STATE OF NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT OF

EAST CAROLINA UNIVERSITY

GREENVILLE, NORTH CAROLINA

FOR THE YEAR ENDED JUNE 30, 2004

OFFICE OF THE STATE AUDITOR

RALPH CAMPBELL, JR.

STATE AUDITOR

FINANCIAL STATEMENT AUDIT REPORT OF

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GREENVILLE, NORTH CAROLINA

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STATE OF NORTH CAROLINA
Office of the State Auditor

Ralph Campbell, Jr.
State Auditor

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AUDITOR'S TRANSMITTAL

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

This report presents the results of our financial statement audit of East Carolina 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, 2004. 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 East Carolina 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 East Carolina 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 East Carolina 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.

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

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

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 with federal 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 - Our tests disclosed no significant deficiencies in internal control over compliance and no instances of noncompliance which require disclosure herein under *OMB Circular A-133*.

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.

Ralph Campbell, Jr.
State Auditor

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
East Carolina University
Greenville, North Carolina

We have audited the accompanying financial statements of East Carolina University, a constituent institution of the sixteen-campus University of North Carolina System, which is a component unit of the State of North Carolina, and its discretely presented component unit, as of and for the year ended June 30, 2004, which collectively comprise the East Carolina University's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of East Carolina University Foundation, Inc. and Consolidated Affiliate, the University's discretely presented component unit. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for the discretely presented component unit, is based on the report of the other auditors.

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. The financial statements of East Carolina University Foundation, Inc. and Consolidated Affiliate were not audited in accordance with *Government Auditing Standards.* 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 and the report of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of East Carolina University and its discretely presented component unit, as of June 30, 2004, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

As discussed in Note 16 to the financial statements, the University implemented Governmental Accounting Standards Board Statement No. 39, *Determining Whether Certain Organizations Are Component Units,* during the year ended June 30, 2004.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 31, 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 grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

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 the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the East Carolina University's basic financial statements. Schedules 1 and 2 are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Ralph Campbell, Jr.

Ralph Campbell, Jr.
State Auditor

October 31, 2004

MANAGEMENT'S DISCUSSION AND ANALYSIS

Introduction

The discussion and analysis that follows provides an indication of the financial position and activities of East Carolina University for the fiscal year ended June 30, 2004. The preceding transmittal letter and the following financial statements and notes comprise our complete set of financial information. The MD&A identifies significant transactions that have financial impact and highlights favorable and unfavorable trends. Comparative data for the current and past year will be presented, with an emphasis on the current year.

Using the Financial Statements

There are three statements included in the University's financial report: the Statement of Net Assets, the Statement of Revenues, Expenses, and Changes in Net Assets and the Statement of Cash Flows. These financial statements are prepared in accordance with Government Accounting Standards Board (GASB) principles, which emphasize the University as a whole and not by fund groups. During fiscal year 2004, the University continued to follow the guidelines established by GASB statements 35, 37 and 38. These were first adopted for the year ended 2002 and provided for the division of revenues and expenses into operating and nonoperating, the separation of the Statement of Net Assets into current and noncurrent and the recording of depreciation expense for the first time, among other changes. Since there have been very few changes in accounting policies between this year and last year, it is possible to present comparative data.

The only significant change in this year's statements is the adoption of GASB statement 39, which impacts universities that have foundations and similarly affiliated organizations whose financial data has not been blended in the institution's annual report. The statement requires the University to include these organizations as part of the institution's financial reporting entity (as a discretely presented component unit) if they are found to be "significant". Significance is established if either the assets or revenues of the organization surpass 5% of the assets or revenues of the University. For 2004, the East Carolina University Foundation, Inc. is the only foundation that exceeded this threshold.

Financial Highlights

- At June 30, 2004, the University had assets of $690 million and liabilities of $139 million. These resulted in net assets of $551 million, which represent the residual interest in the assets after liabilities are deducted. The increase from last year's $532 million in net assets indicates an improvement of financial position.

- The statewide financial environment has begun to improve over the past fiscal year. This is evidenced by a $10 million increase in State appropriations.

Statement of Net Assets

The Statement of Net Assets presents a fiscal snapshot of the University as of June 30, 2004 and includes all assets and liabilities of the University. Net assets, as described above, is an indicator of the current financial condition of the University, while the change in net assets is an indicator of whether the overall financial condition has improved or worsened during the year. This data provides information on assets available to continue operations; amounts due to vendors, investors, and lending institutions; and the net assets available for expenditure by the University. Generally, assets and liabilities are measured using current values. One noteworthy exception is capital assets, which are presented at historical cost less accumulated depreciation. A summarized comparison of the University's assets, liabilities and net assets at June 30, 2004 and 2003 is as follows:

		(in thousands)	
	2004	**2003**	**Variance**
Assets			
Current Assets	$ 182,684	$ 183,330	$ (646)
Noncurrent Assets:			
Capital assets, net	453,923	419,116	34,807
Other	52,924	63,940	(11,016)
Total Noncurrent Assets	506,847	483,056	23,791
Total Assets	689,531	666,386	23,145
Liabilities			
Current Liabilities	40,192	35,451	4,741
Noncurrent Liabilities	98,308	98,467	(159)
Total Liabilities	138,500	133,918	4,582
Net Assets			
Invested in Capital Assets, net of related debt	385,052	341,623	43,429
Restricted - nonexpendable	8,042	8,997	(955)
Restricted – expendable	28,240	44,138	(15,898)
Unrestricted	129,697	137,710	(8,013)
Total Net Assets	$ 551,031	$ 532,468	$ 18,563

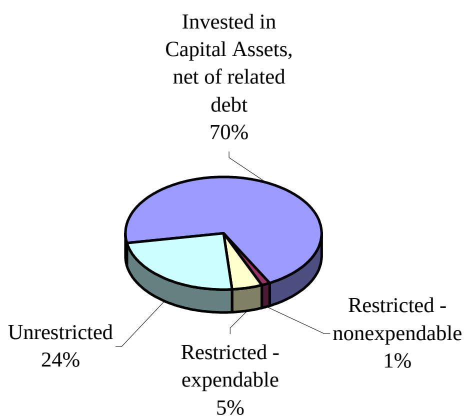
A review of the Statement of Net Assets at June 30, 2004 shows that the University continues to build upon its strong financial foundation. This financial health reflects the prudent utilization of its financial resources, including careful cost control, management of its endowment, conservative utilization of debt and adherence to its long range capital plan for the maintenance and replacement of the physical plant.

Current assets consist primarily of cash and receivables expected to be collected within the next accounting cycle. Current assets for the year ended June 30, 2004 were $182.7 million, which indicated virtually no change from $183.3 million for 2003. Total noncurrent assets increased from $483 million to $506.8 million, largely because of the construction of the West End Dining Hall and the renovations made to the Rivers and Flanagan buildings.

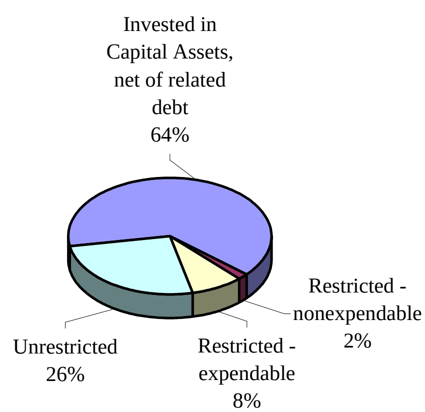
Current liabilities are comprised mostly of accounts payable, accrued compensation, and current portions of long-term liabilities. Current liabilities for the year increased to $40 million, comprised largely of accounts payable and accrued payroll, which together made up almost $24 million. Noncurrent liabilities showed relatively no change due to the fact that bonds were neither issued nor defeased during the fiscal year.

Net assets represent residual interest in the University's assets after all liabilities are deducted. For reporting purposes, they are divided into four categories: invested in capital assets, net of related debt; restricted nonexpendable; restricted expendable; and unrestricted net assets. The following charts display the contribution of each category to the total in both 2004 and 2003:

Net Assets 2004



Net Assets 2003



As the charts indicate, there was little change in the makeup of net assets. The largest portion continued to be assets invested in capital assets, net of related debt. This category encompasses the University's capital assets net of accumulated depreciation and outstanding principal balances of debt resulting from the acquisition, construction or improvement of those assets. Of the $551 million in net assets this year, $385 million was attributable to East Carolina's investment in capital assets. At June 30, 2004, the accumulated depreciation balance was $148 million.

Restricted nonexpendable net assets primarily include the University's permanent endowment funds. This year they accounted for $8 million of total net assets. Restricted expendable net assets are subject to externally imposed restrictions governing their use. This category of net assets made up $28 million of the $551 million net assets total.

Although unrestricted net assets are not subject to externally imposed stipulations, substantially all of the university's unrestricted net assets have been designated for various academic and research programs and initiatives, as well as capital projects. This year, unrestricted net assets amounting to $129 million represent 24% of the total net assets.

Statement of Revenues, Expenses, and Changes in Net Assets

Changes in total net assets as presented on the Statement of Net Assets are based on the activity presented in the Statement of Revenues, Expenses, and Changes in Net Assets. The purpose of this statement is to present the revenues received by the institution, both operating and nonoperating, and any other revenues, expenses, gains or losses received or incurred by the institution.

