



# **STATE OF NORTH CAROLINA**

## **FINANCIAL STATEMENT AUDIT REPORT OF NORTH CAROLINA CENTRAL UNIVERSITY**

**DURHAM, NORTH CAROLINA**

**FOR THE YEAR ENDED JUNE 30, 2003**

**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, 2003**

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Ralph Campbell, Jr.  
State Auditor

STATE OF NORTH CAROLINA  
Office of the State Auditor

2 S. Salisbury Street  
20601 Mail Service Center  
Raleigh, NC 27699-0601  
Telephone: (919) 807-7500  
Fax: (919) 807-7647  
Internet <http://www.ncauditor.net>

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**AUDITOR'S TRANSMITTAL**

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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, 2003. Our audit was made by authority of Article 5A of Chapter 147 of the *North Carolina 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)

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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** - The following significant deficiency in internal control over financial reporting and was noted as a result of our audit:

### **Finding**

#### 2. Controls over Payroll Separations

These matters are described in the Independent Auditor's Report on Compliance and on Internal Control over Financial Reporting and the Audit Findings and Recommendations section of this report.

3. **Objective** – To present significant deficiencies, if any, in internal control over compliance that could adversely affect the University's ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants and present instances of noncompliance, if any, with laws, regulations, contracts, or grants, the effects of which have a material effect in relation to a type of compliance requirement or audit objective identified in OMB Circular A-133 Compliance Supplement.

**Results** - The following instance of noncompliance was noted as a result of our audit:

### **Finding**

#### 1. Controls over Processing Student Withdrawals for Title IV Refunds – Student Financial Assistance Cluster

This matter is described in the Audit Findings and Recommendations section of this report.

*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

STATE OF NORTH CAROLINA  
Office of the State Auditor

2 S. Salisbury Street  
20601 Mail Service Center  
Raleigh, NC 27699-0601  
Telephone: (919) 807-7500  
Fax: (919) 807-7647  
Internet <http://www.ncauditor.net>

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**INDEPENDENT AUDITOR'S REPORT**

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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, 2003, 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, 2003, 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 7, 2004 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 *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), as listed in the table of contents, 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

## INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

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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.

A handwritten signature in black ink, reading "Ralph Campbell, Jr." in a cursive script.

Ralph Campbell, Jr.  
State Auditor

June 7, 2004

## MANAGEMENT'S DISCUSSION AND ANALYSIS

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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 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**

Through the development of a strategic plan, efforts were made to enhance the overall operational efficiencies of the University. The strategic plan brought together the entire campus community, including the local community, to give input about core values, the mission of the University, and external and internal factors that impact the campus.

Much emphasis has been placed on raising the academic achievement of our students via enhancement of computer labs and the overall technological environment in which 450 new computers were installed. Moreover, several Schools at the University obtained reaffirmation of accreditation or were approved for acceptance of a first-year follow-up report. The University continues the establishment of instructional programs such as a 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 in 2001. These bond monies are being used to renovate existing buildings and build new housing and academic structures. During 2002–2003, more than 88 percent of the bond projects were begun with a total budget of \$108 million.

State appropriations, including reversions and retirement funding, were cut by approximately \$3.9 million as compared to \$4.5 million in fiscal year 2002. Despite the budget reduction, the University has managed to protect academic programs, student services, and avoid negative personnel actions. This was made possible through attrition, conservative spending, and the increase in funds other than State appropriations.

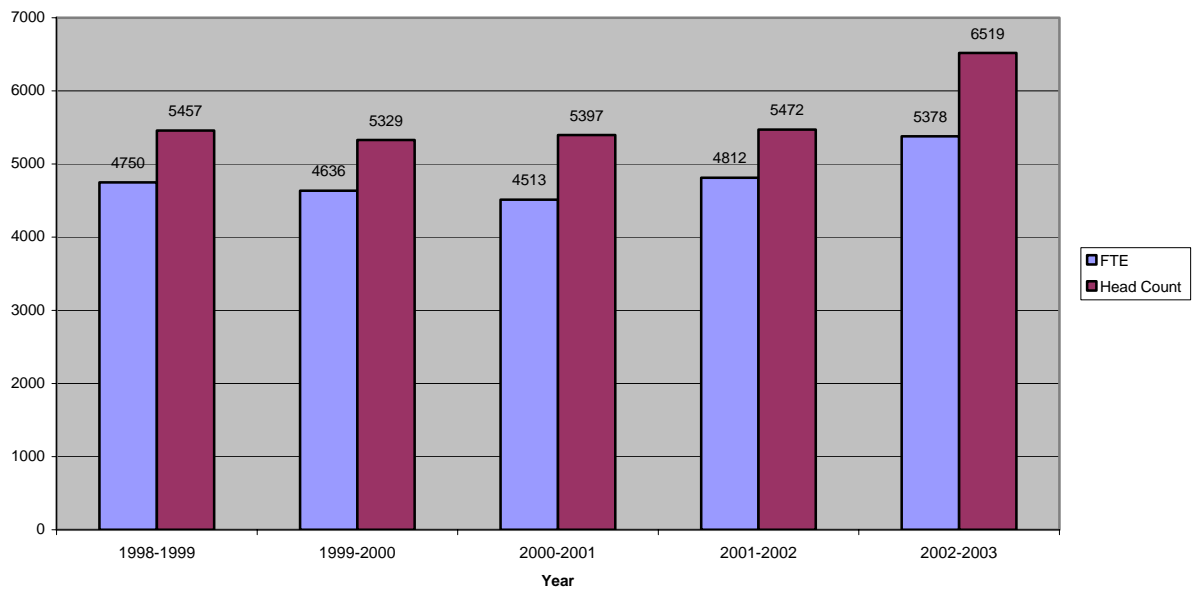
Sponsored research dollars continue to increase; by the end of fiscal year 2003, the University was awarded \$46 million in research grants. The Office of Institutional Advancement raised \$3.2 million in cash gifts, which was an increase from fiscal year 2002. Additionally, the Office of Institutional Advancement was successful with implementing the "Business and Industry" cluster, which provides for the possibility to create corporate partnerships. Two clusters were held in fiscal year 2003 and gave the University the opportunity to intimately share the work of faculty and students with cluster participants.

Student enrollment increased 19.1%. The University continues to strive to recruit talented students. In the fall of 2002, the University enrolled three National Achievement finalists and three semifinalists, a first for the University.



## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FTE and Head Count from 1999 to 2003



### Financial Highlights

#### North Carolina Central University Condensed Statement of Net Assets

	2003	2002
<b>Assets</b>		
Current Assets	\$ 27,967,854	\$ 19,698,227
Capital Assets, Net	90,718,062	84,862,967
Other Assets	25,770,898	26,851,535
<b>Total Assets</b>	<u>144,456,814</u>	<u>131,412,729</u>
<b>Liabilities</b>		
Current Liabilities	8,401,860	7,629,634
Noncurrent Liabilities	16,141,985	15,337,345
<b>Total Liabilities</b>	<u>24,543,845</u>	<u>22,966,979</u>
<b>Net Assets</b>		
Invested in Capital Assets, Net of Related Debt	78,085,571	73,828,315
Restricted - Expendable	17,399,301	16,467,687
Restricted - Nonexpendable	9,779,636	9,434,875
Unrestricted	14,648,461	8,714,873
<b>Total Net Assets</b>	<u>\$ 119,912,969</u>	<u>\$ 108,445,750</u>

## **MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)**

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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, 2003.

