



STATE OF NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT OF ELIZABETH CITY STATE UNIVERSITY

ELIZABETH CITY, 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

ELIZABETH CITY STATE UNIVERSITY

ELIZABETH CITY, NORTH CAROLINA

FOR THE YEAR ENDED JUNE 30, 2005

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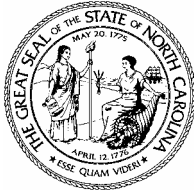
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STATE OF NORTH CAROLINA
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State Auditor

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AUDITOR'S TRANSMITTAL

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

We have completed a financial statement audit of Elizabeth City 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.

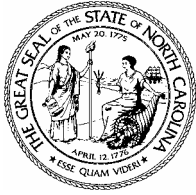
Leslie W. Merritt, Jr.

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

June 23, 2006

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Elizabeth City State University
Elizabeth City, North Carolina

We have audited the accompanying basic financial statements of Elizabeth City 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, as of and for the year ended June 30, 2005, as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the financial statements of Elizabeth City State University Foundation, Inc. and Subsidiary, which represent 15 percent, four percent, and three percent, respectively, of the assets, net assets and revenues of the University. 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 those entities, 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 Elizabeth City 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 opinion.

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 financial position of Elizabeth City State University as of June 30, 2005, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

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 May 11, 2006, 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

May 11, 2006

ELIZABETH CITY STATE UNIVERSITY MANAGEMENT'S DISCUSSION AND ANALYSIS

Elizabeth City State University prepared its financial statements in accordance with Governmental Accounting Standards Board (GASB) Statement Number 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended by GASB Statement Number 35, *Basic Financial Statements - and Management's Discussion and Analysis - for Public Colleges and Universities*. The standards require three basic financial statements: the Statement of Net Assets, the Statement of Revenues, Expenses, and Changes in Net Assets, and the Statement of Cash Flows.

The Statement of Net Assets includes all assets and liabilities. The University's net assets (the difference between assets and liabilities) are one 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 Net Assets provides information about assets and liabilities in a format that distinguishes between current and noncurrent. Individual assets and liabilities are classified as current or noncurrent based on whether they are expected to generate or use cash within the next 12 months after the end of the fiscal period.

Net assets, or the difference between total assets and total liabilities, are divided into three major components. The first component, invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages or notes that are attributable to the acquisition, construction, or improvement of those assets. The next component, restricted net assets, is divided into two categories: expendable and nonexpendable. Net assets are restricted when constraints are placed on them by either external parties (creditors, grantors, donors, etc.) or by enabling legislation or constitutional provisions. Nonexpendable net assets are those that are required to be retained in perpetuity. The final component is unrestricted net assets. These are net assets that are available to the University for any lawful purpose of the University.

The Statement of Revenues, Expenses, and Changes in Net Assets represents 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.

The Statement of Revenues, Expenses, and Changes in Net Assets distinguishes between operating and nonoperating revenues and expenses. Operating revenues and expenses generally result from providing goods and services and the cost of providing those goods and services. Nonoperating revenues are revenues received for which goods and services are not provided. This includes State appropriations for operating and capital purposes.

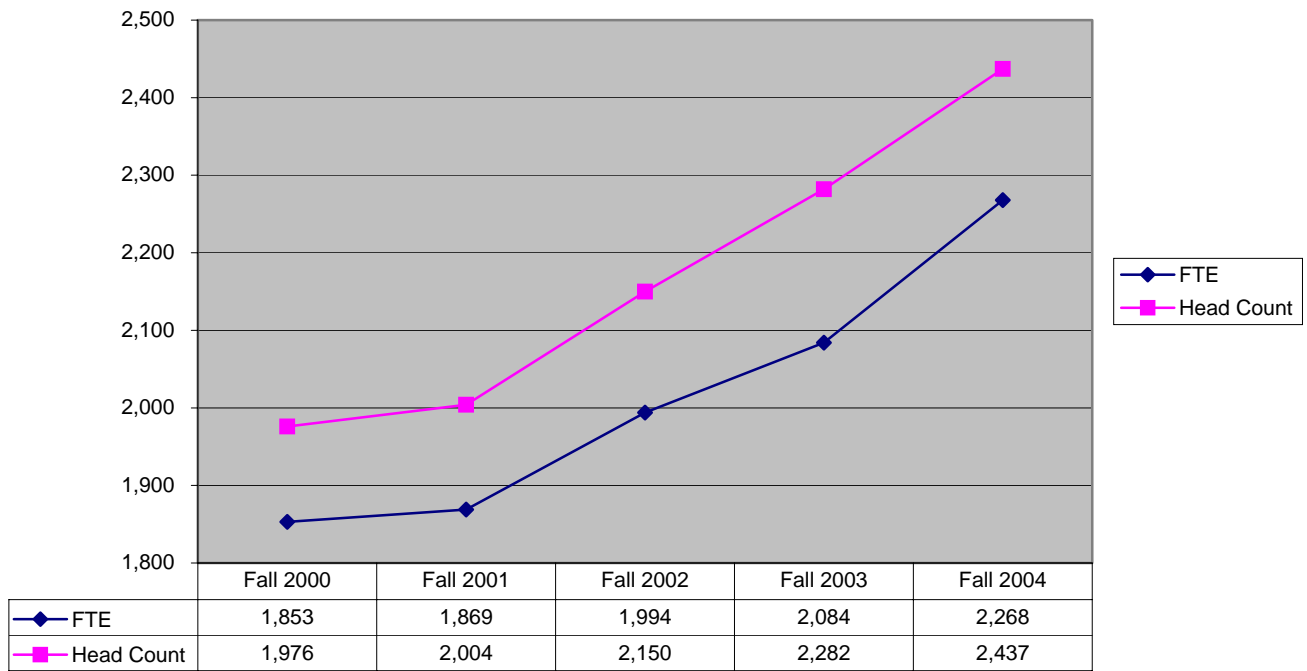
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Another important factor to consider when evaluating financial viability is the University's ability to meet financial obligations as they occur. The Statement of Cash Flows presents information related to cash inflows and outflows summarized by operating, noncapital financing, capital and related financing and investing activities.

