



# **STATE OF NORTH CAROLINA**

**NORTH CAROLINA STATE UNIVERSITY**

**RALEIGH, NORTH CAROLINA**

**FINANCIAL STATEMENT AUDIT REPORT**

**FOR THE YEAR ENDED JUNE 30, 2007**

**OFFICE OF THE STATE AUDITOR**

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

**STATE AUDITOR**

**NORTH CAROLINA STATE UNIVERSITY**

**RALEIGH, NORTH CAROLINA**

**FINANCIAL STATEMENT AUDIT REPORT**

**FOR THE YEAR ENDED JUNE 30, 2007**

**BOARD OF GOVERNORS**

**THE UNIVERSITY OF NORTH CAROLINA**

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STATE OF NORTH CAROLINA  
Office of the State Auditor

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

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

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**AUDITOR'S TRANSMITTAL**

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

We have completed a financial statement and compliance audit of North Carolina State University for the year ended June 30, 2007, 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 and our consideration of the University's administration of federal programs in accordance with applicable laws, regulations, contracts and grants resulted in no audit findings.

*North Carolina General Statutes* require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.

*Leslie W. Merritt, Jr.*

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

February 1, 2008

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**INDEPENDENT AUDITOR'S REPORT**

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Board of Trustees  
North Carolina State University  
Raleigh, North Carolina

We have audited the accompanying financial statements of North Carolina State University, a constituent institution of the multi-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, 2007, 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 State University's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the NC State Investment Fund, Inc., which represent 18 percent, 25 percent, and 6 percent, respectively, of the assets, net assets and revenues of the University; nor the financial statements of the North Carolina State University Foundation, Inc., and the NCSU Student Aid Association, Inc., the University's discretely presented component units. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinions, insofar as they relate to the amounts included for those entities, are 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 North Carolina State University Foundation, Inc., and the NCSU Student Aid Association, Inc., were not audited in accordance with *Government Auditing Standards*. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the 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 State University and its discretely presented component units as of

## INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

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June 30, 2007, 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 28, 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

November 28, 2007

## NORTH CAROLINA STATE UNIVERSITY MANAGEMENT'S DISCUSSION AND ANALYSIS

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### **Introduction**

Management's Discussion and Analysis of the financial report provides an overview of the accompanying basic financial statements. It includes comparative financial analysis with discussion of significant changes from the prior year. The overview also includes information on currently known facts, decisions, or conditions affecting the financial affairs of the University.

### **Financial Highlights**

NC State University's net assets increased by 22.5% to \$1.37 billion in fiscal year 2007. Net assets represent the University's equity, the assets less the liabilities. A major part of this net assets increase was the result of increases of \$106.8 million in capital assets, net of related debt, and \$100.1 million in restricted expendable capital projects. The University's unrestricted net assets also increased by \$21.0 million for a total of \$116.2 million.

Revenues increased by 8.8% to \$1.04 billion in fiscal year 2007. Revenues represent amounts received or accrued that are either operating or nonoperating on the accompanying financial statements. A major part of the revenues increase was the result of increased sales and services (operating) and State appropriations (nonoperating). Sales and services increased by 12.6% to \$154.2 million. State appropriations increased by 7.7% to \$430.9 million.

Operating Expenses increased by 5.9% to \$1.01 billion in fiscal year 2007. Operating expenses represent amounts paid or accrued for operating purposes. A major part of the expense increase was the result of increases in Instruction, Public Service, and Research expenses. These expenses increased as a result of increases in salaries and benefits and services costs.

### **Using the Financial Statements**

The University's financial statements are used to evaluate financial position as of June 30th and the results of operations for the fiscal year then ended. The *Statement of Net Assets* provides information relative to the evaluation of financial position. The *Statement of Revenues, Expenses, and Changes in Net Assets* provides information relative to the evaluation of the results of operations. Its ending net assets agree to the total net assets on the *Statement of Net Assets*.

The financial statements also include a *Statement of Cash Flows*. This statement is used to identify the University's sources and uses of cash. The ending cash on the *Statement of Cash Flows* agrees to the total cash reported on the *Statement of Net Assets*. Also, this statement reconciles the net operating loss reported in the *Statement of Revenues, Expenses, and Changes in Net Assets* to the net cash used by operating activities.

In using the financial statements, the *Notes to the Financial Statements* accompanying the financial statements should be read in conjunction with the financial statements. The notes provide information regarding the significant accounting principles applied in the financial

## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

statements, authority for and associated risk of deposits and investments, detailed information on long-term liabilities, detailed information on accounts receivable, accounts payable, revenues and expenses, required information on pension plans and other post employment benefits, insurance against losses, commitments and contingencies, and accounting changes. If necessary, the disclosures include a discussion of adjustments to prior periods and events subsequent to the University's financial statement period. Overall, these disclosures provide information to better understand details, risk, and uncertainty associated with amounts reported in the financial statements.

### Comparative Condensed Financial Statement Information

#### Statement of Net Assets

The *Statement of Net Assets* provides information regarding the University's assets, liabilities, and net assets as of June 30, 2007. Asset and liability balances are classified as either current or noncurrent. Assets classified as current are those that are available to pay for current liabilities or current year expenditures. Liabilities classified as current are those that are due and payable in the next fiscal year. The net asset balances are classified as either invested in capital assets, net of related debt, restricted or unrestricted. In addition, net assets classified as restricted are classified as either nonexpendable or expendable. Overall, the *Statement of Net Assets* provides information to evaluate the financial strength of the University and its ability to meet current and long-term obligations.

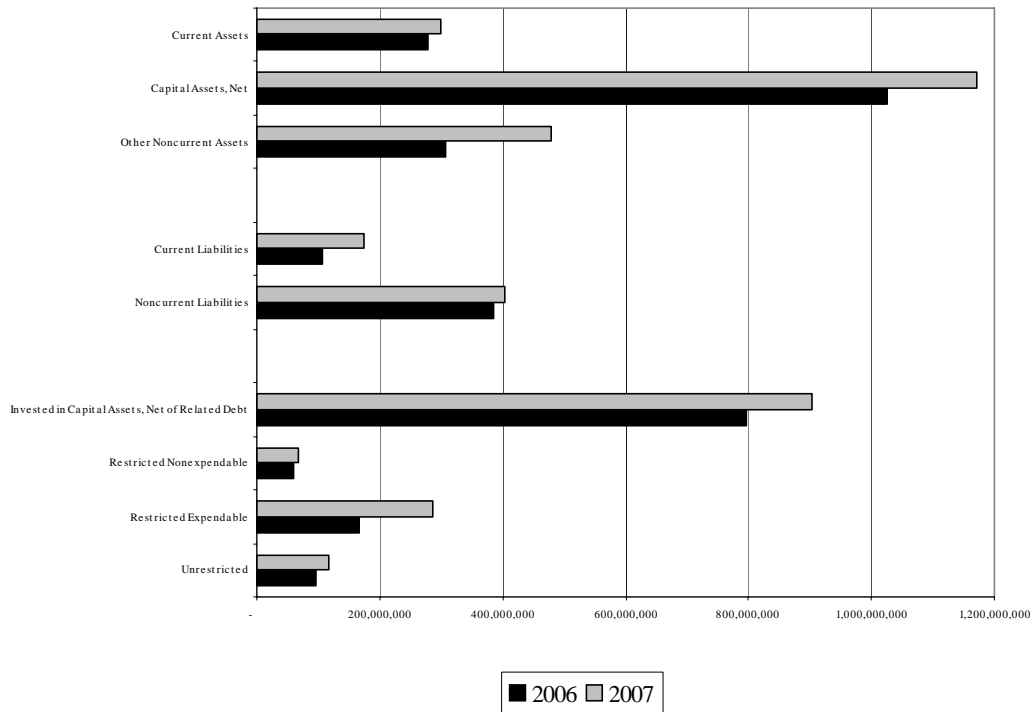
Following is a comparative analysis on the condensed balances reported in the *Statement of Net Assets* as of June 30, 2007, and 2006.

	<u>2007</u>	<u>2006</u>	<u>Increase</u>
<b>Assets</b>			
Current Assets	\$ 298,259,903	\$ 278,960,603	\$ 19,299,300
Capital Assets, Net	1,170,941,973	1,025,755,445	145,186,528
Other Noncurrent Assets	<u>479,896,738</u>	<u>305,914,848</u>	<u>173,981,890</u>
Total Assets	<u>1,949,098,614</u>	<u>1,610,630,896</u>	<u>338,467,718</u>
<b>Liabilities</b>			
Current Liabilities	174,813,192	106,087,466	68,725,726
Noncurrent Liabilities	<u>402,507,848</u>	<u>385,046,545</u>	<u>17,461,303</u>
Total Liabilities	<u>577,321,040</u>	<u>491,134,011</u>	<u>86,187,029</u>
<b>Net Assets</b>			
Invested in Capital Assets, Net of Related Debt	903,982,414	797,135,394	106,847,020
Restricted			
Nonexpendable	66,482,074	60,415,528	6,066,546
Expendable	285,112,254	166,734,710	118,377,544
Unrestricted	<u>116,200,832</u>	<u>95,211,253</u>	<u>20,989,579</u>
Total Net Assets	<u>\$ 1,371,777,574</u>	<u>\$ 1,119,496,885</u>	<u>\$ 252,280,689</u>



## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

The following graph illustrates the assets, liabilities and net assets of the University as of June 30, 2007, as compared to June 30, 2006.



Assets totaled \$1.95 billion, an increase of \$338.5 million over the prior year. The increase in assets includes capital asset growth of \$145.2 million, an increase in other noncurrent assets of \$174.0 million, and an increase in current assets of \$19.3 million.

The capital asset growth is due primarily to \$141.2 million in capital grants, primarily the State's higher education bond program. Another major factor is some \$81.4 million from capital appropriations. Commercial paper financing provided available funds for the remaining capital growth.

Other noncurrent assets increased by \$174.0 million. Increases of \$73.2 million in restricted cash, \$57.1 million in restricted due from primary government, and \$41.6 million in endowment investments and other long-term investments are the primary factors. The noncurrent restricted cash increase is related to the capital asset growth and includes cash from the State bonds and from commercial paper proceeds. The restricted due from primary government increased because the receivable for Statewide bonds rose. The growth in long-term investment balances is the result of improved market values and realized gains in the NC State Investment Fund.

The \$19.3 million net increase in current assets is caused by several items. Cash and cash equivalents increased by \$26.4 million due to auxiliary and carry over cash. Also, current restricted cash rose by \$23.0 million due to improved contract and grant collections and cash

## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

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availability to cover capital and debt current liabilities. These increases are partially offset by decreases in receivables, mainly in due from State of North Carolina component units (The Golden LEAF, Inc.) and receivables for contract and grants.

Liabilities totaled \$577.3 million, an increase of \$86.2 million over the prior year. The increase in liabilities is attributable to an increase in noncurrent liabilities of \$17.5 million and an increase in current liabilities of \$68.7 million.

The most significant factor in the noncurrent liabilities increase is the \$24.3 million rise in funds held in trust for investment pool participants (various foundations). This increase was partially offset by a decrease in long-term liabilities, mainly in bonds payable. The current liability increase is caused by a \$64.0 million increase in commercial paper short-term debt, a \$6.0 million increase in deferred revenue and small decreases in most of the other liability accounts.

Net assets totaled \$1.37 billion, an increase of \$252.3 million over the prior year. The higher net assets are attributable to increases of \$106.9 million in capital assets net of related debt, \$100.1 million in restricted expendable for capital projects balances, \$21.0 million in unrestricted balances and smaller increases in other net asset balances.

The University's current assets are more than sufficient to cover current liabilities with a ratio of 1.7x, as compared to 2.6x in the prior year. The University's total assets excluding capital assets, net of depreciation, are more than sufficient to cover total liabilities with a ratio of 1.3x, as compared to 1.2x in the prior year. The University's total assets are significantly more than the University's liabilities with a ratio of 3.4x, as compared to 3.3x in the prior year. These financial ratios are indicators of NC State's financial strength and its ability to meet current and long-term obligations.

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

The *Statement of Revenues, Expenses, and Changes in Net Assets* provides information regarding the University's activities for the year ending June 30, 2007. The activity balances are classified as operating, nonoperating, or other. Activities classified as operating include all revenues of the University except those considered nonoperating or those associated with funds received to enhance capital assets or permanent endowments, and all expenses except those related to interest expense on financing activities, loss on disposal of capital assets, and investment expenses (shown as net against investment income). Activities classified as nonoperating include State appropriations, noncapital gifts and grants revenue, investment income (net of investment expenses), and gains or losses on disposal of capital assets. Activities classified as other include capital gifts or grants and additions to permanent endowments. Overall, the *Statement of Revenues, Expenses, and Changes in Net Assets* provides information to evaluate the University's management of operations and maintenance of financial strength.

## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Following is a comparative analysis on the condensed balances reported in the *Statement of Revenues, Expenses, and Changes in Net Assets* for the fiscal years ended June 30, 2007, and 2006.

	<u>2007</u>	<u>2006</u>	<u>Increase/ (Decrease)</u>
<b>Operating Activities</b>			
Operating Revenues	\$ 531,864,242	\$ 489,385,302	\$ 42,478,940
Operating Expenses	<u>1,012,932,146</u>	<u>956,888,382</u>	<u>56,043,764</u>
Net Operating Loss	<u>(481,067,904)</u>	<u>(467,503,080)</u>	<u>(13,564,824)</u>
<b>Nonoperating Activities</b>			
Nonoperating Revenues	509,082,127	467,042,836	42,039,291
Nonoperating Expenses	<u>12,925,998</u>	<u>8,187,273</u>	<u>4,738,725</u>
Net Nonoperating Revenues	<u>496,156,129</u>	<u>458,855,563</u>	<u>37,300,566</u>
<b>Other Activities</b>			
Capital Grants and Gifts	232,344,655	94,590,022	137,754,633
Additions to Permanent Endowments	<u>4,847,809</u>	<u>5,290,291</u>	<u>(442,482)</u>
Total Other Activity Increases	<u>237,192,464</u>	<u>99,880,313</u>	<u>137,312,151</u>
Increase in Net Assets	<u>\$ 252,280,689</u>	<u>\$ 91,232,796</u>	<u>\$ 161,047,893</u>

### Operating and Nonoperating Activities

The following illustrates the relationships of operating and nonoperating revenue sources and expense functions to total revenue/expenses for the fiscal year 2007 and 2006, and the consistency of relationships between the two years.

