STATE OF ILLINOIS
GOVERNORS STATE UNIVERSITY

FINANCIAL AUDIT
For the Year Ended June 30, 2012

Performed as Special Assistant Auditors for
the Auditor General, State of Illinois

E.C. ORTIZ & CO., LLP
CERTIFIED PUBLIC ACCOUNTANTS

STATE OF ILLINOIS
GOVERNORS STATE UNIVERSITY
FINANCIAL AUDIT
FOR THE YEAR ENDED JUNE 30, 2012

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Related Report Issued Under a Separate Cover

Governors State University
Compliance Examination (In Accordance with the Single Audit Act and OMB Circular A-133) for the Year Ended June 30, 2012

STATE OF ILLINOIS
GOVERNORS STATE UNIVERSITY
FINANCIAL AUDIT
FOR THE YEAR ENDED JUNE 30, 2012

Agency Officials

President	Dr. Elaine Maimon
Executive Vice President, Chief of Staff, Treasurer	Dr. Gebeyehu Ejigu
Vice President, Administration and Finance	Ms. Karen Kissel
Internal Auditor	Mr. David Dixon
Interim Comptroller	Ms. Cathy Casson, CPA (until 08/24/12)
Controller	Ms. Melinda Gieseke, CPA (as of 07/16/12)

Agency offices are located at:

1 University Parkway
University Park, Illinois 60484

STATE OF ILLINOIS
GOVERNORS STATE UNIVERSITY
FINANCIAL AUDIT
FOR THE YEAR ENDED JUNE 30, 2012

Financial Statement Report

Summary

The audit of the accompanying basic financial statements of Governors State University (University) was performed by E.C. Ortiz and Co., LLP.

Based on their audit, the auditors expressed an unqualified opinion on the University's basic financial statements.

Summary of Findings

The auditors identified a matter involving the University's internal control over financial reporting that they considered to be a material weakness. The material weakness is described in the accompanying Schedule of Findings listed in the table of contents as finding 12-1, *Financial Adjustments*.

Exit Conference

The finding and recommendation appearing in this report was discussed with University personnel at an exit conference on April 18, 2013. Attending were:

<u>Representing Governors State University</u>	
Executive Vice President, Chief of Staff, Treasurer	Dr. Gebeyehu Ejigu
Vice President, Administration and Finance	Ms. Karen Kissel
Internal Auditor	Mr. David Dixon
Controller	Ms. Melinda Gieseke
Assistant Controller	Ms. Andrea Middleton
<u>Representing E.C. Ortiz and Co., LLP</u>	
Partner	Mr. Edilberto C. Ortiz
Partner	Ms. Gilda B. Priebe
Manager	Ms. Villalyn S. Baluga
<u>Representing the Office of the Auditor General</u>	
Audit Manager	Mr. Jose G. Roa

The response to the recommendation was provided by Ms. Karen Kissel in a letter dated April 19, 2013.

E.C. ORTIZ & CO., LLP
CERTIFIED PUBLIC ACCOUNTANTS

INDEPENDENT AUDITORS' REPORT

Honorable William G. Holland
Auditor General
State of Illinois

and

The Board of Trustees
Governors State University

As Special Assistant Auditors for the Auditor General, we have audited the accompanying basic financial statements of the business-type activities of the Governors State University (University) and its aggregate discretely presented component unit, collectively a component unit of the State of Illinois, as of and for the year ended June 30, 2012, which collectively comprise the University's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the financial statements of the aggregate discretely presented component unit. The financial statements of the discretely presented component unit was audited by other auditors whose report thereon has been provided to us, and our opinion, insofar as it relates to the amounts included for the aggregate discretely presented component unit, is based solely on the report of the other auditors. The prior year partial comparative information has been derived from the University's June 30, 2011 financial statements and in our report dated February 8, 2012 we expressed an unqualified opinion on the respective financial statements of the business-type activities and the aggregate discretely presented component unit.

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. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and the aggregate discretely presented component unit of the University, as of June 30, 2012, and the respective changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

333 SOUTH DES PLAINES STREET, SUITE 2-N CHICAGO, IL 60661 tel: 312.876.1900 fax: 312.876.1911

In accordance with *Government Auditing Standards*, we have also issued a report dated April 19, 2013 on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion 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.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 5 through 12 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the University's basic financial statements. The University Facilities System Revenue Bonds financial statements and related information, listed as supplementary information in the table of contents, are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The University Facilities System Revenue Bonds financial statements and related information, listed as supplementary information in the table of contents, have been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America by us and other auditors. In our opinion, based on our audit, the procedures performed as described previously, and the report of the other auditors, the University Facilities System Revenue Bonds financial statements and related information, listed as supplementary information in the table of contents, are fairly stated in all material respects in relation to the basic financial statements as a whole.

E.C. Ortiz & Co., LLP

Chicago, Illinois
April 19, 2013

STATE OF ILLINOIS
GOVERNORS STATE UNIVERSITY
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE YEAR ENDED JUNE 30, 2012

PURPOSE

This section of the Governors State University's (GSU or University) annual financial report presents an analysis and overview of the financial activities of the University for the fiscal year ended June 30, 2012. The GSU Foundation is considered a component unit of the University. Separate financial statements for the Foundation may be obtained by writing the: Vice President for University Advancement, Governors State University, 1 University Parkway, University Park, Illinois 60484.

The financial statement presentation focuses on the University as a whole. The financial statements are designed to emulate corporate presentation models whereby all University activities are consolidated into one total. The focus of the Statement of Net Assets is designed to be similar to bottom line results for the University; it combines and consolidates current financial resources with capital assets. The Statement of Revenues, Expenses and Changes in Net Assets focuses on both the gross and net costs of University activities, which are supported mainly by State appropriations and tuition revenues. The Statement of Cash Flows presents the receipt and use of cash resources by the University. This approach is intended to summarize and simplify the user's analysis of the cost of services provided.

FINANCIAL AND ENROLLMENT HIGHLIGHTS

<u>Accreditations</u>
During fiscal year 2010, the Higher Learning Commission team completed its review and reaccredited GSU for the maximum number of years (ten years, with the next reaffirmation scheduled for academic year 2019-2020).

<u>Appropriations</u>
For fiscal year 2012, the University received State appropriations for general operations.

The fiscal year 2012 total appropriation used to fund ongoing core programs constituted a decrease of 1% over the fiscal year 2011 appropriation.

Net Revenue Available from Operational Appropriations

Fiscal Years	Appropriations	Payments to Health Reserve Fund	Available Appropriations
2012	$ 26,253,400	$ (656,200)	$ 25,597,200
2011	26,558,000	(656,200)	25,901,800

Enrollment

Student credit hours billed during fiscal year 2012 increased by 1.5% from the levels of fiscal year 2011; from 114,853 to 116,570.

Sick and Vacation Payouts

Many of the University's faculty and staff were hired after the University was chartered in 1969 and are now approaching retirement. For the past three years, sick and vacation payouts have averaged near $0.5 million; we anticipate that payouts will continue at this rate.

Statement of Net Assets

The Statement of Net Assets includes all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector institutions. Net assets represent the University's equity and are a way to measure the financial health of the University.

	(in thousands)			
	2012	2011	Change	Percent Change
Current assets	$ 74,641	$ 50,544	$ 24,097	48%
Noncurrent assets	85,808	82,053	3,755	5%
Total assets	160,449	132,597	27,852	21%
Current liabilities	9,725	9,415	310	3%
Noncurrent liabilities	54,182	35,315	18,867	53%
Total liabilities	63,907	44,730	19,177	43%
Net assets	$ 96,542	$ 87,867	$ 8,675	10%

The 10% increase in the University's net assets is due to the following:

Current Assets

Current assets consist primarily of cash and cash equivalents, and receivables. Unrestricted cash increased by $8.1 million primarily due to increased tuition and fee revenues, more timely payments of State appropriation from the State of Illinois, and delayed processing of accounts payable due to the University's conversion to a new Enterprise Resource Planning (ERP) system. Restricted cash increased by $18.6 million primarily due to the issuance of the $20.4 million Revenue Bonds, Series 2012 during the fiscal year 2012. Accounts receivable increased by $1.4 million primarily due to a more customer friendly payment plans offered by the University during the academic year 2011-2012, and increase in tuition and fee revenues brought about by the 1.5% increase in student credit hours and 3% increase in the average tuition and fee rates. Grants receivable decreased by $0.5 million primarily due to the decreased grants and contracts revenues and timely draw downs of federal grants during fiscal year 2012. State appropriation receivable decreased by $3.4 million primarily due to timely payments of State appropriation from the State of Illinois.

Noncurrent Assets

Noncurrent assets consist primarily of long-term portion of student loans receivable, unamortized costs of issuance for the revenue bonds and certificates of participation, and capital assets net of accumulated depreciation. Student loans increased by $0.5 million primarily due to the timing of collections of loans from students and the set-up of loans receivable related to the Nursing Faculty Loan Program grant. Debt issuance costs increased by $0.4 million primarily due to the issuance costs incurred by the University in relation to the Revenue Bonds, Series 2012 issued during the fiscal year 2012. Capital assets net of depreciation increased by $2.8 million primarily due to the substantial completion of deferred maintenance projects that have been underway for the past five years and the ongoing construction of the University's E and F buildings as funded by the Capital Development Board.

