

Financial Report

2011-2012



NORTHERN ARIZONA UNIVERSITY

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This financial report is compiled and issued by the Associate Vice President for Financial Services/Comptroller's Office Northern Arizona University P.O. Box 4069 Flagstaff, AZ 86011-4069

This report is also available online at home.nau.edu/comptr

UNIVERSITY ADMINISTRATION As of June 30, 2012

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Executive Vice President

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Senior Vice President for Enrollment
Management and Student Affairs

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Vice President for Finance
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**The Honorable
John Huppenthal**
Arizona Superintendent
of Public Instruction



INDEPENDENT AUDITORS' REPORT



DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

MELANIE M. CHESNEY
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 the business-type activities and aggregate discretely presented component units of Northern Arizona University as of and for the year ended June 30, 2012, as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the aggregate discretely presented component units. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the aggregate discretely presented component units, is based solely on the reports of the other auditors.

We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The financial statements of the aggregate discretely presented component units were not audited by the other auditors in accordance with *Government Auditing Standards*. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of the other auditors provide a reasonable basis for our opinions.

As described in Note 1, the University's financial statements are intended to present the financial position, and the changes in financial position and, where applicable, cash flows of only those portions of the business-type activities, major fund, and aggregate discretely presented component units of the State of Arizona that are attributable to the University. They do not purport to, and do not, present fairly the financial position of the State of Arizona as of June 30, 2012, and the changes in financial position and, where applicable, cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

INDEPENDENT AUDITORS' REPORT

In our opinion, based on our audit and the reports of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and aggregate discretely presented component units of Northern Arizona University as of June 30, 2012, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in conformity with U.S. generally accepted accounting principles.

Our audit was conducted for the purpose of forming opinions on the University's financial statements. The Management's Discussion and Analysis is presented for purposes of additional analysis and is not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

In accordance with *Government Auditing Standards*, we will also issue our report on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters at a future date. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Debbie Davenport
Auditor General

October 12, 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS

The discussion and analysis of Northern Arizona University's financial statements provides an overview of the University's financial activities for the year ended June 30, 2012. Management has prepared the financial statements and the accompanying note disclosures along with the discussion and analysis. Responsibility for the completeness and fairness of this information rests with the University's management.

USING THIS FINANCIAL REPORT

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

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

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

In accordance with Governmental Accounting Standards Board (GASB) Statement No. 39, *Determining Whether Certain Organizations Are Component Units*, the University reports as a component unit those organizations that raise and hold economic resources for the direct benefit of the University or its constituents.

Based on GASB 39, the University identified two component units, the Northern Arizona University Foundation (Foundation), and the Northern Arizona Capital Facilities Finance Corporation (NACFFC).

Information on the component units can be found in this report in the component units' Statement of Financial Position and Statement of Activities, as well as Note 8.

The Management's Discussion and Analysis focuses only on the University and does not address the component units.

FINANCIAL HIGHLIGHTS

- Total net assets increased \$15.1 million, 3.6 percent from July 1, 2011 to June 30, 2012 based on total sources of funds of \$442.6 million and \$427.5 million of uses.
- Total sources of revenues decreased by \$13.0 million or 2.8 percent while total uses of funds increased by \$21.0 million or 5.2 percent.
- State and capital appropriations decreased \$24.9 million from the prior year, an 18.5 percent reduction.
- Student tuition and fees increased 7.2 percent from the previous year or about \$10.6 million.
- Government grants and contracts decreased \$3.8 million, a 4.7 percent reduction.
- Private gifts, grants and contracts increased \$3.0 million, a 32.3 percent increase.
- Investment income decreased \$300 thousand from the previous fiscal year, a 10.2 percent reduction.
- Auxiliary enterprise revenues decreased by \$1.4 million, or 2.9 percent.
- The University share of state sales tax revenue remained essentially the same as the previous year, with a slight .3 percent reduction.

MANAGEMENT'S DISCUSSION AND ANALYSIS

STATEMENT OF NET ASSETS

The Statement of Net Assets presents the financial position of the University at the end of the fiscal year and includes all assets and liabilities of the University. A summarized comparison of the University's assets, liabilities, and net assets at June 30, 2012 and 2011 (in thousands), is as follows:

	2012	2011
Current assets	\$ 186,913	\$ 227,942
Noncurrent assets:		
Cash, cash equivalents, investments, and student loans receivable	85,607	80,510
Endowment investments	19,169	18,296
Capital assets – net of accumulated depreciation	670,710	618,674
Other noncurrent assets	<u>3,642</u>	<u>365</u>
Total noncurrent assets	<u>779,128</u>	<u>717,845</u>
Total assets	<u>966,041</u>	<u>945,787</u>
Long-term liabilities	<u>485,820</u>	<u>466,547</u>
Other liabilities	<u>47,191</u>	<u>61,343</u>
Total liabilities	<u>533,011</u>	<u>527,890</u>
Net assets	<u>\$ 433,030</u>	<u>\$ 417,897</u>

A review of NAU's Statement of Net Assets at June 30, 2012 and 2011 shows that the University's financial position continues to improve with an increase in net assets of \$15.1 million.

Current assets consist primarily of cash and investments, state appropriation receivable, government grants and contracts receivable, and accounts receivable. Current assets are generally considered to be convertible to cash within one year. Current assets decreased overall by \$41.0 million over the prior fiscal year. The change was the result of a decrease in cash and investments of \$35.7 million, a \$4.3 million decrease in receivables and a decrease of \$1.0 million in other assets.

Noncurrent assets increased \$61.3 million over the prior year due to an increase of \$52.0 million in capital assets, a \$6.0 million increase in cash and investments, and a \$3.3 million increase in other noncurrent assets.

Capital assets, net of accumulated depreciation, increased \$52.0 million over the prior fiscal year as the University continued with major capital improvement projects, including the ongoing construction of the Health and Learning Center and other capital facilities and infrastructure projects. The changes in capital assets are discussed in more detail in the

Capital Assets and Debt Administration section.

The net increase of \$6.0 million in noncurrent cash and investments was due to increases in noncurrent investments of \$20.3 million and endowment investments of \$9 million offset by a \$15.0 million decrease in cash and cash equivalents held by trustee.

Long-term liabilities increased by \$19.3 million over the prior fiscal year. The increase is mainly attributable to the increase of long-term debt, which is discussed further in the Capital Assets and Debt Administration section.

Current liabilities, which include accounts payable, accrued expenses, and deferred revenue, decreased by \$13.1 million over the prior fiscal year. The decrease is mainly attributable to a decrease in accounts payable of \$6.3 million (primarily high construction payables the prior year), a \$6.0 million decrease in accrued payroll and employee benefits and a \$.8 million decrease in other current liabilities.

MANAGEMENT'S DISCUSSION AND ANALYSIS

NET ASSETS

A summarized comparison of the University's net assets at June 30, 2012 and 2011 (in thousands), is as follows:

	2012	2011
Invested in capital assets, net of related debt	\$ 218,676	\$ 200,274
Restricted:		
Nonexpendable	19,517	19,047
Expendable	17,571	16,366
Unrestricted	177,266	182,210
Total net assets	<u>\$ 433,030</u>	<u>\$ 417,897</u>

Invested in capital assets, net of related debt, increased \$18.4 million, resulting from a \$52.0 million increase in capital assets (net of depreciation) offset by \$33.6 million of related debt. Net assets at June 30, 2012 increased in total by \$15.1 million or 3.6 percent from 2011. This is a result of total combined sources of \$442.6 million and total uses of \$427.5 million. The University continues to manage operating expenses, resulting in positive net asset growth.

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

The Statement of Revenues, Expenses, and Changes in Net Assets presents the operating results of the University, as well as the nonoperating revenues and expenses. Annual state appropriations, while budgeted for operations, are considered nonoperating revenues according to U.S. generally accepted accounting principles. See the table of Combined Sources and Uses of Funds on pages 12-13 for an overview of the composition of revenues and expenses (sources and uses). A summarized comparison of the University's revenues, expenses, and changes in net assets for the years ended June 30, 2012 and 2011 (in thousands), is as follows:

	2012	2011
Operating revenues:		
Tuition and fees, net of scholarship allowances	\$ 157,865	\$ 147,224
Grants and contracts	20,580	27,622
Auxiliary enterprises	45,806	47,172
Other	17,189	10,603
Total operating revenues	<u>241,440</u>	<u>232,621</u>
Nonoperating revenues:		
State appropriations	103,670	128,528
Share of state sales tax - technology and research initiative funding	11,157	11,189
Grants and gifts	70,567	64,327
Federal fiscal stabilization funds		292
Investment income	2,678	2,983
Other nonoperating revenues	5,909	6,341
Total nonoperating revenues	<u>193,981</u>	<u>213,660</u>
Total revenues	<u>435,421</u>	<u>446,281</u>
Operating expenses:		
Educational and general	338,668	333,465
Auxiliary enterprises	37,035	34,351
Depreciation	27,260	21,990
Total operating expenses	<u>402,963</u>	<u>389,806</u>
Nonoperating expenses:		
Interest expense on capital asset related debt	22,852	14,023
Other nonoperating expenses	1,680	2,699
Total nonoperating expenses	<u>24,532</u>	<u>16,722</u>
Total expenses	<u>427,495</u>	<u>406,528</u>
Increase before capital appropriations, capital grants and gifts and endowment additions	<u>7,926</u>	<u>39,753</u>
Capital appropriations, capital grants and gifts and endowment additions	<u>7,207</u>	<u>9,313</u>
Increase in net assets	<u>\$ 15,133</u>	<u>\$ 49,066</u>

MANAGEMENT'S DISCUSSION AND ANALYSIS

REVENUES ANALYSIS

The Statement of Revenues, Expenses, and Changes in Net Assets presents the University's operating, nonoperating, and capital related financial activity during the fiscal year. Tuition and fees and state appropriations continue to be the major funding sources for operations related to educational purposes. Operating revenues are provided as a result of the University's ongoing operations such as tuition and fees, government grants and contracts, and auxiliary enterprises. Operating revenues (which does not include state appropriations) increased by \$8.8 million or 3.8 percent from fiscal year 2011. Tuition and fees revenue increased \$10.6 million or 7.2 percent, due to higher student enrollment coupled with an increase in board approved tuition rates. Operating grants and contracts revenue decreased \$7.0 million or 25.5 percent due to ARRA and other research projects closing out and state grant activity being lower than previous years. Auxiliary enterprise revenues decreased by \$1.4 million, a 2.9 percent decrease.

Nonoperating revenues decreased overall by \$19.7 million or 9.2 percent. State and capital appropriations decreased \$24.9 million or 18.5 percent from the prior fiscal year. Nonoperating grants and gifts increased \$6.2 million or 9.7 percent largely due to Pell Grants increasing \$2.6 million and gifts increasing \$2.5 million from the prior year. The share of state sales taxes - technology and research initiated funding (TRIF) revenues declined only slightly over the 2011 fiscal year. Investment income totaled \$2.7 million in 2012 compared to \$3.0 million in 2011. Other nonoperating revenue increased by \$400 thousand or 6.8 percent.

EXPENSES ANALYSIS

Overall, operating expenses increased \$13.2 million.

