

UNIVERSITY OF ALASKA

(A Component Unit of the State of Alaska)

Financial Statements

June 30, 2002

(With Independent Auditors' Report Thereon)

University of Alaska
(A Component Unit of the State of Alaska)
Financial Statements
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Table of Contents

	Page
Management's Discussion and Analysis	1
Independent Auditors' Report	7
Statements of Net Assets	8
Statements of Revenues, Expenses and Changes in Net Assets	9
Statements of Cash Flows	10
Notes to Financial Statements	12

MANAGEMENT'S DISCUSSION AND ANALYSIS

(Unaudited – see accompanying accountants' report)

A review of the university's statement of net assets shows a decrease in working capital and unrestricted and restricted expendable net assets. The decline in net assets was offset somewhat by capital additions in excess of depreciation for the period. A more detailed analysis of the reasons for these changes follows.

Although working capital (current assets less current liabilities) declined by \$25.4 million in 2002, \$14.2 million was due to management's decision to transfer the majority of its short-term investments to longer-term securities. The decrease in unrestricted cash and cash equivalents of

MANAGEMENT'S DISCUSSION AND ANALYSIS

(Unaudited – see accompanying accountants' report)

The Statement of Revenues, Expenses and Changes in Net Assets reflects an overall decrease in net assets of 1.67 percent, or \$12.5 million. Major factors contributing to this change are discussed below.

State of Alaska general fund appropriations continue to be the single major source of revenue for the university, providing \$201.6 million in 2002, as compared to \$190.7 million in 2001. Despite increased appropriation levels, operating costs exceeded the rise in operating and nonoperating revenues. Appropriations are used primarily to cover basic operating costs including salaries, travel, equipment, supplies and contractual services. Historically, the Legislature has funded the university at an amount equal to or above the prior period's appropriation.

Revenues from federal and other sources for sponsored research and education-related programs increased 16 percent, from \$128.5 million in 2001

MANAGEMENT'S DISCUSSION AND ANALYSIS
(Unaudited – see accompanying accountants' report)

The university is self-insured for health care costs. Rising health care costs were a significant factor in the reduction of unrestricted net assets. Health claims and administrative costs for non-

MANAGEMENT'S DISCUSSION AND ANALYSIS
(Unaudited – see accompanying accountants' report)

Capital and Debt Activities

The University of Alaska has continued to modernize its complement of older facilities and to build new facilities to maintain or enhance the quality of the university's academic, research and student service programs.

Net capital additions totaled \$50.1 million in 2002, as compared with \$45.1 million in 2001. These capital additions primarily comprise replacement, renovation and new construction of

MANAGEMENT'S DISCUSSION AND ANALYSIS
(Unaudited – see accompanying accountants' report)

Other Economic and Financial Conditions

The following is a description of currently known facts, decisions, or conditions that are expected to have a significant effect on the financial position (net assets) or results of operations (revenues, expenses, and other changes in net assets) of the university.

The level of annual state appropriation funding is conditional upon the legislative process, which is directly influenced by current economic conditions and other factors. While it is not possible to predict annual appropriation levels, management is active in maximizing other revenue sources to keep pace with the anticipated growth in enrollment. One response has been a proposed 10 percent tuition rate increase for academic year 2004 and 2005. In terms of instructional expenditures as compared to tuition revenue, the proposed tuition increases would move the university closer to the industry average.

The university has made a commitment to enhance its competitive research capacity. Within the

Independent Auditor's Report

The Board of Regents

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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, on pages 1 through 6 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.