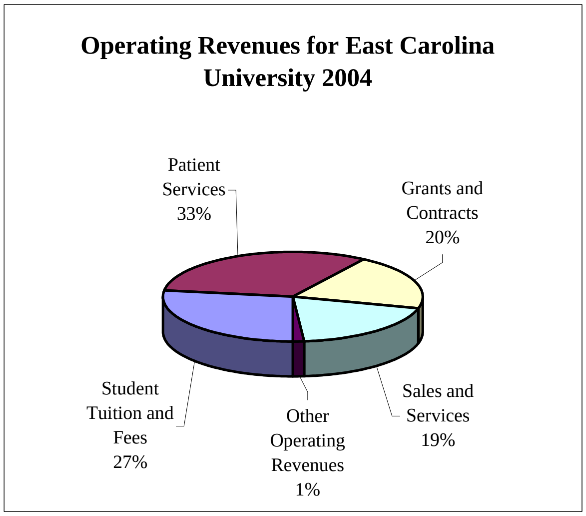
Operating revenues are received for providing goods and services to the various customers and constituencies of the University. Operating expenses are used to acquire or produce the goods and services provided in return for the operating revenues and to carry out the mission of the University. Nonoperating revenues are revenues received for which goods and services are not provided, i.e., state appropriations and investment income. Nonoperating expenses include interest expense, extraordinary items, and results of accounting changes, i.e. expenses not involved in the normal operation of the University. Operating income is the residual amount after operating expenses are deducted from operating revenues. The following is a condensed Statement of Revenues, Expenses, and Changes in Net Assets for East Carolina University as of June 30, 2004, compared with that of 2003.

(in thousands)

	2004	2003	Variance
Operating Income (Loss)			
Operating Revenues	$ 292,902	$ 277,563	$ 15,339
Operating Expenses	(473,512)	(424,277)	(49,235)
Total Operating Income (Loss)	(180,610)	(146,714)	(33,896)
Nonoperating Revenues (Expenses)	178,494	167,427	11,067
Income (Loss) before other revenues, expenses, gains and losses	(2,116)	20,713	(22,829)
Other revenues, expenses gains and losses	20,679	45,396	(24,717)
Change in Net Assets	18,563	66,109	(47,546)
Net Assets - July 1	532,468	466,359	66,109
Change in Net Assets (above)	18,563	66,109	(47,546)
Net Assets - June 30	$ 551,031	$ 532,468	$ 18,563

One of the University's greatest strengths is the diversity in the streams of revenue that supplement its student tuition and fees and State appropriations. These include voluntary private support from individuals, foundations, and corporations, along with government and other sponsored programs, and investment income. The University has in the past and will continue to seek funding from all possible sources consistent with its mission and to prudently manage the financial resources realized from these efforts to fund its operating activities.

The Statement of Revenues, Expenses, and Changes in Net Assets reflects a positive year with an increase in net assets at year-end of almost $19 million.

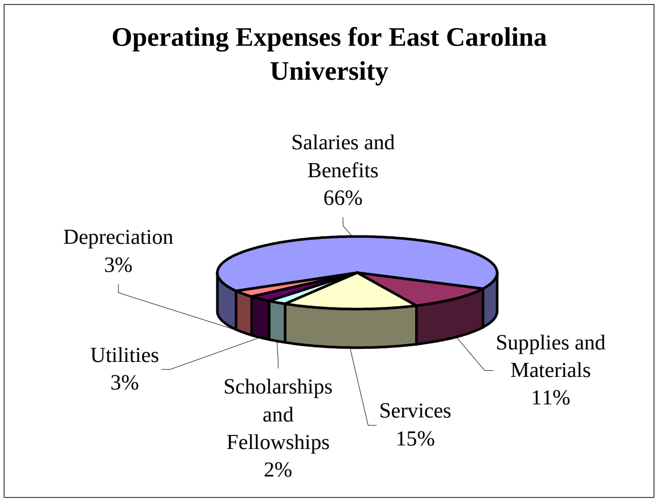


Operating revenues totaled $293 million and consisted of five areas: student tuition and fees, net; patient services, net; grants and contracts; sales and services, net; and other operating revenues. The chart to the left shows each component of operating revenue as it relates to total operating revenues as a whole.

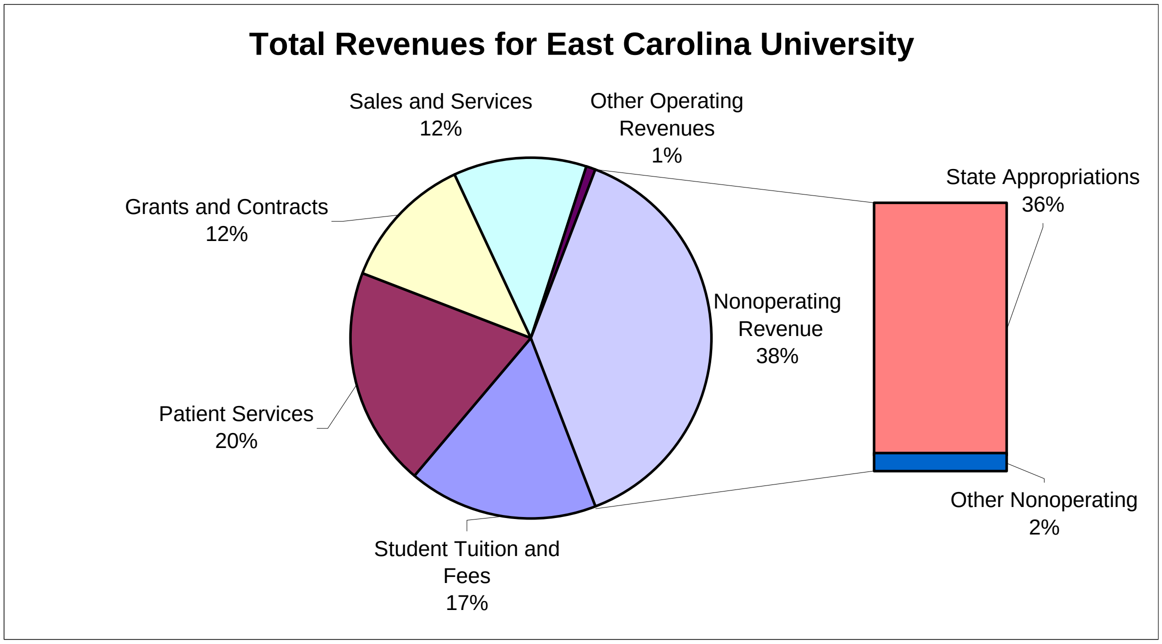
As is evident by the graph, patient services make up one-third of all operating revenues. Student tuition and fees are the second largest and are presented net of the tuition discount. The tuition discount is an offset to revenues for the scholarships and fellowships that are applied to student accounts.

There were no major differences in the areas of operating revenues between 2003 and 2004. None of the parts changed more than 1% in either direction.

As depicted in the chart to the right, operating expenses are mainly attributable to salaries and benefits for the faculty and staff of the University. Of the $474 million in operating expenses, $311 million were used for this purpose. Other elements included in operating expenses are supplies and materials, services, scholarships and fellowships, utilities and depreciation. Almost all areas were identical to last year in terms of their percent of contribution. Supplies and materials went up by two percent and salaries and benefits went down by two percent.



As mentioned before, nonoperating revenue consists primarily of State appropriations and investment income. Of the $182 million recognized as nonoperating revenue, disregarding nonoperating expenses, $171 million reflect appropriated funds from the State. As expected, these appropriations contribute greatly to the overall revenues of the University. The following graph examines the effect of these nonoperating revenues in conjunction with all revenues for the institution.



As illustrated by the above graph, State appropriations represent a very significant component of total revenues for the University. They account for thirty-six percent of total revenue and ninety-four percent of nonoperating revenue. Although the percentages were about the same as last year, the amount received for State appropriations increased by $10 million. As mentioned before, this increase reflects an improvement in the State economic situation as a whole.

Nonoperating expenses for the University were mostly comprised of interest and fees on capital asset-related debt, which totaled $2.8 million. This is slightly higher than the $2.4 million in interest and fees paid last year. This increase can be explained by rising interest rates on which the variable bond debt is based. The amount for interest and fees represents less than one percent of all University expenses for the year.

Statement of Cash Flows

The Statement of Cash Flows provides detail on the cash activity for the year. Cash provided or used is categorized based on the type of activity, i.e., operating, noncapital financing, capital financing or investing. Net cash used is reconciled to the operating income or loss reflected on the Statement of Revenues, Expenses, and Changes in Net Assets. The following is a condensed version of the Statement of Cash Flows for the year ended June 30, 2004.

		(in thousands)
Cash Provided (Used) by:		
Operating activities	$	(162,691)
Noncapital financing activities		175,193
Capital financing activities		(28,538)
Investing activities		6,669
Net change in cash		(9,367)
Cash, beginning of year		160,576
Cash, end of Year	$	151,209

Operating activities are those activities that result from providing goods and services and include the cash effects of transactions that enter into the determination of operating income. This is also the residual category, meaning that it covers transactions that do not fit into any of the other categories. The most significant source of operating cash is cash that has been received from customers, which increased to $292 million. This includes tuition and fees, grants and contracts, patient services, and sales and services of educational and auxiliary nature. The most notable use of operating cash was for compensation and benefits for University employees, which totaled $307 million.