As of June 30, 2003, the University's total assets were \$144.5 million as compared to \$131.4 million in the prior year, an increase of \$13.1 million. This increase is mostly attributable to the rise in student enrollment and better collection efforts, which resulted in \$6.8 million more of current cash in 2003. Moreover, net capital assets (buildings, machinery, infrastructure, land, and construction in progress) increased \$5.8 million, while other assets (non-current cash, receivables, and investments) decreased approximately \$1 million. The increase in capital assets is in direct correlation to the bond construction and renovation of academic buildings and dormitories.

The University's liabilities totaled \$24.5 million in 2003 and \$23 million in 2002 with the debt service on housing and stadium bonds comprising \$10.6 million (current and noncurrent portions). The total liabilities increased by a net \$1.6 million in 2003. The bulk of the increase is due to short-term debt of \$2 million. The increase in short-term debt is a function of having to blend (GASB 14) the NCCU Real Estate Foundation's financial data with the University's.

The total current liability of \$8.4 million is well covered by current assets of \$28 million, which indicates the University's ability to pay current liabilities as they become due. Total net assets are \$119.9 million, which is an increase of \$11.5 million from the prior year.

## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

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

	2003	2002
<b>Operating Revenues</b>		
Student Tuition and Fees, Net	\$ 14,472,220	\$ 11,131,978
Contracts and Grants	16,371,525	14,919,133
Sales and Services, Net	16,628,953	14,961,926
Other Operating Revenues	292,658	368,973
Total Operating Revenues	47,765,356	41,382,010
Operating Expenses	101,764,811	97,787,818
Operating Loss	(53,999,455)	(56,405,808)
<b>Nonoperating Revenues and Expenses</b>		
State Appropriations	44,008,436	41,720,970
Noncapital Grants	4,964,033	5,059,249
Noncapital Gifts	4,077,643	2,651,553
Investment Income, Net	(666,024)	(799,065)
Other Nonoperating Revenues (Expenses)	(213,519)	(532,832)
Loss Before Other Revenues, Expenses, Gains or Losses	(1,828,886)	(8,305,933)
Capital Grants	13,291,605	5,121,411
Capital Gifts	4,500	
Total Other Revenues	13,296,105	5,121,411
Increase in Net Assets	11,467,219	(3,184,522)
Net Assets - Beginning of Year	108,445,750	111,630,272
Net Assets - End of Year	\$ 119,912,969	\$ 108,445,750

The Statement of Revenues, Expenses, and Changes in 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.

Operating revenues increased by \$6.4 million when compared to 2002. The contributing factors to this increase were the increases in student enrollment, tuition (8% in-State/12% out-of-State), auxiliary sales and service revenues, and federal contracts and grants revenues.

## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

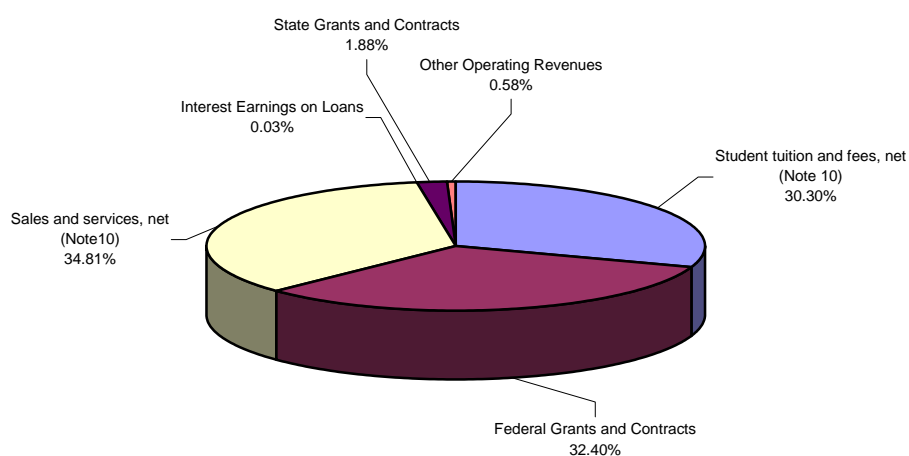
Operating expenses increased by \$4 million when compared to 2002. Services was the major component of this increase in the amount of \$4.7 million. As previously stated, the University had to exercise care when spending in other areas and was able to reduce expenditures on supplies and materials by \$2 million.

Overall, the University sustained a total operating loss of \$54 million in the current fiscal year, which is 4.3% less than the loss in fiscal year 2002. The 4.3% reduction in operating loss was due to the increase in operating revenues over expenses as explained above. Operating losses are likely to continue, due in part, to the accounting requirement to categorize State appropriations (a major source of funding) as nonoperating revenues. In 2003, State appropriations were \$44 million.

Nonoperating revenues and expenses 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, noncapital grants and gifts, investment income/expenses, and capital-related interest primarily represent the nonoperating revenues and expenses.

Of the nonoperating revenues (\$52.2 million), there were noticeable changes in the State appropriations, noncapital gifts, and capital grants. State appropriations increased by \$2.3 million as a result of enrollment growth funds, noncapital gifts increased by \$1.4 million, and capital grants increased by \$8.2 million due to the majority (88%) of the bond funded projects being well underway with designs, demolition, and/or renovations.

### Operating Revenues by Source



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**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)**

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**North Carolina Central University**  
**Condensed Statement of Cash Flows**

	2003	2002
Cash Provided (Used) by:		
Operating Activities	\$ (49,661,859)	\$ (51,491,060)
Noncapital Financing Activities	54,240,166	48,947,851
Capital Financing Activities	(250,395)	(220,668)
Investing Activities	560,708	25,744
Net Increase (Decrease) in Cash and Cash Equivalents	4,888,620	(2,738,133)
Cash and Cash Equivalents - Beginning of Year	21,283,073	24,021,206
Cash and Cash Equivalents - End of Year	<u>\$ 26,171,693</u>	<u>\$ 21,283,073</u>

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 \$49.7 million, which is a 3.6% decrease from 2002. The major outflows were payments to employees for services (\$55.4 million), vendors for goods and services (\$37.5 million), and students for educational assistance (\$3.9 million). The major sources of operating inflows were student tuition and fees (\$14.5 million), auxiliary sales (\$16.6 million), and contracts/grants (\$16.4 million). The increases of cash inflows related to student tuition and fees and auxiliary sales account for the net decrease in operating outflows.