September 30, 2002



Assets	2002	2001
Currents assets:		
Cash and cash equivalents	\$ 17,178	\$ 33,835
Short-term investments	1,147	22,333
Accounts receivable, less allowance of \$4,257 in 2002 and \$4,720 in 2001	62,495	48,572
State appropriations receivable	400	260
Other assets	1,214	228
Inventories	6,906	7,014
Total current assets	89,340	112,242
Noncurrent assets:		
Restricted cash and cash equivalents	9,755	6,296
Notes receivable	5,283	5,626
Endowment investments	75,430	82,452
Other endowment assets	40,473	40,657
Long-term investments	19,029	4,563
Assets held in trust	5,017	5,806
Capital assets, net of accumulated depreciation	651,268	650,323
Total noncurrent assets	806,255	795,723
Total assets	895,595	907,965
Liabilities		
Current liabilities:		
Accounts payable	10,825	12,647
Accrued expenses	2,893	1,861
Accrued payroll	10,475	11,223
Deferred revenue	3,479	2,701
Accrued annual leave	7,563	7,075
Deferred lease revenue - current portion	1,281	1,281
Long-term debt - current portion	3,903	4,153
Insurance and risk management	19,578	16,947
Deposits from students and others	2,554	2,199
Total current liabilities	62,551	60,087
Noncurrent liabilities:		
Capital appropriation advances	8,946	6,678

UNIVERSITY OF ALASKA
(A Component Unit of the State of Alaska)
Statements of Revenues, Expenses and Changes in Net Assets
For the Years Ended June 30, 2002 and 2001
(in thousands)

	2002	2001
Operating revenues		
Student tuition and fees	\$ 54,245	\$ 50,434
less tuition allowances	(5,358)	(4,713)
	48,887	45,721
Federal grants and contracts	97,356	77,191
State grants and contracts	12,542	10,425
Local grants and contracts	3,700	3,055
Private grants and contracts	35,218	37,797
Federal appropriations	1,296	962
Local appropriations	705	715
Sales and services, educational departments	3,677	3,798
Sales and services, auxiliary enterprises, net of tuition allowances of \$1,266 in 2002 and \$1,113 in 2001	29,685	27,542
Other	11,237	12,994
Total operating revenues	244,303	220,200
Operating expenses		
Instruction	124,040	111,543
Academic support	30,443	27,721
Research	97,193	81,327
 State grants d77,191 Sta s2 113.82447ts		

UNIVERSITY OF ALASKA
(A Component Unit of the State of Alaska)
Statements of Cash Flows
For the Years Ended June 30, 2002 and 2001
(in thousands)

	2002	2001
Cash flows from operating activities		
Student tuition and fees, net	\$ 48,889	\$ 47,031
Grants and contracts	135,735	118,971
Sales and services, educational departments	3,677	3,798
Sales and services, auxiliary enterprises	29,649	27,863
Federal appropriations	1,296	962
Local appropriations	705	715
Other operating receipts	8,970	12,591
Payments to employees for salaries and benefits	(273,504)	(249,100)
Payments to supplier[LoerprB]		

UNIVERSITY OF ALASKA
(A Component Unit of the State of Alaska)
Statements of Cash Flows
For the Years Ended June 30, 2002 and 2001
(in thousands)

Reconciliation of operating loss to net cash used by operating activities:

	2002	2001
Operating loss	\$ (252,751)	\$ (225,800)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation expense	57,764	55,460
Changes in assets and liabilities:		
Accounts receivable, net	(13,775)	(8,134)
Other assets	(986)	878
Inventories	108	398
Accounts payable	(3,024)	4,208
Accrued expenses	1,377	(1,019)
Accrued payroll	(747)	(2,371)
Deferred revenue	798	270
Accrued annual leave	488	589
Deferred lease revenue - current portion	(1,281)	(1,281)
Insurance and risk management	2,631	1,226
Deposits from students and others	(26)	83
Net cash used by operating activities	\$ (209,424)	\$ (175,493)

Noncash Investing, Capital and Financing Activities (in thousands):

- During 2002, the university purchased equipment through a lease purchase contract totaling \$425. Payments are scheduled quarterly for a period of three years.
- During 2002, the university received a gift of real property totaling \$127 for a new endowment.

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

NOTES TO FINANCIAL STATEMENTS

June 30, 2002 and 2001

1. Organization and Summary of Significant Accounting Policies:

Organization and Basis of Presentation:

NOTES TO FINANCIAL STATEMENTS

- **Restricted Net Assets:**

Expendable – Assets, net of related liabilities, which are subject to externally-imposed restrictions that may or will be met by actions of the university and/or that expire with the passage of time.

