THE UNIVERSITY
of NORTH CAROLINA
at CHAPEL HILL

A Constituent Institution of
the University of
North Carolina System
and a component unit of
the State of North Carolina

2003
Comprehensive Annual Financial Report

Chapel Hill, North Carolina • Fiscal Year Ended June 30, 2003

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Office of the Vice Chancellor
for Finance and Administration

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Introductory Section

Chapel Hill, North Carolina
Fiscal Year Ended June 30, 2003

THE UNIVERSITY *of* NORTH CAROLINA *at* CHAPEL HILL

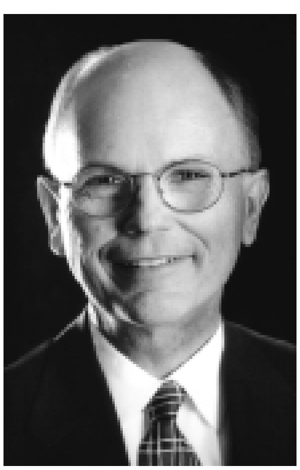
Message from the Chancellor

Our vision at the University of North Carolina at Chapel Hill is to become the leading public university in the United States. In pursuing such an ambitious goal, we are remaining true to our heritage as the nation's first public university. We want Carolina to be the best that it can be to for the people of North Carolina and beyond.

Consistent with our leadership role, Carolina has launched a groundbreaking initiative that is contributing to an ongoing nation-wide conversation about the rising cost of college and the need to keep higher education accessible to all. Starting next year, the Carolina Covenant will give children of low-income families the opportunity to attend the University debt-free. This is the first program of its kind at a public university in the United States.

A Successful Year

Among noteworthy developments over the past year are the completion of an academic plan that will guide our future investments; significant progress in a multi-year construction program that is bringing our campus master plan to life; the faculty's record-setting pace in attracting sponsored research funding; and the extraordinary generosity of our alumni, parents, and friends who are making gifts to the Carolina First campaign.



These examples underscore the positive momentum pushing Carolina forward as we strive to achieve our long-term vision. At the same time, we remain keenly focused on the pressing needs of North Carolina during a critical period of economic transformation and recovery. The University's future success will benefit all North Carolinians, and our pledge is to enhance the quality of life — through advances in education, health care, and economic development — for citizens in all 100 counties across the state.

Carolina's most recent successes included securing crucial support during the North Carolina General Assembly's budget deliberations in the summer of 2003. We enjoy a far greater level of support historically in North Carolina than in almost every other state. Governor Mike Easley and the General Assembly shielded higher education from the full impact of budget cuts to state government. We were thankful for those efforts as we compared our cuts with those handed out in other states.

Although state support remains essential to the University's future, our appropriations have declined as a total percentage of our operating budget as other fund sources have grown faster. We are generating new revenue streams to help meet pressing needs. For example, we rely more today on our faculty's ability to attract research funding. We are grateful for the enlightened philanthropy of our private donors, who have shown remarkable support for Carolina during these recent difficult economic times. Ultimately, their sustained support and the success of the Carolina First campaign will ensure the University's future excellence.

The Carolina Covenant: Connecting With Core Values

The successful launch of our Carolina Covenant program helped shed new light on national discussions about rising college costs and the impact on access to education for students of limited financial means. Two statistics help illustrate this issue. The national average student loan debt has nearly doubled to $17,000 in the last decade. At the same time, about one-fifth of America's college students must work more than 35 hours a week. More students are forgoing college, or dropping out, because of this debt burden. Too often, these are first-generation students, as well as students of color. It is a lose-lose scenario when bright young people feel forced to give up on a quality education because of limited family resources.

Against this backdrop, the time was right again for Carolina to lead American higher education policy, as we did two years ago by eliminating binding early-decision admissions. With the Carolina

Covenant, we are promising our most needy students that they will have the opportunity to graduate here without having to borrow and regardless of their family's income.

The covenant is for students who are admitted to Carolina, who qualify for federal student aid, and who come from a family with an income at or below 150 percent of the federal poverty level, indexed by family size. Using those criteria, a student from a family of four with an income of about $28,000 in 2002-2003 would qualify. Carolina will meet 100 percent of this student's financial need through a combination of federal, state, campus-based, privately funded grants and scholarships, as well as his or her participation in the federal work-study job program.

