ANNUAL FINANCIAL REPORT

2003

ARIZONA STATE UNIVERSITY

ARIZONA STATE UNIVERSITY

2003 ANNUAL FINANCIAL REPORT

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A LETTER FROM THE PRESIDENT

ARIZONA STATE UNIVERSITY

We are pleased to present the 2003 Annual Financial Report for Arizona State University. Despite an uncertain economic climate, during the past year we have taken decisive steps toward the implementation of what I term a "culture of academic enterprise." As a major research institution, ASU has the potential not only to generate new knowledge, but to emerge as a powerful engine for economic development, leveraging public investment in the university and contributing to the region's prosperity. Never before has the economic impact of knowledge been greater, and we have been moving at an accelerated pace to secure the resources necessary to build the research infrastructure that will allow Arizona to compete for the industries, corporations, and jobs the state needs to prosper.

During the past few years the people of Arizona have made an unprecedented commitment to university science and technology research that will open the door to a knowledge-based state economy. The approval of Proposition 301 in November 2000 represented public recognition of the need to invest in the future prosperity of our region by providing a long-term funding stream for science and technology investments. And the passage of the research infrastructure bill by the state legislature in June authorizes $14.5 million of annual state appropriations starting in fiscal year 2007–2008 for lease-purchase capital financing of approximately $185 million of important new research facilities. To help bridge the lease-purchase cost funding needs until that time, the legislature exempted contractors building the infrastructure projects from state sales tax, which will lower the overall project costs to the university.

It is projected that the research infrastructure projects, when completed, will generate $70 million of additional research grant and contract revenues. Immediate benefits will arise directly from construction activity—as many as 3,000 jobs will be created. The investment will yield $330 million in immediate local economic impact, and generate approximately $15 million in tax revenue.

We have only begun to explore the entrepreneurial potential of university teaching and research. Groundbreaking research leading to new products with commercial application has the capacity to generate new revenues for the university. ASU has the potential to capitalize on its knowledge content and intellectual property, expediting the transfer of knowledge and technology developed in our laboratories and classrooms to the commercial sector. Our technology transfer program is already among the leaders in national higher education, according to rankings released by the *Chronicle of Higher Education*.

Entrepreneurial institutions require investors, and ASU has worked hard to attract private support. Since January the ASU Foundation has received four historic endowment gifts that promise to bring new excellence to programs across the campus. In January ASU received a $50 million gift to our business school, the second largest donation in the history of American business education, and at the time the largest gift ever to the university. The gift from William Polk Carey, chairman of W. P. Carey & Co. LLC, a New York City-based investment firm, has endowed the W. P. Carey School of Business at ASU, making possible the development of a world-class business school with a global focus, and increasing ASU's capacity to undertake strategic partnerships with business, industry, and government. In June, Ira A. Fulton, chief executive officer of Fulton Homes, Inc., one of the nation's preeminent residential builders, announced a $50 million gift for the benefit of the College of Engineering and Applied Sciences. The gift endows the Ira A. Fulton School of Engineering at ASU, and will enable a highly ranked national school to become world-class. ASU has also received a $10 million gift from the Virginia G. Piper Charitable Trust to establish the Virginia G. Piper Center for Creative Writing, and a further $5 million gift from Ira Fulton, to the College of Education.

In accordance with new requirements of the Governmental Accounting Standards Board, beginning next fiscal year the ASU audited financial report will include more information about organizations financially related to the university, including the Arizona State University Foundation, ASU Alumni Association, Sun Angel Foundation, Collegiate Golf Foundation, and Price-Elliott Research Park. Net assets (fund balances) for these interrelated organizations total approximately $258 million, largely comprising donor-restricted and endowment funds. In the past ASU has disclosed aggregated financial information for these entities in the notes to our audited financial statements.

The report reveals promising trends, including a $6.9 million increase in net assets (fund balances). Consistent with the objectives of the Changing Directions initiative of the Arizona Board of Regents, we anticipate ever greater funding source diversification—in the long term, this means less reliance on state appropriations because of increased tuition revenues, and, most importantly, with additional research facilities will come increased research funding. We also look forward to the launch of an ambitious fundraising campaign in 2005. These initiatives promise to further strengthen ASU's financial position as we lay the foundations for a New American University.

Michael M. Crow
President, Arizona State University

OFFICE OF THE PRESIDENT

PO BOX 872203, TEMPE, AZ 85287-2203
(480) 965-5606 FAX: (480) 965-0865

MANAGEMENT'S DISCUSSION AND ANALYSIS

Introduction

The following Management's Discussion and Analysis (MD&A) provides an overview of the financial performance of Arizona State University (ASU, the University) and is designed to assist readers in the understanding of the accompanying financial statements. The MD&A should be read in conjunction with the accompanying financial statements and notes to the financial statements and is the responsibility of the University's management. These financial statements were prepared in accordance with the Governmental Accounting Standards Board (GASB) principles, specifically with GASB Statement No. 35, *Basic Financial Statements - and Management's Discussion and Analysis - for Public Colleges and Universities*, as amended by GASB Statement No. 37; and GASB Statement No. 38, *Certain Financial Statement Note Disclosures*. The three basic financial statements are the statement of net assets, the statement of revenues, expenses, and changes in net assets, and the statement of cash flows. Where appropriate, prior year information has been restated to conform with current year presentations.

FINANCIAL HIGHLIGHTS

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. Assets are what the University owns and are generally measured in current value, except for property and equipment, which are recorded at historical cost less accumulated depreciation. Assets are categorized as either current or noncurrent. Current assets are generally considered to be convertible to cash within one year. Liabilities are what the University owes to others or what it has collected from others before it has provided the related services and are generally recorded at current values. Liabilities are also categorized as either current or noncurrent. Current liabilities are the amounts becoming due and payable within the next fiscal year.

The following table shows a condensed statement of net assets at June 30, 2003 and 2002 (Dollars in Millions).

		2003	2002
ASSETS			
	Current assets	$ 143.2	$ 151.5
	Noncurrent assets (excluding capital assets)	257.2	306.2
	Noncurrent capital assets, net	998.7	932.0
	Total Assets	$ 1,399.1	$ 1,389.7
LIABILITIES			
	Current liabilities	$ 80.0	$ 70.6
	Noncurrent liabilities	443.4	450.3
	Total Liabilities	$ 523.4	$ 520.9
NET ASSETS			
	Invested in capital assets, net	$ 649.1	$ 643.4
	Restricted:		
	Nonexpendable	42.4	39.1
	Expendable	53.1	66.8
	Unrestricted	131.1	119.5
	Total Net Assets	$ 875.7	$ 868.8

GASB requires that net assets be reported in specific net assets categories. Invested in capital assets, net of related debt represents the historical costs of property and equipment, reduced by the balance of related outstanding debt and depreciation expense charged over the years. Restricted nonexpendable net assets represent the value of endowments which donors have required be invested in perpetuity and the Perkins Loan Program federal and related institutional capital contributions. Restricted expendable net assets include amounts committed for such things as debt service, student loans, and debt financed capital projects. Unrestricted net assets include the amounts institutionally designated or committed to support specific academic and research programs, capital construction projects, and unrestricted funds functioning as endowments.

Current assets at June 30, 2003 primarily consisted of cash and investments, accounts receivable, and inventories. The decrease in noncurrent assets was primarily due to the $72.5 million decrease in restricted investments with bond trustee, as a result of the use of bond proceeds to finance construction projects during fiscal 2003, partially offset by an increase in noncurrent (long-term) other investments. This was a result of a University strategy to improve investment returns by investing a larger portion of operating funds in securities with longer maturities.

