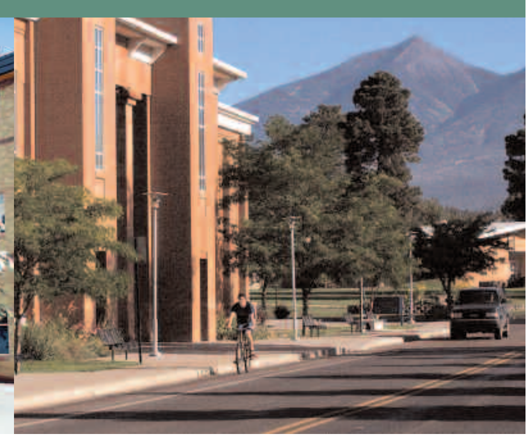
NORTHERN ARIZONA UNIVERSITY

Financial Report 2004-2005



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This financial report is compiled and issued by the
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Northern Arizona University
P.O. Box 4069
Flagstaff, AZ 86011-4069

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INDEPENDENT AUDITORS' REPORT

DEBRA K. DAVENPORT, CPA
Auditor General

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

WILLIAM THOMSON
Deputy Auditor General

Members of the Arizona State Legislature

The Arizona Board of Regents

We have audited the accompanying financial statements of the business-type activities and aggregate discretely presented component units of Northern Arizona University as of and for the year ended June 30, 2005, as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the aggregate discretely presented component units. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts for the aggregate discretely presented component units, is based solely on the reports of the other auditors.

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

As discussed in Note 1, the University's financial statements are intended to present the financial position, and the changes in financial position and cash flows, where applicable, of only those portions of the business-type activities, major fund, and aggregate discretely presented component units of the State of Arizona that are attributable to the University. They do not purport to, and do not, present fairly the financial position of the State of Arizona as of June 30, 2005, and the changes in financial position and cash flows, where applicable, for the year then ended in conformity with U.S. generally accepted accounting principles.

In our opinion, based on our audit and the reports of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and aggregate discretely presented component units of Northern Arizona University as of June 30, 2005, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with U.S. generally accepted accounting principles.

As discussed in Note 1, the University implemented the provisions of Governmental Accounting Standards Board (GASB) Statement No. 40, *Deposit and Investment Risk Disclosures*, for the year ended June 30, 2005, which represents a change in accounting principle.

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

Debbie Davenport
Auditor General

January 25, 2006

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, 2005. 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 report of independent auditors, management's discussion and analysis, the financial statements in the format referred to below, and notes to the financial statements, which include the summary of significant accounting policies.

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

- The Statement of Net Assets presents the financial position of the University at the end of the fiscal year. This statement is classified between current assets/liabilities and non-current assets/liabilities. In addition, capital assets are depreciated over the useful life of the asset and the annual depreciation amount is shown as a current year expense.

- The Statement of Revenues, Expenses, and Changes in Net Assets distinguishes between operating and nonoperating revenues and expenses, with state appropriations reported as nonoperating revenue. Student tuition and fee revenues, and certain other revenues from students, are reported net of scholarship discounts and allowances.

- The financial statements include a Statement of Cash Flows prepared using the direct method. This statement provides information about the University's sources and uses of cash during the year.

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 9.

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

Financial Highlights

- Total net assets increased $23.3 million from July 1, 2004 to June 30, 2005.

- Student tuition and fees increased 4.7 percent from the previous year or about $3.3 million.

- Government grants and contracts increased approximately $2.3 million from the prior year.

- Proposition 301 share of state sales tax revenues increased $3.9 million, or approximately 41 percent from the prior year to a total of $13.5 million in 2005.

- State appropriations increased by approximately $6.0 million from the prior year.

- During the fiscal year the University issued $39.7 million of system revenue and refunding bonds, at an average interest rate of 4.34 percent, to refund $25,255,000 of the series 1997 bonds and to finance several construction and renovation projects on the Mountain Campus (see Capital Assets and Debt Administration section).

- During the fiscal year the University issued $37.6 million of certificates of participation, at an average interest rate of 4.45 percent, to construct the Applied Research and Development Project and the College of Engineering and Technology Renovation project (see Capital Assets and Debt Administration section).

- University cash and investments increased by $27.8 million to a total of $131.8 million at June 30, 2005.

MANAGEMENT'S DISCUSSION AND ANALYSIS

STATEMENT OF NET ASSETS

The Statement of Net Assets presents the financial position of the University at the end of the fiscal year and includes all assets and liabilities of the University. A summarized comparison of the University's assets, liabilities, and net assets for the years ended June 30, 2005 and 2004 (in thousands), is as follows:

	2005	2004
Current assets	$ 57,079	$ 75,370
Noncurrent assets:		
Cash, cash equivalents, investments, and student loans receivable	93,436	43,214
Endowment investments	11,680	10,668
Capital assets – net of accumulated depreciation	253,131	204,422
Other noncurrent assets	119	181
Total noncurrent assets	358,366	258,485
Total assets	415,445	333,855
Long-term liabilities	181,903	128,008
Other liabilities	30,096	25,725
Total liabilities	211,999	153,733
Net assets	**$ 203,446**	**$ 180,122**

A review of NAU's Statement of Net Assets at June 30, 2005 and 2004 shows that the University's financial position continues to improve.

Current assets consist primarily of cash and investments, government grants and contracts receivable, and accounts receivable. Current assets decreased by approximately $18.3 million during fiscal year 2005, mainly due to the University investing more cash in government backed agency notes with longer maturity dates. This in part was the reason for a 70.2% increase in investment income. (See Statement of Revenues, Expenses, and Changes in Net Assets section)

Noncurrent assets increased by approximately $99.9 million over the prior year. The majority of the increases are as follows. Noncurrent investments increased by $33.8 million due to the University investing additional cash in government backed notes with longer maturity dates. Capital assets, representing a majority of noncurrent assets, increased approximately $48.7 million over the fiscal year. Cash and investments held by trustee increased by $17.2 million as unspent funds from bond proceeds were deposited until needed for capital projects. The changes in capital assets are discussed in more detail in the Capital Assets and Debt Administration section.

Long-term liabilities increased by $53.9 million as of June 30, 2005. The increase is mainly attributed to the issuance of long-term debt, which is discussed further in the Capital Assets and Debt Administration section.

Other liabilities include accounts payable, accrued expenses, and deferred revenue. Other liabilities are higher by $4.4 million, from $25.7 million as of June 30, 2004 to $30.1 million as of June 30, 2005. This increase is mainly due to a $1.3 million increase in accrued payroll due to the timing of pay dates between fiscal years. Accrued interest increased $642 thousand due to increased debt activity. Deferred revenue increased by $1.5 million, due to timing changes in fall tuition billing statements and a later end date for the first 5-week summer session, as compared to the prior year.

NET ASSETS

A summarized comparison of the University's net assets for the years ended June 30, 2005 and 2004 (in thousands), is as follows:

	2005	2004
Invested in capital assets, net of related debt	$ 124,849	$ 114,348
Restricted:		
Nonexpendable	15,177	14,163
Expendable	18,345	14,367
Unrestricted	45,075	37,244
Total net assets	**$ 203,446**	**$ 180,122**

Net assets at June 30, 2005 increased in total by $23.3 million or about 13.0 percent from 2004. This is a result of total combined sources of $310.6 million and total uses of $287.3 million. The University continues to invest in capital assets, physical plant, and infrastructure, the net increase of $10.5 million is a result of the increase in the net capital assets for the fiscal year, less the related debt used to fund those assets.

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

The Statement of Revenues, Expenses, and Changes in Net Assets presents the operating results of the University, as well as the nonoperating revenues and expenses. Annual state appropriations, while budgeted for operations, are considered nonoperating revenues according to U.S. generally accepted accounting principles. See the table of Combined Sources and Uses of Funds on pages 10-11 for an overview of the composition of revenues and expenses. A summarized comparison of the University's revenues, expenses, and changes in net assets for the years ended June 30, 2005 and 2004 (in thousands), is as follows:

	2005	2004
Operating revenues:		
Tuition and fees, net of scholarship allowances	$ 74,121	$ 70,821
Government grants and contracts	54,026	51,751
Auxiliary enterprises	34,048	33,349
Other	9,341	9,234
Total operating revenues	171,536	165,155
Nonoperating revenues:		
State appropriations	117,635	111,643
Share of state sales tax	13,475	9,564
Grants and contracts	3,730	3,968
Investment income	3,550	2,085
Other nonoperating revenues	—	655
Total nonoperating revenues	138,390	127,915
Total revenues	309,926	293,070
Operating expenses:		
Educational and general	234,804	227,798
Auxiliary enterprises	27,886	29,587
Depreciation	16,227	16,070
Total operating expenses	278,917	273,455
Nonoperating expenses:		
Interest expense on capital asset related debt	7,296	5,206
Other nonoperating expenses	1,049	575
Total expenses	287,262	279,236
Increase before capital grants and gifts and endowment additions	22,664	13,834
Capital grants and gifts and endowment additions	660	789
Increase in net assets	**$ 23,324**	**$ 14,623**

