



CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Financial Statements

June 30, 2008 and 2007

(With Independent Auditors' Report Thereon)

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

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KPMG LLP
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Independent Auditors' Report

Dr. Karen Haynes
President
California State University, San Marcos:

We have audited the accompanying financial statements of California State University, San Marcos (the University), an agency of the State of California, and its aggregate discretely presented component units as of and for the years ended June 30, 2008 and 2007, 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 upon our audits. We did not audit the financial statements of the aggregate discretely presented component units. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinions, insofar as they relate to the amounts included for the aggregate discretely presented component units, are based solely on the reports of the other auditors.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the reports of other auditors provide a reasonable basis for our opinions.

As discussed in note 2, the financial statements of the University, an agency of the State of California, are intended to present the statements of net assets, statements of revenues, expenses, and changes in net assets, and statements of cash flows of only that portion of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State of California that is attributable to the transactions of the University. They do not purport to, and do not, present fairly the financial position of the State of California as of June 30, 2008 and 2007, the changes in their financial position and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

In our opinion, based on our audits and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the California State University, San Marcos and of its aggregate discretely presented component units as of June 30, 2008 and 2007, and the respective changes in financial position and, where applicable, cash flows thereof, for the years then ended in conformity with U.S. generally accepted accounting principles.

As discussed in notes 2 and 12 to the financial statements, effective July 1, 2007, the University adopted Governmental Accounting Standards Board (GASB) Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, in accounting for its postretirement healthcare costs.

Management's discussion and analysis on pages 3 through 16 is not a required part of the basic financial statements but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

March 17, 2009

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis

June 30, 2008 and 2007

This section of California State University, San Marcos (the University) annual financial report presents our discussion and analysis of the financial performance of the University for fiscal years ended June 30, 2008 and 2007. This discussion has been prepared by management and should be read in conjunction with the financial statements and notes.

Introduction to the Financial Statements

This annual report consists of a series of financial statements prepared in accordance with the Governmental Accounting Standards Board (GASB) Statements No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, No. 35, *Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities*, No. 37, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments: Omnibus*, and No. 38, *Certain Financial Statement Note Disclosures*. For reporting purposes, the University is considered a special-purpose government engaged only in business-type activities, which best represents the activities of the University.

The financial statements include the statement of net assets; the statement of revenues, expenses, and changes in net assets; and the statement of cash flows. These statements are supported by the notes to the financial statements and this section. All sections must be considered together to obtain a complete understanding of the financial picture of the University.

Statement of Net Assets – The statement of net assets includes all assets and liabilities. Assets and liabilities are reported at their book value, on an accrual basis, as of the statement date. It also identifies major categories of restrictions on the net assets of the University.

Statement of Revenues, Expenses, and Changes in Net Assets – The statement of revenues, expenses, and changes in net assets presents the revenues earned and expenses incurred during the year on an accrual basis.

Statement of Cash Flows – The statement of cash flows presents the inflows and outflows of cash for the year and is summarized by operating, noncapital financing, capital and related financing, and investing activities. The statement is prepared using the direct method of cash flows and, therefore, presents gross rather than net amounts for the year's activities.

The statement of cash flows for the discretely presented auxiliary organizations is not included in the University's financial statements.

Analytical Overview

Summary

The following discussion highlights management's understanding of the key financial aspects of the University's financial activities as of and for the years ended June 30, 2008 and 2007. Included is a comparative analysis of current year and prior year activities and balances; a discussion of the restrictions of University net assets; a discussion of capital assets and long-term debt; and factors impacting future reporting periods.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis

June 30, 2008 and 2007

The University's condensed summary of net assets as of June 30, 2008, 2007, and 2006 is as follows:

Condensed Summary of Net Assets

	June 30		
	2008	2007	2006
Assets:			
Current assets	\$ 29,801,581	31,800,643	26,730,357
Capital assets	171,710,197	172,000,458	169,471,459
Other noncurrent assets	91,430,166	27,931,784	36,977,448
Total assets	292,941,944	231,732,885	233,179,264
Liabilities:			
Current liabilities	20,144,307	18,247,622	14,094,304
Long-term debt obligations, net of current portion	40,800,119	33,100,434	32,730,963
Other noncurrent liabilities	3,081,919	2,759,408	2,532,370
Total liabilities	64,026,345	54,107,464	49,357,637
Net assets:			
Invested in capital assets, net of related debt	161,404,962	164,089,064	162,692,393
Restricted, expendable	55,094,473	1,366,841	8,784,354
Unrestricted	12,416,164	12,169,516	12,344,880
Total net assets	\$ 228,915,599	177,625,421	183,821,627

As of June 30, 2008

Assets

Total assets increased \$61.2 million from prior year due to a \$2.0 million decrease in current assets and a \$0.3 million decrease in capital assets, offset by a \$63.5 million increase in other noncurrent assets. Total current assets decreased \$2.0 million primarily due to a \$1.6 million decrease in prepaid assets due to a reduction in the prepaid for the University's portion of the CSU Risk Management Insurance program.

The \$0.3 million decrease in capital assets is due to \$9.7 million of current year additions from ongoing capital projects, primarily due to the University's Energy Conservation Project, The McMahon House, and the Social and Behavioral Science Building. These additions are offset by \$10.0 million in current year depreciation expense. Capital expansion is financed through the University's funds, issuance of debt, and general obligation bonds of the State of California and the California State University System, which are not reflected in the accompanying financial statements.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis

June 30, 2008 and 2007

Other noncurrent assets increased \$63.5 million primarily due to an \$11.0 million increase in other long-term investments, representing unspent construction funds for the McMahon House and Energy Conservation projects, and a \$52.7 million increase in accounts receivable, noncurrent, for unspent capital state appropriations for the Social and Behavioral Science Building.

Liabilities

Total liabilities increased \$9.9 million from prior year due to a \$1.9 million increase in current liabilities and a \$7.7 million increase in long-term debt obligations, net of current portion, and a \$0.3 million increase in other noncurrent liabilities. Total current liabilities increased \$1.9 million primarily due to a \$0.8 million increase in accounts payable primarily associated with the construction work in progress for the Energy Conversation project and a \$1.3 million increase in accrued salaries and benefits expense. These increases were partially offset by a \$0.7 million decrease in deferred revenue due to registration and payment period being one week less in the current year than prior year combined with decrease in headcount for the respective summer terms.

Total long-term debt obligations, net of current portion, increased \$7.7 million primarily due to a \$2.5 million increase in capital leases for the development and implementation of the PeopleSoft CMS Student Module, the University's computer refresh program, and a \$7.8 million increase in long term debt for the University's Energy Conservation project. These increases are offset by a \$2.5 million decrease in the University's debt.

Net Assets

Total net assets increased \$51.3 million from the prior year. A significant portion, \$161.4 million, of net assets at the end of the year is invested in capital assets, net of related debt. Restricted net assets totaling \$55.1 million of net assets at the end of the year is restricted for scholarships and fellowships, loans, capital projects, debt service, and sponsored programs, which increased \$53.7 million from prior year as discussed below. Unrestricted net assets totaled \$12.4 million at the end of the year. Unrestricted net assets represent all other net resources available to the University for general and educational obligations.

As of June 30, 2007

Assets

The \$1.4 million decrease in total assets is primarily due to a \$9.0 million decrease in state appropriations receivable used to complete capital projects combined with a \$1.0 million decrease in prepaid assets due to a reduction in the prepaid for the University's portion of the CSU Risk Management Insurance program. These are offset by a \$7.6 million increase in cash and investments.

The \$2.5 million increase in capital assets is due to \$12.0 million in additions from ongoing capital projects, primarily due to the completion of the Craven Hall renovations and the completion of Parking Lot F. These additions are offset by \$9.4 million in depreciation. Capital expansion is financed through University funds, issuance of debt, and general obligation bonds of the State of California and the California State University System, which are not reflected in the accompanying financial statements.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis

June 30, 2008 and 2007

Liabilities

The \$4.8 million increase in total liabilities from the prior year is primarily due to a \$1.8 million increase in accounts payable, a \$1.2 million increase in capital leases for the development of the PeopleSoft CMS Student Module, a \$1.6 million increase in long-term debt for the University's computer refresh program, a \$0.7 million increase in accrued salaries and benefits, and \$0.6 million increase in deferred revenue. These increases are offset by a \$1.7 million decrease in the University's debt.

Net Assets

The reduction in net assets of \$6.2 million from the prior year is primarily related to an increase of \$5.2 million in general fund state appropriations, a \$3.3 million increase in tuition revenue due to increased tuition costs combined with increased enrollment. These revenues were offset by a \$9.4 million increase in salaries and benefit costs due to increased staff and faculty combined with increased costs for benefits, a \$1.1 million increase in scholarship expense, and a \$0.7 million increase in depreciation and amortization expense.

Restricted Resources

Net assets of the University include funds that are restricted by donor or law. The following table summarizes which funds are restricted, the type of restriction, and the amount:

Restricted Net Assets

	June 30		
	2008	2007	2006
Expendable:			
Scholarships and fellowships	\$ 20,801	150,740	157,319
Loans	53,345	54,541	53,559
Capital projects	54,737,963	1,161,560	8,573,476
Other	282,364	—	—
Total restricted net assets – expendable	<u>\$ 55,094,473</u>	<u>1,366,841</u>	<u>8,784,354</u>

As of June 30, 2008

The \$53.7 million increase in restricted net assets – expendable is primarily due to a \$54.7 million increase in capital state appropriations revenue received in fiscal year 2008.

As of June 30, 2007

The \$7.4 million decrease in restricted net assets – expendable is primarily due to capital projects that were completed and transferred to capital assets during fiscal year 2007.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis

June 30, 2008 and 2007

The University's condensed summary of revenues, expenses, and changes in net assets for the years ended June 30, 2008, 2007, and 2006 is as follows:

Condensed Summary of Revenues, Expenses, and Changes in Net Assets

	Year ended June 30		
	2008	2007	2006
Operating revenues:			
Student tuition and fees, net	\$ 28,372,626	26,194,782	22,867,810
Grants and contracts, noncapital	835,561	370,006	539,955
Sales and services of auxiliary enterprises, net	3,975,336	3,910,557	2,886,925
Other operating revenues	1,165,736	970,934	790,347
Total operating revenues	34,349,259	31,446,279	27,085,037
Operating expenses	122,681,738	110,680,605	100,198,743
Operating loss	(88,332,479)	(79,234,326)	(73,113,706)
Nonoperating revenues (expenses):			
State appropriations, noncapital	67,071,786	59,921,313	54,723,975
Federal financial aid grants, noncapital	6,838,776	5,928,883	4,869,843
State and local financial aid grants, noncapital	2,863,849	2,390,997	2,066,439
Investment income, net	2,637,243	2,628,340	1,918,433
Other nonoperating revenues (expenses), net	986,575	304,090	(416,754)
Total nonoperating revenues	80,398,229	71,173,623	63,161,936
Loss before other additions	(7,934,250)	(8,060,703)	(9,951,770)
State appropriations, capital	56,087,000	1,349,000	767,000
Grants and gifts, capital	3,137,428	515,497	865,633
Increase (decrease) in net assets	51,290,178	(6,196,206)	(8,319,137)
Beginning net assets	177,625,421	183,821,627	192,140,764
Ending net assets	\$ 228,915,599	177,625,421	183,821,627

Certain reclassifications have been made to the 2007 and 2006 condensed financial information to conform to the 2008 financial information presented. The changes were primarily related to the classification of certain financial aids grant revenues from operating revenues to nonoperating revenues. There was no impact on the previously reported changes in net assets or total net assets of the University.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis

June 30, 2008 and 2007

Operating Revenues and Expenses

Operating revenues and expenses come from sources that are connected directly to the University's primary business function. These include revenues from categories such as tuition and fees, certain grants and contracts that will be used for noncapital purposes, and sales and services of auxiliary enterprises. Expenses include categories such as salaries, benefits, supplies and other services, scholarships and fellowships, and depreciation and amortization. In this discussion and analysis, expenses are reported by functional program such as instruction, research, public service, academic support, student services, institutional support, operation and maintenance of plant, student grants and scholarships, auxiliary enterprise expenses, and depreciation and amortization.

Operating Revenues

Year ended June 30, 2008

The University recognized \$34.3 million in operating revenues during this fiscal year, as compared to \$31.4 million in the prior year. This comprised 29.9% of total revenues for the year ended June 30, 2008, compared to 30.1% of total revenues for the year ended June 30, 2007. Although the state university fee did not change from the prior year, student tuition and fees, net, increased \$2.2 million (8.3%) from prior year primarily due to increased full-time equivalent students. Grants and contracts, noncapital, increased \$0.4 million from the prior year primarily due to new state grants and contracts in the current year related to Extended Learning Commission Project Operations. Sales and services of auxiliary enterprises, net, remained consistent increasing by \$0.1 million from \$3.9 million in 2007 to \$4.0 million in 2008.