Noncapital financing activities include borrowing money for purposes other than to acquire, construct, or improve capital assets. These activities also include repaying those amounts borrowed, including interest, along with certain other interfund or intergovernmental receipts and payments. Almost all of this activity results from State appropriations.

Capital financing activities include borrowing money for the acquisition, construction, improvement and disposal of capital assets used in providing services or producing goods. This also includes repayments as well as interest. Sources in this area incorporate $25 million in capital grants and $2 million in proceeds from capital debt. Acquisition and construction of capital assets in the amount of $49 million was the most significant capital use.

The final group on the Statement of Cash Flows is investing. Investing activities include making and collecting loans and acquiring or disposing of debt or equity instruments. Proceeds from sales and maturities of investments, along with interest on investments, make up the $24 million in investing sources. The major related use of these funds was $18 million for the purchase of investments and related fees.

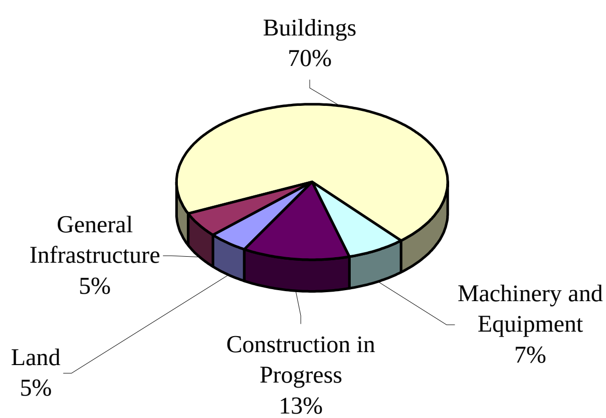
Capital Assets

A critical factor in continuing the quality of the University's academic and research programs and residential life is the acquisition, construction and improvement of its capital assets. The University continues to implement its long-range plan to modernize its complement of older teaching and research facilities, balanced with new construction. This goal has been significantly enhanced by the 2000 Higher Education Bond issue that has provided East Carolina University with $190 million of funding to construct new academic buildings, renovate older facilities and update or replace campus infrastructure.

The University had $454 million invested in capital assets at year-end. There was a net increase from $419 million from last year, which is mostly attributable to the construction of the new West End Dining Hall and the renovations made to the Rivers and Flanagan buildings.

Capital assets for the University were comprised of nondepreciable and depreciable assets. Nondepreciable assets were land and construction in progress. Depreciable assets were buildings, machinery and equipment, and general infrastructure. The following chart displays the relationship of each category to total capital assets as a whole.

Capital Assets for East Carolina University



As is evident from the capital asset chart, most of the University's capital assets are in the form of buildings which have been completed or that are construction in progress. Construction in progress lost nine percentage points, which was offset by the nine point increase for buildings.

Capital additions consist primarily of replacement, renovation and new construction of capital assets as well as significant investments in equipment, including information technology. Capital additions totaled $49 million. As noted above, a major component of this was funded from the $2.5 billion Higher Education Bond issue allocated to the University system that was approved by the voters in North Carolina in 2000.

In order to continue to provide quality educational experiences, it is imperative that the University maintains a constant level of growth in regards to capital assets. A plan of this nature will assist the University in avoiding obsolescence and will also provide a marketable tool for attracting more students to the school. Significant capital additions already committed for next fiscal year are depicted below.

Description	Funding Source	Amount in Thousands
West End Dining Hall	Self-Liquidating	$ 4,020
Expansion of Harrington Field	Restricted Gifts	7,662
Third Floor Nursing Building	Appropriated	1,419
Flanagan Building Improvements	Appropriated	4,534
Clement, White, Greene A/C	Bond Proceeds	1,447

Also on the horizon for East Carolina University is the development of a new cardiovascular research center. House Bill 1264, which was signed on August 5, 2004, provides the University with $60 million for the construction of this facility.

More detailed information on the University's capital assets is presented in note 5 to the financial statements.

Debt

The University had $68.9 million in outstanding bonds, notes and capital leases on June 30, 2004. Of this, $66.6 million was for bonds, $1.9 million was for capital leases and $359 thousand was for notes payable. No new bonds were issued during the year, but there was a $1.9 million capital lease established for the acquisition of a linear accelerator for the Leo Jenkins Cancer Center.

More detailed information on the University's long-term obligations is presented in note 7 to the financial statements.

Economic Forecast

Management believes that the University is well positioned to continue its strong financial condition and level of excellence in service to students, the community, and governmental agencies. The University's strong financial position, as evidenced by its continued growth in enrollment, the overwhelming support by the citizens of North Carolina for the issuance of the $2.5 billion bond issue for which East Carolina University received $190 million for key capital projects and an A1 rating from Moody's on the latest bond issuance will provide a high degree of flexibility in supporting expected growth in the future. This flexibility, along with the University's ongoing efforts toward revenue enhancement and cost containment, will enable the University to provide the necessary resources to support this level of excellence.

The North Carolina economy continues to lag due to the weak financial markets and a large economic dependency on textiles and tobacco. This provides a challenge to the North Carolina General Assembly to identify other revenue streams. This also provides an opportunity for East Carolina University to expand its partnership with local and State governments to establish an environment that will bring new businesses to North Carolina and provide additional revenues to the State.

A crucial element of the University's future will continue to be our relationship with the State of North Carolina. Education continues to be recognized as an investment in North Carolina's future and is well supported by the State of North Carolina General Assembly, Board of Governors and the North Carolina citizens. The State continues to fully fund enrollment increases, providing substantial additional resources to East Carolina University based on significant growth in our student population through the end of the decade.

The University continues to execute its long-range plan to modernize and expand its complement of teaching and research facilities with a balance of new construction. The majority of the funding for these projects was provided by the $2.5 billion Higher Education Bond issue overwhelmingly passed by the voters in 2000. This strategy addresses the University's need for infrastructure growth and the continuing effects of technology on teaching and research methodologies.

Private gifts are an important supplement to the fundamental support from the State and student tuition, and a significant factor in the growth of academic units. Economic pressures affecting donors may also affect the future level of support the University receives from corporate and individual giving.

For endowments, the University will continue to employ its long-term investment strategy to maximize total returns, at an appropriate level of risk, while utilizing a spending rate policy to insulate the University's operations from temporary market volatility.

While it is not possible to predict the ultimate results, management believes that the University's financial condition is strong enough to weather any economic uncertainties.

Contacting the University's Financial Management

This financial report is designed to provide our citizens, investors and creditors with a general overview of the University's finances and show accountability for all funds received. If you have any questions or need additional financial information, please contact David Price, Financial Director for East Carolina University, at (252) 328-6252.

East Carolina University
Statement of Net Assets
June 30, 2004 — ***Exhibit A-1***

ASSETS	
Current Assets:	
Cash and Cash Equivalents	$ 114,353,893.75
Restricted Cash and Cash Equivalents	16,623,310.05
Receivables, Net (Note 4)	40,746,264.03
Due from Primary Government	4,289,442.35
Due from State of North Carolina Component Units	550,000.00
Due from University Component Units	99,850.01
Inventories	2,922,643.05
Notes Receivable, Net (Note 4)	1,912,731.92
Other Assets	1,185,722.78
Total Current Assets	182,683,857.94
Noncurrent Assets:	
Restricted Cash and Cash Equivalents	20,231,357.61
Restricted Due from Primary Government	6,005,981.14
Endowment Investments	11,860,106.46
Other Long-Term Investments	4,286,157.19
Notes Receivable, Net (Note 4)	10,540,168.33
Capital Assets - Nondepreciable (Note 5)	79,318,034.05
Capital Assets - Depreciable, Net (Note 5)	374,605,181.27
Total Noncurrent Assets	506,846,986.05
Total Assets	689,530,843.99
LIABILITIES	
Current Liabilities:	
Accounts Payable and Accrued Liabilities (Note 6)	24,186,109.19
Deferred Revenue	9,454,824.71
Interest Payable	445,978.21
Long-Term Liabilities - Current Portion (Note 7)	6,105,405.92
Total Current Liabilities	40,192,318.03
Noncurrent Liabilities:	
Deposits Payable	2,003,519.41
Funds Held for Others	8,019,569.96
U. S. Government Grants Refundable	12,133,020.28
Long-Term Liabilities (Note 7)	76,151,540.68
Total Noncurrent Liabilities	98,307,650.33
Total Liabilities	138,499,968.36

East Carolina University
Statement of Net Assets **_Exhibit A-1_**
June 30, 2004 **_Page 2_**

NET ASSETS	
Invested in Capital Assets, Net of Related Debt	385,052,304.67
Restricted for:	
Nonexpendable:	
Scholarships and Fellowships	811,953.82
Endowed Professorships	5,558,184.71
Departmental Uses	317,852.27
Loans	1,353,522.08
Expendable:	
Scholarships and Fellowships	2,650,057.77
Research	953,268.49
Departmental Uses	686,656.67
Loans	1,534,760.08
Capital Projects	18,237,255.29
Debt Service	3,888,721.25
Other	289,331.75
Unrestricted	129,697,006.78
Total Net Assets	$ 551,030,875.63

