

Ohio University
(A Component Unit
of the State of Ohio)

Financial Statements for the Years
Ended June 30, 2004 and 2003
and Independent Auditors' Report

OHIO UNIVERSITY
(A Component Unit of the State of Ohio)

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INDEPENDENT AUDITORS' REPORT

To the Board of Trustees of
Ohio University
Athens, Ohio

We have audited the accompanying statements of net assets of Ohio University (the "University"), a component unit of the State of Ohio, as of June 30, 2004 and 2003 and the related statements of revenues, expenses and changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audits.

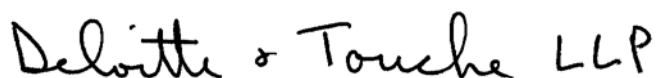
We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the respective financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 1 to the financial statements, in fiscal year 2004, the University adopted Governmental Accounting Standards Board ("GASB") Statement No. 39, *Determining Whether Certain Organizations are Component Units*.

In our opinion, such financial statements present fairly, in all material respects, the financial position of Ohio University as of June 30, 2004 and 2003, and their changes in net assets and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis ("MD&A") on pages 2 through 9 is not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of the University's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit such information and we do not express an opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 22, 2004, on our consideration of internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.



October 22, 2004

OHIO UNIVERSITY

Management's Discussion and Analysis

The following Management's Discussion and Analysis ("MD&A") of the financial statements of Ohio University (the "University") provides an overview of its financial activities for the fiscal year ("FY") ended June 30, 2004 with comparative data for FY 2003 and FY 2002. Its purpose is to enhance the understandability and usefulness of the basic external financial reports. The overriding goal is to respond to the needs of the primary users of these statements, i.e., those to whom the University is primarily accountable (the citizenry), those who directly represent the citizens (legislative and oversight bodies), and those who lend or who participate in the lending process (investors and creditors).

University management has prepared the financial statements and the related footnote disclosures along with this discussion and analysis and the reader is encouraged to read them in conjunction with this MD&A. Responsibility for the completeness and fairness of this information rests with University management.

ABOUT OHIO UNIVERSITY

Ohio University is a public institution established by the State of Ohio (the "State") in 1804 under Chapter 3337 of the Ohio Revised Code ("ORC"). It is the oldest public institution of higher learning in the State of Ohio. It is defined by statute to be a body politic and corporate and an instrumentality of the State.

The University is governed by a 13-member Board of Trustees. The Governor, with the advice and consent of the State Senate, appoints 9 trustees for staggered 9-year nonrenewable terms. In addition, 2 non-voting student members are appointed to the Board of Trustees for staggered 2-year terms. The Ohio University Board of Trustees created 2 National Trustee positions and have invited 2 distinguished out-of-state University alumni to sit with the Trustees and participate in the deliberations of the Board. One term is 2 years and the other is 3 years. Both are non-voting members.

The University consists of the main campus in Athens, Ohio and 5 regional campuses. Total Fall 2003 enrollment for all campuses was 29,088. Eighty-five percent of the students enrolled on the Athens campus are residents of the State of Ohio. The University has a total faculty of approximately 1,070 full-time and 750 part-time, with a total workforce of approximately 4,700 non-student employees. The student to faculty ratio on the Athens campus in the Fall of 2003 was 21:1. The University offers 26 Associate majors, 254 Baccalaureate majors, 167 Masters majors, 56 PhD majors and 1 DO major.

Governmental Accounting Standards Board ("GASB") Statement No. 39, *Determining Whether Certain Organizations Are Component Units*, an amendment of GASB Statement No. 14 and implemented by the University effective July 1, 2003 lead to the conclusion that The Ohio University Foundation, a 501(c)(3) organization incorporated in Ohio in October 1945 to support the educational undertakings of Ohio University, is to be reported in the University's statements as a component unit. The University has chosen a discrete presentation and the Foundation's information appears in a separate column next to the University on the Statements of Net Assets and the Statements of Revenues, Expenses and Changes in Net Assets. The University is not required to prepare a Statement of Cash Flows for the Foundation. A separate financial report for the Foundation is available by contacting The Ohio University Foundation, HDL Center, Room 164, Athens, Ohio 45701 or (740)593-1884.

The Ohio University Osteopathic Medical Center Inc. ("MCI") ceased to exist as an entity effective July 1, 2003. The appearance of five months of MCI's data in a discrete column on the University's financial statements will be the last year that MCI is included in this report. The successor organization, University Medical Associates ("UMA") has been evaluated and was determined to not meet the tests of Statement No. 14 and Statement No. 39 for component unit treatment.

This MD&A is intended to address issues of the primary entity and not those of its component units.

FINANCIAL HIGHLIGHTS OF FY 2004

The state funding environment for higher education continues to present funding challenges to public institutions. Actual state appropriations were virtually flat for FY 2004, increasing by only \$382,535. What the University needs, but is unable to fund through the receipt of state appropriations, must be made up with tuition increases or by finding alternative revenue streams.

For the second year in a row the University increased tuition by 9.9% for returning undergraduate and graduate students. Six percent is to fund general education with the additional 3.9% earmarked for need-based aid and technology initiatives. Room and board rates increased by 8%.

During FY 2004 the University committed to a payout of \$1.6 million over a 2 year period to upgrade faculty salaries. Half of that amount was distributed in FY 2004. The goal is to move to the top of the Ohio public institution quartile of pay for faculty in order to continue to attract and retain quality faculty.

The University issued additional debt in FY 2004, increasing its bonds and notes payable on the FY 2004 Statement of Net Assets by 32%. Additional details of the debt issuances and retirements are contained in the footnotes to the financial statements.

The University's planning process resulted in a decision to implement an Early Retirement Incentive Plan ("ERIP") buyout in FY 2003 for eligible employees in the Ohio Public Employees Retirement System ("OPERS"). An ERIP allows the University to purchase additional service credit, in this case two years, which enables eligible employees to retire early or to retire with a larger retirement benefit than they may have otherwise. The buyout period began on May 1, 2003 and the period remained open until June 30, 2004. A \$10,000 incentive was offered to employees who signed up for the buyout by June 30, 2003 and who would retire by September 1, 2003. The advantage to the University is personnel costs savings over time to the extent that vacated positions are either abolished or filled at lower salaries/wages. As of June 30, 2004, 192 employees had signed up for the ERIP for a total cost estimate for the program of \$9.5 million that includes sick leave and vacation payouts in accordance with standard policy, a \$10,000 incentive bonus for the 131 employees who left by September 1, 2003 and the OPERS payment calculated and billed by OPERS. All employees taking the buyout were required to be retired by September 1, 2004.

The University's implementation of an enterprise-wide information system continued to evolve. The Enterprise Project's mission was to replace the University's legacy administrative systems with the financial and human resource management/payroll modules from the Oracle Corporation. The human resource management/payroll module went live on July 1, 2001. The financial modules were implemented on April 1, 2003. Implementation of Workforce, a time and attendance system utilizing the Web and card swiping for time capturing, is currently in use with a pilot group. An automated method of entering data into Payroll for graduate appointments was nearly complete by the end of FY 2004 and operational in FY 2005. On the horizon is "Business On-Line" – an automated approach to submitting financial transactions for processing. The system will have work rules built into it and allow for data entry at the departmental level, thus eliminating the need for paper flow and redundant data entry, including the maintenance of duplicative systems within individual departments.

The rising costs of health care continue to be of concern in the budget planning process. Ohio University has had a few recent years of significant positive budget-to-actual variances due to conservative budgeting in this area, and better than expected experience. Positive variance dollars have been set aside to offset the cost of future initiatives related to providing health care coverage to University employees. A significant amount of all projected new operating monies (20-25%) is set aside out of necessity to deal with this issue.

The University celebrated its bicentennial year (established in 1804) with a Bicentennial Fundraising Campaign victory of surpassing its \$200 million fundraising goal. The amount received or pledged in support of the campaign was \$221,442,916. Of the monies collected, \$23.1 million will establish 8 new endowed chairs and 35 new named professorships, \$40.1 million will support existing scholarships and create 1,226 new scholarships, \$17.6 million will be used for new or to improve capital facilities, \$29.3 million will be used for innovative programs and \$13.9 million will be used for technological enhancements.

CURRENT YEAR RESULTS

The Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Net Assets

One of the most important questions asked about a University's finances is whether the University is better off as a result of the year's activities. The Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Net Assets report information on the University as a whole and on its activities in a way that helps answer this question. Net assets, the difference between total assets and total liabilities are the measure of the current financial condition. Increases or decreases in the University's net assets are one indicator of whether its financial health is improving or deteriorating. Numerous other nonfinancial factors, such as the number and quality of applicants, freshman class size and composition, student retention and graduation rates, strength of the faculty, condition of the campus infrastructure and the safety of the campus, must be considered when assessing the overall health of the University.

Points of interest relative to the Statements of Net Assets are as follows:

- The Statement of Net Assets classifies assets and liabilities as current or noncurrent. Generally, current liabilities are those that will be paid within one year of the date of the Statement. Current assets are those that are available to satisfy current liabilities.
- Total **Cash and cash equivalents** increased by \$52,725,025 over FY 2003. A major contributor to this was an increase of \$30,711,230 in **Restricted cash and cash equivalents** which are monies held by bond trustees awaiting expenditure.
- **Investments** include the net appreciation on endowment investments available for expenditure, if authorized by the Board, in accordance with donors' restrictions.
- **Restricted cash and cash equivalents** primarily represent unspent bond proceeds as of June 30 of each year.
- **Endowment investments** represent the contributed value of University endowments incremented each year by new contributions, \$10,601 and \$16,099 for FY 2004 and FY 2003, respectively, and annual unused earnings on one larger endowment whose donor has requested they be added to principal each year. The University usually does not take on any new endowments unless the donor's bequest specifically states that the gift is to be administered by the Board of Trustees of Ohio University. Otherwise, the University's Foundation (The Ohio University Foundation) receives and administers new endowments.
- **Capital assets** are recorded at historical cost and presented net of their accumulated depreciation. The amount of accumulated depreciation was \$357,475,056 and \$335,071,026 for FY 2004 and FY 2003, respectively.
- **Refundable Advances for Federal Student Loans** represents the cumulative Federal capital contribution (FCC) to Federal student loan programs, presented as a potential long-term liability.

The following chart depicts the breakdown of Assets, Liabilities and Net Assets for Ohio University for the years ended June 30, 2004, 2003 and 2002:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Assets:			
Capital assets, net	\$ 481,247,608	\$ 453,103,537	\$ 411,925,152
Other assets	<u>244,482,774</u>	<u>192,627,325</u>	<u>199,123,491</u>
	<u>\$ 725,730,382</u>	<u>\$ 645,730,862</u>	<u>\$ 611,048,643</u>
Liabilities:			
Current Liabilities	\$ 78,535,421	\$ 93,446,995	\$ 75,178,808
Noncurrent Liabilities	<u>184,710,468</u>	<u>121,534,356</u>	<u>135,966,142</u>
	<u>\$ 263,245,889</u>	<u>\$ 214,981,351</u>	<u>\$ 211,144,950</u>
Net assets	<u>\$ 462,484,493</u>	<u>\$ 430,749,511</u>	<u>\$ 399,903,693</u>

Net assets, expressed as a percent of total assets, are 64% for FY 2004, 67% for FY 2003 and 65% for FY 2002.

The Net Assets for the years ended June 30, 2004, 2003 and 2002 are further displayed as follows:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Invested in capital assets, net of related debt	\$ 345,803,896	\$334,620,636	\$285,269,795
Restricted nonexpendable	11,836,376	11,727,151	11,604,413
Restricted expendable	42,898,264	33,749,128	57,253,381
Unrestricted	<u>61,945,957</u>	<u>50,652,596</u>	<u>45,776,104</u>
	<u>\$ 462,484,493</u>	<u>\$430,749,511</u>	<u>\$399,903,693</u>

Invested in capital assets net of related debt represents the historic dollar value of capital assets reduced by their related depreciation and outstanding debt related to their purchase or construction. It is increased by the value of any **restricted cash and cash equivalents** representing funds held by bond trustees and available for future capital initiatives.

Restricted nonexpendable net assets are equal to **endowment investments**, previously described.

Restricted expendable net assets is made up primarily of loan funds revenues in excess of their expenses, restricted grants and contracts revenues in excess of their expenses and net market appreciation of endowment funds available for expenditure, all of whose use has been restricted by external sources.

Unrestricted net assets is made up of funds available for expenditure at the discretion of the Board of Trustees and includes the accumulation of unrestricted revenues received in excess of expenses, including that of auxiliary enterprises.

Points of interest relative to the Statements of Revenues, Expenses, and Changes in Net Assets:

- The Statement of Revenues, Expenses and Changes in Net Assets differentiates between operating and nonoperating revenue. Sales of goods and services are recorded as operating revenues, where it is generally assumed that the buyer receives something of value equal to the amount given up. Essentially all other types of revenue are nonoperating, or other revenue. Nonoperating revenues include State appropriations, grants that do not require any services to be performed for the benefit of the grantor and investment income. The operating income (loss) line will typically display a loss for state-supported public institutions since state appropriations, that have historically played a significant role in the funding of public institutions, are mandated to be reported as nonoperating revenue. Other revenues include state capital appropriations, capital gifts and grants and additions to permanent endowments.