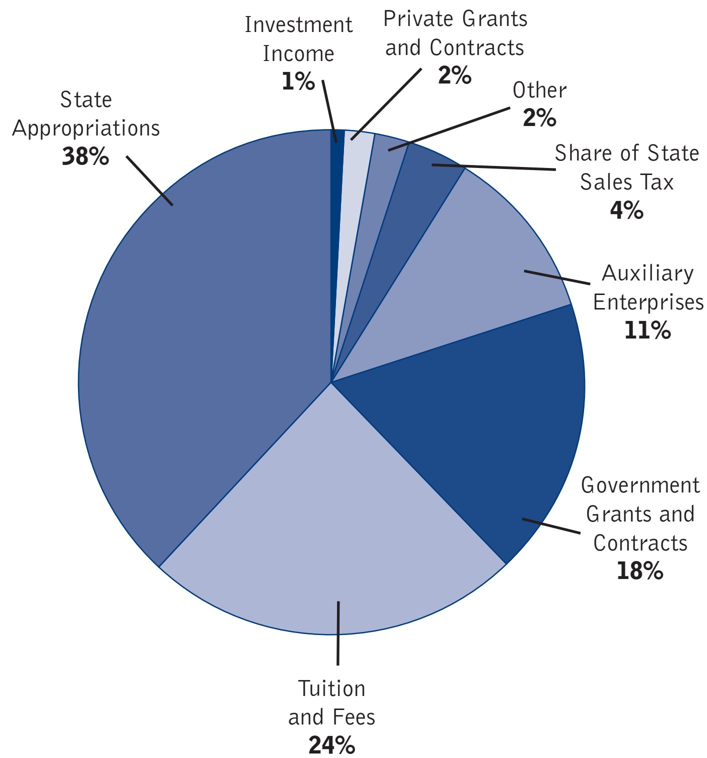
REVENUES ANALYSIS

State appropriations and tuition and fees continue to be the major funding sources for current operations related to educational purposes. Operating revenues (not including state appropriations) increased 3.9 percent or about $6.4 million in fiscal year 2005. This increase is due mainly to an increase in additional tuition revenue of $3.3 million and an increase of $2.3 million in government grants and contracts. The $3.3 tuition revenue increase from fiscal year 2004 is mainly due to a board approved tuition rate increase. Government grants and contracts revenue increased mainly due to additional grant funding from the U.S. Department of Commerce for the new Applied Research and Development building of $1.9 million, and approximately $311 thousand from the U.S. Office of Naval Research. Nonoperating revenues include state appropriations which increased by $6.0 million. The $6.0 million increase is mainly due to salary and employee related expenses of $2.1 million, a general increase of $2.6 million, and a health insurance appropriation of $1.3 million. The revenues from share of state sales tax increased by 41% or about $3.9 million during the year. Share of state sales tax are revenues appropriated to the Arizona Board of Regents for the Technology and Research Initiative Fund (TRIF).

EXPENSES ANALYSIS

Educational and general expenses continued to account for a majority of the operating expenses. Educational and general expenses increased in fiscal year 2005 by $7.0 million. Significant components of the increase within educational and general expenses were instruction, $3.0 million; operation and maintenance of plant, $2.7 million; research, $800 thousand; and student services, $900 thousand. There was a decrease in scholarships and fellowships of $1.3 million. The increase in educational and general expenses is due mainly to an increase of employee salary and benefit costs funded by the state legislature appropriation. Overall, employee related expenses increased from $38.7 million in fiscal year 2004 to $41.0 million in fiscal year 2005, a 5.9% increase. The significant increase in employee related expenses was $1.65 million in health insurance. The increase in operation and maintenance of plant was due to a $365 thousand increase in utilities expense, $952 thousand increase in institutional projects, $766 thousand in bond costs and $935 thousand in expenses related to a new student housing project. The decrease in scholarships and fellowships is due to a greater amount of student aid allocated to tuition and fees; thus, increasing tuition and fees allowances. Tuition and fees allowances increased by $2.9 million in fiscal year 2005. The reduction in auxiliary enterprise expenditures is due primarily to improved reporting of interdepartmental revenue, which resulted in elimination of related interdepartmental expenses. The change in nonoperating expenses included a $2.1 million increase in interest expense on capital related debt. This was due to the additional debt service the University incurred as a result of issuing new long-term debt.

Total Revenues
Fiscal Year 2005



Expenses - By functional classification

A comparative summary of the University's expenses by functional classification for the years ended June 30, 2005 and June 30, 2004, is as follows:

	2005	2004
Operating:		
Instruction	$ 98,137,817	$ 95,100,334
Research	19,615,438	18,824,650
Public service	22,184,784	21,918,764
Academic support	20,564,192	20,159,750
Student services	20,031,546	19,129,780
Institutional support	27,207,682	26,992,423
Operation and maintenance of plant	16,434,690	13,738,356
Scholarships and fellowships	10,627,631	11,934,017
Total educational and general expenses	234,803,780	227,798,074
Auxiliary enterprises	27,885,480	29,587,505
Depreciation	16,227,387	16,069,536
Total operating expenses	278,916,647	273,455,115
Nonoperating:		
Interest and other	8,344,980	5,780,915
Total Expenses	$ 287,261,627	$ 279,236,030

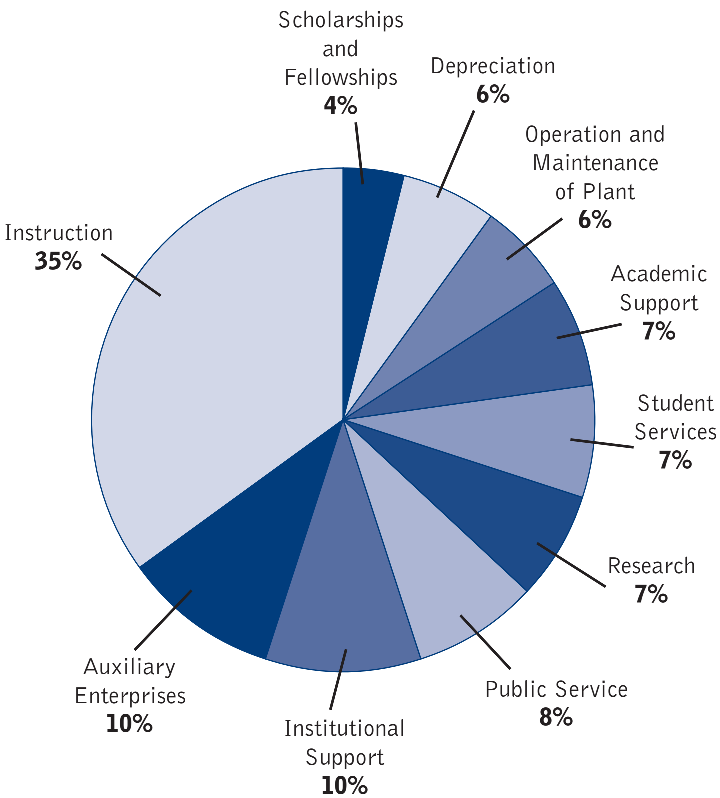
MANAGEMENT'S DISCUSSION AND ANALYSIS

Expenses - By natural classification

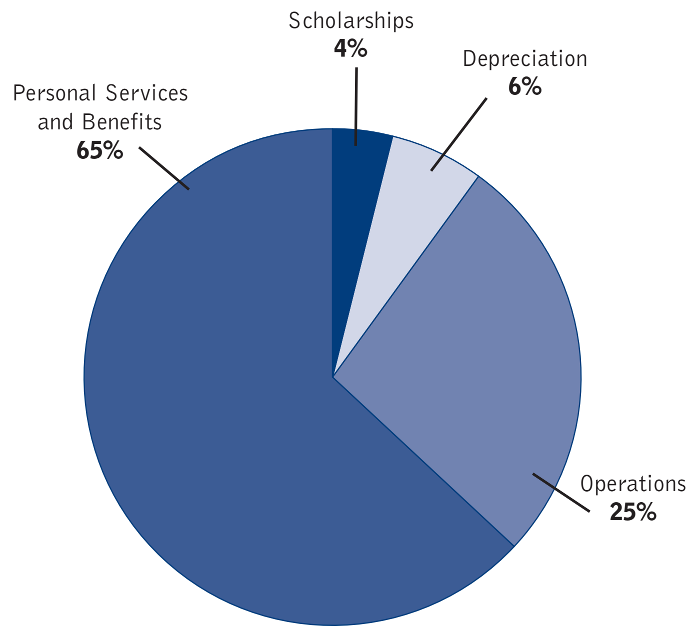
In addition to their functional (program) classification, it is also informative to review operating expenses by their natural (object) classification. A comparative summary of the University's expenses by natural classification for the years ended June 30, 2005 and June 30, 2004, is as follows:

	2005	2004
Operating:		
Personal services and benefits	$ 182,661,618	$ 173,520,202
Operations	69,400,011	71,931,360
Scholarships	10,627,631	11,934,017
Depreciation	16,227,387	16,069,536
Total operating	278,916,647	273,455,115
Nonoperating:		
Interest and other	8,344,980	5,780,915
Total expenses	$ 287,261,627	$ 279,236,030

Operating Expenses
Functional Classifications
Fiscal Year 2005



Operating Expenses
Natural Classifications
Fiscal Year 2005



CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets at June 30, 2005

At June 30, 2005, the University had $253.1 million invested in capital assets. During the year the University added $65.7 million in new capital assets and retired $7.9 million of obsolete assets. In addition, accumulated depreciation increased by $9.1 million. Details of capital assets for the years ended June 30, 2005 and 2004 are as follows:

	2005	2004
Land	$ 5,598,637	$ 5,283,663
Infrastructure	52,977,202	40,998,869
Buildings	288,375,885	258,176,852
Equipment	76,848,916	75,886,469
Library books and media	45,681,678	44,463,722
Construction in progress	34,807,074	21,662,411
Accumulated depreciation	(251,158,082)	(242,049,578)
Total capital assets	**$ 253,131,310**	**$ 204,422,408**

Significant capital additions completed or commenced, and the resources that funded their acquisitions for fiscal year 2005, were:

- Library acquisitions, $1,267,487, unrestricted net assets
- Communications Building renovation $2,368,898, bond proceeds
- Campus infrastructure upgrades, $8,772,253, bond and certificates of participation proceeds
- Applied Research and Development Building, $2,128,373, federal grant
- New College of Business Administration, $15,316,197, bond proceeds
- College of Engineering renovation and addition, $9,296,564, certificates of participation proceeds
- New Laboratory facility, $2,708,849, certificates of participation proceeds

The University's Capital Improvement Plan, which is updated annually, provides for the issuance of approximately $40.3 million in certificates of participation (COPS) and $15.3 million of bonds in fiscal year 2006. These monies will be used for the renovation of existing buildings and new building construction.

Projects in progress, or planned to commence in fiscal year 2006 funded, from fiscal years 2004 and 2005 COPS and system revenue bonds include:

- Campus infrastructure upgrades
- Completion of a new College of Business Administration building
- New Laboratory facility
- Wayfinding signage and landscape project
- College of Engineering and Technology renovation
- Completion of a new Applied Research and Development building
- Old College of Business stabilization project
- 4 level, 900 car parking structure project

In accordance with Arizona Revised Statutes § 15-1670, NAU will receive $5.9 million in State appropriations annually for lease-purchase capital financing in fiscal years 2008-2031 to fund research infrastructure projects. The construction of the Applied Research and Development Building, the College of Engineering and Technology renovation, the new laboratory facility and the north campus infrastructure projects are also to be funded from this source.

MANAGEMENT'S DISCUSSION AND ANALYSIS

CAPITAL ASSETS AND DEBT ADMINISTRATION (continued)

Outstanding Debt at June 30, 2005

At June 30, 2005, the University had $179.7 million in outstanding bonds, certificates of participation, long-term obligations, and capital leases, an increase of approximately $54.6 million or 44 percent from fiscal year 2004. This is due to a reduction of $35.9 million of principal and fiscal year borrowings of $90.5 million. The $179.7 million is made up of $126.9 million in bonds, $37.6 million of certificates of participation and $15.2 million in long-term obligations and capital leases. During the year ended June 30, 2005, the University issued $39.7 million in system revenue and refunding bonds, with an average interest rate of 4.34 percent, for various project renovations on the mountain campus and a portion was used to refund a portion of the series 1997 bonds. The University also issued certificates of participation in the amount of $37.6 million, with an average interest rate of 4.45 to finance the Applied Research and Development building and the College of Engineering and Technology Renovation project. The University entered into a capital lease for an additional $13.2 million for a student housing complex. The table below summarizes the University's outstanding debt from fiscal years 2005 and 2004.

	2005	2004
System revenue and housing bonds	$ 126,860,000	$ 122,710,000
Capital leases	13,225,000	
Certificates of participation	37,585,000	
Other long-term obligations	2,018,795	2,395,161
Subtotal	179,688,795	125,105,161
Less deferred amount on refunding	(1,823,914)	(586,852)
Plus bonds premium	4,037,928	1,755,901
Total	$ 181,902,809	$ 126,274,210

At June 30, 2005, the University maintained an A2 rating by Moody's Investors Service and an A+ rating from Standard and Poor's Rating Services. Effective in fiscal year 2003, the University was required by Arizona state law to calculate its debt capacity ratio based on the amount of debt service per fiscal year not to exceed 8 percent of projected total expenditures and mandatory transfers. At June 30, 2005, the projected ratio for the University's total debt service to projected expenditures and mandatory transfers was 6.2 percent and is well within the requirement of 8 percent. In August 2005, the University issued approximately $40.3 million of certificates of participation (COPS). The COPS were issued for various capital projects and renovations on the main campus. In November 2005, the University issued approximately $15.3 million of system revenue bonds for a parking structure on the mountain campus. Both of these debt issuances fit comfortably into the University's debt capacity according to the latest debt study as submitted to the Arizona Board of Regents.

Economic Outlook

As 2005 draws to a close, the national economy remains relatively strong considering some extraordinary events during the year. Overall economic growth, as measured by real Gross Domestic Product (GDP), will likely average 3.6% in 2005. For Arizona, the economy remained strong in 2005 and is expected to slow moderately with the national economy in the years ahead. In October 2005, the state's unemployment rate was 4.9% which nearly matched the national rate of 5.0%. In the previous 12 months, job creation in Arizona was much stronger (4.2%) than the nation (0.4%). The same trend is also found in total personal income where Arizona recorded an increase of 1.9% in the second quarter of 2005, while the national increase in total personal income was 1.5%. The 1.9% increase from the first quarter of 2005 to the second quarter placed Arizona 5th in the nation in its rate of increase.

Collection of tax receipts continued surprisingly strong in Arizona this year. The combination of strong retail sales, record breaking construction, and a strong housing market that pushed housing prices to record levels, all combined to cause the state's General Fund to grow more quickly than expected. From July to September 2005, total revenue collections by the state were $2.134 billion. That is $361.5 million (20.4%) above the same time period a year earlier and $205.6 million (10.7%) above the forecast for those 4 months. With housing prices and sales slowing, automobile sales falling, and a slowdown in the local economy, it is very unlikely that this differential will be maintained. But it does mean that the state will have significant one-time funds for the upcoming fiscal year.

The universities continue to face their unique challenges. While the state is recording significant revenue increases, it is questionable how much of that will flow to the universities. In FY 1979, Arizona's three public universities received 19.4 percent of General Fund appropriations. Currently, that level has fallen to 10.3 percent of the General Fund. And in terms of General Fund appropriations per full time equivalent student, Arizona's three universities currently receive $7,824, down $512 from its peak in 2000. Additionally, the universities have recorded more growth in this decade (15,040 students) than was recorded in all of the decade of the 1990s (9,657 students). Much of this growth is due to the State's continued population growth. Since the 1950s, Arizona has consistently ranked among the top 2-4 states in the nation for population growth, which is not expected to change in the foreseeable future.

Since the 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.

COMBINED SOURCES AND USES OF FUNDS
For the Year Ended June 30, 2005

SOURCES

State Appropriations **37.9%** Includes legislative appropriations from state of Arizona general revenue for current operations of the University and $389,000 for financial aid.	**$ 117,635,000**
Tuition and Fees, Net of Scholarship Allowances **23.9%** Includes $51,494,919 to support the operating budget, $8,245,234 for summer sessions, $40,560,860 for funding of local budgets, scholarships, and retirement of non-housing bonded indebtedness, less $26,179,623 for scholarship allowances.	**$ 74,121,390**
Government Grants and Contracts **17.5%** Includes revenues of $44,382,914 from federal grants and contracts, $4,722,213 from state grants and contracts, and $5,303,050 from local government grants and contracts.	**$ 54,408,177**
Auxiliary Enterprises **11.0%** Operations of substantially self-supporting activities such as housing, bookstore, student unions, and intercollegiate athletics.	**$ 34,047,840**
Share of State Sales Tax **4.3%** University's share of state sales tax collections from Proposition 301.	**$ 13,475,254**
Private Gifts, Grants, and Contracts **2.4%** Includes gifts, grants, and contracts for scholarships, endowments, and plant facility additions.	**$ 7,415,898**
Other Sources **1.9%** Includes additions to permanent endowments, capital grants and gifts, and other operating miscellaneous revenues.	**$ 5,932,330**
Investment Income **1.1%** Earnings from short-term investments of funds not necessary for immediate operational expenses and long-term investment of endowment and bond-retirement sinking funds.	**$ 3,549,572**
Total Sources	**$ 310,585,461**

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.

COMBINED SOURCES AND USES OF FUNDS
For the Year Ended June 30, 2005

USES

Instruction and Academic Support
41.3% — **$ 118,702,009**
Instruction, totaling $98,137,817, includes expenses of academic departments and other organizational units for undergraduate and graduate courses, and for occupational or technical instruction, including regular academic year, summer sessions, and continuing education. Academic support, totaling $20,564,192, includes libraries, audio-visual services, and academic administration.

Student Services and Institutional Support
16.5% — **$ 47,239,228**
Student services, totaling $20,031,546, includes areas such as admissions, registrar, minority services, counseling, placement, student aid administration, and health services. Institutional support, totaling $27,207,682, includes executive management, financial operations, computing support, human resource services, security, and University relations.

Research and Public Service
14.6% — **$ 41,800,222**
Research, totaling $19,615,438 are 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 $22,184,784 are 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
9.7% — **$ 27,885,480**
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.