#### Operating and Nonoperating Revenues

<u>Title</u>	<u>% to Total 2007</u>	<u>% to Total 2006</u>
State Appropriations	42%	42%
Research Contracts and Grants	19%	20%
Student Tuition and Fees	14%	14%
Sales and Services	15%	14%
Noncapital Grants and Gifts	5%	5%
Federal Appropriations	2%	2%
Other	<u>3%</u>	<u>3%</u>
Total	<u>100%</u>	<u>100%</u>

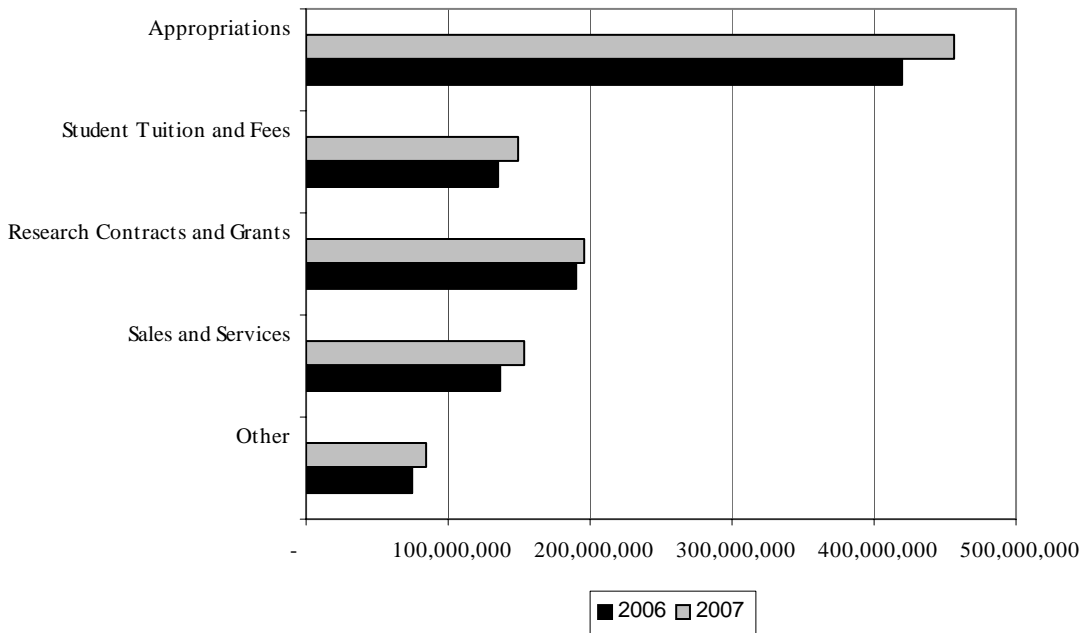
**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)**

**Operating and Nonoperating Expenses**

The following graphs illustrate the University's operating and nonoperating revenues/expenses by source/function.

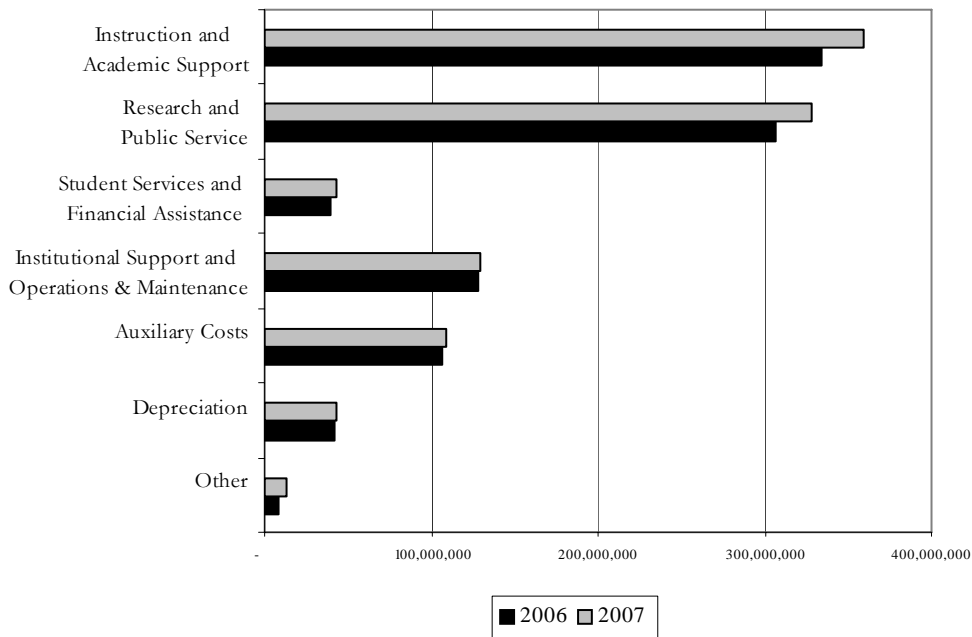
Title	% to Total 2007	% to Total 2006
Instruction	28%	28%
Research	20%	21%
Public Service	12%	11%
Auxiliary Enterprises	11%	11%
Operations & Maintenance of Plant	7%	8%
Academic Support	7%	7%
Institutional Support	5%	5%
Depreciation	4%	4%
Student Financial Aid	3%	2%
Student Services	2%	2%
Other	1%	1%
Total	100%	100%

**Operating and Nonoperating Revenues**



## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

### Operating and Nonoperating Expenses



Total revenues (operating and nonoperating) increased \$84.5 million or 8.8% over the prior year. Appropriations (State and Federal Land Grant Institution), increased by \$36.7 million or 8.7% over the prior year as a result of increased enrollments and legislative salary increases. Student tuition and fees increased by \$14.0 million or 10.4% over the prior year because of enrollment growth and approved tuition and fee rate increases. Research contracts and grants increased by \$5.6 million or 2.9% over the prior year due to additional demand for services. Sales and services increased by \$17.3 million or 12.6% over the prior year. This increase resulted from auxiliary growth, primarily in housing, athletics, Veterinary Hospital, student stores and food services revenues. Other revenues (including operating and nonoperating sources) had a net increase of \$10.9 million or 14.6% over the prior year, primarily as a result of increases in noncapital gifts and investment earnings. Investment income rose due to higher interest rates and market values and realized gains. These other revenue increases were partially offset because the 2006 total included a \$6.2 million gain on the sale of real property.

Total expenses (operating and nonoperating) increased \$60.8 million or 6.3% over the prior year, primarily as a result of increases in salaries and benefits of \$41.6 million and services of \$10.6 million. The salaries and benefits increase is due primarily to a 5.5% to 6.0% salary increase granted by the legislature. The services increase is the result of increased spending on contract and service agreements.

## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

### Other Activity

Other activity totaled \$237.2 million, up \$137.3 million from the prior year. This increase is caused by increases of \$70.3 million in State bond proceeds, \$63.0 million in capital appropriations, \$4.4 million in capital gifts and \$.4 million in additions to endowments.

### Statement of Cash Flows

The *Statement of Cash Flows* provides information about the University's cash activities for the year. The sources and uses of cash are classified as operating activities, noncapital financing activities, capital financing activities, and investing activities.

Following is a comparative analysis on the condensed balances reported in the *Statement of Cash Flows* for the fiscal years ended June 30, 2007, and 2006.

	2007	2006	Increase/ (Decrease)
<b>Operating Activities</b>			
Sources	\$ 548,817,354	\$ 490,559,619	\$ 58,257,735
Uses	973,168,933	908,745,554	64,423,379
Cash Used by Operating Activities	<u>(424,351,579)</u>	<u>(418,185,935)</u>	<u>(6,165,644)</u>
<b>Noncapital Financing Activities</b>			
Sources	570,843,307	543,487,391	27,355,916
Uses	<u>80,420,643</u>	<u>76,679,873</u>	<u>3,740,770</u>
Cash Provided by Noncapital Financing Activities	<u>490,422,664</u>	<u>466,807,518</u>	<u>23,615,146</u>
<b>Capital Financing Activities</b>			
Sources	258,279,163	128,517,096	129,762,067
Uses	<u>207,795,453</u>	<u>161,624,501</u>	<u>46,170,952</u>
Cash Provided (Used) by Financing Activities	<u>50,483,710</u>	<u>(33,107,405)</u>	<u>83,591,115</u>
<b>Investing Activities</b>			
Sources	792,147,665	466,833,938	325,313,727
Uses	<u>786,056,698</u>	<u>474,522,614</u>	<u>311,534,084</u>
Cash Provided (Used) by Investing Activities	<u>6,090,967</u>	<u>(7,688,676)</u>	<u>13,779,643</u>
Net Increase in Cash	<u>\$ 122,645,762</u>	<u>\$ 7,825,502</u>	<u>\$ 114,820,260</u>

Cash increased by \$122.6 million during fiscal year 2007, compared to an increase of \$7.8 million in the prior year. Major factors in the current year were the net increases in cash provided by noncapital financing activities of \$23.6 million, capital financing activities of \$83.6 million, and investing activities of \$13.8 million.

Operating activities reflect increased net cash used of \$6.2 million. It includes major sources such as tuition and fees and contracts and grants. Major operating uses of cash include

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

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salaries and payments to vendors. Because appropriations, gifts, and some grants are not considered operating activities, a net outflow of cash is reported for operating activities.

Cash provided by noncapital financing activities includes sources such as appropriations, Federal Family Education Loan receipts, foundations' deposits for investment, and noncapital gifts and grants. Noncapital financing uses include Federal Family Education Loan disbursements and other payments. The major factor causing the net rise in cash provided by noncapital financing activities is the increase in State appropriations.

Cash provided by capital financing activities includes sources such as proceeds from capital debt and capital appropriations, grants and gifts. Major capital financing uses include purchases of capital assets and payment of principal and interest on capital debt. The cash flows from capital financing showed net cash provided of \$50.5 million. Cash provided exceeded cash used, primarily because of the State bond, capital appropriation and commercial paper proceeds received during the year and not yet spent on acquisition and construction of capital assets.

Cash flows from investing activities include sources such as proceeds from investment transactions and dividend and interest income. The major investing use of cash is the purchase of investments. The cash flows from investing activities showed net cash provided of \$6.1 million. Cash provided exceeded cash used because interest and realized gains increased in 2007.

### **Capital Assets and Long-Term Debt Activities**

#### **Capital Assets**

The University capitalizes assets that have a value or cost equal to or greater than \$5,000 at the date of acquisition and an expected useful life of more than one year. Repairs and renovations that do not extend the life of the building beyond the expected useful life at acquisition, nor increase the future service potential of the building are expensed and not capitalized.

Machinery and Equipment are depreciated over their estimated useful lives, generally 3 to 15 years beginning in the year of acquisition. Buildings and General Infrastructure are depreciated over their estimated useful lives, generally 10 to 50 years for buildings and 15 to 75 years for general infrastructure beginning in the year that the construction is completed or, if purchased after construction, when acquired. Land and Construction in Progress are nondepreciable capital assets. When a construction project is completed, the capital project costs are moved from the Construction in Progress account to either Buildings or General Infrastructure as appropriate.

## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

As shown in the following table, the University increased its net capital assets by \$145.2 million during fiscal year 2007.

	<u>2007</u>	<u>2006</u>	<u>Increase/ (Decrease)</u>
Land	\$ 23,578,371	\$ 23,330,450	\$ 247,921
Construction in Progress	154,018,144	97,809,121	56,209,023
Buildings	1,127,685,467	1,025,273,474	102,411,993
Machinery and Equipment	226,625,994	223,790,341	2,835,653
General Infrastructure	<u>116,082,143</u>	<u>104,423,851</u>	<u>11,658,292</u>
Total Capital Assets	1,647,990,119	1,474,627,237	173,362,882
Accumulated Depreciation	<u>(477,048,146)</u>	<u>(448,871,792)</u>	<u>(28,176,354)</u>
Net Capital Assets	<u>\$ 1,170,941,973</u>	<u>\$ 1,025,755,445</u>	<u>\$ 145,186,528</u>

In addition to costs incurred, the University had \$101.8 million in outstanding commitments for construction projects as of June 30, 2007.

Major changes in capital assets during fiscal year 2007 came from an increase in building renovations relating to the improvement and modernization of the campus. Funding for these improvements primarily come from funds provided by the State of North Carolina Education Improvement Bond Referendum (State Bond Program), State capital appropriations, and University debt financing.

Following are some of the major construction projects that were completed or in progress as of June 30, 2007.

The conversion of 67,500 square feet of laboratory space to General Academic use in Withers Hall was completed. Work done includes the renovation of existing teaching classroom and laboratory spaces, installation of a central HVAC system, and modernization of electrical and mechanical systems for classrooms and office spaces for the College of Humanities and Social Sciences. This building now houses the Departments of Foreign Languages and Literature, Philosophy and Religion, and History.

Leazar Hall underwent a comprehensive renovation of over 66,000 square feet with its completion in fiscal year 2007. This renovation addresses the need for additional design studio and shop space for the School of Design as well as meeting critical safety code standards. It also provides a new entrance to the building from the Court of North Carolina and exposes the original clearstory and structure to provide a new gallery for faculty and staff.

North Carolina State University's Electrical and Computing Engineering Department received another major upgrade to one of the oldest buildings on campus, Daniels Hall. This Phase I renovation was completed in FY 2007 and provides a shift for the International Department to



## MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

the second floor and allows for the Industrial Engineering department to take over the entire first floor.

University Housing finished major renovations on several University dormitories as well as adding a new building in First Year College, which opened in May. Air conditioning and sprinklers were added to Syme, Gold, Welch, Alexander, Turlington and Wood Halls bringing the total of dorm rooms on campus complete with air conditioning and sprinklers to 100%. As well as the comprehensive renovations in the above dorms, E.S. King Village also received major renovations.

Carter Finley Stadium completed major renovations to the North End zone that resulted in an additional 7,000 seats, more accessible concession stands and restrooms and a state of the art scoreboard.

Also finishing up construction in FY 2007 was the Animal and Poultry Teaching Complex on Lake Wheeler Road. This project includes new buildings for both Poultry holding and teaching facilities as well as state of the art swine holding facilities for nutrition and metabolism research as well as waste management.

