

Kansas State University

Annual Financial Report

Fiscal Year Ended June 30, 2007



Kansas State University Manhattan, Kansas

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TABLE OF CONTENTS

Management's Discussion and Analysis	3
Statement of Net Assets	10
Statement of Revenues, Expenses and Changes in Net Assets	11
Statement of Cash Flows	12
Notes to Financial Statements	14

Kansas State University

Management's Discussion and Analysis

For the Year Ended June 30, 2007

The following Management's Discussion and Analysis (MD&A) provides an overview of the financial performance of Kansas State University (University) based on currently known facts, decisions and conditions. Readers are encouraged to consider this information in conjunction with the statements and footnotes. The financial statements, footnotes, and this discussion are the responsibility of management.

USING THE FINANCIAL STATEMENTS

This report consists of the three financial statements. The Statement of Net Assets, the Statement of Revenues, Expenses, and Changes in Net Assets, and the Statement of Cash Flows. These financial statements are prepared in accordance with Governmental Accounting Standards Board (GASB) Statement 35, *Basic Financial Statements---and Management's Discussion and Analysis---for Public Colleges and Universities*, as amended by GASB Statements 37 and 38. These statements establish standards for external financial reporting for public colleges and universities and require that financial statements be presented on a consolidated basis to focus on the University as a whole.

STATEMENT OF NET ASSETS

The Statement of Net Assets presents the assets, liabilities, and net assets of the University at a point in time (at the end of the fiscal year). The Statement of Net Assets includes all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector institutions. Under the accrual basis of accounting all of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

Within the Statement of Net Assets, assets and liabilities are further classified as current or non-current. The current classification distinguishes those assets that are highly liquid and available for immediate and unrestricted use by the University, and those liabilities likely to be settled in the next 12 months.

Net assets are divided into three categories:

1. **Invested in capital assets, net of debt**, indicates the university's equity in property, plant, and equipment owned by the University.
2. **Restricted net assets** are further divided into two subcategories, non-expendable and expendable. The corpus of non-expendable restricted resources is only available for investment purposes. Expendable restricted net assets are available for expenditure by the University but must be spent for purposes as determined by donors and/or external entities who have placed time or purpose restrictions on the use of the assets.
3. **Unrestricted net assets** are available to the University for any lawful purpose of the institution.

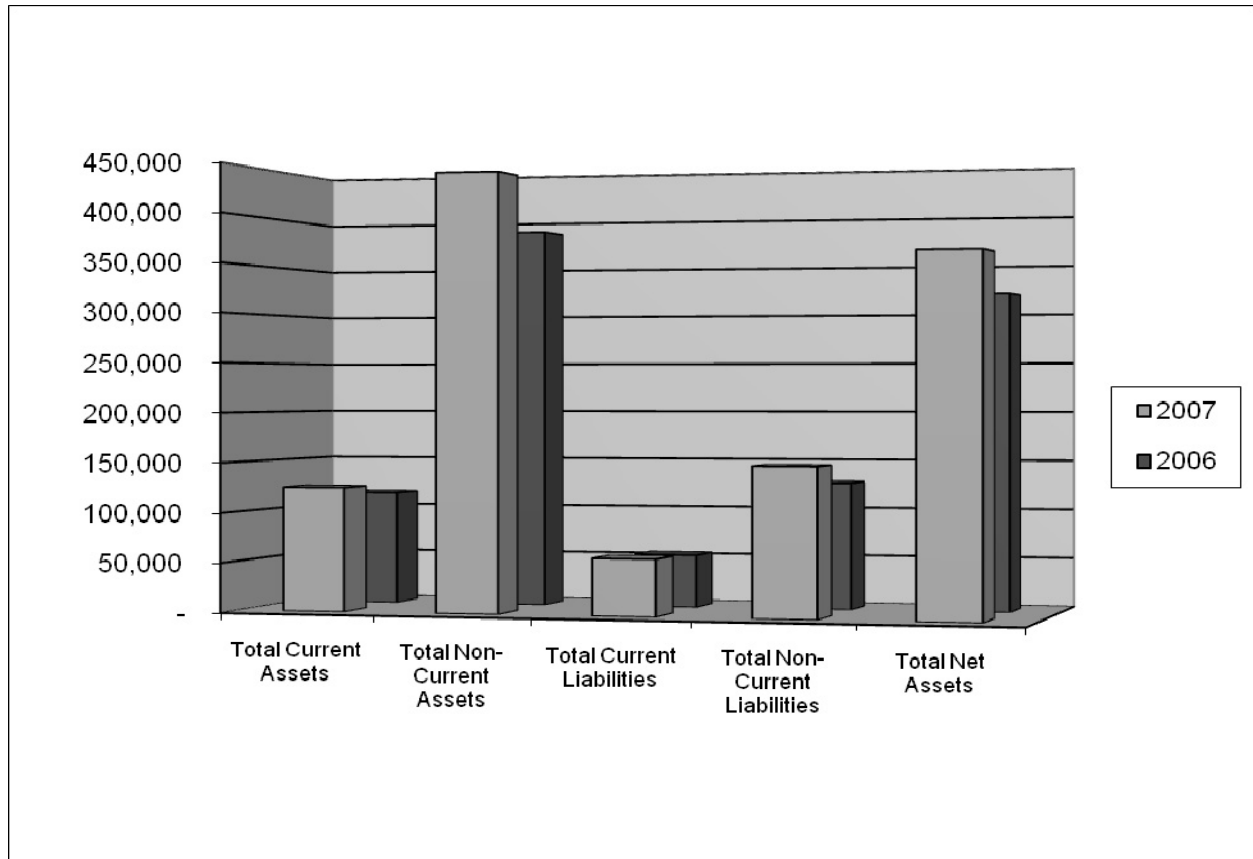
Total assets at June 30, 2007 were \$563.8 million, an increase of \$62.9 million (12.6%). Capital assets, net of depreciation, comprised 69.1%, or \$389.7 million of the total assets.

Total liabilities were \$205.8 million at June 30, 2007, an increase of \$24.2 million (13.3%), compared to \$181.6 million at June 30, 2006. Long-term liabilities comprised 72.3%, or \$148.7 million of the total liabilities.

Total net assets at June 30, 2007 were \$357.9 million, an \$38.7 million increase over the prior year. The breakout of net assets is shown below:

Capital assets, net of related debt.....	\$236,666,335
Restricted net assets	50,781,213
Unrestricted net assets	70,517,349
Total net assets.....	\$357,964,897

The composition of current and non-current assets and liabilities and net assets is displayed below for both the 2006 and 2007 fiscal year ends (in thousands):



STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

The Statement of Revenues, Expenses and Changes in Net Assets presents the total revenues earned and expenses incurred by the University for operating, non-operating and other related activities during a period of time. Its purpose is to assess the University's operating results.

Revenues

Operating revenues at the University as of June 30, 2007 increased by 2.6% over the previous fiscal year. The following is a brief summary of the significant changes:

- Student fee revenues, after scholarship allowances, were \$131.9 million in 2007, compared to \$119.5 million in 2006. This increase is a result of a tuition increase approved by the Kansas Board of Regents for fiscal year 2007. The goal of the tuition increase, which was the result of collaboration between University Administration and University students, was to provide additional funds to the University to improve or enhance student education while State appropriations decreased significantly. The increase was used for specific expenses including faculty salary increases, instructional and technological upgrades, and additional scholarships.

- Grants and contracts (federal, state and local, and non-governmental) decreased \$7 million from the previous fiscal year. This category of revenue includes funds received from the federal government for financial aid as well as other sponsored research revenue.
- Sales and services of educational activities decreased \$1.6 million from the previous fiscal year. These revenues are generated by activities that are related incidentally or exist primarily to afford hands on experience related to providing instruction, research, and public service.
- Auxiliary enterprises increased \$1 million from the previous fiscal year. Auxiliary enterprises include Housing, Parking, University health services, and a variety of other smaller services.

