



CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Financial Statements

June 30, 2006 and 2005

(With Independent Auditors' Report Thereon)

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Table of Contents

	Page
Independent Auditors' Report	1
Management's Discussion and Analysis	3
Basic Financial Statements:	
Statements of Net Assets	15
Statements of Revenues, Expenses, and Changes in Net Assets	17
Statements of Cash Flows	19
Notes to Financial Statements	21



KPMG LLP
Suite 700
600 Anton Boulevard
Costa Mesa, CA 92626-7651

Independent Auditors' Report

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

We have audited the accompanying financial statements of the California State University, San Marcos (the University) and its aggregate discretely presented component units as of and for the years ended June 30, 2006 and 2005, which collectively comprise the University's basic financial statements as listed in the accompanying table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express opinions on these financial statements based upon our audits. We did not audit the financial statements of the aggregate discretely presented component units. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinions, insofar as they relate to the amounts included for the aggregate discretely presented component units, are based solely on the reports of the other auditors.

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

As discussed in note 2, the financial statements present only the statements of net assets, statements of revenues, expenses, and changes in net assets, and statements of cash flows of the University and do not purport to, and do not, present fairly the financial position of the California State University System as of June 30, 2006 and 2005, and the changes in its financial position and its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

In our opinion, based on our audits and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the University and of its aggregate discretely presented component units as of June 30, 2006 and 2005, and the respective changes in financial position and, where applicable, cash flows thereof, for the years then ended, in conformity with U.S. generally accepted accounting principles.

Management's discussion and analysis on pages 3 through 14 is not a required part of the basic financial statements, but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

December 1, 2006

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis (Unaudited)

June 30, 2006 and 2005

This section of California State University, San Marcos (the University) annual financial report presents management's discussion and analysis of the financial performance of the University for the fiscal years ended June 30, 2006 and 2005. This discussion has been prepared by management and should be read in conjunction with the financial statements and notes.

Introduction to the Financial Statements

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

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

Statements of Net Assets – The statements of net assets include all assets and liabilities. Assets and liabilities are reported at their book value, on an accrual basis, as of the statement date. They also identify major categories of restrictions on the net assets of the University.

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

Statements of Cash Flows – The statements of cash flows present the inflows and outflows of cash for the year and are summarized by operating, noncapital financing, capital and related financing, and investing activities. The statements are prepared using the direct method of cash flows and, therefore, present gross rather than net amounts for the years' activities.

Analytical Overview

Summary

The following discussion highlights management's understanding of the key financial aspects of the University's financial activities as of and for the years ended June 30, 2006 and 2005. Included is a comparative analysis of current-year and prior-year activities and balances; a discussion of restrictions of University net assets; a discussion of capital assets and long-term debt; and factors impacting future reporting periods.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis (Unaudited)

June 30, 2006 and 2005

The University's condensed summary of net assets as of June 30, 2006, 2005, and 2004 is as follows:

Condensed Summary of Net Assets

	June 30		
	2006	2005	2004
Assets:			
Current assets	\$ 26,730,357	28,238,591	28,489,769
Capital assets	169,471,459	162,968,819	149,570,121
Other noncurrent assets	36,977,448	49,554,216	30,657,688
Total assets	233,179,264	240,761,626	208,717,578
Liabilities:			
Current liabilities	14,094,304	14,158,858	15,636,856
Long-term debt obligations, net of current portion	32,730,963	32,424,322	7,279,677
Other noncurrent liabilities	2,532,370	2,037,682	2,118,793
Total liabilities	49,357,637	48,620,862	25,035,326
Net assets:			
Invested in capital assets, net of related debt	162,692,393	156,463,965	141,373,505
Restricted – expendable	8,784,354	20,570,018	29,886,422
Unrestricted	12,344,880	15,106,781	12,422,325
Total net assets	\$ 183,821,627	192,140,764	183,682,252

As of June 30, 2006

Assets

The \$7.6 million decrease in assets is primarily due to a \$12.3 million decrease in noncurrent accounts receivable relating to State Appropriations for capital projects. The funds were used to complete the University's new Business Building which was completed in January 2006.

The \$6.5 million increase in capital assets is due to \$15.3 million in additions from ongoing capital projects, primarily due to the completion of the Campus' Business Building. These additions are offset by \$8.7 million in current-year depreciation expense. Capital expansion is financed through University funds, issuance of debt, as well as general obligation bonds of the State of California and the California State University System which is not reflected in the accompanying financial statements.

Liabilities

The \$0.7 million increase in total liabilities from the prior year is primarily due to a \$1.4 million increase in long term debt and capital leases to fund the University's computer refresh program and PeopleSoft CMS implementation costs. Accrued compensated absences increased by \$0.4 million. These increases are offset by a decrease in accounts payable by \$0.4 million due to a decrease in accruals for capital construction projects and a \$0.8 million decrease in other liabilities.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis (Unaudited)

June 30, 2006 and 2005

Net Assets

A significant portion of net assets at the end of the year is invested in capital assets. The decrease in net assets of \$8.3 million from the prior year is primarily related to a decrease of \$9.2 million in state appropriations used for capital projects.

As of June 30, 2005

Assets

The \$32.0 million increase in total assets is primarily due to a \$25.2 million lease receivable added in the fiscal year ending June 30, 2005. The lease agreement is the result of a transaction whereby the University refinanced certain San Marcos University Corporation bonds used to build campus housing that was placed into service in August 2003. The San Marcos University Corporation debt was refinanced through the issuance of System-wide revenue bonds Series 2005A that are recorded as a long-term liability with the University. In return for the University refinancing the San Marcos University Corporation debt, the University entered into a 30-year lease agreement whereby the San Marcos University Corporation agreed to lease the campus housing facilities.

The \$13.4 million increase in capital assets is due to ongoing capital projects, primarily due to the construction of the campus' Business Building. Capital expansion is financed through University funds, issuance of debt, as well as general obligation bonds of the State of California and the California State University System, which are not allocated to the campus and thus not reflected in the accompanying financial statements. Depreciation expense for the year totaled \$7.3 million.

These increases in assets are offset by a \$6.3 million decrease in accounts receivable from state appropriations for funds used to construct capital projects.

Liabilities

The \$23.6 million increase in total liabilities from prior year is primarily due to the issuance of a \$25.2 million System-wide revenue bond. As discussed above, these bonds were used to refinance the San Marcos University Corporation Corps debt in return for a \$25.2 million lease receivable. Accounts payable increased by \$2.6 million due to an increase in accruals for capital construction projects. These increases are offset by a \$3.4 million reduction in deferred revenue.

Net Assets

A significant portion of net assets at the end of the year is invested in capital assets. The increase in net assets of \$8.5 million from the prior year is primarily related to \$10.0 million in state appropriations for capital projects.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis (Unaudited)

June 30, 2006 and 2005

Restricted Resources

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

	Restricted Net Assets		
	June 30		
	2006	2005	2004
Expendable:			
Scholarships and fellowships	\$ 157,319	98,764	208,925
Loans	53,559	53,479	51,091
Capital projects	8,573,476	20,078,277	29,088,185
Debt service	—	339,498	538,221
Total restricted net assets – expendable	<u>\$ 8,784,354</u>	<u>20,570,018</u>	<u>29,886,422</u>

As of June 30, 2006

The \$11.8 million decrease in restricted net assets – expendable is primarily due to the decrease in state appropriations for capital projects.

As of June 30, 2005

The \$9.3 million decrease in restricted net assets – expendable is primarily due to the decrease in state appropriations for capital projects received during the years, as well as a decrease in state appropriations receivable for capital projects.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis (Unaudited)

June 30, 2006 and 2005

The University's condensed summary of revenues, expenses, and changes in net assets for the years ended June 30, 2006, 2005, and 2004 is as follows:

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

Year ended June 30

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Operating revenues:			
Student tuition and fees	\$ 22,867,810	19,944,432	18,162,391
Grants, contracts, and gifts	7,476,237	7,650,686	7,899,917
Sales and services of auxiliary enterprises, net	2,886,925	2,791,347	2,687,295
Other operating revenue	<u>790,347</u>	<u>177,575</u>	<u>323,132</u>
Total operating expenses	<u>34,021,319</u>	<u>30,564,040</u>	<u>29,072,735</u>
Operating expenses	<u>100,198,743</u>	<u>87,705,824</u>	<u>91,795,320</u>
Operating loss	<u>(66,177,424)</u>	<u>(57,141,784)</u>	<u>(62,722,585)</u>
Nonoperating revenues (expenses):			
State appropriations	54,723,975	53,307,764	54,573,409
Investment income	1,918,433	354,716	140,314
Interest on capital-related debt	(1,548,154)	(726,360)	(377,508)
Other nonoperating revenues (expenses)	<u>1,131,400</u>	<u>2,662,176</u>	<u>904,328</u>
Total nonoperating revenues (expenses)	<u>56,225,654</u>	<u>55,598,296</u>	<u>55,240,543</u>
Other capital-related revenues:			
State appropriations, capital	767,000	10,002,000	26,008,455
Grants and gifts, capital	<u>865,633</u>	<u>—</u>	<u>—</u>
Increase (decrease) in net assets	<u>(8,319,137)</u>	<u>8,458,512</u>	<u>18,526,413</u>
Net assets at beginning of year	<u>192,140,764</u>	<u>183,682,252</u>	<u>165,155,839</u>
Net assets at end of year	<u>\$ 183,821,627</u>	<u>192,140,764</u>	<u>183,682,252</u>

Operating Revenues and Expenses

Operating revenues and expenses come from sources that are connected directly to the University's primary business function. This includes revenues from categories such as tuition and fees, grants, and contracts that will be used for noncapital purposes, and sales and services of auxiliary enterprises. Expenses include categories such as salaries and wages, benefits, supplies and services, student grants and scholarships, and depreciation. In this discussion and analysis, expenses are reported by functional program such as instruction, academic support, and student services.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis (Unaudited)