Year ended June 30, 2007

The University recognized \$31.4 million in operating revenues during this fiscal year, as compared to \$27.1 million in the prior year. This comprised 30.1% of total revenues for the year ended June 30, 2007, compared to 29.5% of total revenues for the year ended June 30, 2006. Sales and services of auxiliary enterprises increased primarily due to an increase in student parking fees by \$1.0 million from \$2.9 million to \$3.9 million for the fiscal years ended June 30, 2006 and 2007, respectively. Student fees were increased again by the California State University (CSU) board of trustees in 2007. Student fee revenue increased by \$3.3 million, from \$22.9 million in 2006 to \$26.2 million in 2007.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis

June 30, 2008 and 2007

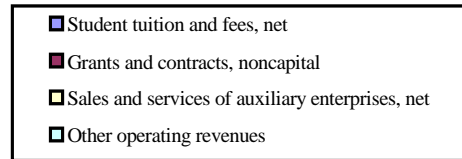
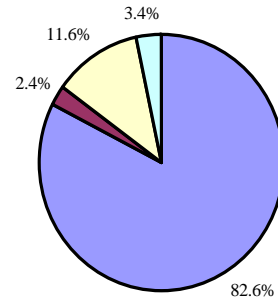
The following charts present the proportional share that each category of operating revenues contributed to the total for fiscal years 2008, 2007, and 2006:

Operating Revenues

Year ended June 30, 2008

(In thousands)

Student tuition and fees, net	\$ 28,373	82.6%
Grants and contracts, net	836	2.4
Sales and services of auxiliary enterprises, net	3,975	11.6
Other operating revenues	<u>1,165</u>	<u>3.4</u>
Total operating revenues	\$ <u><u>34,349</u></u>	<u><u>100.0%</u></u>

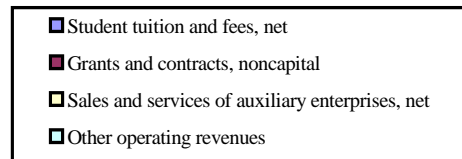
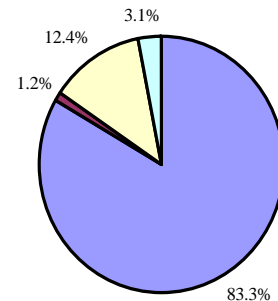


Operating Revenues

Year ended June 30, 2007

(In thousands)

Student tuition and fees, net	\$ 26,195	83.3%
Grants and contracts, net	370	1.2
Sales and services of auxiliary enterprises, net	3,910	12.4
Other operating revenues	<u>971</u>	<u>3.1</u>
Total operating revenues	\$ <u><u>31,446</u></u>	<u><u>100.0%</u></u>



CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis

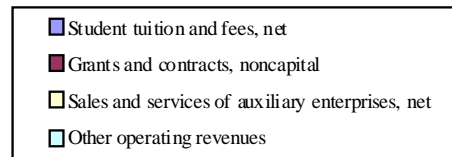
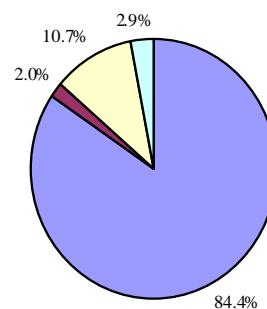
June 30, 2008 and 2007

Operating Revenues

Year ended June 30, 2006

(In thousands)

Student tuition and fees, net	\$ 22,868	84.4%
Grants and contracts, net	540	2.0
Sales and services of auxiliary enterprises, net	2,887	10.7
Other operating revenues	790	2.9
Total operating revenues	\$ 27,085	100.0%



Operating Expenses

Year ended June 30, 2008

The University's operating expenses consist of salaries and fringe benefits of \$81.3 million, supplies and services of \$19.5 million, scholarships and fellowships of \$11.8 million, and depreciation of \$10.1 million. Total operating expenses, excluding depreciation, increased by \$11.4 million, or 12.4%, primarily due to a \$4.6 million increase in instruction due to an increase in salaries and benefits expense and faculty headcount; a \$4.0 million increase in institutional support due to salaries and benefits costs as well as an increase in supplies and services. Salaries and benefits costs increased by \$9.1 million due to salary rate increases and health and retirement benefit increases for all employees as well as an increase in the number of faculty members. The University contribution to the California Employees' Retirement System (CalPERS) alone increased by \$0.8 million, or 10.0%. Student grants and scholarships increased by \$1.4 million. The percentage of students receiving aid increased from 44.0% in 2007 to 50.0% in 2008. The increase in depreciation expense of \$0.6 million relates to current year capital asset additions.

Year ended June 30, 2007

The University's operating expenses consist of salaries and fringe benefits of \$72.3 million, supplies and services of \$18.7 million, scholarships and fellowships of \$10.4 million, and depreciation of \$9.4 million. Total operating expenses, excluding depreciation, increased by \$9.8 million, or 10.7%, primarily due to grants and scholarships, academic support, and student services. Salaries and benefits costs increased by \$9.4 million due to salary rate increases and health and retirement benefit increases for all employees as well as an increase in faculty. The University contribution to CalPERS alone increased by \$1.3 million, or 20.0%. Student grants and scholarships increased by \$1.1 million. The percentage of students receiving aid increased from 43.0% in 2006 to 44.0% in 2007 while enrollment increased by 11.0%. The increase in depreciation expense of \$0.7 million relates to current year capital asset additions.

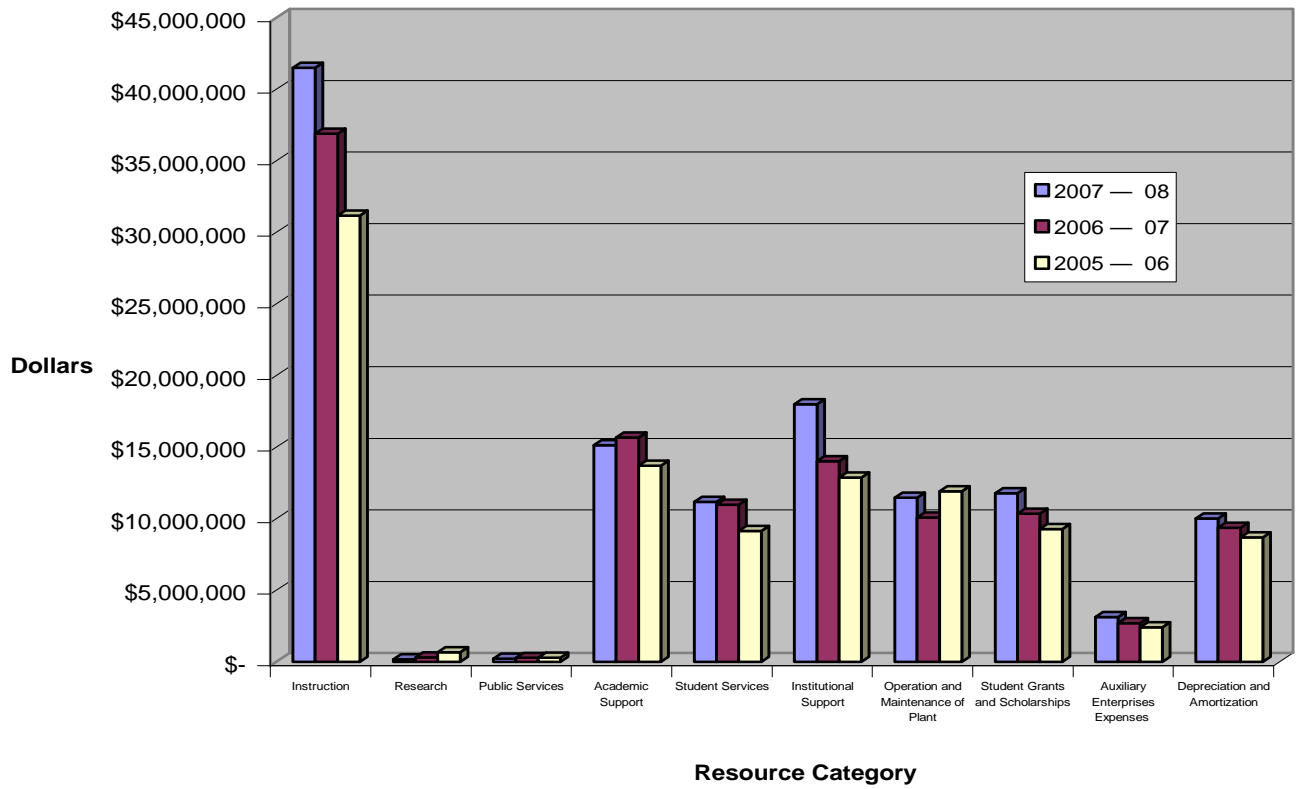
CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis

June 30, 2008 and 2007

The following chart presents the distribution of resources in support of the University's mission for fiscal years 2008, 2007, and 2006:

Comparative Distribution of Resources for Fiscal Years 2008, 2007, and 2006



CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis

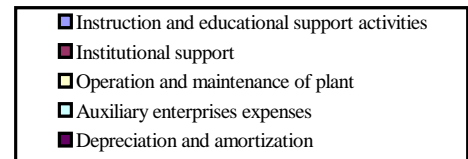
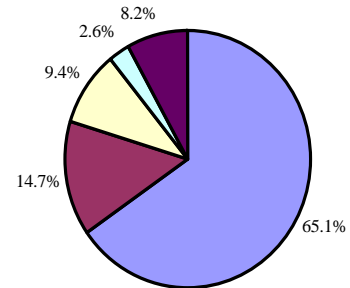
June 30, 2008 and 2007

The following charts present the distribution of resources in support of the University's mission for fiscal years 2008, 2007, and 2006:

Operating Expenses

Year ended June 30, 2008

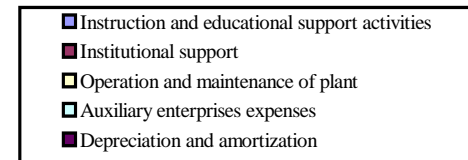
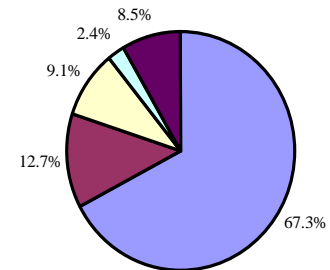
Instruction	\$ 41,512	33.8%
Research	176	0.1
Public service	224	0.2
Academic support	15,140	12.3
Student services	11,190	9.1
Student grants and scholarships	<u>11,791</u>	<u>9.6</u>
Total instruction and educational support activities	80,033	65.1
Institutional support	18,003	14.7
Operation and maintenance of plant	11,480	9.4
Auxiliary enterprises expenses	3,144	2.6
Depreciation and amortization	<u>10,022</u>	<u>8.2</u>
Total operating expenses	\$ <u>122,682</u>	<u>100.0%</u>



Operating Expenses

Year ended June 30, 2007

Instruction	\$ 36,879	33.2%
Research	315	0.3
Public service	283	0.3
Academic support	15,678	14.2
Student services	10,973	9.9
Student grants and scholarships	<u>10,364</u>	<u>9.4</u>
Total instruction and educational support activities	74,492	67.3
Institutional support	14,030	12.7
Operation and maintenance of plant	10,085	9.1
Auxiliary enterprises expenses	2,700	2.4
Depreciation and amortization	<u>9,374</u>	<u>8.5</u>
Total operating expenses	\$ <u>110,681</u>	<u>100.0%</u>



CALIFORNIA STATE UNIVERSITY, SAN MARCOS

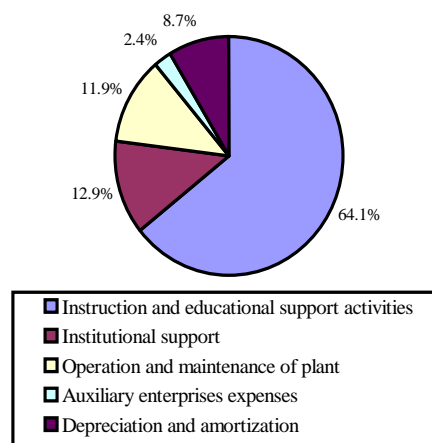
Management's Discussion and Analysis

June 30, 2008 and 2007

Operating Expenses

Year ended June 30, 2006

Instruction	\$ 31,180	31.0%
Research	670	0.7
Public service	299	0.3
Academic support	13,704	13.7
Student services	9,152	9.1
Student grants and scholarships	9,279	9.3
Total instruction and educational support activities	64,284	64.1
Institutional support	12,878	12.9
Operation and maintenance of plant	11,915	11.9
Auxiliary enterprises expenses	2,426	2.4
Depreciation and amortization	8,696	8.7
Total operating expenses	\$ 100,199	100.0%



Nonoperating Revenues (Expenses)

Nonoperating revenues (expenses) come from sources that are not part of the University's primary business functions. Included in this classification are categories such as state appropriations, certain financial aid grants, noncapital, grants and gifts, capital, investment income, and interest on capital-related debt.

Year ended June 30, 2008

As the University is part of the California State University System, which is an agency of the State of California, the University's operations are funded primarily from appropriations of state tax revenues. Appropriations used for purposes of acquisition of capital assets totaled \$56.1 million for the fiscal year ended June 30, 2008, up from \$1.4 million for the fiscal year ended June 30, 2007. Capital state appropriations in the current year included one-time appropriations of \$53.7 million for the construction of the Social and Behavioral Science Building and \$1.7 million for the nursing facility improvements and \$0.7 million in other minor capital projects. General (noncapital) appropriation revenues totaled \$67.1 million, an increase of \$7.2 million from the prior year due to increased operating costs as a result of an increase in enrollment and programs.

Year ended June 30, 2007

Appropriations used for purposes of acquisition of capital assets totaled \$1.4 million for the fiscal year ended June 30, 2007, an increase of \$0.6 million from \$0.8 million for the fiscal year ended June 30, 2006. General (noncapital) appropriation revenues totaled \$59.9 million, an increase of \$5.2 million from \$54.7 million for the fiscal year ended June 30, 2006.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis

June 30, 2008 and 2007

Capital Assets and Long-Term Debt Obligations

Capital Assets

Capital assets, net of accumulated depreciation, are shown below:

	June 30		
	2008	2007	2006
Land and land improvements	\$ 10,981,328	10,981,328	10,981,328
Works of art and historical treasures	25,000	25,000	25,000
Buildings and building improvements	124,093,602	129,530,456	127,104,513
Improvements, other than buildings	4,789,763	5,649,585	2,846,281
Infrastructure	15,246,990	15,495,738	13,909,444
Personal property	5,587,304	6,352,541	7,256,097
Intangible assets	2,447,210	1,165,625	801,422
Construction work in progress (CWIP)	8,539,000	2,800,185	6,547,374
Total capital assets, net of accumulated depreciation	\$ <u>171,710,197</u>	<u>172,000,458</u>	<u>169,471,459</u>

As of June 30, 2008

At June 30, 2008 and 2007, the University had \$171.7 million and \$172.0 million, respectively, in capital assets, net of accumulated depreciation of \$85.9 million and \$76.8 million, respectively. Depreciation expense totaled \$10.0 million and \$9.4 million for the years ended June 30, 2008 and 2007, respectively.

Capital assets decreased \$0.3 million primarily due to \$9.7 million of current year additions, which were offset by \$10.0 million in current year depreciation expense. The \$9.7 million in current year additions is primarily due to an increase in construction work in progress. The increase in CWIP is due to a \$1.4 million increase for the Social and Behavioral Science Building, \$1.5 million for the McMahon House, and \$2.4 million in the University's Energy Conservation Project. These projects were funded through private donations, capital state appropriations, and debt financing.

Capital assets commitments at June 30, 2008 totaled \$6.8 million.