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

East Carolina University
Statement of Revenues, Expenses, and
Changes in Net Assets
For the Fiscal Year Ended June 30, 2004 ***Exhibit A-2***

REVENUES		
Operating Revenues:		
Student Tuition and Fees, Net (Note 9)	$	80,093,896.77
Patient Services, Net (Note 9)		93,318,434.44
Federal Grants and Contracts		26,594,734.22
State and Local Grants and Contracts		8,048,939.05
Nongovernmental Grants and Contracts		24,103,985.80
Sales and Services, Net (Note 9)		56,739,806.19
Interest Earnings on Loans		140,302.93
Other Operating Revenues		3,862,045.35
Total Operating Revenues		292,902,144.75
EXPENSES		
Operating Expenses:		
Salaries and Benefits		310,849,204.22
Supplies and Materials		51,218,905.70
Services		73,219,372.40
Scholarships and Fellowships		11,008,595.51
Utilities		13,082,067.83
Depreciation		14,133,601.70
Total Operating Expenses		473,511,747.36
Operating Loss		(180,609,602.61)
NONOPERATING REVENUES (EXPENSES)		
State Appropriations		171,008,133.40
Noncapital Gifts		4,184,896.86
Investment Income		6,458,033.67
Interest and Fees on Capital Asset-Related Debt		(2,829,903.79)
Other Nonoperating Expenses		(326,734.28)
Net Nonoperating Revenues		178,494,425.86
Loss Before Other Revenues, Expenses, Gains, or Losses		(2,115,176.75)
Capital Appropriations		387,500.00
Capital Grants		19,588,556.00
Capital Gifts		702,486.88
Increase in Net Assets		18,563,366.13
NET ASSETS		
Net Assets - July 1, 2003		532,467,509.50
Net Assets - June 30, 2004	$	551,030,875.63

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

East Carolina University
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2004 — ***Exhibit A-3***

CASH FLOWS FROM OPERATING ACTIVITIES	
Received from Customers	$ 292,276,258.96
Payments to Employees and Fringe Benefits	(307,184,705.02)
Payments to Vendors and Suppliers	(135,861,512.65)
Payments for Scholarships and Fellowships	(11,008,595.51)
Loans Issued	(3,111,765.00)
Collection of Loans	2,127,690.67
Interest Earned on Loans	143,351.49
Student Deposits Received	2,927,333.64
Student Deposits Returned	(2,998,975.22)
Net Cash Used by Operating Activities	(162,690,918.64)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
State Appropriations	171,008,133.40
Noncapital Gifts	4,184,896.86
Net Cash Provided by Noncapital Financing Activities	175,193,030.26
CASH FLOWS FROM CAPITAL FINANCING AND RELATED FINANCING ACTIVITIES	
Proceeds from Capital Debt	1,986,174.66
State Capital Appropriations	387,500.00
Capital Grants	24,977,739.14
Capital Gifts	702,486.88
Proceeds from Sale of Capital Assets	67,589.82
Acquisition and Construction of Capital Assets	(49,335,564.52)
Principal Paid on Capital Debt and Leases	(4,537,335.94)
Interest and Fees Paid on Capital Debt and Leases	(2,787,003.11)
Net Cash Used by Capital Financing and Related Financing Activities	(28,538,413.07)
CASH FLOWS FROM INVESTING ACTIVITIES	
Proceeds from Sales and Maturities of Investments	18,785,477.66
Investment Income	5,435,757.26
Purchase of Investments and Related Fees	(17,551,988.32)
Net Cash Provided by Investing Activities	6,669,246.60
Net Decrease in Cash and Cash Equivalents	(9,367,054.85)
Cash and Cash Equivalents - July 1, 2003	160,575,616.26
Cash and Cash Equivalents - June 30, 2004	$ 151,208,561.41

East Carolina University

Statement of Cash Flows — ***Exhibit A-3***

For the Fiscal Year Ended June 30, 2004 — ***Page 2***

RECONCILIATION OF NET OPERATING REVENUES (EXPENSES) TO NET CASH USED BY OPERATING ACTIVITIES		
Operating Loss	$	(180,609,602.61)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:		
Depreciation Expense		14,133,601.70
Changes in Assets and Liabilities:		
Receivables (Net)		(352,355.48)
Due from Primary Government		(1,206,267.75)
Due from State of North Carolina Component Units		(482,200.00)
Due from University Component Units		(99,850.01)
Inventories		(311,237.90)
Prepaid Items		131,028.65
Accounts Payable and Accrued Liabilities		2,302,580.97
Funds Held for Others		621,654.75
U. S. Government Grants Refundable		351,637.28
Deferred Revenue		1,645,120.19
Compensated Absences		2,240,687.48
Deposits Payable		(71,641.58)
Note Principle Repayments		2,127,690.67
Notes Issued		(3,111,765.00)
Net Cash Used by Operating Activities	$	(162,690,918.64)
RECONCILIATION OF CASH AND CASH EQUIVALENTS		
Current Assets:		
Cash and Cash Equivalents	$	114,353,893.75
Restricted Cash and Cash Equivalents		16,623,310.05
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		20,231,357.61
Total Cash and Cash Equivalents - June 30, 2004	$	151,208,561.41
NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES		
Change in Fair Value of Investments	$	1,389,132.11
Loss on Disposal of Capital Assets		394,324.10

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

East Carolina University Foundation, Inc.
and Consolidated Affiliate
Consolidated Statement of Financial Position
June 30, 2004 — *Exhibit B-1*

ASSETS		
Cash and Cash Equivalents	$	194,127
Investments		44,642,091
Investment in Joint Venture		2,100,000
Cash Surrender Value of Life Insurance		120,842
Assets Held in Charitable Trusts and Annuities		2,452,503
Real Estate Held for Resale		1,573,396
Receivables, Net		5,908,219
Prepaid Expenses		4,396
Total Assets		56,995,574
LIABILITIES		
Accounts Payable and Accrued Expenses		69,704
Due to University and Other Foundations		104,832
Funds Held for Others		1,035,511
Split Interest Agreement Obligations		590,367
Annuities Payable		805,754
Total Liabilities		2,606,168
NET ASSETS		
Unrestricted		5,163,287
Temporarily Restricted		14,128,130
Permanently Restricted		35,097,989
Total Net Assets	$	54,389,406

See Note 1 in the Notes to the Financial Statements

East Carolina University Foundation, Inc.
and Consolidated Affiliate
Consolidated Statement of Activities
For the Fiscal Year Ended June 30, 2004

Exhibit B-2

REVENUES	
Gifts, Donations, and Contributions	4,849,867
Contributed Services and Facilities	1,559,528
Change in Fair Value of Split Interest Agreements	920,793
Investment Income	421,180
Net Realized and Unrealized Gains on Investments	5,918,702
Loss on Sale of Capital Assets	(2,330,892)
Miscellaneous Income	225,095
Total Revenues	11,564,273
EXPENSES	
Program services:	
Gifts, Scholarships, Professorships, Support, etc. to or for East Carolina University	2,214,029
General and Administrative	540,975
Fund Raising	1,484,449
Total Expenses	4,239,453
Change in Net Assets	7,324,820
NET ASSETS	
Net Assets - Beginning of Year	47,064,586
Net Assets - End of Year	54,389,406

See Note 1 in the Notes to the Financial Statements

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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. East Carolina 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. The University's component units are either blended or discretely presented in the University's financial statements. The blended component unit, although legally separate, is, in substance, part of the University's operations and therefore, is reported as if it were part of the University. Discretely presented component unit's financial data is reported in separate financial statements because of its use of different GAAP reporting models and to emphasize its legal separateness.

Blended Component Units - Although legally separate, the ECU International Human Performance Center, Inc. (Corporation), a component unit of the University, is reported as if it were part of the University.

The Corporation is governed by a fifteen-member board of which the majority is appointed by the Chancellor of East Carolina University. The Corporation's purpose is to aid, support and promote teaching, research, and service in the various educational, scientific, scholarly, professional, artistic, and creative endeavors of the University. Because a majority of the board members of the Corporation are appointed by the Chancellor of East Carolina University and the Corporation's sole purpose is to benefit

East Carolina University, its financial statements have been blended with those of the University.

Separate financial statements for the Corporation may be obtained from the University Financial Service's Office, 120 Reade Street, Greenville, NC 27858, or by calling (252) 328-6757. Other related foundations and similar nonprofit corporations for which the University is not financially accountable are not part of the accompanying financial statements.

Discretely Presented Component Unit – East Carolina University Foundation, Inc. is a legally separate not-for-profit corporation and is reported as a discretely presented component unit based on the nature and significance of its relationship to the University. The East Carolina University Real Estate Foundation, Inc. is the consolidated affiliate of the East Carolina University Foundation, Inc.

The East Carolina University Foundation, Inc. is a legally separate, tax-exempt component unit of the University. The Foundation acts primarily as a fund-raising organization to supplement the resources that are available to the University in support of its programs. The Foundation board consists of thirty-six members. Although the University does not control the timing or amount of receipts from the Foundation, the majority of resources, or income thereon, that the Foundation holds and invests are restricted to the activities of the University by the donors. Because these restricted resources held by the Foundation can only be used by, or for the benefit of the University, the Foundation is considered a component unit of the University and is reported in separate financial statements because of the difference in its reporting model, as described below.