June 30, 2006 and 2005

Operating Revenues

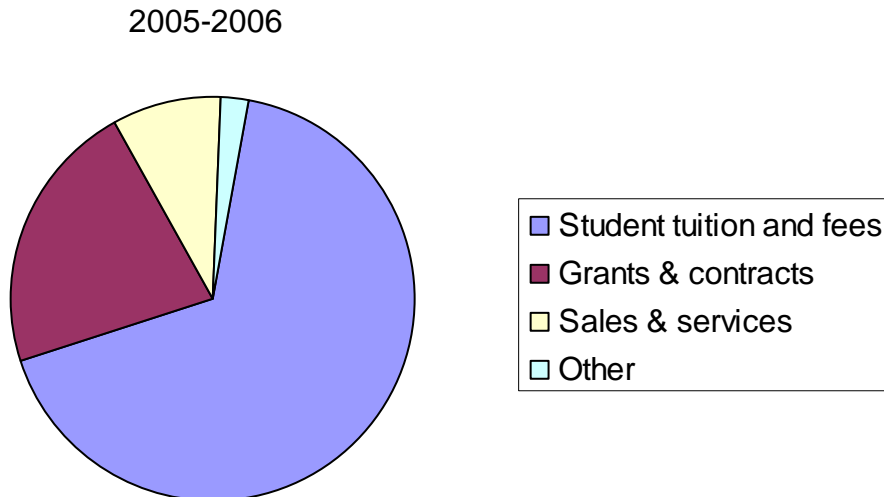
Year Ended June 30, 2006

The University recognized \$34.0 million in operating revenues during this fiscal year, as compared to \$30.6 million in the prior year. Operating revenues comprised 37% of total revenues for the year ended June 30, 2006, compared to 32% of total revenues for the year ended June 30, 2005. Federal and state grants and contracts revenue decreased \$0.2 million from \$7.7 million to \$7.5 million for the fiscal year ended June 30, 2005 and 2006, respectively. Finally, student fees were increased again by the California State University (CSU) board of trustees in 2006. Student fee revenue increased by \$3.0 million, from \$19.9 million in 2005 to \$22.9 million in 2006.

Year Ended June 30, 2005

The University recognized \$30.6 million in operating revenues during this fiscal year, as compared to \$29.1 million in the prior year. Operating revenues comprised 32% of total revenues for the year ended June 30, 2005, compared to 26% of total revenues for the year ended June 30, 2004. Federal and state grants and contracts revenue decreased \$0.2 million from \$7.9 million to \$7.7 million for the fiscal years ended June 30, 2004 and 2005, respectively. Finally, student fees were increased again by the California State University Board of Trustees in 2005 to compensate for the loss of state appropriations for operations. Student fee revenue increased by \$1.7 million, from \$18.2 million in 2004 to \$19.9 million in 2005.

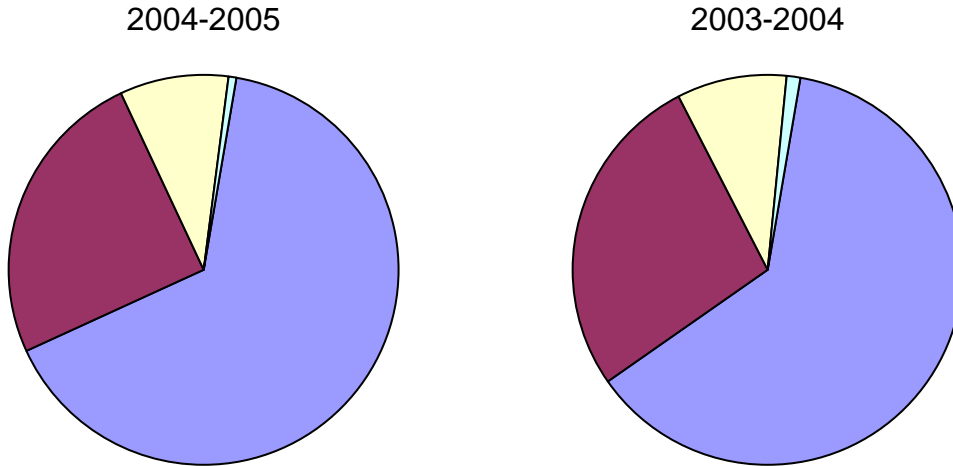
The following charts present the proportional share that each category of operating revenues contributed to the total for fiscal years 2006, 2005, and 2004:



CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis (Unaudited)

June 30, 2006 and 2005



Operating Expenses

Year Ended June 30, 2006

The University's operating expenses consist of salaries and fringe benefits of \$62.9 million, supplies and services of \$19.3 million, scholarships and fellowships of \$9.3 million, and depreciation of \$8.7 million. Total operating expenses, excluding depreciation, increased by \$11.1 million, or 13.9% due to an increase of \$4.4 million of salaries and benefits expense, \$2.8 million in scholarship and fellowship expense and \$3.9 million in supplies and services. Enrollment remained stable for the fiscal year 2005-2006, increasing by 0.7% and the percentage of students receiving aid decreased from approximately 47.0% in 2005 to 43.0% in 2006. The increase in depreciation expense of \$1.4 million relates to current-year capital asset additions.

Year Ended June 30, 2005

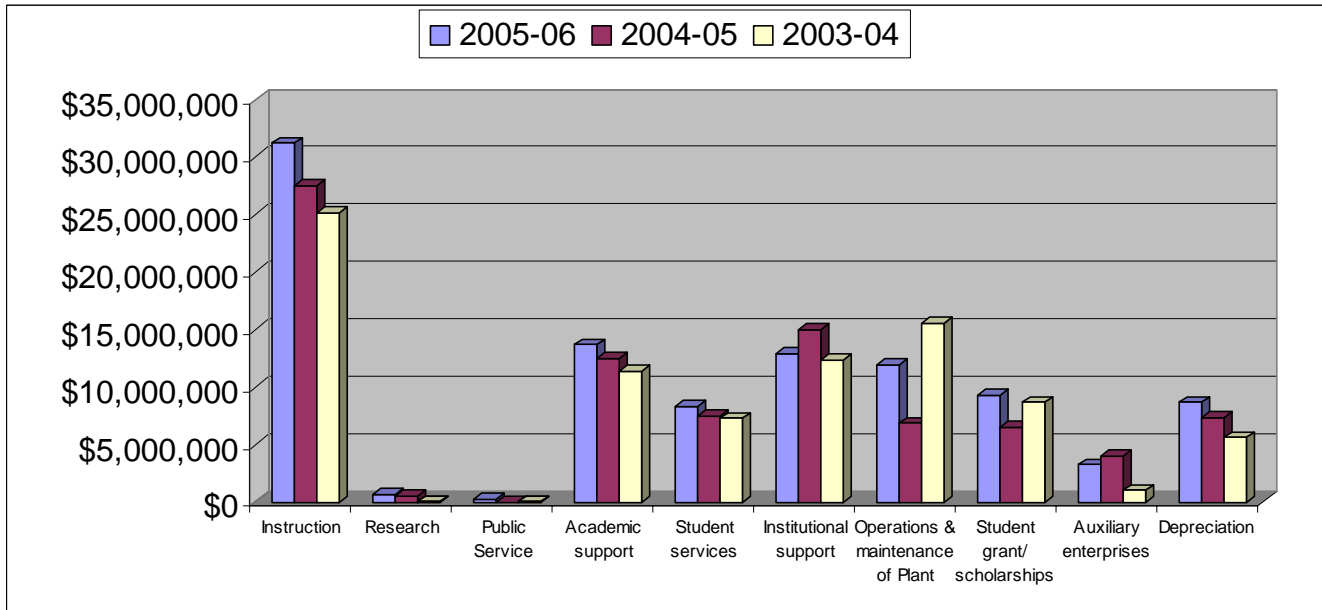
The University's operating expenses consist of salaries and fringe benefits of \$58.4 million, supplies and services of \$15.4 million, scholarships and fellowships of \$6.5 million, and depreciation of \$7.3 million. Total operating expenses, excluding depreciation, decreased by \$4.6 million, or 5% due to a decrease of \$5.3 million of scholarship and fellowship expense. Enrollment remained stable for the fiscal year 2004-2005, decreasing by 0.9%, and the percentage of students receiving aid remained relatively consistent, increasing from approximately 46.0% in 2004 to 47.0% in 2005. The increase in depreciation expense of \$0.5 million relates to current-year capital asset additions.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis (Unaudited)

June 30, 2006 and 2005

The following chart presents the distribution of resources in support of the University's mission for fiscal years 2006, 2005, and 2004:



Nonoperating and Other Revenues (Expenses)

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

Year Ended June 30, 2006

As the University is part of the California State University System, which is an agency of the State of California, the University's operations are funded primarily from appropriations of State tax revenues. Appropriations used for purposes of acquisition of capital assets totaled \$0.8 million for the fiscal year ended June 30, 2006, a decrease of \$9.2 million from the fiscal year ended June 30, 2005. General (noncapital) appropriation revenues totaled \$54.7 million, an increase of \$1.4 million from the prior year.

Year Ended June 30, 2005

Appropriations used for purposes of acquisition of capital assets totaled \$10.0 million for the fiscal year ended June 30, 2005, a decrease of \$16.0 million from the fiscal year ended June 30, 2004. General (noncapital) appropriation revenues totaled \$53.3 million, a decrease of \$1.3 million from the prior year. For the second consecutive year, the CSU experienced a shift in funding, with reduced state general fund allocation and increased state university fee revenue per student.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis (Unaudited)

June 30, 2006 and 2005

Capital Assets and Long-Term Debt Obligations

Capital Assets

Capital assets, net of accumulated depreciation are shown below:

	June 30		
	2006	2005	2004
Land and land improvements	\$ 10,981,328	10,981,328	10,981,328
Buildings and building improvements	127,104,513	108,203,900	112,673,789
Improvements, other than buildings	2,846,281	2,925,873	2,585,504
Infrastructure	13,909,444	13,771,983	14,277,813
Personal property	7,256,097	5,862,522	7,071,786
Intangible assets	801,422	102,128	77,108
Works of art and historical treasures	25,000	25,000	25,000
Construction work in progress (CWIP)	6,547,374	21,096,085	1,877,793
	<hr/>	<hr/>	<hr/>
Total capital assets, net of accumulated depreciation	\$ <u>169,471,459</u>	<u>162,968,819</u>	<u>149,570,121</u>

As of June 30, 2006

At June 30, 2006 and 2005, the University had \$169.5 million and \$163.0 million, respectively, in capital assets, net of accumulated depreciation of \$71.2 million and \$63.8 million, respectively. Depreciation expense totaled \$8.7 million and \$7.3 million for the years ended June 30, 2006 and 2005, respectively.

