

# The Ohio State University Research Foundation

(A Component Unit of The Ohio State University)

Financial Statements as of and for the  
Year Ended June 30, 2007, and  
Independent Auditors' Report

**THE OHIO STATE UNIVERSITY RESEARCH FOUNDATION**  
**(A Component Unit of The Ohio State University)**

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## INDEPENDENT AUDITORS' REPORT

To the Board of Directors of  
The Ohio State University Research Foundation  
Columbus, Ohio

We have audited the accompanying statement of net assets of The Ohio State University Research Foundation (the "Research Foundation"), a component unit of The Ohio State University, as of June 30, 2007, and the related statement of revenues, expenses, and changes in net assets, and of cash flows for the year then ended. These financial statements are the responsibility of the Research Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit 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 respective 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 Research Foundation's internal control over financial reporting. Accordingly, we express no such opinion. An audit 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 audit provides a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Research Foundation as of June 30, 2007, and its changes in net assets and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Management's Discussion and Analysis ("MD&A") on pages 2 through 7 is not a required part of the financial statements, but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the Research Foundation's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and we do not express an opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 17, 2007, on our consideration on internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. 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 considered in assessing the results of our audit.



October 17, 2007

# **THE OHIO STATE UNIVERSITY RESEARCH FOUNDATION (A COMPONENT UNIT OF THE OHIO STATE UNIVERSITY)**

## **MANAGEMENT'S DISCUSSION AND ANALYSIS YEAR ENDED JUNE 30, 2007**

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The following Management's Discussion and Analysis, or MD&A, provides an overview of the financial position and operations of The Ohio State University Research Foundation (the "Research Foundation") for the years ended June 30, 2007. We encourage you to read this MD&A section in conjunction with the audited financial statements and footnotes appearing in this report.

### **ABOUT THE FINANCIAL STATEMENTS**

The Research Foundation has implemented a governmental financial reporting model, which is set forth in Governmental Accounting Standards Board ("GASB") Statement Nos. 34 and 35. Under these accounting standards, the Research Foundation will present its financial reports in a single-column "business-type activity" format. GASB Statement No. 35 defines business-type activities as those financed in whole or in part by fees charged to external parties for goods and services. Most public colleges and universities have elected to use the business-type activity format.

In addition to this MD&A section, the financial report includes a statement of net assets, a statement of revenues, expenses, and changes in net assets, statement of cash flows, and footnotes.

The statement of net assets is the Research Foundation's balance sheet. It reflects the total assets, liabilities, and net assets (equity) of the Research Foundation as of June 30, 2007. Liabilities due within one year, and assets available to pay those liabilities, are classified as current. Other assets and liabilities are classified as noncurrent. Investment assets are carried at market value. Capital assets, which include the Research Foundation's furniture and equipment, are shown net of accumulated depreciation. Net assets are grouped in the following categories:

- Invested in capital assets, net of plant debt
- Restricted—Nonexpendable (endowment and annuity funds)
- Restricted—Expendable (primarily current restricted and loan funds)
- Unrestricted

The statement of revenues, expenses, and changes in net assets is the Research Foundation's income statement. It details how net assets have increased (or decreased) during the fiscal year that ended June 30, 2007. Depreciation is provided for capital assets, and there are required subtotals for net operating income or loss and net income or loss before additions to nonexpendable funds.

It should be noted that the required subtotal for net operating income or loss will generally reflect a loss for the Research Foundation. This is primarily due to the way operating and nonoperating items are being reported. Operating expenses include virtually all Research Foundation expenses. Operating revenues, however, exclude certain significant revenue streams, including our corporate operating budget. Under this paradigm, our operating loss will increase or decrease based upon the amount of our corporate operating budget.

The statement of cash flows details how cash has increased (or decreased) during the year ended June 30, 2007. It breaks out the sources and uses of Research Foundation cash into the following categories:

- Operating activities
- Noncapital financing activities
- Capital and related financing activities
- Investing activities

Cash flows associated with the Research Foundation's expendable net assets appear in the operating and noncapital financing categories. Capital financing activities include payments for capital assets, proceeds from long-term debt, and debt repayments. Purchases and sales of investments are reflected as investing activities.

