

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
June 30, 2002

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

Introduction

The following discussion and analysis provides an overview of the financial position and activities of the University of Alaska (university) for the year ended June 30, 2002 with selected comparative information for the year ended June 30, 2001. This discussion has been prepared by management and should be read in conjunction with the financial statements including the notes thereto, which follow this section.

Using the Financial Statements

The university's financial report includes three basic financial statements: the Statement of Net Assets, the Statement of Revenues, Expenses and Changes in Net Assets and the Statement of Cash Flows. These statements are prepared in accordance with generally accepted accounting principles and Government Accounting Standards Board (GASB) pronouncements. During 2002, the university implemented GASB Statement No. 35, *Basic Financial Statements - and Management's Discussion and Analysis – for Public Colleges and Universities*, and applied the statement effective July 1, 2000. The statement establishes standards for external financial reporting for public colleges and universities and requires that financial statements be presented on a consolidated basis to focus better on the university as a whole. Resources are classified into three net asset categories – unrestricted, restricted and invested in capital assets, net of related debt. Previously, financial statements focused on the accountability of individual fund groups rather than the university as a whole.

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. The difference between total assets and total liabilities (net assets) is one indicator of the financial condition of the university, while the change in net assets is an indicator of whether the financial condition has improved or declined during the year. A summarized comparison of the university's assets, liabilities and net assets at June 30, 2002 and 2001 follows (in thousands):

	<u>2002</u>	<u>2001</u>
Assets:		
Current assets	\$ 89,340	\$ 112,242
Other assets	154,987	145,400
Capital assets, net of depreciation	<u>651,268</u>	<u>650,323</u>
Total assets	<u>895,595</u>	<u>907,965</u>
Liabilities:		
Current liabilities	62,551	60,087
Noncurrent liabilities	<u>98,412</u>	<u>100,774</u>
Total liabilities	<u>160,963</u>	<u>160,861</u>
Net assets		
Invested in capital assets, net of debt	564,771	558,868
Restricted – expendable	32,631	42,638
Restricted – nonexpendable	100,716	100,123
Unrestricted	<u>36,514</u>	<u>45,475</u>
Total net assets	<u>\$ 734,632</u>	<u>\$ 747,104</u>

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 \$16.7 million was nearly offset by an increase in accounts receivable of \$13.9 million. The remaining change in working capital is attributed to a combination of steadily rising fixed costs and a sharp increase in health care costs outpacing the growth in nonoperating revenue sources such as state appropriations and endowment and investment earnings. These factors are further discussed in the Statement of Revenue, Expenses and Changes in Net Assets section.

Accounts receivable increased 29 percent, from \$48.6 million at June 30, 2001, to \$62.5 million at June 30, 2002 due to sustained growth in cost reimbursable sponsored programs (primarily research) over the past several years. Days of operating revenue in accounts receivable grew from 80 in 2001, to 93 in 2002. Management is continuing to work on improving the billing and collection process.

Unrestricted net assets totaled \$36.5 million at June 30, 2002, of which \$27.6 million is designated by Board of Regents or management for specific purposes. See Note 2 of the financial statements for a detailed list of these designations.

Statement of Revenues, Expenses and Changes in Net Assets

The statement of revenues, expenses and changes in net assets presents the results of operations for the university as a whole. Revenues, expenses and other changes in net assets are reported as either operating or nonoperating. Significant recurring sources of university revenue, state appropriations and investment earnings, are defined by GASB Statement No. 35 as nonoperating.

A summarized comparison of the university's revenues, expenses and changes in net assets for the years ended June 30, 2002 and 2001 follows (in thousands):

	<u>2002</u>	<u>2001</u>
Operating revenues	\$ 244,303	\$ 220,200
Operating expenses	<u>497,054</u>	<u>446,000</u>
Operating loss	(252,751)	(225,800)
Net nonoperating revenues	<u>195,723</u>	<u>195,515</u>
Loss before other revenues, expenses, gains, or losses	(57,028)	(30,285)
Other revenues, expenses, gains or losses	<u>44,556</u>	<u>23,112</u>
Decrease in net assets	<u>(12,472)</u>	<u>(7,173)</u>
Net assets at beginning of year, as originally reported	747,104	1,032,913
Cumulative effect of changes in accounting principle	<u>-</u>	<u>(278,636)</u>
Net assets at beginning of year, as restated	<u>747,104</u>	<u>754,277</u>
Net assets at end of year	<u>\$ 734,632</u>	<u>\$ 747,104</u>

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.