The University's new Business Building was placed into service in January 2006 and was the primary reason for the increase in fixed assets and decrease in CWIP from \$21.1 million to \$6.5 million for the fiscal years ended June 30, 2005 and 2006, respectively.

As of June 30, 2005

At June 30, 2005 and 2004, the University had \$163.0 million and \$149.6 million, respectively, in capital assets, net of accumulated depreciation of \$63.8 million and \$56.8 million, respectively. Depreciation expense totaled \$7.3 million and \$6.8 million for the years ended June 30, 2005 and 2004, respectively.

The University did not complete a major project during fiscal year 2005; however, the Business Building was completed in January 2006. The Business Building is the primary factor for the increase in CWIP to \$21.1 million from \$1.9 million for the fiscal year ended June 30, 2005 and 2004, respectively.

See note 6 of the notes to the financial statements for further information on capital assets.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis (Unaudited)

June 30, 2006 and 2005

Long-Term Debt Obligations

Debt outstanding at June 30, 2006, 2005, and 2004 is summarized below by type of debt instrument:

	June 30		
	2006	2005	2004
System-wide revenue bonds	\$ 30,625,000	30,715,000	5,580,000
Capital leases	506,000	4,516	1,484,068
Other	2,931,801	1,924,062	1,132,548
Total long-term debt	34,062,801	32,643,578	8,196,616
Less current portion	(1,331,838)	(219,256)	(916,939)
Long-term debt, net of current portion	<u>\$ 32,730,963</u>	<u>32,424,322</u>	<u>7,279,677</u>

The interest rates on outstanding debt range from 2.5% to 6%.

As of June 30, 2006

At June 30, 2006 and 2005, the University had \$34.1 million and \$32.6 million, respectively, in long-term debt outstanding. The \$1.5 million increase is primarily due to the addition of \$0.5 million increase in capital leases for PeopleSoft CMS and \$1.8 million in financing of noncapital assets. Offsetting these increases is \$0.9 million for the retirement of the University's debt.

As of June 30, 2005

At June 30, 2005 and 2004, the University had \$32.6 million and \$8.2 million, respectively, in long-term debt outstanding. The \$24.4 million increase is primarily due to the issuance of \$25.2 million System-wide revenue bonds. As discussed above, these bonds were used to refinance the San Marcos University Corporation debt in return for a \$25.2 million lease receivable. The University also incurred \$0.8 million of additional debt for the financing of equipment. Offsetting these increases is \$1.5 million for the retirement of the University's capital lease obligations.

Bond Ratings

Moody's Investors Service currently provides an intrinsic rating for the System-wide revenue bonds at A1 and the Student Union Revenue Bonds at A2 (however, these bonds are insured to Aaa). Standard & Poor's currently rates the Systemwide Revenue Bonds at A+ and the Student Union Revenue Bonds at A (however, these bonds are insured to AAA).

See notes 7 through 10 of the notes to the financial statements for further information on long-term debt obligations.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Management's Discussion and Analysis (Unaudited)

June 30, 2006 and 2005

Factors Impacting Future Periods

The legislative process has approved the state general fund allocation to the California State University (CSU) for fiscal year 2006–2007. The allocation provided to the University is \$58.6 million. This increase included funds to provide for an overall compensation increase of 3.5% for permanent staff.

The Governor's compact with the CSU serves 2.5% system enrollment growth annually through 2010–2011 and adds 3.0-5.0% in general funding increases per year. The University was able to negotiate a slight increase in FTE for 2005–2006 and a greater increase in 2006/2007. This increase was necessary to accommodate the rapid growth in the region and our new academic programs.

Palomar Pomerado Health spent \$2.5 million to renovate, furnish, and equip a Nursing Education Center in the San Marcos Ambulatory Care Center building that houses the California State University San Marcos School of Nursing and the nursing skills lab. The facility will be leased to the University for \$1 per year. The program accepted 44 basic/generic Bachelor of Science and Nursing (BSN) students in the nursing program for fall 2006.

The California State University Board of Trustees approved construction of a Business Building for the University in 2003–2004 and occupancy took place in 2006. The project addresses the classroom needs of approximately 3,000 full-time equivalent students and houses the College of Business Administration and the programs of History, Literature and Writing and World Languages and Hispanic Literatures.

The University Foundation was approved for a grant of approximately \$7.7 million in the fiscal year ended June 30, 2005 to design, construct, and equip the Center for Children and Families. The approximately 18,000 square feet facility will be licensed for 152 children. These children will be selected in order from student families first, then faculty and staff families, and finally from families in the community at large. Completion is scheduled for July 2007.

Parking Services at the University is a self-supporting program established to provide parking facilities and resources. It derives no support from the state for capital outlay or operational costs. Parking fee increases are prohibited for faculty and staff unless negotiated in their collective bargaining agreements, therefore fees cannot be increased for all users in response to the cost to build and maintain parking facilities. Parking fee increases for management personnel and confidential employees and students were approved (as of January 1, 2003) and took effect for fall 2006 (increase from \$35/month to \$55/month, approximately a 57.0% increase) and for fall 2009 (from \$55/month to \$75/month, approximately a 36.5% increase).

Parking Services opened a 1,200 space surface lot in fall 2006, Although Parking Services continues to add to the current parking inventory, these interim parking lots reduce the funding available for future permanent parking lots.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

In the November 7, 2006 ballot, Proposition 1D was passed, allowing the State to sell general obligation bonds for K-12 schools and higher education. The measure included \$3.1 billion for California higher education systems including \$690.0 million to the California State University System. At the University, Proposition 1D funds would provide the funds for construction of the Social and Behavioral Sciences Building, as well as funds for nursing facility renovations and minor capital outlay projects as outlined below.

Social and Behavioral Sciences Building – 2006–2007 and 2007–2008 \$54,766,000

This project will build a new 68,000 Actual Square Feet/111,000 Gross Square Foot classroom building. The proposed facility (#31) will provide laboratories and lecture space for communications/mass media, economics, human development, liberal studies, psychology, sociology and women's studies, and political science. This facility will build capacity for 644 full time equivalent students (FTE); 461 FTE in lecture space, 51 FTE in Lower Division laboratory space, and 132 FTE in Upper Division laboratory space and 125 faculty offices including the dean's office.

Nursing Renovation – 2007–2008 \$1,704,000

This project will provide educational capacity for pre-licensure nursing students; promote in-services recertification for local hospital nursing staff; provide continuing education for nursing educators seeking to update their teaching skills; and, redesign nursing education by incorporating evolving healthcare delivery system innovations that maximize the use of clinical simulation technology in educating nurses. The project will renovate 3,600 gross square footage of an existing facility and provide a new teaching lab that will accommodate 25 FTE.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Statement of Net Assets

June 30, 2006

Assets	University	Discretely presented component units	Total
		FASB Auxiliary Organizations	
Current assets:			
Cash and cash equivalents	\$ 3,592,088	11,260,004	14,852,092
Short-term investments	17,117,098	—	17,117,098
Accounts receivable, net	2,874,155	2,225,165	5,099,320
Leases receivable, current portion	225,000	—	225,000
Pledges receivable, net	—	783,896	783,896
Prepaid expenses and other assets	2,922,016	1,344,523	4,266,539
Total current assets	<u>26,730,357</u>	<u>15,613,588</u>	<u>42,343,945</u>
Noncurrent assets:			
Restricted cash and cash equivalents	129,495	—	129,495
Accounts receivable, net	11,426,849	—	11,426,849
Leases receivable, net of current portion	25,005,000	—	25,005,000
Student loans receivable, net	280,848	—	280,848
Pledges receivable, net	—	1,247,409	1,247,409
Other long-term investments	135,256	12,306,214	12,441,470
Capital assets, net	169,471,459	25,265,098	194,736,557
Other assets	—	691,202	691,202
Total noncurrent assets	<u>206,448,907</u>	<u>39,509,923</u>	<u>245,958,830</u>
Total assets	<u>233,179,264</u>	<u>55,123,511</u>	<u>288,302,775</u>
Liabilities and Net Assets			
Current liabilities:			
Accounts payable	3,929,392	705,790	4,635,182
Accrued salaries and benefits payable	3,982,889	453,251	4,436,140
Accrued compensated absences – current portion	1,607,058	226,692	1,833,750
Deferred revenue	2,936,175	894,697	3,830,872
Capitalized lease obligations, current portion	48,000	—	48,000
Long-term debt obligations, current portion	1,283,838	225,000	1,508,838
Other liabilities	306,952	472,754	779,706
Total current liabilities	<u>14,094,304</u>	<u>2,978,184</u>	<u>17,072,488</u>
Noncurrent liabilities:			
Accrued compensated absences, net of current portion	1,669,248	—	1,669,248
Grants refundable	508,476	—	508,476
Capitalized lease obligations, net of current portion	458,000	25,793,432	26,251,432
Long-term debt obligations, net of current portion	32,272,963	—	32,272,963
Depository accounts	354,646	—	354,646
Total noncurrent liabilities	<u>35,263,333</u>	<u>25,793,432</u>	<u>61,056,765</u>
Total liabilities	<u>49,357,637</u>	<u>28,771,616</u>	<u>78,129,253</u>
Net assets:			
Invested in capital assets, net of related debt	162,692,393	(753,334)	161,939,059
Restricted for:			
Nonexpendable – endowments	—	12,342,233	12,342,233
Expendable:			
Scholarships and fellowships	157,319	98,481	255,800
Loans	53,559	—	53,559
Capital projects	8,573,476	2,787,181	11,360,657
Other	—	1,832,754	1,832,754
Unrestricted	12,344,880	10,044,580	22,389,460
Total net assets	<u>\$ 183,821,627</u>	<u>26,351,895</u>	<u>210,173,522</u>

See accompanying notes to financial statements.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Statement of Net Assets