The following discussion and analysis provides an overview of the University's financial activities.

Enrollment increased from 2,282 students in the fall of 2003 to 2,437 in the fall of 2004 based on headcount. This equates to a 6.8% increase.

FTE and Head Count from Fall 2000 to Fall 2004



MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Comparative, Condensed Statement of Net Assets

	<u>2005</u>	<u>2004</u>	<u>% Change</u>
Assets			
Current Assets	\$ 14,885,705	\$ 13,319,711	11.8 %
Capital Assets, Net	94,881,082	84,582,113	12.2 %
Other Assets	<u>11,984,153</u>	<u>13,442,439</u>	<u>(10.8) %</u>
Total Assets	<u>121,750,940</u>	<u>111,344,263</u>	<u>9.3 %</u>
Liabilities			
Current Liabilities	3,533,723	4,662,361	(24.2) %
Noncurrent Liabilities	<u>22,184,662</u>	<u>22,570,623</u>	<u>(1.7) %</u>
Total Liabilities	<u>25,718,385</u>	<u>27,232,984</u>	<u>(5.6) %</u>
Net Assets			
Invested in Capital Assets, Net of Related Debt	75,374,765	67,802,609	11.2 %
Restricted - Expendable	12,405,545	6,803,562	82.3 %
Restricted - Nonexpendable	2,624,054	2,402,325	9.2 %
Unrestricted	<u>5,628,191</u>	<u>7,102,783</u>	<u>(20.8) %</u>
Total Net Assets	<u>\$ 96,032,555</u>	<u>\$ 84,111,279</u>	<u>14.2 %</u>

As of June 30, 2005, total University assets were \$121.8 million. Buildings, less accumulated depreciation, make up \$58.6 million of this total. The University's current construction in progress is \$25.8 million.

The University's current assets of \$14.9 million fully covered the current liabilities of \$3.5 million, as the current ratio was \$4.3 in current assets to every \$1 in current liabilities.

Capital assets grew from \$84.6 million to \$94.9 million, net of depreciation, in fiscal year 2005. This increase was due to construction activity, which totaled \$11.7 million.

University liabilities totaled \$25.7 million at June 30, 2005. Current liabilities decreased by \$1.1 million. This decrease was due to fewer accounts payable related to construction activity at June 30, 2005, as several construction projects came to a close during the year. Bonds payable totaling \$20.1 million is the largest single liability.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Comparative, Condensed Statement of Revenues, Expenses, and Changes in Net Assets

	<u>2005</u>	<u>2004</u>	<u>% Change</u>
Operating Revenues			
Student Tuition and Fees, Net	\$ 5,157,266	\$ 4,545,343	13.5 %
Federal Contracts and Grants	5,900,914	5,978,053	(1.3) %
Sales and Services, Net	4,006,123	3,156,567	26.9 %
Other Operating Revenues	477,788	378,815	26.1 %
Total Operating Revenues	<u>15,542,091</u>	<u>14,058,778</u>	10.6 %
Operating Expenses	<u>50,566,509</u>	<u>45,778,240</u>	10.5 %
Operating Loss	(35,024,418)	(31,719,462)	10.4 %
Nonoperating Revenues and Expenses:			
State Appropriations	26,071,821	24,559,904	6.2 %
Noncapital Grants	6,177,716	6,764,430	(8.7) %
Other Nonoperating Revenues	1,290,068	992,313	30.0 %
Interest and Fees on Debt	(786,121)	(409,340)	92.0 %
Net Nonoperating Revenues	<u>32,753,484</u>	<u>31,907,307</u>	2.7 %
Income (Loss) Before Other Revenues	(2,270,934)	187,845	(1308.9) %
Capital Grants and Appropriations	14,023,831	11,252,840	24.6 %
Capital Gifts	20,000	32,000	(37.5) %
Additions to Permanent Endowment	148,379	317,765	(53.3) %
Total Other Revenues	<u>14,192,210</u>	<u>11,602,605</u>	22.3 %
Increase in Net Assets	11,921,276	11,790,450	1.1 %
Net Assets at the Beginning of Year	<u>84,111,279</u>	<u>72,320,829</u>	16.3 %
Net Assets at the End of the Year	<u>\$ 96,032,555</u>	<u>\$ 84,111,279</u>	14.2 %

Tuition and fees, net of scholarship allowances, increased by \$611,923 over the prior year. This increase was due to a 7% increase in enrollment, as well as a small increase in tuition and fees charged to students. Sales and Service revenue, net of scholarship, discounts and allowances for uncollectible amounts, increased by \$849,556 over the prior year. This was also due to an increase in enrollment, as well as an increase in fees charged to students for Residence Life and Dining.