The net cash from noncapital financing activities is an inflow of \$54.2 million, \$5.3 million more than 2002. State appropriations of \$44 million account for the bulk of this inflow.

Cash flow from capital and related financing activities is a net outflow of \$250,395. The net outflow results from the receipt of bond monies of which North Carolina Central University received approximately \$10.2 million in fiscal year 2003. The University expended \$12.4 million for capital assets and debt service. The major capital acquisitions related to the Science Complex for \$3.1 million, significant renovations on various dormitories and other buildings for \$3.3 million, and land for \$2.2 million.

The University has a net cash inflow from investing activities of \$560,708. This results from investment income of \$663,133 and proceeds from the sales of investments in the amount of \$10.8 million and purchases of investments and related fees of \$10.9 million.

In summary, the cash position of the University increased \$4.9 million or 23%.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS (CONCLUDED)**

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### **Economic Outlook**

Looking toward the future, management believes that North Carolina Central University will continue to sustain an overall positive financial position. However, we acknowledge that the environmental challenges related to residential and other buildings will negatively impact net assets and the financial growth realized during 2003. The University will encounter additional expenses to remedy unhealthy building environments, acquire off-campus housing, and transport students for the next 18 months.

Although, we are faced with the above challenge, there are several factors that will positively 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.

Student enrollment continues to grow. The enrollment for 2003-2004 reached another all-time high of 7,191. Through diligent recruitment efforts and future offerings of attractive curricula such as molecular biology, genomics, bioprocessing technology, and laboratory animal science, we expect enrollment to steadily increase. The University is student-centered and committed to providing students with a challenging learning environment. Moreover, for fiscal year 2003–2004, the State legislature approved a 5.5% tuition increase; therefore, projected tuition and fees revenues look favorable.

To accommodate the growth in students, the two additional residential facilities will be constructed with university bond funds and ready for occupancy in fiscal year 2004–2005. The North Carolina Central University Real Estate Foundation will provide a new 400-bed privatized dormitory.

North Carolina Central University's faculty is steadily writing, applying, and receiving research grant funds to augment State funding. 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.

With the sagging State economy, private gifts from corporate sponsors and alumni are critical to the success of the University's mission. The Office of Institutional Advancement has obtained 50 dues-paying "Business and Industry" corporate partners.

Although State funding was down due to the economic conditions, the University will again be eligible to receive "enrollment growth" monies of \$2.6 million resulting from the increase in enrollment in 2002. 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 in truth and service.

***North Carolina Central University***  
***Statement of Net Assets***  
***June 30, 2003***

***Exhibit A***

**ASSETS**

Current Assets:

Cash and Cash Equivalents	\$	16,296,487
Restricted Cash and Cash Equivalents		1,767,623
Restricted Short-Term Investments		2,178,686
Receivables, Net (Note 4)		6,965,278
Due from Primary Government		184,834
Inventories		228,574
Notes Receivable, Net (Note 4)		346,372

Total Current Assets		27,967,854
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Noncurrent Assets:

Restricted Cash and Cash Equivalents		8,107,583
Receivables, Net (Note 4)		16,000
Restricted Due from Primary Government		5,090,026
Endowment Investments		9,560,691
Other Long-Term Investments		469,627
Notes Receivable, Net (Note 4)		2,526,971
Capital Assets - Nondepreciable (Note 5)		9,859,211
Capital Assets - Depreciable, Net (Note 5)		80,858,851

Total Noncurrent Assets		116,488,960
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Total Assets		144,456,814
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**LIABILITIES**

Current Liabilities:

Accounts Payable and Accrued Liabilities (Note 6)		5,067,857
Due to Primary Government		99,125
Deferred Revenue		415,138
Interest Payable		108,698
Short-Term Debt		1,939,069
Long-Term Liabilities - Current Portion (Note 8)		771,973

Total Current Liabilities		8,401,860
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Noncurrent Liabilities:

Deposits Payable		400
Funds Held for Others		59,227
U. S. Government Grants Refundable		2,574,154
Long-Term Liabilities (Note 8)		13,508,204

Total Noncurrent Liabilities		16,141,985
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Total Liabilities		24,543,845
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# ***North Carolina Central University***

## ***Statement of Net Assets***

***June 30, 2003***

***Exhibit A***

***Page 2***

### **NET ASSETS**

Invested in Capital Assets, Net of Related Debt	78,085,571
Restricted for:	
Nonexpendable:	
Scholarships and Fellowships	4,090,912
Endowed Professorships	5,197,023
Loans	491,701
Expendable:	
Scholarships and Fellowships	613,786
Research	740,675
Endowed Professorships	2,130,360
Departmental Uses	532,614
Capital Projects	12,057,574
Debt Service	1,104,911
Other	219,381
Unrestricted	14,648,461
Total Net Assets	<b>\$ 119,912,969</b>

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, 2003***

***Exhibit B***

**REVENUES**

Operating Revenues:

Student Tuition and Fees, Net (Note 10)	\$	14,472,220
Federal Grants and Contracts		15,472,368
State and Local Grants and Contracts		899,157
Sales and Services, Net (Note 10)		16,628,953
Interest Earnings on Loans		14,658
Other Operating Revenues		278,000
Total Operating Revenues		47,765,356

**EXPENSES**

Operating Expenses:

Salaries and Benefits		56,432,472
Supplies and Materials		14,443,258
Services		21,008,019
Scholarships and Fellowships		3,670,182
Utilities		3,034,053
Depreciation		3,176,827

Total Operating Expenses		101,764,811
Operating (Loss)		(53,999,455)

**NONOPERATING REVENUES (EXPENSES)**

State Appropriations		44,008,436
Noncapital Grants		4,964,033
Noncapital Gifts		4,077,643
Investment Income (Net of Investment Expense of \$32,408)		(666,024)
Interest and Fees on Capital Asset-Related Debt		(536,591)
Other Nonoperating Revenues (Expenses)		323,072

Net Nonoperating Revenues		52,170,569
Income Before Other Revenues, Expenses, Gains, or Losses		(1,828,886)

Capital Grants		13,291,605
Capital Gifts		4,500

Increase in Net Assets		11,467,219
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**NET ASSETS**

Net Assets - July 1, 2002		108,445,750
Net Assets - June 30, 2003	\$	119,912,969

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, 2003***

***Exhibit C***

**CASH FLOWS FROM OPERATING ACTIVITIES**

Received from Customers	\$ 47,392,653
Payments to Employees and Fringe Benefits	(55,384,953)
Payments to Vendors and Suppliers	(37,489,054)
Payments for Scholarships and Fellowships	(3,938,775)
Loans Issued	(727,453)
Collection of Loans	535,542
Interest Earned on Loans	12,028
Other Receipts (Payments)	(61,847)
Net Cash Used by Operating Activities	(49,661,859)

**CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES**

State Appropriations	44,008,436
Grants for Other than Capital Purposes	5,809,554
Noncapital Gifts	4,077,643
William D. Ford Direct Lending Receipts	34,547,446
William D. Ford Direct Lending Disbursements	(34,547,446)
Related Activity Agency Receipts	22,861
Other Receipts (Payments)	321,672
Net Cash Provided by Noncapital Financing Activities	54,240,166

**CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES**

Proceeds from Capital Debt	1,939,069
Capital Grants	10,248,382
Proceeds from Sale of Capital Assets	1,400
Acquisition and Construction of Capital Assets	(11,535,343)
Principal Paid on Capital Debt and Leases	(368,820)
Interest and Fees Paid on Capital Debt and Leases	(535,083)
Net Cash Used by Capital Financing and Related Financing Activities	(250,395)

**CASH FLOWS FROM INVESTING ACTIVITIES**

Proceeds from Sales and Maturities of Investments	10,803,849
Interest on Investments	663,133
Purchase of Investments and Related Fees	(10,906,274)
Net Cash Provided by Investing Activities	560,708

Net Increase in Cash and Cash Equivalents	4,888,620
Cash and Cash Equivalents - July 1, 2002	21,283,073
Cash and Cash Equivalents - June 30, 2003	\$ 26,171,693

**North Carolina Central University****Statement of Cash Flows****For the Fiscal Year Ended June 30, 2003****Exhibit C****Page 2****RECONCILIATION OF NET OPERATING REVENUES (EXPENSES)  
TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES**

Operating Loss	\$	(53,999,455)
Adjustments to Reconcile Operating Loss to Net Cash Provided (Used) by Operating Activities:		
Depreciation Expense		3,176,827
Allowances, Write-Offs, and Amortizations		(281,380)
Loss on Disposals		250,209
Other Receipts/Payments		(61,847)
Changes in Assets and Liabilities:		
Receivables (Net)		(3,848)
Due from Primary Government		(184,834)
Inventories		299,933
Accounts Payable and Accrued Liabilities		259,931
Due to Primary Government		9,260
Deferred Revenue		103,274
Compensated Absences		961,982
Note Principle Repayments		535,542
Notes Issued		(727,453)
Net Cash Used by Operating Activities	\$	(49,661,859)

**RECONCILIATION OF CASH AND CASH EQUIVALENTS**

Current Assets:		
Cash and Cash Equivalents	\$	16,296,487
Restricted Cash and Cash Equivalents		1,767,623
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		8,107,583
Total Cash and Cash Equivalents - June 30, 2003	\$	26,171,693

**NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES**

Assets Acquired through a Gift	\$	4,500
Change in Fair Value of Investments		(140,894)

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, 2003**

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**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 and its component units. 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. Although legally separate, the NCCU Real Estate Foundation, Inc. (Foundation), a component unit of the University, is reported as if it were part of the University.

The Foundation is governed by a four-member board. The Foundation's purpose is to acquire property and to construct and own residential facilities for students, which it will manage for the University. Because the directors of the Foundation are appointed by the Chancellor and the Foundation's sole purpose is to benefit North Carolina Central University, its financial statements have been blended with those of the University.

Separate financial statements for the Foundation may be obtained from the University Controller's Office, 1801 Fayetteville Street, Durham, NC 27707, or by calling (919) 530-7432. Other related foundations and similar nonprofit corporations for which the University is not financially accountable are not part of the accompanying financial statements.

- 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).

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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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*, 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.

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, unless the GASB amends its pronouncements to specifically adopt FASB pronouncements issued after that date.

- 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.

Nonexchange transactions, in which the University receives (or gives) value without directly giving (or receiving) equal value in exchange includes State appropriations, certain grants, and donations. Revenues are recognized, net of estimated uncollectible amounts, as soon as all eligibility requirements imposed by the provider have been met, if probable of collection.

- D. Cash and Cash Equivalents** – This classification includes petty cash, cash on deposit with private bank accounts, and deposits held by the State Treasurer in the short-term investment portfolio. 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 long-term fixed income investments, equity investments, mutual funds, and money market funds held by the University. Except for money market funds, investments are accounted for at fair value, as determined by quoted market prices, or an amount determined by management if quoted market prices are not available. The net increase (decrease) in the fair value of investments is recognized as a component of investment income.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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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 provider's conditions have been satisfied. Receivables are recorded net of estimated uncollectible amounts.
- G. Inventories** – Inventories, consisting of expendable supplies, are valued at cost using the first-in, first-out method.
- 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 value of assets constructed includes all material direct and indirect construction costs.

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 more than one year. Library books are generally not considered to have a useful life of more than one year unless part of a collection and are expensed in the year of acquisition.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 20 to 50 years for general 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** – Unexpended proceeds of revenue bonds and unexpended capital contributions are classified as restricted assets because their use is limited by applicable bond covenants or donor/grantor agreements. Certain other assets are classified as restricted because their use is limited by external parties or statute.
- J. Noncurrent Long-Term Liabilities** – Noncurrent long-term liabilities include principal amounts of bonds 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

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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premiums/discounts over the life of the bonds using the straight-line method. The deferred losses on refundings are amortized 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 non-faculty 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.

In addition to the vacation leave described above, compensated absences includes the accumulated unused portion of the special annual leave bonus awarded by the North Carolina General Assembly to all full-time permanent employees as of September 30, 2002. The unused portion of this leave remains available until used, notwithstanding the limitation on annual leave carried forward described above.

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

There is no liability for unpaid accumulated sick leave because the University has no obligation to pay sick leave upon termination or retirement. However, additional service credit for retirement pension benefits is given for accumulated sick leave upon retirement.

- 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 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 for which the University is legally or contractually

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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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. For projects funded by tax-exempt debt proceeds and other sources, the debt proceeds are always used first.

- 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 classifies its revenues and expenses as operating or nonoperating in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the University's principal ongoing operations. Operating revenues include activities that have characteristics of exchange transactions, such as (1) student tuition and fees, (2) sales and services of auxiliary enterprises, (3) certain federal, State and local grants and contracts that are essentially contracts for services, and (4) interest earned on loans. Operating expenses are all expense transactions incurred other than those related to capital and noncapital financing or investing activities as defined by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*.



## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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Nonoperating revenues include activities that have the characteristics of nonexchange transactions. 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 investing, capital or noncapital financing activities. Capital contributions are presented separately after nonoperating revenues and expenses.

- 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 - DEPOSITS AND INVESTMENTS

- A. Deposits** – Unless specifically exempt, the University is required by General Statute 147-77 to deposit moneys received with the State Treasurer or with a depository institution in the name of the State Treasurer. In addition, the University of North Carolina Board of Governors, pursuant to General Statute 116-36.1, requires the University to deposit its institutional trust funds with the State Treasurer. Although specifically exempted, the University may voluntarily deposit endowment funds, special funds, revenue bond proceeds, and debt service funds with the State Treasurer. Special funds consist of moneys for intercollegiate athletics and agency funds held directly by the University.

