VERMONT STATE COLLEGES
(a Component Unit of the State of Vermont)

FINANCIAL STATEMENTS AND MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2014

VERMONT STATE COLLEGES
(a Component Unit of the State of Vermont)

Financial Statements and Management's Discussion and Analysis

June 30, 2014 and 2013

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O'Connor & Drew P.C.
Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

To the Board of Trustees of
Vermont State Colleges
Montpelier, Vermont

Report on the Financial Statements

We have audited the accompanying financial statements of the Vermont State Colleges (a component unit of the State of Vermont) (the "Colleges"), which comprise the statements of net position as of June 30, 2014 and 2013, the related statements of revenues and expenses, changes in net position and cash flows for the years then ended, and the related notes to the financial statements, which collectively comprise the Colleges' basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Vermont State Colleges at June 30, 2014 and 2013 and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Emphasis of a Matter

As discussed in Note 2 to the financial statements, Vermont State Colleges restated prior balances with regards to the adoption of GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. Our opinion is not modified with respect to that matter.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that management's discussion and analysis on pages 3-18 and the schedule of funding progress on page 55 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 22, 2014, on our consideration of Vermont State Colleges' internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audits.

O'Connor and Drew, P.C.

Certified Public Accountants
Braintree, Massachusetts

October 22, 2014

Introduction

The Management's Discussion and Analysis (MD&A) is required supplemental information due to the Governmental Accounting Standards Board (GASB) reporting model. It is designed to help the reader's understanding of the accompanying financial statements and notes. As this MD&A contains summarized information, tables and graphs, it should be read in conjunction with the accompanying financial statements and notes.

Vermont State College System

The Vermont State College System unites five distinctive public colleges in the common purposes of providing first-rate higher education at reasonable cost in order to improve the quality of life for the citizens of Vermont.

The colleges are:
Community College of Vermont (CCV)
Castleton State College (CSC)
Johnson State College (JSC)
Lyndon State College (LSC)
Vermont Technical College (VTC)

Using the Financial Statements

The following discussion and analysis provides an overview of the financial statements and activities of Vermont State Colleges (VSC) for the year ended June 30, 2014 and selected comparative information for the previous 4 years. Since this MD&A is designed to focus on current activities, resulting changes and currently known facts, please read in conjunction with the financial statements and notes that follow this section.

These financial statements have been prepared in accordance with GASB principles. In June 1999, GASB released Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis*. Changes in Statement No. 34 compared to prior GASB pronouncements require a comprehensive consolidated look at the entity as a whole, as well as capitalization and depreciation of assets. In November 1999, GASB issued Statement No. 35, *Basic Financial Statements and Management's Discussion and Analysis for Public Colleges and Universities*. This essentially applies Statement No. 34 to public colleges and universities. Previously, the financial statements focused on the individual fund groups rather than VSC as a whole.

A brief explanation of each financial statement required by the GASB reporting model follows:

Financial Statements

The Vermont State College System's financial statements include three primary components:

- Statement of Net Position (SNP)
- Statement of Revenues and Expenses and Changes in Net Position (SRECNP)
- Statement of Cash Flow (SCF)

Statement of Net Position

The Statement of Net Position presents the financial position of VSC at one point in time - June 30, and includes all assets, liabilities, and the net position of the System. Net position represents the residual interest in the System's assets after liabilities are deducted. The change in net position is an indicator of whether the overall financial condition has improved or deteriorated during the year. Table 1 on page 5 shows the condensed Statement of Net Position for the past five years.

Significant events that affect these statements during the past five years include: accrual of other post-employment benefits (OPEB) totaling over $40 million through FY2014, which is not being funded at this time; the maturing of a Certificate of Deposit that was considered long term cash, and subsequent new investments in FY2013 are broken up between short term and long term investments; debt financing secured for constructions projects in FY2008 and FY2010, with construction projects placed in service through FY2013; enrollments leveling off and in some instances declining at the end of this period.

Total assets are categorized as either current or noncurrent. Current assets are available to satisfy current liabilities, which are those amounts expected to be payable within the next year. The major component of current assets is accounts receivable, primarily funds due by students and granting agencies. Total assets of $269 million decreased by $7 million or 2% from FY2013 to FY2014, primarily in Capital Assets due to depreciation. Over the 5 years, Assets have grown by $29 million, primarily in Capital Assets constructed using bond financing.

Noncurrent assets consist primarily of endowment and other investments, in addition to capital assets. Investments were $55 million at June 30, 2014, an increase of $4 million or 8% since June 30, 2013 – this increase was primarily from investment returns. At the beginning of the 5-year period, current assets included the CD which matured in FY2012. Invested funds from this CD are now reflected in Long Term investments.

Current liabilities of $22 million and $23 million as of June 30, 2014 and 2013 respectively include primarily accounts payable, and unearned revenue related to the next fiscal year. Current liabilities have not changed significantly from FY2010.

Statement of Net Position - Continued

Noncurrent liabilities increased by $3 million to $194 million during FY2014. An increase in post-employment benefits liability of $6 million was partially offset by a decrease in long term debt of $4 million. During the 5-year period, OPEB liability has increased steadily. Bonds payable increased due to new bonds issued during this time, but have begun to decline as bond holders are being paid.

TABLE 1: Condensed Statement of Net Position as of June 30

($ in millions)

	2014	% change	2013	% change	2012	2011	2010
Current Assets	21	-19%	26	-60%	65	84	40
Noncurrent Assets							
Investments	55	8%	51	155%	20	19	28
Capital assets, net	187	-4%	194	7%	181	161	155
Other	6	20%	5	-19%	10	13	18
Deferred outflows	11	0%	11	-35%	17	8	10
Total Assets and Def'd outflows	280	-2%	287	-2%	293	285	251
Current liabilities	22	-4%	23	-12%	26	24	26
Non current liabilities							
Post employm't benefit oblig	49	14%	43	19%	36	28	22
Bonds and Notes payable	127	-3%	131	-4%	136	141	115
Other	18	6%	17	-26%	23	15	17
Total Liabilities	216	1%	214	-3%	221	208	180
Net investment in cap'l assets	60	-9%	66	27%	52	52	51
Restricted							
Nonexpendable	16	7%	15	0%	15	13	12
Expendable	10	25%	8	33%	6	6	3
Unrestricted	-22	38%	-16	1500%	-1	6	5
Total Net Position	64	-12%	73	1%	72	77	71
Total Liabilties and Net Positior	280		287		293	285	251

Statement of Net Position - Continued

Net Position

Net investment in capital assets represents the historical cost of the System's capital assets reduced by total accumulated depreciation and outstanding principal balances on debt attributable to the acquisition, construction, or improvement of those assets.

Total net position decreased from $73 million to $64 million or 13% from June 30, 2013 to June 30, 2014. It generally increased from FY2010 to FY2013, with a blip in FY2011 related to the timing of borrowings vs use of debt for capital assets.

Net investment in capital assets decreased by $6 million from June 30, 2013 to June 30, 2014 due to a net change downward in capital assets of $8 million less a decrease in principal owed on construction debt of $2 million. Net investment in capital assets increased during the prior years during a period of capital construction.

The restricted nonexpendable portion of Net Position represents the permanent endowment funds for the system. The increase of $1 million in FY2014 and $4 million over 5 years is due to gifts received for endowments during the period.

The restricted expendable portion of Net Position includes unexpended gifts and grants, and unexpended endowment appreciation, above corpus, subject to externally imposed conditions on spending. The increase of $2 million from June 30, 2013 to June 30, 2014 is due to return on endowment investments. In FY2010, endowment fund earnings were depleted due to the downturn in the market. The earnings have recovered over this 5-year period. The balance of unexpended gifts and grants has remained stable throughout this period.

The unrestricted portion of the Net Position is affected primarily by OPEB obligations, which are unfunded. That liability increased by $6 million in FY2014 to $49 million as of June 30, 2014. Since FY2010, the unrestricted net position has declined by $27 million as post-employment benefit obligations are recorded.

During FY2014 the system's total Net Position declined from $73 million to $64 million. This is due primarily to our unrestricted net assets being reduced from the annual booking of the VSC OPEB liability. The details of this change are shown in the Statement of Revenues, Expenses, and Changes in Net Position beginning on page 8.

Capital Assets and Debt Administration

The System's facilities are critical to accomplishing the mission of the System as they provide the physical framework and environment for educational, research, cultural programs and residential life. Table 2 on page 7 provides detail from the past 5 years related to the Capital Assets held by the System.

Statement of Net Position - Continued

Capital Assets and Debt Administration - Continued

Construction in Progress reflects amounts paid for buildings or other assets that are not completed at year end. When completed and placed in service, the total cost is moved to the appropriate capital asset category. Depreciation of that asset begins the month after it is placed in service.

During the 5-year period, there was significant construction done at all five colleges, funded by debt acquired in FY2008 and FY2010. Construction in Progress increased during the years of construction, representing construction not completed on June 30. During FY2014 as construction projects were completed Construction in Progress returned to an amount similar to FY2010. Building and Improvements increased throughout the period, reflecting the completed projects. Infrastructure includes water & sewer systems, heating & electrical systems, telecommunication systems, and roads. The increase in infrastructure over the five-year period is due to projects on the campuses as well as enhanced communications systems for the entire System. Equipment shows a significant increase in FY2013 due to a donation of software valued at $12 million. Table 2 provides detail about Capital Assets, including related information (depreciation expense and outstanding principal on construction loans).

Table 2: Capital Assets as of June 30
($ in millions)

	2014	% Change	2013	% Change	2012	2011	2010
Land	6	0%	6	0%	6	6	6
Construction in progress	3	-63%	8	14%	7	7	4
Infrastructure	38	6%	36	3%	35	33	31
Buildings and improvements	250	4%	241	3%	233	210	203
Leasehold improvements	2	0%	2	0%	0	0	
Equipment	32	3%	31	82%	17	15	15
Total Capital Assets	331		324		298	271	259
Accumulated Depreciation	-144	12%	-129	10%	-117	-110	-104
Capital Assets, Net	187		195		181	161	155
Related information							
Depreciation Expense	14	8%	13	63%	8	8	7
Outstanding Principal, Related Loans	131	-3%	135	-4%	141	146	119

VERMONT STATE COLLEGES
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Management's Discussion and Analysis (Unaudited) - Continued

June 30, 2014 and 2013

Statement of Revenues, Expenses, and Changes in Net Position

The Statement of Revenues, Expenses, and Changes in Net Position reports total operating revenues, operating expenses, non-operating revenues and expenses, and other changes in net position, showing the total change in net position for the fiscal year. Table 3 shows the Condensed Statements of Revenues, Expenses, and Changes in Net Position for the past five fiscal years.

