



# STATE OF NORTH CAROLINA

**FINANCIAL STATEMENT AUDIT REPORT OF**

**WINSTON-SALEM STATE UNIVERSITY**

**WINSTON-SALEM, NORTH CAROLINA**

**FOR THE YEAR ENDED JUNE 30, 2005**

**OFFICE OF THE STATE AUDITOR**

**LESLIE W. MERRITT, JR., CPA, CFP**

**STATE AUDITOR**

**FINANCIAL STATEMENT AUDIT REPORT OF**

**WINSTON-SALEM STATE UNIVERSITY**

**WINSTON-SALEM, NORTH CAROLINA**

**FOR THE YEAR ENDED JUNE 30, 2005**

**BOARD OF GOVERNORS**

**THE UNIVERSITY OF NORTH CAROLINA**

**MOLLY CORBETT BROAD, PRESIDENT**

**BOARD OF TRUSTEES**

**KEVIN A. MYATT, CHAIRMAN**

**TOMMY J. PAYNE, VICE CHAIRMAN**

**NIGEL D. ALSTON  
JOSEPH S. AMADO  
LORETTA C. BIGGS  
DR. CLIFFORD A. JONES, SR.**

**LUCILLE MAUGE  
MARGARET S. NEWMAN  
GLORIA ROSS REESE  
THOMAS E. TERRELL, JR.**

**ADMINISTRATIVE OFFICERS**

**DR. HAROLD L. MARTIN, SR., CHANCELLOR**

**PAULA M. JEFFRIES, VICE CHANCELLOR FOR FINANCE AND ADMINISTRATION**



STATE OF NORTH CAROLINA  
Office of the State Auditor

Leslie W. Merritt, Jr., CPA, CFP  
State Auditor

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

---

**AUDITOR'S TRANSMITTAL**

---

The Honorable Michael F. Easley, Governor  
The General Assembly of North Carolina  
Board of Trustees, Winston-Salem State University

We have completed a financial statement audit of Winston-Salem State University for the year ended June 30, 2005, and our audit results are included in this report. You will note from the independent auditor's report that we determined that the financial statements are presented fairly in all material respects.

Our consideration of internal control over financial reporting and compliance and other matters based on an audit of the financial statements resulted in no audit findings.

*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.

*Leslie W. Merritt, Jr.*

Leslie W. Merritt, Jr., CPA, CFP  
State Auditor

February 27, 2006

# TABLE OF CONTENTS

---

	PAGE
INDEPENDENT AUDITOR'S REPORT .....	1
MANAGEMENT'S DISCUSSION AND ANALYSIS .....	3
BASIC FINANCIAL STATEMENTS	
University Exhibits	
A-1 Statement of Net Assets .....	10
A-2 Statement of Revenues, Expenses, and Changes in Net Assets .....	12
A-3 Statement of Cash Flows .....	13
Component Unit Exhibits	
B-1 Consolidated Statement of Financial Position .....	15
B-2 Consolidated Statement of Activities .....	16
Notes to the Financial Statements .....	17
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 <i>GOVERNMENT AUDITING STANDARDS</i> .....	41
DISTRIBUTION OF AUDIT REPORT .....	43



STATE OF NORTH CAROLINA  
Office of the State Auditor

Leslie W. Merritt, Jr., CPA, CFP  
State Auditor

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

---

**INDEPENDENT AUDITOR'S REPORT**

---

Board of Trustees  
Winston-Salem State University  
Winston-Salem, North Carolina

We have audited the accompanying financial statements of Winston-Salem State University, a constituent institution of the 16-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, 2005, which collectively comprise the University's basic financial statements as listed in the table of contents. These financial statements are the responsibility of Winston-Salem State 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 Winston-Salem State University Foundation, Inc., and Subsidiary, which represent 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.

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 Winston-Salem State University Foundation, Inc., and Subsidiary 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 the 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 Winston-Salem State University and its discretely presented component unit as of June 30, 2005, 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 15 to the financial statements, the University implemented Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures*, during the year ended June 30, 2005.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 29, 2005, 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, 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.



Leslie W. Merritt, Jr., CPA, CFP  
State Auditor

December 29, 2005

## WINSTON-SALEM STATE UNIVERSITY MANAGEMENT'S DISCUSSION AND ANALYSIS

---

This section of the Winston-Salem State University (the "University") annual financial report presents our discussion and analysis of the financial performance of the University during the fiscal year ended June 30, 2005. This discussion has been prepared by University management along with the financial statements and notes to the financial statements and should be read in conjunction with, and is qualified in its entirety by, the financial statements and notes. The Management's Discussion and Analysis has comparative data for the applicable years (past and current) with emphasis on the current year. The financial statements, notes, and this discussion are the responsibility of University management.

### **Using the Annual Report**

This annual report consists of a series of financial statements, prepared in accordance with the Governmental Accounting Standards Board (GASB) Statement No. 35, *Basic Financial Statements - and Management's Discussion and Analysis - for Public Colleges and Universities*, and GASB Statement No. 38, *Certain Financial Statement Note Disclosures*. These GASB statements establish standards for external financial reporting for public colleges and universities and require that financial statements be presented on a consolidated basis for the University as a whole, with resources classified for accounting and reporting purposes into four net asset categories. Prior to 2002, financial reporting requirements focused on the accountability of individual funds groups rather than on the University as a whole. One of the most important questions asked is whether the University as a whole is better or worse off as a result of the year's activities. The key to understanding this question is the Statement of Net Assets and the Statement of Revenues, Expenses, and Changes in Net Assets. These statements present financial information in a form similar to that used by corporations. It is prepared under the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service, regardless of when cash is exchanged.

The Statement of Net Assets includes all assets and liabilities. The University's net assets (the difference between assets and liabilities) are an indicator of the University's financial health. Over time, increases or decreases in net assets is one indicator of the improvement or erosion of the University's financial health when considered with nonfinancial facts such as enrollment levels and the condition of the facilities.

The Statement of Revenues, Expenses, and Changes in Net Assets presents the revenues earned and expenses incurred during the year. Activities are reported as either operating or nonoperating. All things being equal, a public University's dependency on State appropriations and gifts will result in operating deficits, because GASB Statement No. 35 classifies State appropriations and gifts as nonoperating revenues. Prior to 2002, these two revenue classifications were included within the scope of normal revenues and contributed to revenues over expenditures, typically a net positive number.

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

---

### **Reporting Entity**

The financial statements report information about the University as a whole using accounting methods similar to those used by private-sector companies. The University's supporting organization, the Winston-Salem State University Foundation, Inc. (the "Foundation"), is an independent nonprofit corporation formed for the exclusive benefit of the University. According to Governmental Accounting Standards Board Statement No. 39, *Determining Whether Certain Organizations are Component Units*, the Winston-Salem State University Foundation, Inc., meets the requirements to be reported discretely in these financial statements.

### **Financial Highlights**

The University's financial position, as a whole, remained relatively stable during the fiscal year ended June 30, 2005. Its combined net assets increased \$19,185,748.11 from the previous year, which is an increase of approximately 22.9 percent.

