



STATE OF NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT OF

NORTH CAROLINA CENTRAL UNIVERSITY

DURHAM, NORTH CAROLINA

FOR THE YEAR ENDED JUNE 30, 2002

OFFICE OF THE STATE AUDITOR

RALPH CAMPBELL, JR.

STATE AUDITOR

FINANCIAL STATEMENT AUDIT REPORT OF

NORTH CAROLINA CENTRAL UNIVERSITY

DURHAM, NORTH CAROLINA

FOR THE YEAR ENDED JUNE 30, 2002

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Ralph Campbell, Jr.
State Auditor

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AUDITOR'S TRANSMITTAL

The Honorable Michael F. Easley, Governor
The General Assembly of North Carolina
Board of Trustees, North Carolina Central University

This report presents the results of our financial statement audit of North Carolina Central University, a constituent institution of the sixteen-campus University of North Carolina System, which is a component unit of the State of North Carolina, for the year ended June 30, 2002. Our audit was made by authority of Article 5A of Chapter 147 of the General Statutes.

The accounts and operations of the University are an integral part of the State's reporting entity represented in the State's *Comprehensive Annual Financial Report (CAFR)* and the State's *Single Audit Report*. In those reports, the State Auditor expresses an opinion on the State's financial statements. In the *Single Audit Report*, the State Auditor also presents the audit results on the State's internal controls and on the State's compliance with laws, regulations, contracts, and grants applicable to the State's financial statements and to its federal financial assistance programs.

As part of the audit work necessary for the CAFR and the *Single Audit Report*, the accounts and operations of the University were subjected to audit procedures as we considered necessary. In addition, we performed auditing procedures that we considered necessary for us to report on the accompanying financial statements that relate solely to North Carolina Central University. The audit procedures were conducted in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards* issued by the Comptroller General of the United States.

The purpose of this report is to present the results of our audit on the accompanying financial statements that relate solely to North Carolina Central University. A summary of our reporting objectives and audit results is:

- 1. Objective** – To express an opinion on the accompanying financial statements that relate solely to North Carolina Central University.

Results - The accompanying financial statements present fairly, in all material respects, the amounts and disclosures made in accordance with accounting principles generally accepted in the United States of America. These matters are more fully described in the Independent Auditor's Report on the Financial Statements.

AUDITOR'S TRANSMITTAL (CONCLUDED)

2. **Objective** – To present significant deficiencies, if any, in internal control over financial reporting which could adversely affect the University's ability to record, process, summarize, and report financial data in the financial statements and present instances of noncompliance, if any, with laws, regulations, contracts, or grants.

Results - Our tests disclosed no material weaknesses in internal control over financial reporting and no instances of noncompliance which require disclosure herein under *Government Auditing Standards*. These matters are more fully described in the Independent Auditor's Report on Compliance and on Internal Control over Financial Reporting.

North Carolina General Statutes require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.



Ralph Campbell, Jr.
State Auditor

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Ralph Campbell, Jr.
State Auditor

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
North Carolina Central University
Durham, North Carolina

We have audited the accompanying basic financial statements of North Carolina Central University, a constituent institution of the sixteen-campus University of North Carolina System, which is a component unit of the State of North Carolina, as of and for the year ended June 30, 2002, as listed in the table of contents. These financial statements are the responsibility of the University'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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes 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, the financial statements referred to above present fairly, in all material respects, the financial position of North Carolina Central University as of June 30, 2002, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 17 to the financial statements, the University implemented Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – For Public Colleges and Universities* and Statement No. 38, *Certain Financial Statement Note Disclosures* during the year ended June 30, 2002.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 13, 2003 on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with

INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

The Management's Discussion and Analysis (MD&A) on pages 3 to 9 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. 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 express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. Schedule 1 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit 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.



Ralph Campbell, Jr.
State Auditor

June 13, 2003

MANAGEMENT'S DISCUSSION AND ANALYSIS

Management's Discussion and Analysis is intended to give the reader an overview of factors that have affected operations and may affect operations in the future. The University is required by the Governmental Accounting Standards Board's (GASB) Statement No. 34/35 to present three basic financial statements. Those statements are the Statement of Net Assets, Statement of Revenues, Expenses, and Changes in Fund Net Assets, and the Statement of Cash Flows. These statements provide both long-term and short-term financial information for North Carolina Central University.

Brief Institutional Highlights

In addition to the University's current degree offerings, four more instructional programs are in developmental stages. Those programs are B.S. in Computer Information Systems, Distance Education Degree in Elementary Education, B.A. in Mass Communication, and a Ph.D. in Communication Disorders.

The University was allocated \$121 million from the State's Higher Education Bond Referendum. Many projects have been fast-tracked to the design phase. Additionally, as part of our expansion plans for more academic buildings and housing, the University has acquired several properties.

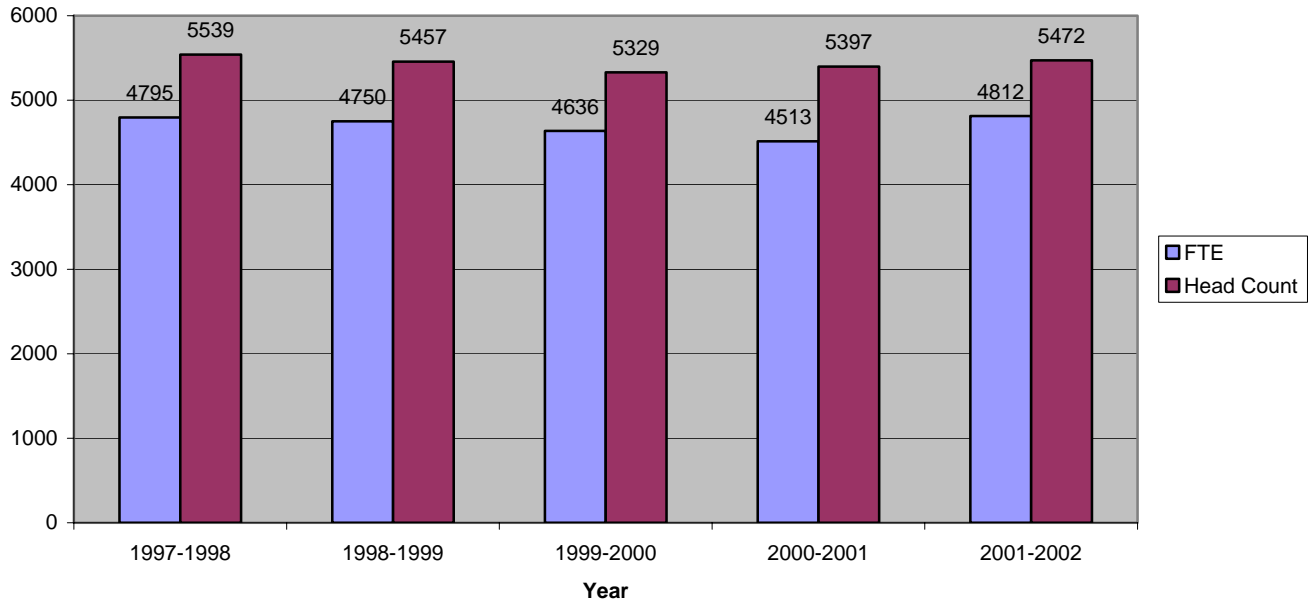
Sponsored research dollars reached a record \$23.8 million. The Office of Institutional Advancement secured private cash, grants, and awards of more than \$9.5 million. Faculty and Staff giving increased by 63%.

State appropriations were cut by approximately \$4.5 million. The budget reduction presented challenges that the University met head on by not filling vacancies in all areas and reducing spending on capital items and supplies.

Student enrollment increased 6.6%. The University continues to strive to recruit talented students and faculty that will stimulate those minds in search of excellence.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FTE and Head Count from 1998 to 2002



Financial Highlights

North Carolina Central University Condensed Statement of Net Assets

	2002
Assets	
Current Assets	\$ 19,698,227
Capital Assets, Net	84,862,967
Other Assets	26,851,535
Total Assets	131,412,729
Liabilities	
Current Liabilities	7,629,634
Noncurrent Liabilities	15,337,345
Total Liabilities	22,966,979
Net Assets	
Invested in Capital Assets, Net of Related Debt	73,828,315
Restricted - Expendable	16,467,687
Restricted - Nonexpendable	9,434,875
Unrestricted	8,714,873
Total Net Assets	\$ 108,445,750

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

The Statement of Net Assets reports all assets and liabilities of the University; additionally, the Statement classifies those assets and liabilities as current and noncurrent depending on the availability of the assets or satisfaction of the obligation within 12 months (current) or longer. This Statement also reports the net assets, which is the difference between the total assets and total liabilities. The reader may use the net assets to gauge the financial position of the University as of June 30, 2002.

