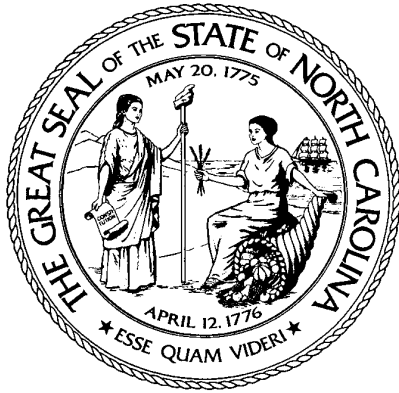




STATE OF NORTH CAROLINA

FINANCIAL STATEMENT AUDIT REPORT OF

NORTH CAROLINA STATE UNIVERSITY

RALEIGH, NORTH CAROLINA

FOR THE YEAR ENDED JUNE 30, 2002

OFFICE OF THE STATE AUDITOR

RALPH CAMPBELL, JR.

STATE AUDITOR

FINANCIAL STATEMENT AUDIT REPORT OF

NORTH CAROLINA STATE UNIVERSITY

RALEIGH, NORTH CAROLINA

FOR THE YEAR ENDED JUNE 30, 2002

BOARD OF GOVERNORS

THE UNIVERSITY OF NORTH CAROLINA

MOLLY CORBETT BROAD, PRESIDENT

BOARD OF TRUSTEES

PEACHES GUNTER BLANK, CHAIRMAN

RICHARD G. ROBB, VICE CHAIRMAN

EDWARD E. HOOD, JR., VICE CHAIRMAN

D. MCQUEEN CAMPBELL, III

DERICK S. CLOSE

W. STEVEN EDWARDS

ANN B. GOODNIGHT

SUZANNE GORDON

VERNON MALONE

BOB MATTOCKS, II

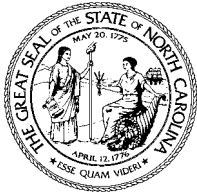
WENDELL MURPHY

C. RICHARD VAUGHN

ADMINISTRATIVE OFFICERS

DR. MARYE ANNE FOX, CHANCELLOR

GEORGE WORSLEY, VICE CHANCELLOR FOR FINANCE AND BUSINESS



Ralph Campbell, Jr.
State Auditor

STATE OF NORTH CAROLINA
Office of the 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.osa.state.nc.us>

AUDITOR'S TRANSMITTAL

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

This report presents the results of our financial statement audit of North Carolina State University, a constituent institution of the sixteen-campus University of North Carolina System, which is a component unit of the State of North Carolina, for the year ended June 30, 2002. Our audit was made by authority of Article 5A of Chapter 147 of the General Statutes.

The accounts and operations of the University are an integral part of the State's reporting entity represented in the State's *Comprehensive Annual Financial Report* (CAFR) and the State's *Single Audit Report*. In those reports, the State Auditor expresses an opinion on the State's financial statements. In the *Single Audit Report*, the State Auditor also presents the audit results on the State's internal controls and on the State's compliance with laws, regulations, contracts, and grants applicable to the State's financial statements and to its federal financial assistance programs.

As part of the audit work necessary for the CAFR and the *Single Audit Report*, the accounts and operations of the University were subjected to audit procedures as we considered necessary. In addition, we performed auditing procedures that we considered necessary for us to report on the accompanying financial statements that relate solely to North Carolina State University. The audit procedures were conducted in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards* issued by the Comptroller General of the United States.

The purpose of this report is to present the results of our audit on the accompanying financial statements that relate solely to North Carolina State University. A summary of our reporting objectives and audit results is:

- 1. Objective** – To express an opinion on the accompanying financial statements that relate solely to North Carolina State University.

Results - The accompanying financial statements present fairly, in all material respects, the amounts and disclosures made in accordance with accounting principles generally accepted in the United States of America. These matters are more fully described in the Independent Auditor's Report on the Financial Statements.

AUDITOR'S TRANSMITTAL (CONCLUDED)

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

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

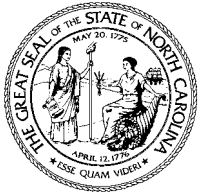
North Carolina General Statutes require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.

A handwritten signature in black ink that reads "Ralph Campbell, Jr." in a cursive script.

Ralph Campbell, Jr.
State Auditor

TABLE OF CONTENTS

	PAGE
INDEPENDENT AUDITOR’S REPORT	1
MANAGEMENT’S DISCUSSION AND ANALYSIS	3
FINANCIAL STATEMENTS	
Exhibits	
A Statement of Net Assets	17
B Statement of Revenues, Expenses, and Changes in Net Assets.....	19
C Statement of Cash Flows	21
Notes to the Financial Statement	23
SUPPLEMENTARY INFORMATION	
Schedule	
1 Schedule of General Obligation Bond Project Authorizations, Budgets, and Expenditures	57
INDEPENDENT AUDITOR’S REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH <i>GOVERNMENT AUDITING STANDARDS</i>	59
DISTRIBUTION OF AUDIT REPORT	61



Ralph Campbell, Jr.
State Auditor

STATE OF NORTH CAROLINA
Office of the 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.osa.state.nc.us>

INDEPENDENT AUDITOR'S REPORT

Board of Trustees
North Carolina State University
Raleigh, North Carolina

We have audited the accompanying basic financial statements of North Carolina State University, a constituent institution of the sixteen-campus University of North Carolina System, which is a component unit of the State of North Carolina, as of and for the year ended June 30, 2002, as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We 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. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of North Carolina State University as of June 30, 2002, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 18 to the financial statements, the University implemented Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities* and Statement No. 38, *Certain Financial Statement Note Disclosures* during the year ended June 30, 2002.

INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

In accordance with *Government Auditing Standards*, we have also issued our report dated December 11, 2002 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 grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The Management's Discussion and Analysis (MD&A) on pages 3 to 16 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 supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. Schedule 1 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.



Ralph Campbell, Jr.
State Auditor

December 11, 2002

MANAGEMENT'S DISCUSSION AND ANALYSIS

Overview of the Basic Financial Statements

Effective July 1, 2001, the University implemented new accounting and reporting standards required by the Governmental Accounting Standards Board (GASB), Statement # 34/35, *Basic Financial Statements and Management's Discussion and Analysis for Public Colleges and Universities*, Statement # 37, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus*, and Statement # 38, *Certain Financial Statement Note Disclosures*. Under these new standards, the University now reports its financial information similar to that required of private universities and uses reporting concepts in a manner similar to that required of a business enterprise. Prior to July 1, 2001, the University reported its financial information using a fund structure presentation.

The new reporting requirements include Management's Discussion and Analysis (MD&A), the Statement of Net Assets, the Statement of Revenues, Expenses, and Changes in Net Assets, the Statement of Cash Flows, and Financial Statement Note Disclosures.

This part of the financial report, Management's Discussion and Analysis, provides an introduction and overview to assist the reader in interpreting and understanding the basic financial statements. Currently known facts, decisions, or conditions are discussed in management's analysis of financial position and results of operations. While comparative analysis with the prior year financial report is important to understanding the University's financial position and results of operations, its use in the year of implementation is not advisable due to the many accounting and reporting changes resulting from the implementation. Such comparative analysis will be presented next year.

The Statement of Net Assets provides information relative to the University's assets, liabilities, and net assets as of the last day of the fiscal year, June 30th. Assets and liabilities on this Statement are categorized as either current or noncurrent. Current assets are those that are available to pay for expenses in the next fiscal year. Current liabilities are those payable in the next fiscal year. Net assets on this Statement are categorized as either invested in capital assets (net of related debt), restricted or unrestricted. Restricted net assets are categorized as either nonexpendable or expendable. Overall, the Statement of Net Assets provides information relative to the financial strength of the University and its ability to meet current and long-term obligations.

The Statement of Revenues, Expenses, and Changes in Net Assets provides information relative to the results of the University's operations, nonoperating activities, and other activities affecting net assets which occurred during the fiscal year ended June 30th. Nonoperating activities include primarily subsidies from the State in the form of appropriations, noncapital gifts and grants, interest expense on financing activities, investment income (net of investment expenses) and loss on disposition of capital assets. Other activities include capital gifts or grants, and additions to permanent endowments.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Overall the Statement of Revenues, Expenses, and Changes in Net Assets provides information relative to the University's management of its operations and its ability to maintain its financial strength.

The Statement of Cash Flows provides information relative to the University's sources and uses of cash funds for operating activities, noncapital financing activities, capital financing activities, and investing activities. This statement provides a reconciliation of beginning cash balances to ending cash balances and is representative of activity reported on the Statement of Revenues, Expenses, and Changes in Net Assets as adjusted for changes in beginning and ending balances of noncash accounts on the Statement of Net Assets.

The Financial Statement Note Disclosures provide information relative to the significant accounting principles applied in the financial 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, accounting changes, and if necessary a discussion of adjustments to prior periods and events subsequent to the University's financial statement period. Overall, the Financial Statement Note Disclosures provide information to better understand details, risk, and uncertainty associated with amounts reported in the Financial Statements.

Analysis of Financial Position and Results of Operations

The University's financial position remains strong with net assets of \$667,426,000, an increase of \$7,924,000. The strength of the University's financial position is attributed to factors including enrollment growth, significant improvements to campus facilities, a strong research program, the evolution of Centennial Campus, advancements provided through the University's endowments and its affiliated foundations, and appropriated funds from the State of North Carolina.

During the fiscal year 2001-02, student enrollment increased from 23,586 FTE (full time equivalent) to 24,339 FTE. The average SAT score for incoming freshmen for the same period was 1175 and the average High School GPA was 3.91. Centennial campus plans continued to evolve with the ground breaking for relocation of the College of Engineering, Phase I on October 25, 2001. Capital improvements to buildings totaled \$28,266,000 with commitments of \$38,230,000 outstanding at June 30th. Research grants totaled 5,522 in number and \$140,607,000 in amount. Endowment gifts received by the University during the period were \$4,254,000 and support received by the University from its affiliated foundations was \$25,427,000.

State funding for operations decreased from \$352,462,000 to \$328,187,000. However, the tuition rates were increased 13% and enrollment was up 2%, which helped offset the decrease in State funding.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

Condensed Financial Information

The following table summarizes the University's assets, liabilities and net assets as of June 30, 2002.