Educational and general expenses, which continued to account for a majority of the operating expenses, increased \$5.2 million or 1.6 percent. Within educational and general expenses, instruction increased \$2.2 million or 1.6 percent. Student services increased \$3.3 million or 9.9 percent, reflecting investments made in technology and support services to support higher enrollment levels. Institutional support increased \$0.9 million or 2.1 percent. Operation and maintenance of plant increased \$4.4 million or 25.0 percent, largely due to furniture and equipment expenditures in the new Health and Learning Center building. Scholarships and fellowships decreased \$3.6 million or 12.5 percent, due to more financial aid resources being directly applied against tuition as tuition rates rise.

Depreciation expense increased by \$5.3 million or 24.0 percent, as the University constructed new buildings and made improvements and renovations. Depreciation expense is expected to continue to increase as the University continues to construct new buildings and renovate older ones.

Nonoperating expenses increased by \$7.8 million or 46.7 percent, including increased interest expense of \$8.8 million, decreased loss on disposal of capital assets of \$1.1 million and a \$1 million increase in other nonoperating expenses.

EXPENSES - BY FUNCTIONAL CLASSIFICATION

A comparative summary of the University's expenses by functional classification for the years ended June 30, 2012 and 2011, is as follows:

	2012	2011
Operating:		
Instruction	\$ 134,271,789	\$ 132,116,474
Research	21,765,938	23,178,173
Public service	28,352,445	27,300,421
Academic support	28,857,958	30,320,981
Student services	36,273,676	32,994,864
Institutional support	41,788,624	40,909,099
Operation and maintenance of plant	21,781,043	17,426,421
Scholarships and fellowships	<u>25,576,141</u>	<u>29,218,295</u>
Total educational and general expenses	<u>338,667,614</u>	<u>333,464,728</u>
Auxiliary enterprises	37,035,147	34,351,311
Depreciation	<u>27,260,505</u>	<u>21,989,831</u>
Total operating expenses	<u>402,963,266</u>	<u>389,805,870</u>
Nonoperating:		
Interest and other	<u>24,531,739</u>	<u>16,721,883</u>
Total expenses	<u>\$ 427,495,005</u>	<u>\$ 406,527,753</u>

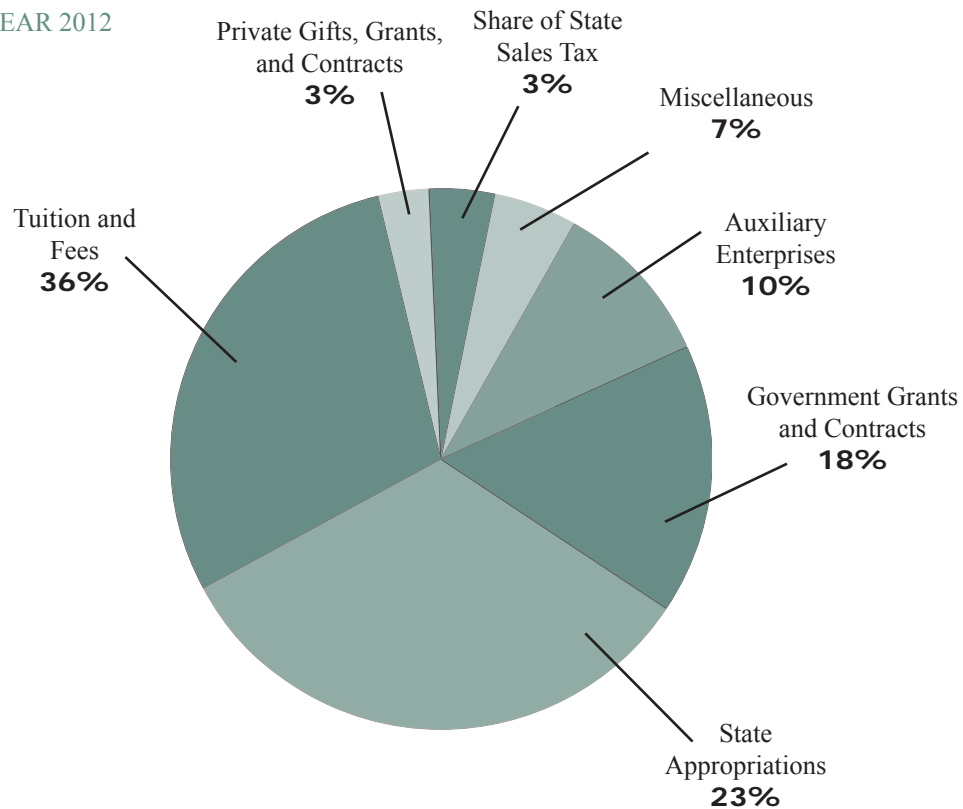
MANAGEMENT'S DISCUSSION AND ANALYSIS

EXPENSES - BY NATURAL CLASSIFICATION

In addition to their functional (program) classification, it is also informative to review operating expenses by their natural (object) classification. A comparative summary of the University's expenses by natural classification for the years ended June 30, 2012 and 2011, is as follows:

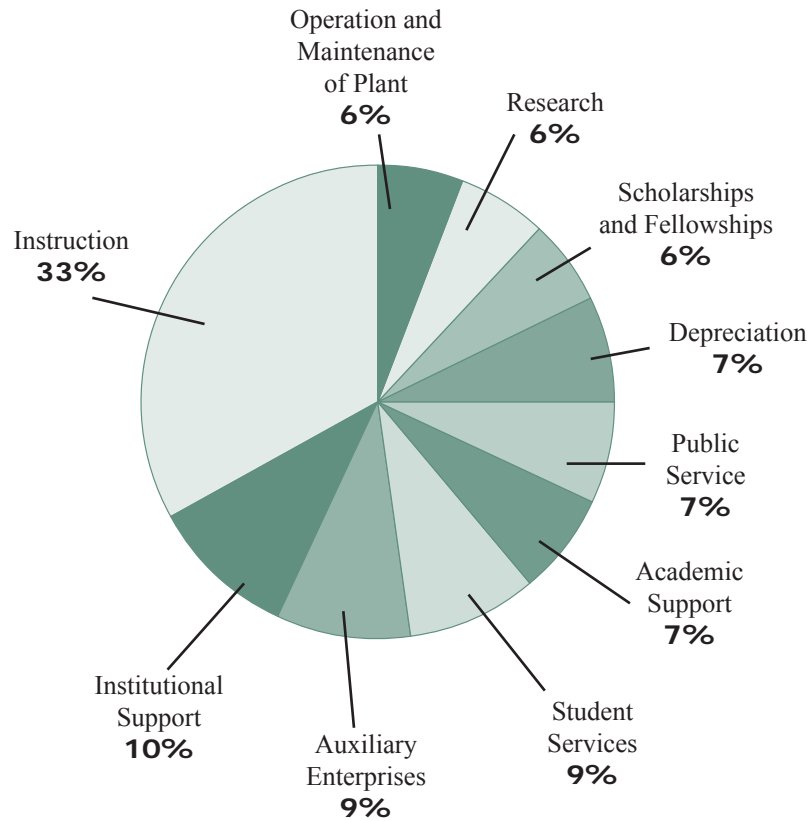
	2012	2011
Operating:		
Personal services and benefits	\$ 254,396,049	\$ 248,042,454
Operations	95,730,571	90,555,290
Scholarships	25,576,141	29,218,295
Depreciation	<u>27,260,505</u>	<u>21,989,831</u>
Total operating	<u>402,963,266</u>	<u>389,805,870</u>
Nonoperating:		
Interest and other	<u>24,531,739</u>	<u>16,721,883</u>
Total expenses	<u>\$ 427,495,005</u>	<u>\$ 406,527,753</u>

TOTAL SOURCES OF FUNDS FISCAL YEAR 2012

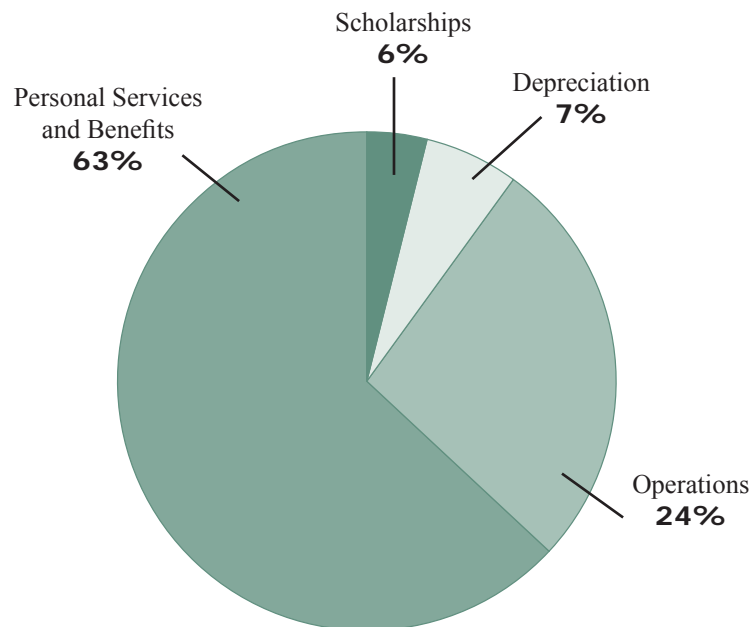


MANAGEMENT'S DISCUSSION AND ANALYSIS

OPERATING EXPENSES FUNCTIONAL CLASSIFICATION FISCAL YEAR 2012



OPERATING EXPENSES NATURAL CLASSIFICATION FISCAL YEAR 2012



MANAGEMENT'S DISCUSSION AND ANALYSIS

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets at June 30, 2012

At June 30, 2012, the University had \$670.7 million invested in capital assets. During the year the University added \$79.5 million in new capital assets and retired \$8.6 million of obsolete assets. Accumulated depreciation increased by \$18.9 million. Details of capital assets at June 30, 2012 and 2011 are as follows:

	2012	2011
Land	\$ 6,851,409	\$ 6,685,920
Construction in progress	40,253,220	168,447,322
Infrastructure	130,766,732	94,745,027
Buildings and improvements	727,121,836	561,680,718
Equipment	61,808,997	63,810,379
Library books and media	46,799,768	47,251,328
Accumulated depreciation	(342,892,133)	(323,946,621)
Total capital assets	\$ 670,709,829	\$ 618,674,073

Outstanding Debt at June 30, 2012

At June 30, 2012, the University had \$482.0 million in outstanding bonds, certificates of participation, other long-term obligations, and capital leases, an increase of approximately \$18.3 million, or 4 percent from fiscal year 2011. This is due to the issuance of \$36.4 million system revenue bonds and other long-term obligations and principal reductions of \$18.1 million.

The table below summarizes the University's outstanding debt from fiscal years 2012 and 2011.

	2012	2011
System revenue bonds	\$ 353,820,000	\$ 335,700,000
Capital leases	46,010,000	46,925,000
Certificates of participation	69,540,000	80,835,000
Other long-term obligations	12,642,400	291,847
Subtotal	482,012,400	463,751,847
Less deferred amount on refunding	(1,325,246)	(1,454,915)
Plus bonds premium	5,132,296	4,249,579
Total	\$ 485,819,450	\$ 466,546,511

Significant capital additions completed or in progress, and the resources that funded their acquisitions for fiscal year 2012 were:

- Parking Structure, \$16.4 million, bond proceeds
- Health and Learning Center, \$7.2 million, bond proceeds
- Skydome renovation, \$7.2 million, bond proceeds
- Ardrey Auditorium renovation, \$4.2 million, unrestricted net assets
- Laboratory renovation, \$3.8 million, bond proceeds
- Native American Center, \$2.4 million, donation/unrestricted net assets
- Liberal Arts renovation, \$2.1 million, bond proceeds

Projects planned to commence in fiscal year 2013, funded from system revenue bonds and unrestricted net assets include:

- Science and Health Building
- NORESKO Energy Savings Project

In accordance with Arizona Revised Statutes § 15-1670, NAU receives \$5.9 million in state appropriations annually for lease-purchase capital financing of research infrastructure projects.