- **Student tuition and fee revenues, auxiliary enterprises revenues, and the corresponding student aid expenses,** are reported net of scholarship discounts and allowances in the Statements of Revenues, Expenses, and Changes in Net Assets. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by the institution and the amount that is paid by students and/or third parties making payments on the student's behalf. For FY 2004 that amount is \$38,156,805 (of which \$30,563,601 is netted against **student tuition and fees** and \$7,593,204 is netted against **auxiliary enterprises** revenues). In FY 2003 that amount was \$33,699,058 (of which \$26,817,711 was netted against **student tuition and fees** and \$6,881,347 was netted against **auxiliary enterprises** revenues).
- **Auxiliary enterprises** revenues consist of the sales and services of such activities as residence halls, dining services, intercollegiate athletics, airport operations, telephone operations and campus recreation. The bulk of this revenue is the activity of the Residence and Dining Hall auxiliary whose room and board rates were increased 8% in FY 2004 over FY 2003, which was previously increased 8% over FY 2002.
- The University, as a component unit of the State of Ohio, is required to report its **operating expenses** on the face of its financial statements using a functional view. Functional categories are presented as defined by the National Association of College and University Business Officers ("NACUBO"). In FY 2004 the University performed an analysis of all its unrestricted accounts for proper classification within those definitions.
- The expense line "**Student aid**" represents institutional resources provided **in excess** of amounts owed by the students to the institution and refunded to them. It **does not** represent the amount of financial aid made available to students.
- Expenditures for capital assets are capitalized on the Statement of Net Assets and systematically reduced through the use of **depreciation** expense in the Statement of Revenues, Expenses, and Changes in Net Assets. The University has chosen to display depreciation on a separate line in the Statements of Revenues, Expenses, and Changes in Net Assets as opposed to allocating it among the various functional categories.
- Allocated throughout the functional categories is the cost of the **Early Retirement Incentive Plan (ERIP)** discussed under "Financial Highlights of FY 2004". The estimated cost for all employees who have elected the ERIP as of June 30, 2004 is \$9.5 million.
- **State appropriations** consist primarily of state share of instruction revenues. State support continues to decline in prominence relative to other income streams.
- **Investment income** increased over last year by \$2,754,244.
- **State capital appropriations** stayed fairly even with FY 2004 coming in at \$13,216,346 compared to \$12,623,786 in FY 2003.
- **Capital grants and gifts** dropped to \$5,612,306 in FY 2004 compared to \$13,173,470 in FY 2003. The nature of this revenue stream is that it fluctuates in amount dependent on the particular grants and gifts received.

The following charts depict total revenue by source for FY 2004, FY 2003 and FY 2002, respectively:

<u>Revenues by source</u>	<u>2004</u>	<u>2003</u>	<u>2002</u>
State appropriations	\$ 142,388,900	\$ 142,006,365	\$ 144,819,888
Student tuition and fees, net	183,845,137	163,581,009	143,115,709
Grants and contracts	77,254,757	82,130,090	72,219,822
Sales and services	10,683,223	9,097,035	6,926,473
Auxiliary enterprises, net	53,887,294	53,445,582	46,812,756
Investment income, net	7,650,469	4,896,225	(3,930,184)
State capital appropriations	13,216,346	12,623,786	32,658,816
Other	5,403,554	5,657,241	8,399,900
Total	<u>\$ 494,329,680</u>	<u>\$ 473,437,333</u>	<u>\$ 451,023,180</u>

The following chart depicts operating and nonoperating expenses for FY 2004, FY 2003 and FY 2002, respectively:

<u>Expenses by source</u>	<u>2004</u>	<u>2003</u>	<u>2002</u>
Instruction and departmental research	\$ 169,763,301	\$ 170,495,306	\$ 165,131,818
Separately budgeted research	29,321,541	26,388,575	27,255,898
Public service	18,039,685	16,205,555	14,879,215
Academic support	46,156,862	36,422,783	32,212,536
Student services	23,794,386	23,563,230	20,807,467
Institutional support	36,254,600	38,248,929	36,882,740
Operation and maintenance of plant	37,160,727	36,664,688	33,934,978
Student aid	11,214,000	12,201,431	5,706,074
Depreciation	27,310,496	24,215,215	21,979,684
Auxiliary enterprises	58,122,051	60,707,809	59,552,681
Interest on capital asset-related debt	5,022,680	3,762,188	5,453,686
Disposal and write-offs of plant facilities	434,369	765,403	767,581
Total	<u>\$ 462,594,698</u>	<u>\$ 449,641,112</u>	<u>\$ 424,564,358</u>

- **Extraordinary Items – Reversal of 2002 Workers’ Compensation allocation** – For FY 2003, the State of Ohio reversed an earlier decision that required state-assisted universities to record a portion of the State’s workers’ compensation liability in their respective financial statements. This had a favorable impact on the University’s financial statements for FY 2003 with a resultant increase to net income in the amount of \$7,049,597. There are no extraordinary items for FY 2004.
- **Senate Bill 6 ratios**, one of the measures by which the University’s activities are monitored at the state level, returned a composite score of 3.1 in FY 2004 and 3.4 in each of FY 2003 and FY 2002. The highest possible score is 5.0. The University remained the same in the scores assigned to the primary reserve ratio (expendable net assets divided by operating expenses) and the net income ratio (change in total net assets divided by total revenues). The score assigned to the viability ratio (expendable net assets divided by plant debt) dropped by 1. This particular ratio is 30% of the composite score.

Statement of Cash Flows

The Statement of Cash Flows presents detailed information about the major sources and uses of cash. The four categories of presentation and their respective FY 2004, FY 2003 and FY 2002 amounts are:

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Net cash used in operating activities	\$(140,900,912)	\$(152,681,747)	\$(157,250,400)
Net cash provided by noncapital financing activities	174,437,158	172,899,737	177,469,952
Net cash provided by (used in) capital financing activities	3,862,416	(41,269,983)	(24,215,217)
Net cash provided by (used in) investing activities	15,326,363	4,373,695	(6,250,226)

Total cash and cash equivalents increased to \$79,938,032 compared to \$27,213,007 in FY 2003 and \$43,891,305 in FY 2002.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

Major capital additions completed during the fiscal year ended June 30, 2004 and the primary resources that funded their acquisition/construction included (in millions):

Bentley Hall Renovation and Annex	\$ 19.2	Capital Appropriations and Sale of Bonds
Margaret M. Walter Hall	13.7	Sale of Bonds and Private Gift
District Water Cooling	13.4	Capital Appropriations and Sale of Bonds
Performance Contracting	6.6	Sale of Bonds and Internal Funding
Innovation Center	6.1	Sale of Bonds and Federal Grants
Read Hall Renovation	4.3	Internal Funds
Utility Infrastructure Project	3.9	Sale of Bonds
Bennett Hall Improvements - Chillicothe Campus	3.3	Capital Appropriations and Internal Funding
Richard H. McFarland Avionics Building	1.8	Sale of Bonds and Internal Funding
Golf Course Reconfiguration	1.6	Capital Appropriations and Internal Funding
Yamada International House Renovation/Addition	1.5	Private Gift, Capital Appropriations and Internal Funding

Cumulative costs associated with capital projects continuing after the fiscal year ended June 30, 2004 totaled approximately \$27.6 million at June 30, 2004. These projects include (in millions):

University Center	\$ 9.2
Bromley Hall Renovation	4.1
Lausche Heating Plant Fluesorbent Processing	3.6
Putnam Hall Rehabilitation	3.2
Lausche Heating Plant Upgrade	1.0

The University's estimated future capital commitments, for which funding has been identified, total approximately \$64,388,000 at June 30, 2004.

Debt Administration

At year-end, the University had \$175,380,000 in bonds and notes obligations outstanding versus \$132,665,000 at the end of FY 2003 and \$125,880,000 at the end of FY 2002. The University's Standard and Poor's revenue bond rating of A+ and Moody's revenue bond rating of A1 have not changed from the prior year. The footnotes to the financial statements provide additional details of the issuances and retirements of debt in FY 2004.

ECONOMIC FACTORS THAT WILL AFFECT THE FUTURE

The University provided for a 3.5% salary/wage increase for FY 2005. In addition, \$750,000 has been set aside centrally for equity adjustments for faculty and staff to address inequities across positions within departments, across the campus and in comparisons with peers across the State. Planning units are expected to match the central funding with 25% of unit funds in order to qualify.

Tuition rates for FY 2005 have increased by a rate of 9%, with room and board rates increasing by 3%.

The University is projecting a 2% drop in state share of instruction for FY 2005. The next State of Ohio biennial budget does not promise to deliver better news to those with budgeting and planning responsibilities.

The University has an obligation to its students, their families and the taxpayers of the State of Ohio to ensure that it operates as efficiently and effectively as possible. Along that line an Accounting/Business Services Task Force has been created to explore whether the University can attain greater efficiencies through some level of consolidation or centralization of the business function across campus. Other university models are being examined for viability on Ohio University's campuses.

The goal of attracting and retaining quality faculty and staff is of paramount importance to all the University hopes to accomplish. Issues of increasing health care costs and the University's desire to remain competitive in the pay structure for faculty and staff present the challenges to be faced. A Health Benefits Task Force has been created to explore the University's health benefits package to ensure that it is competitive and to examine the structure of the benefits to ensure it encourages judicious use. Conservative budgeting has afforded the University positive health care variances in the last few years, which have been set aside in reserves to use in University health care strategies.

Dr. Roderick McDavis became the 20th President of Ohio University on July 1, 2004. Previously he held the position of Provost at Virginia Commonwealth University. He is a graduate of Ohio University and so continues his devotion to Ohio University in his current role. A number of initiatives have been identified by Dr. McDavis that will set a course for the months to come. Among those initiatives are:

- **Increase Diversity Among Students, Faculty, Administration and Staff** – Dr. McDavis has challenged the University community to increase the percent of minority enrollment from the present day of 6%. One tool to use in that campaign is a scholarship program called the Urban Scholars Program, designed to attract students from urban areas.
- **Strengthen and Expand the Base of Financial Support** – A goal has been set to increase out-of-state enrollment, to increase the level of outside support for research and to take advantage of entrepreneurial opportunities to increase revenue. Success in these areas will mitigate the uncertainty of the level of state support.
- **Build the University's Reputation as a Prominent Research University and Raise National Rankings of Academic and Research Programs** – The latest "U.S. News and World Report" rankings showed Ohio University moving to the 98th spot from No. 107 in the ranking among doctoral universities.
- **Increase Partnerships Locally, Statewide, Nationally and Internationally** – The intent in creating these partnerships is to enhance economic development opportunities for the region.

Under the leadership of Interim Provost Kathy Krendl, a Presidential Task Force on the future of Ohio University is being formed to chart the path that will lead us to the successful accomplishment of these goals.

OHIO UNIVERSITY
(A Component Unit of the State of Ohio)

STATEMENTS OF NET ASSETS
JUNE 30, 2004 AND 2003

ASSETS	June 30, 2004			June 30, 2003		
	Primary Institution	The Ohio University Foundation	MCI	Primary Institution	The Ohio University Foundation	MCI
CURRENT ASSETS:						
Cash and cash equivalents	\$ 34,240,775	\$ 10,009,291	\$1,165,401	\$ 12,226,980	\$ 8,271,692	\$ 105,478
Investments	83,968,220	45,740,364	56,203	90,360,051	46,104,776	
Accounts and pledges receivable—net	37,698,411	12,354,752	1,839,961	38,766,796	7,515,671	1,756,311
Accrued interest and dividends receivable	313,327	126,535		515,972	291,076	1,437
Notes receivable—net	2,844,659	49,761		1,934,318	94,761	
Prepaid expenses and deferred charges	17,408,774	1,871,358	6,748	11,477,965	1,761,490	358,567
Inventories	1,653,341	1,125,984		1,536,875	680,379	
Total current assets	<u>178,127,507</u>	<u>71,278,045</u>	<u>3,068,313</u>	<u>156,818,957</u>	<u>64,719,845</u>	<u>2,221,793</u>
NONCURRENT ASSETS:						
Restricted cash and cash equivalents	45,697,257	3,059,378		14,986,027	4,330,998	
Pledges receivable—net		9,225,298			7,633,664	
Bequests receivable		1,558,378			390,000	
Cash surrender value—life insurance policies		2,636,067			2,422,464	
Charitable remainder trusts		1,324,704			1,087,527	
Charitable remainder annuities		3,659,103			3,193,969	
Investment in unconsolidated subsidiary			33,569			25,741
Endowment investments	11,836,376	96,970,424		11,727,151	82,971,048	
Notes receivable—net	8,821,634			9,095,190		
Intangible assets and deferred charges		3,418,197			2,980,459	
Capital assets—net	<u>481,247,608</u>	<u>34,435,826</u>		<u>453,103,537</u>	<u>35,942,618</u>	
Total noncurrent assets	<u>547,602,875</u>	<u>156,287,375</u>	<u>33,569</u>	<u>488,911,905</u>	<u>140,952,747</u>	<u>25,741</u>
TOTAL ASSETS	<u>\$ 725,730,382</u>	<u>\$ 227,565,420</u>	<u>\$ 3,101,882</u>	<u>\$ 645,730,862</u>	<u>\$ 205,672,592</u>	<u>\$ 2,247,534</u>

See notes to the financial statements.

