

**LAKE SUPERIOR STATE UNIVERSITY**

**ANNUAL FINANCIAL REPORT**

**FISCAL YEARS ENDED  
JUNE 30, 2012 AND 2011**

# LAKE SUPERIOR STATE UNIVERSITY

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# Lake Superior State University

## Board of Trustees

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Term Expires January 27, 2018

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## **Lake Superior State University Management's Discussion and Analysis**

This discussion and analysis section of the Lake Superior State University (the "University") annual financial report provides an overview of our financial activities during the years ended June 30, 2012, 2011 and 2010. University management has prepared the financial statements and the related footnote disclosures along with this discussion and analysis, which includes the Lake Superior State University Foundation whenever appropriate. This discussion should be read in conjunction with the accompanying financial statements and footnotes. Responsibility for the completeness and fairness of this information rests with University management.

### **Reporting Entity**

Lake Superior State University is an institution of higher education and is considered to be a component unit of the State of Michigan. The Governor of the State of Michigan appoints the University's Board of Trustees. The University is included in the State's financial statements as a discrete component unit. Transactions with the State of Michigan primarily relate to appropriations for operations, appropriations for Charter Schools, receipt of grants, payments to State retirement programs on behalf of certain University employees, and reimbursements for capital outlay projects.

The basic financial statements include not only the University itself, but also a legally separate entity, the Lake Superior State University Foundation, for which the University is financially accountable. Financial statement information for this *component unit* is reported separately from the financial information presented for the University.

### **Using the Annual Report**

This annual report includes financial statements prepared in accordance with Governmental Accounting Standards Board ("GASB") Statement No. 35, *Basic Financial Statements and Management's Discussion and Analysis for Public Colleges and Universities*. The accompanying financial statements, which focus on the financial condition, results of operations and cash flows of the University as a whole, present financial information in a form similar to that used by commercial enterprises. The financial statements are prepared using the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service, regardless of when cash is exchanged.

### **Financial Highlights**

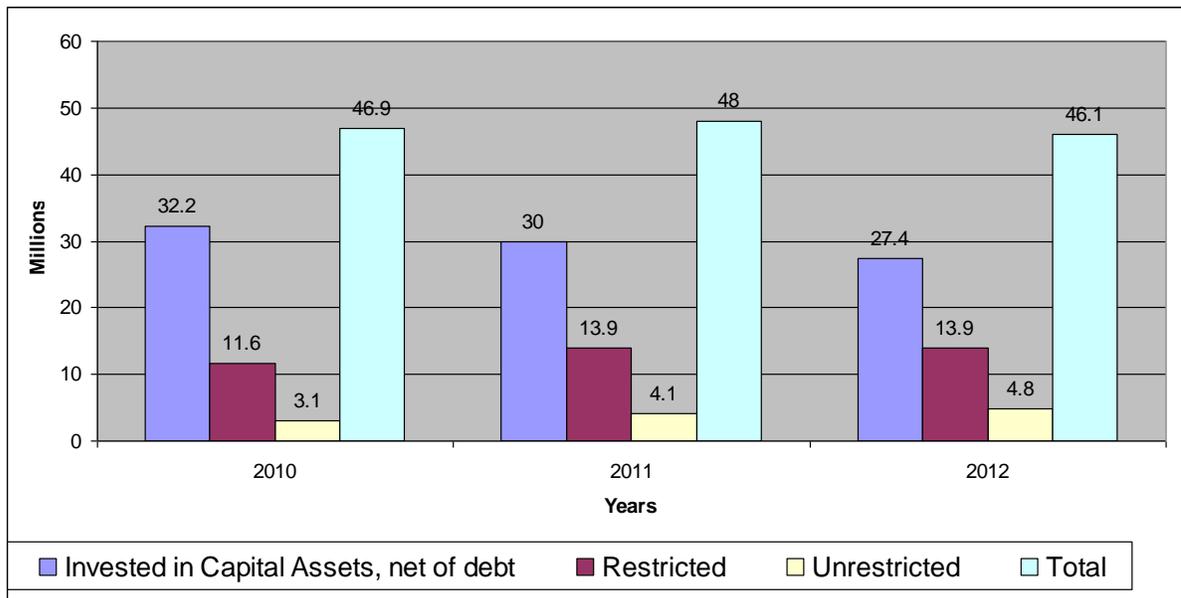
Lake Superior State University refinanced its long-term debt in March 2012. The general revenue refunding bonds, series 2012 were sold in the amount of \$23,355,000. The bonds were issued for the purpose of paying the costs of refunding its then outstanding 1997 and 2001 bonds and to pay the costs of issuing the bonds. The series 2012 refunding bonds reduce the University's interest expense by more than \$3.5 million and will occur through lower debt payments over the next 20 years.

In the course of refunding the bonds, the Board of Trustees determined that it was in the best interest of the University to pay off the interest rate swap related to the underlying debt of the 2001 bonds. That transaction had a negligible effect on the University’s financial position and it eliminated the liability with respect to the swap and the uncertainties that surrounded it.

In February 2012, just prior to the bond refunding, Standard and Poor’s Rating Service revised its outlook to positive from stable and affirmed its ‘BBB+’ underlying rating on the 1997 and 2001 bonds. At the same time, Standard & Poor’s assigned its ‘BBB+’ long-term rating to the series 2012 general revenue refunding bonds. Standard & Poor’s said “the outlook revision reflects our view of the University’s improved operating performance, stabilized management team, and growth in student enrollment.”

The University’s financial position was fairly stable at June 30, 2012. Net assets for the year ended June 30, 2012 of \$46.1 million decreased by \$1.9 million from the prior year as compared to an increase of \$1.0 million the previous year. Unrestricted net assets increased by \$785,000. The decrease in total net assets is largely due to depreciation in excess of new capital projects of \$2.6 million. This ongoing trend is expected to continue until 2014 when two new capital projects are expected to add as much as \$16 million in net assets.

The following chart provides a graphical breakdown of net assets by category for the fiscal years ended June 30, 2012, 2011, and 2010.



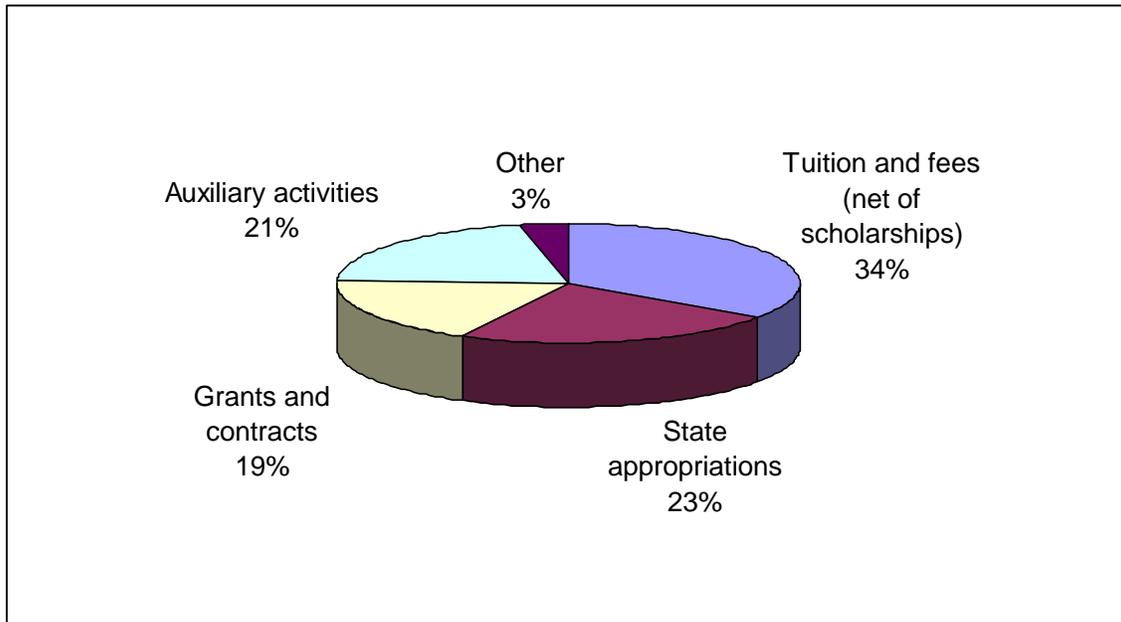
Operating revenues include all transactions that result in the sales and/or receipts from goods and services such as tuition and fees, housing and other rental and sales activities. In addition, certain federal, state and private grants and contracts are considered operating if they are not for capital purposes and are considered a contract for services.

Nonoperating revenues consist primarily of State appropriations, investment income, and grants and contracts that do not require any service to be performed. Annual appropriations, while budgeted for operations, are considered nonoperating revenues according to generally accepted accounting principles.

Revenue of the University consists of four main categories: Tuition, State appropriations, auxiliary activities and other revenue.

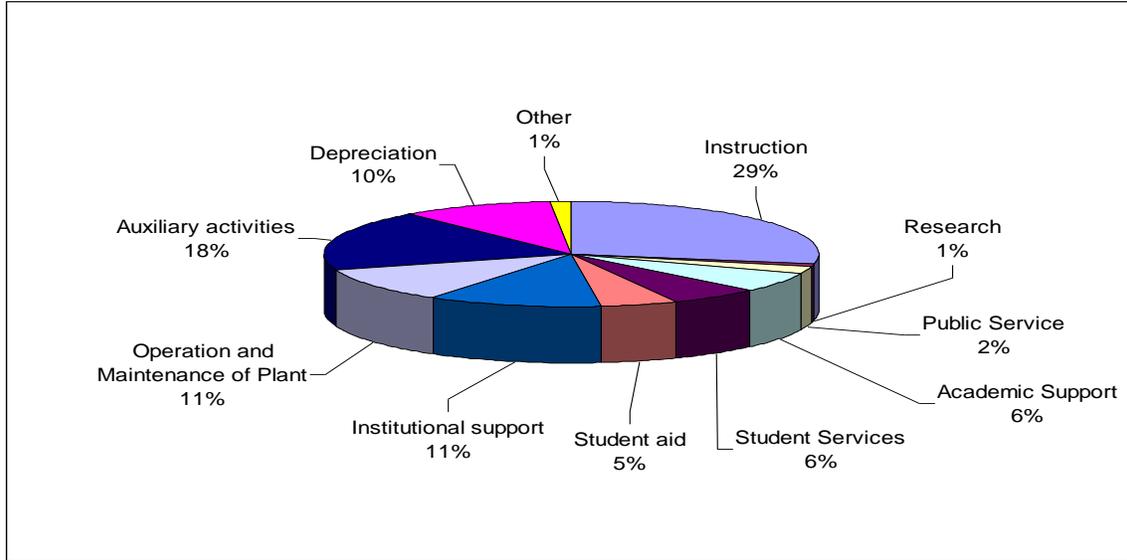
Tuition and fees, net of scholarship allowances, make up the largest contribution to the total revenue of the University. State appropriations are the next largest. Auxiliary activities consist of primarily housing, food services, and athletics. Other revenue includes investment income and gifts.

The following is a graphical illustration of revenues by source for the fiscal year ended June 30, 2012:



Operating expenses are all of the costs necessary to perform and conduct the programs and purposes of the University. Universities traditionally use functional classifications of expenses to represent the types of programs and services they provide.

The following is a graphical illustration of the University's operation expenses by functional classification for the year ended June 30, 2012:



### **The Statement of Net Assets**

The Statements of Net Assets include all assets and liabilities. Over time, increases or decreases in net assets (the difference between assets and liabilities) is one indicator of the improvement or erosion of the University's financial health when considered with operating measures such as enrollment levels and the physical condition of facilities.

|   | <b>June 30</b>              |                             |                             |
|---|-----------------------------|-----------------------------|-----------------------------|
|   | <b>2012</b>                 | <b>2011</b>                 | <b>2010</b>                 |
| <b>Assets:</b>                                  |                             |                             |                             |
| Current assets                                  | \$ 14,007,127               | \$ 13,477,688               | \$ 11,722,435               |
| Capital assets                                  | 50,620,780                  | 54,290,041                  | 57,849,540                  |
| Other noncurrent assets                         | <u>11,196,678</u>           | <u>12,181,075</u>           | <u>10,581,756</u>           |
| <b>Total Assets</b>                             | <b><u>\$ 75,824,585</u></b> | <b><u>\$ 79,948,804</u></b> | <b><u>\$ 80,153,731</u></b> |
| <b>Liabilities:</b>                             |                             |                             |                             |
| Current liabilities                             | \$ 4,840,972                | \$ 5,671,343                | \$ 5,744,131                |
| Noncurrent liabilities                          | <u>24,880,553</u>           | <u>26,319,075</u>           | <u>27,475,063</u>           |
| Total liabilities                               | <u>29,721,525</u>           | <u>31,990,418</u>           | <u>33,219,194</u>           |
| <b>Net Assets:</b>                              |                             |                             |                             |
| Invested in capital assets, net of related debt | 27,340,744                  | 29,980,781                  | 32,182,038                  |
| Restricted, nonexpendable                       | 205,327                     | 205,327                     | 205,327                     |
| Restricted, expendable                          | 13,716,872                  | 13,717,093                  | 11,404,290                  |
| Unrestricted                                    | <u>4,840,117</u>            | <u>4,055,185</u>            | <u>3,142,882</u>            |
| Total net assets                                | <u>46,103,060</u>           | <u>47,958,386</u>           | <u>46,934,537</u>           |
| <b>Total Liabilities and Net Assets</b>         | <b><u>\$ 75,824,585</u></b> | <b><u>\$ 79,948,804</u></b> | <b><u>\$ 80,153,731</u></b> |

**Changes from 2011 to 2012:**

Cash and cash equivalents and short-term investments, collectively, increased by \$.8 million to \$10 million. Accounts receivable were unchanged from the previous year. We attribute the majority of the increase in current assets to an increase in tuition, auxiliary and other revenues and controlled spending.