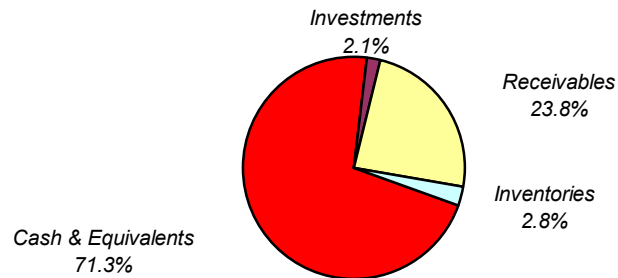
Condensed Statement of Net Assets**June 30, 2002***(in thousands)*

	Amount	Percent
Assets		
Current Assets	\$ 182,982	19.87%
Capital Assets, Net	486,825	52.87%
Other Noncurrent Assets	250,977	27.26%
Total Assets	920,784	100.00%
Liabilities		
Current Liabilities	64,453	25.44%
Noncurrent Liabilities	188,905	74.56%
Total Liabilities	253,358	100.00%
Net Assets		
Invested in Capital Assets, Net of Related Debt	399,440	59.85%
Restricted:		
Nonexpendable	43,368	6.50%
Expendable	147,185	22.05%
Unrestricted	77,433	11.60%
Total Net Assets	\$ 667,426	100.00%

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

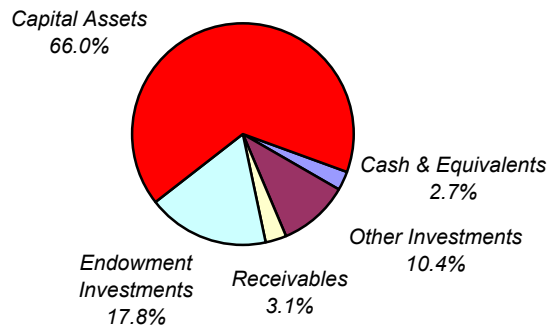
The following graphically illustrates the assets, liabilities and net assets of the University.

Current Assets



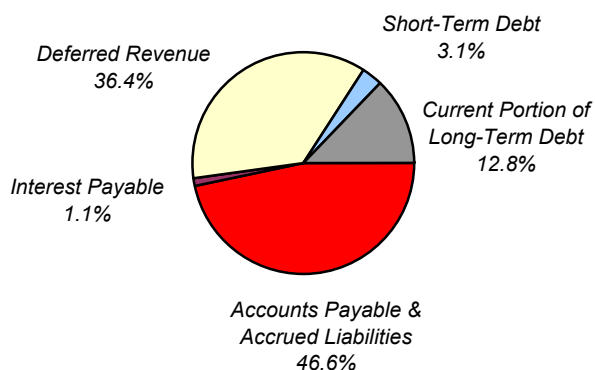
Current assets consist primarily of cash and equivalents, \$130,444,000, and accounts receivable, \$42,092,000.

Noncurrent Assets



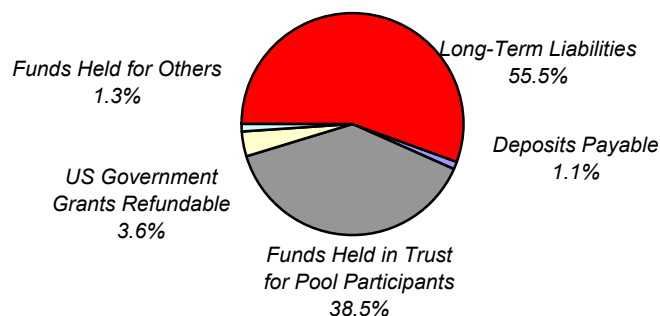
Noncurrent assets consist primarily of capital assets, \$486,825,000, endowment investments, \$131,241,000 and other investments, \$76,781,000. Other investments consist primarily of investments held for affiliated foundations in the University's external investment pool.

Current Liabilities



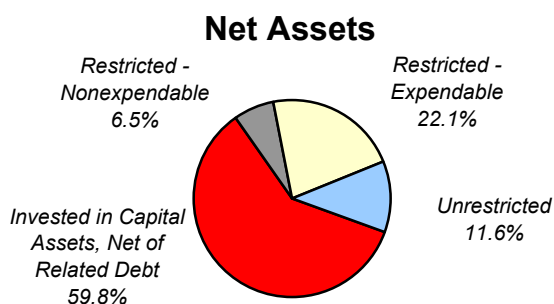
Current liabilities consist primarily of accounts payable and accrued liabilities, \$29,013,000, deferred revenue, \$23,451,000, and the current portion of long-term debt, \$8,267,000. Deferred revenue consists primarily of advance payments on operating grants/contracts.

Noncurrent Liabilities



Noncurrent liabilities consist primarily of long-term liabilities, \$104,788,000, and funds held in trust for pool participants, \$72,684,000. Long-term liabilities consist of \$80,781,000 in bonds payable, \$23,785,000 in accrued compensated absences, and \$222,000 in capital leases.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)



Net assets invested in capital assets, net of related debt, are \$399,440,000. Restricted expendable net assets of \$147,185,000 represent amounts subject to externally imposed restrictions. Unrestricted net assets of \$77,433,000 represent amounts not subject to externally imposed stipulations but are internally designated for various activities, research programs and initiatives, as well as capital improvement projects. Restricted nonexpendable net assets of \$43,368,000 represent endowment gifts held for investment purposes for which the principal amount is not available for expenditure, as stipulated by the donor.

The Statement of Revenues, Expenses, and Changes in Net Assets presents the results of the University operations for the report period. The following table summarizes the University's revenues, expenses, and changes in net assets for the year ended June 30, 2002.

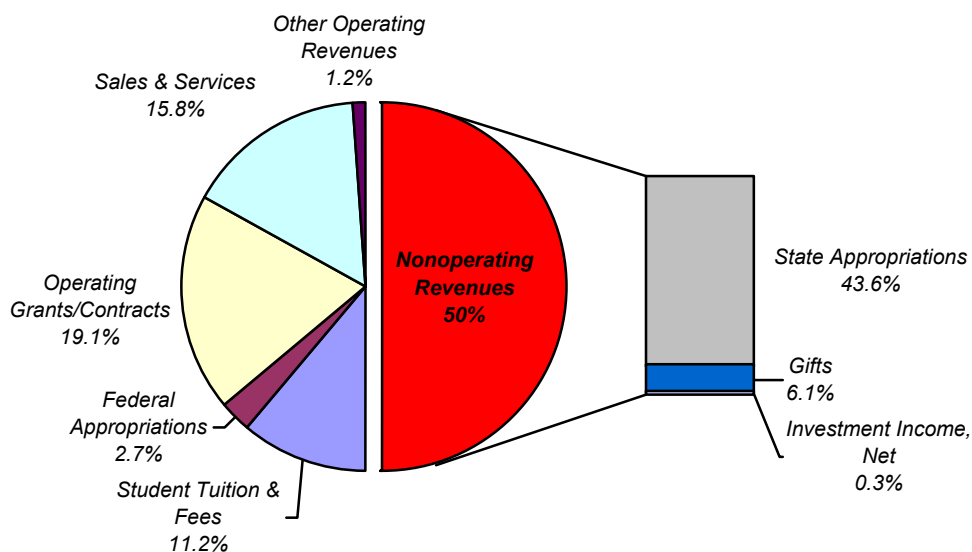
MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

**Condensed Statement of Revenues, Expenses, and Changes in Net Assets
For the Fiscal Year Ended June 30, 2002
(in thousands)**

	<u>Amount</u>
Operating Revenues	\$ 375,774
Operating Expenses	<u>(774,280)</u>
Operating Loss	<u>(398,506)</u>
Nonoperating Revenues	376,315
Nonoperating Expenses	<u>(7,145)</u>
Loss Before Other Revenues and Expenses	(29,336)
Other Revenues	<u>37,260</u>
Increase in Net Assets	7,924
Net Assets Beginning of Year (restated)	<u>659,502</u>
Net Assets End of Year	<u><u>\$ 667,426</u></u>

While the University shows an operating loss, this is an expected outcome for public universities under the new accounting and reporting requirements. The operating loss is the result of State appropriations being reported as nonoperating revenue and expenses associated with nonoperating and capital grants and gifts being reported as operating expenses. In all, the University increased its net assets by \$7,924,000 of which \$2,586,000 was the result of permanent endowment additions. The following is a graphic illustration of revenues by source (both operating and nonoperating).

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)



Operating revenues consist primarily of student tuition and fees, \$84,436,000, federal appropriations, \$20,529,000, operating grants/contracts, \$143,593,000, and sales and services, \$118,113,000. Nonoperating revenues consist primarily of State appropriations, \$328,187,000.

As a result of the new accounting and reporting standards, tuition and fees are now shown net of amounts received in other revenue accounts for student financial aid. This method of net reporting is referred to as Discounting. In addition, sales and services are now shown net of amounts charged internally to other University departments. This method of net reporting is referred to as Elimination of Internal Sales. These changes remove the duplication of revenues and expenses on the University's financial statements as a whole. In prior years these items were shown as revenues and expenses as required in the fund based financial statements. Another change resulting from the new accounting and reporting standards is that the change in allowance for uncollectible accounts is now reported as a reduction to revenues rather than expensed as in prior years.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

The following table summarizes the University's operating grants/contracts by funding source.

Operating Grants/Contracts by Funding Source
(in thousands)

	<u>Amount</u>
Federal Government Grants and Contracts	\$ 87,538
State Government Grants and Contracts	24,925
Nongovernmental Grants and Contracts	<u>31,130</u>
Total	<u><u>\$ 143,593</u></u>

Other revenues and expenses impact the change in the University's net assets for the reporting period. Other revenues represent gifts, grants, and other bequests received for improvement to capital assets or additions to permanent endowments. The following table summarizes the University's other revenues. There were no other expenses for the reporting period.

Other Revenues and Expenses
(in thousands)

	<u>Amount</u>
Capital Grants	\$ 24,763
Capital Gifts	9,911
Additions to Permanent Endowments	<u>2,586</u>
Total	<u><u>\$ 37,260</u></u>

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

The following table summarizes the University's expenses (operating and nonoperating) for the reporting period.

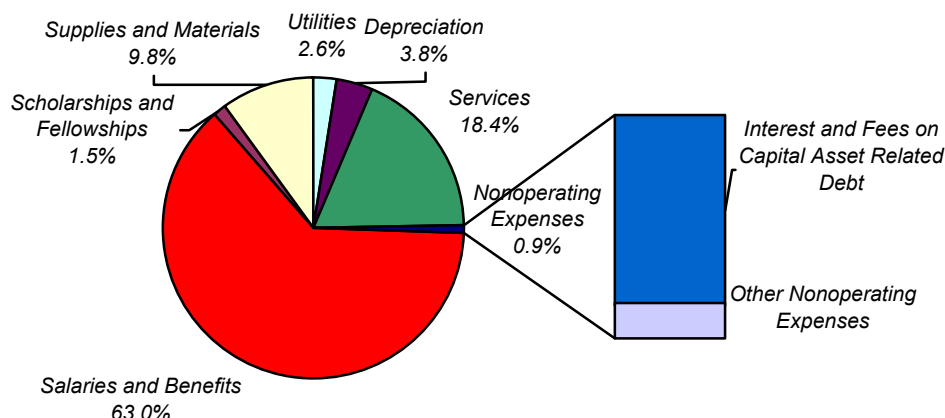
Operating and Nonoperating Expenses
(in thousands)

	<u>Amount</u>
Operating Expenses:	
Salaries and Benefits	\$ 492,421
Supplies and Materials	76,951
Services	143,439
Scholarships and Fellowships	11,751
Utilities	20,030
Depreciation	<u>29,688</u>
 Total Operating Expenses	 <u><u>\$ 774,280</u></u>
 Nonoperating Expenses:	
Interest and Fees on Capital Asset Related Debt	\$ 6,088
Other Nonoperating Expenses	<u>1,057</u>
 Total Nonoperating Expenses	 <u><u>\$ 7,145</u></u>

As a result of the new accounting and reporting standards, operating expenses are reduced for discounting the elimination of internal sales. Scholarships and fellowships now represent payments to students exclusive of tuition and fees amounts received from other University revenue sources. In addition, depreciation is now recorded to report the utilization of long-lived assets. In prior years, capital assets were shown at historical cost with no depreciation.