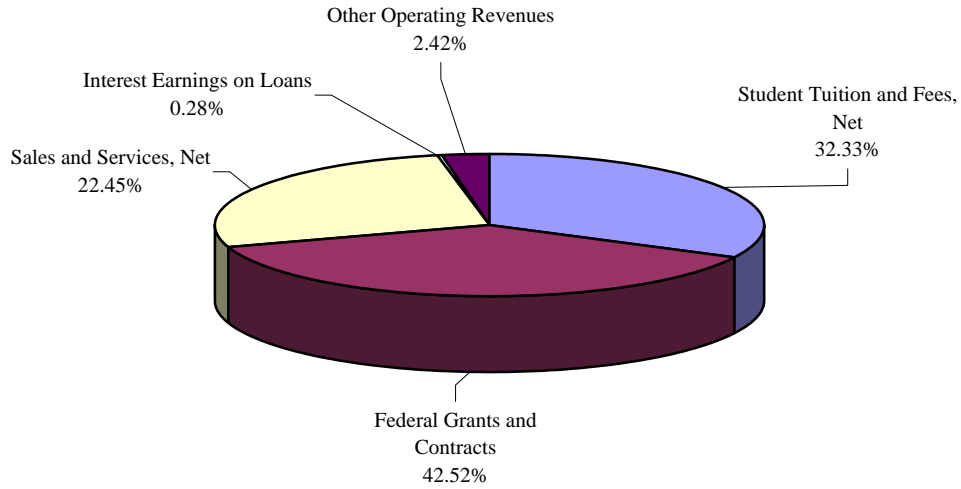
Total operating loss for fiscal year 2005 was \$35 million. Since the State of North Carolina appropriation is not included within operating revenue per GASB Statement No. 35, the University will show an operating loss.

Capital grants increased by \$2.8 million. This increase was due to an increase in the amount available to the University, for construction projects funded through the 2000 Higher Education Bonds.

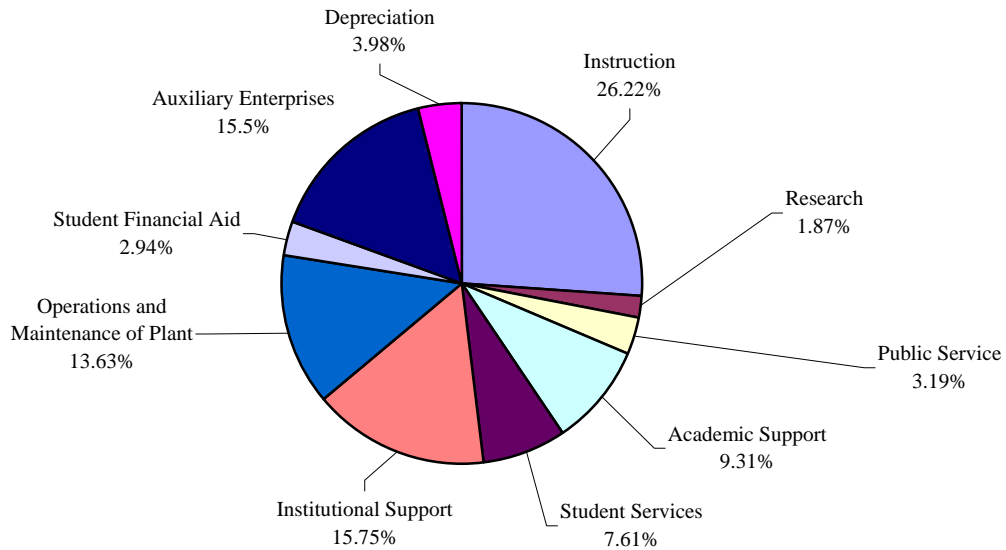
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

The sources of operating revenue for the University include tuition and fees, certain grants and contracts, and auxiliary services.

Operating Revenues by Source



Expenses by Function



MANAGEMENT'S DISCUSSION AND ANALYSIS (CONCLUDED)

Comparative Condensed Statement of Cash Flows

	<u>2005</u>	<u>2004</u>
Net Cash Used by Operating Activities	\$ (34,201,041)	\$ (29,650,237)
Net Cash Provided by Noncapital Financing Activities	32,677,082	32,056,319
Net Cash Provided (Used) by Capital Financing Activities	(2,343,544)	2,092,242
Net Cash Provided (Used) by Investing Activities	<u>3,223,018</u>	<u>(3,880,992)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	(644,485)	617,332
Cash and Cash Equivalents - Beginning of the Year	<u>10,437,417</u>	<u>9,820,085</u>
Cash and Cash Equivalents - End of Year	<u>\$ 9,792,932</u>	<u>\$ 10,437,417</u>

Major sources of funds included in operating activities include student tuition and fees \$5,157,266, sales and services of auxiliary enterprises \$4,006,123, and operating contracts and grants \$5,910,677. Major uses of funds included in operating activities include payments to employees \$30,599,112 and payments to vendors and suppliers \$18,195,564.

Net cash used by operating activities increased by \$4.6 million dollars. The largest increase in this category was an increase of \$5.1 million in the amount paid to vendors and suppliers over the prior year. This was due to the overall growth of the university, as well as an increase in the amount spent to renovate existing facilities at the University.

The North Carolina State appropriation of \$26,071,821 is the largest inflow of cash in noncapital financing activities.

Economic Outlook

The economic environment has shown signs of improvement. The University's net assets grew from \$84 million to over \$96 million over the fiscal year ending June 30, 2005. State appropriations grew from \$24.6 million in the fiscal year ending June 30, 2004, to over \$26 million in the fiscal year ending June 30, 2005.

Enrollment increased from 2,282 students in fall 2003 to 2,437 in fall 2004 based on head count. This equates to a 6.8% increase.

The UNC Higher Education Bond Referendum projects were well under way with \$33,943,321 expended of the University's total allotment of \$46.3 million.

The University recorded an increase of total net assets of \$11,921,276 which included investment income, including market appreciation of investments totaling \$405,175 net of related investment fees.

In 2004-05, the UNC Board of Governors and the North Carolina General Assembly approved the construction of a \$28 million building for the Joint School of Pharmacy between Elizabeth City State University and UNC Chapel Hill.

