



# Northern Arizona University

## Financial Report

2003-2004



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This financial report is compiled and issued by the Comptroller's Office  
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Flagstaff, AZ 86011-4069

This report is also available online at  
[www.nau.edu/comptroller](http://www.nau.edu/comptroller)



## UNIVERSITY ADMINISTRATION As of June 30, 2004

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President

**David Bousquet**  
Vice President for Enrollment  
Management and Student Affairs

**Liz Grobsmith**  
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**Frederick Hurst**  
Vice President for Extended  
Learning and Dean of Distance  
Learning

**David Lorenz**  
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and Financial Services

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Executive Vice President

**Molly Williams**  
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Advancement

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**The Honorable  
Janet Napolitano**  
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**The Honorable  
Tom Horne**  
Arizona Superintendent of  
Public Instruction

# INDEPENDENT AUDITORS' REPORT



DEBRA K. DAVENPORT, CPA  
AUDITOR GENERAL

STATE OF ARIZONA  
OFFICE OF THE  
AUDITOR GENERAL

WILLIAM THOMSON  
DEPUTY AUDITOR GENERAL

Members of the Arizona State Legislature

The Arizona Board of Regents

We have audited the accompanying financial statements of the business-type activities and aggregate discretely presented component units of Northern Arizona University as of and for the year ended June 30, 2004, as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the aggregate discretely presented component units. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts for the aggregate discretely presented component units is based solely on the reports of the other auditors.

We conducted our audit in accordance with U.S. generally accepted auditing standards. 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 and the reports of the other auditors provide a reasonable basis for our opinions.

As discussed in Note 1, the University's financial statements are intended to present the financial position, and the changes in financial position and cash flows, where applicable, of only those portions of the business-type activities, major fund, and aggregate discretely presented component units of the State of Arizona that are attributable to the University. They do not purport to, and do not, present fairly the financial position of the State of Arizona as of June 30, 2004, and the changes in its financial position and its cash flows, where applicable, for the year then ended in conformity with U.S. generally accepted accounting principles.

In our opinion, based on our audit and the reports of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and aggregate discretely presented component units of Northern Arizona University as of June 30, 2004, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with U.S. generally accepted accounting principles.

As described in Note 1, the University implemented the provisions of the Governmental Accounting Standards Board Statement No. 39, *Determining Whether Certain Organizations Are Component Units*, for the year ended June 30, 2004, which requires reporting as component units those organizations that raise and hold economic resources for the direct benefit of the University or its constituents.

The information included in the Management's Discussion and Analysis section listed in the table of contents has not been subjected to the auditing procedures applied in our audit of the financial statements and, accordingly, we express no opinion on such information.

Debbie Davenport  
Auditor General

November 17, 2004

# MANAGEMENT'S DISCUSSION AND ANALYSIS

The discussion and analysis of Northern Arizona University's financial statements provides an overview of the University's financial activities for the year ended June 30, 2004.

Management has prepared the financial statements and the accompanying note disclosures along with the discussion and analysis. Responsibility for the completeness and fairness of this information rests with the University's management.

## Using this Financial Report

During the year ended June 30, 2004, the University implemented the provisions of the Governmental Accounting Standards Board Statement No. 39, Determining Whether Certain Organizations Are Component Units, which requires reporting as a component unit those organizations that raise and hold economic resources for the direct benefit of the University or its constituents. Based on GASB No. 39, the University identified two component units, the Northern Arizona University Foundation (Foundation) and the Northern Arizona Capital Facilities Finance Corporation (NACFFC). The Foundation was incorporated as a not-for-profit corporation in the State of Arizona in January 1959 and operates exclusively for the benefit of Northern Arizona University. The Foundation receives gifts and bequests, administers and invests securities and property, and disburses payments to and on behalf of the University for advancement of its mission. NACFFC was incorporated in October 2001, as a nonprofit corporation under the laws of the State of Arizona for the purpose of acquiring, developing, constructing, maintaining and operating student housing and other capital facilities and equipment for the use and benefit of the University's students. The transactions between the University and its component units are similar to prior years and no material transactions occurred in fiscal year 2004.

This annual financial report includes the report of independent auditors, management's discussion and analysis, the financial statements in the format referred to below, and notes to the financial statements, which include the summary of significant accounting policies.

The financial statements presented by the University include the Statement of Net Assets, the Statement of Revenues, Expenses, and Changes in Net Assets, and the Statement of Cash Flows.

- The Statement of Net Assets presents the financial position of the University at the end of the fiscal year. This statement is classified between current assets/liabilities and non-current assets/liabilities. In addition, capital assets are depreciated over the useful life of the asset and the annual depreciation amount is shown as a current year expense.
- The Statement of Revenues, Expenses, and Changes in Net Assets distinguishes between operating and nonoperating revenues and expenses, with state appropriations reported as nonoperating revenue. Student tuition and fee revenues, and certain other revenues from students, are reported net of scholarship discounts and allowances.
- The financial statements include a Statement of Cash Flows prepared using the direct method. This statement provides information about the University's sources and uses of cash during the year.

## Financial Highlights

- Student tuition and fees increased 33 percent from the previous year or about \$17.5 million.
- Government grants and contracts increased approximately \$3.7 million from the prior year while private grants and contracts decreased by approximately \$1.6 million.
- University auxiliary enterprise revenues including residence life and the bookstore increased by approximately \$3.6 million.
- Proposition 301 share of state sales tax revenues increased 12.3 percent from the prior year to \$9.6 million in 2004.
- State appropriations increased by approximately \$455 thousand.
- During the fiscal year the University issued \$31.0 million of system revenue bonds, at an average interest rate of 4.6 percent, to finance several construction and renovation projects on the Mountain Campus (see Capital Assets and Debt Administration section).
- University current cash and investments increased by \$11.4 million to a total of \$55.5 million.



# MANAGEMENT'S DISCUSSION AND ANALYSIS

## STATEMENT OF NET ASSETS

The Statement of Net Assets presents the financial position of the University at the end of the fiscal year and includes all assets and liabilities of the University. A summarized comparison of the University's assets, liabilities, and net assets for the years ended June 30, 2004 and 2003 (in thousands), is as follows:

	2004	2003
Current assets	\$ 75,370	\$ 62,300
Noncurrent assets:		
Cash, cash equivalents, investments, and student loans receivable	43,214	31,749
Endowment investments	10,668	9,735
Capital assets – net of accumulated depreciation	204,422	194,522
Other noncurrent assets	<u>181</u>	<u>243</u>
Total noncurrent assets	<u>258,485</u>	<u>236,249</u>
Total assets	<u>333,855</u>	<u>298,549</u>
Long-term liabilities	<u>128,008</u>	<u>105,636</u>
Other liabilities	<u>25,725</u>	<u>27,414</u>
Total liabilities	<u>153,733</u>	<u>133,050</u>
Net assets	<u>\$ 180,122</u>	<u>\$ 165,499</u>

A review of NAU's Statement of Net Assets at June 30, 2004 and 2003 shows that the University's financial position remains stable and is improving.

**Current assets** consist primarily of cash and investments, government grants and contracts receivable, and accounts receivable. Cash and investments increased to approximately \$55.5 million at June 30, 2004 from \$44.1 million in the prior year primarily due to increased tuition revenues.

**Noncurrent assets** increased by approximately \$22.2 million over the prior year. Capital assets, representing a majority of noncurrent assets, increased approximately \$9.9 million over the fiscal year. Cash and investments held by trustee increased by \$12.0 million as unspent funds from the 2003 series bond proceeds were deposited until needed for capital projects. The changes in capital assets are discussed in more detail in the Capital Assets and Debt Administration section.

**Long-term liabilities** increased by \$22.4 million as of June 30, 2004. The increase is mainly attributed to the issuance of bonds in the amount of \$31.0 million which is discussed further in the Capital Assets and Debt Administration section.

**Other liabilities** include accounts payable, accrued expenses, and deferred revenue. Other liabilities are lower mainly due to a \$1.4 million decrease in accounts payable, and a \$3.2 million decrease in deferred revenue. The decrease in accounts payable was mainly due to the reduction in retainage on construction contracts. The decrease in deferred revenue is mainly attributed to a timing change in how the University records housing revenues and a decrease in revenues from the summer music camps.



# MANAGEMENT'S DISCUSSION AND ANALYSIS

## NET ASSETS

A summarized comparison of the University's net assets for the years ended June 30, 2004 and 2003 (in thousands), is as follows:

	<b>2004</b>	<b>2003</b> as adjusted
Invested in capital assets, net of related debt	\$ 114,348	\$ 110,914
Restricted:		
Nonexpendable	14,163	12,728
Expendable	14,367	14,382
Unrestricted	<u>37,244</u>	<u>27,475</u>
<b>Total net assets</b>	<b><u>\$ 180,122</u></b>	<b><u>\$ 165,499</u></b>

Net assets at June 30, 2004 increased overall by \$14.6 million or about 9.0 percent from 2003. The change in unrestricted net assets represents a significant portion of the overall increase, and was primarily due to additional tuition revenues of \$17.5 million, and an increase of \$3.6 million in auxiliary revenue. The 2003 net assets are shown as adjusted to correct misstatements in prior year classifications.

## STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

The Statement of Revenues, Expenses, and Changes in Net Assets presents the operating results of the University, as well as the nonoperating revenues and expenses. Annual state appropriations, while budgeted for operations, are considered nonoperating revenues according to U.S. generally accepted accounting principles. See the table of Combined Sources and Uses of Funds on pages 10-11 for an overview of the composition of revenues and expenses. A summarized comparison of the University's revenues, expenses, and changes in net assets for the years ended June 30, 2004 and 2003 (in thousands), is as follows:

	<b>2004</b>	<b>2003</b>
Operating Revenues		
Tuition and fees, net of scholarship allowances	\$ 70,821	\$ 53,272
Government grants and contracts	51,751	47,926
Auxiliary enterprises	33,349	29,770
Other	<u>9,234</u>	<u>12,541</u>
Total operating revenues	<u>165,155</u>	<u>143,509</u>
Operating Expenses:		
Educational and general	227,798	216,080
Auxiliary enterprises	29,587	30,007
Depreciation	<u>16,070</u>	<u>17,468</u>
Total operating expenses	<u>273,455</u>	<u>263,555</u>
Nonoperating Revenues (Expenses):		
State appropriations	111,643	111,187
Share of state sales tax	9,564	8,520
Grants and contracts	3,968	4,649
Investment income	2,085	1,545
Interest expense on capital asset related debt	(5,206)	(5,022)
Other nonoperating revenues/expenses	<u>80</u>	<u>610</u>
Total nonoperating revenues and expenses	<u>122,134</u>	<u>121,489</u>
Increase before capital and endowment additions	13,834	1,443
Capital and endowment additions	<u>789</u>	<u>911</u>
<b>Increase in net assets</b>	<b><u>\$ 14,623</u></b>	<b><u>\$ 2,354</u></b>