The following is a graphic illustration of expenses (operating and nonoperating) for the reporting period.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)



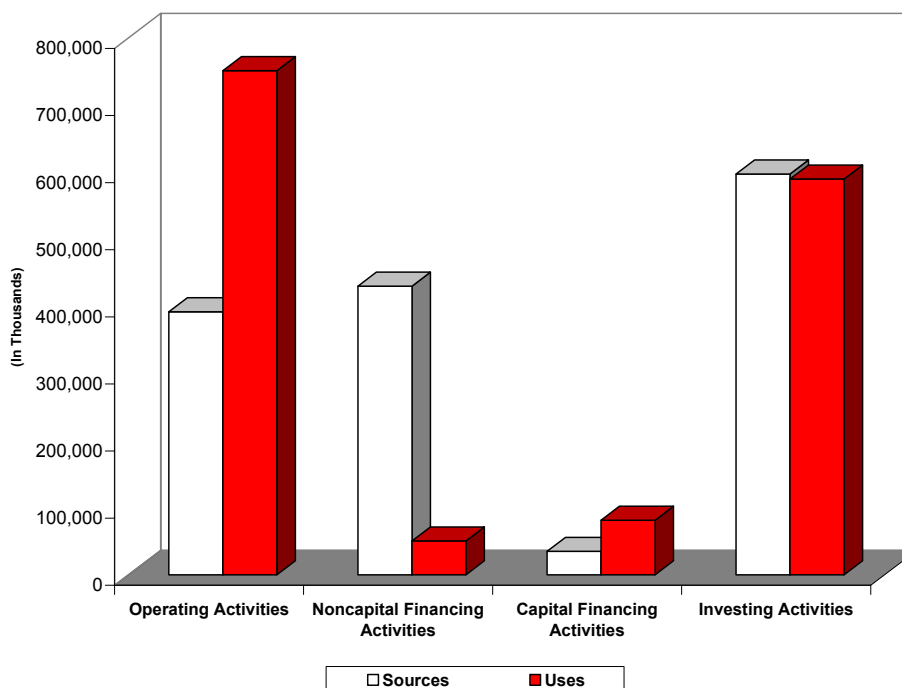
The Statement of Cash Flows provides additional information about the University's financial results, by reporting the major sources and uses of cash. The following table summarizes the University's cash receipts and payments for the year ended June 30, 2002.

Condensed Statement of Cash Flows
For the fiscal year ended June 20, 2002
(in thousands)

	Amount
Cash Provided (Used) by:	
Operating Activities	\$ (359,271)
Noncapital Financing Activities	379,560
Capital and Related Financing Activities	(46,483)
Investing Activities	7,628
Net Decrease in Cash	(18,566)
Cash – Beginning of the Year	169,040
Cash – End of the Year	\$ 150,474

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

The following is a graphic illustration of operating activities, noncapital financing activities, capital financing activities, and investing activities for the reporting period.



Capital Assets and Long-Term Debt Activities

Capital Assets

With the passage of the Higher Education Improvement Bond Referendum by North Carolina voters on November 7, 2000, the University is in excellent position to improve and modernize its facilities. The referendum provided \$468,257,000 in State funds to the University over a six-year period beginning in fiscal year 2001. As of June 30, 2002, the University had received \$29,050,000 from the State and had \$439,207,000 outstanding pending future bond sales and allotment approvals.

During the report period, the University received \$23,590,000 in funds from the referendum, \$1,172,000 from federal funds, \$2,000,000 from debt financing, and \$16,127,000 from available unrestricted funds. In total, the University received or made available from available funds \$42,889,000 during the report period for its capital improvements.

The University expended \$48,524,000 during the year for the construction of new buildings/infrastructure or for the renovation or repair of its facilities. Of this amount, \$10,302,000 was expended on improvements to Centennial Campus.

At June 30, 2002, outstanding commitments on construction contracts were \$38,230,000.

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)

More information about the Universities long-range capital plan is located at <http://www.ncsu.edu/facilities/masterplan/index.htm>.

Centennial Campus is a research and advanced technology community where the University, industry and government partners interact in multi-disciplinary programs directed toward the solution of contemporary problems. Since the Centennial Campus opened its first laboratory in 1988, its inventory of buildings has grown to 17 buildings, containing a total of approximately 1.5 million square feet of developed space and investment of \$340 million to date. Of this space, approximately 24% was for the University's use, 9% was for governmental use, and 67% was leased to private companies.

More information about Centennial Campus is located at <http://www.centennial.ncsu.edu/>.

Long-Term Debt Activities

As authorized by the General Assembly in fiscal year 2000, the University adopted a new financing methodology to allow it to pledge its available funds using general revenue bond acquisitions. Under this new financing methodology, the University entered into a joint Commercial Paper program with the University of North Carolina at Chapel Hill (UNC-CH) in March 2002. Proceeds of the program will be made available to UNC-CH (up to \$75,000,000) and to the University (up to \$25,000,000). In June 2002, the University issued \$2,000,000 in commercial paper with an interest rate of 1.45% and term of 161 days to finance construction projects. While considered a short-term loan, the University intends to refinance the borrowings either through additional short-term loans or by acquiring a long-term general revenue bond, depending on market interest rates.

In April 2002, the University issued \$15,960,000 in general revenue refunding bonds. The refunding was used to defease \$1,125,000 of outstanding North Carolina State University at Raleigh Housing System Revenue Refunding Bonds of 1991, Series L; \$7,520,000 of outstanding North Carolina State University at Raleigh Housing System Revenue Bonds of 1994, Series M; and \$7,290,000 of outstanding North Carolina State University at Raleigh Taxable Revenue Bonds Centennial Campus Projects, Series 1993. With this refunding, the University reduced its debt service requirements by \$3,702,000 and recognized an economic gain of \$534,000 over the next 12 years.

As a result of this new financing methodology and the pledge of its available funds, the University's bond rating from Moody's Investor Service was upgraded to Aa3 from A1 for its outstanding Housing, Dining and Student Center bonds. In addition, Moody's assigned an Aa3 rating with a stable outlook for the University's series 2002B and C General Revenue Refunding Bonds. The bond rating from Standards and Poor's remained the same at AA for the reporting period.

At June 30, 2002, the University had outstanding long-term bond indebtedness in the principal amount of \$87,092,000.

Economic Factors That Will Affect the Future

A major source of funding for the University is appropriations from the State of North Carolina. As a result of increased enrollment growth at North Carolina State University in fiscal year 2002, the State authorized new appropriations to the University for fiscal year 2003 of more than \$22,000,000. Tuition rates were also increased providing for \$8,000,000 in enhancements to the University's revenue stream. As a result of the Higher Education Improvement Bond program, the University has \$439,207,000 in State resources still available for construction and facilities improvement over the next four years.

Other major sources of funding are from federal, State, and nongovernmental resources for research and technology development. With the development of Centennial Campus and the reputation of NCSU's research faculty and research centers, these resources are expected to increase. Research outcomes contribute to patents and technology transfers that will benefit the citizens of the State and contribute to the improvement of the State's economy.

North Carolina State University				
Statement of Net Assets				
June 30, 2002				
(dollars expressed in thousands)				Exhibit A
ASSETS				
Current Assets:				
Cash and Cash Equivalents		\$	99,966	
Restricted Cash and Cash Equivalents			30,478	
Restricted Short-Term Investments			3,872	
Receivables, Net (Note 5)			33,835	
Due from Primary Government			8,257	
Inventories			5,174	
Notes Receivable, Net (Note 5)			1,400	
Total Current Assets			182,982	
Noncurrent Assets:				
Restricted Cash and Cash Equivalents			20,030	
Restricted Due from Primary Government			13,626	
Endowment Investments			131,241	
Other Long-Term Investments			76,781	
Notes Receivable, Net (Note 5)			9,299	
Capital Assets, Net (Note 6)			486,825	
Total Noncurrent Assets			737,802	
Total Assets			920,784	
LIABILITIES				
Current Liabilities:				
Accounts Payable and Accrued Liabilities (Note 7)			29,013	
Due to Primary Government			999	
Deferred Revenue			23,451	
Interest Payable			723	
Long-Term Liabilities - Current Portion (Notes 8 & 9)			10,267	
Total Current Liabilities			64,453	
Noncurrent Liabilities:				
Deposits Payable			2,135	
Funds Held for Others			2,469	
U. S. Government Grants Refundable			6,829	
Funds Held in Trust for Pool Participants			72,684	
Long-Term Liabilities (Note 9)			104,788	
Total Noncurrent Liabilities			188,905	
Total Liabilities			253,358	

North Carolina State University				
Statement of Net Assets				
June 30, 2002				Exhibit A
(dollars expressed in thousands)				Page 2
NET ASSETS				
Invested in Capital Assets, Net of Related Debt				399,440
Restricted for:				
Nonexpendable:				
Scholarships and Fellowships				6,961
Endowed Professorships				22,355
Departmental Uses				13,041
Other				1,011
Expendable:				
Scholarships and Fellowships				10,052
Research				7,822
Endowed Professorships				47,070
Departmental Uses				25,431
Loans				5,921
Capital Projects				30,639
Debt Service				7,100
Other				13,150
Unrestricted				77,433
Total Net Assets			\$	667,426
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, 2002				
(dollars expressed in thousands)				Exhibit B
REVENUES				
Operating Revenues:				
Student Tuition and Fees, Net (Note 11)		\$	84,436	
Federal Appropriations			20,529	
Federal Grants and Contracts			87,538	
State and Local Grants and Contracts			24,925	
Nongovernmental Grants and Contracts			31,130	
Sales and Services, Net (Note 11)			118,113	
Interest Earnings on Loans			232	
Other Operating Revenues			8,871	
Total Operating Revenues			375,774	
EXPENSES				
Operating Expenses:				
Salaries and Benefits			492,421	
Supplies and Materials			76,951	
Services			143,439	
Scholarships and Fellowships			11,751	
Utilities			20,030	
Depreciation			29,688	
Total Operating Expenses			774,280	
Operating Loss			(398,506)	