### **Condensed Financial Information**

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

The Statement of Net Assets presents the assets (current and noncurrent), liabilities (current and noncurrent), and the net assets (total assets less total liabilities) of the University. This financial statement provides a comparative University fiscal snapshot as of June 30, 2005, and June 30, 2004. This provides the readers of this statement with information on assets available to continue operations.

## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

### Condensed Statement of Net Assets June 30, 2005

	2005		2004	
<b>Assets</b>				
Current Assets	\$ 14,986,467.67	10.5%	\$ 10,748,641.47	10.2%
Other Noncurrent Assets:				
Capital	106,262,634.94	74.8%	77,208,428.58	73.1%
Other	20,894,394.92	14.7%	17,608,783.38	16.7%
Total Assets	142,143,497.53	100.0%	105,565,853.43	100.0%
<b>Liabilities</b>				
Current Liabilities	5,635,213.59	14.4%	5,368,825.66	24.8%
Noncurrent Liabilities	33,391,216.70	85.6%	16,265,708.64	75.2%
Total Liabilities	39,026,430.29	100.0%	21,634,534.30	100.0%
<b>Net Assets*</b>				
Invested in Capital Assets, Net of Related Debt	75,564,765.51	73.3%	63,826,415.20	76.0%
Restricted:				
Nonexpendable	10,375,198.80	10.1%	10,289,743.79	12.3%
Expendable	12,767,761.96	12.3%	8,109,385.54	9.7%
Unrestricted	4,409,340.97	4.3%	1,705,774.60	2.0%
Total Net Assets	\$ 103,117,067.24	100.0%	\$ 83,931,319.13	100.0%

\*Net Asset categories are defined in Note 1L of the Notes to the Financial Statements.

As of June 30, 2005, total University assets were \$142,143,497.53. The University's largest asset is investment in capital assets of \$106,262,634.94. Cash and investments increased \$6,128,172.54 primarily due to increased revenues of \$3,074,629.93 from providing student services to a growing student enrollment. Capital grants and appropriations designated for capital projects increased \$2,442,879.51, and net realized and unrealized gains on endowments increased \$610,663.10.

The \$14,986,467.67 in current assets covered the current liabilities of \$5,635,213.59, as the current ratio was \$2.66 in current assets to every \$1 in current liabilities.

University liabilities totaled \$39,026,430.29. Bonds payable of \$12,667,869.43 and a capital lease of \$18,030,000.00 were the largest liabilities, representing 78.65 percent of the total. The University had outstanding bonds of \$6,965,000.00, \$2,797,869.43, and \$2,905,000.00 from 1998, 2002, and 2004 bond issues, respectively.

### Statement of Revenues, Expenses, and Changes in Net Assets

The Statement of Revenues, Expenses, and Changes in Net Assets presents the activity that shows the changes in net assets. The activity is represented by the revenues received by the University, both operating and nonoperating, and the expenses paid by the University,

## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

operating and nonoperating, as well as any other revenues, expenses, gains and losses received or expended by the University.

Operating revenues are received for providing goods and services to the various customers of the University. Operating expenses are used to acquire goods and services provided in return for the operating revenues, and to carry out the mission of the University. Nonoperating revenues are received for which goods and services are not provided, i.e., State appropriations and investment income. Nonoperating expenses are expenses not involved in the normal operation of the University that can include interest expense, extraordinary items, and accounting changes and corrections.

### Condensed Statement of Revenues, Expenses, and Changes in Net Assets For the Year Ended June 30, 2005

	2005		2004	
<b>Operating Revenues:</b>				
Student Tuition and Fees, Net	\$ 11,817,062.72	38.8%	\$ 8,885,376.57	36.9%
Grants and Contracts	9,047,148.08	29.7%	7,561,140.78	31.4%
Sales and Services, Net	8,869,633.89	29.1%	6,818,268.46	28.4%
Other	727,624.97	2.4%	798,452.51	3.3%
Total Operating Revenues	30,461,469.66	100.0%	24,063,238.32	100.0%
<b>Operating Expenses:</b>				
Salaries and Benefits	48,323,011.58	57.5%	41,964,317.50	56.1%
Supplies, Materials, and Services	25,071,228.49	29.8%	23,574,697.98	31.5%
Scholarships and Fellowships	5,422,158.64	6.5%	4,992,925.24	6.7%
Utilities	2,144,382.11	2.5%	1,870,980.67	2.5%
Depreciation	3,078,380.61	3.7%	2,414,971.06	3.2%
Total Operating Expenses	84,039,161.43	100.0%	74,817,892.45	100.0%
Operating Loss	(53,577,691.77)		(50,754,654.13)	
<b>Nonoperating Revenues:</b>				
State Appropriations	43,264,836.91	59.5%	35,570,851.56	63.9%
Capital Grants	15,105,846.00	20.8%	7,546,582.00	13.6%
Capital Appropriations	2,643,100.00	3.6%	108,400.00	0.2%
Noncapital Grants	11,069,592.84	15.2%	11,078,044.93	19.9%
Noncapital Gifts	152,261.54	0.2%	223,164.58	0.4%
Additions to Permanent Endowments	82,406.30	0.1%	28,025.50	0.1%
Other	445,396.29	0.6%	1,054,830.08	1.9%
Net Nonoperating Revenues	72,763,439.88	100.0%	55,609,898.65	100.0%
Increase in Net Assets	19,185,748.11		4,855,244.52	
<b>Net Assets:</b>				
Beginning of Year	83,931,319.13		79,076,074.61	
End of Year	\$ 103,117,067.24		\$ 83,931,319.13	

## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Total operating loss for fiscal year 2005 was \$53,577,691.77. Since the State of North Carolina appropriation is not included within operating revenue per GASB Statement No. 35, the University will show a significant operating loss on a continuing basis.

The sources of operating revenue for the University are tuition and fees, grants and contracts, auxiliary services, and other educational activities.

The University strives to provide students with the opportunity to obtain a quality education. Future University enrollments may be affected by a number of factors, including any material increase in tuition and other mandatory charges, stemming from any material decrease in appropriation funding from the State of North Carolina.

The following table details the University's noncapital grants and contracts revenue for the fiscal year ended June 30, 2005.

	<u>Amount</u>
Federal:	
Department of Education	\$ 14,208,989.56
Department of Health and Human Services	2,699,967.18
National Science Foundation	318,582.37
Department of Housing and Urban Development	305,116.34
Department of Justice	215,869.36
National Aeronautics Space Administration	132,673.54
Department of Agriculture	34,344.78
National Security Agency	<u>31,370.47</u>
Total Federal	17,946,913.60
Private, State, and Local	<u>2,169,827.32</u>
Total All Sources	<u><u>\$ 20,116,740.92</u></u>

Operating expenses, including depreciation of \$3,078,380.61, totaled \$84,039,161.43. Of this total, \$41,781,571.69 or 49.7 percent was used for instruction and student support.