Current liabilities at June 30, 2003 primarily consisted of accounts payable and accrued liabilities, deferred revenue, funds held for others, and the current portion of lease purchases and other long-term obligations. The major components of noncurrent liabilities are the long-term portions of the University's debt, including bonds payable of $277.9 million and lease purchases and other long-term obligations of $144.4 million. The overall increase in current liabilities was due to increases in all categories, except the current portion of bonds payable. The largest current liability increase was in accounts payable where a $10.4 million increase between years was primarily due to increased debt service interest payable at June 30, 2003, as well as increased (vendor) accounts payable due to increased construction activity during fiscal year 2003. The decrease in the current portion of the bonds payable liability was the result of the restructuring of ASU's debt service obligations.

This debt restructuring resulted in an increase in unrestricted net assets of approximately $7.0 million, with the remaining increase in unrestricted net assets occurring primarily in accounts that fund University initiatives, including the managing of growth of the University and increasing the quality of the education provided to students. Essentially all of the University's unrestricted net assets as of June 30, 2003 had been internally designated for academic and research programs and initiatives, or for contractually committed goods and services, including capital projects in various stages of planning and completion.

Capital and Debt Activities

An important element in continuing the quality of academic programs, research activities, and student residential life is the sustained development and renewal of the University's capital assets. The University must provide and equip adequate facilities to support instruction, research, public service, residential life, and other related programs. The University continues to work aggressively to manage its financial resources effectively.

Major capital projects underway or in advanced planning during fiscal 2003 included -

- Lattie F. Coor Hall is a new 275,000 square feet building that will provide highly mediated classrooms and facilities for eleven academic units. Included in the building will be classrooms, open computer laboratories, research space, and special purpose facilities. Completion is anticipated before January 2004.

- The Arizona Biodesign Institute Phase 1 building which will provide substantial new research space totaling 172,000 square feet. Now under construction and scheduled for completion in fall 2004, this will be the first world-class, flexible, and dedicated research facility at ASU. Research in the Phase 1 building will focus on such real-world developments as plant-based vaccines that can be easily grown and distributed in third-world countries, enhanced pharmaceuticals, improved bio-materials to aid surgeons and organ transplant recipients, new DNA sequencing to fight disease, and instant blood tests.

- Planning began on the Arizona Biodesign Institute Phase 2 with construction scheduled to begin in January 2004. Current plans provide for 172,000 square feet of space to be used for neural rehabilitation and neural interface and brain control research. The design plan includes an open, flexible interior that encourages research collaboration and allows the building to adapt to fit specific project needs.

- Infrastructure improvement projects during the year included extensive underground utility tunnel upgrades to improve and expand utility services for current and future development of the University.

Statement of Revenues, Expenses, and Changes in Net Assets

The Statement of Revenues, Expenses, and Changes in Net Assets (SRECNA) presents the University's results of operations. A summarized comparison of the University's revenues, expenses, and changes in net assets for the years ended June 30, 2003 and 2002 is as follows (Dollars in Millions).

	2003	2002
Operating revenues	$ 475.2	$ 439.1
Operating expenses	806.6	766.0
Net nonoperating revenues	328.9	333.7
Income before capital and endowment additions	$ (2.5)	$ 6.8
Capital and endowment additions	$ 9.4	$ 36.7
Increase in net assets	6.9	43.5
Net assets, end of the year	$ 875.7	$ 868.8

Activities are reported as either operating or nonoperating. Generally, operating revenues are earned in exchange for providing goods and services and operating expenses are incurred in the normal operation of the University. Included in operating expenses is a provision for depreciation on property and equipment. The difference between the two generally results in an operating loss. All public universities, including ASU, will typically have an operating loss since significant recurring revenues, such as state appropriations and private gifts, are required to be shown as nonoperating revenues.

Revenues. Operating revenues include student tuition and fees, and grants and contracts, as well as sales and services of auxiliary enterprises and educational departments. Tuition and fees revenues, net of scholarship allowances, increased between years by $18.2 million, due to a 5.2% increase in enrollment and a slight tuition rate increase. Grants and contracts increased by $15.0 million between years with the majority of the increase occurring in federally funded research grants and contracts.

MANAGEMENT'S DISCUSSION AND ANALYSIS

There was a $8.9 million decrease in state operating and capital appropriations between years due to budgetary concerns of the State of Arizona. Other revenue sources included in nonoperating revenues are the University's Technology and Research Initiative Funding, private gifts, and net investment income. Net investment income increased $5.7 million over fiscal 2002, primarily due to an increase in the market value of the University's endowments at June 30, 2003. There was a $21.5 million decrease in private gifts between years due to a $27.9 million decrease in private capital gifts partially offset by a $6.4 million increase in "cash" gifts. Capital private gifts returned to normal levels in fiscal 2003, after an extraordinary year in fiscal 2002 which included more than $20 million in historic printing presses being donated to the Katherine K. Herberger College of Fine Arts.

Expenses. The University relies primarily on state appropriations and student tuition and fees as revenue sources to support its non-grant funded core operating expenses for instruction and academic support functions such as expenses for ASU's libraries and academic information technology. Increases in research expenses were primarily funded from Technology and Research Initiative Funding and increased federal grants. The two primary functions of the University, instruction and research, comprised 46.8% of total operating expense in fiscal 2003. Also included in operating expenses is a provision for depreciation of property and equipment.

Net Assets. During the year ended June 30, 2003, an investment of the State of Arizona Local Government Investment Pool (of which ASU is a member) became questionable as to its recovery. The University's share of this investment was $4.0 million. The University decided to charge off this investment against investment income during fiscal 2003, which resulted in a $4.0 million decrease in the change in net assets for the year, and a corresponding $4.0 million decrease in net investment income for fiscal 2003.

Another useful presentation of revenues and expenses is by combined sources and uses. Combined sources and uses for the years ended June 30, 2003, and 2002 follow (Dollars in Millions):

	2003		2002		Percentage Change
SOURCES					
State appropriations	$ 311.8	37%	$ 320.7	39%	(3%)
Tuition and fees, net of allowances	206.2	24%	188.0	23%	10%
Grants and contracts	158.7	19%	143.7	17%	10%
Private gifts	28.9	3%	50.4	6%	(43%)
Technology and research initiatives funding	18.5	2%	17.7	2%	5%
Auxiliary enterprises	89.3	11%	86.3	10%	3%
Other sources	32.6	4%	25.7	3%	27%
Total Sources	$ 846.0	100%	$ 832.5	100%	2%
USES					
Instruction and academic support	$ 375.3	45%	$ 362.4	46%	4%
Research and public service	122.8	15%	103.0	13%	19%
Student services and institutional support	93.5	11%	92.4	12%	1%
Operation and maintenance of plant	42.0	5%	42.3	5%	(1%)
Scholarships and fellowships, net	37.1	4%	35.3	5%	5%
Auxiliary enterprises	80.1	9%	77.0	9%	4%
Depreciation	55.9	7%	53.7	7%	4%
Other uses	32.4	4%	22.9	3%	41%
Total Uses	$ 839.1	100%	$ 789.0	100%	6%