More information about the University's long-range capital plan is located at [http://www.ncsu.edu/facilities/construction\\_info/index.htm](http://www.ncsu.edu/facilities/construction_info/index.htm)

### Long-Term Debt Activities

The University incurs long-term debt to finance construction projects, to purchase equipment using lease arrangements and to provide for accumulated unused vacation benefits for employees. As shown in the following chart, the University decreased its long-term debt by \$8.0 million during fiscal year 2007.

	<u>2007</u>	<u>2006</u>	<u>Increase/ (Decrease)</u>
Bonds Payable	\$ 200,704,206	\$ 211,173,722	\$ (10,469,516)
Capital Leases Payable	151,382	273,821	(122,439)
Compensated Absences	53,371,329	50,825,595	2,545,734
Total Long-Term Liabilities	<u>\$ 254,226,917</u>	<u>\$ 262,273,138</u>	<u>\$ (8,046,221)</u>

Bond debt principal payments and early payment of \$.6 million in Housing bonds explain the \$10.5 million decrease in bonds payable. Debt payments increased by \$1.2 million, mainly because of the increase in principal payments from the \$81.6 million bond issue in fiscal year 2005. The legislative pay raise was the primary cause of the \$2.5 million increase in compensated absences.

### **Economic Factors That Will Affect the Future**

NC State University was created to improve the lives of North Carolinians. Supported by continuing solid financial performance in the fiscal year 2007, NC State is well prepared to meet the challenges of improving the lives of its students, the people of North Carolina, the nation and the world.

The University's Net Assets increased \$252.3 million to \$1.37 billion in fiscal year 2007. Important factors in NC State's financial growth include increased support from the State of North Carolina, growth in tuition and fees and sales and service revenues, and improved investment returns. The Governor and the General Assembly have continued to provide strong financial support for NC State. State appropriations (including capital appropriations) increased 22.5% in fiscal year 2007. For fiscal year 2008, total budgeted appropriations remained constant, with operating appropriations increasing by some \$43 million and capital appropriations decreasing by approximately the same amount. Enrollment increased by 672 students to 31,802 for fall semester 2007, and undergraduate and graduate tuition and fee rates increased by \$230 and \$104, respectively. The rate increases were the same for non-resident students. NC State is the largest four-year institution in North Carolina with students from all the North Carolina counties and nearly 100 foreign countries.

Chancellor Oblinger has identified five focus areas for the University: preparing leaders for the State, nation, and world; creating educational innovation; improving health and well-being; fueling economic development; and driving innovation in energy and the environment. Recent developments include the Golden LEAF Biomanufacturing Training and Education Center (BTEC), dedicated in September 2007. BTEC supports North Carolina's growing biomanufacturing industry and represents a broad partnership of industry, universities, and community colleges. Another current University project is the Centennial Biomedical Campus. Anchored by the NCSU College of Veterinary Medicine, the Centennial Biomedical Campus is an extension of the original NCSU Centennial Campus concept. The Centennial Biomedical Campus will emphasize partnerships between the University, government and industry in improving biomedical applications for animals and humans.

**North Carolina State University**  
**Statement of Net Assets**  
**June 30, 2007**

**Exhibit A-1**

**ASSETS**

Current Assets:	
Cash and Cash Equivalents	\$ 166,757,092
Restricted Cash and Cash Equivalents	73,401,248
Restricted Short-Term Investments	280,012
Receivables, Net (Note 4)	29,714,204
Due from Primary Government	10,667,293
Due from State of North Carolina Component Units	12,224,853
Inventories	4,001,324
Notes Receivable, Net (Note 4)	1,213,877
	<hr/>
Total Current Assets	298,259,903
Noncurrent Assets:	
Restricted Cash and Cash Equivalents	83,252,529
Restricted Due from Primary Government	61,045,442
Endowment Investments	173,193,120
Other Investments	149,313,206
Notes Receivable, Net (Note 4)	13,092,441
Capital Assets - Nondepreciable (Note 5)	177,596,515
Capital Assets - Depreciable, Net (Note 5)	993,345,458
	<hr/>
Total Noncurrent Assets	1,650,838,711
	<hr/>
Total Assets	1,949,098,614

**LIABILITIES**

Current Liabilities:	
Accounts Payable and Accrued Liabilities (Note 6)	46,966,477
Due to Primary Government	303,225
Unearned Revenue	34,078,211
Interest Payable	2,578,625
Short-Term Debt (Note 7)	80,000,000
Long-Term Liabilities - Current Portion (Note 8)	10,886,654
	<hr/>
Total Current Liabilities	174,813,192
Noncurrent Liabilities:	
Deposits Payable	84,586
Funds Held for Others	3,522,272
U. S. Government Grants Refundable	6,154,763
Funds Held in Trust for Pool Participants	149,405,964
Long-Term Liabilities (Note 8)	243,340,263
	<hr/>
Total Noncurrent Liabilities	402,507,848
	<hr/>
Total Liabilities	577,321,040

**North Carolina State University**  
**Statement of Net Assets**  
**June 30, 2007**

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

**NET ASSETS**

Invested in Capital Assets, Net of Related Debt	903,982,414
Restricted for:	
Nonexpendable:	
Scholarships and Fellowships	9,582,856
Endowed Professorships	34,687,228
Departmental Uses	14,156,856
Loans	6,062,434
Other	1,992,700
Expendable:	
Scholarships and Fellowships	25,882,670
Research	17,034,541
Endowed Professorships	60,364,935
Departmental Uses	23,094,012
Loans	1,152,303
Capital Projects	147,128,417
Debt Service	3,744,711
Other	6,710,665
Unrestricted	116,200,832
Total Net Assets	<u>\$ 1,371,777,574</u>

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

**North Carolina State University**  
**Statement of Revenues, Expenses, and**  
**Changes in Net Assets**  
**For the Fiscal Year Ended June 30, 2007**

**Exhibit A-2**

**REVENUES**

Operating Revenues:

Student Tuition and Fees, Net (Note 10)	\$ 149,148,767
Federal Appropriations	25,808,162
Federal Grants and Contracts	114,272,249
State and Local Grants and Contracts	34,405,395
Nongovernmental Grants and Contracts	46,544,638
Sales and Services, Net (Note 10)	154,221,030
Interest Earnings on Loans	236,219
Other Operating Revenues, Net (Note 10)	7,227,782
	<hr/>
Total Operating Revenues	531,864,242

**EXPENSES**

Operating Expenses:

Salaries and Benefits	638,273,931
Supplies and Materials	116,573,630
Services	160,439,671
Scholarships and Fellowships	24,985,144
Utilities	29,980,249
Depreciation	42,679,521
	<hr/>
Total Operating Expenses	1,012,932,146
	<hr/>
Operating Loss	(481,067,904)

**NONOPERATING REVENUES (EXPENSES)**

State Appropriations	430,923,172
Noncapital Grants	3,766,038
Noncapital Gifts	46,824,874
Investment Income (Net of Investment Expense of \$617,001)	27,568,043
Interest and Fees on Debt	(10,552,862)
Other Nonoperating Expenses	(2,373,136)
	<hr/>
Net Nonoperating Revenues	496,156,129

Income Before Other Revenues, Expenses, Gains, or Losses	15,088,225
--	------------

Capital Appropriations	81,353,100
Capital Grants	141,158,266
Capital Gifts	9,833,289
Additions to Endowments	4,847,809
	<hr/>
Increase in Net Assets	252,280,689

**NET ASSETS**

Net Assets - July 1, 2006	1,119,496,885
	<hr/>
Net Assets - June 30, 2007	\$ 1,371,777,574
	<hr/>

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

**North Carolina State University**  
**Statement of Cash Flows**  
**For the Fiscal Year Ended June 30, 2007**

**Exhibit A-3**

**CASH FLOWS FROM OPERATING ACTIVITIES**

Received from Customers	\$ 538,986,996
Payments to Employees and Fringe Benefits	(634,180,144)
Payments to Vendors and Suppliers	(309,465,421)
Payments for Scholarships and Fellowships	(24,985,144)
Loans Issued	(4,538,224)
Collection of Loans	2,407,911
Interest Earned on Loans	194,665
Other Receipts	7,227,782
	<hr/>
Net Cash Used by Operating Activities	(424,351,579)

**CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES**

State Appropriations	430,923,172
Noncapital Grants	2,124,252
Noncapital Gifts	45,777,874
Additions to Endowments	4,847,809
Federal Family Education Loan Receipts	80,279,919
Federal Family Education Loan Disbursements	(80,420,643)
External Participation in Investment Fund	5,513,687
Other Receipts	1,376,594
	<hr/>
Net Cash Provided by Noncapital Financing Activities	490,422,664

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

Proceeds from Capital Debt	64,000,000
State Capital Appropriations	81,353,100
Capital Grants	104,333,980
Capital Gifts	4,479,926
Proceeds from Sale of Capital Assets	4,112,157
Acquisition and Construction of Capital Assets	(183,414,975)
Principal Paid on Capital Debt and Leases	(10,117,439)
Interest and Fees Paid on Capital Debt and Leases	(10,181,315)
Other Payments	(4,081,724)
	<hr/>
Net Cash Provided by Capital Financing and Related Financing Activities	50,483,710

**CASH FLOWS FROM INVESTING ACTIVITIES**

Proceeds from Sales and Maturities of Investments	771,192,701
Investment Income	20,954,964
Purchase of Investments and Related Fees	(786,056,698)
	<hr/>
Net Cash Provided by Investing Activities	6,090,967
	<hr/>
Net Increase in Cash and Cash Equivalents	122,645,762
Cash and Cash Equivalents - July 1, 2006	200,765,107
	<hr/>
Cash and Cash Equivalents - June 30, 2007	\$ 323,410,869

**North Carolina State University**  
**Statement of Cash Flows**  
**For the Fiscal Year Ended June 30, 2007**

**Exhibit A-3**

**Page 2**

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

Operating Loss	\$ (481,067,904)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:	
Depreciation Expense	42,679,521
Allowances, Write-Offs, and Amortizations	491,227
Changes in Assets and Liabilities:	
Receivables (Net)	5,584,368
Inventories	122,522
Accounts Payable and Accrued Liabilities	(591,737)
Unearned Revenue	5,958,847
Compensated Absences	2,441,919
Deposits Payable	29,658
	<hr/>
Net Cash Used by Operating Activities	<u>\$ (424,351,579)</u>

**RECONCILIATION OF CASH AND CASH EQUIVALENTS**

Current Assets:	
Cash and Cash Equivalents	\$ 166,757,092
Restricted Cash and Cash Equivalents	73,401,248
Noncurrent Assets:	
Restricted Cash and Cash Equivalents	83,252,529
	<hr/>
Total Cash and Cash Equivalents - June 30, 2007	<u>\$ 323,410,869</u>

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

Assets Acquired through a Gift	\$ 6,400,363
Change in Fair Value of Investments	(5,805,153)
Loss on Disposal of Capital Assets	(2,373,136)

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

**North Carolina State University Foundations**  
**Statement of Financial Position**  
**June 30, 2007**

**Exhibit B-1**

	<b>North Carolina State University Foundation, Inc.</b>	<b>NCSU Student Aid Association, Inc.</b>
<b>ASSETS</b>		
Cash and Cash Equivalents	\$ 2,387,038	\$ 18,290,509
Investments	13,235,370	25,967,254
Investments with University Investment Pool	68,478,848	
Cash Surrender Value of Life Insurance	133,401	214,634
Real Estate Held for Resale	331,500	7,539,929
Receivables, Net		576,712
Pledges Receivable/Promises	7,648,575	40,920,780
Prepaid Expenses		113,085
Swap Contracts		1,375,021
Notes/Loans Receivable, Net	653,746	46,350
Property and Equipment, Net	240,832	58,197,147
	<hr/>	<hr/>
Total Assets	93,109,310	153,241,421
<b>LIABILITIES</b>		
Accounts Payable and Accrued Expenses	105,955	888,599
Deferred Revenue		2,217,722
Interest Payable		313,549
Deposits Payable		54,103
Funds Held for Others	176,821	
Split Interest Agreement Obligations	4,784,897	
Notes Payable		4,141,986
Bonds Payable		69,895,000
	<hr/>	<hr/>
Total Liabilities	5,067,673	77,510,959
<b>NET ASSETS</b>		
Unrestricted	14,304,530	20,034,260
Temporarily Restricted	36,523,025	28,328,146
Permanently Restricted	37,214,082	27,368,056
	<hr/>	<hr/>
Total Net Assets	\$ 88,041,637	75,730,462

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



**North Carolina State University Foundations**  
**Statement of Activities**  
**For the Fiscal Year Ended June 30, 2007**

**Exhibit B-2**

	<b>North Carolina State University Foundation, Inc.</b>	<b>NCSU Student Aid Association, Inc.</b>
<b>CHANGES IN UNRESTRICTED NET ASSETS</b>		
Revenues and Gains:		
Contributions	\$ 154,902	\$ 8,816,184
Donated Services and Noncash Contributions	168,300	2,137,792
Annual Membership and Sales	1,017,788	313,663
Student Housing Rents		1,917,127
Investment Income	838,216	1,297,604
Net Unrealized and Realized Gains on Long-Term Investments	1,808,540	508,902
Unrealized Loss on Swap Contracts		(183,011)
Other	1,391,358	1,374,489
Total Unrestricted Revenues and Gains	5,379,104	16,182,750
Net Assets Released from Restrictions:		
Satisfaction of Program Restrictions	6,328,201	100,000
Satisfaction of Equipment Acquisition Restrictions		13,044,039
Total Net Assets Released from Restrictions	6,328,201	13,144,039
Total Unrestricted Revenues, Gains, and Other Support	11,707,305	29,326,789
Expenses:		
University Support	7,873,731	7,095,016
University Facilities Support		13,044,039
Alumni Activities	934,835	
Student Housing		3,044,315
Management and General	273,926	710,325
Fund Raising	594,843	2,870,309
Total Expenses	9,677,335	26,764,004
Increase in Unrestricted Net Assets	2,029,970	2,562,785
<b>CHANGES IN TEMPORARILY RESTRICTED NET ASSETS</b>		
Contributions	8,495,410	6,852,178
Donated Services and Noncash Contributions	205,000	51,267
Alumni Membership and Sales	181,827	
Investment Income	1,599,176	532,788
Net Unrealized and Realized Gains on Long-Term Investments	5,795,915	12,666
Unrealized Loss on Swap Contracts		(261,765)
Other		4,359,576
Net Assets Released from Restrictions:		
Satisfaction of Program Restrictions	(6,328,201)	(100,000)
Satisfaction of Equipment Acquisition Restrictions		(13,044,039)
Increase (Decrease) in Temporarily Restricted Net Assets	9,949,127	(1,597,329)
<b>CHANGES IN PERMANENTLY RESTRICTED NET ASSETS</b>		
Contributions	2,761,713	1,880,556
Investment Income	155,194	
Net Unrealized and Realized Gains on Long-Term Investments	250,934	1,767,967
Change in Value of Split Interest Agreements	(561,883)	
Other		41,024
Increase in Permanently Restricted Net Assets	2,605,958	3,689,547
Increase in Net Assets	14,585,055	4,655,003
Net Assets at Beginning of Year	73,456,582	71,075,459
Net Assets at End of Year	<u>\$ 88,041,637</u>	<u>\$ 75,730,462</u>

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

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**NORTH CAROLINA STATE UNIVERSITY  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2007**

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**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES**

- A. Financial Reporting Entity** - The concept underlying the definition of the financial reporting entity is that elected officials are accountable to their constituents for their actions. As required by accounting principles generally accepted in the United States of America, the financial reporting entity includes both the primary government and all of its component units. An organization other than a primary government serves as a nucleus for a reporting entity when it issues separate financial statements. North Carolina State University is a constituent institution of the multi-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 units, although legally separate, are, in substance, part of the University's operations and therefore, are reported as if they were part of the University. Discretely presented component units' financial data are reported in separate financial statements because of their use of different GAAP reporting models and to emphasize their legal separateness.