Elizabeth City State University
Statement of Net Assets
June 30, 2005

Exhibit A-1

ASSETS

Current Assets:

Cash and Cash Equivalents	\$ 7,536,041.28
Restricted Cash and Cash Equivalents	1,298,518.24
Receivables, Net (Note 4)	3,746,045.46
Due from State of North Carolina Component Units	8,000.00
Inventories	878,305.88
Notes Receivable (Note 4)	87,935.80
Other Assets	1,330,858.33
	<hr/>
Total Current Assets	14,885,704.99

Noncurrent Assets:

Restricted Cash and Cash Equivalents	958,372.68
Restricted Due from Primary Government	5,948,844.51
Endowment Investments	2,262,951.07
Other Long-Term Investments	2,222,749.35
Notes Receivable, Net (Note 4)	591,235.90
Capital Assets - Nondepreciable (Note 5)	27,445,249.68
Capital Assets - Depreciable, Net (Note 5)	67,435,832.10
	<hr/>
Total Noncurrent Assets	106,865,235.29

Total Assets	<hr/> <hr/> 121,750,940.28
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LIABILITIES

Current Liabilities:

Accounts Payable and Accrued Liabilities (Note 6)	1,744,241.64
Due to Primary Government	23,305.71
Deferred Revenue	953,470.25
Interest Payable	94,976.45
Long-Term Liabilities - Current Portion (Note 7)	717,728.44
	<hr/>
Total Current Liabilities	3,533,722.49

Noncurrent Liabilities:

Deposits Payable	80,551.32
Funds Held for Others	179,696.01
U. S. Government Grants Refundable	708,765.52
Long-Term Liabilities (Note 7)	21,215,649.29
	<hr/>
Total Noncurrent Liabilities	22,184,662.14

Total Liabilities	<hr/> <hr/> 25,718,384.63
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Elizabeth City State University
Statement of Net Assets
June 30, 2005

Exhibit A-1
Page 2

NET ASSETS

Invested in Capital Assets, Net of Related Debt	75,374,765.38
Restricted for:	
Nonexpendable:	
Scholarships and Fellowships	1,371,394.89
Endowed Professorships	1,252,659.16
Expendable:	
Scholarships and Fellowships	2,619,087.68
Endowed Professorships	166,792.25
Loans	221,471.26
Capital Projects	7,620,792.05
Debt Service	1,777,402.32
Unrestricted	5,628,190.66
Total Net Assets	<u>\$ 96,032,555.65</u>

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

Elizabeth City 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)	\$ 5,157,266.07
Federal Grants and Contracts	5,900,914.19
Nongovernmental Grants and Contracts	9,763.07
Sales and Services, Net (Note 9)	4,006,123.17
Interest Earnings on Loans	24,428.76
Other Operating Revenues	443,595.73
	<hr/>
Total Operating Revenues	15,542,090.99
	<hr/>

EXPENSES

Operating Expenses:	
Salaries and Benefits	30,599,112.32
Supplies and Materials	4,114,205.38
Services	10,221,935.39
Scholarships and Fellowships	1,494,577.63
Utilities	2,110,693.76
Depreciation	2,025,984.46
	<hr/>
Total Operating Expenses	50,566,508.94
	<hr/>
Operating Loss	(35,024,417.95)
	<hr/>

NONOPERATING REVENUES (EXPENSES)

State Appropriations	26,071,821.16
Noncapital Grants	6,177,716.05
Noncapital Gifts	896,601.39
Investment Income (Net of Investment Expense of \$18,557)	405,174.83
Interest and Fees on Debt	(786,120.63)
Other Nonoperating Expenses	(11,707.88)
	<hr/>
Net Nonoperating Revenues	32,753,484.92
	<hr/>
Income Before Other Revenues	(2,270,933.03)
	<hr/>
Capital Appropriations	619,500.00
Capital Grants	13,404,330.76
Capital Gifts	20,000.00
Additions to Endowments	148,379.15
	<hr/>
Increase in Net Assets	11,921,276.88
	<hr/>

NET ASSETS

Net Assets - July 1, 2004	<hr/> 84,111,278.77
Net Assets - June 30, 2005	<hr/> \$ 96,032,555.65
	<hr/>

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

Elizabeth City 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	\$ 15,547,616.47
Payments to Employees and Fringe Benefits	(30,468,766.34)
Payments to Vendors and Suppliers	(18,195,563.51)
Payments for Scholarships and Fellowships	(1,494,577.63)
Loans Issued	(191,515.00)
Collection of Loans	115,918.00
Interest Earned on Loans	28,373.74
Other Receipts	457,473.04
	<hr/>
Net Cash Used by Operating Activities	(34,201,041.23)

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

State Appropriations	26,071,821.16
Noncapital Grants	5,656,435.57
Noncapital Gifts	797,883.89
Additions to Endowments	148,379.15
William D. Ford Direct Lending Receipts	7,383,007.00
William D. Ford Direct Lending Disbursements	(7,383,007.00)
Related Activity Agency Receipts	62,605.54
Other Payments	(60,042.83)
	<hr/>
Net Cash Provided by Noncapital Financing Activities	32,677,082.48

CASH FLOWS FROM CAPITAL FINANCING AND RELATED FINANCING ACTIVITIES

State Capital Appropriations	619,500.00
Capital Grants	10,785,883.38
Capital Gifts	20,000.00
Proceeds from Sale of Capital Assets	5,127.20
Acquisition and Construction of Capital Assets	(12,431,786.22)
Principal Paid on Capital Debt and Leases	(555,000.00)
Interest and Fees Paid on Capital Debt and Leases	(787,268.19)
	<hr/>
Net Cash Used by Capital Financing and Related Financing Activities	(2,343,543.83)