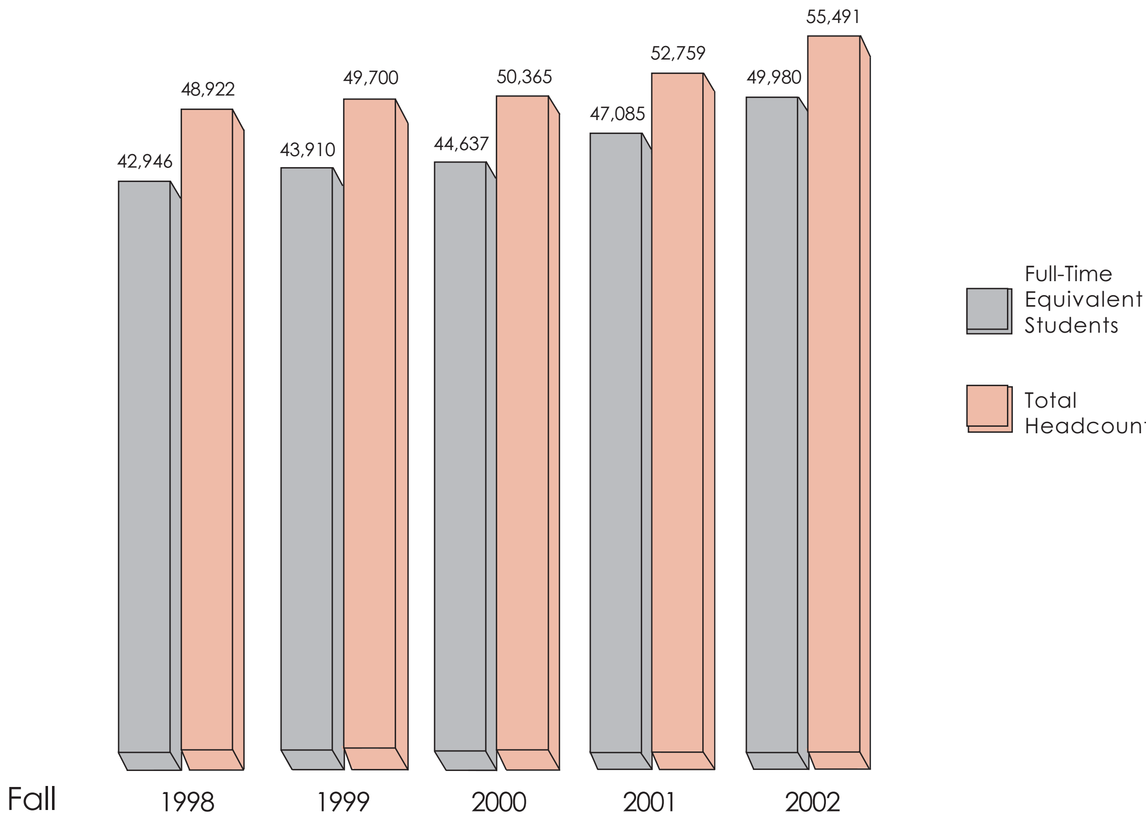
Statement of Cash Flows

The statement of cash flows provides additional information about the University's financial results, by reporting the major sources and uses of cash. This statement shows the University's primary sources of operating and noncapital related cash in fiscal 2003 were state appropriations, tuition and fees, and gifts, grants, and contracts. Uses of these cash sources included salaries and benefits for faculty, staff, and student employees, payments to suppliers of goods and services to the University, and scholarship and fellowship payments to ASU students. Cash flows from operating activities will typically be negative for state universities since GASB requires state appropriations to be reported as cash flows from noncapital financing activities. Cash flows from capital financing activities include all plant fund and related long-term debt activities. Cash flows from investing activities show all uses of cash and cash equivalents to purchase investments, and all increases in cash and cash equivalents as a result of selling investments or earning income on cash and investments.

Economic Factors

Management believes the University is well positioned for the challenges facing it in the future. Even with the decrease in state appropriations funding during the fiscal year, the University's overall financial position remained sound in fiscal 2003. Sources of recurring operational revenues were strong in fiscal 2003 and are expected to remain strong in fiscal 2004 - including net tuition and fees, grants and contracts, auxiliary enterprises revenues, and private gifts. Growth in private gifts and governmental grants and contracts provides essential support to state appropriations and student tuition and fees. The passage of the research infrastructure bill by the Arizona State Legislatures in June 2003, will help build a research infrastructure of approximately $185 million in important new research facilities. It is anticipated that once completed, these research infrastructure facilities will generate an additional $70 million annually of research grants and contracts revenue to the University, and will have an overall annual local economic impact of $330 million.

ENROLLMENT



Degrees Granted in Academic Year 2002-2003

Undergraduate	8,566
Graduate	3,280
	11,846

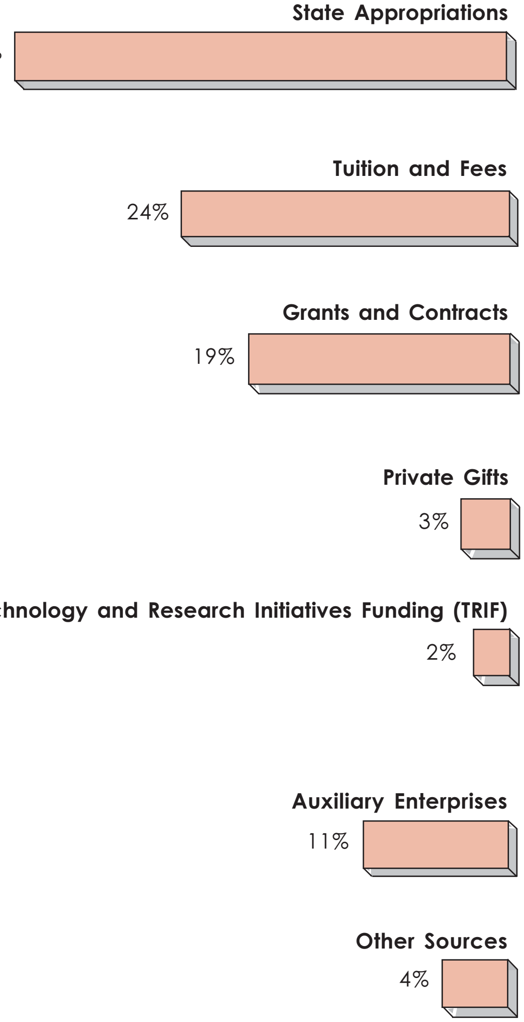
Fall 2002 Enrollment

Undergraduate	42,877
Graduate	12,614
In-State	41,801
Out-of-State	13,690

COMBINED SOURCES AND USES

Sources

For the year ended June 30, 2003
(Dollars in Millions)



State Appropriations	37%	**$ 311.8**	Represents State of Arizona legislative appropriations for operations of the University.
Tuition and Fees	24%	**206.2**	Includes $218.4 million in collected tuition and fees and $27.4 million in tuition waivers, net of $39.6 million in scholarship allowances.
Grants and Contracts	19%	**158.7**	Represents both governmental and nongovernmental grants and contracts. Includes $126.3 million in federally funded grants and contracts and $3.0 million in capital grants.
Private Gifts	3%	**28.9**	Voluntary private support from individuals, foundations, and corporations.
Technology and Research Initiatives Funding (TRIF)	2%	**18.5**	TRIF is generated from part of a 0.6% education sales tax approved by Arizona voters in November 2000. A detailed set of performance measurements are used to determine the overall effectiveness of each TRIF funded initiative.
Auxiliary Enterprises	11%	**89.3**	Represents operations of essentially self-supporting activities such as bookstore, intercollegiate athletics, residential halls, and parking.
Other Sources	4%	**32.6**	Consists primarily of sales and services, including ASU hosted national and international conferences and programs, of educational departments.
Total Sources		**$ 846.0**	

Note:

The Combined Sources and Uses statement highlights major financial data. The explanations provided are not intended to be all-inclusive.

This statement provides an overview of total University financial operations including the ASU Main, ASU West, and ASU East Campuses. Restricted and unrestricted operating and nonoperating funds are included. Restricted funds have specific purposes stipulated by outside donors and agencies.

Unrestricted funds may be designated by management for specified purposes, including academic and research programs and initiatives, or capital projects. Sources and uses are allocated and controlled by budgets.