MANAGEMENT'S DISCUSSION AND ANALYSIS

ECONOMIC OUTLOOK

Arizona and the nation recorded moderate economic improvement in 2011-12. Some observers are looking for a return to the incredible economic prosperity recorded in 2004 through 2007. Those experiences are unlikely to be repeated in the next decade. But recovery is underway at a slow and measured pace. For example, in July 2011 the national unemployment rate was 9.1% and a year later stands at 8.3%. In Arizona, a similar and slightly better improvement has been recorded, with the statewide unemployment rate falling from 9.6% in July 2011 to 8.3% in July 2012. This occurred with job creation growing by 2.4%.

That is not to say that there still is not substantial economic weaknesses at the national and state levels. Arizona lost nearly a quarter of a million jobs, with construction probably being the hardest hit. As recently as 2010, Arizona ranked 49th in the nation in job creation. By 2012, the state's rank rose to 4th with the addition of about 47,000 new jobs. At this pace, it will take a number of years to recover the jobs that were lost.

The news is improving in other areas as well. The state's population in 2011 is up 0.6% which is still far below historical levels but is an improvement over the prior two years. Some of that is due to improving home prices and new home construction. After many quarters of decline, the Arizona house price index was up 2.6% in the second quarter of 2012 and the number of housing permits were up over 25% in July 2012. But much of that improvement was due to the extraordinarily low number issued previously.

Arizona tax collections saw recovery in 2011-12, though growth has not returned to levels seen in the heady years of FY 2004 through FY 2006. And it is very unlikely that those levels will be repeated in the foreseeable future. Total sales tax collections, the largest source of revenue to the state, were up 5.9% in FY 2012. This is the most rapid increase the state has seen since FY 2006 when sales tax collections grew an unprecedented 16.7%. After the incredible double digit losses in FY 2009 and FY 2010, this is actually a good year for collections. In fact, it is over twice the average growth rate of FY 2001 through FY 2011. A combination of factors lead to this growth. Car sales have seen substantial strength, new construction and renovation is recovering and tourism activity has been good. Though it is unlikely that there will be much additional growth in the years ahead, Arizona retail sales should bring growth rates of 5.0-6.5% for the next few years.

The news for individual income tax collections in FY 2012 was not quite as good. After an unexpected good year in FY 2011 when individual tax collections were up 18.0% in Arizona, the state recorded a respectable 7.7% growth rate in FY 2012. Since FY 2001, the state has averaged 4.4% growth in individual income tax collections. Much of the unexpected growth in FY 2011 had to do with capital gains, individual business income and general economic recovery from the 24.5% loss in FY 2009. Here too, the outlook is for growth in the next few fiscal years to range from 5.7 to 8.6%. Though not spectacular, this would be above average for the state.

Corporate income tax collections are the smallest of the big three tax categories and are the most volatile. In the last twelve years, corporate tax collections have increased as much as 42.1% in FY 2005 or declined as much as 28.5% in FY 2002. At 16.8% growth in FY 2012, this was a significant decline from the prior year's growth of 38.2%. But it too is far above the average of the last eleven years. This category of tax collections is difficult to forecast for two reasons. First, it is very volatile. Second, a number of statutory provisions decreasing a corporation's tax liability may be implemented in the next few years. The magnitude of the impact is somewhat unknown, but generally is considered significant. To be safe, growth rates in this group can be expected to be a moderate 3-5% annually.

Since Northern Arizona University is subject to the same economic variables that affect other financial entities, it is not possible to predict future outcomes. Management is well aware of the challenges ahead and is working diligently to continue to provide quality education and research activities to the state of Arizona and to the nation as a whole.

MANAGEMENT'S DISCUSSION AND ANALYSIS

COMBINED SOURCES AND USES OF FUNDS For the Year Ended June 30, 2012

SOURCES

Tuition and Fees, Net of Scholarship Allowances 35.7% Net of \$63,636,288 for scholarship allowances.	\$ 157,864,535
State Appropriations 23.4% Includes legislative appropriations from State of Arizona general revenue for current operations of the University and \$1,317,900 for financial aid.	\$ 103,669,800
Government Grants and Contracts 17.8% Includes revenues of \$69,621,012 from federal grants and contracts, \$3,359,003 from state grants and contracts, and \$5,681,665 from local government grants and contracts.	\$ 78,661,680
Auxiliary Enterprises 10.4% Net of \$4,072,348 for scholarship allowances. Operations of substantially self-supporting activities such as student housing, student unions, and intercollegiate athletics.	\$ 45,805,525
Other Sources 6.8% Includes \$851,856 additions to permanent endowments, \$455,398 capital grants and gifts, \$5,900,000 capital appropriations, \$17,189,830 other operating and \$5,909,112 nonoperating miscellaneous revenues.	\$ 30,306,196
Private Gifts, Grants, and Contracts 2.8% Includes gifts, grants, and contracts for scholarships, endowments, and plant facility additions.	\$ 12,485,648
Share of State Sales Tax 2.5% University's share of state sales tax collections from Proposition 301.	\$ 11,157,018
Investment Income 0.6% Net earnings and losses from short-term investments of funds not necessary for immediate operating expenses and long-term investment of endowment and bond-retirement sinking funds.	\$ 2,677,977
Total Sources	<u><u>\$ 442,628,379</u></u>

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

MANAGEMENT'S DISCUSSION AND ANALYSIS

COMBINED SOURCES AND USES OF FUNDS For the Year Ended June 30, 2012

USES

Instruction and Academic Support

38.1%

\$ 163,129,747

Instruction, totaling \$134,271,789, includes expenses of academic departments and other organizational units for undergraduate and graduate courses, and for occupational or technical instruction, including academic year, summer sessions, and continuing education. Academic support, totaling \$28,857,958, includes libraries, audio-visual services, and academic administration.

Student Services and Institutional Support

18.3%

\$ 78,062,300

Student services, totaling \$36,273,676, includes areas such as admissions, registrar, minority services, counseling, placement, student aid administration, and health services. Institutional support, totaling \$41,788,624, includes executive management, financial operations, computing support, human resource services, security, and University relations.

Research and Public Service

11.7%

\$ 50,118,383

Research, totaling \$21,765,938, consists of activities in which the primary objective is the discovery or application of knowledge that may be sponsored by external agencies or separately budgeted by organizational units within the University. Public service, totaling \$28,352,445, includes activities that make available to the general public the benefits of the instructional or research activities and include local school consortiums and public broadcasting.

Auxiliary Enterprises

8.7%

\$ 37,035,147

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

Depreciation

6.4%

\$ 27,260,505

Depreciation expense of capital assets over their useful lives.

Scholarships and Fellowships

6.0%

\$ 25,576,141

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

Other Uses

5.7%

\$ 24,531,739

Other uses include \$22,851,704 in interest expense on capital asset related debt, a \$144,124 net loss on disposal of capital assets, and other nonoperating expenses of \$1,535,911.

Operation and Maintenance of Plant

5.1%

\$ 21,781,043

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

Total Uses

\$ 427,495,005

FINANCIAL STATEMENTS

STATEMENT OF NET ASSETS June 30, 2012

ASSETS

Current assets:

Cash and cash equivalents	\$ 43,747,655
Investments	80,650,990
Receivables, net of allowance for uncollectibles:	
Accounts receivable	16,882,389
Accrued interest	691,016
Endowment	31,585
Government grants and contracts	12,306,018
Student loans, current portion	987,157
State appropriation receivable	30,494,800
Other assets	784,086
Inventories	337,700
Total current assets	<u>\$ 186,913,396</u>

Noncurrent assets:

Restricted cash and cash equivalents held by trustee for capital projects	\$ 35,255,736
Investments	45,823,307
Student loans receivable, net of allowance	4,527,922
Endowment investments	19,168,554
Other noncurrent assets	3,641,873
Capital assets, not being depreciated	47,104,629
Depreciable capital assets, net of depreciation	623,605,200
Total noncurrent assets	<u>\$ 779,127,221</u>

Total assets

\$ 966,040,617

LIABILITIES

Current liabilities:

Accounts payable	\$ 14,447,095
Accrued payroll and employee benefits	5,603,434
Interest payable	4,160,444
Deferred revenue	11,997,107
Accrued compensated absences	5,265,980
Deposits held in custody for others	4,426,957
Current portion of long-term debt funded by:	
University operating revenues	7,872,208
State appropriations and share of state sales tax	2,670,000
Total current liabilities	<u>\$ 56,443,225</u>

Noncurrent liabilities:

Deposits held in custody for others	\$ 1,290,286
Long-term debt funded by:	
University operating revenues	356,579,242
State appropriations, share of state sales tax, and lottery revenue	118,698,000
Total noncurrent liabilities	<u>\$ 476,567,528</u>

Total liabilities

\$ 533,010,753

NET ASSETS

Invested in capital assets, net of related debt	\$ 218,676,478
Restricted:	
Nonexpendable:	
Scholarships and fellowships	12,875,493
Student loans	6,641,026
Expendable:	
Scholarships and fellowships	6,454,230
Academic department uses	11,116,652
Unrestricted	177,265,985
Total net assets	<u>\$ 433,029,864</u>

See Notes to Financial Statements

BUSINESS-TYPE ACTIVITIES

FINANCIAL STATEMENTS

STATEMENT OF FINANCIAL POSITION - Component Units June 30, 2012

	NAU FOUNDATION	NACFFC	TOTAL
ASSETS			
Cash and cash equivalents	\$ 2,318,264	\$ 12,331	\$ 2,330,595
Investments	89,108,814		89,108,814
Accounts receivable	126,167	178,739	304,906
Prepaid expense		7,599	7,599
Unconditional promises to give (net of allowance)	6,170,216		6,170,216
Assets held by trustee	3,062,857	8	3,062,865
Property, plant and equipment, net of depreciation	5,376,694		5,376,694
Net investment in sales-type lease	2,892,782	46,010,000	48,902,782
Educational broadcasting system licenses	3,499,864		3,499,864
Other assets	5,573,523	1,307,408	6,880,931
TOTAL ASSETS	<u>\$ 118,129,181</u>	<u>\$ 47,516,085</u>	<u>\$ 165,645,266</u>
LIABILITIES			
Accounts payable and accrued liabilities	\$ 2,353,338	\$ 176,070	\$ 2,529,408
Bonds payable		45,982,820	45,982,820
Assets held in custody for others	20,083,193		20,083,193
Deferred revenue	5,452,290	22,599	5,474,889
Other liabilities	1,345,818		1,345,818
Total liabilities	<u>\$ 29,234,639</u>	<u>\$ 46,181,489</u>	<u>\$ 75,416,128</u>
NET ASSETS			
Unrestricted	\$ 29,469,949	\$ 1,334,596	\$ 30,804,545
Temporarily restricted	18,356,443		18,356,443
Permanently restricted	41,068,150		41,068,150
Total net assets	<u>\$ 88,894,542</u>	<u>\$ 1,334,596</u>	<u>\$ 90,229,138</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 118,129,181</u>	<u>\$ 47,516,085</u>	<u>\$ 165,645,266</u>

