



STATE OF NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT OF

NORTH CAROLINA CENTRAL UNIVERSITY

DURHAM, 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

NORTH CAROLINA CENTRAL UNIVERSITY

DURHAM, NORTH CAROLINA

FOR THE YEAR ENDED JUNE 30, 2005

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THE UNIVERSITY OF NORTH CAROLINA

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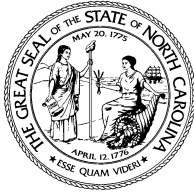
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STATE OF NORTH CAROLINA
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AUDITOR'S TRANSMITTAL

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

We have completed a financial statement audit of North Carolina Central 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

March 9, 2007

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
North Carolina Central University
Durham, North Carolina

We have audited the accompanying financial statements of North Carolina Central 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 the North Carolina Central 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 the NCCU Real Estate Foundation, Inc., which represent 8.4 percent, (0.34) percent, and 0.89 percent, respectively, of the assets, net assets and revenues of the University; nor the financial statements of the NCCU Foundation, Inc., which represent 100% of the University's discretely presented component unit. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for those entities, is based on the reports 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 the NCCU Real Estate Foundation, Inc., and the NCCU Foundation, Inc., were not audited in accordance with *Governmental 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 reports of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of North Carolina Central University and its discretely presented component unit as of

INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

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.

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 January 31, 2007, 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

January 31, 2007

NORTH CAROLINA CENTRAL UNIVERSITY MANAGEMENT'S DISCUSSION AND ANALYSIS

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

Brief Institutional Highlights

Academically, a new degree program and a new concentration in the School of Education's Birth to Kindergarten Master of Arts in Teaching program and the Department of Criminal Justice's Homeland Security Studies, respectively, were approved and developed. The Athletic Training Education Program received the first ever accreditation among Historically Black Colleges or Universities. The School of Education established Project LEAP (Lateral Entry Alternative Programs), which provides full services to licensure only and lateral entry teachers. The School of Education has also been selected as an implementation site for three national projects, one of which involves collaboration among 15 universities designed to assist students with the technology component in the Master of School Administration program. Lastly, the University launched the New Birth College Program at the New Birth Missionary Baptist Church in Lithonia, Ga. This program offers undergraduate studies in hospitality and tourism, business administration, and criminal justice.

The University was allocated \$121 million from the State's Higher Education Bond Referendum in 2001. These bond monies are being used to renovate existing buildings and build new housing and academic structures. During 2004-2005, several bond projects were completed including the Graduate Apartments, New Baynes Residence Hall, and the renovation and expansion of the Annie Day Shepard Residence Hall.

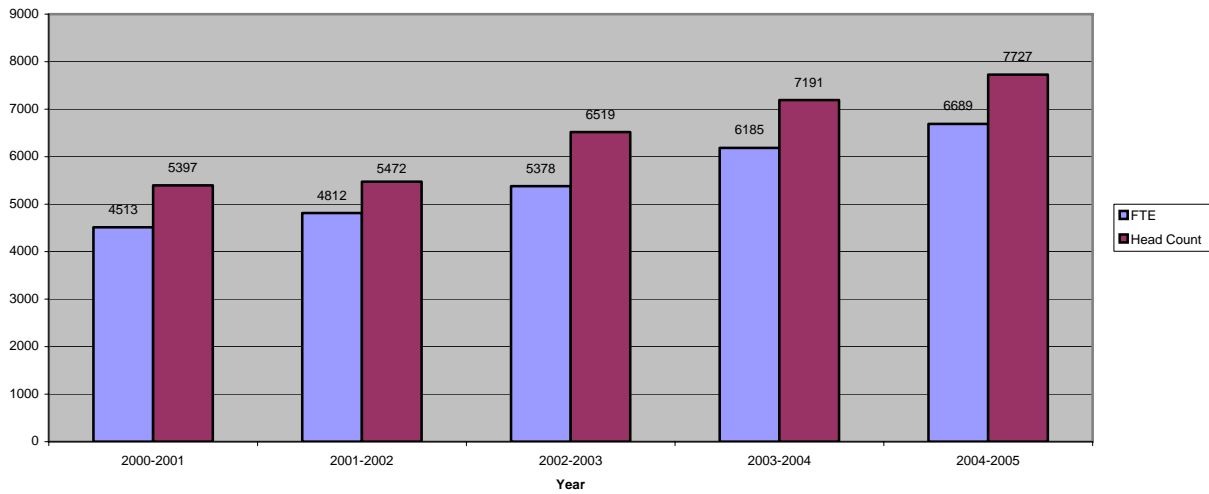
State appropriations, including reversions, were cut by approximately \$1.8 million as compared to \$2.8 million in fiscal year 2004. Despite the budget reduction, the University has managed to protect academic programs, student services, and avoid negative personnel actions. This was made possible through attrition and other non-State funds.

Sponsored research dollars remain strong; by the end of fiscal year 2005, the University's research and other grant awards were \$62.5 million. The Office of Institutional Advancement had significant successes in fundraising by securing funds from the Wachovia Foundation (\$1 million), and several other corporations and foundations.

Student enrollment increased 7.5% in fall 2004, totaling 7,727 in comparison to the 7,191 students enrolled in fall 2003. The University continues to strive to recruit talented students. In the fall of 2004, the University enrolled four National Achievement finalists, seven semifinalists, and two National Merit semifinalists.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

FTE and Head Count from 2000 to 2005



Financial Highlights

	<u>2005</u>	<u>2004</u>
Assets		
Current Assets	\$ 40,031,513	\$ 58,251,405
Capital Assets, Net	168,581,036	122,107,018
Other Assets	41,999,228	20,911,468
Total Assets	<u>250,611,777</u>	<u>201,269,891</u>
Liabilities		
Current Liabilities	34,792,301	11,454,622
Noncurrent Liabilities	16,883,908	38,464,719
Total Liabilities	<u>51,676,209</u>	<u>49,919,341</u>
Net Assets		
Invested in Capital Assets, Net of Capital Related Debt	136,350,884	98,568,213
Restricted - Expendable	30,406,017	22,265,357
Restricted - Nonexpendable	10,433,593	10,050,042
Unrestricted	21,745,074	20,466,938
Total Net Assets	<u>\$ 198,935,568</u>	<u>\$ 151,350,550</u>

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

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

total liabilities. The reader may use the net assets to gauge the financial position of the University as of June 30, 2005.