Deposits include cash and cash equivalents \$26,169,785. At year-end, cash on hand was \$1,908. The University's portion of the State Treasurer's Investment Pool was \$26,158,381. 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 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 \$11,404 and the bank balance was \$11,404. Of the bank balance, \$11,404 was covered by federal depository insurance.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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*North Carolina General Statutes* 147-69.1(c), applicable to the State's General Fund, and 147-69.2, applicable to institutional trust funds, 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 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 and Chapter VI of the Administrative Manual of the University of North Carolina, 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 the investment funds to manage investments and distribute investment income. Purchases in the investment funds are allowed at the beginning of each month. Fund ownership is measured based on the participating funds purchases and accumulated gain/loss reinvestment. The investment

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 are categorized 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. Money market funds and mutual funds are investments not categorized to indicate the level of custodial credit risk.

A summary of the University's investments at June 30, 2003 is presented below:

### *Scholarship/Professorship Investments*

	Fair Value			
	Risk Category			Total
	1	2	3	
<b>Categorized Investments:</b>				
U.S. Government Securities	\$ 608,861	\$ 0	\$ 0	\$ 608,861
Corporate Bonds	1,945,335			1,945,335
Corporate Stocks	4,004,077			4,004,077
<b>Total Categorized Investments</b>	<u>\$ 6,558,273</u>	<u>\$ 0</u>	<u>\$ 0</u>	6,558,273
<b>Investments Not Categorized:</b>				
Money Market Funds				1,044,832
Mutual Funds				4,605,899
<b>Total Investments Not Categorized</b>				<u>5,650,731</u>
<b>Total External Pool Investments</b>				\$ 12,209,004

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### NOTE 3 - ENDOWMENT INVESTMENTS

Investments of the University's endowment funds are separately invested and pooled unless required to be separately invested by the donor. 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 of the Endowment Fund. At June 30, 2003, net appreciation of \$841,366 was available to be spent, of which \$0 was restricted to specific purposes.

### NOTE 4 - RECEIVABLES

Receivables at June 30, 2003 were as follows:

	Gross Receivables	Less Allowance for Doubtful Accounts	Net Receivables
<b>Current Receivables:</b>			
Students	\$ 3,641,892	\$ 1,503,630	\$ 2,138,262
Accounts	537,562		537,562
Intergovernmental	4,051,113		4,051,113
Pledges	16,750		16,750
Investment Earnings	75,013		75,013
Interest on Loans	146,578		146,578
<b>Total Current Receivables</b>	<u>\$ 8,468,908</u>	<u>\$ 1,503,630</u>	<u>\$ 6,965,278</u>
<b>Noncurrent Receivables:</b>			
Pledges	<u>\$ 16,000</u>	<u>\$ 0</u>	<u>\$ 16,000</u>
<b>Notes Receivable:</b>			
<b>Notes Receivable - Current:</b>			
Federal Loan Programs	<u>\$ 772,717</u>	<u>\$ 426,345</u>	<u>\$ 346,372</u>
<b>Notes Receivable - Noncurrent:</b>			
Federal Loan Programs	<u>\$ 5,422,180</u>	<u>\$ 2,895,209</u>	<u>\$ 2,526,971</u>

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### NOTE 5 - CAPITAL ASSETS

A summary of changes in the capital assets for the year ended June 30, 2003, is presented as follows:

	Balance July 1, 2002	Adjustments	Increases	Decreases	Balance June 30, 2003
Capital Assets, Nondepreciable:					
Land	\$ 1,944,025	\$ 0	\$ 2,177,626	\$ 0	\$ 4,121,651
Art, Literature, and Artifacts	494,240		4,500		498,740
Construction in Progress	2,963,708	(530,800)	2,805,912		5,238,820
<b>Total Capital Assets, Nondepreciable</b>	<b>5,401,973</b>	<b>(530,800)</b>	<b>4,988,038</b>		<b>9,859,211</b>
Capital Assets, Depreciable:					
Buildings	111,664,892	530,800	2,765,537	15,466	114,945,763
Machinery and Equipment	9,459,308		1,528,556	955,254	10,032,610
General Infrastructure	14,238,148				14,238,148
<b>Total Capital Assets, Depreciable</b>	<b>135,362,348</b>	<b>530,800</b>	<b>4,294,093</b>	<b>970,720</b>	<b>139,216,521</b>
Less Accumulated Depreciation/Amortization for:					
Buildings	45,188,786	224,152	1,685,298	15,466	47,082,770
Machinery and Equipment	5,494,631		858,686	929,197	5,424,120
General Infrastructure	5,217,937		632,843		5,850,780
<b>Total Accumulated Depreciation</b>	<b>55,901,354</b>	<b>224,152</b>	<b>3,176,827</b>	<b>944,663</b>	<b>58,357,670</b>
<b>Total Capital Assets, Depreciable, Net</b>	<b>79,460,994</b>	<b>754,952</b>	<b>1,117,266</b>	<b>26,057</b>	<b>80,858,851</b>
<b>Capital Assets, Net</b>	<b>\$ 84,862,967</b>	<b>\$ 224,152</b>	<b>\$ 6,105,304</b>	<b>\$ 26,057</b>	<b>\$ 90,718,062</b>

### NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2003 were as follows:

	Amount
Accounts Payable	\$ 2,764,472
Accrued Payroll	1,927,295
Contract Retainage	140,548
Intergovernmental Payables	67,680
Other	167,862
<b>Total Accounts Payable and Accrued Liabilities</b>	<b>\$ 5,067,857</b>

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### NOTE 7 - SHORT-TERM DEBT – LINE OF CREDIT

Short-term debt activity for the year ended June 30, 2003 was as follows:

	Balance July 1, 2002	Draws	Repayments	Balance June 30, 2003
Line of Credit	\$ 0	\$ 1,939,069	\$ 0	\$ 1,939,069

The NCCU Real Estate Foundation, Inc., a component unit of the University, uses a revolving line of credit to be drawn upon as needed. This line of credit was necessary to finance the acquisition, construction, and equipping of a residential facility, which will be capitalized in the applicable asset categories upon completion.

### NOTE 8 - LONG-TERM LIABILITIES

**A. Changes in Long-Term Liabilities** - A summary of changes in the long-term liabilities for the year ended June 30, 2003 is presented as follows:

	Balance July 1, 2002	Additions	Reductions	Balance June 30, 2003	Current Portion
Bonds Payable	\$ 11,050,000	\$ 0	\$ 330,000	\$ 10,720,000	\$ 350,000
Add/Deduct Premium/Discount	(96,660)		(4,683)	(91,977)	
Total Bonds Payable	10,953,340		325,317	10,628,023	350,000
Capital Leases Payable	106,753		38,820	67,933	38,820
Compensated Absences	2,622,239	4,027,875	3,065,893	3,584,221	383,153
<b>Total Long-Term Liabilities</b>	<b>\$ 13,682,332</b>	<b>\$ 4,027,875</b>	<b>\$ 3,430,030</b>	<b>\$ 14,280,177</b>	<b>\$ 771,973</b>

Additional information regarding capital lease obligations is included in Note 9.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