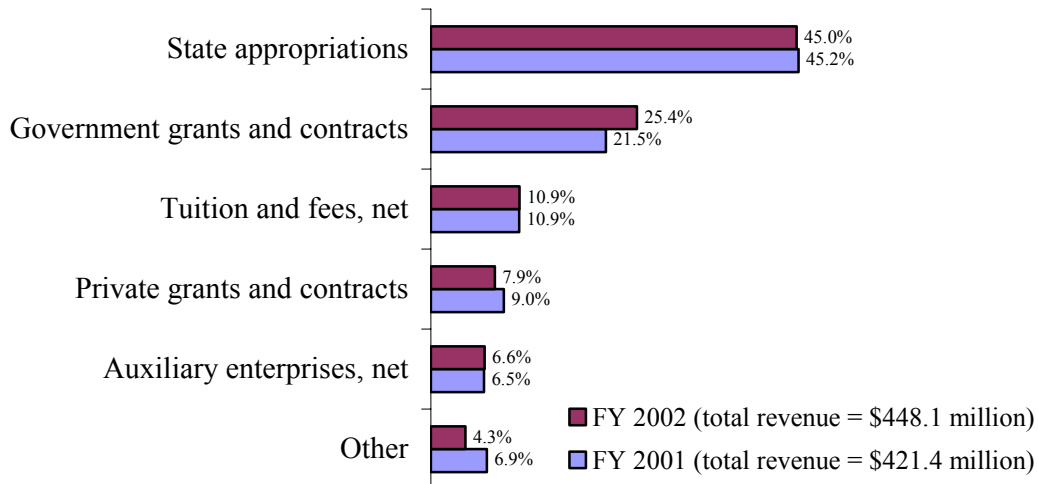
State of Alaska general fund appropriations continue to be the single major source of revenue for the university, providing \$201.6 million in 2002, as compared to \$190.7 million in 2001. Despite increased appropriation levels, operating costs exceeded the rise in operating and nonoperating revenues. 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 to \$148.8 million in 2002. Facility and administrative cost recovery provided \$22.7 million in recovery in 2002 as compared to \$18.6 million in 2001. Increased funding enables the university to expand existing programs, and start new programs, like those in global logistics, fisheries, data analysis and applied research. In addition to supporting new programs, facility and administrative cost recovery reimburses the university for facility and administrative costs necessary to operate and support the sponsored programs.

Student enrollment and tuition rate increases for the 2002 academic year provided for gross student tuition and fee revenue of \$54.2 million in 2002 as compared to \$50.4 million in 2001. Student full-time equivalent enrollment for Fall 2001 was 15,374, a 2.9 percent increase from the prior period. Tuition rates increased 3.2 percent for 2002 based on the estimated inflationary impact on the costs of providing higher education.

A comparison of operating and nonoperating revenues by source for 2002 and 2001 follows:

Operating and Nonoperating Revenues by Year



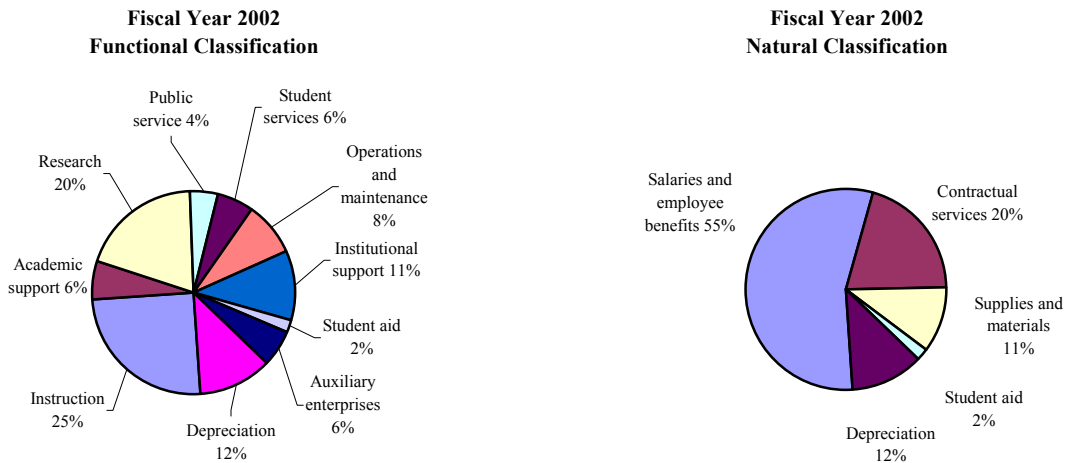
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Unaudited – see accompanying accountants' report)

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-union and represented employees exceeded the university's defined contribution by \$4.4 million in 2002. Recovery of the excess costs will be realized through increased employee contributions beginning in calendar year 2003.