As of June 30, 2005, the University's total assets were \$250.6 million as compared to \$201.3 million in the prior year, an increase of \$49.3 million. This increase is attributable to the growth in buildings for \$46.5 million. This increase is consistent with all of the bond projects being fully under construction and/or completed.

The University's liabilities totaled \$51.6 million in 2005, and \$49.9 million in 2004, with the debt service on housing and stadium bonds comprising \$31.2 million (current and noncurrent portions).

The total current liability of \$34.8 million is well covered (1.15 times) by current assets of \$40 million, which indicates the University's ability to pay current liabilities as they become due. Total net assets are \$198.9 million, which is an increase of \$47.6 million from the prior year.

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

	2005	2004
Operating Revenues		
Student Tuition and Fees, Net	\$ 23,667,231	\$ 19,226,865
Contracts and Grants	20,908,246	19,365,773
Sales and Services, Net	15,019,102	11,416,880
Other Operating Revenues	308,543	923,998
Total Operating Revenues	59,903,122	50,933,516
Operating Expenses	129,557,707	121,047,154
Operating Loss	(69,654,585)	(70,113,638)
Nonoperating Revenues and Expenses		
State Appropriations	53,515,638	48,006,532
Noncapital Grants	7,398,769	14,929,707
Noncapital Gifts	64,283	112,812
Investment Income, Net	1,727,863	1,732,939
Other Nonoperating Expenses	(1,885,481)	(1,138,434)
Loss Before other Revenues	(8,833,513)	(6,470,082)
Capital Appropriations	9,984,642	181,500
Capital Grants	46,433,889	37,726,163
Total Other Revenues	56,418,531	37,907,663
Increase in Net Assets	47,585,018	31,437,581
Net Assets - Beginning of Year	151,350,550	119,912,969
Net Assets - End of Year	\$ 198,935,568	\$ 151,350,550

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

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

Operating revenues increased by \$9 million when compared to 2004. The contributing factors to this increase were the increases in student enrollment coupled with higher tuition (\$225 in-State and \$300 out-of-State increase).

Operating expenses increased by \$8.5 million when compared to 2004. Salaries and benefits for University employees, supplies and materials, and scholarships and fellowships were the major components of this increase in the amounts of \$5.3 million, \$5.3 million, and \$2.8 million, respectively. Services expenses declined by \$5.5 million mostly due to more dormitory space being inhabitable for on-campus living, which drastically cut the cost of renting off-campus housing for our students.

Overall, the University sustained a total operating loss of \$69.7 million in the current fiscal year, which is \$459,000 less than the loss in fiscal year 2004. Operating losses are likely to continue due, in part, to the accounting requirement to categorize State appropriations (a major source of funding) as nonoperating revenues. In 2005, State appropriations were \$53.5 million.

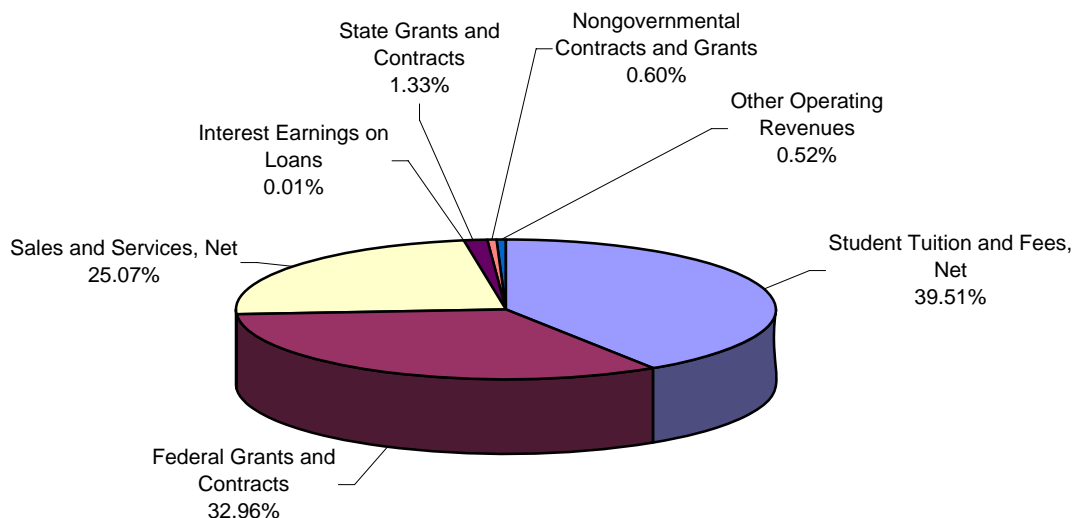
Nonoperating revenues and expenses stem from transactions that occur outside of the primary scope of the University's existence and for which no goods or services are provided. State appropriations, capital grants, noncapital grants and gifts, investment income/expenses, and capital-related interest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

Of the nonoperating revenues (\$60.8 million), there were noticeable changes in the State appropriations and noncapital grants. State appropriations increased by \$5.5 million as a result of enrollment growth and special academic initiative funds. Noncapital grants decreased by \$7.5 million mainly as a result of not having any repair and renovation cost to recognize as revenue that was paid on the University's behalf by the State as in the prior year.

Capital appropriations and capital grants increased by \$9.8 and \$8.7 million, respectively. These increases are a direct result of all bond funded projects being well underway with designs, renovations, and/or construction; therefore, the University was able to draw on the allotted bond funds available.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Operating Revenues by Source



North Carolina Central University Condensed Statement of Cash Flows

	2005	2004
Cash Provided (Used by):		
Operating Activities	\$ (64,504,725)	\$ (60,285,520)
Noncapital Financing Activities	61,046,903	53,939,666
Capital Financing Activities	10,061,378	5,346,142
Investing Activities	9,941,778	(6,445,501)
Net Increase (Decrease) in Cash and Cash Equivalents	16,545,334	(7,445,213)
Cash and Cash Equivalents- Beginning of Year	18,726,480	26,171,693
Cash and Cash Equivalents - End of Year	<u>\$ 35,271,814</u>	<u>\$ 18,726,480</u>

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

The net cash used by operating activities shows a net outflow of funds of \$64.5 million, which is a 7% increase from 2004. The major outflows were payments to employees for

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONCLUDED)

services (\$67 million), vendors for goods and services (\$53 million), and students for educational assistance (\$5.8 million). The major sources of operating inflows were student tuition and fees (\$23.6 million), auxiliary sales (\$15 million), and federal contracts/grants (\$19.7 million).