(Continued)

OHIO UNIVERSITY
(A Component Unit of the State of Ohio)

STATEMENTS OF NET ASSETS
JUNE 30, 2004 AND 2003

LIABILITIES AND NET ASSETS	June 30, 2004			June 30, 2003		
	Primary Institution	The Ohio University Foundation	MCI	Primary Institution	The Ohio University Foundation	MCI
CURRENT LIABILITIES:						
Accounts payable and accrued liabilities	\$ 38,973,394	\$ 3,346,030	\$ 543,803	\$ 38,890,077	\$ 6,072,909	\$ 1,204,937
Deferred revenue	21,417,003			20,418,048		
Refunds and other liabilities	1,971,239	3,755,134		2,273,998	3,638,852	
Capital lease obligations	93,017			249,836		
Bonds and notes payable	15,597,740	1,013,094		30,642,761	958,332	
Deposits held in custody for others	483,028	337,728		972,275	417,618	
Total current liabilities	<u>78,535,421</u>	<u>8,451,986</u>	<u>543,803</u>	<u>93,446,995</u>	<u>11,087,711</u>	<u>1,204,937</u>
NONCURRENT LIABILITIES:						
Compensated absences	11,478,477			12,249,793		
Capital lease obligations	119,147			87,366		
Bonds and notes payable	159,782,260	33,325,046		102,022,239	33,400,215	
Bond premium—net	5,548,806					
Refundable advances for federal student loans	7,781,778			7,174,958		
Total noncurrent liabilities	<u>184,710,468</u>	<u>33,325,046</u>		<u>121,534,356</u>	<u>33,400,215</u>	
Total liabilities	<u>263,245,889</u>	<u>41,777,032</u>	<u>543,803</u>	<u>214,981,351</u>	<u>44,487,926</u>	<u>1,204,937</u>
DHI MINORITY INTEREST		3,958,041			2,530,253	
NET ASSETS:						
Invested in capital assets—net of related debt	345,803,896	6,105,204		334,620,636	8,628,616	
Restricted:						
Nonexpendable	11,836,376	96,970,424		11,727,151	82,971,048	
Expendable	42,898,264	84,651,271		33,749,128	78,073,910	
Unrestricted	61,945,957	(5,896,552)	2,558,079	50,652,596	(11,019,161)	1,042,597
Total net assets	<u>462,484,493</u>	<u>181,830,347</u>	<u>2,558,079</u>	<u>430,749,511</u>	<u>158,654,413</u>	<u>1,042,597</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 725,730,382</u>	<u>\$ 227,565,420</u>	<u>\$ 3,101,882</u>	<u>\$ 645,730,862</u>	<u>\$ 205,672,592</u>	<u>\$ 2,247,534</u>

See notes to the financial statements.

(Concluded)

OHIO UNIVERSITY
(A Component Unit of the State of Ohio)

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
YEARS ENDED JUNE 30, 2004 AND 2003

	2004			2003		
	Primary Institution	The Ohio University Foundation	MCI	Primary Institution	The Ohio University Foundation	MCI
OPERATING REVENUES:						
Student tuition and fees—net of scholarship allowances	\$ 183,845,137	\$ -	\$ -	\$ 163,581,009	\$ -	\$ -
Federal grants and contracts	28,968,560			26,208,619		
State grants and contracts	5,554,850			8,262,062		
Local grants and contracts	686,248			634,608		
Private grants and contracts	8,400,998			6,417,402		
Sales and services	10,683,223			9,097,035		
Auxiliary enterprises—net of scholarship allowances	53,887,294			53,445,582		
Patient and professional services			4,169,159			10,455,443
Other sources	5,392,953	28,544,446		5,641,142	23,356,626	
Total operating revenues	<u>297,419,263</u>	<u>28,544,446</u>	<u>4,169,159</u>	<u>273,287,459</u>	<u>23,356,626</u>	<u>10,455,443</u>
OPERATING EXPENSES:						
Educational and general:						
Instruction and departmental research	169,763,301	4,862,511		170,495,306	5,779,265	
Separately budgeted research	29,321,541	574,321		26,388,575	477,822	
Public service	18,039,685	131,273		16,205,555	96,787	
Academic support	46,156,862	1,635,454		36,422,783	1,160,733	
Student services	23,794,386	452,369		23,563,230	502,694	
Institutional support	36,254,600	8,653,545		38,248,929	7,809,867	
Operation and maintenance of plant	37,160,727	4,203		36,664,688	7,172	
Student aid	11,214,000	3,781,519		12,201,431	3,701,191	
Depreciation	27,310,496	1,840,144		24,215,215	1,439,230	2,500
Auxiliary enterprises	58,122,051			60,707,809		
Operating expenses—Foundation subsidiaries and MCI		23,107,782	2,662,289		19,205,703	10,003,840
Total operating expenses	<u>457,137,649</u>	<u>45,043,121</u>	<u>2,662,289</u>	<u>445,113,521</u>	<u>40,180,464</u>	<u>10,006,340</u>
OPERATING INCOME (LOSS)	<u>\$(159,718,386)</u>	<u>\$(16,498,675)</u>	<u>\$1,506,870</u>	<u>\$(171,826,062)</u>	<u>\$(16,823,838)</u>	<u>\$ 449,103</u>

See notes to the financial statements.

(Continued)

OHIO UNIVERSITY
(A Component Unit of the State of Ohio)

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
YEARS ENDED JUNE 30, 2004 AND 2003

	2004			2003		
	Primary Institution	The Ohio University Foundation	MCI	Primary Institution	The Ohio University Foundation	MCI
NONOPERATING REVENUES AND EXPENSES:						
State appropriations	\$ 142,388,900	\$ -	\$ -	\$ 142,006,365	\$ -	\$ -
Federal grants	20,741,312			20,835,465		
State grants	5,458,934			4,484,965		
Local grants				6,130		
Private gifts	1,831,549	8,148,727		2,107,369	7,245,917	
University support		3,471,369			3,523,995	
Investment income—net of investment expense	7,650,469	15,204,508	8,612	4,896,225	(1,731,331)	49,627
Income taxes						(5,476)
Interest on capital asset-related debt	(5,022,680)			(3,762,188)		
Disposal and write-offs of plant facilities	(434,369)			(765,403)		2,098
Net nonoperating revenues	<u>172,614,115</u>	<u>26,824,604</u>	<u>8,612</u>	<u>169,808,928</u>	<u>9,038,581</u>	<u>46,249</u>
INCOME (LOSS) BEFORE OTHER REVENUES, EXPENSES, GAINS OR LOSSES	<u>12,895,729</u>	<u>10,325,929</u>	<u>1,515,482</u>	<u>(2,017,134)</u>	<u>(7,785,257)</u>	<u>495,352</u>
OTHER REVENUES, EXPENSES, GAINS, OR LOSSES						
State capital appropriations	13,216,346			12,623,786		
Capital grants and gifts	5,612,306			13,173,470		
Additions to permanent endowments	10,601	12,850,005		16,099	5,394,895	
Total other revenues	<u>18,839,253</u>	<u>12,850,005</u>	<u>-</u>	<u>25,813,355</u>	<u>5,394,895</u>	<u>-</u>
INCOME (LOSS) BEFORE EXTRAORDINARY ITEMS	<u>31,734,982</u>	<u>23,175,934</u>	<u>1,515,482</u>	<u>23,796,221</u>	<u>(2,390,362)</u>	<u>495,352</u>
EXTRAORDINARY ITEMS—						
Reversal of 2002 Workers' Compensation allocation				7,049,597		
INCREASE (DECREASE) IN NET ASSETS	<u>31,734,982</u>	<u>23,175,934</u>	<u>1,515,482</u>	<u>30,845,818</u>	<u>(2,390,362)</u>	<u>495,352</u>
NET ASSETS:						
Beginning of year	<u>430,749,511</u>	<u>158,654,413</u>	<u>1,042,597</u>	<u>399,903,693</u>	<u>161,044,775</u>	<u>547,245</u>
End of year	<u>\$ 462,484,493</u>	<u>\$ 181,830,347</u>	<u>\$ 2,558,079</u>	<u>\$ 430,749,511</u>	<u>\$ 158,654,413</u>	<u>\$ 1,042,597</u>

See notes to the financial statements.

(Concluded)

Ohio University
(A Component Unit of the State of Ohio)

STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2004 AND 2003

	2004	2003
	Primary	Primary
	Institution	Institution
CASH FLOWS FROM OPERATING ACTIVITIES:		
Student tuition and fees	\$ 179,723,774	\$ 151,400,163
Grants and contracts	40,563,341	25,802,126
Payments to suppliers	(93,008,659)	(71,111,746)
Payments to employees	(238,684,000)	(236,090,000)
Payments for benefits	(64,135,706)	(66,545,837)
Payments for scholarships and fellowships	(35,144,707)	(38,668,868)
Loans issued to students	(4,372,213)	(3,115,819)
Collection of loans to students	2,753,629	2,497,686
Auxiliary enterprise sales	52,171,874	54,926,830
Sales and services	10,122,265	11,080,524
Other receipts (payments)	<u>9,109,490</u>	<u>17,143,194</u>
Net cash used in operating activities	<u>(140,900,912)</u>	<u>(152,681,747)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:		
State appropriations	142,388,900	142,006,365
Gifts and grants for other than capital purposes	32,387,439	27,433,929
Federal direct student loan programs receipts	101,983,848	89,197,992
Federal direct student loan programs disbursements	(102,471,723)	(89,197,992)
Student organization agency transactions	<u>148,694</u>	<u>3,459,443</u>
Net cash provided by noncapital financing activities	<u>174,437,158</u>	<u>172,899,737</u>
CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES:		
Proceeds from capital debt	121,323,917	22,800,000
Capital appropriations	12,453,069	13,291,782
Capital grants and gifts received	5,612,306	13,173,470
Purchases of capital assets	(56,120,155)	(68,629,434)
Principal paid on capital debt and leases	(73,185,637)	(16,685,481)
Interest paid on capital debt and leases	<u>(6,221,084)</u>	<u>(5,220,320)</u>
Net cash provided by (used in) capital financing activities	<u>3,862,416</u>	<u>(41,269,983)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sales and maturities of investments	22,771,506	62,986,320
Investment income	5,121,337	1,746,394
Purchase of investments	<u>(12,566,480)</u>	<u>(60,359,019)</u>
Net cash provided by investing activities	<u>15,326,363</u>	<u>4,373,695</u>
NET INCREASE (DECREASE) IN CASH	52,725,025	(16,678,298)
CASH AND CASH EQUIVALENTS—Beginning of year	<u>27,213,007</u>	<u>43,891,305</u>
CASH AND CASH EQUIVALENTS—End of year	<u>\$ 79,938,032</u>	<u>\$ 27,213,007</u>

See notes to the financial statements.

(Continued)

Ohio University
(A Component Unit of the State of Ohio)

STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2004 AND 2003

	2004 Primary Institution	2003 Primary Institution
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH USED IN OPERATING ACTIVITIES:		
Operating income (loss)	\$(159,718,386)	\$(171,826,062)
Adjustments to reconcile operating income (loss) to net cash used in operating activities:		
Depreciation expense	27,310,496	24,215,215
Changes in assets and liabilities:		
Accounts receivable—net	(2,296,880)	(3,418,847)
Notes receivable—net	(1,706,508)	(339,718)
Deferred revenue	(298,062)	3,751,477
Prepaid expenses and deferred charges	(1,832,604)	(5,471,475)
Inventories	(116,466)	64,032
Accounts payable and accrued liabilities	(1,939,743)	209,044
Refunds and other liabilities	<u>(302,759)</u>	<u>134,587</u>
NET CASH USED IN OPERATING ACTIVITIES	<u>\$(140,900,912)</u>	<u>\$(152,681,747)</u>

See notes to financial statements.

(Concluded)

OHIO UNIVERSITY

(A Component Unit of the State of Ohio)

NOTES TO FINANCIAL STATEMENTS

YEARS ENDED JUNE 30, 2004 AND 2003

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Organization

Ohio University (“University”) is a public institution established by the State of Ohio (“State”) in 1804 under Chapter 3337 of the Ohio Revised Code (“ORC”). As such it is a component unit of the State of Ohio and is included as a discretely presented entity in the State of Ohio’s Comprehensive Annual Financial Report. The University is the oldest of the state-assisted universities in Ohio. It is defined by statute to be a body politic and corporate and an instrumentality of the State.

The University is governed by a 13-member Board of Trustees. The Governor, with the advice and consent of the State Senate, appoints 9 trustees for staggered 9-year nonrenewable terms. In addition, 2 non-voting student members are appointed to the Board of Trustees for staggered 2-year terms. The Ohio University Board of Trustees created 2 new National Trustee positions and have invited 2 distinguished out-of-state University alumni to sit with the Trustees and participate in the deliberations of the Board. One term is 2 years and the other is 3 years. Both are non-voting members.

(b) Basis of Presentation

The financial statements of the University have been prepared in accordance with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (“GASB”) including Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*, and GASB No. 35, *Basic Financial Statements – and Management’s Discussion and Analysis – for Public Colleges and Universities (an amendment of GASB No. 34)*. The presentation required by GASB No. 34 and GASB No. 35 provides a comprehensive, entity-wide perspective of the University’s assets, liabilities, net assets, revenues, expenses and changes in net assets and cash flows. It replaces fund-groups with net asset-groups, and requires the direct method of cash flow presentation.

The University follows all GASB pronouncements as well as Financial Accounting Standards Board (“FASB”) Statements and Interpretations, Accounting Principles Board (“APB”) Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989 unless those pronouncements conflict with or contradict GASB pronouncements. The University has elected not to apply FASB Statements and Interpretations issued after November 30, 1989.

The accompanying financial statements comply with the provisions of GASB Statement No. 14, *The Financial Reporting Entity*, in that the financial statements include all the organizations, activities, functions and component units for which the University is financially accountable. Financial accountability is defined as the appointment of a voting majority of the component unit’s board and either (1) the University’s ability to impose its will over the component unit or (2) the possibility that the component unit will provide a financial benefit to or impose a financial burden on the University. The

University has blended the presentation of its component unit, Athena Cinemas Company, and presents discretely its component unit, Ohio University Osteopathic Medical Center, Inc. (“MCI”).

The accompanying financial statements display MCI as a discretely presented component unit to comply with GASB Statement No. 14, *The Financial Reporting Entity*. MCI reports a fiscal year end of January 31, on a cash basis, which is converted to the accrual basis for presentation herein.

GASB Statement No. 39, *Determining Whether Certain Organizations Are Component Units*, an amendment of GASB Statement No. 14 and implemented by the University effective July 1, 2003, further clarifies that certain organizations warrant inclusion as part of the financial reporting entity because of the nature and significance of their relationship with the primary government, including their ongoing financial support of the primary government. The University has determined that The Ohio University Foundation (“Foundation”) meets this definition and is therefore included as a discretely presented component unit in the University’s financial statements.

The accompanying financial statements display the Foundation as a discretely presented component unit. The Foundation’s financial statements have been prepared on the accrual basis of accounting in accordance with generally accepted accounting principles as prescribed by the FASB.