Operation and Maintenance of Plant
5.7% — **$ 16,434,690**
Represents expenses for the operation and maintenance of plant, including administration, maintenance and custodial services, landscaping and grounds upkeep, minor repairs and renovation, utilities, and property insurance.

Depreciation
5.6% — **$ 16,227,387**
Depreciation expense of capital assets over their useful lives.

Scholarships and Fellowships
3.7% — **$ 10,627,631**
Scholarships and fellowships are awarded to students enrolled in formal coursework for which the students are not required to perform personal services or repay the awards.

Other Uses
2.9% — **$ 8,344,980**
Other uses include $7,296,214 in interest expense on capital asset-related debt, a $689,794 loss on disposal of capital assets, and $358,972 in nonoperating expenses.

Total Uses — **$ 287,261,627**

STATEMENT OF NET ASSETS
June 30, 2005

ASSETS	Business-Type Activities
Current assets:	
Cash and cash equivalents	$ 29,629,621
Investments	1,660,172
Receivables, net of allowance for uncollectibles:	
Accounts receivable	6,382,877
Accrued interest	830,164
Endowment - land sale	6,015
Government grants and contracts	14,202,781
Student loans	1,233,475
Other assets	841,361
Inventories	2,292,613
Total current assets	$ 57,079,079
Noncurrent assets:	
Restricted cash and investments held by trustee for capital projects	$ 54,998,217
Investments	33,807,295
Student loans receivable, net of allowance	4,630,174
Endowment investments	11,680,081
Other noncurrent assets	118,864
Capital assets, not being depreciated	40,405,711
Depreciable capital assets, net of depreciation	212,725,599
Total noncurrent assets	$ 358,365,941
Total assets	$ 415,445,020
LIABILITIES	
Current liabilities:	
Accounts payable	$ 6,033,194
Accrued payroll and employee benefits	6,894,239
Interest payable	1,132,627
Deferred revenue	9,266,636
Accrued compensated absences	4,108,217
Deposits held in custody for others	1,653,611
Current portion of long-term debt	10,762,588
Total current liabilities	$ 39,851,112
Noncurrent liabilities:	
Deposits held in custody for others	$ 1,007,953
Long-term debt	171,140,221
Total noncurrent liabilities	$ 172,148,174
Total liabilities	$ 211,999,286
NET ASSETS	
Invested in capital assets, net of related debt	$ 124,848,996
Restricted:	
Nonexpendable:	
Scholarships and fellowships	8,245,632
Student loans	6,931,095
Expendable:	
Scholarships and fellowships	1,185,967
Research	5,615,477
Academic department use	11,543,220
Unrestricted	45,075,347
Total net assets	$ 203,445,734

See Notes to Financial Statements

FINANCIAL STATEMENTS

STATEMENT OF FINANCIAL POSITION - Component Units
June 30, 2005

	NAU FOUNDATION	NACFFC	TOTAL
ASSETS			
Cash and cash equivalents	$ 1,506,719		$ 1,506,719
Investments	46,182,442		46,182,442
Accounts receivable	263,828	$ 49,717	313,545
Unconditional promises to give (net of allowance)	2,044,822		2,044,822
Assets held by trustee	1,363,636	20,096,328	21,459,964
Property, plant and equipment, net of depreciation	2,029	3,216,329	3,218,358
Net investment in sales-type lease		13,225,000	13,225,000
Other assets	463,683	701,368	1,165,051
Total assets	$ 51,827,159	$ 37,288,742	$ 89,115,901
LIABILITIES			
Accounts payable and accrued liabilities	$ 204,963	$ 951,191	$ 1,156,154
Bonds payable		35,480,362	35,480,362
Assets held in custody	5,320,302		5,320,302
Other liabilities	429,382	565,300	994,682
Total liabilities	$ 5,954,647	$ 36,996,853	$ 42,951,500
NET ASSETS			
Unrestricted	$ 7,081,177	$ 291,889	$ 7,373,066
Temporarily restricted	14,532,589		14,532,589
Permanently restricted	24,258,746		24,258,746
Total net assets	$ 45,872,512	$ 291,889	$ 46,164,401
TOTAL LIABILITIES AND NET ASSETS	$ 51,827,159	$ 37,288,742	$ 89,115,901

See Notes to Financial Statements

FINANCIAL STATEMENTS

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
For Year Ended June 30, 2005

	Business-Type Activities
REVENUES	
Operating Revenues	
Tuition and fees, net of scholarship allowances of $26,179,624, pledged as security for revenue bonds	$ 74,121,390
Government grants and contracts	54,025,890
Private grants and contracts	4,068,038
Auxiliary enterprises, includes revenues pledged as security for revenue bonds:	
Bookstore	8,425,495
Residence life, net of scholarship allowances of $1,906,857	15,798,055
Other auxiliaries	9,824,290
Other	5,272,627
Total operating revenues	$ 171,535,785
EXPENSES	
Operating Expenses	
Educational and general:	
Instruction	$ 98,137,817
Research	19,615,438
Public service	22,184,784
Academic support	20,564,192
Student services	20,031,546
Institutional support	27,207,682
Operation and maintenance of plant	16,434,690
Scholarships and fellowships	10,627,631
Auxiliary enterprises	27,885,480
Depreciation	16,227,387
Total operating expenses	$ 278,916,647
Operating loss	$ (107,380,862)
NONOPERATING REVENUES AND (EXPENSES)	
State appropriations	$ 117,635,000
Share of state sales tax	13,475,254
Government grants and contracts	382,287
Private gifts, grants, and contracts	3,347,860
Investment income	3,549,572
Interest expense on capital asset related debt	(7,296,214)
Loss on disposal of capital assets	(689,794)
Other nonoperating expenses	(358,972)
Total nonoperating revenues and expenses	$ 130,044,993
Income before other revenues, expenses, gains or losses	$ 22,664,131
Capital grants and gifts	$ 80,611
Additions to permanent endowments	579,092
Increase in net assets	$ 23,323,834
NET ASSETS	
Total net assets, July 1, 2004	$ 180,121,900
Total net assets, June 30, 2005	$ 203,445,734

See Notes to Financial Statements

FINANCIAL STATEMENTS

STATEMENT OF ACTIVITIES - Component Units
For Year Ended June 30, 2005

	NAU FOUNDATION	NACFFC	TOTAL
CHANGES IN UNRESTRICTED NET ASSETS			
Unrestricted support	$ 667,303	$	$ 667,303
Investment earnings	1,809,501	148,867	1,958,368
Rent		1,485,969	1,485,969
Capital lease revenue		13,225,000	13,225,000
Other	69,536	19,364	88,900
Total unrestricted support	$ 2,546,340	$ 14,879,200	$ 17,425,540
Net assets released from restrictions	3,226,830		3,226,830
Total unrestricted revenues and support	$ 5,773,170	$ 14,879,200	$ 20,652,370
Expenses and losses:			
Scholarships	$ 965,364	$	$ 965,364
Operating	1,157,619	331,085	1,488,704
Interest		505,033	505,033
Educational purposes	2,101,972		2,101,972
Amortization and depreciation		379,931	379,931
Other		523,158	523,158
Assets expensed under capital lease agreement		12,242,219	12,242,219
Total expenses and losses	$ 4,224,955	$ 13,981,426	$ 18,206,381
Increase in unrestricted net assets	$ 1,548,215	$ 897,774	$ 2,445,989
CHANGES IN TEMPORARILY RESTRICTED NET ASSETS			
Public contributions	$ 4,078,953		$ 4,078,953
Investment earnings	647,295		647,295
Other income changes	406,277		406,277
Net assets released from restrictions	(3,226,830)		(3,226,830)
Increase in temporarily restricted assets	$ 1,905,695		$ 1,905,695
CHANGES IN PERMANENTLY RESTRICTED NET ASSETS			
Public contributions	$ 963,507		$ 963,507
Investment earnings	32,575		32,575
Unrealized gain on investment or impairment of assets	5,142		5,142
Increase in permanently restricted net assets	$ 1,001,224		$ 1,001,224
INCREASE IN NET ASSETS BEFORE EXTRAORDINARY ITEM	$ 4,455,134	$ 897,774	$ 5,352,908
Loss on early debt extinguishment–unrestricted		(134,074)	(134,074)
INCREASE IN NET ASSETS AFTER EXTRAORDINARY ITEM	$ 4,455,134	$ 763,700	$ 5,218,834
NET ASSETS (DEFICIT), BEGINNING OF YEAR, AS RESTATED	$ 41,417,378	$ (471,811)	$ 40,945,567
NET ASSETS, END OF YEAR	$ 45,872,512	$ 291,889	$ 46,164,401