**B. Bonds Payable** - The University was indebted for bonds payable for the purposes shown in the following table:

Purpose	Series	Interest Rate/ Ranges	Final Maturity Date	Original Amount of Issue	Principal Paid Through 06/30/2003	Principal Outstanding 06/30/2003
Housing System Revenue Bonds	1996	5.4% to 5.9%	11/1/2022	\$ 8,890,000	\$ 975,000	\$ 7,915,000
Stadium System Revenue Bonds	1998	4.4% to 5.0%	4/1/2023	3,320,000	515,000	2,805,000
Total Bonds Payable (principal only)				<u>\$ 12,210,000</u>	<u>\$ 1,490,000</u>	10,720,000
Less: Unamortized Discount						<u>91,977</u>
Total Bonds Payable						<u>\$ 10,628,023</u>

**C. Annual Requirements** - The annual requirements to pay principal and interest on the long-term obligations at June 30, 2003 are as follows:

Fiscal Year	Annual Requirements	
	Bonds Payable	
	Principal	Interest
2004	\$ 350,000	\$ 578,833
2005	360,000	560,913
2006	380,000	542,453
2007	405,000	522,743
2008	430,000	501,635
2009-2013	2,145,000	2,174,906
2014-2018	2,855,000	1,504,224
2019-2023	<u>3,795,000</u>	<u>584,265</u>
Total Requirements	<u>\$ 10,720,000</u>	<u>\$ 6,969,972</u>

Interest on the Housing Revenue Bonds is calculated at 5.4 to 5.9% at June 30, 2003.

Interest on the Stadium Revenue Bonds is calculated at 4.4 to 5.0% at June 30, 2003.

**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 3/2/95, 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 Statement of

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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Net Assets. At June 30, 2003, the outstanding balance of the defeased *Dormitory System* Revenue Bonds was \$129,000.

### 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, 2003:

<u>Fiscal Year</u>	<u>Amount</u>
2004	\$ 45,228.00
2005	<u>33,921.00</u>
Total Minimum Lease Payments	79,149.00
Amount Representing Interest (6% Rate of Interest)	<u>11,216.00</u>
Present Value of Future Lease Payments	<u><u>\$ 67,933.00</u></u>

Machinery and equipment acquired under capital lease amounted to \$194,096 at June 30, 2003.

- B. Operating Lease** – Rental expense for all operating leases during the year was \$282,187.



## 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	Net Revenues Pledged as Security for Debt
<b>Operating Revenues:</b>						
<b>Student Tuition and Fees</b>	<u>\$ 18,001,683</u>	<u>\$ 0</u>	<u>\$ 3,696,060</u>	<u>\$ (166,597)</u>	<u>\$ 14,472,220</u>	<u>\$ 0</u>
<b>Sales and Services:</b>						
Sales and Services of Auxiliary Enterprises:						
Residential Life	\$ 5,894,509	\$ 0	\$ 1,314,111	\$ (122,925)	\$ 4,703,323	\$ 5,894,509 (A)
Dining	4,560,076		1,040,220	(102,466)	3,622,322	
Student Union Services	1,193,861		264,238	(13,955)	943,578	
Health, Physical Education, and Recreation Services	1,502,837		328,324	(14,844)	1,189,357	
Bookstore	936,772	29,075			907,697	
Parking	957,114			(2,016)	959,130	
Athletic	2,099,179		497,546	(19,324)	1,620,957	
Other	2,811,596	243,194		(23,461)	2,591,863	702,445 (B)
Sales and Services of Education and Related Activities	<u>108,455</u>	<u>17,729</u>			<u>90,726</u>	
<b>Total Sales and Services</b>	<u>\$ 20,064,399</u>	<u>\$ 289,998</u>	<u>\$ 3,444,439</u>	<u>\$ (298,991)</u>	<u>\$ 16,628,953</u>	<u>\$ 6,596,954</u>

Revenue Bonds Secured by Pledged Revenues:

(A) Housing System

(B) Stadium 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	\$ 29,365,762	\$ 2,917,671	\$ 2,470,326	\$ 0	\$ 3,033	\$ 0	\$ 34,756,792
Research	2,582,614	997,854	446,539				4,027,007
Public Service	1,051,433	206,777	561,997				1,820,207
Academic Support	5,924,694	2,608,051	3,726,689				12,259,434
Student Services	1,786,327	148,087	529,788				2,464,202
Institutional Support	7,302,619	642,614	1,008,806	133,860			9,087,899
Operations and Maintenance of Plant	2,636,295	3,969,939	2,743,776		2,720,969		12,070,979
Student Financial Aid	539,225		3,737,861	3,050,264			7,327,350
Auxiliary Enterprises	5,243,503	2,952,265	5,782,237	486,058	310,051		14,774,114
Depreciation						3,176,827	3,176,827
<b>Total Operating Expenses</b>	<u>\$ 56,432,472</u>	<u>\$ 14,443,258</u>	<u>\$ 21,008,019</u>	<u>\$ 3,670,182</u>	<u>\$ 3,034,053</u>	<u>\$ 3,176,827</u>	<u>\$ 101,764,811</u>

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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### 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. Eligible employees can elect to participate in the Optional Retirement Program at the time of employment, otherwise they are automatically enrolled in the Teachers' and State Employees' Retirement System.

The Teachers' and State Employees' Retirement System is a cost sharing multiple-employer defined benefit pension plan established by the State to provide pension benefits for employees of the State, its component units and local boards of education. The plan is administered by the North Carolina State Treasurer.

Benefit and contribution provisions for the Teachers' and State Employees' Retirement System are established by *North Carolina General Statutes* 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contribution rates are set each year by the North Carolina General Assembly based on annual actuarial valuations. For the year ended June 30, 2003, the General Assembly required no contribution by employers and 6% of covered payroll for members.

For the year ended June 30, 2003, the University had a total payroll of \$47,318,334, of which \$34,804,912 was covered under the Teachers' and State Employees' Retirement System. Total employee contributions for pension benefits for the year were \$2,088,295. No employer contributions were required. The University made one hundred percent of its annual required contributions for the years ended June 30, 2003, 2002, and 2001, which were \$0, \$664,527, and \$1,721,148, respectively.

The Teachers' and State Employees' Retirement System's financial information is 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.

The Optional Retirement Program (Program) is a defined contribution retirement plan that provides retirement benefits with options for payments to beneficiaries in the event of the participant's death. Administrators and eligible faculty of the University may join the Program instead of the Teachers' and State Employees' Retirement

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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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 the carrier of their choice. Each carrier offers a variety of investment funds, including both fixed and variable account investment options and mutual funds.

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.

Participant eligibility and contributory requirements are established by General Statute 135-5.1. Employer and member contribution rates are set each year by the North Carolina General Assembly. For the year ended June 30, 2003, 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.

For the year ended June 30, 2003, the University had a total payroll of \$47,318,334, of which \$10,126,264 was covered under the Optional Retirement Program. Total employee and employer contributions for pension benefits for the year were \$607,576 and \$692,636, 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 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

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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University. The voluntary contributions by employees amounted to \$43,945 for the year ended June 30, 2003.