(c) Basis of Accounting

The University is a special-purpose government engaged only in business type activities as defined by GASB Statements No. 34 and No. 35. Accordingly, the financial statements are presented using an economic resources measurement focus and are presented on the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when incurred. All significant interfund transactions have been eliminated. The financial statements of all discretely component units are also presented under the accrual basis of accounting.

(d) Cash and Cash Equivalents

Cash consists primarily of petty cash, cash in banks and money market accounts. Cash equivalents are short-term highly liquid investments readily converted to cash with original maturities of three months or less.

(e) Investments

All investments are carried at fair value in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. Investments in publicly traded securities are stated at fair value as established by major securities markets. Nonpublicly traded investments are valued based on independent appraisals and estimates considering market prices of similar investments. Changes in unrealized gain (loss) on the carrying value of investments are reported as a component of investment income in the statements of revenues, expenses, and changes in net assets. Investments classified as current assets in the statements of net assets include those that can be withdrawn on demand.

(f) Accounts Receivable

Accounts receivable consist of amounts due for tuition and fees, grants and contracts, and auxiliary enterprise services. Grants and contracts accounts receivable include amounts due from the Federal government, State and local governments, or private sources, as reimbursement of certain expenditures made in accordance with agreements. Uncollectible amounts have been reserved.

(g) Inventories

Inventories are stated at lower of weighted-average cost or net realizable value.

(h) Restricted Cash and Cash Equivalents

Restricted cash and cash equivalents are primarily funds externally restricted for capital expenditures subject to bond and note agreements and are either held by bond trustees or temporarily invested in STAROhio. In addition, it includes some funds held in escrow for successful completion of construction contracts.

(i) Capital Assets

Capital assets are presented in the statements of net assets of the University. Purchased or constructed capital assets are recorded at cost. Donated capital assets are recorded at their estimated fair market value as of the date received. Depreciation is computed using the straight-line method over the estimated useful life of the asset.

Following are the capitalization levels and estimated useful lives of the asset classes:

Asset class	Capitalize at	Estimated useful life
Land	Any amount	N/A
Land improvements	\$100,000	N/A
Works of art and historical treasures	\$2,500	N/A
Infrastructure	\$100,000	10-50 years
Buildings	Any amount	40 years
Machinery and equipment	\$2,500	5-25 years
Library books and publications	Any amount	10 years
Transportation equipment	\$2,500	5-10 years

Building renovations that materially increase the value or extend the useful life of the structure are also capitalized. The costs of normal maintenance and repairs are not capitalized. Interest incurred during the construction of capital assets is included in the cost of the asset when capitalized. Land, land improvements and works of art and historical treasures are not depreciated.

(j) Deferred Revenue

Deferred revenue includes amounts received for tuition and fees and certain auxiliary activities prior to the end of the fiscal year, related to the subsequent accounting period. The effect of not allocating the summer term between fiscal years does not have a significant impact on the financial statement presentation.

(k) Compensated Absences

University employees earn vacation and sick leave benefits based, in part, on length of service. Upon separation from service, employees are paid their accumulated vacation and sick pay based upon the nature of separation (termination, retirement or death). Certain limitations are placed on the hours of vacation and sick leave that employees may accumulate and carry over for payment at termination, retirement or death. Unused hours exceeding their limitations are forfeited. The liability incurred is recorded at year-end in the statements of net assets, and as a component of operating expense in the statements of revenues, expenses, and changes in net assets.

(l) Net Assets

The University's net assets are categorized as described below:

Invested in capital assets—net of related debt: This represents the University's investment in capital assets, net of debt obligations related to those capital assets.

Restricted net assets-nonexpendable: Restricted nonexpendable net assets represent contributed values of permanent endowments restricted or unrestricted as to income.

Restricted net assets-expendable: Restricted expendable net assets represent assets that are restricted by a third party either legally or contractually.

Unrestricted net assets: Unrestricted net assets are resources derived primarily from student tuition, fees, state appropriations, and auxiliary enterprises. These net assets are used for general obligations of the University. They may be used at the discretion of the Board of Trustees for any purpose furthering the University's mission.

When an expense is incurred that can be paid using either restricted or unrestricted resources, the University's policy is to apply the expense at the discretion of University management.

(m) Income Taxes

The University is an organization described in Section 115 of the Internal Revenue Code of 1986 (the "Code") and has further been classified as an organization that is not a private foundation in accordance with Sections 509(a)(1) and 170(b)(1)(A)(ii) of the Code. However, certain revenues are considered unrelated business income and are taxable under Internal Revenue Code Sections 511 through 513.

(n) Classification of Revenues

Revenues are classified as either operating or nonoperating according to the following:

Operating revenues: Operating revenues include revenues from activities that have characteristics similar to exchange transactions. These include student tuition and fees (net of scholarship discounts and allowances), sales and services of auxiliary enterprises (net of scholarship discounts and allowances), and certain Federal, State, local and private grants and contracts.

Nonoperating revenues: Nonoperating revenues include revenues from activities that have the characteristics of nonexchange transactions, such as State appropriations, and certain Federal, State, local and private gifts and grants. Nonoperating revenues also include investment income.

(o) Scholarship Discounts and Allowances

Student tuition and fees revenue, and certain other payments recorded as auxiliary enterprises revenue, are net of scholarship discounts and allowances in the statements of revenues, expenses, and changes in net assets. Scholarship discounts and allowances are the difference between the charge for tuition and fees, and the amount paid by students or by third parties making the payments on the students' behalf. As of June 30, 2004 and 2003, respectively, scholarship discounts and allowances are \$38,156,805 (of which \$30,563,601 is netted against student tuition and fees and \$7,593,204 is netted against auxiliary enterprises revenues) and \$33,699,058 (of which \$26,817,711 is netted against student tuition and fees and \$6,881,347 is netted against auxiliary enterprises revenues).

(p) *Auxiliary Enterprises*

Auxiliary revenues are derived primarily from revenues generated from residence halls, dining services, intercollegiate athletics, airport operations, telephone operations, and campus recreation. They are shown net of scholarship discounts and allowances, primarily for room and board.

(q) *Eliminations*

The University eliminates interfund assets and liabilities, and revenues and expenses related to internal activities.

(r) *Use of Estimates*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (“GAAP”) may require management to make estimates and assumptions that affect certain amounts reported in the financial statements. The estimates and assumptions are based on currently available information and actual results could differ from those estimates.

(s) *Newly Issued Accounting Pronouncements*

In March, 2003, GASB issued Statement No. 40, *Deposit and Investment Risk Disclosures*. This statement requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rate risk. The provisions of this statement are effective for financial statements for periods beginning after June 15, 2004. The University has not yet evaluated the impact that the adoption of this statement will have on its financial statements.

In November, 2003, GASB issued Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. This statement requires certain disclosures when the value of a capital asset has declined significantly and unexpectedly. This statement also clarifies and establishes accounting requirements for insurance recoveries. The provisions of this statement are effective for financial statements for periods beginning after December 15, 2004. The University has not yet evaluated the impact that the adoption of this statement will have on its financial statements.

In April, 2004, GASB issued Statement No. 43, *Financial Reporting for Postemployment Benefits Other than Pension Plans*. The standards in this statement apply for trust funds included in the financial reports of plan sponsors or employers, as well as for the stand-alone financial reports of OPEB plans or the public employee retirement systems, or other third parties, that administer them. The provisions of this statement are effective for financial statements for periods beginning after December 15, 2005. The University has not yet evaluated the impact that the adoption of this statement will have on its financial statements.

In June 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. This statement establishes standards for the measurement, recognition and display of other postemployment benefit expenses/expenditures and related liabilities (assets), note disclosures, and, if applicable, required supplementary information (“RSI”) in the financial reports of employers subject to governmental accounting standards. The provisions of this statement are effective for financial statements for fiscal periods beginning after December 15, 2006. The University has not yet evaluated the impact that the adoption of this statement will have on its financial statements.

(i) Reclassifications

Certain prior-year amounts have been reclassified to conform to current-year presentations.

2. DEPOSITS WITH FINANCIAL INSTITUTIONS, CASH AND CASH EQUIVALENTS, AND INVESTMENTS

The University manages cash and investments in accordance with the Board of Trustees' policy that conforms to the authority granted by the Ohio Revised Code. The purchase of specific investment instruments is at the discretion of the University Treasurer within these policy guidelines.

Cash and Cash Equivalents - The University's cash and cash equivalents consist of cash on hand, deposits and highly liquid investments with original maturities of three months or less. As of June 30, 2004 and 2003, current cash and cash equivalents for the University are \$34,240,775 and \$12,226,980, respectively. Bond proceeds held by bond trustees and bond anticipation note proceeds held in STAROhio are the primary components of restricted cash and cash equivalents. In addition it includes some funds held in escrow for the successful completion of construction contracts. The amounts for restricted cash and cash equivalents are \$45,697,257 and \$14,986,027 at June 30, 2004 and 2003, respectively.

At June 30, 2004, the carrying amount of the University's cash and cash equivalents, including restricted and excluding cash on hand of \$86,986 is \$79,851,046 and the bank balance is \$83,975,631. At June 30, 2003, the amount of the University's deposits, including restricted and excluding cash on hand of \$113,197 was \$27,099,810 and the bank balance was \$31,209,211. The differences between carrying amount and bank balances are caused by outstanding checks and deposits in transit. Of the bank balance:

- \$513,573 and \$546,738 are covered by federal depository insurance as of June 30, 2004 and 2003, respectively.
- \$2,317,499 and \$12,472,979 are held in STAROhio. STAROhio is an investment pool managed by the State Treasurer's Office that allows governments within the State to pool their funds for investment purposes. STAROhio is not registered with the Securities Exchange Commission as an investment company, but does operate in a manner consistent with Rule 2a7 of the Investment Company Act of 1940. Investments in STAROhio are valued at STAROhio's share price, which is the price the investment could be sold for on June 30, 2004.

Investments in STAROhio are backed by the securities purchased by STAROhio. Historically, over 90% of the investments purchased by STAROhio are U.S. government obligations and all securities purchased are held in a third party custodial arrangement on behalf of STAROhio.

- \$81,144,559 and \$18,189,494 are covered by collateral held by third party trustees pursuant to Section 135.181 of the Ohio Revised Code in collateral pools securing all public funds on deposit with specific depository institutions, as of June 30, 2004 and 2003, respectively.

Investments—The University's investments, both current and noncurrent, are categorized below to give an indication of the level of custodial credit risk assumed by the entity at year-end. Category 1 includes investments that are insured or registered or securities held by the University or its agent in the University's name. Category 2 includes investments that are uninsured and unregistered with securities held by the counterparty or its trust department in the University's name. Category 3 includes investments that are uninsured and unregistered with securities held by the counterparty or its trust

department but not in the University's name. All long-term investments except for certain fixed income holdings reported in Category 2 are deposited in mutual funds with various managers. The investments are registered in each manager's name and the University's ownership is recorded in the managers' internal records. The investments in mutual funds and STAROhio are not required to be categorized due to their nature.

	2004	2003
	Fair value	Fair value
Category 2:		
U.S. Treasury obligations	\$ 1,776,655	\$ 5,345,479
U.S. Agency obligations	5,666,552	7,871,393
U.S. Corporate obligations	3,564,222	9,382,428
Category 3:		
Money market funds	588,401	2,072,284
Not Categorized:		
Mutual funds	<u>84,208,766</u>	<u>77,415,618</u>
 Total	 <u>\$95,804,596</u>	 <u>\$102,087,202</u>

The fair value of investments is based on market values provided by a third party.

The University's investment strategy incorporates certain financial instruments that involve, to varying degrees, elements of market risk and credit risk in excess of amounts recorded in the financial statements. Market risk is the potential for changes in the value of financial instruments due to market changes, including interest and foreign exchange rate movements and rate fluctuations embodied in forward, futures, commodity or security prices. Market risk is directly impacted by the volatility and liquidity of the markets in which the related underlying assets are traded. Credit risk is the possibility that a loss may occur due to the failure of the counterparty to perform according to the terms of the contract. The University's risk of loss in the event of a counterparty default is typically limited to the amounts recognized in the statements of net assets and is not represented by the contract or notional amounts of the instruments.

3. ACCOUNTS RECEIVABLE

The composition of accounts receivable at June 30, 2004 and 2003, is summarized as follows:

	2004	2003
Student receivables for fees, room and board	\$ 11,478,936	\$ 9,837,176
Research and other sponsored programs	18,569,393	20,013,266
Other	<u>11,436,722</u>	<u>12,373,383</u>
	41,485,051	42,223,825
Less allowance for doubtful accounts	<u>(3,786,640)</u>	<u>(3,457,029)</u>
Net accounts receivable	<u>\$37,698,411</u>	<u>\$38,766,796</u>

4. NOTES RECEIVABLE

The University notes receivable at June 30, 2004 and 2003, is net of allowances for uncollectible amounts of \$1,069,723 and \$999,940, respectively. Principal repayment and interest terms vary. Federal loan programs are funded primarily through Federal contributions under Perkins and various nursing programs.

The University distributed \$102,471,723 and \$89,197,992 for student loans through the U.S. Department of Education Federal Direct Lending program during the years ended June 30, 2004, and 2003, respectively. These distributions and the related funding sources are included as cash disbursements and cash receipts in the accompanying statements of cash flows.

