John Keel, CPA
State Auditor

Accreditation Reviews Fiscal Year 2008

June 2009

Report No. 09-335

Introduction

The State Auditor’s Office completed accreditation reviews of four higher education institutions’ fiscal year 2008 financial statements:

- Lamar University.
- Sam Houston State University.
- Texas Tech University Health Sciences Center.
- The University of Texas Southwestern Medical Center at Dallas.

These reviews are performed to comply with the accreditation reaffirmation requirements of the Southern Association of Colleges and Schools. <u>The reports included in this document were prepared by the higher education institutions</u>, but they include the following documents issued by the State Auditor’s Office:

- Auditor’s Review Report.
- A management letter.

A review consists principally of inquiries of personnel and analytical procedures applied to financial data. A review is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, the State Auditor’s Office did not express such opinions.

LAMAR UNIVERSITY

A Member of the Texas State University System

BEAUMONT, TEXAS

Southern Association of Colleges and Schools Review

For the Year Ended August 31, 2008

LAMAR UNIVERSITY
SACS Review
For the Year Ended August 31, 2008

Contents

State Auditor's Office
John Keel, CPA
State Auditor

Auditor's Review Report

May 21, 2009

Dr. James M. Simmons, President
Lamar University
P.O. Box 1001
Beaumont, TX 77710

Dear Dr. Simmons:

We have reviewed the accompanying Statement of Net Assets; Statement of Revenues, Expenses, and Changes in Net Assets; Statement of Cash Flows; and Notes to the Financial Statements of Lamar University (University) as of and for the fiscal year ended August 31, 2008, in accordance with *Statements on Standards for Accounting and Review Services* issued by the American Institute of Certified Public Accountants. The review was performed in accordance with the Southern Association of Colleges and Schools' (Southern Association) *Criteria for Accreditation*. All information included in these financial statements is the representation of management of the University.

A review consists principally of inquiries of University personnel and analytical procedures applied to financial data. A review is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

The accompanying statements were prepared to present the financial position, the changes in financial position and the cash flows of the University. These statements are prepared pursuant to criteria of the Southern Association for supplementary special reports by institutions in states that conduct statewide audits.

Based on our review, with the exception of the matter described in the following paragraph, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with generally accepted accounting principles.

The University has not presented a management's discussion and analysis section that the Governmental Accounting Standards Board has identified as required supplementary information that is not part of the basic financial statements. However, such required supplementary information for the Texas State University System (System) is presented in the System's consolidated annual financial report.

This report is intended for use by the Board of Regents of the System, management of the University, and the Southern Association. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

Sincerely,

John Keel, CPA
State Auditor

Robert E. Johnson Building
1501 N. Congress Avenue
Austin, Texas 78701

P.O. Box 12067
Austin, Texas 78711-2067

Phone:
(512) 936-9500

Fax:
(512) 936-9400

Internet:
www.sao.state.tx.us

LAMAR UNIVERSITY

Statement of Net Assets

For the Fiscal Year Ended August 31, 2008
(See Auditor's Review Report on page 1.)

ASSETS		
Current Assets		
Cash and Cash Equivalents (Note 3)	$	30,547,608
Restricted:		
Cash and Cash Equivalents (Note 3)		5,053,399
Legislative Appropriations		16,549,318
Receivables, Net of Allowances:		
Federal		3,716,929
Interest and Dividends		33,330
Accounts		17,379,388
Other		1,306,779
Due from Other State Entities (Note 9)		212,109
Consumable Inventories		185,260
Merchandise Inventories		112,913
Prepaid Expenses		7,547,799
Total Current Assets	$	82,644,832
Non-Current Assets		
Restricted:		
Cash and Cash Equivalents (Note 3)	$	18,947,254
Gifts Receivable		4,219,248
Investments (Note 3)		8,208,674
Capital Assets (Note 2):		
Non-Depreciable		35,790,801
Depreciable		252,731,431
Less: Accumulated Depreciation		(146,410,423)
Total Non-Current Assets	$	173,486,985
Total Assets	$	256,131,817
LIABILITIES		
Current Liabilities		
Payables:		
Accounts	$	3,764,222
Payroll		8,982,032
Due to Other State Entities (Note 9)		8,568,541
Deferred Revenue		36,874,940
Employees' Compensable Leave (Note 5)		242,207
Funds Held for Others		217,300
Other Current Liabilities		70,680
Total Current Liabilities	$	58,719,922

Non-Current Liabilities		
Employees' Compensable Leave (Note 5)		2,179,865
Other Non-Current Liabilities		636,126
Total Non-Current Liabilities	$	2,815,991
Total Liabilities	$	61,535,913
NET ASSETS		
Invested in Capital Assets, Net of Related Debt	$	142,111,809
Restricted for:		
Non-Expendable		
Permanent Funds, True Endowments, Annuities		10,664,364
Expendable		
Other		14,644,586
Unrestricted		27,175,145
Total Net Assets	$	194,595,904

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

LAMAR UNIVERSITY

Statement of Revenues, Expenses, and Changes in Net Assets

For the Fiscal Year Ended August 31, 2008
(See Auditor's Review Report on page 1.)

OPERATING REVENUES		
Tuition and Fees - Non-Pledged	$	69,372,983
Discounts and Allowances		(8,958,991)
Auxiliary Enterprises - Non-Pledged		5,330,583
Discounts and Allowances		(2,766,496)
Other Sales of Goods and Services - Non-Pledged		1,222,366
Federal Revenue		19,271,952
State Grant Revenue		3,836,949
Other Operating Grant Revenue		1,020,238
Other Operating Revenues		2,961,567
Total Operating Revenues	$	91,291,151
OPERATING EXPENSES		
Salaries and Wages		65,269,540
Payroll Related Costs		12,846,988
Professional Fees and Services		13,030,635
Travel		2,082,097
Materials and Supplies		15,911,634
Communications and Utilities		298,734
Repairs and Maintenance		2,773,196
Rentals and Leases		581,995
Printing and Reproduction		735,797
Depreciation and Amortization		5,771,949
Scholarships		13,628,094
Other Operating Expenses		6,917,689
Total Operating Expenses	$	139,848,348
Operating Income (Loss)	$	(48,557,197)
NONOPERATING REVENUES (EXPENSES)		
Legislative Appropriations	$	42,105,891
Gifts		3,023,319
Interest and Investment Income (Loss)		2,120,935
Net Increase (Decrease) in Fair Value of Investments		(921,845)
Other Nonoperating Revenues - Non-Pledged		225,490
Total Nonoperating Revenues (Expenses)	$	46,553,790
Income (Loss) Before Other Revenues, Expenses, Gains (Losses), and Transfers	$	(2,003,407)
OTHER REVENUES, EXPENSES, GAINS (LOSSES), AND TRANSFERS		
Capital Appropriations (HEAF)		11,210,508
Transfers Out to Other State Entities (Note 9)		(8,938,793)

Legislative Transfers In (Note 9)		6,546,484
Legislative Transfers Out (Note 9)		(5,105,976)
Legislative Appropriations Lapsed		(69,511)
Total Other Revenues, Expenses, Gains (Losses), and Transfers	$	3,642,712
CHANGE IN NET ASSETS	$	1,639,305
Net Assets, September 1, 2007	$	192,956,599
Restatements (Note 16)		
Net Assets, September 1, 2007, as Restated	$	192,956,599
NET ASSETS, August 31, 2008	$	194,595,904

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

LAMAR UNIVERSITY

Statement of Cash Flows

For the Fiscal Year Ended August 31, 2008
(See Auditor's Review Report on page 1.)

CASH FLOWS FROM OPERATING ACTIVITIES		
Proceeds from Tuition and Fees	$	64,275,571
Receipts from Customers		1,304,125
Proceeds from Research Grants and Contracts		4,857,186
Proceeds from Loan Programs		227,357
Proceeds from Auxiliaries		2,564,087
Proceeds from Other Revenues		18,812,057
Payments to Suppliers for Goods and Services		(29,458,259)
Payments to Employees for Salaries		(65,269,540)
Payments to Employees for Benefits		(14,296,871)
Payments for Loans Provided		739,914
Payments for Other Expenses		(26,317,731)
Net Cash Provided (Used) by Operating Activities	$	(42,562,104)
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Proceeds from Legislative Appropriations	$	37,216,771
Proceeds from Gifts		3,023,320
Proceeds from Endowments		2,120,935
Proceeds of Transfers from Other Entities		(985)
Payments for Transfers to Other Entities		(7,133,942)
Payments for Other Uses		
Net Cash Provided (Used) by Non-Capital Financing Activities	$	35,226,099
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from State Appropriations (HEAF)	$	11,210,508
Proceeds from Disposal of Capital Assets		21,125
Payments for Additions to Capital Assets		(5,743,180)
Net Cash Provided (Used) by Capital and Related Financing Activities	$	5,488,453
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from Interest and Investment Income	$	4,769,555
Net Cash Provided (Used) by Investing Activities	$	4,769,555
Net Increase (Decrease) in Cash and Cash Equivalents	$	2,922,003
Cash and Cash Equivalents, September 1, 2007	$	51,626,258
Restatements		
Cash and Cash Equivalents, September 1, 2007, as restated	$	51,626,258

Cash and Cash Equivalents, August 31, 2008	$	54,548,261
Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities		
Operating Income (Loss)	$	(48,557,197)
Adjustments:		
Depreciation and Amortization	$	5,771,949
Operating Income and Cash Flow Categories:		
Classification Differences		
Changes in Assets and Liabilities:		
(Increase) Decrease in Receivables		(9,423,685)
(Increase) Decrease in Due from Other Entities		(22,672)
(Increase) Decrease in Inventories		(6,629)
(Increase) Decrease in Prepaid Expenses		662,988
(Increase) Decrease in Notes Receivable		227,357
(Increase) Decrease in Other Assets		491,715
(Increase) Decrease in State Appropriations		(925,263)
Increase (Decrease) in Payables		(146,882)
Increase (Decrease) in Deposits		81,759
Increase (Decrease) in Due to Other Entities		(55,506)
Increase (Decrease) in Deferred Revenue		5,343,492
Increase (Decrease) in Employees' Compensable Leave		632,214
Increase (Decrease) in Other Liabilities		3,364,256
Total Adjustments	$	5,995,093
Net Cash Provided (Used) by Operating Activities	$	(42,562,104)
Non-Cash Transactions		
Net Increase (Decrease) in Fair Value of Investments	$	(921,845)

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

LAMAR UNIVERSITY

Statement of Changes in Unrestricted Net Assets

For the Fiscal Year Ended August 31, 2008

	8/31/2008	8/31/2007	Difference
Reserved			
Encumbrances	$ 2,075,181	$ 3,693,890	$ (1,618,709)
Accounts Receivable	16,264,710	9,343,798	6,920,912
Inventories	298,172	291,543	6,629
Higher Education Assistance Funds	14,794,718	7,163,967	7,630,751
Funds Functioning as Endowment - Unrestricted	22,376	22,376	0
Other	(440,106)	7,762,648	(8,202,754)
Unallocated	(5,839,906)		(5,839,906)
Total Unrestricted Net Assets	$ 27,175,145	$ 28,278,222	$ (1,103,077)

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

(See Auditor's Review Report on page 1.)

General Introduction

This report has been prepared for the use of the Southern Association of Colleges and Schools (Southern Association) in connection with the review of Lamar University (University) for accreditation purposes. This report includes a Statement of Net Assets; a Statement of Revenues, Expenses, and Changes in Net Assets; a Statement of Cash Flows; and the related Notes to the Financial Statements. In accordance with Southern Association criteria or Governmental Accounting Standards Board requirements, the report also includes a Management's Discussion and Analysis section, a Statement of Changes in Unrestricted Net Assets, and a management letter describing issues noted in the review.

Reporting Entity

The University is a component of the Texas University System and an agency of the State of Texas. The University prepares financial statements that are included in the State's *Comprehensive Annual Financial Report,* which is audited by the Texas State Auditor's Office.

Note 1: Summary of Significant Accounting Policies

Basis of Accounting

The basis of accounting determines when revenues and expenditures or expenses are recognized in the accounts reported in the financial statements. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus.

For financial reporting purposes, the University is considered a special-purpose government engaged only in business-type activities. Accordingly, the University's financial statements have been presented using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized at the time liabilities are incurred. Operating items are distinguished from non-operating items.

Operating revenues and expenses result from providing services or producing and delivering goods in connection with the principle of ongoing operations. Operating revenues include student tuition and fees, net of scholarship allowances; sales and services of auxiliary enterprises; most federal, state, and local grants and contracts and federal appropriations; and interest on student loans. Operating expenses include salaries and wages, payroll related costs, materials and supplies, depreciation, and scholarships.

Nonoperating revenues include activities such as gifts, contributions, State appropriations, investment income, increases in the fair market value of investments, and other revenue sources that are defined as nonoperating revenues by GASB Statement No. 9, *Reporting Cash Flows of Propriety and Nonexpendable Trust Funds and Government Entities That Use Proprietary Fund Accounting*, and GASB Statement No. 34, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*. Nonoperating expenses include activities such as interest expense on capital asset financings and other expenses that are defined as nonoperating expenses by GASB Statement Nos. 9 and 34.

Budget and Budgetary Accounting

The operating budget is prepared annually and represents appropriations authorized by the Legislature and approved by the Governor (the General Appropriations Act). Unencumbered appropriations are generally subject to lapse 60 days after the end of the fiscal year for which they were appropriated.

Capital Assets

Assets with an initial, individual cost of more than $5,000 and an estimated useful life in excess of one year should be capitalized. These assets are capitalized at cost or, if not purchased, at appraised fair value as of the date of acquisition. Depreciation is reported on all "exhaustible" assets. "Inexhaustible" assets such as works of art and historical treasures are not depreciated. Road and highway infrastructure is reported on the modified basis. Routine repairs and maintenance are charged to operating expense in the year in which the expense is incurred. Depreciation is computed using the straight-line method over the estimated useful life of the asset, generally 40 to 50 years for buildings, 20 to 25 years for infrastructure and land improvements, and 3 to 7 years for equipment.

Assets, Liabilities, and Net Assets

Cash and Cash Equivalents: The University considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. Additionally, funds invested through the State Comptroller Cash Management Program are also considered cash equivalents.

Investments: Investments are stated at fair value in all funds except pension trust funds in accordance with GASB Statement 31-*Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. Changes in unrealized gain (loss) on the carrying value of investments are reported in the statements of revenues, expenses, and changes in net assets. For pension trust funds, investments are required to be reported at fair value using the accrual basis of accounting in accordance with GASB Statement 25-*Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contributed Plans*.

Securities Lending Collateral: Securities lent are reported as assets on the balance sheet. The costs of securities lending transactions are reported as expenditures or expenses in the Operating Statement. These costs are reported at gross.

Accounts Receivable: Accounts receivable consists of tuition and fees charged to students and auxiliary enterprise services provided to students, faculty and staff. Accounts receivable also include amounts due from the Federal government, state and local governments, or private sources, in connection with reimbursement of allowable expenditures made pursuant to the University's grants and contracts.

Restricted Assets: Restricted assets include monies or other resources restricted by legal or contractual requirements. These assets include proceeds of enterprise fund general obligation and revenue bonds and revenues set aside for statutory or contractual requirements. Assets held in reserve for guaranteed student loan defaults are also included.

Inventories and Prepaid Items: Inventories include both merchandise inventories on hand for sale and consumable inventories. Inventories are valued at cost, generally utilizing the last-in, first-out method. The consumption method of accounting is used to account for inventories and prepaid items that appear in the proprietary fund types. The cost of these items is expensed when the items are consumed. Total cost of all inventories at August 31, 2008, totaled $298,172.

Deferred Revenue: Deferred revenues include amounts received from students and grant and contract sponsors that have not yet been earned. As of August 31, 2008, the amount of deferred revenues totaled $36,874,940.

Accounts Payable: Accounts Payable represents the liability for the value of assets or services received at the balance sheet date for which payment is pending.

Current Payables-Other: Other payables are the accrual at year-end of expenditure transactions not included in any of the other payable descriptions.

Employees' Compensable Leave Balances: Employees' Compensable Leave Balances represent the liability that becomes "due" upon the occurrence of relevant events such as resignations, retirements, and uses of leave balances by covered employees. Liabilities are reported separately as either current or noncurrent in the statement of net assets.

Capital Lease Obligations: Capital Lease Obligations represent the liability for future lease payments under capital lease contracts contingent upon the appropriation of funding by the Legislature. Liabilities are reported separately as either current or noncurrent in the statement of net assets.

Bonds Payable-General Obligation Bonds and Revenue Bonds: General Obligation and Revenue Bonds are accounted for in the propriety funds by institutions of higher education. The bonds payable are reported at par less unamortized discount or plus unamortized premium. Interest expense is reported on the accrual basis, with amortization of discount or premium. Payables are reported separately as either current or noncurrent in the statement of net assets. Bond proceeds and principal payments are reported in the Statement of Cash Flows.

Invested in Capital Assets, Net of Related Debt: Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bond, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets.

Restricted Net Assets: Restricted net assets result when constraints placed on net asset use are externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.

Unrestricted Net Assets: Unrestricted net assets consist of net assets, which do not meet the definition of the two preceding categories. Unrestricted net assets often have constraints on resources, which are imposed by management, but can be removed or modified. When both restricted and unrestricted net assets are available for use, restricted resources are used first, then unrestricted resources are used as they are needed.

Note 2: Capital Assets

Revenue received from the sale of surplus property will be transferred to Unappropriated General Revenue in accordance with HB7, Sec. 20. A summary of changes in Capital Assets for the year ended August 31, 2008 is presented below: Depreciation expense for the fiscal year ended August 31, 2008 is $5,771,949.

	Balance 9/1/2007	Completed Construction in Progress	Additions	Deductions	Balance 8/31/2008
Non-Depreciable Assets:					
Land and Land Improvements	$ 10,855,051	$	$ 349,058	$	$ 11,204,109
Construction in Progress	39,915,345	(20,888,281)	4,654,639	(1,099,677)	22,582,026
Library Books	0				0
Other Capital Assets	2,004,666				2,004,666
Total Non-Depreciable Assets	$ 52,775,061	$ (20,888,281)	$ 5,003,697	$ (1,099,677)	$ 35,790,801
Depreciable Assets:					
Buildings and Building Improvements	$ 163,098,470	$ 20,808,872	$	$	$ 183,907,342
Infrastructure	17,106,487				17,106,487
Facilities and Other Improvements	11,998,193		269,644		12,267,837
Furniture and Equipment	13,902,679	79,409	1,164,654	(634,008)	14,512,734
Vehicles, Boats, and Aircraft	1,112,282		21,699	(20,283)	1,113,698
Other Capital Assets	24,064,203		212,572	(453,442)	23,823,333
Total Depreciable Assets at Historical Cost	$ 231,282,314	$ 20,888,281	$ 1,668,569	$ (1,107,733)	$ 252,731,431
Less Accumulated Depreciation for:					
Buildings and Building Improvements	$ (98,100,274)	$	$ (3,088,022)	$	$ (101,188,296)
Infrastructure	(8,296,417)		(539,077)		(8,835,494)
Facilities and Other Improvements	(8,269,302)		(412,211)		(8,681,513)
Furniture and Equipment	(8,996,429)		(1,228,697)	603,562	(9,621,564)
Vehicles, Boats, and Aircraft	(961,332)		(61,884)	17,868	(1,005,348)
Other Capital Assets	(16,636,150)		(442,059)		(17,078,208)
Total Accumulated Depreciation	$ (141,259,905)	$ 0	$ (5,771,949)	$ 621,430	$ (146,410,423)
Depreciable Assets, Net	$ 90,022,409	$ 20,888,281	$ (4,103,380)	$ (486,303)	$ 106,321,008
Capital Assets, Net	$ 142,797,470	$ 0	$ 900,318	$ (1,585,979)	$ 142,111,809

Note 3: Deposits, Investments, and Repurchase Agreements

Authorized Investments

The University is authorized to invest in obligations and instruments as defined in the Public Funds Investment Act (Sec. 2256.001 Texas Government Code). Endowment Funds may be invested in accordance with the Uniform Management of Institutional Funds Act, Property Code Chapter 163. Such investments include:

- Obligations of the United States or its agencies
- Direct Obligations of the State of Texas or its agencies
- Obligations of political subdivisions rated not less that A by a national investment rating firm
- Certificates of deposit
- Other instruments and obligations authorized by statute

Lamar University is authorized by statute to make investments following the "prudent person rule". There were no significant violations of legal provisions during the period.

Deposits

	Carrying Amount	Bank Balance
The carrying amount of Cash in Bank (including restricted assets) is	$ 1,761,513	
At August 31, 2008, the actual balances on deposit with local banks were		$2,117,987

Cash on Hand	$ 11,000
Cash in Bank	1,761,513
Cash in State Treasury	20,251,566
Cash Equivalents	32,524,182
Total Cash and Cash Equivalents	$ 54,548,261
Current Assets Cash and Cash Equivalents	$ 30,547,608
Current Assets Restricted Cash and Cash Equivalents	5,053,399
Non-Current Assets Restricted Cash and Cash Equivalents	18,947,254
Total Cash and Cash Equivalents	$ 54,548,261

Custodial credit risk for deposits is the risk that, in the event of the failure of the counterparty, Lamar University will not be able to recover the value of its deposits that are in the possession of an outside party. As of August 31, 2008, Lamar University did not have any deposits that were exposed to custodial credit risk.

Foreign currency for deposits is the risk that changes in exchange rate will adversely affect deposits. Lamar University did not have any deposits exposed to foreign currency risk as of August 31, 2008.

Investments

The investments as of August 31, 2008, are stated at "Fair Market Value". To comply with the reporting requirements of GASB Statement No. 40, the University's investments are shown below to give an indication of credit risk assumed by the University at year-end. Investments may be either categorized to give an indication of the level risk assumed by Lamar University or considered uncategorized. All Lamar University's investments are uncategorized.

- Category 1: Investments that are insured or registered, or for which the securities are held by the agency, or its agent in the agency's name.
- Category 2: Uninsured and unregistered investments for which the securities are held by the broker's or dealer's trust department or agent in the agency's name.
- Category 3: Uninsured and unregistered investments for which the securities are held buy the broker or dealer, or by its trust department or agent, but not in the agency's name.

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. This is not to be confused with market risk which is the risk that the market value of an investment or securities underlying a repurchase agreement will decline. Market risk is not depicted in this note.

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty, Lamar University will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. Lamar University's investment policy limits holding of securities by counterparties to those involved with securities lending. As of August 31, 2008, Lamar University did not have any investments that were exposed to custodial credit risk.

Foreign currency risk for investments is the risk that changes in exchange rate will adversely affect the investments. Lamar University's policy is to limit investments subject to foreign currency risk to 5% of total investments. Lamar University did not have any investments exposed to foreign currency risk as of August 31, 2008.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Through its investment policy, Lamar University manages its exposure to fair value losses arising from increasing interest rates by limiting the modified duration of its investments portfolio to one year.

Concentration of credit risk is the risk of loss attributable to the magnitude of investment in a single issuer. The general investment policy of the University limits investments in debt securities that are not in the top three investment grade ratings issued by nationally recognized statistical rating organizations to 5% of total investments. As of August 31, 2008, Lamar University's credit quality distribution for securities with credit risk exposure was as follows:

Standard & Poor's

Investment Type	**AAA**	**AA**	**A-1**	**Not Rated**
U.S. Government Agency Obligation (Texas Treasury Safekeeping Trust Co.)	$ 303,284			
Commercial Paper		$1,185,333		

Investments

U.S. Government Agency Obligations (Ginnie Mae, Fannie Mae, Freddie Mac, Sallie Mae, etc.)	$	303,284
Equity		5,728,684
Fixed Income Money Market and Bond Mutual Fund		991,145
Commercial Paper		1,185,333
Misc. (e.g., guaranteed investment contract, political subdivision, bankers' acceptance, negotiable CD)		228
Total Investments	$	8,208,674
Non-Current Assets-Investments	$	8,208,674
Total Investments	$	8,208,674

Securities Lending and Reverse Repurchase Agreements

The University does not participate in reverse repurchase agreements or a securities lending program and had no securities out on loan to brokers/dealers at August 31, 2008.

Note 4: Summary of Short-Term Liabilities

See Note 5: Summary of Long-Term Liabilities for a summary of short-term liabilities.

Note 5: Summary of Long-Term Liabilities

During the Year ended August 31, 2008, the following changes occurred in long-term liabilities.

	Balance 9/1/2007	Additions	Deductions	Balance 8/31/2008	Due Within One Year
Deposits Payable	$ 625,048	$ 81,759	$ 0	$ 706,807	$ 70,681
Employees' Compensable Leave	1,789,858	632,214	0	2,422,072	242,207
Total	$ 2,414,906	$ 713,973	$ 0	$ 3,128,679	$ 312,888

Employees' Compensable Leave

Substantially all full-time University employees earn annual leave in the amount of 8 to 21 hours per month depending upon the respective employee's years of state employment. State law permits employees to carry accrued leave forward from one fiscal year to another fiscal year with a maximum of 532 hours for those employees with 35 or more years of state service. Eligible part-time employees' annual leave accrual rate and maximum carryover are proportional to the number of hours appointed to work. Employees with at least six months of state service who terminate their employment are entitled to payment for all accumulated annual leave.