The East Carolina University Foundation, Inc. is a private not-for-profit organization that reports its financial results under Financial Accounting Standards Board (FASB) Statements. As such, certain revenue recognition criteria and presentation features are different from GASB revenue recognition criteria and presentation features. No modifications have been made to the Foundation's financial information in the University's financial reporting entity for these differences.

During the year ended June 30, 2004, the Foundation distributed $2,214,029.00 to the University for both restricted and unrestricted purposes. Complete financial statements for the Foundation can be obtained from the University Financial Service's Office, 120 Reade Street, Greenville, NC 27858, or by calling (252) 328-6757.

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

Pursuant to the provisions of GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*, 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 undeposited receipts, petty cash, cash on deposit with private bank accounts, money market accounts, cash on deposit with fiscal agents, 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, money market funds, and limited partnerships. Except for money market funds and limited partnerships, 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. Money market funds and limited partnerships 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 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 the lower of cost or market value using the first-in, first-out method, except for the University bookstore which uses the retail inventory 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. Interest costs incurred are capitalized during the period of construction.

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 15 to 75 years for general infrastructure, 10 to 50 years for buildings, and 3 to 15 years for equipment. The University does not capitalize the library and art collections. These collections adhere to the University's policy to maintain for public exhibition, education or research; protect, keep unencumbered, care for and preserve; and requires proceeds from their sale to be used to acquire other collection items. Accounting principles generally accepted in the United States of America permit collections maintained in this manner to be charged to operations at time of purchase rather than be capitalized.

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, notes payable, capital lease obligations, and compensated absences that will not be paid within the next fiscal year.

Bonds payable are reported net of unamortized premiums or discounts and deferred losses on refundings. The University amortizes bond premiums/discounts over the life of the bonds using the straight-line method. The deferred losses on refundings are amortized over the life of the old debt or new debt (whichever is shorter) 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 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 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 bonuses awarded by the North Carolina General Assembly to all full-time permanent employees as of September 30, 2002 and as of July 1, 2003. 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 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.*

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, printing and graphics, motor pool, postal services, and telecommunications. 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, except for funds received for services rendered by health care professionals, with the State Treasurer. Although specifically exempted, the University may voluntarily deposit endowment funds, special funds, revenue bond proceeds, debt service funds, and funds received for services rendered by health care professionals 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 totaling $148,051,519.41. At year-end, cash on hand was $3,157,042.00. The University's portion of the State Treasurer's Investment Pool was $147,952,719.34. 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 $98,800.07 and the bank balance was $87,345.94, all of which was covered by federal depository insurance.

North Carolina General Statutes 147-69.1(c), applicable to the State's General Fund, and 147-69.2, applicable to institutional trust funds, 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 Section 600.2.4 of the Policy Manual of the University of North Carolina, to invest its special funds and funds received for services rendered by health care professionals 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 that 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.

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

A summary of the University's investments at June 30, 2004 is presented below:

Investments

	Fair Value			
	Risk Category			
	1	2	3	Total
Categorized Investments:				
U.S. Government Securities	$ 0.00	$ 4,414,188.30	$ 0.00	$ 4,414,188.30
Corporate Bonds		6,120.38		6,120.38
Corporate Stocks		184,221.15		184,221.15
Total Categorized Investments	$ 0.00	$ 4,604,529.83	$ 0.00	4,604,529.83
Investments Not Categorized:				
Money Market Funds				28,770.82
Mutual Funds				9,849,506.00
Limited Partnerships				1,663,457.00
Total Investments Not Categorized				11,541,733.82
Total Investments				$ 16,146,263.65

NOTE 3 - ENDOWMENT INVESTMENTS

Investments of the University's endowment funds are 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 based on an adopted spending policy which limits spending to 2% of the endowment principal's average market value. To the extent that the total return for the current year exceeds the payout and a .5% administrative fee, the excess is added to principal. If current year earnings do not meet the payout requirements, the University uses accumulated income and appreciation from restricted, expendable net asset endowment balances to make up the difference. Due to the decline in the stock market during recent years, the Endowment Board has taken action to stop the spending of those endowments that are currently "underwater" by 106% of the original endowment amount. The spending accounts for those endowments have been transferred to quasi-endowment accounts. At June 30, 2004, net appreciation of $1,127,066.80 was available to be spent, of which $507,618.72 was restricted to specific purposes.

NOTE 4 - RECEIVABLES

Receivables at June 30, 2004 were as follows:

	Gross Receivables	Less Allowance for Doubtful Accounts	Net Receivables
Current Receivables:			
Students	$ 3,663,392.05	$ 134,732.00	$ 3,528,660.05
Accounts	56,360,830.31	24,459,856.33	31,900,973.98
Investment Earnings	2,078.19		2,078.19
Interest on Loans	152,324.66		152,324.66
Other	5,162,227.15		5,162,227.15
Total Current Receivables	$ 65,340,852.36	$ 24,594,588.33	$ 40,746,264.03
Notes Receivable:			
Notes Receivable - Current:			
Federal Loan Programs	$ 2,106,428.10	$ 197,917.62	$ 1,908,510.48
Institutional Student Loan Programs	4,342.44	121.00	4,221.44
Total Notes Receivable - Current	$ 2,110,770.54	$ 198,038.62	$ 1,912,731.92
Notes Receivable - Noncurrent:			
Federal Loan Programs	$ 10,540,168.33	$ 0.00	$ 10,540,168.33

NOTE 5 - CAPITAL ASSETS

A summary of changes in the capital assets for the year ended June 30, 2004, is presented as follows:

	Balance July 1, 2003	Adjustments	Increases	Decreases	Balance June 30, 2004
Capital Assets, Nondepreciable:					
Land	$ 21,397,133.08	$ 0.00	$ 399,510.14	$ 0.00	$ 21,796,643.22
Construction in Progress	90,202,177.33	(70,558,890.89)	37,878,104.39		57,521,390.83
Total Capital Assets, Nondepreciable	111,599,310.41	(70,558,890.89)	38,277,614.53		79,318,034.05
Capital Assets, Depreciable:					
Buildings	352,037,443.44	66,601,959.11	200,561.81		418,839,964.36
Machinery and Equipment	72,646,819.55	2,808,935.93	10,857,388.18	10,061,928.87	76,251,214.79
General Infrastructure	26,161,421.11	1,147,995.85			27,309,416.96
Total Capital Assets, Depreciable	450,845,684.10	70,558,890.89	11,057,949.99	10,061,928.87	522,400,596.11
Less Accumulated Depreciation/Amortization for:					
Buildings	92,551,673.23		7,429,891.54		99,981,564.77
Machinery and Equipment	47,921,670.30		6,140,023.90	9,667,604.77	44,394,089.43
General Infrastructure	2,856,074.38		563,686.26		3,419,760.64
Total Accumulated Depreciation	143,329,417.91		14,133,601.70	9,667,604.77	147,795,414.84
Total Capital Assets, Depreciable, Net	307,516,266.19	70,558,890.89	(3,075,651.71)	394,324.10	374,605,181.27
Capital Assets, Net	$ 419,115,576.60	$ 0.00	$ 35,201,962.82	$ 394,324.10	$ 453,923,215.32

NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2004 were as follows:

	Amount
Accounts Payable	$ 10,496,943.86
Accrued Payroll	11,449,697.22
Contract Retainage	2,117,794.19
Other	121,673.92
Total Accounts Payable and Accrued Liabilities	$ 24,186,109.19

NOTE 7 - LONG-TERM LIABILITIES

A. Changes in Long-Term Liabilities - A summary of changes in the long-term liabilities for the year ended June 30, 2004 is presented as follows:

	Balance July 1, 2003	Additions	Reductions	Balance June 30, 2004	Current Portion
Bonds Payable	$ 70,860,000.00	$ 0.00	$ 4,270,000.00	$ 66,590,000.00	$ 4,305,000.00
Notes Payable	562,071.93		203,257.41	358,814.52	214,020.00
Total Notes and Bonds Payable	71,422,071.93		4,473,257.41	66,948,814.52	4,519,020.00
Capital Leases Payable		1,986,174.66	64,078.53	1,922,096.13	261,107.43
Compensated Absences	11,145,348.47	9,380,796.17	7,140,108.69	13,386,035.95	1,325,278.49
Total Long-Term Liabilities	$ 82,567,420.40	$ 11,366,970.83	$ 11,677,444.63	$ 82,256,946.60	$ 6,105,405.92

Additional information regarding capital lease obligations is included in Note 8.