A decline in market conditions resulted in a decrease in investment returns of the land grant endowment. Accumulated earnings of the endowment decreased \$7.6 million in 2002, causing the majority of the decrease in expendable restricted net assets. Endowment management policies for the land grant endowment are based on long-term total return on investments. Conservative income distributions are designed to preserve the value of the endowment and generate a predictable stream of spendable income. Accordingly, the spending rate income distributions totaled \$3.5 million in 2002, as compared to \$3.4 million in 2001, despite net investment losses of \$1.8 million in 2002. Spending distributions provide assistance for the Alaska Scholars Program and other natural resource fund projects.

In addition to the endowment investment losses, investment earnings from the university's operating capital decreased from \$5.1 million in 2001 to \$2.2 million in 2002. Both revenue sources are reported as nonoperating revenue, and provide additional resources necessary to supplement operating income and other revenues.

A comparison of operating expenses by functional and natural classification for the year ended June 30, 2002 follows:



Statement of Cash Flows

The statement of cash flows provides additional information about the university's financial results, by reporting the major sources and uses of cash. The statement helps users understand or assess:

- How operations and plant and equipment were financed.
- The ability to meet future obligations as they become due.
- The relationship between the change in net assets and the change in cash.

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 academic and research facilities, as well as investments in equipment and information technology. At June 30, 2002, \$88.1 million remain unexpended from current and prior year capital appropriations, of which \$41.2 million is committed to existing construction contracts. At June 30, 2002, \$11.4 million in private gifts and grants for construction of the \$31 million University of Alaska Museum addition and renovation remain unexpended. Such gifts are held by the University of Alaska Foundation and will be received by the university on a reimbursement basis during construction expected to be complete in October 2004.

Construction in progress at June 30, 2002 totaled \$52.9 million. New facility construction in progress includes the University of Alaska Anchorage library and parking garage, the University of Alaska Museum addition and renovation in Fairbanks, and the Egan Library classroom addition at University of Alaska Southeast, Juneau. Renovation projects at the University of Alaska Fairbanks, primarily those for the Rasmuson Library, Brooks Building and Fine Arts complex, comprise a majority of the balance of construction in progress at June 30, 2002.

In July 2002, Standard & Poor's affirmed the university's credit rating of AA- for bonds backed by its broad general revenue pledge. At the same time Moody's Investors Service affirmed its previous rating of A1 with stable outlook. The University has maintained these ratings since its general revenue issues were first rated in 1992.

At June 30, 2002, total debt outstanding was \$73.9 million, comprised of \$41.2 million in general revenue bonds, \$32.3 million in notes payable, and \$.4 million in lease finance contracts.

On July 31, 2002, the university issued general revenue bonds totaling \$33,515,000. Approximately \$3.8 million of the bonds will be used for redemption of general revenue bonds issued in prior years, while the remainder will be used for capital improvement projects. The capital improvement projects include the University of Alaska Anchorage Community and Technical College Center, the Juneau Readiness Center/UAS Joint Facility, and the University of Alaska Fairbanks West Ridge Research Building and related science facilities.

Bonds were issued in prior years to finance construction of student residences at three campuses, a student recreation center, a research facility to house the International Arctic Research Center, the acquisition and renovation of several properties adjacent to the university's campuses, additions to the university's self-operated power, heat, water and telephone utility systems, and to refund debt issued through third-party contracts prior to the Alaska Legislature's authorization for the university to issue less costly university general revenue bonds.

Over the past dozen years, the university has utilized both bank-qualified and non bank-qualified equipment lease financings to provide for its short term needs or to facilitate systematic renewals. Short-term lines of credit are available to provide interim cash flow financing for facilities intended to be funded with general revenue bond proceeds.

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 last year, the university has recruited executive staff and senior faculty in research areas of strategic importance, such as global climate change, remote sensing, transportation logistics, and fisheries. The university sold general revenue bonds in July 2002 for construction of new research facilities. Additional funding of \$61.7 million for these facilities is included in the state's general obligation bond proposition on the November 2002 ballot. Growth in research programs funded through the Alaska Program to Stimulate Competitive Research and those addressed to the National Institutes of Health further contribute to the potential for additional research funding.

The university has initiated several programs to increase the capacity to recruit and retain students. The university has set as a goal, an increase in enrollment of 5 percent a year for the next two years. In an effort to enhance students' experience, the university has implemented a suite of online student services such as registration, web payment, financial aid, transcript requests, and online grades.



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Independent Auditor's Report

The Board of Regents
University of Alaska:

We have audited the accompanying basic financial statements of the University of Alaska (University), a component unit of the State of Alaska, as of and for the year ended June 30, 2002 and 2001 as listed in the table of contents. These financial statements are the responsibility of the university's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards* issued by the Comptroller General of the United States. 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 audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the University of Alaska at June 30, 2002 and 2001, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in note 1 to the financial statements, as of July 1, 2000 the University of Alaska adopted Government Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*, and GASB Statement No. 37 *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus*, and adopted GASB Statement No. 38, *Certain Financial Statement Disclosures*.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 30, 2002 on our consideration of the University of Alaska's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The Management's Discussion and Analysis, 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.