June 30, 2005

Assets	University	Discretely presented component units	Total
		FASB Auxiliary Organizations	
Current assets:			
Cash and cash equivalents	\$ 11,547,805	2,917,666	14,465,471
Short-term investments	10,747,027	5,881,267	16,628,294
Accounts receivable, net	3,628,636	2,274,976	5,903,612
Pledges receivable, net	—	817,520	817,520
Prepaid expenses and other assets	2,315,123	349,284	2,664,407
Total current assets	<u>28,238,591</u>	<u>12,240,713</u>	<u>40,479,304</u>
Noncurrent assets:			
Restricted cash and cash equivalents	181,316	—	181,316
Accounts receivable, net	23,697,935	—	23,697,935
Leases receivable, net of current portion	25,230,000	—	25,230,000
Student loans receivable, net	373,932	—	373,932
Pledges receivable, net	—	1,402,101	1,402,101
Endowment investments	—	11,281,690	11,281,690
Other long-term investments	71,033	—	71,033
Capital assets, net	162,968,819	24,925,120	187,893,939
Other assets	—	239,489	239,489
Total noncurrent assets	<u>212,523,035</u>	<u>37,848,400</u>	<u>250,371,435</u>
Total assets	<u>240,761,626</u>	<u>50,089,113</u>	<u>290,850,739</u>
Liabilities and Net Assets			
Current liabilities:			
Accounts payable	4,326,993	704,510	5,031,503
Accrued salaries and benefits payable	4,285,475	291,890	4,577,365
Accrued compensated absences – current portion	1,608,640	87,116	1,695,756
Deferred revenue	2,636,913	712,416	3,349,329
Capitalized lease obligations, current portion	4,516	—	4,516
Long-term debt obligations, current portion	214,740	—	214,740
Other liabilities	1,081,581	1,077,357	2,158,938
Total current liabilities	<u>14,158,858</u>	<u>2,873,289</u>	<u>17,032,147</u>
Noncurrent liabilities:			
Accrued compensated absences, net of current portion	1,263,955	—	1,263,955
Grants refundable	478,180	—	478,180
Long-term debt obligations, net of current portion	32,424,322	26,047,815	58,472,137
Depository accounts	295,547	—	295,547
Total noncurrent liabilities	<u>34,462,004</u>	<u>26,047,815</u>	<u>60,509,819</u>
Total liabilities	<u>48,620,862</u>	<u>28,921,104</u>	<u>77,541,966</u>
Net assets:			
Invested in capital assets, net of related debt	156,463,965	(1,122,695)	155,341,270
Restricted for:			
Nonexpendable – endowments	—	10,876,670	10,876,670
Expendable:			
Scholarships and fellowships	98,764	95,641	194,405
Loans	53,479	—	53,479
Capital projects	20,078,277	454,261	20,532,538
Debt service	339,498	—	339,498
Other	—	2,814,751	2,814,751
Unrestricted	15,106,781	8,049,381	23,156,162
Total net assets	<u>\$ 192,140,764</u>	<u>21,168,009</u>	<u>213,308,773</u>

See accompanying notes to financial statements.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS
Statement of Revenues, Expenses, and Changes in Net Assets
Year ended June 30, 2006

	<u>University</u>	<u>Discretely presented component units FASB Auxiliary Organizations</u>	<u>Eliminations</u>	<u>Total</u>
Revenues:				
Operating revenues:				
Student tuition and fees (net of scholarship allowances of \$3,449,215)	\$ 22,867,810	1,029,902	—	23,897,712
Grants and contracts, noncapital:				
Federal	4,869,843	5,675,301	—	10,545,144
State and local	2,070,439	165,405	—	2,235,844
Nongovernmental	535,955	2,389,928	—	2,925,883
Sales and services of educational activities	—	2,442,918	—	2,442,918
Sales and services of auxiliary enterprises	2,886,925	7,712,602	—	10,599,527
Other operating revenues	790,347	487,173	—	1,277,520
Total operating revenues	<u>34,021,319</u>	<u>19,903,229</u>	<u>—</u>	<u>53,924,548</u>
Expenses:				
Operating expenses:				
Instruction	31,179,944	1,854,236	—	33,034,180
Research	670,326	4,053,463	—	4,723,789
Public service	298,406	1,385,515	—	1,683,921
Academic support	13,704,306	890,861	—	14,595,167
Student services	8,325,253	4,586,957	—	12,912,210
Institutional support	12,877,600	313,000	—	13,190,600
Operation and maintenance of plant	11,914,971	—	—	11,914,971
Student grants and scholarships	9,278,598	266,398	—	9,544,996
Auxiliary enterprise expenses	3,253,421	6,746,499	(48,602)	9,951,318
Depreciation	8,695,918	1,045,703	—	9,741,621
Total operating expenses	<u>100,198,743</u>	<u>21,142,632</u>	<u>(48,602)</u>	<u>121,292,773</u>
Operating loss	<u>(66,177,424)</u>	<u>(1,239,403)</u>	<u>48,602</u>	<u>(67,368,225)</u>
Nonoperating revenues (expenses):				
State appropriations, noncapital	54,723,975	—	—	54,723,975
Gifts, noncapital	896,369	4,801,602	—	5,697,971
Investment income, net	1,918,433	817,680	—	2,736,113
Endowment income (loss)	—	552,123	—	552,123
Interest on capital-related debt	(1,548,154)	—	—	(1,548,154)
Other nonoperating revenues (expenses), net	235,031	251,884	—	486,915
Net nonoperating revenues (expenses)	<u>56,225,654</u>	<u>6,423,289</u>	<u>—</u>	<u>62,648,943</u>
Income (loss) before other additions	<u>(9,951,770)</u>	<u>5,183,886</u>	<u>48,602</u>	<u>(4,719,282)</u>
State appropriations, capital	767,000	—	—	767,000
Grants and gifts, capital	865,633	—	(48,602)	817,031
Increase in net assets	<u>(8,319,137)</u>	<u>5,183,886</u>	<u>—</u>	<u>(3,135,251)</u>
Net assets:				
Net assets at beginning of year	<u>192,140,764</u>	<u>21,168,009</u>	<u>—</u>	<u>213,308,773</u>
Net assets at end of year	<u>\$ 183,821,627</u>	<u>26,351,895</u>	<u>—</u>	<u>210,173,522</u>

See accompanying notes to financial statements.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS
Statement of Revenues, Expenses, and Changes in Net Assets
Year ended June 30, 2005

	<u>University</u>	<u>Discretely presented component units FASB Auxiliary Organizations</u>	<u>Eliminations</u>	<u>Total</u>
Revenues:				
Operating revenues:				
Student tuition and fees (net of scholarship allowances of \$2,935,913)	\$ 19,944,432	974,275	—	20,918,707
Grants and contracts, noncapital:				
Federal	5,473,044	5,178,647	—	10,651,691
State and local	2,177,642	525,137	—	2,702,779
Nongovernmental	—	309,952	—	309,952
Sales and services of educational activities	—	2,824,694	—	2,824,694
Sales and services of auxiliary enterprises	2,791,347	4,890,403	—	7,681,750
Other operating revenues	177,575	406,204	—	583,779
Total operating revenues	<u>30,564,040</u>	<u>15,109,312</u>	<u>—</u>	<u>45,673,352</u>
Expenses:				
Operating expenses:				
Instruction	27,464,138	2,411,499	—	29,875,637
Research	526,419	2,966,371	—	3,492,790
Public service	27,121	2,137,767	—	2,164,888
Academic support	12,489,035	364,305	—	12,853,340
Student services	7,486,856	1,534,281	—	9,021,137
Institutional support	14,978,589	283,003	—	15,261,592
Operation and maintenance of plant	6,876,488	—	—	6,876,488
Student grants and scholarships	6,489,624	519,821	—	7,009,445
Auxiliary enterprise expenses	4,027,286	6,111,725	—	10,139,011
Depreciation	7,340,268	1,850,187	—	9,190,455
Total operating expenses	<u>87,705,824</u>	<u>18,178,959</u>	<u>—</u>	<u>105,884,783</u>
Operating loss	<u>(57,141,784)</u>	<u>(3,069,647)</u>	<u>—</u>	<u>(60,211,431)</u>
Nonoperating revenues (expenses):				
State appropriations, noncapital	53,307,764	—	—	53,307,764
Gifts, noncapital	860,259	3,097,602	—	3,957,861
Investment income, net	354,716	393,933	—	748,649
Endowment income	—	909,650	—	909,650
Interest on capital-related debt	(726,360)	—	—	(726,360)
Other nonoperating revenues (expenses), net	1,801,917	(586,148)	—	1,215,769
Net nonoperating revenues (expenses)	<u>55,598,296</u>	<u>3,815,037</u>	<u>—</u>	<u>59,413,333</u>
Income (loss) before other additions	<u>(1,543,488)</u>	<u>745,390</u>	<u>—</u>	<u>(798,098)</u>
State appropriations, capital	10,002,000	—	—	10,002,000
Grants and gifts, capital	—	2,300	—	2,300
Increase in net assets	<u>8,458,512</u>	<u>747,690</u>	<u>—</u>	<u>9,206,202</u>
Net assets:				
Net assets at beginning of year	<u>183,682,252</u>	<u>20,420,319</u>	<u>—</u>	<u>204,102,571</u>
Net assets at end of year	<u>\$ 192,140,764</u>	<u>21,168,009</u>	<u>—</u>	<u>213,308,773</u>

See accompanying notes to financial statements.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Statements of Cash Flows