Uses

Instruction and Academic Support	45%	**$ 375.3**	Consists of (1) instruction expenses totaling $283.9 million, which include credit and non-credit courses for academic, occupational, and vocational instruction for regular academic year and summer sessions, and continuing education, and (2) academic support expenses totaling $91.4 million, which include libraries, academic information technology support, and academic administration.
Research and Public Service	15%	**122.8**	Represents (1) research expenses of $93.4 million for activities specifically organized to produce research outcomes, and (2) public service expenses of $29.4 million for non-instructional services beneficial to individuals and groups external to the University, such as public broadcasting and community service programs.
Student Services and Institutional Support	11%	**93.5**	Consists of (1) student services expenses totaling $32.3 million, which include admissions, registrar, student activities, counseling, career guidance, student financial aid administration, and student health services, and (2) institutional support expenses of $61.2 million, which include financial operations, human resources, public safety, community relations, administrative information technology support, and alumni relations.
Operation and Maintenance of Plant	5%	**42.0**	Represents expenses for the operation and maintenance of plant, exclusive of amounts charged to auxiliary enterprises, including services related to facilities and grounds, and utility costs.
Scholarships and Fellowships	4%	**37.1**	Includes restricted grants, including $26.1 million of federally funded Pell grants, and institutionally awarded merit and need-based scholarships.
Auxiliary Enterprises	9%	**80.1**	Consists of departments managed as essentially self-supporting activities that furnish services to students and staff for a fee directly related to, but not necessarily equal to, the cost of the service.
Depreciation	7%	**55.9**	Depreciation is computed using the straight-line method over the estimated useful life of each asset.
Other Uses	4%	**32.4**	Consists primarily of interest payments on debt service and non-capital expenses on plant project accounts.
Total Uses		**$ 839.1**	
Net Increase in Net Assets		**6.9**	
		$ 846.0	

INDEPENDENT AUDITORS' REPORT

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

WILLIAM THOMSON
DEPUTY AUDITOR GENERAL

Independent Auditors' Report

Members of the Arizona State Legislature

The Arizona Board of Regents

We have audited the accompanying financial statements of Arizona State University as of and for the year ended June 30, 2003, as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with U.S. generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note A, the University's financial statements are intended to present the financial position, and changes in financial position and cash flows, of only that portion of the business-type activities of the State of Arizona that is attributable to the transactions of the University. They do not purport to, and do not, present fairly the financial position of the State of Arizona as of June 30, 2003, and the changes in its financial position and its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Arizona State University as of June 30, 2003, and the changes in financial position and cash flows of the University for the year then ended in conformity with U.S. generally accepted accounting principles.

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

Debbie Davenport
Auditor General

October 17, 2003

2910 NORTH 44TH STREET • SUITE 410 • PHOENIX, ARIZONA 85018 • (602) 553-0333 • FAX (602) 553-0051

ARIZONA STATE UNIVERSITY
STATEMENT OF NET ASSETS

June 30, 2003
(Dollars in Thousands)

ASSETS	
Current Assets:	
Cash and cash equivalent investments	$ 92,862
Short-term investments	13,589
Accounts receivable, net of allowance of $1,957	25,741
Student loans receivable	1,425
Inventories	7,790
Deferred expenses	1,799
Total Current Assets	$ 143,206
Noncurrent Assets:	
Restricted cash and cash equivalent investments	$ 38,108
Restricted investments with bond trustee	101,672
Endowment investments	59,545
Other investments	43,848
Student loans receivable, net of allowance of $1,324	10,540
Deferred expenses	1,421
Donated land	2,105
Capital assets, net of accumulated depreciation	998,744
Total Noncurrent Assets	$ 1,255,983
Total Assets	$ 1,399,189
LIABILITIES	
Current Liabilities:	
Accounts payable and accrued liabilities	$ 30,586
Compensated absences	1,317
Employee retirement and benefits deposits	3,693
Deferred revenues	23,667
Funds held for others	11,656
Bonds payable	267
Lease purchases	8,880
Total Current Liabilities	$ 80,066
Noncurrent Liabilities:	
Compensated absences	$ 15,724
Employee retirement and benefits deposits	4,744
Other liabilities	601
Bonds payable	277,879
Lease purchases	144,434
Total Noncurrent Liabilities	$ 443,382
Total Liabilities	$ 523,448
NET ASSETS	
Invested in capital assets, net of related debt	$ 649,116
Restricted for:	
Nonexpendable:	
Scholarships and fellowships	23,292
Academic department uses	7,803
Student loans	11,281
Expendable:	
Scholarships and fellowships	13,257
Academic department uses	27,942
Student loans	1,334
Capital projects	714
Debt service	9,847
Unrestricted (Note G)	131,155
Total Net Assets	**$ 875,741**

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

ARIZONA STATE UNIVERSITY
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

Year ended June 30, 2003
(Dollars in Thousands)

OPERATING REVENUES	
Student tuition and fees, net of scholarship allowances of $39,561	$ 206,243
Federal grants and contracts, primarily research grants	126,332
State and local grants and contracts	7,234
Nongovernmental grants and contracts	22,047
Sales and services -	
Auxiliary enterprises, net of $1,330 in scholarship allowances	89,287
Educational departments	20,363
Other revenues	3,710
Total operating revenues	**$ 475,216**
OPERATING EXPENSES (Note H)	
Educational and general -	
Instruction	$ 283,858
Research	93,432
Public service	29,440
Academic support	91,415
Student services	32,306
Institutional support	61,175
Operation and maintenance of plant	41,963
Scholarships and fellowships	37,107
Auxiliary enterprises	80,113
Depreciation	55,877
Total operating expenses	**$ 806,686**
Operating loss	$ (331,470)
NONOPERATING REVENUES (EXPENSES)	
State appropriations	$ 311,836
Technology and research initiatives funding (TRIF)	18,451
Private gifts	22,520
Financial aid trust funds	2,474
Net investment income	6,094
Interest on indebtedness	(22,219)
Other expenses	(10,219)
Net nonoperating revenues	**$ 328,937**
Loss before other revenues, expenses, gains, or losses	**$ (2,533)**
CAPITAL AND ENDOWMENT ADDITIONS	
Capital grants	$ 3,043
Capital private gifts	4,934
Additions to permanent endowments	1,467
Total capital and endowment additions	**$ 9,444**
Increase in net assets	6,911
Net Assets, beginning of year	868,830
Net Assets, end of year	**$ 875,741**

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

ARIZONA STATE UNIVERSITY

STATEMENT OF CASH FLOWS

Year ended June 30, 2003
(Dollars in Thousands)

CASH FLOWS FROM OPERATING ACTIVITIES	
Student tuition and fees	$ 211,649
Federal, state, local, and private grants and contracts	156,443
Payments to suppliers	(173,236)
Payments to employees for salaries and benefits	(535,224)
Payments for scholarships and fellowships	(37,107)
Student loans issued	(2,972)
Student loans collected	2,941
Sales and services of auxiliary enterprises	91,496
Sales and services of educational departments	18,709
Other receipts	10,737
Net cash used for operating activities	**$ (256,564)**
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
State appropriations	$ 311,836
Technology and research initiatives funding (TRIF)	15,149
Private gifts for other than capital purposes	23,987
Financial aid trust funds	2,474
Direct loan program receipts	137,126
Direct loan program disbursements	(137,160)
Funds held for others received	56,065
Funds held for others disbursed	(44,409)
Other payments	(10,116)
Net cash provided by noncapital financing activities	**$ 354,952**
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Capital gifts and grants	$ 4,537
Proceeds from capital debt	1,989
Purchases of capital assets	(116,052)
Proceeds from sales of capital assets	257
Principal paid on capital debt and leases	(14,045)
Interest paid on capital debt and leases	(22,219)
Net cash used for capital and related financing activities	**$ (145,533)**
CASH FLOWS FROM INVESTING ACTIVITIES	
Purchases of investments	$ (238,357)
Proceeds from sales and maturities of investments	253,107
Interest received on investments	9,241
Net cash provided by investing activities	**$ 23,991**
Net decrease in cash and cash equivalent investments	(23,154)
Cash and cash equivalent investments, beginning of year	154,124
Cash and cash equivalent investments, end of year	**$ 130,970**

Reconciliation of operating loss to net cash used for operating activities:	
Operating loss	$ (331,470)
Adjustments to reconcile operating loss to net cash used for operating activities:	
Depreciation	55,877
Changes in assets & liabilities:	
Accounts receivable, net	(3,159)
Student loans receivable, net	(323)
Inventories	(661)
Deferred expenses	838
Accounts payable and accrued liabilities	18,883
Compensated absences	801
Employee retirement and benefits	(95)
Deferred revenue	2,745
Net cash used for operating activities	$ (256,564)
SIGNIFICANT NONCASH TRANSACTIONS	
Refinancing of long-term debt	$ 7,190

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

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

Note A - Organization and Summary of Significant Accounting Policies

Organization and Basis of Presentation

Arizona State University ("the University") is a major research university located in metropolitan Phoenix with a total Fall 2002 enrollment of 55,491 students. The accompanying statements include the activity of ASU Main (located in Tempe), ASU West (located in northwest Phoenix adjacent to Glendale), ASU East (located in Mesa), and the ASU Downtown Center (located in downtown Phoenix and housing the ASU Extended Campus). For financial reporting purposes, the University includes those funds directly controlled by the University. Control by the University is determined on the basis of financial accountability. The University is classified as a state instrumentality per Internal Revenue Code Section 115. Since fiscal responsibility for the University remains with the State of Arizona, the University is considered a part of the reporting entity for the State's financial reporting purposes. The University's financial statements do not include the financially interrelated organizations described in Note I, although as reported in Note I, those entities will however, be included in the University's financial report beginning in fiscal 2004.