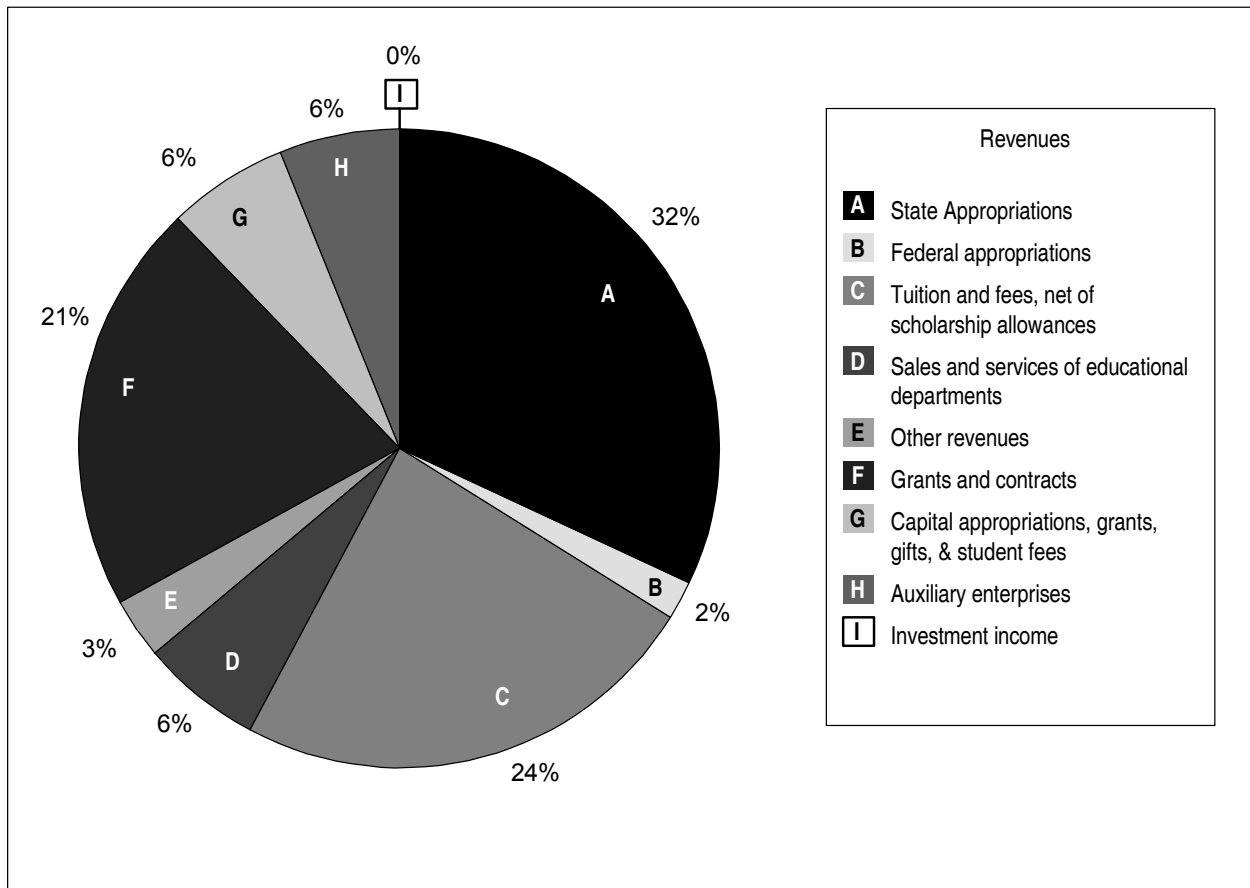
Total non-operating revenues were up 3.6% from the prior year from \$174.9 million to \$180.6 million. The following is a brief summary of the significant changes:

- State appropriations, the largest single source of revenue at the University, increased from \$171.7 million to \$177.2 million.
- Investment income and student fees collected for capital projects remained constant.

Other revenues included the following:

- Capital grants and gifts increased from \$3.2 million to \$26.8 million, due for the most part to the donation of land and buildings during the fiscal year.

In summary, total revenues increased by \$25 million, from \$521.8 million to \$546.8 million, an overall increase of 4.8%. The compositions of these revenues are displayed in the following graph:



Expenses

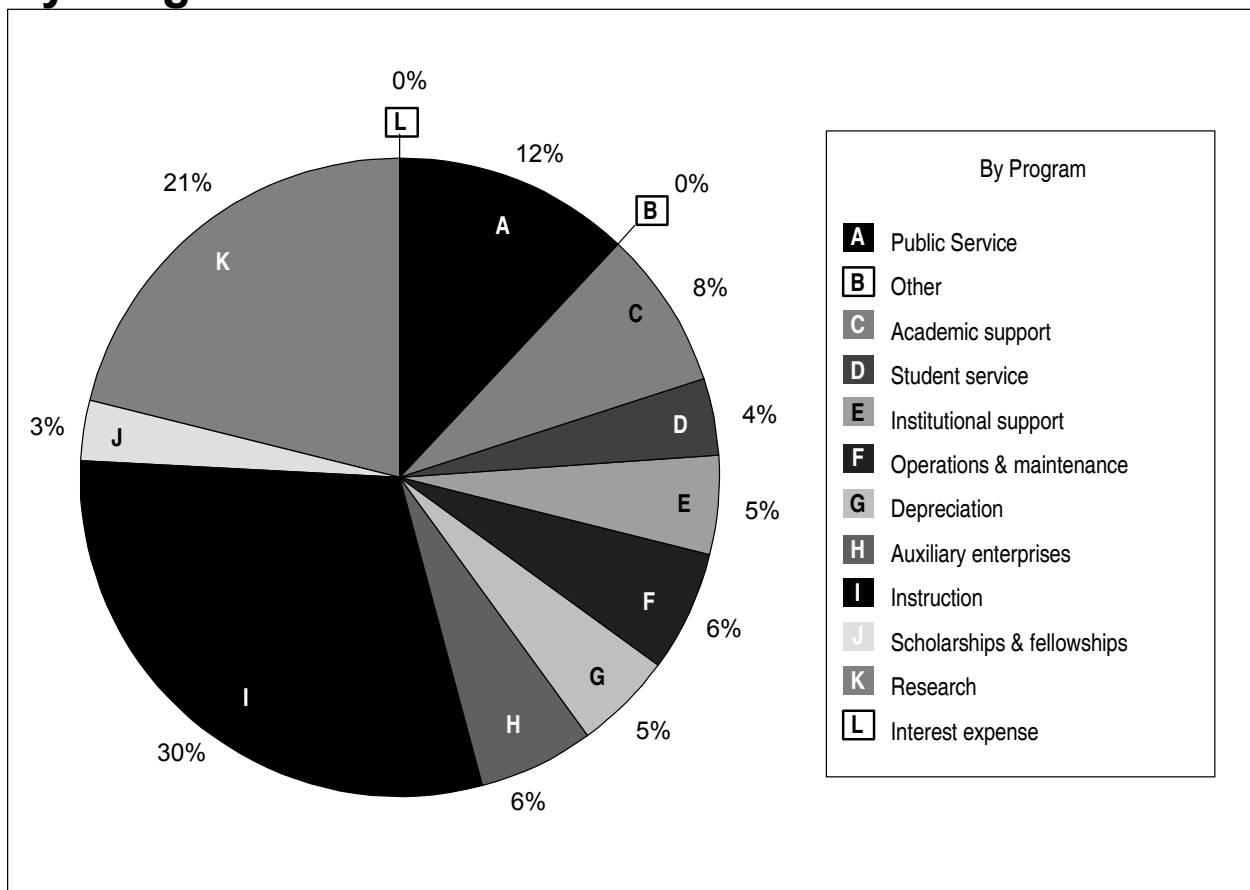
Operating expenses were \$505.7 million for the 2007 fiscal year. This was an increase over the prior year of \$18.4 million, or 3.8%. The following is a brief summary of the significant changes:

- Expenses related to the University's mission of instruction, research and public service increased \$15 million in 2007. This increase is directly related to the University's tuition increase earmarked for faculty salaries.
- Scholarships and fellowships expenses increased from \$12 million in 2006 to \$12.6 million in 2007.