As of June 30, 2007

At June 30, 2007 and 2006, the University had \$172.0 million and \$169.5 million, respectively, in capital assets, net of accumulated depreciation of \$76.8 million and \$71.2 million, respectively. Depreciation expense totaled \$9.4 million and \$8.7 million for the years ended June 30, 2007 and 2006, respectively.

The University completed three major capital projects during the year. The projects were the renovation of Craven Hall, which totaled \$6.6 million and was funded through state appropriations for capital projects; the completion of a parking lot that totaled \$3.4 million and was funded through parking revenues; and the completion of the telecom infrastructure project that totaled \$2.1 million and was funded through state appropriations for capital projects.

See note 7 to the financial statements for further information on capital assets.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis

June 30, 2008 and 2007

Long-Term Debt Obligations

Debt outstanding at June 30, 2008, 2007, and 2006 is summarized below by type of debt instrument:

	June 30		
	2008	2007	2006
Systemwide Revenue Bonds:			
Series 2002A	\$ 5,200,000	5,300,000	5,395,000
Series 2005A	24,730,000	25,005,000	25,230,000
Capital leases	4,319,000	2,903,000	506,000
Other	8,801,568	1,975,352	2,931,801
Total	43,050,568	35,183,352	34,062,801
Less current portion	(2,250,449)	(2,082,918)	(1,331,838)
Long-term debt, net of current portion	\$ 40,800,119	33,100,434	32,730,963

As of June 30, 2008

At June 30, 2008 and 2007, the University had \$43.1 million and \$35.2 million, respectively, in debt outstanding. The \$7.9 million increase is primarily due to the addition of a \$7.9 million increase in long-term debt for the University's Energy Conservation Project and \$2.5 million in capital leases for PeopleSoft CMS and Computer Refresh program. Offsetting these increases is \$2.5 million for the retirement of the University's debt.

As of June 30, 2007

At June 30, 2007 and 2006, the University had \$35.2 million and \$34.1 million, respectively, in debt outstanding. The \$1.1 million increase is primarily due to the addition of a \$1.2 million increase in capital leases for PeopleSoft CMS and \$1.6 million in financing of noncapital assets. Offsetting these increases is \$1.7 million for the retirement of the University's debt.

Bond Ratings

Moody's Investors Service currently provides intrinsic ratings of Aa3, with a "stable outlook," for the Systemwide Revenue Bonds. Standard & Poor's Rating Service currently provides intrinsic ratings of A+, with a "positive outlook," for the Systemwide Revenue Bonds. With the exception of certain maturities of Series 2005C, Series 2007A, and Series 2008A, all Systemwide Revenue Bonds are insured. At the time of issuance, all providers of insurance for Systemwide Revenue Bonds were rated Aaa/AAA by Moody's Investors Service and Standard & Poor's Rating Service, respectively. During fiscal year 2008, some providers of insurance for Systemwide Revenue Bonds were downgraded to ratings below Aaa/AAA, which had no impact on any related bond covenants. See notes 9 and 11 to the financial statements for further information on long-term debt obligations. Those bonds that are uninsured bear the same rating as the Systemwide Revenue Bonds, which are Aa3 from the Moody's Investors Service and A+ from the Standard & Poor's Rating Service.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis

June 30, 2008 and 2007

Factors Impacting Future Periods

The legislative process has approved the State General Fund allocation to the California State University (CSU) for fiscal year 2008/2009. The allocation provided to the University is \$64.9 million, a decrease of \$2.2 million over fiscal year 2007/2008. The increase is budgeted to be used primarily for State University Grants.

Budgeted full-time equivalent enrollment targets for fiscal years 2008/2009 and 2009/2010 are 7,283 and 7,477, representing increases of 0.00% and 2.66%, respectively. This anticipated growth will generate additional revenues of approximately \$4.9 million for the University.

In 2007, the CSU Board of Trustees approved the Social and Behavioral Science Building project for the University. This project will design and construct a 67,438-assignable-square-foot/106,335-gross-square-foot building of lecture rooms, labs, faculty offices, graduate research, and academic support spaces for the Social and Behavioral Sciences. The total cost of the project is projected to be approximately \$40.1 million and will be funded primarily through state appropriations. The project is scheduled to begin construction in December 2008 and take occupancy in January 2011.

In July 2007, The University began planning for the Parking Structure Phase 1 Project and the Public Services Building. The Parking Structure Phase 1 Project will be built in two phases: phase one will provide the necessary road and site improvements at an estimated project cost of \$3.3 million with anticipated completion in February 2009; phase two will provide a parking structure with 1,615 parking spaces at an estimated project cost of \$30.0 million with estimated completion date being July 2010. The Public Services Building will provide a 10,300-assignable-square-foot/13,026-gross-square-foot building that will house the University Parking and Transportation Services Department, University Police, and the Campus Emergency Operation Center. The estimated project cost is \$7.5 million and estimated completion date is February 2011. Funding for these projects will be from parking revenues and bond proceeds.

The McMahon House, which began construction in February 2007, will be a conference center, providing 3,238 square feet of meeting space and is scheduled to be completed in March 2009. The total cost of the project is projected to be \$4.8 million and is funded primarily through donor funds.

On July 1, 2008, the name of the California State University San Marcos Foundation changed to the University Auxiliary and Research Services Corporation. It is the same organization, with its employees continuing to provide support and service to the campus through its commercial operations, grant and contract services, business, and financial services. A new Nonprofit Foundation for the purpose of the generating private support will be established and will reside in University Advancement and will be named the California State University San Marcos Foundation.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Statement of Net Assets

June 30, 2008

Assets	<u>University</u>	<u>Discretely presented component units FASB auxiliary organizations</u>	<u>Total</u>
Current assets:			
Cash and cash equivalents	\$ 10,087	9,910,120	9,920,207
Short-term investments	27,548,362	3,117,323	30,665,685
Accounts receivable, net	1,361,493	1,737,044	3,098,537
Leases receivable, current portion	330,000	—	330,000
Pledges receivable, net	—	1,227,940	1,227,940
Prepaid expenses and other assets	551,639	1,333,597	1,885,236
Total current assets	<u>29,801,581</u>	<u>17,326,024</u>	<u>47,127,605</u>
Noncurrent assets:			
Restricted cash and cash equivalents	—	1,565,559	1,565,559
Accounts receivable, net	55,252,258	—	55,252,258
Leases receivable, net of current portion	24,400,000	—	24,400,000
Student loans receivable, net	446,256	—	446,256
Pledges receivable, net	—	985,655	985,655
Endowment investments	—	14,160,550	14,160,550
Other long-term investments	11,331,652	496,362	11,828,014
Capital assets, net	171,710,197	30,636,962	202,347,159
Other assets	—	64,081	64,081
Total noncurrent assets	<u>263,140,363</u>	<u>47,909,169</u>	<u>311,049,532</u>
Total assets	<u>\$ 292,941,944</u>	<u>65,235,193</u>	<u>358,177,137</u>
Liabilities and Net Assets			
Current liabilities:			
Accounts payable	\$ 6,549,234	506,077	7,055,311
Accrued salaries and benefits payable	5,999,492	613,728	6,613,220
Accrued compensated absences – current portion	2,021,027	155,125	2,176,152
Deferred revenue	2,796,528	1,593,114	4,389,642
Capitalized lease obligations – current portion	1,382,000	—	1,382,000
Long-term debt obligations – current portion	868,449	330,000	1,198,449
Other liabilities	527,577	730,878	1,258,455
Total current liabilities	<u>20,144,307</u>	<u>3,928,922</u>	<u>24,073,229</u>
Noncurrent liabilities:			
Accrued compensated absences, net of current portion	2,195,612	—	2,195,612
Grants refundable	466,737	—	466,737
Capitalized lease obligations, net of current portion	2,937,000	—	2,937,000
Long-term debt obligations, net of current portion	37,863,119	25,129,666	62,992,785
Depository accounts	419,570	—	419,570
Total noncurrent liabilities	<u>43,882,038</u>	<u>25,129,666</u>	<u>69,011,704</u>
Total liabilities	<u>64,026,345</u>	<u>29,058,588</u>	<u>93,084,933</u>
Net assets:			
Invested in capital assets, net of related debt	161,404,962	5,177,296	166,582,258
Restricted for:			
Nonexpendable – endowments	—	15,486,584	15,486,584
Expendable:			
Scholarships and fellowships	20,801	74,591	95,392
Loans	53,345	—	53,345
Capital projects	54,737,963	2,361,376	57,099,339
Other	282,364	2,176,689	2,459,053
Unrestricted	12,416,164	10,900,069	23,316,233
Total net assets	<u>\$ 228,915,599</u>	<u>36,176,605</u>	<u>265,092,204</u>

See accompanying notes to financial statements.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Statement of Net Assets

June 30, 2007

Assets	Discretely presented component units		
	University	FASB Auxiliary Organizations	Total
Current assets:			
Cash and cash equivalents	\$ 10,087	11,826,807	11,836,894
Short-term investments	28,214,619	—	28,214,619
Accounts receivable, net	1,418,434	2,585,034	4,003,468
Leases receivable, current portion	275,000	—	275,000
Pledges receivable, net	—	889,003	889,003
Prepaid expenses and other assets	1,882,503	1,030,957	2,913,460
Total current assets	31,800,643	16,331,801	48,132,444
Noncurrent assets:			
Restricted cash and cash equivalents	—	1,002,857	1,002,857
Accounts receivable, net	2,582,588	—	2,582,588
Leases receivable, net of current portion	24,730,000	—	24,730,000
Student loans receivable, net	278,850	—	278,850
Pledges receivable, net	—	1,058,074	1,058,074
Endowment investments	—	14,122,701	14,122,701
Other long-term investments	340,346	—	340,346
Capital assets, net	172,000,458	29,533,915	201,534,373
Other assets	—	428,458	428,458
Total noncurrent assets	199,932,242	46,146,005	246,078,247
Total assets	\$ 231,732,885	62,477,806	294,210,691
Liabilities and Net Assets			
Current liabilities:			
Accounts payable	\$ 5,716,603	1,500,618	7,217,221
Accrued salaries and benefits payable	4,688,035	566,236	5,254,271
Accrued compensated absences – current portion	1,808,363	145,336	1,953,699
Deferred revenue	3,528,119	1,277,967	4,806,086
Capitalized lease obligations – current portion	704,000	—	704,000
Long-term debt obligations – current portion	1,378,918	275,000	1,653,918
Other liabilities	423,584	550,254	973,838
Total current liabilities	18,247,622	4,315,411	22,563,033
Noncurrent liabilities:			
Accrued compensated absences, net of current portion	1,939,328	—	1,939,328
Grants refundable	479,631	—	479,631
Capitalized lease obligations, net of current portion	2,199,000	—	2,199,000
Long-term debt obligations, net of current portion	30,901,434	25,489,049	56,390,483
Depository accounts	340,449	—	340,449
Total noncurrent liabilities	35,859,842	25,489,049	61,348,891
Total liabilities	54,107,464	29,804,460	83,911,924
Net assets:			
Invested in capital assets, net of related debt	164,089,064	3,769,866	167,858,930
Restricted for:			
Nonexpendable – endowments	—	12,700,961	12,700,961
Expendable:			
Scholarships and fellowships	150,740	131,804	282,544
Loans	54,541	—	54,541
Capital projects	1,161,560	3,049,912	4,211,472
Other	—	4,165,749	4,165,749
Unrestricted	12,169,516	8,855,054	21,024,570
Total net assets	\$ 177,625,421	32,673,346	210,298,767

See accompanying notes to financial statements.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS
Statement of Revenues, Expenses, and Changes in Net Assets
Year ended June 30, 2008

	<u>University</u>	<u>Discretely presented component units FASB Auxiliary Organizations</u>	<u>Eliminations</u>	<u>Total</u>
Revenues:				
Operating revenues:				
Student tuition and fees (net of scholarship allowances of \$5,558,013)	\$ 28,372,626	1,077,449	(63,412)	29,386,663
Grants and contracts, noncapital:				
Federal	—	4,399,588	—	4,399,588
State	501,090	870,920	—	1,372,010
Local	—	2,279,352	—	2,279,352
Nongovernmental	334,471	995,810	—	1,330,281
Sales and services of educational activities	—	3,085,037	(443,951)	2,641,086
Sales and services of auxiliary enterprises	3,975,336	10,291,917	—	14,267,253
Other operating revenues	1,165,736	477,106	—	1,642,842
Total operating revenues	<u>34,349,259</u>	<u>23,477,179</u>	<u>(507,363)</u>	<u>57,319,075</u>
Expenses:				
Operating expenses:				
Instruction	41,511,883	2,274,091	—	43,785,974
Research	175,737	2,582,223	—	2,757,960
Public service	224,520	474,269	—	698,789
Academic support	15,139,687	790,040	—	15,929,727
Student services	11,189,897	864,249	(63,412)	11,990,734
Institutional support	18,003,201	3,476,629	(443,951)	21,035,879
Operation and maintenance of plant	11,479,581	—	—	11,479,581
Student grants and scholarships	11,791,180	611,683	(611,683)	11,791,180
Auxiliary enterprise expenses	3,144,084	8,798,499	(187,501)	11,755,082
Depreciation and amortization	10,021,968	1,342,337	—	11,364,305
Total operating expenses	<u>122,681,738</u>	<u>21,214,020</u>	<u>(1,306,547)</u>	<u>142,589,211</u>
Operating income (loss)	<u>(88,332,479)</u>	<u>2,263,159</u>	<u>799,184</u>	<u>(85,270,136)</u>
Nonoperating revenues (expenses):				
State appropriations, noncapital	67,071,786	—	—	67,071,786
Federal financial aid grants, noncapital	6,838,776	—	—	6,838,776
State and local financial aid grants, noncapital	2,863,849	—	—	2,863,849
Gifts, noncapital	1,820,247	1,643,193	(949,184)	2,514,256
Investment income, net	2,637,243	331,480	—	2,968,723
Endowment loss	—	(919,575)	—	(919,575)
Interest expense	(1,580,157)	(1,040,045)	—	(2,620,202)
Other nonoperating revenues (expenses), net	746,485	(3,042,896)	3,110,463	814,052
Net nonoperating revenues (expenses)	<u>80,398,229</u>	<u>(3,027,843)</u>	<u>2,161,279</u>	<u>79,531,665</u>
Income (loss) before other additions	<u>(7,934,250)</u>	<u>(764,684)</u>	<u>2,960,463</u>	<u>(5,738,471)</u>
State appropriations, capital	56,087,000	—	—	56,087,000
Grants and gifts, capital	3,137,428	—	(2,960,463)	176,965
Additions to permanent endowments	—	2,785,623	—	2,785,623
Increase in net assets	<u>51,290,178</u>	<u>2,020,939</u>	<u>—</u>	<u>53,311,117</u>
Net assets:				
Net assets at beginning of year, as restated (note 2(c))	<u>177,625,421</u>	<u>34,155,666</u>	<u>—</u>	<u>211,781,087</u>
Net assets at end of year	<u>\$ 228,915,599</u>	<u>36,176,605</u>	<u>—</u>	<u>265,092,204</u>