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 6/30/2004	Principal Outstanding 6/30/2004
Housing and Dining Services						
Residence Hall Renovation-Jarvis	1998	4.00-4.75	11/1/2018	$ 5,095,000.00	$ 880,000.00	$ 4,215,000.00
Jones Hall and Gallery Dining Facility Renovations	2001A	4.25-5.75	11/1/2021	12,570,000.00		12,570,000.00
Housing and Dining Revenue Refunding Bonds	2001B	4.25-5.75	11/1/2015	11,985,000.00	2,980,000.00	9,005,000.00
West End Dining Hall	2003A	2.60-5.00	5/1/2024	14,960,000.00		14,960,000.00
Total Housing and Dining Services				44,610,000.00	3,860,000.00	40,750,000.00
Student Services System						
Student Health Center	1999	4.75-5.25	5/1/2019	3,500,000.00	625,000.00	2,875,000.00
Student Recreation Center Refunding Bonds	2001C	3.00-4.75	5/1/2019	14,555,000.00	1,830,000.00	12,725,000.00
Total Student Services System				18,055,000.00	2,455,000.00	15,600,000.00
Athletic Facilities Revenue System						
Athletic Facilities Student Fee Refunding Bonds	2003A	2.00-4.00	5/1/2009	4,630,000.00	725,000.00	3,905,000.00
Athletic Department Variable Rate Demand Revenue Bonds	1996	1.1, variable	5/1/2017	7,000,000.00	1,900,000.00	5,100,000.00
Total Athletic Facilities Revenue System				11,630,000.00	2,625,000.00	9,005,000.00
The University of North Carolina System Pool Revenue Bonds						
Blount Intramural Field	(A)	1.1, variable	10/1/2008	1,050,000.00	555,000.00	495,000.00
Reade Street Parking Lot	(A)	1.1, variable	10/1/2008	1,575,000.00	835,000.00	740,000.00
Total The University of North Carolina System Pool Revenue Bonds				2,625,000.00	1,390,000.00	1,235,000.00
Total Bonds Payable (principal only)				$ 76,920,000.00	$ 10,330,000.00	$ 66,590,000.00

(A) The University of North Carolina System Pool Revenue Bonds, Series 1998A

C. **Demand Bonds** - Included in bonds payable are several variable rate demand bond issues. Demand bonds are securities that contain a "put" feature that allows bondholders to demand payment before the maturity of the debt upon proper notice to the University's remarketing or paying agents.

With regards to the following demand bonds, the University has not entered into legal agreements, which would convert the demand bonds not successfully remarketed into another form of long-term debt.

East Carolina University Athletic Department Variable Rate Demand Bonds, Series 1996: On December 1, 1996 the University issued tax-exempt adjustable mode demand bonds in the amount of $7,000,000.00 that have a final maturity date of May 1, 2017. The bonds are subject to mandatory sinking fund redemption that began on May 1, 1998. The proceeds of this issuance are to pay the cost of renovating and expanding Dowdy-Ficklen Stadium on the campus of East Carolina University and to pay the cost incurred in connection with the issuance of the 1996 bonds. The bonds are subject to purchase on demand with seven days' notice and delivery to the University's remarketing agent, Alex, Brown & Sons, Inc.

Under an irrevocable letter of credit issued by Wachovia Bank of North Carolina, N.A., the trustee is entitled to draw amounts sufficient to pay principal and interest on the bonds and amounts sufficient to pay the purchase price and accrued interest on bonds delivered for purchase. The University is required to pay an annual commitment fee of .30% of the amount of the bonds then currently outstanding plus an amount for accrued interest.

The University has entered into a reimbursement agreement with Wachovia Bank of North Carolina, N.A. in which it has agreed upon termination of the letter of credit to repay all amounts that are drawn under the letter of credit. Interest is at the rate of prime. At June 30, 2004, no drawings had been made under the letter of credit.

The letter of credit automatically extends every month so that termination will not occur until 13 months after notice is received from Wachovia Bank of North Carolina, N.A., that the letter of credit will not be extended. As of June 30, 2004, the earliest such termination date is July 5, 2005.

The University of North Carolina System Variable Rate Demand Pool Revenue Bonds, Series 1998A: In 1998, the Board of Governors of the University of North Carolina issued variable rate demand bonds in a system-wide financing arrangement for the benefit of its constituent universities. Through this system-wide financing, the University issued debt in the amount of $3,645,000.00 with a final maturity date of October 1, 2008. These bonds are subject to mandatory sinking fund redemption that began on October 1, 1999. The University's proceeds from this issuance were used to refinance notes payable for repairs to Dowdy-Ficklen Stadium, construction of the Blount Intramural Field, and construction of the Reade Street Parking Lot. While bearing interest at a weekly rate, these bonds are subject to purchase on demand with seven days' notice and delivery to the bond paying agent, The Bank of New York. Upon notice from the bond paying agent, the remarketing agent, Salomon Smith Barney, Inc. has agreed to exercise its best efforts to remarket the bonds for which a notice of purchase has been received.

Under a Standby Bond Purchase Agreement (Agreement) between the Board of Governors of the University of North Carolina and NationsBank, N.A. (now part of Bank of America, N.A.), a Liquidity Facility has been established for the Trustee (The Bank of New York) to draw amounts sufficient to pay the purchase price and accrued interest on bonds delivered for purchase when remarketing proceeds or other funds are not available. This Agreement requires a standby fee equal to .13% of the available commitment, payable semiannually in advance, beginning on November 3, 1998, and on each May 1 and November 1 thereafter until the expiration date or the termination date of the Agreement.

Under the Agreement, any bonds purchased through the Liquidity Facility become Liquidity Provider Bonds and shall, from the date of such purchase and while they are Liquidity Provider Bonds, bear interest at the Liquidity Provider Rate (LIBOR plus one percent (1%).) LIBOR is the average of rates per annum for deposits to major money center banks in the London interbank market. Upon remarketing of Liquidity Provider Bonds and the receipt of the sales price by the Liquidity Provider, such bonds are no longer considered Liquidity Provider Bonds. Payment of the interest on the Liquidity Provider Bonds is due the first business day of each month in which Liquidity Provider Bonds are outstanding. At June 30, 2004, there were no Liquidity Provider Bonds held by the Liquidity Facility.

Upon expiration or termination of the Agreement, the University is required to redeem (purchase) the Liquidity Provider Bonds held by the Liquidity Facility in sixty equal monthly installments, beginning the first business day that is at least 180 days following such expiration date or termination date along with accrued interest at the Liquidity Provider Rate.

Amounts due under this Standby Bond Purchase Agreement are allocated by the Trustee directly to and paid by the constituent universities participating in the system-wide bond issuance.

D. Annual Requirements - The annual requirements to pay principal and interest on the long-term obligations at June 30, 2004 are as follows:

	Bonds Payable		Notes Payable	
Fiscal Year	Principal	Interest	Principal	Interest
2005	$ 4,305,000.00	$ 2,831,022.50	$ 214,020.00	$ 13,532.40
2006	4,090,000.00	2,683,877.50	144,794.52	3,034.04
2007	4,195,000.00	2,526,436.25		
2008	4,315,000.00	2,368,900.00		
2009	4,545,000.00	2,201,455.00		
2010-2014	16,835,000.00	8,715,541.25		
2015-2019	18,395,000.00	4,734,852.50		
2020-2024	9,910,000.00	1,269,925.00		
Total Requirements	$ 66,590,000.00	$ 27,332,010.00	$ 358,814.52	$ 16,566.44

Interest on the variable rate revenue bonds is calculated at 1.09% at June 30, 2004.
Debt is remarketed, so interest rates fluctuate based on supply and demand.

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

Athletic Facilities Revenue System: In June 2003, the University defeased $4,490,000.00 of outstanding Athletic Facilities 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 Net Assets. At June 30, 2004, the outstanding balance of the defeased Athletic Facilities Revenue System Revenue Bonds was $0.

Housing and Dining Facilities System: In May 2001, the University defeased $11,655,000 of outstanding Housing and Dining 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 Net Assets. At June 30, 2004 the outstanding balance of the defeased Housing and Dining Revenue Bonds was $4,265,000.00.

F. Notes Payable - The University was indebted for notes payable for the purposes shown in the following table:

Purpose	Financial Institution	Interest Rate/ Ranges	Final Maturity Date	Original Amount of Issue	Principal Paid Through 6/30/2004	Principal Outstanding 6/30/2004
Computer Equipment for Dormitories	Carlyle Capital Markets	5.05	3/1/2006	$ 950,000.00	$ 606,396.06	$ 343,603.94
Athletic Vehicles	Wachovia	8.13	11/1/2005	35,344.47	20,133.89	15,210.58
Total Notes Payable				$ 985,344.47	$ 626,529.95	$ 358,814.52

The University plans to refinance the notes maturing on (date) with other long-term financing.

NOTE 8 - LEASE OBLIGATIONS

A. Capital Lease Obligations - Capital lease obligations relating to medical 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, 2004:

Fiscal Year	Amount
2005	$ 315,303.52
2006	315,303.52
2007	315,303.52
2008	315,303.52
2009	315,303.52
2010-2014	551,781.16
Total Minimum Lease Payments	2,128,298.76
Amount Representing Interest (2.97% Rate of Interest)	206,202.63
Present Value of Future Lease Payments	$ 1,922,096.13

Machinery and equipment acquired under capital lease amounted to $1,986,174.66 at June 30, 2004.

B. Operating Lease Obligations – The University entered into operating leases for equipment and buildings. Future minimum lease payments under noncancelable operating leases consist of the following at June 30, 2004:

Fiscal Year	Amount
2005	$ 1,746,606.24
2006	834,410.96
2007	402,839.95
2008	216,739.35
2009	190,715.24
2010-2014	147,357.00
Total Minimum Lease Payments	$ 3,538,668.74

Rental expense for all operating leases during the year was $2,038,550.89.