Table 3: Condensed Statements of Revenues, Expenses, and Changes in Net Position

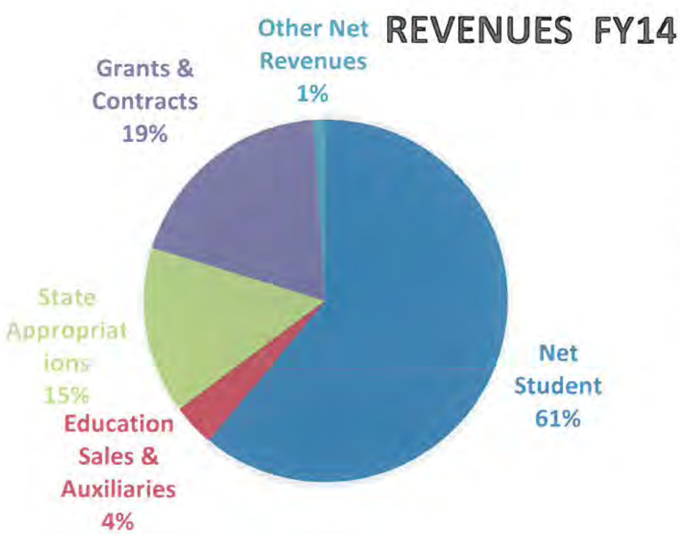
($ in millions)

	2014	% Change	2013	% Change	2012	2011	2010
Net Student Fees	112	0%	112	2%	110	105	103
Grants and contracts	15	0%	15	0%	15	15	15
Other Operating Revenues	8	0%	8	14%	7	8	8
Operating Revenues	135	0%	135	2%	132	128	126
Operating Expenses	195	1%	194	5%	185	179	174
Operating Loss	-60	2%	-59	11%	-53	-51	-48
Nonoperating Revenues (Expenses)							
Non Capital Appropriations	27	4%	26	0%	26	28	29
Federal Grants & Contracts	20	0%	20	0%	20	22	18
Gifts currently expendable	3	0%	3	50%	2	2	3
Investment Income & Interest	4	100%	2	100%	1	6	4
Interest Expense	-6	0%	-6	0%	-6	(6)	-5
Other nonoperating revenues	0	0%	0	-100%	1	1	0
Net Nonoperating Revenues	48	7%	45	2%	44	53	49
Total Change before other Revenues	-12	-14%	-14	56%	-9	2	1
Other Changes in Net Position							
Capital Appropriation	2	-50%	4	100%	2	3	5
Capital gifts and grants	0	-100%	13	-	0	-	0
Endowment gifts	1	0%	0	0%	1	1	1
Change in Net Position	-9	-400%	3	-150%	-6	6	7

Statement of Revenues, Expenses, and Changes in Net Position – Continued

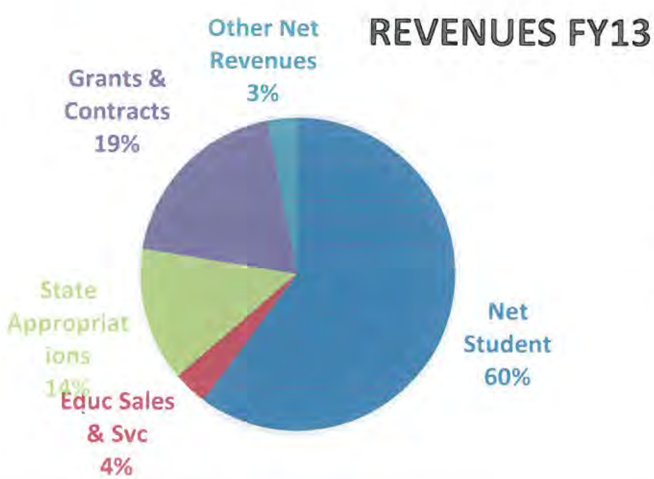
Operating and Non-operating Revenue

Accounting rules require that our audited financial statements include operating revenues, operating expenses and non-operating revenues and expenses. The following sections provide an analysis of the total operating and non-operating revenues and expenses. The VSC's primary source of revenue is from student fees. This accounts for 60% of operating and non-operating income. In addition, the System receives revenue from governmental and privately funded grants and contracts; gifts from individuals, foundations, and corporations; and investment income.



FY2014 Revenues
($ in thousands)

Net Student	$111,611
Educational Sales/Aux	6,766
State Appropriations	27,331
Grants & Contracts	35,053
Other Net Revenues	2,265
TOTAL	$183,026



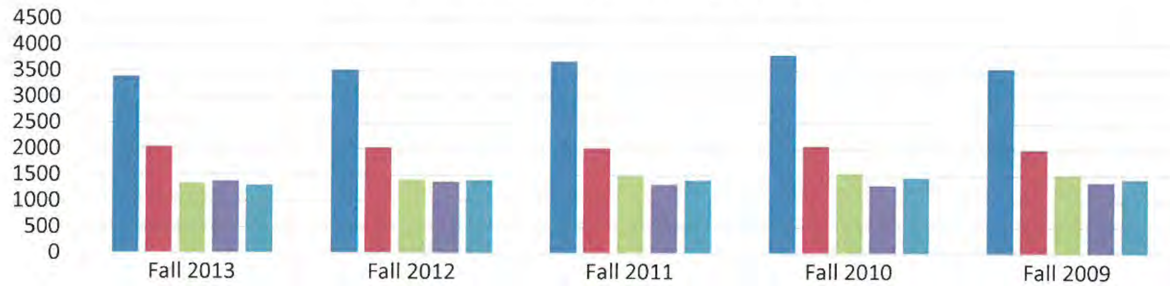
FY2013 Revenues
($ in thousands)

Net Student	$111,681
Educational Sales/Aux	6,488
State Appropriations	25,892
Grants & Contracts	35,931
Other Net Revenues	5,841
TOTAL	$185,883

Statement of Revenues, Expenses, and Changes in Net Position - Continued

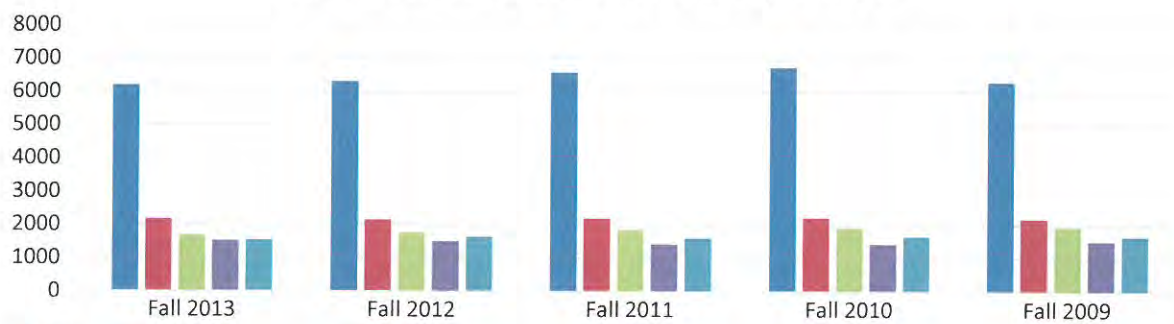
Tuition and Fee Revenue

Fall Enrollment by FTE by College



	Fall 2013	Fall 2012	Fall 2011	Fall 2010	Fall 2009
CCV	3387	3520	3685	3810	3550
CSC	2036	2024	2014	2057	1995
JSC	1343	1415	1493	1543	1528
LSC	1376	1374	1320	1304	1371
VTC	1302	1401	1405	1455	1433

Fall Enrollment by Headcount by College



	Fall 2013	Fall 2012	Fall 2011	Fall 2010	Fall 2009
CCV	6194	6311	6578	6738	6299
CSC	2175	2156	2192	2215	2191
JSC	1692	1783	1859	1924	1964
LSC	1519	1508	1422	1436	1521
VTC	1543	1645	1603	1656	1662

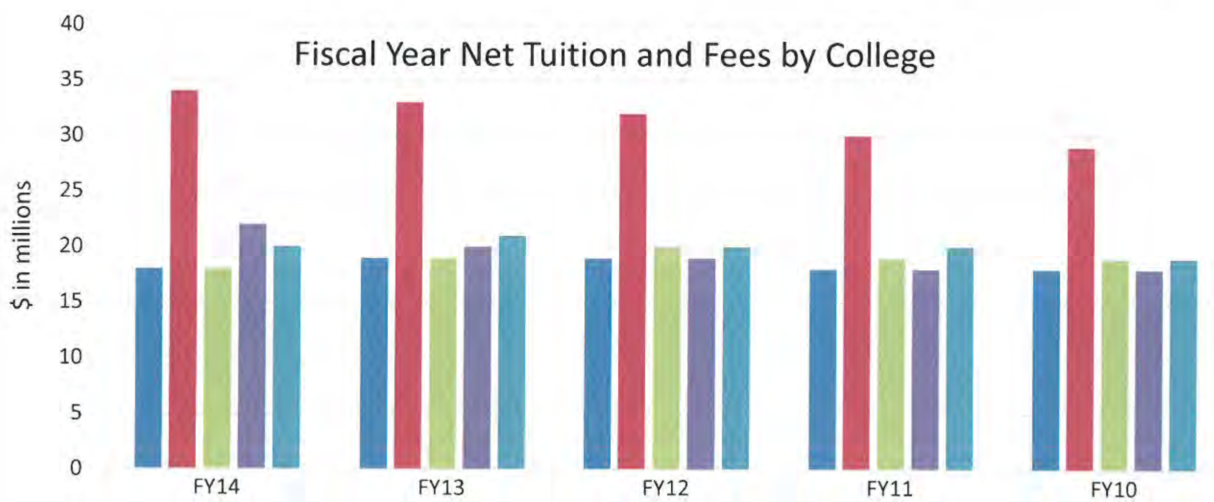
Net Tuition and fees includes tuition and fees plus residence and dining fees less scholarship allowances. Table 3 shows the trend for Tuition and Fee Revenue from FY2010 through FY2014. For the System, student-based revenue increased each year from FY2010 through FY2013.

Statement of Revenues, Expenses, and Changes in Net Position - Continued

Tuition and Fee Revenue - Continued

The charts on page 10 show student enrollment and revenues for each college during this 5 year period. Enrollments are displayed by both FTE and by Headcount. FTE (Full Time Equivalent) provides better comparative information and Headcount shows the total number of individuals who have benefited from VSC education.

The chart below displays Net Tuition and Fees for each college during the five-year period. It is notable that CCV has by far the largest number of students – both FTE and Headcount, but their net tuition is one of the lowest. CCV, as a Community College has the lowest tuition cost and charges for courses on a per credit basis, while the residential schools charge on a semester basis.



	FY14	FY13	FY12	FY11	FY10
CCV	18	19	19	18	18
CSC	34	33	32	30	29
JSC	18	19	20	19	19
LSC	22	20	19	18	18
VTC	20	21	20	20	19

Operating and Non-operating Expenses

Table 4 on page 12 shows the total Operating and Non-operating Expenses for the past 5 years, and the charts on pages 12-13 provide a quick view of the percent of expenses by type for FY2014 and FY2013.

Statement of Revenues, Expenses, and Changes in Net Position - Continued

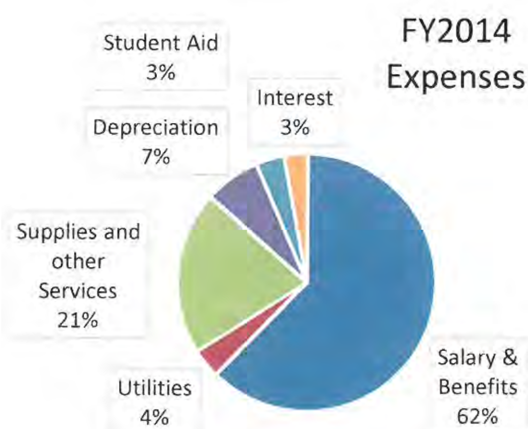
Operating and Non-operating Expenses - Continued

The largest percentage of VSC expenses are for salary and benefits (over 60%). Those expenses have continued to grow through the 5 year period, though there was a slight downturn in the growth last year. The only other expense that has increased significantly during this period is depreciation, related to construction projects in earlier years. Supplies and services is the second largest expense (21%), and there was a slight decrease in monies spent in this area in FY2014.