Capital assets decreased by \$3.7 million as a result of the annual depreciation charge of \$4.8 million and asset additions of \$1.1 million.

Total liabilities decreased by \$2.3 million, mostly due to a reduction of current accounts payable of \$723,000, long-term debt in the amount of \$592,000 being retired during the current year and the pay-off of the swap liability of \$839,000.

Total net assets decreased by \$1.9 million. The University's investment in capital assets, net of related debt, decreased \$2.6 million. This is the result of the depreciation charge being greater than capital asset acquisitions. Restricted, expendable scholarship net assets decreased slightly as a result of a minor downturn in the investment market. Unrestricted reserves increased by \$785,000. The June 30, 2012 unrestricted reserves of \$4.8 million consist of reserves in designated funds, auxiliary funds, insurance and benefit reserves and a general fund deficit of \$379,000.

**Changes from 2010 to 2011:**

Cash and cash equivalents and short-term investments, collectively, increased by \$1.6 million to \$9.2 million. Accounts receivable increased \$360,000 which we attribute to a slightly relaxed tuition payment policy due to a particularly tough economic climate in the State. We attribute the majority of the increase in current assets to an increase in enrollment and corresponding tuition revenue and controlled spending; the result was more cash on hand.

Capital assets decreased by \$3.6 million as a result of the annual depreciation charge of \$4.9 million and asset additions of \$1.3 million.

Total liabilities decreased by \$1.2 million, mostly due to long term debt in the amount of \$1.3 million being retired during the current year.

Total net assets increased by \$1.0 million. The University's investment in capital assets, net of related debt, decreased \$2.2 million. This is the result of the depreciation charge being greater than capital asset acquisitions. Restricted, expendable scholarship net assets increased by \$2.3 million. Unrestricted reserves increased by \$1.0 million. The June 30, 2012 unrestricted reserves of \$4.1 million consist of reserves in designated funds, auxiliary funds, insurance and benefit reserves and a general fund deficit of \$532,000.

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

The Statements of Revenues, Expenses and Changes in Net Assets present the revenues earned and expenses incurred each year. Activities are reported as either operating or nonoperating. A public university's dependency on State aid and grants will result in operating deficits because the financial reporting model classifies State appropriations as nonoperating revenues. The utilization of capital assets is reflected in the financial statements as depreciation, which amortizes the cost of an asset over its expected useful life.

|  | <b>Year Ended June 30</b>   |                             |                             |
|--|-----------------------------|-----------------------------|-----------------------------|
|  | <u>2012</u>                 | <u>2011</u>                 | <u>2010</u>                 |
| Total operating revenues                 | \$ 31,335,660               | \$ 29,989,565               | \$ 28,791,501               |
| Total operating expenses                 | <u>47,801,178</u>           | <u>47,640,518</u>           | <u>46,935,907</u>           |
| Operating loss                           | (16,465,518 )               | (17,650,953)                | (18,144,406)                |
| Net nonoperating revenues                | <u>14,296,566</u>           | <u>18,450,600</u>           | <u>17,366,548</u>           |
| Income (loss) before other revenues      | (2,168,952)                 | 799,647                     | (777,858)                   |
| Total other revenues                     | <u>313,626</u>              | <u>224,202</u>              | <u>323,510</u>              |
| <b>Increase/(decrease) in net assets</b> | <b>(1,855,326)</b>          | <b>1,023,849</b>            | <b>(454,348)</b>            |
| Net assets, beginning of year            | <u>47,958,386</u>           | <u>46,934,537</u>           | <u>47,388,885</u>           |
| <b>Net assets, end of year</b>           | <b><u>\$ 46,103,060</u></b> | <b><u>\$ 47,958,386</u></b> | <b><u>\$ 46,934,537</u></b> |

**Changes from 2011 to 2012:**

Operating revenues increased by \$1.3 million. Tuition and fees, net of scholarship allowance, increased by \$1.2 million or 8.2% after a tuition rate increase of 6.94% with a slight increase in enrollment. Scholarship allowances were almost the same as the prior year. Auxiliary revenues increased by \$239,000 or 2.5% after a 2.9% room and board rate increase and a little less than flat housing occupancy.

Operating expenses increased by \$161,000. Salaries and benefits decreased by \$316,000 during the year. The University spent \$633,000 more on supplies and equipment than the prior year and there were no notable increases or decreases in any other category of spending. Net nonoperating revenues decreased by \$4.1 million. State appropriations decreased \$1.9 million. Federal Pell grants decreased by \$217,000. Investment income decreased by almost \$2 million which appears to be a temporary decline of the investment market at year end.

The net result of operations for the year was a decrease in net assets of \$1.9 million.

**Changes from 2010 to 2011:**

Operating revenues increased by \$1.2 million. Tuition and fees, net of scholarship allowance, increased by \$1 million or 7.2% after a tuition rate increase of 5.8% with a 4.3% increase in enrollment and an increase in scholarship allowance of \$1.1 million. Auxiliary revenues increased by \$816,000 or 9.4% after a 2% room and board rate increase and increased housing occupancy.

Operating expenses increased by \$705,000. Of this amount, salary and benefit costs increased slightly. There were no salary increases during the year. Operating supplies increased by 8% and utilities increased by about 15% which is normal, considering the prior year decreased by 15%. University scholarships increased by \$115,000 or 4%.

Net nonoperating revenues increased by \$1.1 million. State appropriations decreased \$339,000 including the loss of the American Recovery and Reinvestment Act (“ARRA”) stimulus funds received in the previous year. Federal Pell grants increased by \$660,000. Investment income increased by \$902,000 which reflected the continued market correction of both stock and bond fund values throughout the year.

The net result of operations for the year was an increase in net assets of \$1.0 million.

### **The Statement of Cash Flows**

The Statements of Cash Flows present information related to cash inflows and outflows summarized by operating, noncapital financing, capital and related financing, and investing activities, and help measure the University’s ability to meet its financial obligations as they mature.

|   | <b>Year Ended June 30</b>  |                            |                            |
|---|----------------------------|----------------------------|----------------------------|
|   | <b><u>2012</u></b>         | <b><u>2011</u></b>         | <b><u>2010</u></b>         |
| Cash provided by (used in):                   |                            |                            |                            |
| Operating activities                          | \$ (12,525,992)            | \$ (12,850,022)            | \$ (12,898,919)            |
| Noncapital financing activities               | 15,774,521                 | 17,488,802                 | 17,514,578                 |
| Capital and related financing activities      | (4,191,545)                | (3,825,600)                | (3,148,994)                |
| Investing activities                          | <u>1,440,476</u>           | <u>(241,713)</u>           | <u>(5,051,775)</u>         |
| Net change in cash and cash equivalents       | 497,460                    | 571,467                    | (3,585,110)                |
| Cash and cash equivalents, beginning of year  | <u>1,961,636</u>           | <u>1,390,169</u>           | <u>4,975,279</u>           |
| <b>Cash and cash equivalents, end of year</b> | <b><u>\$ 2,459,096</u></b> | <b><u>\$ 1,961,636</u></b> | <b><u>\$ 1,390,169</u></b> |

### **Changes from 2011 to 2012:**

The most significant components of cash flows provided from operating activities are tuition and fees, auxiliary activities, grants and contracts. Net cash used in operating activities for the year ended June 30, 2012 was \$12.5 million decreasing slightly from the prior year. The net cash received from noncapital financing activities, which consisted primarily of State appropriations and Federal Pell grants, was \$15.8 million for the year ended June 30, 2012, down \$1.7 million from 2011. The University received \$1.9 less in State appropriations and \$200,000 less from Federal Pell grants than the prior year. Uses of cash from operating activities include payments to employees, vendors and students. Payments to vendors, for consumables such as food and utilities, increased significantly which corresponds to a significant increase in auxiliary revenue.

Net cash used in capital and related financing activities increased by \$366,000. The swap liquidation used \$839,000 in cash which was more than offset with the sale of a related investment. The University spent less on capitalized improvements in 2012.

Cash from investing activities increased by \$1.7 million is mostly attributable to the sale of the investment related to the swap being sold and used to liquidate the swap.

Overall, cash and cash equivalents increased by \$497,000 for the year ended June 30, 2012.

### **Changes from 2010 to 2011:**

The most significant components of cash flows provided from operating activities are tuition and fees, auxiliary activities, grants and contracts. Net cash used in operating activities for the year ended June 30, 2011 was almost identical to the year ended June 30, 2010 at \$12.9 million. The net cash received from noncapital financing activities, which consisted primarily of State appropriations and Federal Pell grants, was \$17.5 million for the year ended June 30, 2011, the same as reported in 2010. Uses of cash from operating activities include payments to employees, vendors and students. Payments to vendors, for consumables such as food and utilities, increased significantly which corresponds to a significant increase in auxiliary revenue.

Net cash used in capital and related financing activities increased by \$677,000. This is indicative of the increased spending for capital improvements

Cash used to purchase investments of \$3,464,000 and cash from investment income of \$470,000 plus \$2,752,000 from the sales and maturities of investments resulted in net cash outflow from investing activities of \$242,000.

Overall, cash and cash equivalents increased by \$571,000 for the year ended June 30, 2011.

### **Factors that Will Affect the Future**

Lake Superior State University achieved reaccreditation by the Higher Learning Commission (HLC) for five years with the next visit to occur in 2016-2017. The accreditation team recognized that the leadership, organization, and strategic direction of the University had been in flux much of the previous ten years and had only recently stabilized. The team believed that there was a need for a shortened reaccreditation timeline to ensure that the University is moving forward and has implemented the structural mechanisms for a culture of communication with the new shared governance model. The next reaccreditation visit will also lead the University into a new pathways model being implemented by the HLC.

The team commented “Lake Superior State University seems to have almost a new lease on life. It has weathered very significant financial and leadership challenges. Now it is poised to embrace shared governance approaches to planning for the future. There will likely be more changes in leadership at the institution and faculty leaders have said their hope for shared governance is to provide institutional stability and preserve progress.”

Appropriations from the State were reduced 15% for the 2011-2012 academic year. This is a \$1.9 million reduction for the University from the previous year and the lowest annual State support received in more than a decade. In 2012-2013, appropriations will increase 3% overall to Michigan’s public universities. The increase will be tied to certain university performance measures. In addition, the State appropriated a very small amount to be distributed to the universities for the Michigan Public Schools Retirement System (MPSERS). This is a small step in the right direction.

Two programs that are mandated by the State but underfunded are the Michigan Indian Tuition Waiver (MITW) and MPSERS. The University paid \$665,900 in MITW in 2011-2012. We estimate a shortfall of over \$3 million over the life of this unfunded mandate to date. The long history behind MPSERS has resulted in an unsustainable burden to the Michigan public universities for which we have no control. There has been some legislative activity on both of these issues and we hope to receive relief and/or more control over these expenses going forward.

Enrollment was up in the fall of 2011 and saw a slight decline in the spring of 2012 from the previous year. Summer enrollment was reported down at colleges and universities across the nation and that held true at Lake Superior State University. University officials here and elsewhere believe enrollments have been heavily impacted by changes in federal financial aid eligibility. The loss of summer Pell grants is thought to be at least partially responsible for lower summer enrollments. It is also thought that with the economy improving, some students may have returned to the work force either because they no longer need a college education to find work or because they are able to work and save money to lessen dependence on student loans during the academic year.

The University will continue to face enrollment challenges in the near future. It is recognized that our geographic area has a limited pool of potential full-time students and the number of traditional age high school graduates are statistically predicted to decline across the nation through 2016. The HLC team was quick to point out these challenges but also commented as follows:

“Lake Superior has a very unique campus, a strong, caring faculty, and a supportive local community that should enable it to shape its image and niche, to market that niche successfully to people in the Eastern Upper Peninsula of Michigan and Canada, and to develop increasing pride among its students, faculty, staff, and alumni. LSSU is postured well to make important strategic decisions that can stabilize enrollment and can solidify the public image that it desires – what a great opportunity for the leadership of this University.”

The University received \$12 million planning authorization for its School of Business renovation project and has submitted its preliminary design to the State. Both the Board of Trustees and the Foundation Board of Directors put their support behind the approximately \$3 million capital campaign needed to match University’s twenty-five percent share of this project. This will be the University’s first State supported capital outlay project in twelve years. The project will add much needed flexible classroom and collaborative space and will also strengthen the University’s financial position.

In November 2011 the Board of Trustees adopted revised mission and vision statements and core values to guide our strategic planning process. They are as follows:

**Mission Statement:** Our mission at Lake Superior State University is to help students develop their full potential. We launch students on paths to rewarding careers and productive, satisfying lives. We serve the regional, state, national and global communities by contributing to the growth, dissemination, and application of knowledge.