The accompanying financial statements include a statement of net assets; a statement of revenues, expenses, and changes in net assets; and a statement of cash flows, each of which provide a comprehensive, entity-wide perspective of the University. A statement of net assets provides information about the assets, liabilities, and net assets of the University at the end of the year. Assets and liabilities are classified as either current or noncurrent. Net assets are classified according to external donor restrictions, or availability of assets to satisfy the University's obligations. A statement of revenues, expenses, and changes in net assets provides information about the University's financial activities during the year. Revenues and expenses are classified as either operating or nonoperating, and all changes in net assets are reported, including capital additions and additions to endowments. A statement of cash flows provides information about the University's sources and uses of cash and cash equivalents during the year. Increases and decreases in cash and cash equivalents are classified as operating, noncapital financing, capital and related financing, or investing activities.

The financial statements have been prepared in accordance with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The University follows Financial Accounting Standards Board (FASB) Statements and Interpretations issued on or before November 30, 1989: Accounting Principles Board Opinions; and Accounting Research Bulletins, unless such pronouncements conflict with GASB pronouncements.

For financial reporting purposes under GASB, the University is considered a public institution engaged only in business-type activities. Accordingly, the University's financial statements have been presented under the economic resources measurement focus and the accrual basis of accounting. The economic resources measurement focus emphasizes the long-term effects of operations on overall net resources, i.e., total assets and total liabilities. The statement of revenues, expenses, and changes in net assets prepared using the economic resources measurement focus includes only transactions and events that increase or decrease net assets during the year. Under the accrual basis, revenues are recognized when earned and expenses are recorded when an obligation has been incurred, or benefit has been received. All significant intra-university transactions have been eliminated.

Summary of Significant Accounting Policies

Cash and cash equivalent investments. In accordance with GASB Statement No. 9, all highly liquid investments with an original maturity of three months or less, are considered to be cash and cash equivalent investments. University funds invested through the State of Arizona's Local Government Investment Pool are considered cash and cash equivalent investments, since such investments are available for withdrawal by the University at any time, even though some of the investments of the Pool are invested for over three months.

Investments. Short-term, endowment, and other investments are stated at fair value at June 30, 2003. Fair value typically is the quoted market price for investments. Investment income includes realized and unrealized gains and losses on investments.

Accounts receivable. Accounts receivable includes $2.8 million due from the Federal government and $7.7 million due from the State government, primarily for the reimbursement of allowable expenses made pursuant to the University's grants and contracts, $5.4 million for auxiliary enterprises services provided to students, faculty, and staff, and $3.4 million primarily due from students for tuition and fees.

Student loans receivable. Loans receivable from students bear interest primarily at 5% and are generally repayable in installments to the University over a ten-year period commencing nine months from date of separation from the University. Student loans receivable are recorded net of an allowance for estimated uncollectible amounts and related collection costs.

Inventories. Auxiliary enterprises use various methods to value their inventory. The ASU Bookstore comprises approximately 85% of the total inventory reported on the statement of net assets and is valued at cost using the retail method.

Capital assets. Capital assets are recorded at cost at the date of acquisition, or fair market value at the date of donation in the case of gifts. For equipment, the University's capitalization policy includes all items with a unit cost of $2,000 or more. Renovations to buildings, infrastructure, and land improvements that significantly increase the value or extend the useful life of structures and have a project cost of at least $5,000 are capitalized. Routine repairs and maintenance are charged to operating expenses in the year in which the expense was incurred.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 40 years for buildings and infrastructure, 10 years for library books, and 5 to 12 years for equipment. The University does not depreciate works of art or historical treasures that are considered inexhaustible and are held for exhibition, education, research, and public service.

Compensated absences. Compensated absences are employee vacation leave balances, which have been earned, but not used. Vacation leave benefits are accrued as a liability on the statement of net assets and reported as an expense in the statement of revenues, expenses, and changes in net assets.

Deferred revenues. Deferred revenues consist primarily of student tuition and fees and residential housing payments related to the ensuing year. Also included are amounts received from grant and contract sponsors which have not yet been earned.

Net assets. The University's net assets are classified based on the following three categories:

- Invested in capital assets, net of related debt: includes capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction, or improvement of those assets.
- Restricted:
  - Nonexpendable – gifts that have been received for endowment purposes, the corpus of which cannot be expended, and the balance in the Perkins Loan program.
  - Expendable – grants, contracts, gifts, and other resources that have been externally restricted for specific purposes.
- Unrestricted: all other net assets, including those designated by management for specific purposes. Substantially all unrestricted net assets are committed and/or designated for educational and research programs and initiatives, or capital projects.

When an expense is incurred that can be paid from either restricted or unrestricted net assets, the University's policy is to allow the department incurring the expense to determine the appropriate funding source. Factors used by departments to determine which resources to use include relative priorities of the department in accordance with the University's strategic initiatives, externally imposed matching requirements of certain restricted funds, and any pertinent lapsing provisions of the available restricted or unrestricted funding resources. Major capital purchases are many times split funded from multiple restricted and unrestricted funding sources.

Revenues. Revenues and expenses are classified as operating or nonoperating. Generally, revenues generated by the University, such as student tuition and fees, sales and services of auxiliary enterprises, and most Federal, state, local, and private research grants and contracts are considered operating. Other significant revenues relied upon for operations, including state appropriations, private gifts, and investment activity, are considered nonoperating revenues, as defined by GASB Statement No. 35.

Scholarship allowances. Student tuition and fee revenues and other student related revenues are reported net of scholarship allowances in the statement of revenues, expenses, and changes in net assets. Scholarship allowances are the difference between the stated charge for services provided by the University, and the amount that is paid by the students (and/or third parties making payments on a student's behalf). To the extent that revenues from such programs are used to satisfy tuition and fees, and other student charges, the University has recorded a scholarship allowance.

Included in scholarship allowances is $24.5 million of tuition waivers. Not included in scholarship allowances is $2.9 million in faculty and staff tuition waivers that are recorded as either instruction or institutional support program expenses on the statement of revenues, expenses, and changes in net assets – and as personal services and benefits expenses, in Note H. Effective for fiscal 2003, the Arizona Board of Regents (ABOR) modified its policy regarding graduate assistants and associates. The change redefined the tuition obligations of all graduate assistants and associates to that of resident students, instead of awarding non-resident graduate students non-resident waivers, as had been the policy. This change in policy resulted in a decrease in scholarship allowances between fiscal 2002 and fiscal 2003.

Technology and research initiatives funding (TRIF). As passed by Arizona voters in November 2000, TRIF is generated from a part of a 0.6% education sales tax. Collection of the tax began on June 1, 2001. As the governing board of the three state universities, the Arizona Board of Regents ("the Board") administers the portion of the collected education sales tax which funds the universities' TRIF initiatives. The Board receives funding requests from each university and determines the amount and duration of awards. The Board is required to submit an annual report to the governor and other Arizona state officials which uses a detailed set of performance measures to determine the overall effectiveness of each TRIF funded initiative.