Years ended June 30, 2006 and 2005

	University	
	2006	2005
Cash flows from operating activities:		
Student tuition and fees	\$ 23,147,796	16,577,599
Federal grants and contracts	5,033,907	5,500,044
State and local grants and contracts	2,070,439	2,177,642
Nongovernmental grants and contracts	535,955	—
Payments to suppliers	(22,145,106)	(14,195,820)
Payments to employees	(62,782,139)	(59,040,079)
Payments to students	(9,388,901)	(6,727,640)
Collections of student loans	203,387	188,386
Sales and services of educational activities	2,886,925	2,791,347
Other receipts	399,964	266,244
	<hr/>	<hr/>
Net cash used in operating activities	(60,037,773)	(52,462,277)
	<hr/>	<hr/>
Cash flows from noncapital financing activities:		
State appropriations	55,963,390	52,156,881
Gifts and grants received for other-than-capital purposes	896,369	860,259
Federal loan program receipts	16,408,731	16,046,234
Federal loan program disbursements	(16,314,908)	(16,096,406)
Monies received on behalf of others	62,575	288,029
Monies disbursed on behalf of others	(65,137)	(290,428)
Other	1,090,773	3,202,090
	<hr/>	<hr/>
Net cash provided by noncapital financing activities	58,041,793	56,166,659
	<hr/>	<hr/>
Cash flows from capital and related financing activities:		
Proceeds from capital debt	506,000	51,205,000
State appropriations	13,038,086	16,005,798
Capital grants and gifts	429,774	—
Acquisition of capital assets	(13,432,633)	(16,991,769)
Transfers to escrow agent	—	(25,975,000)
Principal paid on capital debt and leases	(231,787)	(1,691,762)
Interest paid on capital debt and leases	(1,602,118)	(470,533)
Repayment of auxiliary organization debt	—	(25,975,000)
	<hr/>	<hr/>
Net cash used in capital and related financing activities	(1,292,678)	(3,893,266)
	<hr/>	<hr/>
Cash flows from investing activities:		
Proceeds from sales and maturities of investments	2,722,702	3,776,176
Purchases of investments	(9,156,998)	(1,960,103)
Investment income received	1,715,416	354,716
	<hr/>	<hr/>
Net cash provided by (used in) investing activities	(4,718,880)	2,170,789
	<hr/>	<hr/>
Net increase (decrease) in cash and cash equivalents	(8,007,538)	1,981,905
	<hr/>	<hr/>
Cash and cash equivalents at beginning of year	11,729,121	9,747,216
	<hr/>	<hr/>
Cash and cash equivalents at end of year	\$ 3,721,583	11,729,121
	<hr/>	<hr/>
Summary of cash and cash equivalents at end of year:		
Cash and cash equivalents	\$ 3,592,088	11,547,805
Restricted cash and investments	129,495	181,316
	<hr/>	<hr/>
Total cash and cash equivalents at end of year	\$ 3,721,583	11,729,121
	<hr/>	<hr/>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Statements of Cash Flows

Years ended June 30, 2006 and 2005

	University	
	2006	2005
Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	\$ (66,177,424)	(57,141,784)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation	8,695,918	7,340,268
Change in assets and liabilities:		
Accounts receivable, net	(373,179)	(10,443)
Student loans receivable, net	93,083	(49,630)
Prepaid expenses and other assets	(606,893)	2,010,211
Accounts payable	(1,476,584)	(900,134)
Accrued salaries and benefits	(302,586)	(106,913)
Accrued compensated absences	403,712	(127,524)
Deferred revenue	299,262	(3,369,030)
Depository accounts	59,099	69,609
Other liabilities	(652,181)	(176,907)
Net cash used in operating activities	\$ (60,037,773)	(52,462,277)
Supplemental schedule of noncash transactions:		
Contributed capital assets	\$ 435,859	—
Construction work in progress acquired from the Office of the Chancellor	338,454	432,897
Accrued capital asset costs (purchased but unpaid at year end)	1,078,984	3,493,646
Operating expenses financed through issuance of long-term debt	1,777,885	—

See accompanying notes to financial statements.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

(1) Organization

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

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

(2) Summary of Significant Accounting Policies

(a) *Financial Reporting Entity*

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

The discretely presented auxiliary organizations are as follows:

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

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

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

<u>June 30, 2006</u>	<u>California State University, San Marcos Foundation</u>	<u>Associated Students, Inc. of California State University San Marcos</u>	<u>San Marcos University Corporation</u>	<u>Total</u>
Current assets	\$ 12,790,108	641,853	2,181,627	15,613,588
Capital assets, net	2,408,096	30,538	22,826,464	25,265,098
Other noncurrent assets	14,241,825	3,000	—	14,244,825
Total assets	<u>29,440,029</u>	<u>675,391</u>	<u>25,008,091</u>	<u>55,123,511</u>
Current liabilities	1,836,804	255,247	886,133	2,978,184
Noncurrent liabilities	—	—	25,793,432	25,793,432
Total liabilities	<u>1,836,804</u>	<u>255,247</u>	<u>26,679,565</u>	<u>28,771,616</u>
Invested in capital assets, net of related debt	2,408,096	30,538	(3,191,968)	(753,334)
Restricted	17,060,649	—	—	17,060,649
Unrestricted	8,134,480	389,606	1,520,494	10,044,580
Total net assets (deficit)	\$ <u>27,603,225</u>	<u>420,144</u>	<u>(1,671,474)</u>	<u>26,351,895</u>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

<u>June 30, 2006</u>	<u>California State University, San Marcos Foundation</u>	<u>Associated Students, Inc. of California State University San Marcos</u>	<u>San Marcos University Corporation</u>	<u>Total</u>
Operating revenues:				
Student tuition and fees	\$ —	1,029,902	—	1,029,902
Grants and contracts, noncapital	8,219,822	10,812	—	8,230,634
Sales and services of education activities	2,442,918	—	—	2,442,918
Sales and services of auxiliary enterprises, net	4,700,057	—	3,012,545	7,712,602
Other	—	264,032	223,141	487,173
	<u>15,362,797</u>	<u>1,304,746</u>	<u>3,235,686</u>	<u>19,903,229</u>
Total operating revenues				
Operating expenses:				
Instruction	1,854,236	—	—	1,854,236
Research	4,053,463	—	—	4,053,463
Public service	1,385,515	—	—	1,385,515
Academic support	890,861	—	—	890,861
Student services	4,423,182	163,775	—	4,586,957
Institutional support	313,000	—	—	313,000
Student grants and scholarships	266,398	—	—	266,398
Auxiliary enterprise expenses	2,764,083	1,011,322	2,971,094	6,746,499
Depreciation	327,731	12,666	705,306	1,045,703
	<u>16,278,469</u>	<u>1,187,763</u>	<u>3,676,400</u>	<u>21,142,632</u>
Total operating expenses				
Operating income (loss)	(915,672)	116,983	(440,714)	(1,239,403)
Net nonoperating revenues	<u>6,418,027</u>	<u>5,262</u>	<u>—</u>	<u>6,423,289</u>
Increase (decrease) in net assets				
	5,502,355	122,245	(440,714)	5,183,886
Net assets (deficit) at beginning of year	<u>22,100,870</u>	<u>297,899</u>	<u>(1,230,760)</u>	<u>21,168,009</u>
Net assets (deficit) at end of year	<u>\$ 27,603,225</u>	<u>420,144</u>	<u>(1,671,474)</u>	<u>26,351,895</u>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

<u>June 30, 2005</u>	<u>California State University, San Marcos Foundation</u>	<u>Associated Students, Inc. of California State University San Marcos</u>	<u>San Marcos University Corporation</u>	<u>Total</u>
Current assets	\$ 8,939,760	512,336	2,788,617	12,240,713
Capital assets, net	1,470,841	33,614	23,420,665	24,925,120
Other noncurrent assets	<u>12,920,280</u>	<u>3,000</u>	<u>—</u>	<u>12,923,280</u>
Total assets	<u>23,330,881</u>	<u>548,950</u>	<u>26,209,282</u>	<u>50,089,113</u>
Current liabilities	1,230,011	251,051	1,392,227	2,873,289
Noncurrent liabilities	<u>—</u>	<u>—</u>	<u>26,047,815</u>	<u>26,047,815</u>
Total liabilities	<u>1,230,011</u>	<u>251,051</u>	<u>27,440,042</u>	<u>28,921,104</u>
Invested in capital assets, net of related debt	1,470,841	33,614	(2,627,150)	(1,122,695)
Restricted	14,241,323	—	—	14,241,323
Unrestricted	<u>6,388,706</u>	<u>264,285</u>	<u>1,396,390</u>	<u>8,049,381</u>
Total net assets (deficit)	\$ <u><u>22,100,870</u></u>	<u><u>297,899</u></u>	<u><u>(1,230,760)</u></u>	<u><u>21,168,009</u></u>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

<u>June 30, 2005</u>	<u>California State University, San Marcos Foundation</u>	<u>Associated Students, Inc. of California State University San Marcos</u>	<u>San Marcos University Corporation</u>	<u>Total</u>
Operating revenues:				
Student tuition and fees	\$ —	974,275	—	974,275
Grants and contracts, noncapital	6,003,768	9,968	—	6,013,736
Sales and services of education activities	2,824,694	—	—	2,824,694
Sales and services of auxiliary enterprises, net	1,481,013	—	3,409,390	4,890,403
Other	—	194,792	211,412	406,204
	<u>10,309,475</u>	<u>1,179,035</u>	<u>3,620,802</u>	<u>15,109,312</u>
Total operating revenues				
Operating expenses:				
Instruction	2,411,499	—	—	2,411,499
Research	2,966,371	—	—	2,966,371
Public service	2,137,767	—	—	2,137,767
Academic support	364,305	—	—	364,305
Student services	1,326,028	208,253	—	1,534,281
Institutional support	283,003	—	—	283,003
Student grants and scholarships	519,821	—	—	519,821
Auxiliary enterprise expenses	2,081,558	850,450	3,179,717	6,111,725
Depreciation	255,927	16,155	1,578,105	1,850,187
	<u>12,346,279</u>	<u>1,074,858</u>	<u>4,757,822</u>	<u>18,178,959</u>
Total operating expenses				
Operating income (loss)	(2,036,804)	104,177	(1,137,020)	(3,069,647)
Net nonoperating revenues	<u>3,810,088</u>	<u>4,949</u>	<u>—</u>	<u>3,815,037</u>
Income (loss) before other additions	1,773,284	109,126	(1,137,020)	745,390
Grants and gifts, capital	<u>2,300</u>	<u>—</u>	<u>—</u>	<u>2,300</u>
Increase (decrease) in net assets	1,775,584	109,126	(1,137,020)	747,690
Net assets (deficit) at beginning of year	<u>20,325,286</u>	<u>188,773</u>	<u>(93,740)</u>	<u>20,420,319</u>
Net assets (deficit) at end of year	\$ <u><u>22,100,870</u></u>	<u><u>297,899</u></u>	<u><u>(1,230,760)</u></u>	<u><u>21,168,009</u></u>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

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

The financial statements present only the statements of net assets, statements of revenues, expenses, and changes in net assets, and statements of cash flows of the University and do not purport to, and do not, present fairly the financial position of the System as of June 30, 2006 and 2005, and the changes in its financial position and its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

(b) *Basis of Presentation*

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

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

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

(c) *Election of Applicable FASB Statements*

The University has elected not to adopt the pronouncements issued by the FASB after November 30, 1989.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

(d) *Classification of Current and Noncurrent Assets and Liabilities*

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

(e) *Cash and Cash Equivalents*

The University considers all highly liquid investments with an original maturity date of three months or less to be cash and cash equivalents.