**Vision Statement:** Our programs grow and evolve in ways that keep our graduates at the cutting edge of technological and societal advances. As such, we will be viewed by our constituents as:

- The preferred regional choice for students who seek a quality education which provides a competitive edge in an evolving job market.
- An institution where relevant concepts are taught by quality faculty, and are paired with practical real-world experience to provide a well-rounded education.
- An institution which capitalizes on its location to instill graduates with an understanding of environmental issues and an overarching desire to be responsible stewards of the environment.
- A university that is highly student centered and empowers all students to realize their highest individual potential.

Core Values:

- Excellence in Teaching and Learning: Teaching is our first priority and focuses on providing student/faculty interaction, learning, and research in current, relevant programs.
- Opportunity: Students have a wide range of opportunities to grow academically, professionally, culturally and socially. Opportunities are provided via work-study assignments, student organizations, internships, community outreach and leadership.
- Diversity: Students experience a campus community environment which is inclusive and welcoming.
- Ethics and Values: The University promotes an environment which values honesty, openness, and courteous behavior where everyone is treated with respect.
- Stewardship: LSSU provides a framework in which to leave the university and region financially and environmentally sound for future generations of LSSU students, alumni, and friends.

In July 2012 the Board of Trustees adopted our new Strategic Plan. The strategic planning process began with a Board initiated retreat in the spring of 2010. Seven goals evolved from this retreat which had broad campus representation and are as follows:

Within the next 3-5 years, LSSU would:

- be seen as a collaborative, committed campus community as evidenced by a culture of giving, positive attitudes, and campus-wide Laker pride.
- achieve status as a competitive, desirable school of choice for students and families that attracts an internationally diverse student body.
- build bridges to and from the community that create pride and prosperity for both.
- develop superior services and facilities for students that are designed to respond to changing student needs.
- offer excellent programs that maximize regional assets and opportunities as demonstrated by incorporation of experiential learning, student marketability, and use of best practices.
- provide high value, up-to-date educational resources that support learning.
- be positioned for long-term growth and sustainability with a sound strategy for long-term financial stability.

The Strategic Planning and Budget Committee continued with this work and chose to use a balanced scorecard approach to develop strategies and critical outcomes related to the seven goals. The balanced scorecard was utilized to prioritize the strategies and further develop the strategic plan and will continue to be used as an implementation and tracking tool to ensure the University is progressing toward its intended goals. The balanced scorecard also ties the strategic plan to the University's budget.

## INDEPENDENT AUDITORS' REPORT

October 3, 2012

Board of Trustees  
Lake Superior State University  
Sault Ste. Marie, Michigan

We have audited the accompanying financial statements of the business-type activities and the discretely presented component unit of *Lake Superior State University* (“the University”), a component unit of the State of Michigan, as of June 30, 2012 and 2011 and for the years then ended, 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 opinions on these financial statements based on our audits.

We conducted our audits 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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. The financial statements of the Lake Superior State University Foundation were not audited in accordance with *Government Auditing Standards*. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and the discretely presented component unit of *Lake Superior State University* as of June 30, 2012 and 2011 and the respective changes in financial position and cash flows of the University for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued under separate cover our report on our consideration of *Lake Superior State 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, which is included in the University’s single audit 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 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 assurance.

The image shows a handwritten signature in black ink that reads "Lehmann Johnson". The signature is written in a cursive, flowing style with a large initial 'L' and 'J'.

# LAKE SUPERIOR STATE UNIVERSITY

## STATEMENTS OF NET ASSETS

| Assets  | June 30              |                      |
|---|----------------------|----------------------|
|   | 2012                 | 2011                 |
| <b>Current assets</b>                             |                      |                      |
| Cash and cash equivalents                         | \$ 2,459,096         | \$ 1,961,636         |
| Short-term investments                            | 7,517,614            | 7,222,557            |
| Accounts receivable, net                          | 1,533,120            | 1,502,985            |
| State appropriations receivable                   | 1,961,729            | 2,308,036            |
| Inventories                                       | 227,103              | 239,568              |
| Other   | 308,465              | 242,906              |
| <b>Total current assets</b>                       | <b>14,007,127</b>    | <b>13,477,688</b>    |
| <b>Noncurrent assets</b>                          |                      |                      |
| Student loans receivable, net                     | 2,592,713            | 2,762,746            |
| Investments                                       | 4,229                | 1,195,974            |
| Endowment investments                             | 8,019,962            | 8,222,355            |
| Unamortized bond issuance costs                   | 579,774              | -                    |
| Land and art collection                           | 2,512,525            | 2,522,103            |
| Depreciable capital assets, net                   | 48,108,255           | 51,767,938           |
| <b>Total noncurrent assets</b>                    | <b>61,817,458</b>    | <b>66,471,116</b>    |
| <b>Total assets</b>                               | <b>\$ 75,824,585</b> | <b>\$ 79,948,804</b> |
| <b>Liabilities</b>                                |                      |                      |
| <b>Current liabilities</b>                        |                      |                      |
| Accounts payable and accrued expenses             | \$ 2,196,493         | \$ 2,919,063         |
| Unearned revenue                                  | 968,010              | 1,073,446            |
| Deposits  | 177,115              | 189,060              |
| Current portion of long-term debt                 | 1,293,354            | 1,318,774            |
| Current portion of employee benefit programs      | 206,000              | 171,000              |
| <b>Total current liabilities</b>                  | <b>4,840,972</b>     | <b>5,671,343</b>     |
| Interest rate swap liability                      | -                    | 839,000              |
| Long-term debt, net of current portion            | 23,496,153           | 24,063,130           |
| Employee benefit programs, net of current portion | 1,384,400            | 1,416,945            |
| <b>Total liabilities</b>                          | <b>29,721,525</b>    | <b>31,990,418</b>    |
| <b>Net assets</b>                                 |                      |                      |
| Invested in capital assets, net of related debt   | 27,340,744           | 29,980,781           |
| Restricted  |                      |                      |
| Nonexpendable                                     |                      |                      |
| Scholarships and research                         | 205,327              | 205,327              |
| Expendable  |                      |                      |
| Scholarships and research                         | 8,965,550            | 9,097,891            |
| Loans   | 3,047,456            | 3,064,422            |
| Capital projects and debt service                 | 1,703,866            | 1,554,780            |
| Unrestricted                                      | 4,840,117            | 4,055,185            |
| <b>Total net assets</b>                           | <b>46,103,060</b>    | <b>47,958,386</b>    |
| <b>Total liabilities and net assets</b>           | <b>\$ 75,824,585</b> | <b>\$ 79,948,804</b> |

The accompanying notes are an integral part of these financial statements.

## LAKE SUPERIOR STATE UNIVERSITY

### STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

|  | Year Ended June 30   |                      |
|--|----------------------|----------------------|
|  | 2012                 | 2011                 |
| <b>Operating revenues</b>  |                      |                      |
| Tuition and fees (net of scholarship allowances of \$7,832,429 and \$7,815,998 in 2012 and 2011, respectively) | \$ 16,309,655        | \$ 15,078,886        |
| Federal grants and contracts   | 1,111,037            | 1,390,764            |
| State grants and contracts   | 97,286               | 224,644              |
| Nongovernmental grants and contracts   | 2,871,253            | 2,851,825            |
| Auxiliary activities   | 9,749,205            | 9,509,887            |
| Other  | 1,197,224            | 933,559              |
| <b>Total operating revenues</b>  | <b>31,335,660</b>    | <b>29,989,565</b>    |
| <b>Operating expenses</b>  |                      |                      |
| Instruction  | 13,385,670           | 13,423,513           |
| Research   | 396,020              | 369,014              |
| Public service   | 1,053,557            | 966,754              |
| Academic support   | 2,968,127            | 3,068,742            |
| Student services   | 2,719,361            | 2,736,864            |
| Student aid  | 2,514,045            | 2,675,056            |
| Institutional support  | 5,424,953            | 5,506,192            |
| Operation and maintenance of plant   | 5,035,842            | 4,921,187            |
| Auxiliary activities   | 8,840,275            | 8,634,320            |
| Depreciation   | 4,792,374            | 4,892,209            |
| Other  | 670,954              | 446,667              |
| <b>Total operating expenses</b>  | <b>47,801,178</b>    | <b>47,640,518</b>    |
| <b>Operating loss</b>  | <b>(16,465,518)</b>  | <b>(17,650,953)</b>  |
| <b>Nonoperating revenues (expenses)</b>  |                      |                      |
| State appropriations   | 10,740,629           | 12,595,896           |
| Federal Pell grants  | 4,651,340            | 4,868,079            |
| Interest on capital debt and leases  | (1,459,161)          | (1,359,797)          |
| Investment income, net of investment expenses  | 341,395              | 2,291,531            |
| Gifts for expendable endowments  | 33,736               | 50,090               |
| (Loss) gain on assets sold or retired  | (11,373)             | 4,801                |
| <b>Net nonoperating revenues</b>   | <b>14,296,566</b>    | <b>18,450,600</b>    |
| <b>(Loss) gain before other revenues</b>   | <b>(2,168,952)</b>   | <b>799,647</b>       |
| <b>Other revenues</b>  |                      |                      |
| Capital grants and gifts   | 313,626              | 224,202              |
| <b>(Decrease) increase in net assets</b>   | <b>(1,855,326)</b>   | <b>1,023,849</b>     |
| Net assets, beginning of year  | 47,958,386           | 46,934,537           |
| <b>Net assets, end of year</b>   | <b>\$ 46,103,060</b> | <b>\$ 47,958,386</b> |

The accompanying notes are an integral part of these financial statements.

# LAKE SUPERIOR STATE UNIVERSITY

## STATEMENTS OF CASH FLOWS

|  | Year Ended June 30  |                     |
|--|---------------------|---------------------|
|  | 2012                | 2011                |
| <b>Cash flows from operating activities</b>                      |                     |                     |
| Tuition and fees   | \$ 16,070,829       | \$ 14,991,922       |
| Grants and contracts   | 4,298,256           | 4,226,718           |
| Payments to employees  | (28,080,032)        | (27,784,741)        |
| Payments to vendors  | (13,286,451)        | (12,098,948)        |
| Payments for financial aid                                       | (2,514,045)         | (2,675,056)         |
| Loans issued to students   | (325,491)           | (472,630)           |
| Collections of interest and principal on loans to students       | 495,524             | 412,868             |
| Auxiliary activities   | 9,703,611           | 9,534,258           |
| Other receipts   | 1,111,807           | 1,015,587           |
| <b>Net cash used in operating activities</b>                     | <b>(12,525,992)</b> | <b>(12,850,022)</b> |
| <b>Cash flows from noncapital financing activities</b>           |                     |                     |
| State appropriations   | 11,086,936          | 12,575,429          |
| Federal Pell grants  | 4,653,849           | 4,863,283           |
| Gifts for expendable endowments                                  | 33,736              | 50,090              |
| Federal Direct Lending receipts                                  | 14,740,890          | 14,800,517          |
| Federal Direct Lending disbursements                             | (14,740,890)        | (14,800,517)        |
| <b>Net cash provided by noncapital financing activities</b>      | <b>15,774,521</b>   | <b>17,488,802</b>   |
| <b>Cash flows from capital and related financing activities</b>  |                     |                     |
| Payment of interest rate swap liability                          | (839,000)           | -                   |
| Proceeds from bond issue   | 23,871,827          | -                   |
| Refunded bonds   | (23,435,000)        | -                   |
| Payment of bond issuance costs                                   | (579,774)           | -                   |
| Capital grants and gifts received                                | 277,362             | 193,202             |
| Purchases and construction of capital assets                     | (759,733)           | (1,301,515)         |
| Proceeds from disposal of capital assets                         | 7,946               | 7,000               |
| Principal paid on debt and capital leases                        | (1,374,528)         | (1,358,242)         |
| Interest paid on debt and capital leases                         | (1,360,645)         | (1,366,045)         |
| <b>Net cash used in capital and related financing activities</b> | <b>(4,191,545)</b>  | <b>(3,825,600)</b>  |
| <b>Cash flows from investing activities</b>                      |                     |                     |
| Proceeds from sales and maturities of investments                | 2,478,610           | 2,752,082           |
| Purchases of investments   | (1,442,103)         | (3,463,801)         |
| Investment income, net   | 403,969             | 470,006             |
| <b>Net cash provided by (used in) investing activities</b>       | <b>1,440,476</b>    | <b>(241,713)</b>    |
| Net increase in cash and cash equivalents                        | 497,460             | 571,467             |
| Cash and cash equivalents, beginning of year                     | 1,961,636           | 1,390,169           |
| <b>Cash and cash equivalents, end of year</b>                    | <b>\$ 2,459,096</b> | <b>\$ 1,961,636</b> |

The accompanying notes are an integral part of these financial statements.