As of June 30, 2002, the University's total assets were \$131.4 million. Of this total, \$84.9 million was capital assets (buildings, machinery, infrastructure, land, and construction in progress), net of accumulated depreciation as applicable.

The University's liabilities totaled \$23 million with the debt service on housing and stadium bonds totaling \$10.9 million (current and noncurrent portion). The total current liability of \$7.6 million is well covered by current assets of \$19.7 million, which indicates the University's ability to pay current liabilities as they become due. Total net assets were \$108.4 million, which was a decrease of \$3.2 million from the prior year.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Condensed Financial Statements

North Carolina Central University
Condensed Statement of Revenues, Expenses, and Changes in Fund Net Assets

	<u>2002</u>
Operating Revenues	
Student Tuition and Fees, Net	\$ 11,131,978
Grants and Contracts	14,919,133
Sales and Services, Net	14,961,926
Other Operating Revenues	<u>368,973</u>
Total Operating Revenues	<u>41,382,010</u>
Operating Expenses	<u>97,787,818</u>
Operating Loss	(56,405,808)
Nonoperating Revenues and Expenses	
State Appropriations	41,720,970
Noncapital Grants	5,059,249
Noncapital Gifts	2,651,553
Investment Income, Net	(799,065)
Other Nonoperating Revenues (Expenses)	<u>(532,832)</u>
Loss Before Other Revenues, Expenses, Gains or Losses	<u>(8,305,933)</u>
Capital Grants	<u>5,121,411</u>
Total Other Revenues	<u>5,121,411</u>
Decrease in Net Assets	<u>(3,184,522)</u>
Net Assets - Beginning of Year as Restated	<u>111,630,272</u>
Net Assets - End of Year	<u><u>\$ 108,445,750</u></u>

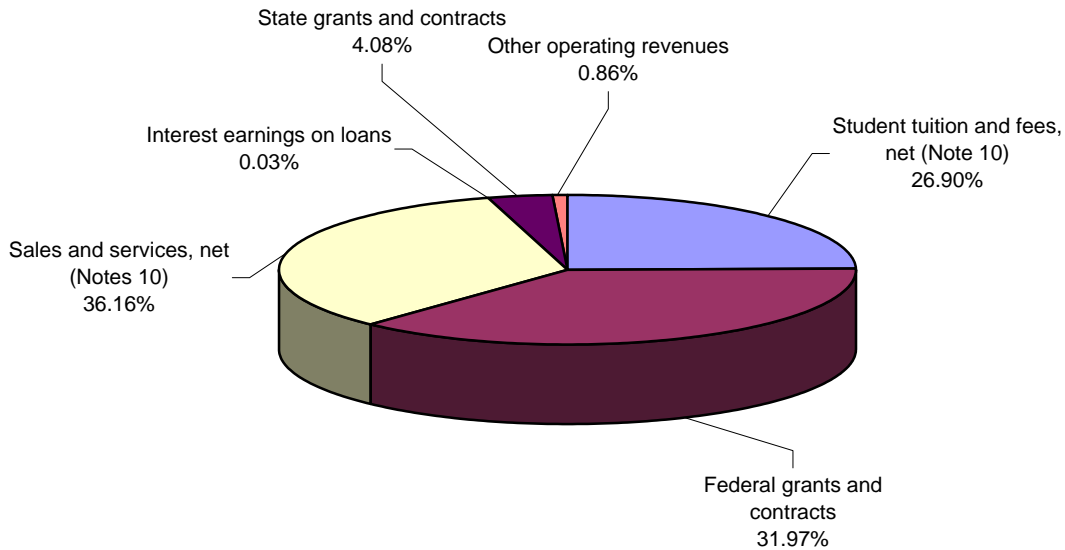
The Statement of Revenues, Expenses, and Changes in Fund Net Assets reports the revenues earned and expenses incurred during the fiscal year. The increase or decrease of revenues over expenses directly affects (increases/decreases) the total net assets reported on the Statement of Net Assets. These transactions are classified as operating or nonoperating. Operating revenues primarily consist of student tuition and fees reported net of discounts and scholarship allowances, federal and State contracts and grants, and auxiliary sales and services revenues. Operating expenses primarily consist of salaries, supplies, services, scholarships, utilities, and depreciation.

Nonoperating revenues stem from transactions that occur outside of the primary scope of the University's existence and for which no goods or services are provided. State appropriations, capital grants, and noncapital grants and gifts primarily represent the nonoperating revenues.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

The University sustained a total operating loss of \$56.4 million. This is mostly explained by the categorization of State appropriations (a major source of funding) as nonoperating revenues. The nonoperating revenues totaled \$48.1 million, with the State appropriations representing 87% of that total. Due to budget restraints of the State of North Carolina, the University suffered State budget cuts of approximately \$4.5 million of the appropriations.

Operating Revenues by Source



**North Carolina Central University
Condensed Statement of Cash Flows
For the Year Ended June 30, 2002**

	<u>Amount</u>
Cash Provided (Used by)	
Operating Activities	\$ (51,491,060)
Noncapital Financing Activities	48,947,851
Capital Financing Activities	(220,668)
Investing Activities	<u>25,744</u>
Net Decrease in Cash and Cash Equivalents	(2,738,133)
Cash and Cash Equivalents - Beginning of Year	<u>24,021,206</u>
Cash and Cash Equivalents - End of Year	<u><u>\$ 21,283,073</u></u>

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

A very useful measure of financial operations is the Statement of Cash Flows. This Statement provides the sources of cash inflows and outflows for four major activities: operating, noncapital financing, capital and related financing, and investing activities. The Ending Cash and Cash Equivalents on this Statement correspond directly with the sum of the cash and cash equivalents balances on the Statement of Net Assets.

The net cash from operating activities shows a net outflow of funds of \$51.5 million. The major outflows were payments to employees for services (\$54.3 million), vendors for goods and services (\$35.7 million), and students for educational assistance (\$3.6 million). The major sources of operating inflows were student tuition and fees (\$11.1 million), auxiliary sales (\$15.0 million), and contracts/grants (\$14.9 million).

The net cash from noncapital financing activities is an inflow of \$48.9 million. As previously referenced, State appropriations of \$41.7 million account for the bulk of this inflow.

Cash flow from capital and related financing activities is a net outflow of \$220,668. The bulk of this net inflow results from the receipt of the Higher Education bond monies of which North Carolina Central University received approximately \$3.1 million in fiscal 2002. Moreover, the University expended \$3.3 million for capital assets and debt service.

The University has a net cash inflow from investing activities of \$25,744. This results from the purchases of investments of \$725,326, investment income of \$557,346, and proceeds from the sales of investments in the amount of \$193,724.

Economic Outlook

Looking toward the future, management believes that North Carolina Central University is uniquely positioned to sustain its financial position. However, it is the vision of our new and innovative management team to continually improve our financial and academic positions.

There are several factors that will impact the economic outlook for the University. Those factors are student enrollment, employment of the bonds funds for campus expansion, research grants, private gifts, and State funding.

The University is deeply pleased with the increase in enrollment in academic year 2001-2002. The enrollment for 2002-2003 has exceeded expectation, with enrollment at an all-time high of 6,521 students. Through diligent recruitment efforts, we expect enrollment to steadily grow. The University is student centered and committed to providing students with a challenging learning environment.

The learning environment is a vital part of higher education. The University was allocated \$121 million from the State's Higher Education Bond referendum to expand the campus and begin major construction projects. Additionally, the campus is renovating academic and auxiliary buildings. All of these projects will enable more advanced technological instructional techniques and living conditions for current and prospective students.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONCLUDED)

North Carolina Central University's faculty is steadily writing, applying, and receiving research grant funds. Research is one of three components that faculty must strive to accomplish. The Sponsored Research Office works diligently with faculty to provide ongoing training and opportunities for research. Grants dollars awarded have increased \$3,000,000 over the record level reached at the end of the 2002 academic year.

With the turn down in the State's economy, private gifts from corporate sponsors and alumni are critical to the success of the University's mission. Utilizing the "industry cluster" concept, the Office of Institutional Advancement is poised to present the assets of the University to potential donors for consideration in their annual giving programs. Overall, giving has increased.

Although State funding was down due to the economic conditions, the University will be eligible to receive "enrollment growth" monies resulting from the increase in enrollment in the prior year. These "growth" funds will allow the University to continue providing excellent academic and administrative services. We are committed to honoring the legacy of leadership of this University; hence, we will go forth with truth and service.