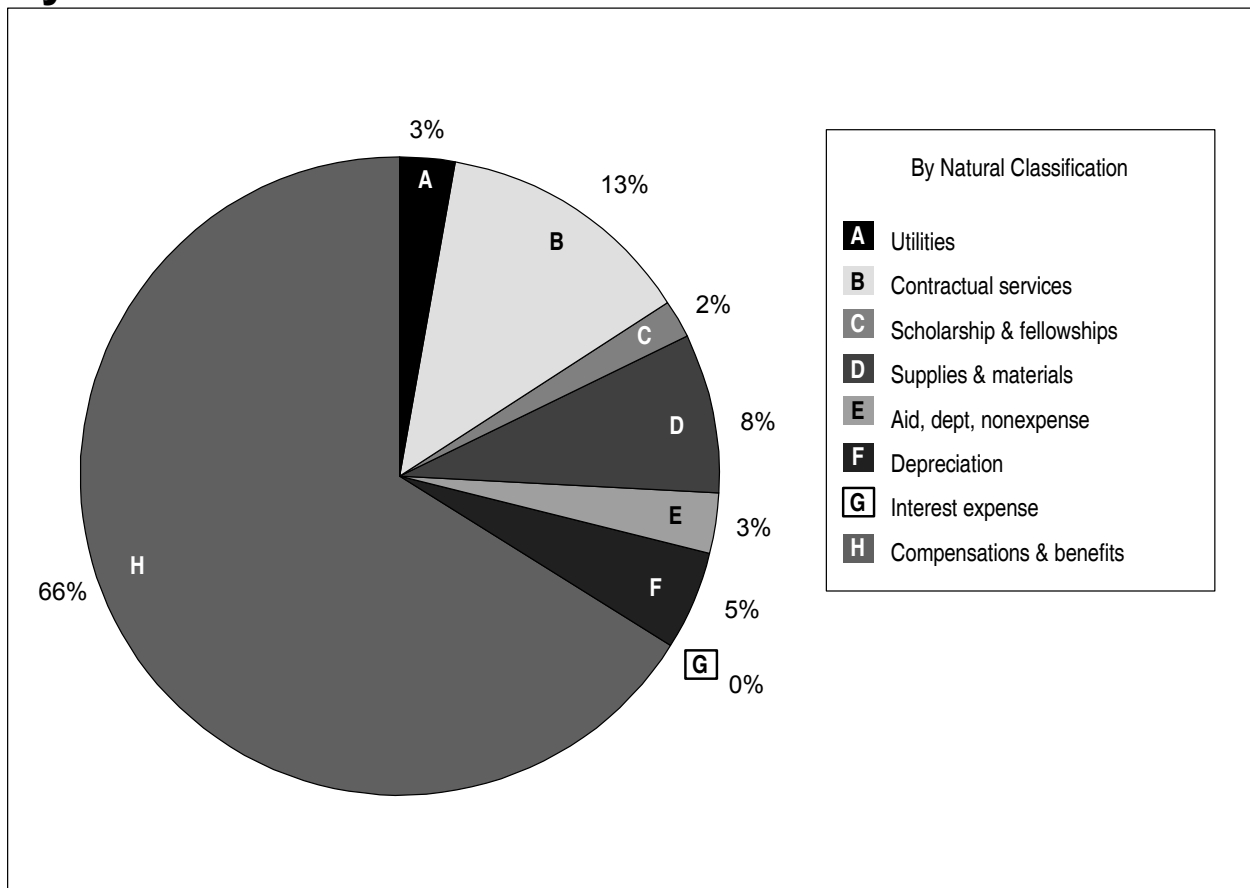
Non-operating expenses are represented primarily by interest expense, which remained consistent with fiscal year 2006.

The composition of total expenses, including operating and non-operating are displayed below:

By Program



By Natural Classification



Extraordinary Items

The University did not have any special and extraordinary items in 2007.

Net Assets

Net assets increased by \$38.7 million compared to the previous fiscal year, which generally indicates that the financial condition has improved over the year. There were many offsetting variances, but the increase is primarily due to an increase in capital assets, net of depreciation.

STATEMENT OF CASH FLOWS

The Statement of Cash Flows presents cash receipts and payments of the University during a period of time. Its purpose is to assess the University's ability to generate future net cash flows and meet its obligations as they come due.

SUMMARY OF THE STATEMENT OF CASH FLOWS (in thousands of dollars):

	June 30, 2007	June 30, 2006
Net cash provided (used) by:		
Operating activities	\$ (145,860)	\$ (151,988)
Non-capital financing activities	177,103	171,493
Capital and related financing/appropriations	(40,542)	(57,785)
Investing activities	16,320	28,328
Net increase in cash	7,021	(9,952)
Beginning cash and cash equivalent balances	93,713	103,665
Component Unit Prior Period Adjustment	74	
Ending cash and cash equivalent balances	\$ 100,808	\$ 93,713

Cash provided by operating activities includes tuition and fee and grant and contract revenues. Cash used for operating activities includes payments to employees and suppliers. Cash provided by non-capital financing/appropriations includes state appropriations and the receipt and disbursement of the federal direct student loan program. Cash provided for capital and related financing activities represents proceeds from debt, the principal and interest payments towards debt, capital appropriations and grants, and the purchase and construction of capital assets. Cash provided by investing activities includes purchases and sales of investments as well as investment income earnings and losses realized.

The University's overall liquidity increased by \$7 million during fiscal year 2007. This increase is the net result of an increase in state appropriations and tuition and fees during the year, offset by the expenditure of existing bond proceeds.

CAPITAL ASSETS

The University made significant investments in capital during the 2006-2007 fiscal year. Detailed information regarding capital asset additions, retirements & depreciation is available in Note 3 to the financial statements.

The following is a brief summary of the construction projects that were completed during the current fiscal year:

- A \$5.9 million addition to the Marianna Kistler Beach Museum of Art was completed. The privately funded project provided galleries to exhibit the permanent collection and additional storage space.
- Ten buildings of the Jardine Terrace Apartments renovation were completed at a cost of \$39.6 million in FY2007. This Department of Housing and Dining Services project has an estimated total cost of \$102 million and will be funded through a 30-year series of bond agreements with future repayment of the bonds coming from Housing Operation revenues.
- The Hal Ross Flour Mill was completed Fall 2007 at a cost of approximately \$6.8 million and was funded through private gifts. A feed mill and teaching/research/administration building will complete the Grain Science Complex and will be funded through private gifts.
- The Biosecurity Research Institute was completed Spring 2007. This \$54 million project will enable investigation of infectious diseases and provide for safe handling of biotechnology products. The majority of the funding was provided through the issuance of revenue bonds, with future repayment of the bonds coming from state appropriations and various university revenue funds
- Renovations to Haymaker Hall, which is a part of the Department of Housing and Dining Services, were finalized. The \$3.1 million renovation project converted the old style student rooms to suites of rooms.
- A multi-year renovation and addition to the Vanier Football Complex was completed at an estimated cost of \$7.5 million and was funded through private gifts.

- Construction and renovation projects affecting a variety of buildings were completed during the year at an estimated cost of \$1.4 million.

Additionally, the University was involved in several construction projects that were in physical construction or planning and design phases at year-end:

- Construction of a 1,400 space Parking Garage started the Summer 2007. The \$17.5 million project on the south side of the Student Union is to increase availability of parking places for the entire university community as well as visitors.
- The Board of Regents formally approved a five-year building maintenance project plan for each of the state universities effective for FY 2008, to preserve and strengthen higher education infrastructure. Kansas State University's first year of funding is approximately \$12.6 million.
- Several projects are in the planning stages, including a \$6.4 million Student Life Center at the Salina Campus and a \$6 million Child Care Center at the Manhattan Campus.

DEBT ADMINISTRATION

At June 30, 2007, the University had \$149.9 million in debt outstanding, compared to \$127.5 million at June 30, 2006. The increase is due to the issuance of Housing System Revenue Bonds of \$27,750,000. The University paid \$11,659,941 in principal and interest payments related to all outstanding debt.

Moody's Investors Service currently rates the University "Aa3". More detailed information about the University's long-term liabilities is available in Notes 7, 8, and 9 to the financial statements.

ECONOMIC OUTLOOK

The State of Kansas revenues exceeded estimates in FY 2007 and revenues for FY 2008 are coming in higher than projected. The Kansas economy is expected to continue the trend of positive growth through FY 2008. Future increases in State funding are likely to be moderate. Thirty-three percent of the total resources for the University, during a fiscal year, are provided by the State. Appropriations for fiscal year 2008 are currently set at \$186.8 million, which is an increase of 4% from fiscal year 2007.

The University is not aware of any additional currently known facts, decisions, or conditions that are expected to have significant effect on the financial position or results of operations during this fiscal year beyond those unknown variations having a global effect on virtually all types of business operations.

Overall, the financial position of the University continues to be strong. Enrollment for the academic 2007-2008 year is expected to be relatively consistent with academic 2006-2007 year.