**Blended Component Units** - Although legally separate, the NC State Investment Fund, Inc., (Investment Fund) and the NC State University Partnership Corporation (Corporation), component units of the University, are reported as if they were part of the University.

The Investment Fund is governed by a Members Board consisting of six ex officio directors and five elected representatives. The Investment Fund's purpose is to support the University by operating an investment fund for charitable, nonprofit foundations, associations, trusts, endowments, and funds that are organized and operated primarily to support the University. The Investment Fund is a governmental external investment pool. Because the majority of the Members Board of the Investment Fund consist of University administrators and Board Members

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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and the Investment Fund's primary purpose is to benefit North Carolina State University, its financial statements have been blended with those of the University.

The Corporation is governed by a Board of Directors appointed by the Chancellor of the University. The Corporation's purpose is to support and benefit the University with the aims of creating new knowledge and improving the lives of the people of North Carolina. The Corporation formed NC State University Centennial Development, LLC on January 25, 2002, to develop, construct, own, finance, manage and otherwise deal with a nonprofit hotel, golf course, conference center and related meeting facilities on the Centennial Campus as outlined in the Campus Master Plan. In addition, the Corporation formed NC State Upfit, LLC on October 27, 2006, to develop, construct, own, finance, manage and otherwise upfit facilities and other infrastructure on Centennial Campus and it formed NC State Residence, LLC on October 27, 2006, to develop, construct, own, finance, manage and otherwise deal with a nonprofit chancellor's residence on Centennial Campus. Also, the Corporation formed NC State CBC Land I, LLC on June 1, 2007, to acquire, develop, own, lease, hold, manage, sell, and otherwise exercise all right of ownership of land and flex lab facilities on Centennial Biomedical Campus. Because the Corporation's Board is appointed by the Chancellor and its sole purpose is to support and benefit the University, the Corporation and the LLCs are considered part of the University for financial reporting purposes.

Separate financial statements for the Investment Fund may be obtained from the Foundations Accounting and Investments Office, Campus Box 7207, Raleigh, NC 27695, or by calling (919) 513-7149. Financial information relative to the Corporation and the LLCs may be obtained from the President of the Board of Directors, Campus Box 7201, Raleigh, NC 27695, or by calling (919) 515-2155. 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 Units** – North Carolina State University Foundation, Inc. (Foundation) and NCSU Student Aid Association, Inc. (Athletic Club) are legally separate not-for-profit corporations and are reported as discretely presented component units based on the nature and significance of their relationship to the University.

The Foundation and Athletic Club are legally separate, tax-exempt component units of the University. These entities act primarily as fund-

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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raising organizations to supplement the resources that are available to the University in support of its programs. Separate Boards of Directors govern these entities independent of the University's Board of Trustees. Although the University does not control the timing or amount of receipts from these entities, the majority of resources, or income thereon, that these entities hold and invest are restricted to the activities of the University by the donors. Because these restricted resources held by these entities can only be used by, or for the benefit of the University, these entities are considered component units of the University and are reported in separate financial statements because of the difference in their reporting model, as described below.

The Foundation and Athletic Club are private not-for-profit organizations that report their financial results under Financial Accounting Standards Board (FASB) Statements. As such, certain revenue recognition criteria and presentation features are different from the Governmental Accounting Standards Board (GASB) revenue recognition criteria and presentation features. No modifications have been made to their financial information in the University's financial reporting entity for these differences.

During the year ended June 30, 2007, the Foundation distributed \$7,517,015 to the University for both restricted and unrestricted purposes. Complete financial statements for the Foundation can be obtained from the Foundations Accounting and Investments Office, Campus Box 7207, Raleigh, NC 27695, or by calling (919) 513-7149.

During the year ended June 30, 2007, the Athletic Club distributed \$10,058,757 to the University for both restricted and unrestricted purposes. Complete financial statements for the Athletic Club can be obtained from the NCSU Student Aid Association, PO Box 37100, Raleigh, NC 27627, or by calling (919) 865-1500.

- 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.

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.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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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, for proprietary activities, 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, regardless of the timing of the cash flows.

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

- D. Cash and Cash Equivalents** – This classification includes undeposited receipts, petty cash, cash on deposit with private bank accounts, savings accounts, money market accounts, cash on deposit with fiscal agents, and deposits held by the State Treasurer in the short-term investment 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, foreign equity mutual funds, money market funds, certificates of deposit, limited partnerships, real estate investment trusts, real estate, alternative investments such as private equity, and other asset holdings by the University. Private equities include venture capital partnerships, buy-outs, and international funds. Except for money market funds, certificates of deposit, private equity, real estate not held by a governmental external investment pool, and other asset holdings, investments are accounted for at fair value, as determined by quoted market prices, or an amount determined by management if quoted market prices are not available. The net increase (decrease) in the fair value of investments is recognized as a component of investment income.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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Money market funds, certificates of deposit, real estate not held by a governmental external investment pool and other asset holdings are reported at cost, if purchased, or at fair value or appraised value at date of gift, if donated. Private equity funds consist primarily of investments that are not readily marketable. Investments in these categories, which are managed externally, are valued utilizing the most current information provided by the general partner.

- 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 and merchandise for resale, are valued at the lower of cost or market value using the first-in, first-out method. Exceptions are the bookstore, which uses the retail inventory method, and physical plant, which uses the moving weighted average method.
- H. Capital Assets** – Capital assets are stated at cost at date of acquisition or fair value at date of donation in the case of gifts. The value of assets constructed includes all material direct and indirect construction costs. Interest costs incurred are capitalized during the period of construction.

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

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 15 to 75 years for general infrastructure, 10 to 50 years for buildings, and 3 to 15 years for equipment.

The University does not capitalize its collections. These collections adhere to the University's policy to maintain for public exhibition, education or research; protect, keep unencumbered, care for and preserve; and requires proceeds from their sale to be used to acquire other collection items. Accounting principles generally accepted in the United

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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States of America permit collections maintained in this manner to be charged to operations at time of purchase rather than be capitalized.

- I. Restricted Assets** – Unexpended proceeds of revenue bonds and unexpended capital contributions are classified as restricted assets because their use is limited by applicable bond covenants or donor/grantor agreements. Certain other assets are classified as restricted because their use is limited by external parties or statute.
- J. Funds Held in Trust for Pool Participants** – Funds held in trust for pool participants represent the external portion of the University’s governmental external investment pool more fully described in Note 2.
- K. Noncurrent Long-Term Liabilities** – Noncurrent long-term liabilities include principal amounts of bonds payable, capital lease obligations, and compensated absences that will not be paid within the next fiscal year.

Bonds payable are reported net of unamortized premium or discount. The University amortizes bond premiums/discounts over the life of the bonds using the straight-line method. Losses on refundings and issuance costs on bonds payable are not material to the accompanying financial statements and are expensed in the year incurred.

- L. Compensated Absences** - The University’s policy is to record the cost of vacation leave when earned. The policy provides for a maximum accumulation of unused vacation leave of 30 days which can be carried forward each January 1 or for which an employee can be paid upon termination of employment. When classifying compensated absences into current and noncurrent, leave is considered taken using a last-in, first-out (LIFO) method. Also, any accumulated vacation leave in excess of 30 days at year-end is converted to sick leave. Under this policy, the accumulated vacation leave for each employee at June 30 equals the leave carried forward at the previous December 31 plus the leave earned, less the leave taken between January 1 and June 30.

In addition to the vacation leave described above, compensated absences include the accumulated unused portion of the special annual leave bonuses awarded by the North Carolina General Assembly. The bonus leave balance on December 31 is retained by employees and transferred into the next calendar year. It is not subject to the limitation on annual leave carried forward described above and is not subject to conversion to sick leave.

There is no liability for unpaid accumulated sick leave because the University has no obligation to pay sick leave upon termination or



## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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retirement. However, additional service credit for retirement pension benefits is given for accumulated sick leave upon retirement.

**M. Net Assets** – The University’s net assets are classified as follows:

**Invested in Capital Assets, Net of Related Debt** – This represents the University’s total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of invested in capital assets, net of related debt.

**Restricted Net Assets – Nonexpendable** – Nonexpendable restricted net assets include endowments and similar type assets whose use is limited by donors or other outside sources, and, as a condition of the gift, the principal is to be maintained in perpetuity.

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

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

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

**N. 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 operating revenues in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. To the extent that

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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revenues from these programs are used to satisfy tuition, fees, and other charges, the University has recorded a scholarship discount.

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

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

- P. 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, University Graphics, the Copy Center, the Creamery, Telecommunications, Physical Plant, and Motor Pool. In addition, the University has other miscellaneous sales and service units that operated either on a reimbursement or charge basis. All internal sales activities to University departments from auxiliary operations and sales and service units have been eliminated in the accompanying financial statements. These eliminations are recorded by removing the revenue and expense in the auxiliary operations and sales and service units and, if significant, allocating any residual balances to those departments receiving the goods and services during the year.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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### NOTE 2 - DEPOSITS AND INVESTMENTS

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

At June 30, 2007, the amount shown on the Statement of Net Assets as cash and cash equivalents includes \$322,592,261 which represents the University's equity position in the State Treasurer's Short-Term Investment Fund. 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 1.6 years as of June 30, 2007. Assets and shares of the Short-Term Investment Fund are valued at amortized cost, which approximates fair value. Deposit and investment risks associated with the State Treasurer's Investment Pool (which includes the State Treasurer's Short-Term Investment Fund) are included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.ncosc.net/> and clicking on "Financial Reports," or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

Cash on hand at June 30, 2007, was \$21,230. The carrying amount of the University's deposits not with the State Treasurer, including \$400,000 in certificates of deposit, was \$1,197,378 and the bank balance was \$1,227,402. 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 follows the Cash Management Plan (Plan) approved by the North Carolina Office of State Controller. As provided by the Plan, all funds belonging to the University are deposited with the State Treasurer pursuant to G.S. 147-77 and G.S. 147-69.1. As provided by the Plan, imprest checking accounts are established with outside banks when considered effective in meeting management objectives. All imprest checking accounts are authorized by the University Treasurer and are

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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limited to the minimum amount needed for sanctioned purposes. In addition, pursuant to G.S. 116-36(e), the University invests certain endowment funds with outside bank accounts. As of June 30, 2007, \$534,482 of the bank balance was exposed to custodial credit risk.

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

G.S. 147-69.1(c), applicable to the State's General Fund, and G.S. 147-69.2, applicable to institutional trust funds, authorize the State Treasurer to invest in the following: obligations of or fully guaranteed by the United States; obligations of certain federal agencies; repurchase agreements; obligations of the State of North Carolina; time deposits of specified institutions; prime quality commercial paper, and asset-backed securities with specified ratings. Also, G.S. 147-69.1(c) authorizes the following: specified bills of exchange or time drafts and corporate bonds and notes with specified ratings. G.S. 147-69.2 authorizes the following: general obligations of other states; general obligations of North Carolina local governments; and obligations of certain entities with specified ratings.

In accordance with the bond resolutions, bond proceeds and debt service funds are invested in obligations that will by their terms mature on or before the date funds are expected to be required for expenditure or withdrawal.

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

Investments of the Investment Fund, a University component unit, 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.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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Investments are subject to the following risks.

*Interest Rate Risk:* Interest rate risk is the risk the University may face should interest rate variances affect the fair value of investments. The University does not have a formal policy that addresses interest rate risk.

*Credit Risk:* Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The University does not have a formal policy that addresses credit risk.

*Custodial Credit Risk:* 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.

*Foreign Currency Risk:* Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. The University does not have a formal policy for foreign currency risk.

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

**Long-Term Investment Pool** - This is an internal investment pool that is utilized for the investment of the endowment funds. Pool ownership is measured using the unit value method. Under this method, each participating fund's investment balance is determined on a market value basis. The investment strategy, including the selection of investment managers, is based on the directives of the University's Endowment Board. This pool also participates in the Investment Fund.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

The following table presents the fair value of investments by type and investments subject to interest rate risk at June 30, 2007, for the Long-Term Investment Pool.