No other public university — and only Princeton and Harvard among the privates — has made a similar guarantee for access to higher education. The covenant begins with the fall 2004 entering class and will be phased in over four years for both North Carolina and out-of-state students.

We believe the covenant sends the right message about Carolina's core values and the traditional commitment of our campus to both access and excellence. The covenant embodies what we proclaim to be, "The University of the People." To paraphrase the late North Carolina Governor Terry Sanford, it says to people of limited means everywhere, "If you have the will, we have the way."

Academic Plan Completed

Being the best possible steward of the dollars that North Carolina's taxpayers and our private donors so generously provide requires careful strategic planning. We have finalized an academic plan that will guide decisions about critical investments in academic priorities over the next five years. The plan, developed through a campus task force, has received strong support from our Board of Trustees and university leaders. It is closely linked with our efforts to develop a rolling five-year financial plan.

The academic plan's six key priorities are: (1) provide the strongest possible academic experiences for undergraduate, graduate, and professional students; (2) further integrate interdisciplinary research, education, and public service; (3) improve faculty recruitment, retention, and development; (4) increase diversity among faculty, students, and staff; (5) enhance public engagement; and (6) extend Carolina's global presence, research, and teaching. I am confident that the plan, successfully executed, will produce its ultimate objective: to significantly strengthen Carolina's excellence consistent with our core values and future aspirations as one of America's leading universities.

Capital Construction Program Progresses

Critical to Carolina's future success is our capital construction program, among the most ambitious at any American university. Carolina continued carrying out the campus master plan and benefiting from the investment state taxpayers made through their approval of the Higher Education Bond Referendum of 2000. The referendum is providing $510 million for repairs, renovations, utilities, and new buildings. We are investing another $600-plus million from non-state sources, including private gifts and overhead receipts, for buildings essential to continued excellence.

Several new or renovated buildings came on line this year, offering modern teaching and research technology and meeting contemporary standards of comfort and safety. Two linchpin projects supporting our genomics research initiative opened: the Medical Biomolecular Research Building, which houses the Department of Genetics and the Genomic Science Center, and the Bioinformatics Building. The School of Pharmacy addition, Kerr Hall, also opened and 79-year-old Murphey Hall, home of the classics department, reopened following a complete renovation. The School of Public Health broke ground for an addition that will expand laboratory space and we began a major renovation of Memorial Hall, which helps anchor our plans for an arts common.

We broke ground for two buildings that are part of the largest construction project in our history — the Carolina Physical Science Complex. This complex will provide state-of-the-art teaching and research facilities for key science units in the College of Arts and Sciences, as well as a new Institute for Advanced Materials, Nanoscience and Technology. These faculty perform world-class research with potential for business development; yet they work in over-crowded, antiquated buildings. When completed in 2009 this complex will ensure that Carolina plays a vital role in scientific research and discovery.

Faculty Research Gains Again

North Carolina, as the home of strong public and private research universities, now ranks seventh among all states in funding from the National Institutes of Health. UNC-Chapel Hill accounts for a major portion of those research dollars. In fiscal 2002, Carolina ranked 13th in NIH funding among private and public universities and fifth overall among all publics. Carolina also is the top public university in the South and one of only five Southern universities - public or private - in the NIH's top 20.

Overall, the faculty set another university record by recording a 10 percent increase in research funding for 2003 to $537 million — up from $488 million in 2002. This is a remarkable achievement by our scientists and investigators. Part of this success can also be attributed to our practice of reinvesting into our research enterprise the reimbursements, or overhead receipts, that we receive from the federal government for the cost of conducting the research.

Faculty Support Top Carolina First Goal

To keep attracting the best and brightest students, Carolina must retain and recruit outstanding faculty. The top goal of the $1.8 billion Carolina First campaign is faculty support, and our donors and friends are responding. At this writing, we have exceeded the $1.1 billion mark in total gifts and pledges. The campaign has secured $165 million toward a total goal for faculty support of $300 million. Those funds have created 107 endowed professorships, which recognize excellence in teaching and research, toward our goal of 200. Thirty-five of these professorships are already fully funded, including 29 with matching state funds. We have appointed 23 faculty to professorships created during the campaign. Funds raised for other campaign goals, especially for research and buildings, contribute to faculty support.