# LAKE SUPERIOR STATE UNIVERSITY

## STATEMENTS OF CASH FLOWS

(Continued)

|  | Year Ended June 30     |                        |
|--|------------------------|------------------------|
|  | 2012                   | 2011                   |
| <b>Reconciliation of operating loss to net cash used in operating activities</b> |                        |                        |
| Operating loss   | \$ (16,465,518)        | \$ (17,650,953)        |
| Adjustments to reconcile operating loss to net cash used in operating activities |                        |                        |
| Depreciation   | 4,792,374              | 4,892,209              |
| Provision for uncollectible accounts and student loans receivables               | 64,239                 | 38,494                 |
| Change in assets and liabilities:  |                        |                        |
| Accounts receivable, net   | (86,733)               | (423,073)              |
| Student loans receivable, net  | 158,751                | (33,087)               |
| Inventories  | 12,465                 | 53,427                 |
| Other  | (65,559)               | 137,248                |
| Accounts payable and accrued expenses  | (821,086)              | (32,496)               |
| Unearned revenue   | (105,436)              | 115,486                |
| Deposits   | (11,945)               | 21,338                 |
| Employee benefit programs  | 2,456                  | 31,385                 |
| <b>Net cash used in operating activities</b>                                     | <b>\$ (12,525,992)</b> | <b>\$ (12,850,022)</b> |
| <b>Supplemental disclosures of non-cash financing and investing activities</b>   |                        |                        |
| Gifts in-kind received and recorded as capital assets                            | \$ 37,396              | \$ 33,394              |
| Entered into capital lease to purchase capital equipment                         | \$ 345,304             | \$ -                   |

The accompanying notes are an integral part of these financial statements.

# LAKE SUPERIOR STATE UNIVERSITY FOUNDATION

## STATEMENTS OF NET ASSETS

|  | June 30             |                     |
|--|---------------------|---------------------|
|  | 2012                | 2011                |
| <b>Assets</b>  |                     |                     |
| <b>Current assets</b>                                  |                     |                     |
| Cash and cash equivalents                              | \$ 865,257          | \$ 802,416          |
| Short-term investments                                 | 1,200,000           | 1,000,000           |
| Other current assets                                   | 28,597              | 28,984              |
| Current portion of unconditional promises to give, net | 70,042              | 12,340              |
| <b>Total current assets</b>                            | <b>2,163,896</b>    | <b>1,843,740</b>    |
| <b>Noncurrent assets</b>                               |                     |                     |
| Investments  | 6,037,815           | 5,881,404           |
| Unconditional promises to give, net of current portion | 78,036              | 77,086              |
| Beneficial interest in charitable remainder trust      | 330,335             | 341,819             |
| <b>Total noncurrent assets</b>                         | <b>6,446,186</b>    | <b>6,300,309</b>    |
| <b>Total assets</b>                                    | <b>\$ 8,610,082</b> | <b>\$ 8,144,049</b> |
| <b>Liabilities</b>                                     |                     |                     |
| <b>Current liabilities</b>                             |                     |                     |
| Accounts payable and accrued expenses                  | \$ 19,113           | \$ 12,140           |
| Employee benefit programs                              | 22,919              | 20,891              |
| <b>Total current liabilities</b>                       | <b>42,032</b>       | <b>33,031</b>       |
| Annuity obligations                                    | 52,097              | 55,453              |
| <b>Total liabilities</b>                               | <b>94,129</b>       | <b>88,484</b>       |
| <b>Net assets</b>                                      |                     |                     |
| Restricted   |                     |                     |
| Nonexpendable  | 5,063,140           | 4,725,990           |
| Expendable   | 2,830,945           | 2,801,900           |
| Unrestricted   | 621,868             | 527,675             |
| <b>Total net assets</b>                                | <b>8,515,953</b>    | <b>8,055,565</b>    |
| <b>Total liabilities and net assets</b>                | <b>\$ 8,610,082</b> | <b>\$ 8,144,049</b> |

The accompanying notes are an integral part of these financial statements.

**LAKE SUPERIOR STATE UNIVERSITY FOUNDATION**  
**STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS**

|   | <b>Year Ended June 30</b> |                     |
|---|---------------------------|---------------------|
|   | <b>2012</b>               | <b>2011</b>         |
| <b>Operating revenues</b>                       |                           |                     |
| Contributions                                   | \$ 1,454,356              | \$ 1,219,014        |
| Change in value of split interest agreements    | (8,562)                   | 45,641              |
| <b>Total operating revenues</b>                 | <b>1,445,794</b>          | <b>1,264,655</b>    |
| Operating expenses                              | 447,271                   | 402,340             |
| <b>Operating income</b>                         | <b>998,523</b>            | <b>862,315</b>      |
| <b>Nonoperating revenues (expenses)</b>         |                           |                     |
| Investment income, net                          | 203,219                   | 215,580             |
| Net unrealized (losses) gains on investments    | (112,889)                 | 954,698             |
| Distributions to Lake Superior State University | (628,465)                 | (590,232)           |
| <b>Net nonoperating (expenses) revenues</b>     | <b>(538,135)</b>          | <b>580,046</b>      |
| <b>Increase in net assets</b>                   | <b>460,388</b>            | <b>1,442,361</b>    |
| Net assets, beginning of year                   | 8,055,565                 | 6,613,204           |
| <b>Net assets, end of year</b>                  | <b>\$ 8,515,953</b>       | <b>\$ 8,055,565</b> |

The accompanying notes are an integral part of these financial statements.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

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### 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### **Reporting Entity**

*Lake Superior State University* (“the University”) is an institution of higher education and is considered a discrete component unit of the State of Michigan (“State”) because its Board of Trustees is appointed by the Governor. Accordingly, the University's financial statements are included in those of the State. Transactions with the State relate primarily to appropriations for operations, appropriations for charter schools, grants from various State agencies, State Building Authority (SBA) revenues and payments to the State retirement program on behalf of certain University employees.

As required by the Governmental Accounting Standards Board (“GASB”), the University’s basic financial statements include the financial statements of both the University and its component unit, the *Lake Superior State University Foundation* (the “Foundation”) which is a legally separate tax-exempt component unit of the University. The Foundation acts primarily as a fund-raising organization established to supplement the resources that are available to the University in support of its programs. The Foundation’s Board of Directors includes members of the University’s Board of Trustees, certain officers of the University and other community representatives elected by the Foundation Board. Although the University does not necessarily control the timing or amount of receipts from the Foundation, the majority of its resources or income earned thereon are restricted by the donors to the activities of the University. Because these restricted resources held by the Foundation can be used only by, or for the benefit of, the University, the Foundation is considered a component unit of the University. The Foundation financial statements are reported on separate pages to emphasize that a) it is legally separate from the University and b) its assets are not necessarily available to satisfy all liabilities of the University.

Contributions to the University by the Foundation (reported primarily as other revenues-capital gifts and grants) have been made in the amount of \$628,465 and \$590,232 during 2012 and 2011, respectively. Support from the University provided to the Foundation amounted to \$432,227 and \$418,000 during 2012 and 2011, respectively.

#### **Basis of Presentation - University**

The accompanying University financial statements have been prepared using the economic resource measurement focus and the accrual basis of accounting with the exception that certain investment income and interest earned on the Federal Perkins student loan program are recorded only when received.

In accordance with generally accepted accounting principles, the University follows all applicable GASB pronouncements. In applying these accounting pronouncements, the University follows the guidance for special purpose governments engaged only in “business-type” activities rather than issuing financial statements that focus on accountability of individual funds.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

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### **Basis of Presentation - Foundation**

The Foundation is a nonprofit organization that reports under Financial Accounting Standards Board (FASB) standards, including Accounting Standards Codification (“ASC”) Topic 958-605-05, *Accounting for Contributions Received and Contributions Made*, and ASC Topic 958-205-05, *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. With the exception of necessary presentation adjustments, no modifications have been made to the Foundation’s financial information in the University’s financial report for these differences.

### **Use of Estimates**

The preparation of the financial statements in conformity with generally accepted accounting principles require management to make estimates and assumptions that affect the amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates include but are not limited to the accounts receivable allowance and insurance reserves.

### **Cash and Cash Equivalents**

Cash and cash equivalents at the University and the Foundation consist of demand deposits and highly liquid investments, excluding noncurrent investments, with an original maturity when purchased of three months or less.

### **Short-Term Investments**

Short-term investments consist of certificates of deposit with maturities of less than one year and liquid bond/fixed income funds.

### **Investments and Endowment Investments**

University and Foundation investments and endowment investments consist primarily of mutual funds and are stated at fair value. Realized and unrealized gains and losses are reflected in the statements of revenues, expenses and changes in net assets. The Foundation maintains investment accounts for its expendable and nonexpendable endowments.

### **Accounts Receivable**

Accounts receivable are stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a provision for bad debt expense when necessary and an adjustment to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

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### Inventories

Inventories, consisting primarily of supplies and petroleum products, are valued at cost (using the specific identification method) not in excess of market.

### Capital Assets

Capital assets, consisting of institutional physical properties used in University operations, are stated at cost when purchased and at estimated fair value at date of receipt for other acquisitions. Building additions and improvements with a cost in excess of \$10,000 are capitalized if the life of the building is extended. Equipment with a cost in excess of \$2,500 with a useful life of 3 or more years is capitalized. Certain maintenance and replacement reserves have been established to provide for significant repair and maintenance costs to residence halls and certain other facilities.

Depreciation is provided on a straight-line basis over the estimated useful life of the related capital assets as follows:

| <u>Classification</u>               | <u>Life</u>    |
|-------------------------------------|----------------|
| Buildings and building improvements | 40 to 60 years |
| Land improvements                   | 20 years       |
| Infrastructure                      | 20 years       |
| Equipment                           | 7 years        |
| Personal computers                  | 3 years        |
| Library books                       | 7 years        |
| Vehicles                            | 7 years        |

### Revenue Recognition

Revenues are recognized when earned and expenses are recognized when the service is provided or when materials are received. Restricted grant revenue is recognized only to the extent expended. Operating revenues of the University consist of tuition and fees, grants and contracts, and auxiliary enterprise revenues. Transactions related to capital and financing activities, noncapital financing activities, investing activities, State appropriations, and Federal Pell grant revenue are components of nonoperating revenue. Restricted and unrestricted resources are allocated to the appropriate departments within the University which are responsible for adhering to any donor restrictions.

State appropriation revenue is recognized in the period for which it is appropriated.

During 2012 and 2011, the University received \$32,371,759 and \$26,407,851 (net of a 3% administrative fee retained by the University), respectively, of State appropriations which were forwarded to ten and seven charter schools, respectively. The University also received \$100,000 in State appropriations for Bay Mills Community College during fiscal 2012 and 2011, which was forwarded to Bay Mills Community College on a monthly basis when received. Appropriations received and related disbursements passed on to the charter schools and Bay Mills Community College are considered agency transactions and, accordingly, are not reported in the accompanying financial statements.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

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Contributions, including unconditional promises to give, are recognized by the Foundation as revenues in the period received. Conditional promises to give are recognized when the conditions on which they depend are substantially met. The Foundation records donations of non-cash assets at their appraised or fair value at the date of the gift.

### **Unearned Revenue**

Unearned revenue consists primarily of advance payment for sports camps, room and board, sales for athletic events and summer tuition not earned during the current year.

### **Income Taxes**

The University is classified as a State instrumentality under Internal Revenue Code Section 115, and is also classified as a charitable organization under Internal Revenue Code section 501 (c) (1), and is therefore exempt from federal income taxes. Certain activities of the University may be subject to taxation as unrelated business income under Internal Revenue Code Sections 511 to 514. No such taxes were incurred for either fiscal year 2012 or 2011.

The Foundation is also exempt from federal income taxes under Section 501(c) (3) and qualifies as a nonprofit foundation under Section 509 (a) (1) of the Internal Revenue Code. Accordingly, no provision for income taxes has been recorded in the accompanying financial statements.

ASC Topic 740, *Accounting for Uncertainty in Income Taxes*, prescribes the recognition threshold and measurement attribute for disclosures of tax positions previously taken or expected to be taken on an income tax return. The Foundation analyzed its filing positions in the state jurisdictions where it is required to file income tax returns, including tax years 2008 through 2012 in these jurisdictions. The Foundation has also elected to retain its existing accounting policy with respect to the treatment of interest and penalties attributable to income taxes, and continues to reflect any charges for such, to the extent they arise, as a component of operating expenses. The continued application of ASC Topic 740 had no significant impact on the Foundation's financial statements.

### **Split-Interest Agreements**

#### ***Beneficial Interest in Charitable Remainder Trust***

The Foundation is a beneficiary of certain irrevocable charitable remainder trusts. Contribution revenue was recognized at the date the trust was established based on the expected present value of the Foundation's interest in the trust assets. Changes in the value of the assets and other changes in the estimates of future receipts are reported in the statements of revenues, expenses and changes in net assets of the Foundation.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

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### *Annuity Obligations*

The Foundation's annuity and life income agreements require payments during the life of the annuitant at various rates up to 7% of the principal amounts. The obligation for annuity obligations payable is reported at the present value of the future payments based on life expectancy tables and an implied discount rate of 5.8%. Changes in the value of annuity obligations payable are reported in the statements of revenues, expenses and changes in net assets of the Foundation.

### **Fair Value Measurements**

As required by ASC Topic 820, *Fair Value Measurements*, the Foundation has categorized its financial assets and liabilities into a three-level fair value hierarchy, based on the nature of the inputs used in determining fair value. The hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). For a further discussion of ASC Topic 820, refer to Note 4.