Sick leave, the accumulation of which is unlimited, is earned at the rate of eight hours per month and is paid only when an employee is off due to illness or to the estate of an employee in the event of his or her death. The maximum sick leave that may be paid to an employee's estate is one-half of the employee's accumulated entitlement or 336 hours, whichever is less. The University's policy is to recognize the cost of sick leave when paid, and the liability is not shown in the financial statements because experience indicates that the expense for sick leave will be minimal. Eligible part-time employees' sick leave accrual rate is proportional to the number of hours appointed to work.

Note 6: Bonded Indebtedness

The University receives proceeds from revenue bonds issued and held by the System to support capital projects of the System and its institutions. These proceeds are recorded as transfers from the System. The University disburses funds to the System for payments of principal and interest related to the University's share of bond proceeds. These disbursements are recorded as transfers to the System. At August 31, 2008, the System had outstanding bonds payable of $633,021,475. All bonds issued by the System are defined as revenue bonds. As such, the revenues of the System, including the University, are pledged for repayment of the bonds. Segment information requirements are not applicable, due to the bond indentures' lack of specifically identifiable activities and separate accounting requirements imposed by an external party.

No amount of indebtedness related to these bonds has been recorded in the University's financial statements as the System is the party directly liable for these bonds. At August 31, 2008, however, the University's remaining unpaid share of the bond proceeds was $101,129,380.

Note 7: Capital Leases

As of August 31, 2008, University management was not aware of any significant capital leases.

Note 8: Operating Leases

Future minimum lease rental payments under non-cancellable operating leases having an initial term in excess of one year are as follows:

Fiscal Year Ended August 31, 2008	**Total**
2009	$ 1,087,925
2010	1,084,976
2011	1,081,880
2012	1,078,625
2013	1,075,676
2014-2018	4,262,714
2019-2022	2,827,774
Total Minimum Future Lease Rental Payments	**$12,499,571**

Note 9: Interagency Balances / Activity

DUE FROM/TO OTHER STATE ENTITIES

Entity	Due from Other State Entities	Due to Other State Entities	Purpose
Lamar State College-Port Arthur	169,792	2,479	Eber Ephlin Student Loan
Lamar Institute of Technology	42,047		Utilities
TXDOT	270		FEMA Hurricane Rita
TSUS		1,625	System Office Support
TSUS		242,370	Loan for O/S Eber Ephlin Funds
TSUS		8,322,067	Endowment Balance
	212,109	8,568,541	

TRANSFERS IN FROM/OUT TO OTHER STATE ENTITIES

Entity	Transfers In from Other State Entities	Transfers Out to Other State Entities	Purpose
TSUS		321,298	System Office Support
TSUS		7,143,008	HB 63/ Debt Service
Public Finance Authority		1,034,383	Debt Service
THECB		440,104	Tuition Set Aside
	0	8,938,793	

LEGISLATIVE TRANSFERS IN/OUT

Entity	Legislative Transfers In	Legislative Transfers Out	Purpose
General Revenue (01) TRB		2,606,033	Debt Service
TSUS	6,546,484		HB 63
Lamar Institute of Technology		2,499,943	HEAF
	6,546,484	5,105,976	

Note 10: Contingent Liabilities

During the fiscal year August 31, 2008, there were two (2) lawsuits and claims involving Lamar University. At August 31, 2008, two (2) lawsuits and claims involving Lamar University were pending; the lawsuits and claims will not likely have a material impact on the University.

Note 11: Risk Financing and Related Insurance

The State provides coverage for workers' compensation and unemployment compensation benefits from appropriations made to other State agencies for University employees. The current General Appropriations Act provides that the University must reimburse General Revenue Fund Consolidated, from University appropriations, one-half of the unemployment benefits paid and twenty-five percent of the workers' compensation benefits paid for former and current employees. The Comptroller of Public Accounts determines the proportionate amount to be reimbursed from each appropriated fund type. The University must reimburse the General Revenue Fund one-hundred percent of the cost of workers' compensation and unemployment compensation for any employee paid from funds held in local bank accounts. Workers' compensation and unemployment plans are on a pay-as-you-go basis, in which no assets are set aside to be accumulated for the payment of claims. No material outstanding claims are pending at August 31, 2008. The University has reserved funds for uninsured losses. At August 31, 2008, there were no claims liabilities.

Lamar University is required by certain bond covenants and FEMA to carry Fire and Extended Coverage and boiler insurance on buildings financed through the issuance of bonds using pledged Auxiliary Enterprise or other non-Educational and General Funds. The insurance protects the bond holders from a disruption to the revenue stream that is being utilized to make the bond interest and principal payments and the federal government for storm damage. Insurance claims made during the fiscal year ended August 31, 2008 were related to Hurricane Rita.

The Texas Motor Vehicle Safety Responsibility Act requires that every non-governmental vehicle operated on a state highway be insured for minimum liability in the amount of $20,000/$40,000 bodily injury and $15,000 property damage. However, the University has chosen to carry liability insurance on its licensed vehicles in the amount of $1,000,000 combined single liability. The coverage exceeds the extent of the waivers of state immunity specified in the tort claims act.

Note 12: Subsequent Events

Hurricane Ike made landfall in Southeast Texas September 13, 2008. Damage was sustained by Lamar University. The total cost of repairs, equipment replacement, and other damages has not been determined, but is estimated to total several million dollars. Effects from the storm on student enrollment do not appear to be material. Campus assets are insured under the State Office of Risk Management's property and casualty program. On September 29, 2008 the insurer, American International Group, advanced the Texas State University System $10 million toward the cost of repairs and replacements. Financial recoveries from the insurance policy and the Federal Emergency Management Agency are anticipated to compensate the system for the majority of financial losses from Hurricane Ike. The long-term effect of Hurricane Ike on the student enrollment is indeterminable at this time.

The University has reimbursed $3,276,223 to the State of Texas General Revenue Fund for duplicate reimbursements for expenses related to Hurricanes Katrina and Rita. In addition, the 81st Legislature's Conference Committee on Senate Bill 1 (General Appropriations Act) adopted a rider which requires that a study be conducted to determine the full amount that the University owes the State. However, because of the growth in student enrollment and the corresponding increase in funding, this will not materially affect the University's financial condition.

Note 13: Related Parties

There have been no material transactions between the University and related parties during the fiscal year ended August 31, 2008.

Note 14: Stewardship, Compliance, and Accountability

Lamar University has no material violations of finance related and contract provisions and no new component units are included in the financial report. Per the laws of the State of Texas, Lamar University cannot spend amounts in excess of appropriations granted by the Texas Legislature and there are no deficits reported in net assets.

Note 15: The Financial Reporting Entity

The Lamar University Foundation is a nonprofit organization with the sole purpose of supporting educational activities of Lamar University. The Foundation solicits donations and acts as coordinator of gifts made by other parties. The Foundation remitted restricted gifts of $1,077,518 to the University during the year ended August 31, 2008. During the fiscal year the University furnished certain services, such as office space and utilities, to the Foundation, for which the Foundation was billed at cost, $126,838. Accounts receivable of $502,116 is due from the Foundation at August 31, 2008. This organization is not considered a component unit as defined by generally accepted accounting principles. Therefore, the assets, liabilities, and equities of the Foundation are not contained in the financial statements of the University. Financial information on the Foundation is available upon request at Lamar University Foundation, John Gray Center-Building B, P.O. Box 11500, Beaumont, Texas 77710.

Lamar University is an agency of the State of Texas, and its financial records reflect compliance with applicable state statutes and regulations. Lamar University is a component of the Texas State University System. Components of the System are System Administration, Lamar University, Sam Houston State University, Sul Ross State University, Texas State University-San Marcos, Lamar Institute of Technology, Lamar State College-Orange, and Lamar State College-Port Arthur. The System is governed by an appointed nine member Board of Regents.

Note 16: Restatement of Net Assets

As of August 31, 2008, the University did not restate net assets.

Note 17: Employee Retirement Plans

The State of Texas has joint contributory retirement plans for substantially all of its employees. One of the primary plans in which the University participates is administered by the Teacher Retirement System of Texas (Retirement System). The contributory percentages currently provided by the State and by each participant are 6.58 percent and 6.4 percent, respectively, of annual compensation.

The Retirement System does not separately account for each of its component government agencies because the Retirement System itself bears sole responsibility for retirement commitments beyond contributions fixed by the State Legislature. According to an independent actuarial valuation as of August 31, 2008, the present value of the Retirement System's actual and projected liabilities, including projected benefits payable to its retirees and active members and their beneficiaries, was more than the actuarial valuation of Retirement System assets. Further information regarding actuarial assumptions and conclusions, together with audited financial statements, are included in the Retirement System's annual financial report.

The State has also established an Optional Retirement Program for institutions of higher education. Participation in the Optional Retirement Program is in lieu of participation in the Retirement System. The Optional Retirement Program provides for the purchase of annuity contracts and mutual funds. The contributory percentages of participant salaries provided by the State and by each participant enrolled in the plan on or before August 31, 1995, are 8.5 percent and 6.65 percent, respectively. The 8.5 percent is composed of 6.0 percent contributed by the State and an additional 2.5 percent contributed by the University. For participants who enrolled after September 1, 1995, State and participant contributions are 6.58 percent and 6.65 percent, respectively. Because these are individual annuity contracts, the State has no additional or unfunded liability for this program, and the University bears no responsibility for retirement commitments beyond contributions.

Note 18: Deferred Compensation Program

University employees may elect to defer a portion of their earnings for income tax and investment purposes pursuant to authority granted in Texas Government Code, Section 609.001. Deferred compensation plans are administered by the Employees Retirement System.

The State's 457 Plan complies with Internal Revenue Code, Section 457. This plan is referred to as the TexaSaver Deferred Compensation Plan and is available to all employees. Deductions, purchased investments, and earnings attributed to the 457 Plan are the property of the State and subject only to the claims of the State's general creditors. Participant rights under the plan are equal to those of the general creditors of the State in an amount equal to the fair market value of the 457 account for each participant. The State has no liability under the 457 Plan, and it is unlikely that plan assets will be used to satisfy the claims of general creditors in the future.

The University also administers a Tax-Deferred Account Program, created in accordance with Internal Revenue Code, Section 403(b). All employees are eligible to participate. The Tax-Deferred Account Program is a private plan, and the deductions, purchased investments, and earnings attributed to each employee's 403(b) plan are held by vendors chosen by the employee. The vendors may be insurance companies, banks, or approved non-bank trustees such as mutual fund companies. The assets of this plan do not belong to the University, and thus it does not have a liability related to this plan.

Note 19: Donor-Restricted Endowments

Donor Restricted Endowment	Amounts of Net Appreciation	Reported in Net Assets
True Endowments	$2,711,000	Restricted for Expendable
Total Restricted Endowments	$2,711,000	

These amounts are reported as Expendable Restricted by Other on the Statement of Net Assets. The University endowment investment income spending policy is a percent return on fair market value at August 31st of each year for the next year. The authorization for the fiscal year ended August 31, 2008 was 5%.

The balances, or transactions, of funds held in trust by others on behalf of Lamar University are not reflected in the financial statements. At August 31, 2008, there was one such fund for the benefit of the University. Based upon the most recent available information, the assets of this fund as reported by the Trustees are valued at $14,157,549.

Expenditure of endowed funds is not permitted without the express consent of the donor. The majority of the endowments are held in perpetuity. In many cases, endowment earnings are expendable for student financial assistance or other purposes specified by the donor. In other cases, endowment earnings are reinvested. Chapter 163 of the Texas Property Code (also cited as the Uniform Prudent Management of Institutional Funds Act) grants the University the authority to spend net appreciation.

Note 20: Post-Employment Health Care and Life Insurance Benefits

In addition to providing pension benefits, the State provides certain health and life insurance benefits for retired employees, in accordance with state statutes. Substantially all of the employees may become eligible for the health and life insurance benefits if they reach normal retirement age while working for the State. Currently, there are 397 University retirees who are eligible for these benefits. Similar benefits for active employees are provided through a self-funded plan and fully insured plans.

Depending upon the status of the employee at the time of retirement, the State or the System recognizes the cost of providing these benefits. The cost of retiree post-employment benefits is recognized when paid. This contribution paid all of the “employee/retiree only” premiums and a portion of the premiums for those employees/retirees selecting dependent coverage. The employee/retiree was required to pay a portion of the cost of dependent coverage. For the fiscal year ended August 31, 2008, the cost of providing those benefits for the retirees was $1,936,912 for the State and $20,670 for the University.

Note 21: Special or Extraordinary Items

As of August 31, 2008, University management was not aware of any significant special or extraordinary items.

Note 22: Disaggregation of Receivable and Payable Balances

Current Receivables and Other Current Liabilities as of August 31, 2008 are comprised of the following:

Federal Receivables	
Instruction	$ 284,439
Research	877,571
Public Service	15,147
Scholarship	2,500,648
Institutional Support	39,123
TOTAL FEDERAL RECEIVABLES	**$ 3,716,928**
Other Receivables	
Auxiliary Enterprises	$ 922,000
Loan	156,909
Pledges Receivables (Restricted)	200,370
Endowment and Similar Funds	27,500
TOTAL OTHER RECEIVABLES	**$ 1,306,779**
Other Current Liabilities	
Other Accrued Liabilities	$ 242,207
Current Portion/Deposit Payable	70,681
TOTAL OTHER CURRENT LIABILITIES	**$ 312,888**
Other Non Current Liabilities	
Noncurrent Portion/Deposit Payable	$ 636,126
TOTAL OTHER NONCURRENT LIABILITIES	**$ 636,126**

Note 23: Termination Benefits

As of August 31, 2008, there were no material termination benefits.

State Auditor's Office
John Keel, CPA
State Auditor

May 21, 2009

Dr. James M. Simmons, President
Lamar University
P.O. Box 1001
Beaumont, TX 77710

Subject: Management Letter Resulting from a Review of Lamar University's Fiscal Year 2008 Financial Statements

Dear Dr. Simmons:

We offer this management letter in conjunction with our review of the financial statements of Lamar University (University) for the fiscal year ended August 31, 2008. We reviewed the Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; the Statement of Cash Flows; and the Notes to the Financial Statements. In the course of our review, which was substantially less in scope than an audit, we did not find that material modifications needed to be made to the financial statements in order for them to be in conformity with generally accepted accounting principles.

Our review determined that the University did not maintain adequate documentation to support information in its fiscal year 2008 annual financial report. As a result, the University re-created documentation for auditors' review.

Additionally, our review determined that the University does not have adequate processes in place to ensure that it consistently reports correct financial information. As a result of miscalculations identified in the University's fiscal year 2008 annual financial report, the University made the following restatements in its report for the Southern Association of Colleges and Schools:

- The University made one line item restatement for $4,475,240 and another line item restatement for negative $4,475,240 on its Statement of Net Assets. These restatements had a net effect of $0 on the Statement of Net Assets.
- The University made eight line item restatements totaling $13,380,897 and seven line item restatements totaling negative $11,028,390 on its Statement of Cash Flows. These restatements had a net effect of $2,352,507 on the Statement of Cash Flows..

While the net effect of the restatements was not material, the number of restatements indicates that the University should improve its financial reporting processes.

Robert E. Johnson Building
1501 N. Congress Avenue
Austin, Texas 78701

P.O. Box 12067
Austin, Texas 78711-2067

Phone:
(512) 936-9500

Fax:
(512) 936-9400

Internet:
www.sao.state.tx.us

Recommendation

The University should improve its financial reporting and review processes to ensure that the financial information it reports is correct and supported by sufficient documentation.

Management Response

Management concurs that the University should improve its financial reporting and review processes to ensure that the financial information it reports is correct and supported by sufficient documentation. Fiscal year 2008 was the first year of implementation of a new financial system, and at the time the financial statements were prepared, the reporting module of the new system had not been utilized. Turnover in personnel and evacuations due to Hurricanes Gustav and Ike (and the resultant impact on the campus from the Hurricanes' landfall) complicated day-to-day operations, and impacted our ability to provide the same level of oversight and support as in prior reporting periods. We are in the process of evaluating our organizational structure and personnel resource allocations with the intent of re-organizing our reporting and review process to ensure that financial information is reported correctly and timely. We anticipate to have the new structure in place by fiscal year end. The person responsible for implementation is the Vice-President for Finance and Operations.

We appreciate the assistance provided during this review by the management of the University and Internal Audit. If you have any questions, please call me at (512) 936-9500.

Sincerely,

Sandra Vice

Sandra Vice, CIA, CGAP, CISA
Assistant State Auditor

Annual Financial Report

for the fiscal year ended August 31, 2008

SAM HOUSTON STATE UNIVERSITY

Huntsville, Texas

Sam Houston State University is a Member of The Texas State University System

Contents

State Auditor's Office
John Keel, CPA
State Auditor

Auditor's Review Report

March 3, 2009

Dr. James F. Gaertner, President
Sam Houston State University
1806 Ave. J, Suite 303
Huntsville, TX 77340

Dear Dr. Gaertner:

We have reviewed the accompanying Statement of Net Assets; Statement of Revenues, Expenses, and Changes in Net Assets; Statement of Cash Flows; and Notes to the Financial Statements of Sam Houston State University (University) as of and for the fiscal year ended August 31, 2008, in accordance with *Statements on Standards for Accounting and Review Services* issued by the American Institute of Certified Public Accountants. The review was performed in accordance with the Southern Association of Colleges and Schools' (Southern Association) *Criteria for Accreditation*. All information included in these financial statements is the representation of management of the University.

A review consists principally of inquiries of University personnel and analytical procedures applied to financial data. A review is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

The accompanying statements were prepared to present the financial position, the changes in financial position, and the cash flows of the University. These statements are prepared pursuant to criteria of the Southern Association for supplementary special reports by institutions in states that conduct statewide audits.

Based on our review, with the exception of the matter described in the following paragraph, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with generally accepted accounting principles.

The University has not presented a management's discussion and analysis section that the Governmental Accounting Standards Board has identified as required supplementary information that is not part of the basic financial statements.

This report is intended for use by the Board of Regents of the Texas State University System, management of the University, and the Southern Association. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

Sincerely,

John Keel, CPA
State Auditor

Robert E. Johnson Building
1501 N. Congress Avenue
Austin, Texas 78701

P.O. Box 12067
Austin, Texas 78711-2067

Phone:
(512) 936-9500

Fax:
(512) 936-9400

Internet:
www.sao.state.tx.us

SAO Report No. 09-328

SAM HOUSTON STATE UNIVERSITY

Statement of Net Assets

At August 31, 2008

ASSETS		
Current Assets		
Cash and Cash Equivalents (Note 3)	$	78,316,029
Restricted:		
Cash and Cash Equivalents (Note 3)		59,458,783
Legislative Appropriations		4,815,585
Receivables, Net of Allowances:		
Federal		3,330,111
Accounts		10,451,335
Due from Other State Entities (Note 9)		155,089
Merchandise Inventories		297,517
Loans and Contracts		2,047,862
Other Current Assets		14,228,161
Total Current Assets	$	173,100,472
Non-Current Assets		
Restricted:		
Cash and Cash Equivalents (Note 3)	$	12,892,349
Gifts Receivable		289,164
Investments (Note 3)		60,921,234
Loans and Contracts		388,275
Capital Assets (Note 2):		
Non-Depreciable		43,484,509
Depreciable		330,702,887
Less: Accumulated Depreciation		(169,140,723)
Total Non-Current Assets	$	279,537,695
Total Assets	$	452,638,167
LIABILITIES		
Current Liabilities		
Payables:		
Accounts	$	5,052,746
Payroll		4,356,732
Due to Other State Entities (Note 9)		1,400
Deferred Revenue		56,966,211
Capital Lease Obligations (Notes 5, 7)		102,819
Employees' Compensable Leave (Note 5)		1,986,566
Funds Held for Others		2,578,827
Deposits Payable		640,821
Total Current Liabilities	$	71,686,122
Non-Current Liabilities		
Capital Lease Obligations (Notes 5, 7)	$	282,538
Employees' Compensable Leave (Note 5)		1,186,473
Deposits Payable		641,903

SAM HOUSTON STATE UNIVERSITY

Statement of Net Assets

At August 31, 2008

US Government Grants Refundable		599,182
Total Non-Current Liabilities	$	2,710,096
Total Liabilities	$	74,396,218
NET ASSETS		
Invested in Capital Assets, Net of Related Debt	$	204,661,316
Restricted for:		
Non-Expendable		
Permanent Funds, True Endowments, Annuities		36,102,070
Expendable		
Capital Projects		48,049,928
Other		15,019,692
Unrestricted		74,408,943
Total Net Assets	$	378,241,949

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

SAM HOUSTON STATE UNIVERSITY

Statement of Revenues, Expenses, and Changes in Net Assets

For the Fiscal Year Ended August 31, 2008
(See Auditor's Review Report on page 1.)

OPERATING REVENUES		
Tuition and Fees - Non-Pledged	$	88,636,235
Discounts and Allowances		(16,339,207)
Auxiliary Enterprises - Non-Pledged		25,755,911
Other Sales of Goods and Services - Non-Pledged		1,640,291
Federal Revenue		20,149,070
State Grant Revenue		6,129,635
Other Operating Grant Revenue		494,588
Other Operating Revenues		10,029,266
Total Operating Revenues	$	136,495,789
OPERATING EXPENSES		
Cost of Goods Sold	$	529,598
Salaries and Wages		91,064,503
Payroll Related Costs		22,129,622
Professional Fees and Services		2,061,325
Travel		3,820,568
Materials and Supplies		19,573,397
Communications and Utilities		8,558,666
Repairs and Maintenance		2,782,146
Rentals and Leases		1,935,404
Printing and Reproduction		632,389
Depreciation and Amortization		11,187,991
Bad Debt Expense		(319,698)
Interest Expense		13,921
Scholarships		14,417,355
Other Operating Expenses		11,702,555
Total Operating Expenses	$	190,089,742
Operating Income (Loss)	$	(53,593,953)
NONOPERATING REVENUES (EXPENSES)		
Legislative Appropriations	$	56,440,674
Gifts		6,808,897
Interest and Investment Income (Loss)		1,798,572
Investing Activities Expense		(75,839)
Net Increase (Decrease) in Fair Value of Investments		(1,128,855)
Claims and Judgments		(256,020)
Other Nonoperating Revenues - Non-Pledged		4,117,486
Total Nonoperating Revenues (Expenses)	$	67,704,915

SAM HOUSTON STATE UNIVERSITY

Statement of Revenues, Expenses, and Changes in Net Assets

For the Fiscal Year Ended August 31, 2008
(See Auditor's Review Report on page 1.)