The footnotes, which follow the financial statements, provide additional details on the numbers in the financial statements.

## **GENERAL**

The Ohio State University Research Foundation is a nonprofit corporation created as a vehicle to promote sponsored research at The Ohio State University (the "University").

In November 1936, the Ohio Secretary of State issued a charter to The Ohio State University Research Foundation as a nonprofit educational corporation. Incorporators of the Research Foundation included the renowned inventor Charles F. Kettering and James F. Lincoln, president of the Lincoln Electric Company. The Board of Directors consists of the following member directors:

Trustee Member (1):

Appointed by the Board of Trustees of the University.

University Administration Members (3):

Including the Vice President for Research, the Executive Vice President for Academic Affairs and Provost, and the Dean of the Graduate School as designated by the Board of Trustees of the University.

Faculty Members (4):

Selected from the faculty by the Research Committee of the University Senate.

Alumni Members (2):

Designated by The Ohio State University Alumni Association from alumni of the University.

At-Large (1):

Designated by the President of the University from among members of national organizations of distinguished engineers, scientists, and scholars.

The Research Foundation Board of Directors elects officers during the regular annual meeting. The officers include the President, Vice President, Secretary, Assistant Secretary, Treasurer, and Executive Director of the Research Foundation. The Directors appoint an Executive Committee and other committees as needed.

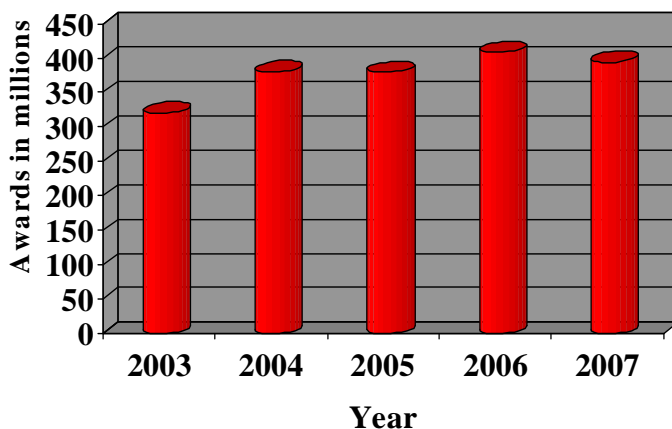
The function of the Research Foundation has evolved over the years in response to the needs of the research community within the University. The Research Foundation began as an organization created to encourage industry sponsorship of University research. It now provides specialized integrated administrative and financial services for research and other activities supported by a wide range of external sponsors.

The Research Foundation does not own or operate research facilities but utilizes facilities provided by the University under an agreement between the Board of Trustees of the University and the Research Foundation. Personnel working on Research Foundation projects are appointed as University personnel and are paid through the University under provisions of the agreement. The Research Foundation Board of Directors approves the operating budget for the Research Foundation's administrative expenses.

### **FINANCIAL HIGHLIGHTS AND KEY TRENDS**

Awards totaled \$394 million in Fiscal Year 2007, a 3.4% decrease from \$408 million in Fiscal Year 2006. Although there was a 4% increase in federal awards, that increase was offset by significant decreases in non-federal awards. The Departments of Defense, Agriculture, and Energy accounted for the only significant federal growth. The decrease in non-federal awards was largely the result of less funding from the State of Ohio.

### **Award Growth**



Sponsor revenues and expenditures in Fiscal Year 2007 increased by \$10 million (2.8%) to \$377 million. Most of the increase can be attributed to federal sponsors.

### **STATEMENT OF NET ASSETS**

From June 30, 2006 to June 30, 2007, the cash balance increased by \$23 million (177%). This increase was due to continuing improvements within the billing teams and the increase in deferred revenue. The increase in deferred revenue was due to the amount of cash advanced from sponsors increasing by \$4.8 million during the year. The statement of cash flows, which is discussed in more detail below, provides additional detail on the sources and the uses of Research Foundation cash.