### **Net Assets**

The net assets and revenues, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, the net assets of the Foundation have been grouped into the following three classes:

***Unrestricted net assets:*** Generally result from revenues derived from providing services, receiving unrestricted contributions, unrealized and realized gains and losses, and dividends and interest from investing in income-producing assets, less the expenses incurred in providing services, raising contributions, and performing administrative functions.

***Temporarily restricted net assets:*** Generally result from contributions, unrealized and realized gains and losses, and dividends and interest from investing in income-producing assets, and other inflows of assets, which are held for specific purposes as stipulated by the donor. Temporarily restricted net assets are released from restrictions by the passage of time or by actions of the Foundation, pursuant to the donors' stipulations.

***Permanently restricted net assets:*** Generally result from contributions and other inflows of assets that represent permanent endowments where use is limited by donor-imposed stipulations that neither expire by the passage of time nor can be fulfilled or otherwise removed by the Foundation.

### **Subsequent Events**

In preparing these financial statements, Foundation management has evaluated, for the potential recognition or disclosure, significant events or transactions that occurred during the period subsequent to June 30, 2012, the most recent statement of financial position presented herein, through October 3, 2012, the date these financial statements were available to be issued. No such significant events or transactions were identified.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

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### 2. CASH AND CASH EQUIVALENTS AND INVESTMENTS - UNIVERSITY

**Cash and short-term investments** - The University utilizes the "pooled cash" method of accounting for substantially all of its cash and short-term investments. Investment policies for cash and short-term investments, as set forth by the Board of Trustees, authorize the University to invest, with limitations, in commercial paper of companies with a rating within the two highest classifications of prime as established by at least one of the standard rating services. Investments may also be made in securities of the U.S. Treasury and federal agencies and in time savings accounts. Short-term investments are stated at fair value.

**Investments** - The Board of Trustees has authorized certain University administrators to invest in short, intermediate and long-term pools of investments, depending on the nature and need of funds. An established Board policy is followed for the investment of University funds. The primary investment objective for the investment pools is as follows:

- *Short-term investment pool* - to provide for the preservation of capital. Funds needed for expenditures in less than one year will be considered short-term.
- *Intermediate investment pool* - to provide for preservation of capital and maximization of income without undue exposure to risk. Funds needed for expenditures within one to five years will be considered intermediate term.
- *Long-term investment pool* - to provide for long-term growth of principal and income without undue exposure to risk. Funds not needed for expenditures within five years will be considered long-term. The University's general policy toward the long-term investment pool shall be to diversify investments within both equity and fixed income securities so as to provide a balance that will enhance total return. The University invests with selected money managers as part of an institutional mutual fund or in segregated accounts.

Performance objectives for each pool of investments have been established to measure the total return of a manager against a comparable index, as well as the amount of risk the manager is taking. The University uses the service of outside investment counsel in providing performance measurements and asset allocation recommendations.

Reports are submitted to the Board of Trustees on an annual basis to ensure compliance with the prescribed policy.

Investment income and realized gains or losses are allocated using an average balance method on accounts designated to receive investment earnings. Unrealized gains or losses are allocated based on investment balances on June 30.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

University cash and cash equivalents consist of the following amounts at June 30:

|  | <b>2012</b>         | <b>2011</b>         |
|--|---------------------|---------------------|
| Disbursement accounts                  | \$ 1,689,017        | \$ 1,198,723        |
| Money market funds                     | 770,079             | 762,913             |
| <b>Total cash and cash equivalents</b> | <b>\$ 2,459,096</b> | <b>\$ 1,961,636</b> |

At June 30, 2011, \$1,165,416 held by the University in disbursement accounts were held at Central Savings Bank ("CSB"), whose Chief Executive officer was the Chair of the University's Board of Trustees during the year ended June 30, 2011.

The University utilizes the "pooled" method of accounting for substantially all investments, which consist of the following amounts at June 30:

|  | <b>2012</b>         | <b>2011</b>         |
|--|---------------------|---------------------|
| <u>University short-term investments</u>       |                     |                     |
| Certificates of deposit                        | \$ 1,269,164        | \$ 1,270,024        |
| Mutual funds                                   |                     |                     |
| Bond/fixed income funds                        | 6,248,450           | 5,952,533           |
| <b>Total University short-term investments</b> | <b>\$ 7,517,614</b> | <b>\$ 7,222,557</b> |
| <u>University endowment investments</u>        |                     |                     |
| Mutual funds                                   |                     |                     |
| Equity funds                                   | \$ 5,382,488        | \$ 5,600,928        |
| Bond/fixed income funds                        | 2,040,839           | 1,994,809           |
| Exchange traded funds                          | 596,635             | 626,618             |
| <b>Total University endowment investments</b>  | <b>8,019,962</b>    | <b>8,222,355</b>    |
| <u>University investments</u>                  |                     |                     |
| Mutual funds                                   |                     |                     |
| Money market funds                             | \$ 4,229            | \$ 844              |
| Bond/fixed income funds                        | -                   | 616,303             |
| Equity funds                                   | -                   | 578,827             |
| <b>Total University investments</b>            | <b>4,229</b>        | <b>1,195,974</b>    |
| <b>Total investments</b>                       | <b>\$ 8,024,191</b> | <b>\$ 9,418,329</b> |

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

**Interest Rate Risk** – The University’s investment policy does not limit investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. The maturity dates for each investment type (including investment types classified as cash and cash equivalents) susceptible to interest rate risk are identified below for investments held at year end.

As of June 30, 2012, the University had the following investments with related maturities:

|                          | Maturities (in Years) |                     |             |                     |
|--------------------------|-----------------------|---------------------|-------------|---------------------|
|                          | Fair Market           |                     |             |                     |
|                          | Value                 | Less Than 1         | 1-5         | 6-10                |
| Money market funds       | \$ 774,308            | \$ 774,308          | \$ -        | \$ -                |
| Bond/fixed income funds  | 8,289,289             | 6,248,450           | -           | 2,040,839           |
| <b>Total investments</b> | <b>\$ 9,063,597</b>   | <b>\$ 7,022,758</b> | <b>\$ -</b> | <b>\$ 2,040,839</b> |

As of June 30, 2011, the University had the following investments with related maturities:

|                          | Maturities (in Years) |                     |             |                     |
|--------------------------|-----------------------|---------------------|-------------|---------------------|
|                          | Fair Market           |                     |             |                     |
|                          | Value                 | Less Than 1         | 1-5         | 6-10                |
| Money market funds       | \$ 763,757            | \$ 763,757          | \$ -        | \$ -                |
| Bond/fixed income funds  | 8,563,645             | 6,091,359           | -           | 2,472,286           |
| <b>Total investments</b> | <b>\$ 9,327,402</b>   | <b>\$ 6,855,116</b> | <b>\$ -</b> | <b>\$ 2,472,286</b> |

**Credit Risk** - State law limits investments to specific government securities, certificates of deposits and bank accounts with qualified financial institutions, commercial paper with specific maximum maturities and ratings when purchased and qualified mutual funds. The University’s investment policy does not have specific limits in excess of state law on investment credit risk.

**Custodial Credit Risk – Deposits** - Custodial credit risk is the risk that in the event of a bank failure, the University’s deposits may not be returned. State law does not require a policy for deposit custodial credit risk. The University believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all bank deposits. As a result, management evaluates each financial institution it deposits University funds with and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories. As of June 30, 2012, \$19,011 of the University’s bank balance of \$2,775,485 was exposed to custodial credit risk because it was uninsured and uncollateralized.

**Custodial Credit Risk – Investments** - For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the University will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. State law does not require the University to have a policy for investment custodial credit risk. Custodial credit risk for the University’s mutual fund investments cannot be determined as these investments are not evidenced by specifically identifiable securities.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

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**Concentration of Credit Risk** - State law limits allowable investments but does not limit concentration of credit risk. The University's investment policy does not have specific limits in excess of state law on concentration of credit risk.

**Foreign Currency Risk** – The University's exposure to foreign currency risk is derived from its positions in international investments consisting solely of foreign currency denominated mutual fund equity investments. The University's investment policy permits investments in these asset types. At June 30, 2012 and 2011, the University held 31,414 and 30,625 units, respectively, of the EuroPacific Growth Fund Class F (Security identifier: AEGFX) with a fair value of \$1,156,975 and \$1,317,178, respectively. The University holds no other assets which may be subject to the risks of foreign currency.

No foreign currency risk exists with respect to any holdings under the caption "cash and cash equivalents" in the accompanying statements of net assets and all international investments are equity investments held through mutual funds.

Policies regarding marketable securities in the University endowment investments, as set forth by the Board of Trustees, authorize the investment manager to invest in high-grade equities, bonds or other marketable securities. The University endowment income spending policy is 4.5% of the 20-quarter rolling average of the market value of the endowment pool. The annual spending income allocation cannot reduce the original gift principal. The spending policy is reviewed periodically by the finance committee, which recommends changes to the Board of Trustees. The net appreciation on University investments of donor-restricted endowments approximated \$1,338,000 and \$1,566,000 at June 30, 2012 and 2011, respectively. Net appreciation is a component of restricted, expendable net assets.

The yields of the University endowment investments were as follows for the years ended June 30:

|  | <u>2012</u>        | <u>2011</u>         |
|--|--------------------|---------------------|
| Interest and dividends                     | 2.1%               | 3.0%                |
| Net realized and unrealized (losses) gains | <u>(1.3)</u>       | <u>20.0</u>         |
| <b>Total investment gain</b>               | <b><u>0.8%</u></b> | <b><u>23.0%</u></b> |

According to the law of the State of Michigan, the Board of Trustees may appropriate for expenditure for the uses and purposes for which an endowment is established an allocation of the net appreciation, realized and unrealized, in the fair value of the assets of an endowment over the historic dollar value as is prudent under the facts and circumstances prevailing at the time of the action or decision.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

### 3. INVESTMENTS - FOUNDATION

The Foundation also utilizes the "pooled" method of accounting for substantially all investments, which consist of the following amounts at June 30:

|                                     | <u>2012</u>                | <u>2011</u>                |
|-------------------------------------|----------------------------|----------------------------|
| Mutual funds                        |                            |                            |
| Index funds                         | \$ 1,871,272               | \$ 1,826,332               |
| Growth funds                        | 1,613,381                  | 1,687,053                  |
| Bond/fixed income funds             | 2,962,232                  | 2,566,411                  |
| Exchange traded funds               | 467,863                    | 465,445                    |
| Value funds                         | 306,544                    | 321,228                    |
| Money market                        | <u>1,165</u>               | <u>920</u>                 |
| Subtotal                            | 7,222,457                  | 6,867,389                  |
| Marketable securities               | <u>15,358</u>              | <u>14,015</u>              |
| <b>Total Foundation investments</b> | <b><u>\$ 7,237,815</u></b> | <b><u>\$ 6,881,404</u></b> |

The following is a summary of unrealized gains and losses for the Foundation as of June 30:

|   | <u>2012</u>                | <u>2011</u>              |
|---|----------------------------|--------------------------|
| Mutual funds                                      |                            |                          |
| Index funds                                       | \$ 48,328                  | \$ 392,118               |
| Growth funds                                      | (170,067)                  | 394,096                  |
| Bond/fixed income funds                           | 41,222                     | (33,998)                 |
| Exchange traded funds                             | (12,910)                   | 108,327                  |
| Value funds                                       | <u>(20,805)</u>            | <u>92,173</u>            |
| Subtotal  | (114,232)                  | 952,716                  |
| Marketable securities                             | <u>1,343</u>               | <u>1,982</u>             |
| <b>Total Foundation unrealized (losses) gains</b> | <b><u>\$ (112,889)</u></b> | <b><u>\$ 954,698</u></b> |

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

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### 4. FAIR VALUE

The Foundation utilizes fair value measurements to record fair value adjustments to investments and the beneficial interest in charitable remainder trust and to determine fair value disclosures. These assets are recorded at fair value on a recurring basis.

**Fair Value Hierarchy** - Under ASC Topic 820, the Foundation groups its assets at fair value into three levels, based on the markets in which the investments are traded and the reliability of the assumptions used to determine fair value. These levels are:

*Level 1:* Valuation is based upon quoted prices for identical instruments traded in active markets. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange, U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets, and money market funds.

*Level 2:* Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

*Level 3:* Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates that market participants would use in pricing the asset or liability.

Following is a description of the valuation methodologies used for assets recorded at fair value:

**Investments:** Fair value measurement is based upon quoted prices, if available. Level 1 investments include mutual funds and marketable securities. Level 3 investments include bond/fixed income fund which is based on a value provided by a third party investment manager. The value is quoted on a private market that is not active.