Current Liabilities

Current liabilities include accounts payable, agency funds payable, accrued compensated absences, deferred revenue, and the current portion of long-term liabilities, which are payable in less than one year. Accounts payable increased by $0.7 million primarily due to timing differences on vendor payments and delayed processing of payables due to the University's conversion to a new ERP system. Deferred revenue decreased by $0.5 million primarily due to the lower number of credit hours during the summer 2012 term.

Noncurrent Liabilities

Noncurrent liabilities are liabilities with due dates beyond one year, which include accrued compensated absences, refundable grants, revenue bonds payable, notes payable, and certificates of participation. The $18.9 million increase in noncurrent liabilities was mainly due to the issuance of the $20.4 million Revenue Bonds, Series 2012 during fiscal year 2012. This increase was partially offset by the $1.7 million principal payments in revenue bonds payable, notes payable, and certificates of participation.

More detailed information about the University's long-term debt is presented in the notes to the basic financial statements.

Statement of Revenues, Expenses and Changes in Net Assets

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

	(in thousands)			
	2012	2011	Change	Percent Change
OPERATING REVENUES				
Net student tuition and fees	$ 33,072	$ 30,499	$ 2,573	8%
Grants and contracts	8,403	9,546	(1,143)	-12%
Sales and services of educational Departments	6,259	6,264	(5)	0%
Auxiliary enterprises	1,307	1,671	(364)	-22%
Other operating revenues	2,169	1,686	483	29%
Total operating revenues	51,210	49,666	1,544	3%
OPERATING EXPENSES	99,736	91,911	7,825	9%
Net operating loss	(48,526)	(42,245)	(6,281)	15%

Statement of Revenues, Expenses and Changes in Net Assets (Continued)

	(in thousands)			
	2012	2011	Change	Percent Change
NONOPERATING REVENUES (EXPENSES)				
State appropriation	26,253	26,558	(305)	-1%
Payments made on behalf of the University	22,668	18,832	3,836	20%
Federal Pell grant	6,607	6,519	88	1%
Investment income	27	38	(11)	-29%
Interest expense	(1,162)	(296)	(866)	293%
Capital additions provided by the State of Illinois	2,812	283	2,529	894%
Other nonoperating expense	(4)	(11)	7	-64%
Net nonoperating revenues	57,201	51,923	5,278	10%
Increase in net assets	8,675	9,678	(1,003)	-10%
Net assets - beginning of year	87,867	78,189	9,678	12%
Net assets - end of year	$ 96,542	$ 87,867	$ 8,675	10%

Increase in Net Assets
This year, the increase in net assets was 10% or $1.0 million lower than fiscal year 2011 due to the following:

Operating Revenues
Student tuition and fees increased by $2.6 million primarily due to the 1.5% increase in student credit hours and 3% increase in the average tuition and fee rates. Grants and contracts decreased by $1.1 million mostly due to the decrease in federal grants and contracts. Auxiliary enterprises decreased by $0.4 million mostly due to the decrease in the Center for Performing Arts revenues attributable to the decrease in ticket sales and rentals. Other operating revenues increased by $0.5 million mostly due to the increase in revenues related to the University's Family Development Center and South Metropolitan Higher Education Consortium.

Operating Expenses (by functional classification)

	(in thousands)			
	2012	2011	Change	Percent Change
Instruction	$ 46,092	$ 41,840	$ 4,252	10%
Research	1,020	1,092	(72)	-7%
Public service	14,695	13,868	827	6%
Academic support	2,009	2,231	(222)	-10%
Student services	6,688	6,225	463	7%
Institutional support	16,506	14,979	1,527	10%
Operation and maintenance of plant	8,096	6,992	1,104	16%
Auxiliary enterprises	1,072	1,519	(447)	-29%
Depreciation	3,558	3,165	393	12%
	$ 99,736	$ 91,911	$ 7,825	9%

Instruction increased by $4.3 million mostly due to the increase in salaries and benefits expense attributable to the increase in allocated on behalf payments made by the State. Academic support decreased by $0.2 million mostly due to lower operating expenses by the University's library operations. Institutional support increased by $1.5 million primarily due to the increase in aid internally provided by the University in response to the decreased financial aid from outside sources. Operation and maintenance of plant increased by $1.1 million mostly due to the increase in salaries and benefits expense attributable to the increase in allocated on behalf payments made by the State, and the overall increase in operating costs. Auxiliary enterprises decreased by $0.4 million mostly due to lower production costs incurred by the University's Center for Performing Arts. Depreciation increased by $0.4 million primarily due to the substantial completion of deferred maintenance projects that have been underway for the past five years.

Operating Expenses (by natural classification)

	(in thousands)			
	2012	2011	Change	Percent Change
Salaries and benefits	$ 74,924	$ 69,410	$ 5,514	8%
Scholarships and awards	4,552	2,108	2,444	116%
Capital expenditures	1,442	1,122	320	29%
Services, supplies and others	15,260	16,106	(846)	-5%
Depreciation	3,558	3,165	393	12%
	$ 99,736	$ 91,911	$ 7,825	9%

Salaries and benefits, representing the University's largest operating expense, increased by $5.5 million mostly due to the 20% increase in on behalf payments made by the State. Scholarships and awards increased by $2.4 million primarily due to the increase in aid internally provided by the University in response to the decreased financial aid from outside sources. Capital expenditures increased by $0.3 million primarily due to the ongoing construction of the University's E and F buildings.

<u>Nonoperating Revenues (Expenses)</u>
Payments made by the State on behalf of the University to fund retirement, health, life, and dental insurance benefits for University employees and retirees are paid directly by other State agencies on behalf of the University. In fiscal year 2012, the State's funding of retirement benefits increased by $2.1 million and its funding of health care increased by $1.7 million. Interest expense increased by $0.9 million primarily due to the noncapitalization of interest expense related to Revenue Bonds, Series 2007 and Certificates of Participation, Series 2008 as the related projects funded by these debts were already fully completed during the fiscal year 2012. Capital additions provided by the State of Illinois increased by $2.5 million primarily due to the additional funding from the Capital Development Board for the construction of the University's E and F buildings.

Statement of Cash Flows

The Statement of Cash Flows provides information about cash receipts and cash payments received and made during the year. This statement also helps users assess the University's ability to generate net cash flows, its ability to meet its obligations as they become due, and its need for external financing.

	(in thousands)			
	2012	2011	Change	Percent Change
Cash provided by (used in):				
Operating activities	$ (23,634)	$ (21,266)	$ (2,368)	11%
Noncapital financing activities	36,822	27,460	9,362	34%
Capital financing activities	13,511	(9,832)	23,343	-237%
Investing activities	27	38	(11)	-29%
Net increase (decrease) in cash and cash equivalents	26,726	(3,600)	30,326	-842%
Cash and cash equivalents - beginning of year	33,294	36,894	(3,600)	-10%
Cash and cash equivalents - end of year	$ 60,020	$ 33,294	$ 26,726	80%

The primary cash receipts from operating activities consist of student tuition and fees and grants and contracts revenues. Cash outlays include payment of wages, benefits, services, supplies, and scholarships. Net cash used in operating activities increased primarily due to the increase in overall operating expenses. Cash provided by noncapital financing activities improved since significant amount of the fiscal year 2011 State appropriation was collected from the State of Illinois during fiscal year 2012, in addition to more timely payments of State appropriation from the State of Illinois during fiscal year 2012. Net cash provided by (used in) capital financing activities significantly improved due to the issuance of the $20.4 million Revenue Bonds, Series 2012, and the substantial completion of deferred maintenance projects that have been underway for the past five years.

FACTORS AFFECTING FUTURE OPERATIONS

The strongest effects on the financial operations of the University in fiscal year 2013 and beyond will lie in:

- The University's success on creating the lower-division program and admitting lower-division students starting fall 2014. On December 6, 2011, the Illinois Board of Higher Education authorized the University to admit freshman and sophomore students in 2014.
- The 6% reduction in the fiscal year 2013 State appropriation from fiscal year 2012.
- The University's continuous success with the dual degree programs, which built pathways from the Illinois community colleges to Governors State University.
- The University's ability to continue to innovate with new quality program offerings to the community.
- The University's ability to market itself to new and continuing students to continue to increase registered student credit hours.