See accompanying notes to financial statements.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS
Statement of Revenues, Expenses, and Changes in Net Assets
Year ended June 30, 2007

	<u>University</u>	<u>Discretely presented component units FASB Auxiliary Organizations</u>	<u>Eliminations</u>	<u>Total</u>
Revenues:				
Operating revenues:				
Student tuition and fees (net of scholarship allowances of \$4,297,109)	\$ 26,194,782	1,186,445	—	27,381,227
Grants and contracts, noncapital:				
Federal	—	5,175,081	—	5,175,081
State	125,138	6,152,202	—	6,277,340
Local	—	55,034	—	55,034
Nongovernmental	244,868	937,280	—	1,182,148
Sales and services of educational activities	—	1,934,190	—	1,934,190
Sales and services of auxiliary enterprises	3,910,557	9,999,005	—	13,909,562
Other operating revenues	970,934	386,648	—	1,357,582
Total operating revenues	<u>31,446,279</u>	<u>25,825,885</u>	<u>—</u>	<u>57,272,164</u>
Expenses:				
Operating expenses:				
Instruction	36,879,767	1,487,489	—	38,367,256
Research	314,606	4,482,862	—	4,797,468
Public service	282,700	1,295,620	—	1,578,320
Academic support	15,677,611	345,194	—	16,022,805
Student services	10,973,443	5,568,508	—	16,541,951
Institutional support	14,029,746	1,182,423	—	15,212,169
Operation and maintenance of plant	10,084,801	—	—	10,084,801
Student grants and scholarships	10,363,981	448,100	—	10,812,081
Auxiliary enterprise expenses	2,700,115	6,875,675	(497,006)	9,078,784
Depreciation and amortization	9,373,835	1,085,498	—	10,459,333
Total operating expenses	<u>110,680,605</u>	<u>22,771,369</u>	<u>(497,006)</u>	<u>132,954,968</u>
Operating income (loss)	<u>(79,234,326)</u>	<u>3,054,516</u>	<u>497,006</u>	<u>(75,682,804)</u>
Nonoperating revenues (expenses):				
State appropriations, noncapital	59,921,313	—	—	59,921,313
Federal financial aid grants, noncapital	5,928,883	—	—	5,928,883
State and local financial aid grants, noncapital	2,390,997	—	—	2,390,997
Gifts, noncapital	1,273,863	953,637	(30,368)	2,197,132
Investment income, net	2,628,340	1,456,139	—	4,084,479
Endowment income	—	808,533	—	808,533
Interest expense	(1,531,210)	—	—	(1,531,210)
Other nonoperating revenues (expenses), net	561,437	(310,102)	—	251,335
Net nonoperating revenues (expenses)	<u>71,173,623</u>	<u>2,908,207</u>	<u>(30,368)</u>	<u>74,051,462</u>
Income (loss) before other additions	<u>(8,060,703)</u>	<u>5,962,723</u>	<u>466,638</u>	<u>(1,631,342)</u>
State appropriations, capital				
Grants and gifts, capital	1,349,000	—	—	1,349,000
Additions to permanent endowments	515,497	—	(466,638)	48,859
Additions to permanent endowments	—	358,728	—	358,728
Increase (decrease) in net assets	<u>(6,196,206)</u>	<u>6,321,451</u>	<u>—</u>	<u>125,245</u>
Net assets:				
Net assets at beginning of year	<u>183,821,627</u>	<u>26,351,895</u>	<u>—</u>	<u>210,173,522</u>
Net assets at end of year	<u>\$ 177,625,421</u>	<u>32,673,346</u>	<u>—</u>	<u>210,298,767</u>

See accompanying notes to financial statements.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Statements of Cash Flows

Years ended June 30, 2008 and 2007

	<u>University</u>	
	<u>2008</u>	<u>2007</u>
Cash flows from operating activities:		
Student tuition and fees	\$ 27,606,508	26,585,786
Federal grants and contracts	60,660	—
State grants and contracts	501,090	125,138
Nongovernmental grants and contracts	334,471	244,868
Payments to suppliers	(15,715,214)	(17,776,796)
Payments to employees	(79,567,594)	(71,128,496)
Payments to students	(12,137,255)	(10,531,078)
Collections of student loans	178,668	169,095
Sales and services of auxiliary enterprises	3,975,336	3,910,557
Other receipts	1,038,555	1,705,774
Net cash used in operating activities	<u>(73,724,775)</u>	<u>(66,695,152)</u>
Cash flows from noncapital financing activities:		
State appropriations	67,265,199	61,318,556
Federal financial aid grants	6,838,776	5,928,883
State and local financial aid grants	2,863,849	2,390,997
Gifts and grants received for other than capital purposes	1,804,247	1,211,723
Federal loan program receipts	20,258,135	18,794,468
Federal loan program disbursements	(20,246,658)	(18,789,224)
Monies received on behalf of others	896,613	74,744
Monies disbursed on behalf of others	(900,000)	(71,720)
Other	(1,959,225)	653,571
Net cash provided by noncapital financing activities	<u>76,820,936</u>	<u>71,511,998</u>
Cash flows from capital and related financing activities:		
Proceeds from capital debt	7,831,000	—
State appropriations	3,389,240	10,221,351
Capital grants and gifts	2,960,463	439,688
Acquisition of capital assets	(8,104,356)	(8,478,709)
Principal paid on capital debt and leases	(1,302,698)	(368,000)
Interest paid on capital debt and leases	(507,814)	(1,532,781)
Principal payments received on capital leases	275,000	225,000
Interest payments received on capital leases	1,163,615	1,215,288
Net cash provided by capital and related financing activities	<u>5,704,450</u>	<u>1,721,837</u>
Cash flows from investing activities:		
Proceeds from sales and maturities of investments	135,410,764	16,905,912
Purchases of investments	(145,735,810)	(28,540,270)
Investment income received	1,524,435	1,384,179
Net cash used in investing activities	<u>(8,800,611)</u>	<u>(10,250,179)</u>
Net decrease in cash and cash equivalents	—	(3,711,496)
Cash and cash equivalents at beginning of year	<u>10,087</u>	<u>3,721,583</u>
Cash and cash equivalents at end of year	<u>\$ 10,087</u>	<u>10,087</u>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Statements of Cash Flows

Years ended June 30, 2008 and 2007

	<u>University</u>	
	<u>2008</u>	<u>2007</u>
Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	\$ (88,332,479)	(79,234,326)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation and amortization	10,021,968	9,373,835
Change in assets and liabilities:		
Accounts receivable, net	(167,276)	382,737
Student loans receivable, net	(167,407)	1,998
Prepaid expenses and other assets	1,330,859	1,039,512
Accounts payable	2,368,597	(268,573)
Accrued salaries and benefits	1,311,457	705,146
Accrued compensated absences	468,946	471,386
Deferred revenue	(731,591)	591,944
Depository accounts	79,121	(14,197)
Other liabilities	93,030	255,386
Net cash used in operating activities	<u>\$ (73,724,775)</u>	<u>(66,695,152)</u>
Supplemental schedules of noncash transactions:		
Contributed capital assets	\$ 176,965	75,089
Acquisition of capital asset through capital lease	2,497,000	2,822,000
Construction work in progress acquired from the Office of the Chancellor	369,450	54,213
Accrued capital asset costs (purchased but unpaid at year-end)	597,959	2,117,928

See accompanying notes to financial statements.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2008 and 2007

(1) Organization

California State University, San Marcos (the University), an agency of the State of California (the State), was established as a campus of the California State University under the State of California Education Code to offer undergraduate and graduate instruction for professional and occupational goals emphasizing a broad liberal arts education. As one of 23 campuses in the California State University System (the System), the University is included in the financial statements of the System. Responsibility for the University is vested in the Trustees of the System (the Trustees) who, in turn, appoint the Chancellor, the chief executive officer of the System, and the University president, the chief executive officer of the University.

The University provides instruction for baccalaureate and master's degrees and certificate programs, and operates various auxiliary enterprises such as student dormitories, student unions, and parking facilities. In addition, the University administers a variety of financial aid programs, which are funded primarily through state and federal programs.

(2) Summary of Significant Accounting Policies

(a) *Financial Reporting Entity*

In accordance with Governmental Accounting Standards Board (GASB) Statements No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, and No. 35, *Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities*, the accompanying financial statements include the accounts of the University and the University's three recognized auxiliary organizations. These auxiliary organizations are legally separate entities that provide services primarily to the University's students and faculty. Separate financial statements are issued for each of the recognized auxiliary organizations and may be obtained from the University.

The discretely presented auxiliary organizations are as follows:

- California State University, San Marcos Foundation
- Associated Students Incorporated of California State University, San Marcos
- San Marcos University Corporation

On July 1, 2008, the name of the California State University, San Marcos Foundation changed to the University Auxiliary and Research Services Corporation. It is the same organization and will function in a similar manner to provide support and service to the campus. A new non-profit foundation for the purposes of generating private support will be established and named the California State University, San Marcos Foundation.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

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Summary information for the discretely presented auxiliary organizations is as follows:

June 30, 2008	California State University, San Marcos Foundation	Associated Students, Inc. of California State University, San Marcos	San Marcos University Corporation	Total
Current assets	\$ 12,899,618	738,035	3,688,371	17,326,024
Capital assets, net	1,237,762	15,503	29,383,697	30,636,962
Other noncurrent assets	17,269,207	3,000	—	17,272,207
Total assets	<u>31,406,587</u>	<u>756,538</u>	<u>33,072,068</u>	<u>65,235,193</u>
Current liabilities	1,885,143	257,748	1,786,031	3,928,922
Noncurrent liabilities	—	—	25,129,666	25,129,666
Total liabilities	<u>1,885,143</u>	<u>257,748</u>	<u>26,915,697</u>	<u>29,058,588</u>
Invested in capital assets, net of related debt	1,237,762	15,503	3,924,031	5,177,296
Restricted	20,099,240	—	—	20,099,240
Unrestricted	8,184,442	483,287	2,232,340	10,900,069
Total net assets	\$ <u>29,521,444</u>	<u>498,790</u>	<u>6,156,371</u>	<u>36,176,605</u>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2008 and 2007

<u>June 30, 2008</u>	<u>California State University, San Marcos Foundation</u>	<u>Associated Students, Inc. of California State University, San Marcos</u>	<u>San Marcos University Corporation</u>	<u>Total</u>
Operating revenues:				
Student tuition and fees, net	\$ —	1,077,449	—	1,077,449
Grants and contracts, noncapital	8,542,473	3,197	—	8,545,670
Sales and services of education activities	3,085,037	—	—	3,085,037
Sales and services of auxiliary enterprises, net	5,739,165	—	4,552,752	10,291,917
Other	—	60,360	416,746	477,106
Total operating revenues	<u>17,366,675</u>	<u>1,141,006</u>	<u>4,969,498</u>	<u>23,477,179</u>
Operating expenses:				
Instruction	2,274,091	—	—	2,274,091
Research	2,582,223	—	—	2,582,223
Public service	474,269	—	—	474,269
Academic support	790,040	—	—	790,040
Student services	686,170	178,079	—	864,249
Institutional support	3,476,629	—	—	3,476,629
Student grants and scholarships	611,683	—	—	611,683
Auxiliary enterprises expenses	5,007,243	957,598	2,833,658	8,798,499
Depreciation and amortization	282,801	12,739	1,046,797	1,342,337
Total operating expenses	<u>16,185,149</u>	<u>1,148,416</u>	<u>3,880,455</u>	<u>21,214,020</u>
Operating income (loss)	1,181,526	(7,410)	1,089,043	2,263,159
Net nonoperating revenues (expenses)	<u>(7,019,049)</u>	<u>24,790</u>	<u>6,752,039</u>	<u>(242,220)</u>
Increase (decrease) in net assets	(5,837,523)	17,380	7,841,082	2,020,939
Beginning net assets, July 1, 2007, as restated (note 2(c))	<u>35,358,967</u>	<u>481,410</u>	<u>(1,684,711)</u>	<u>34,155,666</u>
Ending net assets, June 30, 2008	<u>\$ 29,521,444</u>	<u>498,790</u>	<u>6,156,371</u>	<u>36,176,605</u>

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<u>June 30, 2007</u>	<u>California State University, San Marcos Foundation</u>	<u>Associated Students, Inc. of California State University, San Marcos</u>	<u>San Marcos University Corporation</u>	<u>Total</u>
Current assets	\$ 12,838,296	758,086	2,735,419	16,331,801
Capital assets, net	7,290,816	28,242	22,214,857	29,533,915
Other noncurrent assets	16,609,090	3,000	—	16,612,090
Total assets	<u>36,738,202</u>	<u>789,328</u>	<u>24,950,276</u>	<u>62,477,806</u>
Current liabilities	2,861,555	307,918	1,145,938	4,315,411
Noncurrent liabilities	—	—	25,489,049	25,489,049
Total liabilities	<u>2,861,555</u>	<u>307,918</u>	<u>26,634,987</u>	<u>29,804,460</u>
Invested in capital assets, net of related debt	7,290,816	28,242	(3,549,192)	3,769,866
Restricted	20,048,426	—	—	20,048,426
Unrestricted	6,537,405	453,168	1,864,481	8,855,054
Total net assets (deficit)	<u>\$ 33,876,647</u>	<u>481,410</u>	<u>(1,684,711)</u>	<u>32,673,346</u>

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<u>June 30, 2007</u>	<u>California State University, San Marcos Foundation</u>	<u>Associated Students, Inc. of California State University, San Marcos</u>	<u>San Marcos University Corporation</u>	<u>Total</u>
Operating revenues:				
Student tuition and fees	\$ —	1,186,445	—	1,186,445
Grants and contracts, noncapital	12,308,620	10,977	—	12,319,597
Sales and services of education activities	1,934,190	—	—	1,934,190
Sales and services of auxiliary enterprises, net	5,958,446	—	4,040,559	9,999,005
Other	—	243,643	143,005	386,648
Total operating revenues	<u>20,201,256</u>	<u>1,441,065</u>	<u>4,183,564</u>	<u>25,825,885</u>
Operating expenses:				
Instruction	1,487,489	—	—	1,487,489
Research	4,482,862	—	—	4,482,862
Public service	1,295,620	—	—	1,295,620
Academic support	345,194	—	—	345,194
Student services	5,373,436	195,072	—	5,568,508
Institutional support	1,182,423	—	—	1,182,423
Student grants and scholarships	448,100	—	—	448,100
Auxiliary enterprises expenses	2,250,799	1,195,732	3,429,144	6,875,675
Depreciation	303,599	14,242	767,657	1,085,498
Total operating expenses	<u>17,169,522</u>	<u>1,405,046</u>	<u>4,196,801</u>	<u>22,771,369</u>
Operating income (loss)	3,031,734	36,019	(13,237)	3,054,516
Net nonoperating revenues, net	<u>3,241,688</u>	<u>25,247</u>	<u>—</u>	<u>3,266,935</u>
Increase (decrease) in net assets	6,273,422	61,266	(13,237)	6,321,451
Net assets (deficit) at beginning of year	<u>27,603,225</u>	<u>420,144</u>	<u>(1,671,474)</u>	<u>26,351,895</u>
Net assets (deficit) at end of year	<u>\$ 33,876,647</u>	<u>481,410</u>	<u>(1,684,711)</u>	<u>32,673,346</u>

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The auxiliary organizations are presented in the accompanying financial statements as component units due to the nature and significance of their relationship with the University. The relationships are such that exclusion of these organizations from the reporting entity would render the financial statements incomplete, primarily due to the activities that the organizations carry out on behalf of the University, such as research, grant administration, foodservice, and academic support. The auxiliary organizations are discretely presented to allow the financial statement users to distinguish them from the University.