**Beneficial Interest in Charitable Remainder Trust:** Fair value measurement is based upon the fair value of the underlying investments in the trusts, an estimated rate of return, anticipated future payments to be made to beneficiaries, living beneficiaries' life expectancies, and an assumed discount rate as discussed further in Note 7.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

The following table sets forth by level, within the fair value hierarchy, the Foundation's assets at fair value as of June 30, 2012:

|  | <b>Level 1</b>             | <b>Level 2</b>     | <b>Level 3</b>           | <b>Total</b>               |
|--|----------------------------|--------------------|--------------------------|----------------------------|
| Mutual funds                           |                            |                    |                          |                            |
| Index funds                            | \$ 1,871,272               | \$ -               | \$ -                     | \$ 1,871,272               |
| Growth funds                           | 1,613,381                  | -                  | -                        | 1,613,381                  |
| Bond/fixed income fund                 | 2,685,501                  | -                  | 276,731                  | 2,962,232                  |
| Exchange traded funds                  | 467,863                    | -                  | -                        | 467,863                    |
| Value funds                            | 306,544                    | -                  | -                        | 306,544                    |
| Money market                           | 1,165                      | -                  | -                        | 1,165                      |
| Marketable securities                  | 15,358                     | -                  | -                        | 15,358                     |
| <b>Total investments at fair value</b> | <b><u>\$ 6,961,084</u></b> | <b><u>\$ -</u></b> | <b><u>\$ 276,731</u></b> | <b><u>\$ 7,237,815</u></b> |
| <b>Beneficial Interest in</b>          |                            |                    |                          |                            |
| <b>Charitable Remainder Trust</b>      | <b><u>\$ -</u></b>         | <b><u>\$ -</u></b> | <b><u>\$ 330,335</u></b> | <b><u>\$ 330,335</u></b>   |

The following table sets forth by level, within the fair value hierarchy, the Foundation's assets at fair value as of June 30, 2011:

|  | <b>Level 1</b>             | <b>Level 2</b>     | <b>Level 3</b>           | <b>Total</b>               |
|--|----------------------------|--------------------|--------------------------|----------------------------|
| Mutual funds                           |                            |                    |                          |                            |
| Index funds                            | \$ 1,826,332               | \$ -               | \$ -                     | \$ 1,826,332               |
| Growth funds                           | 1,687,053                  | -                  | -                        | 1,687,053                  |
| Bond/fixed income fund                 | 2,301,141                  | -                  | 265,270                  | 2,566,411                  |
| Exchange traded funds                  | 465,445                    | -                  | -                        | 465,445                    |
| Value funds                            | 321,228                    | -                  | -                        | 321,228                    |
| Money market                           | 920                        | -                  | -                        | 920                        |
| Marketable securities                  | 14,015                     | -                  | -                        | 14,015                     |
| <b>Total investments at fair value</b> | <b><u>\$ 6,616,134</u></b> | <b><u>\$ -</u></b> | <b><u>\$ 265,270</u></b> | <b><u>\$ 6,881,404</u></b> |
| <b>Beneficial Interest in</b>          |                            |                    |                          |                            |
| <b>Charitable Remainder Trust</b>      | <b><u>\$ -</u></b>         | <b><u>\$ -</u></b> | <b><u>\$ 341,819</u></b> | <b><u>\$ 341,819</u></b>   |

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

The following table sets forth a summary of changes in the fair value of the Foundation's Level 3 assets for the year ended June 30, 2012:

|  | <b><u>Bond/Fixed<br/>Income Fund</u></b> | <b><u>Beneficial<br/>Interest in<br/>Charitable<br/>Remainder<br/>Trust</u></b> |
|--|--|---|
| Balance at beginning of year                                 | \$ 265,270                               | \$ 341,819  |
| Unrealized gains relating to investments<br>held at year end | 11,461                                   | -   |
| Change in value  | <u>-</u>                                 | <u>(11,484)</u>   |
| <b>Balance, end of year</b>                                  | <b><u>\$ 276,731</u></b>                 | <b><u>\$ 330,335</u></b>  |

The following table sets forth a summary of changes in the fair value of the Foundation's Level 3 assets for the year ended June 30, 2011:

|  | <b><u>Bond/Fixed<br/>Income Fund</u></b> | <b><u>Beneficial<br/>Interest in<br/>Charitable<br/>Remainder<br/>Trust</u></b> |
|--|--|---|
| Balance at beginning of year                                 | \$ 227,461                               | \$ 307,235  |
| Unrealized gains relating to investments<br>held at year end | 37,809                                   | -   |
| Change in value  | <u>-</u>                                 | <u>34,584</u>   |
| <b>Balance, end of year</b>                                  | <b><u>\$ 265,270</u></b>                 | <b><u>\$ 341,819</u></b>  |

### 5. ACCOUNTS AND STUDENT LOAN RECEIVABLES

Accounts receivable result primarily from student tuition and fee billings and auxiliary enterprise sales, such as food service and student residence. In addition, receivables arise from grant awards and financial aid. These receivables are reported net of an allowance for collection losses in the amount of \$323,524 and \$312,711 at June 30, 2012 and 2011, respectively.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

University accounts receivable consist of the following net amounts at June 30:

|                                   | <b>2012</b>         | <b>2011</b>         |
|-----------------------------------|---------------------|---------------------|
| Tuition and fees                  | \$ 671,190          | \$ 524,838          |
| Governmental grants and contracts | 352,302             | 580,605             |
| Auxiliary activities              | 228,514             | 196,453             |
| Other                             | 234,802             | 192,731             |
| Private grants and contracts      | 46,312              | 8,358               |
| <b>Accounts receivable, net</b>   | <b>\$ 1,533,120</b> | <b>\$ 1,502,985</b> |

In addition, the University has student loans receivable, in the amount of \$2,592,713 and \$2,762,746, which are recorded net of an allowance for uncollectible loans of \$451,509 and \$441,402 as of June 30, 2012 and 2011, respectively. Approximately 50% of student loans receivable are expected to be collected in periods beyond one year.

### 6. UNCONDITIONAL PROMISES TO GIVE

The following is a summary of unconditional promises to give for the Foundation as of June 30:

|  | <b>2012</b>      | <b>2011</b>      |
|--|------------------|------------------|
| Unconditional promises due in less than one year   | \$ 74,555        | \$ 12,340        |
| Unconditional promises due in one to five years, net of discount to net present value at 1% of \$1,725 and \$ -0-        | 63,610           | 12,000           |
| Unconditional promises due in more than five years, net of discount to net present value at 8% of \$27,574 and \$120,474 | 14,426           | 68,171           |
| Present value of promises to give  | 152,591          | 92,511           |
| Less allowance for uncollectible amounts   | 4,513            | 3,085            |
| <b>Net unconditional promises to give</b>  | <b>148,078</b>   | <b>89,426</b>    |
| Less current portion   | 70,042           | 12,340           |
| <b>Unconditional promises to give, net of current portion</b>  | <b>\$ 78,036</b> | <b>\$ 77,086</b> |

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

### 7. CHARITABLE REMAINDER TRUST

A donor having a charitable remainder unitrust managed by a third party named the Foundation as the remainder beneficiary. Under the terms of the split-interest agreement, the third party trustee must pay to the donor in each taxable year of the trust during the donor's life the lesser of the trust income for the taxable year or five percent (5%) of the net fair market value of the assets of the trust valued as of the first day of each taxable year of the trust. At the time of the donor's death, the trust is to terminate, and the remaining trust assets are to be distributed to the Foundation.

At June 30, 2012 and 2011, based on the donor's life expectancy and an assumed 5.8% discount rate, the present value of the future benefits expected to be received by the Foundation were estimated to be \$330,335 and \$341,819, respectively.

### 8. CAPITAL ASSETS

Changes in the components of capital assets are as follows for the years ended June 30:

|   | 2012                    |                       |                  | Balance<br>June 30, 2012 |
|---|-------------------------|-----------------------|------------------|--------------------------|
|   | Balance<br>July 1, 2011 | Additions             | Reductions       |                          |
| Capital assets not being depreciated        |                         |                       |                  |                          |
| Land - restricted                           | \$ 838,684              | \$ -                  | \$ -             | \$ 838,684               |
| Land  | 1,096,844               | -                     | -                | 1,096,844                |
| Art collection                              | 586,575                 | -                     | 9,578            | 576,997                  |
| Total capital assets not being depreciated  | 2,522,103               | -                     | 9,578            | 2,512,525                |
| Capital assets being depreciated            |                         |                       |                  |                          |
| Land improvements                           | 5,395,733               | 88,997                | -                | 5,484,730                |
| Infrastructure                              | 3,244,705               | -                     | -                | 3,244,705                |
| Building and building improvements          | 115,762,518             | 272,305               | -                | 116,034,823              |
| Equipment and other                         | 18,994,419              | 781,131               | 315,644          | 19,459,906               |
| Total capital assets being depreciated      | 143,397,375             | 1,142,433             | 315,644          | 144,224,164              |
| Accumulated depreciation                    | (91,629,437)            | (4,792,374)           | (305,902)        | (96,115,909)             |
| Total capital assets being depreciated, net | 51,767,938              | (3,649,941)           | 9,742            | 48,108,255               |
| <b>Total capital assets, net</b>            | <b>\$ 54,290,041</b>    | <b>\$ (3,649,941)</b> | <b>\$ 19,320</b> | <b>\$ 50,620,780</b>     |

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

|   | 2011                    |                       |                 | Balance<br>June 30, 2011 |
|---|-------------------------|-----------------------|-----------------|--------------------------|
|   | Balance<br>July 1, 2010 | Additions             | Reductions      |                          |
| Capital assets not being depreciated        |                         |                       |                 |                          |
| Land - restricted                           | \$ 838,684              | \$ -                  | \$ -            | \$ 838,684               |
| Land  | 1,096,844               | -                     | -               | 1,096,844                |
| Art collection                              | 586,575                 | -                     | -               | 586,575                  |
| Total capital assets not being depreciated  | 2,522,103               | -                     | -               | 2,522,103                |
| Capital assets being depreciated            |                         |                       |                 |                          |
| Land improvements                           | 5,395,733               | -                     | -               | 5,395,733                |
| Infrastructure                              | 3,244,705               | -                     | -               | 3,244,705                |
| Building and building improvements          | 114,994,842             | 767,676               | -               | 115,762,518              |
| Equipment and other                         | 18,566,667              | 567,233               | 139,481         | 18,994,419               |
| Total capital assets being depreciated      | 142,201,947             | 1,334,909             | 139,481         | 143,397,375              |
| Accumulated depreciation                    | (86,874,510)            | (4,892,209)           | (137,282)       | (91,629,437)             |
| Total capital assets being depreciated, net | 55,327,437              | (3,557,300)           | 2,199           | 51,767,938               |
| <b>Total capital assets, net</b>            | <b>\$ 57,849,540</b>    | <b>\$ (3,557,300)</b> | <b>\$ 2,199</b> | <b>\$ 54,290,041</b>     |

### 9. ACCOUNTS PAYABLE AND ACCRUED EXPENSES

University accounts payable and accrued expenses consist of the following liabilities at June 30:

|  | 2012                | 2011                |
|--|---------------------|---------------------|
| Accounts payable to vendors                        | \$ 839,415          | \$ 1,003,229        |
| Payroll and payroll taxes                          | 672,516             | 1,409,788           |
| Health insurance claims                            | 267,000             | 267,000             |
| Interest   | 257,562             | 159,046             |
| Workers' compensation claims                       | 160,000             | 80,000              |
| <b>Total accounts payable and accrued expenses</b> | <b>\$ 2,196,493</b> | <b>\$ 2,919,063</b> |

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

### Worker's Compensation

The University is self-insured for workers' compensation claims up to \$500,000 per claim. The accrued workers' compensation obligation represents claims made prior to June 30, 2012 and 2011, which remain unpaid at those dates. The University's third party administrator bases these amounts upon an analysis of workers' compensation claims, which includes historical incident rates and other related factors.