CASH FLOWS FROM INVESTING ACTIVITIES

Proceeds from Sales and Maturities of Investments	3,686,239.21
Investment Income	299,514.53
Purchase of Investments and Related Fees	(762,735.51)
	<hr/>
Net Cash Provided by Investing Activities	3,223,018.23

Net Decrease in Cash and Cash Equivalents	(644,484.35)
Cash and Cash Equivalents - July 1, 2004	10,437,416.55
	<hr/>
Cash and Cash Equivalents - June 30, 2005	\$ 9,792,932.20

Elizabeth City 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	\$	(35,024,417.95)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:		
Depreciation Expense		2,025,984.46
Allowances, Write-Offs, and Amortizations		7,098.00
Nonoperating Other Expenses		(47,530.65)
Changes in Assets and Liabilities:		
Receivables (Net)		328,983.77
Inventories		(11,404.35)
Accounts Payable and Accrued Liabilities		(1,557,994.57)
Due to Primary Government		12,958.01
Deferred Revenue		115,262.52
Compensated Absences		25,616.53
Note Principal Repayments		136,996.00
Notes Issued		(212,593.00)
		<u> </u>
Net Cash Used by Operating Activities	\$	<u><u>(34,201,041.23)</u></u>

RECONCILIATION OF CASH AND CASH EQUIVALENTS

Current Assets:		
Cash and Cash Equivalents	\$	7,536,041.28
Restricted Cash and Cash Equivalents		1,298,518.24
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		958,372.68
		<u> </u>
Total Cash and Cash Equivalents - June 30, 2005	\$	<u><u>9,792,932.20</u></u>

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

Assets Acquired through a Gift	\$	20,000.00
Change in Fair Value of Investments		108,598.00
Loss on Disposal of Capital Assets		(29,108.00)

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

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ELIZABETH CITY 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. Elizabeth City 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 units. While the Board of Governors of the University of North Carolina System has ultimate responsibility, the Chancellor, the Board of Trustees, and the Board of Trustees of the Endowment Fund have delegated responsibilities for financial accountability of the University's funds. The University's component unit is blended in the University's financial statements. The blended component unit, although legally separate, is, in substance, part of the University's operations and therefore, is reported as if it was part of the University.

Blended Component Unit - Although legally separate, Elizabeth City State University Foundation, Inc. and Subsidiary (Foundation), a component unit of the University, is reported as if it was part of the University.

The Foundation is governed by a 25-member board consisting of 13 ex officio directors and 12 elected directors. The Foundation's purpose is to aid, support and promote teaching, research, and service in the various educational, scientific, scholarly, professional, artistic, and creative endeavors of the University. Because the elected directors of the Foundation are appointed by the members of the Elizabeth City State University Board of Trustees and the Foundation's sole purpose is to benefit Elizabeth City State University, its financial statements have been blended with those of the University.

Separate financial statements for the Foundation may be obtained from the University Controller's Office, 1704 Weeksville Road, Elizabeth City,

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NC 27909, or by calling (252)-335-3224. Other related foundations and similar nonprofit corporations for which the University is not financially accountable are not part of the accompanying financial statements.

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

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.

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

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

- D. Cash and Cash Equivalents** – This classification includes undeposited receipts, petty cash, cash on deposit with private bank accounts, savings accounts, money market accounts, cash on deposit with fiscal agents, and deposits held by the State Treasurer in the short-term investment portfolio. The short-term investment portfolio maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit and withdraw cash at any time without prior notice or penalty.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

- E. Investments** - This classification includes long-term fixed income investments 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 the federal government, State and local governments, private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants, and pledges that are verifiable, measurable, and expected to be collected and available for expenditures for which the resource provider's conditions have been satisfied. Receivables are recorded net of estimated uncollectible amounts.

- G. Inventories** – Inventories, consisting of expendable supplies, are valued at cost using the first-in, first-out method. Merchandise for resale is valued using the retail inventory method.

- H. Capital Assets** – Capital assets are stated at cost at date of acquisition or fair value at date of donation in the case of gifts. The value of assets constructed includes all material direct and indirect construction costs. Interest costs incurred are capitalized during the period of construction.

The University capitalizes assets that have a value or cost in excess of \$5,000 at the date of acquisition and an expected useful life of more than one year. Library books are generally not considered to have a useful life of more than one year unless part of a collection and are expensed in the year of acquisition.

Depreciation is computed using the straight-line and/or units of output method over the estimated useful lives of the assets, generally 25 years for general infrastructure, 50 years for buildings, and 15 years for equipment.

- 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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

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

- K. Compensated Absences** - The University's policy is to record the cost of vacation leave when earned. The policy provides for a maximum accumulation of unused vacation leave of 30 days which can be carried forward each January 1 or for which an employee can be paid upon termination of employment. Also, any accumulated vacation leave in excess of 30 days at yearend 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.

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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

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

Restricted and unrestricted resources are tracked using a fund accounting system and are spent in accordance with established fund authorities. Fund authorities provide rules for the fund activity and are separately established for restricted and unrestricted activities. When both restricted and unrestricted funds are available for expenditure, the decision for funding is transactional based within the departmental management system in place at the University. For projects funded by tax-exempt debt proceeds and other sources, the debt proceeds are always used first.

M. Scholarship Discounts – Student tuition and fees revenues and certain other revenues from University charges are reported net of scholarship discounts in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. The scholarship discount is the difference between the actual charge for goods and services provided by the University and the amount that is paid by students or by third parties on the students' behalf. Student financial assistance grants, such as Pell grants, and other federal, State, or nongovernmental programs, are recorded as either operating or nonoperating revenues in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. To the extent that revenues from these programs are used to satisfy tuition, fees, and other charges, the University has recorded a scholarship discount.