KPMG LLP

September 30, 2002



UNIVERSITY OF ALASKA
(A Component Unit of the State of Alaska)
Statements of Net Assets
June 30, 2002 and 2001
(in thousands)

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
Deferred lease revenue	13,771	15,052
Long-term debt	70,025	73,536
Security deposits on long-term contracts	5,670	5,508
Total noncurrent liabilities	98,412	100,774
Total liabilities	160,963	160,861
Net Assets		
Invested in capital assets, net of related debt	564,771	558,868
Restricted:		
Expendable:		
Restricted funds	1,830	2,467
Student loan funds	922	915
Education Trust of Alaska	5,028	5,263
Capital projects	4,227	5,188
Debt service	2,509	2,509
Endowment	18,115	26,296
Nonexpendable	100,716	100,123
Unrestricted (see Note 2)	36,514	45,475
Total net assets	\$ 734,632	\$ 747,104

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

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
Public service	22,267	20,053
Student services	28,709	26,175
Operations and maintenance	42,210	35,634
Institutional support	56,132	52,234
Student aid	9,405	7,616
Auxiliary enterprises	28,891	28,237
Depreciation	57,764	55,460
Total operating expenses	497,054	446,000
Operating loss	(252,751)	(225,800)
Nonoperating revenues (expenses)		
State appropriations	201,596	190,650
Investment earnings	2,188	5,074
Endowment earnings	(1,812)	5,451
Interest on debt	(2,886)	(3,057)
Other nonoperating expenses	(3,363)	(2,603)
Net nonoperating revenues	195,723	195,515
Loss before other revenues, expenses, gains or losses	(57,028)	(30,285)
Capital appropriations, grants and contracts	44,429	23,112
Additions to permanent endowments	127	-
Net decrease in net assets	(12,472)	(7,173)
Net assets		
Net assets - beginning of year, as originally reported	747,104	1,032,913
Cumulative effect of change in accounting principle	-	(278,636)
Net assets - beginning of year, as restated	747,104	754,277
Net assets - end of year	\$ 734,632	\$ 747,104

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

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 suppliers	(155,547)	(130,793)
Payments to students for financial aid	(9,294)	(7,531)
Net cash used by operating activities	(209,424)	(175,493)
Cash flows from noncapital financing activities		
State appropriations	201,345	192,426
Other payments, net	(900)	(186)
Direct lending receipts	37,719	15,426
Direct lending payments	(37,453)	(15,469)
Net cash provided by noncapital financing activities	200,711	192,197
Cash flows from capital and related financing activities		
Capital appropriations	7,872	8,915
Capital grants and contracts	38,797	16,568
Purchase of capital assets	(59,648)	(44,950)
Principal paid on capital debt and leases	(4,186)	(3,967)
Interest paid on capital debt and leases	(2,871)	(3,042)
Net cash used by capital and related financing activities	(20,036)	(26,476)
Cash flows from investing activities		
Proceeds from sales and maturities of investments	25,549	5,000
Purchase of investments	(16,335)	(14,600)
Interest received on investments	928	2,559
Interest and other sales receipts from endowment investments	4,649	8,521
Education Trust of Alaska	760	(1,470)
Net cash provided by investing activities	15,551	10
Net decrease in cash and cash equivalents	(13,198)	(9,762)
Cash and cash equivalents, beginning of the year	40,131	49,893
Cash and cash equivalents, end of the year	\$ 26,933	\$ 40,131
Cash and cash equivalents (current)	\$ 17,178	\$ 33,835
Restricted cash and cash equivalents (noncurrent)	9,755	6,296
Total cash and cash equivalents	\$ 26,933	\$ 40,131

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

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:

	<u>2002</u>	<u>2001</u>
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	<u>\$ (209,424)</u>	<u>\$ (175,493)</u>

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:

The University of Alaska (university) is a constitutionally created corporation of the State of Alaska which is authorized to hold title to real and personal property and to issue debt in its own name. The university is a component unit of the State of Alaska for purposes of financial reporting. As an instrumentality of the State of Alaska, the university is exempt from federal income tax under Internal Revenue Code Section 115, except for unrelated business activities as covered under Internal Revenue Code Sections 511 to 514.

In preparing the financial statements, management is required to make estimates that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the statement of net assets. Actual results could differ from those estimates. The more significant accounting and reporting policies and estimates applied in the preparation of the accompanying financial statements are discussed below.

During 2002 the university adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 34 *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management’s Discussion and Analysis – for Public Colleges and Universities*, and GASB Statement No. 37 *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments: Omnibus*. These standards and GASB Statement No. 38, *Certain Financial Statement Disclosures* were applied effective July 1, 2000.