Kansas State University
Statement of Net Assets
For the Year Ended June 30, 2007

	University Funds		Component Units	
	2007	2006	2007	2006
<u>ASSETS</u>				
Current Assets				
Cash and cash equivalents	\$ 89,164,050	\$ 83,487,230	\$ 18,818,598	\$ 22,465,019
Accounts receivable, net	23,969,042	22,468,695	7,210,274	5,626,233
Pledges receivable	-	-	62,000	28,695
Investments	2,706,148	1,963,733	4,154,942	2,687,968
Loans to students, net	3,573,175	2,997,632	-	-
Inventories	4,377,402	3,222,933	405,260	437,288
Prepaid expenses	964,163	899,227	316,110	1,626,617
Total Current Assets	<u>124,753,980</u>	<u>115,039,450</u>	<u>30,967,184</u>	<u>32,871,820</u>
Noncurrent Assets				
Restricted cash and cash equivalents	11,643,795	10,225,690	18,075,005	17,002,831
Pledges receivable	-	-	584,867	42,866
Investments	23,732,725	38,526,509	2,038,625	2,038,625
Loans to students, net	13,935,570	13,640,414	-	-
Other assets	-	-	1,556,140	1,441,757
Capital assets, net	389,726,502	323,475,132	7,893,816	5,791,150
Total Noncurrent Assets	<u>439,038,592</u>	<u>385,867,745</u>	<u>30,148,453</u>	<u>26,317,229</u>
TOTAL ASSETS	<u>563,792,572</u>	<u>500,907,195</u>	<u>61,115,637</u>	<u>59,189,049</u>
<u>LIABILITIES</u>				
Current Liabilities				
Accounts payable and accrued liabilities	15,987,734	15,761,435	6,220,380	8,147,149
Deferred revenue	20,164,241	16,423,468	16,713,765	16,248,601
Revenue bonds payable	4,570,000	4,985,000	945,000	1,276,700
Other loan payable	1,590,467	231,159	376,700	-
Accrued compensated absences	12,642,244	12,383,960	696,727	849,172
Other liabilities	756,187	1,430,948	1,859,806	1,705,115
Capital lease payable	611,511	1,364,352	-	419
Deposits held in custody for others	745,134	830,329	323,409	387,639
Total Current Liabilities	<u>57,067,518</u>	<u>53,410,651</u>	<u>27,135,787</u>	<u>28,614,795</u>
Noncurrent Liabilities				
Other liabilities	3,416,279	4,172,464	-	-
Revenue bonds payable	141,310,000	118,130,000	13,405,889	13,974,189
Other loan payable	875,186	3,465,653	623,300	1,000,000
Accrued compensated absences	2,151,737	1,344,631	-	-
Capital lease payable	1,006,955	1,125,309	-	-
Total Noncurrent Liabilities	<u>148,760,157</u>	<u>128,238,057</u>	<u>14,029,189</u>	<u>14,974,189</u>
TOTAL LIABILITIES	<u>205,827,675</u>	<u>181,648,708</u>	<u>41,164,976</u>	<u>43,588,984</u>
<u>NET ASSETS</u>				
Invested in capital assets, net of related debt	236,666,335	191,421,657	(5,802,040) *	(9,460,158) *
Restricted for:				
Nonexpendable	2,768,858	2,614,105	14,717,945	12,599,818
Expendable				
Scholarships, research, instruction, public service, & other	(6,717,476)	(6,307,934)	3,320,590	4,359,679
Loans	19,633,793	19,507,470	-	-
Capital projects	24,193,902	36,699,753	42,264	43,334
Debt service	10,902,136	11,138,008	-	3,433,756
Unrestricted	70,517,349	64,185,428	7,671,902	4,623,636
TOTAL NET ASSETS	<u>\$ 357,964,897</u>	<u>\$ 319,258,487</u>	<u>\$ 19,950,661</u>	<u>\$ 15,600,065</u>

*See accompanying Note 14.

Kansas State University
Statement of Revenues, Expenses and Changes in Net Assets
For the Year Ended June 30, 2007

	University Funds		Component Units	
	2007	2006	2007	2006
Operating Revenues:				
Tuition and fees, net of scholarship allowances of \$12,733,501	\$ 131,851,672	\$ 119,458,305	\$ 2,309,855	\$ 2,370,476
Federal appropriations	9,029,957	8,047,319	-	-
Federal grants and contracts	88,283,728	91,229,795	-	-
State and local grants and contracts	4,425,871	5,287,648	-	-
Nongovernmental grants and contracts	23,254,791	26,372,800	12,082,496	9,556,786
Sales and services of educational activities	32,369,243	33,991,435	23,616,642	20,865,116
Auxiliary enterprises				
Housing revenues (revenues are pledged as security for bonds)	24,961,654	24,977,139	-	-
Parking revenues (revenues are pledged as security for bonds)	2,454,489	2,053,938	-	-
Student health revenues	5,877,933	5,243,490	-	-
Other auxiliary revenues	90,302	62,846	-	-
Interest earned on loans to students	268,722	282,006	-	-
Other operating revenues	12,180,640	9,583,178	8,109,212	6,313,193
Contributions	-	-	8,486,759	6,897,987
	<u>-</u>	<u>-</u>	<u>8,486,759</u>	<u>6,897,987</u>
Total Operating Revenues	<u>335,049,002</u>	<u>326,589,899</u>	<u>54,604,964</u>	<u>46,003,558</u>
Operating Expenses:				
Instruction	152,967,028	142,910,562	-	-
Research	106,887,529	104,674,318	-	-
Public Service	59,768,867	56,705,814	989,523	871,798
Academic Support	42,050,814	39,780,938	-	-
Student Service	19,568,368	18,955,789	35,376,069	31,107,742
Institutional Support	25,397,982	24,815,001	2,828,201	2,463,440
Operations & Maintenance of Plant	32,908,772	35,711,754	-	-
Depreciation	23,267,084	22,226,899	1,420,485	1,110,741
Scholarships & Fellowships	12,660,501	12,021,619	5,460,999	4,726,155
Auxiliary Enterprises	29,405,385	29,008,931	-	-
Other Expenses	808,512	440,411	3,848,171	2,924,864
	<u>808,512</u>	<u>440,411</u>	<u>3,848,171</u>	<u>2,924,864</u>
Total Operating Expenses	<u>505,690,842</u>	<u>487,252,036</u>	<u>49,923,448</u>	<u>43,204,740</u>
Operating Income (Loss)	<u>(170,641,840)</u>	<u>(160,662,137)</u>	<u>4,681,516</u>	<u>2,798,818</u>
Nonoperating Revenues (Expenses)				
State appropriations	177,174,300	171,676,343	1,536,908	1,522,182
Gifts	849,158	-	-	-
Investment income	962,925	921,652	2,779,836	1,994,250
Interest expense	(1,727,073)	(1,835,443)	(1,379,226)	(1,348,548)
Gain/Loss on disposal of assets	(688,574)	156,935	-	-
Student fees for capital projects	2,206,588	2,186,376	-	-
	<u>2,206,588</u>	<u>2,186,376</u>	<u>-</u>	<u>-</u>
Net Nonoperating Revenues	<u>178,777,324</u>	<u>173,105,863</u>	<u>2,937,518</u>	<u>2,167,884</u>
Income (Loss) Before Other Revenues, Expenses, Gains and Losses	<u>8,135,484</u>	<u>12,443,726</u>	<u>7,619,034</u>	<u>4,966,702</u>
Capital appropriations	4,392,000	4,374,000	-	-
Capital grants and gifts	26,808,611	3,172,780	-	-
Additions to permanent endowment	102,830	132,521	2,133,371	4,731,658
Other additions/deductions, net	(806,255)	137,078	(5,401,809)	(3,264,129)
	<u>(806,255)</u>	<u>137,078</u>	<u>(5,401,809)</u>	<u>(3,264,129)</u>
Increase (Decrease) in Net Assets	<u>38,632,670</u>	<u>20,260,105</u>	<u>4,350,596</u>	<u>6,434,231</u>
Net Assets				
Net Assets -- Beginning of Year, as previously reported	319,258,487	298,112,599	15,600,065	9,165,834
Prior Period Restatement	73,740	885,783	-	-
Net Assets, Beginning of Year, as restated	<u>319,332,227</u>	<u>298,998,382</u>	<u>15,600,065</u>	<u>9,165,834</u>
Net Assets -- End of Year	<u>\$ 357,964,897</u>	<u>\$ 319,258,487</u>	<u>\$ 19,950,661</u>	<u>\$ 15,600,065</u>

Kansas State University
Statement of Cash Flows
For the Year Ended June 30, 2007

	University Funds	
	2007	2006
Cash Flows from Operating Activities		
Tuition and fees	\$ 144,973,076	\$ 129,009,291
Endowment income	79,560	87,702
Sales and services of educational activities	34,180,435	33,680,916
Auxiliary enterprise charges		
Housing	24,686,239	24,911,484
Parking	2,365,072	2,018,362
Student Health	5,855,162	5,231,927
Other	88,087	62,846
Grants and contracts	117,330,062	121,411,955
Federal appropriations	9,029,957	8,047,319
Payments to suppliers	(173,925,399)	(171,100,844)
Compensation & benefits	(338,343,248)	(331,173,239)
Loans issued to students and employees	(4,784,344)	(5,265,932)
Collections on loans issued to students and employees	4,204,784	5,132,495
Other receipts (payments)	28,400,727	25,957,843
	<u>(145,859,830)</u>	<u>(151,987,875)</u>
Net Cash Flows from Operating Activities	(145,859,830)	(151,987,875)
Cash Flows from Noncapital Financing Activities		
State appropriations	177,174,300	171,676,343
Direct lending receipts	95,004,815	95,153,511
Direct lending payments	(95,270,332)	(94,995,342)
Funds held for others	(85,195)	(60,630)
Other	279,377	(281,220)
	<u>177,102,965</u>	<u>171,492,662</u>
Net Cash Flows from Noncapital Financing Activities	177,102,965	171,492,662
Cash Flows from Capital and Related Financing Activities		
Proceeds from capital debt	27,750,000	-
Capital appropriations	4,392,000	4,374,000
Capital Grants and gifts	1,097,434	110,996
Student fees for capital projects	2,206,588	2,186,376
Purchases of capital assets	(63,734,939)	(56,524,445)
Principal paid on capital debt and leases	(5,985,000)	(3,145,000)
Interest paid on capital debt and leases	(5,674,941)	(5,635,602)
Other	(593,341)	848,936
	<u>(40,542,199)</u>	<u>(57,784,739)</u>
Net Cash Flows from Capital and Related Financing Activities	(40,542,199)	(57,784,739)
Cash Flows from Investing Activities		
Investment income	2,268,879	3,126,861
Purchase/Redemption of investments	14,051,370	25,200,714
	<u>16,320,249</u>	<u>28,327,575</u>
Net Cash Flows from Investing Activities	16,320,249	28,327,575
Net change in cash and cash equivalents	7,021,185	(9,952,377)
Cash and cash equivalents -- beginning of year	93,712,920	103,665,297
Prior Period Restatement	73,740	-
Cash and cash equivalents -- beginning of year	<u>93,786,660</u>	<u>103,665,297</u>
Cash and cash equivalents -- end of year	<u>\$ 100,807,845</u>	<u>\$ 93,712,920</u>