See Notes to Financial Statements

FINANCIAL STATEMENTS

STATEMENT OF CASH FLOWS
For Year Ended June 30, 2005

	Business-Type Activities
Cash flows from operating activities:	
Tuition and fees	$ 72,190,130
Grants and contracts	52,037,893
Payments to suppliers and providers of goods and services	(69,535,379)
Payments to employees	(178,326,141)
Payments for scholarships and fellowships	(10,627,631)
Loans issued to students	(1,204,597)
Collection of loans to students	1,708,008
Auxiliary enterprise receipts:	
Residence halls	16,943,744
Bookstore	8,469,107
Other auxiliaries	11,601,479
Other receipts	4,744,382
Net cash used by operating activities	$ (91,999,005)
Cash flows from noncapital financing activities:	
State appropriations	$ 117,635,000
Share of state sales tax	12,689,421
Gifts and grants for other than capital purposes	3,730,147
Federal direct student lending received	79,933,860
Federal direct student lending disbursed	(79,933,860)
Private gifts for endowment purposes	579,092
Funds held for others	(407,852)
Net cash provided by noncapital financing activities	$ 134,225,808
Cash flows from capital financing activities:	
Proceeds from issuance of capital debt	$ 52,005,000
Capital grants and gifts received	13,867
Proceeds from sale of capital assets	104,582
Purchases of capital assets	(52,438,921)
Principal paid on capital debt and leases	(10,646,366)
Interest paid on capital debt and leases	(7,232,178)
Net cash used by capital financing activities	$ (18,194,016)
Cash flows from investing activities:	
Proceeds from sales and maturities of investments	$ 3,021,678
Interest on investments	3,870,914
Purchase of investments	(18,845,388)
Net cash used by investing activities	$ (11,952,796)
Net increase in cash and cash equivalents	$ 12,079,991
Cash and cash equivalents - beginning of year	72,547,847
Cash and cash equivalents - end of year	$ 84,627,838
Reconciliation of operating loss to net cash used by operating activities:	
Operating loss	$ (107,380,862)
Adjustments to reconcile operating loss to net cash used by operating activities:	
Depreciation expense	16,227,387
Changes in assets and liabilities - cash increase (decrease) related to:	
Receivables:	
Accounts receivable	981,008
Government grants and contracts	(5,515,857)
Student loans receivables and accrued interest from student loans	513,552
Inventories	(222,718)
Other assets	(330,596)
Accounts payable	87,350
Accrued payroll and employee benefits	1,311,791
Deferred revenue	1,446,506
Deposits held in custody for others	567,694
Accrued compensated absences	315,738
Net cash used by operating activities	$ (91,999,005)
Noncash transactions	
Book value of refunded debt	$ 25,255,000
Payment to escrow agent for advanced debt refunding	(26,700,087)
Deferred loss on advanced debt refunding	1,445,087
Capital asset acquired through capital lease	13,225,000
Capital lease liability	(13,225,000)
Gifts of capital assets	66,744
Decrease in fair value of investments	(124,795)
Amortization on loss of refunding and bond premium	111,742
Losses on disposal of capital assets, net	689,794

See Notes to Financial Statements

Note 1—Summary of Significant Accounting Policies

Financial Statement Presentation

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

During the year ended June 30, 2005, the University implemented the provisions of GASB Statement No. 40, *Deposit and Investment Risk Disclosures*. GASB Statement No. 40 establishes and modifies the risk disclosures about the University's deposits and investments. The implementation of GASB Statement No. 40 requires only additional disclosures, and had no effect on reported amounts for deposits, investments, net assets, or changes in net assets.

Reporting Entity

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

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

NACFFC was incorporated in October 2001, as a legally separate 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.

Basis of Accounting

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

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

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

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

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

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

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

Cash and Cash Equivalents

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

Investments

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

Receivables

Student loans and accounts receivable as of June 30, 2005, are reported less allowances for both estimated uncollectible amounts and collection costs of $951,750 and $1,164,500, respectively.

Inventories

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

Special Collections

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

Compensated Absences

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

Investment Income

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

Capital Assets

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

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

Scholarship Allowances

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

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

Note 2—Cash and Investments

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 govern 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 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 and constitute the University's investment policy.

Gifts and endowments monies are invested in accordance with conditions stipulated by the donor.

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, 2005, cash on hand was $51,286, the carrying amount of the University's deposits was ($647,671) and the bank balance was $2,778,199. 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, 2005, $2,678,199 of the University's bank balance was uninsured with collateral held by the pledging financial institution.

Investments

	Amount
State Treasurer's investment pool	$ 29,719,082
U.S. agency securities	35,467,467
Student Financial Aid Trust Fund	7,866,314
Bond Trustee Funds:	
Government Money Market Mutual Fund	54,484,832
State Treasurer's investment pool	513,385
Investments with NAU Foundation	4,320,691
	$ 132,371,771

The State Board of Investment provides oversight for the State Treasurer's investment pools, and the Local Government Investment Pool Advisory Committee provides consultation and advice to the Treasurer. The fair value of the University's investment in the pool approximates the value of the University's pool shares and the University's shares are not identified with specific investments.

Credit Risk

Beyond the requirements established by ABOR, the University does not have a formal policy with respect to credit risk. At June 30, 2005, credit risk for the University investments were as follows:

Investment Type	Rating	Rating Agency	Amount
U.S. agency securities	AAA	Standard and Poors	$ 35,467,467
State Treasurer's investment pool	unrated	N/A	29,719,082
Student Financial Aid Trust Fund	unrated	N/A	7,866,314
Bond Trustee Funds:			
Government Money Market Mutual Fund	AAA	Standard and Poors	54,484,832
State Treasurer's investment pool	unrated	N/A	513,385
Investments with NAU Foundation	unrated	N/A	4,320,691
			$ 132,371,771

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

The Student Financial Aid Trust Fund was established in accordance with A.R.S. §15-1642 for the purpose of providing aid to students with verifiable financial need. The three state universities participate in the Trust Fund, which is held with and managed by the University of Arizona. The University's ownership interest is recorded in the University of Arizona's records.

Trust agreements between the University and the NAU Foundation, Inc. authorize the Foundation to invest certain University restricted and endowment monies according to the Foundation's established investment policies and procedures. The University's portion is not identified with specific investments. The University's ownership interest is recorded in the Foundation's records.

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, 2005, the University had $35,467,467 of U.S. agency securities that were uninsured and held by the counterparty not in the University's name and $54,484,832 of mutual funds in trustee accounts that were uninsured and held by the counterparty not in the University's name.

Concentration of Credit Risk
The University does not have a formal policy in regards to concentration of credit risk. The University places no limit on the amount that the University may invest in any one issuer. Five percent or more of the University's investments at June 30, 2005, were in Federal Home Loan Bank securities and Federal Home Loan Mortgage Corporation securities. These investments were 12.32 percent, and 8.79 percent, respectively, of the University's total investments.

Interest Rate Risk
The University does not have a formal policy in regards to interest rate risk.

Investment Type	Fair Value	Less Than 1 Year	1-5 Years	6-10 Years	More than 10 Years
State Treasurer's investment pool	$ 30,232,467	$ 30,232,467			
U.S. agency securities	35,467,467	1,660,172	$ 33,807,295		
NAU Foundation	4,320,691	638,598	2,477,484	$ 973,020	$ 231,589
Student Financial Aid Trust Fund	7,866,314		7,866,314		
Government Money Market Mutual Fund	54,484,832	54,484,832			
Total	$ 132,371,771	$ 87,016,069	$ 44,151,093	$ 973,020	$ 231,589

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	$ 51,286
Cash in bank	(647,671)
Total investments	132,371,771
	$ 131,775,386

Statement of Net Assets:

Cash and cash equivalents	$ 29,629,621
Current investments	1,660,172
Restricted cash and investments held by trustee for capital projects	54,998,217
Noncurrent investments	33,807,295
Endowment investments	11,680,081
	$ 131,775,386

Note 3—Capital Assets

Capital asset activity for the year ended June 30, 2005, was as follows:

	Balance June 30, 2004	Additions	Retirements	Transfers	Balance June 30, 2005
Capital assets not being depreciated:					
Land	$ 5,283,663	$ 314,974			$ 5,598,637
Construction in progress	21,662,411	44,147,747	$ 8,212	$ (30,994,872)	34,807,074
Total capital assets not being depreciated	26,946,074	44,462,721	8,212	(30,994,872)	40,405,711
Capital assets being depreciated:					
Infrastructure	40,998,869	226,402		11,751,931	52,977,202
Buildings	258,176,852	15,227,137	4,271,045	19,242,941	288,375,885
Equipment	75,886,469	4,546,918	3,584,471		76,848,916
Library books and media	44,463,722	1,267,487	49,531		45,681,678
Total capital assets being depreciated	419,525,912	21,267,944	7,905,047	30,994,872	463,883,681
Less accumulated depreciation for:					
Infrastructure	19,042,989	1,452,434			20,495,423
Buildings	128,147,134	7,657,967	3,582,542		132,222,559
Equipment	58,775,963	5,106,778	3,486,810		60,395,931
Library books and media	36,083,492	2,010,208	49,531		38,044,169
Total accumulated depreciation	242,049,578	16,227,387	7,118,883		251,158,082
Total capital assets being depreciated, net	177,476,334	5,040,557	786,164	30,994,872	212,725,599
Capital assets, net	**$204,422,408**	**$ 49,503,278**	**$ 794,376**	**$ –**	**$ 253,131,310**

The estimated cost to complete construction in progress at June 30, 2005, totaled $90,902,600.