As a result of GASB Statement No. 35, significant changes to the financial statements are as follows:

- Depreciation of capital assets is now recorded.
- Management’s Discussion and Analysis is presented as required supplementary information.
- Revenues and expenses are now categorized as either operating or nonoperating. Previously, a measure of operations was not presented.
- Student aid costs such as scholarships, fellowships and Pell grants, applied to student accounts, are now shown as a reduction of tuition and fees and room and board revenues; while other payments made directly to students continue to be reported as student aid expense. Previously, all student aid was presented as an expense.
- A statement of cash flows using the direct method is now presented.

GASB Statement No. 35 establishes standards for external financial reporting for public colleges and universities and requires that resources be classified for accounting and reporting purposes into the following net asset categories:

- **Unrestricted Net Assets:** Assets, net of related liabilities, which are not subject to externally-imposed restrictions. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Regents or may otherwise be limited by contractual agreements with outside parties.

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.

As a result of GASB Statement No. 35 the university was required to make changes in accounting principles primarily related to recording depreciation and certain other changes to capital assets. These changes are reported as a cumulative effect adjustment and decrease net assets as of July 1, 2000 as follows (in thousands):

Accumulated depreciation	\$ (286,383)
Government titled property with university reversionary interest	17,988
Unexpended bond proceeds	<u>(10,241)</u>
Cumulative effect of changes in accounting principle	<u>\$ (278,636)</u>

In addition to the above change, total asset and total liability balances previously reported as of June 30, 2001 were equally decreased by approximately \$276.9 million because participant account balances of the Education Trust of Alaska and pension plan assets of the university's defined contribution pension plan were removed from the statement of net assets. In accordance with GASB Statement No. 35 guidance, participant balances in these fiduciary activities are now reported only in the notes to the financial statements. This change has no effect on net assets.

Summary of Significant Accounting Policies:

The accompanying financial statements have been prepared on the economic resources measurement focus and the accrual basis of accounting. All significant intra-university transactions have been eliminated. The university reports as a business type activity, as defined by GASB Statement No. 35. Business type activities are those that are financed in whole or in part by fees charged to external parties for goods or services.

The university has the option to apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless FASB conflicts with GASB. The university has elected to not apply FASB pronouncements issued after the applicable date.

Cash and Cash Equivalents

All highly liquid investments, not held for long-term investment, with original maturities of three months or less are reported as cash and cash equivalents.

Inventories

Inventories are stated at the lower of cost (first-in, first-out method) or market.

Investments

Investments are stated at fair value. Investment securities are exposed to various risks, such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near

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 infrastructure and other improvements, and 4 to 10 years for equipment. Library and museum collections are not depreciated because they are preserved and cared for and have an extraordinarily long useful life.

Endowments

Endowments consist primarily of the university's land grant endowments. The net appreciation on investments of the endowments available for authorization and expenditure by the Board of Regents is \$18.1 million and \$26.3 million, respectively, at June 30, 2002 and 2001. These amounts are recorded in the restricted expendable net asset category. Alaska Statute 14.40.400 provides the Board of Regents with authority to manage the endowments using the total return concept of investment management which is intended to preserve and maintain the purchasing power of the principal.

In accordance with Board of Regents policy, the annual spending allowance is based on five percent of a five-year moving average of the invested balance. Withdrawals of net appreciation to meet the spending allowance are limited to the unexpended accumulated net appreciation of the endowments.

Operating Activities

The university's policy for defining operating activities as reported on the statement of revenues, expenses and changes in net assets are those that generally result from exchange transactions such as payments received for providing services and payments made for services or goods received. Certain significant revenue streams relied upon for operations are recorded as non-operating revenues, as defined by GASB Statement No. 35, including state appropriations and investment earnings.

Tuition Allowances

Student tuition and fee revenues and certain other revenues from students are reported net of tuition allowances in the statement of revenues, expenses and changes in net assets. Tuition allowances are the difference between the stated charge for tuition and room and board provided by the university and the amount paid by the student and/or third parties making payments on the students' behalf.

Lapse of State Appropriations

Alaska statutes provide that unexpended balances of one-year appropriations will lapse on June 30 of the fiscal year of the appropriation; however, university receipts in excess of expenditures may be expended by the university in the next fiscal year. University receipts include student fees, donations, sales, rentals, facilities and administrative cost recovery, auxiliary and restricted revenues. The unexpended balances of capital appropriations lapse upon completion of the project or upon determination that the funds are no longer necessary for the project.