### 10. LONG-TERM DEBT

Changes in the components of long-term debt are as follows for the years ended June 30:

|   | Interest Rate | Maturity  | 2012                        |                             |                            |                             |                            |
|---|---------------|-----------|-----------------------------|-----------------------------|----------------------------|-----------------------------|----------------------------|
|   |               |           | July 1<br>2011              | Outstanding Principal       |                            | June 30<br>2012             | Current<br>Portion         |
|   |               |           |                             | Additions                   | Reductions                 |                             |                            |
| <b>Bonds payable</b>                          |               |           |                             |                             |                            |                             |                            |
| General Revenue                               |               |           |                             |                             |                            |                             |                            |
| Bonds, Series 2012                            |               |           |                             |                             |                            |                             |                            |
| Series bonds                                  | 2.0%-4.0%     | 2012-2031 | \$ -                        | \$ 23,355,000               | \$ -                       | \$ 23,355,000               | \$ 1,035,000               |
| General Revenue                               |               |           |                             |                             |                            |                             |                            |
| Bonds, Series 2001                            |               |           |                             |                             |                            |                             |                            |
| Series bonds                                  | 5.0%          | 2011-2016 | 2,555,000                   | -                           | 2,555,000                  | -                           | -                          |
| Term bonds                                    | 5.125%-5.5%   | 2018-2031 | 16,525,000                  | -                           | 16,525,000                 | -                           | -                          |
| General Revenue                               |               |           |                             |                             |                            |                             |                            |
| Bonds, Series 1997                            |               |           |                             |                             |                            |                             |                            |
| Term bonds                                    | 5.0%-5.125%   | 2012-2019 | 5,455,000                   | -                           | 5,455,000                  | -                           | -                          |
| Net premium on bond issuance                  |               |           | -                           | 516,827                     | -                          | 516,827                     | -                          |
| <b>Total – bonds payable</b>                  |               |           | <b>24,535,000</b>           | <b>23,871,827</b>           | <b>24,535,000</b>          | <b>23,871,827</b>           | <b>1,035,000</b>           |
| Capital leases                                | up to 5.24%   |           | 846,904                     | 345,304                     | 274,528                    | 917,680                     | 258,354                    |
| <b>Total – long-term debt</b>                 |               |           | <b><u>\$ 25,381,904</u></b> | <b><u>\$ 24,217,131</u></b> | <b><u>\$24,809,528</u></b> | <b>24,789,507</b>           | <b><u>\$ 1,293,354</u></b> |
| Less current portion                          |               |           |                             |                             |                            | 1,293,354                   |                            |
| <b>Long-term debt, net of current portion</b> |               |           |                             |                             |                            | <b><u>\$ 23,496,153</u></b> |                            |

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

|   |               | 2011                  |                             |                    |                            |                             |                            |
|---|---------------|-----------------------|-----------------------------|--------------------|----------------------------|-----------------------------|----------------------------|
|   |               | Outstanding Principal |                             |                    |                            |                             |                            |
| Bonds payable                                 | Interest Rate | Maturity              | July 1 2010                 | Additions          | Reductions                 | June 30 2011                | Current Portion            |
| General Revenue                               |               |                       |                             |                    |                            |                             |                            |
| Bonds, Series 2001                            |               |                       |                             |                    |                            |                             |                            |
| Series bonds                                  | 5.0%          | 2011-2016             | \$ 2,915,000                | \$ -               | \$ 360,000                 | \$ 2,555,000                | \$ 375,000                 |
| Term bonds                                    | 5.125%-5.5%   | 2018-2031             | 16,525,000                  | -                  | -                          | 16,525,000                  | -                          |
| General Revenue                               |               |                       |                             |                    |                            |                             |                            |
| Bonds, Series 1997                            |               |                       |                             |                    |                            |                             |                            |
| Term bonds                                    | 5.0%-5.125%   | 2012-2019             | <u>6,145,000</u>            | -                  | <u>690,000</u>             | <u>5,455,000</u>            | <u>725,000</u>             |
| <b>Total –bonds payable</b>                   |               |                       | <b>25,585,000</b>           | <b>-</b>           | <b>1,050,000</b>           | <b>24,535,000</b>           | <b>1,100,000</b>           |
| Capital leases                                | up to 7.0%    |                       | <u>1,155,146</u>            | -                  | <u>308,242</u>             | <u>846,904</u>              | <u>218,774</u>             |
| <b>Total – long-term debt</b>                 |               |                       | <b><u>\$ 26,740,146</u></b> | <b><u>\$ -</u></b> | <b><u>\$ 1,358,242</u></b> | <b>25,381,904</b>           | <b><u>\$ 1,318,774</u></b> |
| Less current portion                          |               |                       |                             |                    |                            | <u>1,318,774</u>            |                            |
| <b>Long-term debt, net of current portion</b> |               |                       |                             |                    |                            | <b><u>\$ 24,063,130</u></b> |                            |

### ***Bonded Debt***

#### **General Revenue Bonds, Series 2012**

In March, 2012, the University issued fixed rate General Revenue Bonds in the amount of \$23,355,000. As of June 30, 2012, serial bonds payable in the amount of \$23,355,000 are payable from general revenues, maturing in varying amounts through November 2031, with interest charged at annual rates ranging from 2.0% to 4.0%. All of the bonds are callable after November 15, 2021.

The University used the proceeds from above mentioned bond issue to currently refund \$4,670,000 and \$18,685,000 in outstanding fixed rate General Revenue Bonds, Series 1997 and 2001, respectively. As of June 30, 2012, the certificates are considered defeased and the liability has been removed from the statement of net assets. The refunding resulted in an interest savings of \$3,540,834 and a net present value savings of \$2,821,221.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

### Debt Service Requirements

Principal and interest on the bonds are payable only from certain general revenues. The following table summarizes debt service requirements by years of scheduled maturity:

| <u>Year<br/>Ending<br/>June 30</u> | <u>Principal</u>            | <u>Interest</u>            | <u>Total</u>                |
|------------------------------------|-----------------------------|----------------------------|-----------------------------|
| 2013                               | \$ 1,035,000                | \$ 928,989                 | \$ 1,963,989                |
| 2014                               | 1,220,000                   | 746,275                    | 1,966,275                   |
| 2015                               | 1,245,000                   | 721,625                    | 1,966,625                   |
| 2016                               | 1,270,000                   | 696,475                    | 1,966,475                   |
| 2017                               | 890,000                     | 674,875                    | 1,564,875                   |
| 2018-2022                          | 4,875,000                   | 2,933,062                  | 7,808,062                   |
| 2023-2027                          | 5,800,000                   | 1,974,875                  | 7,774,875                   |
| 2028-2032                          | <u>7,020,000</u>            | <u>724,600</u>             | <u>7,744,600</u>            |
| <b>Total – bonds payable</b>       | <b><u>\$ 23,355,000</u></b> | <b><u>\$ 9,400,776</u></b> | <b><u>\$ 32,755,776</u></b> |

### Interest Rate Swap

During the fiscal year ended June 30, 2012, the University terminated the twenty-six year forward-looking basis interest rate swap agreement (original amount of \$20,115,000, notional amount of \$19,080,000 at June 30, 2011), effective dated May 15, 2008, which was associated with the General Revenue Bonds of 2001. The termination was effective January 30, 2012 and payoff amount was \$1,061,000 which was paid with the original proceeds of the swap of \$839,000 plus interest and capital gains earned on the invested proceeds since May 2008.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

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### Obligations Under Capital Leases

The University leases certain equipment with a net book value of \$2,325,460 at June 30, 2012, under lease agreements which meet the capitalization criteria specified by generally accepted accounting principles.

The following is a schedule of annual future minimum lease payments required under capitalized leases obligations as of June 30, 2012:

| <b><u>Year<br/>Ending<br/>June 30</u></b>   | <b><u>Amount</u></b>     |
|---|--------------------------|
| 2013  | \$ 298,620               |
| 2014  | 288,443                  |
| 2015  | 318,832                  |
| 2016  | 76,073                   |
| 2017  | <u>15,127</u>            |
| Total minimum payments due  | 997,095                  |
| Less amounts representing interest,<br>imputed at annual rates ranging up<br>to 5.24% | <u>79,415</u>            |
| <b>Present value of net minimum<br/>lease payments</b>                                | <b><u>\$ 917,680</u></b> |

Commitments and related rental expenses under operating leases with initial or remaining non-cancelable lease terms in excess of one year as of and for the years ended June 30, 2012 and 2011, are insignificant.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

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### 11. EMPLOYEE RETIREMENT PLANS AND OTHER POSTEMPLOYMENT BENEFITS

#### Retirement Plans

The University provides noncontributory retirement plans for all qualified employees. In December 1995, the State enacted Public Act 272 of 1995 that precludes University employees hired after January 1, 1996, from participating in the Michigan Public School Employees Retirement System (MPERS). MPERS and the Teachers Insurance and Annuity Association - College Retirement Equities Fund (TIAA-CREF) were the two retirement plans offered by the University to its eligible employees. Employees currently covered under the MPERS plan will continue to remain in that plan. The University will contribute to MPERS the percentage mandated by state statute of their eligible wages.

Support personnel represented by the Michigan Education Association/National Education Association (MEA) hired after January 1, 1996, faculty and administrative employees are eligible for the TIAA-CREF plan. TIAA-CREF is a defined contribution plan where the University contributes an amount equal to 12.0 percent of administrative and faculty group employees' pay, and 10.0 percent of MEA employees' pay. The University contributed approximately \$1,566,000 and \$1,558,000 to this plan for the years ended June 30, 2012 and 2011, respectively. Plan participants maintain individual annuity contracts with TIAA-CREF, the plan administrator, which are fully vested.

Plan provisions and contribution requirements of the TIAA-CREF plan are established and may be amended by the University's Board of Trustees.

MPERS is a noncontributory cost-sharing multiple-employer defined benefit plan administered by the Michigan State Employees' Retirement System. The cost of the MPERS plan allocated to the University was approximately \$816,000, \$647,000 and \$577,000, for the years ended June 30, 2012, 2011 and 2010, respectively, all of which was contributed during the applicable year.

Beginning October 1, 2011 the University is required to contribute 3.21% of MPERS covered payroll for normal pension costs and 13.41% for unfunded pension liability. In addition, separately computed supplemental contributions will be required for retiree health care benefits. Future contribution requirements, which depend on the level of MPERS covered payroll, cannot be determined. Additional pension data for MPERS is contained in MPERS's comprehensive Annual Financial Report, which may be obtained by writing to the Office of Retirement Systems, 7150 Harris Dr., P. O. Box 30026, Lansing, MI 48901.

The University also contributes to the MPERS healthcare plan, a cost-sharing multiple-employer defined benefit postemployment healthcare plan administered by MPERS. This plan provides medical benefits to retired employees of participating universities. Participating universities are contractually required to make monthly contributions to the plan at amounts assessed each year by MPERS. The MPERS Board of Trustees sets the employer contributions based on the annual required contribution of the employers (ARC), an amount actuarially determined in accordance with the parameters of generally accepted accounting principles. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) of the plan over a period not to

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

exceed thirty years. The University's contributions to the MPSERS healthcare plan for the years ended June 30, 2012, 2011 and 2010, were approximately \$929,000, \$937,000 and \$849,000, respectively, which equaled the required contributions each year.

Benefit provisions and contribution requirements of MPSERS are established and may be amended by state statute.

### Compensated Absences

The University pays eligible employees for their unused accumulated vacation under various contracts, up to a maximum of 288 hours, upon termination of employment with the University.

### Accumulated Sick Leave Benefits

The University pays eligible employees for their unused accumulated sick leave under various contracts, up to a maximum of 800 hours, at retirement from the University, if the employee has met certain vesting and age requirements at that date. Employees in the Faculty and Administrative and Professional groups hired after June 30, 1987, and employees in the Support Staff group hired after December 31, 1989, are not eligible for participation in the program.

Activity in University employee benefit programs is summarized below for the years ended June 30:

|  | 2012                       |                          |                          |                            |                          |
|--|----------------------------|--------------------------|--------------------------|----------------------------|--------------------------|
|  | July 1<br>2011             | Additions                | Payments                 | June 30<br>2012            | Current<br>Portion       |
| Compensated absences                   | \$ 720,190                 | \$ 109,163               | \$ 65,189                | \$ 764,164                 | \$ 71,000                |
| Accumulated sick leave benefits        | 867,755                    | 142,000                  | 183,519                  | 826,236                    | 135,000                  |
| <b>Total employee benefit programs</b> | <b><u>\$ 1,587,945</u></b> | <b><u>\$ 251,163</u></b> | <b><u>\$ 248,708</u></b> | <b><u>\$ 1,590,400</u></b> | <b><u>\$ 206,000</u></b> |
|  | 2011                       |                          |                          |                            |                          |
|  | July 1<br>2010             | Additions                | Payments                 | June 30<br>2011            | Current<br>Portion       |
| Compensated absences                   | \$ 693,002                 | \$ 118,039               | \$ 90,851                | \$ 720,190                 | \$ 71,000                |
| Accumulated sick leave benefits        | 863,557                    | 142,000                  | 137,802                  | 867,755                    | 100,000                  |
| <b>Total employee benefit programs</b> | <b><u>\$ 1,556,559</u></b> | <b><u>\$ 260,039</u></b> | <b><u>\$ 228,653</u></b> | <b><u>\$ 1,587,945</u></b> | <b><u>\$ 171,000</u></b> |

### Other Post Employment Health Benefits

The University allows retirees who are not covered by the MPSERS healthcare plan to purchase healthcare benefits at cost and has 19 retirees participating in this health coverage at June 30, 2012. The University segregates these retiree payments and health care expenses separately from current employee costs. Premium rates are adjusted on July 1 each year to cover projected health care increases for the next year and any funding deficits. Rates are set by the University from a cost analysis through the University's third party health care administrators. Since retirees are required to pay all monthly premiums, there is no liability to the University, accordingly, no post employment health care liability has been recorded in the accompanying statements of net assets.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

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### 12. SELF INSURANCE

#### **Liability and Property**

The University participates with 10 other Michigan universities in the Michigan Universities Self-Insurance Corporation (“MUSIC”). MUSIC’s purpose is to provide indemnity to members against auto, comprehensive general liability, errors and omissions and property losses commonly covered by insurance. MUSIC also provides risk management and loss control services and programs.

Loss coverages are structured on a three-layer basis with each member retaining a portion of its losses, MUSIC covering the second layer of losses and commercial carriers covering the third layer. Comprehensive general liability coverage is provided on an occurrence basis; errors and omissions coverage is provided on a claims-made basis.

Premiums are assessed annually for (1) insurance risks retained by MUSIC, (2) costs related to excess coverage and (3) general and administrative expenses. The amount assessed reflects the claims experience of each University.

#### **Insurance Reserves**

The University provides coverage for up to a maximum of \$500,000 for each workers’ compensation claim and \$75,000 for each health insurance claim. The University purchases commercial insurance for workers’ compensation and health insurance claims in excess of coverage provided by the self insurance reserves. Settled claims have not exceeded this commercial coverage in any of the past three fiscal years.