North Carolina Central University
Statement of Net Assets
June 30, 2002

Exhibit A

ASSETS

Current Assets:

Cash and Cash Equivalents	\$	8,916,705
Restricted Cash and Cash Equivalents		2,342,738
Restricted Short-Term Investments		682,991
Receivables, Net (Note 5)		6,934,447
Inventories		528,508
Notes Receivable, Net (Note 5)		292,838
Total Current Assets		19,698,227

Noncurrent Assets:

Restricted Cash and Cash Equivalents		10,023,630
Receivables, Net (Note 5)		16,000
Restricted Due from Primary Government		2,046,803
Endowment Investments		12,238,665
Other Long-Term Investments		474,625
Notes Receivable, Net (Note 5)		2,051,812
Capital Assets, Net (Note 6)		84,862,967
Total Noncurrent Assets		111,714,502

Total Assets

131,412,729

LIABILITIES

Current Liabilities:

Accounts Payable and Accrued Liabilities (Note 7)		6,437,840
Due to Primary Government		89,865
Deferred Revenue		311,864
Interest Payable		111,873
Long-Term Liabilities - Current Portion (Note 8)		678,192
Total Current Liabilities		7,629,634

Noncurrent Liabilities:

Deposits Payable		400
Funds Held for Others		38,949
U. S. Government Grants Refundable		2,293,856
Long-Term Liabilities (Note 8)		13,004,140
Total Noncurrent Liabilities		15,337,345

Total Liabilities

22,966,979

North Carolina Central University
Statement of Net Assets
June 30, 2002

Exhibit A

Page 2

NET ASSETS

Invested in Capital Assets, Net of Related Debt	73,828,315
Restricted for:	
Nonexpendable:	
Scholarships and Fellowships	3,853,379
Endowed Professorships	5,318,510
Loans	262,986
Expendable:	
Scholarships and Fellowships	830,527
Research	1,030,136
Endowed Professorships	2,194,217
Departmental Uses	427,671
Capital Projects	11,061,721
Debt Service	761,950
Library Acquisitions	644
Instruction and Educational Service Agreements	160,821
Unrestricted	8,714,873
Total Net Assets	\$ 108,445,750

The accompanying notes to the financial statements are an integral part of this statement.

North Carolina Central University
Statement of Revenues, Expenses, and
Changes in Net Assets
For the Fiscal Year Ended June 30, 2002

Exhibit B

REVENUES

Operating Revenues:

Student Tuition and Fees, Net (Note 10)	\$	11,131,978
Federal Grants and Contracts		13,229,413
State and Local Grants and Contracts		1,689,720
Sales and Services, Net (Note 10)		14,961,926
Interest Earnings on Loans		12,028
Other Operating Revenues		356,945
Total Operating Revenues		41,382,010

EXPENSES

Operating Expenses:

Salaries and Benefits		54,744,579
Supplies and Materials		16,530,809
Services		16,308,078
Scholarships and Fellowships		3,569,981
Utilities		2,511,818
Depreciation		4,122,553
Total Operating Expenses		97,787,818
Operating (Loss)		(56,405,808)

NONOPERATING REVENUES (EXPENSES)

State Appropriations		41,720,970
Noncapital Grants		5,059,249
Noncapital Gifts, Net (Note 10)		2,651,553
Investment Income (Net of Investment Expense of \$44,802)		(799,065)
Interest and Fees on Capital Asset-Related Debt		(624,630)
Other Nonoperating Revenues (Expenses)		91,798

Net Nonoperating Revenues 48,099,875

Income Before Other Revenues, Expenses, Gains, or Losses (8,305,933)

Capital Grants 5,121,411

Increase (Decrease) in Net Assets (3,184,522)

NET ASSETS

Net Assets - July 1, 2001, as Restated (Note 18) 111,630,272

Net Assets - June 30, 2002 \$ 108,445,750

The accompanying notes to the financial statements are an integral part of this statement.

North Carolina Central University
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2002

Exhibit C

CASH FLOWS FROM OPERATING ACTIVITIES

Received from Customers	\$	41,979,762
Payments to Employees and Fringe Benefits		(54,361,032)
Payments to Vendors and Suppliers		(35,748,099)
Payments for Scholarships and Fellowships		(3,569,981)
Loans Issued		(662,156)
Collection of Loans		582,486
Interest Earned on Loans		12,261
Other Receipts (Payments)		275,699
Net Cash Used by Operating Activities		(51,491,060)

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

State Appropriations		41,720,970
Grants for Other than Capital Purposes		4,008,814
Noncapital Gifts		2,554,519
Additions to Permanent and Term Endowments		708,651
William D. Ford Direct Lending Receipts		29,085,964
William D. Ford Direct Lending Disbursements		(29,085,964)
Related Activity Agency Disbursements		(136,630)
Other Receipts (Payments)		91,527
Net Cash Provided by Noncapital Financing Activities		48,947,851

CASH FLOWS FROM CAPITAL FINANCING AND RELATED FINANCING ACTIVITIES

Capital Grants		3,074,630
Proceeds from Sale of Capital Assets		271
Acquisition and Construction of Capital Assets		(2,368,616)
Principal Paid on Capital Debt and Leases		(315,000)
Interest and Fees Paid on Capital Debt and Leases		(611,953)
Net Cash Used by Capital Financing and Related Financing Activities		(220,668)

CASH FLOWS FROM INVESTING ACTIVITIES

Proceeds from Sales and Maturities of Investments		193,724
Interest on Investments		557,346
Purchase of Investments and Related Fees		(725,326)
Net Cash Provided by Investing Activities		25,744

Net Decrease in Cash and Cash Equivalents		(2,738,133)
Cash and Cash Equivalents - July 1, 2001		24,021,206
Cash and Cash Equivalents - June 30, 2002	\$	21,283,073

North Carolina Central University
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2002

Exhibit C

Page 2

**RECONCILIATION OF NET OPERATING REVENUES (EXPENSES)
TO NET CASH USED BY OPERATING ACTIVITIES**

Operating (Loss)	\$ (56,405,808)
Adjustments to Reconcile Operating (Loss) to Net Cash Provided (Used) by Operating Activities:	
Depreciation Expense	4,122,553
Other Receipts/Payments	(79,099)
Perkins Interest Income Cancellations/Misc. Income	(1,915)
Decrease in allowances and write-offs	407,384
Nonoperating Other Income (Expense)	60,349
Changes in Assets and Liabilities:	
Receivables (Net)	47,409
Inventories	69,004
Accounts Payable and Accrued Liabilities	(255,588)
Due to Primary Government	(20,138)
Deferred Revenue	125,760
Compensated Absences	518,699
Note Principle Repayments	582,486
Notes Issued	(662,156)
Net Cash Used by Operating Activities	\$ (51,491,060)

NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES

Change in Fair Value of Investments	\$ (1,370,824)
Loss on Disposal of Capital Assets	(60,349)

RECONCILIATION OF CASH AND CASH EQUIVALENTS

Current Assets:	
Cash and Cash Equivalents	8,916,705
Restricted Cash and Cash Equivalents	2,342,738
Noncurrent Assets:	
Restricted Cash and Cash Equivalents	10,023,630
Total Cash and Cash Equivalents - June 30, 2002	\$ 21,283,073

The accompanying notes to the financial statements are an integral part of this statement.

NORTH CAROLINA CENTRAL UNIVERSITY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2002

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

- A. Financial Reporting Entity** - The concept underlying the definition of the financial reporting entity is that elected officials are accountable to their constituents for their actions. As required by accounting principles generally accepted in the United States of America, the financial reporting entity includes both the primary government and all of its component units. An organization other than a primary government serves as a nucleus for a reporting entity when it issues separate financial statements. North Carolina Central University is a constituent institution of the sixteen-campus University of North Carolina System, which is a component unit of the State of North Carolina and an integral part of the State's *Comprehensive Annual Financial Report*.

The accompanying financial statements present all funds belonging to the University. While the Board of Governors of the University of North Carolina System has ultimate responsibility, the Chancellor, the Board of Trustees, and the Board of Trustees of the Endowment Fund have delegated responsibilities for financial accountability of the University's funds. Related foundations and similar non-profit corporations for which the University is not financially accountable are not part of the accompanying financial statements. These entities are not included because they are separately incorporated and there are neither common directors nor other evidence of common control.

- B. Basis of Presentation** - The accompanying financial statements are presented in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

Pursuant to the provisions of GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – For Public Colleges and Universities* effective for the University's year ended June 30, 2002, the full scope of the University's activities is considered to be a single business-type activity (BTA) and accordingly, is reported within a single column in the basic financial statements.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

- C. **Basis of Accounting** - The financial statements of the University have been prepared using the economic resource measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred.

In accordance with GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the University does not apply Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, for proprietary activities, unless the GASB amends its pronouncements to specifically adopt FASB pronouncements issued after that date.

- D. **Cash and Cash Equivalents** – This classification appears on the Statement of Net Assets and the Statement of Cash Flows and includes petty cash, cash on deposit with private bank accounts, money market accounts, and short-term investments with the State Treasurer’s Cash and Investment Pool (a governmental external investment pool). The short-term investment portfolio maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit and withdraw cash at any time without prior notice or penalty.

