2005 and 2004. These pledges are payable in installments over periods ranging from one to forty-three years. Unconditional promises to give that are expected be collected for future years are recorded at the present value of the estimated cash flows. Amortization of discount will be included in contribution revenue. Management of the Foundation is of the opinion that the net outstanding balance is collectible in subsequent fiscal years and has reserved for all other long-term receivables.

Included in pledges receivable are the following unconditional promises to give:

	<u>2005</u>	<u>2004</u>
SBPA (School of Business and Public Administration) Building	\$ 1,070,000	1,000,000
Other	<u>96,000</u>	<u>101,000</u>
	1,166,000	1,101,000
Less: Unamortized discount	<u>(517,018)</u>	<u>(518,474)</u>
	648,982	582,526
Less: Allowance for uncollectibles	<u>(100,000)</u>	<u>(100,000)</u>
	\$ <u>548,982</u>	<u>482,526</u>

UOG Endowment Foundation Investments

Investments are carried at fair market value. Gains and losses on investments are reported in the statements of activities as increases or decreases in unrestricted net assets unless their use is temporarily or permanently restricted by explicit donor stipulations or by laws. The composition of investments in securities as of December 31, 2005 and 2004, follows:

	<u>2005</u>	<u>2004</u>
Cash	\$ 1,182,368	308,845
Equities	3,977,984	5,086,116
Fixed income	<u>1,327,625</u>	<u>1,365,556</u>
	\$ <u>6,487,977</u>	<u>6,760,517</u>

UNIVERSITY OF GUAM

Notes to Financial Statements September 30, 2006 (with comparative information for 2005)

3. Summary of Significant Accounting Policies, continued

The composition of net investment earnings for the years ended December 31, 2005 and 2004, is as follows:

	<u>2005</u>	<u>2004</u>
Increase in fair value	\$ 268,252	819,017
Interest income	71,558	66,913
Dividends	<u>108,871</u>	<u>87,710</u>
	\$ <u>448,681</u>	<u>973,640</u>

Investments also include shares of stock in Bank of Guam (BOG) and Citizens Security Bank (CSB) that are recorded at their fair market values at December 31, 2005 and 2004. The CSB shares are permanently restricted, as the shares cannot be sold. Dividends received from these shares will be used for scholarship purposes. The BOG shares contain no restrictions and are classified as unrestricted net assets.

4. Long-Term Debt

Financing for the construction of the dormitory complex and a student union building was obtained from the issuance of "University of Guam Dormitory and Student Union Revenue Bonds of 1968," in the amount of \$2,140,000. Interest is payable semi-annually on April 1 and October 1 of each year at a rate of 6% per annum. The bonds mature in varying amounts from \$30,000 to \$90,000 on October 1 of each year through 2008. Principal and interest are payable from, and are collateralized by, a first charge and lien on the net revenues derived by the University Dormitory Revenue Fund, as defined in the bond resolution. The bonds are not an obligation of the Government of Guam, but are solely that of the University Dormitory Revenue Fund.

As a requirement of the bond resolution, the University Dormitory Revenue Fund is to transfer semi-annually on March 15, and September 15, to the University Dormitory Interest and Redemption Fund, a sum equal to sixty-two and one-half percent (62 ½%) of the aggregate amount of principal and interest becoming due on the bonds during the next succeeding twelve months until such time as the funds in the Interest Redemption Fund are sufficient to pay the interest and one-half of the principal next coming due, and to provide a reserve in an amount equal to the average annual debt service which approximates \$91,917.

The bond resolution also requires that when the annual debt service reserve has been satisfied, the Fund is to deposit into an account, to the extent available, up to \$14,000 per year to the credit of the repair and replacement reserve account. These deposits are to continue until a balance of \$280,000 is reached. Bond principal payments for the succeeding years are shown below:

UNIVERSITY OF GUAM

Notes to Financial Statements September 30, 2006 (with comparative information for 2005)

4. Long-Term Debt, continued

<u>Year Ending September 30,</u>	<u>Interest</u>	<u>Principal</u>	<u>Total</u>
2007	\$ 5,250	85,000	90,250
2008	<u>2,700</u>	<u>90,000</u>	<u>92,700</u>
	\$ <u>7,950</u>	<u>175,000</u>	<u>182,950</u>

In November 1997, the University entered into a ten-year capital lease agreement to obtain equipment for an energy conservation project. Obligations under the capital lease consist of the following at September 30, 2006.