Note B - Cash and Investments

Under Arizona State law and Arizona Board of Regents' policies, the University may invest its operating funds only in the State of Arizona Local Government Investment Pool, collateralized time certificates of deposit or repurchase agreements, U.S. Treasury securities, or Federal agency securities. Gift and endowment funds may be invested under the direction of an investment committee in such a manner as to obtain the most favorable rate of return and income stability commensurate with safety of principal. Bond trustee funds are invested by the bond trustee in accordance with the financing indenture. Components of cash and investments at June 30, 2003 consisted of the following (Dollars in Thousands):

	Fair Value
Cash and Cash Equivalent Investments	
Operating funds:	
State of Arizona Local Government Investment Pool, net of outstanding checks	$ 92,862
Short-term Investments	
Operating funds:	
U.S. Treasury and Other Federal Agency Securities	13,589
Noncurrent Investments	
Endowment funds:	
Arizona State University Foundation, as endowment investment manager and trustee for the University	45,813
Arizona Universities' Financial Aid Trust	13,732
Operating funds:	
U.S. Treasury and Other Federal Agency Securities	43,848
Bond trustee funds:	
Cash and Cash Equivalent Investments	38,108
U.S. Treasury and Other Federal Agency Securities	101,226
Guaranteed Investment Contract	446
	$ 349,624

NOTES TO FINANCIAL STATEMENTS

Bond trustee funds. The bond trustee funds are managed by Bank of New York, Bank One, and U.S. Bank, and generally consist of U.S. Government securities (Treasury securities or other Federal agency securities), cash, certificates of deposit, and Federal money market accounts. Each bank's trust department purchases U.S. Government securities for the University. U.S. Government securities are held by either the Federal Reserve Bank or the Depository Trust Company (DTC) in custodial accounts for Bank of New York, Bank One, and U.S. Bank, in computerized book-entry systems in which changes of financial institutions' interests are recorded. In turn, changes in the University's ownership interests are recorded in Bank of New York's, Bank One's, and U.S. Bank's records.

Generally, funds not directly invested in U.S. Government securities are invested in pooled Federal money market accounts in which securities are purchased and held by the trustee. Occasionally, small cash balances are maintained, or certificates of deposit are purchased by the bank's trust department. For cash and certificates of deposit, book-entry pledges of Federal government securities are obtained as collateral and held by the trust department on a pooled basis.

Endowment funds. The University has entered into a contract for management of its pooled endowment funds by the ASU Foundation in order to attract a higher level of asset management and permit more diversification of the portfolio than available by the University. The University still retains its fiduciary responsibility and oversight over the endowment funds managed by the ASU Foundation. The ASU Foundation is a nonprofit corporation that exists to support ASU. The endowment funds are currently invested in equity and bond mutual funds. The financial aid trust fund is funded from student fees and by the Arizona State Legislature. The fund is managed in a pool by the University of Arizona along with the financial aid trust funds for the other two state universities.

Pooled cash and short-term investments. Pooled cash and short-term investments at June 30, 2003, were principally with the State of Arizona Local Government Investment Pool. The State Board of Investment provides oversight for the State Treasurer's pools, and the Local Government Investment Pool Advisory Committee provides consultation and advice to the Treasurer. The fair value of a participant's position in the pool approximates the value of that participant's pool shares. The University's investment in the pool represents shares in that pool's portfolio. The shares are not identified with specific investments and are not subject to custodial credit risk. During the year ended June 30, 2003, an investment of the pool became questionable as to its recovery, with the University's share of this investment being $4.0 million. The $4.0 million was charged off to investment income during fiscal 2003 with any recoveries to be considered additional investment income when received. The University also has investments in U.S. Treasury securities and Federal agency securities. U.S. Treasury and Federal agency securities are held in the custodial account of Bank of New York with the Federal Reserve Bank or DTC and in the University's name in the bank's records. These securities are either purchased from a broker/dealer or a financial institution.

The University's bank and collected (portion of bank balance available for investment) balances at the bank at June 30, 2003, were $1.0 million and $0.3 million, respectively, and the carrying value of deposits on the University's accounting system was a deficit $6.9 million. The carrying value of deposits balance has been netted against the State of Arizona Local Government Investment Pool in the preceding table. The cash deficit balance on the accounting system occurs because cash is not transferred from investments to the bank account until outstanding checks are expected to be presented to the bank for payment. The University's deposits are fully collateralized with governmental securities (U.S. or investment grade municipals) held by either the bank's agent or the bank's agent's custodial account with either the Federal Reserve or the DTC in the University's name.

Note C - Capital Assets

Capital asset activity for the year ended June 30, 2003 consisted of the following (Dollars in Thousands):

	Beginning Balances	Additions/ Increases	Retirements/ Decreases	Ending Balances
Capital Assets:				
Land	$ 72,333			$ 72,333
Infrastructure	80,130	$ 4,095		84,225
Buildings	881,624	37,042	$ (916)	917,750
Construction in Progress	18,177	51,054		69,231
Equipment	251,783	22,106	(11,526)	262,363
Works of Art and Historical Treasures	32,528	1,052	(436)	33,144
Library Books	153,703	9,333	(1,404)	161,632
Total	$ 1,490,278	$ 124,682	$ (14,282)	$ 1,600,678
Less Accumulated Depreciation:				
Infrastructure	$ 21,799	$ 2,077		$ 23,876
Buildings	271,841	22,991	$ (321)	294,511
Equipment	154,918	22,289	(10,520)	166,687
Library Books	109,744	8,520	(1,404)	116,860
Total	$ 558,302	$ 55,877	$ (12,245)	$ 601,934
Capital Assets, Net	$ 931,976	$ 68,805	$ (2,037)	$ 998,744

The beginning balances have been adjusted by $20.2 million to reflect a reclassification of historical printing presses from equipment to historical treasures. These presses were given to ASU in fiscal 2002 and are considered museum pieces and as such should not be depreciated. Construction in progress additions represent expenses for new projects net of capital assets placed in service. It is estimated $190.0 million in additional expenses will be required to complete projects under construction at June 30, 2003.

Note D - Bonds Payable

Bonds payable at June 30, 2003, consisted of the following (Dollars in Thousands):

	Average Interest Rate	Final Maturity	Balance 7/1/2002	Additions	Reductions	Balance 6/30/2003	Current Portion
Housing Revenue Bonds	3.00%-3.70%	2003-2006	$ 993		$ (355)	$ 638	$ 267
1989 System Revenue Bonds	7.09%	2004	7,240		(4,650)	2,590	
1991 System Revenue Bonds	7.13%	2005	5,545		(2,580)	2,965	
1992A System Revenue Refunding Bonds	5.88%	2002	4,005		(4,005)		
1993 System Revenue Refunding Bonds	4.93%	2008	21,170		(3,165)	18,005	
2000 System Revenue Bonds	5.86%	2025	14,760		(610)	14,150	
2002 System Revenue Bonds	4.84%	2028	85,000			85,000	
2002 System Revenue Refunding Bonds	4.16%	2019	141,380		(1,875)	139,505	
2003 System Revenue Refunding Bonds	4.35%	2017		$ 7,130		7,130	
Subtotal: Par Amount of Bonds			$ 280,093	$ 7,130	$ (17,240)	$ 269,983	$ 267
Premium on Sale of Bonds			11,385	398	(1,227)	10,556	
Deferred Amount on Refundings			(4,427)	(338)	2,372	(2,393)	
			$ 287,051	$ 7,190	$ (16,095)	$ 278,146	$ 267

The University's bonded debt consists of various issues of system revenue bonds that are generally callable at a prescribed date with interest payable semi-annually. In prior years, certain system revenue bonds of the University were defeased through advance refundings by depositing sufficient U.S. Government securities to pay all future debt service in an irrevocable trust. Accordingly, the liabilities for these defeased bonds are not included in the University's financial statements. The principal amount of all such bonds outstanding at June 30, 2003 was $11.1 million.