Kansas State University
Statement of Cash Flows (Continued)
For the Year Ended June 30, 2007

	University Funds	
	2007	2006
Reconciliation		
Operating income (loss)---SRECNA	\$ (170,641,840)	\$ (160,662,137)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:		
Depreciation expense	23,267,084	22,226,899
Changes in assets and liabilities:		
Accounts receivable, net	(1,539,248)	(3,645,838)
Loans to students, net	(579,560)	(133,437)
Inventories	(1,154,469)	(124,306)
Prepaid expenses	(64,935)	(725,817)
Accounts payable and accrued liabilities	48,106	(8,757,123)
Deferred revenue	3,739,642	(460,619)
Accrued compensated absences	1,065,390	294,503
Net cash used in operating activities---Cash Flow	<u>\$ (145,859,830)</u>	<u>\$ (151,987,875)</u>

Kansas State University

Notes to Financial Statements
For the Year Ended June 30, 2007

Note 1 - Organization and Summary of Significant Accounting Policies

Organization. Kansas State University (University) is a comprehensive, research, federal land grant institution governed by the Kansas Board of Regents and is an agency of the State of Kansas. Accordingly, for financial reporting purposes, the University is included in the financial report of the State of Kansas.

The University is currently classified as a Doctoral/Research University – Extensive under the Carnegie Classification system and is accredited by the North Central Association of Colleges and Schools. Undergraduate, graduate and post-graduate degrees are available from nine colleges: Agriculture, Architecture, Planning & Design, Arts & Sciences, Business Administration, Education, Engineering, Human Ecology, Veterinary Medicine, and Technology & Aviation.

Other major operating units of the University are the Agricultural Experiment Station and a statewide Cooperative Extension Service. The main campus covers 668 acres in the cities of Manhattan and Salina, Kansas. Additional University sites include 18,000 acres of the Agricultural Experiment Station (AES) located in research centers at Hays, Garden City, Colby, and Parsons and 8,600 acres in the Konza Prairie Research Natural Area, jointly operated by the AES and the Division of Biology.

Financial Reporting Entity. As required by the accounting principles generally accepted in the United States of America, as prescribed by the Governmental Accounting Standards Board (GASB), these financial statements present the financial position and financial activities of the University and its component units.

The Kansas State University Research Foundation (KSURF), The IDEA Center, Inc., The K-State Union Corporation, the Intercollegiate Athletic Council of Kansas State University, Inc., and the Kansas State University Student Financial Assistance Foundation, Inc. have been discretely presented.

K-State Olathe Innovation Campus, Inc., Kansas State University Veterinary Clinical Outreach, Inc., K-State Diagnostic and Analytical Services, Inc., Universal K-State, Inc., and K-State Comprehensive Assessment Tools, Inc. have been blended.

In preparing the financial statements, all significant transactions and balances between the University and the blended component units have been eliminated.

The Kansas State University Foundation is not included in the University's financial statements.

Basis of Accounting. For financial reporting purposes, the University is considered a special-purpose government engaged only in business-type activities. Accordingly, the University's financial statements have been presented using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. All significant intra-agency transactions have been eliminated.

The University has the option to apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless FASB conflicts with GASB. The University has elected to not apply FASB pronouncements issued after the applicable date.

Cash Equivalents. For the purposes of the Statement of Cash Flows, the University considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

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

Accounts Receivable. Accounts receivable consists of tuition and fee charges to students and auxiliary enterprise services provided to students, faculty, and staff. Accounts receivable also include amounts due from the Federal, state and local governments or private sources, in connection with reimbursement of allowable expenditures made pursuant to the University's grants and contracts. Accounts receivable are recorded net of estimated uncollectible amounts.

Inventories. Inventories are stated at cost.

Kansas State University

Notes to Financial Statements (Continued) For the Year Ended June 30, 2007

Noncurrent Cash and Investments. Cash and investments that are externally restricted to make debt service payments, maintain sinking or reserve funds, or to purchase or construct capital or other noncurrent assets, are classified as noncurrent in the Statement of Net Assets.

Capital Assets. Capital assets are recorded at cost at the date of acquisition, or fair market value at the date of donation in the case of gifts. For equipment, the University's capitalization policy includes all items with a unit cost of \$5,000 or more, and an estimated useful life of greater than one year. Renovations to buildings, infrastructure, and land improvements that significantly increase the value or extend the useful life of the structure are capitalized if the related project cost is \$100,000 or greater. Routine repairs and maintenance are charged to operating expense in the year in which the expense was incurred.

Depreciation is computed using the straight-line method and half-year convention over the estimated useful lives of the assets, generally 40 years for buildings, 25 years for infrastructure and land improvements, 8 years for equipment, 5 years for vehicles, and 5 to 40 years for componentized buildings and building improvements.

Deferred Revenue. Deferred revenues consist primarily of summer school tuition not earned during the current year and amounts received from grant and contract sponsors that have not yet been earned.

Compensated Absences. Employee vacation and sick pay is accrued at year-end for financial statement purposes. The liability and expense incurred are recorded as accrued compensated absences in the Statement of Net Assets, and as a component of compensation and benefit expense in Note 13 Operating Expenses by Natural Classification.

Noncurrent Liabilities. Noncurrent liabilities include principal amounts of revenue bonds and loans payable, capital lease obligations with contractual maturities greater than one year, and other liabilities that are to be paid from funds that are classified as noncurrent assets.

Net Assets. The University's net assets are classified as follows:

Invested in capital assets, net of related debt: This represents the University's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets such amounts are not included as a component of invested in capital assets, net of related debt.

Restricted net assets – nonexpendable: Restricted nonexpendable net assets consist of endowment and similar type funds in which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to principal.

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

Unrestricted net assets: Unrestricted net assets represent resources derived from student tuition and fees, state appropriations, and sales and services of educational departments. These resources are used for transactions relating to the educational and general operations of the University, and may be used at the discretion of the governing board to meet current expenses for any purpose. These resources also include auxiliary enterprises, which are substantially self-supporting activities that provide services for students, faculty and staff.

Tax Status. As a state institution of higher education, the income of the University is generally exempt from federal and state income taxes under Section 115(a) of the Internal Revenue Code; however, income generated from activities unrelated to the University's exempt purpose is subject to income taxes under Internal Revenue Code Section 511(a)(2)(B).

Kansas State University

Notes to Financial Statements (Continued) For the Year Ended June 30, 2007

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

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

Nonoperating revenues: Nonoperating revenues include activities that have the characteristics of nonexchange transactions, such as gifts and contributions, and other revenue sources that are defined as nonoperating revenues by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting* and GASB Statement No. 35, *Basic Financial Statements and Management's Discussion and Analysis for Public Colleges and Universities*, such as state appropriations and investment income.

Scholarship Discounts and Allowances. Student tuition and fee revenues, and certain other revenues from students, are reported net of scholarship discounts and allowances in the Statement of Revenues, Expenses, and Changes in Net Assets. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by the University, and the amount that is paid by students and/or third parties making payments on the students' behalf. Certain governmental grants, such as Pell grants, and other Federal, state or nongovernmental programs, are recorded as either operating or nonoperating revenues in the University's financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees and other student charges, the University has recorded a scholarship discount and allowance.

Summer Session. Revenues and expenses for the summer session are reported within the fiscal year in which the summer session is predominately conducted. Accordingly, only revenues and expenses for the 2006 summer session are reported in the Statement of Revenues, Expenses, and Changes in Net Assets. For the 2007 summer session, revenues received prior to June 30, 2007 are reported as deferred revenues in the Statement of Net Assets while expenses paid prior to June 30, 2007 are reported as prepaid expenses. Kansas Board of Regents officials determined this methodology and believe the departure from generally accepted accounting principles will not have a material effect on the University's financial position.

Use of Estimates. The preparation of financial statements in conformity with generally accepted accounting principles require management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from those estimates.