See Notes to Financial Statements

FINANCIAL STATEMENTS

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS For the Year Ended June 30, 2012

REVENUES

	Business-Type Activities
Operating Revenues	
Tuition and fees, net of scholarship allowances of \$63,636,288	\$ 157,864,535
Government grants and contracts	18,461,626
Private grants and contracts	2,118,681
Auxiliary enterprises	
Residence life, net of scholarship allowances of \$4,072,348	29,533,754
Other auxiliaries	16,271,771
Other	17,189,830
Total operating revenues	<u>\$ 241,440,197</u>

EXPENSES

Operating Expenses	
Educational and general:	
Instruction	\$ 134,271,789
Research	21,765,938
Public service	28,352,445
Academic support	28,857,958
Student services	36,273,676
Institutional support	41,788,624
Operation and maintenance of plant	21,781,043
Scholarships and fellowships	25,576,141
Auxiliary enterprises	37,035,147
Depreciation	27,260,505
Total operating expenses	<u>\$ 402,963,266</u>
Operating loss	<u>\$ (161,523,069)</u>

NONOPERATING REVENUES AND (EXPENSES)

State appropriations	\$ 103,669,800
Share of state sales tax - technology and research initiative funding	11,157,018
Government grants	60,200,054
Private gifts and grants	10,366,967
Net investment income	2,677,977
Interest expense on capital asset related debt	(22,851,704)
Loss on disposal of capital assets	(144,124)
Other nonoperating revenues, net	4,373,201
Total nonoperating revenues and expenses	<u>\$ 169,449,189</u>

Income before other revenues, expenses, gains or losses	<u>\$ 7,926,120</u>
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Capital appropriations	\$ 5,900,000
Capital grants and gifts	455,398
Additions to permanent endowments	<u>851,586</u>

Increase in net assets	<u>\$ 15,133,104</u>
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NET ASSETS

Total net assets, July 1, 2011	\$ 417,896,760
Total net assets, June 30, 2012	<u>\$ 433,029,864</u>

See Notes to Financial Statements

FINANCIAL STATEMENTS

STATEMENT OF ACTIVITIES - COMPONENT UNITS For the Year Ended June 30, 2012

	NAU FOUNDATION	NACFFC	TOTAL
CHANGES IN UNRESTRICTED NET ASSETS			
Unrestricted support	\$ 106,939		\$ 106,939
Investment earnings (loss)	(300,081)	\$ 2,143,392	1,843,311
Licensing revenue	1,280,914		1,280,914
Rent		34,525	34,525
Other	946,846		946,846
Total unrestricted support	<u>\$ 2,034,618</u>	<u>\$ 2,177,917</u>	<u>\$ 4,212,535</u>
Net assets released from restrictions	9,974,437		9,974,437
Total unrestricted revenues and support	<u>\$ 12,009,055</u>	<u>\$ 2,177,917</u>	<u>\$ 14,186,972</u>
Expenses:			
Scholarships	\$ 1,971,461		\$ 1,971,461
Operating	3,585,056	\$ 34,525	3,619,581
Interest		2,146,923	2,146,923
Educational purposes	4,158,263		4,158,263
Amortization and depreciation	1,648,093	60,282	1,708,375
Total expenses	<u>\$ 11,362,873</u>	<u>\$ 2,241,730</u>	<u>\$ 13,604,603</u>
Increase (decrease) in unrestricted net assets	<u>\$ 646,182</u>	<u>\$ (63,813)</u>	<u>\$ 582,369</u>
CHANGES IN TEMPORARILY RESTRICTED NET ASSETS			
Public contributions	\$ 5,986,802		\$ 5,986,802
Investment earnings (loss)	(530,439)		(530,439)
Other income changes	611,713		611,713
Net assets released from restrictions	(9,974,437)		(9,974,437)
Decrease in temporarily restricted net assets	<u>\$ (3,906,361)</u>	<u> </u>	<u>\$ (3,906,361)</u>
CHANGES IN PERMANENTLY RESTRICTED NET ASSETS			
Public contributions	\$ 1,812,172		\$ 1,812,172
Investment earnings	43,973		43,973
Other income changes	(14,931)		(14,931)
Increase in permanently restricted net assets	<u>\$ 1,841,214</u>	<u> </u>	<u>\$ 1,841,214</u>
INCREASE (DECREASE) IN NET ASSETS	<u>\$ (1,418,965)</u>	<u>\$ (63,813)</u>	<u>\$ (1,482,778)</u>
NET ASSETS, BEGINNING OF YEAR	<u>\$ 90,313,507</u>	<u>\$ 1,398,409</u>	<u>\$ 91,711,916</u>
NET ASSETS, END OF YEAR	<u>\$ 88,894,542</u>	<u>\$ 1,334,596</u>	<u>\$ 90,229,138</u>

See Notes to Financial Statements

FINANCIAL STATEMENTS

STATEMENT OF CASH FLOWS For the Year Ended June 30, 2012

Business-Type Activities

Cash flows from operating activities:	
Tuition and fees	\$ 150,863,628
Grants and contracts	21,559,247
Payments to suppliers and providers of goods and services	(102,018,485)
Payments for employee wages and benefits	(254,960,704)
Payments for scholarships and fellowships	(25,576,141)
Loans issued to students	(1,282,207)
Collection of loans to students	837,368
Auxiliary enterprise receipts:	
Residence halls	29,522,453
Other auxiliaries	21,381,178
Other receipts	12,121,679
Net cash used for operating activities	<u>\$ (147,551,984)</u>
Cash flows from noncapital financing activities:	
State appropriations	\$ 103,669,800
Share of state sales tax - technology and research initiative funding	11,157,018
Gifts and grants for other than capital purposes	70,567,022
Federal direct student lending received	161,818,557
Federal direct student lending disbursed	(162,813,386)
Funds held for others received	15,702,218
Funds held for others disbursed	(14,557,463)
Financial aid trust funds	851,586
Pgv'bcuj 'rtqxlf gf 'd{ 'bqpecr kcrnEpcpelpi 'c'evkslsgu	<u>\$ 186,395,352</u>
Cash flows from capital financing activities:	
Capital appropriations	\$ 5,900,000
Proceeds from issuance of capital debt	37,571,987
Build America Bonds - federal subsidy	5,768,231
Proceeds from sale of capital assets	27,266
Capital grants and gifts received	434,398
Purchases of capital assets	(79,446,651)
Principal paid on capital debt and leases	(18,114,736)
Interest paid on capital debt and leases	(23,121,751)
Pgv'bcuj 'wugf 'hqt 'c'cr kcrnEpcpelpi 'c'evkslsgu	<u>\$ (70,981,256)</u>
Cash flows from investing activities:	
Proceeds from sales and maturities of investments	\$ 74,507,178
Interest on investments	1,832,398
Purchase of investments	(110,874,786)
Net cash used for investing activities	<u>\$ (34,535,210)</u>
Net decrease in cash and cash equivalents	\$ (66,673,098)
Cash and cash equivalents - beginning of year	145,676,489
Cash and cash equivalents - end of year	<u>\$ 79,003,391</u>
Reconciliation of operating loss to net cash used for operating activities:	
Operating loss	\$ (161,523,069)
Adjustments to reconcile operating loss to net cash used for operating activities:	
Depreciation expense	27,260,505
Miscellaneous nonoperating expenses	(4,687,955)
Changes in assets and liabilities - cash increase (decrease) related to:	
Receivables:	
Accounts receivable	3,859,479
Government grants and contracts	1,182,194
Student loans receivables and accrued interest from student loans	(16,026)
Inventories	23,230
Other assets	1,024,550
Accounts payable	(6,605,581)
Accrued payroll and employee benefits	(5,984,931)
Deferred revenue	(2,273,285)
Accrued compensated absences	188,905
Net cash used for operating activities	<u>\$ (147,551,984)</u>

See Notes to Financial Statements

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

Note 1—Summary of Significant Accounting Policies

Financial Statement Presentation

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

Reporting Entity

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

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

NACFFC was incorporated in October 2001, as a legally separate not-for-profit corporation under the laws of the State of Arizona for the purpose of acquiring, developing, constructing, maintaining and operating student housing and other capital facilities and equipment for the use and benefit of the University's students.

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

For financial reporting purposes, the Foundation and the NACFFC follow the Financial Accounting Standards Board (FASB) statements for not-for-profit organizations. As such, certain revenue recognition criteria and presentation features are different from GASB revenue recognition criteria and presentation features. Accordingly, those financial statements have been reported on separate pages following the respective counterpart statements of the University. The Foundation and the NACFFC have a June 30 year end. Complete financial statements as originally presented for the Foundation and the NACFFC can be obtained from the Northern Arizona University Comptroller's Office, P.O. Box 4069, Flagstaff, AZ 86011.

During the year ended June 30, 2012, the Foundation distributed \$4.5 million to the University for restricted and unrestricted purposes.

Basis of Accounting

The University's financial statements are presented using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. State appropriations are recognized as revenue in the year in which the appropriation is first made available for use. Grants and donations are recognized as revenue as soon as all eligibility requirements imposed by the provider are met. All significant transactions resulting from internal activity have been eliminated.

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

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

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

The statement of revenues, expenses, and changes in net assets provides information about the University's financial activities during the year. Revenues and expenses are classified as either operating or nonoperating, and all changes in net assets are reported, including capital contributions and additions to endowments. Operating revenues and expenses are those that generally result from exchange transactions generated from providing instructional, research, public, and auxiliary services, which are consistent with the University's mission. Accordingly, revenues such as tuition and fees, sales and services of auxiliary enterprises and most government and nongovernment research grants and contracts are considered operating. Certain significant revenue streams relied upon for operations are recorded as nonoperating revenues, as defined by GASB Statement No. 35, including state appropriations, nonexchange grants, gifts, and investment income. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. Other expenses, such as interest expense on debt, are considered to be nonoperating expenses.

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

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

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

Cash and Cash Equivalents

The University considers all short-term, highly liquid investments with maturities of less than three months from the date of acquisition to be cash equivalents. Cash and investments held by trustee and Money Market Mutual Funds are also considered cash equivalents.

Investments

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

Receivables

Student loans and accounts receivable as of June 30, 2012, are reported less allowances for both estimated uncollectible amounts and collection costs of \$1,522,500 and \$5,030,750 respectively.

The fiscal year 2012 appropriation to Arizona Board of Regents for the support and maintenance of institutions under its jurisdiction was deferred in the amount of \$200 million to fiscal year 2013 with payment to be no later than October 1, 2012. Northern Arizona University's \$30,494,800 portion of the \$200 million deferred appropriation payment was recorded as a receivable in fiscal year 2012.