The net cash provided by noncapital financing activities is an inflow of \$61 million, which is a 13% increase over 2004. State appropriations of \$53.5 million account for the bulk of this inflow.

Cash flow from capital and related financing activities is a net inflow of \$10 million, which is an 88% increase over 2004. The net inflow results from proceeds from capital grants of \$51 million and State capital appropriations of \$10 million related to the 2001 State bond program. The University expended \$45.6 million for capital assets. The major capital expenses related to the construction and/or renovation of new dormitories (Baynes Hall replacement, Annie Day Shepard, Eagle Landing) in the amount of \$16 million and the Science Complex for \$19.8 million.

The University has a net cash inflow from investing activities of \$9.9 million which is a 254% increase from 2004. This results from \$8.1 million in proceeds from sales and maturities of investments, investment income of \$1.8 million, and outflows from purchases of investments and related fees of \$45,230.

In summary, the cash position of the University increased by \$16,545,334 or 88%.

Economic Outlook

The outlying years appear to be promising. Student enrollment continues to increase. The enrollment for 2005-2006 reached another all-time high of 8,219. The University expects enrollment to maintain. Moreover, for fiscal year 2005-2006, the State legislature approved a \$300 tuition increase for all but in-State undergraduates; therefore, projected tuition and fee revenues look favorable.

In 2005-2006, the University will again be eligible to receive "enrollment growth" monies of \$3.2 million resulting from the increase in enrollment in 2004. These "growth" funds will allow the University to continue providing academic and administrative services.

North Carolina Central University's faculty is steadily writing, applying, and receiving research grant funds to augment State funding. Research is one of three components that faculty must strive to accomplish. The Sponsored Research Office works diligently with faculty to provide ongoing training and opportunities for research. Through our dedicated faculty and staff, we will continue to fulfill our mission of serving the State, nation, and the world through teaching, research, and service.

North Carolina Central University
Statement of Net Assets
June 30, 2005

Exhibit A-1

ASSETS

Current Assets:

Cash and Cash Equivalents	\$ 21,964,699
Restricted Cash and Cash Equivalents	6,166,342
Restricted Short-Term Investments	2,194,896
Receivables, Net (Note 4)	9,043,468
Due from State of North Carolina Component Units	175,459
Inventories	306,990
Notes Receivable, Net (Note 4)	176,659
Other Assets	3,000
	<hr/>
Total Current Assets	40,031,513
	<hr/>

Noncurrent Assets:

Restricted Cash and Cash Equivalents	7,140,773
Restricted Due from Primary Government	2,246,931
Due from State of North Carolina Component Units	17,300,000
Endowment Investments	12,164,269
Other Long-Term Investments	138,982
Notes Receivable, Net (Note 4)	3,008,273
Capital Assets - Nondepreciable (Note 5)	38,132,224
Capital Assets - Depreciable, Net (Note 5)	130,448,812
	<hr/>
Total Noncurrent Assets	210,580,264
	<hr/>
Total Assets	250,611,777
	<hr/>

LIABILITIES

Current Liabilities:

Accounts Payable and Accrued Liabilities (Note 6)	11,078,327
Due to Primary Government	37,377
Deferred Revenue	1,312,832
Interest Payable	114,847
Long-Term Liabilities - Current Portion (Note 7)	22,248,918
	<hr/>
Total Current Liabilities	34,792,301
	<hr/>

Noncurrent Liabilities:

Deposits Payable	400
Funds Held for Others	93,853
U. S. Government Grants Refundable	2,736,947
Long-Term Liabilities (Note 7)	14,052,708
	<hr/>
Total Noncurrent Liabilities	16,883,908
	<hr/>
Total Liabilities	51,676,209
	<hr/>

North Carolina Central University
Statement of Net Assets
June 30, 2005

Exhibit A-1
Page 2

NET ASSETS

Invested in Capital Assets, Net of Related Debt	136,350,884
Restricted for:	
Nonexpendable:	
Scholarships and Fellowships	4,018,145
Endowed Professorships	5,692,801
Loans	722,647
Expendable:	
Scholarships and Fellowships	425,845
Research	268,787
Endowed Professorships	2,161,427
Departmental Uses	18,451,589
Capital Projects	7,757,692
Debt Service	1,283,473
Other	57,204
Unrestricted	<u>21,745,074</u>
Total Net Assets	<u><u>\$ 198,935,568</u></u>

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

***North Carolina Central University
Statement of Revenues, Expenses, and
Changes in Net Assets
For the Fiscal Year Ended June 30, 2005***

Exhibit A-2

REVENUES

Operating Revenues:

Student Tuition and Fees, Net (Note 9)	\$ 23,667,231
Federal Grants and Contracts	19,749,956
State and Local Grants and Contracts	798,210
Nongovernmental Grants and Contracts	360,080
Sales and Services, Net (Note 9)	15,019,102
Interest Earnings on Loans	7,310
Other Operating Revenues	301,233

Total Operating Revenues	59,903,122
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EXPENSES

Operating Expenses:

Salaries and Benefits	66,789,317
Supplies and Materials	23,347,175
Services	26,328,055
Scholarships and Fellowships	5,826,623
Utilities	3,088,893
Depreciation	4,177,644

Total Operating Expenses	129,557,707
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Operating Loss	(69,654,585)
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NONOPERATING REVENUES (EXPENSES)

State Appropriations	53,515,638
Noncapital Grants	7,398,769
Noncapital Gifts, Net	64,283
Investment Income (Net of Investment Expense of \$45,230)	1,727,863
Interest and Fees on Debt	(941,963)
Other Nonoperating Expenses	(943,518)

Net Nonoperating Revenues	60,821,072
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Income Before Other Revenues, Expenses, Gains, or Losses	(8,833,513)
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Capital Appropriations	9,984,642
Capital Grants	46,433,889

Increase in Net Assets	47,585,018
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NET ASSETS

Net Assets - July 1, 2004	151,350,550
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Net Assets - June 30, 2005	\$ 198,935,568
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The accompanying notes to the financial statements are an integral part of this statement.