Note 2 – Deposits and Investments

A summary of the University's deposits and investments at June 30 is as follows:

	<u>2007</u>	<u>2006</u>
Cash deposits with State Treasury	\$ 97,933,718	\$ 92,559,828
Cash deposits with financial institutions	2,535,077	866,102
Mutual funds	339,050	286,990
Certificates of deposits	2,706,148	2,613,733
Repurchase agreements	932,000	932,000
Guaranteed investment contracts	<u>22,800,725</u>	<u>36,944,509</u>
	\$127,246,718	\$134,203,162

A reconciliation of deposits and investments to the Statement of Net Assets as of June 30 is as follows:

	<u>2007</u>	<u>2006</u>
Cash and cash equivalents (current)	\$ 89,164,050	\$ 83,487,230
Investments (current)	2,706,148	1,963,733
Restricted cash and cash equivalents (non-current)	11,643,795	10,225,690
Investments (non-current)	<u>23,732,725</u>	<u>38,526,509</u>
	\$127,246,718	\$134,203,162

Kansas State University

Notes to Financial Statements (Continued) For the Year Ended June 30, 2007

Deposits.

The carrying amount of the University's cash and cash equivalents with the State Treasurer and other financial institutions at June 30, 2007 were \$100,807,845. The University's deposits with the State Treasurer are pooled with the funds of other State Agencies and then, in accordance with statutory limitations, placed in short-term investments with the exception of the bond funds. All bond proceeds are invested in conjunction with specifications stated in the bond resolutions.

State law requires the University to deposit the majority of its cash balances with the State Treasurer, who holds and invests the funds. These investments are managed by the Pooled Money Investment Board, which maintains a published Investment Policy. The exceptions to this are any funds maintained in the University's imprest fund, organizational safekeeping, and any funds held by external entities on behalf of the University.

Cash balances maintained by the State Treasurer are pooled and are held in a general checking account and other special purpose bank accounts. The available cash balances beyond immediate need are pooled for short-term investments purposes by the Pooled Money Investment Board and are reported at fair value, based on quoted market prices.

The majority of deposit balances not maintained by the State Treasurer are covered by FDIC or collateralized. The University does not have a formal deposit policy regarding custodial credit risk. However, management has evaluated the financial stability of the financial institutions involved and feels the deposit custodial credit risk is minimal.

Investments.

Pooled Money Investment Board (PMIB). The investment policy of the PMIB is governed by State statutes. The primary objectives are to attain safety, liquidity, and yield. Allowable investments for State pooled moneys not held in Kansas financial institutions are as follows:

- Direct obligations of, or obligations except mortgage backed securities, that are insured as to principal and interest by the U.S. Government, or any direct agency thereof, with maturities up to four years
- Repurchase agreements with Kansas banks or with primary government securities dealers
- Interfund loans to various State agencies as mandated by the Kansas Legislature limited to not more than the lesser of 10 percent or \$80,000,000 of total investments
- Certain Kansas agency and IMPACT Act projects and bonds
- Linked deposit loans for agricultural production not to exceed \$55,000,000
- High grade commercial paper

Kansas Development Finance Authority (KDFA). For investments related to the University's revenue bonds, state statutes permit cash balances to be invested as permitted by bond documents and bond covenants. KDFA manages the University's revenue bond investments. Allowable investments include:

- U.S. Government obligations
- Obligations of government-sponsored agencies
- Federal funds, unsecured certificates of deposit, time deposits and banker's acceptances
- Deposits – fully insured by FDIC
- Certain State or municipal debt obligations
- Certain pre-refunded municipal obligations
- Commercial paper
- Investments in money market funds
- Repurchase agreements
- Stripped securities
- Investments in the Municipal Investment Pool Fund
- Investment agreements
- Guaranteed investment contracts

Kansas State University

Notes to Financial Statements (Continued) For the Year Ended June 30, 2007

The Kansas State University Foundation (Foundation). The Foundation is authorized by state statute to act as the investing agent for the state agricultural university fund. Allowable investments include:

- Time deposit, open accounts for periods of not less than 30 days, or certificates of deposit for periods of not less than 90 days, in commercial banks located in Kansas
- United States treasury bills or notes with maturities as the investing agent shall determine
- Insured savings and loan associations to the extent of the insurance provided by the F.S.L.I.C.

Interest Rate Risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The University does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

PMIB minimizes interest rate risk structuring the investment portfolio so that securities mature to meet cash requirement for ongoing operations, thereby avoiding the need to sell securities on the open market prior to maturity, and by investing operating funds primarily in shorter-term securities.

For revenue bond investments managed by KDFA, due to the tax-exempt status of the bonds, it is generally the practice of KDFA and the University to match reserve fund interest rates to the arbitrage yield on the bonds and the term of the investments to the maturity of the bonds. For invested loan funds, KDFA generally invests to maximize the interest rate and set a term of investment based on estimated expenditures, which is generally 3 – 5 years.

The state agricultural university funds are invested in certificates of deposit at a fixed rate and are non-negotiable instruments. Therefore they are not exposed to interest rate risk.

As of June 30, 2007 the University had the following investments:

Investment Type	Fair Value	Less Than 1 Year	1 - 5 Years	6 - 10 Years	More Than 10 Years
Certificates of Deposit	\$ 2,706,148	\$2,706,148			
Repurchase Agreements	932,000			\$ 932,000	
Guaranteed Investment Contracts	22,800,725		\$ 18,274,729	84,500	\$ 4,441,496
Total	\$26,438,873	\$2,706,148	\$ 18,274,729	\$1,016,500	\$ 4,441,496

Credit Risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to the University. The University investments may have credit risk, since the underlying securities may include securities other than those that take the form of U.S. Treasuries or obligations explicitly guaranteed by the U.S. government. The investments are unrated and certain investments have an underlying collateral agreement.

Custodial Credit Risk for investments is the risk that, in the event of the failure of the counterparty, the University will not be able to recover the value of the investments that are in the possession of an outside party. The University's investment securities are exposed to custodial credit risk if the securities are uninsured, are not registered in the University's name, and are held by either the counterparty or the counterparty's trust department or agent.

The University does not have a formal investment policy that addresses custodial credit risk. However, the University's custodial credit risk is estimated to be minimal based on the expressed investment policies of PMIB, KDFA and the Foundation.

Concentration of Credit Risk is the risk of loss attributed to the magnitude of the University's investment in a single issuer that exceeds 5 percent or more of its total investments. Investments issued or explicitly guaranteed by the U.S. Government and investments in mutual funds, external investment pools, and other pooled investments are excluded from this requirement.

Kansas State University

Notes to Financial Statements (Continued)
For the Year Ended June 30, 2007

Note 3 – Capital Assets

Capital asset activity for the University for the year ended June 30, 2007 is summarized as follows:

	Beginning Balance	Additions	Retirements	Ending Balance
Capital Assets (not depreciated)				
Land and Improvements	7,399,668	1,580,663	-	8,980,331
Art Collections	1,953,150	5,008	-	1,958,158
Construction in Progress	62,477,507	47,345,726	100,724,573	9,098,660
Capital Assets (being depreciated)				
Buildings & Improvements	407,572,256	129,058,731	714,251	535,916,736
Land Improvements	17,545,528	450,909	11,490	17,984,947
Infrastructure	7,984,691	378,150	-	8,362,841
Equipment and Furnishings	140,643,710	10,799,690	8,422,333	143,021,067
Vehicles	21,261,186	1,312,723	855,917	21,717,992
Total Capital Assets	666,837,696	190,931,160	110,728,564	747,040,732
Accumulated Depreciation				
Buildings & Improvements	212,843,594	11,457,160	712,824	223,587,930
Land Improvements	7,101,963	688,096	8,472	7,781,587
Infrastructure	4,336,941	229,897	-	4,566,838
Equipment and Furnishings	99,664,177	10,070,128	7,753,517	101,980,788
Vehicles	19,415,889	821,803	840,605	19,397,087
Total Depreciation	343,362,564	23,267,084	9,315,418	357,314,230
Capital Assets, net	323,475,132	167,664,516	101,413,146	389,726,502

The University elected not to capitalize its library book collections. These collections adhere to the University's policy to (a) maintain them for public exhibition, education, or research; (b) protect, keep encumbered, care for, and preserve them; and (c) require proceeds from their sale to be used to acquire other collection items. Generally accepted accounting principles permit collections maintained in this manner to be charged to operations at the time of purchase rather than be capitalized.