Included in Salaries and Benefits are annual accruals related to OPEB.

Table 4: Total Operating and Non-operating Expenses for Years Ended June 30
($ in millions)

	2014	% chang	2013	% change	2012	2011	2010
Operating							
Salaries & Benefits	125	2%	123	3%	120	116	112
Utilities	7	0%	7	0%	7	6	5
Supplies and Svcs	42	-2%	43	2%	42	40	42
Depreciation	14	8%	13	63%	8	8	8
Student Aid	7	-13%	8	0%	8	9	7
Total Operating	195		194		185	179	174
Nonoperating							
Interest on Debt	6	0%	6	0%	6	6	5
TOTAL Expenses	201	1%	200	5%	191	185	179

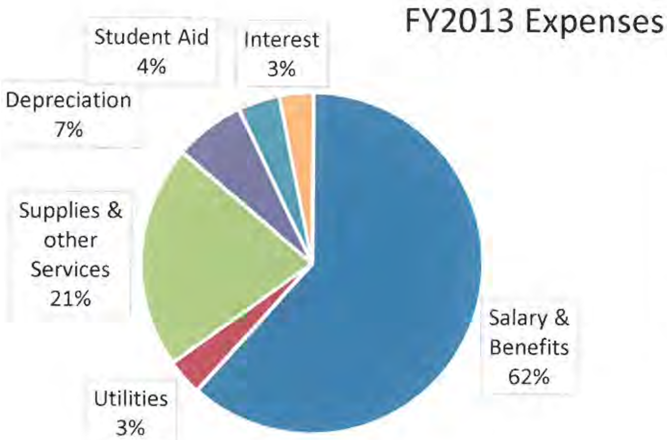


FY2014 Expenses
($ in thousands)

Salary/Benefits	$125,287
Utilities	7,289
Supplies/Services	41,491
Depreciation	14,030
Student Aid	7,191
Interest on Debt	5,916
TOTAL	$201,204

Statement of Revenues, Expenses, and Changes in Net Position – Continued

Operating and Non-operating Expenses - Continued



FY2013 Expenses
($ in thousands)

Salary/Benefits	$123,650
Utilities	6,926
Supplies/Services	42,568
Depreciation	13,238
Student Aid	8,008
Interest on Debt	6,435
TOTAL	$200,825

Student Financial Aid

Student financial aid awards are made from a variety of sources including federal, state, private, and system funds. Aid received from third parties is recognized as grants and contracts revenue on the Statements of Revenues, Expenses, and Changes in Net Position while the distribution of aid from all sources is shown as one of two components:

- Scholarship Allowances – financial aid retained by the System to cover students' tuition, fees, and on-campus housing and meals. These amounts are reported as a direct offset to operating revenues.
- Scholarships and Fellowships Expense – financial aid refunded to students to cover off-campus living costs, books, and other personal living expenses. These amounts are reported as operating expense.

Total student financial aid over the past five years is show below.

Table 5: Student Finance Aid
($ in millions)

	FY14	FY13	FY12	FY11	FY10
Scholarship Allowances (inc in revenue)	25	23	21	21	18
Scholarship Expenses (inc in expenses)	7	8	8	9	7
Total Student Aid	32	31	29	30	25

Statement of Cash Flows

The Statement of Cash Flows shows inflows and outflows of cash without regard to accrual items. The Condensed Statement for VSC is in Table 6 on page 15. The temporary blip in cash at the end of FY2012 is related to the maturation of a Certificate of Deposit. In the following fiscal year, these funds were moved into other investments.

Cash flows from operating activities

Cash flows from operating activities on the Statement of Cash Flows will always be different from the operating gain or loss on the Statement of Revenues, Expenses, and Changes in Net Position (SRECNP) because of the inclusion of noncash items, such as depreciation expenses on the SRECNP. Also, the SRECNP is prepared on the accrual basis of accounting, meaning that it shows revenues earned and expenses incurred. The primary cash receipts from operating activities consist of tuition and fees, grants and contracts, and auxiliary income from housing, food service and bookstore operations. Cash outlays include payment of wages and benefits; operating expenses such as utilities, supplies, insurance and repairs; and scholarship to students. During the last five fiscal years operating cash flow has been fairly consistent.

Cash flows from noncapital financing activities

There are two primary sources of noncapital financing: state appropriations and non-operating federal grants that fund PELL student grants. Accounting standards require that we reflect these sources of revenue as non-operating, even though each of the colleges depend on them to continue the current level of operations. Both the state operating appropriations and PELL grant funds from the federal government have been fairly consistent over the last 5 fiscal years.

Cash flows from capital and related financial activities

Cash flows from capital and related financing activities include all plant funds and related long term debt activities (except depreciation and amortization), as well as capital gifts, grants and appropriations. Purchase and sale of investments and income earned on investments are included in cash flows from investing activities.

Cash flows from investing activities

An item on the cash flow statement belongs in the investing activities section if it results from any gains (or losses) from investments in financial markets and operating subsidiaries. The activity from the last three fiscal years reflect the activity surrounding the VSC CD being liquidated and reinvested into other instruments, as well as activity related to endowment investments.

VERMONT STATE COLLEGES
(a Component Unit of the State of Vermont)

Management's Discussion and Analysis (Unaudited) - Continued

June 30, 2014 and 2013

Statement of Cash Flows - Continued

Table 6: Condensed Statements of Cash Flows
($ in millions)

Cash flows from:	2014	% change	2013	% change	2012	2011	2010
Operating	-42	-2%	-43	23%	-35	-41	-42
Non capital financing	51	4%	49	0%	49	53	50
Capital and related financing	-10	-17%	-12	-29%	-17	-21	-33
Investing	0	-100%	-29	-171%	41	-2	1
Net increase (decrease)	-1	-97%	-35	-192%	38	-11	-24
Cash, Beginning of Year	4	-90%	39	3800%	1	12	36
Cash, End of Year	3	-25%	4	-90%	39	1	12
Operating cash flows adding noncapital appropriations and PELL grants							
Operating	-42	-2%	-43	23%	-35	-41	-42
Non capital appropriations	27	4%	26	0%	26	28	29
Non operating federal grants	20	-5%	21	5%	20	22	18
Operating cash flows including appropriation and fed grants	5	25%	4	-64%	11	9	5

Consistent with accounting standards, cash flows from state operating appropriations and federal PELL grant revenue are included in noncapital financing activities, even though they provide funding for operating activities. The bottom section of Table 6 shows that with these revenue sources added to the operating cash flows, the result is positive cash flows in all years.

Economic Factors That Will Affect the Future

Demographic Trend

Vermont continues to experience a demographic decline in the overall number of graduating Vermont high school students. Accordingly, the VSC continues to proactively enhance its recruiting and retention efforts. Because the majority of VSC enrollees are Vermonters, this trend could continue to affect enrollment in future years. All of the colleges have adopted programs and strategies to better recruit in this shrinking market. In addition, the State of Vermont has been initiating programs that permit high school students to attend college, and get both high school and college credits for courses. The VSC has taken a lead in participating in these programs that will benefit the students by reducing the overall cost of college, as well as provide some additional revenue for the colleges. Each of the member colleges is working to develop strategies to deal with controlling tuition costs and initiatives are constantly under way to help reduce expenses. Due to the fact that wages and benefits account for a substantial part of expenses, VSC must continually strive to become more efficient in its operations.

Economic Factors That Will Affect the Future – Continued

Vermont State Appropriations
For FY2014, State Operating Appropriations were $27,331,000, or 15%, of total operating and non-operating revenues. VSC continues to rely on this important revenue source from the State of Vermont to help keep tuition as low as possible. For FY2014, in-state tuition increased 4% at Community College of Vermont (CCV), Castleton State College (CSC), Johnson State College (JSC) and Lyndon State College (LSC), and Vermont Technical College (VTC). FY2014 out-of-state tuition increased 4% at CCV, LSC and VTC while increasing 5% at JSC and 7% at CSC. VSC will continue to promote the cause of higher education to the State administration and legislature.

Post-Employment Benefits
GASB 45, or OPEB, which became effective in FY2008, requires the recognition of the employer costs of medical, prescription, dental and life insurance plans for all eligible employees during the period of their active employment rather than when the benefits are paid during their retirement. Because of VSC's unique early retirement wages benefit for the full-time faculty, VSC must also account for this liability under GASB 45.

The annual cost to VSC is equal to the actuarially calculated costs for the year and a component for the amortization of the unrecognized liability for the plan over a period not to exceed 30 years, less payments made to our self-insurance plan for current retirees and early retirement benefits paid to retired full-time faculty.

For financial reporting purposes, an actuarial valuation is required at least biennially for OPEB plans with total eligible employees (active, retirees and beneficiaries) of 200 or more. At each valuation time, the pattern of cost sharing between VSC and the employee as well as certain legal or contractual caps should be considered.

VSC's current actuarial study estimated that the accumulated value of prior benefits liability for the current list of employees, as of July 1, 2013, was approximately $135,345,000 for post-retirement health, dental and life insurance benefits and for early retirement benefits. The present value of all benefits (past and future obligations) is estimated to be $140,327,000.

Economic Factors That Will Affect the Future – Continued

Other Factors
As a result of positive market conditions during FY2014, VSC had net realized and unrealized gains on the endowments, and other investments.

Approximately 761 of the 1,090 full-time employees at VSC are covered by union contracts. VSC employs approximately 2,305 full and part-time employees.

VSC Employees as of November 1,2013

Bargaining Unit Employees	
Full Time	761
Part Time	203
TOTAL	964
Non-Bargaining Unit Employees	
Full Time	329
Part Time & Temp	1012
TOTAL	1341
TOTAL Employees	2305

VSC has contractual commitments for various construction projects currently under way. The funds have been set aside for these projects.