The housing revenue bonds are payable from housing revenues as defined in the bond indentures. The 1992A, 1993, 2002 and 2003 system revenue refunding bonds, and the outstanding 1989, 1991, 2000, and 2002 system revenue bonds are payable from ASU Main tuition and fees, certain auxiliary enterprises revenues, and certain other revenues as defined in the bond indentures.

Securities and cash restricted for bond retirement funds and maintenance and replacement reserves held by trustees at June 30, 2003 totaled $7.7 million. Future debt service funding commitments, including interest, for bonds outstanding consisted of the following (Dollars in Thousands):

	System Revenue Bonds		Housing Bonds	
	Principal	Interest	Principal	Interest
2004		$ 13,754	$ 267	$ 18
2005	$ 11,340	13,190	226	10
2006	15,180	12,496	145	4
2007	14,290	11,776		
2008	14,470	11,054		
2009-13	78,420	43,696		
2014-18	79,030	22,111		
2019-23	26,595	10,848		
2024-28	30,020	3,246		
	$ 269,345	$ 142,171	$ 638	$ 32

The University has pledged portions of its gross revenues towards the payment of debt related to various system revenue bonds outstanding at June 30, 2003. These pledged revenues include student tuition and fees, auxiliary enterprises revenue, investment income, and indirect cost recovery revenue. Pledged revenues do not include state appropriations, gifts, endowment income, or other restricted revenues.

The University presently plans to issue approximately $65 million of system revenue bonds during fiscal year 2004.

Note E - Lease Purchases

Certificates of participation (COPS) and other lease purchases at June 30, 2003, consisted of the following (Dollars in Thousands):

Certificates of Participation:	Average Interest Rate	Final Maturity	Balance 7/1/2002	Additions	Reductions	Balance 6/30/2003	Current Portion
1991 Towers Project (through ASU Foundation)	6.89%	2010	$ 2,885		$ (240)	$ 2,645	$ 260
1993 West Campus Refunding	5.18%	2009	33,675		(3,540)	30,135	3,705
1999A Downtown Center	5.75%	2024	5,495		(130)	5,365	135
1999B Downtown Center	8.00%	2024	5,085		(90)	4,995	95
2002 Main/East/West Campuses	4.75%	2026	103,800			103,800	3,915
Other Lease Purchases	3.77%-10.50%	2013	3,832	$ 913	(922)	3,823	770
Subtotal: Par Amount of COPS/ Other Lease Purchases			$154,772	$ 913	$ (4,922)	$ 150,763	$ 8,880
Premium on Sale of COPS			2,680		(129)	2,551	
			$157,452	$ 913	$ (5,051)	$ 153,314	$ 8,880

Securities and cash restricted for non-bond retirement funds and maintenance and replacement reserves held by trustees at June 30, 2003, totaled $17.7 million. Funding commitments, including interest, for lease purchases consisted of the following (Dollars in Thousands):

	Certificates of Participation		Other Lease Purchases	
	Principal	Interest	Principal	Interest
2004	$ 8,110	$ 7,021	$ 770	$ 161
2005	6,580	6,733	605	125
2006	6,870	6,427	525	99
2007	7,180	6,095	340	76
2008	8,205	5,712	278	63
2009-13	31,730	23,412	1,305	134
2014-18	27,970	16,587		
2019-23	32,660	7,891		
2024-28	17,635	1,337		
	$ 146,940	$ 81,215	$ 3,823	$ 658

The University plans to issue approximately $185 million of Certificates of Participation (COPS) for the University's Research Infrastructure facilities projects. It is anticipated that the COPS financings will be done in phases with the first phase occurring in late fiscal 2004 or early fiscal 2005. During the Spring 2003 session, the State Legislature authorized $14.5 million of annual state appropriations starting in fiscal 2008 to fund the annual debt service. In addition, the State Legislature exempted contractors who are building the Research Infrastructure Projects from state sales tax, which will reduce the project costs in order to assist the University with the COPS financing needs until fiscal 2008.

Note F - Compensated Absences

The University has recorded a liability for accruals of vacation leave earned, but not taken at fiscal year end. Changes in accrued compensated absences for the year ended June 30, 2003 follows (Dollars in Thousands):

Balance 7/1/2002	Additions	Reductions	Balance 6/30/2003	Current Portion
$ 16,240	$ 16,687	$ (15,886)	$ 17,041	$ 1,317

Note G - Unrestricted Net Assets

As discussed in the Summary of Significant Accounting Policies, the University is following standards for external reporting purposes, which require net assets to be classified for accounting and reporting purposes into one of three net asset categories according to externally imposed restrictions. Unrestricted net assets, as defined by GASB Statement No. 35, are not subject to externally imposed stipulations; however, they are subject to internal restrictions. For example, unrestricted net assets may be designated for specific purposes by actions of management or may otherwise be limited by contractual purchase obligation agreements with outside parties. As of June 30, 2003, substantially all of the University's unrestricted assets were from University generated revenues and were internally designated for academic and research programs and initiatives, and capital projects.

Note H - Operating Expenses by Classification

Operating expenses by functional and natural classification for the year ended June 30, 2003, are summarized as follows (Dollars in Thousands):

	Year ended June 30, 2003				
	Personal Services & Benefits	Supplies & Services	Scholarships & Fellowships	Depreciation	Total
Instruction	$ 259,932	$ 23,233	$ 693		$ 283,858
Research	63,623	28,798	1,011		93,432
Public service	19,261	9,721	458		29,440
Academic support	69,494	21,770	151		91,415
Student services	25,536	6,705	65		32,306
Institutional support	45,476	15,699			61,175
Operation & maintenance of plant	20,031	21,932			41,963
Scholarships & fellowships	1,108	645	35,354		37,107
Auxiliary enterprises	29,597	47,683	2,833		80,113
Depreciation				$ 55,877	55,877
Total Operating Expenses	$ 534,058	$ 176,186	$ 40,565	$ 55,877	$ 806,686

Note I - Financially Interrelated Organizations

Not included in the financial statements of the University are six financially interrelated organizations that are non-profit corporations controlled by separate Boards of Directors whose goals are to support Arizona State University. Financial statements of these organizations are audited by independent auditors.

Four of these financially interrelated organizations — the Arizona State University Foundation, Arizona State University Alumni Association, Sun Angel Foundation, and Sun Angel Endowment — receive funds primarily through donations and dues, and contribute funds to the University for support of various programs.

A fifth financially interrelated organization, Price-Elliott Research Park, Inc. (Park), is developing a research park to promote and support research activities, in coordination with the University. In developing the research park, the Park has issued bonds guaranteed by the University.

As of June 30, 2003, the Park had $18.0 million of revenue bonds outstanding at an average interest rate of 5.26%. The debt service on the bonds is secured by a subordinated lien on ASU Main revenues. Park revenues are not pledged in order to provide development flexibility to the Park.

Annual debt service on the Park bonds will be $0.9 million in fiscal year 2004 and varies from a low of $0.9 million in fiscal 2004 to a high of $1.7 million in fiscal 2006. The University is obligated to pay the annual debt service, if not paid by the Park, under a debt service assurance agreement.

Beginning in fiscal 1990, the University provided operating cash advances to the Park repayable with interest to the University (1) upon the Park's total gross receipts for a fiscal year exceeding its total disbursements for that fiscal year and (2) before any Park surpluses are transferred to the Arizona State University Foundation, for the benefit of Arizona State University. The last year for cash transfers to the Park was fiscal 1998. Since the Parks's repayment to the University was dependent upon successful future operations and the entering into of additional land leases, the transfers to the Park were recorded by the University as current year expenses when made and not as an asset on the University's Statement of Net Assets. Total cash advances repayable to the University at June 30, 2003, including accrued interest, totaled $5.4 million. During fiscal year 2003, the Park repaid $1.2 million to the University, with this amount being recorded as other revenues with the timetable for future repayments dependent upon the Park entering into additional land leases.