- E. **Investments** - This classification includes mutual funds and money market funds held by the University. Mutual fund investments are accounted for at fair value, as determined by quoted market prices. The net increase (decrease) in the fair value of investments is recognized as a component of investment income.

Money market funds are reported at cost, if purchased, or at fair value or appraised value at date of gift, if donated.

- F. **Receivables** – Receivables consist of tuition and fees charges to students and charges for auxiliary enterprises’ sales and services. Receivables also include amounts due from the federal government, State and local governments, private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants, and pledges that are verifiable, measurable, and expected to be collected and available for expenditures for which the resource providers conditions have been satisfied. Receivables are recorded net of estimated uncollectible amounts.

- G. **Inventories** – Inventories, consisting of expendable supplies and merchandise for resale, are stated at the lower of cost or market value using the first-in, first-out method.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

- H. Capital Assets** – Capital assets are stated at cost at date of acquisition or fair value at date of donation in the case of gifts. The University capitalizes assets that have a value or cost in excess of \$5,000 at the date of acquisition and an expected useful life of one or more years. Library books are expensed.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 20 to 50 years for infrastructure, 50 years for buildings and 5 to 15 years for equipment.

Art collections are capitalized at cost or fair value at the date of donation. These collections are considered inexhaustible and are therefore not depreciated.

- I. Restricted Assets** – Restricted assets represent assets whose use is restricted by external parties or by law through constitutional provisions or enabling legislation.

- J. Noncurrent Long-Term Liabilities** – Noncurrent long-term liabilities include principal amounts of bonds payable, notes payable, capital lease obligations and compensated absences that will not be paid within the next fiscal year.

Bonds payable are reported net of unamortized premiums or discounts and deferred losses on refundings. The University amortizes bond premiums/discounts over the life of the bonds using the straight-line method. Issuance costs are expensed.

- K. Compensated Absences** - The University's policy is to record the cost of vacation leave when earned. The policy provides for a maximum accumulation of unused vacation leave of 30 days which can be carried forward each January 1st (for SPA employees) and July 1st (for EPA employees) or for which an employee can be paid upon termination of employment. Also, any accumulated vacation leave in excess of 30 days at year-end is converted to sick leave. Under this policy, the accumulated vacation leave for each SPA employee at June 30th equals the leave carried forward at the previous December 31st plus the leave earned, less the leave taken between January 1st and June 30th.

When classifying compensated absences into current and noncurrent, leave is considered taken using a last in, first out method.

- L. Net Assets** – The University's net assets are classified as follows:

Invested in Capital Assets, Net of Related Debt – This represents the University's total investment in capital assets, net of outstanding debt

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of invested in capital assets, net of related debt.

Restricted Net Assets – Nonexpendable – Nonexpendable restricted net assets include endowments and similar type assets whose use is limited by donors or other outside sources and, as a condition of the gift, the principal is to be maintained in perpetuity.

Restricted Net Assets – Expendable – Expendable restricted net assets include resources in which the University is legally or contractually obligated to spend in accordance with restrictions imposed by external parties.

Unrestricted Net Assets – Unrestricted net assets include resources derived from student tuition and fees, sales and services, unrestricted gifts, royalties, and interest income.

Restricted and unrestricted resources are tracked using a fund accounting system and are spent in accordance with established fund authorities. Fund authorities provide rules for the fund activity and are separately established for restricted and unrestricted activities. When both restricted and unrestricted funds are available for expenditure, the decision for funding is transactional based within the departmental management system in place at the University.

- M. Scholarship Discounts** – Student tuition and fees revenues and certain other revenues from University charges are reported net of scholarship discounts in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. The scholarship discount is the difference between the actual charge for goods and services provided by the University and the amount that is paid by students or by third parties on the students' behalf. Student financial assistance grants, such as Pell grants, and other federal, State or nongovernmental programs, are recorded as either operating or nonoperating revenues in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. To the extent that revenues from these programs are used to satisfy tuition, fees, and other charges, the University has recorded a scholarship discount.
- N. Revenue and Expense Recognition** – The University presents its revenues and expenses as operating or nonoperating based on recognition definitions from GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*. Operating activities are those

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

activities that are necessary and essential to the mission of the University. Operating revenues include all charges to customers, grants received for student financial assistance, research contracts and grants, and interest earned on loans. Grants received for student financial assistance are considered operating revenues because they provide resources for student charges and such programs are necessary and essential to the mission of the University. Revenues from nonexchange transactions and State appropriations that represent subsidies or gifts to the University, as well as investment income, are considered nonoperating since these are either capital or noncapital financing or investing activities. Operating expenses are all expense transactions incurred other than those related to capital or noncapital financing or investing activities. Revenues received for capital financing activities, as well as related expenses, are considered neither operating nor nonoperating activities and are presented after nonoperating activities on the accompanying Statement of Revenues, Expenses, and Changes in Net Assets.

- O. Internal Sales Activities** – Certain institutional auxiliary operations provide goods and services to University departments as well as to its customers. These institutional auxiliary operations include activities such as Central stores, Copy Centers, Motor Pool, and Postal Services. In addition, the University has other miscellaneous sales and service units that operated either on a reimbursement or charge basis. All internal sales activities to University departments from auxiliary operations and sales and service units have been eliminated in the accompanying financial statements. These eliminations are recorded by removing the revenue and expense in the auxiliary operations and sales and service units and, if significant, allocating any residual balances to those departments receiving the goods and services during the year.

NOTE 2 - BUDGETING AND BUDGETARY CONTROL

The State of North Carolina operates on a biennial budget cycle with separate annual departmental and institutional certified budgets adopted by the General Assembly.

Chapter 116, Article 1, Part 2A of the North Carolina General Statutes authorizes the universities within the sixteen campus University of North Carolina System to apply for special responsibility status, which sets the legal level of budgetary control at the institution's budget code level. A budget code is a convention used in the State's accounting system to distinguish the type of fund and the responsible department or institution. Budget codes are also used to segregate certain purposes within departments or institutions. Institutions with special responsibility status must still have

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

certain budget revisions, primarily those associated with unanticipated revenues, approved by the Office of State Budget and Management. Additionally, universities must maintain programs and services in accordance with the guidelines established by the Board of Governors of the consolidated University of North Carolina System. North Carolina Central University has applied for and received special responsibility status.

After the budget is approved by the General Assembly and adopted by the Board of Governors, the University follows an established system of budgetary controls. Periodic interim budget statements to department heads guide them in managing budget allocations. Monthly financial reports, which include budget and actual data, are provided for each fund to individual managers responsible for the fund. When actual conditions require changes to the budget, revisions are prepared and communicated to those affected. Changes to the budget are reviewed and approved at the University or State level as required. The University maintains an encumbrance accounting system as another method to ensure that imposed expenditure constraints are observed. The State budgetary control is maintained on a cash basis of accounting.

NOTE 3 - DEPOSITS AND INVESTMENTS

A. Deposits - The University is required by General Statute 147-77 to deposit its budget code cash, as defined in Note 2, and by the University of North Carolina Board of Governors pursuant to General Statute 116-36.1 to deposit its institutional trust funds in the State Treasurer's Cash and Investment Pool. In addition, the University may voluntarily deposit endowment funds, special funds, revenue bond proceeds, and debt service funds with the State Treasurer's Cash and Investment Pool. Special funds consist of moneys for intercollegiate athletics and agency funds held directly by the University.

Deposits include cash and cash equivalents and certificates of deposit totaling \$21,279,563. At year-end, cash on hand was \$3,510. The University's portion of the State Treasurer's Cash and Investment Pool was \$21,278,686. It is the State Treasurer's policy and practice for deposits not covered by federal depository insurance to be covered by collateral held by the State of North Carolina's agent in the name of the State and for his investments to be held by the State's agent in the State's name. The carrying amount of the University's deposits not with the State Treasurer was \$877 and the bank balance was \$877. Of the bank balance, \$877 was covered by federal depository insurance.

North Carolina General Statutes 147-69.1(c), applicable to the State's General Fund, and 147-69.2, applicable to institutional trust funds,

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

authorize the State Treasurer to invest in the following: obligations of or fully guaranteed by the United States; obligations of certain federal agencies; repurchase agreements; obligations of the State of North Carolina; time deposits of specified institutions; prime quality commercial paper, and asset-backed securities with specified ratings. Also, General Statute 147-69.1(c) authorizes the following: specified bills of exchange or time drafts and corporate bonds and notes with specified ratings. General Statute 147-69.2 authorizes the following: general obligations of other states; general obligations of North Carolina local governments; and obligations of certain entities with specified ratings.