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, 2003 were \$45,562. The voluntary contributions by employees amounted to \$166,460 for the year ended June 30, 2003.

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 nonprofit 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 \$719,763 for the year ended June 30, 2003.

### **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 Retirement Program for these health care benefits. For the fiscal year ended June 30, 2003, the University's total contribution to the Plan was \$1,055,883. The University assumes no liability for retiree health care

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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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 and 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, 2003, the University's total contribution to the DIPNC was \$233,642. 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. 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.

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 University pays the premium, based on a composite rate, directly to the private insurer.

The University is required to maintain fire and lightning coverage on all State-owned buildings and contents through the State Property Fire Insurance Fund (Fund), an internal service fund of the State. Such coverage is provided at no cost to operations supported by the State's General Fund. Other operations not supported by the State's General Fund are charged for the coverage. Losses covered by the Fund are subject to a \$500 per occurrence deductible. The

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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University also purchased through the Fund extended coverage, vandalism, and “all risk” for certain buildings and contents.

All State-owned vehicles are covered by liability insurance through a private insurance company and handled by the North Carolina Department of Insurance. The liability limits for losses occurring in-State are \$500,000 per claim and \$5,000,000 per occurrence and out-of-State are \$1,000,000 per claim and \$5,000,000 per occurrence. The University pays premiums to the Department of Insurance for the coverage.

The University is protected for losses from employee dishonesty and computer fraud. This coverage is with a private insurance company and is handled by the North Carolina Department of Insurance. Universities are charged a premium by the private insurance company. Coverage limit is \$5,000,000 per occurrence with a \$50,000 deductible and a 10% participation in each loss above the deductible.

The University purchased other authorized coverage from private insurance companies through the North Carolina Department of Insurance.

University employees and retirees are provided comprehensive major medical care benefits. Coverage is funded by contributions to the State Health Plan (Plan), a pension and other employee benefit trust fund of the State of North Carolina. The Plan has contracted with third parties to process claims.

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 (death benefits) of \$25,000 to \$50,000 is provided to eligible workers. This Death Benefit Plan is administered by the State Treasurer and funded via employer contributions. The employer contribution rate was .16% for the current fiscal year.

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.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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### 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 \$9,844,879 at June 30, 2003.
- 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 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 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 \$102,833,187 is contingent on future bond sales and OSBM allotment approval. Because of uncertainty and time restrictions the remaining 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

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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:

Purpose	Amount
Pledges to Permanent Endowments	\$ 32,750

### NOTE 16 - RELATED PARTIES

- A. North Carolina Central University Foundation, Inc.** - The North Carolina Central University Foundation, Inc. (NCCU Foundation) is a separately incorporated nonprofit foundation associated with the University. 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 foundations, except for support from each organization to the University. This support approximated \$3,847,645 for the year ended June 30, 2003. The University remitted \$125,258 in payroll deducted employee contributions and \$144,743 in other reimbursements to the NCCU Foundation.
- B. Board Member** - The University's Endowment Fund Committee is responsible for investment decisions related to University endowment funds. The committee placed investments totaling \$7.2 million with a company owned in part by a bank (12% ownership) where the bank president and CEO is an Endowment Fund Committee member and a University Board of Trustees member. The Board member disclosed these facts and abstained from voting.

### NOTE 17 - SUBSEQUENT EVENTS

In August 2003, the University discovered that two residential buildings and other academic buildings were not environmentally safe. Due to these safety concerns, a decision was made by the University to close the residential facilities. As a result, the University will encounter additional expenses to remedy unhealthy building environments, acquire off-campus housing, and



## **NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)**

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transport students for the next 12 months. The total approximate cost to the University will be \$7.4 million, as the State of North Carolina will pay the remediation costs for the residential buildings.

In October 2003, the North Carolina Capital Facilities Finance Agency issued the Student Housing Facilities Revenue Bonds (NCCU Real Estate Foundation, Inc. Project), Series 2003A in the amount of \$21,475,000 and Series 2003B in the amount of \$100,000. The 2003A Bonds will mature, subject to mandatory and optional redemption, from October 1, 2005 to October 1, 2034, with amounts varying from \$190,000 due October 1, 2005 to \$1,420,000 due October 1, 2034. The Series 2003B Bonds are due October 1, 2005. The bonds will initially bear interest at a variable weekly rate. However, the interest rate on the Series 2003 bonds is subject to conversion to another interest rate mode. During a weekly rate period, interest on the 2003 Bonds is payable on the first business day of each calendar month, commencing November 3, 2003. The issuer, the North Carolina Capital Facilities Finance Agency, loaned the proceeds of the Series 2003 Bonds to the NCCU Real Estate Foundation, Inc. The Foundation is using the proceeds to finance the costs of building a student housing facility at North Carolina Central University, to fund a debt service reserve fund for the 2003A Bonds, to pay a portion of the interest on the bonds during construction of the project, and to pay certain costs of issuance of the bonds. The issuer and the Foundation have entered a loan agreement dated October 1, 2003 and the Foundation has executed promissory notes to evidence its obligation to repay the loan.

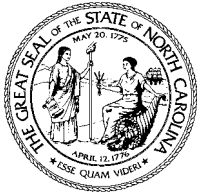
**North Carolina Central University**  
**Schedule of General Obligation Bond Project Authorizations,**  
**Budgets, and Expenditures**  
**For Project-to-Date as of June 30, 2003**