The University's largest source of nonoperating revenue is the State of North Carolina appropriation. This is received in monthly payments, beginning in July of each year, since the State's fiscal year begins on July 1. There is no direct connection between the amount of tuition revenues collected by the University and the amount of State funds appropriated in any given year. For the fiscal year ended June 30, 2005, the State of North Carolina appropriated to the University \$43,264,836.91 for operations. The State of North Carolina provided \$17,748,946.00 in capital grants and capital appropriations during the fiscal year.

Total net revenues were \$103,224,909.54 for fiscal year 2005, compared to \$79,673,136.97 for fiscal year 2004, resulting in a net increase of \$23,551,772.57, which is primarily contributed to the following:

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

---

- Student tuition and fees reflect a \$2,931,686.15 increase due to increases in student enrollment and in tuition and fee rates.
- State appropriations reflect a \$7,693,985.35 increase due to increased funding from the State of North Carolina.
- Capital grants reflect a \$7,559,264.00 increase due to a \$7,001,974.00 increase in construction projects funded under the University Improvement General Obligation Bonds, in addition to \$557,290.00 of capital project funding received from The University of North Carolina General Administration.
- Capital appropriations reflect a \$2,534,700.00 increase due to increased funding in repair and renovation projects as funded by the State of North Carolina.

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

### **Capital Assets**

With the passage of the University Improvement General Obligation Bonds in 2000, the University was authorized to receive \$46,786,581.00 over the next six years for capital improvements. Major capital expenditures for the year ended June 30, 2005, include the Physical and Life Science Building, \$5,569,402.00, Anderson Center Renovations, \$2,991,347.00, and the Carolina Hall Renovation, \$2,939,376.00. The bond referendum is discussed in detail in Note 14(D) to the financial statements.

During the year the University entered into a capital lease with the Winston-State University Housing Foundation, LLC, for the Rams Commons Housing Facility. The capital asset and the capital lease liability recorded was \$18,180,000.00.

### **Factors Impacting Future Periods**

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. This flexibility, along with the University's ongoing efforts toward revenue diversification and cost containment, will enable the University to provide the necessary resources to support this level of excellence.

A crucial element to the University's future will continue to be our relationship with the State of North Carolina, as we work to manage tuition to make it competitive while providing an outstanding college education for our students. There is a direct relationship between the growth of State support and the University's ability to control tuition growth, as declines in State appropriations generally result in increased tuition levels.

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

---

The University continues to execute its long-range plan to modernize and expand its complement of facilities with a balance of new construction. This strategy addresses the University's growth and the continuing effects of technology on teaching 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.

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.

**Winston-Salem State University**  
**Statement of Net Assets**  
**June 30, 2005**

**Exhibit A-1**

**ASSETS**

Current Assets:

Cash and Cash Equivalents	\$ 8,355,492.03
Restricted Cash and Cash Equivalents	5,073,954.53
Receivables, Net (Note 4)	1,264,558.00
Inventories	106,694.51
Notes Receivable, Net (Note 4)	185,768.60
	<hr/>
Total Current Assets	14,986,467.67

Noncurrent Assets:

Restricted Cash and Cash Equivalents	2,019,852.25
Restricted Due from Primary Government	3,322,472.90
Endowment Investments	13,672,125.03
Other Long-Term Investments	1,084,854.35
Notes Receivable, Net (Note 4)	795,090.39
Capital Assets - Nondepreciable (Note 5)	14,572,026.75
Capital Assets - Depreciable, Net (Note 5)	91,690,608.19
	<hr/>
Total Noncurrent Assets	127,157,029.86
	<hr/>
Total Assets	142,143,497.53

**LIABILITIES**

Current Liabilities:

Accounts Payable and Accrued Liabilities (Note 6)	3,305,054.41
Due to Primary Government	84,837.10
Deferred Revenue	596,867.62
Interest Payable	229,288.13
Long-Term Liabilities - Current Portion (Note 7)	1,419,166.33
	<hr/>
Total Current Liabilities	5,635,213.59

Noncurrent Liabilities:

Deposits Payable	195,833.13
Funds Held for Others	300,910.25
U. S. Government Grants Refundable	932,130.22
Long-Term Liabilities (Note 7)	31,962,343.10
	<hr/>
Total Noncurrent Liabilities	33,391,216.70
	<hr/>
Total Liabilities	39,026,430.29

**Winston-Salem State University**  
**Statement of Net Assets**  
**June 30, 2005**

**Exhibit A-1**  
**Page 2**

**NET ASSETS**

Invested in Capital Assets, Net of Related Debt	75,564,765.51
Restricted for:	
Nonexpendable:	
Scholarships and Fellowships	3,125,074.11
Endowed Professorships	4,680,500.00
Departmental Uses	2,468,532.19
Loans	101,092.50
Expendable:	
Scholarships and Fellowships	1,146,449.74
Endowed Professorships	2,342,530.34
Departmental Uses	3,359,958.83
Loans	181,625.31
Capital Projects	4,881,631.52
Debt Service	855,566.22
Unrestricted	4,409,340.97
Total Net Assets	<u>\$ 103,117,067.24</u>

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

**Winston-Salem State University**  
**Statement of Revenues, Expenses, and**  
**Changes in Net Assets**  
**For the Fiscal Year Ended June 30, 2005**

**Exhibit A-2**

**REVENUES**

Operating Revenues:	
Student Tuition and Fees, Net (Note 9)	\$ 11,817,062.72
Federal Grants and Contracts	9,047,148.08
Sales and Services, Net (Note 9)	8,869,633.89
Interest Earnings on Loans	4,188.12
Other Operating Revenues	723,436.85
	<hr/>
Total Operating Revenues	30,461,469.66
	<hr/>

**EXPENSES**

Operating Expenses:	
Salaries and Benefits	48,323,011.58
Supplies and Materials	7,724,776.72
Services	17,346,451.77
Scholarships and Fellowships	5,422,158.64
Utilities	2,144,382.11
Depreciation	3,078,380.61
	<hr/>
Total Operating Expenses	84,039,161.43
	<hr/>
Operating Loss	(53,577,691.77)
	<hr/>

**NONOPERATING REVENUES (EXPENSES)**

State Appropriations	43,264,836.91
Noncapital Grants	11,069,592.84
Noncapital Gifts	152,261.54
Investment Income (Net of Investment Expense of \$48,544.20)	1,573,604.15
Interest and Fees on Capital Asset-Related Debt	(1,128,207.86)
	<hr/>
Net Nonoperating Revenues	54,932,087.58
	<hr/>
Income Before Other Revenues	1,354,395.81
	<hr/>
Capital Appropriations	2,643,100.00
Capital Grants	15,105,846.00
Additions to Endowments	82,406.30
	<hr/>
Increase in Net Assets	19,185,748.11
	<hr/>

**NET ASSETS**

Net Assets - July 1, 2004	<hr/> 83,931,319.13
Net Assets - June 30, 2005	<hr/> <hr/> \$ 103,117,067.24