5. CAPITAL ASSETS

The following tables present the changes in the various fixed asset class categories for the years ended June 30, 2004 and June 30, 2003 for the University:

	Balance July 1, 2003	Additions	Transfers In (Out)	Retirements	Balance June 30, 2004
Capital assets not being depreciated:					
Land	\$ 16,249,524	\$ -	\$ (47,300)	\$ -	\$ 16,202,224
Land improvements	4,701,091				4,701,091
Construction in progress	69,163,238	37,794,806	(79,354,804)		27,603,240
Works of art and historical treasures	<u>6,125,757</u>	<u>1,151,255</u>	<u>926,540</u>		<u>8,203,552</u>
Total capital assets not being depreciated	<u>96,239,610</u>	<u>38,946,061</u>	<u>(78,475,564)</u>	<u>-</u>	<u>56,710,107</u>
Capital assets being depreciated:					
Infrastructure	60,508,864	624,789	26,705,660		87,839,313
Buildings	455,562,688	188,316	51,769,904		507,520,908
Machinery and equipment	94,071,723	7,222,402		(3,521,078)	97,773,047
Library books and publications	67,350,815	3,407,490			70,758,305
Transportation equipment	<u>14,440,863</u>	<u>5,731,097</u>		<u>(2,050,976)</u>	<u>18,120,984</u>
Total capital assets being depreciated	<u>691,934,953</u>	<u>17,174,094</u>	<u>78,475,564</u>	<u>(5,572,054)</u>	<u>782,012,557</u>
Total capital assets	<u>788,174,563</u>	<u>56,120,155</u>	<u>-</u>	<u>(5,572,054)</u>	<u>838,722,664</u>
Less accumulated depreciation:					
Infrastructure	23,439,998	3,105,030			26,545,028
Buildings	199,528,067	10,954,759			210,482,826
Machinery and equipment	53,751,080	8,421,756		(3,139,037)	59,033,799
Library books and publications	49,477,286	3,426,471			52,903,757
Transportation equipment	<u>8,874,595</u>	<u>1,402,480</u>		<u>(1,767,429)</u>	<u>8,509,646</u>
Total accumulated depreciation	<u>335,071,026</u>	<u>27,310,496</u>	<u>-</u>	<u>(4,906,466)</u>	<u>357,475,056</u>
Total capital assets being depreciated—net	<u>356,863,927</u>	<u>(10,136,402)</u>	<u>78,475,564</u>	<u>(665,588)</u>	<u>424,537,501</u>
Capital assets—net	<u>\$ 453,103,537</u>	<u>\$ 28,809,659</u>	<u>\$ -</u>	<u>\$ (665,588)</u>	<u>\$ 481,247,608</u>

	Balance July 1, 2002	Additions	Transfers In (Out)	Retirements	Balance June 30, 2003
Capital assets not being depreciated:					
Land	\$ 16,249,524	\$ -	\$ -	\$ -	\$ 16,249,524
Land improvements	3,026,340	1,674,751			4,701,091
Construction in progress	62,210,357	47,389,457	(40,436,576)		69,163,238
Works of art and historical treasures	<u>6,125,757</u>				<u>6,125,757</u>
Total capital assets not being depreciated	<u>87,611,978</u>	<u>49,064,208</u>	<u>(40,436,576)</u>	<u>-</u>	<u>96,239,610</u>
Capital assets being depreciated:					
Infrastructure	54,073,478	317,115	6,118,271		60,508,864
Buildings	429,764,907	2,791,461	23,127,159	(120,839)	455,562,688
Machinery and equipment	82,918,194	9,423,457	10,037,709	(8,307,637)	94,071,723
Library books and publications	63,925,968	3,424,847			67,350,815
Transportation equipment	<u>12,993,798</u>	<u>1,396,329</u>	<u>1,153,437</u>	<u>(1,102,701)</u>	<u>14,440,863</u>
Total capital assets being depreciated	<u>643,676,345</u>	<u>17,353,209</u>	<u>40,436,576</u>	<u>(9,531,177)</u>	<u>691,934,953</u>
Total capital assets	<u>731,288,323</u>	<u>66,417,417</u>	<u>-</u>	<u>(9,531,177)</u>	<u>788,174,563</u>
Less accumulated depreciation:					
Infrastructure	21,307,389	2,132,609			23,439,998
Buildings	189,502,708	10,048,740		(23,381)	199,528,067
Machinery and equipment	54,297,394	6,893,098		(7,439,412)	53,751,080
Library books and publications	46,154,506	3,322,780			49,477,286
Transportation equipment	<u>8,101,174</u>	<u>1,817,988</u>		<u>(1,044,567)</u>	<u>8,874,595</u>
Total accumulated depreciation	<u>319,363,171</u>	<u>24,215,215</u>	<u>-</u>	<u>(8,507,360)</u>	<u>335,071,026</u>
Total capital assets being depreciated—net	<u>324,313,174</u>	<u>(6,862,006)</u>	<u>40,436,576</u>	<u>(1,023,817)</u>	<u>356,863,927</u>
Capital assets—net	<u>\$ 411,925,152</u>	<u>\$ 42,202,202</u>	<u>\$ -</u>	<u>\$(1,023,817)</u>	<u>\$ 453,103,537</u>

6. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities as of June 30, 2004 and June 30, 2003, consisted of the following:

	2004	2003
Accounts payable	\$ 13,554,580	\$ 15,441,458
Accrued liabilities	<u>25,418,814</u>	<u>23,448,619</u>
Total	<u>\$ 38,973,394</u>	<u>\$ 38,890,077</u>

7. BONDS AND NOTES PAYABLE

The University's bonds and notes payable at June 30, 2004 and 2003, are summarized as follows:

	July 1, 2003	Borrowed	Retired	June 30, 2004	Current
Subordinated general receipts bonds, series 2004	\$ -	\$ 52,885,000	\$ -	\$ 52,885,000	\$ 455,000
Subordinated general receipts bonds, series 2003	-	47,860,000	-	47,860,000	2,575,000
Subordinated general receipts bond anticipation notes, series 2003B	-	6,590,000	6,590,000	-	-
Subordinated general receipts bond anticipation notes, series 2003A	14,400,000	-	14,400,000	-	-
General receipts bond anticipation notes	8,400,000	8,150,000	8,400,000	8,150,000	8,150,000
Subordinated variable general receipts bonds, series 2001	42,120,000	-	5,005,000	37,115,000	3,557,740
General receipts bonds, series 1999	30,200,000	-	830,000	29,370,000	860,000
General receipts bonds, series 1993	<u>37,545,000</u>	<u>-</u>	<u>37,545,000</u>	<u>-</u>	<u>-</u>
Total bonds and notes payable	<u>\$ 132,665,000</u>	<u>\$ 115,485,000</u>	<u>\$ 72,770,000</u>	<u>\$ 175,380,000</u>	<u>\$ 15,597,740</u>

	July 1, 2002	Borrowed	Retired	June 30, 2003	Current
Subordinated general receipts bond anticipation notes, series 2003A	\$ -	\$ 14,400,000	\$ -	\$ 14,400,000	\$ 14,400,000
General receipts bond anticipation notes	8,550,000	8,400,000	8,550,000	8,400,000	8,400,000
Subordinated variable general receipts bonds, series 2001	46,310,000	-	4,190,000	42,120,000	4,427,761
General receipts bonds, series 1999	31,000,000	-	800,000	30,200,000	830,000
General receipts bonds, series 1993	<u>40,020,000</u>	<u>-</u>	<u>2,475,000</u>	<u>37,545,000</u>	<u>2,585,000</u>
Total bonds and notes payable	<u>\$ 125,880,000</u>	<u>\$ 22,800,000</u>	<u>\$ 16,015,000</u>	<u>\$ 132,665,000</u>	<u>\$ 30,642,761</u>

On March 15, 2004, the University issued \$52,885,000 in Subordinated General Receipts Bonds, Series 2004 (the "Series 2004 Bonds"). The proceeds were used to refund the Series 2003B notes, to retire an internal loan for the purchase of a King Air 350, and to finance construction of the University Center including costs associated with capitalized interest.

On September 3, 2003, the University issued \$47,860,000 in Subordinated General Receipts Bonds, Series 2003 (the "Series 2003 Bonds"). The proceeds were used to refund Series 1993 and the Series 2003A notes.

On October 30, 2003, the University issued \$6,590,000 in Subordinated General Receipts Bond Anticipation Notes, Series 2003B in anticipation of the issuance of the Series 2004 Bonds. The proceeds were used for the following purposes: costs associated with University Center site preparation, performance contracting (including Life Sciences heat recovery and steam extension to the Ridges), and the partial renovation of the Lausche Heating Plant. The interest rate on the notes was 1.80% and they matured on May 3, 2004. Prior to the maturity date, the notes were refinanced and rolled into the Series 2004 issue.

On March 12, 2003, the University issued \$14,400,000 in Subordinated General Receipts Bond Anticipation Notes, Series 2003A in anticipation of the issuance of the Series 2003 Bonds. The proceeds were used for the following purposes: construction costs associated with the Avionics Engineering Center and the Lecture Hall, design costs of the University Center, and to retire an internal loan to Regional Higher Education for the purchase of the Pickerington Center. The interest rate on the notes

was 1.69% and they matured on September 3, 2003. At that time the bond anticipation notes, along with the Series 1993 bonds, were refinanced.

During the year ended June 30, 2004, the University issued a series of General Receipts Bond Anticipation Notes totaling \$8,150,000, the proceeds of which are being used to finance the replacement of major administrative systems which include: human resources, payroll, financial and the purchase of an imaging system. The principal payouts on such Notes were made as scheduled and the Notes were re-issued. Notes outstanding of \$8,150,000 at June 30, 2004 mature on January 20, 2005. Principal amounts of \$4,725,000 and \$3,425,000 bear interest rates of 1.45% and 1.50%, respectively.

On May 3, 2001, the University issued \$48,025,000 in Subordinated Variable Rate General Receipts Bonds, Series 2001 (the "Series 2001 Bonds"). The proceeds were for capital equipment and construction costs on various building projects. The balance outstanding as of June 30, 2004 was \$37,115,000.

On October 3, 2001, the University entered into a swap agreement with Morgan Guaranty Trust Company of New York to hedge \$31,020,000 of the University's Series 2001 Bonds. The swap agreement converts the Series 2001 Bonds' variable interest rate to a fixed rate of 4.039%, settled on the first day of each month. The total amount paid related to the swap agreement for the year ended June 30, 2004 and 2003 is \$887,927 and \$841,368, respectively. These amounts are included as an adjustment to interest on capital asset-related debt in the statements of revenues, expenses and changes in net assets. As of June 30, 2004, the swap had a negative fair value of \$578,172. As the swap has a negative fair value the University is not exposed to credit risk. However, should interest rates begin to rise; the negative fair value of the swap would be reduced and could eventually become positive. At that point, the University would be exposed to the counterparty credit risk since the counterparty would be obligated to make payments to the University. The occurrence of a credit event with respect to the University or the counterparty, defined as a reduction in the long term bond rating to less than Baa2 by Moody's Investors Service, Inc. or BBB by Standard & Poor's, would result in termination of the swap agreement. As of June 30, 2004, no termination events have occurred.

On March 15, 1999, the University issued \$32,520,000 in General Receipts Bonds, Series 1999, with which to pay construction costs on various building projects. The balance outstanding as of June 30, 2004 was \$29,370,000.

On January 13, 1994, the University issued \$55,450,000 in General Receipts Bonds, Series 1993, which were issued for advance refunds of the Series 1972, Series 1977 and Series 1978 General Receipts Bonds. The remaining proceeds from this issue were used for the payment of construction costs on the student recreation center. On September 3, 2003, the bonds were refinanced and rolled into the Series 2003 issue.

The 1999 issue (Superior Obligation) is bound by the provisions of the 1972 Trust Agreement (Prior Indenture) and its supplements as described below. The 1972 Trust Agreement and its supplements relates to the provisions of the General Receipts Bonds. These bonds are pledged on a gross pledge and first lien basis of the "General Receipts" of the University. The receipts include the full amount of every type and character of campus receipts, except for State appropriations and receipts previously pledged or otherwise restricted. The University has complied with all covenants of the Trust Agreement and its supplements.

The First Supplemental Trust Agreement binds the 2001 bond issue. While Superior Obligation bonds issued are outstanding, the pledge and lien on the General Receipts authorized and granted on the 2001 issue shall be subordinate to the pledge and lien on the General Receipts that secure the Superior

Obligations. The variable rate of interest in effect at June 30, 2004 was 1.08%. The average variable rate of interest for the year ending June 30, 2004 was 0.99%.

The Second Supplemental Trust Agreement binds the 2003 bond issue. The Series 2003B Bond Anticipation Notes were issued pursuant to a Third Supplemental Trust Agreement. The Fourth Supplemental Trust Agreement binds the 2004 bond issue.

Details of the series are as follows:

Series	Interest Rate	Maturity Fiscal Year	Initial Issue Amount	Outstanding at June 30, 2004
1999	3.60%-5.25%	2005-2025	\$ 32,520,000	\$ 29,370,000
2001	Variable	2005-2027	48,025,000	37,115,000
2003	5.00%-5.25%	2005-2024	47,860,000	47,860,000
2004	2.00%-5.00%	2005-2032	52,885,000	<u>52,885,000</u>
				<u>\$ 167,230,000</u>

Principal and interest payment requirements for the bonded debt for the years subsequent to June 30, 2004 are summarized as follows:

Year ended June 30	Principal	Interest	Swap Interest	Total
2005	\$ 7,447,740	\$ 6,956,665	\$ 1,207,498	\$ 15,611,903
2006	9,642,738	6,171,589	1,141,777	16,956,104
2007	8,139,522	5,881,509	1,070,946	15,091,977
2008	8,685,000	5,596,682	1,000,013	15,281,695
2009	9,215,000	5,275,029	919,086	15,409,115
2010-2014	39,805,000	21,637,573	3,365,091	64,807,664
2015-2019	37,515,000	14,541,191	1,185,191	53,241,382
2020-2024	22,575,000	8,056,021	460,142	31,091,163
2025-2029	15,680,000	3,433,942	89,728	19,203,670
2030-2032	<u>8,525,000</u>	<u>593,913</u>	<u>0</u>	<u>9,118,913</u>
	<u>\$ 167,230,000</u>	<u>\$ 78,144,114</u>	<u>\$ 10,439,472</u>	<u>\$ 255,813,586</u>

8. LEASES

The University has \$212,164 in capital lease obligations that have varying maturity dates through 2008 and carry implicit interest rates ranging from 3.27 % to 12.51 %. Lease arrangements are being used to provide partial financing for certain movable equipment. Capital asset balances as of June 30, 2004 that are financed under capital leases are \$449,846.