The financial statements and disclosures for the State Treasurer's Cash and Investment Pool are included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.state.nc.us/> and clicking on "Financial Reports", or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

- B. Investments** - The University is authorized by The University of North Carolina Board of Governors pursuant to General Statute 116-36.2 to invest its special funds in the same manner as the State Treasurer is required to invest, as previously discussed.

In accordance with the bond resolutions, bond proceeds and debt service funds are invested in obligations which will by their terms mature on or before the date funds are expected to be required for expenditure or withdrawal.

General Statute 116-36(e) provides that the trustees of the Endowment Fund shall be responsible for the prudent investment of the Fund in the exercise of their sound discretion, without regard to any statute or rule of law relating to the investment of funds by fiduciaries but in compliance with any lawful condition placed by the donor upon that part of the Endowment Fund to be invested.

Investments of various funds may be pooled unless prohibited by statute or by terms of the gift or contract. The University utilizes investment pools to manage investments and distribute investment income. The University utilizes the following investment pools:

Scholarship/Professorship Endowment Pool - This is an internal investment pool that is utilized for the investment of the scholarship and professorship endowment funds with less than \$50,000. These funds are invested in a mutual fund. Purchases in the fund are allowed at the

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

beginning of each month. Fund ownership is measured based on the participating funds purchases and accumulated gain/loss reinvestment. The investment strategy, including the selection of investment managers, is based on the directives of the University's Endowment Board.

Credit Risk Categories - The University's investments (pooled and non-pooled) are categorized below to give an indication of the level of risk assumed by the entity at year-end. The credit risk categories are concerned with custodial credit risk, which is the risk that a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party if the counterparty to the investment transaction fails. There are three categories of credit risk. Category 1 includes investments that are insured or registered or for which the securities are held by the University or its agent in the University's name. Category 2 includes uninsured and unregistered investments for which the securities are held by a counterparty's trust department or agent in the University's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the broker or dealer, or by a counterparty's trust department or agent but not in the University's name.

A summary of the University's investments at June 30, 2002 is presented below.

Scholarship/Professorship Investment Pool

Investments Not Categorized:	
Mutual Funds	\$ 544,669

Non Pooled Investments

Investments Not Categorized:	
Money Market Funds	\$ 474,625
Mutual Funds	12,376,987
Total Non Pooled Investments	\$ 12,851,612

Total Investments

Total Investments	\$ 13,396,281
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NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

C. Derivative and Similar Transactions - A derivative is a financial instrument created from, or whose value depends on (is derived from), the value of one or more underlying assets, reference rates, or indexes of asset values. These instruments may include forwards, futures, currency and interest rate swaps, options, floaters/inverse floaters, and caps/floors/collars. During the year the University did invest indirectly in derivatives. As required by accounting principles generally accepted in the United States of America, the nature of derivative or similar transactions entered into by the University, and the reasons for entering into those transactions follow:

Indirect Derivative Holdings - The University identifies various mutual funds that meet asset allocation and investment management objectives. The University invests in these funds to increase the yield and return on its investment portfolio given the available alternative investment opportunities and to diversify its asset holdings. Investments of mutual funds generally include equity and bond funds. Certain funds expose the University to significant amounts of market risk by trading or holding derivative instruments and by leveraging the securities in the fund.

The mutual funds that utilized derivative securities for the fiscal year ending June 30, 2002 are summarized in the chart below. The amounts shown in the chart represent the market value of the University's investment in the mutual funds and the market value and percent of holdings held in derivatives by those funds.

<u>Indirect Derivatives Analysis</u>			
<u>Mutual Fund</u> Common Fund-Domestic Equity	<u>Total Market</u> Value	<u>% Invested</u> Derivatives	<u>Amount</u>
Multi-Strategy Equity Fund	\$ 9,403,498	8.4%	\$ 789,894
Multi-Strategy Bond Fund	3,518,158	29.6%	1,041,375
Total	<u>12,921,656</u>		<u>\$ 1,831,269</u>
Total Fund Market Value For Restricted and Endowment	<u>\$ 12,921,656</u>		

Total % of Market Value for Indirect Dervative Exposure – 14.17%

The Multi-Strategy Equity Fund and Multi-Strategy Bond Fund respectively invest in sub-funds that utilize derivatives for various reasons including: maintaining market exposure, improving liquidity, hedging foreign currency exposure, decreasing transactions costs or implementing investment strategies that will benefit the respective portfolios in certain market conditions. The sponsor of these funds provides the University with audited financial statements on an annual basis.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 4 - ENDOWMENT INVESTMENTS

Investments of the University's endowment funds are separately invested, except for scholarship and professorship endowments with less than \$50,000, which are pooled in a separate investment account. If a donor has not provided specific instructions, State law permits the Board of Trustees to authorize for expenditure the net appreciation, realized and unrealized, of the investments of the endowment funds.

Investment return of the University's endowment funds is predicated on the total return concept (yield plus appreciation). Annual payouts from the University's endowment funds are determined by 5.5% of the five-year moving average of the fund's market value. If current year earnings do not meet the payout requirements, the University uses accumulated income and appreciation to make up the difference. Expenditures in excess of the payout are authorized by the University's Board of Trustees Endowment Committee. At June 30, 2002, net appreciation of \$3,337,929 was available to be spent of which \$257,965 was restricted to specific purposes.

NOTE 5 - RECEIVABLES

Receivables at June 30, 2002 were as follows:

	Gross Receivables	Allowance for Doubtful Accounts	Net Receivables
Current Receivables:			
Students	\$ 3,976,690	\$ 1,766,603	\$ 2,210,087
Accounts	642,537		642,537
Intergovernmental	3,728,204		3,728,204
Pledges	28,750		28,750
Investment Earnings	33,813		33,813
Interest on Loans	120,279		120,279
Other	170,777		170,777
Total Current Receivables	\$ 8,701,050	\$ 1,766,603	\$ 6,934,447
Noncurrent Receivables:			
Pledges	\$ 16,000	\$ 0	\$ 16,000
Notes Receivables:			
Notes Receivable - Current			
Federal Loan Programs	661,656	373,048	288,608
Institutional Student Loan Programs	4,230		4,230
Total Notes Receivable Current	\$ 665,886	\$ 373,048	\$ 292,838
Notes Receivable - Noncurrent:			
Federal Loan Programs	\$ 5,201,981	\$ 3,150,169	\$ 2,051,812

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 6 - CAPITAL ASSETS

A summary of changes in the capital assets is presented as follows:

	Balance July 1, 2001	Increases	Decreases	Balance June 30, 2002
Capital Assets, Non-Depreciable:				
Land	\$ 1,676,925	\$ 267,100	\$ 0	\$ 1,944,025
Art, Literature, and Artifacts	377,240	117,000		494,240
Construction in Progress		2,963,708		2,963,708
Total Capital Assets, Non-Depreciable	<u>2,054,165</u>	<u>3,347,808</u>		<u>5,401,973</u>
Capital Assets, Depreciable:				
Buildings	110,258,094	1,406,798		111,664,892
Machinery and Equipment	9,543,548	989,214	1,073,454	9,459,308
General Infrastructure	14,238,148			14,238,148
Totals	<u>134,039,790</u>	<u>2,396,012</u>	<u>1,073,454</u>	<u>135,362,348</u>
Less Accumulated Depreciation/Amortization for:				
Buildings	43,202,179	1,986,607		45,188,786
Machinery and Equipment	4,708,587	1,529,984	743,940	5,494,631
General Infrastructure	4,611,975	605,962		5,217,937
Totals	<u>52,522,741</u>	<u>4,122,553</u>	<u>743,940</u>	<u>55,901,354</u>
Total capital assets, depreciable, net	<u>81,517,049</u>	<u>(1,726,541)</u>	<u>329,514</u>	<u>79,460,994</u>
Capital Assets, net	<u>\$ 83,571,214</u>	<u>\$ 1,621,267</u>	<u>\$ 329,514</u>	<u>\$ 84,862,967</u>

NOTE 7 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2002 were as follows:

	<u>Totals</u>
Accounts Payable	\$ 4,052,676
Accrued Payroll	2,058,853
Contract Retainage	169,194
Intergovernmental Payables	79,973
Other	<u>77,144</u>
Total accounts payable and accrued liabilities	<u>\$ 6,437,840</u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 8 - LONG-TERM LIABILITIES