# MANAGEMENT'S DISCUSSION AND ANALYSIS

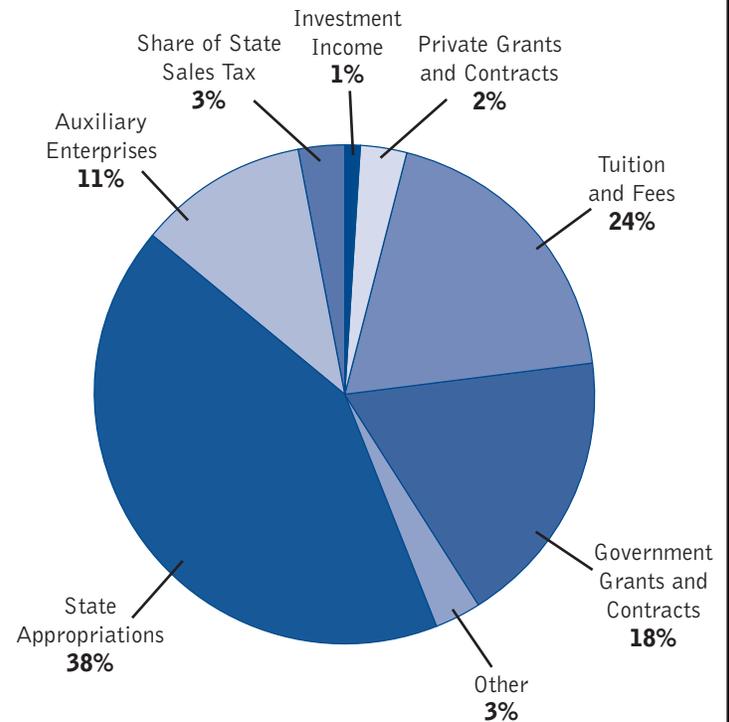
## REVENUES ANALYSIS

State appropriations and tuition and fees continue to be the major funding sources for current operations related to educational purposes. Operating revenues (not including state appropriations) increased 15 percent or about \$21.6 million in 2004. This increase is due mainly to additional tuition revenue of \$17.5 million and an increase of \$3.6 million in auxiliary revenues. The \$17.5 tuition revenue increase from 2003 is mainly due to a board approved tuition rate increase. The increase in auxiliary revenues is due to higher sales at the University bookstore of \$832,000, an increase in residential life revenues of \$930,000 and an increase in Other Auxiliaries revenue of \$1.8 million due to the reclassification of food service revenue from other revenues. Government Grants and Contracts revenue increased mainly due to additional grant funding from the U.S. Department of Education - Gear Up of \$2.1 million. State appropriations increased from \$111.2 million in fiscal year 2003 to \$111.6 million in 2004.

## EXPENSES ANALYSIS

Educational and general expenses continued to account for a majority of the operating expenses. Educational and general expenses increased in fiscal year 2004 by \$11.7 million. Significant components of the increase within educational and general expenses were instruction, \$4.8 million; public service, \$2.4 million; scholarships and fellowships, \$3.1 million; and student services, \$1.8 million. The increase in overall expenditures is due in part to significant increases in employee related costs. Overall, employee related expenses increased from \$34.3 million in FY 2003 to \$38.7 million in FY 2004, a 13% increase. Significant increases were in retirement benefit expenses; \$1.8 million and health insurance; \$2.2 million. The increase in scholarships and fellowships is due to a board approved increase in need-based scholarships of approximately \$3.0 million.

## Total Revenues Fiscal Year 2004



## Expenses - By functional classification

A comparative summary of the University's expenses by functional classification for the years ended June 30, 2004 and June 30, 2003, is as follows:

	2004	2003
<b>Operating:</b>		
Instruction	\$ 95,100,334	\$ 90,284,592
Research	18,824,650	18,080,532
Public service	21,918,764	19,541,187
Academic support	20,159,750	19,622,315
Student services	19,129,780	17,310,914
Institutional support	26,992,423	28,386,305
Operation and maintenance of plant	13,738,356	13,991,319
Scholarships and fellowships	11,934,017	8,862,509
Total educational and general expenses	<u>227,798,074</u>	<u>216,079,673</u>
Auxiliary enterprises	29,587,505	30,007,017
Depreciation	16,069,536	17,467,988
Total operating expenses	<u>273,455,115</u>	<u>263,554,678</u>
<b>Nonoperating:</b>		
Interest and other	<u>5,780,915</u>	<u>5,540,139</u>
<b>Total Expenses</b>	<u>\$ 279,236,030</u>	<u>\$ 269,094,817</u>

# MANAGEMENT'S DISCUSSION AND ANALYSIS

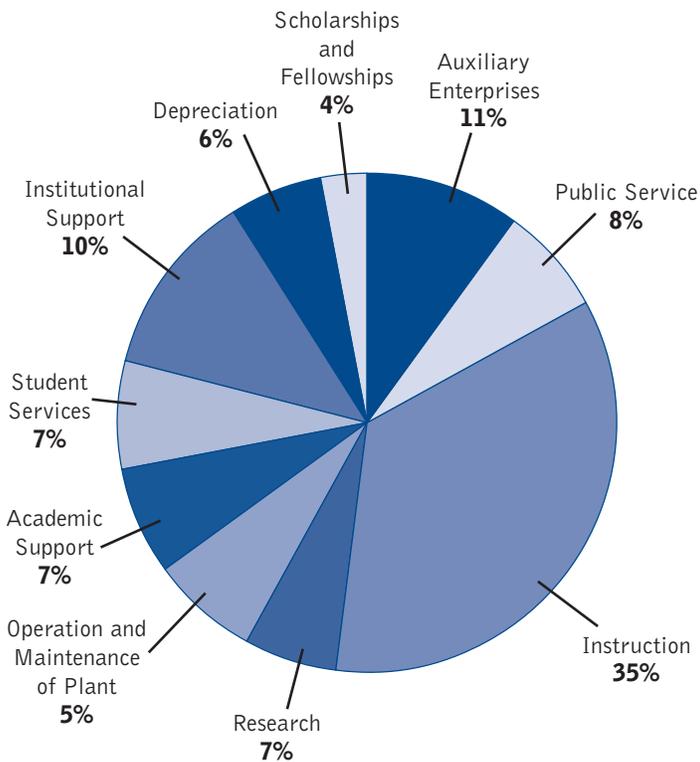
## Expenses - By natural classification

In addition to their functional (program) classification, it is also informative to review operating expenses by their natural (object) classification. A comparative summary of the University's expenses by natural classification for the years ended June 30, 2004 and June 30, 2003, is as follows:

	2004	2003
Operating:		
Personal services and benefits	\$ 173,520,202	\$ 169,118,948
Operations	71,931,360	68,105,233
Scholarships	11,934,017	8,862,509
Depreciation	16,069,536	17,467,988
Nonoperating:		
Interest and other	<u>5,780,915</u>	<u>5,540,139</u>
<b>Total Expenses</b>	<b><u>\$ 279,236,030</u></b>	<b><u>\$ 269,094,817</u></b>

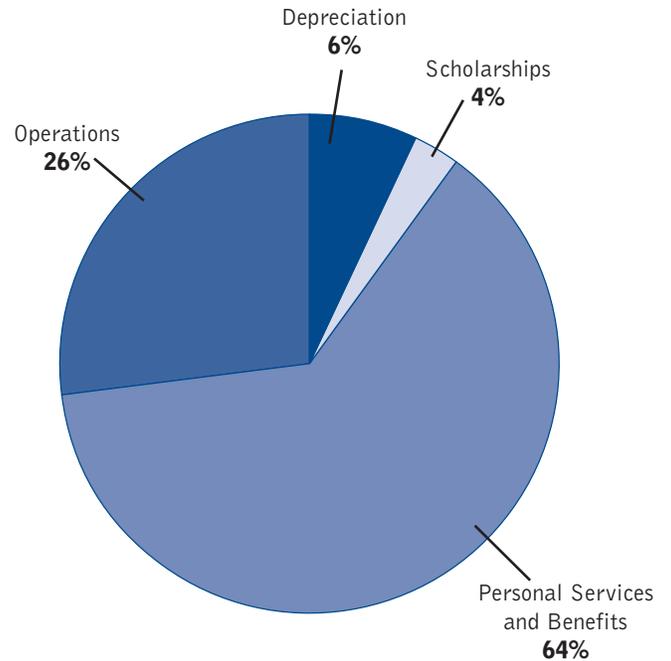
### Operating Expenses

Functional Classifications  
Fiscal Year 2004



### Operating Expenses

Natural Classifications  
Fiscal Year 2004



# MANAGEMENT'S DISCUSSION AND ANALYSIS

## CAPITAL ASSETS AND DEBT ADMINISTRATION

### Capital Assets at June 30, 2004

At June 30, 2004, the University had \$204.4 million invested in capital assets. During the year the University added \$26.8 million in new capital assets and retired \$6.4 million of obsolete assets. In addition, accumulated depreciation increased by \$10.5 million. Details of capital assets for the years ended June 30, 2004 and 2003, are as follows:

	2004	2003
Land	\$ 5,283,663	\$ 5,283,663
Infrastructure	40,998,869	39,687,569
Buildings	258,176,852	257,574,458
Equipment	75,886,469	76,602,924
Library books and media	44,463,722	43,436,044
Construction in progress	21,662,411	3,522,704
Accumulated depreciation	<u>(242,049,578)</u>	<u>(231,584,875)</u>
<b>Total capital assets</b>	<b><u>\$ 204,422,408</u></b>	<b><u>\$ 194,522,487</u></b>

**S**ignificant capital additions completed or commenced, and the resources that funded their acquisitions for fiscal year 2004, were:

- Library acquisitions, \$1,092,710, unrestricted net assets
- Communications Building renovation \$10,947,323, bond proceeds
- Campus infrastructure upgrades, \$2,979,677, unrestricted net assets and bond proceeds.
- Applied Research and Development Building, \$929,118, bond proceeds
- New College of Business Administration, \$1,965,919, bond proceeds

The University's Capital Improvement Plan, which is updated annually, provides for the issuance of approximately \$38.0 million in certificates of participation and \$15.0 million of bonds in fiscal year 2005. These monies will be used for the renovation of existing buildings and new building construction.

Projects planned to commence in fiscal year 2005 funded from fiscal years 2004 and 2005 COPS and system revenue bonds include:

- Campus infrastructure upgrades
- Completion of a new College of Business Administration building
- College of Engineering and Technology renovation
- Communications Building renovation completion
- Old College of Business stabilization project

Per A.R.S. § 15-1670, NAU will receive \$5.9 million in State appropriations annually for lease-purchase capital financing in fiscal years 2008-2031 to fund research infrastructure projects. The construction of the Applied Research and Development Building and the College of Engineering and Technology renovation are to be funded from this source.



# MANAGEMENT'S DISCUSSION AND ANALYSIS

## CAPITAL ASSETS AND DEBT ADMINISTRATION (continued)

### Outstanding Debt at June 30, 2004

At June 30, 2004, the University had \$125.1 million in outstanding bonds, long-term obligations, and capital leases, an increase of approximately \$20.7 million or 20 percent from fiscal year 2003. This is due to repayment of \$10.3 million of principal and fiscal year borrowings of \$31.0 million. The \$125.1 million is made up of \$122.7 million in bonds and \$2.4 million in long-term obligations and capital leases. During the year ended June 30, 2004, the University issued \$31.0 million in system revenue bonds, with an average interest rate of 4.6 percent, for various project renovations on the mountain campus. The table below summarizes the University's outstanding debt from fiscal years 2004 and 2003.