Non-expendable – Assets, net of related liabilities, which are subject to externally-imposed restrictions requiring that they be maintained permanently by the university.

- **Invested in capital assets, net of related debt** – Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.

NOTES TO FINANCIAL STATEMENTS

term and that such changes could materially affect the amounts reported in the statement of net assets. Long-term investments include those restricted by outside parties as to withdrawal or use for other than current operations, or are designated for expenditure in the acquisition or construction of noncurrent assets or held with an intent not to be used for operations.

Capital Assets

Capital assets are stated at cost when purchased and at fair value when donated. Equipment with a unit value of less than \$2,500 is not capitalized. Certain land and other resources acquired through land grants and donated museum collections for which fair value at date of acquisition was not determinable are reported at zero basis in the financial statements.

Depreciation is computed on a straight-line basis with useful lives of building and building components ranging from 12 to 50 years, 10 to 35 years for infrast

NOTES TO FINANCIAL STATEMENTS

2. Unrestricted Net Assets:

At June 30 unrestricted net assets included the following:

	2002	2001
Designated:		
Auxiliaries	\$ 9,022,047	\$ 7,795,237
Working capital fund	4,715,368	4,715,368
Service centers	3,905,339	4,238,619
Computing/telecommunications technology	941,799	1,576,200
Deferred maintenance/renovation	245,664	305,482
Renewal and replacement funds	2,046,563	1,530,446
Quasi-endowment funds	78,610	78,131
Employee benefit funds	(7,302,894)	(1,947,515)
Endowment earnings	5,973,471	6,695,281
Retirement Incentive Program	-	(1,254,968)
Encumbrances	7,954,140	13,835,506
Total designated	27,580,107	37,567,787
Undesignated	8,933,953	7,906,656
Total unrestricted net assets	\$ 36,514,060	\$ 45,474,443

Unrestricted net assets include non-lapsing university receipts of \$21 million at June 30, 2002. Non-lapsing university receipts of \$25.2 million from 2001 were fully expended in 2002.

At June 30, 2002 and 2001, \$30 million and \$32.1 million, respectively, of auxiliary funds, encumbrances and other unrestricted net assets were pledged as collateral for the university's general revenue bonds, as calculated under the terms of the 1992 General Revenue Bonds Trust Indenture.

3. Cash and Investments:

Alaska statutes and Board of Regents' policy provide the university with broad authority to invest funds. GASB requires that bank balances and investment securities be disclosed or classified by category of credit risk as follows:

Deposits: Insured or collateralized with securities held by the university or its agent in the name of the university (category 1); collateralized with securities held by the pledging financial institution's trust department or agent in the name of the university (category 2); uncollateralized including collateralized balances for which securities are held by the pledging financial institution or by its trust department or agent but not in the name of the university (category 3).

Investment Securities: Insured or registered, with securities held by the university or its agent in the name of the university (category 1); Uninsured and unregistered, with securities held by the counterparty's (another party to the transaction, i.e. seller or dealer) trust department or agent in the name of the university (category 2); Uninsured and unregistered, with securities held by the counterparty's trust department or agent but not in the name of the university (category 3).

NOTES TO FINANCIAL STATEMENTS

	<u>2002</u>		<u>2001</u>	
	<u>Book</u>	<u>Bank</u>	<u>Book</u>	<u>Bank</u>
Deposits (in thousands):				
Insured or collateralized (Category 1):				
Demand deposits	\$ 340	\$ 340	\$ 315	\$ 316
Time deposits	100	100	100	100
Uncollateralized (Category 3):				
Demand deposits	(7,195)	394	(6,667)	456
Time deposits	<u>4,100</u>	<u>4,100</u>	<u>1,900</u>	<u>1,900</u>
Total deposits	<u>\$ (2,655)</u>	<u>\$ 4,934</u>	<u>\$ (4,352)</u>	<u>\$ 2,772</u>
Investment securities:				
Insured and registered (Category 1)				
Common stock		\$ 2		\$ 2
Uninsured and unregistered (Category 3)				
Repurchase agreements		<u>6,317</u>		<u>7,634</u>
Total investment securities		<u>\$ 6,319</u>		<u>\$ 7,636</u>
Other deposits and investments:				
Money market funds		\$ 262		\$ 171
Commonfund, short and intermediate term funds		29,884		62,284
Commonfund, absolute return fund		12,244		-
Funds held by others:				
Endowment funds		73,900		80,749
Bond proceeds and redemption funds		<u>2,585</u>		<u>2,991</u>
Total other deposits and investments		<u>\$ 118,875</u>		<u>\$ 146,195</u>