A sixth financially interrelated organization, the Collegiate Golf Foundation, operates a University owned golf course.

Assets, net assets, and revenues for these organizations, from fiscal 2003 financial statements, aggregated $356.1 million, $258.0 million, and $95.2 million, respectively, with substantially all of the net assets being donor restricted or endowment funds.

Beginning with the year ending June 30, 2004, the University will be required to prepare its audited financial statements following GASB Statement No. 39 - *Determining Whether Certain Organizations are Componet Units,* as issued by the Governmental Accounting Standards Board. The implementation of GASB Statement No. 39 will significantly change the reporting format used by the University in future audited financial reports. Beginning with fiscal 2004, financial information for all financially interrelated organizations of the University will be included in the University's annual financial report.

Note J - Retirement Plans

The University participates in one cost-sharing multiple-employer defined benefit pension plan and five defined contribution pension plans. The following disclosures are required by Governmental Accounting Standards Board (GASB) Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers.* In addition to the below mentioned plans, there are two other retirement plans totaling $0.4 million in total University and employee contributions for the year ended June 30, 2003.

<u>Defined Benefit Plan</u>

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

Funding Policy. For the year ended June 30, 2003, active ASRS members and the University were each required by statute to contribute at the actuarially determined rate of 2.49% (2.00% retirement and 0.49% long-term disability) of the employees' annual covered payroll. The Arizona State Legislature establishes and may amend active plan members' and the University's contribution rates. Both the University and the covered employees made the required contributions for the years ended June 30, 2003, 2002, and 2001 as follows (Dollars in Thousands):

	Contributions Rates (Each)	University Contributions	Employee Contributions	Total Contributions
2003	2.49%	$ 4,408	$ 4,408	$ 8,816
2002	2.49%	4,191	4,191	8,382
2001	2.66%	4,227	4,227	8,454

<u>Defined Contribution Plans</u>

Plan Description. In accordance with A.R.S. § 15-1628, University faculty, academic professionals, service professionals and administrative staff have the option to participate in defined contribution pension plans. These plans are administered by independent insurance and annuity companies approved by the Arizona Board of Regents. For the year ended June 30, 2003, plans offered by the Teachers Insurance Annuity Association/College Retirement Equities Fund (TIAA/CREF), Variable Annuity Life Insurance Company (VALIC), Fidelity Investments Tax-Exempt Services Company (Fidelity), Aetna Life Insurance and Annuity Company (Aetna), and The Vanguard Group were approved by the Arizona Board of Regents. Benefits under these plans depend solely on the contributed amounts and the returns earned on the investment of those contributions. Contributions made by employees vest immediately and University contributions vest no later than after five years of full-time employment. Employee and University contributions and associated returns earned on investments may be withdrawn starting upon termination of employment, death, or retirement. The distribution of employee contributions and associated investment earnings are made in accordance with the employee's contract with the applicable insurance and annuity company. University contributions and associated investment earnings must be distributed to the employee in the form of an annuity paid over the employee's life.

Funding Policy. The Arizona State Legislature establishes and may amend active plan members' and the University's contribution rates. For the year ended June 30, 2003, plan members and the University were each required by statute to contribute an amount equal to 7.00% of an employee's compensation. Contributions to these plans for year ended June 30, 2003, were as follows (Dollars in Thousands):

	Contributions Rates (Each)	University Contributions	Employee Contributions	Total Contributions
TIAA/CREF	7%	$ 9,566	$ 9,566	$ 19,132
VALIC	7%	1,641	1,641	3,282
Fidelity	7%	1,423	1,423	2,846
Aetna	7%	290	290	580
Vanguard	7%	395	395	790

Note K - Other Matters

Pursuant to A.R.S. § 41-621, the University participates in a self-insurance program administered by the State of Arizona, Department of Administration, Risk Management Section. The State's Risk Management Program covers the University, subject to certain deductibles, for risks of loss related to such situations as theft, damage and destruction of property, buildings, and equipment; errors and omissions; injuries to employees; natural disasters; and liability for acts or omissions of any nature while acting in authorized governmental or proprietary capacities and in the course and scope of employment or authorization, except as prescribed in A.R.S. § 41-621. Loss risks not covered by the Risk Management Section and where the University has no insurance coverage are losses arising from contractual breaches and losses that arise out of and are directly attributable to an act or omission determined by a court to be a felony. From time to time, various claims and lawsuits associated with the normal conduct of University business are pending or may arise against the University. In the opinion of University management, any losses from the resolution of any pending claims or litigation not covered by the Risk Management Section should not have a material effect on the University financial statements taken as a whole. Also, in accordance with the disclosure requirements of GASB Statement No. 10, we note that judgments and claims not covered by the Risk Management Section during the three years ended June 30, 2003, have not been material to the University's financial statements taken as a whole.

In November 2000, the Arizona Cardinals NFL football team (the "Cardinals") requested an administrative review of its rights pursuant to its license to use the University's Sun Devil Stadium, claiming that the Cardinals had the right to approve any new signage at Sun Devil Stadium and that the University, by installing a new matrix videoboard and permanent advertising panels without the Cardinals' express approval, had violated the Cardinals' license. This review was resolved in favor of the University, and the Cardinals appealed. In April 2001, the then-president of the University referred the matter to the American Arbitration Association for final decision.

The arbitration was divided into two phases: 1) liability, and 2) remedy. During the liability phase, the arbitrator found in favor of the Cardinals. The parties are in the remedy phase now. The Cardinals' have asserted several theories, pursuant to which the maximum damages total $12.6 million. The University intends to vigorously defend itself against the Cardinals' damage claims. The University cannot predict the outcome of this matter at this time, however, the University believes that any damages that may be awarded will be significantly less than the amounts claimed by the Cardinals, and, in any event, will not materially and adversely impact the financial position of the University.

Federal grants provided to the University are subject to review and audit by Federal agencies. In the opinion of the University, any adjustments or repayments which may be required would not be material to the overall financial condition of the University.

The University has, or is in the process of entering into several privatized/third party arrangements for on-campus student housing and campus energy management where an independent management company is responsible for providing services to the University and/or students served by the University. In conjunction with these privatized arrangements, the independent management companies, with the approval and assistance of the University, have, or are in the process of, obtaining tax-exempt financings in order to maximize the overall financial benefits to the University and its students. As of June 30, 2003, independent management companies through separately incorporated non-profit entities formed by the independent companies to do the tax-exempt financings had completed four tax-exempt financings. The University is not legally responsible for repayment of the tax-exempt debt, and there is no pledge or guarantee by the University for repayment of the debt. As of June 30, 2003, there were $79.1 million of bonds outstanding for these four privatized arrangements with approximately $14 million of financings for another privatized arrangement in process. Upon final principal repayment of the financings, title to the student housing and energy management equipment effectively transfers to the University. In addition to the privatized and third party financings existing as of June 30, 2003 or in process as of this date, the possibility exists for several more third party financings to occur during fiscal 2004, totaling around $100 million.

Subsequent to June 30, 2003, the University received approval from the Arizona Board of Regents to enter into a lease with ASUF, LLC, an Arizona limited liability company to be formed by the ASU Foundation. The University will lease a portion of the project, approximately 90,000 square feet of office space and the related parking structure. The lease payments will begin during fiscal 2005, after construction is completed and will be approximately $2.4 million per year for approximately thirty years.

Also subsequent to June 30, 2003, the University issued $103 million of variable rate system revenue bonds with a final maturity of 2034 for various projects, including Arizona Biodesign Institute Phase I.

Effective July 1, 2003, the capitalization thresholds for equipment increased to $5,000, and the capital threshold for renovations to buildings, infrastructure, and land improvements that significantly increase the value or extend the useful life of structures increased to $100,000.

Arizona State University

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