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

**Winston-Salem State University**  
**Statement of Cash Flows**  
**For the Fiscal Year Ended June 30, 2005**

**Exhibit A-3**

**CASH FLOWS FROM OPERATING ACTIVITIES**

Received from Customers	\$ 30,408,290.62
Payments to Employees and Fringe Benefits	(47,919,440.35)
Payments to Vendors and Suppliers	(27,197,608.58)
Payments for Scholarships and Fellowships	(5,422,158.64)
Loans Issued	(182,538.00)
Collection of Loans	201,278.81
Interest Earned on Loans	1,319.45
Student Deposits Received	195,833.13
Student Deposits Returned	(106,376.97)
	<hr/>
Net Cash Used by Operating Activities	(50,021,400.53)

**CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES**

State Appropriations	43,264,836.91
Noncapital Grants	11,110,326.76
Noncapital Gifts	152,261.54
Additions to Permanent and Term Endowments	82,406.30
Other Receipts	62,915.27
	<hr/>
Cash Provided by Noncapital Financing Activities	54,672,746.78

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

State Capital Appropriations	2,643,100.00
Capital Grants	13,587,051.09
Acquisition and Construction of Capital Assets	(14,323,272.95)
Principal Paid on Capital Debt and Leases	(855,000.00)
Interest and Fees Paid on Capital Debt and Leases	(1,143,839.68)
Payment to Bond Escrow Agent	(4,816.32)
	<hr/>
Net Cash Used by Capital Financing and Related Financing Activities	(96,777.86)

**CASH FLOWS FROM INVESTING ACTIVITIES**

Proceeds from Sales and Maturities of Investments	4,807,301.98
Investment Income	717,360.91
Purchase of Investments and Related Fees	(3,997,375.83)
	<hr/>
Net Cash Provided by Investing Activities	1,527,287.06

Net Increase in Cash and Cash Equivalents	6,081,855.45
Cash and Cash Equivalents - July 1, 2004	9,367,443.36
	<hr/>
Cash and Cash Equivalents - June 30, 2005	\$ 15,449,298.81

**Winston-Salem State University**  
**Statement of Cash Flows**  
**For the Fiscal Year Ended June 30, 2005**

**Exhibit A-3**  
**Page 2**

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

Operating Loss	\$ (53,577,691.77)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:	
Depreciation Expense	3,078,380.61
Allowances, Write-Offs, and Amortizations	2,364.48
Changes in Assets and Liabilities:	
Receivables (Net)	(70,465.42)
Inventories	(27,030.04)
Accounts Payable and Accrued Liabilities	223,340.20
Due to Primary Government	59,930.05
Deferred Revenue	18,605.83
Compensated Absences	162,968.56
Deposits Payable	89,456.16
Student Loans Issued	(182,538.00)
Student Loan Principal Repayments	201,278.81
	<hr/>
Net Cash Used by Operating Activities	<u>\$ (50,021,400.53)</u>

**RECONCILIATION OF CASH AND CASH EQUIVALENTS**

Current Assets:	
Cash and Cash Equivalents	\$ 8,355,492.03
Restricted Cash and Cash Equivalents	5,073,954.53
Noncurrent Assets:	
Restricted Cash and Cash Equivalents	<u>2,019,852.25</u>
Total Cash and Cash Equivalents - June 30, 2005	<u>\$ 15,449,298.81</u>

**NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES**

Assets Acquired through the Assumption of a Liability	\$ 18,180,000.00
Change in Fair Value of Investments	498,343.63
Loss on Disposal of Capital Assets	2,364.48

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

***Winston-Salem State University Foundation, Inc., and Subsidiary***  
***Consolidated Statement of Financial Position***  
***June 30, 2005***

***Exhibit B-1***

**ASSETS**

Cash and Cash Equivalents	\$ 4,468,181
Restricted Cash	9,003,559
Accounts Receivable	85,768
Lease Obligation Receivable, Net of Unearned Interest Income of \$3,911,975	14,118,025
Pledges Receivable	3,372,049
Investment Securities	3,033,997
Property and Equipment, Net	1,848,545
Construction in Progress	11,097,154
Deferred Financing Costs, Net	1,401,167
Other	<u>2,128</u>
 Total Assets	 <u>48,430,573</u>

**LIABILITIES**

Due to Board of Trustees of the Endowment	1,040,166
Accounts Payable and Other Accruals	2,296,484
Due to WSSU	40,453
Bonds Payable	<u>35,750,000</u>
 Total Liabilities	 <u>39,127,103</u>

**NET ASSETS**

Unrestricted	1,698,575
Temporarily Restricted	4,857,951
Permanently Restricted	<u>2,746,944</u>
 Total Net Assets	 <u>\$ 9,303,470</u>

See Note 1 in the Notes to the Financial Statements

**Winston-Salem State University Foundation, Inc., and Subsidiary**  
**Consolidated Statement of Activities**  
**For the Year Ended June 30, 2005**

**Exhibit B-2**

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>SUPPORT AND REVENUE</b>				
Rental Income	\$ 1,222,444	\$ 0	\$ 0	\$ 1,222,444
Gifts and Grants	407,462	2,921,650	337,457	3,666,569
Investment Income	234,687	21,539		256,226
Administrative Fees	109,272			109,272
Unrealized Gain on Investment Activities		436,059		436,059
Passport Income	116,746			116,746
	<u>2,090,611</u>	<u>3,379,248</u>	<u>337,457</u>	<u>5,807,316</u>
Net Assets Released from Restrictions	870,876	(870,876)		
Total Support and Revenue	<u>2,961,487</u>	<u>2,508,372</u>	<u>337,457</u>	<u>5,807,316</u>
<b>EXPENSES</b>				
Rental Operating Costs	286,710			286,710
Depreciation and Amortization	536,451			536,451
Interest	1,131,548			1,131,548
Scholarships	471,480			471,480
Special Programs	399,396			399,396
Management and General	395,595			395,595
Unrelated Business Income Tax	20,514			20,514
Fundraising Expense	195,459			195,459
Total Expenses	<u>3,437,153</u>			<u>3,437,153</u>
Change in Net Assets	(475,666)	2,508,372	337,457	2,370,163
<b>NET ASSETS</b>				
Net Assets, Beginning	<u>2,174,241</u>	<u>2,349,579</u>	<u>2,409,487</u>	<u>6,933,307</u>
Net Assets, Ending	<u>\$ 1,698,575</u>	<u>\$ 4,857,951</u>	<u>\$ 2,746,944</u>	<u>\$ 9,303,470</u>

See Note 1 in the Notes to the Financial Statements

**WINSTON-SALEM STATE UNIVERSITY**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2005**

---

**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. Winston-Salem State University is a constituent institution of the 16-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 unit. 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 unit is discretely presented in the University's financial statements. The 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.

**Discretely Presented Component Unit** - Winston-Salem State 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 Winston-Salem State University Housing Foundation, LLC, is the wholly owned subsidiary of the Winston-Salem State University Foundation, Inc.