Inventories

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

Special Collections

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

Capital Assets

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

	Capitalization Threshold	Depreciation Method	Estimated Useful Life
Building improvements	\$5 thousand	Straight Line	20 years
Buildings	All	Straight Line	40 years
Infrastructure	All	Straight Line	20-40 years
Land	All	None	
Equipment			
Machinery, vehicles, and other equipment	\$5 thousand	Straight Line	5-15 years
Intangible assets:			
Computer software > \$10 million	\$10 million	Straight Line	10 years
Computer software < \$10 million	\$1 million	Straight Line	5 years
All other (1)	\$100 thousand	Straight Line	(1)
Library books and media	All	Straight Line	10 years

(1) Includes websites, non-software licenses and permits, patents, copyrights and trademarks, rights-of-way and easements, natural resource extraction rights and other intangible assets. In general, the estimated useful life is the shorter of the legal or the estimated useful life.

Compensated Absences

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

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

Investment Income

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

Scholarship Allowances

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

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

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

Note 2—Deposits and Investments

Arizona Revised Statutes (A.R.S.) § 15-1668 require that deposits of the University not covered by federal deposit insurance be secured by government bonds or by a safekeeping receipt of the institution accepting the deposit. Further, policy regarding deposits is provided by the Arizona Board of Regents (ABOR). Deposits can be made only at depository banks approved by the Board. A.R.S. and ABOR policies constitute the University's policy regarding custodial credit risk for deposits.

There is no statutory requirement that governs university investment activities. A.R.S. § 15-1625 gives the ABOR jurisdiction and control over the universities, and A.R.S. § 15-1626 allows ABOR to authorize the universities to adopt regulation, policies, rules, or measures as deemed necessary. ABOR investment policies require that the University invest its operating funds only in the State Treasurer's Local Government Investment Pool, collateralized time certificates of deposit and repurchase agreements, U.S. Treasury securities, and obligations of other agencies sponsored by the federal government. In addition, ABOR has authorized the University to establish an investment committee. The investment committee establishes investment policies and makes investment decisions. ABOR policies guide the investment committee decisions. The University's deposit and investment policies mirror that of the ABOR policies.

University policy states that restricted (gift) and endowment funds will be invested according to the conditions stipulated by the donor, but if no conditions are imposed, such funds may be invested under the direction of the investment committee in such a manner as to obtain the most favorable rate of return and income stability.

The bond indentures constitute the investment policy for University monies held with bond trustees. The bond indentures authorize the bond trustees to invest in obligations of or guaranteed by the federal government or any agency or instrumentality thereof, municipal obligations, collateralized certificates of deposit with federally insured banks, trust companies, savings and loan associations within the State of Arizona, or repurchase agreements.

Deposits

At June 30, 2012, cash on hand was \$23,047, the carrying amount of the University's deposits was \$45,964,612 and the bank balance was \$51,542,062. Beyond the requirements established by A.R.S. and ABOR, the University does not have a policy that specifically addresses custodial credit risk. At June 30, 2012, \$30,023,989 of the University's bank balance was uninsured with collateral held by the pledging financial institution and \$12,420,289 was being held in escrow and was uninsured and uncollateralized.

Investments	Amount
U.S. agency securities	\$ 125,995,580
Bond Trustee Funds:	
Government Money Market Mutual Fund	22,835,447
NAU Foundation Investment Pool	19,827,556
Money Market Mutual Funds	10,000,000
	<u>\$ 178,658,583</u>

U.S. agency securities include Federal Home Loan Mortgage Corporation, Federal Home Loan Bank, and Federal National Mortgage Association securities.

Trust agreements between the University and the NAU Foundation, Inc. authorize the Foundation to invest certain University restricted (gift) and endowment monies. The NAU Foundation Investment Pool invests in a variety of asset classes, including common stocks and fixed income and international equity funds. The Foundation's Board of Directors-appointed Investment Committee is responsible for oversight of the Pool in accordance with NAU Foundation policies and procedures. The fair value of the University's position in the Pool is based on the University's proportionate share of the Pool and is not identified with specific investments. The University's ownership interest is recorded in the Foundation's records.

The Arizona Student Financial Aid Trust Fund (ASFAT) was established in accordance with A.R.S. §15-1642 for the purpose of providing aid to students with verifiable financial need. The Northern Arizona University Foundation holds and manages the University's share of ASFAT within its pool. The University's ownership interest is recorded in the Northern Arizona University Foundation's records. The fair value of the ASFAT at June 30, 2012 was \$13,525,225.

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

Credit Risk

For its operating funds, University policy requires negotiable certificates of deposit; corporate bonds, debentures, and notes; banker acceptances; and State of Arizona bonds to carry a minimum rating of BBB or better from Standard and Poor's Rating Service. There is no formal policy with regards to gift and endowment funds. Gift and endowment funds are held in the NAU Foundation Investment Pool, which is not rated. At June 30, 2012, credit risk for the University's investments in debt securities was as follows:

Investment Type	Rating	Rating Agency	Amount
U.S. agency securities	AA+	Standard and Poor's	\$ 125,995,580
Bond Trustee Funds:			
Government Money Market Mutual Fund	AAAm	Standard and Poor's	22,835,447
Money Market Mutual Funds	AAAm	Standard and Poor's	10,000,000
			<u>\$ 158,831,027</u>

Custodial Credit Risk

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the University will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The University does not have a formal policy in regards to custodial credit risk. At June 30, 2012, the University had \$125,995,580 of U.S. agency securities that were uninsured and held by the counterparty not in the University's name.

Concentration of Credit Risk

University policy limits investments in a single issuer to 5 percent or less of the fair value of the total portfolio. However, securities issued or expressly guaranteed by the federal government are exempt from this provision. The following investments represent five percent or more of the University's investments at June 30, 2012: Federal National Mortgage Association securities, 31.2 percent, Federal Home Loan Mortgage Corporation securities, 30.9 percent, and Federal Home Loan Bank securities, 8.4 percent.

Interest Rate Risk

University policy for its operating funds limits the maximum maturity of any fixed or variable rate security to five years.

Investment type	Fair Value	Maturity	
		Less than 1 Year	1-5 Years
U.S. agency securities**	\$ 125,995,580	\$ 80,180,280	\$ 45,815,300*
Government Money Market Mutual Fund	22,835,447	22,835,447	
Money Market Mutual Fund	10,000,000	10,000,000	
Total	<u>\$ 158,831,027</u>	<u>\$ 113,015,727</u>	<u>\$ 45,815,300</u>

*These securities mature in fiscal years 2014 through 2017; of this amount, \$20,183,300 is currently callable.

**At June 30, 2012, the University held \$125,995,580 or 70.5 percent of investments in U.S. Agency securities, including the Federal National Mortgage Association, Federal Home Loan Mortgage Corporation and Federal Home Loan Bank, which may be considered to be highly sensitive to interest rate fluctuations because borrower repayment terms may vary.

A reconciliation of cash, deposits, and investments to amounts shown on the Statement of Net Assets is as follows:

Cash, deposits and investments:

Cash on hand	\$ 23,047
Cash in bank	45,964,612
Total investments	178,658,583
	<u>\$ 224,646,242</u>

Statement of Net Assets:

Cash and cash equivalents	\$ 43,747,655
Current investments	80,650,990
Restricted cash and cash equivalents held by trustee for capital projects	35,255,736
Noncurrent investments	45,823,307
Endowment investments	19,168,554
	<u>\$ 224,646,242</u>

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

Note 3—Capital Assets

Capital asset activity for the year ended June 30, 2012 was as follows:

	Balance July 1, 2011	Additions	Retirements	Transfers	Balance June 30, 2012
Capital assets not being depreciated:					
Land	\$ 6,685,920	\$ 165,489			\$ 6,851,409
Construction in progress	168,447,322	69,628,169	\$	\$ (197,822,271)	40,253,220
Total capital assets not being depreciated	175,133,242	69,793,658		(197,822,271)	47,104,629
Capital assets being depreciated:					
Infrastructure	94,745,027	643,083		35,378,622	130,766,732
Buildings and improvements	561,680,718	3,449,095	451,626	162,443,649	727,121,836
Equipment	63,810,379	5,390,183	7,391,565		61,808,997
Library books and media	47,251,328	269,912	721,472		46,799,768
Total capital assets being depreciated	767,487,452	9,752,273	8,564,663	197,822,271	966,497,333
Less accumulated depreciation for:					
Infrastructure	33,569,958	3,890,973			37,460,931
Buildings and improvements	201,954,435	18,421,813	426,562		219,949,686
Equipment	44,281,189	4,161,173	7,166,959		41,275,403
Library books and media	44,141,039	786,546	721,472		44,206,113
Total accumulated depreciation	323,946,621	27,260,505	8,314,993		342,892,133
Total capital assets being depreciated, net	443,540,831	(17,508,232)	249,670	197,822,271	623,605,200
Capital assets, net	\$ 618,674,073	\$ 52,285,426	\$ 249,670	\$	\$ 670,709,829

Construction - The University had major contractual commitments related to various capital projects at June 30, 2012, including the construction of a parking structure, a Health and Learning Center, a Native American Center, major building renovations and major infrastructure upgrades. At June 30, 2012, the University had spent \$28.1 million on these projects and had remaining contractual commitments with contractors of \$12.2 million. These projects are being financed with a combination of system revenue bond monies, series 2008, 2009, 2010 and 2012 and University reserves.

Note 4—Long-Term Liabilities

Long-term liability activity for the year ended June 30, 2012 was as follows:

	Balance July 1, 2011	Additions	Reductions	Balance June 30, 2012	Due Within One Year
Long-term obligations	\$ 291,847	\$ 12,420,289	\$ 69,736	\$ 12,642,400	\$ 71,843
Capital leases	46,925,000		915,000	46,010,000	985,000
Certificates of participation	80,835,000		11,295,000	69,540,000	2,670,000
Revenue bonds payable	335,700,000	23,955,000	5,835,000	353,820,000	6,610,000
Deferred amount on refunding	(1,454,915)		(129,669)	(1,325,246)	(125,712)
Discounts/premiums	4,249,579	1,196,698	313,981	5,132,296	331,077
Total long-term liabilities	\$ 466,546,511	\$ 37,571,987	\$ 18,299,048	\$ 485,819,450	\$ 10,542,208

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

The University's bonded debt and certificates of participation (COPs) consist of various issues that are generally callable at a prescribed date with interest payable semiannually. All issues are at a fixed rate. Bond proceeds primarily pay for acquiring, constructing or renovating capital facilities. System revenue bonds are repaid from pledged gross revenues that primarily consist of student tuition and fees and certain auxiliary revenues.

