



**CALIFORNIA STATE UNIVERSITY
HEADQUARTERS BUILDING AUTHORITY**

Financial Statements and Supplementary Information

June 30, 2006 and 2005

(With Independent Auditors' Report Thereon)

**CALIFORNIA STATE UNIVERSITY
HEADQUARTERS BUILDING AUTHORITY**

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Independent Auditors' Report

The Board of Trustees
California State University:

We have audited the accompanying financial statements of the California State University Headquarters Building Authority as of and for the years ended June 30, 2006 and 2005, as listed in the accompanying table of contents. These financial statements are the responsibility of the California State University's management. 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the California State University Headquarters Building Authority's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

The accompanying financial statements present only the financial position and the changes in financial position and cash flows of the California State University Headquarters Building Authority, and do not purport to, and do not, present fairly the financial position of the California State University as of June 30, 2006 and 2005, and the changes in its financial position and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the California State University Headquarters Building Authority, as of June 30, 2006 and 2005, and the changes in its financial position and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

The California State University has not presented the management's discussion and analysis that U.S. generally accepted accounting principles require to supplement, although not to be part of, the basic financial statements.

Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information included in Schedules 1 through 3 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information, except for schedule 3, which is marked "unaudited," on which we express no opinion, has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

KPMG LLP

December 1, 2006

**CALIFORNIA STATE UNIVERSITY
HEADQUARTERS BUILDING AUTHORITY**

Statements of Net Assets

June 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Assets:		
Current assets:		
Cash and cash equivalents (notes 2 and 4)	\$ 10,813,856	8,259,593
Restricted cash (notes 2, 3, 4, and 6)	—	1,930,000
Interest receivable	99,798	68,886
Total current assets	<u>10,913,654</u>	<u>10,258,479</u>
Noncurrent assets:		
Lease receivable – noncurrent portion (note 3)	—	24,585,000
Total assets	<u>10,913,654</u>	<u>34,843,479</u>
Liabilities:		
Current liabilities:		
Due to the California State University Trustees (notes 4 and 5)	6,601,179	—
Due to the Systemwide Revenue Bond Program (notes 4 and 5)	4,312,475	—
Interest payable	—	445,527
Bonds payable – current portion (note 3)	—	945,000
Deferred revenue – current portion (note 4)	—	1,712,734
Total current liabilities	<u>10,913,654</u>	<u>3,103,261</u>
Noncurrent liabilities:		
Bonds payable – less current portion (note 3)	—	25,570,000
Deferred revenue – less current portion (note 4)	—	1,643,180
Total liabilities	<u>10,913,654</u>	<u>30,316,441</u>
Net assets:		
Restricted for:		
Building maintenance and repair	—	1,619,931
Unrestricted	—	2,907,107
Total net assets	<u>\$ —</u>	<u>4,527,038</u>

See accompanying notes to financial statements.

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Statements of Revenues, Expenses, and Changes in Net Assets

Years ended June 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Operating revenues:		
Lease income (notes 3 and 4)	\$ 428,184	1,781,248
Total operating revenues	<u>428,184</u>	<u>1,781,248</u>
Operating expenses:		
General, administrative, and other operating costs	27,909	3,123
Interest on bonds	222,763	1,343,045
Total operating expenses	<u>250,672</u>	<u>1,346,168</u>
Operating income	177,512	435,080
Nonoperating revenues:		
Investment income	77,851	208,335
Income before transfers	255,363	643,415
Transfers to California State University Trustees (note 4)	<u>(4,782,401)</u>	<u>—</u>
Increase (decrease) in net assets	(4,527,038)	643,415
Net assets – beginning of year	<u>4,527,038</u>	<u>3,883,623</u>
Net assets – end of year	<u>\$ —</u>	<u>4,527,038</u>

See accompanying notes to financial statements.