The Winston-Salem State 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 is governed by a 25-member board consisting of five ex-officio directors and 20 elected directors. Although the University does not control the timing or amount of receipts from the Foundation, the

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

---

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 Winston-Salem State 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, 2005, the Foundation distributed \$654,750.38 to the University for both restricted and unrestricted purposes. Complete financial statements for the Foundation can be obtained from the Winston-Salem State University Foundation, Inc., S.G. Atkins House, Winston-Salem, NC 27110, or by calling (336) 750-3005.

- 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 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.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

---

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

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 cash on deposit with fiscal agents and deposits held by the State Treasurer in the short-term investment fund. The short-term investment fund maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit and withdraw cash at any time without prior notice or penalty.

- E. Investments** - This classification includes mutual funds and money market funds. Except for money market funds, investments are accounted for at fair value, as determined by quoted market prices, or an amount determined by management if quoted market prices are not available. The net increase in the fair value of investments is recognized as a component of investment income.

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

- F. Receivables** - Receivables consist of tuition and fees charged to students and charges for auxiliary enterprises' sales and services. Receivables also include amounts due from federal and State governments, and private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants. Receivables are recorded net of estimated uncollectible amounts.

- G. Inventories** - Inventories, consisting of fuel oil held for consumption, are valued at cost using the last invoice cost. Inventories of postage are valued at the retail cost.

- 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.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

---

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 10 to 40 years for general infrastructure, 20 to 50 years for buildings, and 5 to 20 years for equipment.

The Diggs Gallery collection is capitalized at cost or fair value at the date of donation. This collection is considered inexhaustible and is therefore not depreciated.

- I. Restricted Assets** - Unexpended proceeds of revenue bonds and unexpended capital contributions are classified as restricted assets because their use is limited by applicable bond covenants or donor/grantor agreements. Certain other assets are classified as restricted because their use is limited by external parties or statute.
- J. Noncurrent Long-Term Liabilities** - Noncurrent long-term liabilities include principal amounts of bonds payable, capital lease obligations, and compensated absences that will not be paid within the next fiscal year.

Bonds payable are reported net of unamortized premiums. The University amortizes bond premiums over the life of the bonds using the straight-line method. Issuance costs are expensed.

- K. Compensated Absences** - The University's policy is to record the cost of vacation leave when earned. The policy provides for a maximum accumulation of unused vacation leave of 30 days which can be carried forward each January 1 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 30 equals the leave carried forward at the previous December 31 plus the leave earned, less the leave taken between January 1 and June 30.

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.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

---

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

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

---

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 copy centers, motor pool, postal services, telecommunications, and facilities rental. 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.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

---

### NOTE 2 - DEPOSITS AND INVESTMENTS

- A. Deposits** - Unless specifically exempt, the University is required by *North Carolina 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 G.S. 116-36.1, requires the University to deposit its institutional trust funds with the State Treasurer. Although specifically exempted, the University may voluntarily deposit endowment funds, special funds, revenue bond proceeds, and debt service funds with the State Treasurer. Special funds consist of moneys for intercollegiate athletics and agency funds held directly by the University.

At June 30, 2005, the University's deposit with the State Treasurer's Short-Term Investment Fund totaled \$15,324,552.48. Deposit and investment risks associated with the State Treasurer's Investment Pool (which includes the State Treasurer's Short-Term Investment Fund) 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.ncosc.net/> and clicking on "Financial Reports", or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

The carrying amount of the University's deposits not with the State Treasurer, as well as the bank balance, was \$124,746.33. Custodial credit risk is the risk that in the event of a bank failure, the University's deposits may not be returned to it. The University does not have a deposit policy for custodial credit risk. As of June 30, 2005, the University's bank balance was exposed to custodial credit risk as follows:

Uninsured and Uncollateralized	<u><u>\$ 24,746.33</u></u>
--------------------------------	----------------------------

- B. Investments** - The University is authorized by The University of North Carolina Board of Governors pursuant to G.S. 116-36.2 and Section 600.2.4 of the Policy Manual of the University of North Carolina, to invest its special funds in the same manner as the State Treasurer is required to invest, as discussed below.

G.S. 147-69.1(c), applicable to the State's General Fund, and G.S. 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

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

---

specified institutions; prime quality commercial paper, and asset-backed securities with specified ratings. Also, G.S. 147-69.1(c) authorizes the following: specified bills of exchange or time drafts and corporate bonds and notes with specified ratings. G.S. 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.

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.

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

Investments of the University's component unit, the Foundation, is subject to and restricted by G.S. 36B "Uniform Management of Institutional Funds Act" (UMIFA) and any requirements placed on them by contract or donor agreements.

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

**Long-Term Investment Pool** - This is an internal investment pool that is utilized for the investment of the endowment funds. Endowment funds of the University and its' discretely presented component unit represent the pool's internal participants. Fund ownership and allocation of investment income are based on the equity interest that each fund holds in the internal investment pool. The investment strategy, including the selection of investment managers, is based on the directives of the University's Endowment Board.

The following table presents the fair value of investments by type and investments subject to interest rate risk at June 30, 2005, for the Long-Term Investment Pool. Interest rate risk is defined by GASB Statement No. 40 as the risk a government may face should interest rate

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

variances affect the fair value of investments. Per the University's Endowment Board Statement of Investment Policy and Objectives, the average maturity of the fixed income portion shall range within 25 percent of the fixed income benchmark, the Lehman Aggregate.

### *Long-Term Investment Pool*

Investment Type	Fair Value	Investment Maturities (in Years)		
		Less Than 1	1 to 5	6 to 10
Debt Securities				
Money Market Funds	\$ 52,070.81	\$ 52,070.81	\$ 0.00	\$ 0.00
Mutual Bond Funds	4,838,830.64	<u>                    </u>	<u>634,619.41</u>	<u>4,204,211.23</u>
		<u>\$ 52,070.81</u>	<u>\$ 634,619.41</u>	<u>\$ 4,204,211.23</u>
Other Securities				
Other Mutual Funds	<u>8,781,223.58</u>			
Total Long-Term Investment Pool	<u>\$ 13,672,125.03</u>			

*Credit Risk:* Per the University's Endowment Board Statement of Investment Policy and Objectives, the investment quality of bonds is to be investment grade with ratings at least "Baa" by a recognized rating service, such as Moody's or equivalent. As of June 30, 2005, the investments in the Long-Term Investment Pool were rated as follows:

	Fair Value	AAA Aaa	AA Aa
Money Market Funds	\$ 52,070.81	\$ 52,070.81	\$ 0.00
Mutual Bond Funds	<u>4,838,830.64</u>	<u>634,619.41</u>	<u>4,204,211.23</u>
Total	<u>\$ 4,890,901.45</u>	<u>\$ 686,690.22</u>	<u>\$ 4,204,211.23</u>

Rating Agency: Standard and Poors

*Custodial Credit Risk:* For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the University will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The University Endowment Board does not have a formal policy for custodial credit risk. The University's investments in the Long-Term Investment Pool were not exposed to custodial credit risk.

*Concentration of Credit Risk:* The University Endowment Board places no limit on the amount the Board may invest in any one issuer. At

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

June 30, 2005, no more than 5% of the long-term investment pool investments are invested in any single issuer.