VERMONT STATE COLLEGES

(a Component Unit of the State of Vermont)

Statements of Net Position

June 30,

Assets and Deferred Outflows of Resources

	2014	(Restated) 2013
Current Assets:		
Cash and equivalents (Note 3)	**$ 2,451,670**	$ 3,446,616
Accounts receivable, net (Note 4)	**11,462,983**	11,296,610
Inventories	**452,563**	304,797
Deposit with bond trustees (Note 3)	**4,426,154**	7,710,558
Other current assets	**2,389,683**	2,868,378
Total Current Assets	**21,183,053**	25,626,959
Non-Current Assets:		
Cash and equivalents (Note 3)	**581,822**	783,947
Long-term investments (Note 3)	**54,972,307**	51,274,407
Notes receivable, net (Note 4)	**5,419,391**	5,223,078
Other assets	**52,260**	14,982
Capital assets, net (Note 11)	**186,999,848**	194,012,250
Total Non-Current Assets	**248,025,628**	251,308,664
Total Assets	**269,208,681**	276,935,623
Deferred Outflows of Resources:		
Interest rate swap, accumulated decrease in fair value (Note 5)	**10,674,356**	10,603,309
Total Assets and Deferred Outflows of Resources	**$ 279,883,037**	$ 287,538,932

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

Liabilities and Net Position

	2014	(Restated) 2013
Current Liabilities:		
Accounts payable and accrued liabilities (Note 12)	**$ 12,126,093**	$ 12,734,330
Unearned revenue and deposits	**6,663,699**	6,481,816
Current portion of long-term debt (Note 5)	**3,759,760**	3,637,524
Total Current Liabilities	**22,549,552**	22,853,670
Non-Current Liabilities:		
Accounts payable and accrued liabilities (Note 12)	**136,055**	220,129
Unearned revenue and deposits	**427,302**	798,016
Refundable grants	**6,044,136**	6,049,434
Post-employment benefit obligations (Note 9)	**48,943,729**	42,753,755
Interest rate swap (Note 5)	**10,674,356**	10,603,309
Long-term debt, excluding current portion (Note 5)	**127,176,209**	130,935,970
Total Non-Current Liabilities	**193,401,787**	191,360,613
Total Liabilities	**215,951,339**	214,214,283
Net Position:		
Investment in capital assets, net	**60,152,724**	65,590,456
Restricted nonexpendable	**16,497,265**	15,128,413
Restricted expendable	**10,279,496**	8,255,108
Unrestricted	**(22,997,787)**	(15,649,328)
Total Net Position	**63,931,698**	73,324,649
Total Liabilities and Net Position	**$ 279,883,037**	$ 287,538,932

VERMONT STATE COLLEGES
(a Component Unit of the State of Vermont)

Statements of Revenues and Expenses

For the Years Ended June 30,

	2014	(Restated) 2013
Operating Revenues:		
Tuition and fees	**$ 115,690,089**	$ 113,637,743
Residence and dining	**20,674,084**	20,651,576
Less: scholarship allowances	**(24,752,899)**	(22,608,571)
Net Tuition, Fees, and Residence and Dining Revenue	**111,611,274**	111,680,748
Federal grants and contracts	**11,917,991**	12,094,281
State and local grants and contracts	**2,144,216**	1,696,272
Non-governmental grants and contracts	**1,081,688**	1,343,831
Interest income	**87,029**	105,440
Sales and services of educational activities	**5,848,881**	5,529,267
Other auxiliary enterprises	**916,820**	959,296
Other operating revenues	**1,001,239**	1,535,602
Total Operating Revenues	**134,609,138**	134,944,737
Operating Expenses (Notes 6, 10 and 12):		
Salaries and wages	**82,488,029**	81,453,823
Employee benefits (Notes 8 and 9)	**42,798,448**	42,196,246
Scholarships and fellowships	**7,191,107**	8,007,863
Supplies and other services	**41,490,709**	42,567,893
Utilities	**7,289,372**	6,926,313
Depreciation (Note 11)	**14,030,027**	13,238,072
Total Operating Expenses	**195,287,692**	194,390,210
Net Operating Loss	**(60,678,554)**	(59,445,473)
Non-Operating Revenues (Expenses):		
State appropriations (Note 7)	**27,330,899**	25,891,792
Federal grants and contracts	**19,909,045**	20,797,045
Gifts	**3,220,107**	2,623,021
Investment income, net of expenses (Note 3)	**3,861,415**	2,189,117
Interest expense on capital debt	**(5,916,020)**	(6,434,642)
Other non-operating revenues	**11,533**	853
Net Non-Operating Revenues	**48,416,979**	45,067,186
Decrease in Net Position Before Other Revenues	**(12,261,575)**	(14,378,287)
Other Revenues:		
State appropriations for capital expenditures (Note 7)	**1,688,000**	4,099,241
Capital grants and gifts	**110,302**	12,568,125
Additions to non-expendable assets	**1,070,322**	536,886
Increase (Decrease) in Net Position	**$ (9,392,951)**	$ 2,825,965

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

VERMONT STATE COLLEGES
(a Component Unit of the State of Vermont)

Statements of Changes in Net Position

For the Years Ended June 30, 2014 and 2013

	Investment in Capital Assets	Restricted Nonexpendable	Restricted Expendable	Unrestricted	Total
Balance June 30, 2012, as previously reported	**$ 51,786,211**	**$ 14,446,789**	**$ 6,191,758**	**$ (994,647)**	**$ 71,430,111**
Prior Period Adjustment - Change in Accounting Principle (Note 2)	-	-	-	(931,427)	(931,427)
Balance, June 30, 2012 as restated	**51,786,211**	**14,446,789**	**6,191,758**	**(1,926,074)**	**70,498,684**
Changes in net position, as previously reported 2013	13,804,245	681,624	2,063,350	(13,818,527)	2,730,692
Prior period adjustment - change in accounting principle (Note 2)	-	-	-	95,273	95,273
Changes in net position for 2013, as restated	13,804,245	681,624	2,063,350	(13,723,254)	2,825,965
Balance, June 30, 2013 as restated	**65,590,456**	**15,128,413**	**8,255,108**	**(15,649,328)**	**73,324,649**
Changes in net position for 2014	(5,437,732)	1,368,852	2,024,388	(7,348,459)	(9,392,951)
Balance, June 30, 2014	**$ 60,152,724**	**$ 16,497,265**	**$ 10,279,496**	**$ (22,997,787)**	**$ 63,931,698**

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

VERMONT STATE COLLEGES
(a Component Unit of the State of Vermont)

Statements of Cash Flows

For the Years Ended June 30,

	2014	(Restated) 2013
Cash Flows from Operating Activities:		
Tuition and fees	**$ 111,179,537**	$ 103,614,930
Grants and contracts	**14,763,594**	14,345,004
Sales and services of educational activities	**5,848,881**	5,529,267
Auxiliary enterprises	**916,820**	959,296
Interest received	**87,029**	105,440
Payments to suppliers	**(57,131,056)**	(53,004,669)
Payments to employees	**(118,499,313)**	(115,900,598)
Loans issued to students	**(1,003,012)**	(373,109)
Collection of loan payments	**838,519**	283,403
Other cash receipts	**1,584,972**	1,016,416
Net Cash Applied to Operating Activities	**(41,414,029)**	(43,424,620)
Cash Flows from Non-Capital Financing Activities:		
State appropriations	**27,330,899**	25,891,792
Non-operating federal grants	**19,909,045**	20,797,045
Gifts and grants	**3,220,107**	2,623,021
Net Cash Provided by Non-Capital Financing Activities	**50,460,051**	49,311,858
Cash Flows from Capital and Related Financing Activities:		
Capital appropriations	**1,688,000**	4,099,241
Capital and non-expendable grants and gifts	**1,180,624**	579,281
Purchase of capital assets	**(7,056,165)**	(13,417,391)
Change in deposits with bond trustee	**3,284,404**	10,142,299
Proceeds from capital debt borrowings	**-**	20,063,889
Payments on capital debt	**(3,637,525)**	(26,689,652)
Interest expense on capital debt	**(5,916,020)**	(6,434,642)
Proceeds from disposal of capital assets	**50,073**	853
Net Cash Applied to Capital and Related Financing Activities	**(10,406,609)**	(11,656,122)

VERMONT STATE COLLEGES
(a Component Unit of the State of Vermont)

Statements of Cash Flows - Continued

For the Years Ended June 30,

	2014	(Restated) 2013
Cash Flows from Investing Activities:		
Proceeds from sales and maturities of investments	**$ 22,567,016**	$ 41,324,878
Purchase of investments	**(23,607,730)**	(71,564,092)
Interest and dividends received on investments	**1,204,230**	701,301
Net Cash (Applied to) Provided by Investing Activities	**163,516**	(29,537,913)
Net Decrease in Cash and Equivalents	**(1,197,071)**	(35,306,797)
Cash and Equivalents, Beginning of Year	**4,230,563**	39,537,360
Cash and Equivalents, End of Year	**$ 3,033,492**	$ 4,230,563
Reconciliation of Operating Loss to Net Cash Applied to Operating Activities:		
Operating loss	**$ (60,678,554)**	$ (59,445,473)
Adjustments to reconcile operating loss to net cash applied to operating activities:		
Depreciation	**14,030,027**	13,238,072
Bad debts	**966,763**	126,127
Net (gain) loss on disposal of capital assets	**(11,533)**	41,162
Changes in assets and liabilities:		
Accounts receivable	**(1,121,604)**	(1,331,525)
Inventories	**(147,766)**	(50,958)
Other assets	**441,417**	(1,786,985)
Notes receivable	**(196,313)**	(15,363)
Accounts payable and accrued liabilities	**(608,237)**	(1,261,925)
Unearned revenues, deposits and refundable grants	**(278,203)**	(1,018)
Post-employment benefit obligations	**6,189,974**	7,063,266
Net Cash Applied to Operating Activities	**$ (41,414,029)**	$ (43,424,620)
Non-Cash Transactions:		
Equipment provided by capital grants and gifts	**$ -**	$ 12,525,730

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

Note 1 - **Summary of Significant Accounting Policies**

Organization
Vermont State Colleges include the following entities: System Office and Services, Community College of Vermont (CCV), Castleton State College (CSC), Johnson State College (JSC), Lyndon State College (LSC), Vermont Technical College (VTC), Vermont Interactive Television (VIT), Allied Health Nursing Program (Allied Health), Vermont Manufacturing Extension Center (VMEC), Small Business Development Center (SBDC), and Vermont Tech Office of Continuing Education and Workforce Development (TED). VIT is an audio-video network bringing instruction and public service events to sites throughout Vermont (currently Bennington, Brattleboro, Johnson, Lyndon, Middlebury, Montpelier, Newport, Randolph Center, Rutland, Springfield, St. Albans, White River and Williston). Budgetary management of VIT is maintained separately.

The accounting policies and procedures used by the Vermont State Colleges ("VSC" or the "Colleges") in accounting for and reporting their financial transactions are based on the accrual method of accounting. The significant accounting policies followed by the Colleges are described below.

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 accounting principles generally accepted in the United States of America, as prescribed by the Governmental Accounting Standards Board (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 accompanying statements of revenues and expenses demonstrate the degree to which the direct expenses of a given function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues primarily include charges to students or others who enroll or directly benefit from services that are provided by a particular function. Items not meeting the definition of program revenues are reported as general revenues.

Note 1 - **Summary of Significant Accounting Policies - Continued**

Basis of Presentation - Continued
The Colleges have determined that they function as a business-type activity, as defined by GASB. The effect of inter-fund activity has been eliminated from these financial statements. The basic financial statements and required supplementary information for general-purpose governments consist of management's discussion and analysis, basic financial statements and required supplementary information. The Colleges present the statements of net position, revenues and expenses, changes in net position and cash flows on a combined college-wide basis.

The Colleges' policy is to define operating activities in the statement of revenues and expenses as those that generally result from exchange transactions such as charges for services provided to students and for the purchase of goods and services. Certain other transactions are reported as non-operating activities. These non-operating activities include the Colleges' operating appropriations from the State of Vermont (the "State"), net investment income, gifts, certain grants and interest expense.

Net Position
GASB Statement No. 34 requires that resources be classified for accounting purposes into the following four net position categories:

Investment in capital assets, net: Capital assets, net of accumulated depreciation and of outstanding principal balances of debt attributable to the acquisition, construction, repair or improvement of those assets.

Restricted - nonexpendable: Net position subject to externally imposed conditions that VSC must maintain in perpetuity.

Restricted - expendable: Net position that is subject to externally-imposed conditions that can be fulfilled by the actions of the Colleges or by the passage of time.

Unrestricted: All other categories of net position. Unrestricted net position may be designated by actions of the Colleges' Board of Trustees.