Following is a summary of the major components of the net assets of the Research Foundation for the years ended June 30, 2007 and 2006:

	<b>2007</b>	<b>2006</b>
CURRENT ASSETS	\$ 92,915,432	\$ 85,061,106
CAPITAL ASSETS—furniture and equipment	<u>826,724</u>	<u>639,373</u>
Total assets	<u>\$ 93,742,156</u>	<u>\$ 85,700,479</u>
CURRENT LIABILITIES	\$ 85,341,673	\$ 77,219,940
NONCURRENT LIABILITIES		
—accrued vacation and sick leave	<u>349,676</u>	<u>358,900</u>
Total liabilities	<u>85,691,349</u>	<u>77,578,840</u>
Net assets:		
Invested in capital assets	826,724	639,373
Unrestricted	<u>7,224,083</u>	<u>7,482,266</u>
Total net assets	<u>8,050,807</u>	<u>8,121,639</u>
Total liabilities and net assets	<u>\$ 93,742,156</u>	<u>\$ 85,700,479</u>

Accounts receivable and unbilled project costs decreased \$14.8 million (21%) this year primarily due to improved billing, reporting, and collections processing. Under the current billing paradigm approximately \$4 million a month in fringe benefit expense cannot be drawn and deposited until after month-end. The Research Foundation is requesting that improvements be made to the University Payroll system that will facilitate collecting this cash by month-end.

In 2007 the Research Foundation remitted Facilities and Administrative balances payable to the University on a monthly basis. For 2006 and 2005, the Research Foundation remitted Facilities and Administrative balances payable to the University on a quarterly basis.

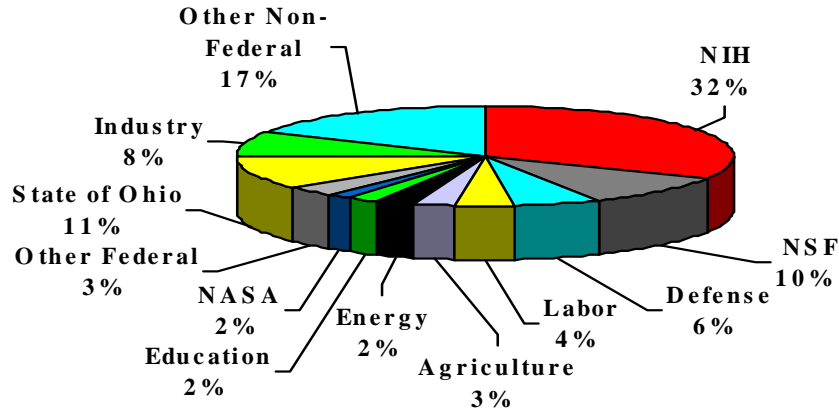
**2006–2005 Highlights**—From June 30, 2005 to June 30, 2006, the cash balance decreased by \$7.3 million (36%). The primary cause of this reduction in cash was a decline in deferred revenue. The decline in deferred revenue was due to the amount of cash advanced from sponsors being relatively stable throughout the year, while expenditures against these advances increased significantly in the second half of the year. The secondary cause of the reduction in the cash balance was that payments from the State of Ohio were delayed because of burdensome cost-share agreements. As of June 30, 2006, \$4.1 million in State of Ohio invoices remained unpaid.

#### **STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS**

Our sponsored project revenue/expenditures increased modestly by \$10 million (2.8%) over last year. Twenty-seven colleges generated Sponsored Project Revenue in this fiscal year with Medicine and Engineering combining to generate 53% of the total. Federal sponsors were the major source of revenue. The

National Institutes of Health (NIH), our largest federal sponsor, accounted for 32% of our total sponsored revenue.

### Revenues / Expenditures by Source Funds Fiscal Year 2007



The largest growth occurred in sponsored project personnel expenditures and sponsored project equipment, with equipment accounting for \$7 million of the increase.

Net interest revenue increased by approximately \$254,000 due to higher average cash balances throughout the year coupled with higher interest rates.

We recognize Sponsored Project Revenue as Sponsored Project Expenses are incurred. The excerpt below from our statement of revenues, expenses, and changes in net assets demonstrates this relationship.