The financial statements present only the statements of net assets, statements of revenues, expenses, and changes in net assets, and statements of cash flows of only that portion of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State that is attributable to the transactions of the University and the financial statements do not purport to, and do not, present fairly the financial position of the State or the System as of June 30, 2008 and 2007 and the changes in their financial position, or, where applicable, their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

In September 2007, the San Marcos University Corporation received property and equipment from the California State University, San Marcos Foundation to provide day-care services to the faculty, staff, and the community. The total value of the property transferred by the California State University, San Marcos Foundation was \$7,681,138. The San Marcos University Corporation recorded the transaction as gifts, capital, and the California State University, San Marcos Foundation recorded the transfer as a nonoperating expense.

(b) Basis of Presentation

The accompanying financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting in accordance with U.S. generally accepted accounting principles, as prescribed by the GASB. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements have been met.

The financial statements required by GASB Statement Nos. 34 and 35 include a statement of net assets, a statement of revenues, expenses, and changes in net assets, and a statement of cash flows. As a public institution, the University is considered a special-purpose government under the provisions of GASB Statement No. 35. The University records revenue in part from fees and other charges for services to external users and, accordingly, has chosen to present its financial statements using the reporting model for special-purpose governments engaged only in business-type activities. This model allows all financial information for the University to be reported in a single column in each of the financial statements, accompanied by aggregated financial information for the auxiliary organizations. In accordance with the business-type activities reporting model, the University prepares its statements of cash flows using the direct method.

The auxiliary organizations included in these financial statements apply the accounting and reporting standards promulgated by the Financial Accounting Standards Board (FASB).

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

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(c) Auxiliary Organizations Restatement

The beginning net assets of the auxiliary organizations have been restated due to the correction of an error related to contributions receivable reported in the separately audited financial statements of the California State University, San Marcos Foundation. A summary of the restatement to net assets at July 1, 2007 related to the California State University, San Marcos Foundation is as follows:

Net assets as of June 30, 2007, as previously reported	\$ 33,876,647
Recognition of contribution receivable previously unrecorded	<u>1,482,320</u>
Net assets as of July 1, 2007, as restated	<u><u>\$ 35,358,967</u></u>

(d) Election of Applicable FASB Statements

The University has elected to follow standards of accounting and financial reporting issued by the FASB prior to November 30, 1989, unless those standards conflict with or contradict guidance of the GASB. The University also has the option of following subsequent private sector guidance subject to the same limitation. The University has elected not to adopt the pronouncements issued by the FASB after November 30, 1989.

(e) Classification of Current and Noncurrent Assets (Other Than Investments) and Liabilities

The University considers assets to be current that can reasonably be expected, as part of its normal business operations, to be converted to cash and be available for liquidation of current liabilities within 12 months of the statement of net assets date. Liabilities that reasonably can be expected, as part of normal business operations, to be liquidated within 12 months of the statement of net assets date are considered to be current. All other assets and liabilities are considered to be noncurrent. For classification of current and noncurrent investments, refer to note 2(g).

(f) Cash and Cash Equivalents

The University considers all highly liquid investments with an original maturity date of three months or less to be cash and cash equivalents. The University considers amounts included in the California State University Investment Pool to be investments. The statement of cash flows does not include the cash flows of the discretely presented auxiliary organizations.

(g) Investments

Investments are reflected at fair value using quoted market prices. Realized and unrealized gains and losses are included in the accompanying statements of revenues, expenses, and changes in net assets as investment income, net.

Investments that are restricted for withdrawal or use, for other than current operations, are designated for the acquisition of construction or noncurrent assets, or are segregated for the liquidation of long-term debt are classified within other long-term investments.

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(h) Capital Assets

Capital assets are stated at cost or estimated historical cost if purchased, or if donated, at estimated fair value at date of donation. Capital assets, including infrastructure, with a value of \$5,000 or more and with a useful life of one year or more are capitalized. Such costs include, where applicable, interest capitalized as part of the cost of constructed capital assets. Title to all assets, whether purchased, constructed, or donated, is held by the State. Although title is not with the University for land and buildings, the University has exclusive use of these assets and is responsible for the maintenance of these assets and thus has recorded the cost of these assets on the accompanying financial statements. Capital assets, with the exception of land and land improvements, works of art and historical treasures, and construction work in progress, are depreciated on a straight-line basis over their estimated useful lives, which range from 3 to 45 years. Library books, unless considered rare collections, are capitalized and depreciated over a 10-year period. Periodicals and subscriptions are expensed as purchased. Works of art and historical treasures are valued at cost if purchased or the fair market value at the date of donation if contributed. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend its life are expensed as incurred.

Depreciation expense is shown separately in the statements of revenues, expenses, and changes in net assets rather than being allocated among other categories of operating expenses.

(i) Deferred Revenue

Deferred revenue consists primarily of fees collected in advance for summer and fall terms and continuing education programs.

(j) Compensated Absences

University employees accrue annual leave at rates based on length of service and job classification.

(k) Grants Refundable

The University periodically receives contributions from the federal government in support of its operation of the Federal Perkins and Nursing Loan programs, approved Title IV loan programs. The federal government has the ability to terminate its support of these programs at any time and to request the University to return those contributions that it has made on a cumulative basis. Accordingly, the federal contributions received and retained by the University at year-end are considered to be liabilities of the University, and are reflected as such in the accompanying statements of net assets.

(l) Net Assets

The University's net assets are classified into the following net asset categories:

Invested in capital assets, net of related debt – Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction, or improvement of those assets.

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Restricted – nonexpendable – Net assets subject to externally imposed conditions that the University retains them in perpetuity. Net assets in this category consist of endowments held by the University or its related auxiliaries.

Restricted – expendable – Net assets subject to externally imposed conditions that can be fulfilled by the actions of the University or by the passage of time.

Unrestricted – All other categories of net assets. In addition, unrestricted net assets may be designated for use by management of the University or have legislative or bond indenture requirements associated with their use. These requirements limit the area of operations for which expenditures of net assets may be made and require that unrestricted net assets be designated to support future operations in these areas. Campus housing programs are a primary example of operations that have unrestricted net assets with designated uses.

Restricted Net Assets

	June 30	
	2008	2007
Expendable:		
Scholarships and fellowships	\$ 20,801	150,740
Loans	53,345	54,541
Capital projects	54,737,963	1,161,560
Other	282,364	—
	<hr/>	<hr/>
Total restricted net assets – expendable	\$ 55,094,473	1,366,841
	<hr/> <hr/>	<hr/> <hr/>

(m) Classification of Revenues and Expenses

The University considers operating revenues and expenses in the statements of revenues, expenses, and changes in net assets to be those revenues and expenses that result from exchange transactions or from other activities that are connected directly to the University’s primary functions. Exchange transactions include charges for services rendered and the acquisition of goods and services. Moreover, the Office of the Chancellor administers and charges campuses for centralized expenses such as State pro rata and management of capital projects and pooled investments, which are included in operating expenses by function in the accompanying statements of revenues, expenses, and changes in net assets.

Certain other transactions are reported as nonoperating revenues and expenses or capital contributions in accordance with GASB Statement No. 35. These nonoperating activities include the University’s capital and noncapital appropriations from the State, certain financial aid grants, noncapital, net investment income, gifts, interest expense, and capital contributions.

The State appropriates funds to the System on an annual basis. The appropriations are, in turn, allocated among the campuses by the Office of the Chancellor. Appropriations are recognized as revenue when authorization is received, and are reported as either noncapital appropriations when used to support general operations or capital appropriations when used for capital projects.

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Student tuition and fee revenue, and sales and services of auxiliary enterprises, including revenues from student housing programs, are presented net of scholarships and fellowships applied to student accounts. Certain other scholarship amounts are paid directly to, or refunded to, the student and are reflected as expenses.

(n) Internal Services Activities

Certain institutional internal service providers offer goods and services to University departments, as well as to their external customers. These include activities such as copy centers, postal services, and telecommunications. All internal service activities to University departments have been eliminated in the accompanying financial statements. These eliminations are recorded by removing the revenue and expense in the internal service sales and service units and, if significant, allocating any residual balances to those departments receiving the goods and services during the year.

(o) Income Taxes

As a campus of the System, the University is generally not subject to federal or state income taxes. However, the University remains subject to income taxes on any net income that is derived from a trade or business, regularly carried on and not in furtherance of the purpose for which it was granted exemption. No income tax provision has been recorded as the net income, if any, from any unrelated trade or business, in the opinion of management, is not material to the financial statements taken as a whole.

(p) New Accounting Pronouncements

On July 1, 2007, the University adopted GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, in accounting for its postretirement healthcare costs. The University participates in a postretirement healthcare program sponsored by the State administered by the California Public Employees' Retirement System (CalPERS). The State provides medical and prescription drug (healthcare benefits) to retired statewide employees, including retirees from the University (OPEB Plan). Currently, the majority of the University's retiree premium payments are paid by the State and not reflected within the University's financial statements. The OPEB liability and expense related to GASB Statement No. 45 for the System have been reported in the System's consolidated financial statements. The accrued OPEB liability and expense for the System are not allocated and are therefore not a liability to the University. See note 12 for a description of the OPEB plan.

On July 1, 2007, the University adopted GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets*, which requires additional disclosures related to pledged future revenues. The University has pledged future student union and auxiliary revenues to repay system revenue bonds. The bonds are payable solely from student union and auxiliary revenues. See note 9(b) for further details.

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(q) Eliminations

All significant nonexchange transactions between the University and the discretely presented auxiliary organizations have been eliminated from the total column and are separately presented in the eliminations column in the accompanying statements of revenues, expenses, and changes in net assets.

(r) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(s) Reclassifications

Certain reclassifications have been made to the 2007 financial statement information to conform to the 2008 financial statement presentation, including a reclassification of approximately \$8,320,000 relating to federal, state, local, and nongovernmental financial aid grants, noncapital from operating revenue to nonoperating revenues on the statement of revenues, expenses, and changes in net assets and approximately \$8,320,000 from cash flows from operating activities to net cash provided by noncapital financing activities on the statement of cash flows. The reclassifications had no impact on the previously reported changes in net assets of the University.

(3) Cash and Cash Equivalents and Investments

The University's cash and cash equivalents and investments as of June 30, 2008 and 2007 are classified in the accompanying statements of net assets as follows:

	June 30	
	<u>2008</u>	<u>2007</u>
Cash and cash equivalents	\$ 10,087	10,087
Total cash and cash equivalents	<u>10,087</u>	<u>10,087</u>
Short-term investments	27,548,362	28,214,619
Other long-term investments	11,331,652	340,346
Total investments	<u>38,880,014</u>	<u>28,554,965</u>
Total cash, cash equivalents, and investments	<u>\$ 38,890,101</u>	<u>28,565,052</u>

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(a) ***Cash and Cash Equivalents***

At June 30, 2008 and 2007, cash and cash equivalents consisted of petty cash. Total cash and cash equivalents were \$10,087 for both June 30, 2008 and 2007.

Custodial Credit Risk for Deposits

Custodial credit risk for deposits is the risk that the University will not be able to recover deposits or will not be able to recover collateral securities that are in possession of an outside party. The California Government Code and Education Code do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits, other than the provision that a financial institution must secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law. This risk is mitigated in that the University's deposits are maintained at financial institutions that are fully insured or collateralized as required by state law.

(b) ***Investments***

At June 30, 2008 and 2007, the University's investment portfolio consists primarily of investments in the State of California Surplus Money Investment Fund (SMIF) and the California State University Investment Pool. For the California State University Investment Pool, separate accounting is maintained as to the amounts allocable to the University's various funds and programs.

Investment Policy

State law and regulations require that surplus monies of the University must be invested. The primary objective of the University's investment policy is to safeguard the principal. The secondary objective is to meet the liquidity needs of the University. The third objective is to return an acceptable yield. The University's investment policy authorizes funds held in local trust accounts under Education Code Sections 89721 and 89724 to be invested in any of the securities authorized by Government Code Section 16430 and Education Code Section 89724, subject to certain limitations. In general, the University's investment policy permits investments in obligations of the federal and California state governments, certificates of deposit, high grade corporate and fixed income securities, and certain other investment instruments.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the University manages its exposure to interest rate risk is by purchasing a combination of short-term and long-term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or nearing maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations. The University monitors the interest rate risk inherent in its portfolio by measuring the weighted average maturity of its portfolio. The weighted average maturity of the University's investment portfolio for each investment type as of June 30, 2008 and 2007 is presented on the table in the following page.

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Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization.