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	Average Interest Rate	Final Maturity	Balance 7/01/2011	Additions	Reductions	Balance 6/30/2012	Current Portion
Revenue Bonds:							
2004 System Refunding	4.749%	6/1/2034	\$ 24,590	\$	\$ (3,735)	\$ 20,855	\$ 3,925
2005 System Revenue	4.685%	6/1/2040	14,100		(255)	13,845	265
2006 System Refunding	4.675%	6/1/2034	42,030		(65)	41,965	65
2007 System Revenue	4.929%	6/1/2037	35,740		(730)	35,010	760
2008 System Revenue	5.041%	6/1/2038	39,955		(1,050)	38,905	1,095
2009A System Revenue	6.490%	6/1/2039	108,860			108,860	
2009B System Revenue	5.000%	6/1/2016	5,640			5,640	
2010 System Revenue	6.164%	8/1/2030	64,785			64,785	
2012 System Revenue	4.459%	6/1/2041		23,955		23,955	500
Subtotal: Par Amount of Bonds			\$ 335,700	\$ 23,955	\$ (5,835)	\$ 353,820	\$ 6,610
Certificates of Participation:							
2004 Certificates of Participation	4.852%	9/1/2030	\$ 33,730	\$	\$ (1,050)	\$ 32,680	\$ 1,095
2005 Certificates of Participation	4.650%	9/1/2030	35,975		(1,160)	34,815	1,200
2006 Certificates of Participation	4.350%	9/1/2017	11,130		(9,085)	2,045	375
Subtotal: Par Amount of COPS			\$ 80,835	\$	\$ (11,295)	\$ 69,540	\$ 2,670
Total Par Amount of Bonds and COPS			\$ 416,535	\$ 23,955	\$ (17,130)	\$ 423,360	\$ 9,280
Premium on Sale of Bonds and COPS			\$ 4,249	\$ 1,197	\$ (314)	\$ 5,132	\$ 331
Deferred Amount on Refundings			(1,455)		130	(1,325)	(126)
Total Revenue Bonds Payable and COPS			\$ 419,329	\$ 25,152	\$ (17,314)	\$ 427,167	\$ 9,485

The following schedule details debt service requirements to maturity for the University's bonds payable at June 30, 2012.

Year ending June 30,	Revenue Bonds	
	Principal	Interest
2013	\$ 6,610,000	\$ 19,250,660
2014	6,615,000	18,960,674
2015	7,170,000	18,663,789
2016	7,510,000	18,297,636
2017	11,200,000	17,835,048
2018-22	61,475,000	80,539,038
2023-27	75,050,000	62,707,868
2028-32	85,575,000	39,660,591
2033-37	68,270,000	18,453,707
2038-41	24,345,000	2,355,617
Total	\$ 353,820,000	\$ 296,724,628

The following schedule details debt service requirements to maturity for the University's certificates of participation payable at June 30, 2012.

Year ending June 30,	Egt v'lecvgu'qh'ct v'le'c'v'lp	
	Principal	Interest
2013	\$ 2,670,000	\$ 3,184,441
2014	2,780,000	3,076,787
2015	2,890,000	2,957,658
2016	3,015,000	2,836,966
2017	3,135,000	2,709,439
2018-22	15,495,000	11,426,802
2023-27	19,820,000	7,030,520
2028-31	19,735,000	1,682,640
Total	\$ 69,540,000	\$ 34,905,253

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

Revenue Bonds Payable and Certificates of Participation

On January 25, 2012, the University sold \$23,955,000 of Tax-exempt 2012 System Revenue Bonds for the purpose of construction and equipping of an approximately 463,086 square foot, six-story parking garage accommodating up to approximately 1,400 cars, to be located on the University's main campus.

The University on May 31, 2012, defeased \$8,720,000 in Certificates of Participation. Defeased were the 2006 Certificates of Participation for maturities from September 1, 2012 to September 1, 2030. The defeasance was accomplished by depositing \$10,203,527 into an irrevocable trust account and investing the monies in SLGS Certificates and Notes with maturities between September 1, 2012 and September 1, 2016. The present value of defeased debt prior to May 31, 2012 was \$13,604,336 and the net present value of savings was \$714,349.

In the prior years, the University defeased certain revenue bonds by either placing the proceeds of new bonds, or cash and investments accumulated in a sinking fund, in an irrevocable trust to provide for all future debt service payments on the refunded bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the University's financial statements. At June 30, 2012, the University had \$26,645,000 and \$8,295,000 in 2003 and 2004 System Revenue Bonds, respectively, outstanding that are considered defeased.

The Series 2009A and 2010 Bonds were issued as designated Build America Bonds under the provisions of the American Recovery and Reinvestment Act. As such, the University is eligible to receive direct payments from the U. S. Treasury Department equal to 35% of the interest payments on such bonds on each interest payment date. In order to receive such payments, the University must file certain required information with the Federal government between 90 and 45 days prior to the interest payment date. The amount paid to the University by the Federal government may be reduced or eliminated due to such issues as failure by the University to submit the required information, any amounts owed by the University to the Federal government, or changes in the law that would reduce or eliminate such payments. The University is currently not aware of any such issues that may adversely affect the amount of payments to be received from the Federal government related to such designated Build America Bonds. For accounting purposes, any direct payments received from the U. S. Treasury Department are recorded as nonoperating revenue.

For the 2010 revenue bonds, up to 80% of the debt service payments are payable from the University's SPEED (Stimulus Plan for Economic and Educational Development) revenue bond account monies, which are derived from certain revenues of the Arizona State Lottery. To the extent SPEED revenue bond account monies are not sufficient to make debt service payments, the SPEED revenue bonds are secured by a pledge of certain gross revenues, such as student tuition and fees, but that pledge is subordinate to the pledge of those gross revenues for the University's system revenue bonds.

The University has pledged portions of its gross revenues towards the payment of debt related to system revenue bonds, system revenue refunding bonds, and SPEED revenue bonds outstanding at June 30, 2012. The bonds generally provide financing for various capital projects of the University. These pledged revenues include student tuition and fees, certain auxiliary enterprises revenue, investment income, and indirect cost recovery revenue. Pledged revenues do not include state appropriations, gifts, endowment income, or other restricted revenues. Pledged revenue has averaged \$195 million for the prior five years. At June 30, 2012 pledged revenues totaled \$246.1 million of which 8.5% (\$20.9 million) was required to cover current year debt service not related to this year's defeasance. Future pledged revenues required to pay all remaining related debt service for the bonds through final maturity of June 1, 2041 is \$650.5 million.

Long-term Obligations

On June 28, 2012 the University entered into an Energy Conservation Equipment Lease-Purchase Agreement with Capital One Public Funding LLC. This is for the acquisition, construction, and installation of energy efficiency equipment at the University facilities over the next two years. The interest rate is 3.530% and the first two years of the University's payments are interest-only payments of approximately \$446,000. After two years, the University's payments are approximately \$1.2 million each year through June 1, 2027. The lease-purchase agreement was recorded as a long-term obligation in the amount of \$12,420,289.

Funding responsibility for the June 30, 2012 outstanding debt (dollars in thousands)

	Current Portion	Noncurrent Portion	Total
From Northern Arizona University operating revenues	\$ 7,872	\$ 356,579	\$ 364,451
From State of Arizona provided state appropriations, share of state sales tax, and lottery revenue (NAU in substance acting as conduit)	2,670	118,698	121,368
	<u>\$ 10,542</u>	<u>\$ 475,277</u>	<u>\$ 485,819</u>

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

Capital Leases

On May 19, 2005, the University entered into a lease agreement with Pine Ridge Village/Campus Heights, LLC (PRV/CH). The Company is a subsidiary of the Northern Arizona Capital Facilities Finance Corporation (NACFFC). During the 28-year lease term, the University will make lease payments on two apartment-style student housing complexes, Pine Ridge Village (PRV), and McKay Village (MV). The University recorded a capital lease of \$13.2 million in fiscal 2005 for the PRV complex and a capital lease of \$22.7 million in fiscal year 2007 for the MV complex.

On September 1, 2006, the University entered into a lease agreement with North Campus Facilities L.L.C. (NCF), a subsidiary of the NACFFC. During the 30-year lease term, the University will make lease payments on a 41,000 sq. ft. conference center and 344 space parking garage (High Country Conference Center). The University recorded a capital lease of \$12.4 million in fiscal year 2008 for the High Country Conference Center. Lease payments are based on the debt service schedule of fixed rate bonds with an average coupon rate of 4.89%. As part of the lease agreement, the University contributed additional funds of approximately \$12 million towards construction of the project, \$2 million of which was provided by the City of Flagstaff.

Capital lease commitments to lessors at June 30, 2012 based on present value of lease payments

	Average Interest Rate	Final Maturity	Balance June 30, 2011	Additions	Reductions	Balance June 30, 2012	Current Portion
Pine Ridge/McKay Village	4.61%	6/1/2033	\$ 35,245,000	\$	\$ 655,000	\$ 34,590,000	\$ 715,000
North Campus Facilities LLC	4.89%	6/1/2036	11,680,000		260,000	11,420,000	270,000
Total: Capital Leases			<u>\$ 46,925,000</u>	<u>\$</u>	<u>\$ 915,000</u>	<u>\$ 46,010,000</u>	<u>\$ 985,000</u>

Minimum lease payment commitments, including interest reimbursed to the lessor, for the capital leases described above are summarized in the table below.

Year ending June 30,	Capital Lease Payments	Capital Lease Assets – the book value, accumulated depreciation and net book value for capitalized leased assets as of June 30, 2012 were as follows:			
		Asset	Book Value	Accumulated Depreciation	Net Book Value
2013	\$ 3,094,858				
2014	3,133,648				
2015	3,167,720				
2016	3,206,060	Pine Ridge	\$ 13,225,000	\$ (2,644,516)	\$ 10,580,484
2017	3,244,165				
2018-22	9,985,823	McKay Village	\$ 22,685,000	\$ (3,403,563)	\$ 19,281,437
2023-27	17,447,366				
2028-32	18,483,741	Conference Center	\$ 24,679,964	\$ (3,084,243)	\$ 21,595,721
2033-36	14,037,711				
Total minimum lease payments	<u>\$ 75,801,092</u>	Total	<u>\$ 60,589,964</u>	<u>\$ (9,132,322)</u>	<u>\$ 51,457,642</u>
Less amount representing interest	(29,791,092)				
Present value of net minimum lease payments	<u>\$ 46,010,000</u>				

Operating Leases

The University leases numerous classroom facilities for extended campus instruction and a limited number of administrative facilities under long-term lease agreements classified as operating leases for accounting purposes. Rental expenses under the terms of operating leases were \$2.9 million for the year ended June 30, 2012. The operating leases have remaining noncancelable terms from 1 to 5 years and provide renewal options. The future minimum payments required under the operating leases at June 30, 2012 were as follows:

Year ending June 30,	
2013	\$ 1,830,114
2014	1,482,635
2015	1,232,898
2016	1,049,040
2017	442,362
Total minimum lease payments	<u>\$ 6,037,049</u>

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

Note 5—Retirement Plans

The University participates in a cost-sharing multiple-employer defined benefit pension, health, and long-term disability plan administered by the Arizona State Retirement System (ASRS) and a defined contribution pension plan available through one of three independent insurance and annuity companies approved by the Arizona Board of Regents.

Under the University's defined benefit plan, the ASRS (through its Retirement Fund) provides retirement (i.e., pension), death, and survivor benefits; the Health Benefit Supplement Fund provides health insurance premium benefits (i.e., a monthly subsidy); and the Long-Term Disability Fund provides long-term disability benefits. Benefits are established by state statute. The System is governed by the Arizona State Retirement System Board according to the provisions of A.R.S. Title 38, Chapter 5, Article 2. The ASRS issues a Comprehensive Annual Financial Report that includes its financial statements and required supplementary information. That report may be obtained by writing to the ASRS, 3300 North Central Avenue, P.O. Box 33910, Phoenix, Arizona 85067-3910, calling (602) 240-2000 or (800) 621-3778, or online at www.AZASRS.gov.