<u>Year Ending September 30,</u>	<u>Capital Lease</u>
2007	\$ 173,530
2008	<u>130,151</u>
Total payments	<u>303,681</u>
Less amounts representing interest	<u>(17,190)</u>
Total obligation under capital lease	\$ <u>286,491</u>

Approximately One Million Dollars (\$1,000,000) of construction in progress related to the energy conservation project was subsequently written off.

In October 2001, Public Law 26-48 authorized the Board of Regents of the University of Guam to enter into a loan agreement with the United States Department of Agriculture (USDA) of an amount not to exceed \$13.5 million for the purpose of funding construction of certain facilities. The loan agreement with USDA for \$13.5 million was signed on June 12, 2003 and construction began in March 2005. As of September 30, 2006, \$10,788,028 has been drawn down. Monthly payments of \$62,505 began in July 2006. The loan security agreement pledges revenues derived from the operation of the facility be transferred to an account designated for debt service, operation and maintenance of the facility. After the payment of principal and interest, \$6,251 a month is required to be transferred to a reserved account until a sum of \$760,060 is accumulated. In addition, the University assigned and granted to the debtor its security interest in all equipment, furniture and fixtures located at the Business and Public Administration Building.

Debt service to maturity is not disclosed for the amount drawn to September 30, 2006. However, the debt service to maturity for the entire debt, once drawdown, will be as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2006	\$ 35,774	151,741	187,515
2007	147,181	602,879	750,060
2008	153,942	596,118	750,060
2009	161,014	589,046	750,060
2010	168,411	581,649	750,060
2011 – 2015	965,466	2,784,834	3,750,300
2016 – 2020	1,208,567	2,541,733	3,730,300

UNIVERSITY OF GUAM

Notes to Financial Statements September 30, 2006 (with comparative information for 2005)

4. Long-Term Debt, continued

2021 – 2025	1,512,879	2,237,421	3,750,300
2026 – 2030	1,893,815	1,856,485	3,750,300
2031 – 2035	2,370,670	1,379,630	3,750,300
2036 – 2040	2,967,595	782,705	3,750,300
2041 – 2043	<u>1,914,686</u>	<u>123,032</u>	<u>2,037,718</u>
	<u>\$ 13,500,000</u>	<u>14,227,273</u>	<u>27,727,273</u>

Public Law 26-48 also provided supplemental annual funding of \$500,000 to pay for the loan. At September 30, 2006 and 2005, \$2.0 million and \$1.5 million, respectively, have been received. The funds received are classified as restricted expendable net assets.

5. Noncurrent Liabilities

Noncurrent liability activity was as follows:

	Beginning Balance September <u>30, 2005</u>	<u>Additions</u>	<u>Reductions</u>	Ending Balance September <u>30, 2006</u>	Amount due within <u>one year</u>
Bonds, notes and capital lease obligations:					
Revenue bond payable	\$ 260,000	-	85,000	175,000	85,000
Capital lease payable	436,331	-	149,840	286,491	173,530
Notes payable	<u>4,485,122</u>	<u>6,302,906</u>	<u>-</u>	<u>10,788,028</u>	<u>126,470</u>
 Total bonds, notes and capital leases	 <u>5,181,453</u>	 <u>6,302,906</u>	 <u>234,840</u>	 <u>11,249,519</u>	 <u>385,000</u>
Other liabilities:					
Deposit held on behalf of others	2,389,690	1,634,464	2,440,262	1,583,892	-
Accrued annual leave	1,504,785	1,234,244	1,078,892	1,660,137	930,827
DCRS sick leave liability	863,155	57,580	3,183	917,552	-
Total other noncurrent liabilities	<u>4,757,630</u>	<u>2,926,288</u>	<u>3,522,337</u>	<u>4,161,581</u>	<u>930,827</u>
Total noncurrent liabilities	<u>\$ 9,939,083</u>	<u>9,229,194</u>	<u>3,757,177</u>	<u>15,411,100</u>	<u>1,315,827</u>