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Statements of Cash Flows

Years ended June 30, 2006 and 2005

	2006	2005
Cash flows from operating activities:		
Cash received from lease	\$ —	985,000
General, administrative, and other operating costs	(27,909)	(3,123)
Interest paid	(668,290)	(1,356,016)
Interest income on lease	—	1,643,180
	<u>(696,199)</u>	<u>1,269,041</u>
Cash flows from noncapital financing activities:		
Moneys received on behalf of others	2,744,628	—
Moneys disbursed on behalf of others	(625,903)	—
	<u>2,118,725</u>	<u>—</u>
Cash flows used in capital and related financing activities:		
Retirement of indebtedness	(945,000)	(905,000)
Cash flows provided by investing activities:		
Interest received	146,737	158,248
	<u>624,263</u>	<u>522,289</u>
Cash and cash equivalents:		
Cash and cash equivalents (including \$1,930,000 and \$1,850,000, respectively, of cash and cash equivalents included in restricted cash) at beginning of year	10,189,593	9,667,304
Cash and cash equivalents (including \$0 and \$1,930,000, respectively, of cash and cash equivalents included in restricted cash) at end of year	\$ 10,813,856	10,189,593
Reconciliation of operating income to net cash provided by (used in) operating activities:		
Operating income	\$ 177,512	435,080
Change in assets and liabilities:		
Lease receivable	—	985,000
Deferred revenue	(428,184)	(138,068)
Interest payable	(445,527)	(12,971)
Total adjustments	<u>(873,711)</u>	<u>833,961</u>
Net cash provided by (used in) operating activities	<u>\$ (696,199)</u>	<u>1,269,041</u>
Supplemental disclosure of noncash capital and related financing activities:		
Bond defeasance and lease termination	\$ 25,570,000	—
Conversion of deferred revenue to Systemwide Revenue Bond liability	2,157,000	—
Conversion of deferred revenue to California State University Trustees liability	1,129,627	—
Transfers to California State University Trustees	4,782,401	—

See accompanying notes to financial statements.

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Notes to Financial Statements

June 30, 2006 and 2005

(1) Summary of Significant Accounting Policies

(a) Description of the Authority

The board of trustees of the California State University established the California State University Headquarters Building Authority (Authority), specifically to issue bonds to finance the acquisition, construction, maintenance, and operation of buildings for public education purposes, including a headquarters building.

(b) Basis of Presentation

The accompanying financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting in accordance with U.S. generally accepted accounting principles, as prescribed by the 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.

The financial statements required by GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, include a statement of net assets, a statement of revenues, expenses, and changes in net assets, and a statement of cash flows. The Authority is considered a special purpose government under the provisions of GASB Statement No. 34. The Authority records revenue primarily from lease fees collected from the Chancellor's Office of the California State University and, accordingly, has chosen to present its financial statements using the reporting model for special purpose governments engaged only in business-type activities. This model allows all financial information for the Authority to be reported in a single column in each of the financial statements. In accordance with the business-type activities reporting model, the Authority prepares its statements of cash flows using the direct method.

(c) Election of Applicable FASB Statements

The Authority has elected not to adopt the pronouncements issued by the Financial Accounting Standards Board (FASB) after November 30, 1989.

(d) Classification of Current and Noncurrent Assets and Liabilities

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

(e) Net Assets

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

Restricted – Net assets subject to restriction based on the bond indenture document.

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Notes to Financial Statements

June 30, 2006 and 2005

Unrestricted – All other categories of net assets. In addition, unrestricted net assets may be designated for use by the Authority.

The Authority has adopted a policy of utilizing restricted funds, when available, prior to unrestricted funds.

(f) Classification of Revenues and Expenses

The Authority considers operating revenues and expenses in the statements of revenues, expenses, and changes in net assets to be those revenues and expenses that result from exchange transactions or other activities that are connected directly to the Authority's primary functions. Exchange transactions include charges for services rendered and the acquisition of goods and services. Certain other transactions are reported as nonoperating revenues and expenses in accordance with GASB Statement No. 34. These nonoperating activities primarily include the Authority's net investment income and transfers to the California State University Trustees (Trustees) for cash collected (see note 4).

(g) Principal and Interest Payment Dates

In fiscal year 2005, interest ranging from 4.40% to 5.25% was due on outstanding bonds, payable semiannually on March 1 and September 1 with principal payments due September 1. These terms continued in effect for fiscal year 2006 until October 2005 when the bonds were defeased (see note 5).