The following table presents the fair value, weighted average maturity, and actual rating by investment type of the University's investment portfolio as of June 30, 2008:

Investment type	Fair value	Weighted average maturity (in years)	Rating as of year-end				
			AAA	AA	A	BBB	Not rated
Money market	\$ 7,855,878	—	\$ 7,855,878	—	—	—	—
Commercial paper	7,367,533	0.05	—	—	7,367,533	—	—
Certificates of deposit	6,259,228	0.13	—	—	6,259,228	—	—
Repurchase agreements	689,951	0.50	—	—	689,951	—	—
U.S. agency securities	3,602,503	1.17	3,051,781	—	550,722	—	—
Corporate and fixed income securities	10,039,647	1.68	3,095,972	3,310,055	3,395,433	83,764	154,423
State of California Surplus Money Investment Fund	2,029,490	0.58	—	—	—	—	2,029,490
U.S. Treasury	68,939	1.68	68,939	—	—	—	—
Mortgage-backed securities	966,845	11.97	966,845	—	—	—	—
Total investments	\$ 38,880,014		\$ 15,039,415	3,310,055	18,262,867	83,764	2,183,913

The following table presents the fair value, weighted average maturity, and actual rating by investment type of the University's investment portfolio as of June 30, 2007:

Investment type	Fair value	Weighted average maturity (in years)	Rating as of year-end			
			AAA	AA	A	Not rated
Money market	\$ 9,059	0.01	\$ —	—	—	9,059
Commercial paper	7,099,627	0.38	—	—	7,099,627	—
Certificates of deposit	7,230,048	0.01	—	5,303,103	1,926,945	—
Corporate and fixed income securities	10,676,786	1.42	1,099,786	4,513,770	5,063,230	—
Mortgage-backed securities	29,896	15.56	29,896	—	—	—
Total	25,045,416		\$ 1,129,682	9,816,873	14,089,802	9,059
Not subject to ratings:						
State of California Local Agency Investment Fund	3,509,549					
Total investments	\$ 28,554,965					

Concentration of Credit Risk

The University's investment policy contains no limitations on the amount that can be invested in any one issuer beyond that stipulated by the California Government Code. As of June 30, 2008, the

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following investments (other than U.S. Treasury securities, mutual funds, and external investment pools) represented 5.0% or more of the University's investment portfolio: Federal Home Loan Bank bonds \$2,032,694, (5.2%), Federated Government Obligations Fund \$7,845,044 (20.2%), and SMIF \$2,029,490 (5.2%). As of June 30, 2007 there were no investments representing 5% or more of the University's investment portfolio.

Market Uncertainties

The University invests in securities with contractual cash flows, such as asset-backed securities and mortgage-backed securities. The value, liquidity, and related income of these securities are sensitive to changes in economic conditions, including real estate value, delinquencies or defaults, or both, and may be adversely affected by shifts in the market's perception of the issuers and changes in interest rates.

For information regarding the investments of the individual discretely presented auxiliary organizations, refer to the separately issued auxiliary organizations' reports.

(4) Accounts Receivable

Accounts receivable at June 30 consisted of the following:

	2008		
	<u>Current</u>	<u>Noncurrent</u>	<u>Total</u>
State appropriations	\$ 10,088	55,252,258	55,262,346
Auxiliary organizations	574,712	—	574,712
Student accounts	595,973	—	595,973
Government grants and contracts	24,931	—	24,931
Other	577,482	—	577,482
	<u>1,783,186</u>	<u>55,252,258</u>	<u>57,035,444</u>
Less allowance for doubtful accounts	(421,693)	—	(421,693)
Total	<u>\$ 1,361,493</u>	<u>55,252,258</u>	<u>56,613,751</u>
	2007		
	<u>Current</u>	<u>Noncurrent</u>	<u>Total</u>
State appropriations	\$ 203,502	2,554,498	2,758,000
Auxiliary organizations	446,587	28,090	474,677
Student accounts	466,434	—	466,434
Government grants and contracts	19,364	—	19,364
Other	539,786	—	539,786
	<u>1,675,673</u>	<u>2,582,588</u>	<u>4,258,261</u>
Less allowance for doubtful accounts	(257,239)	—	(257,239)
Total	<u>\$ 1,418,434</u>	<u>2,582,588</u>	<u>4,001,022</u>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2008 and 2007

(5) Lease Receivable

In fiscal year 2004 – 2005, the University entered into a lease agreement with the San Marcos University Corporation. The lease agreement is the result of a transaction whereby the University refinanced certain San Marcos University Corporation bonds used to build campus housing that was placed into service in August 2003. The San Marcos University Corporation debt was refinanced through the issuance of Systemwide Revenue Bonds Series 2005A that are recorded as a long-term debt obligation in the accompanying financial statements. In return for the University refinancing the San Marcos University Corporation debt, the University entered into a 30-year lease agreement whereby the San Marcos University Corporation agreed to lease the campus housing facilities. Lease payments are due twice a year on May 1 and November 1.

Lease payments are due to the University as follows:

Fiscal year ending:		
2009	\$	330,000
2010		385,000
2011		450,000
2012		520,000
2013		590,000
Thereafter		<u>22,455,000</u>
Total lease receivable		24,730,000
Less current portion		<u>(330,000)</u>
Long-term lease receivable, net of current portion	\$	<u><u>24,400,000</u></u>

(6) Student Loans Receivable

Student loans receivable, net, at June 30 consisted of the following:

		<u>2008</u>	<u>2007</u>
Perkins loans	\$	280,806	301,082
Nursing loans		180,000	—
Other loans		<u>5,426</u>	<u>4,744</u>
Total student loans receivable, gross		466,232	305,826
Less allowance for doubtful accounts		<u>(19,976)</u>	<u>(26,976)</u>
Total student loans receivable, net	\$	<u><u>446,256</u></u>	<u><u>278,850</u></u>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2008 and 2007

(7) Capital Assets

Capital assets activity for the year ended June 30, 2008 consisted of the following:

	<u>Balance, June 30, 2007</u>	<u>Additions</u>	<u>Retirements</u>	<u>Transfers</u>	<u>Balance, June 30, 2008</u>
Nondepreciable capital assets:					
Land and land improvements	\$ 10,981,328	—	—	—	10,981,328
Works of art and historical treasures	25,000	—	—	—	25,000
Construction work in progress	<u>2,800,185</u>	<u>8,125,332</u>	<u>—</u>	<u>(2,386,517)</u>	<u>8,539,000</u>
Total nondepreciable capital assets	<u>13,806,513</u>	<u>8,125,332</u>	<u>—</u>	<u>(2,386,517)</u>	<u>19,545,328</u>
Depreciable capital assets:					
Buildings and building improvements	170,950,151	4,000	—	256,530	171,210,681
Improvements, other than buildings	17,492,537	—	—	60,499	17,553,036
Infrastructure	23,828,628	9,463	—	1,053,897	24,891,988
Personal property:					
Equipment	10,185,721	330,924	(792,054)	29,501	9,754,092
Library books and materials	10,108,676	336,510	(102,838)	—	10,342,348
Intangible assets	<u>2,397,905</u>	<u>968,649</u>	<u>—</u>	<u>986,090</u>	<u>4,352,644</u>
Total depreciable capital assets	<u>234,963,618</u>	<u>1,649,546</u>	<u>(894,892)</u>	<u>2,386,517</u>	<u>238,104,789</u>
Total cost	<u>248,770,131</u>	<u>9,774,878</u>	<u>(894,892)</u>	<u>—</u>	<u>257,650,117</u>
Less accumulated depreciation:					
Buildings and building improvements	(41,419,695)	(5,697,384)	—	—	(47,117,079)
Improvements, other than buildings	(11,842,952)	(920,321)	—	—	(12,763,273)
Infrastructure	(8,332,890)	(1,312,108)	—	—	(9,644,998)
Personal property:					
Equipment	(6,261,971)	(924,847)	748,883	—	(6,437,935)
Library books and materials	(7,679,885)	(494,154)	102,838	—	(8,071,201)
Intangible assets	<u>(1,232,280)</u>	<u>(673,154)</u>	<u>—</u>	<u>—</u>	<u>(1,905,434)</u>
Total accumulated depreciation	<u>(76,769,673)</u>	<u>(10,021,968)</u>	<u>851,721</u>	<u>—</u>	<u>(85,939,920)</u>
Net capital assets	\$ <u><u>172,000,458</u></u>	<u><u>(247,090)</u></u>	<u><u>(43,171)</u></u>	<u><u>—</u></u>	<u><u>171,710,197</u></u>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2008 and 2007

Capital assets activity for the year ended June 30, 2007 consisted of the following:

	<u>Balance, June 30, 2006</u>	<u>Additions</u>	<u>Retirements</u>	<u>Transfers</u>	<u>Balance, June 30, 2007</u>
Nondepreciable capital assets:					
Land and land improvements	\$ 10,981,328	—	—	—	10,981,328
Works of art and historical treasures	25,000	—	—	—	25,000
Construction work in progress	6,547,374	10,255,052	—	(14,002,241)	2,800,185
Total nondepreciable capital assets	<u>17,553,702</u>	<u>10,255,052</u>	<u>—</u>	<u>(14,002,241)</u>	<u>13,806,513</u>
Depreciable capital assets:					
Buildings and building improvements	163,089,364	14,806	—	7,845,981	170,950,151
Improvements, other than buildings	13,925,987	25,995	—	3,540,555	17,492,537
Infrastructure	21,212,923	—	—	2,615,705	23,828,628
Personal property:					
Equipment	13,123,241	884,339	(3,821,859)	—	10,185,721
Library books and materials	9,969,036	174,639	(34,999)	—	10,108,676
Intangible assets	1,786,077	611,828	—	—	2,397,905
Total depreciable capital assets	<u>223,106,628</u>	<u>1,711,607</u>	<u>(3,856,858)</u>	<u>14,002,241</u>	<u>234,963,618</u>
Total cost	<u>240,660,330</u>	<u>11,966,659</u>	<u>(3,856,858)</u>	<u>—</u>	<u>248,770,131</u>
Less accumulated depreciation:					
Buildings and building improvements	(35,984,851)	(5,434,844)	—	—	(41,419,695)
Improvements, other than buildings	(11,079,706)	(763,246)	—	—	(11,842,952)
Infrastructure	(7,303,479)	(1,029,411)	—	—	(8,332,890)
Personal property:					
Equipment	(8,669,105)	(1,350,900)	3,758,034	—	(6,261,971)
Library books and materials	(7,167,075)	(547,809)	34,999	—	(7,679,885)
Intangible assets	(984,655)	(247,625)	—	—	(1,232,280)
Total accumulated depreciation	<u>(71,188,871)</u>	<u>(9,373,835)</u>	<u>3,793,033</u>	<u>—</u>	<u>(76,769,673)</u>
Net capital assets	\$ <u>169,471,459</u>	<u>2,592,824</u>	<u>(63,825)</u>	<u>—</u>	<u>172,000,458</u>

For information regarding the capital assets of the individual discretely presented auxiliary organizations, refer to the separately issued auxiliary organizations' reports.

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Notes to Financial Statements

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(8) Lease Obligations

The University is obligated under various capital and operating leases and installment purchase agreements for the acquisition of equipment and facility rentals.

Capital leases consist primarily of leases of certain facilities and office equipment. Total capital assets related to capital leases have a carrying value of \$1,765,848 and \$1,318,357 at June 30, 2008 and 2007, respectively. Substantially all of these assets are pledged as security for the related leases. The leases bear interest an interest of 3.6% and have terms expiring in various years through 2015.

Operating leases consist primarily of leases for the use of real property and have terms expiring in various years through fiscal year 2013. The leases can be canceled if the State does not provide adequate funding.

Future minimum lease payments under capital and operating leases having remaining terms in excess of one year are as follows:

	<u>Capital leases</u>	<u>Operating leases</u>
Year ending June 30:		
2009	\$ 1,511,133	627,460
2010	1,145,391	331,595
2011	582,317	124,406
2012	441,315	100,255
2013	441,087	54,746
2014 – 2018	<u>615,893</u>	<u>—</u>
Total minimum lease payments	4,737,136	\$ <u><u>1,238,462</u></u>
Less amount representing interest	<u>(418,136)</u>	
Present value of future minimum lease payments	4,319,000	
Less current portion	<u>(1,382,000)</u>	
Capital lease obligations, net of current portion	\$ <u><u>2,937,000</u></u>	

Rent expense under operating leases for the years ended June 30, 2008 and 2007 totaled \$666,888 and \$643,329, respectively.

Lease financing is provided to the System for the construction of various System and campus facilities through its participation with the State in the State Public Works Board Lease Revenue Bond Program. Certain capital assets recorded by the University may have been financed under these arrangements. However, since the obligation for the repayment of this financing rests with the System and the proceeds of such financing are not readily identifiable with a campus or project, a substantial portion of such financing is not allocated to the individual campuses of the System. Unallocated Lease Revenue Bonds outstanding for the System as of June 30, 2008 and 2007 totaled \$536,727,000 and \$570,858,000, respectively.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2008 and 2007

(9) Long-Term Debt Obligations

(a) *General Obligation Bond Program*

The General Obligation Bond program of the State has provided capital outlay funds for the three segments of California Higher Education through voter-approved bonds. Each of the approved bond programs provides a pool of available funds, which is allocated on a project-by-project basis among the University of California, the System, and the Community Colleges. Financing provided to the University through State General Obligation Bonds is not allocated to the System by the State. This debt remains the obligation of the State and is funded by state tax revenues. Accordingly, such debt is not reflected in the accompanying financial statements. Total General Obligation Bond debt carried by the State related to System projects is approximately \$1,494,093,000 and \$1,393,141,000 as of June 30, 2008 and 2007, respectively.

(b) *Revenue Bond Programs*

The Revenue Bond Act of 1947 provides the Trustees with the ability to issue revenue bonds to fund five specific self-supporting programs and the health facilities program. The statute has enabled the Trustees to finance student housing, student unions, parking facilities, health facilities, continuing education facilities, and auxiliary organization facilities.

The housing program provides on-campus housing primarily for students. Housing is a self-supporting program deriving its revenues from fees collected for the use of the residence facilities. Funds are used for current operating expenses, maintenance and repair, improvements to facilities, and interest and principal payments on outstanding bonds. Available balances after payment of all operating expenses and required charges remain available for future program expenses and capital needs.