Income (Loss) Before Other Revenues, Expenses, Gains (Losses), and Transfers	$	14,110,962
OTHER REVENUES, EXPENSES, GAINS (LOSSES), AND TRANSFERS		
Capital Appropriations (HEAF)	$	9,916,306
Transfers In from Other State Entities (Note 9)		50,000,000
Transfers Out to Other State Entities (Note 9)		(7,672,518)
Legislative Transfers Out (Note 9)		(2,882,898)
Legislative Appropriations Lapsed		(21,966)
Total Other Revenues, Expenses, Gains (Losses), and Transfers	$	49,338,924
CHANGE IN NET ASSETS	$	63,449,886
Net Assets, September 1, 2007	$	314,792,063
Restatements (Note 16)		
Net Assets, September 1, 2007, as Restated	$	314,792,063
NET ASSETS, August 31, 2008	$	378,241,949

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

SAM HOUSTON STATE UNIVERSITY
Statement of Cash Flows
For the Fiscal Year Ended August 31, 2008

CASH FLOWS FROM OPERATING ACTIVITIES		
Proceeds from Tuition and Fees	$	73,845,275
Proceeds from Research Grants and Contracts		29,453,624
Proceeds from Loan Programs		4,475,437
Proceeds from Auxiliaries		25,725,737
Proceeds from Other Revenues		11,492,955
Payments to Suppliers for Goods and Services		(63,322,104)
Payments to Employees for Salaries		(90,718,982)
Payments to Employees for Benefits		(22,129,622)
Payments for Loans Provided		(4,590,806)
Net Cash Provided (Used) by Operating Activities	$	(35,768,486)
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Proceeds from Legislative Appropriations	$	60,081,953
Proceeds from Gifts		7,009,104
Payments for Other Uses		(919,228)
Net Cash Provided (Used) by Non-Capital Financing Activities	$	66,171,829
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds of Transfers from Other Entities		50,000,000
Proceeds from State Appropriations (HEAF)		9,916,306
Payments for Additions to Capital Assets		(31,401,727)
Payments of Principal on Capital-Related Debt		(9,442,781)
Net Cash Provided (Used) by Capital and Related Financing Activities	$	19,071,798
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from Sales of Investments	$	78,256
Proceeds from Interest and Investment Income		5,916,058
Payments to Acquire Investments		(115,054)
Net Cash Provided (Used) by Investing Activities	$	5,879,260
Net Increase (Decrease) in Cash and Cash Equivalents	$	55,354,401
Cash and Cash Equivalents, September 1, 2007	$	95,312,760
Restatements		
Cash and Cash Equivalents, September 1, 2007, as restated	$	95,312,760
Cash and Cash Equivalents, August 31, 2008	$	150,667,161

SAM HOUSTON STATE UNIVERSITY

Statement of Cash Flows

For the Fiscal Year Ended August 31, 2008

Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities

Operating Income (Loss)	$	(53,593,953)
Adjustments:		
Depreciation and Amortization	$	11,187,991
Bad Debt Expense		(319,698)
Operating Income and Cash Flow Categories:		
Classification Differences		
Changes in Assets and Liabilities:		
(Increase) Decrease in Receivables		2,667,128
(Increase) Decrease in Inventories		(8,191)
(Increase) Decrease in Prepaid Expenses		(305,446)
(Increase) Decrease in Other Assets		(121,417)
Increase (Decrease) in Payables		2,816,944
Increase (Decrease) in Deferred Revenue		1,626,818
Increase (Decrease) in Employees' Compensable Leave		227,736
Increase (Decrease) in Other Liabilities		53,602
Total Adjustments	$	17,825,467
Net Cash Provided (Used) by Operating Activities	$	(35,768,486)
Non-Cash Transactions		
Net Increase (Decrease) in Fair Value of Investments	$	(1,128,855)
Other Deductions to Capital Assets		385,357

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

SAM HOUSTON STATE UNIVERSITY

Statement of Changes in Unrestricted Net Assets

For the Fiscal Year Ended August 31, 2008

	8/31/2008	8/31/2007	Difference
Reserved			
Encumbrances	$ 19,149,068	$ 20,943,392	$ (1,794,324)
Legislative Appropriations to be Lapsed	4,105		4,105
Accounts Receivable	10,055,718	7,787,661	2,268,057
Inventories	276,518	262,442	14,076
Higher Education Assistance Funds	2,000,438	178,798	1,821,640
Fees with Use Restricted by Statute:			
International Education Fees (54.5132)	36,314	48,851	(12,537)
Student Service Fees (54.503)		769,370	(769,370)
University Center Fee (54.527)	905,401	901,273	4,128
Prepaid Expenses	6,066,153	6,403,605	(337,452)
Petty Cash	24,350	24,350	0
Texas Public Education Grants	1,031,455	2,188,164	(1,156,709)
Unreserved			
Allocated			
Auxiliary Enterprises Operating Funds	8,271,700	7,568,003	703,697
Funds Functioning as Endowment - Unrestricted	5,775,512	5,833,092	(57,580)
Student Fees	15,039,536	20,352,170	(5,312,634)
Other	4,782,527	2,747,878	2,034,649
Unallocated	990,148	5,989,705	(4,999,557)
Total Unrestricted Net Assets	$ 74,408,943	$ 81,998,754	$ (7,589,811)

(See Auditor's Review Report on page 1.)

General Introduction

This report has been prepared for the use of the Southern Association of Colleges and Schools (Southern Association) in connection with the review of Sam Houston State University (University) for accreditation purposes. This report includes a Statement of Net Assets; a Statement of Revenues, Expenses, and Changes in Net Assets; a Statement of Cash Flows; and the related Notes to the Financial Statements. In accordance with Southern Association criteria or Governmental Accounting Standards Board requirements, the report also includes a Statement of Changes in Unrestricted Net Assets, and a management letter describing issues noted in the review.

Reporting Entity

The University is a component of the Texas State University System and an agency of the State of Texas. The University prepares financial statements that are included in the State's *Comprehensive Annual Financial Report,* which is audited by the Texas State Auditor's Office.

Note 1: Summary of Significant Accounting Policies

Basis of Accounting

The basis of accounting determines when revenues and expenditures or expenses are recognized in the accounts reported in the financial statements. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus.

For financial reporting purposes, the University is considered a special-purpose government engaged only in business-type activities. Accordingly, the University's financial statements have been presented using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized at the time liabilities are incurred. Operating items are distinguished from non-operating items. Operating revenues and expenses result from providing services or producing and delivering goods in connection with the principle of ongoing operations. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets.

Capital Assets

Capital assets are recorded at cost at the date of acquisition, or fair market value at the date of donation in the case of gifts. For equipment, the University capitalizes all items with a unit cost of $5,000 or more. Renovations to buildings, infrastructure, and land improvements that significantly increase the value or extend the useful life of the structure are capitalized. Routine repairs and maintenance are charged to operating expense in the year in which the expense is incurred.

Depreciation is computed using the straight-line method over the estimated useful life of the asset, generally 40 to 50 years for buildings, 20 to 25 years for infrastructure and land improvements, and 3 to 7 years for equipment. Inexhaustible assets such as works of art and historical treasures are not depreciated.

BUDGET AND BUDGETARY ACCOUNTING

The budget is prepared biennially and represents appropriations authorized by the legislature and approved by the Governor (the General Appropriations Act).

Unencumbered appropriations are generally subject to lapse 60 days after the end of the fiscal year for which they were appropriated.

ASSETS, LIABILITIES, AND NET ASSETS

ASSETS

Cash and Cash Equivalents
All highly liquid investments with a maturity of three months or less at the time of purchase are considered cash and cash equivalents. Additionally, funds invested trough the State Comptroller Cash Management Program are also considered cash equivalents.

Investments
The University accounts for its investments at fair value in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. Changes in unrealized gain (loss) on the carrying value of investments are reported in the Statements of Revenues, Expenses and Changes in Net Assets.

Accounts Receivable
Accounts receivable consists of tuition and fees charged to students and auxiliary enterprise service provided to students, faculty, and staff. Accounts receivable also include amounts due from the Federal government, state and local governments, or private sources, in connection with reimbursement of allowable expenditures made pursuant to the University's grants and contracts.

Inventories and Prepaid Expense
Inventories are valued at cost, generally utilizing the last-in, first-out method. The consumption method of accounting is used to account for inventories and prepaid items. The cost of these items is expensed when the items are consumed. Total cost of all inventories and prepaid expenses at August 31, 2008 totaled $14,525,678.

LIABILITIES

Accounts Payable
Accounts Payable represents the liability for the value of assets or services received at the balance sheet date for which payment is pending. As of August 31, 2008, accounts payable totaled $5,052,746.

Capital Lease Obligations

Capital Lease Obligations represent the liability for future lease payments under capital lease contracts contingent upon the appropriation of funding by the Legislature. Liabilities are reported separately as either current or noncurrent in the statement of net assets.

Deferred Revenue

Deferred revenues include amount received from students and grant and contract sponsors that have not yet been earned. As of August 31, 2008, the amount of Deferred Revenues totaled $56,966,211.

NET ASSETS

Invested in Capital Assets, Net of Related Debt

Invested in Capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bond, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets.

Restricted Net Assets

Restricted assets include cash and investments that are externally restricted to make debt service payments, maintain sinking or reserve funds, or to purchase or construct capital or other non-current assets, or imposed by law through constitutional provisions or enabling legislation.

Unrestricted Net Assets

Unrestricted net assets consist of net assets which do not meet the definition of the two preceding categories. Unrestricted net assets often have constraints on resources which are imposed by management, but can be removed or modified. When both restricted and unrestricted net assets are available for use, restricted resources are used first, then unrestricted resources are used as they are needed.

Note 2: Capital Assets

	Balance 9/1/2007	Adjustments	Completed Construction in Progress	Additions	Deductions	Balance 8/31/2008
Non-Depreciable Assets:						
Land and Land Improvements	$ 12,894,758	$	$ 817,349	$ 355,000	$ (292,120)	$ 13,774,987
Construction in Progress	11,919,032		(9,466,200)	26,496,972	(186)	28,949,618
Library Books						0
Other Capital Assets	759,904					759,904
Total Non-Depreciable Assets	$ 25,573,694	$ 0	$ (8,648,851)	$ 26,851,972	$ (292,306)	$ 43,484,509
Depreciable Assets:						
Buildings and Building Improvements	$ 263,035,864	$	$ 7,989,292	$	$ (2,472,605)	$ 268,552,551
Infrastructure	9,023,978					9,023,978
Facilities and Other Improvements	17,363,516		573,961			17,937,477
Furniture and Equipment	18,489,796		85,598	4,037,949	(536,730)	22,076,613
Vehicles, Boats, and Aircraft	2,419,663			499,533	(127,422)	2,791,774
Other Capital Assets	9,834,854			532,610	(46,970)	10,320,494
Total Depreciable Assets at Historical Cost	$ 320,167,671	$ 0	$ 8,648,851	$ 5,070,092	$ (3,183,727)	$ 330,702,887
Less Accumulated Depreciation for:						
Buildings and Building Improvements	$ (132,928,101)	$	$	$ (7,703,782)	$ 2,348,974	$ (138,282,909)
Infrastructure	(3,470,760)			(347,076)		(3,817,836)
Facilities and Other Improvements	(4,037,059)			(682,861)		(4,719,920)
Furniture and Equipment	(12,104,809)			(1,902,191)	479,301	(13,527,699)
Vehicles, Boats, and Aircraft	(1,696,703)			(222,043)	127,422	(1,791,324)
Other Capital Assets	(6,670,997)			(330,038)		(7,001,035)
Total Accumulated Depreciation	$ (160,908,429)	$ 0	$ 0	$ (11,187,991)	$ 2,955,697	$ (169,140,723)
Depreciable Assets, Net	$ 159,259,242	$ 0	$ 8,648,851	$ (6,117,899)	$ (228,030)	$ 161,562,164
Capital Assets, Net	$ 184,832,936	$ 0	$ 0	$ 20,734,073	$ (520,336)	$ 205,046,673

Note 3: Deposits, Investments, and Repurchase Agreements

Sam Houston State University is authorized by statute to make investments following the "prudent person rule." There were no significant violations of legal provisions during the period.

The carrying amount of Cash in Bank (including restricted assets) is $2,769,407.

DEPOSITS

Carrying Amount	Bank Balance
$ 2,679,407	$ 7,941,869

Cash on Hand	$ 24,325
Cash in Bank	2,769,407
Reimbursement Due from Treasury	4,811,213
Cash in State Treasury	21,950,148
Cash Equivalents	121,112,068
Total Cash and Cash Equivalents	$ 150,667,161
Current Assets Cash and Cash Equivalents	$ 78,316,029
Current Assets Restricted Cash and Cash Equivalents	59,458,783
Non-Current Assets Restricted Cash and Cash Equivalents	12,892,349
Total Cash and Cash Equivalents	$ 150,667,161

Custodial Credit Risk for Deposits

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the University will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The University does not have a deposit policy for custodial credit risk. As of August 31, 2008, Sam Houston State University was not subject to custodial credit risk for deposits due to collateralized securities held by the pledging financial institution's trust department in Sam Houston State University's name.

Foreign Currency Risk for Deposits

Foreign currency risk for deposits is the risk that changes in exchange rates will adversely affect the deposit. The University's policy is to limit deposits subject to foreign currency risk to 5% of total deposits. Sam Houston State University held no exposure to foreign currency risk for deposits as of August 31, 2008.

Investments

Sam Houston State University invests its endowment funds to provide funding for scholarships, fellowships, professorships, academic chairs, and other uses as specified by donors. Investments of University funds for endowments and quasi endowments shall be accomplished in accordance with the following principals:

1. There are two primary investment objectives. One is to provide a continuing and dependable cash payout, stable, and preferably growing in real terms, after giving effect to inflation. The second is to cause the total value of the funds to appreciate, over time, exclusive of growth derived from donations.

2. The cash payout requirement for endowment and quasi endowment funds are significant and continuous. Income must be sufficient to provide an adequate cash stream to support the programs for which the endowments and quasi endowment accounts need to appreciate to insure preservation of purchasing power, and also to satisfy the need for future growth in payouts.

3. The endowment and quasi endowment funds will be invested to meet these objectives, by maximizing returns consistent with an appropriate level of risk and subject to generation of adequate current income. Additionally, the investments shall be diversified at all times to provide reasonable assurance that investment in a single security, a class of securities, or industry will not have an excessive impact on the funds.

Custodial Credit Risk for Investments

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty, the University will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The University's investment policy limits holding of securities by counterparties to those involved with securities lending. As of August 31, 2008, Sam Houston State University had no investments subject to custodial credit risk.

Foreign Currency Risk for Investments

Foreign currency risk for investments is the risk that changes in exchange rates will adversely affect the investment. The University's policy is to limit investments subject to foreign currency risk to 5% of total investments. As of August 31, 2008 Sam Houston State University was not subject to foreign currency risk.

Credit Risk for Investments

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The general investment policy of the agency limits investments in debt securities that are not in the top three investment grade ratings issued by nationally recognized statistical rating organizations to 5% of total investments. As of August 31, 2008, Sam Houston State University was not subject to credit risk.

Interest Rate Risk for Investments

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Sam Houston State University is not required to disclose interest rate risk.

Concentration of Credit Risk for Investments

Concentration of credit risk is the risk of loss attributable to the magnitude of investment in a single issuer. Investments issued or explicitly guaranteed by the U.S. government and investments in mutual funds, external investment pools, and other pooled investments are excluded from this disclosure requirement. As of August 31, 2008, Sam Houston State University was not subject to concentration of credit risk.

INVESTMENTS

Fixed Income Money Market and Bond Mutual Fund	$	60,631,470
Other Commingled Funds		289,764
Total Investments	$	60,921,234
Non-Current Assets – Investments	$	60,921,234
Total Investments	$	60,921,234

REVERSE REPURCHASE, SECURITIES LENDING, DERIVATIVE INVESTING

Sam Houston State University did not participate in Reverse Repurchase Agreements, Securities Lending, or Derivative Investing during fiscal year 2008.

Note 4: Summary of Short-Term Liabilities

Sam Houston State University as of August 31, 2008 had no short-term liabilities.

Note 5: Summary of Long-Term Liabilities

	Balance 9/1/2007	Additions	Deductions	Balance 8/31/2008	Amounts Due Within One Year	*Non-Current Amounts*
Capital Lease Obligations	$ 491,022	$	$ 105,665	$ 385,357	$ 102,819	*282,538*
Employees' Compensable Leave	2,945,303	227,736		3,173,039	1,986,566	*1,186,473*
Total	$ 3,436,325	$ 227,736	$ 105,665	$ 3,558,396	$ 2,089,385	

Employees' Compensable Leave

Substantially all full-time University employees earn annual leave in the amount of 8 to 21 hours per month depending upon the respective employee's years of state employment. State law permits employees to carry accrued leave forward from one fiscal year to another fiscal year with a maximum of 532 hours for those employees with 35 or more years of state service. Eligible part-time employees' annual leave accrual rate and maximum carryover are proportional to the number of hours appointed to work. Employees with at least six months of state service who terminate their employment are entitled to payment for all accumulated annual leave.

Sick leave, the accumulation of which is unlimited, is earned at the rate of eight hours per month and is paid only when an employee is off due to illness or to the estate of an employee in the event of his or her death. The maximum sick leave that may be paid to an employee's estate is one-half of the employee's accumulated entitlement or 336 hours, whichever is less. The University's policy is to recognize the cost of sick leave when paid, and the liability is not shown in the financial statements because experience indicates that the expense for sick leave will be minimal. Eligible part-time employees' sick leave accrual rate is proportional to the number of hours appointed to work.

Note 6: Bonded Indebtedness

The University receives proceeds from revenue bonds issued and held by the System to support capital projects of the System and its institutions. These proceeds are recorded as transfers from the System. The University disburses funds to the System for payments of principal and interest related to the University's share of bond proceeds. These disbursements are recorded as transfers to the System. At August 31, 2008, the System had outstanding bonds payable of $669,422,168. All bonds issued by the System are defined as revenue bonds. As such, the revenues of the System, including the University, are pledged for repayment of the bonds. Segment information requirements are not applicable, due to the bond indentures' lack of specifically identifiable activities and separate accounting requirements imposed by an external party.

No amount of indebtedness related to these bonds has been recorded in the University's financial statements as the System is the party directly liable for these bonds. At August 31, 2008, however, the University's remaining unpaid share of the bond proceeds was $130,247,531.

Note 7: Capital Leases

The University has entered into long-term leases for financing the purchase of certain capital assets. Such leases are classified as capital leases for accounting purposes and, therefore, have been recorded at the present value of the future minimum lease payments at the inception of the lease. The following is a summary of original capitalized costs of all such property under lease as well as the accumulated depreciation as of August 31, 2008.

DEBT SERVICE REQUIREMENTS TO MATURITY

Year Ended August 31,		Total
2009	$	105,300
2010		127,800
2011		114,695
2012		73,050
Total Minimum Lease Payments	$	420,845
Less: Amount Representing Interest at Various Rates		(35,488)
Present Value of Net Minimum Lease Payments	$	385,357

ORIGINAL CAPITALIZED COSTS OF ASSETS UNDER CAPITAL LEASE OBLIGATIONS

		Assets under Capital Lease		Accumulated Depreciation
Furniture and Equipment	$	569,251	$	6,777
Total	$	569,251	$	6,777

Note 8: Operating Leases

Future minimum lease rental payments under non-cancellable operating leases having an initial term in excess of one year as of August 31, 2008 are:

Year Ended August 31,		Total
2009		44,719
2010		25,195
2011		17,401
Total Minimum Future Lease Payments	$	87,314

Note 9: Interagency Balances / Activity

DUE FROM/TO OTHER STATE ENTITIES

Entity		Due from Other State Entities		Due to Other State Entities	Purpose
THECB	$	1,420	$		Federal P-T
Texas Agrilife Research		18,637			Federal P-T
TX DOT		78,406			Federal P-T
University of Houston		45,876			Federal P-T
TSUS				1,400	Shared Expense
TX DOT		10,550			License Plate Revenue for Scholarships
THECB		200			Over Payment in Transit to SHSU
	$	155,089	$	1,400	

TRANSFERS IN FROM/OUT TO OTHER STATE ENTITIES

Entity		Transfers In from Other State Entities		Transfers Out to Other State Entities	Purpose
TSUS	$	50,000,000	$		Bond Proceeds
TSUS				6,454,218	Bond Payment
TSUS				507,592	Shared Expense
THECB				699,184	Be on Time
THECB				11,524	Doctoral Set Asides
	$	50,000,000	$	7,672,518	

LEGISLATIVE TRANSFERS IN/OUT

Entity		Legislative Transfers In		Legislative Transfers Out	Purpose
TSUS	$		$	2,882,898	Bond Payment
	$	0	$	2,882,898	

Note 10: Contingent Liabilities

At August 31, 2008, various lawsuits and claims involving Sam Houston State University were pending. While the ultimate liability with respect to litigation and other claims asserted against the University cannot be reasonably estimated at this time, such liability, to the extent not provided for by insurance or otherwise, is not likely to have a material effect on the University.

Note 11: Risk Financing and Related Insurance

The State provides coverage for unemployment benefits for University employees from appropriations made to the Texas Workforce Commission (TWC). The current General Appropriations Act provides that the University must reimburse the General Revenue Fund, from University appropriations, 50% of the unemployment benefits paid for State funded positions and 100% of the cost for unemployment compensation for any positions paid from funds held in local bank accounts and local funds held in the State Treasury. The Comptroller of Public Accounts determines the proportionate amount to be reimbursed from each appropriated fund type. The unemployment benefit plan is on a pay-as-you-go basis, in which no assets are set aside to be accumulated for the payment of claims. It is estimated that there were no material liabilities as of August 31, 2008.

The administration of the State's employee workers' compensation program is vested with the State Office of Risk Management (SORM). In accordance with H.B. No. 1203, 77th Legislature, SORM developed and imposed a formula driven charge for workers' compensation costs upon participating agencies. The workers' compensation assessment is prepaid to SORM through an Interagency Contract for risk management services and workers' compensation coverage for its employees in compliance with TEX.LABOR CODE Chapter 412 and Chapter 501. The assessment for the University for FY 2008 was $243,572. The assessment for the University for FY 2009 is $270,840.

The University is required by certain bond covenants to carry fire and extended coverage and boiler insurance on buildings financed through the issuance of bonds using pledged Auxiliary Enterprise or other non-Educational and General Funds. The insurance protects the bond holders from a disruption to the revenue stream that is being utilized to make the bond interest and principal payments. The University had no insurance claims made during the fiscal year ended August 31, 2008.

The Texas Motor Vehicle Safety Responsibility Act requires that every non-governmental vehicle operated on a state highway be insured for minimum limits of liability in the amount of $20,000/$40, 000 bodily injury and $15,000 property damage. All vehicles owned and/or leased by the University are covered by one of two commercial insurance policies specifically customized for the Texas State University System. Both policies provide coverage to the extent of $1,000,000 combined single liability. The coverage exceeds the extent of the waivers of state immunity specified in the Texas Tort Claims Act, Civil Properties and Remedies Code Section 101.023.

The University is exposed to a variety of civil claims resulting from the performance of its duties. It is University policy to periodically assess the proper combination of commercial insurance and retention of risk to cover losses to which it may be exposed.

The University assumes substantially all risks associated with tort and liability claims due to the performance of its duties. Currently, there is no purchase of commercial insurance, nor is the University involved in any risk pools with other governmental entities.

The University's liabilities are reported when it is both probable that a loss has occurred and the amount of that loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported. Liabilities are reevaluated periodically to consider current settlements, frequency of claims, past experience and economic factors. There have been no significant reductions in insurance coverage in the past year and losses did not exceed coverage or funding arrangements during the past three years.

Note 12: Subsequent Events

There have been no subsequent events that would have a material effect on the University's financial statements for fiscal year ended August 31, 2008.

Note 13: Related Parties

There were no material transactions between the University and related parties during the fiscal year ended August 31, 2008.

Note 14: Stewardship, Compliance, and Accountability

Sam Houston State has no material violations of finance related and contract provisions and no new component units are included in the financial report. Per the laws of the State of Texas, Sam Houston State cannot spend amounts in excess of appropriations granted by the Texas Legislature and there are no deficits reported in net assets.

Note 15: The Financial Reporting Entity

Sam Houston State University is an agency of the State of Texas and a component of the Texas State University System and its financial records comply with applicable State statutes and regulations.

Component Units

Component Units are legally separate organizations for which the elected officials of the primary government are financially accountable. Sam Houston State University does not have any component units.

Related Organizations

"Related organizations" are organizations for which Sam Houston State University is accountable because the Texas State University System (TSUS) Board of Regents appoints a voting majority of the organization's board, but is not financially accountable. The Sam Houston Foundation is a related organization for Sam Houston State University.

The Sam Houston Foundation is a separate nonprofit organization which was established for the purpose of cooperating with and working on behalf of the University. Neither the balance nor the transactions of this organization's fund are reflected in the financial statements during the year ended August 31, 2008.

Gifts were made to the University from the Sam Houston Foundation for fiscal year 2008 of $25,000 to Endowment Funds.

Although not a "related organization" (because the TSUS Board of Regents does not appoint the organization's board), the SHSU Lettermen's Association's resources are held by the University in a purely custodial capacity. The SHSU Lettermen's Association was created in October 1974 for the stated purpose of providing a means for the former students of Sam Houston State University who won varsity letters in any of the sports recognized by the Conference to gather from time to time for certain fraternal beneficiary society purposes and to encourage support of the athletic staff and athletic programs of Sam Houston State University through the efforts of its members, including donations to Sam Houston State University for use by such educational institution.

The Lettermen's Association's funds are carried on the University's books, and comprise $20,975.31 of Total Deposits Held in Custody for Others - Agency Funds, at August 31, 2008. Sam Houston State University has performed stewardship functions in support of this account, including the receipt of deposits and payment of expenditures. A gift was made to the University from the Lettermen's Associations for fiscal year 2008 of $10,000 to Restricted Funds and $1,000 to Endowment Funds.

Note 16: Restatement of Net Assets

Sam Houston State University did not have a restatement of net assets to report.

Note 17: Employee Retirement Plans

The State of Texas has joint contributory retirement plans for substantially all of its employees. One of the primary plans in which the University participates is administered by the Teacher Retirement System of Texas (Retirement System). The contributory percentages currently provided by the State and by each participant are 6.58 percent and 6.4 percent, respectively, of annual compensation.