	2004	2003
System revenue and housing bonds	\$ 122,710,000	\$ 101,645,000
Long-term obligations and capital leases	<u>2,395,161</u>	<u>2,753,559</u>
Subtotal	<u>125,105,161</u>	<u>104,398,559</u>
Less deferred amount on refunding	(586,852)	(736,687)
Plus bond premium	<u>1,755,901</u>	<u></u>
Total	<u>\$ 126,274,210</u>	<u>\$ 103,661,872</u>

At June 30, 2004, the University maintained an A2 rating by Moody's Investors Service and an A+ rating from Standard and Poor's Rating Services. Effective in fiscal year 2003, the University was required by Arizona state law to calculate its debt capacity ratio based on the amount of debt service per fiscal year not to exceed 8 percent of projected total expenditures and mandatory transfers. At June 30, 2004, the projected ratio for the University's total debt service to projected expenditures and mandatory transfers was 4.70 percent and is well within the requirement of 8 percent. In July 2004, the University issued approximately \$38.0 million of lease certificates of participation (COPS). The COPS were issued for research infrastructure projects and fit comfortably into the University's debt capacity according to the latest debt study as submitted to the Arizona Board of Regents.

### Economic Outlook

As the nation and State of Arizona continue to recover from the economic downturn, Northern Arizona University continues to evaluate changes necessary to providing excellence in undergraduate education and offering graduate programs and research. University management continues to develop long and short term strategic plans to address this and other challenges to the financial health of the institution. At the same time, the Arizona Board of Regents and the three State universities are actively evaluating creative solutions to contain costs and generate new revenues in order to continue providing quality and affordable education.

Part of the strategic plan includes positioning the University for future expansion of externally sponsored research through capital improvements and additional facilities. The University plans to issue \$44.0 million dollars of new debt in Spring 2005 to fund research

infrastructure. Ongoing planned projects include new lab facilities and other campus research infrastructure improvements. At a time when other state legislatures were cutting appropriations and support to higher education, the Arizona State Legislature passed A.R.S. § 15-1670 in support of expanded research infrastructure needs for each of the three State universities. The legislature recognized the need for facilities to spur research activity and make an investment in the future of Northern Arizona University by providing needed long-term financing. The University has moved forward to create buildings that form the core of this new research infrastructure by starting the construction of the Applied Research and Development Building, College of Engineering and Technology renovation, and campus infrastructure upgrades.

With current trends in State appropriations continuing to decline, the University requested and received approval from the Arizona Board of Regents to increase tuition. Due to increased financial needs to attract and retain talented faculty and staff, it is the intention of management to continue these requests until the University reached the top of the bottom one third of the top fifty public institutions in tuitions costs.

Since the University is ultimately subject to the same economic variables that affect other financial entities, it is not possible to predict future outcomes. Management is well aware of the challenges ahead and is working diligently to continue to provide quality instruction, research and public service to the State of Arizona and the nation.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## COMBINED SOURCES AND USES OF FUNDS For the Year Ended June 30, 2004

### SOURCES

<b>State Appropriations</b> <b>38.0%</b>	<b>\$ 111,642,600</b>
Includes legislative appropriations from state of Arizona general revenue for current operations of the University, and \$205,300 for financial aid.	
<b>Tuition and Fees, Net of Scholarship Allowances</b> <b>24.1%</b>	<b>\$ 70,820,903</b>
Includes \$47,392,871 to support the operating budget, \$12,016,391 for summer sessions, \$34,655,926 for funding of local budgets, scholarships, and retirement of nonhousing bonded indebtedness, less \$23,244,255 for scholarship allowances.	
<b>Government Grants and Contracts</b> <b>17.8%</b>	<b>\$ 52,117,453</b>
Includes operating revenues of \$43,252,845 from federal grants and contracts, \$3,757,254 from state grants and contracts, and \$5,107,354 from local government grants and contracts.	
<b>Auxiliary Enterprises</b> <b>11.3%</b>	<b>\$ 33,348,992</b>
Operations of substantially self-supporting activities such as housing, bookstore, student unions, and intercollegiate athletics.	
<b>Share of State Sales Taxes</b> <b>3.3%</b>	<b>\$ 9,564,155</b>
University's share of state sales tax collections from Proposition 301.	
<b>Private Gifts, Grants, and Contracts</b> <b>2.4%</b>	<b>\$ 7,151,700</b>
Includes gifts, grants, and contracts for scholarships, endowments, and plant facility additions.	
<b>Other Sources</b> <b>2.4%</b>	<b>\$ 7,128,058</b>
Includes interest on loans receivable, commissions, internal services, commissions, conferences, facility user fees, additions to permanent endowments, capital grants and gifts, and other operating and nonoperating miscellaneous revenues.	
<b>Investment Income</b> <b>0.7%</b>	<b>\$ 2,085,221</b>
Earnings from short-term investments of funds not necessary for immediate operational expenses and long-term investment of endowment and bond-retirement sinking funds.	
<b>Total Sources</b>	<b><u>\$ 293,859,082</u></b>

Note: The Combined Sources and Uses of Funds is presented to highlight major financial data. The explanations provided are not intended to be all inclusive. This summary is presented to give an overview of total University financial operations. Operating and nonoperating funds are included. Sources and uses are allocated and controlled by budgets.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## COMBINED SOURCES AND USES OF FUNDS For the Year Ended June 30, 2004

### USES

#### **Instruction and Academic Support**

**41.2%** **\$ 115,260,084**

Instruction, totaling \$95,100,334, includes expenses of academic departments and other organizational units for undergraduate and graduate courses, and for occupational or technical instruction, including regular academic year, summer sessions, and continuing education. Academic support, totaling \$20,159,750, includes libraries, audio-visual services, and academic administration.

#### **Student Services and Institutional Support**

**16.5%** **\$ 46,122,203**

Student services, totaling \$19,129,780, includes areas such as admissions, registrar, minority services, counseling, placement, student aid administration, and health services. Institutional support, totaling \$26,992,423, includes executive management, financial operations, computing support, human resource services, security, and University relations.

#### **Research and Public Service**

**14.6%** **\$ 40,743,414**

Activities for which the primary objective is the discovery or application of knowledge that may be sponsored by external agencies or separately budgeted by organizational units within the University. Public service activities make available to the general public the benefits of the instructional or research activities and include local school consortiums and public broadcasting.

#### **Auxiliary Enterprises**

**10.6%** **\$ 29,587,505**

Expenses of organizational units that furnish services to students, faculty and staff, and the general public for a fee directly related to the cost of the service and are managed as essentially self-supporting activities.

#### **Depreciation**

**5.8%** **\$ 16,069,536**

Depreciation expense of capital assets over their useful lives.

#### **Operation and Maintenance of Plant**

**4.9%** **\$ 13,738,356**

Represents expenses for the operation and maintenance of plant, including administration, maintenance and custodial services, landscaping and grounds upkeep, minor repairs and renovation, utilities, and property insurance.

#### **Scholarships and Fellowships**

**4.3%** **\$ 11,934,017**

Scholarships and fellowships are awarded to students enrolled in formal coursework for which the students are not required to perform personal services or repay the awards.

#### **Other Uses**

**2.1%** **\$ 5,780,915**

Other uses include \$5,205,808 in interest expense on capital asset-related debt and a \$575,107 loss on disposal of capital assets.

#### **Total Uses**

**\$ 279,236,030**

# FINANCIAL STATEMENTS

## STATEMENT OF NET ASSETS June 30, 2004

### ASSETS

### Business-Type Activities

Current assets:	
Cash and cash equivalents	\$ 34,735,206
Investments	20,780,440
Receivables, net of allowance for uncollectibles:	
Accounts receivable	7,363,885
Accrued interest	629,958
Endowment - land sale	412,912
Government grants and contracts	7,901,090
Student loans	965,408
Other assets	510,765
Inventories	2,069,895
<b>Total current assets</b>	<u>\$ 75,369,559</u>
Noncurrent assets:	
Restricted cash and investments held by trustee	\$ 37,812,641
Student loans receivable, net of allowance	5,401,652
Endowment investments	10,668,193
Other noncurrent assets	180,880
Capital assets, not being depreciated	26,946,074
Depreciable capital assets, net of depreciation	177,476,334
<b>Total noncurrent assets</b>	<u>\$ 258,485,774</u>
<b>Total assets</b>	<u>\$ 333,855,333</u>

### LIABILITIES

Current liabilities:	
Accounts payable	\$ 5,945,844
Accrued payroll and employee benefits	5,582,448
Interest payable	491,090
Deferred revenue	7,820,130
Accrued compensated absences	3,792,479
Deposits held in custody for others	1,863,813
Current portion of long-term debt	10,300,777
<b>Total current liabilities</b>	<u>\$ 35,796,581</u>
Noncurrent liabilities:	
Deposits held in custody for others	\$ 230,056
Long-term debt	117,706,796
<b>Total noncurrent liabilities</b>	<u>\$ 117,936,852</u>
<b>Total liabilities</b>	<u>\$ 153,733,433</u>

### NET ASSETS

Invested in capital assets, net of related debt	\$ 114,347,814
Restricted:	
Nonexpendable:	
Scholarships and fellowships	7,163,293
Student loans	6,999,262
Expendable:	
Scholarships and fellowships	1,023,823
Research	5,227,312
Academic department use	7,271,305
Debt service	844,677
Unrestricted	37,244,414
<b>Total net assets</b>	<u>\$ 180,121,900</u>

See Notes to Financial Statements

# FINANCIAL STATEMENTS

## STATEMENT OF FINANCIAL POSITION - Component Units June 30, 2004

	NAU FOUNDATION	NACFFC	TOTAL
<b>ASSETS</b>			
Cash and cash equivalents	\$ 1,121,348	\$ 78,629	\$ 1,199,977
Investments	42,061,663		42,061,663
Accounts receivable	229,989	94,500	324,489
Unconditional promises to give (net of allowance)	2,256,226		2,256,226
Assets held by trustee	1,309,333	2,863,372	4,172,705
Property, plant and equipment, net of depreciation	3,038	12,544,289	12,547,327
Other assets	465,439	526,069	991,508
<b>Total assets</b>	<u>\$ 47,447,036</u>	<u>\$ 16,106,859</u>	<u>\$ 63,553,895</u>
<b>LIABILITIES</b>			
Accounts payable and accrued liabilities	\$ 405,336	\$ 687,513	\$ 1,092,849
Bonds payable		15,725,528	15,725,528
Assets held in custody	4,461,341		4,461,341
Other liabilities	443,888	165,629	609,517
<b>Total liabilities</b>	<u>\$ 5,310,565</u>	<u>\$ 16,578,670</u>	<u>\$ 21,889,235</u>
<b>NET ASSETS</b>			
Unrestricted (deficit)	\$ 5,532,962	\$ (471,811)	\$ 5,061,151
Temporarily restricted	12,656,357		12,656,357
Permanently restricted	23,947,152		23,947,152
<b>Total net assets (deficit)</b>	<u>\$ 42,136,471</u>	<u>\$ (471,811)</u>	<u>\$ 41,664,660</u>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<u>\$ 47,447,036</u>	<u>\$ 16,106,859</u>	<u>\$ 63,553,895</u>