In accordance with VSC's policy pertaining to the expenditure of restricted dollars, unrestricted dollars are spent first, followed by restricted dollars, if appropriate.

Note 1 - **Summary of Significant Accounting Policies - Continued**

Cash and Equivalents
The Colleges consider all highly liquid debt instruments purchased with an original maturity date of three months or less to be cash equivalents.

Inventories
Inventories are stated at the lower of cost (first-in, first-out retail inventory method) or market, and consist of bookstore items.

Capital Assets
Real estate assets, including improvements, are generally stated at cost. Furnishings and equipment are stated at cost as of date of acquisition or, in the case of gifts, at fair value as of date of donation. In accordance with the Board's capitalization policy, vehicles, equipment and works of art and historical treasures with a unit cost of at least $5,000 are capitalized. Land, building, leasehold and infrastructure improvements with a unit cost of $50,000 or more are capitalized. Software with a unit cost of $500,000 or more is capitalized. Interest cost on debt related to capital assets is capitalized during the construction period and then depreciated over the life of the project. The Colleges' capital assets, with the exception of land and construction in progress are depreciated on a straight-line basis over their estimated useful lives, which range from 3 to 50 years. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized.

Restricted expendable net position includes certain capital funds appropriated by the State of Vermont to the Vermont Department of Buildings and General Services for the benefit of VSC and unexpended as of fiscal year-end.

Investments
Investments are stated at fair value. Investment securities are exposed to various risks, such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is possible that changes in the values of the investment securities will occur and that such changes could materially affect the amounts reported in the statement of net position.

Note 1 - **Summary of Significant Accounting Policies - Continued**

Other Significant Accounting Policies
The Colleges' employees are granted vacation and sick leave in varying amounts. In the event of termination, an employee is paid for those accumulated vacation and sick days allowable in accordance with the applicable union contract in force or in the case of non-union personnel, according to the State or Colleges policy.

Amounts of vested and accumulated vacation leave are reported as accrued compensation and benefits. Amounts are determined based upon the personal service rates in effect as of the balance sheet date. No liability is recorded for non-vesting accumulating rights to receive vacation and sick pay benefits.

Refundable Grants
Refundable grants consist primarily of the refundable portion of the Federal Perkins and Nursing Student loans.

Unearned Revenue and Deposits
Deposits and advance payments received for tuition and fees related to certain summer programs and tuition received for the following academic year are reported as unearned revenues.

Student Fees
Student tuition and fees are presented net of scholarships and fellowships applied to students' accounts. Certain other scholarship amounts are paid directly to, or refunded to students, and they are reflected as expenses.

Bond and Note Premiums
Bond and note underwriter's premiums are amortized on the straight line basis over the life of the respective bond. VSC incurred bond premiums related to the 2010 and 2013 bonds at the time of the issuance of the bonds. The bond premium for the 2010 bond of $377,743 is amortized on a straight-line basis over approximately 8.5 years. The bond premium for the 2013 bond of $1,898,889 is amortized over 20 years. Cumulative amortization of the bond premium totals $275,843 and $136,783 as of June 30, 2014 and 2013, respectively. The bond premium is included in bonds and notes payable.

Note 1 - **Summary of Significant Accounting Policies - Continued**

Post-Employment Benefits
GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions* (GASBS 45), requires governments to account for other post-employment benefits (OPEB), primarily healthcare, on an accrual basis rather than on a pay-as-you-go basis. The effect is the recognition of an actuarially required contribution as an expense on the statement of revenues and expenses when a future retiree earns their postemployment benefits, rather than when they use their postemployment benefit. To the extent that an entity does not fund their actuarially required contribution, a post-employment benefit liability is recognized on the balance sheet over time.

Income Taxes
The Internal Revenue Service has determined that the Colleges are a wholly-owned instrumentality of the State of Vermont, and as such are generally exempt from federal income tax. However, the Colleges are subject to federal income tax on unrelated business income.

Grants
The Colleges receive financial assistance from federal and state agencies in the form of grants and entitlements. Expenditures of funds under these programs require compliance with the grant agreements and are subject to audit by the granting agency.

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

New Governmental Accounting Pronouncements
GASB 68, *Accounting and Financial Reporting for Pensions - an amendment of GASB Statement No. 27* is required for periods beginning after June 15, 2014. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. Management is in the process of reviewing this Statement and its potential effect upon their financial reporting, but does not expect any material impact.

Note 1 - **Summary of Significant Accounting Policies - Continued**

New Governmental Accounting Pronouncements - Continued
GASB 69, *Government Combinations and Disposals of Government Operations* is required for periods beginning after December 15, 2013. This Statement establishes accounting and financial reporting standards related to government combinations and disposals of government operations. As used in this Statement, the term government combination includes a variety of transactions referred to as mergers, acquisitions, and transfers of operations. Management is in the process of reviewing this Statement and its potential effect upon their financial reporting. It does not expect any material impact.

GASB 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date- an amendment of GASB 68* is required for periods beginning after June 15, 2014. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and inter-period equity, and creating additional transparency. Management is in the process of reviewing this Statement and its potential effect upon their financial reporting.

Reclassifications
Certain amounts on the 2013 financial statements have been reclassified to conform to the 2014 presentation.

Note 2 - Restatement of Prior Year Balances

Change in Accounting Principles
As a result of implementing GASB No. 65, *Items Previously Reported as Assets and Liabilities*, VSC increased net position by $95,273 at June 30, 2013 and decreased net position by $931,427 at June 30, 2012. The changes result from no longer reflecting the unamortized balance of bond issuance costs on the Statement of Net Position.

	As originally reported	As restated
As of June 30, 2013		
Statements of Net Position:		
Other assets	$ 851,136	$ 14,982
Unrestricted	(14,813,174)	(15,649,328)
Statements of Revenues and Expenses:		
Supplies and other services	42,663,166	42,567,893

Note 3 - Cash, Equivalents and Investments

Cash and equivalents with maturities of 90 days or less from purchase date are recorded at cost, which approximates market value.

In operating a central treasury and investment pool, individual college cash receipts (except the Federal Loan Funds) are deposited in separate collection deposit accounts in the name of VSC. Disbursements are made from other bank accounts that are funded by transfers from the central treasury.

In accordance with the Uniform Prudent Management of Institutional Funds Act, VSC deems all realized and unrealized gains on permanently restricted investments to be temporarily restricted if the income is restricted by the donor. Absent donor restrictions, the Board of Trustees has adopted a spending policy whereby 5% of the lesser of the current market value of investments or the average portfolio value over the last three years is allowed to be drawn down and allocated to operations.

Cash and Equivalents
Cash and equivalents included with non-current assets are restricted primarily for specific programs or to be used to pay for capital construction projects.

Note 3 - **Cash, Equivalents and Investments - Continued**

Cash and Equivalents - Continued

At June 30, 2014, the balance of current assets - cash and equivalents consists of approximately $18,000 in petty cash, and the remainder deposited in Federal Deposit Insurance Corporation (FDIC) insured banking institutions of approximately $2,434,000 per the accounting records of the Colleges, and approximately $3,106,000 per bank records. Of the bank balances, approximately $786,000 was covered by federal depository insurance and approximately $2,321,000 was uninsured and uncollateralized at June 30, 2014.

At June 30, 2014, the balances of non-current assets - cash and equivalents deposited in FDIC insured banking institutions were approximately $582,000 per the accounting records of the Colleges, and approximately $569,000 per bank records. The bank balances of approximately $569,000 were covered by federal depository insurance.

At June 30, 2013, the balance of current assets - cash and equivalents consist of approximately $18,000 in petty cash, and the remainder deposited in FDIC insured banking institutions of approximately $3,429,000 per the accounting records of the Colleges, and approximately $5,318,000 per bank records. Of the bank balances, approximately $1,139,000 was covered by federal depository insurance and approximately $4,179,000 was uninsured and uncollateralized at June 30, 2013.

At June 30, 2013, the balances of non-current assets - cash and equivalents deposited in FDIC insured banking institutions were approximately $784,000 per the accounting records of the Colleges, and approximately $777,000 per bank records. Of the bank balances, approximately $269,000 was covered by federal depository insurance and approximately $508,000 was uninsured and uncollateralized at June 30, 2013.

Note 3 - **Cash, Equivalents and Investments - Continued**

Investments
Investments of the various funds at June 30, 2014 are as follows:

	Fair Value	Cost
U.S. Government bonds	$ 15,602,328	$ 15,857,678
Corporate bonds	12,968,607	13,032,119
Common stock	7,161,656	6,693,097
Mutual funds	12,403,889	9,111,365
Money market	6,835,827	6,835,827
Held by bond trustee	4,426,154	4,426,154
Total Investments	$ 59,398,461	$ 55,956,240

Investments of the various funds at June 30, 2013 are as follows:

	Fair Value	Cost
U.S. Government bonds	$ 19,451,817	$ 19,543,271
Corporate bonds	13,397,791	13,436,645
Common stock	5,380,913	6,038,616
Mutual funds	10,980,785	9,210,466
Money market	2,063,101	2,063,101
Held by bond trustee	7,710,558	7,710,558
Total Investments	$ 58,984,965	$ 58,002,657

Investment maturities include deposits held by the bond trustee, which are invested in various government securities, corporate bonds, commercial grade paper, and money market accounts. The majority of these funds are related to the 2013 and 2010 bonds, and they are held in the bond fund, the reserve fund and the construction fund. Within the bond fund, there is a principal account, an interest account, and a sinking fund account.

VERMONT STATE COLLEGES
(a Component Unit of the State of Vermont)

Notes to the Financial Statements

June 30, 2014 and 2013

Note 3 - **Cash, Equivalents and Investments - Continued**

Investments - Continued

2014
Investment Maturities (in years)

Investment Type	Market Value	Less than 1	1-5	6-10	More than 10
Money Market Investments	$ 6,835,827	$ 6,835,827	$ -	$ -	$ -
Corporate Bonds	12,968,607	3,013,711	7,655,719	2,284,917	14,260
U.S. Govt. Bonds	15,602,328	7,711,521	6,095,301	1,795,506	-
Total	35,406,762	$ 17,561,059	$ 13,751,020	$ 4,080,423	$ 14,260
Other Investments					
Equity Securities and Mutual Funds	19,565,545				
Held by Bond Trustee	4,426,154				
Total	$ 59,398,461				

2013
Investment Maturities (in years)

Investment Type	Market Value	Less than 1	1-5	6-10	More than 10
Money Market Investments	$ 2,063,101	$ 2,063,101	$ -	$ -	$ -
Corporate Bonds	13,397,791	2,522,241	7,627,180	3,207,942	40,428
U.S. Govt. Bonds	19,451,817	8,403,371	8,126,577	2,921,869	-
Total	34,912,709	$ 12,988,713	$ 15,753,757	$ 6,129,811	$ 40,428
Other Investments					
Equity Securities and Mutual Funds	16,361,698				
Held by Bond Trustee	7,710,558				
Total	$ 58,984,965				

Note 3 - **Cash, Equivalents and Investments - Continued**

Investments - Continued
Investment income for the years ended June 30, is as follows:

	2014	2013
Interest and dividend income	**$ 1,367,083**	$ 962,731
Net realized and unrealized gain	**2,721,427**	1,386,936
Total investment income	**4,088,510**	2,349,667
Less: management fees	**(227,095)**	(160,550)
Investment income, net	**$ 3,861,415**	$ 2,189,117

Realized gain (loss) is included as a component of investment income. The calculation of realized gains (losses) is independent of the calculation of the net increase (decrease) in the fair value of investments. Realized gains and losses on investments that had been held in more than one fiscal year and sold in the current year may have been recognized as an increase or decrease in the fair value of investments reported in the prior year.