6. Student Loans

The Guam Legislature appropriates funds for the student loan program available to residents of Guam who attend institutions of higher education. The University is responsible for awarding the loans and monitoring compliance with respect to repayment. Due to the uncertainty of collection and due to recipient ability to repay the loans through work credits, student loan receivables are fully reserved in the year granted, and payments are reflected as recoveries in the year received. At September 30, 2006 and 2005, loan receivables are reserved in the amount of \$12,168,050 and \$11,594,238, respectively, and recoveries collected are \$314,366 and \$357,100 for the years then ended, respectively.

UNIVERSITY OF GUAM

Notes to Financial Statements September 30, 2006 (with comparative information for 2005)

7. Deposits and Investments

GASB Statement No. 40 addresses common deposit and investment risks related to credit risk, concentration of credit risk, interest rate risk and foreign currency risk. As an element of interest rate risk, disclosure is required of investments that have fair values that are highly sensitive to changes in interest rates. GASB Statement No. 40 also requires disclosure of formal policies related to deposits and investment risks.

The deposit and investment policies of the University are governed by pertinent restrictions existing under the laws of Guam with respect to investments (fund). The Board of Regents, with the assistance of a consultant, is required to engage investment managers to manage the fund assets. Legally authorized investments are as follows:

(i) General Guidelines

- a. U.S. and Non-U.S. Equities include American Depository Receipts, convertible bonds, preferred stock, fixed-income securities, mutual funds and short-term securities.
- b. No individual security of any issuer, other than that of the United States Government, shall constitute more than 5% (at cost) of the total fund or 10% (at cost) of any investment manager's portfolio.
- c. No investment may be made in the securities of a single corporate entity in excess of 15% (at market) of any individual investments manager's portfolio, without prior approval from the University.
- d. Holdings of any issuer shall constitute no more than 5% of the outstanding securities of such issuer.
- e. Investments in a registered mutual fund managed by the investment manager are subject to prior approval of the University.
- f. The following securities and transactions are not authorized without prior written approval from the University: letter stock and other unregistered securities; non-negotiable securities; commodities or other commodity contracts; options; futures; short sales; and, margin transactions.
- g. No investment manager's portfolio shall be excessively over weighted in any one industry (as compared to respective benchmark index) without prior approval by the University.

(ii) U.S. Fixed Income

- a. All fixed income securities held in the portfolio shall have Moody's, Standard & Poor's and/or Fitch's credit quality rating of no less than "BBB".
- b. U.S. Treasury and U.S. Government agencies, which are unrated securities, are qualified for inclusion in the portfolio and will be considered to be of the highest rating.
- c. No more than 20% of the market value of the portfolio shall be rated less than single "A" quality, unless the manager has specific prior written authorization from the University.

UNIVERSITY OF GUAM

Notes to Financial Statements
September 30, 2006
(with comparative information for 2005)

7. Deposits and Investments, continued

(iii) Equities

- a. Consistent with the desire to maintain broad diversification, allocation to any economic or industry sector should not be excessive.
- b. Equity holdings shall be restricted to readily marketable securities of corporations that actively traded on the major exchanges and over the counter.
- c. The managers shall have the discretion to invest a portion of the assets in cash reserves when they deem appropriate.
- d. Common stock and preferred stock of any institution or entity created or existing under the laws of the United States or any other country are permissible investments.