(f) *Investments*

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

(g) *Capital Assets*

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

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

(h) *Deferred Revenue*

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

(i) *Compensated Absences*

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

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

(j) **Grants Refundable**

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

(k) **Net Assets**

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

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

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

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

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

The University has adopted a policy of generally utilizing restricted – expendable funds, prior to unrestricted funds, when an expense is incurred for purposes for which both are available.

(l) **Classification of Revenues and Expenses**

The University considers operating revenues and expenses in the statements of revenues, expenses, and changes in net assets to be those revenues and expenses that result from exchange transactions or from other activities that are connected directly to the University's primary functions. Exchange transactions include charges for services rendered and the acquisition of goods and services. Certain other transactions are reported as nonoperating revenues and expenses or capital contributions in accordance with GASB Statement No. 35. These nonoperating activities include the University's operating and capital appropriations from the State of California, net investment income, gifts, and interest expense.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

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

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

(m) *Income Taxes*

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

(n) *Eliminations*

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

(o) *Use of Estimates*

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts in the accompanying financial statements. Actual results could differ from those estimates.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

(3) Cash and Cash Equivalents and Investments

The University's cash and cash equivalents and investments as of June 30, 2006 and 2005 are classified in the accompanying financial statements as follows:

	June 30	
	2006	2005
Cash and cash equivalents	\$ 3,592,088	11,547,805
Restricted cash and cash equivalents	129,495	181,316
Total cash and cash equivalents	<u>3,721,583</u>	<u>11,729,121</u>
Short-term investments	17,117,098	10,747,027
Other long-term investments	135,256	71,033
Total investments	<u>17,252,354</u>	<u>10,818,060</u>
Total cash and cash equivalents and investments	<u>\$ 20,973,937</u>	<u>22,547,181</u>

(a) Cash and Cash Equivalents

At June 30, 2006 and 2005, cash and cash equivalents consisted of demand deposits held at the State Treasury and petty cash. Total cash and cash equivalents of \$3,721,583 and \$11,729,121 had a corresponding carrying value balance with the State Treasury of \$4,467,176 and \$12,948,101 at June 30, 2006 and 2005, respectively. The differences related primarily to deposits in transit and outstanding checks.

(b) Investments

At June 30, 2006 and 2005, the University's investment portfolio consisted primarily of investments held in the California State University Investment Pool, an internal investment pool, as well as interest-bearing accounts held in the State Treasury. For the California State University Investment Pool, separate accounting is maintained as to the amounts allocable to the various funds and programs.

Investment Policy

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

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways that the University manages its exposure to interest rate risk is by purchasing a combination of short-term and mid-term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or nearing maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations. The University monitors the interest rate risk inherent in its portfolio by measuring the weighted average maturity of its portfolio. The weighted average maturity of the University's investment portfolio for each investment type as of June 30, 2006 is presented in the table below.

Credit Risk

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

The following table presents the fair value, weighted average maturity, and actual rating by investment type of the University's investment portfolio as of June 30, 2006:

Investment type	Fair value	Weighted average maturity (in years)	Rating as of year end			
			AAA	Aa	A	Not rated
Money market mutual funds	\$ 318,565	0.01	\$ —	—	—	318,565
Certificates of deposit	2,719,702	1.41	—	1,019,797	1,699,905	—
Commercial paper	1,109,456	0.01	—	—	—	1,109,456
U.S. agency securities	2,334,554	0.50	2,334,554	—	—	—
Mortgage-backed securities	589,650	10.57	589,650	—	—	—
Corporate and fixed-income securities	5,886,657	1.74	316,485	1,649,143	3,921,029	—
State of California Surplus Money Investment Fund	3,531,401	0.42	—	—	—	3,531,401
High rate money market	158,009	0.01	—	—	—	158,009
Total	16,647,994		\$ 3,240,689	2,668,940	5,620,934	5,117,431
Not subject to ratings:						
U.S. Treasury securities	604,360	1.85				
Total investments	\$ 17,252,354					

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

The following table presents the fair value, weighted average maturity, and actual rating by investment type of the University's investment portfolio as of June 30, 2005:

Investment type	Fair value	Weighted average maturity (in years)	Rating as of year end			
			AAA	Aa	A	Not rated
Money market mutual funds	\$ 454,768	0.00	\$ 135,052	—	—	319,716
Certificates of deposit	239,352	0.80	—	63,804	175,548	—
U.S. agency securities	3,646,127	1.66	3,646,127	—	—	—
Mortgage-backed securities	494,660	12.13	494,660	—	—	—
Corporate and fixed income securities	2,577,022	2.09	221,985	321,380	2,033,657	—
State of California Surplus Money Investment Fund	2,746,857	0.42	—	—	—	2,746,857
High rate money market	92,808	0.01	—	—	—	92,808
Total	10,251,594		\$ 4,497,824	385,184	2,209,205	3,159,381
Not subject to ratings:						
U.S. Treasury securities	566,466	2.46				
Total investments	\$ 10,818,060					

Concentration of Credit Risk

The University's investment policy contains no limitations on the amount that can be invested in any one issuer beyond that stipulated by the California Government Code. As of June 30, 2006, the following investment (other than U.S. Treasury securities, mutual funds, and external investment pools) represented 5% or more of the University's investment portfolio: Federal Home Loan Bank, \$1,385,632.

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

(4) Accounts Receivable

Accounts receivable at June 30 consisted of the following:

	2006		
	Current	Noncurrent	Total
State appropriations	\$ 1,600,746	11,426,849	13,027,595
Auxiliary organizations	628,876	—	628,876
Student accounts	243,278	—	243,278
Government grants and contracts	38,775	—	38,775
Other	599,820	—	599,820
	<u>3,111,495</u>	<u>11,426,849</u>	<u>14,538,344</u>
Less allowance for doubtful accounts	(237,340)	—	(237,340)
Total	\$ 2,874,155	11,426,849	14,301,004

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

	2005		
	<u>Current</u>	<u>Noncurrent</u>	<u>Total</u>
State appropriations	\$ 2,840,161	23,697,935	26,538,096
Auxiliary organizations	141,260	—	141,260
Student accounts	155,337	—	155,337
Government grants and contracts	111,408	—	111,408
Other	540,296	—	540,296
	<u>3,788,462</u>	<u>23,697,935</u>	<u>27,486,397</u>
Less allowance for doubtful accounts	<u>(159,826)</u>	<u>—</u>	<u>(159,826)</u>
Total	\$ <u>3,628,636</u>	<u>23,697,935</u>	<u>27,326,571</u>

(5) Lease Receivable

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

Lease payments are due to the University as follows:

Fiscal year ending:	
2007	\$ 225,000
2008	275,000
2009	330,000
2010	385,000
2011	450,000
Thereafter	<u>23,565,000</u>
Total lease receivable	25,230,000
Less current portion	<u>225,000</u>
Long-term lease receivable, net of current portion	\$ <u>25,005,000</u>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

(6) Capital Assets

Capital assets activity for the year ended June 30, 2006 consisted of the following:

	<u>Balance, June 30, 2005</u>	<u>Additions</u>	<u>Retirements</u>	<u>Transfers</u>	<u>Balance, June 30, 2006</u>
Nondepreciable capital assets:					
Land and land improvements	\$ 10,981,328	—	—	—	10,981,328
Works of art and historical treasures	25,000	—	—	—	25,000
Construction work in progress	<u>21,096,085</u>	<u>10,756,000</u>	<u>—</u>	<u>(25,304,711)</u>	<u>6,547,374</u>
Total nondepreciable capital assets	<u>32,102,413</u>	<u>10,756,000</u>	<u>—</u>	<u>(25,304,711)</u>	<u>17,553,702</u>
Depreciable capital assets:					
Buildings and building improvements	139,050,766	191,222	—	23,847,376	163,089,364
Improvements, other than buildings	13,448,359	—	—	477,628	13,925,987
Infrastructure	20,233,216	—	—	979,707	21,212,923
Personal property:					
Equipment	11,572,218	2,839,676	(1,351,255)	62,602	13,123,241
Library books and materials	9,389,232	674,932	(95,128)	—	9,969,036
Intangible assets	<u>961,977</u>	<u>824,100</u>	<u>—</u>	<u>—</u>	<u>1,786,077</u>
Total depreciable capital assets	<u>194,655,768</u>	<u>4,529,930</u>	<u>(1,446,383)</u>	<u>25,367,313</u>	<u>223,106,628</u>
Total cost	<u>226,758,181</u>	<u>15,285,930</u>	<u>(1,446,383)</u>	<u>62,602</u>	<u>240,660,330</u>
Less accumulated depreciation:					
Buildings and building improvements	(30,846,866)	(5,137,985)	—	—	(35,984,851)
Improvements, other than buildings	(10,522,486)	(557,220)	—	—	(11,079,706)
Infrastructure	(6,461,233)	(842,246)	—	—	(7,303,479)
Personal property:					
Equipment	(8,328,556)	(1,541,830)	1,263,883	(62,602)	(8,669,105)
Library books and materials	(6,770,372)	(491,831)	95,128	—	(7,167,075)
Intangible assets	<u>(859,849)</u>	<u>(124,806)</u>	<u>—</u>	<u>—</u>	<u>(984,655)</u>
Total accumulated depreciation	<u>(63,789,362)</u>	<u>(8,695,918)</u>	<u>1,359,011</u>	<u>(62,602)</u>	<u>(71,188,871)</u>
Net capital assets	\$ <u><u>162,968,819</u></u>	<u><u>6,590,012</u></u>	<u><u>(87,372)</u></u>	<u><u>—</u></u>	<u><u>169,471,459</u></u>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