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June 30, 2014 and 2013

Note 3 - **Cash, Equivalents and Investments - Continued**

Investments - Continued
The risk categories for the bond fund holdings held by VSC at June 30, are as follows:

Investment rating*	2014	2013
AA+	**$ 16,558,229**	$ 20,093,891
AA	**2,596,218**	1,956,037
AA-	**1,285,138**	2,242,423
A+	**1,962,841**	2,938,966
A	**2,424,357**	1,661,660
A-	**1,315,657**	1,338,194
BBB+	**135,593**	124,264
BBB	**603,646**	1,326,981
BBB-	**456,119**	124,460
BB+	**155,945**	169,470
BB	**331,670**	152,612
BB-	**356,173**	198,318
B+	**148,816**	227,896
B	**95,812**	179,528
B-	**131,688**	62,569
CCC+	**13,033**	52,339
	$ 28,570,935	$ 32,849,608

*These ratings are determined by Standard & Poor's, a division of The McGraw-Hill Companies, Inc. All ratings represent the opinions of the research provider and are disclaimed as not representations or guarantees of performance.

The applicable risk ratings as defined by Standard & Poor's are as follows:

AAA - An obligation rated 'AAA' has an extremely strong capacity to meet its financial commitments. It is the highest rating given to an obligor.

AA - An obligation rated 'AA' differs from the highest-rated obligations only to a small degree. The obligor's capacity to meet its financial commitment on the obligation is very strong.

Note 3 - **Cash, Equivalents and Investments - Continued**

Investments - Continued

A - An obligation rated 'A' is somewhat more susceptible to the adverse effects of changes in circumstances and economic conditions than obligations in higher-rated categories. However, the obligor's capacity to meet its financial commitment on the obligation is still strong.

BBB - An obligation rated 'BBB' exhibits adequate protection parameters. However, adverse economic conditions or changing circumstances are more likely to lead to a weakened capacity of the obligor to meet its financial commitment on the obligation.

BB - An obligation rated 'BB' is less vulnerable to non-payment than other speculative issues. However, it faces major ongoing uncertainties or exposure to adverse business, financial or economic conditions, which could lead to the obligor's inadequate capacity to meet its financial commitment on the obligation.

B - An obligation rated 'B' is more vulnerable to nonpayment than obligations rated 'BB', but the obligor currently has the capacity to meet its financial commitment on the obligation. Adverse business, financial, or economical conditions will likely impair the obligor's capacity or willingness to meet its financial commitment on the obligation.

CCC - An obligation rated 'CCC' is currently vulnerable to non-payment, and is dependent upon favorable business, financial and economic conditions for the obligor to meet its financial commitment on the obligation. In the event of adverse business, financial or economic conditions, the obligor is not likely to have the capacity to meet its financial commitment on the obligation.

Plus (+) or minus (-) - The ratings from 'AAA' to 'CCC' may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within the major rating categories.

Note 4 - **Accounts Receivable, Notes Receivable and Allowance for Bad Debts**

The composition of the Colleges' accounts receivable at June 30, is summarized as follows:

	2014	2013
Student accounts receivable	**$ 6,707,508**	$ 6,814,704
Grants receivable	**3,528,283**	3,962,607
Other receivable	**2,822,954**	2,611,206
Subtotal	**13,058,745**	13,388,517
Allowance for doubtful accounts	**(1,595,762)**	(2,091,907)
Total accounts receivable, net	**$ 11,462,983**	$ 11,296,610

The notes receivable balance in the statement of net position represents the Perkins notes receivable. It is shown net of an allowance for bad debts of approximately $580,000 and $515,000 at June 30, 2014 and 2013, respectively. This allowance is the aggregate that was reserved for by each college based upon historical bad loan reserve requirements, the net increase in the allowance of $65,000 in 2014 and the net decrease in the allowance of $22,000 in 2013 has been reflected in operating expenses.

Note 5 - **Long-Term Liabilities**

Long-term liabilities consist of the following at June 30:

	2014				
	Beginning balances	**Additions**	**Reductions**	**Ending balances**	**Current portion**
Long-term liabilities					
Bonds and notes payable	**$ 134,573,494**	**$ -**	**$ 3,637,525**	**$ 130,935,969**	**$ 3,759,760**
Fair market value of interest rate swap	**10,603,309**	**71,047**	**-**	**10,674,356**	**-**
Net OPEB obligation	**42,753,755**	**11,548,353**	**5,358,379**	**48,943,729**	**-**
Accounts payable and accrued liabilities	**12,954,459**	**12,046,640**	**12,738,951**	**12,262,148**	**12,126,093**
Unearned revenue and deposits	**7,279,832**	**978,913**	**1,167,744**	**7,091,001**	**6,663,699**
Refundable grants	**6,049,434**	**-**	**5,298**	**6,044,136**	**-**
Total long-term liabilities	**$ 214,214,283**	**$ 24,644,953**	**$ 22,907,897**	**$ 215,951,339**	**$ 22,549,552**

	2013				
	Beginning balances	Additions	Reductions	Ending balances	Current portion
Long-term liabilities					
Bonds and notes payable	$ 141,199,257	$ 20,063,889	$ 26,689,652	$ 134,573,494	$ 3,637,524
Fair market value of interest rate swap	16,808,535	-	6,205,226	10,603,309	-
Net OPEB obligation	35,690,489	12,047,665	4,984,399	42,753,755	-
Accounts payable and accrued liabilities	14,216,384	12,954,459	14,216,384	12,954,459	12,734,330
Unearned revenue and deposits	7,271,640	6,492,402	6,484,210	7,279,832	6,481,816
Refundable grants	6,058,644	-	9,210	6,049,434	-
Total long-term liabilities	$ 221,244,949	$ 51,558,415	$ 58,589,081	$ 214,214,283	$ 22,853,670

Note 5 - **Long-Term Liabilities - Continued**

Bonds and Notes Payable
Outstanding debt is as follows:

	2014	2013
VSC - Capital Construction Projects: Variable rate (69% of one-month LIBOR plus 3.12%) term loan of $2,750,000 for 20 years with monthly payments of principal and interest due through January 2029; loan has a negative pledge against assets. [4]	**$ 2,258,024**	$ 2,359,365
Revenue Bonds, Series 1998: 4.9% - 5.45% capital appreciation serial bonds aggregating $5,205,000, maturing 2006 through 2013, and a 5.125% term bond of $4,850,000. Interest on the capital appreciation serial bonds accrues semi-annually and is compounded. Interest is payable only at maturity.	**-**	640,000
CSC - New Student Housing: Variable rate (69% of one-month LIBOR plus 1.31%) term loan of $5,200,000 for 20 years with monthly payments of principal and interest due through December 2025; collateralized by substantially all unrestricted revenue and assets not previously pledged as collateral on other debt. [1,3]	**3,600,340**	3,825,850
VSC - Capital Construction Projects: Variable rate (69% of the one-month LIBOR plus 1.21%) term loan of $72,000,000 for 20 years with monthly payments of principal and interest due through May 2028; collateralized by substantially all unrestricted revenue, accounts receivable, contract rights, inventory and machinery and equipment not previously pledged as collateral on other debt. [2, 3]	**66,356,816**	67,838,430

Note 5 - **Long-Term Liabilities - Continued**

	2014	2013
Bonds and Notes Payable - Continued		
Revenue Bonds, Series 2010A: 3.0% - 4.0% serial bonds aggregating $5,710,000 maturing 2011 through 2018 and a $5,375,000 4.0% term bond due July 2017. Interest on the serial bonds is paid semi-annually on the unpaid balances. Unamortized bond premium of $220,580 and $264,696 has been added to this liability at June 30, 2014 and 2013, respectively.	**$ 8,510,580**	$ 9,604,696
Revenue Bonds, Series 2010B: 4.751% - 5.101% serial bonds aggregating $3,800,000 maturing 2018 through 2020, and 6.101%, 6.861%, and 7.211% term bonds of $6,255,000, $5,580,000, and $14,630,000 due July 2025, July 2030, and July 2040, respectively. Interest on the term bond is payable semi-annually on the unpaid balances.	**30,265,000**	30,265,000
Revenue Bonds, Series 2013: 4.0% - 5.0% serial bonds aggregating $13,715,000 maturing 2015 through 2032 and 3.125% - 5.0% term bonds aggregating $4,450,000 maturing 2027 through 2030. Interest on serial bonds is paid semi-annually on the unpaid balances. Unamortized bond premium of $1,780,209 and $1,875,153 has been added to the liability at June 30, 2014 and 2013, respectively.	**19,945,209**	20,040,153
	$ 130,935,969	$ 134,573,494

Note 5 - **Long-Term Liabilities - Continued**

Bonds and Notes Payable - Continued
In December 2010, VSC issued Revenue Bonds, Series 2010A, in the principal amount of $11,085,000. The 2010A Bonds were issued for the purpose of (1) refinancing a portion of the Series 1998 Bonds; (2) refinancing certain indebtedness of VSC including loans to improve the Blair Park, Williston, Randolph, and Vermont campuses of VSC; and (3) paying the costs of issuance of the 2010A Bonds.

In December 2010, VSC issued Federally Taxable Build America Bonds, Series 2010B, in the principal amount of $30,265,000. The 2010B Bonds were issued for the purpose of (1) financing certain upgrades to the Community College of Vermont's Montpelier campus, including a 12,000 square foot building addition; (2) constructing a new residence hall and other related improvements at Castleton State College; (3) renovating an academic building and a visual arts center at Johnson State College; (4) expanding parking facilities at Lyndon State College together with building improvements for Lyndon State College's journalism program; (5) financing library renovations, the installation of certain energy or heating systems, construction of additional on-campus housing at the Randolph campus of Vermont Technical College ("VTC"), and improvements at VTC's Blair Park, Williston, Vermont campus; and (6) paying the costs of issuance of the 2010B Bonds. VSC is expected to receive a 35% subsidy of the interest paid on the Series 2010B Build America Bonds from the Federal Government, which will be recorded as a reduction of bond interest expense. (Sequester for federal budget reduced subsidy of interest by 7.6%).

[1] To manage its borrowing costs, VSC entered into an interest swap in connection with its $5,200,000 variable-rate loan. The intention of the swap was to effectively change the variable interest rate on the loan to a synthetic fixed rate of 4.97%.

The loan and the related swap agreement mature on December 16, 2025, and the swap's notional amount of $5,200,000 matches the $5,200,000 variable rate loan. The swap was entered into at the same time the loan was issued in December 2005. Under the swap, VSC pays the counterparty a fixed payment of 4.97% and receives a variable payment computed as 69% of the one-month London Interbank Offered Rate (LIBOR) plus 1.31%. Because of interest rate fluctuations since execution of the swap, the swap had a negative fair value of $469,030 as of June 30, 2014 and $519,533 as of June 30, 2013.

Note 5 - **Long-Term Liabilities - Continued**

Bonds and Notes Payable - Continued

[2] To manage its borrowing costs, VSC entered into an interest rate swap in connection with its $72,000,000 variable-rate loan. The intention of the swap was to effectively change VSC's variable interest rate on the loan to a synthetic fixed rate of 4.63%.