(iv) Cash and Cash Equivalents

- a. Cash equivalent reserves shall consist of cash instruments having a quality rating of A-I, P-I or their equivalent. U.S. Treasury and Agency securities, Bankers Acceptances, Certificates of Deposit and Collateralized Repurchase Agreements are also acceptable investment vehicles. Custodial Sweep Accounts must be, in the judgment of the investment managers, of credit quality equal or superior to the standards described above.
- b. In the case of Certificates of Deposit, they must be issued by FDIC insured institutions. Deposits in institutions with less than \$10,000,000 in assets may not be made in excess of \$100,000, unless the deposit is fully collateralized by U.S. Treasury Securities.
- c. No single issue shall have a maturity of greater than two years.
- d. Custodial Sweep Account portfolios must have an average maturity of less than one year.

A. Deposits:

GASB Statement No.3 previously required the University to present deposits into three categories of custodial credit risk generally described as follows:

Category 1 Insured or registered, or securities held by the University or its agent in the University's name.

Category 2 Uninsured and unregistered, or securities held by a party other than the University or its agent, but in the University's name.

Category 3 Uninsured and unregistered, with securities held by a party other than the University and not in the University's name.

UNIVERSITY OF GUAM

Notes to Financial Statements September 30, 2006 (with comparative information for 2005)

7. Deposits and Investments, continued

A. Deposits, continued:

GASB Statement No. 40 amended GASB Statement No.3 to in effect eliminate disclosure for deposits falling into categories 1 and 2 but retained disclosures for deposits falling under category 3. Category 3 deposits are those deposits that have exposure to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the University's deposits may not be returned to it. Such deposits are not covered by depository insurance and are either uncollateralized, or collateralized with securities held by the pledging financial institution or held by the pledging financial institution but not in the University's name.

B. Investments:

Investments exclusive of physical plant are recorded at market value; investments received by gift are recorded at market value at the date of acquisition. Realized gains and losses are recognized in the Statement of Revenues, Expenses and Changes in Net Assets upon disposition, and unrealized gains and losses are recorded as net appreciation (depreciation) of fair value in investments. Approximately \$14,393,266 of these investments and cash at September 30, 2006, are accounted for on a pooled basis. The University employs the share method of accounting for pooled investments and for proportionate distribution of income and fees to each fund which participates in the pool. Investments held by the University consist of money market funds, fixed income securities, and common stock. These investments are held in the name of the University.

	<u>2006</u>	<u>2005</u>
Investments:		
Money market funds	\$ 304,921	309,026
Fixed income securities	1,455,088	1,370,828
Common stock	<u>4,481,428</u>	<u>4,144,394</u>
	\$ <u>6,241,437</u>	<u>5,824,248</u>

Endowment investments consist primarily of the land grant endowment trust fund established pursuant to federal land grant legislation. Public Law 19-40 requires that the principal amount be held in trust in perpetuity. At September 30, 2006 and 2005, the accumulated net earnings and appreciation on investments is \$5,248,097 and \$4,736,479, respectively. These amounts, which are recorded in the restricted expendable net assets category, are available for expenditure in accordance with spending policies established by the Board of Regents in its capacity as trustee. The Board of Regents is authorized by the above public law to manage investments consistent with the University's investment policy.

UNIVERSITY OF GUAM

Notes to Financial Statements September 30, 2006 (with comparative information for 2005)

7. Deposits and Investments, continued

B. Investments, Continued

	<u>2006</u>	<u>2005</u>
Endowment investments:		
Money market funds	\$ 239,195	410,486
Fixed income securities	1,963,047	1,820,901
Common stock	<u>6,045,855</u>	<u>5,505,090</u>
	<u>\$ 8,248,097</u>	<u>7,736,477</u>

The composition of investment income (expense) for the years ended September 30, 2006 and 2005, is as follows:

	<u>2006</u>	<u>2005</u>
Interest and dividends from investments	\$ 550,278	740,183
Investment fees	(131,202)	(169,655)
Realized (loss) gain	(366,436)	(157,222)
Appreciation of fair value of investments, net	<u>805,121</u>	<u>1,152,208</u>
	<u>\$ 857,761</u>	<u>1,565,514</u>

GASB Statement No. 40 amended GASB Statement No.3 to in effect eliminate disclosure for investments falling into categories 1 and 2, and provided for disclosure requirements addressing other common risks of investments such as credit risk, interest rate risk, concentration of credit risk, and foreign currency risk. GASB Statement No. 40 did retain and expand the element of custodial credit risk in GASB Statement No.3. As of September 30, 2006, the University's fixed income securities had the following maturities and credit risk exposure.