Note 4—Long-Term Liabilities

Long-term liability activity for the year June 30, 2005, was as follows:

	Balance June 30, 2004	Additions	Reductions	Balance June 30, 2005	Due Within One Year
Long-term obligations	$ 2,395,161		$ 376,366	$ 2,018,795	$ 348,071
Capital leases		$ 13,225,000		13,225,000	114,167
Certificates of participation		37,585,000		37,585,000	
Revenue and housing bonds payable	122,710,000	39,675,000	35,525,000	126,860,000	10,310,000
Less deferred amount on refunding	(586,852)	(1,445,087)	(208,025)	(1,823,914)	(266,217)
Bonds premium	1,755,901	2,440,326	158,299	4,037,928	256,567
Total long-term liabilities	**$126,274,210**	**$ 91,480,239**	**$ 35,851,640**	**$181,902,809**	**$ 10,762,588**

Optional retirement monies held by the University for employees that have not been with the University for five years and therefore have not vested, were included in long-term debt on the Statement of Net Assets in the prior year. In the current year, these monies are reported as deposits held in custody for others on the Statement of Net Assets.

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

Bonds payable at June 30, 2005, are as follows:

Student housing bonds (2 issues) - 5.5 percent to 6.1 percent, principal payable annually on April 1 through 2009, revenues of various housing projects pledged for payment	$ 645,000
System revenue bonds, Series of 1997 - 6.5 percent, principal maturing serially on June 1, 2009 and 2010, secured by a first lien on certain gross revenues, on parity with the Series 2002 system revenue refunding bonds, Series 2002 system revenue bonds, Series 2003 system revenue bonds, and Series 2004 system revenue and refunding bonds	$ 5,645,000
System revenue refunding bonds, Series of 2002 - 3.0 percent to 4.0 percent, principal maturing serially on June 1 through 2008, secured by a first lien on certain gross revenues, on parity with the Series 1997 system revenue bonds, Series 2002 system revenue bonds, Series 2003 system revenue bonds, and Series 2004 system revenue and refunding bonds	$ 24,625,000
System revenue bonds, Series of 2002 - 3.0 percent to 5.125 percent, principal maturing serially on June 1 through 2034, secured by a first lien on certain gross revenues, on parity with the Series 1997 system revenue bonds, Series 2002 system revenue refunding bonds, Series 2003 system revenue bonds, and Series 2004 system revenue and refunding bonds	$ 26,115,000
System revenue bonds, Series of 2003 - 2.5 percent to 5.5 percent, principal maturing serially on June 1 through 2034, secured by a first lien on certain gross revenues, on parity with the Series 1997 system revenue bonds, Series 2002 system revenue refunding bonds, Series 2002 system revenue bonds, and Series 2004 system revenue and refunding bonds	$ 30,905,000
System revenue and refunding bonds, Series of 2004 - 3.0 percent to 5.25 percent, principal maturing serially on June 1 through 2034, secured by a first lien on certain gross revenues, on parity with the Series 1997 system revenue bonds, Series 2002 system revenue refunding bonds, Series 2002 system revenue bonds, and Series 2003 system revenue bonds.	$ 38,925,000
	$ 126,860,000

The following schedule details debt service requirements to maturity for the University's bonds payable at June 30, 2005.

	Revenue and Housing Bonds	
	Principal	**Interest**
Year Ending June 30,		
2006	$ 10,310,000	$ 5,959,756
2007	10,155,000	5,568,706
2008	9,330,000	5,184,491
2009	4,485,000	4,828,756
2010	4,580,000	4,592,856
2011-15	26,190,000	19,606,434
2016-20	19,220,000	13,373,881
2021-25	13,810,000	9,635,769
2026-30	14,360,000	6,109,350
2031-34	14,420,000	1,937,388
Total	$126,860,000	$ 76,797,387

Bonds

On December 16, 2004, the University sold System Revenue and Refunding Bonds Series 2004 for $39,675,000 dated December 1, 2004. The 2004 Bonds include $35,225,000 of serial bonds with interest rates ranging from 3.00% to 5.25% and maturity dates ranging from June 1, 2005 to June 1, 2024. The 2004 Bonds also include $4,450,000 of term bonds, with interest rates ranging from 4.375% to 4.75% and maturing on June 1, 2021, 2029, and 2034. The 2004 Bonds were sold with net original issue premium of $2,440,326. The University realized net proceeds of $41,700,087 after payment of $415,239 for issuance costs, underwriter discounts, and bond insurance. The costs associated with this issue were recorded in the current fiscal year. The net proceeds of $15,000,000 are being used to finance five separate projects on the University's Mountain Campus and $26,700,087 was used to purchase U.S. government obligations placed in an irrevocable trust to advance refund $25,255,000 of the System Revenue Bonds Series 1997 previously issued by the University.

The Series 2004 System Revenue and Refunding Bonds, have an average interest rate of 4.34%, and the refunded portion of the Series 1997 system revenue bonds had an average interest rate of 5.03%. Although the recognition of the difference between the reacquisition price and the net carrying amount of the old debt of $1,445,087, which was reported in the financial statements as a deferred charge, for the year ended June 30, 2005, the University reduced its aggregate debt service payments by $1,077,005 over the next 12 years and obtained an economic gain (i.e., the difference between present values of the old and the new debt service payments) of $834,524.

In prior years, the University defeased certain revenue bonds by either placing the proceeds of new bonds, or cash and investments accumulated in a sinking fund, in an irrevocable trust to provide for all future debt service payments on the refunded bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the University's financial statements. At June 30, 2005, $25,475,000 of such bonds outstanding are considered defeased.

Certificates of Participation

On July 29, 2004, the University issued Certificates of Participation, Series 2004 for $37,585,000, dated July 1, 2004. The Series 2004 Certificates included $20,100,000 of serial certificates with interest rates ranging from 2.5% to 5.125% and maturity dates ranging from 2007 to 2026. The Series 2004 Certificates also included $17,485,000 of term certificates with interest rates ranging from 4.75% to 5.00% and maturing on September 1, 2019, 2026, and 2030. The 2004 Certificates were issued at a premium of $582,811. The University realized net proceeds of $37,512,611 after payment of $655,200 for issuance costs, underwriters discount, and bond insurance. The premium and costs associated with this issue were recorded in the current fiscal year. The net proceeds are being used to finance the Applied Research and Development building and the College of Engineering and Technology Renovation project.

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), an existing complex, and McKay Village (MV), a complex under construction. The University recorded a capital lease of $13.2 million in fiscal 2005 for the PRV complex. The University will record a capital lease of approximately $22.7 million for the MV complex when construction is completed. Cash outflows for MV related lease payments are not scheduled to begin until the end of fiscal year 2006.

Base lease payments for both housing complexes are tied to the variable rate interest payments on the Variable Rate Demand Revenue Bonds, Series 2005 issued by PRV/CH. The interest on these bonds is adjusted weekly to the Bond Market Association Municipal Index. However, through an interest rate swap agreement, interest payments on the bonds are fixed for the first 10 years at 3.161%. Subsequent years' interest payments were calculated based on the actual variable rate of 2.320% as of June 30, 2005. A capitalized interest account for the MV complex was funded to cover MV-related bond payments through completion of construction.

Minimum lease payment commitments for the PRV complex, including interest reimbursement to the lessor at a fixed rate for the first ten years and at the variable rates in effect at June 30, 2005, for all subsequent years consisted of the following:

The following schedule details debt service requirements to maturity for the University's certificates of participation payable at June 30, 2005.

	Certificates of participation	
	Principal	**Interest**
Year ended June 30,		
2006	$ –	$ 1,743,069
2007	–	1,743,069
2008	920,000	1,723,902
2009	950,000	1,696,319
2010	975,000	1,667,194
2011-15	5,480,000	7,718,806
2016-20	6,785,000	6,380,644
2021-25	8,710,000	4,412,317
2026-30	11,175,000	1,908,941
2031	2,590,000	21,583
Total	$ 37,585,000	$ 29,015,844

Year ended June 30,	Capital Lease Payments (in thousands)
2006	$ 494
2007	524
2008	540
2009	551
2010	566
2011-15	3,113
2016-20	3,061
2021-25	3,678
2026-30	4,397
2031-33	3,068
Total minimum lease payments	19,992
Less amount representing interest	(6,767)
Present value of minimum lease payments	$ 13,225

Note 5—Retirement Plans

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

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

For the year ended June 30, 2005, active ASRS members and the University were each required by statute to contribute at the actuarially determined rate of 5.70 percent (5.20 percent retirement and 0.50 percent long-term disability) of the members' annual covered payroll. The University's retirement contributions to the ASRS for the years ended June 30, 2005, 2004, and 2003 were $2,964,056, $2,822,407 and $1,148,814, respectively, which were equal to the required contributions for the year. The Arizona State Legislature establishes and may amend active plan members' and the University's contribution rates.

In accordance with A.R.S. § 15-1628, University faculty, academic professionals, and administrative officers have the option to participate in defined contribution pension plans. These plans are administered by independent insurance and annuity companies approved by the Arizona Board of Regents. For the year ended June 30, 2005, plans offered by the Teachers Insurance Annuity Association/College Retirement Equities Fund (TIAA/CREF), Variable Annuity Life Insurance Company (VALIC), Fidelity Investments Tax-Exempt Service Company (Fidelity), Aetna Life Insurance and Annuity Company (Aetna), and Vanguard Group (Vanguard) were approved by the Board. Benefits under these plans depend solely on the contributed amounts and the returns earned on investments of those contributions.