STATE OF ILLINOIS
GOVERNORS STATE UNIVERSITY
STATEMENT OF NET ASSETS

	JUNE 30,			
	2012		(Comparative totals only) 2011	
	University	Component Unit	University	Component Unit
ASSETS				
Current assets				
Cash and cash equivalents (Notes 2 and 3)	$ 36,666,214	$ 589,155	$ 28,587,392	$ 716,116
Cash and cash equivalents, restricted (Notes 2, 3 and 4)	23,353,814	-	4,706,536	-
Accounts receivable, net of allowance for uncollectible accounts of $4,092,600 (Note 2)	4,358,228	10,606	2,998,668	67,796
Grants receivable (Note 2)	1,629,390	-	2,152,285	-
State appropriation receivable	8,157,160	-	11,534,898	-
Student loans - current (Note 2)	323,010	-	397,000	-
Unamortized debt issuance costs - current (Note 2)	37,297	-	50,095	-
Inventories (Note 2)	76,712	-	65,883	-
Other assets	39,120	-	50,905	-
Total current assets	74,640,945	599,761	50,543,662	783,912
Noncurrent assets				
Investments (Notes 2 and 3)	-	1,502,387	-	1,202,868
Student loans, net of allowance for uncollectible loans of $766,000 (Note 2)	2,921,681	-	2,386,027	-
Unamortized debt issuance costs (Note 2)	962,897	-	533,293	-
Other noncurrent assets (Note 2)	168,703	-	149,497	-
Capital assets (Note 7)	137,233,171	1,717,356	131,347,826	1,614,351
Accumulated depreciation (Note 7)	(55,478,675)	-	(52,363,347)	-
Total noncurrent assets	85,807,777	3,219,743	82,053,296	2,817,219
Total assets	160,448,722	3,819,504	132,596,958	3,601,131
LIABILITIES				
Current liabilities				
Accounts payable	3,885,366	52,366	3,224,012	11,348
Agency funds payable	203,953	-	149,101	-
Accrued compensated absences (Notes 2 and 9)	500,000	-	500,000	-
Deferred revenue (Note 2)	3,315,333	-	3,806,802	-
Revenue bonds payable (Note 8)	350,853	-	336,738	-
Notes payable (Note 8)	451,889	-	410,958	-
Certificates of participation (Note 8)	1,017,672	-	987,672	-
Total current liabilities	9,725,066	52,366	9,415,283	11,348
Noncurrent liabilities				
Accrued compensated absences (Notes 2 and 9)	4,121,197	-	4,355,661	-
Refundable grants	3,611,829	-	3,067,701	-
Revenue bonds payable (Note 8)	27,729,775	-	7,691,945	-
Notes payable (Note 8)	3,145,401	-	3,608,452	-
Certificates of participation (Note 8)	15,573,243	-	16,590,915	-
Total noncurrent liabilities	54,181,445	-	35,314,674	-
Total liabilities	63,906,511	52,366	44,729,957	11,348
NET ASSETS (Note 2)				
Invested in capital assets, net of related debt	54,881,276	1,717,356	52,287,488	1,614,351
Restricted:				
Nonexpendable	-	1,338,404	-	1,236,831
Expendable				
Loans	675,534	-	607,744	-
Debt service	1,223,379	-	649,856	-
Other	-	695,055	-	712,140
Unrestricted	39,762,022	16,323	34,321,913	26,461
Total net assets	$ 96,542,211	$ 3,767,138	$ 87,867,001	$ 3,589,783

The accompanying notes to basic financial statements are an integral part of this statement.

STATE OF ILLINOIS
GOVERNORS STATE UNIVERSITY
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

	FOR THE YEAR ENDED JUNE 30,			
	2012		(Comparative totals only) 2011	
	University	Component Unit	University	Component Unit
OPERATING REVENUES				
Student tuition and fees, net of scholarship allowances of $5,576,946 (Note 2)	$ 33,071,685	$ -	$ 30,499,092	$ -
Federal grants and contracts	6,547,597	-	7,687,585	-
State grants and contracts	1,326,691	-	982,355	-
Other grants and contracts	529,154	-	876,290	-
Sales and services of educational departments	6,258,494	-	6,263,669	-
Auxiliary enterprises	1,306,975	-	1,671,660	-
Other operating revenues	2,169,073	207,928	1,685,746	192,706
Total operating revenues	51,209,669	207,928	49,666,397	192,706
OPERATING EXPENSES				
Instruction	46,092,139	-	41,840,108	-
Research	1,019,479	-	1,092,589	-
Public service	14,695,209	-	13,867,709	-
Academic support	2,008,781	-	2,230,926	-
Student services	6,688,295	-	6,224,729	-
Institutional support	16,505,830	-	14,978,608	-
Operation and maintenance of plant	8,096,132	-	6,991,748	-
Auxiliary enterprises	1,071,820	-	1,519,539	-
Depreciation	3,558,226	-	3,165,298	-
University support	-	312,308	-	242,521
Other expense	-	246,985	-	216,809
Total operating expenses	99,735,911	559,293	91,911,254	459,330
Net operating loss	(48,526,242)	(351,365)	(42,244,857)	(266,624)
NONOPERATING REVENUES (EXPENSES)				
State appropriation	26,253,400	-	26,558,000	-
Payments made on behalf of the University	22,668,000	-	18,832,000	-
Federal Pell grant	6,606,874	-	6,519,196	-
Gifts	-	304,758	-	396,818
Investment income	25,835	19,384	30,660	99,269
Investment income on debt proceeds	1,505	-	7,005	-
Interest expense	(1,162,385)	-	(295,619)	-
Other nonoperating expense	(3,500)	-	(10,982)	-
Net nonoperating revenues	54,389,729	324,142	51,640,260	496,087
Income (loss) before other revenues, expenses, gains and losses	5,863,487	(27,223)	9,395,403	229,463
Capital additions provided by State of Illinois	2,811,723	-	282,600	-
Additions to permanent endowments	-	101,573	-	103,269
Capital asset contributions	-	103,005	-	76,000
Increase in net assets	8,675,210	177,355	9,678,003	408,732
NET ASSETS				
Net assets - beginning of year	87,867,001	3,589,783	78,188,998	3,181,051
Net assets - end of year	$ 96,542,211	$ 3,767,138	$ 87,867,001	$ 3,589,783

The accompanying notes to basic financial statements are an integral part of this statement.

STATE OF ILLINOIS
GOVERNORS STATE UNIVERSITY
STATEMENT OF CASH FLOWS

	FOR THE YEAR ENDED JUNE 30,			
			(Comparative totals only)	
	2012		2011	
	University	Component Unit	University	Component Unit
CASH FLOWS FROM OPERATING ACTIVITIES				
Student tuition and fees	$ 30,595,901	$ -	$ 29,512,767	$ -
Grants and contracts	8,644,123	-	9,361,034	-
Payments to suppliers	(15,267,303)	(269,156)	(16,837,915)	(185,236)
Payments for scholarships	(4,551,710)	(73,705)	(2,108,074)	(92,773)
Payments to employees and fringe benefits	(52,649,694)	-	(50,963,705)	-
Auxiliary enterprises	1,306,975	-	1,671,660	-
Sales and services of educational departments	6,258,494	-	6,263,669	-
Student loans issued	(389,317)	-	(167,600)	-
Student loans collected	248,803	-	316,559	-
Other operating revenues	2,169,073	32,514	1,685,746	13,020
Net cash used in operating activities	(23,634,655)	(310,347)	(21,265,859)	(264,989)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
State appropriations	29,631,138	-	21,463,527	-
Federal Pell grant	7,190,921	-	5,996,573	-
Contributions	-	361,948	-	392,618
Contributions for permanent endowments	-	101,573	-	103,269
Cash provided by noncapital financing activities	36,822,059	463,521	27,460,100	495,887
CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES				
Purchase of capital assets	(3,520,342)	-	(6,847,097)	-
Proceeds from issuance of debt, net	19,988,514	-	-	-
Principal payments on capital debt	(1,752,120)	-	(1,686,861)	-
Interest payments on capital debt	(1,204,696)	-	(1,297,596)	-
Net cash provided by (used in) capital financing activities	13,511,356	-	(9,831,554)	-
CASH FLOWS FROM INVESTING ACTIVITIES				
Proceeds from sales and maturities of investment securities	-	873,034	-	652,190
Investment income	27,340	25,661	37,665	15,986
Investment management fees	-	(15,832)	-	(11,068)
Purchase of investment securities	-	(1,162,998)	-	(1,333,567)
Net cash provided by (used in) investing activities	27,340	(280,135)	37,665	(676,459)
Net increase (decrease) in cash and cash equivalents	26,726,100	(126,961)	(3,599,648)	(445,561)
Cash and cash equivalents - beginning of year	33,293,928	716,116	36,893,576	1,161,677
Cash and cash equivalents - end of year	$ 60,020,028	$ 589,155	$ 33,293,928	$ 716,116
RECONCILIATION OF NET OPERATING LOSS TO NET CASH USED IN OPERATING ACTIVITIES:				
Net operating loss	$ (48,526,242)	$ (351,365)	$ (42,244,857)	$ (266,624)
Adjustments to reconcile net operating loss to net cash used in operating activities:				
Noncash expenses included in net operating loss:				
Depreciation	3,558,226	-	3,165,298	-
Payments made on behalf of the University	22,668,000	-	18,832,000	-
Changes in assets and liabilities:				
Accounts and grants receivable	(1,405,445)	-	(69,690)	-
Inventories	(10,829)	-	(32,282)	-
Other assets	11,785	-	425,205	-
Other noncurrent assets	(19,206)	-	(149,497)	-
Student loans	(461,664)	-	253,423	-
Accounts payable	692,940	41,018	(217,493)	1,635
Agency funds payable	54,852	-	(224,278)	-
Deferred revenue	(506,736)	-	(804,930)	-
Accrued compensated absences	(234,464)	-	(192,104)	-
Refundable grants	544,128	-	(6,654)	-
Net cash used in operating activities	$ (23,634,655)	$ (310,347)	$ (21,265,859)	$ (264,989)
NONCASH CAPITAL FINANCING AND INVESTING ACTIVITIES				
Capitalized interest payments	$ 161,051	$ -	$ 1,039,637	$ -
Unrealized gain (loss) on investments	$ -	$ (22,975)	$ -	$ 77,558
Donations of capital assets	$ -	$ 103,005	$ -	$ 76,000

The accompanying notes to basic financial statements are an integral part of this statement.