Deposits reported in Category 1 by the university were insured by federal depository insurance. Deposits and investments reported in Category 3 were secured under a tri-party agreement with Bank of New York to hold the collateral for the benefit of the university; however, the securities are not held in the name of the university. At June 30, 2002 and 2001, securities with an estimated fair value of \$20.5 million and \$15.3 million were held as collateral under the tri-party agreement. Time deposits consist of a non-interest bearing deposit in the amount of \$4.2 million maintained as a compensating balance in exchange for banking services.

Repurchase agreements represent overnight investments secured under tri-party agreements with various bank trust departments to hold the collateral for the benefit of the university; however, the securities are not held in the name of the university. The Commonfund is a not-for-profit provider of pooled multi-manager investment vehicles for colleges and universities. Endowment funds are managed by the University of Alaska Foundation under a consolidated fund agreement. Bond proceeds and related redemption funds are held by bank trustees in accordance with debt covenants.

Certain funds held in trust are not included in the financial statements as the university has only limited control over their administration. These funds are in the custody of independent fiduciaries and at June 30, 2002 and 2001, had an estimated fair value of approximately \$6.4 million and \$5.7 million, respectively.

NOTES TO FINANCIAL STATEMENTS

4. Accounts Receivable:

Accounts receivable consisted of the following at June 30, 2002 and 2001 (in thousands):

	2002	2001
Student tuition and fees	\$ 3,333	\$ 2,604
Grants and contracts	53,526	40,986
Auxiliary services and other operating activities	1,076	1,021
Capital appropriations, grants and contracts	8,817	8,681
	66,752	53,292
Less allowance for doubtful accounts	4,257	4,720
Accounts receivable, net	\$ 62,495	\$ 48,572

5. Assets Held in Trust:

Assets held in trust include operating funds of the Education Trust of Alaska (Trust). The Trust was established pursuant to state statute on April 20, 2001 by the Board of Regents to facilitate administration of the state's Section 529 College Savings Program. The program is a nationally marketed college savings program developed in accordance with Internal Revenue Code Section 529 and includes the resources of the former Advance College Tuition (ACT) Program. Participant account balances of approximately \$400 million and \$24.4 million at June 30, 2002 and 2001, respectively, are not included in the financial statements.

Assets of the Trust are invested in various mutual funds at the direction of T. Rowe Price Associates, Inc., the program manager. The net assets of the Trust, which include a reserve for University of Alaska (UA) Tuition Value Guarantees, are available for payment of program administrative costs, benefits and other purposes of the Trust. Management estimates reserve requirements for the UA Tuition Value Guarantees to be approximately \$200,000 and \$250,000 at June 30, 2002 and 2001, respectively.

6. Other Endowment Assets:

Other endowment assets consist of real property and timber and other rights. By Acts of Congress in 1915 and 1929, the university was granted approximately 110,000 acres of land which the territory, and later the state of Alaska managed on behalf of the university. At June 30, 2002 and 2001, the university held approximately 88,000 acres of these lands at no basis because fair value at the date of transfer was not determinable. In 1982 and 1988 the university was allowed to select certain state lands including timber and other rights as replacement for lands disposed of or adversely affected during the period of administration by the territory and the state. These lands and property interests were recorded at their fair value as of the date of transfer.