Capital assets activity for the year ended June 30, 2005 consisted of the following:

	Balance, June 30, 2004	Additions	Retirements	Transfers	Balance, June 30, 2005
Nondepreciable capital assets:					
Land and land improvements	\$ 10,981,328	—	—	—	10,981,328
Works of art and historical treasures	25,000	—	—	—	25,000
Construction work in progress	1,877,793	20,166,973	—	(948,681)	21,096,085
Total nondepreciable capital assets	<u>12,884,121</u>	<u>20,166,973</u>	<u>—</u>	<u>(948,681)</u>	<u>32,102,413</u>
Depreciable capital assets:					
Buildings and building improvements	138,732,654	214,112	—	104,000	139,050,766
Improvements, other than buildings	12,603,678	—	—	844,681	13,448,359
Infrastructure	20,233,216	—	—	—	20,233,216
Personal property:					
Equipment	11,881,672	198,962	(508,416)	—	11,572,218
Library books and materials	9,134,641	254,591	—	—	9,389,232
Intangible assets	878,303	83,674	—	—	961,977
Total depreciable capital assets	<u>193,464,164</u>	<u>751,339</u>	<u>(508,416)</u>	<u>948,681</u>	<u>194,655,768</u>
Total cost	<u>206,348,285</u>	<u>20,918,312</u>	<u>(508,416)</u>	<u>—</u>	<u>226,758,181</u>
Less accumulated depreciation:					
Buildings and building improvements	(26,086,311)	(4,627,163)	—	—	(30,713,474)
Improvements, other than buildings	(10,018,174)	(504,312)	—	—	(10,522,486)
Infrastructure	(5,955,403)	(505,830)	—	—	(6,461,233)
Personal property:					
Equipment	(7,621,320)	(1,169,698)	329,070	—	(8,461,948)
Library books and materials	(6,295,761)	(474,611)	—	—	(6,770,372)
Intangible assets	(801,195)	(58,654)	—	—	(859,849)
Total accumulated depreciation	<u>(56,778,164)</u>	<u>(7,340,268)</u>	<u>329,070</u>	<u>—</u>	<u>(63,789,362)</u>
Net capital assets	\$ <u>149,570,121</u>	<u>13,578,044</u>	<u>(179,346)</u>	<u>—</u>	<u>162,968,819</u>

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

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

(7) Lease Obligations

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

Capital leases consist primarily of leases of certain facilities and office equipment. Total capital assets related to capital leases had a carrying value of \$715,529 and \$978,668 at June 30, 2006 and 2005, respectively. Substantially all of these assets are pledged as security for the related leases. The leases bear interest at rates 4.4% and have terms expiring in various years through 2013.

Operating leases consist primarily of leases for the use of real property and have terms expiring in various years through fiscal year 2012. The leases can be canceled if the state does not provide adequate funding.

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

	<u>Capital leases</u>	<u>Operating leases</u>
Year ending June 30:		
2007	\$ 64,124	352,410
2008	84,148	360,722
2009	84,171	372,303
2010	84,146	384,290
2011	84,956	366,876
2012 – 2016	<u>188,976</u>	<u>379,717</u>
Total future minimum lease payments	590,521	\$ <u><u>2,216,318</u></u>
Less amount representing interest	<u>(84,521)</u>	
Present value of future minimum lease payments	\$ <u><u>506,000</u></u>	

Rent expense under operating leases for the years ended June 30, 2006 and 2005 totaled \$639,510 and \$648,479, respectively.

Lease financing is provided to the System for the construction of various system and campus facilities through its participation with the State of California in the State Public Works Board Lease Revenue Bond Program. Certain capital assets recorded by the University may have been financed under these arrangements. However, since the obligation for the repayment of this financing rests with the System and the proceeds of such financing are not readily identifiable with a campus or project, a substantial portion of such financing is not allocated to the individual campuses of the System. Unallocated Lease Revenue Bonds outstanding for the System as of June 30, 2006 and 2005 totaled \$554,748,000 and \$546,127,000, respectively.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

(8) Long-Term Debt Obligations

(a) *General Obligation Bond Program*

The General Obligation Bond program of the State of California has provided capital outlay funds for the three segments of California Higher Education through voter-approved bonds. Each of the approved bond programs provides a pool of available funds which is allocated on a project-by-project basis among the University of California, the System, and the Community Colleges. Financing provided to the University through State of California General Obligation Bonds is not allocated to the System by the State of California. This debt remains the obligation of the state and is funded by state tax revenues. Accordingly, such debt is not reflected in the accompanying financial statements. Total General Obligation Bond debt carried by the state related to System projects is approximately \$1,277,682,000 and \$534,097,000 as of June 30, 2006 and 2005, respectively.

(b) *Revenue Bond Programs*

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

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

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

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

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

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

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

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

The Systemwide Revenue Bond program, formerly the Housing Revenue Bond program, was approved by the Trustees in fiscal year 2003. This program provides funding for various construction projects, including student residence and dining halls facilities, continuing education buildings, student unions, parking facilities, health facilities, and auxiliary organization facilities at designated campuses within the System as specified by the individual bond documents. It is designed to provide lower-cost debt and greater flexibility to finance revenue bond projects of the System. Rather than relying on specific pledged revenues to support specific debt obligations, this program pools several sources of revenue as the pledge for the related revenue-producing projects. The System's total outstanding balance of revenue bond indebtedness under the Systemwide Revenue Bond program was \$1,982,433,000 and \$1,510,223,000 at June 30, 2006 and 2005, respectively. The University's portion of the total outstanding balance under this program was \$30,625,000 and \$30,715,000 at June 30, 2006 and 2005, respectively.

Senior to the Systemwide Revenue Bonds are the Student Union Revenue Bonds Series A, B, and C. At June 30, 2006 and 2005, the System's outstanding balance for these senior bonds totaled \$70,820,000 and \$145,545,000, respectively. The University had no outstanding balances for these senior bonds.

(c) ***Revenue Bond Anticipation Notes***

The Revenue Bond Anticipation Notes are issued for a one- to three-year period in anticipation of issuing permanent revenue bonds at a future date. As of June 30, 2006 and 2005, these Revenue Bond Anticipation Notes were converted to Systemwide Revenue Bonds; therefore, the University has no Revenue Bond Anticipation Notes outstanding at June 30, 2006 and 2005, respectively.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

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

Description	Interest rate	Fiscal year maturity date	Original issue amount	Amount outstanding at June 30	
				2006	2005
Systemwide Revenue Bonds:					
2002A – Student Union	3.0% – 5.5%	2033	\$ 5,655,000	5,395,000	5,485,000
2005A – Auxiliary Org	2.5% – 5.0%	2038	25,230,000	25,230,000	25,230,000
Other:					
Koch Financial Corporation	5.0%	2012	2,000,000	878,067	1,015,338
Koch Financial Corporation	4.0%	2010	495,936	395,762	495,936
Koch Financial Corporation	4.0%	2006	1,018,281	338,059	342,401
Koch Financial Corporation	4.0%	2007	1,427,885	936,905	
GE Capital	4.0%	2008	129,646	33,008	70,387
CSUSM Foundation/SBRI Loan	6.0%	2011	350,000	350,000	—
Total long-term debt				33,556,801	32,639,062
Less current portion				(1,283,838)	(214,740)
Long-term debt, net of current portion				\$ 32,272,963	32,424,322

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

	Principal	Interest
Year ending June 30:		
2007	\$ 1,283,838	1,580,427
2008	1,149,430	1,572,155
2009	752,902	1,518,892
2010	825,093	1,487,731
2011	799,253	1,450,567
2012 – 2016	4,241,285	6,670,984
2017 – 2021	5,190,000	5,509,388
2022 – 2026	6,690,000	4,028,062
2027 – 2031	8,560,000	2,129,413
2032 – 2036	4,065,000	205,625
	\$ 33,556,801	26,153,244

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

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

(d) Koch Financial Corporation

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

(e) CSUSM Foundation SBRI Loan

During the current year, the University entered into an agreement with the California State University San Marcos Foundation to guarantee a loan for the Social and Behavioral Research Institute (SBRI). Since it has been determined that SBRI's financial viability will continue to be negatively affected by a changing survey industry environment, the University decided to close it and SBRI will cease operations as of July 1, 2007. Therefore the University will be paying the original loan amount of \$350,000 in five equal installments beginning in the fiscal year ended June 30, 2007.

(9) Advance Refundings

Prior-Years' Refundings

In prior years, the University defeased certain bonds of the discretely presented auxiliary organizations (refunded bonds) by placing the proceeds from the issuance of the Systemwide Revenue Bonds Series 2005A refunding bonds in an irrevocable trust with the State Treasurer to provide for all future debt service payments on the refunded bonds. The proceeds from the refunding bonds were used to purchase U.S. government securities that were placed in the trust fund. The investments and fixed earnings from the investments are considered sufficient to fully service the defeased debt until the debt is called or matures. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the University's financial statements. The amount of prior years' defeased bonds outstanding as of June 30, 2006 totaled \$25,230,000.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

(10) Long-term Liabilities Activity

Long-term liabilities activity for the year ended June 30, 2006 was as follows:

	<u>Beginning balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending balance</u>	<u>Current portion</u>
Accrued compensated absences	\$ 2,872,595	2,012,351	(1,608,640)	3,276,306	1,607,058
Capitalized lease obligations	4,516	506,000	(4,516)	506,000	48,000
Long-term debt obligations:					
2002A System-wide revenue bonds (Student Union)	5,485,000	—	(90,000)	5,395,000	95,000
2005A System-wide revenue bonds (Auxiliary org)	25,230,000	—	—	25,230,000	225,000
Koch Financial Corporation	1,015,338	—	(137,271)	878,067	—
Koch Financial Corporation	495,936	—	(100,174)	395,762	84,584
Koch Financial Corporation	342,401	—	(4,341)	338,060	338,060
Koch Financial Corporation	—	1,427,885	(490,980)	936,905	459,763
GE Capital	70,387	—	(37,380)	33,007	19,342
CSUSM Foundation SBRI Loan	—	350,000	—	350,000	62,089
Total long-term debt obligations	<u>32,639,062</u>	<u>1,777,885</u>	<u>(860,146)</u>	<u>33,556,801</u>	<u>1,283,838</u>
Total long-term liabilities \$	<u>35,516,173</u>	<u>4,296,236</u>	<u>(2,473,302)</u>	<u>37,339,107</u>	<u>2,938,896</u>