NOTE 9 - 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 Allowance for Uncollectibles	Less Indigent Care and Contractual Adjustments	Net Revenues	
Operating Revenues:							
Student Tuition and Fees	$ 96,750,561.06	$ 0.00	$ 16,521,932.29	$ 134,732.00	$ 0.00	$ 80,093,896.77	(B), (C)
Patient Services	$ 222,668,216.77	$ 0.00	$ 0.00	$ 24,459,856.33	$ 104,889,926.00	$ 93,318,434.44	
Sales and Services:							
Sales and Services of Auxiliary Enterprises:							
Residential Life	$ 15,421,884.86	$ 0.00	$ 0.00	$ 0.00	$ 0.00	$ 15,421,884.86	(A)
Dining	14,805,874.48	811,197.22				13,994,677.26	(A)
Student Union Services	86,283.96					86,283.96	
Health, Physical Education, and Recreation Services	1,617,895.95					1,617,895.95	
Bookstore	10,422,630.46					10,422,630.46	
Parking	1,829,239.42					1,829,239.42	(C)
Athletic	9,365,783.61					9,365,783.61	
Other	320,226.03					320,226.03	(C)
Sales and Services of Educational and Related Activities	3,681,184.64					3,681,184.64	
Total Sales and Services	$ 57,551,003.41	$ 811,197.22	$ 0.00	$ 0.00	$ 0.00	$ 56,739,806.19	

Revenue Bonds Secured by Pledged Revenues:
(A) Housing and Dining System
(B) Student Services Ststem
(C) University of North Carolina System

NOTE 10 - 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	$ 161,493,281.05	$ 8,372,601.90	$ 8,928,127.43	$ 213,865.00	$ 80,535.06	$ 0.00	$ 179,088,410.44
Research	7,289,208.19	2,052,402.39	2,554,016.51	3,882.00	2,675.80		11,902,184.89
Public Service	78,414,268.95	12,562,951.93	25,133,032.73	5,850.00	10,724.22		116,126,827.83
Academic Support	10,305,971.73	5,573,001.53	1,177,976.55		2,976.99		17,059,926.80
Student Services	3,859,295.31	367,256.25	1,514,655.18	153,000.00			5,894,206.74
Institutional Support	15,849,886.83	2,109,119.66	5,625,468.61		310.50		23,584,785.60
Operations and Maintenance of Plant	14,820,667.00	7,998,639.97	2,554,652.05		8,901,709.70		34,275,668.72
Student Financial Aid	166,410.58		361,347.06	6,790,816.63			7,318,574.27
Auxiliary Enterprises	18,650,214.58	12,182,932.07	25,370,096.28	3,841,181.88	4,083,135.56		64,127,560.37
Depreciation						14,133,601.70	14,133,601.70
Total Operating Expenses	$ 310,849,204.22	$ 51,218,905.70	$ 73,219,372.40	$ 11,008,595.51	$ 13,082,067.83	$ 14,133,601.70	$ 473,511,747.36

NOTE 11 - 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, 2004, these rates were set at .22% of covered payroll for employers and 6% of covered payroll for members.

For the year ended June 30, 2004, the University had a total payroll of $257,244,679.42, of which $115,401,540.16 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were $6,924,092.41 and $253,880.00, respectively. The University made one hundred percent of its annual required contributions for the years ended June 30, 2004, 2003, and 2002, which were $253,880.00, $0.00, and $2,082,381.26, 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 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, 2004, 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, 2004, the University had a total payroll of $257,244,679.42, of which $115,275,680.00 was covered under the Optional Retirement Program. Total employee and employer contributions for pension benefits for the year were $6,916,540.80 and $7,884,856.51, 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 University. The voluntary contributions by employees amounted to $1,051,942.58 for the year ended June 30, 2004.

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, 2004 were $91,668.88. The voluntary contributions by employees amounted to $1,229,186.38 for the year ended June 30, 2004.

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 $4,561,386.90 for the year ended June 30, 2004.

NOTE 12 - OTHER POSTEMPLOYMENT BENEFITS

A. Health Care for Long-Term Disability Beneficiaries and Retirees - The University participates in State-administered programs that 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 3.2% 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, 2004, the University's total contribution to the Plan was $7,381,671.04. The University assumes no liability for retiree health care benefits provided by the programs other than its required contribution. Additional detailed information about these programs can be located in the State of North Carolina's *Comprehensive Annual Financial Report.*

B. Long-Term Disability - The University participates in the Disability Income Plan of North Carolina (DIPNC). Established by Chapter 135, Article 6, of the General Statutes, DIPNC provides short-term and long-term disability benefits to eligible members of the Teachers' and State Employees' Retirement System 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. Employer contributions are established in the Appropriations Bill by the General Assembly. The University was not required to contribute to the DIPNC for the fiscal year ended June 30, 2004. 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 13 - 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. Except for a reduction in the public officers' and employees' liability insurance from $11,000,000 to $5,000,000, 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 $5,000,000 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 University also purchased through the Fund extended coverage on fifty-seven buildings, sprinkler leakage coverage on twelve buildings, vandalism on three buildings and "all risk" coverage on two buildings. Losses covered by the Fund are subject to a $500 per occurrence deductible. Extended coverage against losses caused by windstorm or hail, explosion, smoke, aircraft or vehicles, riot or civil commotion is provided on University buildings by the Fund and its reinsurer with a deductible of $500 per occurrence.

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 North Carolina 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. These coverages provide insurance for on-loan collections of art, medical malpractice (except for the Brody School of Medicine), liability coverage, accident coverage for students participating in University athletic events, and liability and physical damage insurance on University boats. Coverage is obtained through the North Carolina Department of Insurance and it's agent of record, The North Carolina Association of Insurance Agents.

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.

The University provides medical malpractice insurance for facility physicians. The medical malpractice is with a private insurance company with coverage of $3,000,000 per occurrence, $5,000,000 aggregate, and a $200,000 deductible; as well as an excess policy in the amount of $10,000,000. As part of the medical malpractice insurance agreement, the University was required to establish a $1,000,000 non-cancelable letter of credit. There have been no draws against this letter of credit to date.

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. There were no employer contributions required 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.

NOTE 14 - 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 $23,961,650.63 and on other purchases were $5,468,394.08 at June 30, 2004.

B. **Pending Litigation and Claims –** A $26.7 million lawsuit has been filed against the University resulting from a contractual dispute. Since no judgment has been rendered in this case, the amount of the liability, if any, cannot be reasonably estimated at this time. Management has indicated its intent to continue its vigorous defense of this claim.

The University is a party to other 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 of $93,918,580.00 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.

NOTE 15 - RELATED PARTIES

Foundations - There are two separately incorporated nonprofit foundations associated with the University. These foundations are the East Carolina University Educational Foundation, Inc., and the Medical Foundation of East Carolina University, Inc.

The East Carolina University Educational Foundation, Inc. provided $997,241.92 for the Dowdy-Ficklen Stadium Expansion Project, the Strength and Conditioning Center Project, and the Harrington Field Expansion and $3,129,785.63 to the Department of Athletics in primary support of student/athlete scholarships and other expenses. The other Foundation provided indirect support to the University by disbursing funds directly to recipients. The activities of the above Foundations are not included in the accompanying financial statements.

NOTE 16 - CHANGE IN FINANCIAL ACCOUNTING AND REPORTING

For the fiscal year ended June 30, 2004, the University implemented Governmental Accounting Standards Board Statement No. 39, *Determining Whether Certain Organizations are Component Units*. This Statement amends GASB Statement No. 14, *The Financial Reporting Entity*, to provide additional guidance to determine whether certain organizations for which the University is not financially accountable should be reported as component units based on the nature and significance of their relationship to the University.

NOTE 17 - SUBSEQUENT EVENTS

On August 5, 2004, the University issued $17,790,000 of Variable Rate General Revenue Bonds, Series 2004. The bond proceeds will be used to renovate three dorms, construct and equip a new baseball facility, refund in advance the 1996 Athletic Department Variable Rate Demand Revenue Bonds, Series 1996, and to refund in advance The University of North Carolina System Variable Rate Demand Pool Revenue Bonds, Series 1998A.