1. Financial Reporting Entity and Component Unit Disclosure

Governors State University (GSU or University) was chartered in 1969 to provide affordable and accessible undergraduate and graduate education to its culturally and economically diverse life-long learners in the Chicago metropolitan area. It is governed by the Board of Trustees of Governors State University created in January 1996 as a result of legislation to reorganize governance of State higher education institutions and provides liberal arts, science, and professional preparation at the upper-division, master and doctorial levels.

The financial reporting entity as defined by Governmental Accounting Standards Board (GASB) Statement No. 14, *The Financial Reporting Entity*, and GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units*, consists of the primary government, organizations for which the primary government is financially accountable and other organizations for which the nature and significance of their relationship with the primary government are such that exclusion could cause the financial statements to be misleading or incomplete. Accordingly, the financial statements include the accounts of Governors State University as the primary government, and the Governors State University Foundation (Foundation) as a component unit of the University.

The Foundation was incorporated as a not-for-profit organization in June 1969. The Foundation provides support services to the University to assist the University in achieving its educational, research, and service goals.

The audit of the Foundation's financial statements for the fiscal year ended June 30, 2012 was conducted by an independent certified public accountant. Complete financial statements for this component unit may be obtained by writing the: Vice President for University Advancement, Governors State University, 1 University Parkway, University Park, Illinois 60484.

The University (and its component unit) is a component unit of the State of Illinois for financial reporting purposes and its fiscal balances and activities are included in the State's comprehensive annual financial report.

2. Summary of Significant Accounting Policies

Basis of Accounting

The financial statements of the University are prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by GASB using the economic resources measurement focus and the accrual basis of accounting.

Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when incurred. When both restricted and unrestricted resources are available for use, it is the University's policy to use restricted resources first, then unrestricted resources as needed.

In accordance with GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the University follows all applicable GASB pronouncements. In addition, the University applies all Financial Accounting Standards Board (FASB) statements and interpretations, Accounting Principles Board (APB) opinions and accounting research bulletins of the Committee of Accounting Procedures issued on or before November 30, 1989 unless those pronouncements conflict with or contradict GASB pronouncements. The University has elected not to apply FASB pronouncements issued after November 30, 1989.

The financial statements are prepared in accordance with GASB Statement No. 35, *Basic Financial Statements - and Management's Discussion and Analysis - for Public Colleges and Universities*, and follow the special purpose governments engaged only in "business-type" activities requirements, which requires the following components of the University's financial statements:

Management's Discussion and Analysis

This provides an objective analysis of the University's financial activities based on facts, decisions and conditions.

Basic financial statements including a Statement of Net Assets, Statement of Revenues, Expenses and Changes in Net Assets and Statement of Cash Flows

- The Statement of Net Assets details current assets/liabilities and noncurrent assets/liabilities. In general, current assets are those that are available to satisfy current liabilities. Current liabilities are those that will be paid within one year of the date of the Statement of Net Assets. Other assets and liabilities due beyond one year are noncurrent. Net assets are divided into three major categories: (1) Invested in capital assets, net of related debt, (2) Restricted net assets, and (3) Unrestricted net assets.

- The Statement of Revenues, Expenses and Changes in Net Assets reports operating and nonoperating revenues and expenses, and displays the net income or loss from operations and total changes in net assets.

- The Statement of Cash Flows details the change in the cash and cash equivalents balance for the fiscal year and is prepared using the direct method. This statement provides information related to cash receipts and cash payments during the year. The statement also helps users evaluate the University's ability to meet financial obligations as they mature.

Notes to Basic Financial Statements

This provides additional analysis of the University's basic financial statements.

Cash and Cash Equivalents

In accordance with GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*, cash equivalents are defined as short-term, highly liquid investments that are both readily convertible to known amounts of cash, and so near to their maturities that they present insignificant risk of changes in value because of changes in interest.

Accounts and Grants Receivable

An aging of accounts and grants receivable as of June 30, 2012 is as follows:

Current	$ 5,211,110
Up to 120 days past due	684,587
From 121 to 365 days past due	482,680
More than 365 days past due	3,701,841
Allowance for doubtful accounts	(4,092,600)
Net accounts and grants receivable	$ 5,987,618

Non-student receivables are not aged and have been presented above as current.

Allowance for Uncollectible Accounts

The allowance for doubtful accounts is based on management's best estimate of uncollectible accounts considering type, age, collection history, and other appropriate factors.

Unamortized Debt Issuance Costs

The costs associated with the issuance of the revenue bonds and certificates of participation are being amortized on a straight-line basis over the life of the related debts.

Inventories

Inventories are stated at the lower of cost or market. Cost is determined using the first-in, first-out inventory valuation method.

Investments

Foundation investments are recorded at fair market value as determined by quoted market prices. Investments are pooled for the purposes of allocating realized gains and losses, unrealized gains and losses and ordinary income, net of investment fees, to the unallocated reserve in the restricted fund. Allocation to specific accounts is based on contractual obligations and the Foundation's investment policy.

Student Loans

Student loans include loans made to students under the Federal Perkins Loan Program and the Nurse Faculty Loan Program. Loan repayments expected during the next fiscal year have been reported as a current asset. Loans that are not expected to be repaid during the next fiscal year, less an allowance for uncollectible loans, have been presented as a noncurrent asset.

Accrued Compensated Absences

Accrued compensated absences include earned but unused vacation and sick leave days valued at the current rate of pay.

Deferred Revenue

Deferred revenue includes amounts received for tuition and fees prior to the end of the fiscal year but related to the subsequent accounting period.

Classification of Revenues

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

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

Nonoperating revenues: Nonoperating revenues include activities that have the characteristics of non-exchange transactions, such as gifts and contributions, and other revenue sources that are defined as nonoperating revenues by GASB Statements No. 9 and No. 35, such as State appropriation, payments made on behalf of the University for healthcare and retirement costs, Federal Pell grant, and investment income.

Scholarship Discounts and Allowances

Student tuition and fees 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 charges and the amounts paid directly by students and/or third parties. Certain governmental grants such as Federal Pell grant 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 used to satisfy tuition and fees and other student charges, the University has recorded a scholarship discount and allowance.

Net Assets

GASB Statement No. 35 requires the University's net resources to be classified into net asset categories and reported in its Statement of 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 accumulated depreciation and outstanding debt obligations used to acquire capital assets.

Restricted net assets - nonexpendable: Nonexpendable restricted net assets consist 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 intact and invested for the purpose of producing present and future income, which may either be expended or added to the principal.

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

Unrestricted net assets: Unrestricted net assets represent resources derived from student tuition and fees, State appropriations, 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.

Risk Management

The University participates in the Illinois Public Higher Education Cooperative (IPHEC) and Midwestern Higher Education Compact (MHEC), which leverages all Illinois public universities' assets to reduce the total and individual cost of property and liability insurances to Illinois public universities. Additionally, the University is a member of the State University Risk Management Association (SURMA), which is an inter-governmental risk sharing pool. The University's general liability coverage has a $350,000 self insured retention level per occurrence, which is covered by SURMA. Participant contributions to SURMA are based upon actuarial valuations.

According to the Bylaws of SURMA, members may withdraw at any time and (subject to the approval by remaining members) be eligible to receive its proportionate share of capital contributions, or upon termination of SURMA, be entitled to receive its proportionate share of capital contributions. The capital contributions are to be allocated based on the proportional premium contributions made by each member over the past five years. In accordance with GASB Interpretation No. 4, *Accounting and Financial Reporting for Capitalization Contributions to Public Entity Risk Pools*, the University has recorded as other assets the estimated amount that could be recoverable in the event of withdrawal or termination.

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 at the financial statement date and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

3. Deposits and Investments

GASB Statement No. 40, *Deposit and Investment Risk Disclosures*, requires general disclosures by investment type with disclosures of the specific risks those investments are exposed to.

Deposits

Deposits consist of the following at June 30, 2012:

	Carrying Amount	Bank Balance
University:		
Cash in bank	$ 4,773,863	$ 5,938,405
Cash on hand	20,884	-
Illinois Funds (Standard & Poor's AAAm)	34,717,410	34,717,410
Total	$ 39,512,157	$ 40,655,815
Foundation:		
Cash in bank	$ 361,568	$ 361,568
Illinois Funds (Standard & Poor's AAAm)	74,001	74,001
Total	$ 435,569	$ 435,569

Custodial Credit Risk: Custodial credit risk is the risk that in the event of a bank failure, deposits may not be returned. The Federal Deposit Insurance Corporation insured bank balances totaling $500,000 (University and Foundation) at June 30, 2012. The remaining bank balances as of June 30, 2012 were fully collateralized. The Illinois Funds are arranged and contracted by the Treasurer of the State of Illinois and collateralized as required by that contract. Depositories and brokers are chosen based on stability and longevity, and due to insurance and collateralization, bank balances were not subject to custodial credit risk.

Interest Rate Risk: Interest rate risk exists when there is a possibility that changes in interest rates could adversely affect an investment's value. The Illinois Funds has a weighted average maturity of less than one year.

Credit Risk: Credit risk exists when there is a possibility that the issuer or other counterparty to an investment may be unable to fulfill its obligations.