<u>Investment type</u>	<u>Fair value</u>	<u>Less than 1</u>	<u>1 to 5</u>	<u>5 to 10</u>	<u>More than 10</u>
Corporate bonds	\$ 162,242	-	63,516	58,457	40,269
Mortgage and asset backed securities	784,884	22,194	37,277	-	725,413
Government bonds:					
Federal Home Loan Mortgage Corp.	580,693	-	219,973	71,110	289,610
Federal National Mortgage Association	428,524	-	9,684	418,840	-
U.S. Treasuries	<u>1,426,643</u>	<u>525,243</u>	<u>391,913</u>	<u>195,201</u>	<u>314,286</u>
	<u>\$ 3,382,986</u>	<u>547,437</u>	<u>722,363</u>	<u>743,608</u>	<u>1,369,578</u>

UNIVERSITY OF GUAM

Notes to Financial Statements
September 30, 2006
(with comparative information for 2005)

7. Deposits and Investments, continued

B. Investments, Continued

The University's exposure to credit risk at September 30, 2006 was as follows:

<u>Moody's Rating</u>	<u>Total</u>	<u>Domestic</u>	<u>International</u>
AAA/AAA	\$ 3,171,027	3,171,027	-
AAA	49,717	49,717	-
AA3/AA-	52,693	52,693	-
AA3/A+	51,092	51,092	-
AA2/A+	<u>58,457</u>	<u>58,457</u>	<u>-</u>
Total credit risk debt securities	\$ <u>3,382,986</u>	<u>3,382,986</u>	<u>-</u>

Custodial credit risk for investments is the risk that in the event of the failure of the counterparty to the transaction, the University will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The University's investments are held and administered by investment managers. Accordingly, these investments are exposed to custodial credit risk. Based on negotiated trust and custody contracts, all of these investments were held in the University's name at September 30, 2006 and 2005.

Concentration of credit risk for investments is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. GASB Statement No. 40 requires disclosure by issuer and amount of investments in anyone issuer that represents five percent (5%) or more of total investments of the University. As of September 30, 2006 and 2005 the University's investment in agency obligations of Federal National Mortgage Association constituted 6.7% and 5%, respectively, of its total investments.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of debt instruments. The University has a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

UNIVERSITY OF GUAM

Notes to Financial Statements September 30, 2006 (with comparative information for 2005)

8. Capital Assets

Activity and balances for capital assets for fiscal year 2006 and 2005 consisted of the following:

	Balance September 30, <u>2005</u>	<u>Additions</u>	<u>Retirements</u>	Balance September 30, <u>2006</u>
Capital assets not being depreciated:				
Land	\$ 2,589,112	-	-	2,589,112
Construction in progress	<u>7,213,149</u>	<u>1,747,095</u>	<u>8,727,797</u>	<u>232,447</u>
Total capital assets not being depreciated	<u>9,802,261</u>	<u>1,747,095</u>	<u>8,727,797</u>	<u>2,821,559</u>
Other capital assets:				
Land improvements	320,754	-	-	320,754
Building	70,374,222	13,738,262	-	84,112,484
Building improvements	1,241,760	-	-	1,241,760
Equipment	8,417,530	1,057,596	12,965	9,462,161
Library books	<u>4,916,919</u>	<u>320,846</u>	-	<u>5,237,765</u>
Total other capital assets	85,271,185	15,116,704	12,965	100,374,924
Less accumulated depreciation	<u>(27,563,740)</u>	<u>(2,241,174)</u>	<u>(12,965)</u>	<u>(29,791,949)</u>
Other capital assets, net	<u>57,707,445</u>	<u>12,875,530</u>	-	<u>70,582,975</u>
Total capital assets, net	\$ <u>67,509,706</u>	<u>14,622,625</u>	<u>8,727,797</u>	<u>73,404,534</u>