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):

	Balance July 1, 2001	Additions	Reductions	Balance June 30, 2002
Capital assets not depreciated				
Land	\$ 24,982	\$ -	\$ 679	\$ 24,303
Construction in progress	27,873	45,357	20,288	52,942
Library and museum collections	44,749	1,598	-	46,347
Other capital assets				
Buildings	696,762	17,997	-	714,759
Infrastructure	31,754	1,761	-	33,515
Equipment	138,786	14,542	10,862	142,466
Leasehold improvements	4,845	-	-	4,845
Other improvements	19,271	679	-	19,950
Total	989,022	81,934	31,829	1,039,127
Less accumulated depreciation:				
Buildings	227,074	35,801	-	262,875
Infrastructure	16,984	2,664	-	19,648
Equipment	85,599	16,324	8,604	93,319
Leasehold improvements	1,372	243	-	1,615
Other improvements	7,670	2,732	-	10,402
Total accumulated depreciation	338,699	57,764	8,604	387,859
Capital assets, net	<u>\$ 650,323</u>	<u>\$ 24,170</u>	<u>\$ 23,225</u>	<u>\$ 651,268</u>

	Balance July 1, 2000	Additions	Reductions	Balance June 30, 2001
Capital assets not depreciated				
Land	\$ 24,999	\$ -	\$ 17	\$ 24,982
Construction in progress	30,365	26,408	28,900	27,873
Library and museum collections	43,274	1,475	-	44,749
Other capital assets				
Buildings	669,260	27,502	-	696,762
Infrastructure	30,488	1,266	-	31,754
Equipment	121,601	20,709	3,524	138,786
Leasehold improvements	4,845	-	-	4,845
Other improvements	19,139	132	-	19,271
Total	943,971	77,492	32,441	989,022
Less accumulated depreciation:				
Buildings	191,455	35,619	-	227,074
Infrastructure	11,379	5,605	-	16,984
Equipment	78,301	10,442	3,144	85,599
Leasehold improvements	1,130	242	-	1,372
Other improvements	4,118	3,552	-	7,670
Total accumulated depreciation	286,383	55,460	3,144	338,699
Capital assets, net	<u>\$ 657,588</u>	<u>\$ 22,032</u>	<u>\$ 29,297</u>	<u>\$ 650,323</u>

NOTES TO FINANCIAL STATEMENTS

8. Long-term Debt:

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

Year ended <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:

	<u>2002</u>	<u>2001</u>
<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 at June 30, 2002 and 2001 was \$2,583,359 and \$2,558,946, respectively.

On July 31, 2002, the university issued general revenue bonds totaling \$33,515,000. The bond proceeds will be used for capital improvement projects and redemption of a portion of 1992 Series C and all of the 1999 Series I general revenue bonds. The bonds mature on October 1, 2028 and bear interest at rates ranging from 1.4 percent to 5 percent.

In prior years, the university defeased housing system revenue bonds and certain general revenue bonds by placing the proceeds of new bonds in irrevocable trusts to provide for all future debt service payments on the old bonds. Trust assets and related liabilities for the defeased bonds are not included in the university's financial statements. At June 30, 2002 and 2001, outstanding defeased bonds were \$12.7 million and \$13.1 million, respectively.

9. Deferred Lease Revenue:

In fiscal year 1997, the university entered into an agreement to construct a facility and establish the International Arctic Research Center (IARC). The university received \$19,215,000 through a Japanese non-profit corporation to support the construction of the IARC in exchange for a commitment to provide research facilities to various Japanese research organizations and agencies for a period of 25 years, including lease extensions. The Japanese research organizations began occupying the IARC in fiscal year 1999. The deferred lease revenue at June 30, 2002 is \$15,051,750 and it is reduced at the rate of \$1,281,000 per year with a corresponding increase to other operating revenue.

10. Long-term Liabilities:

Long-term liability activity was as follows (in thousands):

	Balance			Balance	Amounts
	July 1, 2001	Additions	Reductions	June 30, 2002	due within
					one year
Capital appropriation advances	\$ 6,678	\$ 2,585	\$ 317	\$ 8,946	\$ -
Deferred lease revenue	16,332	-	1,281	15,051	1,281
Long-term debt	77,690	425	4,186	73,929	3,903
Security deposits on long-term contracts	<u>5,508</u>	<u>162</u>	<u>-</u>	<u>5,670</u>	<u>-</u>
	<u>\$ 106,208</u>	<u>\$ 3,172</u>	<u>\$ 5,784</u>	<u>\$ 103,596</u>	<u>\$ 5,184</u>

	Balance			Balance	Amounts
	July 1, 2000	Additions	Reductions	June 30, 2001	due within
					one year
Capital appropriation advances	\$ 3,290	\$ 3,500	\$ 112	\$ 6,678	\$ -
Deferred lease revenue	17,581	32	1,281	16,332	1,281
Long-term debt	81,655	-	3,965	77,690	4,153
Security deposits on long-term contracts	<u>5,230</u>	<u>278</u>	<u>-</u>	<u>5,508</u>	<u>-</u>
	<u>\$ 107,756</u>	<u>\$ 3,810</u>	<u>\$ 5,358</u>	<u>\$ 106,208</u>	<u>\$ 5,434</u>

11. Capital Appropriations and Construction Commitments:

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 other appropriations are received directly from the state or state agencies. Construction commitments at June 30, 2002 aggregated \$41.2 million. At June 30, 2002, the university had received \$8.9 million from State of Alaska capital appropriations in advance of expenditures.