North Carolina Central University
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2005

Exhibit A-3

CASH FLOWS FROM OPERATING ACTIVITIES

Received from Customers	\$ 61,968,980
Payments to Employees and Fringe Benefits	(66,885,241)
Payments to Vendors and Suppliers	(52,991,080)
Payments for Scholarships and Fellowships	(5,826,623)
Loans Issued	(360,000)
Collection of Loans	372,037
Other Payments	(782,798)
	<hr/>
Net Cash Used by Operating Activities	(64,504,725)

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

State Appropriations	53,515,638
Noncapital Grants	8,410,500
Noncapital Gifts	64,283
William D. Ford Direct Lending Receipts	47,103,227
William D. Ford Direct Lending Disbursements	(47,103,227)
Other Payments	(943,518)
	<hr/>
Net Cash Provided by Noncapital Financing Activities	61,046,903

CASH FLOWS FROM CAPITAL FINANCING AND RELATED FINANCING ACTIVITIES

State Capital Appropriations	9,984,642
Capital Grants	51,032,318
Proceeds from Sale of Capital Assets	15,168
Acquisition and Construction of Capital Assets	(45,579,109)
Principal Paid on Capital Debt and Leases	(471,908)
Interest and Fees Paid on Capital Debt and Leases	(4,919,733)
	<hr/>
Net Cash Provided by Capital Financing and Related Financing Activities	10,061,378

CASH FLOWS FROM INVESTING ACTIVITIES

Proceeds from Sales and Maturities of Investments	8,173,853
Investment Income	1,813,155
Purchase of Investments and Related Fees	(45,230)
	<hr/>
Net Cash Provided by Investing Activities	9,941,778

Net Increase in Cash and Cash Equivalents	16,545,334
Cash and Cash Equivalents - July 1, 2004	18,726,480
	<hr/>
Cash and Cash Equivalents - June 30, 2005	\$ 35,271,814

North Carolina Central 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 PROVIDED (USED) BY OPERATING ACTIVITIES**

Operating Loss	\$	(69,654,585)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:		
Depreciation Expense		4,177,644
Allowances, Write-Offs, and Amortizations		(627,864)
Nonoperating Other Income (Expenses)		(958,686)
Changes in Assets and Liabilities:		
Receivables (Net)		1,405,603
Inventories		(64,499)
Accounts Payable and Accrued Liabilities		599,403
Due to Primary Government		(27,091)
Deferred Revenue		602,379
Compensated Absences		(25,659)
Deposits Payable		68,630
		<hr/>
Net Cash Used by Operating Activities	\$	<u><u>(64,504,725)</u></u>

RECONCILIATION OF CASH AND CASH EQUIVALENTS

Current Assets:		
Cash and Cash Equivalents	\$	21,964,699
Restricted Cash and Cash Equivalents		6,166,342
Noncurrent Assets:		
Restricted Cash and Cash Equivalents		7,140,773
		<hr/>
Total Cash and Cash Equivalents - June 30, 2005	\$	<u><u>35,271,814</u></u>

NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES

Assets Acquired through the Assumption of a Liability	\$	1,252,200
Assets Acquired through a Gift		10,000
Change in Fair Value of Investments		504,472
Loss on Disposal of Capital Assets		74,069

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

North Carolina Central University Foundation, Inc.
Statement of Financial Position
June 30, 2005

Exhibit B-1

ASSETS

Cash and Cash Equivalents	\$	1,966,630
Contributions Receivable, Net		1,124,550
Investments		7,861,630
Cash Surrender Value of Life Insurance		<u>35,363</u>
Total Assets		<u>10,988,173</u>

LIABILITIES

Accounts Payable, Related Party		75,426
Accounts Payable and Accrued Expenses		10,784
Funds Held on Behalf of Others		<u>1,428,509</u>
Total Liabilities		<u>1,514,719</u>

NET ASSETS

Unrestricted		7,927
Temporarily Restricted		3,889,044
Permanently Restricted		<u>5,576,483</u>
Total Net Assets	\$	<u><u>9,473,454</u></u>

See Note 1 in the Notes to the Financial Statements

North Carolina Central University Foundation, Inc.
Statement of Activities
For the Fiscal Year Ended June 30, 2005

Exhibit B-2

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
REVENUES				
Revenues, Gains, and Other Support				
Contributions	\$ 7,392	\$ 1,455,930	\$ 354,134	\$ 1,817,456
Interest and Dividends	6,770	121,805		128,575
Realized and Unrealized Gains on Investments	8,440	300,242		308,682
Other Income	84,234	84,476		168,710
Net Assets Released from Donor Restrictions	<u>1,464,757</u>	<u>(1,464,757)</u>		
Total Revenues, Gains, and Other Support	<u>1,571,593</u>	<u>497,696</u>	<u>354,134</u>	<u>2,423,423</u>
EXPENSES				
Program Services				
Scholarships and Grants	630,437			630,437
University Support	292,801			292,801
Management and General	275,456			275,456
Bad Debts	<u>304,943</u>			<u>304,943</u>
Total Expenses	<u>1,503,637</u>			<u>1,503,637</u>
Change in Net Assets	67,956	497,696	354,134	919,786
NET ASSETS				
Net Assets - Beginning, As Previously Reported	1,830,671	4,337,344	5,232,735	11,400,750
Restatement	<u>(1,890,700)</u>	<u>(945,996)</u>	<u>(10,386)</u>	<u>(2,847,082)</u>
Net Assets - Beginning As Restated	<u>(60,029)</u>	<u>3,391,348</u>	<u>5,222,349</u>	<u>8,553,668</u>
Net Assets - End of Year	<u>\$ 7,927</u>	<u>\$ 3,889,044</u>	<u>\$ 5,576,483</u>	<u>\$ 9,473,454</u>

See Note 1 in the Notes to the Financial Statements

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**NORTH CAROLINA CENTRAL 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. North Carolina Central 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 units are either blended or discretely presented in the University's financial statements. The blended component unit, although legally separate, is, in substance, part of the University's operations and therefore, is reported as if it was part of the University. 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.

Blended Component Unit - Although legally separate, The NCCU Real Estate Foundation, Inc. (Real Estate Foundation), a component unit of the University, is reported as if it was part of the University.