East Carolina University
Schedule of General Obligation Bond Project Authorizations, Budgets, and Expenditures
For Project-to-Date as of June 30, 2004

Schedule 1

Capital Improvement Projects	Original Projected Start Date	Revised/ Actual Start Date	General Obligation Bonds Authorized	Other Sources	Total Project Budget	Amount Expended	Percent Completed	Original Expected Completion Date	Revised/ Actual Completion Date
Projects Started									
Science Laboratories and Technology Building	Nov 2000	Nov 2000	$ 59,535,416.00	$ 0.00	$ 59,535,416.00	$ 57,197,934.09	96.07%	Jul 2003	Dec 2004
Flanagan Building - Renovation and Conversion	Feb 2001	Feb 2001	13,894,130.63		13,894,130.63	5,658,874.05	40.73%	Jan 2005	May 2005
Nursing, Allied Health, DEC	Nov 2000	Nov 2000	54,935,955.00	100,000.00	55,035,955.00	3,328,026.69	6.05%	Oct 2005	Jul 2006
Belk Building - Comprehensive Renovation	Aug 2002	Aug 2003	7,588,726.00		7,588,726.00		0.00%	May 2007	Jun 2007
Expansion & Renovation - Old Nursing Building	Aug 2002	Feb 2002	14,615,607.00		14,615,607.00	9,327,806.45	63.82%	Aug 2004	Apr 2005
Classroom Improvements - Technology Upgrades	Mar 2001	Apr 2001	3,305,384.00		3,305,384.00	2,394,632.64	72.45%	Mar 2006	Sep 2005
Academic Space Requirements	Jan 2002	Jun 2002	5,063,732.00	220,000.00	5,283,732.00	256,551.44	4.86%	Feb 2007	Feb 2007
Old Cafeteria Office Building	Aug 2002	May 2003	4,326,605.00		4,326,605.00	99,773.57	2.31%	Sep 2006	Nov 2006
Infrastructure - Repairs and Expansions	Nov 2000	Feb 2000	14,292,415.00	1,000,000.00	15,292,415.00	2,110,564.78	13.80%	Sep 2004	Jan 2007
Campus Computing Center	Nov 2000	Dec 2000	1,785,000.00	1,760,055.50	3,545,055.50	3,343,134.08	94.30%	Mar 2004	Oct 2004
Land Acquisition	Nov 2000	May 2001	7,668,848.52	8,276.38	7,677,124.90	7,677,124.90	100.00%	Nov 2005	Jan 2004
Technology Infrastructure Expansion	Dec 2001	Mar 2002	803,381.85		803,381.85	803,381.85	100.00%	Aug 2002	Sep 2003
Reserve for Effective Project Management	Jan 2002	Jan 2002	2,794,299.00		2,794,299.00	255,466.20	9.14%	Aug 2007	Aug 2007
Total All Projects			$ 190,609,500.00	$ 3,088,331.88	$ 193,697,831.88	$ 92,453,270.74			

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

East Carolina University
Intercollegiate Athletics Program
Statement of Revenues and Expenses
Year Ended June 30, 2004

Schedule 2

	Football	Men's Basketball	Women's Basketball	Other Sports	Nonprogram Specific	Total
Revenues:						
Operating Revenues:						
Student Fees, Net (Note 2)	$ 0.00	$ 0.00	$ 0.00	$ 0.00	$ 5,116,147.85	$ 5,116,147.85
Ticket Sales	3,616,205.00	606,122.00	9,878.00	342,489.00		4,574,694.00
Program Sales	18,028.00	1,495.00		2,566.00		22,089.00
Novelty Sales					140,139.96	140,139.96
Radio and TV Rights	363,267.15	90,816.79				454,083.94
Contest Guarantees	725,000.00	45,000.00				770,000.00
Advertising Income	353,886.05	97,700.26	16,250.00	33,750.00	1,750.00	503,336.31
Institutional Sports Camps and Clinics	101,684.61	58,048.10	15,093.49	124,140.50		298,966.70
Concessions	225,408.69	42,264.13		14,088.04		281,760.86
NCAA/Conference USA					1,856,816.12	1,856,816.12
Other Sources					609,006.64	609,006.64
Total Operating Revenues	5,403,479.50	941,446.28	41,221.49	517,033.54	7,723,860.57	14,627,041.38
Expenses						
Operating Expenses:						
Coaches' Salaries	1,035,800.94	459,485.09	242,784.60	815,846.41	982,929.64	3,536,846.68
Other Salaries	133,385.17	71,177.92	38,253.40	237,387.71	828,312.39	1,308,516.59
Fringe Benefits	226,089.41	80,241.24	57,590.72	201,318.89	344,707.64	909,947.90
Travel:						
Team	555,289.07	169,411.73	102,585.44	611,491.39	561,337.54	2,000,115.17
Recruiting	209,617.08	71,083.67	33,874.89	86,363.56		400,939.20
Financial Aid, Net	1,032,094.04	170,518.10	172,157.50	1,211,707.12	163,750.55	2,750,227.31
Supplies and Uniforms	333,250.11	80,447.84	37,096.16	417,609.06	425,172.21	1,293,575.38
Insurance	3,779.55	3,298.03	425.87	17,334.29	163,411.25	188,248.99
Telephone	17,622.28	6,824.11	4,216.80	15,475.59	52,588.58	96,727.36
Entertainment	6,839.61	2,949.75	660.00	8,359.85	67,282.17	86,091.38
Contest Guarantees	850,800.00	71,000.00	12,700.00			934,500.00
Radio and TV					238,870.67	238,870.67
Printing and Binding	27,523.81	4,440.79	3,723.37	9,310.14	191,087.37	236,085.48
Repairs and Maintenance	51,233.96	12,433.85	6,302.50	27,128.96	297,702.19	394,801.46
Advertising	769.36	500.00	332.25	825.00	88,727.89	91,154.50
Equipment Rentals	49,319.33	388.94	592.41	29,877.46	108,800.41	188,978.55
Ticket Price Adjustments	213,453.00	8,800.00	1,104.00	4,608.00		227,965.00
Other Fixed Charges	480.00	950.00	145.00	2,805.00	316,037.00	320,417.00
Other Contractual Services	199,917.87	64,393.60	14,414.18	247,941.97	380,062.07	906,729.69
Depreciation Expense					1,459,094.52	1,459,094.52
Miscellaneous	397,703.18	181,335.66	82,362.36	236,032.86	970,638.91	1,868,072.97
Total Operating Expenses	5,344,967.77	1,459,680.32	811,321.45	4,181,423.26	7,640,513.00	19,437,905.80
Operating Income (Loss)	58,511.73	(518,234.04)	(770,099.96)	(3,664,389.72)	83,347.57	(4,810,864.42)
Nonoperating Revenues						
State Appropriations					108,563.65	108,563.65
Gifts:						
Noncapital					3,325,805.63	3,325,805.63
Capital					1,449,891.12	1,449,891.12
Investment Income					23,779.15	23,779.15
Net Nonoperating Revenues	0.00	0.00	0.00	0.00	4,908,039.55	4,908,039.55
Excess (Deficiency) of Revenues over Expenses	$ 58,511.73	$ (518,234.04)	$ (770,099.96)	$ (3,664,389.72)	$ 4,991,387.12	$ 97,175.13

The accompanying notes are an integral part of this statement.

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

A. Organization and Purpose - East Carolina University is a constituent institution of The 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*. East Carolina University is classified as a Division I institution by the National Collegiate Athletic Association (NCAA).

B. Basis of Presentation - The preceding statement of revenues and expenses presents the University's intercollegiate athletic program's activity in accordance with the National Collegiate Athletic Association Financial Audit Guidelines. Those guidelines issued on May 2, 1996 require only a presentation of the current funds revenues and expenses by major program. This statement has been updated for Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – For Public Colleges and Universities* and Statement No. 38, *Certain Financial Statement Note Disclosures.* This presentation is not intended to provide a complete presentation of the program's financial position or its changes in net assets and cash flows.

C. Basis of Accounting - The preceding statement of revenues and expenses was 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.

D. Non-Monetary Transactions - The University reports goods and services received either by donation or in an exchange transaction at their fair value at the date of receipt.

During the year, uniforms were provided to the University at no charge. The uniforms were provided in exchange for the University's agreement not to use other manufacturers' clothing. This amount is recorded as advertising income in the preceding statement of revenues and expenses.

During the year, leased vehicles and coaching services were provided at no charge to the University. The values of these donations have been recorded as gifts in the preceding statement of revenues and expenses.

NOTE 2 - 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 and expenses. 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 non-operating revenues in the accompanying statement of revenues and expenses. To the extent that revenues from these programs are used to satisfy tuition, fees, and other charges, the University has recorded a scholarship discount. The amount of tuition discounting applicable to Athletics was $1,092,099.72.

NOTE 3 - EAST CAROLINA UNIVERSITY EDUCATIONAL FOUNDATION, INC.

The East Carolina University Educational Foundation, Inc. (Foundation) is a separate and legal entity established to promote and support the University's intercollegiate athletic program. During the fiscal year, the University received $2,879,840.00 in direct support from the Foundation, as well as $249,945.63 in indirect support through payments made on behalf of the University by the Foundation. The capital gifts on the Statement of Revenues and Expenses were provided by the Foundation and used to fund capital related expenses: $79,617.00 to fund the Dowdy-Ficklen Stadium Expansion Project, $127,131.82 to fund the Strength and Conditioning Center Project and $410,978.00 to fund the Harrington Field Expansion.

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

Board of Trustees
East Carolina University
Greenville, North Carolina

We have audited the financial statements of East Carolina University, a constituent institution of the sixteen-campus University of North Carolina System, which is a component unit of the State of North Carolina, and its discretely presented component unit, as of and for the year ended June 30, 2004, which collectively comprise the University's basic financial statements and have issued our report thereon dated October 31, 2004. We did not audit the financial statements of East Carolina University Foundation, Inc. and Consolidated Affiliate which represents 100% of the University's discretely presented component unit. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for the discretely presented component unit, is based on the report of the other auditors.

As discussed in Note 16 to the financial statements, the University implemented Governmental Accounting Standards Board Statement No. 39, *Determining Whether Certain Organizations Are Component Units,* during the year ended June 30, 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. The financial statements of the discretely presented component unit were not audited in accordance with *Government Auditing Standards,* and accordingly, this report does not extend to the discretely presented component unit.

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 an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that

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

might be material weaknesses. A material weakness is a reportable 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 caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

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 grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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.

Ralph Campbell, Jr.
State Auditor

October 31, 2004

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December 23, 2004

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