Unexpended and unbilled capital funds appropriated by the State of Alaska in prior years, which are not reflected as appropriation revenue or receivables on the university's books at June 30, 2002, totaled approximately \$88.1 million.

12. Pension Plans:

As of June 30, 2002, substantially all regular employees participate in either the State of Alaska Public Employees' Retirement System (PERS), an agent multiple-employer public employees' retirement system, the State of Alaska Teachers' Retirement System (TRS), a cost-sharing multiple-employer plan, or the University of Alaska Optional Retirement Plan (ORP), a single-employer defined contribution plan. In addition, substantially all regular employees and faculty classified as temporary participate in the University of Alaska Pension Plan, a supplemental single-employer defined contribution plan. None of the retirement systems or plans own any notes, bonds or other instruments of the university.

Defined Benefit Plans:

State of Alaska Public Employees' Retirement System (PERS)

Plan Description

The university contributes to PERS, a defined benefit, agent multiple-employer public employee retirement system established and administered by the State of Alaska (State). PERS provides pension, postemployment health care, death and disability benefits to eligible participants. Benefit and contribution provisions are established by State law and may be amended only by the State Legislature.

Each fiscal year, PERS 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 and Annual Pension Cost

Employee contribution rates are 7.5% for peace officers and firefighters and 6.75% for other employees, as required by State statute. The funding policy for PERS provides for periodic employer contributions at actuarially determined rates that, expressed as a percentage of annual covered payroll, are sufficient to accumulate sufficient assets to pay benefits when due.

NOTES TO FINANCIAL STATEMENTS

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

	<u>Pension</u>	<u>Postemployment healthcare</u>	<u>Total</u>
Contribution rates:			
Employee:			
Peace officers and firefighters	5.34%	2.16%	7.50%
Other employees	4.80%	1.95%	6.75%
Employer	2.90%	1.18%	4.08%
Annual pension cost	\$3,006,906	\$1,219,245	\$4,226,151
Contributions made	\$3,006,906	\$1,219,245	\$4,226,151
Actuarial assumptions:			
Inflation rate	3.50%	Same	
Investment return	8.25%	Same	
Projected salary increase:			
Inflation	3.50%	N/A	
Productivity and merit:			
Peace officers and firefighters	2.50%	N/A	
Others	2.00%	N/A	
Health cost trend	N/A	6.50%	

Actuarial assumptions made include a June 30, 2001 valuation date; projected unit credit cost method; level dollar, open amortization method; a rolling 25-year amortization period and a 5-year smoothed market asset valuation method.

During 2002, the annual required contribution (ARC) and the amount contributed by the university for annual pension cost (APC) was \$4,226,151. The university has fully funded its pension obligation; therefore, no net pension obligation (NPO) existed at fiscal year end.

Three year trend information follows:

	<u>Year ended June 30</u>	<u>APC</u>	<u>Employer contribution rate</u>	<u>Percentage of APC contributed</u>	<u>NPO</u>
Pension:	2000	\$3,404,011	4.11%	100%	-
	2001	2,936,457	3.25%	100%	-
	2002	3,006,906	2.90%	100%	-
Postemployment Healthcare:	2000	1,268,619	1.53%	100%	-
	2001	1,171,050	1.30%	100%	-
	2002	1,219,245	1.18%	100%	-

In the current fiscal year, the University determined, in accordance with provisions of GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers* (GASB 27), that no pension liability existed to PERS and there were no previously reported liabilities to PERS.

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 the ORP as an alternative to participation in PERS or TRS. The ORP is an employer funded defined contribution plan which operates in conjunction with a companion mandatory tax-deferred annuity plan. ORP participants are required to make employee contributions to one of the plan's authorized tax-deferred annuity programs at a rate equivalent to the TRS employee contribution rate of 8.65%. The university makes matching employer contributions to one of the plan's authorized employee-selected annuity providers or investment managers at a rate equal to the three-year moving average of the TRS employer contribution rates (11.67% for FY02 and 12% for FY01). In fiscal year 2002 and 2001, the university's total covered payroll for the ORP plan was approximately \$40.5 million and \$34.8 million, respectively. The amounts contributed to ORP by the university during the years ended June 30, 2002, 2001 and 2000 were \$4,729,946, \$4,182,523, and \$3,615,692, respectively. At June 30, 2002 and 2001, plan assets (participants' accounts attributable to employer contributions) had a net value of approximately \$34.4 million and \$33 million, respectively. Each participant is 100% vested at all times.