### *Long-Term Investment Pool* (Excludes Amounts Reported in the Investment Fund)

Investment Type	Fair Value	Investment Maturities (in Years)			
		Less Than 1	1 to 5	6 to 10	More than 10
<b>Debt Securities</b>					
U.S. Treasuries	\$ 650,577	\$ 0	\$ 0	\$ 148,062	\$ 502,515
U.S. Treasury Strips	29,951				29,951
U.S. Agencies	359,815			103,892	255,923
Mortgage Pass Throughs	1,092,678			114,770	977,908
Collateralized Mortgage Obligations	815,469				815,469
State and Local Government	148,467		120,198	28,269	
Asset-Backed Securities	92,683				92,683
Mutual Bond Funds	9,674,133	204,381	6,615,950	2,110,597	743,205
Money Market Funds	270,216	270,216			
Domestic Corporate Bonds	1,155,748	76,112	465,853	362,121	251,662
Foreign Corporate Bonds	147,291		88,574	43,162	15,555
	<u>14,437,028</u>	<u>\$ 550,709</u>	<u>\$ 7,290,575</u>	<u>\$ 2,910,873</u>	<u>\$ 3,684,871</u>
<b>Other Securities</b>					
Pooled Investments	392,091				
Venture Capital	6,709,491				
	<u>6,709,491</u>				
<b>Total Long-Term Investment Pool</b>	<u>\$ 21,538,610</u>				

At June 30, 2007, investments in the Long-Term Investment Pool had the following credit quality distribution for securities with credit exposure (based on Moody's and/or S&P ratings):

Investment Type	Fair Value	AAA Aaa	AA Aa	A	BBB Baa	BB/Ba and Below	Unrated
<b>Debt Securities:</b>							
Mortgage Pass Throughs	\$ 1,056,034	\$ 1,056,034	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0
Collateralized Mortgage Obligations	815,469	613,377	71,568	57,316	29,251	22,588	21,369
State and Local Government	148,467	129,780	18,687				
Asset-Backed Securities	92,683	92,683					
Mutual Bond Funds	9,674,133						9,674,133
Money Market Funds	270,216	43,757		153,439			73,020
Domestic Corporate Bonds	1,155,748			305,797	562,509	287,442	
Foreign Corporate Bonds	147,291		55,983	15,750	51,048	24,510	
	<u>13,360,041</u>	<u>\$ 1,935,631</u>	<u>\$ 146,238</u>	<u>\$ 532,302</u>	<u>\$ 642,808</u>	<u>\$ 334,540</u>	<u>\$ 9,768,522</u>
<b>Debt Securities Exempt From Credit Disclosure:</b>							
U.S. Treasuries	650,577						
U.S. Treasury Strips	29,951						
U.S. Agencies	359,815						
Mortgage Pass Throughs	36,644						
	<u>1,437,028</u>						
<b>Total Long-Term Investment Pool</b>	<u>\$ 14,437,028</u>						

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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**Investment Fund** - The Investment Fund began operations in April 1999 and is classified as a non-rated 2a7-like governmental external investment pool that is not registered with the Securities and Exchange Commission (SEC) as an investment company, but has a policy that it will, and does, operate in a manner consistent with the SEC's Rule 2a7 of the Investment Company Act of 1940. The Investment Fund is utilized as one of the investment managers for the Long-Term Investment Pool and the North Carolina State University Foundation, Inc., a discretely presented component unit in the accompanying financial statements, (the Investment Fund's internal participants). Other affiliated organizations not included in the University's reporting entity represent the pool's external participants. The participants purchase equity in the Fund on an average cost basis. Under this method, each participant has its own distinct asset pool (investments) on the custodian's trust system. Sales and purchases are processed separately in each distinct account. The accounting reflects each participant account's own realized gains or losses based on its distinct transactions. The external portion of the pool is presented in the accompanying financial statements as "Funds Held in Trust for Pool Participants."

The Investment Fund is not subject to any formal oversight other than that provided by the Investment Fund Members Board or its Board of Directors. The Members Board is responsible for adopting investment objectives and policies and for monitoring policy implementation and investment performance. The Members Board has chosen not to make individual security selection decisions. The Board of Directors has the responsibility to oversee the allocation of the Investment Fund's portfolio among the asset classes and investment vehicles.

SEI, Inc. is the institutional manager and custodian of the Investment Fund and provides the University with quarterly statements defining income and fair value information, which is then allocated among the pool's participants. There are no involuntary participants in the pool. The University has not provided or obtained any legally binding guarantees during the period to support the value for the pool's investments. The annual financial report for the Investment Fund may be obtained from the Foundations Accounting and Investments Office, Campus Box 7207, Raleigh, NC 27695, or by calling (919) 513-7149.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### *Investment Fund*

The following table presents the fair value of investments by type and investments subject to interest rate risk at June 30, 2007, for the Investment Fund.

Investment Type	Fair Value	Investment Maturities (in Years)			
		Less Than 1	1 to 5	6 to 10	More than 10
<b>Debt Securities</b>					
Mutual Bond Funds	\$ 102,553,747	\$ 0	\$ 0	\$ 85,398,257	\$ 17,155,490
Money Market Funds	1,019	1,019			
	<u>102,554,766</u>	<u>\$ 1,019</u>	<u>\$ 0</u>	<u>\$ 85,398,257</u>	<u>\$ 17,155,490</u>
<b>Other Securities</b>					
International Mutual Funds	49,620,710				
Other Mutual Funds	107,587,363				
Real Estate Investment Trust	15,476,987				
Hedge Funds	65,297,070				
Limited Partnerships	6,779,817				
	<u>347,316,713</u>				
<b>Total Investment Fund</b>	<u>\$ 347,316,713</u>				

At June 30, 2007, investments in the Investment Fund had the following credit quality distribution for securities with credit exposure (based on Moody's and/or S&P ratings):

Investment Type	Fair Value	AA/Aa	Unrated
<b>Debt Securities</b>			
Mutual Bond Funds	\$ 102,553,747	\$ 0	\$ 102,553,747
Money Market Funds	1,019	1,019	
	<u>102,554,766</u>	<u>\$ 1,019</u>	<u>\$ 102,553,747</u>
<b>Title Investment Fund</b>	<u>\$ 102,554,766</u>	<u>\$ 1,019</u>	<u>\$ 102,553,747</u>

As of June 30, 2007, the Investment Fund was invested in a foreign equity mutual fund and an emerging markets debt mutual fund with fair values of \$49,620,710 and \$17,155,490, respectively which had foreign currency exposure.



## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

**Non-Pooled Investments** - The following table presents the fair value of investments by type and investments subject to interest rate risk at June 30, 2007, for the University's non-pooled investments.

### *Non-Pooled Investments*

Investment Type	Fair Value	Investment Maturities (in Years)			
		Less Than 1	1 to 5	6 to 10	More than 10
<b>Debt Securities</b>					
Money Market Funds	\$ 280,012	<u>\$ 280,012</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>
<b>Other Securities</b>					
Certificates of Deposit	400,000				
Investments in Real Estate	20,153,035				
Domestic Stocks	973,438				
Venture Capital	533,500				
Collections and Mineral Rights	<u>69,878</u>				
<b>Total Non-Pooled Investments</b>	<u>\$ 22,409,863</u>				

Certificates of deposit reported as investments are also a component of the deposit totals reported in the deposits section of this note.

At June 30, 2007, investments in Non-Pooled Investments had the following credit quality distribution for securities with credit exposure (based on Moody's and/or S&P ratings):

Investment Type	Fair Value	AAA Aaa
<b>Debt Securities</b>		
Money Market Funds	<u>\$ 280,012</u>	<u>\$ 280,012</u>

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

**Total Investments** – The following table presents the fair value of the total investments at June 30, 2007:

<b>Investment Type</b>	<u>Fair Value</u>
<i>Total Investments</i>	
Debt Securities	
U.S. Treasuries	\$ 650,577
U.S. Treasury Strips	29,951
U.S. Agencies	359,815
Mortgage Pass Throughs	1,092,678
Collateralized Mortgage Obligations	815,469
State and Local Government	148,467
Asset-Backed Securities	92,683
Mutual Bond Funds	112,227,880
Money Market Funds	551,247
Domestic Corporate Bonds	1,155,748
Foreign Corporate Bonds	147,291
Other Securities	
Certificates of Deposit	400,000
International Mutual Funds	49,620,710
Other Mutual Funds	107,587,363
Investments in Real Estate	20,153,035
Real Estate Investment Trust	15,476,987
Hedge Funds	65,297,070
Limited Partnerships	6,779,817
Pooled Investments	392,091
Domestic Stocks	973,438
Venture Capital	7,242,991
Collections and Mineral Rights	69,878
Total Investments	<u>\$ 391,265,186</u>

Total investments include \$68,478,848 held in the “Investment Fund” for the North Carolina State University Foundation, Inc. This amount is excluded from the University proper financial statements and included in the accompanying component unit financial statements.

### NOTE 3 - ENDOWMENT INVESTMENTS

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

Investment return of the University’s endowment funds is predicated on the total return concept (yield plus appreciation). Annual payouts from the University pooled endowment funds are determined by applying 4% (the Board approved spending rate) to the average market value of the Long-Term

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Investment Pool (for a 20 quarter period), divided by the number of investment units in the pool to determine the "average spending amount" per unit of investment. The individual endowment fund payout or spending budget is then determined by applying the "average spending amount" to the number of investment units held by the individual endowment fund. To the extent that the total return for the current year exceeds the payout, the excess is added to principal. If current year earnings do not meet the payout requirements, the University uses accumulated income and appreciation from restricted, expendable net asset endowment balances to make up the difference. At June 30, 2007, endowment net assets of \$122,768,064 were available to be spent, of which \$105,323,743 was restricted to specific purposes.

### NOTE 4 - RECEIVABLES

Receivables at June 30, 2007, were as follows:

	<u>Gross Receivables</u>	<u>Less Allowance for Doubtful Accounts</u>	<u>Net Receivables</u>
<b>Current Receivables:</b>			
Students	\$ 4,432,360	\$ 2,912,251	\$ 1,520,109
Accounts	18,756,167	1,507,588	17,248,579
Intergovernmental	10,676,394		10,676,394
Interest on Loans	401,536	322,362	79,174
Other	189,948		189,948
<b>Total Current Receivables</b>	<u>\$ 34,456,405</u>	<u>\$ 4,742,201</u>	<u>\$ 29,714,204</u>
<b>Notes Receivable:</b>			
<b>Notes Receivable - Current:</b>			
Federal Loan Programs	\$ 1,012,697	\$ 24,130	\$ 988,567
Institutional Student Loan Programs	195,492	5,755	189,737
Other	35,573		35,573
<b>Total Notes Receivable - Current</b>	<u>\$ 1,243,762</u>	<u>\$ 29,885</u>	<u>\$ 1,213,877</u>
<b>Notes Receivable - Noncurrent:</b>			
Federal Loan Programs	\$ 11,251,647	\$ 759,049	\$ 10,492,598
Institutional Student Loan Programs	547,633	162,217	385,416
Other	2,214,427		2,214,427
<b>Total Notes Receivable - Noncurrent</b>	<u>\$ 14,013,707</u>	<u>\$ 921,266</u>	<u>\$ 13,092,441</u>

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### NOTE 5 - CAPITAL ASSETS

A summary of changes in the capital assets for the year ended June 30, 2007, is presented as follows:

	Balance July 1, 2006	Increases	Decreases	Balance June 30, 2007
Capital Assets, Nondepreciable:				
Land	\$ 23,330,450	\$ 247,921	\$ 0	\$ 23,578,371
Construction in Progress	97,809,121	92,418,131	36,209,108	154,018,144
<b>Total Capital Assets, Nondepreciable</b>	<u>121,139,571</u>	<u>92,666,052</u>	<u>36,209,108</u>	<u>177,596,515</u>
Capital Assets, Depreciable:				
Buildings	1,025,273,474	105,101,867	2,689,874	1,127,685,467
Machinery and Equipment	223,790,341	17,274,050	14,438,397	226,625,994
General Infrastructure	104,423,851	11,658,292		116,082,143
<b>Total Capital Assets, Depreciable</b>	<u>1,353,487,666</u>	<u>134,034,209</u>	<u>17,128,271</u>	<u>1,470,393,604</u>
Less Accumulated Depreciation/Amortization for:				
Buildings	273,458,658	25,164,401	1,203,102	297,419,957
Machinery and Equipment	153,082,709	14,792,787	13,300,065	154,575,431
General Infrastructure	22,330,425	2,722,333		25,052,758
<b>Total Accumulated Depreciation</b>	<u>448,871,792</u>	<u>42,679,521</u>	<u>14,503,167</u>	<u>477,048,146</u>
<b>Total Capital Assets, Depreciable, Net</b>	<u>904,615,874</u>	<u>91,354,688</u>	<u>2,625,104</u>	<u>993,345,458</u>
<b>Capital Assets, Net</b>	<u>\$ 1,025,755,445</u>	<u>\$ 184,020,740</u>	<u>\$ 38,834,212</u>	<u>\$ 1,170,941,973</u>

### NOTE 6 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2007, were as follows:

	Amount
Accounts Payable	\$ 31,986,609
Accrued Payroll	7,948,537
Contract Retainage	6,522,560
Other	508,771
<b>Total Accounts Payable and Accrued Liabilities</b>	<u>\$ 46,966,477</u>

### NOTE 7 - SHORT-TERM DEBT – COMMERCIAL PAPER PROGRAM

The University has available Commercial Paper Program financing for short-term credit up to \$100,000,000 to finance capital construction projects. The University's available funds are pledged to the Commercial Paper Program financing with the anticipation of converting to general revenue bond financing in the future. As of June 30, 2007, \$80,000,000 in Tax-Exempt Commercial Paper was outstanding.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Short-term debt activity for the year ended June 30, 2007, was as follows:

	Balance July 1, 2006	Draws	Repayments	Balance June 30, 2007
Commercial Paper Program	\$ 16,000,000	\$ 64,000,000	\$ 0	\$ 80,000,000

### NOTE 8 - LONG-TERM LIABILITIES

**A. Changes in Long-Term Liabilities** - A summary of changes in the long-term liabilities for the year ended June 30, 2007, is presented as follows:

	Balance July 1, 2006	Additions	Reductions	Balance June 30, 2007	Current Portion
Bonds Payable	\$ 203,360,000	\$ 0	\$ 9,995,000	\$ 193,365,000	\$ 8,230,000
Add/Deduct Premium/Discount	7,813,722		474,516	7,339,206	
Total Bonds Payable	211,173,722		10,469,516	200,704,206	8,230,000
Capital Leases Payable	273,821		122,439	151,382	92,512
Compensated Absences	50,825,595	33,315,441	30,769,707	53,371,329	2,564,142
<b>Total Long-Term Liabilities</b>	<b>\$ 262,273,138</b>	<b>\$ 33,315,441</b>	<b>\$ 41,361,662</b>	<b>\$ 254,226,917</b>	<b>\$ 10,886,654</b>