*Foreign Currency Risk:* Foreign currency risk is defined by GASB Statement No. 40 as the risk that changes in exchange rates will adversely affect the fair value of an investment. The University Endowment Board does not have a formal policy for foreign currency risk. The Long-Term Investment Pool's exposure to foreign currency risk is as follows:

The Long-Term Investment Pool's current position is 10.5%.

Investment	Fair Value (U.S. Dollars)
Delaware Pooled Trust International Equity Portfolio	\$ 739,257.18
Evergreen International Equity Fund Class I	716,050.88
Total	\$ 1,455,308.06

**Non-Pooled Investments** - The following table presents the fair value of investments by type and investments subject to interest rate risk at June 30, 2005, for the University's non-pooled investments. Interest rate risk is defined by GASB Statement No. 40 as the risk a government may face should interest rate variances affect the fair value of investments. The University does not have a formal investment policy that addresses interest rate risk.

### *Non-Pooled Investments*

Investment Type	Fair Value	Investment Maturities (in Years) <u>Less</u> <u>Than 1</u>
Debt Securities		
Money Market Funds	\$ 1,084,854.35	\$ 1,084,854.35

*Credit Risk:* The University does not have a formal policy that addresses credit risk. As of June 30, 2005, the Money Market Funds, with fair value of \$1,084,854.35, were rated AAA by Standard and Poors.

*Custodial Credit Risk:* For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the University will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The University does not have a

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

---

formal policy for custodial credit risk. The University's non-pooled investments were not exposed to custodial credit risk.

*Concentration of Credit Risk:* The University does not have a formal policy that addresses concentration of credit risk. At June 30, 2005, the University's non-pooled investments were not exposed to concentration of credit risk.

*Foreign Currency Risk:* Foreign currency risk is defined by GASB Statement No. 40 as the risk that changes in exchange rates will adversely affect the fair value of an investment. The University does not have a formal policy for foreign currency risk. At June 30, 2005, the University's non-pooled investments were not exposed to foreign currency risk.

### **NOTE 3 - ENDOWMENT INVESTMENTS**

Investments of the University's endowment funds are pooled. 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). The total spending rate is calculated annually by taking the sum of the market value of the endowment investments for the preceding twelve quarters, and dividing the result by twelve. Spending from the average value shall be at a rate of five percent, paid out proportionately on a quarterly basis. To the extent that the total return for the current year exceeds the payout, 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. At June 30, 2005, net appreciation of \$3,522,765.06 was available to be spent for restricted purposes.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### NOTE 4 - RECEIVABLES

Receivables at June 30, 2005, were as follows:

	<u>Gross Receivables</u>	<u>Less Allowance for Doubtful Accounts</u>	<u>Net Receivables</u>
<b>Current Receivables:</b>			
Students	\$ 836,084.79	\$ 616,572.20	\$ 219,512.59
Accounts	49,127.77		49,127.77
Intergovernmental	846,946.47		846,946.47
Interest on Loans	134,750.05		134,750.05
Other	14,221.12		14,221.12
<b>Total Current Receivables</b>	<b><u>\$ 1,881,130.20</u></b>	<b><u>\$ 616,572.20</u></b>	<b><u>\$ 1,264,558.00</u></b>
<b>Notes Receivable:</b>			
<b>Notes Receivable - Current:</b>			
Federal Loan Programs	\$ 257,824.15	\$ 87,327.93	\$ 170,496.22
Institutional Student Loan Programs	19,958.07	4,685.69	15,272.38
<b>Total Notes Receivable - Current</b>	<b><u>\$ 277,782.22</u></b>	<b><u>\$ 92,013.62</u></b>	<b><u>\$ 185,768.60</u></b>
<b>Notes Receivable - Noncurrent:</b>			
Federal Loan Programs	\$ 1,104,237.34	\$ 377,310.97	\$ 726,926.37
Institutional Student Loan Programs	111,538.26	43,374.24	68,164.02
<b>Total Notes Receivable - Noncurrent</b>	<b><u>\$ 1,215,775.60</u></b>	<b><u>\$ 420,685.21</u></b>	<b><u>\$ 795,090.39</u></b>

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### NOTE 5 - CAPITAL ASSETS

A summary of changes in the capital assets for the year ended June 30, 2005, is presented as follows:

	Balance July 1, 2004	Adjustments	Increases	Decreases	Balance June 30, 2005
Capital Assets, Nondepreciable:					
Land	\$ 3,968,242.04	\$ 0.00	\$ 0.00	\$ 0.00	\$ 3,968,242.04
Art, Literature, and Artifacts	619,772.00		6,000.00		625,772.00
Construction in Progress	9,570,398.50	(12,417,765.47)	12,825,379.68		9,978,012.71
<b>Total Capital Assets, Nondepreciable</b>	<b>14,158,412.54</b>	<b>(12,417,765.47)</b>	<b>12,831,379.68</b>		<b>14,572,026.75</b>
Capital Assets, Depreciable:					
Buildings	86,182,334.30	11,958,736.17	18,235,940.44		116,377,010.91
Machinery and Equipment	5,052,822.56	94,139.83	1,067,631.33	71,751.98	6,142,841.74
General Infrastructure	3,772,998.30	442,224.30			4,215,222.60
<b>Total Capital Assets, Depreciable</b>	<b>95,008,155.16</b>	<b>12,495,100.30</b>	<b>19,303,571.77</b>	<b>71,751.98</b>	<b>126,735,075.25</b>
Less Accumulated Depreciation for:					
Buildings	27,193,080.97		2,330,473.44		29,523,554.41
Machinery and Equipment	3,031,142.87	77,334.83	621,357.57	69,387.50	3,660,447.77
General Infrastructure	1,733,915.28		126,549.60		1,860,464.88
<b>Total Accumulated Depreciation</b>	<b>31,958,139.12</b>	<b>77,334.83</b>	<b>3,078,380.61</b>	<b>69,387.50</b>	<b>35,044,467.06</b>
<b>Total Capital Assets, Depreciable, Net</b>	<b>63,050,016.04</b>	<b>12,417,765.47</b>	<b>16,225,191.16</b>	<b>2,364.48</b>	<b>91,690,608.19</b>
<b>Capital Assets, Net</b>	<b>\$ 77,208,428.58</b>	<b>\$ 0.00</b>	<b>\$ 29,056,570.84</b>	<b>\$ 2,364.48</b>	<b>\$ 106,262,634.94</b>

### NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2005, were as follows:

	Amount
Accounts Payable	\$ 1,667,058.01
Accrued Payroll	1,282,998.90
Contract Retainage	354,997.50
<b>Total Accounts Payable and Accrued Liabilities</b>	<b>\$ 3,305,054.41</b>

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### 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, 2005, is presented as follows:

	Balance July 1, 2004	Additions	Reductions	Balance June 30, 2005	Current Portion
Bonds Payable	\$ 13,270,000.00	\$ 0.00	\$ 705,000.00	\$ 12,565,000.00	\$ 630,000.00
Add Premium	112,013.38		9,143.95	102,869.43	
Total Bonds Payable	<u>13,382,013.38</u>		<u>714,143.95</u>	<u>12,667,869.43</u>	<u>630,000.00</u>
Capital Leases Payable		18,180,000.00	150,000.00	18,030,000.00	350,000.00
Compensated Absences	2,520,671.44	2,348,321.00	2,185,352.44	2,683,640.00	439,166.33
<b>Total Long-Term Liabilities</b>	<u>\$ 15,902,684.82</u>	<u>\$ 20,528,321.00</u>	<u>\$ 3,049,496.39</u>	<u>\$ 33,381,509.43</u>	<u>\$ 1,419,166.33</u>

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 June 30, 2005	Principal Outstanding June 30, 2005
<u>Housing and Dining System</u>						
UNC System Pool Revenue Bonds	2002B	3.50% - 5.37%	04/01/2017	\$ 3,090,000.00	\$ 395,000.00	\$ 2,695,000.00
Revenue Refunding Bonds	1998B	3.70% - 5.00%	01/01/2017	<u>8,430,000.00</u>	<u>1,465,000.00</u>	<u>6,965,000.00</u>
Total Housing and Dining System				<u>11,520,000.00</u>	<u>1,860,000.00</u>	<u>9,660,000.00</u>
<u>Student Services System</u>						
UNC System Pool Revenue Bonds	2004B	3.00% - 5.00%	04/01/2022	<u>2,925,000.00</u>	<u>20,000.00</u>	<u>2,905,000.00</u>
Total Bonds Payable (principal only)				<u>\$ 14,445,000.00</u>	<u>\$ 1,880,000.00</u>	12,565,000.00
Plus: Unamortized Premium						<u>102,869.43</u>
Total Bonds Payable						<u>\$ 12,667,869.43</u>

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

**C. Annual Requirements** - The annual requirements to pay principal and interest on the long-term obligations at June 30, 2005, are as follows:

<u>Fiscal Year</u>	Annual Requirements	
	Bonds Payable	
	Principal	Interest
2006	\$ 630,000.00	\$ 571,100.00
2007	775,000.00	544,057.50
2008	805,000.00	512,645.00
2009	835,000.00	479,132.50
2010	875,000.00	443,163.75
2011-2015	5,090,000.00	1,536,692.51
2016-2020	3,075,000.00	355,056.26
2021-2022	480,000.00	29,000.00
Total Requirements	\$ 12,565,000.00	\$ 4,470,847.52

### NOTE 8 - LEASE OBLIGATIONS

**A. Capital Lease Obligations** - Capital lease obligations relating to University student housing is 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, 2005:

<u>Fiscal Year</u>	<u>Amount</u>
2006	\$ 1,137,128.76
2007	1,136,628.76
2008	1,135,828.76
2009	1,134,728.76
2010	1,138,328.76
2011-2015	5,680,431.26
2016-2020	5,691,072.52
2021-2025	5,683,981.26
2026-2030	5,679,732.50
2031-2034	4,553,475.00
Total Minimum Lease Payments	32,971,336.34
Amount Representing Interest (3.00% - 5.00% Interest Rate/Range)	14,941,336.34
Present Value of Future Lease Payments	\$ 18,030,000.00

Buildings acquired under capital lease amounted to \$18,180,000.00 at June 30, 2005.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

**B. Operating Lease Obligations** - The University entered into operating leases for office space. Future minimum lease payments under noncancelable operating leases consist of the following at June 30, 2005:

<u>Fiscal Year</u>	<u>Amount</u>
2006	<u>\$ 49,353.56</u>

Rental expense for all operating leases during the year was \$707,160.90.

### NOTE 9 - REVENUES

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

	<u>Gross Revenues</u>	<u>Internal Sales Eliminations</u>	<u>Less Scholarship Discounts</u>	<u>Less Allowance for Uncollectibles</u>	<u>Net Revenues</u>	<u>Revenues Pledged as Security for Debt</u>
<b>Operating Revenues:</b>						
<b>Student Tuition and Fees</b>	\$ 15,683,427.64	\$ 0.00	\$ 3,761,192.92	\$ 105,172.00	\$ 11,817,062.72	\$ 612,542.69 (B)
<b>Sales and Services:</b>						
Sales and Services of Auxiliary Enterprises:						
Residential Life	\$ 5,442,571.02	\$ 0.00	\$ 1,226,152.52	\$ 55,524.51	\$ 4,160,893.99	\$ 4,160,893.99 (A)
Dining	3,722,118.45		831,456.51	18,113.20	2,872,548.74	2,872,548.74 (A)
Student Union Services	573,436.89			9,641.32	563,795.57	563,795.57 (B)
Health, Physical Education, and Recreation Services	20,346.33			10,050.23	10,296.10	
Parking	464,507.24			295.81	464,211.43	
Athletic	149,019.35			11,456.13	137,563.22	
Other	2,023,587.95	1,363,263.11			660,324.84	
<b>Total Sales and Services</b>	<u>\$ 12,395,587.23</u>	<u>\$ 1,363,263.11</u>	<u>\$ 2,057,609.03</u>	<u>\$ 105,081.20</u>	<u>\$ 8,869,633.89</u>	<u>\$ 7,597,238.30</u>

Revenue Bonds Secured by Pledged Revenues:

(A) Housing and Dining System

(B) Student Services System

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### 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	\$ 25,825,980.33	\$ 2,050,241.95	\$ 2,716,947.22	\$ 331,623.20	\$ 0.00	\$ 0.00	\$ 30,924,792.70
Research	984,895.88	351,361.08	313,696.00	66,445.00			1,716,397.96
Public Service	1,612,643.29	116,945.80	655,684.70	2,873.54	617.82		2,388,765.15
Academic Support	4,602,786.26	2,284,767.12	895,637.99	2,777.00			7,785,968.37
Student Services	2,145,549.12	193,555.08	707,082.44	24,562.98	61.00		3,070,810.62
Institutional Support	6,244,264.88	1,127,435.49	3,207,099.85				10,578,800.22
Operations and Maintenance of Plant	3,636,510.25	704,138.13	2,436,367.93		1,555,896.06		8,332,912.37
Student Financial Aid	340,785.37	3,480.36	65,009.28	4,993,876.92			5,403,151.93
Auxiliary Enterprises	2,929,596.20	892,851.71	6,348,926.36		587,807.23		10,759,181.50
Depreciation						3,078,380.61	3,078,380.61
Total Operating Expenses	<u>\$ 48,323,011.58</u>	<u>\$ 7,724,776.72</u>	<u>\$ 17,346,451.77</u>	<u>\$ 5,422,158.64</u>	<u>\$ 2,144,382.11</u>	<u>\$ 3,078,380.61</u>	<u>\$ 84,039,161.43</u>

### 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, 2005, these rates were set at 2.17% of covered payroll for employers and 6% of covered payroll for members.