The loan and the related swap agreement mature in May 2028, and the swap's notional amount of $72,000,000 matches the $72,000,000 variable rate loan. The swap was entered into at the same time the loan was issued in May 2008. Under the swap, VSC pays the counterparty a fixed payment of 4.63% and receives a variable payment computed as 69% of the one-month USD-LIBOR-BBA (United States Dollar - London Interbank Offered Rate - British Bankers Association) plus 1.21%.

The loan has a thirty year amortization with a twenty year term. The first two years of the loan are interest only payments. This will allow VSC to more closely match the revenue streams produced by the capital projects. Because of interest rate fluctuations since execution of the swap, the swap had a negative fair value of $10,129,047 as of June 30, 2014 and $10,017,328 as of June 30, 2013.

[3] A former member of senior management also serves on the Board of the lender. Therefore, once the Board approved the capital construction projects, he recused himself completely from all financing proposal reviews, negotiations, financing or banking discussions or decisions relating to these transactions.

[4] To manage its borrowing costs, VSC entered into an interest rate swap in connection with its $2,750,000 variable-rate loan. The intention of the swap was to effectively change the variable interest rate on the loan to a synthetic fixed rate of 5.25%.

The loan and the related swap agreement mature on January 15, 2029, and the swap's notional amount of $2,750,000 matches the $2,750,000 variable rate loan. The swap was entered into at the same time the loan was issued in January 2009. Under the swap, VSC pays the counterparty a fixed payment of 2.25% and receives a variable payment computed as 69% of the one-month LIBOR plus 3.12%. Because of interest rate fluctuations since execution of the swap, the swap had a negative fair value of $76,279 and $66,448 as of June 30, 2014 and 2013, respectively.

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Notes to the Financial Statements

June 30, 2014 and 2013

Note 5 - **Long-Term Liabilities - Continued**

Debt Roll-Forward

Long-term debt activity for the years ended June 30, 2014 and 2013 was as follows:

	Balance June 30, 2013	Additions	Repayments	Balance June 30, 2014	Current Portion
Series 1998 with accreted interest	$ 640,000	$ -	$ (640,000)	$ -	$ -
New Housing - CSC	3,825,850	-	(225,510)	3,600,340	237,162
TD Banknorth - FY 2008 Capital Projects	67,838,430	-	(1,481,614)	66,356,816	1,551,838
CCV Montpelier	2,359,365	-	(101,341)	2,258,024	106,700
Series 2010-A	9,340,000	-	(1,050,000)	8,290,000	1,725,000
Series 2010-B	30,265,000	-	-	30,265,000	-
Series 2010 Bond Premium	264,696	-	(44,116)	220,580	44,116
Series 2010 Bonds	39,869,696	-	(1,094,116)	38,775,580	1,769,116
Series 2013	18,165,000	-	-	18,165,000	-
Series 2013 Bond Premium	1,875,153	-	(94,944)	1,780,209	94,944
Series 2013 Bonds	20,040,153	-	(94,944)	19,945,209	94,944
Total Bonds and Notes Payable	$ 134,573,494	$ -	$ (3,637,525)	$ 130,935,969	$ 3,759,760

Note 5 - **Long-Term Liabilities - Continued**

Debt Roll-Forward - Continued

	Balance June 30, 2012	Additions	Repayments	Balance June 30, 2013	Current Portion
Series 1977-A	$ 315,000	$ -	$ (315,000)	$ -	$ -
Series 1977-B	60,000	-	(60,000)	-	-
Series 1998	1,360,000	-	(720,000)	640,000	640,000
Series 2003	23,170,000	-	(23,170,000)	-	-
Series 2003 original issue discount	(308,438)	-	308,438	-	-
Series 2003 Bond	22,861,562	-	(22,861,562)	-	-
New Housing - CSC	4,040,272	-	(214,422)	3,825,850	225,510
TD Banknorth - FY 2008 Capital Projects	69,252,988	-	(1,414,558)	67,838,430	1,481,613
CCV Montpelier	2,455,623	-	(96,258)	2,359,365	101,341
Series 2010-A	10,280,000	-	(940,000)	9,340,000	1,050,000
Series 2010-B	30,265,000	-	-	30,265,000	-
Series 2010 Bond Premium	308,812	-	(44,116)	264,696	44,116
Series 2010 Bonds	40,853,812	-	(984,116)	39,869,696	1,094,116
Series 2013	-	18,165,000	-	18,165,000	-
Series 2013 Bond Premium	-	1,898,889	(23,736)	1,875,153	94,944
Series 2013 Bonds	-	20,063,889	(23,736)	20,040,153	94,944
Total bonds and notes payable	$ 141,199,257	$ 20,063,889	$ (26,689,652)	$ 134,573,494	$ 3,637,524

Note 5 - **Long-Term Liabilities - Continued**

Debt Roll-Forward - Continued
Maturities of long-term debt for the next five fiscal years and thereafter are as follows:

Years Ending June 30,	Principal Amount	Interest Amount
2015	$ 3,759,760	$ 5,745,501
2016	4,661,213	5,560,090
2017	5,422,083	5,325,744
2018	5,647,584	5,078,704
2019	5,707,937	4,854,637
2020-2024	23,876,537	21,337,839
2025-2029	59,924,806	13,604,977
2030-2034	10,986,049	3,608,018
2035-2039	7,445,000	1,608,673
2040-2041	3,505,000	108,211
	$ 130,935,969	$ 66,832,394

The interest amounts above reflect the 4.63%, 4.97% and 5.25% fixed rates on the debt subject to the swap agreements previously described (and interest rebate on 2010 bond).

According to the terms of the agreements under which the revenue bonds were sold, the bonds are general obligations of VSC. The 2013, 2010 and 1998 Revenue Bonds are also collateralized by deposits held by the trustee in the Bond Fund. VSC is required to make payments to the trustee for deposit into the Bond Fund sufficient to pay the principal, interest and sinking fund requirements, when due.

Note 6 - Functional Expense Classification

The following table details VSC's operating expenses by functional expense classification:

	2014	2013
Instruction	**$ 58,399,475**	$ 58,112,105
Research	**30,947**	39,554
Public service	**10,825,104**	10,538,004
Academic support	**22,566,674**	22,637,181
Student services	**29,400,400**	30,514,111
Institutional support	**44,830,185**	45,703,158
Physical plant	**7,931,182**	5,000,441
Student financial support	**7,273,698**	8,607,584
Depreciation	**14,030,027**	13,238,072
Total	**$ 195,287,692**	$ 194,390,210

Note 7 - Appropriations

VSC's operating appropriation from the State of Vermont is made directly to the Colleges and is drawn down on the basis of a monthly allotment. Included in the annual state appropriation for operations is funding for Allied Health of approximately $1,150,000 in 2014 and $1,117,000 in 2013; VMEC of approximately $428,000 in 2014 and 2013; and VIT of approximately $809,000 in 2014 and $786,000 in 2013.

Capital appropriations for VSC made from the State Bond Funds were approximately $1,688,000 and $4,099,000 in fiscal years 2014 and 2013, respectively.

Note 8 - **Retirement Plans**

Eligible faculty and staff participate in a defined contribution retirement plan administered by Teachers Insurance Annuity Association and College Retirement Equities Fund (TIAA-CREF). For the years ended June 30, 2014 and 2013, the Colleges' total payroll expense was approximately $82,488,000 and $81,454,000, respectively, of which approximately $54,018,000 and $52,914,000 represented salaries and wages of employees covered under the defined contribution plan, respectively. The Colleges' requirements to contribute to the retirement plan are specified by four collective bargaining agreements and by personnel policies for non-represented employees. Employer contribution rates are established by employee category. There are no required employee contributions to the plan. Depending upon the position category, employees may be eligible for the plan from as early as date of hire to as long as two years from date of hire. All eligible employees are vested from the date of eligibility. During the years ended June 30, 2014 and 2013, contributions made by the Colleges under this plan totaled approximately $6,432,000 and $6,251,000, or approximately 11.91% and 11.81% of covered salaries, respectively.

Additionally, certain employees participate in one of two defined benefit plans (Vermont Employees Retirement System or Vermont State Teachers Retirement System). Employees who were participants in either of these plans prior to their employment by the Colleges are allowed to continue participation. Covered salaries for employees participating in the Vermont Employees Retirement System during the years ended June 30, 2014 and 2013 were approximately $61,800 and $61,500, respectively, and employer contributions were approximately $6,300 and $6,000, respectively. There were no contributions to the Vermont State Teachers Retirement System during 2014 and 2013.

In addition, full-time faculty employees who have worked for the Colleges for 15 years may elect early retirement at age 55 and receive 50% of their annual salary as of their retirement date; full-time faculty employees who have worked for VSC for ten years may elect early retirement at age 55 and receive 40% of their annual salary as of their retirement date. In addition, VSC will pay 12% of the retiree's early retirement wages to the individual. This 12% payment represents VSC's contribution, which would have been made to the individual TIAA/CREF pension account. The payments due under this program are funded by VSC, as needed. During the years ended June 30, 2014 and 2013, contributions for these benefits were approximately $1,083,000 and $1,313,000, respectively.

Note 8 - **Retirement Plans - Continued**

The early retirement benefit is no longer being offered to new hires, but those employees who were eligible for early retirement before the benefit was discontinued have the option of electing for early retirement in October of every year. The benefit will be completely phased out when those employees currently eligible for early retirement either elect for early retirement or reach the age of 65.

Note 9 - **Post-Employment Benefits Other Than Pension**

Plan Description: VSC administers a self-insured single-employer defined benefit healthcare plan. The plan provides lifetime healthcare payments for eligible employees, spouses or civil union partners. The self-insured plan, administered by CIGNA, covers both active and retired members. Benefit provisions are established through negotiations between VSC and the unions representing VSC employees, and they are reviewed during the bargaining period prior to the termination date of each union contract. The retiree healthcare plan does not issue a publicly available financial report. During the years ended June 30, 2014 and 2013, 465 and 470 retirees were receiving post-retirement benefits, respectively.

Funding Policy: Contribution requirements are also negotiated between VSC and union representatives. VSC contributes 100% of the current-year utilization costs for eligible employees, spouses or civil union partners. For the fiscal years 2014 and 2013, VSC recognized employer contributions of $5,358,379 and $4,984,399, respectively, for both healthcare and early retirement. The plan is financed on a pay-as-you-go basis. In fiscal years 2014 and 2013, there were no member contributions.

Annual OPEB Cost and Net OPEB Obligation: VSC's OPEB cost (expense) is calculated based on the annual required contribution of the employer (ARC). VSC has elected to calculate the ARC and related information using the unit credit actuarial cost method permitted by GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover estimated utilization of healthcare and the special early retirement payments each year, and to amortize any unfunded actuarial liabilities over a period not to exceed thirty years for healthcare and not to exceed ten years for early retirement using a closed period, level dollar amortization method.