University of Alaska Pension Plan (Pension)

In addition to the other retirement plans, substantially all regular employees and faculty classified as temporary participate in the Pension plan which was established effective January 1, 1982, when the university withdrew from the federal social security program. Effective January 1, 2002, employer contributions for regular employees were 7.65% of covered wages up to a maximum of \$42,000 and \$84,900 for certain faculty classified as temporary. The plan provides for employer contributions to be invested in accordance with participant-directed investment elections to the plan's fixed income and/or equity funds. Each participant is 100% vested at all times.

In 2002 and 2001, the university's total covered payroll for the Pension plan was approximately \$148.8 million and \$133.6 million, respectively. The university's costs to fund and administer the plan amounted to approximately \$11.4 million, or 7.69% of covered payroll. At June 30, 2002 and 2001, plan assets (participants' accounts) had a net value of approximately \$211.9 million and \$219.6 million, respectively.

13. Insurance and Risk Management:

The university is exposed to a wide variety of risks including property loss, bodily and personal injury, intellectual property, errors and omissions, aviation and marine. Exposures are handled with a combination of self-insurance, commercial insurance, and membership in a reciprocal risk retention group.

The university is self-insured up to the maximum of \$2 million per occurrence for casualty claims and \$250,000 for property claims. Private carriers provide coverage in excess of these amounts. Health care, workers' compensation and unemployment claims are fully self-insured.

Liabilities have been established to cover estimates for specific reported losses, estimates for unreported losses based upon past experience modified for current trends, and estimates of expenses for investigating and settling claims.

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

NOTES TO FINANCIAL STATEMENTS

provides in-kind administrative and accounting support for the Foundation, the costs of which are included as expenditures in the university's financial statements.

The investable resources of the university's land grant endowment trust fund and the Foundation's pooled endowment funds are combined into a consolidated fund (fund) for investment purposes. At June 30, 2002 and 2001, the fair value of the fund was \$129.6 million and \$140.4 million, respectively. The university's share of this fund was \$73.9 million and \$80.7 million, which is reflected in endowment investments. The fund is managed by the Foundation's investment committee and treasurer on a total return basis in accordance with an investment policy approved by the Board of Regents. The net assets and related activity for the university's land grant endowment trust's investment in the fund is reflected in the university's financial statements.

16. Functional Classifications with Natural Classifications:

The university's operating expenses by natural classification were as follows (in thousands):

	Year ended June 30, 2002						Total
	Compensation & Benefits	Contractual Services	Supplies & Materials	Other	Student Aid	Depreciation	
Instruction	\$ 96,736	\$ 18,497	\$ 8,715	\$ 92	\$ -	\$ -	\$124,040
Academic support	21,351	4,566	4,478	48	-	-	30,443
Research	56,391	32,170	8,656	(24)	-	-	97,193
Public service	13,666	7,098	1,465	38	-	-	22,267
Student services	19,359	6,889	2,274	187	-	-	28,709
Operations and maintenance	19,814	9,742	12,117	537	-	-	42,210
Institutional support	41,347	10,921	3,379	485	-	-	56,132
Student aid	-	-	-	-	9,405	-	9,405
Auxiliary enterprises	6,728	10,881	11,075	207	-	-	28,891
Depreciation	-	-	-	-	-	57,764	57,764
	<u>\$275,392</u>	<u>\$100,764</u>	<u>\$52,159</u>	<u>\$1,570</u>	<u>\$9,405</u>	<u>\$57,764</u>	<u>\$497,054</u>

	Year ended June 30, 2001						Total
	Compensation & Benefits	Contractual Services	Supplies & Materials	Other	Student Aid	Depreciation	
Instruction	\$ 89,559	\$ 13,835	\$ 7,946	\$ 203	\$ -	\$ -	\$111,543
Academic support	19,447	4,238	3,974	62	-	-	27,721
Research	49,058	24,451	7,643	175	-	-	81,327
Public service	12,107	6,620	1,308	18	-	-	20,053
Student services	17,295	6,791	2,015	74	-	-	26,175
Operations and maintenance	18,493	7,063	9,463	615	-	-	35,634
Institutional support	35,348	11,264	3,546	2,076	-	-	52,234
Student aid	-	-	-	-	7,616	-	7,616
Auxiliary enterprises	6,385	9,331	12,379	142	-	-	28,237
Depreciation	-	-	-	-	-	55,460	55,460
	<u>\$247,692</u>	<u>\$83,593</u>	<u>\$48,274</u>	<u>\$3,365</u>	<u>\$7,616</u>	<u>\$55,460</u>	<u>\$446,000</u>