The Arizona State Legislature establishes and may amend active plan members' and the University's contribution rates. For the year ended June 30, 2012, active plan members were required by statute to contribute at the actuarially determined rate of 10.74 percent (10.50 percent for retirement and 0.24 percent for long-term disability) of the members' annual covered payroll and the University was required by statute to contribute at the actuarially determined rate of 10.74 percent (9.87 percent for retirement, 0.63 percent for health insurance premium, and 0.24 percent for long-term disability) of the members' annual covered payroll.

The University's contributions for the current and two preceding years, all of which were equal to the required contributions, were as follows:

Years ended June 30,	Retirement Fund	J gcnj 'DgggLv" Supplement Fund	Nqpi /Vgto " Disability Fund
2012	\$ 7,975,201	\$ 509,055	\$ 193,755
2011	\$ 7,244,168	\$ 474,368	\$ 200,687
2010	\$ 6,222,744	\$ 492,477	\$ 296,901

In accordance with A.R.S. § 15-1628, University faculty, academic professionals, and administrative officers have the option to participate in defined contribution pension plans. These plans are administered by independent insurance and annuity companies approved by the Arizona Board of Regents. During the fiscal year ended June 30, 2012, plans offered by the Teachers Insurance Annuity Association/College Retirement Equities Fund (TIAA/CREF), Variable Annuity Life Insurance Company (VALIC), and Fidelity Investments Tax-Exempt Service Company (Fidelity) were approved by the Board. The contract with VALIC was terminated by the University in September 2011. Benefits under these plans depend solely on the contributed amounts and the returns earned on investments of those contributions. Contributions made by members vest immediately, and University contributions vest after five years of benefit eligible employment.

Employee and University contributions and associated returns earned on investments may be withdrawn upon termination of employment, death, or retirement. The distribution of contributions and associated investment earnings are made in accordance with the member's contract with the applicable insurance and annuity company. The Arizona State Legislature establishes and may amend active plan members' and the University's contribution rates. For the year ended June 30, 2012, plan members and the University were each required by statute to contribute an amount equal to 7 percent of a member's compensation.

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for the year ended June 30, 2012, are summarized below.

Plan	University Contributions	Member Contributions	Total Contributions
TIAA/CREF	\$ 3,282,777	\$ 3,282,777	\$ 6,565,554
VALIC	\$ 48,456	\$ 48,456	\$ 96,912
Fidelity	\$ 1,863,709	\$ 1,863,709	\$ 3,727,418

Note 6—Risk Management

Pursuant to A.R.S. § 41-621, Northern Arizona University (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 for which the University has no insurance coverage are losses resulting from contractual breaches and losses that arise out of and are directly attributable to an act of 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 other pending claims or litigation not covered by the Risk Management Section should not have a material effect on the University's financial statements. All estimated losses for unsettled claims and actions covered by the State's Risk Management Program are determined on an actuarial basis and are included in the State of Arizona Comprehensive Annual Financial Report.

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

Note 7—Expense Classification

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

For the Year Ended June 30, 2012	Personal Services	Operations	Permanently Restricted Assets	Depreciation	Total
Functional Classification:					
Education and general:					
Instruction	\$ 121,026,998	\$ 13,244,791			\$ 134,271,789
Research	14,385,099	7,380,839			21,765,938
Public service	15,178,607	13,173,838			28,352,445
Academic support	22,482,395	6,375,563			28,857,958
Student services	22,110,326	14,163,350			36,273,676
Institutional support	30,049,430	11,739,194			41,788,624
Operation and maintenance of plant	7,764,281	14,016,762			21,781,043
Scholarships and fellowships			\$ 25,576,141		25,576,141
Auxiliary enterprises	21,398,913	15,636,234			37,035,147
Depreciation				\$ 27,260,505	27,260,505
Total	\$ 254,396,049	\$ 95,730,571	\$ 25,576,141	\$ 27,260,505	\$ 402,963,266

Note 8—Discretely Presented Component Units Disclosures

A. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of Northern Arizona University Foundation, Inc. (Foundation) and Northern Arizona Capital Facilities Finance Corporation (NACFFC) including its Pine Ridge Village/Campus Heights and North Campus Facilities (limited liability companies) subsidiaries, have been prepared on the accrual basis of accounting.

Financial Statement Presentation

Both the Foundation and the NACFFC follow the Financial Accounting Standards Board Accounting Standards Codification (FASB ASC 958-205), *Not-for-Profit - Presentation of Financial Statements*.

Under FASB ASC 958-205, the Foundation and the NACFFC are required to report information regarding their financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

- Unrestricted net assets – include assets and contributions that are not restricted by donors or for which such restrictions have expired.
- Temporarily restricted net assets – include contributions for which donor imposed restrictions have not been met (either by the passage of time or by actions of the Foundation), charitable remainder unitrusts, pooled income funds, gift annuities, and pledges receivable for which the ultimate purpose of the proceeds is not permanently restricted. Donor-restricted contributions are classified

as temporarily restricted if restrictions are satisfied in the same reporting period in which the contributions are received.

- Permanently restricted net assets – include contributions, charitable remainder unitrusts, pooled income funds, gift annuities, and pledges receivable which require by donor restriction that the corpus be invested in perpetuity and only the board-approved payout be made available for program operations in accordance with donor restrictions.

Cash and Cash Equivalents

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

Investments

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

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

Revenue Recognition

The Foundation - Contributions, including unconditional promises to give, are recognized as revenues in the period received. Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value. Contributions to be received after one year are discounted at rates commensurate with the risks involved. Amortization of discount is recorded as additional contribution revenue in accordance with donor-imposed restrictions, if any, on the contributions. An allowance for uncollectible contributions receivable is provided based upon management's judgment including such factors as prior collection history.

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

NACFFC - Rent and lease income is recognized as payments become due. Payments received in advance will be deferred until earned.

Net Investments in Sales-Type Financing Leases

NACFFC - Net investments in sales-type financing leases are stated at the sum of the minimum lease payments less unearned income. Unearned income is amortized over the lease terms, which approximate the related bond terms. No valuation allowance has been established as title to the assets associated with the lease would be transferred back to the Pine Ridge Village/Campus Heights and North Campus Facilities LLC's in the event of default.

Property, Plant and Equipment

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

Buildings and improvements	28-30 years
Furniture and equipment	5-10 years

Use of Estimates

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

Tax Status

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

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

Bonds Issuance Costs

NACFFC - Issuance costs of \$1,114,894 relating to the Pine Ridge Village/Campus Heights Series 2008 Bonds are being amortized on a straight-line basis over the life of the Series 2008 Bonds. Amortization expense for the year ended June 30, 2012 was \$44,596 for issuance costs related to the Series 2008 Bonds.

Issuance costs of \$470,590 relating to the North Campus Series 2006 Bonds are being amortized on a straight-line basis over the life of the Series 2006 Bonds. Amortization expense for the year ended June 30, 2012 was \$15,686 for issuance costs related to the Series 2006 bonds.

B. ASSETS HELD BY TRUSTEE

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

NACFFC - Pursuant to the terms of the Trust Indenture, relating to the Series 2006 and 2008 Bonds, proceeds of the Series 2006 and 2008 Bonds were deposited into certain funds and accounts established with the Trustee. Assets held by Trustee consist of various reserves and operating accounts required by the Trust Indenture and totaled \$8 at June 30, 2012. These assets are invested in 100% treasury money market funds. Currently all accounts in use by the Trustee are restricted as to use.

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

C. PLEDGES RECEIVABLE

Pledges receivable for the Foundation consist of the following unconditional promises to give:

Gross amounts due in:	
Less than one year	\$ 2,140,010
One to five years	4,502,027
More than five years	4,000
Gross pledges receivable	<u>6,646,037</u>
Discount to present value	(401,920)
Allowance for uncollectible pledges	(73,901)
Total pledges receivable, net	<u>\$ 6,170,216</u>

A concentration of credit risk exists with the unconditional promises to give at June 30, 2012 as approximately 70% of the gross pledges receivable balance at June 30, 2012 is from one donor.

Members of the Foundation's Board of Directors have made contributions and pledges to the Foundation in the current and prior years. At June 30, 2012, gross unconditional pledges receivable from these members total approximately \$326,000. During fiscal year 2012, the Foundation recognized contribution revenue from these donors of approximately \$104,000.

D. INVESTMENTS

The fair value and cost of the Foundation's investments at June 30, 2012 are as follows:

	Fair Value	Cost
U.S. Government/agency bonds	\$ 9,259,282	\$ 6,845,082
Corporate bond mutual funds	14,621,687	12,873,705
Equity mutual funds	46,416,745	40,537,967
International equity funds	18,237,390	6,330,452
Money market funds	573,710	573,710
	<u>\$ 89,108,814</u>	<u>\$ 67,160,916</u>

Investments include funds held for the custody of others of \$18,569,002 at June 30, 2012.

The Foundation had a realized investment gain of \$453,431 and unrealized losses on investments of \$2,279,610 for the year ended June 30, 2012. Investment expenses of \$52,498 for the year ended June 30, 2012 have been netted against investment earnings in the statement of activities.

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

E. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment is comprised of furniture and equipment and is reported net of accumulated depreciation. Balances as of June 30, 2012 are presented as follows:

FOUNDATION

	Cost or Donated Value	Accumulated Depreciation	Net Assets
Furniture and equipment	<u>\$ 5,482,413</u>	<u>\$ 105,719</u>	<u>\$ 5,376,694</u>

F. LEASE PURCHASE AND OTHER LEASE AGREEMENTS

NACFFC - On May 19, 2005, NAU entered into a lease purchase agreement with Pine Ridge Village /Campus Heights LLC. During the 28 year lease term, the University will make lease payments on two apartment style student housing complexes, Pine Ridge Village and McKay Village. The LLC recorded a sales-type lease receivable of \$13,225,000 in fiscal year 2005 for the Pine Ridge complex. The agreement also provided for NAU's lease purchase of the McKay Village complex for \$22,685,000 in fiscal year 2007. Upon expiration of the lease, the real property will become the sole property of NAU without further cost.

Upon renegotiation of the lease purchase agreement on May 1, 2008, base lease payments for both housing complexes are tied to the principal and fixed rate interest payments on the Series 2008 Bonds issued by the LLC. Additional rents are provided for in the lease purchase agreement to cover costs incurred by the LLC for bond related costs and professional expenses. These rents are recognized when the qualifying expense is incurred.

On September 1, 2006, NAU entered into a lease purchase agreement with North Campus Facilities LLC. During the 30 year lease term, the agreement provides for NAU's lease purchase of the convention center/ parking garage complex for \$12,400,000 in fiscal year 2008. Upon expiration of the lease, the real property will become the sole property of NAU without further cost.

At June 30, 2012, minimum lease payments are as follows:

Year ending June 30,	Amount
2013	\$ 3,094,858
2014	3,133,648
2015	3,167,720
2016	3,206,060
2017	3,244,165
Thereafter	<u>59,954,641</u>
	<u>\$ 75,801,092</u>

Additional rents are provided for in the lease purchase agreement to cover costs incurred by North Campus Facilities LLC for bond related costs and professional expenses. These rents are recognized when the qualifying expense is incurred.