North Carolina State University				
Statement of Revenues, Expenses, and				
Changes in Net Assets				
For the Fiscal Year Ended June 30, 2002				Exhibit B
(dollars expressed in thousands)				Page 2
NONOPERATING REVENUES (EXPENSES)				
	State Appropriations			328,187
	Noncapital Grants			1,669
	Noncapital Gifts, Net			44,203
	Investment Income (Net of Investment Expense of \$649)			2,256
	Interest and Fees on Capital Asset-Related Debt			(6,088)
	Other Nonoperating Revenues (Expenses)			(1,057)
	Net Nonoperating Revenues			369,170
	Loss Before Other Revenues, Expenses, Gains, or Losses			(29,336)
	Capital Grants			24,763
	Capital Gifts, Net			9,911
	Additions to Permanent Endowments			2,586
	Increase in Net Assets			7,924
NET ASSETS				
	Net Assets - July 1, 2001, as Restated (Note 19)			659,502
	Net Assets - June 30, 2002		\$	667,426
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, 2002			
(dollars expressed in thousands)			Exhibit C
CASH FLOWS FROM OPERATING ACTIVITIES			
Received from Customers	\$	380,489	
Payments to Employees and Fringe Benefits		(503,137)	
Payments to Vendors and Suppliers		(234,123)	
Payments for Scholarships and Fellowships		(11,751)	
Loans Issued to Students and Employees		(2,231)	
Loans Collected from Students and Employees		2,057	
Interest Earned on Loans		251	
Other Receipts (Payments)		9,174	
Net Cash Used by Operating Activities		(359,271)	
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES			
State Appropriations		328,187	
Grants for Other than Capital Purposes		2,304	
Noncapital Gifts		46,593	
Federal Family Education Loan Receipts		51,359	
Federal Family Education Loan Disbursements		(50,452)	
External Participation in Investment Fund		1,405	
Other Receipts (Payments)		164	
Net Cash Provided by Noncapital Financing Activities		379,560	
CASH FLOWS FROM CAPITAL FINANCING AND RELATED FINANCING ACTIVITIES			
Proceeds from Capital Debt		17,946	
Capital Grants		16,155	
Proceeds from Sale of Capital Assets		789	
Purchases of Capital Assets		(53,232)	
Principal Paid on Capital Debt and Leases		(7,311)	
Interest Paid on Capital Debt and Leases		(4,616)	
Payment to Bond Escrow Agent		(15,958)	
Other Receipts (Payments)		(256)	
Net Cash Used by Capital Financing Activities		(46,483)	
CASH FLOWS FROM INVESTING ACTIVITIES			
Proceeds from Sales and Maturities of Investments		583,431	
Interest on Investments		13,968	
Purchase of Investments		(589,771)	
Net Cash Provided by Investing Activities		7,628	
Net Decrease in Cash and Cash Equivalents		(18,566)	
Cash and Cash Equivalents - July 1, 2001		169,040	
Cash and Cash Equivalents - June 30, 2002	\$	150,474	

North Carolina State University			
Statement of Cash Flows			
For the Fiscal Year Ended June 30, 2002			Exhibit C
(dollars expressed in thousands)			Page 2
RECONCILIATION OF NET OPERATING REVENUES (EXPENSES)			
TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES			
Operating Loss		\$	(398,506)
Adjustments to Reconcile Operating (Loss) to Net Cash Provided (Used)			
by Operating Activities:			
Depreciation Expense			29,688
Provision for Bad Debt Expense			(1,701)
Changes in Assets and Liabilities:			
Receivables (Net)			(1,901)
Inventories			(2,604)
Accounts Payable and Accrued Liabilities			(1,193)
Deferred Revenue			14,153
Compensated Absences			355
Deposits Payable			2,135
Prepaid Items			303
Net Cash Used by Operating Activities		\$	(359,271)
RECONCILIATION OF CASH AND CASH EQUIVALENT BALANCES			
Current Assets:			
Cash and Cash Equivalents		\$	99,966
Restricted Cash and Cash Equivalents			30,478
Noncurrent Assets:			
Restricted Cash and Cash Equivalents			20,030
Total Cash and Cash Equivalent Balances		\$	150,474
NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES			
Assets Acquired through the Assumption of a Liability		\$	319
Assets Acquired through a Gift			10,107
Change in Fair Value of Investments			(4,766)
The accompanying notes to the financial statements are an integral part of this statement.			

**NORTH CAROLINA STATE UNIVERSITY
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2002**

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 sixteen-campus University of North Carolina System, which is a component unit of the State of North Carolina and an integral part of the State's *Comprehensive Annual Financial Report*.

The accompanying financial statements present all funds belonging to the University and its component units. While the Board of Governors of the University of North Carolina System has ultimate responsibility, the Chancellor, the Board of Trustees, and the Board of Trustees of the Endowment Fund have delegated responsibilities for financial accountability of the University's funds. 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 Member's Board consisting of six ex officio directors and five elected representatives from the participating entities. 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 an external governmental investment pool. Because the majority of the Member's Board of the Investment Fund consists of University administrators and Board Members 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. In addition, the

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Corporation formed NC State University Conference Center, LLC (LLC) on January 25, 2002 to develop, own and operate a hotel, conference center, and public golf course on the Centennial Campus as outlined in the Campus Master Plan. Because the Corporation's Board is appointed by the Chancellor and its sole purpose is to support and benefit the University, both the Corporation and the LLC 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) 515-2110. Financial information relative to the Corporation and the LLC may be obtained from the Corporation's Executive Director, Campus Box 7012, Raleigh, NC 27695, or by calling (919) 515-0388. Other related foundations and similar non-profit corporations for which the University is not financially accountable are not part of the accompanying financial statements.

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

Pursuant to the provisions of GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities* effective for the University's year ended June 30, 2002, the full scope of the University's activities is considered to be a single business-type activity (BTA) and accordingly, is reported within a single column in the basic financial statements.

- 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.

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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

D. Cash and Cash Equivalents – This classification appears on the Statement of Net Assets and the Statement of Cash Flows and includes undeposited receipts, petty cash, cash on deposit with private bank accounts, cash on deposit with fiscal agents, and short-term investments with the State Treasurer's Cash and Investment Pool (a governmental external investment pool). The short-term investment portfolio maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit and withdraw cash at any time without prior notice or penalty.

E. Investments - This classification includes long-term fixed income investments, equity investments, mutual funds, money market funds, limited partnerships, real estate investment trusts, real estate, and other asset holdings by the University. Except for money market funds, 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.

Money market funds, 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.

F. Receivables – Receivables consist of tuition and fees charges to students and charges for auxiliary enterprises' sales and services. Receivables also include amounts due from the federal government, State and local governments, private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants, and pledges that are verifiable, measurable, and expected to be collected and available for expenditures for which the resource providers conditions have been satisfied. Receivables are recorded net of estimated uncollectible amounts.

G. Inventories – Inventories, consisting of expendable supplies and merchandise for resale, are stated at the lower of cost or market value using the first-in, first-out method except for the bookstore that uses the retail method and physical plant that 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 University capitalizes assets that have a value or cost in excess of \$5,000 at the date

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

of acquisition and an expected useful life of one or more years. Library books are expensed.

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. Collections not capitalized adhere to the University's policy to maintain for public exhibition, education or research; protect, keep unencumbered, care for and preserve; and requires proceeds from their sale to be used to acquire other collection items. Accounting principles generally accepted in the United States of America permit collections maintained in this manner to be charged to operations at time of purchase rather than capitalized.

- I. Restricted Assets** – Restricted assets represent assets whose use is restricted by external parties or by law through constitutional provisions or enabling legislation.
- 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 3.
- K. Noncurrent Long-Term Liabilities** – Noncurrent long-term liabilities include principal amounts of bonds payable, notes payable, capital lease obligations, and compensated absences that will not be paid within the next fiscal year.

Bonds payable are reported net of unamortized premiums or 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 1st or for which an employee can be paid upon termination of employment. Also, any accumulated vacation leave in excess of 30 days at year-end is converted to sick leave. Under this policy, the accumulated vacation leave for each employee at June 30th equals the leave carried forward at the previous December 31st plus the leave earned, less the leave taken between January 1st and June 30th. When classifying compensated absences into current and noncurrent, leave is considered taken using a last-in, first-out method.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 the resources 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.

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 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 presents its revenues and expenses as operating or nonoperating based on recognition

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

definitions from GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*. Operating activities are those activities that are necessary and essential to the mission of the University. Operating revenues include all charges to customers, grants received for student financial assistance, research contracts and grants, and interest earned on loans. Grants received for student financial assistance are considered operating revenues because they provide resources for student charges and such programs are necessary and essential to the mission of the University. 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. Operating expenses are all expense transactions incurred other than those related to investing, capital or noncapital financing activities. Revenues received for capital financing activities, as well as related expenses, are considered neither operating nor nonoperating activities and are presented after nonoperating activities on the accompanying Statement of Revenues, Expenses, and Changes in Net Assets.

- 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.

NOTE 2 - BUDGETING AND BUDGETING CONTROL

The State of North Carolina operates on a biennial budget cycle with separate annual departmental and institutional certified budgets adopted by the General Assembly.

Chapter 116, Article 1, Part 2A of the North Carolina General Statutes authorizes the universities within the sixteen-campus University of North Carolina System to apply for special responsibility status, which sets the legal level of budgetary control at the institution's budget code level. A budget code

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

is a convention used in the State's accounting system to distinguish the type of fund and the responsible department or institution. Budget codes are also used to segregate certain purposes within departments or institutions. Institutions with special responsibility status must still have certain budget revisions, primarily those associated with unanticipated revenues, approved by the Office of State Budget and Management. Additionally, universities must maintain programs and services in accordance with the guidelines established by the Board of Governors of the consolidated University of North Carolina System. North Carolina State University has applied for and received special responsibility status.

After the budget is approved by the General Assembly and adopted by the Board of Governors, the University follows an established system of budgetary controls. Interim budget statements to department heads guide them in managing budget allocations. Financial reports, which include budget and actual data, are available daily for each fund to individual managers responsible for the fund. When actual conditions require changes to the budget, revisions are prepared and communicated to those affected. Changes to the budget are reviewed and approved at the University or State level as required. The University maintains an encumbrance accounting system as another method to ensure that imposed expenditure constraints are observed. The State budgetary control is maintained on a cash basis of accounting.

NOTE 3 - DEPOSITS AND INVESTMENTS

A. Deposits - The University is required by General Statute 147-77 to deposit its budget code cash, as defined in Note 2, and by the University of North Carolina Board of Governors pursuant to General Statute 116-36.1 to deposit its institutional trust funds, except for funds received for services rendered by health care professionals, in the State Treasurer's Cash and Investment Pool. In addition, 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's Cash and Investment Pool. Special funds consist of moneys for intercollegiate athletics and agency funds held directly by the University.

Deposits include cash and cash equivalents totaling \$150,244,000. At year-end, cash on hand was \$230,000. The University's portion of the State Treasurer's Cash and Investment Pool was \$149,762,000. It is the State Treasurer's policy and practice for deposits not covered by federal depository insurance to be covered by collateral held by the State of North Carolina's agent in the name of the State and for investments to be held by the State's agent in the State's name. The carrying amount of the

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

University's deposits not with the State Treasurer was \$483,000 and the bank balance was \$498,000. Of the bank balance, \$290,000 was covered by federal depository insurance and \$208,000 was uninsured and uncollateralized.