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

Discretely Presented Component Unit – The NCCU Foundation, Inc. (NCCU Foundation), 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 NCCU Foundation acts primarily as a fund-raising organization to supplement the resources that are available to the University in support of its programs. The NCCU Foundation board consists of 20 members. Although the University does not control the timing or amount of receipts from the NCCU Foundation, the majority of resources, or income thereon that the NCCU Foundation holds and invests are restricted to the activities of the University by the donors. Because these restricted resources held by the NCCU Foundation can only be used by, or for the benefit of the University, the NCCU 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 NCCU Foundation 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 Governmental Accounting Standards Board (GASB) revenue recognition criteria and presentation features. No modifications have been made to the NCCU Foundation's financial information in the University's financial reporting entity for these differences.

During the year ended June 30, 2005, the NCCU Foundation distributed \$292,801 to the University for both restricted and unrestricted purposes. The University remitted \$119,989 in payroll deducted employee contributions and \$231,123 in other reimbursements to the NCCU Foundation. Complete financial statements for the Foundation can be obtained from the University Controller's Office, 1801 Fayetteville Street, Durham, NC 27707, or by calling (919) 530-7432.

- 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 GASB.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

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

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

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

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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. The deferred losses on refunds are amortized over the life of the bond 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 (for SPA employees) and July 1 (for EPA non-faculty employees) or for which an employee can be paid upon termination of employment. Also, any accumulated vacation leave in excess of 30 days at 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, and Postal Services. In addition, the University has other miscellaneous sales and service units that operated either on a reimbursement or charge basis. All internal sales activities to University departments from auxiliary operations and sales and service units have been eliminated in the accompanying financial statements. These eliminations are recorded by removing the revenue and expense in the auxiliary operations and sales and service units and, if significant, allocating any residual balances to those departments receiving the goods and services during the year.

NOTE 2 - DEPOSITS AND INVESTMENTS

- A. Deposits** – Unless specifically exempt, the University is required by *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 \$31,109,991. 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 shares of the Short-Term Investment Fund are valued at amortized cost,

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 \$4,152,847 and the bank balance was \$4,152,847. 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>\$ 4,052,175</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 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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 units, the Real Estate Foundation and the NCCU Foundation, are 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 funds to manage investments and distribute investment income. Purchases in the investment funds are allowed at the beginning of each month. Fund ownership is measured based on the participating funds purchases and accumulated gain/loss reinvestment. The investment strategy, including the selection of investment managers, is based on the directives of the University Endowment Board.

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)			
		Less Than 1	1 to 5	6 to 10	More than 10
Debt Securities					
U.S. Treasuries	\$ 194,159	\$ 0	\$ 0	\$ 51,195	\$ 142,964
U.S. Agencies	551,127		50,000	398,634	102,493
Motrgage Pass Throughs	627,201				627,201
Collateralized Mortgage Obligations	512,501				512,501
Asset-Backed Securities	121,894				121,894
Mutual Bond Funds	2,127,946	314,936	336,215	406,438	1,070,357
Domestic Corporate Bonds	1,043,969		408,736	390,205	245,028
		<u>\$ 314,936</u>	<u>\$ 794,951</u>	<u>\$ 1,246,472</u>	<u>\$ 2,822,438</u>
Other Securities					
Money Market Funds	200,105				
Other Mutual Funds	3,334,468				
Domestic Stocks	5,155,656				
Other	629,121				
Total Non-Pooled Investments	<u>\$ 14,498,147</u>				

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 rated as follows:

	Fair Value	AAA Aaa	AA Aa	A	BBB Baa	BB Ba	B
U.S. Agencies	\$ 551,127	\$ 328,216	\$ 222,911	\$ 0	\$ 0	\$ 0	\$ 0
Motrgage Pass Throughs	627,201	627,201					
Collateralized Mortgage Obligations	512,501	387,687	124,814				
Asset-backed Securities	121,894	74,069	47,825				
Mutual Bond Funds	2,127,946	972,471	168,108	346,855	397,926	97,886	42,559
Domestic Corporate Bonds	1,043,969		75,623	430,924	537,422		

Rating Agencies: Moody's/S&P

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

NOTE 3 - ENDOWMENT INVESTMENTS

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

Investment return of the University's endowment funds is predicated on the total return concept (yield plus appreciation). Annual payouts from the University's endowment funds are determined by 5.5% of the five-year moving average of the fund's market value. If current year earnings do not meet the payout requirements, the University uses accumulated income and appreciation to make up the difference. At June 30, 2005, net appreciation of \$2,545,749 was available to be spent, of which \$1,012,663 was restricted to specific purposes.

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	\$ 5,121,892	\$ 1,147,289	\$ 3,974,603
Accounts	867,342		867,342
Intergovernmental	4,058,416		4,058,416
Pledges	32,750		32,750
Investment Earnings	37,254		37,254
Interest on Loans	73,103		73,103
Total Current Receivables	\$ 10,190,757	\$ 1,147,289	\$ 9,043,468
Notes Receivable:			
Notes Receivable - Current:			
Federal Loan Programs	\$ 368,000	\$ 191,341	\$ 176,659
Notes Receivable - Noncurrent:			
Federal Loan Programs	\$ 6,092,675	\$ 3,084,402	\$ 3,008,273

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	\$ 5,318,331	\$ 0	\$ 43,415	\$ 0	\$ 5,361,746
Art, Literature, and Artifacts	507,540				507,540
Construction in Progress	30,948,922	(46,547,444)	47,861,460		32,262,938
Total Capital Assets, Nondepreciable	36,774,793	(46,547,444)	47,904,875		38,132,224
Capital Assets, Depreciable:					
Buildings	121,384,824	46,541,964			167,926,788
Machinery and Equipment	11,553,649		2,820,856	427,347	13,947,158
General Infrastructure	14,244,648	5,480			14,250,128
Total Capital Assets, Depreciable	147,183,121	46,547,444	2,820,856	427,347	196,124,074
Less Accumulated Depreciation/Amortization for:					
Buildings	49,108,596		2,420,346		51,528,942
Machinery and Equipment	6,286,798		1,152,730	353,278	7,086,250
General Infrastructure	6,455,502		604,568		7,060,070
Total Accumulated Depreciation	61,850,896		4,177,644	353,278	65,675,262
Total Capital Assets, Depreciable, Net	85,332,225	46,547,444	(1,356,788)	74,069	130,448,812
Capital Assets, Net	\$ 122,107,018	\$ 0	\$ 46,548,087	\$ 74,069	\$ 168,581,036