A. Changes in Long-Term Liabilities - A summary of changes in the long-term liabilities is presented as follows:

	Balance July 1, 2001	Additions	Reductions	Balance June 30, 2002	Current Portion
Notes, Bonds and Capital Leases Payable					
Bonds Payable	\$ 11,365,000	\$	\$ 315,000	\$ 11,050,000	\$ 330,000
Add/Deduct Premium/Discount	(101,342)		(4,682)	(96,660)	
Total Bonds Payable	11,263,658		310,318	10,953,340	330,000
Capital Leases Payable	106,753			106,753	42,701
Total Notes, Bonds, and Capital Leases	11,370,411		310,318	11,060,093	372,701
Compensated Absences	2,103,540	3,346,374	2,827,675	2,622,239	305,491
Total long-term liabilities	<u>\$ 13,473,951</u>	<u>\$ 3,346,374</u>	<u>\$ 3,137,993</u>	<u>\$ 13,682,332</u>	<u>\$ 678,192</u>

B. Bonds Payable - The University was indebted for bonds payable (net of discount and premium) in the amount of \$10,953,340 at June 30, 2002 for the purposes shown in the following table:

Purpose	Series	Interest Rate/ Ranges	Final Maturity Date	Original Amount of Issue	Principal Paid 6/30/2002	Principal Outstanding 6/30/2002
Housing System Revenue Bonds	1996	5.4% to 5.9%	11/1/2022	\$ 8,890,000	\$ 760,000	\$ 8,130,000
Stadium System Revenue Bonds	1998	4.4% to 5.0%	4/1/2023	3,320,000	400,000	2,920,000
Total Bonds Payable (principal only)				<u>\$ 12,210,000</u>	<u>\$ 1,160,000</u>	11,050,000
Less: Unamortized Discount						<u>96,660</u>
Total Bonds Payable						<u>\$ 10,953,340</u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

C. Annual Requirements - The annual requirements to pay principal and interest on the long-term obligations at June 30, 2002 are as follows:

<u>Fiscal Year</u>	Annual Requirements	
	Bonds Payable	
	Principal	Interest
2003	\$ 330,000	\$ 595,773
2004	350,000	578,833
2005	360,000	560,913
2006	380,000	542,453
2007	405,000	522,743
2008-2012	2,100,000	2,288,407
2013-2017	2,690,000	1,656,364
2018-2022	3,585,000	791,075
2023-2027	850,000	29,175
Total Requirements	\$ 11,050,000	7,565,736

Interest on the variable rate Housing Revenue Bonds is calculated at 5.4 to 5.9% at June 30, 2002.

Interest on the variable rate Stadium Revenue Bonds is calculated at 4.4 to 5.0% at June 30, 2002.

D. Bond Defeasance - The University has extinguished long-term debt obligations by the issuance of new long-term debt instruments as follows:

Dormitory System: On 3/2/1995 the University defeased \$1,020,000 of outstanding *Dormitory Series A, B & C* Revenue Bonds. An irrevocable trust was established with an escrow agent to provide for all future debt service payments on the defeased bonds. The trust assets and the liability for the defeased bonds are not included in the University's balance sheet. As of June 30, 2002, the outstanding balance of the defeased *Dormitory System* Revenue Bonds was \$222,000.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 9 - LEASE OBLIGATIONS

- A. CAPITAL LEASE OBLIGATIONS** - Capital lease obligations relating to educational equipment are recorded at the present value of the minimum lease payments. Future minimum lease payments under capital lease obligations consist of the following at June 30, 2002:

<u>Fiscal Year</u>	<u>Amount</u>
2003	\$ 45,228
2004	45,228
2005	<u>33,921</u>
Total Minimum Lease Payments	\$ 124,377
Amount Representing Interest (6% Rate of Interest)	<u>17,624</u>
Present Value of Future Lease Payments	<u>\$ 106,753</u>

Leased assets amounted to \$194,096 at June 30, 2002.

- B. OPERATING LEASE OBLIGATIONS** - Future minimum lease payments under non-cancelable operating leases consist of the following at June 30, 2002:

<u>Fiscal Year</u>	<u>Amount</u>
2003	<u>\$ 20,204</u>
Total Minimum Lease Payments	<u>\$ 20,204</u>

Rental expense for all operating leases during the year was \$229,134.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 10 - REVENUES

A summary of eliminations and allowances by revenue classification and revenues pledged as security for revenue bonds is presented as follows:

	Gross Revenues	Internal Sales Eliminations	Less Scholarship Discounts	Less Change in Allowance for Uncollectibles	Net Revenues	Revenues Pledged as Security for Debt	
Operating revenues:							
Student tuition and fees	\$ 14,004,772	\$ 0	\$ 3,049,454	\$ (176,660)	\$ 11,131,978	\$ 257,805	(A)
Sales and services:							
Sales and services of auxiliary enterprises:							
Residential life	5,807,418		1,220,289	133,527	4,453,602	5,807,418	(B)
Dining	4,081,162		874,671	13,509	3,192,982		
Student Union services	1,034,831		222,521	3,919	808,391		
Health, physical education and recreation services	1,243,475		266,520	4,027	972,928		
Bookstore	1,666,697	43,815			1,622,882		
Parking	914,637			370	914,267		
Athletic	1,533,042		327,334	10,776	1,194,932		
Other	1,370,683	258,720		10,532	1,101,431		
Sales and services of educational and related activities	701,366	855			700,511		
Total sales and services	\$ 18,353,311	\$ 303,390	\$ 2,911,335	\$ 176,660	\$ 14,961,926	\$ 5,807,418	
Nonoperating - Noncapital gifts	\$ 2,651,553	\$ 0	\$ 0	\$ 0	\$ 2,651,553	\$ 0	

Revenue bonds secured by pledged revenues:

- (A) Stadium System
- (B) Housing System

NOTE 11 - OPERATING EXPENSES BY FUNCTION

The University's operating expenses by functional classification are presented as follows:

	Salaries and Benefits	Supplies and Materials	Services	Scholarships and Fellowships	Utilities	Depreciation	Total
Instruction	\$ 29,305,184	\$ 1,780,828	\$ 1,342,455	\$ 0	\$ 3,083	\$ 0	\$ 32,431,550
Research	1,699,259	458,286	295,219				2,452,764
Public Service	746,210	118,064	219,928		3,974		1,088,176
Academic Support	5,851,733	2,064,610	2,748,255				10,664,598
Student Services	1,893,099	64,913	297,203		3,132		2,258,347
Institutional Support	7,089,493	441,944	1,809,195	1,879			9,342,511
Operations and Maintenance of Plant	2,666,988	8,292,395	2,078,628		2,234,115		15,272,126
Student Financial Aid	434,601		2,120,349	3,150,500			5,705,450
Auxiliary Enterprises	5,058,012	3,309,769	5,396,846	417,602	267,514		14,449,743
Depreciation						4,122,553	4,122,553
Total Operating Expenses	\$ 54,744,579	\$ 16,530,809	\$ 16,308,078	\$ 3,569,981	\$ 2,511,818	\$ 4,122,553	\$ 97,787,818

NOTE 12 - PENSION PLANS

A. Retirement Plans - Each permanent full-time employee, as a condition of employment, is a member of either the Teachers' and State Employees' Retirement System or the Optional Retirement Program. The Teachers' and State Employees' Retirement System (System) is a multiple-employer

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

cost sharing defined benefit pension plan administered by the North Carolina State Treasurer.

After five years of creditable service, members of the Teachers' and State Employees' Retirement System qualify for a vested deferred benefit. Employees who retire on or after age 65 and complete 5 years of membership service (age 55 and 5 years of creditable service for law enforcement officers), reach age 60 with 25 years of membership service, or complete 30 years of creditable service receive a retirement allowance of 1.81% of an average final compensation (based on the 4 consecutive years that produce the highest average) multiplied by the number of years of creditable service. Employees may retire with reduced benefits if they reach age 50 with 20 years of creditable service or reach age 60 with 5 years of creditable service (age 50 with 15 years creditable service for law enforcement officers).

Benefit and contribution provisions for the Teachers' and State Employees' Retirement System are established by North Carolina General Statute 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contributions rates are set each year by the North Carolina General Assembly based on annual actuarial valuations. For the year ended June 30, 2002, these rates were set at 1.97% of covered payroll for employers and 6% of covered payroll for members.

For the year ended June 30, 2002, the University had a total payroll of \$46,113,782 of which \$33,732,332 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were \$2,023,940 and \$664,527, respectively. The University made one hundred percent of its annual required contributions for the years ended June 30, 2002, 2001, and 2000, which were \$664,527, \$1,721,148, and \$2,556,000, respectively.

The Teachers' and State Employees' Retirement System's financial information is included in the State of North Carolina *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.state.nc.us/> and clicking on "Financial Reports", or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

The Optional Retirement Program (Program) is a defined contribution retirement plan, which provides retirement benefits with options for payments to beneficiaries in the event of the participant's death.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Administrators and eligible faculty of the University may join the Program instead of the Teachers' and State Employees' Retirement System. The Board of Governors of The University of North Carolina is responsible for the administration of the Program and designates the companies authorized to offer investment products. The Board has authorized the following carriers: Teachers' Insurance and Annuity Association - College Retirement Equities Fund (TIAA-CREF), Lincoln Life Insurance Company, Variable Annuity Life Insurance Company (VALIC), and Fidelity Investments. Participants may elect to allocate their contributions and the University contributions to any one of the carriers or may direct their contributions to one carrier and the University contributions to another. Each carrier offers a variety of investment funds, including both fixed and variable account investment options and mutual funds.