University Investments

The carrying value of the investment portfolio of the University at June 30, 2012 is as follows:

	Credit Rating	Maturity	Carrying Amount	Fair Value
Money Market Funds	Not rated	< 1 year	$ 20,507,871	$ 20,507,871

Custodial Credit Risk: Custodial credit risk is the risk that in the event of custodian failure, investment principal may not be returned. At June 30, 2012, investments consisted solely of money market funds held in corporate trust accounts at Amalgamated Bank of Chicago.

Interest Rate Risk: Interest rate risk exists when there is a possibility that changes in interest rates could adversely affect an investment's value. The University does not have a formal policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk: Credit risk exists when there is a possibility that the issuer or other counterparty to an investment may be unable to fulfill its obligations. The University does not have a formal policy limiting credit risk.

Foundation Investments

The fair value of the investment portfolio of the Foundation at June 30, 2012 is as follows:

	Fair Value
Money Market Funds	$ 153,586
Mutual Funds investing in stocks	572,664
Mutual Funds investing in bonds	397,342
Corporate Bonds	304,198
U.S. Treasury Obligations	202,967
U.S. Agency Obligations	25,216
	$ 1,655,973

Custodial Credit Risk: Custodial credit risk is the risk that in the event of custodian failure, investment principal may not be returned. At June 30, 2012, investments consisted of money market funds, mutual funds, corporate bonds, U.S. Treasury Obligations and U.S. Agency Obligations. All investments are being held by the First Midwest Bank Trust Division.

Interest Rate Risk: Interest rate risk exists when there is a possibility that changes in interest rates could adversely affect an investment's value. The Foundation's investment policy addresses the overall diversification of the portfolio with consideration for liquidity. It does not limit investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates, but encourages a laddered portfolio with maturities occurring at regular intervals.

Credit Risk: Credit risk exists when there is a possibility that the issuer or other counterparty to an investment may be unable to fulfill its obligations. The Foundation's investment policy encourages the investment manager to focus on high quality bonds, maintaining an average credit quality of AA, to achieve an attractive risk-adjusted total return over the long run. The money market fund was invested in Northern Trust Institutional U.S. Government Select Portfolio which has a maturity of < 1 year and a credit rating of AAAm.

The maturities of the debt securities investment portfolio (at market value) of the Foundation at June 30, 2012 are as follows:

		Investment Maturity (in Years)		
Investment Type	Fair Value	Less Than 1	1-5	5-10
Corporate Bonds	$ 304,198	$ 50,624	$ 201,507	$ 52,067
U.S. Treasury Obligations	202,967	25,211	177,756	-
U.S. Agency Obligations	25,216	-	25,216	-
Mutual Funds investing in Bonds	397,342	397,342	-	-
Total	$ 929,723	$ 473,177	$ 404,479	$ 52,067

The Standard & Poor's credit ratings of the debt securities investment portfolio (at market value) of the Foundation at June 30, 2012 are as follows:

Credit Rating	Total Debt Securities
U.S. Treasury Obligations	$ 202,967
No rating	397,342
AA+	77,177
AA-	50,321
A+	25,543
A	76,338
A-	74,827
BBB+	25,208
Total	$ 929,723

Foreign Currency Risk: Foreign currency risk exists when there is a possibility that the exchange rate of foreign currencies against the U.S. dollar may vary. The Foundation's policy is to limit its investments in foreign securities to 25%.

4. Cash and Cash Equivalents, Restricted

The net proceeds from issuing the University Revenue Bonds and Certificates of Participation were separately deposited in Trust Escrow accounts with Amalgamated Bank of Chicago (Bank). As trustee, the Bank has invested the funds in Illinois Funds and Goldman Sachs "Financial Square Money Market" funds pending expenditure for the University's deferred maintenance and housing projects. In addition, certain accounts created by the University Revenue Bonds and for debt servicing the Certificates of Participation are held by the Bank pending expenditure for debt service. The balance of these accounts as of June 30, 2012 amounted to $23,349,119.

The net proceeds from issuing the promissory note in relation to the University's guaranteed energy savings contract was separately deposited in the Escrow account with Old National Leasing Bank pending expenditure for the University's energy savings projects. The balance of this account as of June 30, 2012 amounted to $4,695.

5. State Universities Retirement System

Plan Description

The University contributes to the State Universities Retirement System of Illinois (SURS), a cost-sharing multiple-employer defined-benefit pension plan with a special funding situation whereby the State of Illinois makes substantially all actuarially determined required contributions on behalf of the participating employers. SURS was established on July 21, 1941, to provide retirement annuities and other benefits for staff members and employees of the State universities, certain affiliated organizations, and certain other State educational and scientific agencies and for survivors, dependents and other beneficiaries of such employees. SURS is considered a component unit of the State of Illinois' financial reporting entity and is included in the State's financial reports as a pension trust fund. SURS is governed by Section 5/15, Chapter 40, of the Illinois Compiled Statutes. SURS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by accessing the website at www.SURS.org or by calling 1-800-275-7877.

Funding Policy

Plan members are required to contribute 8.0% of their annual covered salary and substantially all employer contributions are made by the State of Illinois on behalf of the individual employers at an actuarially determined rate. The current rate (for fiscal year 2013) is 34.51% of annual covered payroll. The contribution requirements of plan members and employers are established and may be amended by the Illinois General Assembly. The University's contributions to SURS for the years ended June 30, 2012, 2011, and 2010 were $10,809,277, $8,713,583, and $7,761,750, respectively, equal to the required contributions for each year.

6. Postemployment Benefits

The State provides health, dental, vision, and life insurance benefits for retirees and their dependents in a program administered by the Department of Healthcare and Family Services along with the Department of Central Management Services. Substantially all State employees become eligible for post-employment benefits if they eventually become annuitants of one of the State sponsored pension plans. Health, dental, and vision benefits include basic benefits for annuitants and dependents under the State's self-insurance plan and insurance contracts currently in force. Annuitants may be required to contribute towards health, dental, and vision benefits with the amount based on factors such as date of retirement, years of credited service with the State, whether the annuitant is covered by Medicare, and whether the annuitant has chosen a managed health care plan. Annuitants who retired prior to January 1, 1998, and who are vested in the State Employee's Retirement System do not contribute towards health, dental, and vision benefits. For annuitants who retired on or after January 1, 1998, the annuitant's contribution amount is reduced five percent for each year of credited service with the State allowing those annuitants with twenty or more years of credited service to not have to contribute towards health, dental, and vision benefits. Annuitants also receive life insurance coverage equal to the annual salary of the last day of employment until age 60, at which time the benefit becomes $5,000.

The State pays the University's portion of employer costs for the benefits provided. The total cost of the State's portion of health, dental, vision, and life insurance benefits of all members, including post-employment health, dental, vision, and life insurance benefits, is recognized as an expenditure by the State in the Illinois Comprehensive Annual Financial Report. The State finances the costs on a pay-as-you-go basis. The total costs incurred for health, dental, vision, and life insurance benefits are not separated by department or component unit for annuitants and their dependents nor active employees and their dependents.

A summary of post-employment benefit provisions, changes in benefit provisions, employee eligibility requirements including eligibility for vesting, and the authority under which benefit provisions are established are included as an integral part of the financial statements of the Department of Healthcare and Family Services. A copy of the financial statements of the Department of Healthcare and Family Services may be obtained by writing to the Department of Healthcare and Family Services, 201 South Grand Ave., Springfield, Illinois, 62763-3838.

7. Capital Assets

Capital assets are recorded at cost at the date of acquisition, or fair market value at the date of donation in the case of gifts. For equipment, the University's capitalization policy includes all items with a unit cost of $5,000 or more. For intangible assets, the University's capitalization policy includes all items with a unit cost of $25,000 or more. Renovations to buildings and site improvements that significantly increase the value or extend the useful life of the structure are also capitalized. Depreciation is computed using the straight-line method over the estimated useful lives of the assets: 40 to 60 years for buildings, 20 to 60 years for site improvements, seven years for intangible assets, and three to 40 years for equipment and library collection.

Interest incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. Interest of $161,051 was capitalized during the year ended June 30, 2012.