The Retirement System does not separately account for each of its component government agencies because the Retirement System itself bears sole responsibility for retirement commitments beyond contributions fixed by the State Legislature. Further information regarding actuarial assumptions and conclusions, together with audited financial statements, are included in the Retirement System's annual financial report, which may be found on the TRS website. (www.trs.state.tx.us)

The State has also established an Optional Retirement Program for institutions of higher education. Participation in the Optional Retirement Program is in lieu of participation in the Retirement System. The Optional Retirement Program provides for the purchase of annuity contracts and mutual funds. The contributory percentages of participant salaries provided by the State and by each participant enrolled in the plan on or before August 31, 1995, are 8.5 percent and 6.65 percent, respectively. The 8.5 percent is composed of 6.58 percent contributed by the State and an additional 1.92 percent contributed by the University. For participants who enrolled after September 1, 1995, State and participant contributions are 6.58 percent and 6.65 percent, respectively. Because these are individual annuity contracts, the State has no additional or unfunded liability for this program, and the University bears no responsibility for retirement commitments beyond contributions.

The retirement expense to the University was $4,372,064 for the year ended August 31, 2008. Of this amount, $2,946,702 represents the portion of appropriations made by the State Legislature expended on behalf of the University and $1,425,362 represents the portion paid from the University's funds.

Note 18: Deferred Compensation Program

University employees may elect to defer a portion of their earnings for income tax and investment purposes pursuant to authority granted in Texas Government Code, Section 609.001. Deferred compensation plans are administered by the Employees Retirement System.

The State's 457 Plan complies with Internal Revenue Code, Section 457. This plan is referred to as the Texa$aver Deferred Compensation Plan and is available to all employees. Deductions, purchased investments, and earnings attributed to the 457 Plan are the property of the State and subject only to the claims of the State's general creditors. Participant rights under the plan are equal to those of the general creditors of the State in an amount equal to the fair market value of the 457 account for each participant. The State has no liability under the 457 Plan, and it is unlikely that plan assets will be used to satisfy the claims of general creditors in the future.

The University also administers a Tax-Deferred Account Program, created in accordance with Internal Revenue Code, Section 403(b). All employees are eligible to participate. The Tax-Deferred Account Program is a private plan, and the deductions, purchased investments, and earnings attributed to each employee's 403(b) plan are held by vendors chosen by the employee. The vendors may be insurance companies, banks, or approved non-bank trustees such as mutual fund companies. The assets of this plan do not belong to the University, and thus it does not have a liability related to this plan.

Note 19: Donor-Restricted Endowments

Nonexpendable restricted net assets consist of endowments in which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income.

Donor-Restricted Endowment	Amounts Of Net Appreciation	Reported in Net Assets
True Endowments	$4,116,084	Restricted for Nonexpendable

Texas State University System Investment policy provides for a spending policy of no more than 5% of a 12 quarter rolling market value. Sam Houston State University defers their policy on spending net appreciation to the Texas State University System policy. This policy states the "Prudent person" standard will be used in the investment function and shall be applied in the context of individual transactions as well as management of the overall portfolio. Accordingly, all investments shall be made with judgment and care, under circumstances then prevailing, which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation, but for investment, emphasizing the probable safety of their capital.

Note 20: Post-Employment Health Care and Life Insurance Benefits

In addition to providing pension benefits, the State provides certain health and life insurance benefits for retired employees, in accordance with state statutes. Substantially all of the employees may become eligible for the health and life insurance benefits if they reach normal retirement age while working for the State. Currently, there are 482 retirees who are eligible for these benefits. Similar benefits for active employees are provided through a self-funded plan and fully insured plans.

Depending upon the status of the employee at the time of retirement, the State or the System recognizes the cost of providing these benefits. The cost of retiree post-employment benefits is recognized when paid. This contribution paid all of the "employee/retiree only" premiums and a portion of the premiums for those employees/retirees selecting dependent coverage.

The employee/retiree was required to pay a portion of the cost of dependent coverage. For the fiscal year ended August 31, 2008, the cost of providing those benefits for the retirees was $2,111,373 for the State and $320,812 for the University.

Note 21: Special or Extraordinary Items

Sam Houston State had no special or extraordinary items to report for the fiscal year ended August 31, 2008.

Note 22: Disaggregation of Receivable and Payable Balances

Sam Houston State University had the following aggregate receivable and payable balances as of August 31, 2008:

Current Receivables:

Federal Receivable	
Instructional and Departmental	$ 421,391
Research	1,769,508
Public Service	789,413
Scholarships and Fellowships	221,612
Academic Support	128,187
Total Net Federal Receivable	$ 3,330,111
As Reported on the Financial Statements	
Current Federal Receivable	$ 3,330,111
Non-Current Federal Receivable	0
Total Net Federal Receivable	$ 3,330,111
Accounts Receivable	
Installment Plans	$ 9,270,530
University Hotel	57,704
Raven Nest Golf Course	16,997
Returned Checks	18,470
Travel Advances	30,959
Contracts and Grants	345,780
Other Receivables	710,895
Total Net Accounts Receivable	$ 10,451,335

Accounts Receivable is reported net of Allowance for Doubtful Accounts. For FY 2008, Allowance for Doubtful Accounts ($454,711.05) decreased from FY 2007 Allowance for Doubtful Accounts ($774,409.08). This difference resulted in negative Bad Debt Expense of $319,698.03. This difference can be attributed to the assignment of collections on accounts to a collection agency on behalf of SHSU.

Noncurrent Receivables:

Pledge Receivables	$ 289,164

Current Payables:

Accounts Payable	
Capital	$ 2,471,407
Financial Aid Residual Checks	1,684,524
Other Payables	896,816
Total Accounts Payable	$ 5,052,747

Noncurrent Payables:

The amount shown on the Statement of Net Assets for "Other Non-Current Liabilities," consists of the following:

Type	Amount
U.S. Government Grants Refundable (Perkins/NDSL)	$ 599,182
Student Deposit Payables	641,903
Total	$1,241,085

Note 23: Termination Benefits

During the fiscal year ended August 31, 2008, Sam Houston State did not provide termination benefits.

State Auditor's Office
John Keel, CPA
State Auditor

March 3, 2009

Dr. James F. Gaertner, President
Sam Houston State University
1806 Ave. J, Suite 303
Huntsville, TX 77340

Subject: Management Letter Resulting from a Review of Sam Houston State University's Fiscal Year 2008 Financial Statements

Dear Dr. Gaertner:

We offer this management letter in conjunction with our review of the financial statements of Sam Houston State University (University) for the fiscal year ended August 31, 2008. We reviewed the Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; the Statement of Cash Flows; and the Notes to the Financial Statements. In the course of our review, which was substantially less in scope than an audit, we did not find that material modifications needed to be made to the financial statements in order for them to be in conformity with generally accepted accounting principles.

The University should ensure that all transactions that affect the information reported in the financial statements are properly recorded in the general ledger. The following are examples of some of the errors auditors identified:

- The University did not post year-to-year changes to the fair market value of investments to the general ledger.
- The University did not post a benefit adjustment for payroll expenses to the general ledger.
- The University did not post end-of-year deferred revenue adjustments for federal grants and state grants to the general ledger.

These issues could potentially create control weaknesses because the support for these adjustments is external documentation maintained by accounting staff. In addition, because the documentation is not included in the University's accounting system, there is no audit trail, and audit staff may not have sufficient documentation to ensure reported amounts are correct.

Robert E. Johnson Building
1501 N. Congress Avenue
Austin, Texas 78701

P.O. Box 12067
Austin, Texas 78711-2067

Phone:
(512) 936-9500

Fax:
(512) 936-9400

Internet:
www.sao.state.tx.us

Recommendations

The University should do the following when preparing future financial reports:

- Ensure that it properly records all transactions in the general ledger.
- Maintain sufficient documentation to ensure reported amounts are correct.

Management's Response

We find the recommendations from the State Auditors office to be sound and helpful. We will gladly comply with these recommendations. The Director of Administrative Accounting will book the recommended transactions each year beginning with the 2009 Annual Financial Report, as well as continuing to maintain the appropriate documentation.

The organization of the fiscal functions of the Division of Finance and Operations at Sam Houston State University is designed for separation of duties and correct control of assets, records, and cash in a way that has served us well. While the Accounting Office maintains the records, the Business Office controls the Cashiers Office, and Accounts Payable. The Business Office is responsible for disbursal of all payments by check, and most financial reporting including the Annual Financial Report. We believe that this separation provides protection against control weaknesses. The support for the adjustments in question is provided by the Accounting Office and reported by the Business Office. There is little opportunity for the Business Office to report otherwise, and we believe the audit trail can be provided by the Accounting Office.

We appreciate the assistance provided during this review by University management and the internal auditor. If you have any questions, please call me at (512) 936-9500.

Sincerely,

Sandra Vice

Sandra Vice, CIA, CGAP, CISA
Assistant State Auditor

TEXAS TECH UNIVERSITY SYSTEM™
Office of Audit Services

Texas Tech University Health Sciences Center

State Auditor's Office Review of 2008 Financial Statements

April 2, 2009
TTUS Project #2009025
SAO Report No. 09-331

Box 41104 | Lubbock, Texas 79409-1104 | T 806.742.3220 | F 806.742.3219

Contents

State Auditor's Office
John Keel, CPA
State Auditor

Auditor's Review Report

April 2, 2009

Dr. John C. Baldwin, President
Texas Tech University Health Sciences Center
3601 4th Street, MS 6258
Lubbock, TX 79430

Dear Dr. Baldwin:

We have reviewed the accompanying Statement of Net Assets; Statement of Revenues, Expenses, and Changes in Net Assets; Statement of Cash Flows; and Notes to the Financial Statements of Texas Tech University Health Sciences Center University (Health Sciences Center) as of and for the fiscal year ended August 31, 2008, in accordance with *Statements on Standards for Accounting and Review Services* issued by the American Institute of Certified Public Accountants. The review was performed in accordance with the Southern Association of Colleges and Schools' (Southern Association) *Criteria for Accreditation*. All information included in these financial statements is the representation of management of the Health Sciences Center.

A review consists principally of inquiries of Health Sciences Center personnel and analytical procedures applied to financial data. A review is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

The accompanying statements were prepared to present the financial position, the changes in financial position and the cash flows of the Health Sciences Center. These statements are prepared pursuant to criteria of the Southern Association for supplementary special reports by institutions in states that conduct statewide audits.

Based on our review, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with generally accepted accounting principles.

The Health Sciences Center has not presented a management's discussion and analysis section that the Governmental Accounting Standards Board has identified as required supplementary information that is not part of the basic financial statements. However, such required supplementary information for the Texas Tech University System (System) is presented in the System's consolidated annual financial report.

This report is intended for use by the Board of Regents of the System, management of the Health Sciences Center, and the Southern Association. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

Sincerely,

John Keel, CPA
State Auditor

Robert E. Johnson Building
1501 N. Congress Avenue
Austin, Texas 78701

P.O. Box 12067
Austin, Texas 78711-2067

Phone:
(512) 936-9500

Fax:
(512) 936-9400

Internet:
www.sao.state.tx.us

Texas Tech University Health Sciences Center

Statement of Net Assets

At August 31, 2008

(See Auditor's Review Report on page 1.)

		Current Year
ASSETS		
Current Assets		
Cash and Cash Equivalents (Note 3)	$	173,846,811
Restricted:		
Cash and Cash Equivalents (Note 3)		30,383,647
Legislative Appropriations		43,725,613
Receivables, Net of Allowances:		
Federal		1,372,370
Interest and Dividends		914,965
Student Accounts		996,193
Patient Accounts		17,323,869
Contract Accounts		14,271,190
Gifts		2,443,610
Other		16,454
Due from Other State Entities (Note 9)		5,095,553
Consumable Inventories		19,419
Merchandise Inventories		852,546
Prepaid Expenses		1,293,303
Loans and Contracts		308,609
Total Current Assets	$	292,864,152
Non-Current Assets		
Restricted:		
Cash and Cash Equivalents (Note 3)	$	(16,066)
Gifts Receivable		5,661,391
Investments (Note 3)		248,313,338
Loans and Contracts		2,576,791
Capital Assets:		
Non-Depreciable		71,072,084
Depreciable		436,162,549
Less: Accumulated Depreciation		(199,627,360)
Total Non-Current Assets	$	564,142,727
Total Assets	$	857,006,879

LIABILITIES		
Current Liabilities		
Payables:		
Accounts	$	19,132,221
Payroll		31,770,614
Due to Other State Entities (Note 9)		158,485
Deferred Revenue		10,952,889
Claims and Judgments (Note 5)		1,862,761
Employees' Compensable Leave (Note 5)		4,894,411
Notes and Loans Payable (Note 5)		3,193,000
Accrued Bond Interest Payable		285,557
Revenue Bonds Payable (Notes 5,6)		5,653,290
Unclaimed Property Due to the State Treasury		29,701
Funds Held for Others		167,339
Other Current Liabilities		210
Total Current Liabilities	$	78,100,478
Non-Current Liabilities		
Claims and Judgments (Note 5)	$	16,764,846
Employees' Compensable Leave (Note 5)		19,577,643
Revenue Bonds Payable (Notes 5, 6)		115,321,259
Unclaimed Property Due to the State Treasury		84,673
Other Non-Current Liabilities		695,990
Total Non-Current Liabilities	$	152,444,411
Total Liabilities	$	230,544,889
NET ASSETS		
Invested in Capital Assets, Net of Related Debt	$	183,439,725
Restricted for:		
Non-Expendable		
Permanent Funds, True Endowments, Annuities		107,275,336
Expendable		
Capital Projects		9,582,754
Other		33,382,592
Unrestricted		292,781,583
Total Net Assets	$	626,461,990

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

Texas Tech University Health Sciences Center

Statement of Revenues, Expenses, and Changes in Net Assets

At August 31, 2008
(See Auditor's Review Report on page 1.)

		Current Year
OPERATING REVENUES		
Tuition and Fees - Non-Pledged	$	4,278,669
Discounts and Allowances		(3,984,359)
Tuition and Fees - Pledged		19,494,567
Professional Fees		245,554,314
Discounts and Allowances		(28,578,097)
Auxiliary Enterprises		464,053
Other Sales of Goods and Services - Non-Pledged		1,430,430
Other Sales of Goods and Services - Pledged		2,547,056
Federal Revenue		14,955,809
State Grant and Contract Revenue		6,639,778
Local Grant and Contract Revenue		84,526,756
Private Grant and Contract Revenue		29,386,672
Total Operating Revenues	$	376,715,648
OPERATING EXPENSES		
Salaries and Wages	$	293,440,991
Payroll Related Costs		70,218,159
Professional Fees and Services		56,210,795
Travel		4,711,203
Materials and Supplies		54,696,489
Communications and Utilities		13,031,773
Repairs and Maintenance		4,340,392
Rentals and Leases		3,268,538
Printing and Reproduction		1,706,687
Depreciation and Amortization		15,221,289
Bad Debt Expense		35,919
Interest Expense		12,926
Scholarships		1,223,967
Claims and Judgments		565,868
Other Operating Expenses		3,449,105
Total Operating Expenses	$	522,134,101
Operating Income (Loss)	$	(145,418,453)

NONOPERATING REVENUES (EXPENSES)		
Legislative Appropriations	$	184,654,319
Gifts		4,064,809
Federal Grants and Contracts		371,621
Interest and Investment Income (Loss)-Unpledged		9,279,839
Interest and Investment Income (Loss)-Pledged		5,765,691
Net Increase (Decrease) in Fair Value of Investments		(11,047,472)
Interest Expense on Capital Asset Financing		(5,239,812)
Gain (Loss) on Sale of Capital Assets		(478,448)
Other Non-operating Revenues - Non-Pledged		155,049
Other Non-operating Revenues - Pledged		283,563
Other Non-operating Expenses		(37,189)
Total Non-operating Revenues (Expenses)	$	187,771,970
Income (Loss) Before Other Revenues, Expenses, Gains (Losses), and Transfers	$	42,353,517
OTHER REVENUES, EXPENSES, GAINS (LOSSES), AND TRANSFERS		
Capital Contributions	$	9,594,330
Capital Appropriations (HEAF)		17,849,441
Capital Recoveries		110,505
Transfers In from Other State Entities (Note 9)		1,662,467
Transfers Out to Other State Entities (Note 9)		(6,920,382)
Legislative Transfers Out (Note 9)		(2,581,987)
Total Other Revenues, Expenses, Gains (Losses), and Transfers	$	19,714,374
CHANGE IN NET ASSETS	$	62,067,891
Net Assets, September 1, 2007	$	564,394,099
NET ASSETS, August 31, 2008	$	626,461,990

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

Texas Tech University Health Sciences Center

Statement of Cash Flows

At August 31, 2008
(See Auditor's Review Report on page 1.)

		Current Year
CASH FLOWS FROM OPERATING ACTIVITIES		
Proceeds from Tuition and Fees	$	21,411,408
Proceeds from Grants and Contracts		131,914,763
Proceeds from Patients and Insurers		215,815,297
Proceeds from Loan Programs		1,139,837
Proceeds from Auxiliaries		464,053
Proceeds from Other Revenues		4,229,004
Payments to Suppliers for Goods and Services		(212,000,022)
Payments to Employees for Salaries		(291,766,383)
Payments for Auxiliary Enterprises		(329,877)
Payments for Loans Provided		(1,434,970)
Payments for Other Expenses		(4,047,300)
Net Cash Provided (Used) by Operating Activities	$	(134,604,190)
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Proceeds from Legislative Appropriations	$	163,497,179
Proceeds from Gifts		7,076,634
Proceeds of Transfers from Other Entities		1,227,416
Proceeds from Other Sources		435,141
Proceeds from Direct Lending		39,032,174
Payments for Net Transfers to Texas Tech University System		(3,943,713)
Payments for Direct Lending		(39,051,218)
Payments for Transfers to Other Entities		(4,617,894)
Net Cash Provided (Used) by Non-Capital Financing Activities	$	163,655,719
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from State Appropriations (HEAF)	$	17,849,441
Proceeds from Gifts		9,594,330
Proceeds from Issuance of Capital-Related Debt		6,000,000
Payments for Additions to Capital Assets		(50,785,680)
Payments of Principal on Capital-Related Debt		(8,214,451)
Payments of Interest on Capital-Related Debt		(6,054,739)
Payments of Other Costs of Capital-Related Debt		(53,659)
Net Cash Provided (Used) by Capital and Related Financing Activities	$	(31,664,758)

CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from Sales of Investments	$	21,297,491
Proceeds from Interest and Investment Income		17,275,102
Payments to Acquire Investments		(8,835,098)
Net Cash Provided (Used) by Investing Activities	$	29,737,495
Net Increase (Decrease) in Cash and Cash Equivalents	$	27,124,266
Cash and Cash Equivalents, September 1, 2007	$	177,090,126
Cash and Cash Equivalents, August 31, 2008	$	204,214,392

Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities

Operating Income (Loss)	$	(145,418,453)
Adjustments:		
Depreciation and Amortization	$	15,221,289
Bad Debt Expense		35,919
Changes in Assets and Liabilities:		
(Increase) Decrease in Receivables		(5,070,699)
(Increase) Decrease in Inventories		(105,477)
(Increase) Decrease in Prepaid Expenses		(776,221)
(Increase) Decrease in Loans and Contracts		(295,133)
Increase (Decrease) in Payables		1,279,843
Increase (Decrease) in Claims Payable		(4,013,806)
Increase (Decrease) in Deferred Revenue		2,006,575
Increase (Decrease) in Employees' Compensable Leave		2,339,924
Increase (Decrease) in Other Liabilities		192,049
Total Adjustments	$	10,814,263
Net Cash Provided (Used) by Operating Activities	$	(134,604,190)
Non-Cash Transactions		
Net Increase (Decrease) in Fair Value of Investments	$	(11,047,472)
Disposal of Capital Assets		9,001,881
Other Deductions to Capital Assets		4,239,762

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

Texas Tech University Health Sciences Center

Statement of Changes in Unrestricted Net Assets

At August 31, 2008

	8/31/2008	8/31/2007	Difference
Reserved			
Encumbrances	$ 28,500,038	$ 22,224,388	$ 6,275,650
Accounts Receivable	30,159,349	27,888,765	2,270,584
Inventories	871,965	766,488	105,477
Self-Insurance Plans	40,843,081	46,308,845	(5,465,764)
Funds Functioning as Endowments	28,168,126	24,403,073	3,765,053
Prepaid Expenses	1,293,303	517,082	776,221
Petty Cash	54,761	51,808	2,953
Unreserved			
Unallocated	162,890,960	132,152,095	30,738,865
Total Unrestricted Net Assets	$ 292,781,583	$ 254,312,544	$ 38,469,039

(See Auditor's Review Report on page 1.)

General Introduction

This report has been prepared for the use of the Southern Association of Colleges and Schools (Southern Association) in connection with the review of Texas Tech University Health Sciences Center (TTUHSC) for accreditation purposes. This report includes a Statement of Net Assets; a Statement of Revenues, Expenses, and Changes in Net Assets; a Statement of Cash Flows; and the related Notes to the Financial Statements. In accordance with Southern Association criteria or Governmental Accounting Standards Board requirements, the report also includes a Management's Discussion and Analysis section, a Statement of Changes in Unrestricted Net Assets, and a Management Letter describing issues noted in the review.

Reporting Entity

TTUHSC is a component of Texas Tech University System and an agency of the State of Texas. TTUHSC prepares financial statements that are included in the State's *Comprehensive Annual Financial Report,* which is audited by the Texas State Auditor's Office.

Note 1: Summary of Significant Accounting Policies

Basis of Accounting

The basis of accounting determines when revenues and expenditures or expenses are recognized in the accounts reported in the financial statements. The accounting and financial reporting treatment applied to a fund is determined by its measurement focus.

For financial reporting purposes, TTUHSC is considered a special-purpose government engaged only in business-type activities. Accordingly, TTUHSC's financial statements have been presented using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized at the time liabilities are incurred. Operating items are distinguished from non-operating items. Operating revenues and expenses result from providing services or producing and delivering goods in connection with the principle of ongoing operations. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets.

Cash and Cash Equivalents

Cash and cash equivalents are defined as all cash on hand, cash in banks, reimbursements due from the State Treasury, local balances of legislative appropriations (held in the State Treasury), and temporary investments with original maturities of 90 days or less. TTUHSC utilizes bank deposits, repurchase agreements and eligible investment pools as cash equivalents in its Short/Intermediate Term Investment Fund. Per policy and state statute all bank deposits are fully collateralized. Eligible investment pools must maintain a $1 net asset value and be continuously rated no lower than AAA or AAA-m by at least one nationally recognized rating service. TTUHSC currently utilizes TexPool and TexStar as eligible investment pools.

Restricted Net Assets

In cases where both restricted and unrestricted net assets are available for use, restricted resources are used first and then unrestricted resources are used as needed.

Note 2: Capital Assets

Capital assets are categorized as either (1) land and land improvements, (2) buildings and building improvements, (3) infrastructure, (4) furniture and equipment, (5) vehicles, (6) construction in progress, (7) other capital assets, or (8) facilities and other improvements. Non-depreciable capital assets include land and land improvements, construction in progress, and other capital assets (representing artwork). All other capital asset categories are depreciated.

Adjustments include loss recovery, restatements, corrections of errors and changes in asset type. Capital assets are recorded at cost at the date of acquisition or, in the case of gifts, at fair value as of the date of donation.

Depreciation of capital assets is recorded as a periodic expense and accumulated as an offset to the asset book values. Depreciation of capital assets is based on allocation methods and estimated lives prescribed by the Statewide Property Accounting (SPA) system as summarized below.

Capital Asset Category	Useful Life
Buildings and Building Improvements	22 years
Infrastructure	20 years
Furniture and Equipment	3 – 15 years
Vehicles	5 – 7 years
Facilities and Other Improvements	10 – 23 years

TTUHSC has adopted the federal standard of capitalizing furniture and equipment assets that exceed an aggregate cost threshold of $5,000. Capitalization thresholds are also utilized for buildings and building improvements ($100,000), infrastructure ($500,000), facilities and other improvements ($100,000), and vehicles ($5,000).

For fabricated assets financed by debt, construction period interest is capitalized as part of the capital asset cost. The capitalized interest is combined with the other costs associated with constructing the asset and depreciated over the appropriate useful life beginning when the asset is placed into service.

As a result of limitations in the SPA system, capital asset betterments that do not individually exceed the full capitalization threshold described above are not capitalized and instead are reported as an expense of the period.