See Notes to Financial Statements

# FINANCIAL STATEMENTS

## STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS For Year Ended June 30, 2004

### REVENUES

### Business-Type Activities

Operating Revenues	
Tuition and fees, net of scholarship allowances of \$23,244,255, pledged as security for revenue bonds	\$ 70,820,903
Government grants and contracts	51,750,883
Private grants and contracts	3,550,039
Auxiliary enterprises, includes revenues pledged as security for revenue bonds:	
Bookstore	8,960,632
Residence life, net of scholarship allowances of \$2,101,690	15,244,694
Other auxiliaries	9,143,666
Other	5,684,294
<b>Total operating revenues</b>	<u>\$ 165,155,111</u>

### EXPENSES

Operating Expenses	
Educational and general:	
Instruction	\$ 95,100,334
Research	18,824,650
Public service	21,918,764
Academic support	20,159,750
Student services	19,129,780
Institutional support	26,992,423
Operation and maintenance of plant	13,738,356
Scholarships and fellowships	11,934,017
Auxiliary enterprises	29,587,505
Depreciation	16,069,536
<b>Total operating expenses</b>	<u>\$ 273,455,115</u>

### Operating loss

\$ (108,300,004)

### NONOPERATING REVENUES AND (EXPENSES)

State appropriations	\$ 111,642,600
Share of state sales tax	9,564,155
Government grants and contracts	366,570
Private gifts, grants, and contracts	3,601,661
Investment income	2,085,221
Interest expense on capital asset related debt	(5,205,808)
Loss on disposal of capital assets	(575,107)
Other nonoperating revenues	654,830
<b>Total nonoperating revenues and expenses</b>	<u>\$ 122,134,122</u>

### Income before other revenues, expenses, gains or losses

\$ 13,834,118

Capital grants and gifts	\$ 235,047
Additions to permanent endowments	553,887

### Increase in net assets

\$ 14,623,052

### NET ASSETS

Total net assets, July 1, 2003	<u>\$ 165,498,848</u>
<b>Total net assets, June 30, 2004</b>	<u><u>\$ 180,121,900</u></u>

*See Notes to Financial Statements*

# FINANCIAL STATEMENTS

## STATEMENT OF ACTIVITIES - Component Units For Year Ended June 30, 2004

	NAU FOUNDATION	NACFFC	TOTAL
<b>CHANGES IN UNRESTRICTED NET ASSETS</b>			
Unrestricted support	\$ 488,203	\$	\$ 488,203
Investment earnings	3,836,880	69,768	3,906,648
Rent		1,625,876	1,625,876
Other	78,173	14,628	92,801
<b>Total unrestricted support</b>	<u>\$ 4,403,256</u>	<u>\$ 1,710,272</u>	<u>\$ 6,113,528</u>
Net assets released from restrictions	3,968,154		3,968,154
<b>Total unrestricted revenues and support</b>	<u>\$ 8,371,410</u>	<u>\$ 1,710,272</u>	<u>\$ 10,081,682</u>
Expenses and losses:			
Scholarships	\$ 985,533	\$	\$ 985,533
Operating	835,159	361,009	1,196,168
Interest		614,200	614,200
Educational purposes	2,901,616		2,901,616
Amortization and depreciation		453,418	453,418
Other		357,448	357,448
Unrealized loss on investment or impairment of assets	398,629		398,629
<b>Total expenses and losses</b>	<u>\$ 5,120,937</u>	<u>\$ 1,786,075</u>	<u>\$ 6,907,012</u>
<b>Increase (decrease) in unrestricted net assets</b>	<u>\$ 3,250,473</u>	<u>\$ (75,803)</u>	<u>\$ 3,174,670</u>
<b>CHANGES IN TEMPORARILY RESTRICTED NET ASSETS</b>			
Public contributions	\$ 3,811,473		\$ 3,811,473
Investment earnings	296,624		296,624
Other income changes	37,533		37,533
Net assets released from restrictions	(3,968,154)		(3,968,154)
Unrealized loss on investment or impairment of assets	(37,567)		(37,567)
<b>Increase in temporarily restricted assets</b>	<u>\$ 139,909</u>		<u>\$ 139,909</u>
<b>CHANGES IN PERMANENTLY RESTRICTED NET ASSETS</b>			
Public contributions	\$ 576,254		\$ 576,254
Investment earnings	411,459		411,459
Unrealized loss on investment or impairment of assets	(849)		(849)
<b>Increase in permanently restricted net assets</b>	<u>\$ 986,864</u>		<u>\$ 986,864</u>
<b>INCREASE (DECREASE) IN NET ASSETS</b>	<u>\$ 4,377,246</u>	<u>\$ (75,803)</u>	<u>\$ 4,301,443</u>
<b>NET ASSETS (DEFICIT), BEGINNING OF YEAR</b>	<u>\$ 37,759,225</u>	<u>\$ (396,008)</u>	<u>\$ 37,363,217</u>
<b>NET ASSETS (DEFICIT), END OF YEAR</b>	<u>\$ 42,136,471</u>	<u>\$ (471,811)</u>	<u>\$ 41,664,660</u>

See Notes to Financial Statements

# FINANCIAL STATEMENTS

## STATEMENT OF CASH FLOWS For Year Ended June 30, 2004

### Business-Type Activities

Cash flows from operating activities:	
Tuition and fees	\$ 66,034,058
Grants and contracts	55,375,303
Payments to suppliers and providers of goods and services	(73,279,424)
Payments to employees	(169,762,332)
Payments for scholarships and fellowships	(11,934,017)
Loans issued to students	(1,876,104)
Collection of loans to students	1,383,106
Auxiliary enterprise receipts:	
Residence halls	15,522,703
Bookstore	8,941,025
Other auxiliaries	6,681,789
Other receipts	7,252,524
<b>Net cash used by operating activities</b>	<u>\$ (95,661,369)</u>
Cash flows from noncapital financing activities:	
State appropriations	\$ 111,642,600
Share of state sales tax	9,463,599
Gifts and grants for other than capital purposes	5,072,983
Federal direct student lending received	68,710,133
Federal direct student lending disbursed	(68,710,133)
Private gifts for endowment purposes	553,887
Funds held for others	(240,600)
<b>Net cash provided by noncapital financing activities</b>	<u>\$ 126,492,469</u>
Cash flows from capital financing activities:	
Proceeds from issuance of capital debt	\$ 32,351,001
Capital grants and gifts received	173,593
Proceeds from sale of capital assets	112,637
Purchases of capital assets	(26,595,747)
Principal paid on capital debt and leases	(10,293,398)
Interest paid on capital debt and leases	(4,943,010)
<b>Net cash used by capital financing activities</b>	<u>\$ (9,194,924)</u>
Cash flows from investing activities:	
Proceeds from sales and maturities of investments	\$ 36,503,855
Interest on investments	2,015,670
Purchase of investments	(36,934,619)
<b>Net cash provided by investing activities</b>	<u>\$ 1,584,906</u>
Net increase in cash and cash equivalents	\$ 23,221,082
Cash and cash equivalents - beginning of year	49,326,765
Cash and cash equivalents - end of year	<u>\$ 72,547,847</u>
Reconciliation of operating loss to net cash used by operating activities:	
Operating loss	\$ (108,300,004)
Adjustments to reconcile operating loss to net cash used by operating activities:	
Depreciation expense	16,069,536
Changes in assets and liabilities - cash increase (decrease) related to:	
Receivables:	
Accounts receivable	(2,605,577)
Government grants and contracts	232,500
Student loans receivables and accrued interest from student loans	(527,890)
Inventories	7,061
Other assets	1,247,728
Accounts payable	(1,355,125)
Accrued payroll and employee benefits	1,456,724
Deferred revenue	(3,190,745)
Deposits held in custody for others	1,341,025
Accrued compensated absences	(36,602)
<b>Net cash used by operating activities:</b>	<u>\$ (95,661,369)</u>
Noncash transactions	
Gifts of capital assets	\$ 176,914
Unrealized change in fair value of investments	355,699
Amortization of deferred amount on bond refunding and bond premium	104,812
Losses on disposal of capital assets	(575,107)

See Notes to Financial Statements

# NOTES TO FINANCIAL STATEMENTS

June 30, 2004

## Note 1—Summary of Significant Accounting Policies

### Financial Statement Presentation

The accounting policies of the University conform to U.S. generally accepted accounting principles applicable to public institutions of higher education engaged only in business-type activities adopted by the Governmental Accounting Standards Board (GASB).

During the year ended June 30, 2004, the University implemented the provisions of the Governmental Accounting Standards Board Statement No. 39, *Determining Whether Certain Organizations Are Component Units*, which requires reporting as a component unit those organizations that raise and hold economic resources for the direct benefit of the University or its constituents.

### Reporting Entity

The financial statements of the University include all monies, financial transactions, and activities for which the University has financial accountability. Fiscal responsibility for the University remains with the State of Arizona; therefore, the University is considered part of the reporting entity of the State for financial reporting purposes. The accompanying financial statements present the activities of the University and its discretely presented component units, the Northern Arizona University Foundation, Inc. (Foundation) and the Northern Arizona Capital Facilities Finance Corporation (NACFFC).

The Foundation was incorporated as a legally separate not-for-profit corporation in the State of Arizona in January 1959 and operates exclusively for the benefit of Northern Arizona University. The Foundation receives gifts and bequests, administers and invests securities and property, and disburses payments to and on behalf of the University for advancement of its mission.

NACFFC was incorporated in October 2001, as a legally separate nonprofit corporation under the laws of the State of Arizona for the purpose of acquiring, developing, constructing, maintaining and operating student housing and other capital facilities and equipment for the use and benefit of the University's students.

Although the University does not control the timing or amount of receipts from the Foundation, or the NACFFC, the restricted resources of both the Foundation, and the NACFFC, can only be used by, or for the benefit of the University or its constituents. Consequently, both the Foundation and the NACFFC are considered component units of the University and are discretely presented in the University's financial statements. For financial reporting purposes only the statement of financial position and the statement of activities of the component units are included in the University's financial statements as required by generally accepted accounting principles for public colleges and universities.

For financial reporting purposes, the Foundation and the NACFFC follow the Financial Accounting Standards Board statements for not-for-profit organizations. As such, certain revenue recognition criteria and presentation features are different from GASB revenue recognition criteria and presentation features. Accordingly, those financial

statements have been reported on separate pages following the respective counterpart statements of the University. The Foundation and the NACFFC have a June 30 year end. Complete financial statements as originally presented for the Foundation and the NACFFC can be obtained from the Northern Arizona University Comptroller's Office, P.O. Box 4069, Flagstaff, AZ 86011.