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

The financial statements and disclosures for the State Treasurer's Cash and Investment Pool are included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.state.nc.us/> and clicking on "Financial Reports", or by calling the State Controller's Financial Reporting Section at (919) 981-5454.

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

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

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Investments of the Investment Fund, a University component unit, are subject to and restricted by General Statute 36B “Uniform Management of Institutional Funds Act” (UMIFA) and any requirements placed on them by contract or donor agreements.

Investments of various funds may be pooled unless prohibited by statute or by terms of the gift or contract. The University utilizes the following investment pools:

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 is based on the directives of the University’s Endowment Board. This pool also participates in the Investment Fund.

The Investment Fund - This is a governmental external investment pooled sponsored by the University. The Investment Fund was established in April 1999. The Investment Fund is utilized as one of the investment managers for the Long Term Investment Pool (the Investment Fund’s internal participant) and to manage the investments for other affiliated organizations that are organized and operated primarily to support the University (the Investment Fund’s external participants). Fund ownership of the pool is measured using the dollar-day method, which assigns a weighted value for the time the funds are on deposit. 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 registered with the SEC and is not subject to any formal oversight other than that provided by the Investment Fund Member’s Board. The Board is responsible for adopting investment objectives and policies, for hiring investment advisors, and for monitoring policy implementation and investment performance. The Board has chosen not to make individual security selection decisions. The Board’s primary role is to oversee the allocation of the pool’s portfolio among the asset classes, investment vehicles, and investment managers.

Deutsche-Bankers Trust is the custodian for the pool and provides the University with quarterly statements defining income and fair value information which is then allocated among the fund’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. Separate financial statements for the Investment Fund may be obtained from the

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Foundations Accounting and Investments Office, Campus Box 7207, Raleigh, NC 27695, or by calling (919) 515-2110.

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

A summary of the University's investments at June 30, 2002 is presented below:

Long Term Investment Pool*

	(in thousands)			
	Fair Value			
	Risk Category			
	1	2	3	Total
Categorized Investments:				
U. S. Government Securities	\$ 2,182	\$ 0	\$ 0	\$ 2,182
Corporate Bonds	1,960			1,960
International Bonds	108			108
Total Categorized Investments	<u>\$ 4,250</u>	<u>\$ 0</u>	<u>\$ 0</u>	4,250
Investments Not Categorized:				
Money Market Funds				3,101
Mutual Funds				11,508
Pooled Investments (Life Income Pools)				219
Other Investments				14,269
Total Investments Not Categorized				<u>29,097</u>
Total Long Term Investment Pool				\$ 33,347

**Excludes amounts reported in the Investment Fund*

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Investment Fund (External Investment Pool)

(in thousands)

	Fair Value			
	Risk Category			Total
	1	2	3	
Categorized Investments:				
U. S. Government Securities	\$ 6,228	\$ 0	\$ 0	\$ 6,228
Collateralized Mortgage Obligations	7,397			7,397
Corporate Bonds	15,571			15,571
International Bonds	1,924			1,924
Commercial Paper	6,587			6,587
Corporate Stocks	70,719			70,719
International Stocks	1,733			1,733
Total Categorized Investments	<u>\$ 110,159</u>	<u>\$ 0</u>	<u>\$ 0</u>	110,159
Investments Not Categorized:				
Money Market Funds				11,217
Mutual Funds				22,515
Real Estate Investment Trusts				<u>5,646</u>
Total Investments Not Categorized				<u>39,378</u>
Total External Pool Investments				<u>\$ 149,537</u>

Non-Pooled Investments

(in thousands)

	Fair Value			
	Risk Category			Total
	1	2	3	
Categorized Investments:				
U. S. Government Securities	\$ 4,132	\$ 0	\$ 0	\$ 4,132
Corporate Stocks	1,522			1,522
Total Categorized Investments	<u>\$ 5,654</u>	<u>\$ 0</u>	<u>\$ 0</u>	5,654
Investments Not Categorized:				
Money Market Funds				3,646
Real Estate				18,498
Other Investments				<u>1,212</u>
Total Investments Not Categorized				<u>23,356</u>
Total Non-Pooled Investments				<u>\$ 29,010</u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Total Investments

	(in thousands)			
	Fair Value			
	Risk Category			
	1	2	3	Total
Total Categorized Investments	\$ 120,063	\$ 0	\$ 0	\$ 120,063
Total Investments Not Categorized				91,831
Total Investments				\$ 211,894

C. Derivative and Similar Transactions - A derivative is a financial instrument created from, or whose value depends on (is derived from), the value of one or more underlying assets, reference rates, or indexes of asset values. These instruments may include forwards, futures, currency and interest rate swaps, options, floaters/inverse floaters, and caps/floors/collars. During the year the University did not invest in derivative investments but did invest in transactions similar to a derivative instrument. Investment transactions similar to a derivative may include securitized assets, such as mortgage-backed securities and other asset-backed securities. As required by accounting principles generally accepted in the United States of America, the nature of derivative or similar transactions entered into by the University, and the reasons for entering into those transactions follow:

Mortgage-Backed Securities - The University invests in mortgage-backed securities issued by the Government National Mortgage Association (GNMA), an agency of the United States government, government sponsored enterprises including the Federal Home Loan Mortgage Corporation (FHLMC) or the Federal National Mortgage Association (FNMA), and private trusts or corporations. The University invests in these securities to increase the yield and return on its investment portfolio given the available alternative investment opportunities.

The values of mortgage-backed securities are generally based on the cash flows from principal and interest receipts on the underlying mortgage pools. These securities may include mortgage pass-through securities and collateralized mortgage obligations (CMOs). Mortgage pass-through securities pay the holder of the security the principal and interest amounts received from the underlying pool of mortgages as these amounts are collected from the mortgage holders. In a CMO, the cash flows from principal and interest payments from one or more mortgage pass-through

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

securities or a pool of mortgages may be reallocated to multiple security classes with different priority claims and payment streams (commonly referred to as tranches.) A holder of the CMO security thus chooses the class of security that best meet its risk and return objectives. Both pass-through securities and CMOs are subject to significant market risk due to fluctuations in interest rates, prepayment rates and various liquidity factors related to their specific markets.

The mortgage pass-through securities issued by GNMA, FNMA, and FHLMC are classified by the University as U.S. government securities. The mortgage pools underlying the GNMA pass-through securities are backed by the full faith and credit of the U.S. government by the Federal Housing Administration (FHA), Veterans Administration (VA), and the Farmers Home Administration (FHA). The FNMA and FHLMC securities are collateralized by underlying pools of mortgages primarily issued by GNMA, FNMA, or FHLMC which guarantee full and timely payment of principal and interest.

The CMOs held by the University include mortgage-backed securities issued by FNMA, FHLMC, and certain trusts and private corporations (including REMIC issuers). In addition, non-traditional mortgage pass-through securities, such as “interest-only strips” and “principal-only strips”, if held by the University, are classified as CMOs. The University did not hold any non-traditional pass-through securities during the year.

As of June 30, 2002, the University was holding \$12,517,000 in mortgage-backed securities valued at fair value representing approximately 5.91% of its total investments. Of this amount \$7,397,000 represent investments in CMOs.

Other Asset-Backed Securities - The University invests in various asset-backed securities such as automobile loan securitizations, credit card securitizations, and home equity loans. The University invests in the various asset-backed securities to increase the yield and return on its investment portfolio given the available alternative investment opportunities.

The values of these other asset-backed securities are generally based on the cash flows to be received from the underlying pools of assets. Accordingly, these securities are subject to market risk due to fluctuations in interest rates, prepayment rates, and various liquidity factors related to their specific markets. The market risk is reduced by the University's preference to invest in the shorter average life securities.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

These security holdings are subject to credit-related losses in the event of non-performance by the issuers or counterparties to these instruments. However, the University does not expect any issuers or counterparties to fail to meet their obligation given their high credit ratings. The assets that collateralize these securities, which could be liquidated at market values at the time of non-performance, reduce the credit risk.

As of June 30, 2002, the University was holding \$2,068,000 in asset-backed securities valued at fair value representing approximately .98% of its total investments.

Indirect Derivative Holdings - The University identifies various external investment funds (mutual funds, external investment pools) that meet asset allocation and investment management objectives. The University invests in these funds to increase the yield and return on its investment portfolio given the available alternative investment opportunities and to diversify its asset holdings. Fund investments generally include equity and bond funds. Certain funds expose the University to significant amounts of market risk by trading or holding derivative instruments and by leveraging the securities in the fund.

The University limits the amount of funds managed by any single asset manager and also limits the amount of funds to be invested in particular security classes. As of June 30, 2002, the University was holding \$11,508,000 in a mutual fund for which investments in mortgage and asset backed securities totaled \$5,150,000 valued at fair value representing approximately 2.43% of its total investments. Of this amount \$4,667,000 represented investments in CMOs.

NOTE 4 - 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 Endowment Board of Trustees to authorize for expenditure the net appreciation, realized and unrealized, of the investments of the endowment funds.

Investment return of the University's endowment funds is predicated on the total return concept (yield plus appreciation). Annual payouts from the University's pooled endowment funds, which were 4.6% for the current year, are determined by applying the 4.6% rate to the average market value of each fund for the twelve quarters ending with the proper fiscal year. 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,

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

expendable net asset endowment balances to make up the difference. At June 30, 2002, the endowment fund had \$96,873,000 in expendable revenues and appreciation of which \$85,474,000 was restricted to specific purposes.