	Balance 9/1/2007	Adjustments	Completed Construction in Progress	Additions	Deductions	Balance 8/31/2008
Non-Depreciable Assets:						
Land and Land Improvements	$ 6,307,286	$	$	$ 1,341,032	$	$ 7,648,318
Construction in Progress	77,251,452		(35,664,760)	20,593,670		62,180,362
Other Capital Assets	618,404			625,000		1,243,404
Total Non-Depreciable Assets	$ 84,177,142	$	$ (35,664,760)	$ 22,559,702	$	$ 71,072,084
Depreciable Assets:						
Buildings and Building Improvements	$ 281,040,652	$ (16,418)	$ 35,664,760	$ 17,366,705	$ (6,545,838)	$ 327,509,861
Infrastructure	5,050,660					5,050,660
Facilities and Other Improvements	9,133,460	(3,851,621)		5,139,492		10,421,331
Furniture and Equipment	$ 54,814,511	$ (6,914)	$	$ 10,639,447	$ (2,955,729)	$ 62,491,315
Vehicles, Boats, and Aircraft	1,662,774			241,146	(90,252)	1,813,668
Other Capital Assets	27,016,094	(20,237)		1,879,857		28,875,714
Total Depreciable Assets at Historical Cost	$ 378,718,151	$ (3,895,190)	$ 35,664,760	$ 35,266,647	(9,591,819)	$ 436,162,549

(table continued on next page)

		Balance 9/1/2007		Adjustments		Completed Construction in Progress		Additions		Deductions		Balance 8/31/2008
Less Accumulated Depreciation for:												
Buildings and Building Improvements	$	(135,194,367)	$		$		$	(8,750,232)	$	3,784,656	$	(140,159,943)
Infrastructure		(911,530)						(213,490)				(1,125,020)
Facilities and Other Improvements		(2,323,710)		700,575				(268,351)				(1,891,486)
Furniture and Equipment		(34,918,385)						(4,818,314)		2,066,051		(37,670,648)
Vehicles, Boats, and Aircraft		(1,143,458)						(174,832)		52,836		(1,265,454)
Other Capital Assets		(16,318,705)						(1,196,104)				(17,514,809)
Total Accumulated Depreciation	$	(190,810,155)	$	700,575	$	0	$	(15,421,323)	$	5,903,543	$	(199,627,360)
Depreciable Assets, Net	$	187,907,996	$	(3,194,615)	$	35,664,760	$	19,845,324	$	(3,688,276)	$	236,535,189
Capital Assets, Net	$	272,085,138	$	(3,194,615)	$	0	$	42,405,026	$	(3,688,276)	$	307,607,273

Note 3: Deposits, Investments, and Repurchase Agreements

TTUHSC's investment portfolio is invested pursuant to the parameters of applicable Texas law and the governing board's Investment Policies. Under Texas law, TTUHSC investments may be "any kind of investment that persons of ordinary prudence, discretion, and intelligence, exercising the judgment and care under the circumstances then prevailing, acquire or retain for their own account in the management of their affairs, not in regard to speculation but in regard to the permanent disposition of their funds, considering the probable income as well as the probable safety of their capital." Further, under Texas law, TTUHSC is required to invest its institutional funds according to written investment policies adopted by the Board of Regents. No person may invest TTUHSC funds without express written authority from the governing board.

The governing investment policy is Regents' Rules Chapter 09, "Investments, Endowments, and Income-Producing Lands." The majority of TTUHSC assets are invested in two investment pools: the Long Term Investment Fund (LTIF) and the Short / Intermediate Term Investment Fund (STIF). Endowment funds and certain eligible long term institutional funds are invested in the LTIF, which invests in equity and fixed income securities and is operated using a total return philosophy. Other institutional funds not in the LTIF are invested in the STIF, which is a fixed income fund. Other assets include securities gifted to TTUHSC with written donor instructions to maintain in their original form, and bond proceeds invested in external investment pools. TTUHSC also maintains a cash balance in the State Treasury (local balance of legislative appropriations).

DEPOSITS

		Bank Balance
Cash on Hand	$	28,998
Cash in Bank		15,418,451
Reimbursement Due from Treasury		6,539,717
Cash in State Treasury		12,031,967
Cash Equivalents		170,195,259
Total Cash and Cash Equivalents	$	204,214,392
Current Assets Cash and Cash Equivalents	$	173,846,811
Current Assets Restricted Cash and Cash Equivalents		30,383,647
Non-Current Assets Restricted Cash and Cash Equivalents		(16,066)
Total Cash and Cash Equivalents	$	204,214,392

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the agency will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The policy of TTUHSC is to require collateralization of bank balances in excess of FDIC protection. At August 31, 2008, TTUHSC had $149,911 of funds considered to be uninsured and uncollateralized. A transfer of that amount was made to the primary depository of TTUHSC after year end to provide sufficient collateral for the institution.

INVESTMENTS

U. S. Government Agency Obligations (Ginnie Mae, Fannie Mae, Freddie Mac, Sallie Mae, etc.)	$	62,054,691
Equity		13,939,000
International Equity		28,279,061
Fixed Income Money Market and Bond Mutual Fund		36,809,444
Other Commingled Funds		22,913,899
Alternative Investments (including limited partnerships and hedge funds)		84,058,422
Misc (e.g., guaranteed investment contract, political subdivision, bankers' acceptance, negotiable CD)		258,821
Total Investments	$	248,313,338
Non-Current Assets – Investments	$	248,313,338
Total Investments	$	248,313,338

Foreign currency risk for investments is the risk that changes in exchange rates will adversely affect the investment. It is the policy of TTUHSC to limit international equity investments to between 10-30% of the LTIF portfolio. The exposure to foreign currency risk as of August 31, 2008 is as follows:

Foreign Currency	International Obligation	International Equity
Argentine peso	-	$ 36,978
Australian dollar	-	514,986
Bermudan dollar	-	81,394
Brazilian real	-	1,350,444
Canadian dollar	-	174,860
Cayman dollar	-	5,159
Chilean peso	-	12,326
Chinese yuan	-	569,055
Czech koruna	-	36,978
Danish krone	-	266,084
Egyptian pound	-	49,304
Euro	-	6,640,273
Hong Kong dollar	-	713,719
Hungarian forint	-	166,400
Indian rupee	-	272,495
Indonesian rupiah	-	43,141
Israeli shekel	-	351,774
Japanese yen	-	4,717,444
Malaysian ringgit	-	165,187
Mexican peso	-	216,573
Moroccan dirham	-	12,326
New Zealand dollar	-	11,124
Norwegian krone	-	216,746
Pakistani rupee	-	36,978
Phillippino peso	-	55,467
Polish zloty	-	67,792
Pound sterling	-	4,930,240
Russian ruble	-	603,970
Singapore dollar	-	595,078
South African rand	-	301,985
South Korean won	-	1,409,863
Swedish krona	-	336,415
Swiss franc	-	1,577,674
Taiwan dollar	-	830,580
Thai baht	-	453,419
Turkish lira	-	454,830
Total		$ 28,279,061

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. TTUHSC's investment policy limits fixed income securities held by the STIF to those issued by the U.S. or its agencies and instrumentalities. Fixed income mutual funds in the STIF must hold securities that are at least rated investment grade.

Standard & Poor's

Investment Type	AAA	Unrated
U. S. Government Agency Obligations	$ 62,054,691	-
Repurchase Agreement	16,288,145	-
Fixed Income Money Market and Bond Mutual Fund	-	36,809,444

Concentration of credit risk is the risk of loss attributable to the magnitude of investment in a single issuer.

As of August 31, 2008, TTUHSC's concentration of credit risk is as follows:

Fund Type	GAAP Fund	Issuer	Carrying Value	% of total portfolio
01	0001	Federal Home Loan Bank	$ 25,701,458	5.07%

Interest rate risk is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. Duration is a measure of the price sensitivity of a debt investment to changes arising from movements in interest rates. Duration is the weighted average maturity of an instrument's cash flows, where the present value of the cash flows serves as the weights. The duration of an instrument can be calculated by first multiplying the time until receipt of cash flow by the ratio of the present value of that cash flow to the instrument's total present value. The sum of these weighted time periods is the duration of the instrument. Modified duration estimates the sensitivity of the institution's investments to changes in interest rates. TTUHSC does not have a formal investment policy with regards to interest rate risk.

TTUHSC's investments by investment type, fair value, and modified duration as of August 31, 2008 are as follows:

Investments Exposed to Interest Rate Risk

Investment Type	Fair Value	Modified Duration
U.S. Government Non-Guaranteed:		
U.S. Agency	53,294,951	0.918
U.S. Agency Asset Backed	10,959,296	7.961
Total U.S. Government	64,254,247	
Fixed Income Mutual Funds	27,140,314	5.426

Derivative Investing

TTUHSC holds collateralized mortgage obligations. These securities were purchased to provide an incremental yield above that available on corporate securities with similar terms. The overall return or yield on mortgage-backed securities depends on the amount of interest collected over the life of the security and the change in the fair value. It is estimated these securities, along with other securities held by TTUHSC, will provide future cash inflows on a time schedule that approximately matches the outflows associated with TTUHSC liabilities. These securities are rated AAA by the major rating agencies.

Note 4: Summary of Short-Term Liabilities

TTUHSC has at times over the past several years issued short term commercial paper to serve as an interim financing source for long term construction projects in advance of issuing authorized bonds. All Notes Payable outstanding will mature within 12 months of fiscal year end and are therefore classified as current liabilities.

	Balance 9/1/2007	Additions	Deductions	Balance 8/31/2008
Commercial Paper Payable	$ 0	$ 6,000,000	$ 2,807,000	$ 3,193,000
Total	$ 0	$ 6,000,000	$ 2,807,000	$ 3,193,000

Note 5: Summary of Long-Term Liabilities

Several categories of long-term liabilities are reported for TTUHSC. These include claims payable, employee compensable leave and revenue bonds payable.

	Balance 9/1/2007	Additions	Deductions	Balance 8/31/2008	Amounts Due Within One Year
Claims and Judgments	$ 22,641,413	$	$ 4,013,806	$ 18,627,607	$ 1,862,761
Employees' Compensable Leave	22,132,130	3,588,396	1,248,472	24,472,054	4,894,411
Revenue Bonds Payable	126,382,000		5,407,451	120,974,549	5,653,290
Total	$ 171,155,543	$ 3,588,396	$ 10,669,729	$ 164,074,210	$ 12,410,462

Claims Payable

Claims payable includes estimates for both known medical malpractice claims and those that have not yet been made against the insured participants. The liability is actuarially estimated to reflect the anticipated future claims for past medical services. Some of these claims are in process, while others are expected to be filed in the future. The liability estimate does not consider the probability of payment on a claim-by-claim basis, and instead considers overall probability of payment for medical malpractice claims. Funding for future claim payments will be from a self-insurance reserve managed by the office of General Counsel.

Employees' Compensable Leave

Substantially all full-time TTUHSC employees earn annual leave in the amount of 8 to 21 hours per month depending upon the respective employee's years of state employment. State law permits employees to carry accrued leave forward from one fiscal year to another fiscal year with a maximum of 532 hours for those employees with 35 or more years of state service. Eligible part-time employees' annual leave accrual rate and maximum carryover are proportional to the number of hours appointed to work. Employees with at least six months of state service who terminate their employment are entitled to payment for all accumulated annual leave.

Sick leave, the accumulation of which is unlimited, is earned at the rate of eight hours per month and is paid only when an employee is off due to illness or to the estate of an employee in the event of his or her death. The maximum sick leave that may be paid to an employee's estate is one half of the employee's accumulated entitlement or 336 hours, whichever is less. TTUHSC's policy is to recognize the cost of sick leave when paid, and the liability is not shown in the financial statements because experience indicates that the expense for sick leave will be minimal. Eligible part-time employees' sick leave accrual rate is proportional to the number of hours appointed to work.

Note 6: Bonded Indebtedness

At August 31, 2008, TTUHSC had outstanding bonds payable of $120,974,549. All bonds issued for TTUHSC are defined as revenue bonds.

REVENUE FINANCING SYSTEM REFUNDING AND IMPROVEMENT BONDS, SERIES 1999

Purpose:	Financing for projects in Amarillo, Midland, and Lubbock, the costs of issuing the bonds, and the advance refunding of a portion of the Revenue Financing System Bonds, 2nd Series 1995
Issued:	May 4, 1999; all authorized bonds ($15,632,182) have been issued
Outstanding:	$5,663,301 outstanding as of August 31, 2008
Interest Rates:	4.00% to 5.25%
Maturity Dates:	1999 through 2029
Balance Changes:	$0 issued; $768,843 retired

REVENUE FINANCING SYSTEM BONDS, 7th SERIES 2001

Purpose: Financing for projects in El Paso and Lubbock, the costs of issuing the bonds, and the retirement of outstanding commercial paper

Issued: January 23, 2002; all authorized bonds ($19,510,000) have been issued

Outstanding: $4,410,000 outstanding as of August 31, 2008

Interest Rates: 3.00% to 5.50%

Maturity Dates: 2002 through 2021

Balance Changes: $0 issued; $755,000 retired

REVENUE FINANCING SYSTEM BONDS, 9th SERIES 2003

Purpose: Financing for projects in El Paso and Lubbock, the costs of issuing the bonds, and the retirement of outstanding commercial paper

Issued: September 24, 2003; all authorized bonds ($64,270,000) have been issued

Outstanding: $56,940,000 outstanding as of August 31, 2008

Interest Rates: 4.00% to 5.25%

Maturity Dates: 2006 through 2023

Balance Changes: $0 issued; $2,520,000 retired

REVENUE FINANCING SYSTEM REFUNDING AND IMPROVEMENT BONDS, 10th SERIES 2006

Purpose: Financing for Medical Education Building project in El Paso, the costs of issuing the bonds, and the advance refunding of a portion of the Revenue Financing System Bonds, Series 1999 and Revenue Financing System Bonds, 7th Series 2001

Issued: February 1, 2006; all authorized bonds ($59,694,524) have been issued which includes $45,000,000 of new bonds for the project

Outstanding: $53,961,248 outstanding as of August 31, 2008

Interest Rates: 4.00% to 5.00%

Maturity Dates: 2006 through 2029

Balance Changes: $0 issued; $1,363,607 retired

Sources of Revenue for Debt Service

On October 21, 1993, the governing board of the Texas Tech University System established a Revenue Financing System for the purpose of providing a financing structure for all revenue supported indebtedness of Texas Tech University System components. The source of revenues for debt service issued under the Revenue Financing System includes pledged general tuition, pledged tuition fees, pledged general fees and any other revenues, income, receipts, rentals, rates, charges, fees, including interest or other income, and balances lawfully available to Texas Tech University System components. Excluded from the revenues described above are amounts received under Article 7, § 17 of the

Constitution of the State of Texas, general revenue funds appropriated by the Texas Legislature except to the extent so specifically appropriated, encumbered housing revenues, and practice plan funds.

Defeased Bonds Outstanding

As of August 31, 2008, a total of $15,285,000 of defeased bonds was outstanding related to an advance refunding of a portion of the Revenue Financing System Bonds, 3rd Series, 1999 and Revenue Financing System Bonds, 7th Series, 2001.

REVENUE BONDS PAYABLE

Year		Total Principal		Total Interest
2009	$	5,653,290	$	5,814,103
2010		5,893,738		5,570,394
2011		6,167,415		5,298,727
2012		6,482,446		4,988,107
2013		6,820,829		4,650,202
2014 - 2018		37,114,625		17,544,490
2019 - 2023		41,864,307		7,835,435
2024 - 2028		10,573,899		1,005,992
2029 - 2033		404,000		10,100
Total	$	120,974,549	$	52,717,550

Note 7: Capital Leases

TTUHSC had no leases that qualified for capitalization as of August 31, 2008.

Note 8: Operating Leases

TTUHSC leases various buildings and equipment under operating lease rental agreements. Operating leases do not give rise to property rights and, therefore, the related assets and liabilities are not reported in this *Annual Financial Report*. Total rental expense under these agreements was $4,161,948 for the year ended August 31, 2008.

Year Ended August 31,		**Total**
2009	$	4,286,807
2010		4,415,411
2011		4,547,873
2012		4,684,310
2013		4,824,839
Total Minimum Future Lease Payments	$	22,759,240

TTUHSC structures all leases to allow for cancellation within the current period. Most of the cancellation clauses are based on a 30-day notice condition or on the condition of continuing appropriations. However, there is little or no historical precedence for lease cancellations at TTUHSC.

Note 9: Interagency Balances / Activity

TTUHSC is regularly involved in both interfund activity and interfund transactions. Interfund activity is defined as financial interaction between internal funds, including blended component units.

Interfund transactions are defined as financial interactions between legally separate entities. Interfund activity and interfund transactions are both clearly identifiable and are eliminated where appropriate.

Interfund transfers represent the flow of assets without equivalent flow of assets in return or a requirement for repayment. Transfers are reported after non-operating revenues and expenses in Statement of Revenues, Expenses and Changes in Net Assets included in this *Annual Financial Report.*

DUE FROM / TO OTHER STATE ENTITIES

Entity		Due from Other State Entities		Due to Other State Entities	Purpose
University of Texas System	$	5,095,553	$		Undistributed earnings from investments
Texas Tech University				158,485	Shared services
	$	5,095,553	$	158,485	

TRANSFERS IN / OUT WITH OTHER STATE ENTITIES

Entity		Transfers In from Other State Entities		Transfers Out to Other State Entities	Purpose
Texas Tech University	$	1,550,382	$	874,011	Shared appropriations for debt payments, student support, capital asset transfers
Texas Tech University System		70,741		1,428,477	System Administration support, capital asset transfers
University of Texas System		41,344			Capital asset transfers
Texas Department of State Health Services				4,500,000	Upper Payment Limit agreement
Texas Higher Education Coordinating Board				117,894	Tuition set asides
	$	1,662,467	$	6,920,382	

LEGISLATIVE TRANSFERS IN / OUT

Entity		Legislative Transfers In		Legislative Transfers Out	Purpose
Texas Tech University System	$		$	2,581,987	System Administration support
	$	0	$	2,581,987	

Note 10: Contingent Liabilities

Pending Litigation

At August 31, 2008, various lawsuits and claims involving TTUHSC were pending. While the ultimate liability with respect to litigation and other claims asserted against TTUHSC cannot be reasonably estimated at this time, such liability, to the extent not provided for by insurance, is not likely to have a material impact on TTUHSC.

Rebatable Arbitrage

As of August 31, 2008, the Revenue Financing System and Improvement Bonds, Series 2006, was the only outstanding bond issue of TTUHSC which had an associated outstanding rebatable arbitrage liability amounting to $687,221. This liability is payable on the fifth anniversary of the bond issue which will occur in 2011. These rebatable excesses were earned during periods when unrestricted yield was allowed on these funds. As required by the Internal Revenue Code, TTUHSC will restrict earnings on these funds to a yield less than the yield of the bond issue after this unrestricted yield period ends.

Construction Contract Commitments

Numerous large contracts have been entered into for the purposes of planning, constructing, and equipping building additions and other projects. Outstanding commitment amounts totaled $22,800,490 as of August 31, 2008. These commitments will be funded by donor contributions, appropriations from the state, issuance of revenue bonds, and other borrowings. As of August 31, 2008, the amount of legislative appropriations for capital from the state available for these commitments totaled $3,286,789.

Direct Lending

TTUHSC participates in the federal Direct Loan Program, which provides loans from the federal government to qualifying students and their families for educational purposes. While TTUHSC helps students to obtain these loans, the institution is not a party to the loans and is not responsible for collection of monies owed or for defaults by borrowers. The amount of direct loans issued during the year ended August 31, 2008 was $39,051,218.

Note 11: Risk Financing and Related Insurance

Medical Malpractice Insurance Plan

The TTUHSC medical malpractice self insurance plan, an occurrence based plan, was established in 1985. The plan had an actuarially determined accrued incurred but not reported (IBNR) liability at August 31, 2008, of $18,627,607. A reconciliation of IBNR is provided in the table in Note 5.

Claim limits associated with the plan are $400,000 per occurrence and $1,200,000 aggregate per annum for services provided by faculty physicians (unless lower limits are set by law, in which case the lower limits set by law apply), $100,000 per occurrence and $300,000 aggregate per annum for services provided by resident physicians, and $25,000 per occurrence and $75,000 aggregate per annum for services provided by students.

As of September 1, 2003, providers of health care (physicians) are no longer excepted from the statutory limits of liability set for public servants as set out in § 108.002 of the Texas Civil Practices and Remedies Code. Public servants are limited in liability to $100,000 to a single person and $300,000 for a single occurrence. There is also a $250,000 per person and $500,000 per occurrence statutory limit in place for tort claims against TTUHSC as an institution.

Worker's Compensation and Unemployment Compensation Plans

The State of Texas provides coverage for workers compensation and unemployment benefits from appropriations made to other state agencies for TTUHSC employees. The *General Appropriations Act* of the 79th Texas Legislature provides that TTUHSC must reimburse the General Revenue Fund, from TTUHSC appropriations, one-half of the unemployment benefits expected to be paid for former and current employees. The Texas Comptroller of Public Accounts determines the proportionate amount to be reimbursed from each appropriated fund type. TTUHSC must also reimburse the General Revenue Fund for all of the cost for unemployment compensation for any employees paid from funds held in local bank accounts or from local balances of legislative appropriations held in the State Treasury. Total payments for unemployment compensation for fiscal year 2008 amounted to $230,190. No material outstanding claims were pending as of August 31, 2008.

For workers compensation, TTUHSC remits an assessed amount from both appropriated and unappropriated fund types to the State Office of Risk Management (SORM). Total payments to SORM for fiscal year 2008 amounted to $765,947. SORM assumes the responsibility for paying all workers compensation claims for current and former employees of TTUHSC.

Note 12: Subsequent Events

House Bill 153 of the 79th Texas Legislature provided authorization for TTUHSC to issue $32,310,000 of additional Revenue Financing System bonds to be used for the expansion of the School of Pharmacy in Amarillo, construction of a research facility in Amarillo and renovations of the El Paso Medical Science building. TTUHSC intends to issue $29,503,000 during fiscal year 2009. Of the total authorized issuance, $2,807,000 was issued during fiscal year 2008 as commercial paper.

Note 13: Related Parties

Blended Component Units

Texas Tech Physician Associates (TTPA) is reported as a blended component unit of TTUHSC. TTPA is a certified non-profit health corporation authorized under the Medical Practice Act § 5.01(a), article 4495b of the State of Texas. TTPA was created for the purpose of entering into prepaid capitation agreements for physician and other medical services. TTPA is exempt from tax under Internal Revenue Code § 501(c)(3). The TTPA board consists of nine directors appointed by TTUHSC.

Although legally separate from TTUHSC, TTPA is reported as a component unit because TTUHSC can impose its will on TTPA. TTPA balances and activities are blended with TTUHSC balances and activities since the sole purpose of TTPA is to financially support TTUHSC. Independent financial statements for TTPA can be obtained from the Health Care Systems division of TTUHSC at 3601 4th Street, Lubbock, Texas 79430.

Texas Tech Foundation, Inc. (TTFI) is a component unit of the consolidated Texas Tech University System as it serves the fundraising needs of TTUHSC, TTU, and TTUSA. No balances or activities associated with TTFI are included in this *Annual Financial Report*.

Note 14: Stewardship, Compliance, and Accountability

TTUHSC has no material stewardship, compliance or accountability issues.

Note 15: The Financial Reporting Entity

TTUHSC is a component unit of the State of Texas as discussed in the introduction to these notes. The accompanying financial statements reflect inclusion of one blended component unit described in detail in Note 13. TTUHSC has no other related organizations, joint ventures or jointly governed organizations.

Note 16: Restatement of Net Assets

TTUHSC had no material prior-period adjustments that would require a restatement of fund balance and net assets for the year ended August 31, 2008.

Note 17: Employee Retirement Plans

The State of Texas has joint contributory retirement plans for substantially all of its employees. One of the primary plans in which TTUHSC participates is administered by the Teacher Retirement System of Texas (Retirement System). The contributory percentages currently provided by the State and by each participant are 6.58 percent and 6.4 percent, respectively, of annual compensation.

The Retirement System does not separately account for each of its component government agencies because the Retirement System itself bears sole responsibility for retirement commitments beyond contributions fixed by the State Legislature. According to an independent actuarial valuation as of August 31, 2007, the present value of the Retirement System's actual and projected liabilities, including projected benefits payable to its retirees and active members and their beneficiaries, was less than the actuarial valuation of Retirement System assets. Further information regarding actuarial assumptions and conclusions, together with audited financial statements, are included in the Retirement System's annual financial report.

The State has also established an Optional Retirement Program for institutions of higher education. Participation in the Optional Retirement Program is in lieu of participation in the Retirement System. The Optional Retirement Program provides for the purchase of annuity contracts and mutual funds. The contributory percentages of participant salaries provided by the State and by each participant enrolled in the plan on or before August 31, 1995, are 8.5 percent and 6.65 percent, respectively. The 8.5 percent is composed of 6.58 percent contributed by the State and an additional 1.92 percent contributed by TTUHSC. For participants who enrolled after September 1, 1995, State and participant contributions are 6.58 percent and 6.65 percent, respectively. Because these are individual annuity contracts, the State has no additional or unfunded liability for this program, and TTUHSC bears no responsibility for retirement commitments beyond contributions.

Total retirement expense to TTUHSC was $16,325,352 for the year ended August 31, 2008. Of this amount, $8,426,705 represents the portion of appropriations made by the State Legislature expended on behalf of TTUHSC and $7,898,647 represents the portion paid from TTUHSC's funds.