The student union program provides facilities and programs aimed at creating and enhancing learning experiences outside the classroom by promoting interaction among students, faculty, and staff. The student union program is self-supporting and derives its revenues primarily from student fees and interest income. Funds are used for maintenance and repair, and improvements to facilities, and interest and principal payments on outstanding bonds. After payment of all authorized charges, the balances of these funds are available for transfer to the campus auxiliary organization that has contracted with the University to operate the facility. The operating entity may derive additional revenue from facility subrental, recreational and commercial activities, and interest income.

The parking program provides parking facilities. The parking program is self-supporting and derives its revenues primarily from student fees and interest income. Funds are used for construction, repair and maintenance, and principal and interest payments on outstanding bonds. Available balances after payment of all operating expenses and required charges remain available for future program expenses and capital needs.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

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The health facilities program provides facilities on campus in which to provide health services to students. The health facilities program derives its revenues primarily from student fees and interest income. Funds are used for current operating expenses, maintenance and repair, improvements to facilities, and interest and principal payments on outstanding bonds. Available balances after payment of all operating expenses and required charges remain available for future program expenses and capital needs.

The continuing education program provides nonstate-supported courses to students. The continuing education program is self-supporting and derives its revenues primarily from student fees and interest income. Funds are used for current operating expenses, maintenance and repair, improvements to facilities, and interest and principal payments on outstanding bonds. Available balances after payment of all operating expenses and required charges remain available for future program expenses and capital needs.

The auxiliary organization program provides for certain additional facilities on campus for the benefit of students and staff. The auxiliary organization program derives its revenues primarily from lease income received by the campus from the auxiliary organization using the facility. Funds are used for current operating expenses, maintenance and repair, improvements to facilities, and interest and principal payments on outstanding bonds. Available balances after payment of all operating expenses and required charges remain available for future program expenses and capital needs.

The Systemwide Revenue Bond program, formerly the Housing Revenue Bond program, was approved by the Trustees in fiscal year 2003. This program provides funding for various construction projects, including student residence and dining halls facilities, continuing education buildings, student unions, parking facilities, health facilities, and auxiliary organization facilities at designated campuses within the System as specified by the individual bond documents. It is designed to provide lower cost debt and greater flexibility to finance revenue bond projects of the System. Rather than relying on specific pledged revenues to support specific debt obligations, this program pools several sources of revenue as the pledge for the revenue-producing projects.

The System has pledged future continuing education, healthcare facilities, housing, parking, and student union revenues, plus designated auxiliary revenues, net of maintenance and operation expenses before extraordinary items (net income available for debt service), to repay \$2,804,033,000 in Systemwide Revenue Bonds issued through fiscal year 2008. The bonds are payable solely from continuing education, healthcare facilities, housing, parking, student union, and designated auxiliary net income available for debt service and are payable through fiscal year 2044/2045. The Systemwide Revenue Bond indenture requires net income available for debt service to be at least equal to aggregate debt service for all bond indebtedness each fiscal year. The total debt service remaining to be paid on the bonds for the System is \$4,939,829,000. In fiscal year 2008, total debt service paid, which excluded the designated auxiliary net income, and net income available for debt service for the System were \$148,395,000 and \$213,695,000, respectively.

The System's total outstanding balance of revenue bond indebtedness under the Systemwide Revenue Bond program was \$2,706,828,000 and \$2,302,428,000 at June 30, 2008 and 2007, respectively. The University's portion of the total outstanding balance under this program was \$29,930,000 and \$30,305,000 at June 30, 2008 and 2007, respectively.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2008 and 2007

Senior to the Systemwide Revenue Bonds are the Student Union Revenue Bonds Series A, B, and C. At June 30, 2008 and 2007, the System's outstanding balance for these senior bonds totaled \$0 and \$68,550,000, respectively. The University had no outstanding balances for these senior bonds.

Revenue Bond Anticipation Notes

The Trustees have authorized the issuance of Revenue Bond Anticipation Notes (BANs) to provide short-term financing to the System for certain projects. The BANs are issued to the California State University Institute, an auxiliary organization of the System, to secure the issuance of its commercial paper. The BANs are generally issued for periods of up to three years in anticipation of issuing permanent revenue bonds at a future date. The University had no BANs outstanding at June 30, 2008 and 2007, respectively.

(c) ***Koch Financial Corporation***

The Koch Financial Corporation debt obligation was established to fund the building of a Thermal Energy Storage Tank in a cooperative effort with San Diego Gas & Electric in an effort to promote energy conservation and provide the University with energy savings costs. Additionally, the University has entered into several debt agreements with Koch Financial Corporation to finance the University's computer refresh program.

(d) ***CSUSM Foundation SBRI Loan***

During the prior year, the University entered into an agreement with the California State University, San Marcos (CSUSM) Foundation to guarantee a loan for the Social and Behavioral Research Institute (SBRI). Since it has been determined that SBRI's financial viability was negatively affected by a changing survey industry environment, the University decided to close SBRI and it ceased operations as of July 1, 2007. The University repaid the balance of the loan of \$395,300 in October 2007.

(e) ***DLL Public Financing LLC***

The DLL Public Financial LLC debt obligation was established to fund the necessary upgrades to accommodate the University's growing energy needs and provide the University with energy cost savings. The energy conservation project includes improvements to the University's central plant as well as upgrades to the University's lighting and heating and air conditioning systems.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2008 and 2007

Long-term debt obligations of the University as of June 30 consist of the following:

Description	Interest rate	Fiscal year maturity date	Original issue amount	Amount outstanding at June 30	
				2008	2007
Systemwide Revenue Bonds:					
2002A – Student Union	4.00% – 5.50%	2033	\$ 5,665,000	5,200,000	5,300,000
2005A – Auxiliary Org	2.75% – 5.00%	2033	25,230,000	24,730,000	25,005,000
Other:					
Koch Financial Corporation		2012	2,000,000	756,369	878,067
Koch Financial Corporation		2010	495,936	211,582	311,178
Koch Financial Corporation		2007	1,427,885	—	477,142
CSUSM Foundation/SBRI Loan		2011	—	—	295,300
DLL Public Financing LLC		2024	7,831,000	7,831,000	—
GE Capital		2008	129,646	2,617	13,665
Total				38,731,568	32,280,352
Total long-term debt				38,731,568	32,280,352
Less current portion				(868,449)	(1,378,918)
Long-term debt, net of current portion				\$ 37,863,119	30,901,434

Long-term debt principal obligations and related interest mature in the following fiscal years:

	Principal	Interest	Total
Year ending June 30:			
2009	\$ 868,449	1,854,815	2,723,264
2010	1,136,045	1,815,306	2,951,351
2011	1,123,126	1,765,221	2,888,347
2012	1,224,308	1,713,756	2,938,064
2013	1,326,736	1,660,988	2,987,724
2014 – 2018	6,987,490	7,333,705	14,321,195
2019 – 2023	9,240,414	5,444,824	14,685,238
2024 – 2028	7,365,000	3,323,987	10,688,987
2029 – 2033	9,460,000	1,228,750	10,688,750
	\$ 38,731,568	26,141,352	64,872,920

Long-term debt obligations of the discretely presented auxiliary organizations have been issued to purchase or construct facilities for University-related uses. For information regarding the long-term debt obligations of the individual discretely presented auxiliary organizations, refer to the separately issued auxiliary organizations' reports.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2008 and 2007

(10) Advance Refundings

(a) Current Year Refundings

The University had no current year refundings.

(b) Prior Years' Refundings

In prior years, the University defeased certain bonds of the discretely presented auxiliary organizations (refunded bonds) by placing the proceeds from the issuance of the Systemwide Revenue Bonds Series 2005A refunding bonds in an irrevocable trust with the State Treasurer to provide for all future debt service payments on the refunded bonds. The proceeds from the refunding bonds were used to purchase U.S. government securities that were placed in the trust fund. The investments and fixed earnings from the investments are considered sufficient to fully service the defeased debt until the debt is called or matures. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the University's financial statements. The amount of prior years' defeased bonds outstanding as of June 30, 2008 totaled \$24,730,000.

(11) Long-Term Liabilities Activity

Long-term liabilities activity for the year ended June 30, 2008 was as follows:

	<u>Beginning balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending balance</u>	<u>Current portion</u>
Accrued compensated absences	\$ 3,747,691	2,277,311	(1,808,363)	4,216,639	2,021,027
Capitalized lease obligations (note 8)	2,903,000	2,497,000	(1,081,000)	4,319,000	1,382,000
Long-term debt obligations (note 9):					
2002A Systemwide revenue bonds (Student Union)	5,300,000	—	(100,000)	5,200,000	110,000
2005A Systemwide revenue bonds (Auxiliary Org)	25,005,000	—	(275,000)	24,730,000	330,000
Koch Financial Corporation	878,067	—	(121,698)	756,369	135,984
Koch Financial Corporation	311,178	—	(99,596)	211,582	103,671
Koch Financial Corporation	477,142	—	(477,142)	—	—
CSUSM Foundation/SBRI Loan	295,300	—	(295,300)	—	—
DLL Public Financing LLC	—	7,831,000	—	7,831,000	186,177
GE Capital	13,665	—	(11,048)	2,617	2,617
	<u>32,280,352</u>	<u>7,831,000</u>	<u>(1,379,784)</u>	<u>38,731,568</u>	<u>868,449</u>
Total long-term debt obligations					
Total long-term liabilities	\$ <u>38,931,043</u>	<u>12,605,311</u>	<u>(4,269,147)</u>	<u>47,267,207</u>	<u>4,271,476</u>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

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June 30, 2008 and 2007

Long-term liabilities activity for the year ended June 30, 2007 was as follows:

	<u>Beginning balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending balance</u>	<u>Current portion</u>
Accrued compensated absences	\$ 3,276,306	2,078,443	(1,607,058)	3,747,691	1,808,363
Capitalized lease obligations (note 8)	506,000	2,822,000	(425,000)	2,903,000	704,000
Long-term debt obligations (note 9):					
2002A Systemwide revenue bonds (Student Union)	5,395,000	—	(95,000)	5,300,000	100,000
2005A Systemwide revenue bonds (Auxiliary Org)	25,230,000	—	(225,000)	25,005,000	275,000
Koch Financial Corporation	878,067	—	—	878,067	121,698
Koch Financial Corporation	395,762	—	(84,584)	311,178	99,596
Koch Financial Corporation	338,060	—	(338,060)	—	—
Koch Financial Corporation	936,905	—	(459,763)	477,142	477,142
GE Capital	33,007	—	(19,342)	13,665	10,182
CSUSM Foundation/SBRI Loan	350,000	—	(54,700)	295,300	295,300
Total long-term debt obligations	<u>33,556,801</u>	<u>—</u>	<u>(1,276,449)</u>	<u>32,280,352</u>	<u>1,378,918</u>
Total long-term liabilities	<u>\$ 37,339,107</u>	<u>4,900,443</u>	<u>(3,308,507)</u>	<u>38,931,043</u>	<u>3,891,281</u>

(12) Pension Plan and Postretirement Benefits

(a) Pension Plan

Plan Description

The University, as an agency of the State, contributes to CalPERS. The State's plan with CalPERS is an agent multiple-employer defined benefit retirement plan and CalPERS functions as an investment and administrative agent for its members. For the University, the plan acts as a cost-sharing, multiple-employer defined benefit pension plan, which provides a defined benefit pension and postretirement program for substantially all eligible University employees.

CalPERS provides benefits based on members' years of service, age, and final compensation. In addition, benefits are provided for disability and death and payments to survivors or beneficiaries of eligible members. Membership is mandatory for those University employees employed full-time for a period of six months or part-time for a period of one year in duration. Members are eligible to retire at the age specified in their benefit formulas. University members become fully vested in their retirement benefits after five years of credited service.

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All University retirees that retire within 120 days of their separation from employment, have been eligible for enrollment in a CalPERS medical plan on their date of separation, and receive a retirement allowance from CalPERS are eligible for retirement health benefits through CalPERS, which include medical and dental coverage. The retiree's family members can also be covered by the plan and eligible dependents include his or her spouse, domestic partner, children under age 23 and never married, and disabled children over age 23. The monthly out-of-pocket enrollment cost to the retiree for medical coverage will depend on which plan and the level of coverage the retiree chooses.

CalPERS issues a publicly available comprehensive annual financial report that includes financial statements and required supplementary information. Copies of the CalPERS annual financial report may be obtained from the California Public Employees' Retirement System Executive Office – 400 P Street – Sacramento, California 95814.

Funding Policy

The benefit structure for state employees (including the University) is defined by statute. CalPERS uses contributions of the employer and the employee as well as income from investments to pay for employee retirement benefits. Employee and employer contributions are a percentage of applicable employee compensation. The employee contribution is 5.00% of salary for Miscellaneous Tier 1 members as defined by the Plan and 8.00% for Peace Officer/Firefighter members (Public Safety Management and Firefighters only) less an exclusion allowance for coordination with Social Security. For eligible University Public Safety employees, the University pays for both the employer and employee contributions. The University is required to contribute at an actuarially determined rate; the current rate is approximately 16.67% of annual covered payroll. The contribution requirements of the plan members are established and may be amended by CalPERS. There is no contractual maximum contribution required for the University by CalPERS.

The University's contributions to CalPERS for the most recent three fiscal years were equal to the required contributions and were as follows:

2006	\$	6,615,415
2007		7,924,685
2008		8,727,777

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(b) *Postretirement Healthcare Plan*

The GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, relating to Other Postemployment Benefits (OPEB), which is effective July 1, 2007. Under this Statement, public employers sponsoring and subsidizing retiree healthcare benefit programs are required to recognize the cost of such benefits on an accrual basis.

Plan Description

The State provides retiree healthcare benefits to statewide employees, including University employees, through the programs administered by the California Public Employees Retirement System (CalPERS). The State's substantive plan represents a single-employer defined benefit OPEB plan which includes medical and prescription drug benefits (collectively healthcare benefits) to the retired University employees. The System provides dental benefits to eligible University's retirees. Eligible retirees receive healthcare and dental benefits upon retirement at age 50 with five years of service credit.

For healthcare benefits, CalPERS offers Preferred Provider Organizations (PPOs), Health Maintenance Organizations (HMOs), and Exclusive Provider Organizations (EPOs) (limited to members in certain California counties); for dental benefits, a Dental Maintenance Organization (DMO) and dental indemnity plans to the University's retirees. Health plans offered, covered benefits, monthly rates, and copayments are determined by the CalPERS Board, which reviews health plan contracts annually.