NOTE 5 - RECEIVABLES

Receivables at June 30, 2002 were as follows:

(in thousands)

	Gross Receivables	Less Allowance for Doubtful Accounts	Net Receivables
Current Receivables:			
Students	\$ 3,366	\$ (2,199)	\$ 1,167
Accounts	22,131	(2,258)	19,873
Intergovernmental	9,530		9,530
Investment Earnings	3,242		3,242
Interest on Loans	300	(277)	23
Total Current Receivables	<u>\$ 38,569</u>	<u>\$ (4,734)</u>	<u>\$ 33,835</u>
Notes Receivables:			
Notes Receivable - Current:			
Federal Loan Programs	\$ 1,220	\$ 0	\$ 1,220
Institutional Student Loan Programs	180		180
Total Notes Receivable - Current	<u>\$ 1,400</u>	<u>\$ 0</u>	<u>\$ 1,400</u>
Notes Receivable - Noncurrent:			
Federal Loan Programs	\$ 9,659	\$ (745)	\$ 8,914
Institutional Student Loan Programs	527	(142)	385
Total Notes Receivable - Noncurrent	<u>\$ 10,186</u>	<u>\$ (887)</u>	<u>\$ 9,299</u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 6 - CAPITAL ASSETS

A summary of changes in the capital assets is presented as follows:

(in thousands)

	Balance July 1, 2001	Adjustments	Increases	Decreases	Balance June 30, 2002
Capital Assets, Non-Depreciable:					
Land	\$ 10,021	\$ 0	\$ 343	\$ 0	\$ 10,364
Construction in Progress	34,394	(20,585)	24,235		38,044
Total Capital Assets, Non-Depreciable	44,415	(20,585)	24,578		48,408
Capital Assets, Depreciable:					
Buildings	503,659	20,585	4,031		528,275
Machinery and Equipment	191,539		26,848	(9,585)	208,802
General Infrastructure	52,801		8,100		60,901
Total Capital Assets, Depreciable	747,999	20,585	38,979	(9,585)	797,978
Less Accumulated Depreciation/Amortization for:					
Buildings	197,039		13,562		210,601
Machinery and Equipment	127,818		14,806	(7,697)	134,927
General Infrastructure	12,713		1,320		14,033
Total Accumulated Depreciation/Amortization	337,570		29,688	(7,697)	359,561
Total Capital Assets, Depreciable, Net	410,429	20,585	9,291	(1,888)	438,417
Capital Assets, Net	\$ 454,844	\$ 0	\$ 33,869	\$ (1,888)	\$ 486,825

NOTE 7 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2002 were as follows:

(in thousands)

	Amount
Accounts Payable	\$ 19,495
Accrued Payroll	3,604
Contract Retainage	1,655
Other	4,259
Total Accounts Payable and Accrued Liabilities	\$ 29,013

NOTE 8 - SHORT-TERM DEBT – COMMERCIAL PAPER PROGRAM

The University has available Commercial Paper Program financing for short-term credit up to \$25,000,000 to finance capital construction projects. As of June 30, 2002, \$2,000,000 of Commercial Paper was issued and is outstanding.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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.

Short-term debt activity for the year ended June 30, 2002 was as follows:

(in thousands)

	Balance July 1, 2001	Issued	Redeemed	Balance June 30, 2002
Commercial Paper Program	\$ 0	\$ 2,000	\$ 0	\$ 2,000

NOTE 9 - LONG-TERM LIABILITIES

A. Changes in Long-Term Liabilities - A summary of changes in the long-term liabilities is presented as follows:

(in thousands)

	Balance July 1, 2001	Additions	Reductions	Balance June 30, 2002	Current Portion
Notes, Bonds, and Capital Leases Payable					
General Revenue Bonds Payable	\$ 0	\$ 15,960	\$ 0	\$ 15,960	\$ 1,115
Revenue Bonds Payable	93,069		(21,937)	71,132	5,213
Add/Deduct Premium/Discount	(40)	(14)	71	17	
Total Bonds Payable	93,029	15,946	(21,866)	87,109	6,328
Notes Payable	140		(140)		
Capital Leases Payable		319	(44)	275	53
Total Notes, Bonds, and Capital Leases Payable	93,169	16,265	(22,050)	87,384	6,381
Compensated Absences	25,315	22,984	(22,628)	25,671	1,886
Total Long-Term liabilities	\$ 118,484	\$ 39,249	\$ (44,678)	\$ 113,055	\$ 8,267

Additional information regarding capital lease obligations is included in Note 10.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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

(in thousands)

Purpose	Series	Interest Rate/ Ranges	Final Maturity Date	Original Amount of Issue	Principal Paid Through 6/30/2002	Principal Outstanding 6/30/2002
STUDENT HOUSING SYSTEM						
Dormitory – Sullivan Hall	(1) F	3.625%	09/01/2004	\$ 2,200	\$ 1,900	\$ 300
Dormitory Complex	(1) G	3.0%	09/01/2006	3,225	2,565	660
Avent Ferry Complex	(1) M	5.3-6.1%	09/01/2014	11,820	10,295	1,525
Refund Housing System Series H, J, and K	(1) N	5-5.8%	09/01/2009	4,110	1,760	2,350
Residence Hall Improvement Project	(1) (A)	3.25-5%	10/01/2010	15,770	3,155	12,615
Housing System Project	(1) (B)	5-5.75%	10/01/2011	3,020	240	2,780
Refunding Housing System Series L and M	(9) 2002B	2-5%	10/01/2014	8,800		8,800
Total Student Housing System				48,945	19,915	29,030
DINING HALL SYSTEM						
Dining Hall System Refunding Bonds	(2) 1996	4-5.3%	02/01/2012	2,345	375	1,970
STUDENT HEALTH SYSTEM						
Student Health Facility Project	(3) (A)	3.25-5.25%	10/01/2013	5,615	835	4,780
PARKING SYSTEM						
Parking System Refunding Bonds	(4) 1996	4-5.1%	06/01/2009	6,530	1,790	4,740
ATHLETIC SYSTEM						
Entertainment and Sports Arena Project	(5) (A)	3.25-5.25%	10/01/2018	6,325	620	5,705
CENTENNIAL CAMPUS SYSTEM						
Centennial Campus Projects	(6) 1997A	6.55-7.04%	12/15/2010	7,765	2,130	5,635
Centennial Campus Projects	(6) 1997B	5.125%	12/15/2016	7,090		7,090
Centennial Campus Projects	(6) 1999A	Variable	12/15/2019	13,500	200	13,300
Centennial Campus Projects	(6) 1999B	7.04%	12/15/2004	2,117	805	1,312
Refunding Centennial Campus Series 1993	(9) 2002C	2.75-6.45%	10/01/2013	7,160		7,160
Total Centennial Campus System				37,632	3,135	34,497
STUDENT CENTER SYSTEM						
University Student Center	(7) 1996	4.5-5.1%	11/01/2009	2,210	445	1,765
OTHER						
Gymnasium Refunding Bonds	(8) (A)	3.25-4%	10/01/2007	1,695	360	1,335
Central Stores Expansion Project	(8) (B)	5-5.5%	10/01/2020	3,370	100	3,270
Total Other				5,065	460	4,605
Total Bonds Payable (principal only)				\$ 114,667	\$ 27,575	87,092
Less: Unamortized Discount						(313)
Plus: Unamortized Premium						330
Total Bonds Payable						\$ 87,109

(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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

addition, fund reservations required by the Bond Indentures have been established and recorded as restricted net assets. The following revenues as summarized in Note 11 have been pledged or are security for the bonds:

- | | |
|---|--|
| (1) Residential Life Revenues (Housing) | (6) Other Revenues (Centennial Campus) |
| (2) Dining Revenues | (7) Student Center Revenues |
| (3) Student Health Revenues | (8) Other Sales and Service Revenues
(Central Stores and Gymnasium) |
| (4) Parking Revenues | (9) Available Funds (General Revenue Bonds) |
| (5) Athletic Revenues | |

Available funds, as defined in the General Indenture date 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 is a variable rate demand bond issue. Demand bonds are securities that contain a “put” feature that allows bondholders to demand payment before the maturity of the debt upon proper notice to the University’s remarketing or paying agents.

With regards to the following demand bond, the University has entered into an agreement, which would convert the demand bond 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 First Union National Bank, 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) paying 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 (7) days notice and delivery to the bank paying agent, The Bank of New York. Upon notice from the bond paying agent,

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 First Union National Bank, 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, payable quarterly in arrears, beginning on October 1, 1999 and on each 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, 2002 there were no Liquidity Provider Bonds held by the Liquidity Facility. The original Liquidity facility is scheduled to expire on September 15, 2003 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 twenty (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.

Effective October 1, 1999, the University entered into an interest rate swap contractual agreement with Lehman Brothers, Inc. on \$9,000,000 of these demand bonds. Under this agreement the University will pay interest at a fixed rate of 4.574%. On a monthly basis the difference between 67% of the weighted average of the weekly LIBOR (London Interbank Offered Rates) rate and the fixed rate will be calculated. If the fixed rate is greater than the LIBOR calculated rate, the University will pay the difference to Lehman Brothers, Inc. If the LIBOR rate is greater, Lehman Brothers will refund the difference to the University. During the

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

fiscal year the University paid Lehman Brothers \$269,000 under this agreement.

- D. Annual Requirements** - The annual requirements to pay principal and interest on the long-term obligations at June 30, 2002 are as follows:

(in thousands)

<u>Fiscal Year</u>	<u>Annual Requirements</u>	
	<u>Bonds Payable</u>	
	<u>Principal</u>	<u>Interest</u>
2003	\$ 6,328	\$ 3,661
2004	6,587	3,399
2005	6,287	3,089
2006	6,525	2,785
2007	6,815	2,488
2008-2012	30,840	7,820
2013-2017	18,305	2,275
2018-2022	5,405	272
Total Requirements	<u>\$ 87,092</u>	<u>\$ 25,789</u>

Interest on the variable rate revenue bonds is calculated at 4.574% at June 30, 2002.

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 an interest rate swap agreement to ensure that the net interest rate will not exceed a fixed rate of 4.574% over the life of the demand bond. See Note 9C for more information on the demand bonds and the interest rate swap.

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

On April 16, 2002 the University defeased \$1,125,000 of outstanding North Carolina State University at Raleigh Housing System Revenue Refunding Bonds of 1991, Series L (original issue amount \$4,985,000); \$7,520,000 of outstanding North Carolina State University at Raleigh Housing System Revenue Bonds of 1994, Series M (original issue amount \$11,820,000), and \$7,290,000 of outstanding North Carolina State University at Raleigh Taxable Revenue Bonds Centennial Campus Projects, Series 1993 (original issue amount \$9,855,000). Securities were deposited into an irrevocable trust 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. As a result, the University reduced its debt

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

service requirements by \$3,702,000 over the next 12 years and obtained an economic gain of \$534,000. At June 30, 2002 the outstanding balance of the defeased bonds was \$14,810,000.

NOTE 10 - LEASE OBLIGATIONS

- A. Capital Lease Obligations** – A Capital lease obligation relating to a DNA Analyzer Sequencer was 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, 2002:

<i>(in thousands)</i>	
<u>Fiscal Year</u>	<u>Amount</u>
2003	\$ 78
2004	79
2005	79
2006	79
2007	13
Total Minimum Lease Payments	\$ 328
Amount Representing Interest (8.77% Rate of Interest)	53
Present Value of Future Lease Payments	<u>\$ 275</u>

Leased assets amounted to \$319,000 less accumulated depreciation of \$23,000 at June 30, 2002.