Components of the net investment in the lease are as follows:

Total minimum lease payments to be received	\$ 75,801,092
Less: Unearned income	<u>(29,791,092)</u>
Net investment in sales-type lease	<u>\$ 46,010,000</u>

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

Educational broadcast system licenses - The Foundation has been granted several educational broadcast system (EBS) licenses from the Federal Communications Commission (FCC). Additionally, the Foundation entered into an agreement to purchase EBS licenses with funding from an outside corporation. Under the agreement, which is considered an exchange transaction and not a contribution under FASB ASC 958-605, the Foundation will purchase the EBS licenses and then lease the licenses to the outside corporation. In fiscal year 2008, the Foundation received approximately \$15,000,000 from the outside corporation to purchase the licenses. As of June 30, 2012, the cumulative purchased EBS licenses total \$8,810,045. There were no purchases of EBS licenses in fiscal year 2012. In addition, the Foundation did receive a one time bonus of \$1,300,000 in fiscal year 2010. The remaining balance to be purchased, plus \$562,335 in interest earned on investments of the advanced funds, comprise the deferred revenue balance in the accompanying consolidated statement of financial position. For the year ended June 30, 2012, amortization expense of \$1,629,606 was computed using the straight line method over estimated useful lives of 10 years and accumulated amortization expense at June 30, 2012 totaled \$5,310,181.

The Foundation leases the licenses to various companies. The licenses are granted for ten-year terms, which are due to expire in June 2022. The terms of the related lease agreements correspond with the terms of the licenses. Most leases have renewal clauses, which provide for a maximum lease term of 30 years. The FCC has certain educational programming requirements. As part of the lease agreements, the lessees are responsible for ensuring that the educational requirements are met. After the educational requirements are met, there is excess frequency capacity that can be used.

The Foundation receives monthly lease payments for the use of the excess capacity. In addition to the monthly payment terms, several leases required the lessee to pay an initial fee. Total revenue received from these agreements was \$1,280,914 for the year ended June 30, 2012.

The future minimum lease payments to be received under these agreements, at June 30, 2012, are as follows:

Year ended June 30,	Amount
2013	\$ 950,332
2014	624,181
2015	487,792
2016	399,799
2017	382,519
Thereafter	<u>1,114,143</u>
	<u>\$ 3,958,766</u>

NOTES TO FINANCIAL STATEMENTS

June 30, 2011

G. BONDS PAYABLE

The NACFFC, through its Pine Ridge Village/Campus Heights LLC and the North Campus LLC subsidiaries, had the following bonds outstanding at June 30, 2012:

Revenue Serial and Term Bonds in the aggregate original principal amount of \$36,780,000 dated May 8, 2008; interest payable semi-annually at various interest rates ranging from 3.5% to 5%; principal payable annually in various amounts beginning June 1, 2009 through June 1, 2033; secured by property, leases and revenues including the Trust Funds, excluding the Rebate Fund, under terms of the Trust Indenture.

\$ 34,590,000

North Campus Lease Revenue Serial and Term Bonds in the aggregate original principal amount of \$12,400,000 dated September 1, 2006; interest payable semi-annually at various interest rates ranging from 4% to 5% based on terms; principal payable annually from June 1, 2009 to June 1, 2036; secured by property, leases and revenues including the Trust Funds, excluding the Rebate Fund, under the terms of the Trust Indenture.

Total bonds payable	11,420,000
Unamortized bond premium/discount	\$ 46,010,000
Bonds payable, net	(27,180)
Less: current maturities	\$ 45,982,820
Bonds payable, noncurrent portion, net	(985,000)
	\$ 44,997,820

At June 30, 2012, maturities of bonds payable are as follows:

Year ended June 30,	Amount
2013	\$ 985,000
2014	1,060,000
2015	1,135,000
2016	1,220,000
2017	1,310,000
Thereafter	40,300,000
	\$ 46,010,000

Interest expense related to bonds for 2012 was \$1,602,487 (Pine Ridge Village/Campus Heights LLC) and \$544,436 (North Campus), net of related discount amortization and bond premium of \$18,423 and \$14,892 respectively.

Pine Ridge Village Campus Heights (PRV/CH) -The Series 2008 Refunding Bonds maturing on or before June 1, 2018 are not subject to optional redemption prior to maturity. The Series 2008 Refunding Bonds maturing on or after June 1, 2019 are subject to optional redemption prior to maturity on any date on or after June 1, 2018, in whole or in part, in Authorized Denominations, following applicable notice, from such maturities as may be selected by PRV/CH at its option, at a redemption price (expressed as a percentage of the principal amount of the Series 2008 Refunding Bonds to be called for redemption) of 100% plus accrued interest thereon to the date of redemption. Additional bonds may be subject to optional redemption as provided in the trust agreement or related issuing document for such additional bonds.

The Series 2008 Refunding Bonds maturing on June 1, 2028 and June 1, 2033 are subject to mandatory Sinking Fund Installments prior to maturity, in Authorized Denominations, at random, as may be selected by the Bond Registrar, at a redemption price equal to the principal amount of the series 2008 Refunding Bonds to be called for redemption plus accrued interest thereon to the date of redemption but without premium, plus accrued interest as follows:

Pine Ridge Village Campus Heights

Series 2008 Refunding Bonds Bonds Due June 1, 2028

Year	Principal Amount to be Redeemed
2027	\$ 2,010,000
2028	2,155,000 (Maturity)

Series 2008 Refunding Bonds Bonds Due June 1, 2033

Year	Principal Amount to be Redeemed
2029	\$ 2,305,000
2030	2,460,000
2031	2,620,000
2032	2,780,000
2033	2,955,000 (Maturity)

NOTES TO FINANCIAL STATEMENTS

June 30, 2012

North Campus - The 2006 Bonds maturing on or before June 2016 will not be subject to optional redemption prior to maturity. The 2006 Bonds maturing on or after June 2017 will be subject to optional redemption prior to maturity on any date on or after June 2016 in whole or in part from such maturities as may be selected by the Company at its option at redemption price (expressed as percentage of the principal amount of the 2006 Bonds to be called for redemption) of 100% plus accrued interest thereon to the date of redemption.

The 2006 Bonds maturing on the following dates will be subject to mandatory sinking fund installments prior to maturity by lot as may be selected by the Trustee at redemption price equal to the principal amount of the 2006 Bonds to be called for redemption plus accrued interest thereon to the date of redemption but without premium on the following dates in the following principal amounts:

North Campus Facilities

Bonds Due June 1, 2025

Year	Principal Amount to be Redeemed
2022	\$ 395,000
2023	415,000
2024	435,000
2025	455,000 (Maturity)

Bonds Due June 1, 2031

Year	Principal Amount to be Redeemed
2026	\$ 480,000
2027	505,000
2028	530,000
2029	555,000
2030	585,000
2031	610,000 (Maturity)

Bonds Due June 1, 2036

Year	Principal Amount to be Redeemed
2032	\$ 645,000
2033	675,000
2034	710,000
2035	745,000
2036	780,000 (Maturity)

H. ASSETS HELD IN CUSTODY FOR OTHERS

The Foundation maintains certain asset balances on behalf of others, which consists of the following at June 30, 2012:

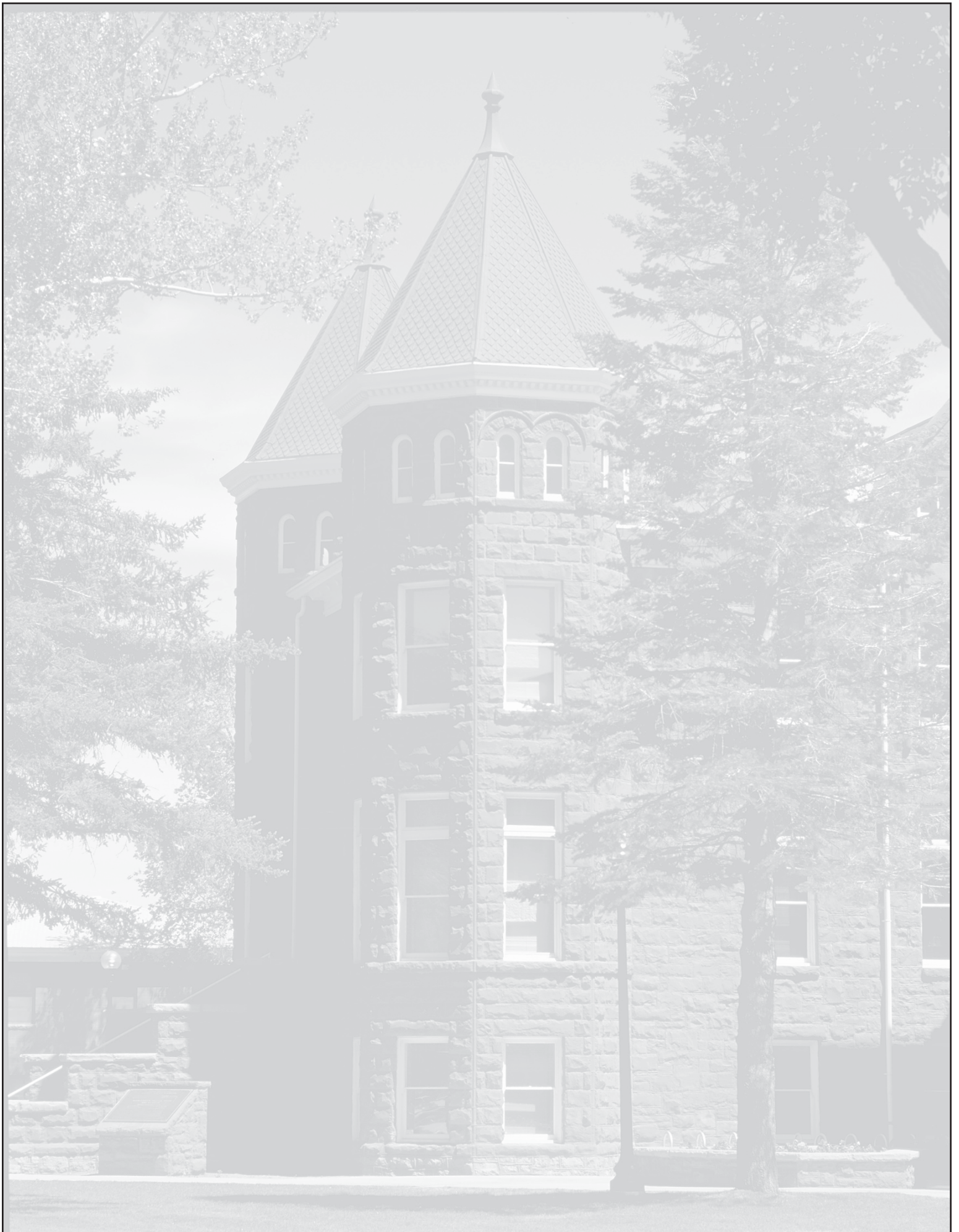
Cash	\$ 939,068
Unconditional promises to give	1,074
Investments	18,569,002
Beneficial interest in perpetual trust	574,049
	<u>\$ 20,083,193</u>

Assets held on behalf of:

Northern Arizona University	\$ 19,827,556
Parents' Association	255,637
	<u>\$ 20,083,193</u>

Note 9—Subsequent Event

In September, 2012, Northern Arizona Real Estate Holdings, LLC (NAREH), a subsidiary of the Northern Arizona University Foundation, completed construction of an office building on property owned by the University at a total expected cost of \$9.8 million. NAREH has leased the office building to the University under a direct financing lease, which commenced upon the completion of construction and has a 20 year term. Total lease payments will be \$14.2 million.



NOTES

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