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

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

	Amount
Accounts Payable	\$ 6,502,841
Accrued Payroll	2,060,145
Contract Retainage	2,054,844
Intergovernmental Payables	368,157
Other	92,340
Total Accounts Payable and Accrued Liabilities	\$ 11,078,327

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	\$ 32,925,000	\$ 0	\$ 450,000	\$ 32,475,000	\$ 21,838,870
Add/Deduct Premium/Discount	(240,584)		(15,550)	(225,034)	
Deduct Deferred Charge on Refunding	(1,064,658)		(56,782)	(1,007,876)	
Total Bonds Payable	31,619,758		377,668	31,242,090	21,838,870
Capital Leases Payable	724,599		94,240	630,359	82,430
Compensated Absences	4,454,837	2,745,265	2,770,925	4,429,177	327,618
Total Long-Term Liabilities	\$ 36,799,194	\$ 2,745,265	\$ 3,242,833	\$ 36,301,626	\$ 22,248,918

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

Purpose	Series	Interest Rate/ Ranges	Final Maturity Date	Original Amount of Issue	Principal Paid Through June 30, 2005	Principal Outstanding June 30, 2005
<hr/>						
Stadium System Revenue Bonds						
	1998	4.4% to 5.0%	04/01/2023	\$ 3,320,000	\$ 765,000	\$ 2,555,000
<hr/>						
NCCU Real Estate Foundaiton, Inc. Housing System						
Student Housing Facilities Revenue Bonds	2003A	Variable	10/01/2034	21,475,000		21,475,000
Taxable Student Housing Facilities Revenue Bonds	2003B	Variable	10/01/2005	100,000		100,000
				<hr/>		<hr/>
Total NCCU Real Estate Foundation, Inc. Housing System				21,575,000		21,575,000
<hr/>						
The University of North Carolina System Pool Revenue Bonds						
	2004B	3.0% to 5.0%	04/01/2023	8,670,000	325,000	8,345,000
				<hr/>		<hr/>
Total Bonds Payable (principal only)				<u>\$ 33,565,000</u>	<u>\$ 1,090,000</u>	32,475,000
Less: Unamortized Loss on Refunding						(1,007,876)
Less: Unamortized Discount						<u>(225,034)</u>
Total Bonds Payable						<u>\$ 31,242,090</u>

C. Demand Bonds – With regards to the following demand bonds, the issuer has not entered into take out agreements, which would convert the demand bonds not successfully remarketed into another form of long-term debt.

North Carolina Central University – Revenue Bonds Series 2003A and 2003B: In October of 2003, the North Carolina Capital Facilities Finance Agency issued Student Housing Facilities Revenue Demand Bonds (\$21,475,000 Variable Rate Revenue Demand Bonds, Series 2003A) and Taxable Student Housing Facilities Revenue Bonds (\$100,000 Variable Rate Revenue Bonds, Series 2003B) that have a maturity date of October 1, 2034 and October 1, 2005, respectively. The issuer, the North Carolina Capital Facilities Finance Agency, loaned the proceeds of the Series 2003 Bonds to the NCCU Real Estate Foundation, Inc. (Foundation). The Foundation used the proceeds to finance the costs of building a student housing facility at North Carolina Central University, to fund a debt service reserve fund for the 2003A Bonds, to pay a portion of the interest on the bonds during construction of the project, and to pay certain costs of issuance of the bonds. The 2003A Bonds are subject to mandatory sinking fund redemption at the principal amount on the interest payment dates or immediately preceding October 1, 2005.

The Student Housing Facilities Revenue Demand Bonds (Series 2003) has an Irrevocable Letter of Credit (LOC) for \$21,819,518. The LOC is to secure the payment of the principal and purchase price of interest on the Series 2003 Bonds. The LOC was issued by Wachovia Bank, N.A.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

and expired on October 15, 2006. The LOC may be extended by request from the Foundation by delivering a notice of extension to the Trustee with a new expiration date. The LOC was extended until June 30, 2007. At June 30, 2005, the LOC rate for the bonds was 1.40% and the total amount drawn on it was \$427,404.

The Foundation paid Wachovia Bank, N.A. a commitment fee of \$109,098 for the letter of credit on the date the bonds were issued. Additionally, the Foundation paid credit facility fees in the amount of \$77,217 during the fiscal year. The Bonds are not under a take out agreement; however, in the event of termination 100% of the unpaid principal will be due and payable plus any unpaid and accrued interest.

Under the LOC agreement, the proceeds of each drawing under the LOC to pay the portion of the purchase price of Series 2003 bonds allocable to principal will constitute a tender advance and must be reimbursed as provided in the agreement. The Foundation is required to repay each tender advance to Wachovia Bank, N.A. plus an interest rate of Prime plus 1.0%. The amount of any tender advance made is repaid based on the earliest to occur of the date the credit provider bonds purchased pursuant to such tender advances are remarketed, the close of business on the date that is 180 days after the tender was made and/or the termination date.

The Student Housing Facilities Revenue Demand Bonds (Series 2003) has remarketing fees. The remarketing fee is an upfront charge to reset the interest rates on a weekly basis. The remarketing agent is Wachovia Bank, N.A. for the Series 2003A Bonds and Wachovia Capital Markets, LLC for the Series 2003B Bonds. At June 30, 2005, the remarketing fee rate for the bonds was 0.125%. The Foundation's remarketing fee as of June 30, 2005, through June 30, 2035, is listed in the SWAP 1 and 2 schedules below.

Interest Rate Swaps:

Objective: As a means to lower its borrowing costs and increase its savings, when compared against fixed-rate refunding bonds at the time of issuance in October 2003, effective March 24, 2004, the Foundation entered into two interest rate swaps with Wachovia Bank, N.A., in connection with its \$21,475,000 Variable Rate Student Housing Revenue Demand Bonds, Series 2003A and \$100,000 Variable Rate Student Housing Revenue Bond, Series 2003B. The intention of the swap agreements was to effectively change the interest rate on the bonds to a synthetic rate of 3.515% (Swap 1) and 2.71% (Swap 2).