- B. Operating Lease Obligations** - Future minimum lease payments under non-cancelable operating leases consist of the following at June 30, 2002:

<i>(in thousands)</i>	
<u>Fiscal Year</u>	<u>Amount</u>
2003	\$ 2,240
2004	1,670
2005	1,473
2006	773
2007	412
Total Minimum Lease Payments	<u>\$ 6,568</u>

Rental expense for all operating leases during the year was \$2,410,000.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 11 - REVENUES

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

(in thousands)

	Gross Revenues	Internal Sales Eliminations	Less Scholarship Discounts	Less Allowance for Uncollectibles	Net Revenues	Revenues Pledged as Security for Debt	
Operating Revenues:							
Student Tuition and Fees	\$ 105,087	\$ (1,486)	\$ (20,948)	\$ 1,783	\$ 84,436	\$ 0	
Sales and Services:							
Sales and Services of Auxiliary Enterprises:							
Residential life	\$ 21,942	\$ (72)	\$ (3,745)	\$ 186	\$ 18,311	\$ 21,942	(A)
Dining	17,709	(1,435)	(3,086)	118	13,306	17,709	(B)
Bookstore	12,725	(645)			12,080		
Athletics	23,404		(399)	3	23,008	23,404	(C)
Parking	7,797	(565)		53	7,285	7,797	(D)
Student Center	4,928	(108)	(925)	24	3,919	4,928	(E)
Student Health	7,769		(437)	25	7,357	7,769	(F)
Other	11,938	(10,412)	(1,207)		319	2,360	(G)
Sales and Services of Educational and Related Activities	48,925	(16,659)		262	32,528	407	(G)
Total Sales and Services	\$ 157,137	\$ (29,896)	\$ (9,799)	\$ 671	\$ 118,113	\$ 86,316	

Revenue bonds secured by pledged revenues:

- (A) Student Housing System
- (B) Dining Hall System
- (C) Athletic System
- (D) Parking System
- (E) Student Center System
- (F) Student Health System
- (G) Other

NOTE 12 - OPERATING EXPENSES BY FUNCTION

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

(in thousands)

	Salaries and Benefits	Supplies and Materials	Services	Scholarships and Fellowships	Utilities	Depreciation	Total
Instruction	\$ 185,252	\$ 16,959	\$ 19,080	\$ 0	\$ 4	\$ 0	\$ 221,295
Research	115,898	7,622	38,909		441		162,870
Public Service	67,580	7,434	23,552		277		98,843
Academic Support	29,522	4,040	6,614		8		40,184
Student Services	9,453	1,932	10,914				22,299
Institutional Support	36,951	2,000	11,583		453		50,987
Operations and Maintenance of Plant	15,534	11,490	5,699		15,969		48,692
Student Financial Aid				11,751			11,751
Auxiliary Enterprises	32,231	25,474	27,088		2,878		87,671
Depreciation						29,688	29,688
Total Operating Expenses	\$ 492,421	\$ 76,951	\$ 143,439	\$ 11,751	\$ 20,030	\$ 29,688	\$ 774,280

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 13 - 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. The Teachers' and State Employees' Retirement System (System) is a multiple-employer cost sharing defined benefit pension plan administered by the North Carolina State Treasurer.

After five years of creditable service, members of the Teachers' and State Employees' Retirement System qualify for a vested deferred benefit. Employees who retire on or after age 65 and complete 5 years of membership service (age 55 and 5 years of creditable service for law enforcement officers), reach age 60 with 25 years of membership service, or complete 30 years of creditable service receive a retirement allowance of 1.81% of an average final compensation (based on the 4 consecutive years that produce the highest average) multiplied by the number of years of creditable service. Employees may retire with reduced benefits if they reach age 50 with 20 years of creditable service or reach age 60 with 5 years of creditable service (age 50 with 15 years creditable service for law enforcement officers).

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, 2002, these rates were set at 1.97% of covered payroll for employers and 6% of covered payroll for members.

For the year ended June 30, 2002, the University had a total payroll of \$438,967,000 of which \$234,943,000 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were \$14,097,000 and \$4,628,000, respectively. The University made one hundred percent of its annual required contributions for the years ended June 30, 2002, 2001, and 2000, which were \$4,628,000, \$11,938,000, and \$17,430,000, respectively.

The Teachers' and State Employees' Retirement System's financial information is included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's Internet home page <http://www.osc.state.nc.us/> and clicking on "Financial

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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, which 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 any one of the carriers or may direct their contributions to one carrier and the University contributions to another. Each carrier offers a variety of investment funds, including both fixed and variable account investment options and mutual funds.

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, 2002, 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.

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.

For the year ended June 30, 2002, the University had a total payroll of \$438,967,000 of which \$120,169,000 was covered under the Optional Retirement Program. Total employee and employer contributions for pension benefits for the year were \$7,210,000 and \$8,220,000, 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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 \$530,000 for the year ended June 30, 2002.

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, 2002 were \$101,000. The voluntary contributions by employees amounted to \$2,748,000 for the year ended June 30, 2002.

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 non-profit 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 \$7,375,000 for the year ended June 30, 2002.

- 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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

Retirement System. Currently, 235 employees participate in CSRS. Participating employees are required by federal statute to contribute 7% of salary and the University 8.51% of salary to CSRS. In addition, the employees may contribute up to 6% of salary to the Thrift Savings Plan (a defined contribution plan managed by the Federal Retirement Thrift Investment Board). The contribution for CSRS for the year ended June 30, 2002, was \$2,418,000 which consisted of \$1,340,000 from the University and \$1,078,000 from the employees. Employees contributed \$54,000 to the Thrift Savings Plan.

Under the Federal Employees Retirement System (FERS), employees are required to contribute .8% of salary and the University 10.7%. Currently, 15 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 11% of their salary. The contribution for the year ended June 30, 2002 was \$276,000 which consisted of \$9,000 from employees and \$128,000 from the University for FERS and \$96,000 from employees and \$43,000 from the University for the Thrift Savings Plan.

NOTE 14 - OTHER POSTEMPLOYMENT BENEFITS

- A. Health Care for Long-Term Disability Beneficiaries and Retirees -** The University participates in State-administered programs which 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 2.35% of the covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program for these health care benefits. For the fiscal year ended June 30, 2002, the University's total contribution to the Plan was \$8,345,000. The University assumes no liability for retiree health care benefits provided by the programs other than its required contribution. Additional detailed information about these programs can be located in the State of North Carolina's *Comprehensive Annual Financial Report*.
- B. Long-Term Disability -** The University participates in the Disability Income Plan of North Carolina (DIPNC). Established by Chapter 135, Article 6, of the General Statutes, DIPNC provides short-term and long-

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

term disability benefits to eligible members of the Teachers' and State Employees' Retirement System or 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 fiscal year ended June 30, 2002, the University's total contribution to the DIPNC was \$1,847,000. 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 15 - 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 been within coverage limits in any of the past three fiscal years.

Tort claims of up to \$500,000 are self-insured under the authority of the State Tort Claims Act. In addition, the State provides excess public officers' and employees' liability insurance up to \$11,000,000 via contract with a private insurance company. The University pays the premium, based on a composite rate, directly to the private insurer.

The University is required to maintain fire and lightning coverage on all State-owned buildings and contents through the State Property Fire Insurance Fund (Fund), an internal service fund of the State. Such coverage is provided at no cost to operations supported by the State's General Fund. Other operations not supported by the State's General Fund are charged for the coverage. Losses covered by the Fund are subject to a \$500 per occurrence deductible, except 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 specific computers and "miscellaneous equipment" on a scheduled basis.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

All State-owned vehicles are covered by a liability insurance program through Travelers Insurance Company as administered 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. The University pays premiums to the 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 administered by the North Carolina Department of Insurance. Coverage limit is \$1,000,000 per occurrence with a \$10,000 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, Motor Sports Liability, Campers Accident and Sickness, Athletic Accident, Boiler and Machinery, Watercraft, Nuclear Energy Liability, and Surety Bonds.

Employees and retirees are provided health care coverage by the Comprehensive Major Medical Plan (Plan), a component unit of the State. The Plan is funded by employer and employee contributions and is administered by a third-party contractor. Effective for the October 1, 2001 through September 30, 2002 year, the Plan no longer offers health coverage through HMO plans.

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

Term life insurance of \$25,000 to \$50,000 is provided to eligible workers. This self-insured death benefit program is administered by the State Treasurer and funded via employer contributions.

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.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

NOTE 16 - 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 \$38,230,000 at June 30, 2002.
- 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, 2002 totaled \$182,000.

As previously reported, litigation is still pending in Superior Court between NC School Boards Association, et. al. V. Harlan Boyles, et. al. which involves various State officials in their official capacity which seeks 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. The complaint alleges in part that the 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. The lawsuit seeks declaratory judgment that the State Civil Penalty and Forfeiture Fund, the State School Technology Fund, and the Public Settlement Reserve Fund are unconstitutional. The Wake County Superior Court ruled in favor of the Plaintiffs. The order is retroactive for a three year statute of limitations from the date the civil action was filed to include all affected civil fines and penalties collected by state agencies since December 1995. The court has stayed enforcement of this ruling, pending the State’s appeal. On January 8, 2002, the Defendants appealed the ruling. The school board plaintiffs have filed a motion for discretionary review by the Supreme Court prior to decision by the Court of Appeals (A.K.A. a “by-pass” motion). The Defendants filed a reply resisting the motion. If the appellate courts uphold the Superior Court decision, the University may be required to pay Wake County School Boards parking and library fines

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

amounting to approximately \$5,828,000 since 1995 and approximately \$900,000 annually.

On May 9, 2002, the UNC Board of Governors authorized a resolution for the University to join as co-plaintiffs in a civil action filed against two business entities. This action is brought by the plaintiffs for patent infringement. An entity affiliated with one of the defendants in this action has filed a complaint for declaratory judgment in the U.S. District Court for the District of Alabama against the co-plaintiffs. The entity seeks a judgment that several of the University's patents relating to pasteurized liquid whole eggs are invalid and unenforceable. If successful, the University would not lose any money in the litigation, but could lose several million dollars in annual revenue that the University now earns from licensing the patents.

A publishing company has reportedly filed a civil action in Wisconsin State Court against the University. The complaint has not yet been officially served on the University. This appears to be a breach of contract action, claiming damages of approximately \$1,000,000.

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

- C. University Improvement General Obligation Bonds** – The 1999-2000 Session of the General Assembly of North Carolina authorized the issuance of two billion five hundred million dollars of general obligation bonds of the State, as subsequently approved by a vote of qualified voters of the State, to provide funds for capital improvements for the University of North Carolina. The funds authorized are to be used solely for capital facilities cost on the University of North Carolina campuses as specified in the legislation. The bond legislation specifies the amount of bond funding for each University campus and the level of bond funding intended for each project. The bonds are authorized to be issued over a six-year period beginning in 2001 at a level not to exceed amounts provided in the legislation. Using a cash flow financing approach, The University of North Carolina – General Administration (UNC-GA), establishes annual amounts not to exceed for each approved project. The amounts not to exceed are subject to change due to actual cash availability and needs during the year. Subsequent to the bond sales and the availability of bond proceeds, UNC-GA notifies the Office of State Budget and Management (OSBM) of the amounts not to exceed for each

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

approved project. Within these amounts, based on an official request of cash needs from the University, OSBM authorizes allotments. The University records the allotments as revenue on the accompanying financial statements. The University's remaining authorization \$439,207,000 is contingent on future bond sales and OSBM allotment approval. Because of uncertainty and time restrictions the remaining authorization is not recorded as an asset or revenue on the accompanying financial statements.

NOTE 18 - RELATED PARTIES

Foundations - There are twelve 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 Dairy 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., North Carolina State University 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. The University's financial statements do not include the assets, liabilities, net assets, or operational transactions of the foundations, except for support from each organization to the University. This support approximated \$30,163,000 for the year ended June 30, 2002.