### Basis of Accounting

For financial reporting purposes, the University is considered a special purpose government engaged only in business-type activities. Accordingly, the University's financial statements have been presented using the economic resources 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. State appropriations are recognized as revenue in the year in which the appropriation is first made available for use. Grants and donations are recognized as revenue as soon as all eligibility requirements imposed by the provider are met. All significant transactions resulting from internal activity have been eliminated.

The University follows Financial Accounting Standards Board (FASB) Statements and Interpretations issued on or before November 30, 1989; Accounting Principles Board Opinions; and Accounting Research Bulletins, unless those pronouncements conflict with GASB pronouncements. The University has chosen the option not to follow FASB Statements and Interpretations issued after November 30, 1989.

The financial statements include a statement of net assets; a statement of revenues, expenses, and changes in net assets; and a statement of cash flows.

The statement of net assets provides information about the assets, liabilities, and net assets of the University at the end of the year. Assets and liabilities are classified as either current or noncurrent. Net assets are classified according to external donor restrictions or availability of assets to satisfy University obligations. Invested in capital assets net of related debt, represents the value of capital assets, net of accumulated depreciation, less any outstanding debt incurred to acquire or construct the assets. Nonexpendable restricted net assets are gifts that have been received for endowment purposes, the corpus of which cannot be expended and monies that are restricted for the purpose of issuing student loans. Expendable restricted net assets represent grants, contracts, gifts, and other resources that have been externally restricted for specific purposes. Unrestricted net assets include all other net assets, including those that have been designated by management to be used for other than general operating purposes.

The statement of revenues, expenses, and changes in net assets provides information about the University's financial activities during the year. Revenues and expenses are classified as either operating or nonoperating, and all changes in net assets are reported, including capital contributions and additions to endowments. Generally, revenues generated by the University for instruction, public service, and research are considered to be operating revenues. Other revenues used for instruction and public service, such as state appropriations, are not generated from operations and are considered to be nonoperating

# NOTES TO FINANCIAL STATEMENTS

June 30, 2004

revenues. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. Other expenses, such as interest expense on debt, are considered to be nonoperating expenses.

The statement of cash flows provides information about the University's sources and uses of cash and cash equivalents during the year. Increases and decreases in cash and cash equivalents are classified as operating, noncapital financing, capital financing, or investing activities.

The University has both restricted and unrestricted resources available for its operations. Generally, the use of these resources is managed at the department level. Restricted resources are primarily externally provided sponsored research grants and contracts, and externally provided student financial aid. When both restricted and unrestricted resources are available for use, typically restricted resources will be used first. University policy is that the funding source to be used is determined by each department based on (1) relative priorities of the department in accordance with University strategic initiatives, (2) externally imposed matching requirements of the restricted grants and contracts, and (3) any pertinent lapsing provisions of the restricted or unrestricted funding resources available for the expense.

## Cash and Cash Equivalents

The University considers all short-term, highly liquid investments with maturities of less than three months from the date of acquisition to be cash equivalents. Cash and investments held by trustee, and funds invested through the State Treasurer's Local Government Investment Pool, are also considered cash equivalents.

## Investments

Investments are reported at fair value. Fair value typically is the quoted market price for investments.

## Receivables

Student loans and accounts receivable as of June 30, 2004, are reported less allowances for both estimated uncollectible amounts and collection costs of \$829,500 and \$1,057,000, respectively.

## Inventories

Inventories are stated at the lower of cost or market. The cost of bookstore inventories is determined by the retail inventory method. The cost of other inventories is determined generally using the first-in, first-out or weighted average cost methods.

## Special Collections

The University does not capitalize its special collections because the items are held for educational and research purposes and not for financial gain. The items are preserved, unencumbered, and protected. It is the University's policy to acquire other items to further or enhance collections with any proceeds from the disposal of special collection items.

## Compensated Absences

Compensated absences consist of vacation leave and compensatory time earned by employees based on services already rendered. Employees may accumulate up to 264 hours of vacation depending on years of service and full-time equivalent employment status, but any vacation hours in excess of the maximum amount that are unused at December 31 are forfeited. Upon termination of employment, all unused vacation benefits not exceeding 176 hours (annual accrual amount), depending on years of service and full-time equivalent employment status, are paid to employees. Accordingly, vacation benefits and compensatory time are accrued as a liability in the financial statements.

Generally, sick leave benefits provide for ordinary sick pay and are cumulative but are forfeited upon termination of employment. Because sick leave benefits do not vest with employees, a liability for sick leave benefits is not accrued in the financial statements. However, upon retirement, employees who have accumulated at least 500 hours of sick leave are paid a formulated benefit amount. The University makes contributions each pay period to the State's Retiree Accumulated Sick Leave Fund and the State makes benefit payments directly to the retired employees from the fund. Consequently, the University has not accrued a liability for these sick leave benefits.

## Investment Income

Investment income is composed of interest, dividends, and net changes in fair value of applicable investments.

## Capital Assets

Capital assets are reported at actual cost. Donated assets are reported at estimated fair value at the time received. Capitalization thresholds, depreciation methods, and estimated useful lives of capital assets reported in the financial statements are as follows:

	Capitalization Threshold	Depreciation Method	Estimated Useful Life
Building improvements	\$5,000	Straight Line	20 years
Buildings	All	Straight Line	40 years
Infrastructure	All	Straight Line	20-40 years
Land	All	None	
Equipment	2,500	Straight Line	5-15 years
Library books and media	All	Straight Line	10 years

# NOTES TO FINANCIAL STATEMENTS

June 30, 2004

## Scholarship Allowances

Student tuition and fee revenues, and certain other revenues from students, are reported net of scholarship discounts and allowances in the statement of revenues, expenses, and changes in net assets. A scholarship discount and allowance is the difference between the stated charge for goods and services provided by the University and the amount that is paid by students or third parties making payments on behalf of the student.

Accordingly, some types of student financial aid such as Pell grants and scholarships awarded by the University are considered to be scholarship allowances. These allowances are netted against tuition and fees and certain auxiliary enterprise revenues in the statement of revenues, expenses, and changes in net assets.

## Note 2—Cash and Investments

Board of Regent's investment policies require that the University invest only in the State Treasurer's Local Government Investment Pool, collateralized time certificates of deposit and repurchase agreements, U.S. Treasury securities, and obligations of other agencies sponsored by the federal government. Gifts and endowments monies may be invested according to conditions stipulated by the donor, but if no conditions are imposed, such monies may be invested under the direction of the University investment committee in such a manner as to obtain the most favorable rate of return and income stability commensurate with safety of principal. Demand deposit accounts with authorized financial institutions are required to be collateralized.

**Cash and Investments** at June 30, 2004, consists of the following:

	<b>Fair Value</b>
Cash on hand and in bank	\$ (1,725,519)
Investments	22,005,491
Student Financial Aid Trust Fund	6,828,434
State Treasurer's Local Government Investment Pool	34,977,763
Bond Trustee Funds	37,812,641
Investments with NAU Foundation	4,097,670
<b>Total</b>	<b>\$ 103,996,480</b>

The University's total cash on hand was \$51,445. The carrying amount of the University's total cash in bank was (\$1,776,964) and the bank balance was \$1,978,744, of which \$100,000 was covered by federal depository insurance and the remaining balance of \$1,878,744 was collateralized by U.S. Government obligations held by the counterparty's agent in the agent's account with the Federal Reserve in the University's name.

The \$22,005,491 in investments is invested in securities of the Federal Home Loan Mortgage Corporation, the Federal Home Loan Bank, and the Federal National Mortgage Association that are registered and held

by the counterparty's agent in the agent's account with the Federal Reserve Bank. The University's ownership interest is recorded in the bank's records.

The Student Financial Aid Trust Fund was established in accordance with Arizona Revised Statutes §15-1642 for the purpose of providing aid to students with verifiable financial need. The three state universities participate in the Trust Fund, which is held with and managed by the University of Arizona. The University's portion is not identified with specific investments and is not subject to custodial credit risk. The University's ownership interest is recorded in the University of Arizona's records.

The University's investment in the State Treasurer's Local Government Investment Pool represents a proportionate interest in the pool's portfolio; however, the University's portion is not identified with specific investments and is not subject to custodial credit risk. The State Board of Investment provides oversight for the State Treasurer's pools, and the Local Government Investment Pool Advisory Committee provides consultation and advice to the Treasurer. The fair value of a participant's position in the pool approximates the value of that participant's pool shares.

Bond indentures authorize the bond trustees to invest in obligations of or guaranteed by the federal government or any agency or instrumentality thereof; municipal obligations; collateralized certificates of deposit with federally insured banks, trust companies, or savings and loan associations within the State of Arizona; or repurchase agreements. At June 30, 2004, the bond trustee funds, of \$37,292,984 held for future construction projects and \$519,657 held to meet debt service requirements, were invested in money market mutual funds that primarily consist of U.S. government securities. The bond trustees are authorized to purchase and sell securities. The University's ownership interest is recorded in the trustee's records.

Trust agreements between the University and the NAU Foundation, Inc., authorize the Foundation to invest certain University restricted and endowment monies according to the Foundation's established investment policies and procedures. At June 30, 2004, the Foundation invested the amount of \$4,097,670 with selected financial institutions. The University's portion is not identified with specific investments and is not subject to custodial credit risk. The University's ownership interest is recorded in the Foundation's records.



# NOTES TO FINANCIAL STATEMENTS

June 30, 2004

## Note 3—Capital Assets

Capital asset activity for the year ended June 30, 2004, was as follows:

	Balance June 30, 2003	Additions	Retirements	Transfers	Balance June 30, 2004
Capital assets not being depreciated:					
Land	\$ 5,283,663				\$ 5,283,663
Construction in progress	3,522,704	\$ 19,295,078		\$ (1,155,371)	21,662,411
Total capital assets not being depreciated	<u>8,806,367</u>	<u>19,295,078</u>		<u>(1,155,371)</u>	<u>26,946,074</u>
Capital assets being depreciated:					
Infrastructure	39,687,569	1,247,378		63,922	40,998,869
Buildings	257,574,458	882,487	\$ (1,371,542)	1,091,449	258,176,852
Equipment	76,602,924	4,255,008	(4,971,463)		75,886,469
Library books and media	43,436,044	1,092,710	(65,032)		44,463,722
Total capital assets being depreciated	<u>417,300,995</u>	<u>7,477,583</u>	<u>(6,408,037)</u>	<u>1,155,371</u>	<u>419,525,912</u>
Less accumulated depreciation for					
Infrastructure	17,831,653	1,211,336			19,042,989
Buildings	122,288,550	6,769,689	(911,105)		128,147,134
Equipment	57,434,027	5,970,632	(4,628,696)		58,775,963
Library books and media	34,030,645	2,117,879	(65,032)		36,083,492
Total accumulated depreciation	<u>231,584,875</u>	<u>16,069,536</u>	<u>(5,604,833)</u>		<u>242,049,578</u>
Total capital assets being depreciated, net	<u>185,716,120</u>	<u>(8,591,953)</u>	<u>(803,204)</u>	<u>1,155,371</u>	<u>177,476,334</u>
Capital assets, net	<u>\$194,522,487</u>	<u>\$ 10,703,125</u>	<u>\$ (803,204)</u>		<u>\$ 204,422,408</u>

The estimated cost to complete construction in progress at June 30, 2004, totaled \$52,801,400.