Capital leases as of June 30, 2004 and 2003 are summarized as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
For the year ended:					
June 30, 2004	<u>\$337,202</u>	<u>\$165,562</u>	<u>\$(290,600)</u>	<u>\$212,164</u>	<u>\$ 93,017</u>
June 30, 2003	<u>\$793,656</u>	<u>\$214,027</u>	<u>\$(670,481)</u>	<u>\$337,202</u>	<u>\$249,836</u>

The scheduled maturities of these leases as of June 30, 2004 are:

	Minimum Lease Payments
2005	\$ 102,826
2006	59,790
2007	43,034
2008	<u>23,700</u>
Total minimum lease payments	229,350
Less amount representing interest	<u>17,186</u>
Net minimum capital lease payments	212,164
Less current portion	<u>93,017</u>
Noncurrent capital lease obligations	<u>\$ 119,147</u>

9. OPERATING LEASES

The University leases various buildings, office space, and equipment under operating lease agreements. These facilities and equipment are not recorded as assets on the balance sheet. The total rental expense under these agreements was \$2,770,672 for the year ended June 30, 2004.

Future minimum payments for all significant operating leases with initial terms in excess of one year as of June 30, 2004, are as follows:

Years Ended June 30	
2005	\$2,908,746
2006	2,188,716
2007	1,764,122
2008	660,734
2009	389,770
2010-2019	<u>328,569</u>
Total minimum lease payments	<u>\$ 8,240,657</u>

10. COMPENSATED ABSENCES

Per University policy, salaried faculty and staff earn vacation at the rate of 22 days per year with a maximum accrual of 32 days. Upon termination they are entitled to a payout of their accumulated balance. Hourly classified employees earn vacation at rates per years of service, ranging from 10 to 25 days per year. The maximum accrual is equal to the amount earned in three years, which is subject to payout upon termination. The liability for accrued vacation at June 30, 2004 and 2003 amounted to approximately \$8,712,000 and \$9,274,000, respectively.

All University employees are entitled to a sick leave credit equal to 15 days per year (earned on a pro-rata monthly basis for salaried employees and on a pro-rata hourly basis for classified hourly employees). Salaried employees with 10 or more years of service are eligible to receive a payout upon retirement of up to 25% of unused days (maximum of 30 days). Hourly classified employees with 10 or more years of service are eligible for payout upon retirement of up to 50% of unused days (maximum of 60 days). The liability for accrued sick leave at June 30, 2004 and 2003 amounted to approximately \$3,880,000 and \$4,126,000, respectively.

A summary of compensated absences as of June 30, 2004 and 2003 follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
For the year ended:					
June 30, 2004	<u>\$13,399,793</u>	<u>\$ 384,950</u>	<u>\$ (1,192,785)</u>	<u>\$12,591,958</u>	<u>\$1,113,481</u>
June 30, 2003	<u>\$13,135,006</u>	<u>\$8,310,147</u>	<u>\$ (8,045,360)</u>	<u>\$13,399,793</u>	<u>\$1,150,000</u>

11. RETIREMENT PLANS

Defined Benefit Plans—All University employees are eligible to participate in contributory retirement plans that are administered by the Ohio Public Employees Retirement System of Ohio (“OPERS”) and the State Teachers Retirement System of Ohio (“STRS”). The particular system in which the employee enrolls is dependent on their position with the University. Both OPERS and STRS are cost sharing, multiple-employer defined benefit pension plans. Both systems provide retirement and disability benefits, annual cost of living adjustments and death benefits to plan members and beneficiaries. Authority to establish and amend benefits is provided by state statute per Chapter 145 of the Ohio Revised Code. The payroll for employees covered by OPERS and STRS for the year ended June 30, 2004 is \$90,227,000 and \$74,818,000, respectively. The payroll for employees covered by OPERS and STRS for the year ended June 30, 2003 is \$93,473,000 and \$74,118,000, respectively. For the years ended June 30, 2004 and 2003, the University’s total payroll is \$238,684,000 and \$236,090,000, respectively.

Both OPERS and STRS issue a stand-alone financial report. Interested parties may obtain a copy of the OPERS report by making a written request to 277 East Town Street, Columbus, Ohio 43215-4642 or by calling (614) 222-6705 or 1-800-222-PERS (7377). The STRS report may be obtained by making a written request to 275 East Broad Street, Columbus, Ohio 43215-3771.

Defined Contribution Plans—The Alternative Retirement Plan (“ARP”) is a defined contribution pension plan, under IRS section 401(a), and established by Ohio Amended Substitute House Bill 586 (ORC 3305.02) on March 31, 1998 for public institutions of higher education. The University’s Board of Trustees adopted the University’s plan on April 18, 1998. Full-time salaried employees are eligible to choose a provider, in lieu of OPERS or STRS, from the list of eight providers currently approved by the

Ohio Department of Insurance and who hold agreements with the University. Employee and employer contributions equal to those required by STRS and OPERS are required for ARP, less any amounts required to be remitted to the state retirement system in which the employee would otherwise have been enrolled.

Eligible employees have 120 days from their date of hire to make an irrevocable election to participate in the alternative retirement plan. Under this plan, employees who would have otherwise been required to be in STRS or OPERS and who elect to participate in the ARP must contribute the employee's share of retirement contributions (10.0% STRS or 8.5% OPERS) to one of eight private providers approved by the Ohio Department of Insurance. The legislation mandates that the employer must contribute an amount to the state retirement system to which the employee would have otherwise belonged, based on an independent actuarial study commissioned by the Ohio Retirement Study Council and submitted to the Ohio Board of Regents. That amount is 0% for OPERS and 3.5% for STRS for the year ended June 30, 2004. The employer also contributes what would have been the employer's share of the appropriate retirement system, less the aforementioned percentages, to the private provider selected by the employee. The University plan provides these employees with immediate plan vesting.

ARP does not provide disability benefits, annual cost-of living adjustments, postretirement health care benefits, or death benefits to plan members and beneficiaries. Benefits are entirely dependent on the sum of contributions and investment returns earned by each participant's choice of investment options.

Retirement Plan Funding—The Ohio Revised Code provides statutory authority for employee and employer contributions to retirement systems. The 2004 employee contribution rates for state employers are 8.5% of covered payroll for OPERS, 10.1% of covered payroll for law enforcement employees and 10.0% of covered payroll for STRS. The 2004 employer contribution rates for state employers is 13.31% of covered payroll for OPERS, 16.7% of covered payroll for law enforcement, and 14.0% of covered payroll for STRS. The employee and employer rates are the same for ARP employees as the retirement system under which they would otherwise be. However, for those who would otherwise be covered by STRS, 3.5% of the employer contribution goes to the STRS retirement system. The University's contributions each year are equal to its required contributions.

University contributions for the current and two preceding years are summarized as follows:

	Employer contributions		
	STRS	OPERS	ARP
2004	\$ 10,474,000	\$ 12,009,000	\$ 6,053,000
2003	10,376,000	12,441,000	5,618,000
2002	10,228,000	12,183,000	4,908,000

Other Post-Employment Benefits—In addition to the pension benefits described above, Ohio Law provides that the University fund postretirement health care benefits to retirees and their dependents through employer contributions to the Ohio Public Employees Retirement System of Ohio ("OPERS") and the State Teachers Retirement System of Ohio ("STRS").

OPERS provides postretirement health care coverage to age and service retirees with ten or more years of qualifying Ohio service credit. Health care coverage for disability recipients and primary survivor recipients is available. The health care coverage provided by the retirement system is considered an Other Post-employment Benefit ("OPEB") as described in GASB Statement No. 12. A portion of each employer's contribution to OPERS is set aside for funding of postretirement health care. The Ohio Revised Code provides statutory authority for employer contributions. The OPERS law enforcement

program is separated into two divisions, law enforcement and public safety, with separate employee contribution rates and benefits. The 2003 employer contribution rate for state employers was 13.31% of covered payroll of which 5.00% was the portion used to fund health care for the year. For both the public safety and law enforcement divisions the 2003 employer rate was 16.70% and 5.00% was used to fund health care. The number of active contributing participants was 364,881.

The actuarial value of the OPERS' net assets available for OPEB at December 31, 2002 (the date of the system's latest actuarial review) is \$10.0 billion. The actuarially accrued liability and the unfunded actuarial accrued liability, based on the actuarial cost method used, is \$18.7 billion and \$8.7 billion, respectively.

STRS provides access to health care coverage to retirees who participated in the Defined Benefit or Combined Plans, and their dependents. Coverage under the current program includes hospitalization, physicians' fees, prescription drugs and partial reimbursement of monthly Medicare Part B premiums. All benefit recipients and sponsored dependents are eligible for health care coverage. Pursuant to the Ohio Revised Code ("ORC"), the State Teachers Retirement Board (the "board") has discretionary authority over how much, if any, of the health care costs will be absorbed by STRS. Most benefit recipients pay a portion of the health care cost in the form of a monthly premium.

The ORC grants authority to STRS to provide health care coverage to benefit recipients, spouses and dependents. By Ohio law the cost of the coverage paid from STRS funds shall be included in the employer contribution rate, currently 14% of covered payroll.

The Retirement Board allocates employer contributions to the Health Care Stabilization Fund from which health care benefits are paid. For the fiscal year ended June 30, 2003, the Board allocated employer contributions equal to 1.0% of covered payroll to the Health Care Stabilization Fund. For the fiscal year ended June 30, 2002, 4.5% of covered payroll was allocated to the fund. The balance in the Health Care Stabilization Fund was approximately \$2.8 billion on June 30, 2003, the date of the most recent information available from STRS.

For the year ended June 30, 2003, the date of the most recent information available from STRS, net health care costs paid by STRS were \$352,301,000. There were 108,294 eligible benefit recipients.

12. EARLY RETIREMENT INCENTIVE PLAN ("ERIP")

In fiscal year 2003 the University Board of Trustees approved an Early Retirement Incentive Plan ("ERIP") buyout for eligible employees in the Ohio Public Employees Retirement System ("OPERS"). An ERIP allows the University to purchase additional service credit, in this case two years, which enables eligible employees to retire early or to retire with a larger retirement benefit than they may have otherwise. The buyout period began on May 1, 2003. The period remained open until June 30, 2004. A \$10,000 incentive was offered to employees who signed up for the buyout by June 30, 2003 and who would retire by September 1, 2003. Eligible employees were those eligible to retire with 5 years of service at age 60, 25 years of service at age 55 or 30 years of service at any age; who became eligible to retire due to the incentive plan; who became eligible to retire during the open period; or who became eligible due to purchasing additional service credit, i.e., exempt, refunded, military or other eligible time.

As of June 30, 2004, 192 employees have signed up for the ERIP for a total cost estimate of \$9.5 million that includes sick and vacation payouts in accordance with standard policy, the \$10,000 incentive bonus for the 131 employees who left by September 1, 2003 and the OPERS payment calculated and billed by OPERS.

13. RISK MANAGEMENT AND CONTINGENCIES

Legal—During the normal course of operations, the University has become a defendant in various legal and administrative actions. In accordance with Statement of Financial Accounting Standards No. 5, *Accounting for Contingencies*, liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. However, in the opinion of in-house legal counsel and University management, the disposition of all pending litigation would not have a material adverse effect on the University's financial position.

Self-insurance—The University provides medical and dental coverage for its employees on a self-insurance basis. Expenses for claims are recorded on an accrual basis based on the date claims are incurred. The University applies GASB Statement No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues*.

A summary of changes in the self-insurance claims liability for each of the periods in the three-year period ending June 30, 2004 is as follows:

	2004	2003	2002
Accrued claims liability at beginning of year	\$ 3,571,000	\$ 4,211,000	\$ 6,150,000
Incurred claims—net of favorable settlements	27,932,000	27,780,000	20,450,000
Claims paid	<u>(28,003,000)</u>	<u>(28,420,000)</u>	<u>(22,389,000)</u>
Accrued claims liability at end of year	<u>\$ 3,500,000</u>	<u>\$ 3,571,000</u>	<u>\$ 4,211,000</u>

Liability for claims is accrued based on estimates of the claims liabilities made by the University's third party actuary. These estimates are based on past experience and current claims outstanding. Actual claims experience may differ from the estimate.

Commercial Insurance Coverage—The University has the following commercial insurance policies.

Type	Deductible	Coverage
Property	\$ 100,000	\$ 1,336,438,247
Excess	100,000	60,000,000
Non-owned aviation	-	25,000,000
Aircraft and airport	50,000	5,000,000 to 50,000,000
Primary umbrella	100,000	4,000,000
Crime	100,000	2,000,000
General	100,000	1,000,000
Educators legal	100,000	1,000,000
Automobile	100,000	1,000,000
Foreign	-	1,000,000

Workers' Compensation Coverage—The University participates in a plan that pays workers' compensation benefits to beneficiaries who have been injured on the job. The Ohio Bureau of Workers' Compensation calculates the estimated amount of cash needed in the subsequent fiscal year to pay the claims for these workers and sets rates to collect this estimated amount from participating state agencies and universities in the subsequent year.