Note 18: Deferred Compensation Program

TTUHSC employees may elect to defer a portion of their earnings for income tax and investment purposes pursuant to authority granted in Texas Government Code, Section 609.001. Deferred compensation plans are administered by the Employees Retirement System.

The State's 457 Plan complies with Internal Revenue Code, Section 457. This plan is referred to as the TexaSaver Deferred Compensation Plan and is available to all employees. Deductions, purchased investments, and earnings attributed to the 457 Plan are the property of the State and subject only to the claims of the State's general creditors. Participant rights under the plan are equal to those of the general creditors of the State in an amount equal to the fair market value of the 457 account for each participant. The State has no liability under the 457 Plan, and it is unlikely that plan assets will be used to satisfy the claims of general creditors in the future.

Note 19: Donor-Restricted Endowments

TTUHSC endowments are categorized as either true endowments or funds functioning as endowments. As of August 31, 2008, TTUHSC had no term endowments. Expenditure of true endowment funds is not permitted without the express consent of the donor. Most TTUHSC endowments are held in perpetuity. In many cases, a portion of the endowment earnings are expendable for student financial assistance or other purposes as designated by the donor or associated agreement. In other cases, endowment earnings are fully reinvested.

Investment authority is granted to TTUHSC by Texas Property Code 163.005. The code section states as follows:

> "§ 163.005. INVESTMENT AUTHORITY. In addition to an investment authorized by other law or by the applicable gift instrument, and without restriction to investments a fiduciary may make, the governing board, subject to any specific limitations in the applicable gift instrument or the applicable law other than law relating to investments by a fiduciary, may:
>
> (1) invest an institutional fund in any real or personal property, including mortgages, stocks, bonds, debentures, and other securities of profit or nonprofit corporations, shares in or obligations of associations, partnerships, or individuals, and obligations of any governmental entity, whether or not the property produces a current return;
>
> (2) retain property contributed by a donor to an institutional fund;
>
> (3) include all or any portion of an institutional fund in a pooled or common fund maintained by the institution; and
>
> (4) invest all or any portion of an institutional fund in a pooled or common fund, including shares or interests in regulated investment companies, mutual funds, common trust funds, investment partnerships, real estate investment trusts, or similar organizations in which funds are commingled and investment determinations are made by persons other than the governing board.
>
> Added by Acts 1989, 71st Leg., ch. 213, § 1, eff. May 26, 1989."

Endowment assets are invested predominantly in the Long Term Investment Fund (LTIF), described in more detail in Note 3. The LTIF allows for quarterly spendable income distributions amounting to 1.125% of the 12-quarter rolling average unitized balance. Spendable income can be supported by both realized earnings and by unrealized earnings.

Per Regent's Rules 09.02.10 (c), the distribution of spendable earnings to each unit of the LTIF shall not exceed 6% nor be less than 4% of the average market value of a unit of the LTIF for the 12 quarters just ended. The target annual distribution rate shall be 4.5% of the average unit market value for the 12 quarters just ended. Distribution shall be made quarterly, as soon as practicable after the last calendar day of November, February, May, and August.

Donor restricted endowment earnings / (losses) for the year ended August 31, 2008 are summarized in the table below.

Endowment Category	Net Appreciation	Statement of Net Assets Reporting Section
True Endowments	$ (1,318,240)	Restricted / Nonexpendable
True Endowments	1,816,244	Restricted / Expendable
True Endowments	5,179,706	Unrestricted / Expendable
Total	$ 5,677,710	

There were also unrealized fair market value losses associated with true endowments that amounted to $7,239,964 for the year ended August 31, 2008.

Note 20: Post-Employment Health Care and Life Insurance Benefits

In addition to providing pension benefits, the State provides certain health and life insurance benefits for retired employees, in accordance with state statutes. Substantially all of the employees may become eligible for the health and life insurance benefits if they reach normal retirement age while working for the State. Similar benefits for active employees are provided through a self-funded plan and fully insured plans.

Depending upon the status of the employee at the time of retirement, the State or TTUHSC recognizes the cost of providing these benefits. The cost of retiree post-employment benefits is recognized when paid. This contribution paid all of the "employee/retiree only" premiums and a portion of the premiums for those employees/retirees selecting dependent coverage. The employee/retiree was required to pay a portion of the cost of dependent coverage. For the fiscal year ended August 31, 2008, the cost of providing those benefits for the retirees was $1,945,991 for the State and $552,805 for TTUHSC.

GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions,* requires accrual-based measurement, recognition and disclosure of other post-employment benefits (OPEB) expense, such as retiree medical and dental costs, over the employees' years of service, along with the related liability, net of any plan assets. TTUHSC's benefit liability is included in that of the Employees Retirement System. As a result, this liability will be reported in the Employees Retirement System financial statements.

Note 21: Special or Extraordinary Items

TTUHSC had no special or extraordinary items during the year ended August 31, 2008.

Note 22: Disaggregation of Receivable and Payable Balances

Receivables

The most significant categories of TTUHSC receivables are patient receivables and contract receivables. Patient receivables are reported net of allowances for contractual and similar adjustments.

Allowances for uncollectibles and other adjustments are estimated using either (1) aging schedules (for student accounts receivable), (2) percentage of revenues (for pledged gifts receivable), or (3) detailed evaluations of past collection performance (for patient accounts receivable, contract accounts receivable, loans and notes receivable, and other accounts receivable).

Receivables that are not expected to be collected within one year are reported as non-current assets and include portions of pledged gifts receivable and loans and notes receivable.

Description	Gross Receivables	Allowances	Net Receivables
Federal Receivable	$ 1,372,370	$ -	$ 1,372,370
Interest and Dividends Receivable	914,965	-	914,965
Patient Accounts Receivable	48,144,252	(30,820,383)	17,323,869
Student Accounts Receivable	1,014,536	(18,343)	996,193
Contract Accounts Receivable	14,271,190	-	14,271,190
Pledged Gifts Receivable	8,355,671	(250,670)	8,105,001
Loans and Notes Receivable	3,218,567	(333,167)	2,885,400
Other	113,012	(96,559)	16,453
Total Receivables	$ 77,404,563	$ (31,519,122)	$ 45,885,441

Contractual Arrangements and Concentrations of Credit Risk

TTUHSC provides care to patients covered by various third party payers such as Medicare, Medicaid, and private insurance companies and health maintenance organizations (HMOs).

Of the listed payers, significant credit risk is only associated with the self pay and medically indigent category. Reserves and allowances associated with these receivables are adjusted periodically based on review and analysis of receivable balances. Patient accounts receivables are reported in this *Annual Financial Report* net of allowances for bad debts, contractual adjustments, and charity care.

Description	Gross Receivables
Medicare	$ 5,751,767
Medicaid	11,822,889
Managed Care, including Blue Cross	7,795,470
Commercial	5,038,297
Self Pay and Medically Indigent	17,523,412
Other	212,417
Total Gross Patient Accounts Receivable	$ 48,144,252

Payables

Major categories of TTUHSC payables include bonds payable, claims payable and general accounts payable (including payroll). Additional categories of payables include deposits payable and unclaimed property due to the State Treasury.

Description	Balance
Vendor Accounts Payable	$ 17,223,241
Patient Refunds Payable	1,908,980
Payroll Payable	31,770,614
Accrued Interest Payable	285,557
Other Current Liabilities	210
Total Short-Term Payables	$ 51,188,601

Note 23: Termination Benefits

TTUHSC had no reportable termination benefits during the year ended August 31, 2008.

State Auditor's Office
John Keel, CPA
State Auditor

April 2, 2009

Dr. John C. Baldwin, President
Texas Tech University Health Sciences Center
3601 4th Street, MS 6258
Lubbock, TX 79430

Subject: Management Letter Resulting from a Review of Texas Tech University Health Sciences Center's Fiscal Year 2008 Financial Statements

Dear Dr. Baldwin:

We offer this management letter in conjunction with our review of the financial statements of the Texas Tech University Health Sciences Center (Health Sciences Center) for the fiscal year ended August 31, 2008. We reviewed the Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; the Statement of Cash Flows; and the Notes to the Financial Statements. In the course of our review, which was substantially less in scope than an audit, we did not find that material modifications needed to be made to the financial statements in order for them to be in conformity with generally accepted accounting principles.

Our review determined that the Health Sciences Center's accounting processes allowed approximately $700,000 in Materials and Supplies Expense to be classified as Tuition and Fees Contra-revenue in its financial statements. Also, the accounting system lacks sufficient detail to enable the Health Sciences Center to efficiently correct the problem.

Recommendation

The Health Sciences Center should ensure that accounting processes accurately record expense transactions within the correct line items in its financial statements.

Robert E. Johnson Building
1501 N. Congress Avenue
Austin, Texas 78701

P.O. Box 12067
Austin, Texas 78711-2067

Phone:
(512) 936-9500

Fax:
(512) 936-9400

Internet:
www.sao.state.tx.us

Management Response

TTUHSC's financial system provides sufficient information for financial reporting. In fiscal year 2008, we over classified certain student related expenses as tuition and fees contra-revenue. As stated in the management letter, these were not material amounts requiring an adjustment to our financial statements. The effort required to restate the financial statements would be more significant than the benefit derived from correcting an item that has a zero dollar impact on reported net income.

In conjunction with implementing Banner as our new accounting system, we have modified our processes to ensure this error does not recur and that these expense transactions are properly classified in the financial statements.

We appreciate the assistance provided during this review by the management of the Health Sciences Center and Internal Audit. If you have any questions, please call me at (512) 936-9500.

Sincerely,

Sandra Vice

Sandra Vice, CIA, CGAP, CISA
Assistant State Auditor

The University of Texas Southwestern Medical Center at Dallas

REVIEW OF FY2008 FINANCIAL STATEMENTS AND NOTES

FOR THE

SOUTHERN ASSOCIATION OF COLLEGES AND SCHOOLS

Office of Internal Audit
5323 Harry Hines Boulevard
Dallas, Texas 75390-9017

Contents

State Auditor's Office
John Keel, CPA
State Auditor

Auditor's Review Report

January 28, 2009

Dr. Daniel K. Podolsky, President
The University of Texas Southwestern Medical Center at Dallas
5323 Harry Hines Blvd.
Dallas, TX 75390-9003

Dear Dr. Podolsky:

We have reviewed the accompanying Statement of Net Assets; Statement of Revenues, Expenses, and Changes in Net Assets; Statement of Cash Flows; and Notes to the Financial Statements of the University of Texas Southwestern Medical Center at Dallas (Medical Center) as of and for the fiscal year ended August 31, 2008, in accordance with *Statements on Standards for Accounting and Review Services* issued by the American Institute of Certified Public Accountants. The review was performed in accordance with the Southern Association of Colleges and Schools' (Southern Association) *Criteria for Accreditation*. All information included in these financial statements is the representation of management of the Medical Center.

A review consists principally of inquiries of Medical Center personnel and analytical procedures applied to financial data. A review is substantially less in scope than an audit conducted in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

The accompanying statements were prepared to present the financial position, the changes in financial position and the cash flows of the Medical Center. These statements are prepared pursuant to criteria of the Southern Association for supplementary special reports by institutions in states that conduct statewide audits.

Based on our review, with the exception of the matter described in the following paragraph, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with generally accepted accounting principles.

The University has not presented a management's discussion and analysis section that the Governmental Accounting Standards Board has identified as required supplementary information that is not part of the basic financial statements. However, such required supplementary information for the University of Texas System (System) is presented in the System's consolidated annual financial report.

This report is intended for use by the Board of Regents of the System, management of the Medical Center, and the Southern Association. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

Sincerely,

John Keel, CPA
State Auditor

Robert E. Johnson Building
1501 N. Congress Avenue
Austin, Texas 78701

P.O. Box 12067
Austin, Texas 78711-2067

Phone:
(512) 936-9500

Fax:
(512) 936-9400

Internet:
www.sao.state.tx.us

SAO Report No. 09-312

The University of Texas Southwestern Medical Center at Dallas

Statement of Net Assets

At August 31, 2008

(See Auditor's Review Report on page 1.)

ASSETS		
Current Assets		
Cash and Cash Equivalents (Note 3)	$	91,795,959
Restricted:		
Cash and Cash Equivalents (Note 3)		20,260,854
Legislative Appropriations		24,096,001
Receivables, Net of Allowances:		
Federal		30,122,196
Other Intergovernmental		2,371,605
Interest and Dividends		1,866,220
Patient Receivables		97,838,970
Gifts		5,726,277
Other		30,515,254
Due from Other State Entities (Note 9)		58,020,086
Consumable Inventories		12,249,241
Loans and Contracts		1,395,946
Prepaid Expenses		9,246,746
Total Current Assets	$	385,505,355
Non-Current Assets		
Restricted:		
Investments (Note 3)	$	371,430,325
Loans and Contracts		7,480,912
Gifts Receivable		3,533,964
Investments (Note 3)		372,570,036
Other Non-Current Assets Held in Trust		824,778,154
Capital Assets (Note 2)		
Non-Depreciable		148,862,786
Depreciable		1,494,220,540
Less: Accumulated Depreciation		(512,132,065)
Total Non-Current Assets	$	2,710,744,652
Total Assets	$	3,096,250,007

The University of Texas Southwestern Medical Center at Dallas

Statement of Net Assets

At August 31, 2008

(See Auditor's Review Report on page 1.)

LIABILITIES		
Current Liabilities		
Payables:		
Accounts	$	47,869,419
Accrued Liabilities		46,091,438
Payroll		34,774,709
Due to Other State Entities (Note 9)		6,861,487
Deferred Revenue		18,537,807
Capital Lease Obligations (Notes 5, 7)		41,565
Employees' Compensable Leave (Note 5)		30,286,717
Notes and Loans Payable (Note 5)		197,139
Liabilities Payable from Restricted Assets (Note 5)		17,802,665
Funds Held for Others		788,101
Other Current Liabilities		117,152
Total Current Liabilities	$	203,368,199
Non-Current Liabilities		
Capital Lease Obligations (Notes 5, 7)	$	36,813
Employees' Compensable Leave (Note 5)		28,923,202
Liability to Beneficiary		5,578
Other Non-Current Liabilities		3,062,744
Total Non-Current Liabilities	$	32,028,337
Total Liabilities	$	235,396,536

The University of Texas Southwestern Medical Center at Dallas

Statement of Net Assets

At August 31, 2008

(See Auditor's Review Report on page 1.)

NET ASSETS		
Invested in Capital Assets, Net of Related Debt	$	1,130,872,882
Restricted for:		
Non-Expendable		
Permanent Funds, True Endowments, Annuities		466,723,794
Expendable		
Capital Projects		49,811,061
Funds Functioning as Endowments		25,242,182
Other		731,689,060
Unrestricted		456,514,492
Total Net Assets	$	2,860,853,471

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

The University of Texas Southwestern Medical Center at Dallas

Statement of Revenues, Expenses, and Changes in Net Assets

For the Fiscal Year Ended August 31, 2008

(See Auditor's Review Report on page 1.)

OPERATING REVENUES		
Tuition and Fees	$	16,878,522
Discounts and Allowances		(2,929,343)
Professional Fees		1,110,775,683
Discounts and Allowances		(754,281,755)
Auxiliary Enterprises		16,795,312
Sales and Services of Hospitals		984,473,424
Discounts and Allowances		(644,368,471)
Other Sales of Goods and Services		7,726,301
Federal Revenue		207,349,009
State Grant Revenue		3,816,869
Local Grant Revenue		110,463,754
Private Revenue		64,839,185
Other Operating Revenues		13,585,103
Total Operating Revenues	$	1,135,123,593
OPERATING EXPENSES		
Cost of Goods Sold	$	2,283,250
Salaries and Wages		709,267,046
Payroll Related Costs		182,915,149
Professional Fees and Services		35,798,219
Travel		10,215,738
Materials and Supplies		191,172,662
Communications and Utilities		36,217,507
Repairs and Maintenance		5,139,114
Rentals and Leases		11,569,892
Printing and Reproduction		1,361,204
Depreciation and Amortization		68,532,417
Bad Debt Expense		244,419
Scholarships		578,698
Other Operating Expenses		115,424,050
Total Operating Expenses	$	1,370,719,365
Operating Income (Loss)	$	(235,595,772)

The University of Texas Southwestern Medical Center at Dallas

Statement of Revenues, Expenses, and Changes in Net Assets

For the Fiscal Year Ended August 31, 2008

(See Auditor's Review Report on page 1.)

NONOPERATING REVENUES (EXPENSES)		
Legislative Appropriations	$	187,427,174
Gifts		82,879,657
Interest and Investment Income (Loss)		72,688,886
Net Increase (Decrease) in Fair Value of Investments		(86,388,207)
Gain (Loss) on Sale of Capital Assets		(1,443,275)
Other Nonoperating Revenues		45,313
Total Nonoperating Revenues (Expenses)	$	255,209,548
Income (Loss) Before Other Revenues, Expenses, Gains (Losses), and Transfers	$	19,613,776
OTHER REVENUES, EXPENSES, GAINS (LOSSES), AND TRANSFERS		
Capital Contributions	$	8,603,736
Capital Appropriations (HEAF)		6,751,826
Transfers In from Other State Entities (Note 9)		142,431,371
Transfers Out to Other State Entities (Note 9)		(61,541,227)
Total Other Revenues, Expenses, Gains (Losses), and Transfers	$	96,245,706
CHANGE IN NET ASSETS	$	115,859,482
Net Assets, September 1, 2007	$	2,744,993,989
Restatements		
Net Assets, September 1, 2007, as Restated	$	2,744,993,989
NET ASSETS, August 31, 2008	$	2,860,853,471

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

The University of Texas Southwestern Medical Center at Dallas

Statement of Cash Flows

For the Fiscal Year Ended August 31, 2008

(See Auditor's Review Report on page 1.)

CASH FLOWS FROM OPERATING ACTIVITIES		
Proceeds from Tuition and Fees	$	14,344,923
Receipts from Patients and Customers		682,638,748
Proceeds from Sponsored Programs		376,412,950
Proceeds from Loan Programs		936,072
Proceeds from Auxiliaries		16,788,562
Proceeds from Other Revenues		22,543,701
Payments to Suppliers for Goods and Services		(402,840,675)
Payments to Employees (Salaries and Benefits)		(885,490,201)
Payments for Loans Provided		(1,793,109)
Net Cash Provided (Used) by Operating Activities	$	(176,459,029)
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Proceeds from Legislative Appropriations	$	179,054,450
Proceeds from Operating Gifts		88,054,393
Proceeds from Endowments		6,751,826
Payments for Transfers to Other Entities		(3,364,724)
Net Cash Provided (Used) by Non-Capital Financing Activities	$	270,495,945
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from Capital Appropriations, Grants and Gifts		6,425,668
Proceeds from Disposal of Capital Assets		131,447
Proceeds from Issuance of Capital-Related Debt		113,959,519
Payments for Additions to Capital Assets		(153,434,118)
Payments of Principal on Capital-Related Debt		(38,890)
Mandatory Transfers to System for Capital Related Debt		(59,021,627)
Net Cash Provided (Used) by Capital and Related Financing Activities	$	(91,978,001)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from Interest and Investment Income	$	73,431,682
Payments to Acquire Investments		(97,685,419)
Net Cash Provided (Used) by Investing Activities	$	(24,253,737)
Net Increase (Decrease) in Cash and Cash Equivalents	$	(22,194,822)

The University of Texas Southwestern Medical Center at Dallas

Statement of Cash Flows

For the Fiscal Year Ended August 31, 2008
(See Auditor's Review Report on page 1.)

Cash and Cash Equivalents, September 1, 2007	$	134,251,635
Restatements		
Cash and Cash Equivalents, September 1, 2007, as restated	$	134,251,635
Cash and Cash Equivalents, August 31, 2008	$	112,056,813

Reconciliation of Operating Income (Loss) to
Net Cash Provided (Used) by Operating Activities

Operating Income (Loss)	$	(235,595,772)
Adjustments:		
Depreciation and Amortization	$	68,532,417
Bad Debt Expense		244,419
Operating Income and Cash Flow Categories:		
Classification Differences		
Changes in Assets and Liabilities:		
(Increase) Decrease in Receivables		(20,783,185)
(Increase) Decrease in Inventories		(1,624,220)
(Increase) Decrease in Loans and Contracts		(857,038)
(Increase) Decrease in Other Assets		(4,141,420)
Increase (Decrease) in Payables		14,054,297
Increase (Decrease) in Due to Other Entities		542,528
Increase (Decrease) in Deferred Revenue		(3,533,194)
Increase (Decrease) in Employees' Compensable Leave		4,727,752
Increase (Decrease) in Funds Held for Others		95,284
Increase (Decrease) in Other Liabilities		1,879,103
Total Adjustments	$	59,136,743
Net Cash Provided (Used) by Operating Activities	$	(176,459,029)
Non-Cash Transactions		
Net Increase (Decrease) in Fair Value of Investments	$	(86,388,207)

The University of Texas Southwestern Medical Center at Dallas

Statement of Cash Flows

For the Fiscal Year Ended August 31, 2008
(See Auditor's Review Report on page 1.)

Donated Capital Assets	533,534
Other Deductions to Capital Assets	(1,397,962)

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

The University of Texas Southwestern Medical Center at Dallas

Statement of Changes in Unrestricted Net Assets

For the Fiscal Year Ended August 31, 2008

	8/31/08	8/31/07	Difference
Reserved			
Encumbrances	$ 40,017,999	$ 37,707,696	$ 2,310,303
Accounts Receivable	114,439,147	103,282,615	11,156,532
Inventories	12,249,241	10,625,020	1,624,221
Advanced Research / Advanced Technology Programs	1,448,106	160,180	1,287,926
Deposits	115,526	111,276	4,250
Prepaid Expenses	8,949,360	4,848,200	4,101,160
Imprest Funds	112,270	39,675	72,595
Travel Advances	32,462	30,193	2,269
Unreserved			
Allocated			
Capital Projects	18,181,051	18,600,117	(419,066)
Funds Functioning as Endowment - Unrestricted	25,526,113	26,599,077	(1,072,964)
Debt Service	56,449,638	50,246,360	6,203,278
Provision for FY 2008 Operating Budgets		2,555,463	(2,555,463)
Practice Plan Minimum Operating Reserve of 90 days	145,795,851	183,555,303	(37,759,452)
Unallocated	33,197,728	9,074,440	24,123,288
Total Unrestricted Net Assets	$ 456,514,492	$ 447,435,615	$ 9,078,877

Notes to the Financial Statements for the Fiscal Year Ended August 31, 2008

(See Auditor's Review Report on page 1)

General Introduction

This report has been prepared for the use of the Southern Association of Colleges and Schools (Southern Association) in connection with the review of the University of Texas Southwestern Medical Center (University) for accreditation purposes. This report includes a Statement of Net Assets; a Statement of Revenues, Expenses, and Changes in Net Assets; a Statement of Cash Flows; and the related Notes to the Financial Statements. In accordance with Southern Association criteria, the report also includes a Statement of Changes in Unrestricted Net Assets, and a Management Letter describing issues noted in the review.

Reporting Entity

The University is a component of the University of Texas System (System) and an agency of the State of Texas. The System is reported as a business-type activity in the State of Texas' *Comprehensive Annual Financial Report* and reflects compliance with applicable state statutes and GASB pronouncements. The System is governed by a Board of Regents, composed of nine members who are appointed by the Governor and confirmed by the Senate. Terms are scheduled for six years each and staggered so that three members' terms will usually expire on February 1 of odd-numbered years.

Southwestern Medical School has grown from a small wartime medical college in 1943 into The University of Texas Southwestern Medical Center at Dallas, a multifaceted academic institution nationally recognized for its excellence in educating physicians, biomedical scientists and health-care personnel. Our mission is to improve the health care in our community, Texas, our nation, and the world through innovation and education. To educate the next generation of leaders in patient care, biomedical science and disease prevention. To conduct high-impact, internationally recognized research and to deliver patient care that brings UT Southwestern's scientific advances to the bedside – focusing on quality, safety and service.

Note 1: Summary of Significant Accounting Policies

Basis of Accounting

The University reports as a business-type activity because it is financed in part by fees charged to external parties for goods or services. The accompanying financial statements present the financial position and operations of the University using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. Operating items are distinguished from non-operating items. Operating revenues and expenses result from providing services or producing and delivering goods in connection with ongoing operations. Operating expenses include the cost of goods and services, administrative expenses, and depreciation on capital assets.

Cash and Cash Equivalents
Short-term, highly liquid investments with maturities of three months or less when purchased are generally considered cash and cash equivalents. It is the System and University policy to exclude items that meet this definition if they are part of an investment pool, which has an investment horizon of one year or greater. Therefore, highly liquid investments that are part of the Intermediate Term Fund and the Long Term Fund are not considered cash and cash equivalents.

Additionally, Funds Functioning as Endowments invested in money market accounts are also excluded from Cash and Cash Equivalents as it is management's intent to invest these funds for more than one year. Cash held in the State Treasury for the Permanent University Fund (PUF), the Permanent Health Fund (PHF) are considered cash and cash equivalents. Other highly liquid investments of these major funds invested with custodians are not considered cash and cash equivalents according to the investment policies of the System.