## Note 4—Long-Term Liabilities

Long-term liability activity for the year June 30, 2004, was as follows:

	Balance June 30, 2003	Additions	Reductions	Balance June 30, 2004	Due Within One Year
Long-term obligations and capital leases	\$ 2,753,559		\$ (358,398)	\$ 2,395,161	\$ 376,366
Revenue and housing bonds payable	101,645,000	\$ 31,000,000	(9,935,000)	122,710,000	9,520,000
Less deferred amount on refunding	(736,687)		149,835	(586,852)	(149,834)
Bonds premium		1,800,924	(45,023)	1,755,901	60,031
Optional retirement monies	1,973,964	717,886	(958,487)	1,733,363	494,214
Total long-term liabilities	<u>\$105,635,836</u>	<u>\$ 33,518,810</u>	<u>\$(11,147,073)</u>	<u>\$128,007,573</u>	<u>\$ 10,300,777</u>

# NOTES TO FINANCIAL STATEMENTS

June 30, 2004

**Bonds** - The University's bonded debt consists of various issues of student housing and system revenue bonds that are generally callable with interest payable semiannually. Bond proceeds primarily pay for acquiring, constructing or renovating of capital facilities. System revenue bonds are repaid from pledged gross revenues that primarily consist of student tuition and fees, and certain auxiliary revenues.

Bonds payable at June 30, 2004, are as follows:

Student housing bonds (2 issues) - 5.5 percent to 6.1 percent, principal payable annually on April 1 through 2009, revenues of various housing projects pledged for payment	\$ 850,000
System revenue bonds, Series of 1997 - 5.0 percent to 6.5 percent, principal maturing serially on June 1, 2009, through 2017, secured by a first lien on certain gross revenues, on a parity with the Series 2002 system revenue refunding bonds and the Series 2002 system revenue bonds	\$ 30,900,000
System revenue refunding bonds, Series of 2002 - 3.0 percent to 4.0 percent, principal maturing serially on June 1, 2003, through 2008, secured by a first lien on certain gross revenues, on a parity with the Series 1997 system revenue bonds and the Series 2002 system revenue bonds	\$ 32,895,000
System revenue bonds, Series of 2002 - 3.0 percent to 5.125 percent, principal maturing serially on June 1, 2003, through 2034, secured by a first lien on certain gross revenues, on a parity with the Series 1997 system revenue bonds and the Series 2002 system revenue refunding bonds	\$ 27,065,000
System revenue bonds, Series of 2003 - 2.5 percent to 5.5 percent, principal maturing serially on June 1, 2005, through 2034, secured by a first lien on certain gross revenues, on a parity with the Series 1997 system revenue bonds, the Series 2002 system revenue refunding bonds, and the Series 2002 system revenue bonds	\$ 31,000,000
	<u>\$ 122,710,000</u>

**The following schedule details debt service requirements to maturity for the University's bonds payable at June 30, 2004.**

Year Ending June 30,	Revenue Bonds	
	Principal	Interest
2005	\$ 9,520,000	\$ 5,775,045
2006	9,850,000	5,416,345
2007	9,680,000	5,039,095
2008	8,835,000	4,669,130
2009	3,975,000	4,328,245
2010-14	22,390,000	18,388,640
2015-19	19,635,000	12,634,387
2020-2024	9,800,000	9,248,757
2025-2029	12,660,000	6,386,850
2030-2034	16,365,000	2,678,800
<b>Total</b>	<u>\$ 122,710,000</u>	<u>\$ 74,565,294</u>

In prior years, the University defeased certain revenue bonds by either placing the proceeds of new bonds, or cash and investments accumulated in a sinking fund, in an irrevocable trust to provide for all future debt service payments on the refunded bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the University's financial statements. At June 30, 2004, \$270,000 of such bonds outstanding are considered defeased.

# NOTES TO FINANCIAL STATEMENTS

June 30, 2004

## Note 5—Retirement Plans

The University participates in one cost-sharing multiple-employer defined benefit pension plan and five defined contribution pension plans.

The Arizona State Retirement System (ASRS) administers a cost-sharing multiple-employer defined benefit pension plan. Benefits are established by state statute and provide retirement, death, long-term disability, survivor, and health insurance premium benefits. The ASRS is governed by the Arizona State Retirement System Board, in accordance with the provisions of A.R.S. Title 38, Chapter 5, Article 2. The ASRS issues a Comprehensive Annual Financial Report that includes its financial statements and required supplementary information. That report may be obtained by writing to the ASRS, 3300 North Central Avenue, P.O. Box 33910, Phoenix, Arizona 85067-3910, or calling (602) 240-2000 or (800) 621-3778.

For the year ended June 30, 2004, active ASRS members and the University were each required by statute to contribute at the actuarially determined rate of 5.70 percent (5.20 percent retirement and 0.50 percent long-term disability) of the members' annual covered payroll. The University's retirement contributions to the ASRS for the years ended June 30, 2004, 2003, and 2002 were \$2,822,407, \$1,148,814 and \$1,094,343, respectively, which were equal to the required contributions for the year. The Arizona State Legislature establishes and may amend active plan members' and the University's contribution rates.

In accordance with A.R.S. § 15-1628, University faculty, academic professionals, and administrative officers have the option to participate in defined contribution pension plans. These plans are administered by independent insurance and annuity companies approved by the Arizona Board of Regents. For the year ended June 30, 2004, plans offered by the Teachers Insurance Annuity Association/College Retirement Equities Fund (TIAA/CREF), Variable Annuity Life Insurance Company (VALIC), Fidelity Investments Tax-Exempt Service Company (Fidelity), Aetna Life Insurance and Annuity Company (Aetna), and Vanguard Group (Vanguard) were approved by the board. Benefits under these plans depend solely on the contributed amounts and the returns earned on investments of those contributions.



Contributions made by members vest immediately, and University contributions vest after five years of benefit eligible employment. The distribution of member contributions and associated investment earnings are made in accordance with the member's contract with the applicable insurance and annuity company. University contributions and associated investment earnings must be distributed to the member in the form of an annuity paid over a period that is not less than the member's life. The Arizona State Legislature establishes and may amend active plan members' and the University's contribution rates. For the year ended June 30, 2004, plan members and the University were each required by statute to contribute an amount equal to 7 percent of a member's compensation.

## Note 6—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. The University participates in a self-insurance program administered by the State of Arizona, Department of Administration, Risk Management Section. Arizona Revised Statutes §41-621 *et seq* provides that losses eligible for coverage and not covered by insurance will be paid by the State from the self-insurance program or by a future appropriation from the State Legislature. Loss risks not covered by Risk Management and where the University has no insurance coverage, are losses that arise from contractual breaches and are directly attributable to an act or omission, and determined to be a felony by a court of law. With this exception, the University has no significant risk of loss beyond

adjustments to future years' premium payments to the State's self-insurance program. All estimated losses for unsettled claims and actions of the State are determined on an actuarial basis and are included in the State of Arizona Comprehensive Annual Financial Report.

## Contributions to Retirement Plans

for the year ended June 30, 2004, are summarized below.

Plan	University Contributions	Member Contributions	Total Contributions
TIAA/CREF	\$ 2,607,045	\$ 2,607,045	\$ 5,214,090
VALIC	\$ 541,843	\$ 541,843	\$ 1,083,686
Fidelity	\$ 566,306	\$ 566,306	\$ 1,132,612
Aetna	\$ 155,181	\$ 155,181	\$ 310,362
Vanguard	\$ 185,936	\$ 185,936	\$ 371,872

# NOTES TO FINANCIAL STATEMENTS

June 30, 2004

## Note 7—Expense Classification

The University's operating expenses by natural and functional classification are summarized in the table below:

### For the Year Ended June 30, 2004 • Natural Classification

Functional Classification:	Personal Service and Benefits	Operations	Scholarships	Depreciation	Total
Instruction	\$ 82,194,831	\$ 12,905,503			\$ 95,100,334
Research	14,128,971	4,695,679			18,824,650
Public service	9,611,279	12,307,485			21,918,764
Academic support	15,532,597	4,627,153			20,159,750
Student services	14,498,677	4,631,103			19,129,780
Institutional support	19,689,862	7,302,561			26,992,423
Operation and maintenance of plant	6,798,471	6,939,885			13,738,356
Scholarships and fellowships			\$11,934,017		11,934,017
Auxiliary enterprises	11,065,514	18,521,991			29,587,505
Depreciation				\$ 16,069,536	16,069,536
<b>Total</b>	<b>\$ 173,520,202</b>	<b>\$ 71,931,360</b>	<b>\$11,934,017</b>	<b>\$ 16,069,536</b>	<b>\$ 273,455,115</b>

## Note 8—Other Matters

### Subsequent Events

In July 2004 the University issued approximately \$38.0 million of certificates of participation (COPS) for various capital projects and renovations on the main campus. The University will be issuing approximately \$39.7 million of system revenue bonds and system revenue refunding bonds in December 2004. The University will use \$15.0 million of the bonds for various capital projects and renovations on the main campus. The remaining \$24.7 million will be used to refund the Series 1997 system revenue bonds. These bonds are secured by a first lien on certain gross revenues and are on parity with the Series 2002 system revenue, the Series 2002 system revenue refunding bonds, and the Series 2003 system revenue bonds.

### Tuition Lawsuit

In August 2003, four University of Arizona students filed a lawsuit against the Arizona Board of Regents and the State of Arizona in Pima County (Arizona) Superior Court. The complaint alleged that the tuition increase approved by the Board for the 2003-04 academic year violates the State's constitution. The plaintiff's requested that the suit be certified as a class action on behalf of all students at the three universities governed by the Board. The complaint also asserted that the State has not provided funding to the three universities governed by the Board at the level required by the state constitution. The complaint sought (i) a declaratory judgement that the actions of each of the defendants violate the state constitution, (ii) preliminary and permanent injunctive relief to prevent the Board from imposing the tuition increase, and to compel repayment of any amounts already collected, and (iii) preliminary and injunctive relief ordering the State to set in place a plan to provide increased funding for maintenance, operation, and improvement of the State's universities. In March 2004,

the Superior Court granted the Board's and the State's motion to dismiss the case. In the related minute entry, the court held that in the exercise of its legislative and administrative function, which includes setting tuition levels for the State's three universities, the Board is absolutely immune from suit and that the conduct of the business of the State legislature is absolutely immune from suit. The plaintiffs have filed a notice of appeal with the Arizona Court of Appeals. The Board intends to vigorously defend the appeal. However, neither the Board or the University is able to predict at the present time whether the lawsuit will proceed or what the ultimate outcome of the matter will be or whether or to what extent it might impact the Board's ability to impose and collect tuition increases or otherwise affect the financial condition of the University.



# NOTES TO FINANCIAL STATEMENTS

June 30, 2004

## Note 9—Discretely Presented Component Units Disclosures

### A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of Northern Arizona University Foundation, Inc. (Foundation) and the Northern Arizona Capital Facilities Finance Corporation (NACFFC) have been prepared on the accrual basis.