14. CAPITAL PROJECT COMMITMENTS

At June 30, 2004 the University is committed to future capital expenditures as follows:

Contractual commitment	\$40,053,057
Estimated completion costs of projects	<u>24,335,197</u>
	<u>\$64,388,254</u>
These projects will be funded by:	
State appropriations	\$14,551,125
University funds	45,928,285
Gifts, federal grants and other	<u>3,908,844</u>
	<u>\$64,388,254</u>

15. OTHER NONCURRENT LIABILITIES

Bureau of Workers' Compensation Liability—The Bureau of Workers' Compensation Liability is summarized as follows for the years ended June 30, 2004 and 2003, respectively:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
For the year ended: June 30, 2003	<u>\$ 7,049,597</u>	<u>\$ -</u>	<u>\$ (7,049,597)</u>	<u>\$ -</u>	<u>\$ -</u>

Refundable Advances for Federal Student Loans—Refundable advances for federal student loans are summarized as follows for the years ended June 30, 2004 and 2003, respectively:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
For the year ended: June 30, 2004	<u>\$ 7,174,958</u>	<u>\$ 606,820</u>	<u>\$ -</u>	<u>\$ 7,781,778</u>	<u>\$ -</u>
June 30, 2003	<u>\$ 6,707,002</u>	<u>\$ 467,956</u>	<u>\$ -</u>	<u>\$ 7,174,958</u>	<u>\$ -</u>

16. DONOR RESTRICTED ENDOWMENTS

Under the standard established by Section 1715.56 of the Ohio Revised Code, an institution may appropriate so much as is prudent of the realized and unrealized net appreciation of the fair value of the assets of the endowment fund over the historic dollar value of the fund for the uses and purposes for which an endowment fund is established. The University's endowment spending policy is based on the concept of total return and the spending rate for any particular year is to be 5%, phased in over a two year period as follows: 5.7% in fiscal year 2004 and 5.4% in fiscal year 2005. However, if the total return rate as of the date on which a spending rate is determined exceeds 5% plus the inflation adjuster, the Board may, but shall not be required to, increase the spending rate up to the amount such excess is greater than 5%, but in no event greater than 9%.

The amounts of net appreciation on investments of donor-restricted endowments that are available for authorization for expenditure by the Board are \$13,765,000 and \$12,209,000 for June 30, 2004 and 2003, respectively. Those amounts are reported as restricted expendable net assets.

17. EXTRAORDINARY ITEM—WORKERS’ COMPENSATION

In fiscal year 2002, the State of Ohio required state universities to record a portion of the state’s workers’ compensation liability in its financial statements. In fiscal year 2003, the State of Ohio reversed this decision and as such the workers’ compensation liability and all related expenses were completely reversed in the 2003 financial statements.

Under the State of Ohio’s Workers’ Compensation program, the University is part of a pool of state agencies and state universities that pays workers’ compensation premiums into the State Insurance Fund on a pay-as-you-go basis. In fiscal year 2002, as part of the State of Ohio’s implementation of GASB Statements No. 34 and No. 35, the State of Ohio required each state agency and state university to record a portion of the estimated actuarial liability for workers’ compensation in its financial statements. Accordingly, the University’s statement of net assets reflected an unfunded workers’ compensation liability of \$7,049,597 at June 30, 2002.

In 2003, the Auditor of State and the Office of Budget and Management agreed to re-examine this accounting treatment. Based on their review and consultation with representatives of the state-assisted universities, the agencies determined that the State of Ohio’s General Revenue Fund would recognize the entire liability for future workers’ compensation claims for the state, including the universities. Accordingly, the University’s 2003 statement of net assets reflected a reallocation of the \$7,049,597 unfunded workers’ compensation liability to the State of Ohio which reduced this liability to \$0 at June 30, 2003. This entire reduction of expense was reported on the University’s 2003 statement of revenues, expenses, and changes in net assets as an Extraordinary Item.

18. INTERNAL DESIGNATION OF FUNDS

The University’s statements of net assets shows \$61,945,957 and \$50,652,596 for Unrestricted Net Assets as of June 30, 2004 and 2003, respectively. Internally those funds have been designated as follows:

	2004	2003
Quasi endowments	\$ 9,233,638	\$ 10,048,611
Auxiliary enterprises, including open purchase orders	13,025,210	7,619,753
Open purchase orders—educational and general	2,801,902	1,881,553
Departmental carryforward	<u>36,885,207</u>	<u>31,102,679</u>
	<u>\$ 61,945,957</u>	<u>\$ 50,652,596</u>

19. THE OHIO UNIVERSITY FOUNDATION

The Ohio University Foundation, a discretely presented component unit, was incorporated in Ohio in October 1945 to support the educational undertakings of Ohio University. The Foundation is authorized to solicit and receive gifts and contributions for the benefit of the University and to ensure that funds and property received are applied to the uses specified by the donor.

The Foundation's wholly owned subsidiary, Inn-Ohio of Athens, Inc. (the "Inn"), owns and operates a 144-room hotel and restaurant facility in Athens, Ohio known as The Ohio University Inn. The Foundation's other wholly owned subsidiary, Housing for Ohio, Inc. ("Housing"), constructed and operates a 182-unit student-housing complex in Athens, Ohio. The Foundation also owns a majority interest in Diagnostic Hybrids, Inc., ("DHI"), which develops and manufactures tissue cell cultures, antibody kits, and biological reagents for use in medical laboratories.

A separate financial report for the Foundation is available by contacting The Ohio University Foundation, HDL Center, Room 164, Athens, Ohio 45701 or (740) 593-1884.

(a) Investments

The Foundation has estimated the fair values of its financial instruments using available quoted market information and other valuation methodologies in accordance with Statement of Financial Accounting Standards No. 107, *Disclosures About Fair Value of Financial Instruments*. Accordingly, the estimates presented are not necessarily indicative of the amounts that the Foundation could realize in a current market exchange. Determinations of fair value are based on subjective data and significant judgment relating to timing of payments and collections and the amounts to be realized. Different market assumptions and/or estimation methodologies might have a material effect on the estimated fair value amounts.

The Foundation's cost and market value of the investments in securities at June 30, 2004 and 2003 are as follows:

	2004		2003	
	Cost	Market	Cost	Market
Common and preferred stock	\$ 84,182,536	\$ 81,417,112	\$ 84,093,483	\$ 71,935,380
Short-term cash investments	2,533,332	2,533,332	4,167,328	4,167,328
Bonds and debentures	22,126,609	21,865,913	47,194,481	47,713,041
Other	37,147,472	36,894,431	5,924,390	5,260,075
Total investments	\$ 145,989,949	\$ 142,710,788	\$ 141,379,682	\$ 129,075,824

(b) Concentration of Credit Risk

Financial instruments, which potentially subject the Foundation to a concentration of credit risk, consist principally of contributions receivable, investments for the Foundation, and receivables related to operations of the Inn. Exposure to losses on contributions receivable is principally dependent on each donor's financial condition. The Foundation monitors the exposure for credit losses and maintains allowances for anticipated losses.

Investments are recorded at fair value. Investment securities are exposed to various risks, such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least possible that changes in the value of investment securities will occur in the near term and that such changes could materially affect the Foundation's consolidated statements of financial position and activities.

(c) Gifts and Contributions

Contributions are recorded at their fair value on the date of receipt. All contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Contributions received that

are designated for future periods or restricted by the donor for specific purposes are reported as temporarily restricted or permanently restricted support that increases those net asset categories. When a donor restriction expires (when a stipulated time restriction ends or the purpose of restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Contributed property is recorded at fair value at the date of donation. If donors stipulate how long the assets must be used or restrict the use of such assets for a specific purpose, the contributions are recorded as restricted support. In the absence of such stipulations, contributions of property are recorded as unrestricted support.

Contributions of charitable gift annuities are reduced by the actuarially determined liability resulting from acceptance of the gift. Contributions are held in charitable remainder trusts at the present value of their estimated future benefits to be received when the trust assets are distributed upon notification of the donor's death.

(d) Pledges Receivable

Unconditional promises to give that are expected to be collected within one year are recorded at net realizable value. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of their estimated future cash flows. The discount on those amounts is computed using a risk-free interest rate. The discount rate utilized was 1.3% for fiscal year 2004 and 0.84% for fiscal year 2003. Amortization of the discounts is included in contribution revenues. Unconditional promises to give, which are silent as to the due date, are presumed to be time restricted by the donor until received and are reported as temporarily restricted net assets. Conditional promises to give are not included as support until the conditions on which they depend are substantially met.

Included in pledges receivable are the following unconditional promises to give at June 30, 2004 and 2003:

	2004	2003
Unconditional promises to give before unamortized discount and allowance for uncollectibles	\$ 18,921,209	\$ 14,063,575
Less allowance for uncollectibles	<u>482,080</u>	<u>796,240</u>
Subtotal	18,439,129	13,267,335
Less unamortized discount	<u>513,940</u>	<u>772,275</u>
Unconditional promises to give—net	<u>\$ 17,925,189</u>	<u>\$ 12,495,060</u>

	2004		2003	
	Temporarily Restricted	Permanently Restricted	Temporarily Restricted	Permanently Restricted
Amounts due in:				
Less than one year	\$ 5,345,349	\$3,354,542	\$3,128,660	\$ 1,732,736
One to five years	5,320,684	3,796,531	5,215,941	2,144,811
More than five years	94,462	13,621	238,702	34,210
Total	<u>\$10,760,495</u>	<u>\$7,164,694</u>	<u>\$8,583,303</u>	<u>\$3,911,757</u>

(e) Intentions

The Foundation receives communications from donors indicating that the Foundation has been included in the donor's will or life insurance policy as beneficiary, representing intentions to give rather than promises to give. Such communications are not unconditional promises to give because the donors retain the ability to modify their wills and insurance policies during their lifetimes. The total realizable value of these intended gifts has not been established, nor have the intended gifts been recognized as an asset or contribution revenue. Such gifts are recorded when the Foundation is notified of the donor's death, the will is declared valid by a probate court, and the proceeds are measurable.

(f) Split-Interest Agreements

Charitable Gift Annuities—Under charitable gift annuity agreements, all assets are held by the Foundation. Therefore, the Foundation has recorded the donated assets at fair value and the liabilities to the donor or his/her beneficiaries discounted to the present value of the estimated future payments to be distributed by the Foundation to such individuals at a rate established at the beginning of the agreement. The amount of the contribution is the difference between the asset and liability and is recorded as contribution revenue. The discount rate applied to gift annuities held at June 30, 2004 and 2003 ranged from 3.6% to 9.8%.

Charitable Remainder Trust—Under charitable remainder trust agreements, the Foundation serves as the remainderman, whereby the Foundation will receive the net assets of the trust upon death of the donor's beneficiary. During the life of the trust, the donor, or the donor-designated beneficiary, will receive regular payments as established by the trust.

In instances where the donor has not specifically reserved the right to change the remainderman, and all assets of charitable remainder trusts are maintained by a third-party trustee in an irrevocable trust for the benefit of the Foundation, the Foundation will recognize, as contribution revenue and as a receivable, the present value of the estimated future benefits to be received when the trust assets are distributed. The trustee disburses income earned on the assets of the charitable remainder trusts to the donor or donor-designated beneficiaries.

In instances where the donor has not specifically reserved the right to change the remainderman, and the Foundation serves as the trustee, the Foundation will recognize the fair market value of the assets of the trust, as well as a liability for the net present value of future payments to be distributed by the Foundation to the donor or his/her designated beneficiaries. The amount of the contribution is the difference between the asset and liability at the inception of the trust. The present value of the future payments to the donor-designated beneficiary is determined using a discount rate established at the beginning of the trust. At June 30, 2004 and 2003, the discount rate applied to the charitable remainder trusts was 1.3% and 6%, respectively.

Certain charitable remainder trust transactions are not reported on the consolidated statement of financial position or the consolidated statement of activities, as in these cases the remainderman can be changed by the donor prior to his/her death.

Adjustments to the receivable to reflect amortization of the discount, revaluation of the present value of the estimated future payments to the donor-designated beneficiaries, and changes in actuarial assumptions during the term of the trust will be recognized as changes in the value of split-interest agreements. Upon the death of the donor-designated beneficiaries, the receivable is closed, the assets received from the trust are recognized at fair value, and any difference is reported as a change in the value of split-interest agreements.

Revocable Trusts—Under revocable trust agreements, the Foundation serves as the remainderman, whereby the Foundation will receive the net assets of the trust upon death of the donor's beneficiary. All assets of the trusts may be maintained by a third-party trustee for the benefit of the Foundation, or by the Foundation if named as a trustee. The trustee disburses income earned on the assets of trusts to the donor or donor-designated beneficiaries. Under revocable trust agreements, the donor maintains the ability to legally dissolve the trusts and may or may not reserve the right to change the remainderman. For these reasons, the Foundation does not report revocable trust transactions on the consolidated statement of financial position or the consolidated statement of activities if the trust is held by a third-party trustee.

(g) Income Taxes

The Internal Revenue Service has determined that The Ohio University Foundation is an exempt organization under Section 501(c)(3) of the Internal Revenue Code, except for taxes on unrelated income. Unrelated income taxes totaled \$1,074,305 in 2004 and \$880,000 in 2003.

(h) Net Assets

Foundation Unrestricted Net Assets—The unrestricted net assets consist of operating funds available for any purpose authorized by the board of trustees. The amount necessary to restore the fair value of assets of donor-related endowment accounts to the required principal levels has been funded from unrestricted net assets. The cumulative affect of these amounts were \$5,355,042 and \$7,201,046 at June 30, 2004 and 2003, respectively.

Foundation Temporarily Restricted Net Assets—Temporarily restricted net assets consist of funds that are restricted for a specific use or time determined by the donor.

Temporarily restricted net assets as of June 30, 2004 and 2003 are available for the following purposes:

	2004	2003
Alumni relations	\$ 950,657	\$ 1,046,320
Institutional support	5,975,053	6,309,280
Instruction and departmental support	30,901,314	27,239,282
Academic services support	10,127,735	9,716,080
Intercollegiate athletics support	742,156	569,546
Student services	1,367,227	875,159
Scholarships and fellowships	31,714,556	28,939,445
Public services	313,279	416,339
Research	1,034,220	1,147,302
Fund-raising and development	1,375,919	1,442,237
Other	<u>149,155</u>	<u>372,920</u>
	<u>\$84,651,271</u>	<u>\$78,073,910</u>

Foundation Permanently Restricted Net Assets—Permanently restricted net assets consist of funds arising from a gift or bequest in which the donor has stipulated, as a condition of the gift, that the principal be maintained in perpetuity and only the investment income from investment of the funds be expended. Certain donor endowments also specify that a portion of the earnings from the investment be reinvested as principal, or that all income earned over a period of time be reinvested. Amounts are also transferred for specific uses as authorized from time to time by the donor.