The contribution requirements of retirees and the State are established and may be amended by the State legislature. For healthcare benefits, the State makes a contribution towards the retiree's monthly health premiums, with the retirees covering the difference between the State's contribution and the actual healthcare premium amount. The State contribution is normally established through collective bargaining agreements. No retiree contribution is required for dental benefits.

Funding Policy

For healthcare benefits, responsibility for funding the cost of the employer share of premiums is apportioned between the State and the System based on "billable" and "nonbillable" accounts. Billable accounts have special revenue sources such as fees, licenses, penalties, assessments, interest, which offset the costs incurred by a State department during the year. The System reimburses the State for retiree's health benefit costs allocated to billable accounts but not for costs allocated to nonbillable accounts. The System is responsible for funding the costs of the billable accounts on a pay-as-you-go basis as part of the statewide general administrative costs charged to the System. The University then reimburses the System for its share of healthcare premiums for all billable funds based on annual retirement expenses.

The State is responsible for funding the cost of the employer share of healthcare premiums of retirees for all nonbillable accounts.

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The System is responsible for funding the cost of dental benefits for all University retirees. The System makes payments directly to Delta Dental for the retiree's monthly dental premiums. The System is funding these benefits on a pay-as-you-go basis. The University does not pay the System for its share of dental premiums.

Annual OPEB Cost and Net OPEB Obligation

In fiscal year 2008, total annual OPEB cost (ARC) and net OPEB obligation (NOO) for the System were \$51.2 million and \$29.1 million respectively, which include the OPEB for the billable accounts and the dental benefit only for the nonbillable accounts. The accrued OPEB liability and expense for the System are not allocated and are therefore not a liability to the University. Refer to the issued System's consolidated financial report for fiscal year ended 2008 for more details.

Actuarial Methods and Assumptions and Plan Funding Information

As an agency of the State, the University was included in the State's OPEB actuarial study. The analysis of the statewide ARC by accounts is performed by the State Controller's Office (SCO) and allocated to the System. The dental portion of the ARC for the nonbillable accounts was estimated based on the percentage of dental contributions compared to the total contributions. Funding progress information specifically related to the System's portion of the statewide OPEB plan is not available. For more details about the actuarial methods and assumptions used by the State as well as the statewide plans funding progress and status, refer to the State of California's Comprehensive Annual Financial Report (CAFR) for the fiscal year ended 2008.

(13) Self-Insurance Program

The System and certain auxiliary organizations have established a public entity risk pool, California State University Risk Management Authority (CSURMA), a blended component unit of the System, to manage centrally workers' compensation, industrial and nonindustrial disability, and general organizational risks. The System's self-insurance claims liability includes estimated amounts that will be required for future payments of claims that have been reported and claims related to events that have occurred but not been reported. The estimated liability is actuarially determined using individual case basis valuations and statistical analyses. Although considerable variability is inherent in such estimates, management believes that the liability is a reasonable estimate at June 30, 2008 and 2007.

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Changes in the System's self-insurance claims liability for the two years ended June 30, 2008 are as follows:

Liability at June 30, 2006	\$ 112,376,000
Incurred claims and changes in estimates	35,794,000
Claim payments	<u>(39,978,000)</u>
Liability at June 30, 2007	108,192,000
Incurred claims and changes in estimates	28,487,000
Claim payments	<u>(32,682,000)</u>
Liability at June 30, 2008	103,997,000
Less current portion	<u>(25,480,000)</u>
Long-term liability at June 30, 2008, net of current portion	<u>\$ 78,517,000</u>

For the year ended June 30, 2008, the CSURMA purchased a program of excess insurance to protect the members from catastrophic losses. The CSURMA maintained excess public entity liability insurance coverage provided by Schools Excess Liability Fund (SELF), a Joint Powers Authority, with coverage for individual claims above \$5,000,000 and up to \$45,000,000 per occurrence. The CSURMA purchases excess workers' compensation insurance provided by the National Union Fire Insurance Company of Pittsburgh, Pennsylvania (AIG) to statutory limits in excess of \$2,500,000 self-insured retention. There have been no settlements in the most recent three fiscal years that have exceeded insurance limits. Although the CSURMA maintains excess policies with SELF, AIG, and other insurers, the ultimate responsibility for payment of claims resides with the CSURMA.

Prior to July 1, 2004, the CSURMA maintained excess workers' compensation insurance coverage provided by SELF. The CSURMA remains liable for assessments from SELF in settlement of claims incurred prior to July 1, 2004. For the years ended June 30, 2008 and 2007, this assessment totaled \$19,834,000 and \$17,509,000, respectively.

Premiums charged to each of the pool participants are based on historical trend information and the pool participant's estimated share of the CSURMA self-insurance claims liabilities. The University's allocation of the System's total self-insurance claims liability as of June 30, 2008 and 2007 was approximately 2% or \$1,853,000 and \$1,987,000, respectively. This allocation reflects the University's estimated share of the ultimate cost of settling claims relating to events that have occurred on or before June 30, 2008 and 2007. Any future fluctuations in the University's estimated share of the self-insurance claims liability will be reflected in subsequent premiums charged to the University for its participation in CSURMA.

The University's receivable from CSURMA totaled \$0 and \$1,564,224 at June 30, 2008 and 2007, respectively, which is recorded as a component of prepaid expenses and other assets in the accompanying statements of net assets. As of June 30, 2008, there is no amount due to or from CSURMA.

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(14) Commitments and Contingencies

Federal grant programs are subject to review by the grantor agencies, which could result in requests for reimbursement to grantor agencies for disallowed expenditures. Management believes that it has adhered to the terms of its grants and that any disallowed expenditures resulting from such review would not have a material effect on the financial position of the University.

Contractual commitments for construction projects unexpended as of June 30, 2008 and 2007 totaled \$6,755,147 and \$2,454,741, respectively. These expenditures will be funded primarily from state appropriations.

The University is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the University's financial position, changes in net assets, or liquidity.

(15) Classification of Operating Expenses

The University has elected to report operating expenses by functional classification in the statements of revenues, expenses, and changes in net assets, but to provide the natural classification of those expenses as an additional disclosure. For the years ended June 30, 2008 and 2007, operating expenses by natural classification consisted of the following:

<u>2008</u>	<u>Salaries</u>	<u>Benefits</u>	<u>Scholarships and fellowships</u>	<u>Supplies and other services</u>	<u>Depreciation and amortization</u>	<u>Total</u>
Functional classification:						
Instruction	\$ 28,555,015	9,439,288	—	3,517,580	—	41,511,883
Research	120,678	40,506	—	14,553	—	175,737
Public service	150,454	50,223	—	23,843	—	224,520
Academic support	9,262,998	3,404,639	—	2,472,050	—	15,139,687
Student services	6,734,549	2,497,336	—	1,958,012	—	11,189,897
Institutional support	9,987,700	3,667,304	—	4,348,197	—	18,003,201
Operation and maintenance of plant	3,872,816	1,590,390	—	6,016,375	—	11,479,581
Student grants and scholarships	—	—	11,791,180	—	—	11,791,180
Auxiliary enterprises expenses	1,372,166	601,934	—	1,169,984	—	3,144,084
Depreciation and amortization	—	—	—	—	10,021,968	10,021,968
Total	\$ <u>60,056,376</u>	<u>21,291,620</u>	<u>11,791,180</u>	<u>19,520,594</u>	<u>10,021,968</u>	<u>122,681,738</u>

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<u>2007</u>	<u>Salaries</u>	<u>Benefits</u>	<u>Scholarships and fellowships</u>	<u>Supplies and other services</u>	<u>Depreciation</u>	<u>Total</u>
Functional classification:						
Instruction	\$ 24,494,814	8,306,266	—	4,078,687	—	36,879,767
Research	215,218	75,733	—	23,655	—	314,606
Public service	200,810	45,199	—	36,691	—	282,700
Academic support	9,574,073	3,496,688	—	2,606,850	—	15,677,611
Student services	6,358,683	2,285,366	—	2,329,394	—	10,973,443
Institutional support	7,952,894	2,779,458	—	3,297,394	—	14,029,746
Operation and maintenance of plant	3,453,382	1,406,843	—	5,224,576	—	10,084,801
Student grants and scholarships	—	—	10,363,981	—	—	10,363,981
Auxiliary enterprises expenses	1,154,179	477,245	—	1,068,691	—	2,700,115
Depreciation	—	—	—	—	9,373,835	9,373,835
Total	\$ 53,404,053	18,872,798	10,363,981	18,665,938	9,373,835	110,680,605

As discussed in note 2(n), the internal services activities between the University departments and the sales and service units have been eliminated in the accompanying financial statements. As a result, salaries and benefits of those internal services activities and sales and service units are reported as supplies and other services in the University departments, that received the services.

(16) Transactions with Related Entities

The System is an agency of the State and receives more than half of its total revenues through State appropriations. While its operating expenses are paid out of the State University Trust Fund through commercial banks as a result of the Revenue Management Program implemented in fiscal year 2007, payroll and capital outlay activities are processed through the Office of the California State Controller. State appropriations, both noncapital and capital, allocated to the University through the Office of the Chancellor aggregated \$123,158,786 and \$61,270,313 for the years ended June 30, 2008 and 2007, respectively. State appropriations receivable aggregated \$55,262,346 and \$2,758,000 at June 30, 2008 and 2007, respectively. The University also received lottery fund distributions from the State in the amount of \$469,000 and \$642,636 for the years ended June 30, 2008 and 2007, respectively, which is included in other nonoperating revenues (expenses) in the accompanying statements of revenues, expenses, and changes in net assets.

Included in other nonoperating revenues (expenses), net, are \$369,450 of revenue from the Office of the Chancellor for the Infrastructure Terminal Resources Project.

Moreover, the State recovers statewide general administrative costs (i.e., indirect costs incurred by central service agencies) from the University. Central service agencies (e.g., Department of Finance, Office of the State Controller, State Personnel Board, and Legislature) provide budgeting, accounting, auditing, payroll, and other services to all state agencies. The State's pro rata process apportions the costs of providing central administrative services to all state departments that benefit from the services. This apportioned amount is further allocated to each state department's funding sources based on the percentage of total expenditures in each fund. The amount allocated to each fund is classified as "billable" accounts or "nonbillable" accounts. Billable accounts (1) have special revenue sources such as fees, licenses, penalties, assessments, interest, etc. and (2) support a state department.

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The State's indirect costs associated with the billable funds are allocated to the individual universities through the Office of the Chancellor of the System. As headquarters for the System, the Office of the Chancellor administers not only the State pro rata charges, but also management of capital projects, and pooled investments centrally for the individual campuses and charges the campuses administrative or overhead fees. These fees are included in the various functional categories of operating expenses in the accompanying statements of revenues, expenses, and changes in net assets. Other activities such as debt administration and risk pool administration associated with the operations of the Office of the Chancellor are not allocated to the individual universities' financial statements.

As discussed in notes 7 and 8, the University has recorded capital assets that have been financed by the System or the State's obligations that are not reflected in the accompanying financial statements. For the years ended June 30, 2008 and 2007, no such additions of capital assets are included in the accompanying financial statements.

The accompanying financial statements also include the following transactions with discretely presented auxiliary organizations and other related parties as of and for the years ended June 30, 2008 and 2007:

	<u>2008</u>	<u>2007</u>
Reimbursements from recognized auxiliary organizations for salaries of University employees working on contracts, grants, and other programs	\$ 911,608	505,562
Reimbursements from recognized auxiliary organizations for other than salaries of University employees	5,545,386	4,503,680
Payments to recognized auxiliary organizations for services, office space rental, and programs	1,687,681	1,554,678
Payments to the Office of the Chancellor for State pro rata charges	179,938	—
Amounts receivable from the Office of the Chancellor	14,268	2,623
Amounts payable to the Office of the Chancellor	308,696	43,606
Accounts receivable from campuses (other than CO)	31,804	71,533
Amounts payable to campuses (other than CO)	42,288	71,935
Amounts receivable from recognized auxiliary organizations	574,712	474,677
Amounts payable to recognized auxiliary organizations	40,671	98,585
State lottery appropriations received	469,000	642,636

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(17) Subsequent Event

In July 2008, a \$36.3 million BAN was authorized for the University's parking structure. In August 2008, \$10.8 million of commercial paper was issued, leaving an unissued amount of commercial paper of \$25.5 million.

In September 2008, the University entered into a capital lease agreement to participate in the capital financing program of the California State University Institute. The program is funded by commercial paper. The \$1.5 million will be used to fund the University's annual computer refresh program.

Recent market conditions have resulted in an unusually high degree of volatility and increased risks associated with investments. As of June 30, 2008, the University's investments were invested 95% in the California State University's Investment Pool and 5% in the State of California's Surplus Money Investment Fund (SMIF). Permitted investments consist primarily of highly rated, fixed-income securities, which could include variable rate instruments. Both the California State University's investment policy and the State of California's SMIF investment policy state that the primary objective of the University's investments shall be the safeguarding of principal, with liquidity a secondary objective. Because of this emphasis on asset quality and liquidity, the University has not had, nor expect to have, any material exposure to the value of investments as a result of illiquidity or volatility in certain investment sectors of the financial markets.

Although neither investment pool has experienced significant declines in the value of the component investment securities since June 30, 2008, it is at least reasonably possible that some changes in the values of investment securities could occur because of changing market conditions.

American Institute of Certified Public Accounts Governmental Audit Quality Center issued alert #91 indicating that, effective September 29, 2008, the liquidity in the Common Fund Short Term Fund (Fund) is substantially restricted. The following auxiliary, California State University, San Marcos has investments in the Fund. The amount in the Fund as of September 28, 2008 is \$61,268. This restriction on liquidity has had no impact on operations.

Due to the State's budget crisis and its difficulty in issuing bonds in the current financial market, the State of California issued a Budget Letter on December 18, 2008, suspending all State-funded capital projects, including General Obligation and Lease Revenue bond projects, and freezing disbursements on these projects beginning December 17, 2008. Capital projects that are financed by non-State sources, such as the Systemwide Revenue Bonds, are not affected by this suspension. Campuses continue to assess the costs of suspending these construction contracts, including any related legal costs or penalties incurred to suspend the projects. These costs, as well as any restart costs, will be paid from a project's contingency allowance, through a reduction in scope and/or augmentation approved by the State Public Works Board, and from other funding sources, where applicable.