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

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### B. Revenue Bonds Payable - The University was indebted for revenue 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, 2007	Principal Outstanding June 30, 2007
<b>STUDENT HOUSING SYSTEM</b>						
Resident Hall Improvement Project	(1) (A)	3.25-5%	10/01/2010	\$ 15,770,000	\$ 9,575,000	\$ 6,195,000
Housing System Project	(1) (B)	5-5.5%	10/01/2010	3,020,000	1,620,000	1,400,000
Total Student Housing System				18,790,000	11,195,000	7,595,000
<b>DINING HALL SYSTEM</b>						
Dining Hall System Refunding Bonds	(2) 1996	4-5.3%	02/01/2012	2,345,000	1,235,000	1,110,000
<b>STUDENT HEALTH SYSTEM</b>						
Student Health Facility Project	(3) (A)	3.25-5.25%	10/01/2013	5,615,000	2,535,000	3,080,000
<b>ATHLETIC SYSTEM</b>						
Entertainment and Sports Arena Project	(4) (A)	3.25-5.25%	10/01/2018	6,325,000	1,880,000	4,445,000
<b>CENTENNIAL CAMPUS SYSTEM</b>						
Centennial Campus Projects	(5) 1997A	6.55-7.04%	12/15/2010	7,765,000	5,105,000	2,660,000
Centennial Campus Projects	(5) 1999A	4.574%*swap	12/15/2019	13,500,000	1,700,000	11,800,000
Total Centennial Campus System				21,265,000	6,805,000	14,460,000
<b>CENTRAL STORES</b>						
Central Stores Expansion Project	(6) (B)	5-5.75%	10/01/2020	3,370,000	675,000	2,695,000
<b>GENERAL REVENUE</b>						
Refund Housing System Series L&M	(7) 2002B	2-5%	10/01/2014	8,800,000	2,600,000	6,200,000
Centennial Campus Projects	(7) 2002C	2.75-6.45%	10/01/2013	7,160,000	2,450,000	4,710,000
Housing System Projects/ Doak Field Project	(7) 2003A	2-5%	10/01/2018	26,735,000	270,000	26,465,000
Housing System Projects/ Doak Field Project	(7) 2003B	3.54%*swap	10/01/2027	45,660,000	910,000	44,750,000
Various Construction Projects	(7) 2005A	3-5%	10/01/2025	81,615,000	3,760,000	77,855,000
Total General Revenue				169,970,000	9,990,000	159,980,000
Total Bonds Payable (principal only)				\$ 227,680,000	\$ 34,315,000	193,365,000
Less: Unamortized Discount						64,385
Plus: Unamortized Premium						7,403,591
Total Bonds Payable						\$ 200,704,206

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

(B) The University of North Carolina System Pool Revenue Bonds, Series 2000

Designated student fees and revenue streams related to the systems financed above have been pledged for the payment of these bonds. In addition, fund reservations required by the Bond Indentures have been established and recorded as restricted net assets. The following revenues as summarized in Note 10 have been pledged or are security for the bonds.

- |  |                                |
|--|--------------------------------|
| (1) Residential Life Revenues (Housing | (5) Centennial Campus Revenues |
| (2) Dining Revenues                    | (6) Central Stores Revenues    |
| (3) Student Health Revenues            | (7) Available Funds            |
| (4) Athletic Revenues                  |                                |

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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Available funds, as defined in the General Indenture dated October 1, 2001, are any funds of NC State in each fiscal year remaining after satisfying debt obligations excluding (1) State appropriations, (2) tuition payments, (3) funds restricted by gift, grant, or payee, (4) revenues from special facilities, and (5) funds restricted by law. Available funds are not pledged to the trustee, but rather are the source from which principal and interest on the bonds will be paid.

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

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

**The North Carolina State University at Raleigh Variable Rate Revenue Bonds (Centennial Campus Projects), Series 1999A:** On September 22, 1999, the University issued tax-exempt variable rate revenue demand bonds in the amount of \$13,500,000 that have a final maturity date of December 15, 2019. The bonds are subject to mandatory sinking fund redemption that began on December 1, 2000. The University’s proceeds of this issuance were used to (i) discharge a portion of a loan from Wachovia Bank, N.A., the proceeds from which were used for the construction and equipping of a building known as the Partners II Building located on the Centennial Campus of NC State, (ii) paying the cost of relocating utility easements on the Centennial Campus of NC State, and (iii) pay the costs incurred in connection with the issuance of the 1999A bonds.

While bearing interest at a weekly rate, the bonds are subject to purchase on demand with seven days notice and delivery to the paying agent, The Bank of New York. Upon notice from the paying agent, the remarketing agent, Lehman Brothers, Inc., has agreed to exercise its best efforts to remarket the bonds for which a notice of purchase has been received.

Under a Standby Bond Purchase Agreement (Agreement) between the Board of Governors of the University of North Carolina and Wachovia Bank, N.A., a Liquidity Facility has been established for the Trustee (The Bank of New York) to draw amounts sufficient to pay the purchase price and accrued interest on bonds delivered for purchase when remarketing proceeds or other funds are not available. This Agreement requires a commitment fee equal to 0.11% of the available commitment,

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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payable quarterly in arrears, beginning on October 1, 1999, and on each January 1, April 1, July 1, and October 1 thereafter until the expiration date or the termination date of the Agreement.

Under the Agreement, any bonds purchased through the Liquidity Facility become Liquidity Provider Bonds and shall, from the date of such purchase and while they are Liquidity Provider Bonds, bear interest at the Liquidity Provider Rate (the greater of the bank prime commercial lending rate and Federal Funds Rate plus 0.5%). Upon remarketing of Liquidity Provider Bonds and the receipt of the sales price by the Liquidity Provider, such bonds are no longer considered Liquidity Provider Bonds. Payment of the interest on the Liquidity Provider Bonds is due the first business day of each month in which Liquidity Provider Bonds are outstanding. At June 30, 2007, there were no Liquidity Provider Bonds held by the Liquidity Facility. The original Liquidity Facility expiration date has been extended and is scheduled to expire on September 15, 2008, unless otherwise extended based on the terms of the Agreement.

Upon expiration or termination of the Agreement, the University is required to redeem (purchase) the Liquidity Provider Bonds held by the Liquidity Facility in 20 quarterly installments, beginning the first business day that is at least 180 days following such expiration date or termination date along with accrued interest at the Liquidity Provider Rate. In the event the entire issue of \$11,800,000 of demand bonds was “put” and not resold, the University would be required to pay \$2,904,037 a year for five years under this agreement assuming an 8.25% interest rate.

**The North Carolina State University at Raleigh General Revenue Bonds, Series 2003B:** On June 20, 2003, the University issued tax-exempt variable rate revenue demand bonds in the amount of \$45,660,000 that have a final maturity date of October 1, 2027. The bonds are subject to mandatory sinking fund redemption that began on October 1, 2004. The University’s proceeds of this issuance were used to pay a portion of the costs of certain improvements on the campus of the University, to refund certain debt previously incurred for that purpose, and to pay the costs incurred in connection with the issuance of the 2003B bonds.

While bearing interest at a weekly rate, the bonds are subject to purchase on demand with seven days notice and delivery to the paying agent, The Bank of New York. Upon notice from the paying agent, the remarketing agent, UBS Financial Services Inc., has agreed to exercise its best efforts to remarket the bonds for which a notice of purchase has been received.



## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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Under a Standby Bond Purchase Agreement (Agreement) between the Board of Governors of the University of North Carolina and Bayerische Landesbank, a Liquidity Facility has been established for the Trustee (The Bank of New York) to draw amounts sufficient to pay the purchase price and accrued interest on bonds delivered for purchase when remarketing proceeds or other funds are not available. This Agreement requires a commitment fee equal to 0.13% of the available commitment, payable quarterly in arrears, beginning on July 1, 2003, and on each October 1, January 1, April 1, and July 1 thereafter until the expiration date or the termination date of the Agreement.

Under the Agreement, any bonds purchased through the Liquidity Facility become Liquidity Provider Bonds and shall, from the date of such purchase and while they are Liquidity Provider Bonds, bear interest at the Liquidity Provider Rate (the greater of the bank prime commercial lending rate and Federal Funds Rate plus 0.5%). Upon remarketing of Liquidity Provider Bonds and the receipt of the sales price by the Liquidity Provider, such bonds are no longer considered Liquidity Provider Bonds. Payment of the interest on the Liquidity Provider Bonds is due the first business day of each month in which Liquidity Provider Bonds are outstanding. At June 30, 2007, there were no Liquidity Provider Bonds held by the Liquidity Facility. The original Liquidity Facility expiration date has been extended and is scheduled to expire on November 30, 2015, unless otherwise extended based on the terms of the Agreement.

Upon expiration or termination of the Agreement, the University is required to redeem (purchase) the Liquidity Provider Bonds held by the Liquidity Facility in 20 quarterly installments, beginning the first business day of January, April, July, or October, whichever first occurs on or following the Purchase Date along with accrued interest at the Liquidity Provider Rate. In the event the entire issue of \$44,750,000 of demand bonds was “put” and not resold, the University would be required to pay \$11,013,190 a year for five years under this agreement assuming an 8.25% interest rate.

### **Interest Rate Swaps:**

*Objective:* In order to protect against the potential of rising interest rates, the University entered into two separate pay-fixed, receive-variable interest rate swaps at a cost anticipated to be less than what the University would have paid to issue fixed-rate debt.

*Terms, fair values, and credit risk:* The University’s swap agreements contain scheduled reductions to outstanding notional amounts that are

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

expected to approximately follow scheduled or anticipated reductions in the associated bonds payable category. The terms, fair values, and credit ratings of the outstanding swaps as of June 30, 2007, were as follows (dollars in thousands):

Associated Bond Issue	Notional Amounts	Effective Date	Fixed Rate Paid	Variable Rate Received	Fair Values	Swap Termination Date	Counterparty Credit Rating Moody's/S&P/Fitch
Centennial Campus 1999A	\$ 8,200	10/1/1999	4.574%	67% of LIBOR	\$ (429)	12/1/2019	A1 / AA- / AA-
General Revenue 2003B	24,655	6/20/2003	3.54%	75% of LIBOR	1,952	10/1/2027	Aaa / AA+ / AA
Total	<u>\$ 32,855</u>				<u>\$ 1,523</u>		

Because rates have changed since the effective dates of the swaps, the 1999A swap has a negative fair value as of June 30, 2007. The negative fair value may be countered by a reduction in total interest payments required under the variable-rate bonds, creating lower synthetic interest rates. Because the coupons on the University's variable-rate bonds adjust to changing interest rates, the bonds do not have corresponding fair value increases. The fair values are the market values as of June 30, 2007.

As of June 30, 2007, the University was exposed to credit risk on the swap with a positive fair value. The University's maximum possible loss is equivalent to the positive fair value of the swap. The swap agreements require termination should the University's or the counterparty's credit rating fall below either Baa2 as issued by Moody's or BBB as issued by S&P or Fitch. Also, under the terms of the swap agreements, should one party become insolvent or otherwise default on its obligations, provisions permit the nondefaulting party to accelerate and terminate all outstanding transactions. To mitigate the potential for credit risk, if the counterparty's credit quality falls below A3 as determined by Moody's or A- as determined by S&P, the swap will be collateralized by the counterparty with cash, U.S. government or agency securities. If the counterparty is required to collateralize, then the collateral will be posted with a third party custodian or secured party. The swap agreements entered into by the University are held with separate counterparties. All the counterparties are rated A1 or better.

*Basis risk:* The University is exposed to basis risk on the swaps when the variable payment received is based on an index other than the Securities Industry and Financial Markets Swap Index (SIFMA). Should the relationship between LIBOR and SIFMA move to convergence, the expected cost savings may not be realized. As of June 30, 2007, the SIFMA rate was 3.73%, whereas 67% of LIBOR was 3.56% and 75% of

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

LIBOR was 3.99%. The SIFMA index replaced the BMA index on November 1, 2006, due to a merger between the Securities Industry and Financial Markets Association and the Bond Market Association.

*Termination risk:* The University or the counterparty may terminate any of the swaps if the other party fails to perform under the terms of the contract. If any of the swaps are terminated, the associated variable-rate bonds would no longer carry synthetic interest rates. Also, if at the time of termination the swap has a negative fair value, the University would be liable to the counterparty for that amount.

*Future swaps:* The University has also entered into two future dated interest rate swap agreements; one for \$50,000,000 and one for \$22,382,500 to be effective September 1, 2008, and March 1, 2017, respectively, on a General Revenue Bond issue planned for 2008.

**D. Annual Requirements** - The annual requirements to pay principal and interest on the long-term obligations at June 30, 2007, are as follows:

Fiscal Year	Annual Requirements		
	Revenue Bonds Payable		
	Principal	Interest	Interest Rate Swaps, Net
2008	\$ 8,230,000	\$ 8,472,677	\$ (32,199)
2009	8,655,000	8,099,168	(37,247)
2010	9,055,000	7,694,800	(42,295)
2011	8,930,000	7,285,322	(47,343)
2012	9,860,000	6,840,017	(53,400)
2013-2017	50,845,000	27,025,626	(360,894)
2018-2022	47,935,000	15,325,046	(523,945)
2023-2027	44,555,000	5,258,561	(339,682)
2028-2032	5,300,000	98,050	(5,962)
Total Requirements	<u>\$ 193,365,000</u>	<u>\$ 86,099,267</u>	<u>\$ (1,442,967)</u>

Interest on the variable rate 1999A bonds is calculated at 3.65% and the 2003B revenue bonds is calculated at 3.70%, the rates in effect at June 30, 2007, for each series.

The variable rate is changed weekly every Wednesday by the Remarketing agent with a maximum rate of 12%. In addition, the University has entered into interest rate swaps to synthetically fix a portion of the 1999A and 2003B bonds. Net amounts reported are based on rates as of June 30, 2007. As rates vary, the net swap payments will vary.