**Schedule 1**

Capital Improvement Projects	Projected Start Date	General Obligation Bonds Authorized	Other Sources	Total Project Budget	Amount Expended	Percent Completed	Expected Completion Date
<b>Projects Started</b>							
Eagleson Hall	Oct 2001	\$ 6,526,025	\$ 0	\$ 6,526,025	\$ 233,296	3.57%	Aug 2005
Rush Residential Hall	Sep 2001	1,984,930		1,984,930	92,894	4.68%	Aug 2003
Student Housing	Mar 2001	1,478,770		1,478,770	80,705	5.46%	Sep 2003
Old Senior Dorm	Mar 2001	2,024,165		2,024,165	81,552	4.03%	Dec 2003
Science Complex	Nov 2000	34,941,000		34,941,000	3,900,126	11.16%	Aug 2004
Baynes Hall Replacement	Mar 2001	14,336,545		14,336,545	1,123,436	7.84%	Nov 2004
Pearson Cafeteria	Mar 2001	1,200,420		1,200,420	91,788	7.65%	Aug 2003
Technology Infrastructure	May 2001	1,350,900		1,350,900	1,241,929	91.93%	Jun 2003
Campus Infrastructure	Jan 2001	9,750,610		9,750,610	1,917,369	19.66%	Jan 2004
Renovate Public Safety	Nov 2000	798,000		798,000	134,553	16.86%	Sep 2003
Land Acquisition	Apr 2005	4,000,000		4,000,000	1,778,191	44.45%	Nov 2005
McLean Residential Hall	Nov 2000	305,800	225,000	530,800	530,800	100.00%	Jan 2003
Shepard Residential Hall	Dec 2000	4,139,910	2,663,395	6,803,305	380,337	5.59%	Feb 2005
Latham Residential Hall	Sep 2001	3,241,020		3,241,020	193,065	5.96%	Aug 2004
Student Residential Hall Fire Safety & Security	Feb 2003	1,463,950		1,463,950	6,138	0.42%	Mar 2005
Turner Law Building	Sep 2001	6,677,360		6,677,360	347,830	5.21%	Oct 2004
Shepard Library	Sep 2001	4,156,060		4,156,060	90,355	2.17%	Aug 2004
Alexander Dunn	Sep 2002	1,690,335		1,690,335	1,050	0.06%	Sep 2005
Code Compliance	Aug 2002	3,491,250		3,491,250	151,997	4.35%	Mar 2005
Health and Safety Repair 2000	Nov 2000	1,809,003		1,809,003	28,796	1.59%	Feb 2004
C I Bond 2000 Administration		5,719,570		5,719,570	1,657,162	28.97%	
<b>Projects Not Started - To Be Funded in Future Years</b>							
Farrison-Newton, Classroom Building	Jun 2005	6,696,265		6,696,265			Jul 2008
Hoey Administration Building	Aug 2004	2,724,315		2,724,315			Aug 2006
B. N. Duke Auditorium Addition	Mar 2002	740,000		740,000			Feb 2004
<b>Total All Projects</b>		<b>\$ 121,246,203</b>	<b>\$ 2,888,395</b>	<b>\$ 124,134,598</b>	<b>\$ 14,063,369</b>		

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 System. 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.

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Ralph Campbell, Jr.  
State Auditor

STATE OF NORTH CAROLINA  
Office of the State Auditor

2 S. Salisbury Street  
20601 Mail Service Center  
Raleigh, NC 27699-0601  
Telephone: (919) 807-7500  
Fax: (919) 807-7647  
Internet <http://www.ncauditor.net>

**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**

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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, 2003, and have issued our report thereon dated June 7, 2004.

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*.

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. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant

**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)**

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deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the University's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable conditions noted as a result of our audit are described in the Audit Findings and Recommendations section of this report.

**Finding**

2. Controls over Payroll Separations

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. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider Finding 2 to be a material weakness.

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 7, 2004

## AUDIT FINDINGS AND RECOMMENDATIONS

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### **Matters Related to Financial Reporting or Federal Compliance Objectives**

The following findings and recommendations were identified during the current audit and describe conditions that represent significant deficiencies in internal control or noncompliance with laws, regulations, contracts, or grants.

#### **1. CONTROLS OVER PROCESSING STUDENT WITHDRAWALS FOR TITLE IV REFUNDS – STUDENT FINANCIAL ASSISTANCE CLUSTER**

The University did not have adequate controls over processing student withdrawals to ensure the required return of Title IV funds. The Office of Scholarships and Student Assistance relied on the enrollment status changes provided through Registration records to determine withdrawals. However, the University did not have an adequate system to ensure all student withdrawal information was included on the enrollment status change information in a timely manner. Examination of student withdrawals revealed 22 Student Financial Assistance recipients whose withdrawals were not processed by the Office of Scholarship and Student Aid. As a result, we are questioning \$24,312 in unearned Title IV funds the University failed to refund.

When a recipient of Title IV grant or loan assistance withdraws from an institution, the institution must determine the amount of Title IV aid earned by the student as of the withdrawal date. If the total amount of Title IV assistance earned by the student is less than the amount disbursed to the student or on his behalf, the difference must be returned to the Title IV programs. Federal regulation 34 CFR 668.22 requires returns of Title IV funds be deposited to the Student Financial Assistance accounts or returned to the appropriate lender within 30 days after the date the institution determines that the student withdrew.

*Recommendation:* The University should improve its controls over student withdrawal processing to ensure that all student withdrawals are identified and required Title IV refunds are prepared. We recommend the University refund the unearned Title IV funds the University failed to return.

*University's Response:* The University concurs with the audit finding. One hundred percent (100%) of the withdrawals were audited and 22 errors were found. A thorough review of the withdrawal process was initiated and the University recognized that the withdrawal process needed to be streamlined. Students were previously responsible for delivering withdrawal cards to key offices and often times missed the most critical office, the Registrar's Office.

The Vice Chancellor for Student Affairs enhanced the process by designating one point of contact for withdrawals. The new process has been simplified by allowing students to complete a withdrawal form in the Dean of Students Office, which finalizes the withdrawal process for the student. The Dean of Students will be responsible for

## AUDIT FINDINGS AND RECOMMENDATIONS (CONCLUDED)

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delivering withdrawal forms to pertinent offices such as Registrar, Scholarships and Student Aid, Federal Loans, and Academic Affairs. We believe this change will significantly improve the withdrawal process and allow the University to capture all withdrawals.

In addition to revising the withdrawal process, the University has hired a Registrar who has implemented specific procedures for processing of withdrawals. The Registrar's Office experienced vacancies in three critical positions during this timeframe (Registrar, Associate, and Assistant). With adequate staffing in the Registrar's Office and streamlining of the withdrawal process, we feel confident that this process will improve.

The unearned Title IV funds of \$24,312 were returned to the appropriate programs on March 1, 2004. Controls have been implemented to ensure that student withdrawals are processed within 30 days of notice as required by the Department of Education. The University shall closely monitor the withdrawal process to ensure that all students who withdraw are processed and unearned funds are returned in a timely manner to remain in compliance with federal guidelines.

### 2. CONTROLS OVER PAYROLL SEPARATIONS

The University did not have adequate internal control procedures to prevent terminated employees from remaining on the payroll. During the audit we identified a former employee who had resigned from his position in February, 2002, and was paid his monthly salary through February 2004, resulting in an overpayment of \$129,499. The University immediately removed the former employee from the payroll and requested repayment of the salary. The University is currently handling this matter through its legal counsel.

A reconciliation of the Human Resource Department's listing of all personnel actions to the payroll register would provide an effective internal control over payroll. This reconciliation would ensure that all personnel activities, including separations, are entered into the payroll. Also, University departments are responsible for their budgets and should closely monitor for unusual activity, such as excess payroll expenses.

*Recommendation:* We recommend that the University implement a control procedure requiring reconciliations of Human Resource personnel action listings to the payroll register. Individual departments should also be held responsible for reviewing their budgets for unusual activity.

*University's Response:* The University concurs with the finding. The University has strengthened its process for separating employees from the payroll. The University has incorporated the process of reconciling the payroll register to the separation report on a monthly basis. This added control would confirm that all employees are valid and no payments subsequent to the termination date will be issued (excluding the last payout). Additionally, through the budget process, departments have been made aware of the significance of monitoring their budgets.

## **DISTRIBUTION OF AUDIT REPORT**

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Director, Fiscal Research Division

August 30, 2004



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