Contributions made by members vest immediately, and University contributions vest after five years of benefit eligible employment. The distribution of member contributions and associated investment earnings are made in accordance with the member's contract with the applicable insurance and annuity company. University contributions and associated investment earnings must be distributed to the member in the form of an annuity paid over a period that is not less than the member's life. The Arizona State Legislature establishes and may amend active plan members' and the University's contribution rates. For the year ended June 30, 2005, plan members and the University were each required by statute to contribute an amount equal to 7 percent of a member's compensation. Contributions to Retirement Plans for the year ended June 30, 2005, are summarized below.

Contributions to Retirement Plans
for the year ended June 30, 2005, are summarized below.

Plan	University Contributions	Member Contributions	Total Contributions
TIAA/CREF	$ 2,666,369	$ 2,666,369	$ 5,332,738
VALIC	$ 564,118	$ 564,118	$ 1,128,236
Fidelity	$ 581,702	$ 581,702	$ 1,163,404
Aetna	$ 133,953	$ 133,953	$ 267,906
Vanguard	$ 204,746	$ 204,746	$ 409,492

Note 6—Risk Management

The University is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The University participates in a self-insurance program administered by the State of Arizona, Department of Administration, Risk Management Section. A.R.S. §41-621 et seq. provides that losses eligible for coverage and which are not covered by insurance will be paid by the State from the self-insurance program or by a future appropriation from the State Legislature. Loss risks which are not covered by Risk Management and where the University has no insurance coverage, are losses that arise from contractual breaches and are directly attributable to an act or omission, and determined to be a felony by a court of law. With this exception, the University has no significant risk of loss beyond adjustments to future years' premium payments to the State's self-insurance program. All estimated losses for unsettled claims and actions of the State are determined on an actuarial basis and are included in the State of Arizona Comprehensive Annual Financial Report.

NOTES TO FINANCIAL STATEMENTS

June 30, 2005

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, 2005 • Natural Classification

	Personal Services and Benefits	Operations	Scholarships	Depreciation	Total
Functional Classification:					
Instruction	$ 85,391,107	$ 12,746,710			$ 98,137,817
Research	14,673,167	4,942,271			19,615,438
Public service	10,860,417	11,324,367			22,184,784
Academic support	16,427,405	4,136,787			20,564,192
Student services	14,862,904	5,168,642			20,031,546
Institutional support	19,067,882	8,139,800			27,207,682
Operation and maintenance of plant	7,144,659	9,290,031			16,434,690
Scholarships and fellowships			$ 10,627,631		10,627,631
Auxiliary enterprises	14,234,077	13,651,403			27,885,480
Depreciation				$ 16,227,387	16,227,387
Total	$ 182,661,618	$ 69,400,011	$ 10,627,631	$ 16,227,387	$ 278,916,647

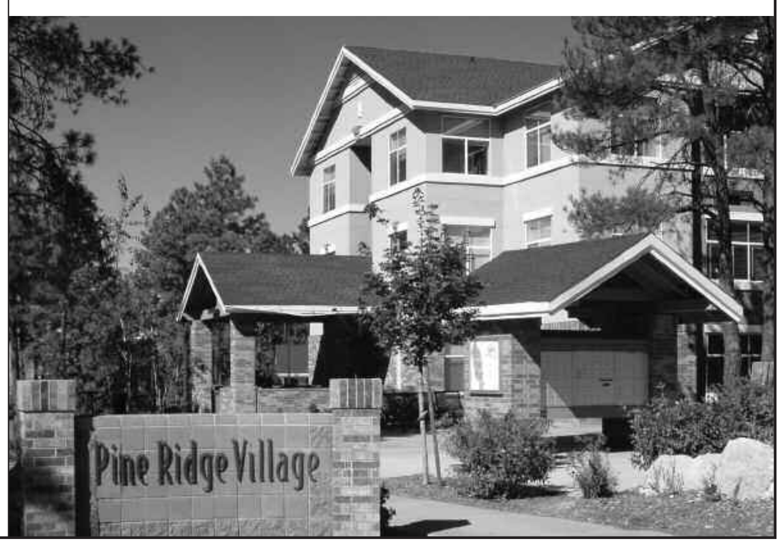
Note 8—Other Matters

Subsequent Events

In August 2005 the University issued approximately $40.3 million of certificates of participation (COPS) for various capital projects and renovations on the main campus. In November 2005, the University issued approximately $15.3 million of system revenue bonds for the purpose of constructing a parking structure on the mountain campus. These bonds are secured by a first lien on certain gross revenues and are on parity with the Series 1997 system revenue bonds, the Series 2002 system revenue bonds, the Series 2002 system revenue refunding bonds, the Series 2003 system revenue bonds, and the Series 2004 system revenue and refunding bonds.

Tuition Lawsuit

In August 2003, four University of Arizona students filed a lawsuit against the Arizona Board of Regents and the State of Arizona in Pima County (Arizona) Superior Court. The complaint alleged that the tuition increase approved by the Board for the 2003-04 academic year violates the State's constitution. The plaintiff's requested that the suit be certified as a class action on behalf of all students at the three universities governed by the Board. The complaint also asserted that the State has not provided funding to the three universities governed by the Board at the level required by the state constitution. The complaint sought (i) a declaratory judgement that the actions of each of the defendants violate the state constitution, (ii) preliminary and permanent injunctive relief to prevent the Board from imposing the tuition increase, and to compel repayment of any amounts already collected, and (iii) preliminary and injunctive relief ordering the State to set in place a plan to provide increased funding for maintenance, operation, and improvement of the State's universities. In March 2004, the Superior Court granted the Board's and the State's motion to dismiss the case. In the related minute entry, the court held that in the exercise of its legislative and administrative function, which includes setting tuition levels for the State's three universities, the Board is absolutely immune from suit and that the conduct of the business of the State Legislature is absolutely immune from suit. The plaintiffs have filed a notice of appeal with the Arizona Court of Appeals, and the State has filed their answering brief in the appeal, and oral arguments took place in February 2005. To date the Court has not issued a decision in the case. The Board intends to vigorously defend the appeal. Management believes that the claim can be adequately and successfully defended, but is not able to predict at the present time what the ultimate outcome of the matter will be or how the case may affect the financial condition of the University. An adverse judgment in the litigation would be covered by the statutory self-insurance program under the State of Arizona, Department of Administration—Risk Management.



Note 9—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 LLC (limited liability company) subsidiary, have been prepared on the accrual basis.

Financial Statement Presentation

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

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

Cash and Cash Equivalents

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

Investments

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

Revenue Recognition

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

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

The NACFFC recognizes rent and lease income 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. Under the sales-type lease, minimum lease payments are based on a variable interest rate determined on a weekly basis. Therefore, the payments and unearned income are periodically revalued to reflect current rates.

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 LLC in the event of default.

Property, Plant and Equipment

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

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

Use of Estimates

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

NOTES TO FINANCIAL STATEMENTS

June 30, 2005

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 $698,762 relating to the Series 2005 Bonds are being amortized on a straight-line basis over the life of the Series 2005 Bonds. Amortization expense for the year ended June 30, 2005, was $2,080 for issuance costs related to the Series 2005 bonds and $14,798 for issuance costs related to the Series 2001 bonds prior to their refunding. Amortization expense for issuance costs related to the Series 2005 bonds is anticipated to be $24,953 annually.

B. RESTATEMENT OF NET ASSETS

During fiscal year 2005, the Foundation determined that there were three funds that the Foundation was holding in custody for Northern Arizona University that should be excluded from the Foundation's net assets. These three funds were not included in the prior year determination of the assets held in custody for others balance. As a result, the beginning temporarily restricted net asset balance was reduced by $29,463 and the beginning permanently restricted net asset balance was reduced by $689,630.

C. ASSETS HELD BY TRUSTEE

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

NACFFC - Pursuant to the terms of the Trust Indenture, relating to the Series 2005 Bonds, proceeds of the Series 2005 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 $20,069,206 at June 30, 2005. These assets are invested in 100% U.S. Treasury money market funds. Cash of $27,122, is restricted by the Series 2005 Bond Trust Indenture, and is covered by Federal Depository Insurance. Currently all accounts held by the Trustee are restricted as to use.

D. INVESTMENTS

The fair value and cost of the Foundation's investments at June 30, 2005 is as follows:

	Fair Value	Cost
U.S. Government/agency bonds	$ 12,126,629	$ 12,418,493
Corporate bonds	5,855,473	5,687,321
Common stock	23,541,165	20,926,143
International equity funds	4,618,357	4,064,838
Real estate investment trust	40,818	36,507
	$ 46,182,442	$ 43,133,302

Investments include funds held for the custody of others of $4,580,385 at June 30, 2005.

The realized gains and unrealized gains on investments were $648,558 and $686,756 for the year ended June 30, 2005. Investment expenses of $119,428 for the year ended June 30, 2005 have been netted against investment earnings in the statement of activities.