(2) Cash and Cash Equivalents

At June 30, 2006 and 2005, cash and cash equivalents consisted of demand deposits held at the State Treasury, as well as deposits in the state's investment pool. Deposits in the state's investment pool are unrated and have a weighted average maturity (in years) of 0.42 and 0.45 at June 30, 2006 and 2005, respectively. The Authority's cash and cash equivalents consist of the following deposits:

	2006	2005
Cash in State Treasury	\$ 1,131,856	1,131,593
State of California Surplus Money Investment Fund	9,682,000	7,128,000
Restricted cash	—	1,930,000
Total	\$ 10,813,856	10,189,593

Restricted cash is invested in the State of California Surplus Money Investment Fund.

(3) Bonds Payable

In connection with the bond issuance of October 1997, the Authority entered into a sublease agreement with the Trustees, whereby, the Authority leased the property known as the Office of the Chancellor to the Trustees. The Trustees were required to make lease payments to the Authority sufficient to pay all debt service costs and certain administrative expenses of the Authority. Accordingly, the financial statements of the Authority included a lease receivable amount equal to the bonds payable amount.

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The bonds were issued in denominations of \$5,000 principal amount each or any integral multiple thereof.

As discussed in notes 4 and 5, the Authority's outstanding bonds were defeased during the 2006 fiscal year.

The change in bonds payable during fiscal years 2006 and 2005 is as follows:

	2006	2005
Bonds payable at beginning of year	\$ 26,515,000	27,420,000
Less:		
Defeased bonds	25,570,000	—
Payment on bonds	945,000	905,000
Bonds payable at end of year	—	26,515,000
Less current portion	—	(945,000)
Bonds payable – noncurrent portion	\$ —	25,570,000

(4) Sale of Headquarters Building

On October 1, 2005, the Authority entered into a Facility Purchase Contract with the Trustees. Under the terms of the purchase contract, the Authority sold the headquarters building to the Trustees in return for the retirement of all of the Authority's outstanding debt. As discussed in note 5, the Trustees defeased the Authority's outstanding debt in connection with the issuance of the Systemwide Revenue Bonds Series 2005C refunding bonds. On the same date, the Authority terminated the 1997 sublease and entered into a new sublease agreement with the Trustees under which the Authority assigned all rights and interest in the portion of the rental payments related to debt service of the Systemwide Revenue Bonds Series 2005C refunding bonds, known as the Base Rental Payments, to the Trustees as custodians of the Systemwide Revenue Bond Program. As a result of termination of the 1997 sublease, all surplus moneys held by the Authority must be returned to the Trustees.

(5) Advance Refunding

Current-Year Refunding

In October 2005, the Authority defeased the Lease Revenue Bonds, Series B by placing a portion of the proceeds from the issuance of the Systemwide Revenue Bonds Series 2005C refunding bonds in an irrevocable trust with the State Treasurer to provide for all future debt service payments on the refunded bonds. The proceeds from the Systemwide Revenue Bonds Series 2005C refunding bonds were used to purchase U.S. government securities that were placed in an escrow account. The investments and fixed earnings from the investments are considered sufficient to fully service the defeased debt until the debt is called or matured. This transaction will reduce the Authority's total debt service payments by \$1,733,636 over the life of the bonds. The economic gain (difference between net present values of the debt service

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Notes to Financial Statements

June 30, 2006 and 2005

payments on the old debt and new debt) from this transaction was \$1,426,140. Accordingly, the refunded bonds have been considered defeased and therefore removed as a liability from the accompanying financial statements. The amount of the Authority's defeased bonds outstanding as of June 30, 2006 totaled \$25,570,000.