Note 9 - **Post-Employment Benefits Other Than Pension - Continued**

The following table shows the components of VSC's annual OPEB costs for the years ended June 30, 2014 and 2013, and the changes in VSC's net OPEB obligation to the Retiree Health and Early Retirement Plans:

	2014	2013
Annual required contribution	**$ 12,610,000**	$ 13,262,000
Interest on net OPEB obligation	**1,603,266**	1,338,393
Adjustment to annual required contribution	**(2,664,913)**	(2,552,728)
Annual OPEB cost	**11,548,353**	12,047,665
Contribution made	**(5,358,379)**	(4,984,399)
Increase in net OPEB obligation	**6,189,974**	7,063,266
Net OPEB Obligation - Beginning of Year	**42,753,755**	35,690,489
Net OPEB Obligation - End of Year	**$ 48,943,729**	$ 42,753,755

VSC's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation as of and for the years ended June 30, 2014, 2013 and 2012 are as follows:

Fiscal Years Ended	Annual OPEB Cost	% of Annual OPEB Cost Contributed	Net OPEB Obligation
June 30, 2014	$ 11,548,353	46.4%	$ 48,943,729
June 30, 2013	$ 12,047,665	41.4%	$ 42,753,755
June 30, 2012	$ 12,580,444	36.2%	$ 35,690,489

Note 9 - **Post-Employment Benefits Other Than Pension - Continued**

Funding Status and Funding Progress: As of the most recent actuarial valuation date, the actuarial accrued liability for benefits was $135,344,000, all of which was unfunded. The annual covered payroll (annual payroll of active employees covered by the plan) was $54,018,000, and the ratio of the unfunded actuarial liability to annual covered payroll was 250.6%. The latest actuarial valuation date was on July 1, 2013.

The projection of future benefit payments for an ongoing plan involves estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, retirement rates, marital status, and the health care cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to revision as actual results are compared with past expectations and new estimates are made about the future.

Methods and Assumptions: Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the specified pattern of sharing of benefit costs between employer and plan members to that point. The methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities consistent with the long-term perspective of the calculations.

The following actuarial assumptions were made:

Discount Rate: The discount rate used in the calculation was 3.75%.

Projected Salary Increase Rate: The projected salary increase rate used was 4.5%.

Future Employment: Age related turnover rates were developed based on the experience from the years ended June 30, 2005 through 2009. These rates were used as the basis for assigning active members a probability of remaining employed until the assumed retirement age and for developing an expected future working lifetime assumption for purposes of allocating to periods the present value of total benefits to be paid.

Note 9 - **Post-Employment Benefits Other Than Pension - Continued**

Mortality: Life expectancies were based on the RP2000 mortality table by gender and status (active versus current retired) published by the Retirement Plans Experience Committee of the Society of Actuaries.

Retirement Rate: Age related retirement rates tables were developed based on input and analysis of the current retiree population overall and the new retirees over the last five years. The age related tables assumed rates of retirement beginning at age 55.

Marital Status: Marital status of member at the calculation date was assumed to be 70% married based on current retiree population. Spousal participation was assumed to be 90% at the calculation date.

Healthcare Cost Trend Rate: Dental claims are expected to increase at 2.0 per annum. Medical trend rates are based on the Society of Actuaries (SOA) Long-Run Medical Cost Trend Model.

The required schedule of funding progress immediately following the notes to the financial statements presents information related to the actuarial accrued liability for benefits. Pursuant to the requirements of GASB Statement No. 45, this schedule will present multi-year trend information in future years about whether the actuarial accrued liability for benefits is increasing or decreasing over time.

Note 10 - **Leases**

The Colleges have various operating leases for classrooms, office space, equipment and motor vehicles. The majority of these leases have terms equal to or less than ten years and in some cases contain escalation and maintenance clauses, as well as renewal options. Total rental expense for all operating leases was approximately $2,801,000 and $2,707,000 in 2014 and 2013, respectively.

Note 10 - **Leases - Continued**

Future minimum rental payments required under operating leases with noncancelable terms in excess of one year at June 30, 2014 are as follows:

Years Ending June 30,	Real Estate	Vehicles and Equipment	Total
2015	$ 2,521,389	$ 254,542	$ 2,775,930
2016	1,831,486	235,557	2,067,043
2017	1,846,311	59,018	1,905,329
2018	1,822,321	38,446	1,860,768
2019	1,757,192	-	1,757,192
2020 and beyond	13,166,165	-	13,166,165
	$ 22,944,864	$ 587,563	$ 23,532,427

Note 11 - **Capital Assets**

Property and equipment activity for the years ended June 30, 2014 and 2013 is summarized below:

	Balance June 30, 2013	Additions	Transfers	Retirements	Balance June 30, 2014
Land	$ 6,428,274	$ -	$ -	$ -	$ 6,428,274
Construction-in-process	7,498,075	6,044,799	(10,345,739)	-	3,197,135
Subtotal - Capital assets not depreciated	13,926,349	6,044,799	(10,345,739)	-	9,625,409
Infrastructure	36,440,568	160,630	1,354,078	-	37,955,276
Buildings and improvements	240,504,212	-	8,963,061	-	249,467,273
Leasehold improvements	2,144,024	-	-	-	2,144,024
Equipment	30,853,774	850,736	28,600	(254,828)	31,478,282
Subtotal - Capital assets depreciated	309,942,578	1,011,366	10,345,739	(254,828)	321,044,855
Less accumulated depreciation	(129,856,677)	(14,030,027)	-	216,288	(143,670,416)
Capital assets, net	$ 194,012,250	$ (6,973,862)	$ -	$ (38,540)	$ 186,999,848

Note 11 - **Capital Assets - Continued**

	Balance June 30, 2012	Additions	Transfers	Retirements	Balance June 30, 2013
Land	$ 6,368,565	$ 59,709	$ -	$ -	$ 6,428,274
Construction-in-process	7,075,650	10,729,832	(10,307,407)	-	7,498,075
Subtotal - Capital assets not depreciated	13,444,215	10,789,541	(10,307,407)	-	13,926,349
Infrastructure	34,420,140	113,824	1,906,604	-	36,440,568
Buildings and improvements	233,344,436	728,707	6,431,069	-	240,504,212
Leasehold improvements	349,821	-	1,913,679	(119,476)	2,144,024
Equipment	16,581,175	14,311,049	56,055	(94,505)	30,853,774
Subtotal - Capital assets depreciated	284,695,572	15,153,580	10,307,407	(213,981)	309,942,578
Less accumulated depreciation	(116,791,424)	(13,238,072)	-	172,819	(129,856,677)
Capital assets, net	$ 181,348,363	$ 12,705,049	$ -	$ (41,162)	$ 194,012,250

Included in construction-in-process is interest expense on borrowing during the construction period. Total interest expense for fiscal year 2013 was $4,641. There was no such interest expense for fiscal year 2014.

Note 12 - **Contingencies and Commitments**

Contingencies
VSC participates in various federally funded programs. These programs are subject to financial and compliance audits and resolution of identified questioned costs. The amount, if any, of expenditures that may be disallowed by the granting agency cannot be determined at this time.

VSC is involved in various claims and legal actions arising in the ordinary course of business. The ultimate disposition of these matters is indeterminable, but in the opinion of management, the amount of ultimate liability would not have a significant impact on VSC's financial condition.

Note 12 - **Contingencies and Commitments - Continued**

Contingencies - Continued

VSC is also exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. VSC manages these risks through a combination of commercial insurance packages purchased in the name of VSC, and through self-insurance for medical and dental claims. VSC has entered into contracts with a third-party claims administrator, which essentially caps medical claim costs (stop-loss) at an agreed-upon level. Individual stop-loss is $150,000 of paid claims per covered member per year. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years. Reserves for medical and dental claims are included in accrued liabilities in the amount of approximately $1,592,000 at June 30, 2014 and $1,537,000 at June 30, 2013 and are based on historical data. A medical and dental claim roll-forward is presented below:

	2014	2013
Medical and dental claims reserve, beginning of year	**$ 1,537,000**	$ 1,544,000
Incurred claims	**21,335,000**	15,162,000
Payments on claims	**(21,280,000)**	(15,169,000)
Medical and dental claims reserve, end of year	**$ 1,592,000**	$ 1,537,000

VSC self-insures its workers' compensation program and uses a third-party claims administrator. Contributions to the plan are based on estimated payroll and rates adjusted by an experience modification factor. VSC has purchased stop-loss insurance, which is effective for aggregate claims in excess of $896,400 per year. VSC has obtained a letter of credit in the amount of $450,000 to be used in the event of failure to pay premiums on the stop-loss policy. This is collateralized by a certificate of deposit. A workers' compensation roll-forward is presented below:

	2014	2013
Workers' compensation reserve, beginning of year	**$ 206,000**	$ 229,000
Workers' compensation accrued during the year	**355,000**	341,000
Claims paid/reserved/claims administration	**(386,000)**	(364,000)
Workers' compensation reserve, end of year	**$ 175,000**	$ 206,000

Note 12 - **Contingencies and Commitments - Continued**

Commitments
VSC has entered into various construction contracts. The following commitments are ongoing projects at June 30, 2014.

Project	Expended through June 30, 2014	Committed Future Costs	Total Committed Costs of Project
VSC Brattleboro Facility	$ 82,162	$ 4,263	$ 86,425
CSC Leavenworth Window Replacement	-	400,123	400,123
VTC Bio-digester Project	3,379,064	78,785	3,457,849
	$ 3,461,226	$ 483,171	$ 3,944,397

At June 30, 2014, invoices related to construction projects of approximately $130,000 were included in accounts payable.

Employment Contracts
The Colleges have employment contracts with certain officers that expire on various dates through fiscal years 2015 and 2016. The agreements provide for aggregate annual base salaries of $1,117,593 in fiscal year 2015 and $723,948 in fiscal year 2016 and may be terminated with cause at any time.

Note 13 - **Management's Acceptance of Financial Statements**

Management has evaluated subsequent events through October 22, 2014, the date for which the financial statements were available for issuance.

REQUIRED SUPPLEMENTARY INFORMATION

VERMONT STATE COLLEGES
(a Component Unit of the State of Vermont)

Schedule of Funding Progress (Unaudited)

June 30, 2014 and 2013

Actuarial Valuation Date	Actuarial Valuation of Assets (a)	Actuarial Accrued Liability (AAL)(b)	Unfunded AAL (UAAL)	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll ([b-a]/c)
July 1, 2013	$ -	$ 135,344,800	$ 135,344,800	0%	$ 54,018,000	250.6%
July 1, 2011	$ -	$ 117,611,000	$ 117,611,000	0%	$ 52,025,735	226.1%
July 1, 2009	$ -	$ 94,168,000	$ 94,168,000	0%	$ 46,127,000	204.1%

VSC has to date performed four actuarial valuations, the latest on July 1, 2013, for purposes of satisfying the requirements of GASB Statement No. 45. The actuarial accrued liability for all benefits at this time was $135,344,800, all of which was unfunded. The annual covered payroll (annual payroll of active employees covered by the plan) was $54,018,000, and the ratio of the unfunded actuarial liability to annual covered payroll was 250.6%.

SUPPLEMENTAL INFORMATION

Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

O'Connor & Drew P.C. Certified Public Accountants

Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

To the Board of Trustees of
Vermont State Colleges
Montpelier, Vermont

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Vermont State Colleges (a component unit of the State of Vermont) (the "Colleges"), which comprise the statements of net position as of June 30, 2014 and 2013, the related statements of revenues and expenses, changes in net position and cash flows for the years then ended, and the related notes to the financial statements, which collectively comprise the Vermont State Colleges' basic financial statements and have issued our report thereon dated October 22, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Vermont State Colleges' internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Colleges' internal control. Accordingly, we do not express an opinion on the effectiveness of the Colleges' internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Vermont State Colleges' financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

O'Connor and Drew, P.C.

Certified Public Accountants
Braintree, Massachusetts

October 22, 2014