The fair value and cost of the NACFFC's investments at June 30, 2005 is as follows:

	Fair Value	Cost
Investments held by Trustee		
Cash	$ 27,122	$ 27,122
U.S. Treasury money market funds	20,069,206	20,069,206
	$ 20,096,328	$ 20,096,328

E. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are comprised of construction in progress, furniture and equipment and are reported net of accumulated depreciation. Construction in progress is not depreciated. Balances as of June 30, 2005 are presented as follows:

FOUNDATION

	Cost or Donated Value	Accumulated Depreciation	Net Assets
Furniture and equipment	$ 13,280	$ (11,251)	$ 2,029

NACFFC

	Cost or Donated Value	Accumulated Depreciation	Net Assets
Construction in progress	$ 3,216,329	$ 0	$ 3,216,329

F. LEASE PURCHASE AGREEMENT

On May 1, 2005, the NACFFC transferred its interest in its ground lease agreement with ABOR to the Pine Ridge Village/Campus Heights LLC. On May 19, 2005, the Pine Ridge Village/Campus Heights LLC entered into a lease purchase agreement with Northern Arizona University. During the 28 year lease term, the University will make lease payments on two apartment-style student housing complexes, Pine Ridge, an existing complex, and Campus Heights, a complex under construction. Pine Ridge Village/Campus Heights LLC recorded a sales-type lease receivable of $13,225,000 in fiscal year 2005 for the Pine Ridge Village complex. The agreement also provides for Northern Arizona University to lease purchase the Campus Heights complex for approximately $22,685,000 upon its completion in fiscal year 2006. Upon expiration of the lease, the real property will become the sole property of the University without further cost.

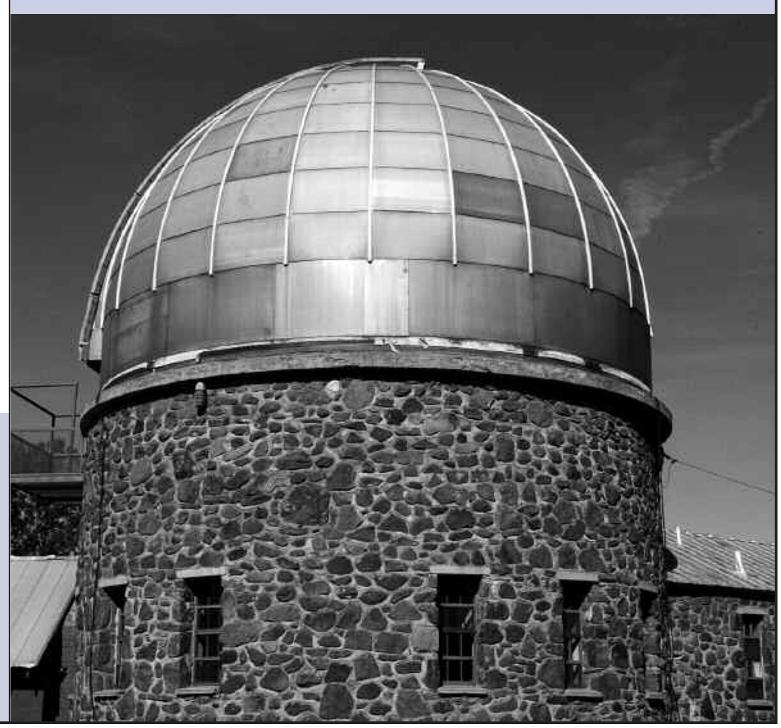
Base lease payments for both housing complexes are tied to the variable rate interest payments on the series 2005 demand revenue bonds issued by the Pine Ridge Village/Campus Heights LLC. However, through an interest rate swap agreement, interest payments on the bonds are fixed for the first 10 years at 3.161%. A capitalized interest account for the Campus Heights project was funded to cover Campus Heights related bond payments through the completion of construction. As a result, cash flows for the Campus Heights related lease payments are not scheduled to begin until the end of fiscal year 2006.

Components of the net investment in the lease (based on interest at the variable rates in effect at June 30, 2005) are as follows:

Total minimum lease payments to be received	$ 19,935,000
Less: Unearned income	(6,710,000)
Net investment in sales-type lease	$ 13,225,000

At June 30, 2005, minimum lease payments are as follows:

Year ended June 30,	Amount
2006	$ 522,000
2007	523,000
2008	539,000
2009	550,000
2010	565,000
Thereafter	17,236,000
	$ 19,935,000



G. BONDS PAYABLE

The NACFFC through its Pine Ridge Village/Campus Heights LLC subsidiary, had the following bonds outstanding at June 30, 2005:

Variable Rate Demand Revenue Bonds, Series 2005 in the aggregate original principal amount of $35,910,000 dated May 19, 2005; interest payable monthly at a variable rate determined on a weekly basis, 2.32 percent at June 30, 2005; interest rate fixed through a swap agreement at 3.161 percent from July 1, 2005 through June 1, 2015; principal payable annually in various amounts beginning June 1, 2006 through June 1, 2033; secured by property, leases and revenues including the Trust Funds, excluding the Rebate Fund, under terms of the Trust Indenture.	$ 35,910,000
Less: Unamortized bond discount	(459,638)
Bonds payable, net	35,480,362
Less: current maturities	(105,000)
Bonds payable, noncurrent portion, net	$ 35,375,362

At June 30, 2005, maturities of bonds payable are as follows:

Year ending June 30,	
2006	$ 105,000
2007	460,000
2008	355,000
2009	400,000
2010	455,000
Thereafter	34,135,000
Total	$ 35,910,000

Interest expense related to bonds for 2005 was $528,565. This includes $23,286 under the terms of the swap agreement. Of this, $23,532 was capitalized. Amortization of the bond discount for 2005 was $1,283 and is included in interest expense in the accompanying financial statements.

The Pine Ridge Village/Campus Heights LLC issued the Series 2005 Variable Rate Demand Bonds (Series 2005 Bonds) for the purpose of financing the acquisition of the Pine Ridge Village Project from the NACFFC, and financing the development, construction, equipping and leasing of a new housing facility on the Flagstaff, Arizona campus of NAU for use by eligible tenants. The NACFFC used the Series 2005 Bond proceeds allocated for the acquisition of the Pine Ridge Village project to refund its outstanding Series 2001 bonds.

Debt Extinguishment

$13,225,000 of the Series 2005 Variable Rate Demand Revenue Bonds, issued May 19, 2005 by the Pine Ridge Village/Campus Heights LLC was used to redeem the NACFFC Series 2001 Bonds, dated October 31, 2001. The Series 2001 Bonds were completely redeemed in June 2005. In accordance with Accounting Principles Board (APB) Opinion, APB 26, *Early Extinguishment of Debt*, the redemption is considered an early extinguishment of debt. Under APB 26, the Series 2001 Bonds were removed from the books at their net carrying value, which represents the amount due at maturity adjusted for accrued interest, costs of issuance and unamortized premium. The extinguishment resulted in a loss of $134,074, which in accordance with APB Opinion 30, *Reporting the Results of Operations – Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions*, is recorded as an extraordinary item in the accompanying financial statements.

As both the 2001 Bond and the 2005 Bond issues were variable rate bonds, no economic gain or loss can be calculated.

Swap Agreement

Pine Ridge Village/Campus Heights LLC entered into an interest rate swap arrangement dated May 26, 2005 that effectively fixed the interest rate on the demand revenue bonds at 3.161 percent. Under the swap agreement, Pine Ridge Village/Campus Heights LLC pays interest at the variable rate and receives interest at 70% of the one month LIBOR. An additional payment is made or received by the Pine Ridge Village/Campus Heights LLC to effectively fix the interest rate at 3.161. The notional amount of the contract as of June 30, 2005 is $35,910,000 and matures June 1, 2015. The notional amount under the swap agreement decreases as principal payments are made on the Series 2005 demand revenue bonds so that the notional amount equals the principal outstanding under the bonds.

Redemption Provisions

The Series 2005 Bonds, while in a weekly rate mode, are subject to redemption, at the option of Pine Ridge Village/Campus Heights LLC , on any business day, in whole or in part, at a redemption price equal to 100% of the principal amount thereof plus accrued interest to the redemption date. The bonds may be converted to a fixed rate mode at the election of Pine Ridge Village/Campus Heights LLC. If the bonds are converted to a fixed rate mode, the bonds can be redeemed, at the option of Pine Ridge Village/Campus Heights LLC, in whole or in part at any time, at a redemption price equal to the percentages of the principal amount of each Series 2005 bond or portion thereof to be redeemed, plus accrued interest as follows.

NOTES TO FINANCIAL STATEMENTS

June 30, 2005

Number of years remaining to maturity at the date of Conversion	Number of years following conversion to the Fixed Rate Mode when the Series 2005 may be redeemed and redemption price	
	More than 10 but less than 11 years	More than 11 years
11 years or more	101%	100%
10 years but less than 11 years	100%	Not applicable
Less than 10 years	Not subject to redemption	

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, 2005:

Cash	$ 147,370
Unconditional promises to give	8,765
Investments	4,580,385
Beneficial interest in perpetual trust	583,782
	$ 5,320,302

Assets held on behalf of:	
Northern Arizona University	$ 4,923,434
Parents' Association	200,525
Alumni Association	196,343
	$ 5,320,302

I. OTHER MATTERS

On May 3, 2005 the Pine Ridge Village/Campus Heights LLC entered into a construction agreement with Kitchell Contractors, Inc. of Arizona. The contract provides for the construction of the residential facility at the Campus Heights project. The anticipated cost of construction is estimated at $19,161,000 with substantial completions by June 29, 2006. Draws are made upon certification of completion from the architect.