#### Financial Statement Presentation

Both the Foundation and the NACFFC follow the Statement of Financial Accounting Standards Board (FASB) No. 117, "Financial Statements of Not-for-Profit Organizations." Under FASB Statement No. 117, the Foundation and the NACFFC are required to report information regarding their financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

- Unrestricted net assets – include assets and contributions that are not restricted by donors or for which such restrictions have expired.
- Temporarily restricted net assets – include contributions for which donor imposed restrictions have not been met (either by the passage of time or by actions of the Foundation), charitable remainder unitrusts, pooled income funds, gift annuities, and pledges receivable for which the ultimate purpose of the proceeds is not permanently restricted. Donor-restricted contributions are classified as temporarily restricted if restrictions are satisfied in the same reporting period in which the contributions are received.
- Permanently restricted net assets – include contributions, charitable remainder unitrusts, pooled income funds, gift annuities, and pledges receivable which require by donor restriction that the corpus be invested in perpetuity and only the board-approved payout be made available for program operations in accordance with donor restrictions.

#### Cash and Cash Equivalents

Highly liquid investments with an original maturity of three months or less are classified as cash equivalents and are stated at fair value.

#### Investments

The Foundation - Investments, consisting primarily of equity securities, U.S. government securities, and corporate bonds, with readily determinable market values are measured at fair value as of year-end. Donated investments are recorded at their fair values, as determined on the date of donation. Investment income or loss (including realized gains and losses on investments, interest and dividends) and unrealized gains, and losses on investments are recognized in the statement of activities. For management efficiency, investments of the unrestricted and restricted net assets are pooled, except for certain net assets that the board of directors or the donors have designated to be segregated and maintained separately.

#### Revenue Recognition

The Foundation - Contributions, including unconditional promises to give, are recognized as revenues in the period received. Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value. Contributions to be received after one year are discounted at rates commensurate with the risks involved.

Amortization of discount is recorded as additional contribution revenue in accordance with donor-imposed restrictions, if any, on the contributions. An allowance for uncollectible contributions receivable is provided based upon management's judgment including such factors as prior collection history.

Contributions received for prospective endowments that have not yet met the minimum requirements for acceptance as an endowment are accumulated in temporarily restricted accounts. The accumulated contributions are transferred to permanently restricted endowment accounts when the minimum requirements are fulfilled.

The NACFFC recognizes rental income as rent becomes due. Rental payments received in advance will be deferred until earned.

#### Property, Plant and Equipment

Property, plant, and equipment are recorded at cost or fair value at the date of donation. Replacements, maintenance and repairs that do not improve or extend the lives of the assets are expensed during the period incurred. Assets are depreciated on a straight-line basis over the estimated useful lives of the assets as follows:

Buildings and improvements	36 years
Furniture and equipment	5-10 years

#### Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

#### Tax Status

The Foundation is a public foundation and is exempt from Federal and State income taxes under Section 501 (c) (3) of the Internal Revenue Code. Accordingly, no provision for Federal or State taxes has been made. Continued tax-exempt status is contingent on future operations being in compliance with the Internal Revenue Code.

The NACFFC is exempt from taxes under the provisions of Section 501(c)(4) of the Internal Revenue Code.

# NOTES TO FINANCIAL STATEMENTS

June 30, 2004

## B. ASSETS HELD BY TRUSTEE

The Foundation has an irrevocable right to receive income earned from the trusts' assets held in perpetuity. The Foundation will never receive the trusts' assets. The trust agreements are administered and related assets are invested by an individual or organization other than the Foundation. Initial recognition and subsequent adjustments to the assets carrying value are recognized as public contributions and changes in value of perpetual trusts, respectively, and are classified as permanently restricted. Income earned is reported as increases in unrestricted, temporarily or permanently restricted net assets depending on the nature of the restrictions of each trust.

The NACFFC has various reserve and operating accounts required by the Indenture. These assets are invested in 100% treasury money market funds. The Corporation, through the Trustee, has invested the balance in the debt service reserve account in a guaranteed investment contract provided by Wachovia Bank, N.A. The debt service reserve account earns interest at a guaranteed rate of 5.4%, payable semi-annually.

## C. INVESTMENTS

The cost and fair value of the Foundation's investments at June 30, 2004 is as follows:

	Fair Value	Cost
U.S. Government/agency bonds	\$ 9,537,912	\$ 9,654,294
Corporate bonds	5,969,999	5,809,238
Common stock	22,535,869	20,330,543
International equity funds	3,973,832	3,901,895
Real estate investment trust	<u>44,051</u>	<u>40,682</u>
	<u>\$ 42,061,663</u>	<u>\$ 39,736,652</u>

Investments include funds held for the custody of others of \$4,252,247 at June 30, 2004.

The realized gains and unrealized losses on investments were \$3,406,455 (reported in Investment earnings) and \$(398,512) (reported in Unrealized loss on investment or impairment of assets) for the year ended June 30, 2004. Investment expenses of \$124,362 for the year ended June 30, 2004 have been netted against investment earnings in the statement of activities.

## D. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are comprised of buildings, improvements, furniture and equipment and are reported net of accumulated depreciation. Balances as of June 30, 2004 are presented as follows:

### FOUNDATION

	Cost or Donated Value	Accumulated Depreciation	Net Assets
Furniture and equipment	<u>\$ 13,280</u>	<u>\$ (10,242)</u>	<u>\$ 3,038</u>

### NACFFC

	Cost or Donated Value	Accumulated Depreciation	Net Assets
Buildings and improvements	\$ 12,513,415	\$ (667,051)	\$ 11,846,364
Furniture and equipment	<u>864,402</u>	<u>(166,477)</u>	<u>697,925</u>
Total	<u>\$ 13,377,817</u>	<u>\$ (833,528)</u>	<u>\$ 12,544,289</u>

# NOTES TO FINANCIAL STATEMENTS

June 30, 2004

## E. GROUND LEASE

In a prior year, the University entered into a privatized agreement with the NACFFC to build on-campus student housing. The student housing project is built on University property that is leased to the NACFFC.

Pursuant to the Lease, NACFFC, as lessee, paid a base rent in the amount of \$1,000 for the entire term of the Lease and is required to pay percentage rent annually equal to 100% of the net cash flows, as defined in the Lease. Pursuant to the Lease, NACFFC is required to hold and operate the Student Housing Project, during the term of the Lease solely for the benefit of the University. All facilities and equipment become the property of the University upon the expiration of the Lease.



## F. BONDS PAYABLE

The NACFFC had the following bonds outstanding at June 30, 2004:

Tax-exempt Series 2001 serial bonds, in the original amount of \$150,000 dated October 31, 2001 due August 1, 2004

\$ 153,327

Tax-exempt Series 2001 term bonds, in the original amount of \$15,205,000 due August 1, 2033

15,572,201  
\$ 15,725,528

Interest on the Series 2001 term bonds is payable in semi-annual installments on August 1 and February 1. The rate of interest on the Series 2001 term bonds is currently 4%; however, the Series 2001 term bonds are subject to an interest rate conversion on October 31, 2004 when the Series 2001 term bonds will be converted, unless and until another interest rate mode is elected by the NACFFC, to Weekly Rate Bonds, with interest reset weekly, subject to the right of the Series 2001 term bonds bondholders to tender for purchase with monies provided by a successor purchaser or pursuant to the Letter of Credit.

### Maturities of long-term debt at June 30, 2004 (based on the mandatory sinking fund redemptions), are as follows:

	<b>2001 Series Bonds</b>
June 30,	
2005	\$ 150,000
2006	100,000
2007	130,000
2008	160,000
2009	195,000
Thereafter	<u>14,620,000</u>
	<u>15,355,000</u>
Plus unamortized bond premium	<u>370,528</u>
<b>Total</b>	<b><u>\$ 15,725,528</u></b>

Amortization of the bond premium will begin in fiscal year 2005, concurrent with the initial interest rate conversion date. The premium will be amortized over the remaining life of the Series 2001 term bonds.

The Series 2001 term bonds cannot be redeemed prior to the initial conversion date unless the Letter of Credit is not extended beyond its two initial renewal dates of October 31, 2002 and October 31, 2003. If the Letter of Credit is not renewed during this period or the Letter of Credit is replaced by an alternate credit facility, the Series 2001 term bonds are subject to a mandatory tender with varying premiums. The Series 2001 term bonds are also required to be redeemed in whole within 90 days following written notification of a termination of the Lease with no premium.

The Series 2001 term bonds are subject to mandatory sinking fund redemption requirements in varying principal amounts annually from August 1, 2005 through August 1, 2033 (maturity). The Series 2001 term bonds are secured by the Letter of Credit as well as by the Deed of Trust and a pledge of gross revenues from Project (i.e. student housing) operations. See H. Other Matters for letter of credit information.

# NOTES TO FINANCIAL STATEMENTS

June 30, 2004

## G. ASSETS HELD IN CUSTODY FOR OTHERS

The Foundation maintains certain asset balances on behalf of others, which consists of the following at June 30, 2004:

Cash	\$ 201,540
Unconditional promises to give	7,554
Investments	<u>4,252,247</u>
	<u>\$ 4,461,341</u>
Assets held on behalf of:	
Northern Arizona University	\$ 4,097,670
Parents' Association	171,756
Alumni Association	<u>191,915</u>
	<u>\$ 4,461,341</u>