	Balance September 30, <u>2004</u>	<u>Additions</u>	<u>Retirements</u>	Balance September 30, <u>2005</u>
Capital assets not being depreciated:				
Land	\$ 2,589,112	-	-	2,589,112
Construction in progress	<u>1,497,821</u>	<u>5,715,328</u>	-	<u>7,213,149</u>
Total capital assets not being depreciated	<u>4,086,933</u>	<u>5,715,328</u>	-	<u>9,802,261</u>
Other capital assets:				
Land improvements	320,754	-	-	320,754
Building	71,370,222	-	996,000	70,374,222
Building improvements	1,241,760	-	-	1,241,760
Equipment	8,284,837	437,110	304,417	8,417,530
Library books	<u>4,709,114</u>	<u>207,805</u>	-	<u>4,916,919</u>
Total other capital assets	85,926,687	644,915	1,300,417	85,271,185
Less accumulated depreciation	<u>(26,368,740)</u>	<u>(2,405,825)</u>	<u>(1,210,825)</u>	<u>(27,563,740)</u>
Other capital assets, net	<u>59,557,947</u>	<u>(1,760,910)</u>	<u>89,592</u>	<u>57,707,445</u>
Total capital assets, net	\$ <u>63,644,880</u>	<u>3,954,418</u>	<u>89,592</u>	<u>67,509,706</u>

9. Encumbrances

The accrual basis of accounting provides that expenses include only amounts associated with goods and services received and liabilities include only the unpaid amounts associated with such expenses. Accordingly, at September 30, 2006 and 2005, \$4,756,299 and \$9,174,541, respectively, of outstanding purchase orders and purchase commitments are not reported in the financial statements.

UNIVERSITY OF GUAM

Notes to Financial Statements September 30, 2006 (with comparative information for 2005)

10. Contingencies

Litigation

The University is a defendant in several legal actions. The ultimate outcome is presently undeterminable; however, University management is of the opinion that resolution of these matters will not have a material effect on the accompanying financial statements.

General Obligation Bonds

In October 1993, the Government of Guam issued \$175 million general obligation bonds to fund the construction of certain educational facilities with \$28 million being earmarked for certain construction projects at the University of Guam. The University is mandated by Public Law No. 22-19 (as amended by Public Law 23-14) to establish a bond fund and deposit all tuition revenues in the bond fund. Monthly remittances are transferred by the University of Guam to the Government of Guam's General Fund to cover the University's proportionate share of principal and interest payments of the bond. At the end of each fiscal year, the balance remaining in the bond fund established by the University shall be retained by the University. Once the University's proportionate share of the principal and interest obligation is satisfied on or about November 2018, the University shall retain control of all future revenues thereafter. For the years ended September 30, 2006 and 2005, monthly payments remitted to the Government of Guam's General Fund of \$2,027,302 and \$2,027,291, respectively, are recorded as debt service - DOA bond.

Medicare

The Government of Guam and its component units, including the University, began withholding and remitting funds to the U.S. Social Security System for the health insurance component of its salaries and wages effective October 1998. Prior to that date, the Government of Guam did not withhold or remit Medicare payments to the U.S. Social Security System. If the Government is found to be liable for Medicare payments on salaries and wages prior to October 1998, an indeterminate liability could result. It has been the practice of the University and all other component units of the Government of Guam that payment of this health insurance component is optional prior to October 1998. Therefore, no liability for any amount which may ultimately arise from this matter has been recorded in the accompanying financial statements.