(6) Restricted Cash/Lease Receivable

Generally, the Authority collected lease payments from the Trustees in periods before the lease payments were due. These advance payments were discounted using the Surplus Money Investment Fund rate at the time of payment, which was 3.626% and 1.995% for 2006 and 2005, respectively. In 2003, the Authority received advance payments for 2004 and 2005 and in subsequent years, the lease payments have been collected two years in advance. The advance lease payments have been recorded as restricted cash equal to the respective bond payable amounts. As described in notes 4 and 5, the Authority will convey the portion of the advance collections related to the bonds outstanding to the Trustees in accordance with the sublease agreement. Total restricted cash as of June 30, 2005 amounted to \$1,930,000.

(7) Buildings, Improvements, and Equipment

The original capitalized cost of buildings, improvements, and equipment at completion of construction was recorded by the California State University.

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Schedule of Net Assets by Fund

June 30, 2006

Assets	Revenue fund	Interest and redemption fund	Repair and replacement reserve fund	Total
Cash	\$ 827	1,130,772	257	1,131,856
Cash equivalents	6,882,000	1,161,000	1,639,000	9,682,000
Total cash and cash equivalents	6,882,827	2,291,772	1,639,257	10,813,856
Interest receivable	68,039	13,091	18,668	99,798
Total assets	6,950,866	2,304,863	1,657,925	10,913,654
Liabilities and Net Assets				
Liabilities:				
Due to Systemwide Revenue Bond Program	4,312,475	—	—	4,312,475
Due to California State University Trustees	2,638,391	2,304,863	1,657,925	6,601,179
Total liabilities	6,950,866	2,304,863	1,657,925	10,913,654
Total net assets	\$ —	—	—	—

See accompanying independent auditors' report.

**CALIFORNIA STATE UNIVERSITY
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Schedule of Revenues, Expenses, and Changes in Net Assets by Fund

Year ended June 30, 2006

	Revenue fund	Interest and redemption fund	Repair and replacement reserve fund	Total
Operating revenues:				
Interest income on lease	\$ 1,373,184	(945,000)	—	428,184
Total operating revenues	<u>1,373,184</u>	<u>(945,000)</u>	<u>—</u>	<u>428,184</u>
Operating expenses:				
General, administrative, and other operating costs	3,023	—	24,886	27,909
Interest on bonds outstanding	—	222,763	—	222,763
Total operating expenses	<u>3,023</u>	<u>222,763</u>	<u>24,886</u>	<u>250,672</u>
Operating income (loss)	<u>1,370,161</u>	<u>(1,167,763)</u>	<u>(24,886)</u>	<u>177,512</u>
Nonoperating revenues (expenses):				
Transfers to California State University Trustees	(904,447)	(2,269,953)	(1,608,001)	(4,782,401)
Investment income	55,406	9,489	12,956	77,851
Interfund transfers:				
Interest and Redemption Fund	(1,581,000)	1,581,000	—	—
Total nonoperating expenses	<u>(2,430,041)</u>	<u>(679,464)</u>	<u>(1,595,045)</u>	<u>(4,704,550)</u>
Decrease in net assets	<u>(1,059,880)</u>	<u>(1,847,227)</u>	<u>(1,619,931)</u>	<u>(4,527,038)</u>
Net assets, beginning of year	<u>1,059,880</u>	<u>1,847,227</u>	<u>1,619,931</u>	<u>4,527,038</u>
Net assets, end of year	<u>\$ —</u>	<u>—</u>	<u>—</u>	<u>—</u>

See accompanying independent auditors' report.

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Schedule of Insurance Coverage

June 30, 2006

(Unaudited)

Expiration date	Coverage	Amount	Company	Policy number
July 1, 2006*	CSU Master Property Policy, All Risk Building, Equipment, and Rental Income	\$ 1,000,000,000	California Public Entity Property Program	PEPIP
July 1, 2006*	CSU Master Property Policy, Boiler and Machinery	100,000,000	Hartford	PBOILER0506
July 1, 2006*	Bodily Injury and Property Damage Liability (Primary)	1,000,000	CSURMA	RMA-CHANC-00506-1
July 1, 2006*	Bodily Injury and Property Damage Liability (Excess)	24,000,000	School's Excess Liability Fund	T07040519J1247

*Additional insurance policies are maintained for the period of July 1, 2006 to July 1, 2007. These policies provide the same coverage indicated above.

See accompanying independent auditors' report.