Kansas State University

Notes to Financial Statements (Continued) For the Year Ended June 30, 2007

Note 4 – Accounts Receivable

Accounts receivable are shown net of allowances for doubtful accounts in the accompanying Statement of Net Assets. At June 30, 2007, accounts receivable consisted of the following:

	<u>June 30, 2007</u>
Student tuition and fees	\$ 6,353,513
Auxiliary enterprises and other operating activities	3,810,149
Federal, state, and private grants and contracts	15,067,601
Interest	<u>527,361</u>
	\$25,758,624
Less allowance for doubtful accounts	<u>1,789,582</u>
Net accounts receivable	\$23,969,042

Note 5 – Loans Receivable

Student loans made through the Federal Perkins Loan Program and the Health Profession Student Loan Program comprise substantially all of the June 30, 2007 loan balances. The Programs provide for cancellation of a loan at rates of 10% to 30% per year up to a maximum of 100%, if the participant complies with certain provisions. The federal government reimburses the University for amounts cancelled under these provisions.

As the University determines that loans are uncollectible and not eligible for reimbursement by the federal government, the loans are written off and assigned to the U.S. Department of Education. The University has provided an allowance for uncollectible loans, which, in management's opinion, is sufficient to absorb loans that will ultimately be written off. At June 30, 2007, the allowance for uncollectible loans was approximately \$1,220,000.

Note 6 – Deferred Revenue

Deferred revenues consist primarily of summer session tuition and fees and advance collections on grants and contracts. The breakdown of deferred revenues is as follows:

Tuition and fees	\$	4,110,598
Grants and contracts		<u>16,053,643</u>
		<u>\$20,164,241</u>

Note 7 – Long-Term Liabilities

Long-term liability activity for the year ended June 30, 2007 consists of the following:

	Beginning			Ending	Current
	Balance	Additions	Deductions	Balance	Portion
Revenue bonds payable	\$123,115,000	\$27,750,000	\$ 4,985,000	\$145,880,000	\$4,570,000
Loans payable	3,696,812		1,231,159	2,465,653	1,350,000
Lease obligations	2,489,661	780,684	1,551,779	1,618,466	611,511
Deposits held in custody for others	830,329	3,209,898	3,295,093	745,134	745,134
Other liabilities	5,603,412		1,430,946	4,172,466	756,187
Total Long-Term Liabilities	\$135,735,214	\$31,740,582	\$12,593,977	\$154,881,719	\$8,032,832

Kansas State University

Notes to Financial Statements (Continued)
For the Year Ended June 30, 2007

Note 8 – Revenue Bonds Outstanding

Revenue bonds payable consisted of the following at June 30, 2007:

	Principal Outstanding 6/30/07
Kansas Development Finance Authority Revenue Bonds-Series 2007A (The Kansas Board of Regents – Kansas State University Housing System, Manhattan Campus) issued on February 1, 2007 in the original amount of \$27,575,000. Due in annual installments beginning 10/1/07 with final maturity on 4/1/37. Interest ranging from 3.75% to 4.39% payable semi-annually.	\$27,750,000
Kansas Development Finance Authority Revenue Bonds-Series 2005D (The Kansas Board of Regents – Kansas State University Research and Development Facilities Projects) issued on May 1, 2005 in the original amount of \$20,980,000. Due in annual installments beginning 4/1/07 with final maturity on 10/1/21. Interest ranging from 3.90% to 5.15% payable semi-annually.	\$18,680,000
Kansas Development Finance Authority Revenue Bonds-Series 2005A (The Kansas Board of Regents – Kansas State University Housing System, Manhattan Campus) issued on February 1, 2005 in the original amount of \$44,535,000. Due in annual installments beginning 10/1/06 with final maturity on 4/1/35. Interest ranging from 3.00% to 5.00% payable semi-annually.	\$43,695,000
Kansas Development Finance Authority Revenue Bonds-Series 2003J-1 (The Kansas Board of Regents – Kansas State University Energy Conservation Projects) issued on August 1, 2003 in the original amount of \$21,020,000. Due in annual installments beginning 8/1/05 with final maturity on 8/1/23. Interest ranging from 4.25% to 5.00% payable semi-annually.	\$18,800,000
Kansas Development Finance Authority Revenue Bonds-Series 2003C (The Kansas Board of Regents – Kansas State University Research and Development Facilities Projects) issued on February 1, 2003 in the original amount of \$22,485,000. Due in annual installments beginning 10/1/22 with final maturity on 10/1/32. Interest ranging from 4.75% to 5.00% payable semi-annually.	\$22,485,000
Kansas Development Finance Authority Refunding Revenue Bonds- Series 2001G-1 (The Kansas Board of Regents – Kansas State University Salina Housing Project) issued on June 15, 2001 in the original amount of \$845,000. Due in annual installments with final maturity on 4/1/14. Interest ranging from 4.25% to 5.00% payable semi-annually.	\$ 540,000
Kansas Development Finance Authority Refunding Revenue Bonds- Series 2001G-2 (The Kansas Board of Regents – Kansas State University Recreation Project) issued on June 15, 2001 in the original amount of \$6,385,000. Due in annual installments with final maturity on 4/1/13. Interest ranging from 4.25% to 5.00% payable semi-annually.	\$ 3,910,000

Kansas State University

Notes to Financial Statements (Continued) For the Year Ended June 30, 2007

Revenue bonds payable consisted of the following at June 30, 2007:

	Principal Outstanding 6/30/07
Kansas Development Finance Authority Revenue Bonds-Series 2000D (The Kansas Board of Regents – Kansas State University Ackert Hall Addition Project) issued on July 15, 2000 in the original amount of \$1,735,000. Due in annual installments with final maturity on 5/1/15. Interest ranging from 4.60% to 5.60% payable semi-annually.	\$ 1,140,000
Kansas Development Finance Authority Revenue Bonds-Series 1998B (The Kansas Board of Regents – Kansas State University Student Union Renovation and Expansion Project) issued on April 1, 1998 in the original amount of \$9,320,000. Due in annual installments with final maturity on 4/1/18. Interest ranging from 3.90% to 5.00% payable semi-annually.	\$ 6,490,000
Kansas Development Finance Authority Revenue Bonds-Series 1995K (The Kansas Board of Regents – Kansas State University Farrell Library Expansion Project) issued on November 1, 1995 in the original amount of \$3,835,000. Due in annual installments with final maturity on 10/1/15. Interest ranging from 3.75% to 5.40% payable semi-annually.	\$ 2,390,000

Series 2001G-2 Recreation Project, Series 1995K Farrell Library Expansion Project, and Series 1998B Student Union Renovation and Expansion Project are collateralized by a pledge of student fees. Series 2001G-1 Salina Housing Project, Series 2005A Housing System Manhattan Campus, and Series 2007A Housing System Manhattan Campus are collateralized by a pledge of housing revenues. Series 2000D Ackert Hall Addition Project is collateralized by a pledge of sponsored research overhead revenues. Series 2003C and Series 2005D Research and Development Facilities Projects are collateralized by a pledge of State appropriations and various university revenue funds. Series 2003J-1 Energy Conservation Projects are collateralized by the annual utility and maintenance savings realized by the implementation of the energy improvement projects.

Future debt service requirements for all bonds outstanding at June 30, 2007 are as follows:

Year Ending June 30:	Principal	Interest	Total
2008	\$ 4,570,000	\$ 6,678,986	\$ 11,248,986
2009	4,880,000	6,387,036	11,267,036
2010	5,085,000	6,197,939	11,282,939
2011	5,320,000	5,995,797	11,315,797
2012	4,830,000	5,787,091	10,617,091
2013-2017	25,525,000	25,472,755	50,997,755
2018-2022	26,110,000	19,549,040	45,659,040
2023-2027	24,180,000	13,476,999	37,656,999
2028-2032	27,820,000	7,710,028	35,530,028
2033-2037	17,560,000	1,755,904	19,315,904
Total	\$145,880,000	\$ 99,011,575	\$ 244,891,575

Kansas State University

Notes to Financial Statements (Continued) For the Year Ended June 30, 2007

Note 9 – Loan and Lease Obligations

In July 2003, Kansas State University and the Pooled Money Investment Board entered into a construction loan agreement for the Biological and Industrial Value Added Program for a maximum amount of \$4,000,000. The loan requires annual interest payments due August 1 of each year in which a principal balance remains outstanding, at a rate of 1.548% per annum. The entire principal balance is due August 1, 2007. As of June 30, 2007, \$3,875,000 had been borrowed and \$2,525,000 in principal payments had been made, leaving an outstanding balance of \$1,350,000.

In June 2000, the University and the KSU Foundation entered into a 15 year financing agreement for the purchase of the Educational and Agricultural Research Facility located in Finney Co. in the amount of \$820,000. Annual payments are due June 1 with semi-annual interest payments due June 1 and December 1 at an interest rate ranging from 5.00% to 6.25%. The outstanding balance at June 30, 2007 is \$545,000.

In October 1997, the University and the KSU Foundation entered into a 10 year agreement for the purchase of the Harbin Residence Hall in the amount of \$2,000,820. Annual payments are due December 1, with an outstanding balance at June 30, 2007 of \$570,653.

In December 2002, the University and the KSU Foundation entered into a 15 year capital lease agreement for the KSU Printing Services building in the amount of \$825,000. Annual lease payments of \$84,899 are due July 31, with an outstanding balance at June 30, 2007 of \$442,956.