UNIVERSITY OF GUAM

Notes to Financial Statements September 30, 2006 (with comparative information for 2005)

11. Receivable from the Government of Guam

The University reflects a receivable from the Government of Guam of \$3,350,000 at September 30, 2006. This is after reducing the receivable by about \$2.7 million based on an agreed-upon reduction in the total appropriation for fiscal year 2006. Subsequently in November 2006, the University received \$109,558 for the Yamashita Educator Corps, a Student Financial Assistance Program which was consolidated into the School of Education beginning in fiscal year 2007. Management does expect the balance at September 30, 2006 to be collected on or before September 30, 2007 or within a reasonable time thereafter.

The Government of Guam is experiencing serious financial difficulty. University management is working closely with the appropriate Government of Guam and Legislature officials to ensure that it maintains financial viability and does not jeopardize its accreditation status.

UNIVERSITY OF GUAM

Schedule of Salaries and Wages
 Year ended September 30, 2006
 (with comparative figures for 2005)

	2006		2005	
	<u>Amount</u>	<u>No. of Personnel</u>	<u>Amount</u>	<u>No. of Personnel</u>
SALARIES AND WAGES:				
Funded by local funds	\$17,967,027	384	\$16,951,035	388
Funded by Federal funds	4,852,099	203	4,310,285	168
Funded by both local and Federal funds	2,315,590	49	2,521,783	47
Other funding sources	<u>3,368,291</u>	<u>196</u>	<u>3,302,846</u>	<u>211</u>
Total salaries and wages	<u>28,503,007</u>	<u>832</u>	<u>27,085,949</u>	<u>814</u>
 BENEFITS:				
Funded by local funds	4,856,457		4,364,917	
Funded by Federal funds	1,114,767		1,251,853	
Funded by both local and Federal funds	307,820		78,912	
Other funding sources	<u>608,052</u>		<u>572,896</u>	
Total benefits	<u>6,887,096</u>		<u>6,268,578</u>	
Salaries, Wages and Benefits Total	<u>\$35,390,103</u>		<u>\$33,354,527</u>	

See accompanying independent auditors' report.

UNIVERSITY OF GUAM

Schedule of Expenses by Object Category
 Year ended September 30, 2006
 (with comparative figures for 2005)

	<u>2006</u>		<u>2005</u>	
	<u>Unrestricted</u>	<u>Restricted</u>	<u>Unrestricted</u>	<u>Restricted</u>
Instruction:				
Salary	\$ 10,302,148	842,798	9,550,891	556,220
Benefits	2,477,565	121,869	2,173,813	88,760
Travel	151,754	175,969	55,583	295,673
Contractual	691,310	1,131,627	572,061	512,551
Supplies	98,844	139,569	80,577	166,114
Equipment	22,119	66,415	50,844	217,870
Utilities	23,095	31,472	24,904	24,115
Capital outlay	4,967	75,146	-	-
Miscellaneous	123,946	353,616	96,787	350,873
	<u>13,895,748</u>	<u>2,938,481</u>	<u>12,605,460</u>	<u>2,212,176</u>
Research:				
Salary	941,639	3,417,756	735,278	3,525,431
Benefits	232,953	728,407	184,001	712,879
Travel	94,504	729,369	90,991	692,274
Contractual	343,844	1,402,935	289,122	1,229,462
Supplies	94,084	434,167	106,963	478,924
Equipment	88,063	242,424	54,427	370,346
Utilities	307	4,902	297	2,670
Capital outlay	88,118	101,097	79,753	162,698
Miscellaneous	22,704	706,587	39,872	636,447
	<u>1,906,216</u>	<u>7,767,644</u>	<u>1,580,704</u>	<u>7,811,131</u>
Institutional Support:				
Salary	2,495,859	-	2,515,585	-
Benefits	740,869	-	687,762	-
Travel	207,572	-	182,966	-
Contractual	2,066,609	-	2,348,417	-
Supplies	94,609	-	75,103	-
Equipment	28,880	-	35,520	-
Utilities	768	-	31	-
Capital outlay	11,490	-	126,043	(566,341)
Miscellaneous	477,907	-	452,277	-
	<u>6,124,563</u>	<u>-</u>	<u>6,423,704</u>	<u>(566,341)</u>

See accompanying independent auditors' report.