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Terms: The bonds and the related swap agreements mature on October 1, 2024 (Swap 1), and April 1, 2009 (Swap 2), and the combined swaps' notional amount of \$17,180,000 hedges 80% of the \$21,475,000 variable-rate bonds. Starting in fiscal year 2006, the combined notional value of the swaps and the combined principal amount of the associated debt will decline. Under the swaps, the Foundation pays Wachovia Bank, N.A. a fixed rate of 3.515% (Swap 1) and 2.71% (Swap 2) and receives a monthly variable rate at 70% and 100% of London Interbank Offered Rate (LIBOR) and Bond Market Association (BMA), respectively. The bonds' variable-rate coupons are closely associated with the BMA.

Swap 1	Terms	Rates (%)
Fixed Payment to Wachovia Bank, N.A.	Fixed	3.515
Variable Payment from Wachovia Bank, N.A.	70% LIBOR	0.958
Net Interest Rate Swap Payments		2.557

Swap 2	Terms	Rates (%)
Fixed Payment to Wachovia Bank, N.A.	Fixed	2.710
Variable Payment from Wachovia Bank, N. A.	BMA	1.050
Net Interest Rate Swap Payments		1.660

Fair Value: As of June 30, 2005, Swap 1 had a negative fair value of \$388,718 and Swap 2 had a positive fair value of \$100,927. The positive fair value of Swap 2 may be countered by an increase in total interest payments required under the variable rate bonds, creating a higher synthetic interest rate. Because the coupons on the Foundation's variable-rate bond are adjusted every seven days to changing interest rates, the bonds do not have a corresponding fair value increase. The mark-to-market valuations were established by market quotations from Wachovia Bank, N.A. representing estimates of the amounts that would be paid upon terminating the transactions.

Credit Risk: As of June 30, 2005, the Foundation was exposed to credit risk because the swaps had a negative fair value in aggregate. However, should interest rates change and the aggregate fair value of the swaps become positive, the Foundation would be exposed to credit risk in the amount of the derivatives' aggregate fair value. Swap 1 and Swap 2's counterparty (Wachovia Bank, N.A.) was rated Aa2 by Moody's

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Investors Service (Moody's), AA- by Standard and Poor's (S & P) and AA- by Fitch Ratings (Fitch).

Basis Risk and Termination Risk: Swap 1 exposes the Foundation to basis risk should the relationship between LIBOR and BMA converge, changing the synthetic rate on the bonds. The effect of this difference in basis is indicated by the difference between the intended synthetic rate of 3.515% and the actual rate of 3.465% (Swap 1) at June 30, 2005. As of June 30, 2005, the rate on the Foundation's Bonds was 2.29%, whereas 70% of LIBOR was 2.340%. Swap 2 exposes the Foundation to basis risk should the actual rate on the Foundation's Bond vary from the BMA. The effect of this difference in basis is indicated by the difference between the intended synthetic rate of 2.71% and the actual rate of 3.525% (Swap 2) at June 30, 2005. As of June 30, 2005, the rate on the Foundation's Bonds was 2.29%, whereas the BMA index was 2.28%. Termination could result in the Foundation being required to make an unanticipated termination payment. The swap agreements are terminated if the Foundation or Wachovia Bank, N.A. fails to perform under the terms of the contract.

Market-Access Risk/Rollover-Risk: Swap 1 and Swap 2 expose the Foundation to market-access and rollover risk when the swaps mature on October 1, 2024 and April 1, 2009, respectively. When Swap 1 and Swap 2 mature, the interest rate on the underlying debt will return to a variable rate.

Swap Payments and Associated Debt: As rates vary, variable-rate debt and net swap payments will vary. As of June 30, 2005, debt service requirements of the University's outstanding variable-rate debt and net swap payments, assuming current interest rates remain the same, for their terms were as follows.

Swap 1 and 2 Variable Rate Bonds						
Fiscal Year	Principal	Interest	Letter of Credit	Remarketing	Interest Rate Swaps, Net	Total
2006	\$ 290,000	\$ 490,403	\$ 299,629	\$ 26,753	\$ 137,996	\$ 1,244,781
2007	310,000	483,109	295,351	26,371	135,064	1,249,895
2008	325,000	477,037	291,638	26,039	133,367	1,253,081
2009	345,000	467,937	286,075	25,542	122,461	1,247,015
2010	365,000	459,677	281,025	25,091	94,344	1,225,137
2011-2015	2,155,000	2,158,654	1,319,701	117,830	443,053	6,194,238
2016-2020	2,830,000	1,871,263	1,144,004	102,143	384,080	6,331,490
2021-2025	3,710,000	1,491,868	912,059	81,434	266,609	6,461,970
2026-2030	4,865,000	996,009	608,914	54,368		6,524,291
2031-2035	6,380,000	346,024	211,543	18,888		6,956,455
Total	<u>\$ 21,575,000</u>	<u>\$ 9,241,981</u>	<u>\$ 5,649,939</u>	<u>\$ 504,459</u>	<u>\$ 1,716,974</u>	<u>\$ 38,688,353</u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

D. 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	\$ 755,000	\$ 1,276,172
2007	800,000	1,244,943
2008	830,000	1,217,952
2009	800,000	1,185,318
2010	835,000	2,165,782
2011-2015	4,840,000	4,859,442
2016-2020	6,225,000	3,628,160
2021-2025	6,145,000	2,543,360
2025-2030	4,865,000	1,659,291
2031-2035	6,380,000	576,455
Total Requirements	\$ 32,475,000	\$ 20,356,875

Interest on the variable rate University of North Carolina System Pool Revenue Bonds is calculated at 3.0% to 5.0% at June 30, 2005. Interest on the variable rate Stadium Revenue Bonds is calculated at 4.5% to 5.0% at June 30, 2005. Interest on the variable rate Student Housing Facilities Revenue Bonds is calculated at 4.5% to 5.0% at June 30, 2005.

This schedule also includes the debt service requirements for debt associated with interest rate swaps. More detailed information about interest rate swaps is presented in Note 7C.

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

Housing Revenue: On March 31, 2004, the University defeased \$7,690,000 of outstanding Housing Revenue Bonds, Series 1996 (original issue amount \$8,890,000). An irrevocable trust was established with an escrow agent to provide for all future debt service payments on the defeased bonds. The trust assets and the liability for the defeased bonds are not included in the University's Statement of Net Assets. At June 30, 2005, the outstanding balance of the defeased Housing Revenue Bonds was \$7,455,000.