Permanently restricted net assets as of June 30, 2004 and 2003 are available for the following purposes:

	2004	2003
Alumni relations	\$ 1,159,005	\$ 603,760
Institutional support	2,163,136	2,361,848
Instruction and departmental support	45,185,308	36,012,303
Academic services support	3,491,537	3,201,640
Intercollegiate athletics support	85,955	39,494
Student services	1,964,259	2,186,425
Scholarships and fellowships	41,006,518	37,294,237
Public services	297,523	406,069
Research	874,718	768,138
Fund-raising and development	124,204	87,868
Other	<u>618,261</u>	<u>9,266</u>
	<u>\$96,970,424</u>	<u>\$82,971,048</u>

(i) Inn-Ohio Of Athens, Inc.

The Ohio University Inn was purchased by the Foundation on August 30, 1986. The primary purpose for which the Foundation invested in the Inn was to provide affordable and convenient housing, dining, and conference facilities for the University employees, alumni, and guests. As a significant portion of the Inn's revenues is derived from these customers, the Foundation is committed to financially supporting the Inn.

The Inn's business is subject to all of the risks inherent in the lodging industry. These risks include, among other factors, varying levels of demand for rooms and related services, adverse effects of general and local economic and market conditions, changes in governmental regulations that influence wages or prices, changes in interest rates, the availability of credit and changes in real estate taxes and other operating expenses, and the recurring need for renovation, refurbishment, and improvements.

Effective November 30, 1996, a management agreement (the "Management Agreement") was entered into with Winegardner & Hammons, Inc, (the "Manager"). The Management Agreement was amended during fiscal year 2001 to automatically renew annually unless notified in writing of renewal 60 days prior to the end of the fiscal year. The Manager's compensation is a base fee plus 15% of the hotel's net available operating profit as defined in the Management Agreement.

In fiscal year 2004 and 2003, base management fees incurred by the Inn with respect to the Manager were \$100,000 and \$100,000 and incentive fees were \$100,060 and \$114,640, respectively.

As of June 30, 2004 and 2003, the Inn has net operating loss ("NOL") carryforwards of \$153,000 and \$365,000, respectively, for Federal income tax purposes. The NOL carryforwards expire in years 2004 through 2012. The Inn has reflected deferred income taxes at a 40% tax rate, which represents a blended statutory Federal and state income tax rate. As of June 30, 2004 and 2003, the Inn has recorded a valuation allowance of approximately \$163,500 and \$279,000, respectively, due to the uncertainty of the future realizability of its remaining net deferred tax asset carryforwards, in accordance with the provisions of SFAS No. 109.

Debt Obligations—Long-term debt of the Inn as of June 30, 2004 and 2003 consists of the following:

	2004	2003
1996 Serial Project Bonds:		
5.75% due November 1, 2003	\$ -	\$ 115,000
5.85% due November 1, 2004	120,000	120,000
5.95% due November 1, 2005	130,000	130,000
6.05% due November 1, 2006	140,000	140,000
1996 Term Project Bonds—		
6.25%, at 97.61%, due November 1, 2011	<u>830,000</u>	<u>830,000</u>
	1,220,000	1,335,000
Less: Unamortized discount on Series 1996 Bonds	<u>9,670</u>	<u>10,989</u>
Total	<u><u>\$1,210,330</u></u>	<u><u>\$1,324,011</u></u>

The 1996 Serial and Term Project Bonds (the "Bonds") are secured by a mortgage on the Inn and a security agreement granted by the Inn. These Bonds are also guaranteed by the Foundation from unrestricted money and investments.

The 1996 Term Project Bonds require the Inn to make monthly payments to a trustee. These payments accumulate in the bond fund to pay principal and interest on the Bonds. Principal payments are due annually on November 1; interest payments are due semiannually each May 1 and November 1 and are payable from the bond fund. The 1996 Serial Project Bonds are subject to redemption prior to maturity, including mandatory sinking fund redemption. After November 1, 2006, the Inn has the option to prepay

the 1996 Bonds. The balance in the bond fund at June 30, 2004 and 2003 was \$92,662 and \$90,653, respectively.

The 1996 Bonds maturing in November 2011 are subject to a mandatory sinking fund requirement to be deposited as set forth in the following schedule:

	Amount
November 1:	
2007	\$ 145,000
2008	155,000
2009	165,000
2010	175,000
2011	<u>190,000</u>
 Total	 <u>\$ 830,000</u>

The fair value of the debt obligations at June 30, 2004 and 2003 approximated their carrying value.

(j) Housing For Ohio, Inc.

In November 1999, the Foundation established Housing for Ohio, Inc. (“Housing”), a limited liability company and 501(c)(3) corporation, with the purpose of acquiring, developing, constructing, and operating a 182-unit student-housing rental project which contains 580 beds. The property, known as University Courtyard Apartments (the “Project”), is located in Athens, Ohio on property owned by Ohio University and leased to Housing. The facility is managed and operated by a private entity.

Debt—In September 2000, Housing offered \$31,985,000 of variable-rate, tax-exempt bonds (the “2000 Bonds”). The proceeds of the 2000 Bonds financed the construction, installation, and equipping of the Project. The 2000 Bonds will be fully matured at June 2032 and bear interest at an adjustable rate as determined weekly by the remarketing agent, based on their knowledge of prevailing market conditions, except that in no event will the interest rate exceed 12%. The average interest rate for the year ended June 30, 2004 and 2003 was 1.03% and 1.32%, respectively, and the actual interest rate at June 30, 2004 and 2003 was 1.10% and 1.04%, respectively.

As collateral, until all principal and interest on any of the 2000 Bonds has been paid, Housing has pledged, assigned, and granted a security interest to its right, title, and interest in gross revenues of University Courtyard and related assets. The Foundation has made no additional pledge of assets or revenues to the 2000 Bonds, which are nonrecourse to the Foundation.

Principal payments for the bonded debt for the years subsequent to June 30, 2004 are summarized as follows:

Year Ending June 30	Principal
2005	\$ 340,000
2006	445,000
2007	530,000
2008	575,000
2009	635,000
Thereafter	<u>28,865,000</u>
Total	<u>\$31,390,000</u>

Debt issuance costs are included in property on the balance sheet and are amortized over the term of the bonds. Amortization during the years ended June 30, 2004 and 2003 was \$34,965 and \$17,675, respectively.

Litigation—Housing, Ambling Companies, Inc., and Subsidiaries (“Ambling”), the developer and manager of Housing for Ohio, and various of its subcontractors were defendants along with Ohio University in a legal action initiated by the United Brotherhood of Carpenters and Joiners of America and joined in by the State of Ohio, Department of Commerce for the payment of back wages and penalties. During fiscal 2003, Housing and Ohio University were relieved as defendants in the litigation.

Furthermore, during fiscal 2004, Housing was a cross-claim plaintiff against Ambling and the general contractor, for indemnification of any expenses related to the cost of the project and litigation expenses beyond the Developer Guaranteed Project Cost of \$26,308,823. During fiscal 2003, Ambling notified Housing, requesting reimbursement by Housing for various additional costs totaling \$2,400,000, incurred during the construction process. Subsequent to June 30, 2003, Ambling filed a formal legal action for the claim in the amount of \$2,600,000. While the \$2,600,000 claim was disputed by Housing, the original \$2,400,000 claim that was identified prior to June 30, 2003 was included in the building cost and related liabilities recorded on Housing’s statement of financial position. Also, subsequent to June 30, 2003, Ambling filed an additional lawsuit against Housing requesting reimbursement from Housing for \$631,000 related to development fees, of which \$300,000 was held in escrow with the bond trustee. Housing filed a counter claim against the general contractor for \$1,000,000 for breach of contract and indemnity. The Ambling claims and the indemnity claims against Ambling and the general contractor were resolved by mediation. The parties came to a settlement agreement on May 19, 2004, in which Housing would pay Ambling a total sum of \$2,000,000. The settlement agreement required an initial payment of \$1,300,000 to Ambling in cash no later than thirty days after the issuance of orders of the court, and a cognovit promissory note for \$700,000 payable in ten annual installments of \$70,000 commencing on June 1, 2005. The entire note balance becomes due and payable if Ambling’s current management agreement is terminated or if certain other events occur.

In the opinion of management, the litigation had no material adverse impact on the Foundation’s consolidated financial statements.

(k) Diagnostic Hybrids, inc. (“DHI”)

DHI, an Ohio corporation located in Athens, Ohio, develops and manufactures genetically engineered and non-engineered tissue cell cultures, monoclonal antibody kits, and biological reagents for use by

laboratory technicians in medical laboratories. These products are used to diagnose viral diseases and endocrine disorders.

The Foundation owns 802,720 shares of Class A Common Stock and 384,622 shares of Convertible Preferred Stock, which represent an approximate 71% ownership of DHI.

The Preferred Shares are convertible into common shares based on an initial conversion price of \$6.50 per common share, adjusted for shares and options issued at prices below \$6.50 per share. The Preferred Shares also convert automatically on a qualified initial public offering and have voting rights equal to common shares and a liquidation preference over common shares. In addition, the Foundation has conversion rights that give the Foundation the right to convert all of the Preferred Shares to an amount of common shares, as defined in the Share Purchase Agreement (the "Agreement") between the Foundation and DHI. These conversion rights expire on February 15, 2006. Through February 15, 2006, in accordance with the Agreement, in the event that all potential common shares of DHI are outstanding, as defined, the Foundation's minimum ownership percentage in DHI would be 50.1%.

DHI accounts for its employee and director stock-based compensation plans in accordance with APB Opinion No. 25. DHI has elected not to adopt the cost recognition provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*. DHI follows only the disclosure provisions of SFAS No. 123, as permitted by the Statement. In accordance with SFAS No. 123, the fair value of each option grant is estimated on the date of each grant using the Black-Scholes option pricing model. If compensation expense had been determined using the estimated fair value of options under SFAS No. 123, the pro forma effects would have been an increase of \$94,000 and \$285,000 for the 12-month period ended June 30, 2004 and 2003 respectively. DHI recorded deferred compensation expense of \$799,947 and \$731,815 for the 12-month periods ended June 30, 2004 and 2003, respectively.

DHI accounts for income taxes under the liability method in accordance with SFAS No. 109, *Accounting for Income Taxes*. Deferred income taxes are provided for the expected tax consequences of differences between the financial reporting and tax basis of assets and liabilities, which is primarily comprised of accounting for stock options and accounts receivable.

DHI has the following debt obligations at June 30, 2004 and 2003:

	2004	2003
State of Ohio Pioneer Loan— 4% installment note, payable monthly through 2008, collateralized by machinery and equipment	\$ 33,178	\$ 53,687
Buckeye Hills—Hocking Valley development loan— 4% installment note payable monthly through 2009, collateralized by machinery and equipment	62,856	89,508
Note payable to BioWhittaker— Payments begin March 2003 with 12% interest, payable in 36 monthly installments, unsecured	941,776	1,084,183
Installment note payable to Neogenex— 5% installment loan, payable in monthly installments through August 2003, unsecured		28,718
Other notes payable to Neogenex— Due in four installments beginning September 2003, unsecured		<u>133,440</u>
Total	<u>\$ 1,037,810</u>	<u>\$ 1,389,536</u>

The aggregate maturities and scheduled payments of debt for each of the next five years are as follows:

**Twelve Months
Ending June 30**

2005	\$ 483,094
2006	464,756
2007	45,125
2008	26,169
2009 and thereafter	<u>18,666</u>
Total debt	<u>\$ 1,037,810</u>

(l) Subsequent Event

On August 5, 2004, DHI amended its Articles of Incorporation and issued 1,030,342 newly created Class A Participating Convertible Preferred Shares (the “Class A Preferred Shares”) to Summit Partners for \$10,000,000 cash. In connection with and as a condition to consummating the issuance of the Class A Preferred Shares, the Foundation converted its outstanding preferred shares into common stock immediately prior to the issuance of the new shares. The Foundation received an additional 59,022 common shares upon conversion in accordance with the articles of incorporation in effect at that time. DHI used \$3,500,000 of the proceeds to immediately pay a special dividend to current outstanding shareholders of record, as of August 4, 2004, on a pro rata basis. The Foundation’s share of the dividend was \$2,482,288. These funds have been allocated to unrestricted and endowment accounts based on the sources of the funds used to purchase the shares.

DHI's Class A Preferred Shares accrue dividends at a rate of 5.2% per annum. Upon a liquidation or sale of the Company, the holders of the Class A Preferred Shares will be entitled to receive an amount in cash equal to the redeemable preference in the amount of \$3,500,000 plus accrued and unpaid dividends before any distribution or payments to common shareholders. In no event, shall the Class A Preferred Shares be entitled to be paid less than the original investment plus accrued and unpaid dividends.

20. THE OHIO UNIVERSITY OSTEOPATHIC MEDICAL CENTER, INC.

The Ohio University Osteopathic Medical Center, Inc. ("MCI"), a discretely presented component unit of Ohio University is a professional association formed under Chapter 1785 of the Ohio Revised Code for the purpose of organizing licensed physicians and surgeons, who are faculty members of the Ohio University College of Osteopathic Medicine, into a multi-specialty faculty group practice. The sole purpose for which this professional association is formed is to render medical care, consultation, diagnosis and treatment through physicians and surgeons licensed to practice medicine in the State of Ohio. MCI ceased to exist as an entity effective July 1, 2003. The accompanying financial statements present the last five months of the entity from February 1, 2003 through June 30, 2003. The successor organization, University Medical Associates has been evaluated and was determined to not meet the tests of GASB Statement No. 39 for component unit treatment.

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