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 will serve as a regional sports entertainment center and be 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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

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 \$40,700 for each men's and \$17,800 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.

Subsequent to year-end 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 18 - ACCOUNTING CHANGES

Effective July 1, 2001, the University implemented 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 financial statement presentation required by these Statements is a single-column enterprise activity rather than the fund-group perspective previously reported. Significant accounting changes in order to comply with the new requirements include adopting depreciation on capital assets, reporting revenues net of discounts and allowances, eliminating interfund activities, classifying activities as operating or nonoperating, classifying assets and liabilities as current or noncurrent, and prorating summer school activities to periods earned.

In addition, the University implemented GASB Statement No. 38, *Certain Financial Statement Note Disclosures*. Changes in existing disclosures include more detailed information on debt service requirements, obligations under leases, and short-term debt. New disclosures include variable debt interest information and the major components of receivable and payable balances.

NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)

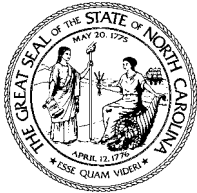
NOTE 19 - NET ASSET RESTATEMENT

As referred to in Note 18, the University implemented 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*.

	(in thousands)
July 1, 2001 Fund Equity as previously reported	\$ 1,118,990
Implementation of GASB 34/35	<u>(459,488)</u>
July 1, 2001 Net Assets as Restated	<u>\$ 659,502</u>

North Carolina State University Schedule of General Obligation Bond Project Authorizations, Budgets, and Expenditures For Project-to-Date as of June 30, 2002 (dollars expressed in thousands)							
							Schedule 1
	Projected	General		Total			Expected
	Start	Obligation Bonds	Other	Project	Amount	Percent	Completion
Capital Improvement Projects	Date	Authorized	Sources	Budget	Expended	Completed	Date
Projects Started							
301/339 Undergraduate Science Teaching Lab - Phase I	Jul 2000	\$ 33,219	\$ 1,898	\$ 35,117	\$ 7,686	21.89%	Apr 2004
302 Wither Hall - Conversion from Laboratory to General Academic Use	Apr 2002	10,934		10,934			Jun 2006
303/336 College of Engineering Complex - Phase I	Nov 2000	34,382	1,800	36,182	3,145	8.69%	Jul 2004
304/335 College of Veterinary Medicine - Research Addition and Renovation of Laboratories and Academic Space	Jul 2000	19,952	1,337	21,289	1,434	6.74%	Jan 2005
305 College of Engineering Complex Phase II	Dec 2000	44,438		44,438			May 2005
306 David Clark and Undergraduate Science Teaching Lab - Phase II	Jan 2001	22,712		22,712	591	2.60%	Nov 2004
309 1911 Classroom Building - Comprehensive Renovation	May 2002	6,640		6,640			Jun 2008
311 Riddick Lab - Comprehensive Renovation and Conversion from Laboratory to Classroom Building	May 2001	24,872		24,872	105	0.42%	Mar 2006
313 Clark Hall Conversion and Renovation	Jan 2001	2,300		2,300	420	18.26%	Mar 2003
314 Schaub Food Science Building - Comprehensive Renovation	Jan 2002	10,105		10,105			May 2006
317 Leazar Hall Laboratory Building - Comprehensive Renovation	Feb 2002	7,963		7,963			Jul 2006
318 Daniels Hall Laboratory Building - Comprehensive Renovation	Jun 2001	7,490		7,490	8	0.11%	Nov 2006
319 Jordan Hall Lab and Classroom Addition	Jun 2001	12,998		12,998	131	1.01%	Nov 2004
320 Library Addition	May 2002	8,756	100	8,856	119	1.34%	May 2006
321 Support Services Center	Jan 2001	8,891	3,500	12,391	290	2.34%	Oct 2004
321 Visitor's Center	Oct 1999	952	3,885	4,837	269	5.56%	Jul 2004
322 Field Research Laboratories and Outlying Research Facilities	Jan 2001	2,381		2,381	20	0.84%	May 2005
323 Horticulture Classroom at Arboretum Education Center	Sep 1997	476	3,713	4,189	3,518	83.98%	Jul 2002
324 Partners III	May 2001	5,785	10,312	16,097	1,358	8.44%	Oct 2004
324 College of Veterinary Medicine - Research Lab Building	Apr 2001	5,700		5,700			Jan 2005
324 Flex Building	Oct 2001	5,100		5,100	901	17.67%	Dec 2002
324 West Research Annex	Oct 2001	1,500		1,500	18	1.20%	Jan 2005
325 Public Safety Facility	Feb 2001	4,480		4,480	157	3.50%	Jun 2004
326 College of Veterinary Medicine - Mechanical and Electrical System Improvements	Jan 2001	20,025		20,025	236	1.18%	Sep 2007
327 Technology Infrastructure Expansion	Jul 2001	2,424		2,424	90	3.71%	Jun 2003
328 Chilled Water Central Plant - North Campus	Dec 2000	39,818	465	40,283	2,680	6.65%	Nov 2005
330 Steam Distribution and Capacity Improvements (Sullivan)	Mar 2001	3,090	48	3,138	57	1.82%	Dec 2003
331 Main Campus Infrastructure (Including Water System)	Feb 2001	1,731		1,731			Jun 2005
331 Backflow Preventors	Feb 2001	2,038		2,038			Jun 2005
331 Wayfinding	Feb 2001	2,119		2,119	50	2.36%	Jun 2005
331 Pedestrian Tunnel	Feb 2001	2,998		2,998			Jun 2005
332 College of Veterinary Medicine - Infrastructure	Jan 2001	5,048	261	5,309	727	13.69%	Dec 2003
333 Centennial Campus - Infrastructure	Mar 2001	10,836	318	11,154	633	5.68%	Feb 2004
334 Land Acquisition	Jan 2001	2,100		2,100	346	16.48%	Jul 2004
337 Meat Processing Laboratory	Jun 2002	4,854	646	5,500	551	10.02%	Mar 2004
338 Research and Teaching Feed Mill	Jan 2001	2,582	288	2,870	2,007	69.93%	Dec 2002
340 Beef Herd Relocation	Sep 2001	1,350	150	1,500	450	30.00%	Oct 2002
340 Land Acquisition Lake Wheeler	Jan 2001	1,701	1,549	3,250	1,526	46.95%	Jan 2003
350 Project Management Costs	Dec 2001	20,423		20,423	659	3.23%	Jun 2009

North Carolina State University							
Schedule of General Obligation Bond Project Authorizations,							
Budgets, and Expenditures							
For Project-to-Date as of June 30, 2002							
(dollars expressed in thousands)							
							Schedule 1
							Page 2
	Projected	General		Total			Expected
	Start	Obligation Bonds	Other	Project	Amount	Percent	Completion
Capital Improvement Projects	Date	Authorized	Sources	Budget	Expended	Completed	Date
Projects Not Started - To Be Funded in Future Years							
308 South Gardner Hall Laboratory Building - Comprehensive Renovation	Jan 2003	14,580		14,580			
310 Park Shops - Comprehensive Renovation and Use Conversion for General Academic Use	May 2004	6,010		6,010			
312 Harrelson Classroom Building - Comprehensive Renovation	Sep 2003	12,960		12,960			
315 Williams Hall Laboratory Building - Comprehensive Renovation	Dec 2002	12,343		12,343			
316 Polk Hall Laboratory - Comprehensive Renovation	Jun 2003	14,426		14,426			
329 Chilled Water Brickyard Loop Expansion and Cooling Tower	Jan 2003	2,775		2,775			
Total All Projects		\$ 468,257	\$ 30,270	\$ 498,527	\$ 30,182		
Note: The 1999-2000 Session of the General Assembly of North Carolina authorized the issuance of two billion five hundred million dollars of general obligation bonds of the State, as subsequently approved by a vote of qualified voters of the State, to provide funds for capital improvements for the University of North Carolina. The projects listed on this schedule are those funded or to be funded by bond proceeds from the general obligation bonds authorized by Senate Bill 912.							



Ralph Campbell, Jr.
State Auditor

STATE OF NORTH CAROLINA
Office of the 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.osa.state.nc.us>

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

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 sixteen-campus University of North Carolina System, which is a component unit of the State of North Carolina, as of and for the year ended June 30, 2002, and have issued our report thereon dated December 11, 2002.

As discussed in Note 18 to the financial statements, the University implemented Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities* and Statement No. 38, *Certain Financial Statement Note Disclosures* during the year ended June 30, 2002.

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.

Compliance

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 grants, 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 that are required to be reported under *Government Auditing Standards*.

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

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the University's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the Audit Committee, the Board of Trustees and Board of Governors, management and staff of the University, the Governor, the State Controller, the General Assembly, and federal awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties.



Ralph Campbell, Jr.
State Auditor

December 11, 2002

DISTRIBUTION OF AUDIT REPORT

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

EXECUTIVE BRANCH

The Honorable Michael F. Easley
The Honorable Beverly M. Perdue
The Honorable Richard H. Moore
The Honorable Roy A. Cooper, III
Mr. David T. McCoy
Mr. Robert L. Powell
Ms. Molly Corbett Broad
Dr. Marye Anne Fox
Mr. George Worsley

Ms. Peaches Gunter Blank

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

LEGISLATIVE BRANCH

Appointees to the Joint Legislative Commission on Governmental Operations

Senator Marc Basnight, Co-Chairman
Senator Charlie Albertson
Senator Kever M. Clark
Senator Daniel G. Clodfelter
Senator Walter H. Dalton
Senator James Forrester
Senator Linda Garrou
Senator Wilbur P. Gulley
Senator Kay R. Hagan
Senator David W. Hoyle
Senator Ellie Kinnaird
Senator Jeanne H. Lucas
Senator William N. Martin
Senator Stephen M. Metcalf
Senator Eric M. Reeves
Senator Larry Shaw
Senator R. C. Soles, Jr.
Senator David F. Weinstein

Representative James B. Black, Co-Chairman
Representative Martha B. Alexander
Representative E. Nelson Cole
Representative James W. Crawford, Jr.
Representative William T. Culpepper, III
Representative W. Pete Cunningham
Representative Beverly M. Earle
Representative Stanley H. Fox
Representative R. Phillip Haire
Representative Dewey L. Hill
Representative Maggie Jeffus
Representative Edd Nye
Representative William C. Owens, Jr.
Representative Drew P. Saunders
Representative Wilma M. Sherrill
Representative Joe P. Tolson
Representative Thomas E. Wright
Representative Douglas Y. Yongue

Other Legislative Officials

Senator Anthony E. Rand
Senator Patrick J. Ballantine
Representative N. Leo Daughtry
Representative Joe Hackney
Mr. James D. Johnson

Majority Leader of the N. C. Senate
Minority Leader of the N. C. Senate
Minority Leader of the N. C. House of Representatives
N. C. House Speaker Pro-Tem
Director, Fiscal Research Division

March 7, 2003

ORDERING INFORMATION

Copies of this report may be obtained by contacting the:

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

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

Telephone: 919/807-7500

Facsimile: 919/807-7647