Capital assets activities for the University and Foundation for the year ended June 30, 2012 are summarized as follows:

	Balance June 30, 2011	Additions	Retirements	Transfers	Balance June 30, 2012
Capital assets not being depreciated					
Land	$ 1,389,086	$ -	$ -	$ -	$ 1,389,086
Construction in progress	-	2,893,328	-	-	2,893,328
Artwork/Sculptures-University	268,323	-	-	-	268,323
Artwork/Sculptures-Foundation	1,614,351	103,005	-	-	1,717,356
Total capital assets not being depreciated	$ 3,271,760	$ 2,996,333	$ -	$ -	$ 6,268,093
Other capital assets					
Site improvements	$ 5,986,726	$ 1,590,047	$ -	$ -	$ 7,576,773
Buildings	100,463,328	951,045	-	-	101,414,373
Intangible assets	1,077,097	-	-	-	1,077,097
Equipment	8,761,733	264,959	(140,377)	169,545	9,055,860
Equipment under capital leases	169,545	-	-	(169,545)	-
Library collection	13,231,988	632,364	(306,021)	-	13,558,331
Total other capital assets	129,690,417	3,438,415	(446,398)	-	132,682,434
Accumulated depreciation					
Site improvements	(1,332,941)	(352,668)	-	-	(1,685,609)
Buildings	(32,730,795)	(1,843,536)	-	-	(34,574,331)
Intangible assets	(153,871)	(153,871)	-	-	(307,742)
Equipment	(6,666,451)	(671,255)	136,877	(168,045)	(7,368,874)
Equipment under capital leases	(168,045)	-	-	168,045	-
Library collection	(11,311,244)	(536,896)	306,021	-	(11,542,119)
Total accumulated depreciation	(52,363,347)	(3,558,226)	442,898	-	(55,478,675)
Other capital assets, net	$ 77,327,070	$ (119,811)	$ (3,500)	$ -	$ 77,203,759
Capital assets summary:					
Capital assets not being depreciated	$ 3,271,760	$ 2,996,333	$ -	$ -	$ 6,268,093
Other capital assets	129,690,417	3,438,415	(446,398)	-	132,682,434
Accumulated depreciation	(52,363,347)	(3,558,226)	442,898	-	(55,478,675)
Total capital assets, net	$ 80,598,830	$ 2,876,522	$ (3,500)	$ -	$ 83,471,852

8. Long-Term Obligations

Changes in Long-Term Obligations

Changes in long-term obligations for the year ended June 30, 2012 were as follows:

	Balance July 1, 2011	Additions	Deductions	Balance June 30, 2012	Amounts Due Within One Year
Notes payable	$ 4,019,410	$ -	$ 422,120	$ 3,597,290	$ 451,889
Revenue bonds 2007	8,000,000	-	335,000	7,665,000	350,000
Revenue bonds 2012	-	20,415,000	-	20,415,000	-
Certificates of participation 2008	9,645,000	-	110,000	9,535,000	115,000
Certificates of participation 2009	8,070,000	-	885,000	7,185,000	910,000
	29,734,410	20,415,000	1,752,120	48,397,290	1,826,889
Unamortized discounts	(147,154)	(26,538)	(8,920)	(164,772)	(9,584)
Unamortized premiums	39,424	-	3,109	36,315	3,109
	$ 29,626,680	$ 20,388,462	$ 1,746,309	$ 48,268,833	$ 1,820,414

Notes Payable

On June 25, 2009, the University entered into an installment payment contract amounting to $4,750,000 to fund a portion of its expenditures related to the guaranteed energy savings contract. The original interest rate was 5.19%; however, the interest rate was renegotiated during fiscal year 2012 to 3.75%. Future maturities at June 30, 2012 are as follows:

Year Ending June 30	Principal	Interest	Total
2013	$ 451,889	$ 127,184	$ 579,073
2014	469,129	109,944	579,073
2015	487,027	92,046	579,073
2016	505,608	73,465	579,073
2017	524,897	54,176	579,073
2018 - 2020	1,158,740	47,661	1,206,401
	$ 3,597,290	$ 504,476	$ 4,101,766

Revenue Bonds, Series 2007

On November 20, 2007, the University issued $8,930,000 of University Facilities System Revenue Bonds, Series 2007, with interest rates ranging from 4.00% to 4.125% to make various improvements and additions to the University included in its deferred maintenance initiative and pay the costs incurred ($175,736) in connection with the issuance of the Series 2007 Bonds. The original issue premium is being accreted to interest expense over the term of the bonds.

Optional Redemption - The Series 2007 Bonds maturing on or after October 1, 2018 are subject to redemption on or after October 1, 2017, at the option of the University.

Mandatory Redemption of Term Bonds - The Series 2007 Term Bonds, maturing on October 1, 2025 and October 1, 2027, are subject to mandatory redemption prior to maturity through the application of sinking fund payments, at a redemption price equal to the principal amount plus accrued interest to the date fixed for redemption, in the following principal amounts on October 1 in each of the years set forth below:

Term Bonds due 10/01/25		Term Bonds due 10/01/27	
Year	Principal Amount	Year	Principal Amount
2024	$ 565,000	2026	$ 610,000
2025	585,000	2027	635,000

Future debt service requirements at June 30, 2012 are as follows:

Year Ending June 30	Principal	Interest	Total
2013	$ 350,000	$ 301,156	$ 651,156
2014	365,000	286,856	651,856
2015	380,000	271,956	651,956
2016	395,000	256,456	651,456
2017	410,000	240,356	650,356
2018 - 2022	2,310,000	937,181	3,247,181
2023 - 2027	2,820,000	425,400	3,245,400
2028	635,000	13,098	648,098
	$ 7,665,000	$ 2,732,459	$ 10,397,459

Revenue Bonds, Series 2012

On April 5, 2012, the University issued $20,415,000 of University Facilities System Revenue Bonds, Series 2012, with interest rates ranging from 2.00% to 4.45% to construct an on-campus student housing complex and pay the costs incurred ($470,824) in connection with the issuance of the Series 2012 Bonds. The original issue discount is being accreted to interest expense over the term of the bonds.

Optional Redemption - The Series 2012 Bonds maturing on or after October 1, 2020 are subject to redemption on or after October 1, 2019, at the option of the University.

Mandatory Redemption of Term Bonds - The Series 2012 Term Bonds, maturing on October 1, 2026, October 1, 2037 and October 1, 2042, are subject to mandatory redemption prior to maturity through the application of sinking fund payments, at a redemption price equal to the principal amount plus accrued interest to the date fixed for redemption, in the following principal amounts on October 1 in each of the years set forth below:

Term Bonds due 10/01/26		Term Bonds due 10/01/37		Term Bonds due 10/01/42	
Year	Principal Amount	Year	Principal Amount	Year	Principal Amount
2024	$ 550,000	2033	$ 800,000	2038	$ 1,010,000
2025	570,000	2034	840,000	2039	1,055,000
2026	595,000	2035	880,000	2040	1,105,000
		2036	920,000	2041	1,160,000
		2037	960,000	2042	1,215,000

Future debt service requirements at June 30, 2012 are as follows:

Year Ending June 30	Principal	Interest	Total
2013	$ -	$ 726,049	$ 726,049
2014	-	832,412	832,412
2015	415,000	828,262	1,243,262
2016	425,000	819,862	1,244,862
2017	430,000	811,313	1,241,313
2018 - 2022	2,320,000	3,892,306	6,212,306
2023 - 2027	2,750,000	3,464,624	6,214,624
2028 - 2032	3,365,000	2,843,721	6,208,721
2033 - 2037	4,205,000	2,010,954	6,215,954
2038 - 2042	5,290,000	920,228	6,210,228
2043	1,215,000	28,249	1,243,249
	$ 20,415,000	$ 17,177,980	$ 37,592,980

Certificates of Participation, Series 2008

On June 12, 2008, the University issued $9,995,000 of University Capital Improvement Project Certificates of Participation, Series 2008, with interest rates ranging from 3.50% to 4.50% to pay a portion of the costs of improvements, to refund in advance of maturity and advance refund all of the $1,760,000 outstanding principal on the Certificates of Participation, Series 1998, and to pay the costs ($256,328) of issuing the Series 2008 Certificates. The original issue discount is being accreted to interest expense over the term of the Certificates.

Optional Redemption - The Series 2008 Certificates are callable on any date on or after January 1, 2018, at the option of the University, upon at least 35 days prior written notice from the University to the Trustee.

Redemption Upon Optional Termination of Purchase Contract - The Certificates are subject to mandatory redemption, in whole, at the redemption prices set forth below, plus accrued interest to the date fixed for redemption, on the following dates, if the University notifies the Trustee not less than 60 days prior thereto that it is exercising its option to terminate the purchase contract:

Redemption Date	Redemption Price
January 1, 2013	110%
On or after January 1, 2018	100%

Redemption Upon Failure to Renew Purchase Contract - The Series 2008 Certificates are subject to mandatory redemption, in whole, at the price of the principal amount thereof, plus accrued interest to the date fixed for redemption, on January 1, 2018, unless the University notifies the Trustee not less than 60 days prior thereto that the purchase contract has been renewed and the Expiration Date extended to January 1, 2028 in accordance with the terms of the purchase contract.

Redemption Upon Event of Non-appropriation and Termination of Purchase Contract - The Series 2008 Certificates are subject to redemption, in whole, at the price of par (100%), plus accrued interest to the date fixed for redemption, on any date on which the purchase contract is terminated by the Board because (i) an event of non-appropriation has occurred, (ii) the Board has determined that there are not sufficient legally available non-appropriated funds to pay the installment payments coming due during the then current fiscal year, and (iii) the Board has exercised its option to prepay the Certificates.

The University defeased its outstanding Certificates of Participation, Series 1998 through advance refunding and, accordingly, those Certificates are not reflected in the accompanying financial statements. Those Certificates of Participation which were advance refunded were paid in full on July 25, 2008.

Future debt service requirements at June 30, 2012 are as follows:

Year Ending June 30	Principal	Interest	Total
2013	$ 115,000	$ 393,150	$ 508,150
2014	125,000	389,125	514,125
2015	125,000	384,750	509,750
2016	130,000	380,375	510,375
2017	140,000	375,500	515,500
2018 - 2022	3,160,000	1,696,312	4,856,312
2023 - 2027	4,685,000	841,763	5,526,763
2028	1,055,000	47,475	1,102,475
	$ 9,535,000	$ 4,508,450	$ 14,043,450

Certificates of Participation, Series 2009

On March 31, 2009, the University issued $9,870,000 of University Capital Improvement Project Certificates of Participation, Series 2010, with interest rates ranging from 3.00% to 4.50% to pay a portion of the costs of the improvements and to pay the costs ($284,914) of issuing the Series 2009 Certificates. The original issue premium is being accreted to interest expense over the term of the Certificates.