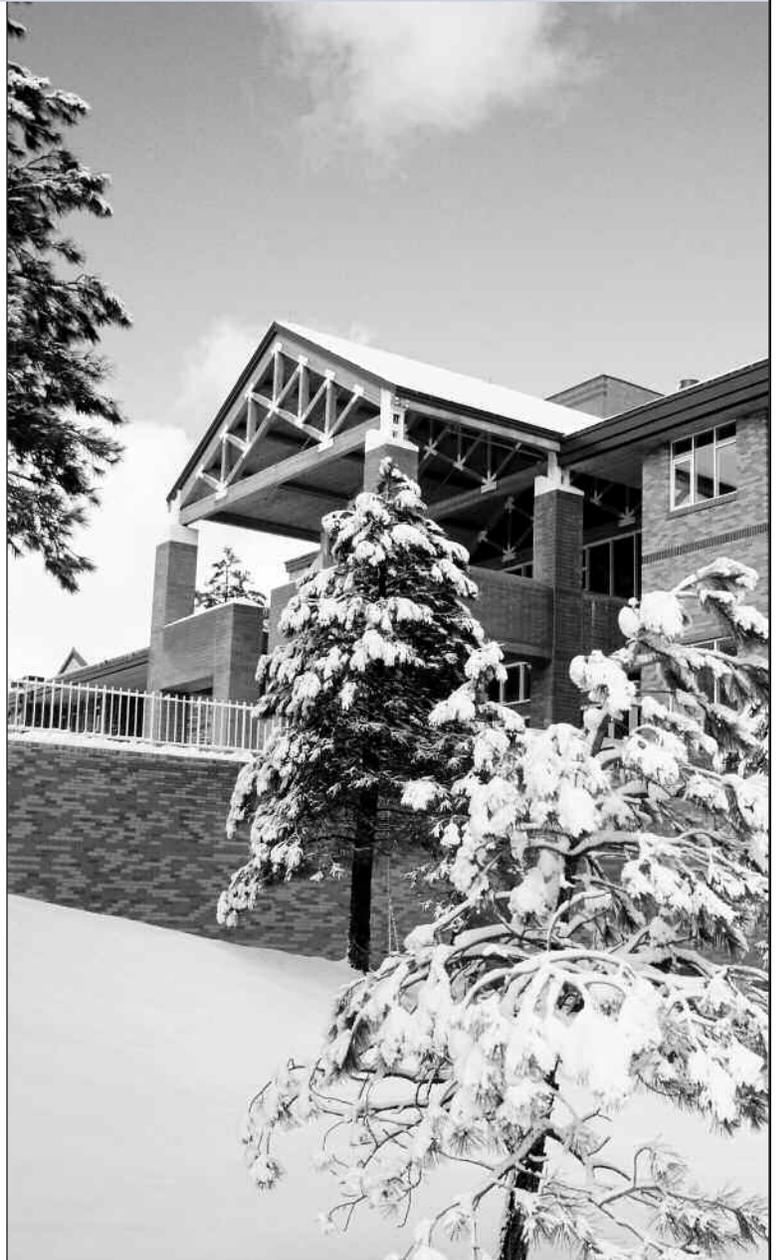
## H. OTHER MATTERS

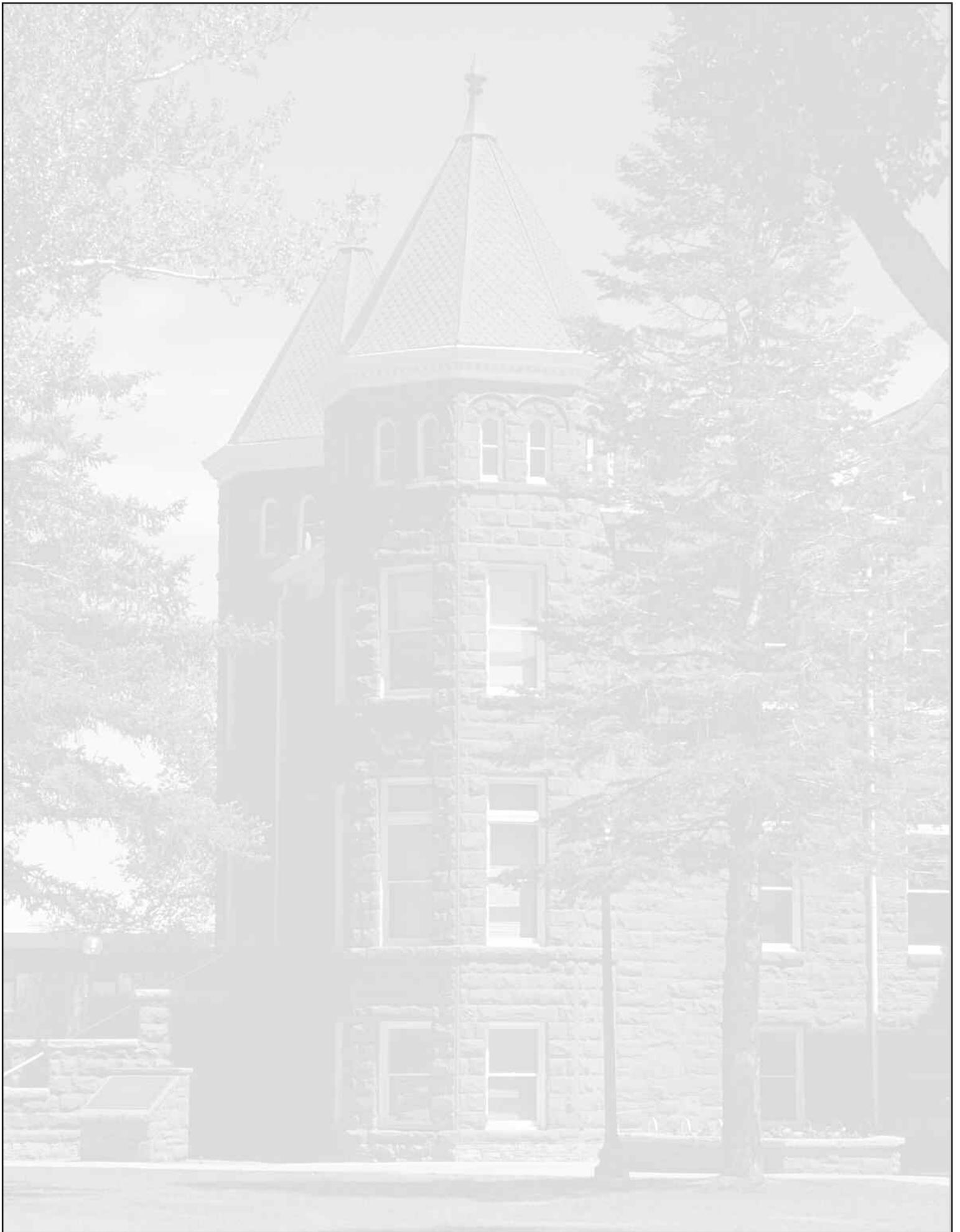
### Letter of Credit

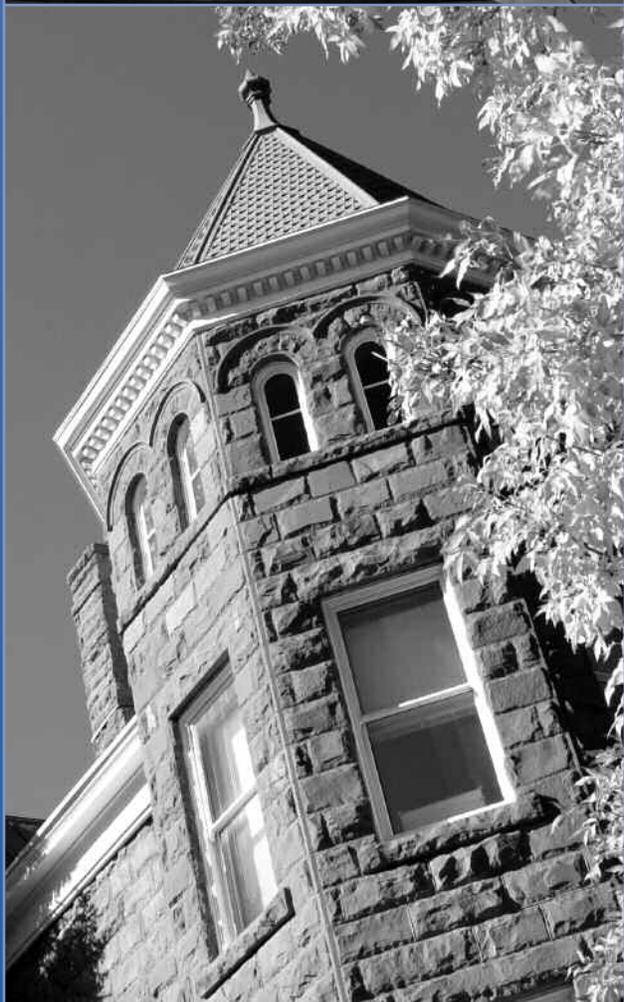
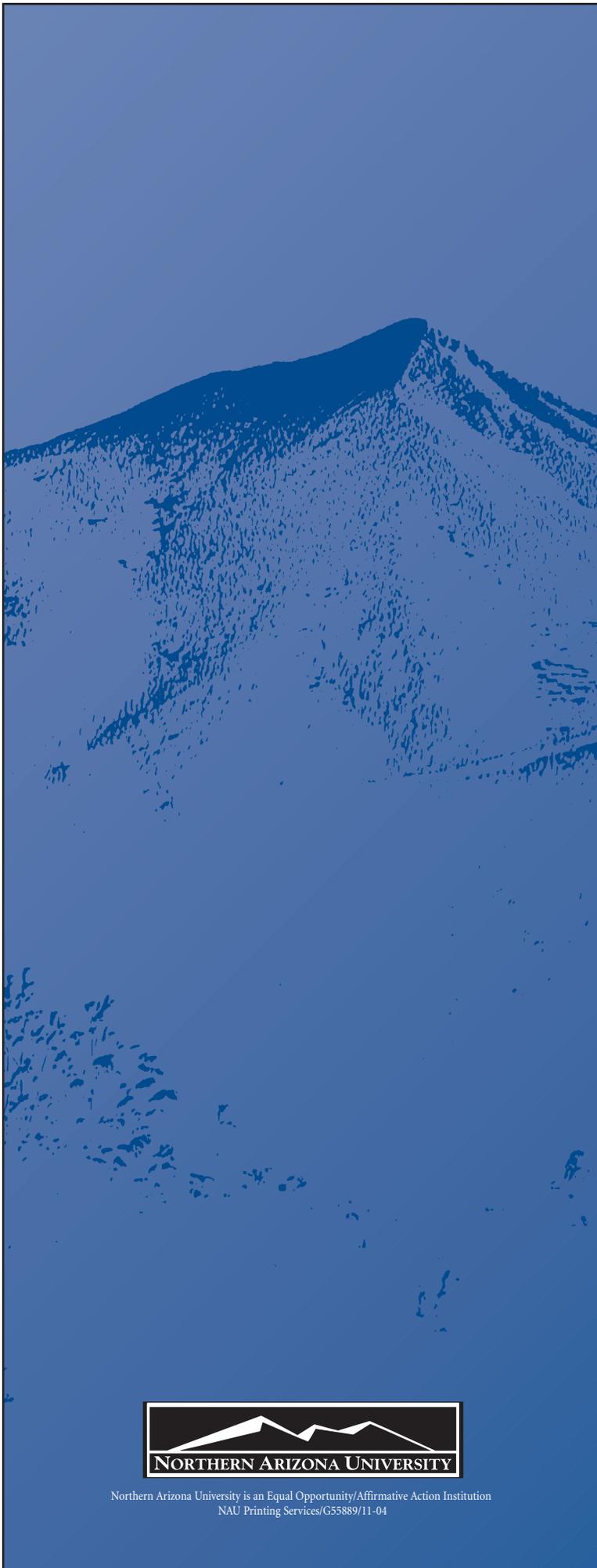
On October 31, 2001, NACFFC entered into a Reimbursement Agreement with Wachovia Bank, N.A., providing for the issuance to the Trustee of a Letter of Credit in the amount of \$15,945,742 securing payments of principal and interest on the Series 2001 Bonds. The Reimbursement Agreement is secured, together with the Series 2001 term bonds, by a Deed of Trust. The Letter of Credit was extended for another one year period effective as of October 31, 2004.

### Subsequent Events

At a meeting held September 28, 2004, the board of NACFFC unanimously authorized the remarketing of the existing bonds to a fixed rate product as soon as possible, and authorized the sale of new bonds not to exceed \$30.0 million dollars for the purpose of construction of new student housing. The board also authorized the manager of the student housing facility to develop and negotiate capital lease agreements between NACFFC and Northern Arizona University for both the current housing project, and the proposed new project for subsequent presentation to the board.







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