Long-term liabilities activity for the year ended June 30, 2005 was as follows:

	<u>Beginning balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending balance</u>	<u>Current portion</u>
Accrued compensated absences	\$ 3,000,119	1,399,220	(1,526,744)	2,872,595	1,608,640
Capitalized lease obligations	1,484,068	—	(1,479,552)	4,516	4,516
Long-term debt obligations:					
2002A System-wide revenue bonds (Student Union)	5,580,000	—	(95,000)	5,485,000	90,000
2005A System-wide revenue bonds (Auxiliary org)	—	25,230,000	—	25,230,000	—
Bond Anticipation Note (Auxiliary org)	—	25,975,000	(25,975,000)	—	—
Koch Financial Corporation	1,132,548	—	(117,210)	1,015,338	—
Koch Financial Corporation	—	495,936	—	495,936	87,361
Koch Financial Corporation	—	1,018,282	(675,881)	342,401	—
GE Capital	—	106,387	(36,000)	70,387	37,379
Total long-term debt obligations	<u>6,712,548</u>	<u>52,825,605</u>	<u>(26,899,091)</u>	<u>32,639,062</u>	<u>214,740</u>
Total long-term liabilities \$	<u>11,196,735</u>	<u>54,224,825</u>	<u>(29,905,387)</u>	<u>35,516,173</u>	<u>1,827,896</u>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

(11) Pension Plan and Postretirement Benefits

(a) Plan Description

The University, as an agency of the State of California, contributes to the California Public Employees' Retirement System (CalPERS). The state's plan with CalPERS is an agent multiple-employer defined benefit pension plan. For the University, the plan acts as a cost-sharing multiple-employer defined benefit pension plan, which provides a defined benefit pension and postretirement benefit program for substantially all eligible University employees. CalPERS functions as an investment and administrative agent for its members. The plan also provides survivor, death, and disability benefits. Eligible employees are covered by the Public Employees' Medical and Hospital Care Act (PEMHCA) for medical benefits.

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

(b) Funding Policy

University personnel are required to contribute 5.0% of their monthly earnings in excess of \$513 to CalPERS. The University is required to contribute at an actuarially determined rate; the current rate is approximately 15.942% of annual covered payroll. The contribution requirements of the plan members are established and may be amended by CalPERS.

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

2004	\$	5,886,722
2005		6,522,662
2006		6,615,415

(c) Faculty Early Retirement Program

During fiscal year 2004, the System implemented the Faculty Early Retirement Program, which was authorized by Executive Order S-8-04 issued by the Governor on May 6, 2004. In order to enroll in the program, participants must meet the CalPERS retirement eligibility requirements of age 50 or more on the date of retirement and have five years or more of service credit. Eligible employees who elect to participate in this program will receive two additional years of service credit in their retirement income calculation if their (1) separation date is no earlier than May 5, 2004, and no later than July 27, 2004, and (2) CalPERS retirement date is no earlier than May 6, 2004, and no later than July 28, 2004. In return, the System must contribute to CalPERS an amount representing the actuarial equivalent of the value of this benefit. The early retirement benefit is not dependent upon future services and, therefore, is already earned as of June 30, 2004 by those who have elected to participate in the program. As of June 30, 2006 and 2005, the University's has paid all benefits and has no liability.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

(12) Self-Insurance Program

The System and certain auxiliary organizations have established a public entity risk pool, California State University Risk Management Authority (CSURMA), a blended component unit of the System, to manage centrally workers' compensation, industrial and nonindustrial disability, and general organizational risks. The System's self-insurance claims liability includes estimated amounts that will be required for future payments of claims that have been reported and claims related to events that have occurred but not been reported. The estimated liability is actuarially determined using individual case basis valuations and statistical analyses. Although considerable variability is inherent in such estimates, management believes that the liability is a reasonable estimate at June 30, 2006 and 2005.

Changes in the System's self-insurance claims liability for the two years ended June 30, 2006 are as follows:

Liability at June 30, 2004	\$ 118,711,000
Incurred claims and changes in estimates	33,419,000
Claim payments	<u>(34,491,000)</u>
Liability at June 30, 2005	117,639,000
Incurred claims and changes in estimates	23,938,000
Claim payments	<u>(29,201,000)</u>
Liability at June 30, 2006	112,376,000
Less current portion	<u>(27,441,000)</u>
Long-term liability at June 30, 2006, net of current portion	\$ <u><u>84,935,000</u></u>

The University maintains excess general liability insurance coverage provided by Schools Excess Liability Fund (SELF), a Joint Powers Authority, with coverage for individual claims between \$1,000,000 and \$49,000,000 per occurrence. The University purchases excess workers' compensation insurance provided by the Insurance Corporation of Hanover (ICH) to limits of \$50,000,000 in excess of \$2,500,000 self-insured retention and coverage from American Home Assurance Company (AIG) for limits of \$50,000,000 in excess of \$50,000,000. There have been no settlements in the most recent three fiscal years that have exceeded insurance limits. Although the University maintains excess policies with SELF, ICH, AIG, and other insurers, the ultimate responsibility for payment of claims resides with the University.

The University's allocation of the System's total self-insurance claims liability as of June 30, 2006 and 2005 was approximately 2% and 2%, or \$2,055,000 and \$2,273,000, respectively. This allocation reflects the University's estimated share of the ultimate cost of settling claims relating to events that have occurred on or before June 30, 2006 and 2005.

The University's receivable due from CSURMA totaled \$2,616,774 and \$1,627,100 at June 30, 2006 and 2005, respectively, which is recorded as a component of prepaid expenses and other assets, in the accompanying financial statements. The receivable balance is a result of amounts paid by the University to CSURMA prior to year end related to the University's share of the estimated future funding liability.

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

(13) Commitments and Contingencies

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

Contractual commitments for construction projects unexpended as of June 30, 2006 and 2005 totaled \$8,281,186 and \$12,123,332, respectively. These expenditures will be funded primarily from state appropriations.

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

(14) Classification of Operating Expenses

The University has elected to report operating expenses by functional classification in the statements of revenues, expenses, and changes in net assets, but to provide the natural classification of those expenses as an additional disclosure. For the years ended June 30, 2006 and 2005, operating expenses by natural classification consisted of the following:

<u>2006</u>	<u>Salaries</u>	<u>Benefits</u>	<u>Scholarships and fellowships</u>	<u>Supplies and other services</u>	<u>Depreciation</u>	<u>Total</u>
Functional classification:						
Instruction	\$ 20,493,005	6,542,406	—	4,144,533	—	31,179,944
Research	222,106	75,526	—	372,694	—	670,326
Public service	253,776	39,751	—	4,879	—	298,406
Academic support	8,252,184	2,784,236	—	2,667,886	—	13,704,306
Student services	5,033,244	1,693,994	—	1,598,015	—	8,325,253
Institutional support	7,651,862	2,815,888	—	2,409,850	—	12,877,600
Operation and maintenance of plant	3,493,846	1,384,101	—	7,037,024	—	11,914,971
Student grants and scholarships	—	—	9,278,598	—	—	9,278,598
Auxiliary enterprise expenses	1,547,062	600,276	—	1,106,083	—	3,253,421
Depreciation	—	—	—	—	8,695,918	8,695,918
Total	\$ <u>46,947,085</u>	<u>15,936,178</u>	<u>9,278,598</u>	<u>19,340,964</u>	<u>8,695,918</u>	<u>100,198,743</u>

CALIFORNIA STATE UNIVERSITY, SAN MARCOS

Notes to Financial Statements

June 30, 2006 and 2005

<u>2005</u>	<u>Salaries</u>	<u>Benefits</u>	<u>Scholarships and fellowships</u>	<u>Supplies and other services</u>	<u>Depreciation</u>	<u>Total</u>
Functional classification:						
Instruction	\$ 18,138,444	6,676,060	—	2,649,634	—	27,464,138
Research	384,751	128,463	—	13,205	—	526,419
Public service	20,701	372	—	6,048	—	27,121
Academic support	7,604,836	2,596,696	—	2,287,503	—	12,489,035
Student services	4,687,553	1,530,764	—	1,268,539	—	7,486,856
Institutional support	7,893,048	2,858,006	—	4,227,535	—	14,978,589
Operation and maintenance of plant	2,692,178	1,093,580	—	3,090,730	—	6,876,488
Student grants and scholarships	—	—	6,489,624	—	—	6,489,624
Auxiliary enterprise expenses	1,540,255	603,881	—	1,883,150	—	4,027,286
Depreciation	—	—	—	—	7,340,268	7,340,268
Total	\$ 42,961,766	15,487,822	6,489,624	15,426,344	7,340,268	87,705,824

(15) Transactions with Related Entities

The System is an agency of the State of California and, as such, processes substantially all of its revenue and expenditure activities through the Office of the California State Controller. State appropriations, both noncapital and capital, allocated to the University through the Office of the Chancellor aggregated \$55,490,975 and \$63,309,764 for the years ended June 30, 2006 and 2005, respectively. State appropriations receivable aggregated \$13,027,595 and \$26,538,096 at June 30, 2006 and 2005, respectively. The University also received lottery fund distributions from the State of California in the amount of \$398,000 and \$395,000 for the years ended June 30, 2006 and 2005, respectively, which are included in other nonoperating revenues and expenses.

As headquarters for the System, the Office of the Chancellor administers certain activities centrally for the individual campuses. Primary among these activities are management of capital projects, debt administration, and risk pool administration. The costs associated with the operations of the Office of the Chancellor are not allocated to the individual universities' financial statements.

(16) Subsequent Event

On September 1, 2006, the University entered into an agreement to participate in the Chancellor's Office commercial paper program. The \$1.6 million in additional debt will be used to fund the University's computer refresh program. The annual rate is 4.4% and payable in equal quarterly installments through August 2009.