NOTES TO FINANCIAL STATEMENTS

7. Capital Assets:

A summary of capital assets follows (in thousands):

<u>Balance</u> <u>July 1, 2001</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>June 30, 2002</u>
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NOTES TO FINANCIAL STATEMENTS

8. Long-term Debt:

Debt service requirements at June 30, 2002 were as follows (in thousands):

<u>Year ended</u> <u>June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2003	\$ 3,903	\$ 2,716	\$ 6,619
2004	4,042	2,551	6,593
2005	4,069	2,390	6,459
2006	4,098	2,231	6,329
2007	4,162	2,069	6,231
2008-2012	15,372	8,417	23,789
2013-2017	16,503	5,652	22,155
2018-2022	16,176	2,490	18,666
2023-2024	<u>5,603</u>	<u>196</u>	<u>5,799</u>
	<u>\$ 73,928</u>	<u>\$ 28,712</u>	<u>\$ 102,640</u>

Long-term debt consisted of the following at June 30, 2002 and 2001:

	2002	2001
<u>Note payable – capital construction</u> 1.826% assisted note to the Alaska Housing Finance Corporation (AHFC) to finance construction of Anchorage campus housing, payable beginning August 1999 to February 2024. In 1996, the university entered into an agreement with AHFC to borrow a total of \$33 million, of which \$30 million was issued on an assisted basis with interest at 1.826% and an additional \$3 million issued on an unassisted basis at 6.0%	\$ 29,905,365	\$ 30,958,092
<u>Note payable – quasi-endowment funds</u> 5.0% note to finance the purchase of two buildings located on University Lake Drive in Anchorage, due serially to May 2022	2,430,188	2,500,004
<u>Revenue bonds payable</u> 3.95% to 6.25% general revenue bonds due serially to 2023, secured by a pledge of unrestricted current fund revenue generated from tuition, fees, recovery of facilities and administrative costs, sales and services of educational departments, miscellaneous receipts and auxiliaries	41,200,735	44,231,306
<u>Installment contracts</u> 5.44% installment contract for the purchase of air traffic control simulation equipment due in quarterly installments through January 2005	<u>391,687</u>	<u>--</u>
	<u>\$ 73,927,975</u>	<u>\$ 77,689,402</u>

Under the terms of the 1992 General Revenue Bonds Trust Indenture, the university is required to maintain a reserve account with a trustee at an amount equal to one-half of the maximum annual debt

NOTES TO FINANCIAL STATEMENTS

service. The balance in the reserve account

NOTES TO FINANCIAL STATEMENTS

Major construction projects of the university are funded primarily by State of Alaska appropriations and university revenue bonds. The majority of appropriations are financed through capital project bonds issued by the Alaska Housing Finance Corporation, a component unit of the State of Alaska, while

NOTES TO FINANCIAL STATEMENTS

The university's annual pension cost for the current year and related information is as follows:

Pension	Postemployment
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NOTES TO FINANCIAL STATEMENTS

Pension and Postemployment Healthcare Benefits
(in thousands)

	Actuarial valuation year ended <u>June 30</u>	Actuarial value of plan assets	Actuarial accrued liability (AAL)	Unfunded (overfunded) actuarial accrued liability (UAAL)	Funded ratio	Covered payroll	UAAL as a percentage of covered payroll
Pension benefits:							
	1998	304,455	284,192	(20,263)	107%	72,338	N/A
	1999	308,959	272,389	(36,570)	113%	74,258	N/A
	2001	360,222	331,693	(28,529)	109%	93,210	N/A
Postemployment healthcare benefits:							
	1998	121,421	113,341	(8,080)	107%	72,338	N/A
	1999	125,249	110,424	(14,825)	113%	74,258	N/A
	2001	152,517	140,438	(12,079)	109%	93,210	N/A
Total:							
	1998	425,876	397,533	(28,343)	107%	72,338	N/A
	1999	434,208	382,813	(51,395)	113%	74,258	N/A
	2001	512,739	472,131	(40,608)	109%	93,210	N/A

Valuation data for fiscal year 2000 is not available since the State of Alaska has decided, in accordance with GASB Statement No. 27, to do a valuation report biennially.

State of Alaska Teachers' Retirement System (TRS)

Plan Description

TRS provides pension, postemployment health care, death and disability benefits to participants. Benefit and contribution provisions are established by State law and may be amended only by the State Legislature.