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

University's Statement of Net Assets. There was no outstanding balance on the defeased Dormitory System Revenue Bonds at June 30, 2005.

NOTE 8 - LEASE OBLIGATIONS

- A. Capital Lease Obligations** - Capital lease obligations relating to motor vehicles are recorded at the present value of the minimum lease payments. Future minimum lease payments under capital lease obligations consist of the following at June 30, 2005:

<u>Fiscal Year</u>	<u>Amount</u>
2006	\$ 114,840
2007	114,840
2008	114,840
2009	<u>344,628</u>
Total Minimum Lease Payments	689,148
Amount Representing Interest (6% Rate of Interest)	<u>58,789</u>
Present Value of Future Lease Payments	<u><u>\$ 630,359</u></u>

Machinery and equipment acquired under capital lease amounted to \$695,486 at June 30, 2005.

- B. 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><u>\$ 36,133</u></u>

Rental expense for all operating leases during the year was \$1,927,131.

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 Change in Allowance for Uncollectibles	Net Revenues	Revenues Pledged as Security for Debt
Operating Revenues:						
Student Tuition and Fees	\$ 30,516,183	\$ 0	\$ 7,434,116	\$ (585,164)	\$ 23,667,231	\$ 277,998 (A)
Sales and Services:						
Sales and Services of Auxiliary Enterprises:						
Residential Life	\$ 7,493,005	\$ 19,216	\$ 1,450,432	\$ (147,156)	\$ 6,170,513	\$ 0
Dining	4,760,336	73,770	1,152,097	(68,626)	3,603,095	
Student Union Services	1,241,650		300,503	(29,871)	971,018	
Health, Physical Education, and Recreation Services	359,543				359,543	
Bookstore	212,676	78,978			133,698	
Parking	1,176,970			(12,402)	1,189,372	
Athletic	472,126				472,126	
Other	1,712,528	78,480		(54,473)	1,688,521	
Sales and Services of Education and Related Activities	431,296	80			431,216	
Total Sales and Services	<u>\$ 17,860,130</u>	<u>\$ 250,524</u>	<u>\$ 2,903,032</u>	<u>\$ (312,528)</u>	<u>\$ 15,019,102</u>	<u>\$ 0</u>

Revenue Bonds Secured by Pledged Revenues:

(A) Stadium System

NOTE 10 - OPERATING EXPENSES BY FUNCTION

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

	Salaries and Benefits	Supplies and Materials	Services	Scholarships and Fellowships	Utilities	Depreciation	Total
Instruction	\$ 35,422,209	\$ 6,092,471	\$ 4,446,048	\$ 0	\$ 755	\$ 0	\$ 45,961,483
Research	2,922,434	958,274	999,876				4,880,584
Public Service	1,169,559	548,496	1,396,023				3,114,078
Academic Support	6,251,042	3,498,631	3,096,477				12,846,150
Student Services	2,108,589	330,519	576,991		493		3,016,592
Institutional Support	9,626,061	4,945,543	4,755,740		93,307		19,420,651
Operations and Maintenance of Plant	4,084,172	5,278,860	2,985,467		2,800,691		15,149,190
Student Financial Aid	554,116		264	5,826,623			6,381,003
Auxiliary Enterprises	4,651,135	1,694,381	8,071,169		193,647		14,610,332
Depreciation						4,177,644	4,177,644
Total Operating Expenses	<u>\$ 66,789,317</u>	<u>\$ 23,347,175</u>	<u>\$ 26,328,055</u>	<u>\$ 5,826,623</u>	<u>\$ 3,088,893</u>	<u>\$ 4,177,644</u>	<u>\$ 129,557,707</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 \$55,906,698, of which \$40,465,795 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were \$2,427,948 and \$878,108, respectively. The University made 100% of its annual required contributions for the years ended June 30, 2005, 2004, and 2003, which were \$878,108, \$83,223, and \$0, 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 \$55,906,698, of which \$11,965,199 was covered under the Optional Retirement Program. Total employee and employer contributions for pension benefits for the year were \$717,912 and \$818,420, 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 \$103,868 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 \$72,003. The voluntary contributions by employees amounted to \$197,517 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 \$812,197 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 \$1,677,792. 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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 \$233,318. 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, vandalism and "all risk" for certain buildings and contents.

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

The University purchased other authorized coverage from private insurance companies through the North Carolina Department of Insurance and the State's Agent of Record. Examples of insurance policies purchased include, but are not limited to fine arts, boiler and machinery, medical professional liability, athletic accident, excess liability, university internship and study abroad health insurance.

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

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

Term life insurance (death benefits) of \$25,000 to \$50,000 is provided to eligible workers. This Death Benefit Plan is administered by the State Treasurer and funded via employer contributions. 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 \$8,226,606 at June 30, 2005.

NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)

- B. Pending Litigation and Claims** – The University is a party to litigation and claims in the ordinary course of its operations. Since it is not possible to predict the ultimate outcome of these matters, no provision for any liability has been made in the financial statements. University management is of the opinion that the liability, if any, for any of these matters will not have a material adverse effect on the financial position of the University.
- C. University Improvement General Obligation Bonds** – The 1999-2000 Session of the General Assembly of North Carolina authorized the issuance of \$2.5 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 \$36,829,793 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
North Carolina Central University
Durham, North Carolina

We have audited the financial statements of North Carolina Central 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 units, 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 January 31, 2007. We did not audit the financial statements of the NCCU Real Estate Foundation, Inc., which represent 8.4 percent, (0.34) percent, and 0.89 percent, respectively, of the assets, net assets, and revenues of the University; nor the financial statements of the NCCU Foundation, Inc., which represent 100% of the University's discretely presented component unit. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the NCCU Real Estate Foundation, Inc., and the NCCU Foundation, Inc., is based on the reports 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 NCCU Real Estate Foundation, Inc., and the discretely presented component unit were not audited in accordance with *Government Auditing Standards*, and accordingly, this report does not extend to the NCCU Real Estate Foundation, Inc., nor the discretely presented component unit.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the University's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control

**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)**

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 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

January 31, 2007

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