For the year ended June 30, 2005, the University had a total payroll of \$40,346,265.32, of which \$22,129,305.14 was covered under the Teachers' and State Employees' Retirement System. Total employee and

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

---

employer contributions for pension benefits for the year were \$1,327,758.31 and \$480,205.92, respectively. The University made 100% of its annual required contributions for the years ended June 30, 2005, 2004, and 2003, which were \$480,205.92, \$45,517.08, and \$0.00, 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, 2005, 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, 2005, the University had a total payroll of \$40,346,265.32, of which \$10,125,030.89 was covered under the Optional Retirement Program. Total employee and employer contributions for

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

---

pension benefits for the year were \$607,501.85 and \$692,552.11, 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 \$143,908.18 for the year ended June 30, 2005.

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, 2005, were \$17,598.97. The voluntary contributions by employees amounted to \$180,124.00 for the year ended June 30, 2005.

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 \$400,485.99 for the year ended June 30, 2005.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

---

### 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, 2005, the University's total contribution to the Plan was \$1,032,138.75. 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. The University contributes .445% of covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the DIPNC. For the year ended June 30, 2005, the University's total contribution to the DIPNC was \$143,531.80. 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*.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

---

### 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. 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 except theft losses carry a \$1,000 per occurrence deductible. The University also purchased through the Fund extended coverage against losses caused by windstorm or hail, explosion, smoke, aircraft or vehicles, and riot or civil commotion on certain buildings and contents. In addition, the University purchased "all risk" coverage through the fund for a particular tower and adjacent building.

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.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

---

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

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

Term life insurance (death benefits) of \$25,000 to \$50,000 is provided to eligible workers. This Death Benefit Plan is administered by the State Treasurer and funded via employer contributions. 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 \$3,811,652.45 and on other purchases were \$2,420,898.65 at June 30, 2005.
- B. **Capital Lease Commitment** - The University entered into a thirty-two year lease agreement with the Winston-Salem University Housing Foundation, LLC, on September 22, 2004. Under the agreement, the Housing Foundation will construct and lease a student housing facility (Hairston-Gleason) to the University.
- C. **Pending Litigation and Claims** - The University is a party to litigation and claims in the ordinary course of its operations. Since it is not possible to predict the ultimate outcome of these matters, no provision for any liability has been made in the financial statements. University management is of the opinion that the liability, if any, for any of these matters will not have a material adverse effect on the financial position of the University.

## NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)

---

**D. University Improvement General Obligation Bonds** - The 1999-2000 Session of the General Assembly of North Carolina authorized the issuance of \$2.5 billion 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 \$5,180,756.00 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 - CHANGE IN FINANCIAL ACCOUNTING AND REPORTING**

For the fiscal year ended June 30, 2005, the University implemented Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures*. This Statement establishes and modifies disclosure requirements related to investment risks: credit risk, interest rate risk, and foreign currency risk. This statement also establishes and modifies disclosure requirements for deposit risks: custodial credit risk and foreign currency risk.

[ This Page Left Blank Intentionally ]



STATE OF NORTH CAROLINA  
Office of the State Auditor

Leslie W. Merritt, Jr., CPA, CFP  
State Auditor

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

**INDEPENDENT AUDITOR'S REPORT  
ON 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  
Winston-Salem State University  
Winston-Salem, North Carolina

We have audited the financial statements of Winston-Salem State University, a constituent institution of the 16-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, 2005, which collectively comprise the University's basic financial statements and have issued our report thereon dated December 29, 2005. We did not audit the financial statements of Winston-Salem State University Foundation, Inc., and Subsidiary, which represent 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 15 to the financial statements, the University implemented Governmental Accounting Standards Board Statement No. 40, *Deposit and Investment Risk Disclosures*, during the year ended June 30, 2005.

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 opinions 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 that might be material

**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)**

---

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 Governors, the Board of Trustees, management 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.

*Leslie W. Merritt, Jr.*

Leslie W. Merritt, Jr., CPA, CFP  
State Auditor

December 29, 2005

## DISTRIBUTION OF AUDIT REPORT

---

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

### EXECUTIVE BRANCH

The Honorable Michael F. Easley  
The Honorable Beverly M. Perdue  
The Honorable Richard H. Moore  
The Honorable Roy A. Cooper, III  
Mr. David T. McCoy  
Mr. Robert L. Powell  
Mr. Erskine B. Bowles  
Dr. Harold L. Martin, Sr.  
Mr. Robert Botley

Mr. Kevin A. Myatt

Governor of North Carolina  
Lieutenant Governor of North Carolina  
State Treasurer  
Attorney General  
State Budget Officer  
State Controller  
President, The University of North Carolina  
Chancellor, Winston-Salem State University  
Interim Vice Chancellor for Finance and Administration  
Winston-Salem State University  
Chairman, Board of Trustees  
Winston-Salem State University

### LEGISLATIVE BRANCH

Appointees to the Joint Legislative Commission on Governmental Operations

President Pro Tempore  
Senator Marc Basnight, Co-Chair  
Senator Charles W. Albertson  
Senator Thomas M. Apodaca  
Senator Daniel G. Clodfelter  
Senator Walter H. Dalton  
Senator Charlie S. Dannelly  
Senator James Forrester  
Senator Linda Garrou  
Senator Kay R. Hagan  
Senator Fletcher L. Hartsell, Jr.  
Senator David W. Hoyle  
Senator John H. Kerr, III  
Senator Ellie Kinnaird  
Senator Jeanne H. Lucas  
Senator Anthony E. Rand  
Senator R. C. Soles, Jr.  
Senator Richard Y. Stevens  
Senator A. B. Swindell, IV

Speaker of the House  
Representative James B. Black, Co-Chair  
Representative Alma S. Adams  
Representative Martha B. Alexander  
Representative Harold J. Brubaker  
Representative Lorene T. Coates  
Representative E. Nelson Cole  
Representative James W. Crawford, Jr.  
Representative W. Pete Cunningham  
Representative Beverly M. Earle  
Representative Pryor A. Gibson, III  
Representative Joe Hackney  
Representative R. Phillip Haire  
Representative Dewey L. Hill  
Representative Lindsey H. Holliman  
Representative Julia C. Howard  
Representative Howard J. Hunter, Jr.  
Representative Margaret M. Jeffus  
Representative Daniel F. McComas  
Representative Charles L. McLawhorn  
Representative Henry M. Michaux, Jr.  
Representative Richard T. Morgan  
Representative Edd Nye  
Representative William C. Owens, Jr.  
Representative Deborah K. Ross  
Representative Drew P. Saunders  
Representative Wilma M. Sherrill  
Representative Joe P. Tolson  
Representative Edith D. Warren  
Representative Thomas E. Wright  
Representative Douglas Y. Yongue

### Other Legislative Officials

Mr. Lynn Muchmore

Director, Fiscal Research Division

February 27, 2006

## ORDERING INFORMATION

---

Copies of this report may be obtained by contacting the:

Office of the State Auditor  
State of North Carolina  
2 South Salisbury Street  
20601 Mail Service Center  
Raleigh, North Carolina 27699-0601

Internet: <http://www.ncauditor.net>

Telephone: 919/807-7500

Facsimile: 919/807-7647