Extraordinary Redemption upon Event of Non-appropriation and Termination of Purchase Contract - The Series 2009 Certificates are subject to redemption upon termination by the Board of the purchase contract due to (i) an event of non-appropriation having occurred, (ii) the Board determining that there are not sufficient legally available non-appropriated funds to pay the installment payments coming due, and (iii) the Board has exercised its option to prepay the outstanding certificates plus accrued interest.

Extraordinary Redemption Upon Optional Termination of Purchase Contract - The Certificates are subject to mandatory redemption, in whole, at the redemption price of 110% of the principal amount thereof, plus accrued interest to the date fixed for redemption, on March 1, 2014, if the University notifies the Trustee not less than 60 days prior thereto that it is exercising its option to terminate the purchase contract.

Future debt service requirements at June 30, 2012 are as follows:

Year Ending June 30	Principal	Interest	Total
2013	$ 910,000	$ 296,500	$ 1,206,500
2014	940,000	269,200	1,209,200
2015	980,000	226,900	1,206,900
2016	1,025,000	182,800	1,207,800
2017	1,065,000	143,081	1,208,081
2018 - 2019	2,265,000	151,125	2,416,125
	$ 7,185,000	$ 1,269,606	$ 8,454,606

9. Accrued Compensated Absences

Accrued compensated absences include earned but unused vacation and sick leave days valued at the current rate of pay. The change in accrued compensated absences for the year ended June 30, 2012 was as follows:

Balance, beginning of year	$ 4,855,661
Movement	(234,464)
Balance, end of year	4,621,197
Less: current portion	500,000
Balance, noncurrent portion	$ 4,121,197

10. Component Unit

The financial statements of the Foundation (the University's component unit) have been discretely presented in the University's financial statements.

The Foundation has an ongoing contract with the University which includes provisions requiring the Foundation to comply with Section VI of the "University Guidelines 1982 (as amended 1997)" as adopted by the State of Illinois Legislative Audit Commission. The contract requires that the University provide the Foundation with accounting and other clerical services at no cost. University officials estimate the value of these services for the year ended June 30, 2012 at $175,414, including all direct payroll expenses and fringe benefits. The Foundation provided the University with support in the amount of $312,308 for the year ended June 30, 2012. As of June 30, 2012, $43,956 is due to the University from the Foundation.

Below are the condensed financial statements of the Foundation.

Condensed Statement of Net Assets

ASSETS	
Current assets	$ 599,761
Noncurrent assets	3,219,743
Total assets	3,819,504
LIABILITIES	
Current liabilities	52,366
Total liabilities	52,366
NET ASSETS	
Invested in capital assets	1,717,356
Restricted	
Nonexpendable	1,338,404
Expendable	695,055
Unrestricted	16,323
Total net assets	$ 3,767,138

Condensed Statement of Revenues, Expenditures and Changes in Net Assets

Operating revenues	$ 207,928
Operating expenses	559,293
Net operating loss	(351,365)
Nonoperating revenues	324,142
Net change to endowments	101,573
Capital asset contributions	103,005
Increase in net assets	177,355
Net assets - beginning of year	3,589,783
Net assets - end of year	$ 3,767,138

Condensed Statement of Cash Flows

Net cash used in operating activities	$	(310,347)
Cash provided by noncapital financing activities		463,521
Net cash used in investing activities		(280,135)
Net decrease in cash and cash equivalents		(126,961)
Cash and cash equivalents - beginning of year		716,116
Cash and cash equivalents - end of year	$	589,155

Reconciliation of net operating loss to net cash used in operating activities:

Net operating loss	$	(351,365)
Adjustment to reconcile net operating loss to net cash used in operating activities:		
Accounts payable		41,018
Net cash used in operating activities	$	(310,347)

11. Commitments and Contingencies

The University is from time to time subject to various claims and legal actions related to the University or the actions of its employees. Although it is difficult to quantify the potential impact of these claims, management believes that the ultimate cost of these matters will not adversely affect the University's future financial condition or results of operations.

The University has outstanding commitments totaling approximately $1.0 million related to its deferred maintenance initiative projects.

12. Restricted Endowments

The Foundation's endowment funds are generally invested in marketable securities which are valued at market as of the statement of net assets date. Investment income is initially assigned to the unallocated reserve in the restricted fund. Income is then allocated to various accounts based on the endowment agreements and the approved spending plans.

On June 30, 2009, the State of Illinois passed the Uniform Prudent Management of Institutional Funds Act. This State law allows the Foundation to appropriate for expenditure an amount that it determines to be prudent for the uses, benefits, purposes, and duration for which the endowment fund was established. In making these appropriations, the Foundation must act in good faith and with the care that an ordinary prudent person in a similar position would do.

The Foundation has adopted a spending policy of not to exceed 6.0% of a trailing twelve month average of the market value of the assets as of April 1. The Foundation transfers available investment earnings to the related expendable accounts on an annual basis.

13. Operating Leases

The University leases equipment and space in various buildings for off-campus classroom use. The rental expense for these lease agreements was $232,645 for the year ended June 30, 2012.

Future minimum lease payments are as follows:

Year Ending June 30	Base Rent
2013	$ 141,188
2014	87,143
2015	25,108
	$ 253,439

14. Pledged Revenues and Debt Service Requirements

The University has pledged specific revenues, net of specific operating expenses, to repay the principal and interest of revenue bonds. The following is a schedule of the pledged revenues and related debt:

PLEDGED REVENUES

BOND ISSUE	PURPOSE	SOURCE OF REVENUES PLEDGED	FUTURE REVENUES PLEDGED[1]	TERM OF COMMITMENT	(CURRENT YEAR) PLEDGED REVENUES TO DEBT SERVICE[2]
Auxiliary Facilities System Revenue Bonds (Series 2007 and 2012)	Various improvements and additions to the University	Net revenues of the Student Center, University Bookstore, University Parking Facilities, University Food Service and Vending Facilities, and University Housing	$ 47,990,439	2043	1.42%

[1] Total future principal and interest payments on debt.
[2] Current year pledged net operating revenues (disregarding depreciation) versus total future debt service.

SUPPLEMENTARY INFORMATION

STATE OF ILLINOIS
GOVERNORS STATE UNIVERSITY
UNIVERSITY FACILITIES SYSTEM REVENUE BONDS
STATEMENT OF NET ASSETS

	JUNE 30, 2012	(Comparative totals only) 2011
ASSETS		
Current assets		
Cash and cash equivalents	$ 99,412	$ 727,218
Cash and cash equivalents, restricted	21,392,547	1,032,704
Unamortized debt issuance costs - current	24,481	8,787
Total current assets	21,516,440	1,768,709
Noncurrent assets		
Unamortized debt issuance costs	578,614	136,194
Capital assets	11,025,702	10,587,910
Accumulated depreciation	(1,734,207)	(1,456,260)
Total noncurrent assets	9,870,109	9,267,844
Total assets	31,386,549	11,036,553
LIABILITIES		
Current liabilities		
Accounts payable	292,530	80,389
Revenue bonds payable	350,853	336,738
Total current liabilities	643,383	417,127
Noncurrent Liabilities		
Revenue bonds payable	27,729,775	7,691,945
Total noncurrent liabilities	27,729,775	7,691,945
Total liabilities	28,373,158	8,109,072
NET ASSETS		
Invested in capital assets, net of related debt	1,071,710	1,405,389
Restricted: expendable - debt service	1,377,205	649,856
Unrestricted	564,476	872,236
Total net assets	$ 3,013,391	$ 2,927,481

STATE OF ILLINOIS
GOVERNORS STATE UNIVERSITY
UNIVERSITY FACILITIES SYSTEM REVENUE BONDS
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

	FOR THE YEAR ENDED JUNE 30,	
	2012	(Comparative totals only) 2011
OPERATING REVENUES		
Bookstore commissions	$ 151,740	$ 144,501
Food and vending commissions	23,336	31,394
Parking fees	478,243	447,250
Student center fees	1,345,232	1,374,949
Total operating revenues	1,998,551	1,998,094
OPERATING EXPENSES		
Salaries and benefits	782,848	718,986
Scholarships and awards	19,499	450
Capital expenditures	64,984	31,769
Services, supplies and others	449,013	646,718
Depreciation	277,947	265,638
Total operating expenses	1,594,291	1,663,561
Net operating income	404,260	334,533
NONOPERATING REVENUES (EXPENSES)		
Investment income	205	445
Interest expense	(318,555)	-
Net nonoperating revenues (expenses)	(318,350)	445
Increase in net assets	85,910	334,978
NET ASSETS		
Net assets - beginning of year	2,927,481	2,592,503
Net assets - end of year	$ 3,013,391	$ 2,927,481

STATE OF ILLINOIS
GOVERNORS STATE UNIVERSITY
UNIVERSITY FACILITIES SYSTEM REVENUE BONDS
STATEMENT OF CASH FLOWS

	FOR THE YEAR ENDED JUNE 30, 2012	(Comparative totals only) 2011
CASH FLOWS FROM OPERATING ACTIVITIES		
Bookstore commissions	$ 151,740	$ 144,501
Food and vending commissions	23,336	31,394
Parking fees	478,243	447,250
Student center fees	1,345,232	1,374,949
Payments to suppliers for goods and services	(470,934)	(678,937)
Payments to employees for services	(778,256)	(718,986)
Net cash provided by operating activities	749,361	600,171
CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES		
Purchase of capital assets	(356,187)	(218,541)
Proceeds from issuance of debt, net	19,988,514	-
Principal payments on capital debt	(335,000)	(320,000)
Interest payments on capital debt	(314,856)	(327,956)
Net cash provided by (used in) capital financing activities	18,982,471	(866,497)
CASH FLOWS FROM INVESTING ACTIVITY		
Investment income	205	445
Cash provided by investing activity	205	445
Net increase (decrease) in cash and cash equivalents	19,732,037	(265,881)
Cash and cash equivalents - beginning of year	1,759,922	2,025,803
Cash and cash equivalents - end of year	$ 21,491,959	$ 1,759,922
RECONCILIATION OF NET OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Net operating income	$ 404,260	$ 334,533
Adjustment to reconcile net operating income to net cash provided by operating activities:		
Noncash expense included in net operating income:		
Depreciation	277,947	265,638
Changes in liabilities:		
Accounts payable	67,154	-
Net cash provided by operating activities	$ 749,361	$ 600,171

<u>Noncash Capital Financing Activities</u>

During fiscal year 2012, interest expense of $81,605 was reclassified to capital assets as interest incurred during the period of construction.