UNIVERSITY OF GUAM

Schedule of Expenses by Object Category Year ended September 30, 2006 (with comparative figures for 2005)

	<u>2006</u>		<u>2005</u>	
	<u>Unrestricted</u>	<u>Restricted</u>	<u>Unrestricted</u>	<u>Restricted</u>
Public Service:				
Salary	292,779	2,867,504	284,373	2,750,417
Benefits	74,856	569,404	70,199	529,125
Travel	4,218	394,883	5,419	402,354
Contractual	23,503	981,688	36,156	592,184
Supplies	23,021	295,970	31,132	215,994
Equipment	1,997	214,225	9,539	217,799
Utilities	10,518	18,056	8,701	18,764
Capital outlay	-	44,757	-	82,684
Miscellaneous	29,719	431,086	46,078	290,033
	<u>460,611</u>	<u>5,817,573</u>	<u>491,597</u>	<u>5,099,354</u>
Academic Support:				
Salary	3,587,737	-	3,563,956	-
Benefits	924,962	-	893,115	-
Travel	213,575	1,220	186,286	-
Contractual	972,831	20,101	1,010,803	77,789
Supplies	241,321	1,852	346,656	4,696
Equipment	184,904	-	405,331	28,194
Utilities	2,756	-	2,525	-
Capital outlay	68,889	339,591	72,525	153,881
Miscellaneous	62,100	-	52,775	-
	<u>6,259,075</u>	<u>362,764</u>	<u>6,533,972</u>	<u>264,560</u>
Student Services:				
Salary	1,598,027	455,128	1,497,480	421,709
Benefits	435,032	2,907	390,630	-
Travel	38,210	12,441	35,509	-
Contractual	156,302	13,335	141,757	3,373
Supplies	56,205	3,215	91,054	2,473
Equipment	38,361	9,135	92,657	5,297
Utilities	35,839	-	40,727	-
Capital outlay	-	-	390	-
Miscellaneous	129,283	706,587	358,053	-
	<u>2,487,259</u>	<u>1,202,748</u>	<u>2,648,257</u>	<u>432,852</u>

See accompanying independent auditors' report.

UNIVERSITY OF GUAM

Schedule of Expenses by Object Category
 Year ended September 30, 2006
 (with comparative figures for 2005)

	<u>2006</u>		<u>2005</u>	
	<u>Unrestricted</u>	<u>Restricted</u>	<u>Unrestricted</u>	<u>Restricted</u>
Operations and Maintenance:				
Salary	1,325,043	-	1,243,037	-
Benefits	389,531	-	346,591	-
Travel	-	-	-	-
Contractual	182,201	-	419,250	-
Supplies	186,603	-	187,318	-
Equipment	29,132	-	86,979	-
Utilities	2,996,246	-	2,533,224	-
Capital outlay	114,791	-	464,644	-
Miscellaneous	969	-	1,433	64,914
	<u>5,224,516</u>	<u>-</u>	<u>5,282,476</u>	<u>64,914</u>
Scholarships and Fellowships:				
Salary	-	-	-	-
Benefits	-	-	-	-
Travel	-	-	-	-
Contractual	-	-	-	-
Supplies	-	-	-	-
Equipment	-	-	-	-
Utilities	-	-	-	-
Capital outlay	-	-	-	-
Miscellaneous	7,546,054	-	161,911	6,989,037
	<u>7,546,054</u>	<u>-</u>	<u>161,911</u>	<u>6,989,037</u>
Auxiliary Enterprises:				
Salary	592,644	-	602,662	-
Benefits	151,021	-	143,785	-
Travel	7,258	-	3,121	-
Contractual	118,729	-	116,266	-
Supplies	52,251	-	44,322	-
Equipment	14,760	-	22,073	-
Utilities	221,081	-	175,106	-
Capital outlay	-	-	-	-
Miscellaneous	1,215,129	-	1,148,048	-
	<u>2,372,873</u>	<u>-</u>	<u>2,255,383</u>	<u>-</u>

See accompanying independent auditors' report.