Balance in State Appropriations
This item represents the balance of General Revenue funds at August 31 as calculated in the Texas State Comptroller's General Revenue Reconciliation.

Investments
Investments of the University are managed by the University of Texas Investment Management Company (UTIMCO), a private investment corporation that provides services entirely to the System. All investments are reported as non-current as these funds have an investment horizon extending beyond one year. The System's investments are primarily valued on the basis of market valuations provided by independent pricing services.

Fixed income securities held directly by the System are valued based upon prices supplied by Merrill Lynch Securities Pricing Service and other major fixed income pricing services, external broker quotes, and internal pricing matrices. Equity security market values are based on the New York Stock Exchange composite closing prices, if available. If not available, the market value is based on the closing price on the primary exchange on which the security is traded (if a closing price is not available, the average of the last reported bid and ask price is used). Private market investments and certain other equity securities are fair valued by management. The fair values of these investments are estimated by management using the partnership's capital account balance at the closest available reporting period, as communicated by the general partner, adjusted for contributions and withdrawals subsequent to the latest available reporting period as well as consideration of any other information, which has been provided by the partnership or other source. In rare cases the private market funds are valued at cost, but only when management feels this is the best approximation of value.

The audited financial statements of the funds managed by UTIMCO may be found on UTIMCO's web site, and inquiries may be directed to UTIMCO via utimco.org. The System is authorized to invest funds, as provided in Section 51.0031 of the Texas Education Code and the Constitution of the State of Texas, under prudent investor investment standards. Such investments include various fixed income and equity type securities. The investments of the System are governed by various investment policies approved by the UT System Board of Regents.

Endowments

The University's endowments are used to support operations, which require the simultaneous achievement of two contradictory objectives of generating a predictable stream of annual revenue at a rate at least equal to the average rate of inflation for current needs and of increasing the purchasing power of the funds (after annual distributions) at a rate at least equal to the average rate of inflation for future periods. Funds are subject to restrictions of endowment and trust instruments, requiring that principal be maintained and that only the income be utilized. Funds may include endowments, term endowments, and funds functioning as endowments. Funds functioning as endowments consist of amounts that have been internally dedicated by the System for long-term investment purposes.

The Permanent Health Fund (PHF) is an internal UT System mutual fund for the pooled investment of state endowment funds for health-related institutions of higher education. The University of Texas System Board of Regents established the PHF in August 1999 with proceeds from state tobacco litigation. Distributions from the PHF fund programs that benefit medical research, health education, or treatment programs. The PHF provides for greater diversification of investments than would be possible if each account were managed separately.

Contributions Receivable

Current and noncurrent contributions receivable are amounts pledged to the University by donors, net of allowances.

Inventories

Inventories, consisting primarily of supplies and merchandise for resale, are valued at cost, typically based on the specific identification, weighted average or first-in, first-out methods, which are not in excess of net realizable value.

Restricted Assets

Restricted assets include funds restricted by legal or contractual requirements, including those related to sponsored programs, donors, constitutional restrictions, and loan agreements.

Loans and Contracts

Current and noncurrent loans and contracts are receivables, net of allowances, related to student loans.

Capital Assets

Capital assets are recorded at the cost on the date of acquisition or fair value at the date of donation in the case of gifts. The University and the System follow the State's capitalization policy with a cost equal to or greater than $5,000 for equipment items; $100,000 for buildings, building improvements and improvements other than buildings; and $500,000 for infrastructure items with an estimated useful life of greater than one year. Purchases of library books are capitalized.

Renovation to buildings, infrastructure, and land improvements that increase the value by at least 25 percent or extend the useful life by at least 25 percent are capitalized. Routine repairs and maintenance are charged to operating expense in the year in which the expenses are incurred. Outlays for construction in progress are capitalized as incurred. Interest expense related to construction is capitalized net of interest income earned on the resources reserved for this purpose.

The University capitalizes, but does not depreciate works of art and historical treasures that are held for exhibition, education, research and public service. These collections are protected and preserved.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 2 to 15 years for equipment items, 15 years for library books, 10 to 50 years for buildings and their components, and 15 to 40 years for infrastructure elements.

Other Assets

Included in other current assets are prepaid expenses due within one year. Included in the other noncurrent assets are prepaid expenses that will be realized beyond one year.

Deferred Revenue

Deferred revenue represents revenues collected but not earned as of August 31 such as tuition recorded in August for the fall semester and payments received in advance for sponsored programs.

Funds Held for Others

Funds held for others represent funds held by the University as custodial or fiscal agent for students, faculty members, foundations, and others. University funds held for others as of August 31, 2008 totaled $ 788,101.

Net Assets

The University has classified resources into the following three 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.

Restricted:

Nonexpendable

Net assets which are subject to externally imposed stipulations that require the amounts to be maintained in perpetuity by the University. Such assets include the University's permanent endowment funds.

Expendable

Net assets whose use by the University is subject to externally imposed stipulations that can be fulfilled by actions of the University pursuant to those stipulations or that expire with the passage of time.

Unrestricted

Net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for special purposes by action of University management or the System Board of Regents or may otherwise be limited by contractual agreements with outside parties. Substantially all unrestricted net assets are designated for academic, research programs, patient care initiatives, and for capital programs.

When an expense is incurred that can be paid using either restricted or unrestricted resources, the University addresses each situation on a case-by-case basis prior to determining the resources to be used to satisfy the obligation. Generally, the University's policy is to first apply the expense toward restricted resources and then toward unrestricted resources.

Revenues and Expenses

Operating revenues include activities such as student tuition and fees, net of scholarship allowances; sales and services of auxiliary enterprises; sales and services of hospitals; professional fees; most federal, state and local grants and contracts and federal appropriations; and interest on student loans. As defined by GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, all operating revenues are considered program revenues since they are charges for services provided and program-specific operating grants and contributions. Operating expenses include salaries and wages, payroll related costs, materials and supplies, depreciation, scholarships and fellowships, and impairment losses and insurance recoveries received in the same year as the associated loss in accordance with GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*.

Non-operating revenues include activities such as gifts and contributions, insurance recoveries received in years subsequent to the associated loss, State appropriations, investment income and other revenue sources that are defined as non-operating revenues by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Government Entities That Use Proprietary Fund Accounting*, GASB Statement No. 34, and GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. Non-operating expenses include other expenses that are defined as non-operating expenses by GASB Statement Nos. 9, 34 and 42.

Scholarship Allowances and Student Aid

Financial aid to students is reported in the financial statements as prescribed by the National Association of College and University Business Officers (NACUBO). Certain aid (student loans, funds provided to students as awarded by third parties and Federal Direct Lending) is accounted for as third party payments (credited to the student's account as if the student made the payment). All other aid is reflected in the financial statements as operating expense or scholarship allowances, which reduce revenues. The amount reported as operating expense represents the portion of aid that was provided to the student in the form of cash. Scholarship allowances represent the portion of aid provided to the student in the form of reduced tuition.

Charity Care

The University provides charity care to patients who meet certain criteria under charity care policies without charge or at amounts less than its established rates. Because the University does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. The University's total unsponsored charity care amounted to approximately $ 416,147,710 for 2008.

Net Patient Service Revenue

The University has agreements with third-party payors that provide for payments to the University at amounts different from their established rates.

Medicare

The University's inpatient acute care services and outpatient services rendered to Medicare program beneficiaries are reimbursed under a prospective reimbursement methodology.

Also, additional reimbursement is received for graduate medical education, disproportionate share, bad debts and other reimbursable costs, as defined, under a variety of payment methodologies.

Medicaid

Inpatient services rendered to Medicaid program beneficiaries are reimbursed under a prospective reimbursement methodology. Certain outpatient services rendered to Medicaid program beneficiaries are reimbursed under a cost reimbursement cost methodology. The University is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the University and audits thereof by the Medicaid fiscal intermediary.

The University has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. The basis for payment to the University under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

Use of Estimates

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

Note 2: Capital Assets

A summary of changes in the capital assets for the year ended August 31, 2008, is presented below.

	Balance 9/1/2007	Completed CIP	Additions	Deductions	Balance 8/31/2008
Non-Depreciable Assets:					
Land and Land Improvements	$ 37,429,171	$	$ 8,998,570	$	$ 46,427,741
Construction in Progress	49,791,830	(17,705,573)	67,700,696	(176,699)	99,610,254
Other Capital Assets	2,607,448		217,643	(300)	2,824,791
Total Non-Depreciable Assets	$ 89,828,449	$ (17,705,573)	$ 76,916,909	$ (176,999)	$ 148,862,786
Depreciable Assets:					
Buildings and Building Improvements	$ 1,031,754,698	$ 14,405,355	$ 41,011,971	$ (1,312,724)	$ 1,085,859,300
Infrastructure	25,524,078				25,524,078
Facilities and Other Improvements	12,428,813	94,025	932,608		13,455,445
Furniture and Equipment	321,131,392	3,206,193	37,920,187	(3,558,458)	358,699,315
Vehicles, Boats, and Aircraft	3,120,594		274,817	(136,204)	3,259,206
Other Capital Assets	7,824,365		33,353	(434,523)	7,423,194
Total Depreciable Assets at Historical Cost	$ 1,401,783,940	$ 17,705,573	$ 80,172,936	$ (5,441,909)	$ 1,494,220,540
Less Accumulated Depreciation for:					
Buildings and Building Improvements	$ (273,401,736)	$	$ (35,601,039)	$ 544,896	$ (308,457,879)
Infrastructure	(5,531,555)		(787,466)		(6,319,021)
Facilities and Other Improvements	(2,638,613)		(813,294)		(3,451,907)
Furniture and Equipment	(158,797,320)		(30,545,137)	3,104,765	(186,237,692)
Vehicles, Boats, and Aircraft	(2,232,171)		(239,638)	126,051	(2,345,758)
Other Capital Assets	(5,051,753)		(545,843)	277,788	(5,319,808)
Total Accumulated Depreciation	$ (447,653,148)	$ 0	$ (68,532,417)	$ 4,053,500	$ (512,132,065)
Depreciable Assets, Net	$ 954,130,792	$ 17,705,573	$ 11,640,519	$ (1,388,409)	$ 982,088,475
Capital Assets, Net	$ 1,043,959,241	$ 0	$ 88,557,428	$ (1,565,408)	$ 1,130,951,261

Note 3: Deposits and Investments

Deposits

University bank information as of August 31, 2008 is presented below.

Carrying Amount	Bank Balance
$ 2,792,767	$ 128,649

Cash on Hand	$	140,013
Cash in Bank		91,655,946
Cash Equivalents		20,260,854
Total Cash and Cash Equivalents	$	112,056,813
Current Assets Cash and Cash Equivalents	$	91,795,959
Current Assets Restricted Cash and Cash Equivalents		20,260,854
Total Cash and Cash Equivalents	$	112,056,813

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the University will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The University maintains depository relationships with two banking institutions. The University's policy is that all deposits are governed by a bank depository agreement between the University and the respective banking institution. This agreement provides that the University's deposits, to the extent such deposits exceed the maximum insured limit under deposit insurance provided by the Federal Deposit Insurance Corporation, shall at all times be collateralized with either government securities or a surety bond issued by an insurer rated "AAA" or equivalent by a nationally recognized rating organization or a combination thereof.

As of August 31, 2008, there was sufficient securities pledged to collateralize all UT Southwestern funds held in depository accounts.

Investments

At the direction of the System Board of Regents, University investments and cash equivalents are pooled at the System level in internal investment pools. The System is responsible for disclosure of all information on the pooled investments and has included these disclosures in its annual financial report.

As of August 31, 2008, the fair value of the University's share of investments is presented below:

Investments held by Related Parties	$	80,561,527
Investment in premier, Inc,-Univ (Non-Hospital)		1,203,431
Investment in Premier Purchasing Partners, L.P.		316,295
Investment in Reata Inc.		462,816
UTIMCO – Intermediate Term Fund		654,119,578
UTIMCO/LTF - Moncrief Cancer Center		7,336,714
Total Investments	$	744,000,361
Non-Current Assets – Restricted Investments		371,430,325
Non-Current Assets – Investments		372,570,036
Total Investments	$	744,000,361

(A) *Credit Risk* - Article VII, Section 11b of the Texas Constitution authorizes the UT System Board of Regents, subject to procedures and restrictions it establishes, to invest System funds in any kind of investment and in amounts it considers appropriate, provided that it adheres to the prudent investor standard. This standard provides that the UT System Board of Regents, in making investments, may acquire, exchange, sell, supervise, manage, or retain, through procedures and subject to restrictions it establishes and in amounts it considers appropriate, any kind of investment that prudent investors, exercising reasonable care, skill and caution, would acquire or retain in light of the purposes, terms, distribution requirements, and other circumstances of the fund then prevailing, taking into consideration the investment of all of the assets of the fund rather than a single investment.

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 (NRSRO). The System's investment policies limit investments in U.S. Domestic bonds and non-dollar denominated bond investments to those that are rated investment grade, Baa3 or better by Moody's Investor Services, BBB- or better by Standard & Poor's Corporation, or BBB- or better by Fitch Investors Service at the time of acquisition. This requirement does not apply to investment managers that are authorized by the terms of an investment advisory agreement to invest in below investment grade bonds. Per GASB Statement No. 40, *Deposit and Investment Risk Disclosures, an amendment to GASB Statement No. 3*, unless there is information to the contrary, obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and do not require disclosure of credit quality. GASB 40 also provides that securities with split ratings, or a different rating assignment between NRSROs, are disclosed using the rating indicative of the greatest degree of risk.

(B) *Concentrations of Credit Risk* – The System's investment policy statements contain the limitation that no more than five percent of the market value of domestic fixed income securities may be invested in corporate or municipal bonds of a single issuer. As of August 31, 2008 and 2007, the System did not hold any direct investments in any one issuer of corporate or municipal bonds that were five percent or more of the market value of the System's domestic fixed income investments.

(C) *Custodial Credit Risk* – Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the System will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the System will not be able to recover the value of its investment or collateral securities that are in the possession of another party. Texas State Statutes and the System's investment policy statements do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments. As of August 31, 2008 and 2007, the System did not have any deposits or investments that are exposed to custodial credit risk.

(D) *Interest Rate Risk* – Interest rate risk is the risk that changes in market 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. Interest rate risk inherent in the System investments is measured by monitoring the modified duration of the overall investment portfolio. Modified duration estimates the sensitivity of the System's investments to changes in interest rates. The System has no specific policy statement limitations with respect to its overall modified duration.

(E) *Investments with Fair Values That Are Highly Sensitive to Interest Rate Changes* – In accordance with the System's investment policy statements, the System may invest in various mortgage backed securities, such as collateralized mortgage backed obligations. The System also may invest in investments that have floating rates with periodic coupon changes in market rates, zero coupon bonds and stripped Treasury and Agency securities created from coupon securities. No percentage of holdings limitations are specified in the investment policy statements regarding these types of securities.

(F) *Foreign Currency Risk* – Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of the System's non-U.S. dollar investments. The System's investment policy statement limits investments in non-U.S. denominated bonds to 50 percent of the System's total fixed income exposure.

Securities Lending

In accordance with the prudent investor investment standards, the System participates in a securities lending program. The System began the program, under a contract with the System's lending agent, on September 1, 1995. The lending agent is authorized to lend any securities held by the System's custodian except those securities which the policy guidelines prohibits lending. Investments received as collateral for securities lending activities are not recorded as assets because the investments remain under the control of the transferor, except in the event of default.

In security lending transactions, the System transfers its securities to brokers/dealers for collateral, which may be cash, securities issued or guaranteed by the United States government or its agencies, and irrevocable bank letters of credit, and simultaneously agrees to return the collateral for the same securities in the future.

Cash collateral received by the lending agent on behalf of the System is invested and reinvested in a non-commingled pool exclusively for the benefit of the System. The pool is managed in accordance with investment guidelines established by the System and is stated in the security lending contract. The maturities of the investments in the pool do not necessarily match the term of the loans, rather the pool is managed to maintain a maximum dollar weighted average maturity of 60 days and an overnight liquidity of 20 percent.

Collateral pool investments are uninsured, and are held by the securities lending agent, in its name, on behalf of the System, except for the investments in repurchase agreements which are held in the securities lending agent’s name by a third party custodian not affiliated with the System or the borrower of the associated loaned securities. Therefore, the collateral pool is not exposed to custodial credit risk because the pool investments are not held by counterparties to the lending transactions or a counterparties’ trust department or agent.

Lending income is earned if the returns on those investments exceed the “rebate” paid to borrowers of the securities. The income is then shared with the lending agent based on a contractually negotiated rate split. However, if the investment of the cash collateral does not provide a return exceeding the rebate or if the investment incurs a loss of principal, part of the payment to the borrower would come from the System’s resources and the lending agent based on the rate split.

Loans that are collateralized with securities generate income when the borrower pays a “loan premium or fee” for the securities loan. This income is split with the same ratio as the earnings for cash collateral. The collateral pledged to the System by the borrower is custodied by the lending agent or through a third party arrangement. These securities held as collateral are not available to the System for selling or pledging unless the borrower is in default of the loan.

The collateral received must have a fair value of 102 percent of the loaned securities of United States issuers. If the fair value of the collateral held in connection with loans of securities of United States issuers is less than 100 percent at the close of trading on any business day, the borrower is required to deliver additional collateral by the close of the next business day to equal 102 percent of the fair value.

For non-United States issuers, the collateral should remain at 105 percent of the fair value of the loaned securities at the close of any business day. If it falls below 105 percent, the borrower must deliver additional collateral by the close of the following business day. In the event of default, where the borrower is unable to return the securities loaned, the System has authorized the lending agent to seize the collateral held. The collateral is then used to replace the borrowed securities where possible. Due to some market conditions, it is possible that the original securities cannot be replaced. If the collateral is insufficient to replace the securities, the lending agent has indemnified the System from any loss due to borrower default.

At August 31, 2008 and 2007, the System had no credit risk exposure to borrowers because the amounts the System owed to borrowers exceeded the amounts the borrowers owed the System.

There were no significant violations of legal or contractual provisions, no borrower or lending agent default losses, and no recoveries of prior period losses during the year.

Derivative Financial Instruments
Derivatives are financial instruments (securities or contracts) whose value is linked to, or "derived" from, changes in interest rates, currency rates, and stock and commodity prices. Derivatives cover a broad range of financial instruments, such as forwards, futures, options, swaps, and mortgage derivatives.

(A) *Mortgage Derivatives* – Mortgage derivatives are used to manage portfolio duration and to enhance portfolio yield, and, are influenced by changes in interest rates, the current economic climate, and the geographic make-up of underlying mortgage loans. There are varying degrees of risk associated with mortgage derivatives. For example, certain Collateralized Mortgage Obligations (CMOs) such as Planned Amortization Class (PACs) are considered a more conservative lower risk investment. In contrast, principal only and interest only strips are considered higher risk investments. The System's investment in CMOs, which was comprised almost exclusively of the lower risk investment class, was 1.7 percent of total investments with a fair value of $423,215,911 at August 31, 2008 and 1.5 percent of total investments with a fair value of $392,563,747 at August 31, 2007.

(B) *Futures Contracts* – Futures contracts are used to facilitate various trading strategies, primarily as a tool to increase or decrease market exposure to various asset classes. The net liability is included in payables from restricted assets. Futures contracts are marked to market daily; that is, they are valued at the close of business each day and a gain or loss is recorded between the value of the contracts that day and on the previous day. The daily gain or loss difference is referred to as the daily variation margin, which is settled in cash with the broker each morning for the amount of the previous day's mark to market. The amount that is settled in cash with the broker each morning is the carrying and fair value of the futures contracts. The amount of the net realized gain on the futures contracts was $3,963,663 for the year ended August 31, 2008. The amount of the net realized loss on the futures contracts was $37,121,227 for the year ended August 31, 2007. The System executes such contracts either on major exchanges or with major international financial institutions and minimizes market and credit risk associated with these contracts through the manager's various trading and credit monitoring techniques.

(C) *Foreign Currency Exchange Contracts* – The System enters into forward foreign currency exchange contracts to hedge against foreign currency exchange rate risks on its non-U.S. dollar denominated investment securities and to facilitate trading strategies primarily as a tool to increase or decrease market exposure to various foreign currencies. When entering into a forward currency contract, the System agrees to receive or deliver a fixed quantity of foreign currency for an agreed-upon price on an agreed future date. These contracts are valued daily and the System's net equity therein (representing unrealized gain or loss on the contracts, as measured by the difference between the forward foreign exchange rates at the dates of entry into the contracts and the forward rates at the reporting date) is included in other receivables. Realized and unrealized gains and losses are included in the consolidated statement of revenues, expenses, and changes in net assets. These instruments involve market and/or credit risk in excess of the amount recognized in the consolidated balance sheet. Risks arise from the possible inability of counter-parties to meet the terms of their contracts and from movement in currency and securities values and interest rates.

(D) *Written Options* – Written options are used to alter the market (systematic) exposure without trading the underlying cash market securities, and to hedge and control risks, so that the actual risk/return profile is more closely aligned with the target risk/return profile. They are included in payables from restricted assets. During the year, call options were written on Treasury Note, commodity, domestic and international equity index and exchange traded funds.

(E) *Swaps* – Swaps are used to adjust interest rate and yield curve exposures. During the year, the System entered into interest rate, total return and commodity swap contracts. They are included in other receivables and payables from restricted assets.

(F) *Investment Funds* – The System's investment funds include exchange traded funds, index funds, Securities Exchange Commission (SEC) regulated mutual funds and externally managed funds, limited partnerships, and corporate structures which are generally unrated and may be unregulated.

Hedge fund pools are invested in private placements with external investment managers who invest in equity and fixed income securities of both domestic and international issuers. These investment managers may invest in both long and short securities and may utilize leverage in their portfolios. The funds invested may be subject to a lock-up restriction of one or more years before the investment may be withdrawn from the manager without significant penalty. There are certain risks associated with these private placements, some of which include investment manager risk, market risk, and liquidity risk, as well as the risk of utilizing leverage in the portfolios.

Private market funds are invested in limited partnerships with external investment managers or general partners who invest primarily in private equity securities. These investments are domestic and international, are illiquid and may not be realized for a period of several years after the investments are made. There are certain risks associated with these investments, some of which are liquidity risk, market risk, event risk, and investment manager risk. The System had committed $2,909,146,371 and $2,045,612,860 of future funding to various private market investments as of August 31, 2008 and 2007, respectively.

Public market funds are invested in exchange traded funds, index funds, and private placements with external investment managers who invest in equity and fixed income securities of both domestic and international issuers. These funds are characterized as public market funds based on individual risk/return characteristics and their relationship to the overall asset mix of the funds. Some of these investment managers may invest in both long and short securities and may utilize modest leverage in their portfolios. There are certain risks associated with these investments, some of which are investment manager risk, market risk, and liquidity risk, as well as the risk of utilizing leverage in the portfolios. Hedge funds, private market and public market funds include investments in private placement vehicles that are subject to risk which could result in the loss of invested capital. The risks include the following:

• *Non-regulation risk* – Some of these funds are not registered with the SEC, and therefore, are not subject to regulatory controls.
• *Key personnel risk* – The success of certain funds is substantially dependent upon key investment managers and the loss of those individuals may adversely impact the fund's performance.
• *Liquidity risk* – Many of the System's investment funds may impose lock-up periods which would cause the System to incur penalties to redeem its units or prevent the System from redeeming its shares until a certain period of time has elapsed.
• *Limited transparency* – As private placement investment vehicles, these funds may not disclose the holdings of their portfolios.
• *Investment strategy risk* – These funds often employ sophisticated investment strategies and may use leverage which could result in the loss of invested capital.

(G) *Securities Sold Short* – The System may sell securities it does not own in anticipation of a decline in the fair value of that security or as means to adjust the duration of certain fixed income portfolios. When the System sells a security short, it must borrow the security sold short and deliver it to the broker-dealer through which it made the short sale as collateral for its obligation to deliver the security upon conclusion of the sale. As of August 31, 2008 the Fund had no securities sold short. The market value of securities sold short as of August 31, 2007 was $35,097,262. As of August 31, 2007 there was no Deposit with Broker for Securities Sold Short. The System must pay dividends or interest on the securities sold short. Until the System covers it shorts sales, it is exposed to market risk to the extent that subsequent market fluctuations may require purchasing securities sold short at prices, which may be significantly higher than the market value reflected in the statements of fiduciary net assets.

Note 4: Summary of Short-Term Liabilities

As of August 31, 2008 the University did not have any short-term liabilities.

Note 5: Summary of Long Term Liabilities

Long-term liabilities are presented below.