STATE OF ILLINOIS
GOVERNORS STATE UNIVERSITY
UNIVERSITY FACILITIES SYSTEM REVENUE BONDS
FOR THE YEAR ENDED JUNE 30, 2012

Student Enrollment by Term (Unaudited)

	Total Enrollment	Full-Time Equivalent
Fall Term, 2011	5,603	3,353
Spring Term, 2012	5,718	3,354
Summer Term, 2012	3,796	1,750

University Fees (Unaudited)

The following fees were in effect during the 2011-2012 academic year:

	Amount
Student Center fee	$ 30
Student Activity fee	36
Counseling and Career Services fee	32
Parking fee	35

Schedule of Insurance In Force (Unaudited)

The Facilities System is insured under a master policy covering the University. The following insurance coverage applicable to the System was effective during the current fiscal year:

Fire and extended coverage ($25,000 deductible) of:	
Buildings	$ 180,270,343
EDP and contents	32,617,873
Business interruption	16,525,694
Boiler and machinery (included in blanket coverage limit)	100,000,000
Earthquake	100,000,000
Flood	100,000,000
General liability	19,650,000

E.C. ORTIZ & CO., LLP
CERTIFIED PUBLIC ACCOUNTANTS

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Honorable William G. Holland
Auditor General
State of Illinois

and

The Board of Trustees
Governors State University

As Special Assistant Auditors for the Auditor General, we have audited the basic financial statements of the business-type activities of the Governors State University (University) and its aggregate discretely presented component unit, collectively a component unit of the State of Illinois, as of and for the year ended June 30, 2012, which collectively comprise the University's basic financial statements and have issued our report thereon dated April 19, 2013. Our report was modified to include a reference to other auditors. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Other auditors audited the financial statements of the University's discretely presented component unit, as described in our report on the University's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors.

Internal Control Over Financial Reporting

Management of the University is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the University's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the University's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of

Findings, we identified a certain deficiency in internal control over financial reporting that we consider to be a material weakness.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying Schedule of Findings as item 12-1 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the University's basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance or other matter that is required to be reported under *Government Auditing Standards* and which is described in the accompanying Schedule of Findings as item 12-1.

The University's response to the finding identified in our audit is described in the accompanying Schedule of Findings. We did not audit the University's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, University management, Board of Trustees and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

E.C. Ortiz & Co., LLP

Chicago, Illinois
April 19, 2013

STATE OF ILLINOIS
GOVERNORS STATE UNIVERSITY
SCHEDULE OF FINDINGS
FOR THE YEAR ENDED JUNE 30, 2012

CURRENT FINDING - *GOVERNMENT AUDITING STANDARDS*

12-1 *Financial Adjustments*

Governors State University (University) draft financial statements provided to auditors contained errors.

During our audit of the financial statements originally submitted by the University to the State of Illinois Office of the Comptroller (Comptroller), we noted the following:

- The University's deferred maintenance projects funded by its borrowed funds (Revenue Bonds, Series 2007 and Certificates of Participation, Series 2008) were fully completed during fiscal year 2012. However, the University capitalized the interest on these borrowed funds totaling $660,159 instead of recognizing it as interest expense which resulted in an overstatement of capital assets and understatement of interest expense. This also resulted in an overstatement of $14,713 in the related depreciation expense and accumulated depreciation accounts.

  Financial Accounting Standards No. 34, *Capitalization of Interest Cost*, paragraph 18, and Statewide Accounting Management System (SAMS) Procedure 03.30.20 state that capitalization of interest on constructed assets shall end when the asset is substantially complete and ready for its intended use.

  The University subsequently made the necessary adjustments in the financial statements.

- Deferred revenue pertaining to the fiscal year 2013 portion of the Summer 2012 tuition and fees was incorrectly calculated. The University recognized as deferred revenue the uncollected portion of tuition and fees instead of adjusting it against accounts receivable. This resulted in an overstatement of $615,403, $575,526, and $39,877 in accounts receivable, deferred revenue, and student tuition and fees, respectively.

  SAMS Procedure 05.50.01 defines deferred revenue as revenues collected in advance of the period in which they were earned.

  The University subsequently made the necessary adjustments in the financial statements.

CURRENT FINDING - *GOVERNMENT AUDITING STANDARDS*, Continued

- The University's calculation for fiscal year 2012 of the scholarship discounts and allowances was inaccurate which resulted in an understatement of $1,526,715 in student tuition and fees revenue and related expenditures.

  The University calculates the scholarship discounts and allowances in accordance with the guidelines set by the National Association of College and University Business Officers (NACUBO). The NACUBO Advisory Report 2000-05 defines scholarship discounts and allowances as the difference between the stated charge for goods and services provided by the institution and the amount that is paid by the student and/or third parties making payments on behalf of the students. The NACUBO Advisory Report 2000-05 also provides guidelines for the accounting and reporting of scholarship discounts and allowances.

  The University subsequently made the necessary adjustments in the financial statements.

- The difference in the balance of accounts receivable between the general ledger and the related subsidiary ledger was adjusted by the University to bad debts expense without first determining the nature of the difference. After the auditors made inquiries about this during the audit, the University subsequently performed an analysis and noted that the difference was due to the incorrect recording of the following: (a) application of Summer 2011 federal student financial aid against student accounts; and (b) student registration for Summer 2011 classes. This resulted in an overstatement of $406,468 in bad debts expense, and an understatement of $499,242 in grants receivable, grants expense, and federal grants and contracts revenue. This also resulted in an understatement of $92,774 in the related student tuition and fees revenue.

  Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires State agencies to establish and maintain a system, or systems, of internal fiscal and administrative controls to provide assurance that financial data is properly recorded and accounted for to permit the preparation of reliable financial reports.

  These amounts were not adjusted since they were determined by the University to be immaterial in relation to the fiscal year 2012 financial statements.

CURRENT FINDING - *GOVERNMENT AUDITING STANDARDS*, Continued

Management has the ultimate responsibility for the University's internal control over financial reporting. This responsibility should include an adequate system of review of the completeness and accuracy of the University's financial statements to ensure that the financial statements are presented in accordance with accounting principles generally accepted in the United States of America.

University officials stated that the conditions noted above were due to problems associated with the University's migration from its old administrative computing system to a new computing system and knowledge loss due to the sudden resignation of the University's long time Controller.

Failure to implement and follow proper internal control procedures over financial reporting may result in a material misstatement in the University's financial statements. (Finding Code No. 12-1)

Recommendation

We recommend the University review its current process for the preparation and review of the annual financial statements to ensure that financial information is complete, accurate, and prepared in accordance with generally accepted accounting principles.

University Response

The University agrees with this finding and accepts the recommendation. To ensure that these exceptions do not occur in the future, the University fully documented the financial close process and financial statement compilation for the new administrative computing system and added additional experienced accounting personnel.

STATE OF ILLINOIS
GOVERNORS STATE UNIVERSITY
PRIOR FINDINGS NOT REPEATED
FOR THE YEAR ENDED JUNE 30, 2012

A *Inaccurate Accounting for Intangible Assets*

During the prior audit, the University did not properly account for the costs capitalized to intangible assets in accordance with accounting principles generally accepted in the United States of America (GAAP). The University initially capitalized training and other post-implementation costs in relation to a new Enterprise Resource Planning (ERP) system instead of recording costs as an expense for the period. The University subsequently made the necessary adjustments in the financial statements.

During the current audit, our testing disclosed that post-implementation costs related to the University's ERP system were recorded as expense. (Finding Code No. 11-1)

B *Inaccurate Accounting for Participation in Public Entity Risk Pool*

During the prior audit, the University did not properly account for its participation in the State Universities Risk Management Association (SURMA) in accordance with GAAP. In addition, the University did not adequately monitor SURMA to ensure an annual audit was performed.

During the current audit, our testing disclosed that the University has accounted its participation in SURMA in accordance with GAAP. In addition, it was noted that SURMA underwent an audit during fiscal year 2012. (Finding Code No. 11-2)