	2007	2006
SPONSOR PROJECT REVENUE	<u>\$ 377,114,762</u>	<u>\$ 366,960,720</u>
EXPENDITURES AND TRANSFERS:		
Sponsored project expenses:		
Personnel	\$ 175,463,288	\$ 171,453,117
Materials and services	98,034,949	98,620,780
Equipment	20,063,354	12,598,407
Travel	7,548,297	7,701,097
F&A charged by the University	76,004,874	76,587,319
Other	<u>8,491,721</u>	<u>7,378,637</u>
Total Sponsored project expenses:	<u>\$ 377,114,762</u>	<u>\$ 366,960,720</u>

The University appropriation line item represents the current year's Research Foundation operating budget. The Research administration expenditure line represents annual Research Foundation expenditures. The difference between these two line items is the budget surplus (deficit) for the fiscal year.

It is important to note that the Research Foundation did not overspend the available budget this year. The Research Foundation's available budget consists of the University appropriation and any unspent budget (budget carry forward) from prior years. The 2006 net income amount of \$1.7 million dollars contained \$1.1 million dollars of unspent budget. In 2007, the Research Foundation spent the entire 2007 University appropriation and a portion of the budget carry forward from 2006. For financial statement purposes, any noncapital spending from budget carry forward will flow through the income statement on the Research administration expenditure line and will therefore reduce net income in the year the spending takes place.

Additionally, for financial statement purposes, any noncapital spending from Net Assets will flow through the income statement as Other Operating Expense and will therefore reduce net income. In 2007, we funded our accounts receivable collection activity and the purchase of new workstations with Board Designated funds in the amount of \$191,474.

**2006–2005 Highlights**—Sponsored Project Revenue/Expenses in Fiscal Year 2006 increased by \$21 million (6%) from Fiscal Year 2005. Federal sponsors generated the majority of our revenue.

## **THE STATEMENT OF CASH FLOWS**

The primary source of cash receipts for operating activities consists of payments from sponsors. Cash outlays represent payments for personnel, materials, services, equipment, and travel incurred for Sponsored Research activities.

It should be noted that our corporate expenditures are carried in Cash Flows from Operating Activities and our corporate operating budget is carried in Net Cash Provided by Noncapital Financing Activities. This results in a large positive cash flow from noncapital financing activities and a corresponding decrease in cash flow from operations.

Net cash provided by investing activities increased by approximately \$254,000 as explained under the Statement of Revenues, Expenses, and Changes in Net Assets.

## **FUTURE**

The Research Foundation will continue to partner with all levels of research administrators, campus researchers, and the research support community to ensure a shared understanding of the current environment of sponsored research. Additionally, the Research Foundation will use this shared understanding as the base from which to formulate a business model that will help secure the continued success of sponsored research at The Ohio State University.

**THE OHIO STATE UNIVERSITY RESEARCH FOUNDATION**  
**(A Component Unit of The Ohio State University)**

**STATEMENT OF NET ASSETS**  
**AS OF JUNE 30, 2007**

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	<b>2007</b>
<b>ASSETS</b>	
CURRENT ASSETS:	
Cash and cash equivalents	\$ 35,971,442
Accounts receivable and unbilled project costs	56,293,710
Other receivables	<u>650,280</u>
Total current assets	92,915,432
FURNITURE AND EQUIPMENT — Net of accumulated depreciation of approximately \$ 958,349 in 2007	<u>826,724</u>
TOTAL	<u>\$ 93,742,156</u>
<b>LIABILITIES AND NET ASSETS</b>	
CURRENT LIABILITIES:	
Accounts payable:	
Trade	\$ 10,851,772
Unclaimed funds	437,215
Accrued payroll	1,608,387
Accrued vacation and sick leave	28,210
Deferred revenue — sponsors	54,192,917
Facilities and administrative costs payable to University departments	17,756,696
Designated funds for University departments	<u>466,476</u>
Total current liabilities	85,341,673
ACCRUED VACATION AND SICK LEAVE — Long term	<u>349,676</u>
Total liabilities	<u>85,691,349</u>
NET ASSETS:	
Invested in capital assets	826,724
Unrestricted	<u>7,224,083</u>
Total net assets	<u>8,050,807</u>
TOTAL	<u>\$ 93,742,156</u>

See notes to financial statements.