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting.

Nonoperating revenues include activities that have the characteristics of nonexchange transactions. Revenues from nonexchange transactions and State appropriations that represent subsidies or gifts to the University, as well as investment income, are considered nonoperating since these are either investing, capital or noncapital financing activities. Capital contributions are presented separately after nonoperating revenues and expenses.

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

NOTE 2 - DEPOSITS AND INVESTMENTS

- A. Deposits** – Unless specifically exempt, the University is required by *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, except for funds received for services rendered by health care professionals, with the State Treasurer. Although specifically exempted, the University may voluntarily deposit endowment funds, special funds, revenue bond proceeds, debt service funds, and funds received for services rendered by health care professionals with the State Treasurer. Special funds consist of moneys for intercollegiate athletics and agency funds held directly by the University.

At June 30, 2005, the University's deposit with the State Treasurer's Short-Term Investment Fund totaled \$9,681,710.50. The Short-Term Investment Fund (a portfolio within the State Treasurer's Investment Pool, an external investment pool that is not registered with the Securities and Exchange Commission and does not have a credit rating) had a weighted average maturity of 1.41 years as of June 30, 2005. Assets and

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

shares of the Short-Term Investment Fund are valued at amortized cost, which approximates fair value. 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 was \$109,476.70 and the bank balance was \$232,727.19. 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>63,525.80</u>
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- 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 and funds received for services rendered by health care professionals 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 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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 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. Fund ownership is measured using the unit value method. Under this method, each participating fund's investment balance is determined on a market value basis. 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 variances affect the fair value of investments. The University's Endowment Board does not have a formal investment policy that addresses interest rate risk.

Long-Term Investment Pool

	Fair Value
Other Securities	
Money Market Funds	\$ 2,383,725.09

Credit Risk: The University's Endowment Board does not have a formal policy that addresses credit risk. As of June 30, 2005, the investments in the Long-Term Investment Pool were unrated.

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. At June 30, 2005, the University did not have any investments requiring disclosure of custodial credit risk.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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. At June 30, 2005, the University did not have any investments requiring disclosure of foreign currency risk.

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	<u>Fair Value</u>	<u>Investment Maturities (in Years) Less Than 1</u>
Debt Securities		
U.S. Treasuries	\$ 263,178.13	<u>\$ 263,178.13</u>
Other Securities		
Money Market Funds	<u>1,838,797.20</u>	
Total Long-Term Investment Pool	<u>\$ 2,101,975.33</u>	

Credit Risk: The University does not have a formal policy that addresses credit risk. As of June 30, 2005, the University's non-pooled investments were unrated.

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 formal policy for custodial credit risk. The University's non-pooled investments were exposed to custodial credit risk as follows:

<u>Investment Type</u>	<u>Held by Counterparty</u>
U.S. Treasuries	<u>\$ 263,178.13</u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 3 - ENDOWMENT INVESTMENTS

Investments of the University's endowment funds are pooled, unless required to be separately invested by the donor. If a donor has not provided specific instructions, State law permits the Board of Trustees to authorize for expenditure the net appreciation, realized and unrealized, of the investments of the endowment funds.

Investment return of the University's endowment funds is predicated on the total return concept (yield plus appreciation). Annual payouts from the University's endowment funds are based on an adopted spending policy which limits spending between 0% and 5% of the endowment principal's market value. Under this policy, the prior year spending percentage is increased by the inflation rate to determine the current year spending percentage. 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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 4 - RECEIVABLES

Receivables at June 30, 2005, were as follows:

	Gross Receivables	Less Allowance for Doubtful Accounts	Net Receivables
Current Receivables:			
Students	\$ 768,720.23	\$ 75,026.69	\$ 693,693.54
Accounts	127,053.03		127,053.03
Intergovernmental	2,190,560.31		2,190,560.31
Pledges	110,355.07		110,355.07
Investment Earnings	17,105.64		17,105.64
Interest on Loans	302,165.44		302,165.44
Other	305,112.43		305,112.43
Total Current Receivables	\$ 3,821,072.15	\$ 75,026.69	\$ 3,746,045.46
Notes Receivable:			
Notes Receivable - Current:			
Federal Loan Programs	\$ 70,398.02	\$ 0.00	\$ 70,398.02
Institutional Student Loan Programs	17,537.78		17,537.78
Total Notes Receivable - Current	\$ 87,935.80	\$ 0.00	\$ 87,935.80
Notes Receivable - Noncurrent:			
Federal Loan Programs	\$ 825,177.95	\$ 416,562.21	\$ 408,615.74
Institutional Student Loan Programs	203,620.16	21,000.00	182,620.16
Total Notes Receivable - Noncurrent	\$ 1,028,798.11	\$ 437,562.21	\$ 591,235.90