Participant eligibility and contributory requirements are established by General Statute 135-5.1. Employer and member contributions rates are set each year by the North Carolina General Assembly. For the year ended June 30, 2002, these rates were set at 6.84% of covered payroll for employers and 6% of covered payroll for members. The University assumes no liability other than its contribution.

Participants in the Program are immediately vested in the value of employee contributions. The value of employer contributions is vested after five years of participation in the Program. Participants become eligible to receive distributions when they terminate employment or retire.

For the year ended June 30, 2002, the University had a total payroll of \$46,113,782 of which \$10,082,331 was covered under the Optional Retirement Program. Total employee and employer contributions for pension benefits for the year were \$604,940 and \$689,631, respectively.

- B. Deferred Compensation and Supplemental Retirement Income Plans**
- IRC Section 457 Plan - The State of North Carolina offers its permanent employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457 through the North Carolina Public Employee Deferred Compensation Plan (the Plan). The Plan permits each participating employee to defer a portion of his or her salary until future years. The deferred compensation is available to employees upon separation from service, death, disability, retirement or financial hardships if approved by the Board of Trustees of the Plan. The Board, a part of the North Carolina Department of Administration, maintains a separate fund for the exclusive benefit of the participating employees and their beneficiaries, *the North Carolina Public Employee Deferred Compensation Trust Fund*. The Board also contracts with an external

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

third party to perform certain administrative requirements and to manage the trust fund's assets. All costs of administering and funding the Plan are the responsibility of the Plan participants. No costs are incurred by the University. The voluntary contributions by employees amounted to \$42,573 for the year ended June 30, 2002.

IRC Section 401(k) Plan - All members of the Teachers' and State Employees' Retirement System and the Optional Retirement Program are eligible to enroll in the Supplemental Retirement Income Plan, a defined contribution plan, created under Internal Revenue Code Section 401(k). All costs of administering the plan are the responsibility of the Plan participants. No costs are incurred by the University except for a 5% employer contribution for the University's law enforcement officers, which is mandated under General Statute 143-166.30(e). Total employer contributions on behalf of University law enforcement officers for the year ended June 30, 2002 were \$26,333. The voluntary contributions by employees amounted to \$148,167 for the year ended June 30, 2002.

IRC Section 403(b) and 403(b)(7) Plans - Eligible University employees can participate in tax sheltered annuity plans created under Internal Revenue Code Sections 403(b) and 403(b)(7). The employee's eligible contributions, made through salary reduction agreements, are exempt from federal and State income taxes until the annuity is received or the contributions are withdrawn. These plans are exclusively for employees of universities and certain charitable and other non-profit institutions. All costs of administering and funding these plans are the responsibility of the Plan participants. No costs are incurred by the University. The voluntary contributions by employees amounted to \$833,657 for the year ended June 30, 2002.

NOTE 13 - OTHER POSTEMPLOYMENT BENEFITS

- A. Health Care for Long-Term Disability Beneficiaries and Retirees -** The University participates in state administered programs which provide postemployment health insurance to eligible former employees. Eligible former employees include long-term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers' and State Employees' Retirement System or the Optional Retirement Program. These benefits were established by Chapter 135, Article 3, Part 3, of the General Statutes and may be amended only by the North Carolina General Assembly. Funding for the health care benefit for long-term disability beneficiaries and retirees is financed on a pay-as-you-go basis. The University contributed 2.35% of the covered payroll under the Teachers' and State Employees' Retirement System and the Optional

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Retirement Program for these health care benefits. For the fiscal year ended June 30, 2002, the University's total contribution to the Plan was \$1,029,645. The University assumes no liability for retiree health care benefits provided by the programs other than its required contribution. Additional detailed information about these programs can be located in the State of North Carolina's *Comprehensive Annual Financial Report*.

- B. Long-Term Disability** - The University participates in the Disability Income Plan of North Carolina (DIPNC). Established by Chapter 135, Article 6, of the General Statutes, DIPNC provides short-term and long-term disability benefits to eligible members of the Teachers' and State Employees' Retirement System or the Optional Retirement Program. Long-term disability income benefits are advance funded on an actuarially determined basis using the one-year term cost method. The University contributes .52% of covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the DIPNC. For the fiscal year ended June 30, 2002, the University's total contribution to the DIPNC was \$227,836. The University assumes no liability for long-term disability benefits under the plan other than its contribution. Additional detailed information about the DIPNC is disclosed in the State of North Carolina's *Comprehensive Annual Financial Report*.

NOTE 14 - RISK MANAGEMENT

The University is 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. These exposures to loss are handled via a combination of methods, including participation in State-administered insurance programs, purchase of commercial insurance, and self-retention of certain risks.

Tort claims of up to \$500,000 are self-insured under the authority of the State Tort Claims Act. In addition, the State provides excess public officers' and employees' liability insurance up to \$11,000,000 via contract with a private insurance company. The premium, based on a composite rate, is paid by the University directly to the private insurer.

The State Property Fire Insurance Fund (Fund), an internal service fund of the State, insures all State owned buildings and contents for fire and various other property losses up to \$2,500,000 per occurrence. The Fund purchases excess insurance from private insurers to cover losses over the amounts insured by the Fund. Coverage for fire losses for operations supported by the State's General Fund is provided at no cost to the University. Other operations not supported

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

by the State's General Fund are charged for fire coverage. The University also purchased through the Fund extended coverage, vandalism, theft, and "all risks" for buildings and contents. Losses covered by the Fund are subject to a \$500 per occurrence deductible except theft losses carry a \$1,000 per occurrence deductible. There have been no significant reductions in insurance coverage from the previous year and settled claims have not exceeded coverage in any of the past three fiscal years.

All State-owned vehicles are covered by liability insurance handled by the North Carolina Department of Insurance. The State is self-insured for the first \$500,000 of any loss through a retrospective rating plan. Excess insurance coverage is purchased through a private insurer to cover losses greater than \$500,000. The liability limits for losses occurring in State are \$500,000 per claimant and \$5,000,000 per occurrence. The University is charged premiums to cover the cost of excess insurance and to pay for those losses falling under the self-insured retention.

The University is protected for losses from employee dishonesty and computer fraud. The blanket honesty bond is with a private insurance company and is handled by the North Carolina Department of Insurance with coverage of \$5,000,000 per occurrence and a \$50,000 deductible.

Other coverage not handled by the State Department of Insurance is purchased through the State's insurance agent of record.

Employees and retirees are provided health care coverage by the Comprehensive Major Medical Plan (Plan), a component unit of the State. The Plan is funded by employer and employee contributions and is administered by a third party contractor. Effective for the October 1, 2001 through September 30, 2002 year, the Plan no longer offers health coverage through HMO plans.

The North Carolina Workers' Compensation Program provides benefits to workers injured on the job. All employees of the State and its component units are included in the program. When an employee is injured, the University's primary responsibility is to arrange for and provide the necessary treatment for work related injury. The University is responsible for paying medical benefits and compensation in accordance with the North Carolina Workers' Compensation Act. The University is self-insured for workers' compensation.

Term life insurance of \$25,000 to \$50,000 is provided to eligible workers. This self-insured death benefit program is administered by the State Treasurer's Office and funded via employer contributions.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Additional details on the state-administered risk management programs are disclosed in the State's *Comprehensive Annual Financial Report*, issued by the Office of the State Controller.

NOTE 15 - COMMITMENTS AND CONTINGENCIES

- A. Commitments** - The University has established an encumbrance system to track its outstanding commitments on construction projects and other purchases. Outstanding commitments on construction contracts were \$6,131,873 at June 30, 2002.
- B. Pending Litigation and Claims** – The University is a party to litigation and claims in the ordinary course of its operations. Since it is not possible to predict the ultimate outcome of these matters, no provision for any liability has been made in the financial statements. University management is of the opinion that the liability, if any, for any of these matters will not have a material adverse effect on the financial position of the University.
- C. University Improvement General Obligation Bonds** – The 1999-2000 Session of the General Assembly of North Carolina authorized the issuance of \$2,500,000,000 of general obligation bonds of the State, as subsequently approved by a vote of qualified voters of the State, to provide funds for capital improvements for the University of North Carolina. The funds authorized are to be used solely for capital facilities cost on the University of North Carolina campuses as specified in the legislation. The bond legislation specifies the amount of bond funding for each University campus and the level of bond funding intended for each project. The bonds are authorized to be issued over a six-year period beginning in 2001 at a level not to exceed amounts provided in the legislation. Using a cash flow financing approach, The University of North Carolina – General Administration (UNC-GA), establishes annual amounts not to exceed for each approved project. The amounts not to exceed are subject to change due to actual cash availability and needs during the year. Subsequent to the bond sales and the availability of bond proceeds, UNC-GA notifies the Office of State Budget and Management (OSBM) of the amounts not to exceed for each approved project. Within these amounts, based on an official request of cash needs from the University, OSBM authorizes allotments. The University records the allotments as revenue on the accompanying financial statements. The University's remaining authorization \$116,124,792 is contingent on future bond sales and OSBM allotment approval. Because of uncertainty and time restrictions the remaining

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

authorization is not recorded as an asset or revenue on the accompanying financial statements.