**THE OHIO STATE UNIVERSITY RESEARCH FOUNDATION**  
**(A Component Unit of The Ohio State University)**

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS**  
**FOR THE YEAR ENDED JUNE 30, 2007**

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	<b>2007</b>
OPERATING REVENUES — Sponsor project revenue	<u>\$377,114,762</u>
Total operating revenues	<u>377,114,762</u>
OPERATING EXPENSES:	
Sponsor project:	
Personnel	175,463,288
Materials and services	98,034,949
Equipment	20,063,354
Travel	7,548,297
Facilities and administrative cost charged by the University	76,004,874
Research administration	8,060,259
Depreciation	239,989
Other operating expense	<u>191,474</u>
Total operating expenses	<u>385,606,484</u>
OPERATING LOSS	(8,491,722)
NONOPERATING REVENUES AND EXPENSES:	
University appropriation	7,564,563
Interest income — net of interest expense	<u>856,327</u>
DECREASE IN NET ASSETS	(70,832)
NET ASSETS — Beginning of year	<u>8,121,639</u>
NET ASSETS — End of year	<u>\$ 8,050,807</u>

See notes to financial statements.

**THE OHIO STATE UNIVERSITY RESEARCH FOUNDATION**  
**(A Component Unit of The Ohio State University)**

**STATEMENT OF CASH FLOWS**  
**FOR THE YEARS ENDED JUNE 30, 2007**

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	<b>2007</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>	
Received from sponsors	\$ 397,095,531
Payments to employees	(183,607,036)
Payments to suppliers	<u>(198,504,832)</u>
Net cash provided by operating activities	<u>14,983,663</u>
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES — University appropriations</b>	<u>7,564,563</u>
Net cash provided by noncapital financing activities	<u>7,564,563</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES — Purchases of furniture and equipment</b>	<u>(427,340)</u>
Net cash used in capital and related financing activities	<u>(427,340)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES —</b>	
Interest on cash investments	<u>856,327</u>
Net cash provided by investing activities	<u>856,327</u>
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>22,977,213</b>
<b>CASH AND CASH EQUIVALENTS — Beginning of year</b>	<u>12,994,229</u>
<b>CASH AND CASH EQUIVALENTS — End of year</b>	<u>\$ 35,971,442</u>

(Continued)

**THE OHIO STATE UNIVERSITY RESEARCH FOUNDATION**  
**(A Component Unit of The Ohio State University)**

**STATEMENT OF CASH FLOWS**  
**FOR THE YEARS ENDED JUNE 30, 2007**

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	<b>2007</b>
OPERATING ACTIVITIES:	
Operating loss	\$ (8,491,722)
Adjustments to reconcile operating loss to net cash used in operating activities:	
Depreciation	239,989
Decrease (increase) in operating assets and increase (decrease) in operating liabilities:	
Accounts receivable and unbilled project costs	14,879,413
Other receivables	243,475
Accounts payable — trade	2,943,655
Unclaimed Funds	437,215
Accrued payroll	(77,403)
Accrued vacation and sick leave	(6,086)
Deferred revenue — sponsors	4,796,756
Facilities and administrative costs payable to University departments	(42,754)
Designated funds for University departments	<u>61,125</u>
Net cash generated by operating activities	<u>\$ 14,983,663</u>

See notes to financial statements.

(Concluded)

# THE OHIO STATE UNIVERSITY RESEARCH FOUNDATION (A Component Unit of The Ohio State University)

## NOTES TO FINANCIAL STATEMENTS AS OF AND FOR THE YEAR ENDED JUNE 30, 2007

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### 1. ORGANIZATION

The Ohio State University Research Foundation (the “Research Foundation”), a component unit of The Ohio State University (the “University”), is a nonprofit educational corporation created in 1936 as a vehicle to promote the development, implementation, and coordination of sponsored research at the University in the furtherance of the University’s educational objectives. The Research Foundation’s financial statements and accounts are consolidated with the University’s for purposes of complying with the University’s reporting requirements.