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	\$ 1,654,818.66	\$ 0.00	\$ 0.00	\$ 0.00	\$ 1,654,818.66
Construction in Progress	33,768,747.73	(19,694,266.71)	11,733,350.00	17,400.00	25,790,431.02
Total Capital Assets, Nondepreciable	<u>35,423,566.39</u>	<u>(19,694,266.71)</u>	<u>11,733,350.00</u>	<u>17,400.00</u>	<u>27,445,249.68</u>
Capital Assets, Depreciable:					
Buildings	61,931,763.73	16,364,076.45			78,295,840.18
Machinery and Equipment	7,601,479.81	464,016.58	513,618.09	377,385.28	8,201,729.20
General Infrastructure	3,369,373.81	2,978,393.68			6,347,767.49
Total Capital Assets, Depreciable	<u>72,902,617.35</u>	<u>19,806,486.71</u>	<u>513,618.09</u>	<u>377,385.28</u>	<u>92,845,336.87</u>
Less Accumulated Depreciation/Amortization for:					
Buildings	18,279,789.81	112,220.00	1,265,531.35		19,657,541.16
Machinery and Equipment	5,063,444.11		538,263.46	360,550.20	5,241,157.37
General Infrastructure	400,836.59		109,969.65		510,806.24
Total Accumulated Depreciation	<u>23,744,070.51</u>	<u>112,220.00</u>	<u>1,913,764.46</u>	<u>360,550.20</u>	<u>25,409,504.77</u>
Total Capital Assets, Depreciable, Net	<u>49,158,546.84</u>	<u>19,694,266.71</u>	<u>(1,400,146.37)</u>	<u>16,835.08</u>	<u>67,435,832.10</u>
Capital Assets, Net	<u>\$ 84,582,113.23</u>	<u>\$ 0.00</u>	<u>\$ 10,333,203.63</u>	<u>\$ 34,235.08</u>	<u>\$ 94,881,081.78</u>

NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

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

	Amount
Accounts Payable	\$ 1,144,967.27
Accrued Payroll	463,417.20
Contract Retainage	103,140.81
Intergovernmental Payables	32,716.36
Total Accounts Payable and Accrued Liabilities	<u>\$ 1,744,241.64</u>

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	\$ 20,685,000.00	\$ 0.00	\$ 555,000.00	\$ 20,130,000.00	\$ 560,000.00
Add/Deduct Premium/Discount	21,117.54	5,351.74	7,666.00	18,803.28	
Deduct Deferred Charge on Refunding	(86,236.28)	3,749.40		(82,486.88)	
Total Bonds Payable	20,619,881.26	9,101.14	562,666.00	20,066,316.40	560,000.00
Compensated Absences	1,841,444.80	1,133,688.00	1,108,071.47	1,867,061.33	157,728.44
Total Long-Term Liabilities	\$ 22,461,326.06	\$ 1,142,789.14	\$ 1,670,737.47	\$ 21,933,377.73	\$ 717,728.44

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

Purpose	Series	Interest Rate/ Ranges	Final Maturity Date	Original Amount of Issue	Principal Paid Through 06/30/2005	Principal Outstanding 06/30/2005
Dormitory System Revenue Bonds of 1981						
Wamack Hall and Mitchell-Lewis Hall	A	3.00%	10/01/2017	\$ 675,000.00	\$ 385,000.00	\$ 290,000.00
Wamack Hall and Mitchell-Lewis Hall	B	3.00%	10/01/2020	1,680,000.00	755,000.00	925,000.00
Total Dormitory System Revenue Bonds of 1981				2,355,000.00	1,140,000.00	1,215,000.00
Educational Facilities Revenue Bonds						
Elizabeth City State University Housing Foundation	A	2.00%-5.25%	06/01/2033	13,895,000.00		13,895,000.00
Elizabeth City State University Housing Foundation	B	2.75%	06/01/2005	260,000.00	260,000.00	
Total Educational Facilities Revenue Bonds				14,155,000.00	260,000.00	13,895,000.00
The University of North Carolina System Pool Revenue Bonds						
Refinance of Dormitory-200 Bed (1992 - Series C Bonds)	B	3.5%-5.375%	04/01/2027	3,410,000.00	308,877.00	3,101,123.00
Bedell Cafeteria Renovation	B	3.5%-5.375%	04/01/2027	1,225,000.00	110,960.00	1,114,040.00
Dormitory Furniture	B	3.5%-5.375%	04/01/2027	885,000.00	80,163.00	804,837.00
Total The University of North Carolina System Pool Revenue Bonds				5,520,000.00	500,000.00	5,020,000.00
Total Bonds Payable (principal only)				\$ 22,030,000.00	\$ 1,900,000.00	20,130,000.00
Less: Unamortized Loss on Refunding						(82,486.88)
Less: Unamortized Discount						(149,848.77)
Plus: Unamortized Premium						168,652.05
Total Bonds Payable						\$ 20,066,316.40

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>	<u>Annual Requirements</u>	
	<u>Bonds Payable</u>	
	<u>Principal</u>	<u>Interest</u>
2006	\$ 560,000.00	\$ 808,896.89
2007	585,000.00	797,559.39
2008	610,000.00	784,384.39
2009	630,000.00	769,309.38
2010	650,000.00	752,384.38
2011-2015	3,740,000.00	3,432,245.02
2016-2020	4,100,000.00	2,696,303.76
2021-2025	3,120,000.00	1,959,425.00
2026-2030	3,620,000.00	1,170,250.00
2031-2035	2,515,000.00	255,500.00
Total Requirements	<u>\$ 20,130,000.00</u>	<u>\$ 13,426,258.21</u>

NOTE 8 - OPERATING LEASE OBLIGATIONS

The University entered into operating leases for equipment. 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>\$ 65,404.58</u>

Rental expense for all operating leases during the year was \$ 298,763.60.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 9 - REVENUES