	Balance 9/1/2007	Additions	Deductions	Balance 8/31/2008	Amounts Due Within One Year
Capital Lease Obligations	$ 117,269	$	$ 38,891	$ 78,378	$ 41,565
Employees' Compensable Leave	54,482,167	4,727,752		59,209,919	30,286,717
Notes and Loans Payable	197,139			197,139	197,139
Liabilities Payable from Restricted Assets	11,669,513	6,133,152		17,802,665	17,802,665
Total	$ 66,466,088	$ 10,860,904	$ 38,891	$ 77,288,101	$ 48,328,086

Employees' Compensable Leave

Substantially all full-time University employees earn annual leave in the amount of 8 to 21 hours per month depending upon the respective employee's years of state employment. State law permits employees to carry accrued leave forward from one fiscal year to another fiscal year with a maximum of 532 hours for those employees with 35 or more years of state service. Eligible part-time employees' annual leave accrual rate and maximum carryover are proportional to the number of hours appointed to work. Employees with at least six months of state service who terminate their employment are entitled to payment for all accumulated annual leave.

Sick leave, the accumulation of which is unlimited, is earned at the rate of eight hours per month and is paid only when an employee is off due to illness or to the estate of an employee in the event of his or her death. The maximum sick leave that may be paid to an employee's estate is one-half of the employee's accumulated entitlement or 336 hours, whichever is less. The University's policy is to recognize the cost of sick leave when paid, and the liability is not shown in the financial statements because experience indicates that the expense for sick leave will be minimal. Eligible part-time employees' sick leave accrual rate is proportional to the number of hours appointed to work.

Notes and Loans Payable

Notes and loans payable obligations are due in annual installments through 2009. General information related to notes and loans payable at August 31, 2008, which in substance are not bonds, is summarized as follows:

Year	Total Principal	Total Interest
2009	$ 197,139	$ 10,113
Total	$ 197,139	$ 10,113

Other Notes and Loans Payable includes:

Note or loan payable issue name: Premier Purchasing Partners L.P.
Purpose: To purchase an ownership stake in this limited partnership
Institution: UT Southwestern Medical Center at Dallas
Issue Date: September 1, 2005
Authorized Amount: $369,190
Source of revenue for debt service: Rebates earned
Terms: Payment time as well as payment amount is dependent on calculation of rebates which is based on the purchasing volume of the medical center.

Note 6: Bonded Indebtedness

The University receives proceeds from revenue bonds issued and held by the System to support capital projects of the System and its institutions. These proceeds are recorded as transfers from the System. The University disburses funds to the System for payments of principal and interest related to the University's share of bond proceeds. These recorded as disbursements are transfers to the System. At August 31, 2008, the System had outstanding bonds payable of $4,408,053,628. All bonds issued by the System are defined as revenue bonds. As such, the revenues of the System, including the University, are pledged for repayment of the bonds. Segment information requirements are not applicable, due to the bond indentures' lack of specifically identifiable activities and separate accounting requirements imposed by an external party.

No amount of indebtedness related to these bonds has been recorded in the University's financial statements as the System is the party directly liable for these bonds. At August 31, 2008, however, the University's remaining unpaid share of the bond proceeds was $572,308,000.

Note 7: Capital Leases

Certain leases to finance the purchase of property are capitalized at the present value of future minimum lease payments.

Debt Service Requirement To Maturity

Year Ended August 31,		Total
2009		45,537
2010		37,948
Total Minimum Lease Payments	$	83,485
Less: Amount Representing Interest at Various Rates		(5,107)
Present Value of Net Minimum Lease Payments	$	78,378

Original Capitalized Costs Of Assets Under Capital Lease Obligations

		Assets under Capital Lease
Furniture and Equipment	$	194,234
Total	$	194,234

Note 8: Operating Leases

As of August 31, 2008, the University's operating lease obligations are as follows:

Year Ended August 31, 2008		Total
2009		4,433,355
2010		3,318,874
2011		2,418,893
2012		1,165,359
2013		898,775
2014-2018		256,992
2019-2023		269,842
2024-2028		283,334
2029-2033		297,500
2034-2038		312,376
Total Minimum Future Lease Payments	$	13,655,300

The University has also leased buildings and land to outside parties under various operating leases. The cost, carrying value and accumulated depreciation of these leased assets as of August 31, 2008 were as follows:

Assets Leased		2008
Buildings:		
Cost	$	38,816,277
Less: Accumulated Depreciation		(7,987,146)
Carrying Value		30,829,131
Land		53,931
Total	$	30,883,062

Note 9: Interagency Balances

At year-end, amounts to be received or paid are reported as Due from Other Entities or Due to Other Entities.

Entity		Due from Other State Entities		Due to Other State Entities	Purpose
UT System Administration	$	57,700,461	$	6,861,487	Estimated employee benefits- mainly insurance
UT Arlington		319,625			Joint Construction Project
	$	58,020,086	$	6,861,487	

Interagency transfers made during the fiscal year are presented below:

Entity		Transfers In from Other State Entities		Transfers Out to Other State Entities	Purpose
Coordinating Board	$		$	106,542	Medical Tuition set aside
UT System Administration				61,434,685	Transfers to UT System-Primarily for Debt Service Payments
UT System Administration		142,431,371			Transfers from UT System-Bond Proceeds for Construction Projects
	$	142,431,371	$	61,541,227	

Note 10: Contingent Liabilities

As of August 31, 2008 the University was not aware of any significant contingent liabilities.

Note 11: Risk Financing and Related Insurance

All risk financing and related insurance for the University is part of coverage provided by the System. The System has self-insurance plans providing coverage in the following areas: employee health and dental, unemployment compensation, workers' compensation, property protection, directors' and officers'/employment practices liability, and construction contractor insurance.

Employee and Retiree Insurance Benefits

The System Employee Benefits program provides health insurance, dental insurance, vision insurance, life insurance, long-term disability, short-term disability, long-term care, and flexible spending account coverage to all benefits-eligible employees and retirees of the System and its fifteen institutions. These insurance benefits are provided through both self- funded and fully-insured arrangements. A portion of the System's cost of providing group health and basic life insurance coverage is paid by the State as specified in the General Appropriations Act. The

System's Office of Employee Benefits (OEB) is responsible for the overall administration of the insurance plans. OEB was established by Chapter 1601 (formerly Article 3.50-3) of the *Texas Insurance Code* and complies with State laws and statutes pertinent to employee benefits for the System.

Unemployment Compensation Insurance

The General Appropriations Act requires the System to reimburse the Texas Workforce Commission (TWC) for 50% of the unemployment benefits paid to former employees that were paid from general revenue funds. The System reimburses the TWC 100% of the unemployment benefits paid to former employees that were paid from local funds.

The University of Texas System Workers' Compensation Insurance (WCI) program provides coverage to all employees of the System and its fifteen institutions. Under the oversight of the System's Office of Risk Management (ORM), the System self-insures and administers the program. The WCI staff is responsible for administering all aspects of the system-wide program, which provides income and medical benefits to all employees who have sustained job-related injuries or occupational diseases. The program's statutory authority is embodied in Chapter 503 of the *Texas Labor Code*.

Professional Medical Liability Benefit Plan

The coverage provided under the Professional Medical Liability Benefit Plan (Plan) is on an occurrence basis; thus, a participant is covered by the Plan for claims and lawsuits relating to events that occurred while enrolled in the Plan, including those filed after the participant has left the System's employment or training. The Plan covers all of the System staff physicians, dentists, residents, fellows, and medical students who have been enrolled. The limits of liability of the Plan include an annual policy aggregate of $30,000,000, an annual aggregate of $1,500,000 for each staff physician ($500,000 per claim), an annual aggregate of $300,000 for each resident or fellow ($100,000 per claim) and a $75,000 annual aggregate for each medical student ($25,000 per claim). Medical students may be eligible for additional coverage when they enroll in an institution approved "externship" outside of the State of Texas. Liability is limited to $2,000,000 per incident, regardless of the number of claimants or physicians involved in an incident. As of September 1, 2003, the limits of liability are prescribed by law as $100,000 per claim per physician. Also effective September 1, 2003, UT institutions are covered under the Plan for actions that could have been brought against an individual plan participant. The liability of a UT institution is limited by law to $250,000 per claimant and $500,000 per occurrence for bodily injury or death.

Comprehensive Property Protection Program

The property protection plan consists of two programs. The first provides coverage for physical damage resulting from Named Windstorms and catastrophic flood losses up to $50 million. Insurance policies providing underlying limits ($1-2 million per building and contents) are purchased through the Texas Windstorm Insurance Association and the National Flood Insurance Program on several facilities in the Tier 1 wind zone and other flood prone areas to provide a primary layer of insurance. The self-insurance component of the program participates in losses that exceed the coverage available under these primary policies or in cases where there is no underlying insurance.

The second program covers fire and other perils and includes commercial coverage for claims exceeding a per occurrence deductible of $7.5 million or an annual aggregate deductible of $25 million. The policy covers all UT System buildings and personal property and business income reported by the institutions. The maximum annual reimbursement under this policy is $1 billion per occurrence.

Directors and Officers/Employment Practices Liability Self-Insurance Plan

The Directors and Officers Liability (D&O) and Employment Practices Liability Self-insurance Plan provides coverage for claims arising from actual or alleged wrongful acts performed by the plan beneficiaries. The plan also provides coverage for employment practices liability (EPL) claims, such as wrongful termination, failure to promote and wrongful discipline. Coverage applies to individual board members, employees, faculty, etc., as well as to the System itself. The limit of liability is a $10 million annual aggregate (Coverages A, B and C combined), except for $5 million annual aggregate sublimit for Coverage C. There is no deductible for Coverage A (individuals), a $100,000 deductible per director or officer with a $300,000 maximum deductible per loss for Coverage B. The deductible for Coverage C is $300,000. In 2003, the UT System Board of Regents allocated $3.7 million from the Available University Fund to establish the D&O/EPL loss reserve fund. Institutions make annual premium contributions to this fund.

Rolling Owner Controlled Insurance Program

The Rolling Owner Controlled Insurance Program (ROCIP) was established for the centralized purchase of construction contractor insurance on various capital projects. This program provides workers' compensation and general liability insurance for all contractors enrolled on projects participating in the program. The insurance carries a $250,000 per occurrence basket deductible, which is paid through the program's self-insurance fund.

Note 12: Subsequent Events

As of August 31, 2008 there are no subsequent events pertaining to the University.

Note 13: Related Parties

UT Southwestern Health Systems (UTSHS), a blended component unit of UT Southwestern Medical Center at Dallas, is a participating member of UT Southwestern DVA Healthcare, LLP (DVA). DVA is a joint venture between UTSHS and Davita Inc. to provide care for dialysis patients in the Dallas-Fort Worth area. UTSHS's equity interest in DVA at August 31, 2008 was $3,557,345.17 or 49%. Separate financial statements for DaVita may be obtained at DaVita Inc., 601 Hawaii Street, El Segundo, CA 90245 or davita.com.

Note 14: Stewardship, Compliance and Accountability

As of August 31, 2008 there are no issues related to stewardship, compliance or accountability pertaining to the University.

Note 15: The Financial Reporting Entity

Blended Component Units

UT Southwestern Health Systems, Inc., 1301 Elmbrook, Dallas, Texas 75390, is governed by a three-member board appointed by the University. Although it is legally separate from the University, UT Southwestern Health Systems, Inc. is reported as if it were part of the University because its primary purpose is to perform services as an integral part of the institution. The corporation's fiscal year end is August 31, 2008.

The National Pediatric Infectious Diseases Foundation, 4712 Wildwood Drive, Dallas, Texas 75209, is governed by a three-member board appointed by the University. The Foundation supports educational, clinical and scientific activities and programs in the area of infectious diseases in infants and children. Although it is legally separate from the University, the National Pediatric Infectious Diseases Foundation is reported as if it were part of the University because it provides grants to the University and its board is appointed by the University. The Foundation's fiscal year end is August 31, 2008.

UT Southwestern Moncrief Cancer Center, 1701 River Run, Suite 500, Fort Worth, Texas 76107, is a nonprofit corporation governed by a five-member board appointed by the President of the University. The Center specializes in providing counseling and support resources to cancer patients and their families within Tarrant County and surrounding areas. Although it is legally separate from the University, UT Southwestern Moncrief Cancer Center is reported as if it were part of the University because its board is appointed by the University. The Center's fiscal year end is August 31, 2008.

Note 16: Restatements

As of August 31, 2008 the University was not aware of any restatements.

Note 17: Employee Retirement Plans

Teacher Retirement System (TRS)

The State of Texas has joint contributory retirement plans for substantially all its employees. One of the primary plans in which the System participates is a cost-sharing multi-employer defined benefit pension plan administered by the Teacher Retirement System of Texas. TRS is primarily funded through State and employee contributions. Depending upon the source of funding for a participant's salary, the System may be required to make contributions in lieu of the State.

All System personnel employed in a position on a half time or greater basis for at least 4½ months or more are eligible for membership in the TRS retirement plan. However, students employed in positions that require student status as a condition of employment do not participate. Members with at least five years of service at age 65 or any combination of age plus years of service, which equals 80, have a vested right to retirement benefits. Additionally, reduced benefits are available at age 55 with at least five years of service or at any age below 50 with 30 years of service. Members are fully vested after five years of service and are entitled to any benefits for which the eligibility requirements have been met.

TRS contribution rates for both employers and employees are not actuarially determined but are legally established by the State Legislature. Contributions by employees are 6.4 percent of gross earnings. Depending upon the source of funding for the employee’s compensation, the State or the System contributes a percentage of participant salaries totaling 6.58 percent of annual compensation. The System’s contributions to TRS for the years ended August 31, 2008, was $4,832,502 which equaled the amounts of the required contributions for that year.

TRS does not separately account for each of its component government agencies since the Retirement System itself bears sole responsibility for retirement commitments beyond contributions fixed by the State Legislature. Further information regarding actuarial assumptions and conclusions, together with audited financial statements are included in the Retirement System’s annual financial report, which may be found on the TRS website at www.trs.state.tx.us.

Optional Retirement Program (ORP)

The State has also established an optional retirement program for institutions of higher education. Participation in the ORP is in lieu of participation in the Teacher Retirement System. The ORP provides for the purchase of annuity contracts and mutual funds. Participants are vested in the employer contributions after one year and one day of service. The contributory percentages of participant salaries currently provided by the State and each participant are 6.0 percent and 6.65 percent, respectively. Depending upon the source of funding for the employee’s compensation, the University may be required to make the employer contributions in lieu of the State. Additionally, the State or the University must make additional contributions above 6.0 percent depending upon the employee’s date of hire. Since these are individual annuity contracts, the State and the University have no additional or unfunded liability for this program.

Note 18: Deferred Compensation Program

University employees may elect to defer a portion of their earnings for income tax and investment purposes pursuant to authority granted in Texas Government Code, Section 609.001. Deferred compensation plans are administered by the Employees Retirement System. The State’s 457 Plan complies with Internal Revenue Code, Section 457. This plan is referred to as the TexaSaver Deferred Compensation Plan and is available to all employees. Deductions, purchased investments, and earnings attributed to the 457 Plan are the property of the State and subject only to the claims of the State's general creditors. Participant rights under the plan are equal to those of the general creditors of the State in an amount equal to the fair market value of the 457 account for each participant. The State has no liability under the 457 Plan, and it is unlikely that plan assets will be used to satisfy the claims of general creditors in the future. The University also administers a Tax-Deferred Account Program, created in accordance with Internal Revenue Code, Section 403(b). All employees are eligible to participate. The Tax-Deferred Account Program is a private plan, and the deductions, purchased investments, and earnings attributed to each employee's 403(b) plan are held by vendors chosen by the employee. The vendors may be insurance companies, banks, or approved non-bank trustees such as mutual fund companies. The assets of this plan do not belong to the University, and thus it does not have a liability related to this plan.

Note 19: Donor-Restricted Endowments

Net Asset Classification of Endowments	2008
Restricted, nonexpendable	416,729,264
Restricted , expendable	
Net Appreciation	294,738,345
Funds Functioning as Endowments	25,242,182
Unrestricted	
Funds Functioning as Endowments	25,526,113
Total	762,235,904

For donor restricted endowments, pursuant to the Uniform Management of Institutional Funds Act, as adopted by Texas, the Board of Regents may distribute net appreciation, realized and unrealized in the fair market value of the assets of endowment holdings over the historic dollar value of the gifts, to the extent prudent. The System's policy is to retain all undistributed net realized and unrealized appreciation within the endowment finds. The book value of endowments is reflected as nonexpendable assets, the appreciated value of endowments is reflected as expendable assets on the net assets sections of the balance sheet. In FY08 the University did not expend any amounts from the appreciated value of its endowments. University is subject to the UT Board of Regents policies and procedures on endowment management.

Note 20: Post-Employment

In addition to providing pension benefits, the University provided certain health and life insurance benefits for retired employees, in accordance with State statutes. Many employees may become eligible for the health and life insurance benefits as a retired employee if they meet certain age and service requirements as defined by the State. Currently there are 1,081 retired employees who are eligible for these benefits. Similar benefits for active employees are provided through the same self-funded plan and fully-insured plans. The State and the

University recognize the cost of providing these benefits to eligible retired employees. The cost of retired employee benefits is recognized when paid. For the fiscal year ended August 31, 2008, the monthly contribution by the State or the University per full-time employee/retiree ranged from $369 to $721 depending upon the plan and level of coverage selected. These contributions paid all of the cost of coverage for the employee/retired employee and a portion of the cost of coverage for enrolled dependents. The employee/retired employee is required to pay a portion of the cost of dependent coverage. For the fiscal year ended August 31, 2008, the costs of providing those benefits for the retired employees are $3,999,971 for the State and $1,508,872 for the University.

In August 2004, the GASB issued Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions, effective for the System in fiscal year 2008. GASB Statement No. 45 requires accrual-based measurement, recognition and disclosure of other postemployment benefits (OPEB) expense, such as retiree medical and dental costs, over the employees' years of service, along with the related liability, net of any plan assets. The System has determined the effect the GASB Statement No. 45 will have on the System's Consolidated financial statements.

PLAN DESCRIPTION AND FUNDING POLICY

OPEB are provided to the System's retirees under the UT System Employee Group Insurance Program (EGIP). The EGIP is a single-employer defined benefit OPEB plan. The authority under which the obligations of the plan members and the System are established and may be amended is Chapter 1601, *Texas Insurance Code*.

The System and member contribution rates are determined annually by the System based on the recommendations of the OEB staff and consulting actuary. The contribution rates are determined based on the benefit and administrative costs expected to be incurred and (i) the funds appropriated and (ii) the funding policy established by the Texas Legislature in connection with benefits provided through the EGIP. The System revises benefits when necessary to match expected benefit and administrative costs with available revenue. The plan is operated on a pay as you go basis.

Because the OPEB plan described herein is not administered through a trust as defined under Paragraph No. 4 of GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, GASB Statement No. 43 accounting is not required for this plan.

2008 ANNUAL OPEB COST, EMPLOYER CONTRIBUTIONS AND NET OPEB OBLIGATION							
(1)	**(2)**	**(3)**	**(4)**	**(5)**	**(6)**	**(7)**	**(8)**
ARC	**Interest on Net OPEB Obligation**	**Adjustment to the ARC**	**Annual OPEB Cost {(1) + (2) - (3)}**	**Employer Contributions**	**Increase (Decrease) in Net OPEB Obligation {(4) - (5)}**	**Net OPEB Obligation at Beginning of Year**	**Net OPEB Obligation at End of Year {(6) + (7)}**
$522,570,019	-	-	522,570,019	99,891,995	422,678,024	-	422,678,024

THREE-YEAR HISTORY OF ANNUAL OPEB COST AND NET OPEB OBLIGATION

Since 2008 is the initial year of application of GASB Statement No. 45, no preceding year information is shown.

(1)	**(2)**	**(3)**	**(4)**	**(5)**
Fiscal Year Ending	**Annual OPEB Cost**	**Employer Contributions**	**Percentage of Annual OPEB Cost Contributed {(3)/(2)}**	**Net OPEB Obligation at End of Year**
August 31, 2008	$522,570,019	99,891,995	19.1%	422,678,024

The OPEB Expense (Cost) reflected on the Statement of Revenues, Expenses and Changes in Net Assets is net of the Employer Contributions as these costs are reflected as a portion of Payroll Related Costs expense.

SCHEDULE OF FUNDING PROGRESS OF THE PLAN AS OF DECEMBER 31, 2007

The Schedule of Funding Progress presents information as of the current valuation date and the two preceding valuation dates. Since this is the initial year of application of GASB Statement No. 45, no preceding year information is shown.

(1)	(2)	(3)	(4)	(5)	(6)	(7)
Actuarial Valuation Date	**Actuarial Value of Assets**	**Actuarial Accrued Liability**	**Unfunded Actuarial Accrued Liability (UAAL) {(3) - (2)}**	**Funded Ratio {(2)/(3)}**	**Annual Covered Payroll**	**Ratio of UAAL to Covered Payroll {(4)/(6)}**
December 31, 2007	$-	5,014.216,756	5,014,216,756	0.0%	4,312,906,627	116.3%

ACTUARIAL METHODS AND ASSUMPTIONS

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future.

The Schedule of Funding Progress shown above presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

GASB Statement No. 45 calculations are based on the types of benefits provided under the terms of the substantive plan at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point. In addition, the projection of benefits for financial reporting purposes *does not* explicitly incorporate the potential effects of legal or contractual funding limitations on the pattern of cost sharing between the employer and plan members in the future.

Actuarial calculations reflect a long-term perspective. In addition, consistent with that perspective, actuarial methods and assumptions used in developing the figures in this report include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities.

The information presented herein was determined as part of the actuarial valuation using the actuarial methods and assumptions summarized below.

Summary of Actuarial Methods and Assumptions	
Actuarial cost method	Entry Age Normal (Level percent of pay)
Asset valuation method	Market
Actuarial assumptions:	
Annual investment return assumption (discount rate)[1]	7.00%
Projected annual salary increases[1]	5.25% to 8.50%
Weighted-average at valuation date[1]	7.01%
Annual Healthcare Trend Rates[1]	8.00% in FYE 2009
	Declining to 6.00% in FYE 2014
Amortization method	Level percent
Amortization period	30 year open period

[1]Includes inflation assumption of 4.00%

SIGNIFICANT FACTORS AFFECTING THE COMPARABILITY OF AMOUNTS REPORTED

Because this is the first actuarial valuation for the plan, there are no such factors to be identified at this time.

DISCLOSURE IN YEAR OF TRANSITION

The System implemented GASB Statement No. 45 on a prospective basis during 2008. Therefore, the OPEB liability at transition was $0.

Note 21: Special or Extraordinary Items

As of August 31, 2008 there are no special or extraordinary items pertaining to the University.

Note 22: Disaggregation of Other Receivable Balances

Net other receivables as of August 31, 2008 are detailed by type as follows:

Net Other Receivables		**2008**
Receivables related to healthcare		18,906,878
Receivables related to gifts, grants and sponsored programs		4,551,284
Receivables related to auxiliary enterprises		384
Receivables related to payroll		50,672
Receivables related to patents		1,269,500
Receivables related to loan funds and financial aid		16,654
Receivables related to other various activities		5,719,882
Total	$	30,515,254

Note 23: Termination Benefits

As of August 31, 2008 there are no termination benefits pertaining to the University.

State Auditor's Office
John Keel, CPA
State Auditor

January 28, 2009

Dr. Daniel K. Podolsky, President
The University of Texas Southwestern Medical Center at Dallas
5323 Harry Hines Blvd.
Dallas, TX 75390-9003

Subject: Management Letter Resulting from a Review of the University of Texas Southwestern Medical Center at Dallas Fiscal Year 2008 Financial Statements

Dear Dr. Podolsky:

We offer this management letter in conjunction with our review of the financial statements of the University of Texas Southwestern Medical Center at Dallas (Medical Center) for the fiscal year ended August 31, 2008. We reviewed the Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; the Statement of Cash Flows; and the Notes to the Financial Statements. In the course of our review, which was substantially less in scope than an audit, we did not find that material modifications needed to be made to the financial statements in order for them to be in conformity with generally accepted accounting principles.

We appreciate the assistance provided during this review by the management of the Medical Center and Internal Audit. If you have any questions, please call me at (512) 936-9500.

Sincerely,

Sandra Vice

Sandra Vice, CGAP, CIA, CISA
Assistant State Auditor

Robert E. Johnson Building
1501 N. Congress Avenue
Austin, Texas 78701

P.O. Box 12067
Austin, Texas 78711-2067

Phone:
(512) 936-9500

Fax:
(512) 936-9400

Internet:
www.sao.state.tx.us

Copies of this report have been distributed to the following:

Legislative Audit Committee

The Honorable David Dewhurst, Lieutenant Governor, Joint Chair
The Honorable Joe Straus III, Speaker of the House, Joint Chair
The Honorable Steve Ogden, Senate Finance Committee
The Honorable Thomas "Tommy" Williams, Member, Texas Senate
The Honorable Jim Pitts, House Appropriations Committee
The Honorable Rene Oliveira, House Ways and Means Committee

Office of the Governor

The Honorable Rick Perry, Governor