### 2. ACCOUNTING POLICIES

The following is a summary of certain significant accounting policies followed in the preparation of the financial statements:

**Basis of Presentation** — The financial statements of the Research Foundation have been prepared on an accrual basis in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (“GASB”) including Statement No. 34, *Basic Financial Statements — and Management’s Discussion and Analysis — for State and Local Governments*, and GASB Statement No. 35, *Basic Financial Statements — and Management’s Discussion and Analysis — for Public Colleges and Universities (an amendment of GASB Statement No. 34)*. The presentation required by GASB Statement No. 34 and GASB Statement No. 35 provides a comprehensive, entity-wide perspective of the Research Foundation’s assets, liabilities, net assets, revenue, expenses, and changes in net assets, and cash flows.

The Research Foundation follows all GASB pronouncements as well as Financial Accounting Standards Board (“FASB”) Statements and Interpretations, Accounting Principles Board (“APB”) Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. The Research Foundation has elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

**Revenue Recognition** — Substantially all of the Research Foundation’s revenues are derived from restricted grants and cost reimbursement contracts which provide for the recovery of direct and related facilities and administrative costs, subject to audit. The Research Foundation recognizes revenue associated with direct costs as the related costs are incurred. Recovery of related facilities and administrative costs is generally recorded at fixed rates negotiated with the Department of Health and Human Services, the cognizant federal audit agency.

Revenues derived from grants and contracts are reported as operating revenues. Transactions which are capital, finance, or investment-related are reported as nonoperating revenues. University appropriations and interest earned on cash investments are reported as nonoperating revenues.

**Cash and Cash Equivalents** — Cash and cash equivalents consist of demand deposit accounts and certificates of deposit with original maturities of less than 90 days. The Research Foundation’s cash is in the University’s account and is commingled with other University-related entities and invested daily in overnight investment vehicles, which are considered cash equivalents. However they are not required to be categorized under GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*. Investment income is allocated to the Research Foundation based on their ownership of the funds included in the University’s account.

**Accounts Receivable and Unbilled Project Costs** — Receivables are reported at their gross value when earned as the underlying exchange transaction occurs. An estimated receivable has been recorded for services rendered but not yet billed as of June 30, 2007. The receivable was arrived at primarily by taking the subsequent payments of expenses related to cost reimbursement contracts invoiced after year-end, and recording at year-end the portions incurred and reimbursable from sponsors as of year-end.

**Furniture and Equipment** — Furniture and equipment are recorded at cost and the capitalization threshold is \$3,000. Provision is made for depreciation of physical properties at rates calculated to absorb costs generally over the asset’s estimated useful life of five years. Depreciation is calculated using the straight-line method. Depreciation expense was \$239,989 for the year ended June 30, 2007.

Expenditures for maintenance and repairs are charged to operating expenses as incurred; major renewals and betterments are capitalized.

	June 30, 2006	Additions	Disposal	June 30, 2007
Capital assets:				
Furniture and equipment	\$ 1,387,075	\$ 427,340	\$ (29,342)	\$ 1,785,073
Less accumulated depreciation	<u>747,702</u>	<u>239,989</u>	<u>(29,342)</u>	<u>958,349</u>
Net capital assets	<u>\$ 639,373</u>	<u>\$ 187,351</u>	<u>\$ -</u>	<u>\$ 826,724</u>

**Compensated Absences** — Research Foundation employees earn vacation and sick leave on a monthly basis. Classified civil service employees may accrue vacation benefits up to a maximum of three years credit. Administrative and professional staff and faculty may accrue vacation benefits up to a maximum of 240 hours. For all classes of employees, any earned but unused vacation benefit is payable upon termination.

Sick leave may be accrued without limit. However, earned but unused sick leave benefits are payable only upon retirement from the Research Foundation with ten or more years of service with the state. The amount of sick leave benefit payable at retirement is one fourth of the value of the accrued but unused sick leave up to a maximum of 240 hours.

Activity for the year ended June 30, 2007, are as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Compensated Absences					
2007	\$ 383,972	\$ -	6,086	\$ 377,886	\$ 28,210

**In-Kind Income** — The Research Foundation is a component unit of the University. As part of the relationship, transfers of funds occur between the University and the Research Foundation for certain sponsored project expenditures and research administration.

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

**New Accounting Pronouncements** — In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. This Statement establishes standards for the measurement, recognition, and display of OPEB expense/expenditures and related liabilities (assets), note disclosures, and, if applicable, required supplementary information in the financial reports of state and local governmental employers. This Statement is effective for periods beginning after December 15, 2006.