The University reserves an amount within unrestricted net assets for health and maintenance reserves and records a liability for workers’ compensation insurance. These reserves are determined by MUSIC for losses relating to catastrophes and amounted to \$3,385,581 and \$3,057,650 at June 30, 2012 and 2011, respectively. The workers’ compensation claims liability of \$160,000 and \$80,000 at June 30, 2012 and 2011, respectively, which is included in accounts payable and accrued expenses, is based on the requirements of generally accepted accounting principles, which requires that a liability for claims be reported if information prior to the issuance of the financial statements indicates that it is probable that a liability has been incurred at the date of the financial statements and the amount of the loss can be reasonably estimated. Health insurance claims incurred but not reported at each June 30, 2012 and 2011, were \$267,000, and, accordingly, a related liability has been recorded in the accompanying statements of net assets.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

### 13. NET ASSET CATEGORIES - FOUNDATION

Unrestricted net assets (deficit) at June 30, consist of the following:

|  | <u>2012</u>              | <u>2011</u>              |
|--|--------------------------|--------------------------|
| Deficiencies for all donor-restricted endowment funds for which fair value of assets is less than donor-stipulated level | \$ (179)                 | \$ (365)                 |
| Board designated   | 198,545                  | 169,945                  |
| Undesignated   | <u>423,502</u>           | <u>358,095</u>           |
|  | <u><b>\$ 621,868</b></u> | <u><b>\$ 527,675</b></u> |

Temporarily restricted net assets at June 30, were restricted for the following:

|  | <u>2012</u>                | <u>2011</u>                |
|--|----------------------------|----------------------------|
| University programs                                  | \$ 1,510,375               | \$ 1,295,177               |
| Net appreciation on donor-restricted endowment funds | <u>1,320,570</u>           | <u>1,506,723</u>           |
|  | <u><b>\$ 2,830,945</b></u> | <u><b>\$ 2,801,900</b></u> |

Permanently restricted net assets at June 30, were restricted for the following:

|  | <u>2012</u>                | <u>2011</u>                |
|--|----------------------------|----------------------------|
| Remainder interests in split-interest agreements | \$ 330,335                 | \$ 341,819                 |
| Corpus of donor-restricted endowment funds       | <u>4,732,805</u>           | <u>4,384,171</u>           |
|  | <u><b>\$ 5,063,140</b></u> | <u><b>\$ 4,725,990</b></u> |

Permanently restricted net assets are held in perpetuity, the income from which supports scholarships and fellowships, faculty chairs, and other University programs.

### 14. FOUNDATION ENDOWMENT

The Foundation's endowment consists of individual funds, all of which are donor restricted, that have been established for a variety of purposes. As required by generally accepted accounting principles, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

### Interpretation of Relevant Law

The Foundation interprets the State of Michigan Prudent Management of Institutional Funds Act (SMPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Foundation classifies as nonexpendable restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument, if any, at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in nonexpendable restricted net assets is classified as expendable restricted net assets until those amounts are appropriated for expenditure by the Foundation in a manner consistent with the standard of prudence prescribed by SMPMIFA. In accordance with SMPMIFA, the Foundation considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. The duration and preservation of the fund
2. The purposes of the Foundation and the donor-restricted endowment fund
3. General economic conditions
4. The possible effect of inflation and deflation
5. The expected total return from income and the appreciation (depreciation) of investments
6. Other resources of the Foundation
7. The investment policies of the Foundation

Following is a summary of the changes in the endowment net assets for the years ended June 30:

|  | <b>2012</b>         |                     |                      |                     |
|--|---------------------|---------------------|----------------------|---------------------|
|  | <b>Unrestricted</b> | <b>Restricted</b>   |                      | <b>Total</b>        |
|  | <b>Unrestricted</b> | <b>Expendable</b>   | <b>Nonexpendable</b> | <b>Total</b>        |
| Investment return:   |                     |                     |                      |                     |
| Investment income  | \$ -                | \$ 128,437          | \$ -                 | \$ 128,437          |
| Net appreciation (depreciation)<br>(realized and unrealized) | 186                 | (73,060)            | -                    | (72,874)            |
| Net investment return  | 186                 | 55,377              | -                    | 55,563              |
| Contributions and other revenue                              | -                   | 435                 | 319,308              | 319,743             |
| Change in value  | -                   | (434)               | (8,128)              | (8,562)             |
| Appropriation of endowment assets<br>for expenditure         | -                   | (215,561)           | -                    | (215,561)           |
| Transfer based on donor<br>specification                     | -                   | (25,970)            | 25,970               | -                   |
| <b>Changes to endowment net assets</b>                       | <b>186</b>          | <b>(186,153)</b>    | <b>311,180</b>       | <b>151,183</b>      |
| Endowment net assets:  |                     |                     |                      |                     |
| Beginning of year  | (365)               | 1,506,723           | 4,725,990            | 6,232,348           |
| <b>End of year</b>   | <b>\$ (179)</b>     | <b>\$ 1,320,570</b> | <b>\$ 5,063,140</b>  | <b>\$ 6,383,531</b> |

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

|   | 2011            |                     |                     |                     |
|---|-----------------|---------------------|---------------------|---------------------|
|   | Unrestricted    | Restricted          |                     | Total               |
|   |                 | Expendable          | Nonexpendable       |                     |
| Investment return:                                |                 |                     |                     |                     |
| Investment income                                 | \$ -            | \$ 175,224          | \$ -                | \$ 175,224          |
| Net appreciation (realized and unrealized)        | 26,602          | 932,660             | -                   | 959,262             |
| Net investment income                             | 26,602          | 1,107,884           | -                   | 1,134,486           |
| Contributions and other revenue                   | -               | 10,657              | 321,303             | 331,960             |
| Change in value                                   | -               | 9,343               | 36,298              | 45,641              |
| Appropriation of endowment assets for expenditure | -               | (197,202)           | -                   | (197,202)           |
| <b>Changes to endowment net assets</b>            | <b>26,602</b>   | <b>930,682</b>      | <b>357,601</b>      | <b>1,314,885</b>    |
| Endowment net assets:                             |                 |                     |                     |                     |
| Beginning of year                                 | (26,967)        | 576,041             | 4,368,389           | 4,917,463           |
| <b>End of year</b>                                | <b>\$ (365)</b> | <b>\$ 1,506,723</b> | <b>\$ 4,725,990</b> | <b>\$ 6,232,348</b> |

### *Return Objectives and Risk Parameters*

The Foundation has adopted investment policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by the endowment while seeking to maintain the purchasing power of the endowment assets, which includes those assets of donor-restricted funds that must be held in perpetuity. Under this policy, the endowment assets are invested in a manner that is intended to produce results that meet or exceed the price and yield results of established indexes for differing investment classes while assuming a moderate level of investment risk. The Foundation expects its endowment funds, over time, to provide an average rate of return of 8.0% annually. Actual returns in any given year may vary from this range.

### *Strategies Employed for Achieving Objectives*

To satisfy its long-term rate-of-return objectives, the Foundation relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Foundation targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve long-term return objectives within prudent risk constraints.

### *Spending Policy and How the Investment Objectives Relate to Spending Policy*

The Foundation has an annual spending policy of 4.5% of its endowment funds' average fair value over the prior 20 quarters through the calendar year-end preceding the fiscal year in which the distribution is planned. In establishing this policy, the Foundation considered the long-term expected return of its endowment. Accordingly, over the long-term, the Foundation expects its current spending policy to allow its endowment to grow at an average of 3.0% to 3.5% annually. This is consistent with the Foundation's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

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### 15. CONTINGENCIES AND COMMITMENTS

#### Union Contracts

The University has three groups of employees, two of which are covered under union collective bargaining agreements. The collective bargaining agreement covering the Support Personnel under the United Steelworkers Local 9997 had expired and the Support Personnel reorganized under the Michigan Education Association/National Education Association (MEA). Their new agreement was ratified effective April 27, 2012. The Faculty Association contract was ratified effective November 12, 2010. The employee groups covered and the expiration of the contracts are as follows:

| <u>Employee Group</u>              | <u>Union Name</u>   | <u>Contract Expired/Expires</u> |
|------------------------------------|---|---------------------------------|
| Support Personnel                  | Michigan Education Association/<br>National Education Association | September 30, 2014              |
| Faculty                            | Michigan Education Association/<br>National Education Association | August 31, 2013                 |
| Administrative and<br>Professional | N/A   | N/A                             |

#### Legal Matters

In the normal course of its activities, the University is a party to various legal and administrative actions. Although some actions have been brought for substantial amounts, the University has not experienced significant losses or costs. After taking into consideration legal counsel's evaluation of pending actions and information relative to potential future claims based on past events, University management is of the opinion that the outcome thereof will not have a material effect on the financial statements.

#### MPSERS Unfunded Liability

Certain employees of the University are covered under the MPSERS retirement plan. As of June 30, 2012 and 2011, the unfunded portion of the related pension benefits is significant. The University's portion of this obligation is not determinable at June 30, 2012 or 2011. While the University has continued to pay the required monthly payments as determined by MPSERS, it is management's position that the University is not responsible for any shortfall in the fund as a result of changes in benefits made by MPSERS.

# LAKE SUPERIOR STATE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS

### 16. NATURAL CLASSIFICATION OF EXPENSES

Operating expenses by natural classification for the University are summarized as follows for the years ended June 30:

2012

|                                 | Salaries,<br>Wages and<br>Benefits | Supplies<br>and<br>Equipment | Utilities           | Scholarship<br>Expenses | Depreciation        | Other             | Total                |
|---------------------------------|------------------------------------|------------------------------|---------------------|-------------------------|---------------------|-------------------|----------------------|
| Instruction                     | \$ 12,167,240                      | \$ 1,218,430                 | \$ --               | \$ --                   | \$ --               | \$ --             | \$ 13,385,670        |
| Research                        | 257,946                            | 138,074                      | --                  | --                      | --                  | --                | 396,020              |
| Public service                  | 475,427                            | 578,130                      | --                  | --                      | --                  | --                | 1,053,557            |
| Academic support                | 2,129,273                          | 838,854                      | --                  | --                      | --                  | --                | 2,968,127            |
| Student services                | 2,207,102                          | 512,259                      | --                  | --                      | --                  | --                | 2,719,361            |
| Student aid                     | --                                 | --                           | --                  | 2,514,045               | --                  | --                | 2,514,045            |
| Institutional support           | 3,598,574                          | 1,826,379                    | --                  | --                      | --                  | --                | 5,424,953            |
| Plant operations                | 2,565,636                          | 830,212                      | 1,639,994           | --                      | --                  | --                | 5,035,842            |
| Auxiliary activities            | 3,944,018                          | 3,859,662                    | 1,036,595           | --                      | --                  | --                | 8,840,275            |
| Depreciation                    | --                                 | --                           | --                  | --                      | 4,792,374           | --                | 4,792,374            |
| Other                           | --                                 | --                           | --                  | --                      | --                  | 670,954           | 670,954              |
| <b>Total operating expenses</b> | <b>\$ 27,345,216</b>               | <b>\$ 9,802,000</b>          | <b>\$ 2,676,589</b> | <b>\$ 2,514,045</b>     | <b>\$ 4,792,374</b> | <b>\$ 670,954</b> | <b>\$ 47,801,178</b> |

2011

|                                 | Salaries,<br>Wages and<br>Benefits | Supplies<br>and<br>Equipment | Utilities           | Scholarship<br>Expenses | Depreciation        | Other             | Total                |
|---------------------------------|------------------------------------|------------------------------|---------------------|-------------------------|---------------------|-------------------|----------------------|
| Instruction                     | \$ 12,283,229                      | \$ 1,140,284                 | \$ --               | \$ --                   | \$ --               | \$ --             | \$ 13,423,513        |
| Research                        | 246,843                            | 122,171                      | --                  | --                      | --                  | --                | 369,014              |
| Public service                  | 472,405                            | 494,349                      | --                  | --                      | --                  | --                | 966,754              |
| Academic support                | 2,403,492                          | 665,250                      | --                  | --                      | --                  | --                | 3,068,742            |
| Student services                | 2,243,762                          | 493,102                      | --                  | --                      | --                  | --                | 2,736,864            |
| Student aid                     | --                                 | --                           | --                  | 2,675,056               | --                  | --                | 2,675,056            |
| Institutional support           | 3,757,992                          | 1,748,200                    | --                  | --                      | --                  | --                | 5,506,192            |
| Plant operations                | 2,499,619                          | 772,206                      | 1,649,362           | --                      | --                  | --                | 4,921,187            |
| Auxiliary activities            | 3,893,422                          | 3,733,714                    | 1,007,184           | --                      | --                  | --                | 8,634,320            |
| Depreciation                    | --                                 | --                           | --                  | --                      | 4,892,209           | --                | 4,892,209            |
| Other                           | --                                 | --                           | --                  | --                      | --                  | 446,667           | 446,667              |
| <b>Total operating expenses</b> | <b>\$ 27,800,764</b>               | <b>\$ 9,169,276</b>          | <b>\$ 2,656,546</b> | <b>\$ 2,675,056</b>     | <b>\$ 4,892,209</b> | <b>\$ 446,667</b> | <b>\$ 47,640,518</b> |

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