- D. Other Contingent Receivables** – The University has received notification of other gifts and grants for which funds have not been disbursed by the resource provider and for which conditions attached to the gift or grant have not been satisfied or, in the case of permanent endowments, cannot begin to be satisfied. In accordance with accounting principles generally accepted in the United States of America these amounts have not been recorded on the accompanying financial statements. The purpose and amount of other contingent receivables at year-end is as follows:

<u>Purpose</u>	<u>Amount</u>
Pledges to Permanent Endowments	<u>\$42,750</u>

NOTE 16 - NORTH CAROLINA CENTRAL UNIVERSITY FOUNDATION, INC.

There is one separately incorporated non-profit foundation associated with the University. This foundation is the North Carolina Central University Foundation, Inc. (NCCU Foundation).

This organization serves as the primary fundraising arm of the University through which individuals, corporations and other organizations support University programs by providing scholarships, fellowships, faculty salary supplements, and unrestricted funds to specific colleges and the University's overall academic environment. The University's financial statements do not include the assets, liabilities, net assets, or operational transactions of the foundation, except for support from the organization to the University. This support approximated \$2,139,831 for the year ended June 30, 2002. The University remitted \$127,194 in payroll deducted employee contributions and \$129,918 in other reimbursements to the NCCU Foundation.

NOTE 17 - ACCOUNTING CHANGES

Effective July 1, 2001, the University implemented GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – For Public Colleges and Universities*. The financial statement presentation required by these Statements is a single-column enterprise activity rather than the fund-group perspective previously reported. Significant accounting changes in order to comply with the new requirements include adopting

NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)

depreciation on capital assets, reporting revenues net of discounts and allowances, eliminating inter-fund activities, classifying activities as operating or nonoperating, classifying assets and liabilities as current or noncurrent, and prorating summer school activities to periods earned.

In addition, the University implemented GASB Statement No. 38, *Certain Financial Statement Note Disclosures*. Changes in existing disclosures include more detailed information on debt service requirements, obligations under leases, and short-term debt. New disclosures include variable debt interest information and the major components of receivable and payable balances.

NOTE 18 - NET ASSET RESTATEMENT

As referred to in Note 17, the University implemented GASB Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management’s Discussion and Analysis – For Public Colleges and Universities*.

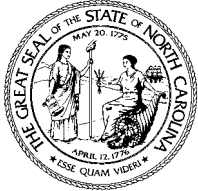
July 1, 2001 Fund Equity as previously reported	\$ 196,217,416
Implementation of GASB 34/35	<u>(84,587,144)</u>
July 1, 2001 Net Assets as Restated	<u>\$ 111,630,272</u>

North Carolina Central University
Schedule of General Obligation Bond Project Authorizations,
Budgets, and Expenditures
For Project-to-Date as of June 30, 2002

Schedule 1

Capital Improvement Project	Projected Start Date	General Obligation Bonds Authorized	Other Sources	Total Project Budget	Amount Expended	Percent Completed	Expected Completion Date
<i>Projects Started</i>							
Eagleson Hall	Oct 2001	\$ 6,526,025	\$ 0	\$ 6,526,025	\$ 58,611	0.90%	Aug 2005
Rush Residential Hall	Sep 2001	1,984,930		1,984,930	47,608	2.40%	Aug 2003
Student Housing	Mar 2001	1,478,770		1,478,770	24,805	1.68%	Sep 2003
Old Senior Dorm	Mar 2001	2,024,165		2,024,165	66,788	3.30%	Dec 2003
Science Complex	Nov 2000	34,941,000		34,941,000	1,413,499	4.05%	Aug 2004
Baynes Hall Replacement	Mar 2001	14,336,545		14,336,545	311,746	2.17%	Nov 2004
Pearson Cafeteria	Mar 2001	1,200,420		1,200,420	77,379	6.45%	Aug 2003
Technology Infrastructure	May 2001	1,350,900		1,350,900	778,369	57.62%	Nov 2002
Campus Infrastructure	Jan 2001	9,750,610		9,750,610	722,755	7.41%	Jan 2004
Renovate Public Safety	Nov 2000	798,000		798,000	105,883	13.27%	Sep 2003
Land Acquisition	Apr 2005	4,000,000		4,000,000	753,823	18.85%	Nov 2005
McLean Residential Hall	Nov 2000	305,800	225,000	530,800	530,800	100.00%	Jan 2003
C I Bond 2000 Administration		5,719,570		5,719,570	34,468	0.60%	
<i>Projects Not Started - To Be Funded in Future Years</i>							
Farrison-Newton, Classroom Building	Jun 2005	6,696,265		6,696,265			Jul 2008
Shepard Residential Hall	Dec 2000	4,139,910		4,139,910			Feb 2005
Latham Residential Hall	Sep 2001	3,241,020		3,241,020			Aug 2004
Student Residential Hall Fire Safety & Security	Feb 2002	1,463,950		1,463,950			May 2003
Turner Law Building	Sep 2001	6,677,360		6,677,360			Oct 2004
Shepard Library	Sep 2001	4,156,060		4,156,060			Aug 2004
Alexander Dunn	Sep 2002	1,690,335		1,690,335			Sep 2005
Hoey Administration Building	Mar 2003	2,724,315		2,724,315			Jan 2007
Code Compliance	Aug 2002	3,491,250		3,491,250			Mar 2005
B. N. Duke Auditorium Addition	Mar 2002	740,000		740,000			Aug 2003
Health and Safety Repair 2000	Nov 2000	1,809,003		1,809,003			Feb 2004
Total All Projects		\$ 121,246,203	\$ 225,000	\$ 121,471,203	\$ 4,926,534		

Note: The 1999-2000 Session of the General Assembly of North Carolina authorized the issuance of two billion five hundred million dollars of general obligation bonds of the State, as subsequently approved by a vote of qualified voters of the State, to provide funds for capital improvements for the University of North Carolina. The projects listed on this schedule are those funded or to be funded by bond proceeds from the general obligation bonds authorized by Senate Bill 912.



Ralph Campbell, Jr.
State Auditor

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**INDEPENDENT AUDITOR'S REPORT
ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING BASED ON AN AUDIT OF
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

Board of Trustees
North Carolina Central University
Durham, North Carolina

We have audited the financial statements of North Carolina Central University, a constituent institution of the sixteen-campus University of North Carolina System, which is a component unit of the State of North Carolina, as of and for the year ended June 30, 2002, and have issued our report thereon dated June 13, 2003.

As discussed in Note 17 to the financial statements, the University implemented Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – For Public Colleges and Universities* and Statement No. 38, *Certain Financial Statement Note Disclosures* during the year ended June 30, 2002.

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.

Compliance

As part of obtaining reasonable assurance about whether the University's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, 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*.

**INDEPENDENT AUDITOR'S REPORT
ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING BASED ON AN AUDIT OF
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS (CONCLUDED)**

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the University's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the Audit Committee, the Board of Trustees and Board of Governors, management and staff of the University, the Governor, the State Controller, the General Assembly, and federal awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties.



Ralph Campbell, Jr.
State Auditor

June 13, 2003

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In accordance with General Statutes 147-64.5 and 147-64.6(c)(14), copies of this report have been distributed to the public officials listed below. Additional copies are provided to other legislators, state officials, the press, and the general public upon request.

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The Honorable Beverly M. Perdue	Lieutenant Governor of North Carolina
The Honorable Richard H. Moore	State Treasurer
The Honorable Roy A. Cooper, III	Attorney General
Mr. David T. McCoy	State Budget Officer
Mr. Robert L. Powell	State Controller
Ms. Molly Corbett Broad	President, The University of North Carolina
Dr. James H. Ammons	Chancellor, North Carolina Central University
Mr. Charles D. O'Duor	Vice Chancellor for Financial Affairs North Carolina Central University
Mr. R. Edward Stewart	Chairman, Board of Trustees North Carolina Central University

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Representative N. Leo Daughtry	N. C. House of Representatives
Mr. James D. Johnson	Director, Fiscal Research Division

August 6, 2003

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