See note 8C for more information on the demand bonds and the interest rate swaps.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

In fiscal year 2004 the University defeased \$935,000 of outstanding University of North Carolina System Pool Revenue Bonds, Series 1998B (original issue amount \$1,695,000). 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, 2007, the outstanding balance of defeased University of North Carolina System Pool Revenue Bonds, Series 1998B bonds was \$250,000.

### NOTE 9 - LEASE OBLIGATIONS

- A. Capital Lease Obligations** - Capital lease obligations relating to equipment are recorded at the present value of the minimum lease payments. Future minimum lease payments under capital lease obligations consist of the following at June 30, 2007:

<u>Fiscal Year</u>	<u>Amount</u>
2008	\$ 100,021
2009	61,874
Total Minimum Lease Payments	161,895
Amount Representing Interest (3.74 - Rate of Interest)	10,513
Present Value of Future Lease Payments	\$ 151,382

Machinery and equipment acquired under capital lease amounted to \$365,000 at June 30, 2007.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

**B. Operating Lease Obligations** – The University entered into operating leases for equipment and property rental. Future minimum lease payments under noncancelable operating leases consist of the following at June 30, 2007:

<u>Fiscal Year</u>	<u>Amount</u>
2008	\$ 2,675,962
2009	1,765,150
2010	985,098
2011-2015	<u>140,019</u>
Total Minimum Lease Payments	<u>\$ 5,566,229</u>

Rental expense for all operating leases during the year was \$2,744,444.

### NOTE 10 - REVENUES

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

	<u>Gross Revenues</u>	<u>Internal Sales Eliminations</u>	<u>Less Scholarship Discounts</u>	<u>Less Allowance for Uncollectibles</u>	<u>Net Revenues</u>	<u>Revenues Pledged as Security Debt</u>
<b>Operating Revenues:</b>						
<b>Student Tuition and Fees</b>	\$ 181,052,200	\$ 0	\$ 31,340,711	\$ 562,722	\$ 149,148,767	\$ 9,954,642 (D,E)
<b>Other Operating Revenues</b>	\$ 11,927,904	\$ 5,131,100	\$ 0	\$ (430,978)	\$ 7,227,782	\$ 6,306,468 (A,B,C,D,E,F)
<b>Sales and Services:</b>						
Sales and Services of Auxiliary Enterprises:						
Residential Life	\$ 33,938,302	\$ 636,536	\$ 5,092,608	\$ 173,022	\$ 28,036,136	33,938,302 (B)
Dining	21,371,974	2,832,012	1,529,650	(15,885)	17,026,197	21,371,974 (C)
Bookstore	16,486,883	681,274		40,850	15,764,759	
Athletics	32,884,349	240,769		(96)	32,643,676	32,884,349 (D)
Parking	6,949,475	1,117,592		(13,088)	5,844,971	
Student Center	603,467	174,594		1,124	427,749	
Student Health	3,808,873	251,664	627,759	15,173	2,914,277	3,808,873 (E)
Other	15,948,308	10,674,089	1,361,464	9,122	3,903,633	409,385 (F)
Sales and Services of Education and Related Activities	<u>76,088,688</u>	<u>28,279,795</u>		<u>149,261</u>	<u>47,659,632</u>	
<b>Total Sales and Services</b>	<u>\$ 208,080,319</u>	<u>\$ 44,888,325</u>	<u>\$ 8,611,481</u>	<u>\$ 359,483</u>	<u>\$ 154,221,030</u>	<u>\$ 92,412,883</u>

Revenue Bonds Secured by Pledged Revenues:

- |                              |                           |
|------------------------------|---------------------------|
| (A) Centennial Campus System | (E) Student Health System |
| (B) Student Housing System   | (F) Central Stores        |
| (C) Dining System            |                           |
| (D) Athletics System         |                           |

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### NOTE 11 - OPERATING EXPENSES BY FUNCTION

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

	Salaries and Benefits	Supplies and Materials	Services	Scholarships and Fellowships	Utilities	Depreciation	Total
Instruction	\$ 242,618,084	\$ 21,862,182	\$ 25,544,770	\$ 0	\$ 8,145	\$ 0	\$ 290,033,181
Research	142,606,122	23,187,865	40,264,994		567,423		206,626,404
Public Service	82,196,945	10,282,837	28,567,600		261,132		121,308,514
Academic Support	39,365,311	14,733,969	15,326,339				69,425,619
Student Services	11,358,201	1,513,251	4,409,491		42		17,280,985
Institutional Support	44,709,446	3,348,610	5,541,944				53,600,000
Operations and Maintenance of Plant	31,397,017	13,538,708	7,737,106		23,639,171		76,312,002
Student Financial Aid	673,791	156,561	452,933	24,985,144			26,268,429
Auxiliary Enterprises	43,349,014	27,949,647	32,594,494		5,504,336		109,397,491
Depreciation						42,679,521	42,679,521
Total Operating Expenses	<u>\$ 638,273,931</u>	<u>\$ 116,573,630</u>	<u>\$ 160,439,671</u>	<u>\$ 24,985,144</u>	<u>\$ 29,980,249</u>	<u>\$ 42,679,521</u>	<u>\$ 1,012,932,146</u>

### NOTE 12 - PENSION PLANS

**A. Retirement Plans** - Each permanent full-time employee, as a condition of employment, is a member of either the Teachers' and State Employees' Retirement System or the Optional Retirement Program. Eligible employees can elect to participate in the Optional Retirement Program at the time of employment, otherwise they are automatically enrolled in the Teachers' and State Employees' Retirement System.

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

Benefit and contribution provisions for the Teachers' and State Employees' Retirement System are established by *North Carolina General Statutes* 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contribution rates are set each year by the North Carolina General Assembly based on annual actuarial valuations. For the year ended June 30, 2007, these rates were set at 2.66% of covered payroll for employers and 6% of covered payroll for members.

For the year ended June 30, 2007, the University had a total payroll of \$557,040,132, of which \$281,148,259 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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contributions for pension benefits for the year were \$16,868,896 and \$7,478,544, respectively. The University made 100% of its annual required contributions for the years ended June 30, 2007, 2006, and 2005, which were \$7,478,544, \$6,088,263, and \$5,342,109, 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.ncosc.net/> and clicking on "Financial Reports," or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

The Optional Retirement Program (Program) is a defined contribution retirement plan that provides retirement benefits with options for payments to beneficiaries in the event of the participant's death. Administrators and eligible faculty of the University may join the Program instead of the Teachers' and State Employees' Retirement System. The Board of Governors of The University of North Carolina is responsible for the administration of the Program and designates the companies authorized to offer investment products. The Board has authorized the following carriers: Teachers' Insurance and Annuity Association - College Retirement Equities Fund (TIAA-CREF), Lincoln Life Insurance Company, Variable Annuity Life Insurance Company (VALIC), and Fidelity Investments. Participants may elect to allocate their contributions and the University contributions to the carrier of their choice. Each carrier offers a variety of investment funds, including both fixed and variable account investment options and mutual funds.

Participants in the Program are immediately vested in the value of employee contributions. The value of employer contributions is vested after five years of participation in the Program. Participants become eligible to receive distributions when they terminate employment or retire.

Participant eligibility and contributory requirements are established by General Statute 135-5.1. Employer and member contribution rates are set each year by the North Carolina General Assembly. For the year ended June 30, 2007, 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, 2007, the University had a total payroll of \$557,040,132, of which \$177,968,131 was covered under the Optional Retirement Program. Total employee and employer contributions for

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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pension benefits for the year were \$10,678,088 and \$12,173,020 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 \$2,307,796 for the year ended June 30, 2007.

IRC Section 401(k) Plan - All members of the Teachers' and State Employees' Retirement System and the Optional Retirement Program are eligible to enroll in the Supplemental Retirement Income Plan, a defined contribution plan, created under Internal Revenue Code Section 401(k). All costs of administering the Plan are the responsibility of the Plan participants. No costs are incurred by the University except for a 5% employer contribution for the University's law enforcement officers, which is mandated under General Statute 143-166.30(e). Total employer contributions on behalf of University law enforcement officers for the year ended June 30, 2007, were \$122,595. The voluntary contributions by employees amounted to \$3,690,328 for the year ended June 30, 2007.

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 \$10,357,607 for the year ended June 30, 2007.



## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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- C. Federal Employment Retirement** – The Federal Retirement System is a multiple-employer retirement system and is composed of three retirement programs: the Civil Service Retirement System (CSRS) for participants employed prior to January 1, 1987, the Federal Employees Retirement System for Participants (FERS) employed after January 1, 1987, and the Civil Service Retirement Offset System for reemployed CSRS employees.

North Carolina Cooperative Extension employees with federal appointments prior to January 1, 1987, participate in the Civil Service Retirement System. Currently, 166 employees participate in CSRS. Participating employees are required by federal statute to contribute 7% of salary and the University 7% of salary to CSRS. In addition, the employees may contribute up to 10% of salary to the Thrift Savings Plan (a defined contribution plan managed by the Federal Retirement Thrift Investment Board). Total employee and employer contributions for CSRS for the year ended June 30, 2007, was \$897,324 and \$928,416 respectively. Employees covered under CSRS contributed \$65,870 to the Thrift Savings Plan.

Under the Federal Employees Retirement System (FERS), employees are required to contribute 0.8% of salary and the University 11.2%. Currently, 7 employees participate in FERS. The University is also required to contribute 1% of participant's salary to the Thrift Savings Plan, plus up to an additional 4% depending upon employee's contribution, which can range from 0% to 15% of their salary. Total employee and employer contributions for the year ended June 30, 2007, were \$5,726 and \$80,164 respectively. For employees covered under FERS the total employee and employer contributions to the Thrift Savings Plan for the year ended June 30, 2007, were \$68,762 and \$34,480 respectively.

### NOTE 13 - 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 3.8% of the covered payroll under the

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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Teachers' and State Employees' Retirement System and the Optional Retirement Program for these health care benefits. For the fiscal year ended June 30, 2007, the University's total contribution to the Plan was \$17,446,423. 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. Disability Income** - The University participates in the Disability Income Plan of North Carolina (DIPNC). Established by Chapter 135, Article 6, of the General Statutes, DIPNC provides short-term and long-term disability benefits to eligible members of the Teachers' and State Employees' Retirement System and the Optional Retirement Program. Long-term disability income benefits are advance funded on an actuarially determined basis using the one-year term cost method. The University contributes .52% of covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the DIPNC. For the year ended June 30, 2007, the University's total contribution to the DIPNC was \$2,387,405. The University assumes no liability for long-term disability benefits under the Plan other than its contribution. Additional detailed information about the DIPNC is disclosed in the State of North Carolina's *Comprehensive Annual Financial Report*.

### NOTE 14 - RISK MANAGEMENT

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

Tort claims of up to \$500,000 per claimant 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

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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cost to the University for operations supported by the State's General Fund. Other operations not supported by the State's General Fund are charged for the coverage. Losses covered by the Fund are subject to a \$500 per occurrence deductible, except for the peril of theft with an applicable \$1,000 per occurrence deductible. University departments, as an individual business decision, may also purchase through the Fund primary extended coverage for buildings and contents. Coverage may also be purchased through the Fund for theft, vandalism, sprinkler leakage, or all-risk perils. University departments also have the option to purchase all-risk coverage for computers and "miscellaneous equipment" on a scheduled basis.

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. While liability coverage is required by Statute for all University vehicles, departments may also individually opt to purchase collision and comprehensive physical damage coverage.

The University is protected for losses from employee dishonesty and computer fraud. This coverage is with a private insurance company and is handled by the North Carolina Department of Insurance. The University is charged a premium by the private insurance company. Coverage limit is \$1,000,000 per occurrence with a \$25,000 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. The types of insurance policies purchased include: Medical Professional Liability, Veterinary Professional Liability, Fine Arts Property, Master Crime, Inland Marine Property for Musical Instruments, Campers Accident and Sickness, Athletic Accident, Boiler and Machinery, Watercraft, Oceanographic Equipment, and Nuclear Energy Liability.

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

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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and compensation in accordance with the North Carolina Workers' Compensation Act. The University is self-insured for workers' compensation.

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

Additional details on the State-administered risk management programs are disclosed in the State's *Comprehensive Annual Financial Report*, issued by the Office of the State Controller.

### NOTE 15 - COMMITMENTS AND CONTINGENCIES

**A. Commitments** - The University has established an encumbrance system to track its outstanding commitments on construction projects and other purchases. Outstanding commitments on construction contracts were \$101,771,636 at June 30, 2007.

**B. Pending Litigation and Claims** - As previously reported, the Environmental Protection Agency (EPA) filed a civil action against the University pursuant to the Comprehensive Environmental Response, Compensation and Liability Act. The complaint sought relief that would cause the University to enter into remediation of a hazardous waste site known as "Lot 86." The University is involved in ongoing discussions and negotiations with the EPA concerning the appropriate means for addressing the remediation. A Consent Decree executed by North Carolina State University and the EPA has been approved by the Court. Remedial clean-up pursuant to the Consent Decree continues. The remediation costs paid by the University for the year ended June 30, 2007, totaled \$145,361.

As previously reported, the NC School Boards Association, et. al. filed a civil action against various State officials in their official capacity seeking a judicial determination as to whether the State Constitution requires certain monetary payments collected by State agencies to be paid to the local county school funds rather than statutorily designated recipients. In part, this civil action includes a determination of whether monetary payments collected pursuant to statutory authority by the University for violations of parking traffic regulations and library fines are "civil penalties" which the State Constitution requires to be paid to the school fund in the county where they are collected. On July 1, 2005, the NC Supreme Court held in favor of the school boards with regard to parking fines and held in favor of the University with regard to library fines. The matter has been remanded back to the trial court for disposition in

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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accordance with the Superior Court's decision. Determination of the amount due from the University is pending. At issue are approximately \$6,197,588 in transportation fines since December 1995.

On May 1, 2006, a group of temporary employees filed a lawsuit claiming that they were, in effect, full time employees of the State and should be paid benefits for the time period they were permanent employees. Though the University is not a named party, the State of North Carolina is a party and therefore, the University is affected by default. Though the original target of this lawsuit was not the university system, the exposure to the universities could be great if the plaintiffs prevail. Given the nature of the claims and potential class members and status of the litigation, the Attorney General's Office has indicated that it is too early to assess any potential financial impact were plaintiffs to prevail.