The University is obligated for the purchase of certain equipment funded through the State of Kansas Equipment Lease Purchase Program in the amount of \$1,175,510 as of June 30, 2007. Payments to liquidate these obligations are scheduled as follows:

Year Ending June 30:	Total
2008	\$ 526,612
2009	333,178
2010	103,211
2011	103,211
2012	94,563
2013	<u>14,735</u>
	\$1,175,510

Note 10 – Retirement Plans

The University participates in one cost-sharing multiple-employer defined benefit pension plan, one defined contribution pension plan, and one federal pension plan.

Defined Benefit Plan

Classified employees participate in the Kansas Public Employees Retirement System (KPERS). Benefit provisions are established by state statute and provide retirement, disability, and death benefits to benefits eligible employees. KPERS issues a publicly available annual financial report that includes its financial statements and required supplementary information and is available upon request from KPERS.

For the year ended June 30, 2007, active KPERS members were required by statute to contribute 4% and the University to contribute 5.77% of the employees' covered payroll. The Kansas Legislature establishes and may amend active plan members' and the University's contribution rates. The University contributed \$2,572,718 during fiscal year 2007 and individual employees contributed \$1,774,235. In addition, payments to KPERS for death and disability coverage for all University employees totaled \$2,245,687.

Kansas State University

Notes to Financial Statements (Continued) For the Year Ended June 30, 2007

Defined Contribution Plan

Eligible unclassified employees are required to participate in the Kansas Board of Regents (Regents) defined contribution retirement plan, which was authorized by K.S.A. 74-4925. The Regents have selected the following companies to provide investment options to participants: 1) Teachers Insurance and Annuity Association/College Retirement Equities Fund (TIAA/CREF), 2) ING Financial Advisers, 3) Lincoln National Life Insurance Company, and 4) Security Benefit Life Insurance Company. Benefits under these plans depend solely on the contributed amounts and the returns earned on the investment of those contributions. All contributions are fully vested with the first contribution.

For the year ended June 30, 2007 active members were required by statute to contribute 5.5% and the University to contribute 8.5% of the employees' covered payroll. The Kansas Legislature establishes and may amend active plan members' and the University's contribution rates. The University contributed \$14,259,556 during fiscal year 2007 and individual employees contributed \$9,080,971.

Federal Retirement Plan

Some Extension Service employees at Kansas State University hold Federal appointments. Prior to December 31, 1986, Federal appointees were required to participate in the Federal Civil Service Retirement System (CSRS), a defined benefit plan. CSRS employees are subject to the Hospital Insurance portion of FICA, the CSRS employee deduction of 7.0%, and the employer contribution of 7.0%.

The Federal Employees Retirement System (FERS), also a defined benefit plan, was created beginning January 1, 1987. Employees hired after December 31, 1983 were automatically converted to FERS. Other Federal employees not covered by FERS had a one-time option to transfer to FERS up to December 31, 1987. New FERS employees contribute 0.8% with an employer contribution rate of 11.2%. FERS employees contribute at the full FICA rate. They also participate in a Thrift Savings Plan with an automatic employer contribution of 1%. Employees may also contribute to this plan at variable rates, in which case the employer contributes at a variable rate up to 4%. CSRS employees are also eligible for participation in the Thrift Savings Plan, but without employer contributions. Acceptance of new member participation was terminated effective July 1, 1986.

For the year ended June 30, 2007, the University contributed \$871,575 and individual employees contributed \$731,628 to these plans.

Voluntary Tax-Sheltered Annuity Program

Employees may also elect to participate, up to the maximum dollar amount permitted by the Internal Revenue Code, in a voluntary tax-sheltered annuity program. This voluntary plan permits employees to designate a part of their earnings into tax-sheltered investments and thus defer federal and state income taxes on their contributions and the accumulated earnings under the plan. Participation and the level of employee contributions are voluntary. The employer is not required to make contributions to the plan.

Note 11 – Postemployment Benefits

In addition to pension benefits, the State provides post-employment health care benefits to eligible retired employees. The benefits are provided in accordance with the rules and regulations of the Kansas State Employees Health Care Commission. The Commission is responsible for the determination of the allocation of premium costs between the participants and the State. These allocations are subject to change each contract year. The University funds the benefits on a pay-as-you-go basis.

Kansas State University

Notes to Financial Statements (Continued) For the Year Ended June 30, 2007

Note 12 – Commitments and Contingencies

At June 30, 2007, the University had outstanding commitments on various construction projects and contracts for repairs and renovation of facilities of approximately \$13,100,000.

The University is a defendant in several lawsuits. However, University officials are of the opinion, based on advice of in-house legal counsel, that the ultimate outcome of all litigation will not have a material effect on the future operations or financial position of the University.

As a result of legislation, the University, as an agency of the State of Kansas, is subject to the state of Kansas' self-insurance program with regard to comprehensive general liability and personal injury insurance. The University is covered by the State's umbrella insurance policies for automobile liability and property insurance. Also, the University is self-insured relative to workers' compensation, medical, and unemployment insurance. These areas include stop-loss provisions that limit the University's exposure.

In the normal course of operations, the University receives grants, contracts, and other forms of reimbursement from various federal and state agencies. These activities are subject to audit and disallowance by agents of the funding authority, the purpose of which is to ensure compliance with conditions precedent to providing such funds. University officials believe that the liability, if any, for any reimbursement that may arise as the result of audits, would not have a material effect on the University's financial position.

Note 13 – Operating Expenses by Natural Classification

Year Ended June 30, 2007

	Compensation and Benefits	Contractual Services	Supplies and Materials	Utilities	Scholarships and Fellowships	Aid, Debt and Nonexpense	Depreciation	Total
Instruction	\$ 130,738,462	\$ 13,812,803	\$ 6,337,850	\$ 469		\$ 2,077,444		\$ 152,967,028
Research	70,616,604	16,968,234	14,924,804	281,236		4,096,651		106,887,529
Public Service	44,252,206	7,590,486	4,700,846	22,918		3,202,411		59,768,867
Academic Support	28,124,679	9,212,415	4,560,355			153,365		42,050,814
Student Service	13,659,132	3,307,212	734,759	4,402		1,862,863		19,568,368
Institutional Support	16,963,167	7,073,695	603,432			757,688		25,397,982
Operations and Maintenance of Plant	15,944,327	3,212,699	2,251,651	11,447,923		52,172		32,908,772
Scholarships & Fellowships					12,660,501			12,660,501
Auxiliary Enterprises	17,652,422	3,859,906	5,935,634	1,909,376		48,047		29,405,385
Depreciation							23,267,084	23,267,084
Other		558,116	250,396					808,512
Total Operating Expenses	\$ 337,950,999	\$ 65,595,566	\$ 40,299,727	\$ 13,666,324	\$ 12,660,501	\$ 12,250,641	\$ 23,267,084	\$ 505,690,842

Kansas State University

Notes to Financial Statements (Continued)
For the Year Ended June 30, 2007

Note 14 – Component Units

Buildings and improvements purchased by The Intercollegiate Athletic Council immediately become the property of Kansas State University. This results in a negative amount being reported for Invested in Capital Assets, Net of Related Debt on the Statement of Net Assets.

Note 15 – Prior Period Adjustment

During FY2007, the University reviewed and corrected several calculations related to capital assets and related debt. A portion of prior year interest expense was capitalized and debt obligations related to certain buildings were recorded as a liability. The effect of these corrections was an increase to capital assets, liabilities, and investment in capital assets, net of debt by \$2,756,251.

Note 16 – Subsequent Event

In August 2007, Kansas Development Finance Authority issued the Kansas State University Parking System Revenue Bonds, Series 2007H in the amount of \$17,855,000 on behalf of Kansas State University. These bonds will bear interest at varying rates between 3.6% and 4.5% with semi-annual interest installments beginning November 1, 2007 and final maturity on May 1, 2037. The proceeds of these bonds will be used to finance the construction and equipping of a new parking structure on the Manhattan campus and are collateralized by the pledge of Parking System fees and charges.

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Kansas State University is committed to nondiscrimination on the basis of race, sex, national origin, disability, religion, age, sexual orientation, or other nonmerit reasons, in admissions, educational programs or activities and employment (including employment of disabled veterans and veterans of the Vietnam Era), as required by applicable laws and regulations. Responsibility for coordination of compliance efforts and receipt of inquiries concerning Title VI of the Civil Rights Act of 1964, Title IX of the Education Amendments of 1972, Section 504 of the Rehabilitation Act of 1973, the Age Discrimination Act of 1975, and the Americans With Disabilities Act of 1990, has been delegated to Clyde Howard, Director of Affirmative Action, Kansas State University, 214 Anderson Hall, Manhattan, KS 66506-0124, (Phone) 785-532-6220; (TTY) 785-532-4807.