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

	Gross Revenues	Internal Sales Eliminations	Less Scholarship Discounts	Less Allowance for Uncollectibles	Net Revenues	Revenues Pledged as Security for Debt
Operating Revenues:						
Student Tuition and Fees	\$ 9,306,343.42	\$ 0.00	\$ 4,083,936.35	\$ 65,141.00	\$ 5,157,266.07	\$ 0.00
Sales and Services:						
Sales and Services of Auxiliary Enterprises:						
Residential Life	\$ 2,855,127.00	\$ 0.00	\$ 1,359,112.00	\$ 27,409.00	\$ 1,468,606.00	\$ 1,468,606.00 (A)
Dining	1,744,521.02		830,435.78	17,787.00	896,298.24	
Viking Village	1,281,943.00		610,237.00	18,768.00	652,938.00	652,938.00 (B)
Bookstore Book Rental	708,763.00		337,388.00	7,699.00	363,676.00	
Other	959,645.79	327,522.86		7,518.00	624,604.93	
Total Sales and Services	<u>\$ 7,549,999.81</u>	<u>\$ 327,522.86</u>	<u>\$ 3,137,172.78</u>	<u>\$ 79,181.00</u>	<u>\$ 4,006,123.17</u>	<u>\$ 2,121,544.00</u>

Revenue Bonds Secured by Pledged Revenues:

- (A) Dormitory System Revenue Bonds of 1981 A and B
- (B) Elizabeth City State University Housing Foundation A and B

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	\$ 12,160,115.29	\$ 549,928.23	\$ 627,018.57	\$ 0.00	\$ 0.00	\$ 0.00	\$ 13,337,062.09
Research	388,553.75	83,556.60	177,676.77				649,787.12
Public Service	950,807.16	48,962.63	623,299.37				1,623,069.16
Academic Support	3,087,682.32	997,537.93	649,389.90				4,734,610.15
Student Services	2,735,305.05	315,887.51	818,279.38				3,869,471.94
Institutional Support	5,553,713.94	253,198.33	2,203,451.18				8,010,363.45
Operations and Maintenance of Plant	3,298,868.51	825,748.81	1,288,643.46		1,520,364.69		6,933,625.47
Student Financial Aid				1,494,577.63			1,494,577.63
Auxiliary Enterprises	2,424,066.30	1,039,385.34	3,834,176.76		590,329.07		7,887,957.47
Depreciation						2,025,984.46	2,025,984.46
Total Operating Expenses	<u>\$ 30,599,112.32</u>	<u>\$ 4,114,205.38</u>	<u>\$ 10,221,935.39</u>	<u>\$ 1,494,577.63</u>	<u>\$ 2,110,693.76</u>	<u>\$ 2,025,984.46</u>	<u>\$ 50,566,508.94</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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 \$25,538,543.82, of which \$18,134,292.33 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were \$1,088,057.54 and \$393,514.44, respectively. The University made 100% of its annual required contributions for the years ended June 30, 2005, 2004, and 2003, which were \$393,514.44, \$38,280.30, 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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 \$25,538,543.82, of which \$3,629,136.16 was covered under the Optional Retirement Program. Total employee and employer contributions for pension benefits for the year were \$217,748.17 and \$248,232.91, 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 \$37,400.00 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%

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 \$19,703.41. The voluntary contributions by employees amounted to \$189,791.00 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 \$179,354.92 for the year ended June 30, 2005.

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 \$696,429.71. 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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 \$96,847.26. The University assumes no liability for long-term disability benefits under the Plan other than its contribution. Additional detailed information about the DIPNC is disclosed in the State of North Carolina's *Comprehensive Annual Financial Report*.

NOTE 13 - RISK MANAGEMENT

The University is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These exposures to loss are handled via a combination of methods, including participation in State-administered insurance programs, purchase of commercial insurance, and self-retention of certain risks. There have been no significant reductions in insurance coverage from the previous year and settled claims have not exceeded coverage in any of the past three fiscal years.

Tort claims of up to \$500,000 are self-insured under the authority of the State Tort Claims Act. In addition, the State provides excess public officers' and employees' liability insurance up to \$5,000,000 via contract with a private insurance company. The University pays the premium, based on a composite rate, directly to the private insurer.

The University is required to maintain fire and lightning coverage on all State-owned buildings and contents through the State Property Fire Insurance Fund (Fund), an internal service fund of the State. Such coverage is provided at no cost to operations supported by the State's General Fund. Other operations not supported by the State's General Fund are charged for the coverage. Losses covered by the Fund are subject to a \$500 per occurrence deductible. The University also purchased through the Fund extended coverage for buildings and contents to cover windstorm, explosions or damage caused by vehicle or aircraft impacts. The extended coverage applies to all campus buildings and contents with coverage amounts varying based on the value of each building and its contents.

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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. 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 \$3,933,761.47 at June 30, 2005.
- B. **Pending Litigation and Claims** – The University is a party to litigation and claims in the ordinary course of its operations. Since it is not possible to predict the ultimate outcome of these matters, no provision for any

NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)

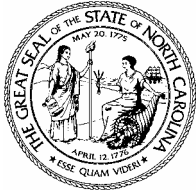
liability has been made in the financial statements. University management is of the opinion that the liability, if any, for any of these matters will not have a material adverse effect on the financial position of the University.

- C. University Improvement General Obligation Bonds** – The 1999-2000 Session of the General Assembly of North Carolina authorized the issuance of \$2.5 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 \$13,717,015.51 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.

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

Board of Trustees
Elizabeth City State University
Elizabeth City, North Carolina

We have audited the financial statements of Elizabeth City 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, as of and for the year ended June 30, 2005, and have issued our report thereon dated May 11, 2006. We did not audit the financial statements of Elizabeth City State University Foundation, Inc. and Subsidiary, which represent 15 percent, four percent, and three percent, respectively, of the assets, net assets, and revenues of the University. 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 Elizabeth City State University Foundation, Inc. and Subsidiary, 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 Elizabeth City State University Foundation, Inc. and Subsidiary were not audited in accordance with *Government Auditing Standards*, and accordingly, this report does not extend to the Foundation.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the University's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material

**INDEPENDENT AUDITOR'S REPORT
ON INTERNAL CONTROL OVER FINANCIAL REPORTING
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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

May 11, 2006

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