The University is a party to other litigation and claims in the ordinary course of its operations. Since it is not possible to predict the ultimate outcome of these matters, no provision for any liability has been made in the financial statements. University management is of the opinion that the liability, if any, for any of these matters will not have a material adverse effect on the financial position of the University.

### NOTE 16 - RELATED PARTIES

**Foundations** - There are 11 separately incorporated non-profit foundations associated with the University. These foundations are the North Carolina Agricultural Foundation, Inc., North Carolina State University Foundation, Inc., North Carolina Tobacco Foundation, Inc., Pulp and Paper Foundation, Inc., North Carolina State University Physical and Mathematical Sciences Foundation, Inc., North Carolina Engineering Foundation, Inc., North Carolina Veterinary Medical Foundation, Inc., The North Carolina Forestry Foundation, Inc., North Carolina Textile Foundation, Inc., NCSU Student Aid Association, Inc., and the North Carolina State Alumni Association, Inc.

These organizations serve as the primary fundraising arm of the University through which individuals, corporations, and other organizations support University programs by providing scholarships, fellowships, faculty salary supplements, and unrestricted funds to specific colleges and the University's overall academic environment. As described in Note 1 to the financial statements, the North Carolina State University Foundation, Inc., and the NCSU Student Aid Association, Inc., are considered component units of the University for reporting purposes and their financial statements are presented separately as part of the University's financial statements. The University's financial statements do not include the assets, liabilities, net assets, or

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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operational transactions of the foundations, except for support from each organization to the University. This support from the foundations, excluding amounts from the North Carolina State University Foundation, Inc., and the NCSU Student Aid Association, Inc., approximated \$25,547,120 for the year ended June 30, 2007.

**Non-Profit Corporation** - The Centennial Authority (Authority) was created by the 1995 General Assembly (Senate Bill 606) for the purpose of studying, designing, planning, constructing, owning, promoting, financing and operating a regional facility on land owned by the State. Prior to this act, the General Assembly authorized the construction by the University of a facility to be known as the "Entertainment and Sports Arena" (ESA). This facility serves as a regional sports entertainment center and is available for cultural performances, sporting events and other activities of the University or of other entities (the Centennial Center project). With the 1995 legislation, the Centennial Center project was transferred to the Authority.

The Authority entered into a Ground Lease with the State of North Carolina to lease land for the ESA for a period of 99 years at an annual rent of \$1. The University entered into a Use Agreement with the Authority. Both parties agreed that the University shall be the primary and preferred user of all areas of the ESA. The University is required to pay the greater of 10% of gross ticket revenues or \$44,712 for each men's and \$19,555 for each women's basketball game to compensate the Authority for facility rental and operating expenses. Rent and expense payments for miscellaneous events will be negotiated on an event by event basis based on the availability of the ESA and the anticipated attendance.

In fiscal year 2003 a naming rights agreement was executed to change the name of the ESA to the "RBC Center." As a result of this agreement, the University will receive \$13,184,000 over a ten-year period beginning in fiscal year 2003.

### **NOTE 17 - DISCRETELY PRESENTED COMPONENT UNITS**

The University's discretely presented component units use the accounting and reporting standards promulgated by FASB. Selected disclosures from the discretely presented component units audited financial statements follow:

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

### THE NORTH CAROLINA STATE UNIVERSITY FOUNDATION, INC.

#### MARKETABLE SECURITIES

Marketable securities at June 30, 2007, consisted of:

	<u>Cost</u>	<u>Fair Value</u>
Cash	\$ 72,713	\$ 72,713
NC State Investment Fund, Inc.	63,934,036	68,478,848
BNY Mellon	6,446,596	7,734,380
Academy Centennial Fund, LLC	1,037,900	74,192
Citicorp Trust Bank	574,092	718,025
Total	<u>\$ 72,065,337</u>	<u>\$ 77,078,158</u>

Marketable securities held by NC State Investment Fund, Inc. at June 30, 2007, consisted of the following:

	<u>Cost</u>	<u>Fair Value</u>
Domestic Equity Mutual Funds	\$ 19,206,337	\$ 21,207,444
Foreign Equity Mutual Funds	8,361,438	9,787,058
Real Estate Investment Trust Mutual Funds	3,177,095	3,046,622
Fixed Income Mutual Funds	20,157,204	20,223,682
Limited Partnerships	13,031,962	14,214,042
Total	<u>\$ 63,934,036</u>	<u>\$ 68,478,848</u>

The Foundation's investment in the NC State Investment Fund, Inc. ("Fund") represents approximately 19.70% of the member equity of the Fund at June 30, 2007. The Fund's net assets were approximately \$347,507,000 at June 30, 2007.

The Foundation's investment in the Academy Centennial Fund, LLC, represents approximately 11.0% of the member capital of the Academy Centennial Fund, LLC at June 30, 2007. The Academy Centennial Fund, LLC's net assets were approximately \$700,000 at December 31, 2006, (latest date available), and consisted primarily of common and preferred stock and convertible debt.

The Foundation's investments held by BNY Mellon primarily consist of bond mutual funds and equity mutual funds.

## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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The Foundation's investments held by Citicorp Trust Bank primarily consist of common equity securities.

The Foundation invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the statement of financial position.

### THE NCSU STUDENT AID ASSOCIATION, INC.

#### CONCENTRATIONS OF CREDIT RISK

The Association maintains cash balances at several financial institutions located in Raleigh, North Carolina, and in several brokerage accounts located in North Carolina. The balances in the financial institution are insured by the Federal Deposit Insurance Corporation up to \$100,000. The balances in the brokerage accounts are insured at varying amounts. The Association's uninsured cash balances totaled \$17,426,377 at June 30, 2007.

#### INVESTMENTS

The Association held the following investments at June 30, 2007:

	Historical Cost	Market Value
U.S. Government Obligations	\$ 5,069,216	\$ 5,077,027
Marketable Equity Securities	12,308,385	15,109,394
Other Marketable Debt Securities	1,799,618	1,778,995
Partnership Interests	2,113,340	2,454,683
Short-Term Investments	119,850	118,830
Mutual Funds	1,307,412	1,428,325
Total	<u>\$ 22,717,821</u>	<u>\$ 25,967,254</u>



## NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Investment income consists of the following:

	Amount
Interest	\$ 987,996
Dividends	378,209
Realized Gain (Loss) on Sale of Investments	848,486
Unrealized Gain on Investments	2,103,854
Investment Expenses	(198,618)
Total	\$ 4,119,927

### PLEDGES RECEIVABLE

The Association carries its pledges receivable at cost less a discount for pledges receivable due in more than a year and less an allowance for doubtful accounts. On a periodic basis, the Association evaluates its receivables and establishes an allowance for doubtful accounts, based on history of past write-offs and current credit conditions.

Pledges receivable at June 30, 2007, are as follows:

	Amount
Pledges Receivable	\$ 55,620,503
Less: Allowance for Uncollectible Pledges	2,781,025
Less: Discount on Pledges	11,918,698
	40,920,780
Less: Current Portion	8,127,421
Pledges Due After One Year	\$ 32,793,359

Pledges receivable due in more than one year are reflected at the present value of estimated future cash flows using a discount rate of 6%.

	Amount
Receivable in Less Than One Year	\$ 8,555,180
Receivable in One to Five Years	25,651,945
Receivable in More Than Five Years	21,413,378
	55,620,503
Less: Allowance for Uncollectible Pledges	2,781,025
Less: Discount on Pledges	11,918,698
Net Pledges Receivable	\$ 40,920,780

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

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At June 30, 2007, Goal Line Drive pledges totaling \$19,436,123 and Wolfpack Pride pledges totaling \$2,874,223 were pledged as collateral for the Goal Line Drive bond payable and the Vaughn Towers bond payable. These pledge totals are reflected at the present value of estimated future cash flows less an allowance for uncollectible pledges.

### **LONG-TERM DEBT**

#### **BOND INDENTURE - GOAL LINE DRIVE**

The Association, through First Citizens Bank, trustee, and Bank of America, administrative agent, issued \$40,000,000 of bonds during 2002. The bonds are secured by the Goal Line Drive pledges, Wolfpack Pride Campaign pledges, and the Medlin property. The bonds are also secured by approximately \$2,000,000 in scoreboard revenues to be received from NCSU through 2012. The proceeds from these bonds were used for the Carter-Finley Stadium expansion and improvements. The bonds pay interest monthly at a variable rate equal to .35% plus the higher of the federal funds rate plus ½% or Bank of America's publicly announced prime rate. The Association also must pay the administrative agent a letter of credit fee. This fee, paid quarterly, is 1.5% of the outstanding debt balance. The Association must also pay annually \$17,000 of agency and \$5,000 of trustee fees. The Association pays a remarketing fee annually to the administrative agent. This fee is .1% of the outstanding debt balance. The bond matures in 2012.

The Association entered into a swap contract for a majority of this debt to hedge against interest rate fluctuations. The swap expired in April 2007. The swap was issued at market terms so that it had no value at its inception.

#### **BOND INDENTURES - WOLFPACK CLUB STUDENT HOUSING FOUNDATION**

The Housing Foundation, through Wachovia Bank, administrative agent and trustee, issued a \$23,710,000 Series 2003A bond and a \$1,235,000 Series 2003B bond in June 2003. The proceeds from these bonds were used to construct a residence hall for NCSU students and student athletes. The bonds pay interest monthly at variable rates. The Series 2003A bonds pay interest based on a variable rate established weekly by Wachovia, remarketing agent. The Series 2003B bonds pay interest based on a variable rate established monthly by the remarketing agent. The Housing Foundation must pay a letter of credit fee quarterly to the administrative agent. This fee, paid quarterly, is 1.25% of the outstanding balance. The Housing Foundation pays a remarketing fee semi-annually to the administrative agent. This fee is .125% of the outstanding balance. The Series 2003A bonds mature in July 2035. The Series 2003B bonds mature in July 2009.

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

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The Housing Foundation has entered into a swap contract for a majority of this debt to hedge against interest rate fluctuations. The swap was issued at market terms so that it had no value at its inception. The carrying amount of the swap has been adjusted to its fair value at June 30, 2007, which, because of changes in forecasted levels of interest rates, resulted in reporting an asset at June 30, 2007, for the fair value of the net payments forecasted under the swap. The swap asset is classified as noncurrent since the Association does not intend to settle it within the next 12 months.

### **BOND INDENTURES - VAUGHN TOWERS**

The Association, through First Citizens Bank, trustee, issued a \$15,855,000 Series 2004A bond and a \$17,685,000 Series 2004B bond in November 2004. The proceeds from these bonds were used to construct Vaughn Towers at Carter-Finley Stadium. The bonds pay interest monthly at variable rates. The Series 2004A bond pays interest based on a variable rate established weekly by Wachovia, remarketing agent. The Series 2004B bond pays interest based on a variable rate established weekly by Banc of America Securities, LLC, remarketing agent. The Association must pay a 2% quarterly letter of credit fee. The Association pays an annual remarketing fee of .10% of the outstanding bonds to the remarketing agents. The Series 2004A bond matures in September 2024. The Series 2004B bond matures in September 2018.

The Association has entered into swap contracts for a majority of this debt to hedge against interest rate fluctuations. The swaps were issued at market terms so that they had no value at their inception. The carrying amount of the swaps have been adjusted to their fair value at June 30, 2007, which, because of changes in forecasted levels of interest rates, resulted in reporting an asset at June 30, 2007, for the fair value of the net payments forecasted under the swap. The swap asset is classified as noncurrent since the Association does not intend to settle it within the next 12 months.

## NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)

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	<u>Amount</u>
Goal Line Drive Bond Indenture	\$ 16,300,000
Wolfpack Club Student Housing Foundation - Series 2003A	22,780,000
Wolfpack Club Student Housing Foundation - Series 2003B	870,000
Vaughn Towers Project - Series 2004A	15,855,000
Vaughn Towers Project - Series 2004B	<u>14,090,000</u>
	69,895,000
Less Amount Classified as Current Liability	<u>1,005,000</u>
Amount Due After One Year	<u><u>\$ 68,890,000</u></u>
Maturities of long-term debt are as follows:	
2008	\$ 1,005,000
2009	5,480,000
2010	5,700,000
2011	5,645,000
2012	5,725,000
Thereafter	<u>46,340,000</u>
Total	<u><u>\$ 69,895,000</u></u>

### LETTERS OF CREDIT

Pursuant to the issuance of the Goal Line Drive bonds payable, the Association obtained an irrevocable letter of credit. The letter of credit will remain in effect until March 15, 2010.

Pursuant to the issuance of the Wolfpack Club Student Housing Foundation bonds payable, the Association obtained an irrevocable letter of credit. The original letter of credit expired June 9, 2006, and has been extended.

Pursuant to the issuance of the Wolfpack Towers bonds payable, the Association obtained two irrevocable letters of credit. The letters of credit will remain in effect until March 15, 2010.



STATE OF NORTH CAROLINA  
Office of the State Auditor

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

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

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

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Board of Trustees  
North Carolina State University  
Raleigh, North Carolina

We have audited the financial statements of North Carolina State University, a constituent institution of the multi-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, 2007, which collectively comprise the University's basic financial statements and have issued our report thereon dated November 28, 2007. Our report was modified to include a reference to 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. Other auditors audited the financial statements of the NC State Investment Fund, Inc., which represent 18 percent, 25 percent, and 6 percent, respectively, of the assets, net assets and revenues of the University and the discretely presented component units, as described in our report on the University's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors. The financial statements of the discretely presented component units were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the University's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the University's internal control over financial reporting.

**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)**

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A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the University's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the University's financial statements that is more than inconsequential will not be prevented or detected by the University's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the University's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

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 management of the University, the Board of Governors, the Board of Trustees, the Audit Committee, the Governor, the General Assembly, and the State Controller, and is not intended to be and should not be used by anyone other than these specified parties.



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

January 24, 2008

## ORDERING INFORMATION

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Audit reports issued by the Office of the State Auditor can be obtained from the web site at [www.ncauditor.net](http://www.ncauditor.net). Also, parties may register on the web site to receive automatic email notification whenever reports of interest are issued. Otherwise, copies of audit reports may be obtained by contacting the:

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

Telephone: 919/807-7500

Facsimile: 919/807-7647