Each fiscal year, TRS issues a publicly available financial report which includes financial statements and required supplementary information. That report may be obtained by writing to the State of Alaska, Department of Administration, Division of Retirement and Benefits, P.O. Box 110203, Juneau, Alaska, 99811-0203 or by calling (907) 465-4460.

Funding Policy

Employees contribute 8.65% of their base salary as required by State statute. The funding policy for TRS provides for periodic employer contributions at actuarially determined rates that, expressed as percentages of annual covered payroll, are sufficient to accumulate sufficient assets to pay benefits when due. During fiscal year 2002, required employee and employer contribution rates were 8.65% and 11%, respectively. The amounts contributed to TRS by the university during the years ended June 30, 2002, 2001 and 2000 were \$4,196,154, \$4,349,722, and \$4,324,920, respectively, equal to the required employer contributions for each year.

NOTES TO FINANCIAL STATEMENTS

Defined Contribution Plans:

University of Alaska Optional Retirement Plan (ORP)

Faculty classified as regular and certain administrators may make a one-time election to participate in

NOTES TO FINANCIAL STATEMENTS

Changes in applicable liability amounts follow (in thousands):

	<u>Balance</u> <u>July 1, 2001</u>	<u>Provision</u> <u>for Claims</u>	<u>Claims</u> <u>Payment</u>	<u>Balance</u> <u>June 30, 2002</u>
Health	\$ 5,378	\$ 26,558	\$ (24,373)	\$ 7,563
General liability	7,401	1,130	(646)	7,885
Workers' compensation	4,055	1,147	(1,190)	4,012
Unemployment	113	520	(515)	118
	<u>\$ 16,947</u>	<u>\$ 29,355</u>	<u>\$ (26,724)</u>	<u>\$ 19,578</u>

	<u>Balance</u> <u>July 1, 2000</u>	<u>Provision</u> <u>for Claims</u>	<u>Claims</u> <u>Payment</u>	<u>Balance</u> <u>June 30, 2001</u>
Health	\$ 4,797	\$ 21,910	\$ (21,329)	\$ 5,378
General liability	6,549	1,273	(421)	7,401
Workers' compensation	4,282	547	(774)	4,055
Unemployment	94	397	(378)	113
	<u>\$ 15,722</u>	<u>\$ 24,127</u>	<u>\$ (22,902)</u>	<u>\$ 16,947</u>

Subsequent to June 30, 2002, insured coverage limits for property claims decreased from \$200 million to \$100 million. Within the \$25 million primary layer of coverage and the \$50 million layer in excess of \$50 million, the university is uninsured for \$7.5 million and \$25 million, respectively. Insurance coverage limits for casualty claims decreased from \$45 million to \$25 million and aviation limits for the flight school and aircraft liability decreased from \$500 million to \$25 million and \$10 million, respectively.

14. Commitments and Contingencies:

Amounts received and expended by the university under various federal and state grants, contracts and other programs are subject to audit and potential disallowance. From time to time the university is named as a defendant in legal proceedings or cited in regulatory actions related to the conduct of its operations. In the normal course of business, the university also has various other commitments and contingent liabilities which are not reflected in the accompanying financial statements. In the opinion of the administration, the university will not be affected materially by the final outcome of any present legal proceedings, environmental investigations, audit adjustments, or other commitments and contingent liabilities.

15. Related Party Transactions:

The University of Alaska Foundation (Foundation) is a tax-exempt organization formed in 1974 to solicit donations for the exclusive benefit of the University of Alaska. At June 30, 2002 and 2001, the Foundation had net assets totaling \$105.4 million and \$102.1 million, respectively. The Foundation's financial statements are not combined with the university's financial statements. During 2002 and 2001, the university transferred \$980,204 and \$396,593, respectively, to the Foundation. Distributions and expenditures by the Foundation for the benefit of the university totaled \$7.4 million and \$4.9 million, of which \$7.1 million and \$4.7 million were direct reimbursements to the university. At June 30, 2002 and 2001 the Foundation owed the university \$1.4 million and \$.8 million, respectively, primarily for reimbursement of grant and contract and scholarship expenditures. The university