In September 2006, GASB issued Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*. This Statement establishes criteria that governments will use to ascertain whether the proceeds received should be reported as revenue or as a liability. This Statement also includes guidance to be used for recognizing other assets and liabilities arising from a sale of specific receivables of future revenues, including residual interest and recourse provisions. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2006.

In December 2006, GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. This Statement identifies the circumstances under which a governmental entity would be required to report a liability related to pollution remediation. According to the standard, a government would have to estimate its expected outlays for pollution remediation if it knows a site is polluted and various recognition triggers occur. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2007.

In May 2007, GASB issued Statement No. 50, *Pension Disclosures – an amendment of GASB Statements No. 25 and No. 27*. This statement more closely aligns the financial reporting requirements for pensions with those for other postemployment benefits (OPEB) and, in doing so, enhances information disclosed in notes to financial statements or presented as required supplementary information (RSI) by pension plans and by employers that provide pension benefits. This Statement is effective for periods beginning after June 15, 2007.

In June 2007, GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. This statement establishes standards for the capitalization, amortization and financial reporting of intangible assets, including easements, water rights, timber rights, patents, trademarks, and computer software. The requirements of this Statement are effective for financial statements for periods beginning after June 15, 2009.

The Research Foundation management has not yet determined the impact that implementation of GASB Statement Nos. 45, 48, 49, 50, and 51 will have on the Research Foundation's financial statements.

### 3. DESIGNATED FUNDS FOR UNIVERSITY DEPARTMENTS

Designated funds for University departments represent unrestricted funds resulting from residual amounts from certain completed projects that are for use at the discretion of University departments and funds payable to the University from royalties held by the Research Foundation.

### 4. TAX-EXEMPT STATUS

The Research Foundation is exempt from federal taxes on income under Section 501(c)(3) of the Internal Revenue Code.

### 5. RETIREMENT PLAN

All eligible University personnel assigned to the Research Foundation are covered by the Public Employees Retirement System of Ohio (“OPERS”). Employees may opt out of OPERS and participate in the Alternative Retirement Plan (“ARP”) if they meet certain eligibility requirements.

**Defined Benefit Plans** — OPERS offers statewide cost-sharing multiple-employer defined-benefit pension plans. OPERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefits are established by state statute and are calculated using formulas that include years of service and final average salary as factors. OPERS issues a separate, publicly available financial report that includes financial statements and required supplemental information. The report may be obtained by contacting OPERS at Ohio PERS, 277 East Town Street, Columbus, OH 43215-4642, (614) 222-5601, (800) 222-PERS (7377), or [www.opers.org](http://www.opers.org).

In addition to the retirement benefits described above, OPERS provides postemployment health care benefits.

OPERS currently provides postemployment health care benefits to retirees with ten or more years of qualifying service credit. These benefits are advance-funded on an actuarially determined basis and are financed through employer contributions and investment earnings. OPERS determines the amount, if any, of the associated health care costs that will be absorbed by OPERS. Under Ohio Revised Code (“ORC”), funding for medical costs paid from the funds of OPERS is included in the employer contribution rate. For the fiscal year ended December 31, 2006, OPERS allocated 4.5% of the employer contribution rate to fund the health care program for retirees.

The actuarial value of assets available for these benefits at December 31, 2005, (the date of the system’s latest actuarial review), was \$11.1 billion. There were 369,214 active contributing participants as of December 31, 2006 and 358,804 active contributing participants used in the December 31, 2005, actuarial valuation.

On September 9, 2004, the OPERS Retirement Board adopted a Health Care Preservation Plan (“HCPP”) with an effective date of January 1, 2007. In response to skyrocketing health care costs, the HCPP restructured OPERS’ health care coverage to improve the financial solvency of the fund by creating a separate investment tool for health care coverage.

Under the HCPP, retirees eligible for health care coverage will receive a graded monthly allocation based on their years of service at retirement. HCPP incorporates a cafeteria approach, offering a broad range of health care options which allows benefit recipients to use their monthly allocation to purchase health care coverage customized to meet their individual needs. If the monthly allocation exceeds the cost of the options selected, the excess is deposited into a Retiree Medical Account that can be used to fund future health care expenses.

**Defined Contribution Plan** — The ARP is a defined-contribution pension plan. Full-time administrative and professional staff and faculty may choose to enroll in ARP in lieu of OPERS. Classified civil service employees hired on or after August 1, 2005, are also eligible to participate in ARP. ARP does not provide disability benefits, annual cost-of-living adjustments, postretirement health care benefits, or death benefits to plan members and beneficiaries. Benefits are entirely dependent on the sum of contributions and investment returns earned by each participant’s choice of investment options.

OPERS also offers a defined-contribution plan, the Member-Directed Plan (“MD”). The MD does not provide disability benefits, annual cost-of-living adjustments, postretirement health care benefits or death benefits to plan members and beneficiaries. Benefits are entirely dependent on the sum of contributions and investment returns earned by each participant’s choice of investment options.

**Combined Plans** — OPERS also offers a combined plan. This is a cost-sharing multiple-employer defined-benefit plan that has elements of both a defined-benefit and defined-contribution plan. In the combined plan, employee contributions are invested in self-directed investments, and the employer contribution is used to fund a reduced defined benefit. Employees electing the combined plan receive postretirement health care benefits. OPERS provides retirement, disability, survivor, and postretirement health care benefits to qualifying members of the combined plan.

**Funding Policy** — ORC provides OPERS statutory authority to set employee and employer contributions. Contributions equal to those required by OPERS are required for ARP. For employees enrolling in ARP, ORC requires a portion (which may be revised pursuant to periodic actuarial studies) of the employer contribution be contributed to OPERS to enhance the stability of these plans. On January 1, 2007, the OPERS employee contribution rate increased from 9.0% to 9.5% and the employer contribution rate increased from 13.54% to 13.77%. The required contributions rates (as a percentage of covered payrolls) for plan members and the Research Foundation are as follows for 2007, 2006, and 2005:

	<b>Share</b>	<b>Share</b>
July 1, 2004 — June 30, 2005	8.5 %	13.31 %
July 1, 2005 — June 30, 2006	9.0	13.54
July 1, 2006 — June 30, 2007	9.5	13.77

For the years ended June 30, 2007, 2006, and 2005, the Research Foundation reimbursed the University for the following costs for contributions associated with the retirement plans:

Years Ending	Contributions	
	PERS	ARP
2005	\$561,041	\$ 99,092
2006	576,138	100,294
2007	584,467	102,161

## 6. COMMITMENTS AND CONTINGENCIES

The Research Foundation, as an associated foundation, is covered under the University's self-insurance arrangements and commercial insurance policies. The University is self-insured for employee health care benefits; and employee life, accidental death, and dismemberment benefits. Additional details regarding these self-insurance arrangements are provided in Note 6 to the University's financial statements. The University also carries commercial insurance policies for various property, casualty, and excess liability risks. Over the past three years, settlement amounts related to these insured risks have not exceeded the University's coverage amounts.

Under the terms of federal grants, periodic audits are required and certain costs may be questioned as not being appropriate expenditures under the terms of the grants. Such audits could lead to reimbursements to the grantor agencies. While questioned costs may occur, ultimate repayments required of the Research Foundation have been infrequent in prior years.

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## **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 Directors of  
The Ohio State University Research Foundation  
Columbus, Ohio

We have audited the financial statements of The Ohio State University Research Foundation (the "Research Foundation") as of and for the year ended June 30, 2007, and have issued our report thereon dated October 17, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Governmental Auditing Standards*, issued by the Comptroller General of the United States.

### **Internal Control Over Financial Reporting**

In planning and performing our audit, we considered the Research Foundation's internal control over financial reporting as a basis for designing our auditing procedures 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 Research Foundation's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Research Foundation's internal control over financial reporting.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the Research Foundation's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

## Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Research Foundation's financial statements are free of 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 that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of the Research Foundation in a separate letter dated October 17, 2007.

This report is intended solely for the information and use of the Board of Directors, management of the Research Foundation, federal awarding agencies, state funding agencies, pass-through entities, and the Auditor of the State of Ohio, and is not intended to be, and should not be, used by anyone other than these specified parties.

*Deloitte + Touche LLP*

October 17, 2007