Conclusion

In 2002-2003, Carolina made significant progress toward its goals for excellence. Although we absorbed some difficult state budget cuts, we benefited from a wise decision by our elected state leaders to protect education as much as possible. We sharpened our capacity for strategic planning, and faculty turned in another stellar performance in the research arena. Our friends are responding with impressive generosity to the needs we are articulating in the Carolina First campaign. We remain focused on the long term and are exceedingly optimistic about what the future holds for our University.

Sincerely,

James Moeser

Letter of Transmittal

THE UNIVERSITY of NORTH CAROLINA at CHAPEL HILL

OFFICE OF THE VICE CHANCELLOR
FOR FINANCE AND ADMINISTRATION

300 SOUTH BUILDING
CAMPUS BOX 1000
CHAPEL HILL, N.C. 27599-1000

T 919.962.3798

November 21, 2003

To Chancellor Moeser, Members of the Board of Trustees, and Friends of The University of North Carolina at Chapel Hill:

INTRODUCTION

This Comprehensive Annual Financial Report includes the financial statements for the year ended June 30, 2003, in addition to other information useful to those we serve and to whom we are accountable. Responsibility for the accuracy of the information and for the completeness and fairness of its presentation, including all disclosures, rests with the management of the University. We believe the information is accurate in all material respects and fairly presents the University's financial position, as well as revenues, expenses, and other changes in net assets. We believe our system of internal controls is sound and sufficient to disclose material deficiencies in controls to the auditors and the audit committee. The Comprehensive Annual Financial Report includes all disclosures necessary for the reader to gain a broad understanding of the University's financial position and results of operations for the year ended June 30, 2003. The report is organized into three sections.

The **Introductory Section** includes a message from the chancellor, the transmittal letter, a listing of the University's Board of Trustees, a list of executive and academic officers, and an organization chart. This section also features the University's major recent initiatives and progress. Overall, this section provides background about the organization and structure of the University, the scope of its operations, significant factors contributing to the current fiscal environment, and expected factors influencing the future.

The **Financial Section** presents management's discussion and analysis, basic financial statements, and a report of the Office of the State Auditor. Management's discussion and analysis provides an objective review of the University's financial activities. The basic financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board.

The **Statistical Section** contains selected financial, statistical, and demographic information. This information provides a broad overview of trends in the University's financial affairs. Also included is historical statistical information reproduced from the 2002 Comprehensive Annual Financial Report.

The accompanying financial statements present all funds belonging to the University and its component units. While the 16-campus University of North Carolina System's Board of Governors has ultimate responsibility, the chancellor, the University's Board of Trustees, and the Board of Trustees of the Endowment Fund have both delegated and statutory responsibilities for financial accountability of the University's funds. Although legally separate, The University of North Carolina at Chapel Hill Foundation Investment Fund, Inc. (Investment Fund), UNC Investment Fund, LLC (System Fund), UNC Management Company, Inc. (Management Company), The University of North Carolina at Chapel Hill Foundation, Inc. (UNC-CH Foundation), The Kenan-Flagler Business School Foundation (Business School Foundation), The School of Social Work Foundation, Inc. (Social Work Foundation), and U.N.C. Law Foundation, Inc. (Law Foundation), are reported as if they were part of the University based on Governmental Accounting Standards Board Statement 14, *The Financial Reporting Entity*.

The Investment Fund supports the University by operating an investment fund for charitable, non-profit foundations, associations, trusts, endowments, and funds that are organized and operated primarily to support the University. The System Fund was organized to allow the University, the University of North Carolina and its constituent institutions (UNC System), affiliated foundations, associations, trust, and endowments that support the University and the UNC System to pool their resources and invest collectively in investment opportunities identified, structured and arranged by the Management Company. The Investment Fund contributed and assigned all of its assets to the System Fund in exchange for membership interest in the System Fund. At year end, the Investment Fund membership interest was approximately 97% of the System Fund total membership interest.

The Management Company is organized and operated exclusively to support the educational mission of the University. The Management Company will also provide investment management services to the University, UNC System, and affiliated tax exempt organizations. The purpose of UNC-CH Foundation, Business School Foundation, Social Work Foundation and Law Foundation is to aid, support, and promote teaching, research, and service in the various educational, scientific, scholarly, professional, artistic, and creative endeavors of the University.

The financial statements of the Investment Fund, System Fund, Management Company, UNC-CH Foundation, Business School Foundation, Social Work Foundation, and UNC Law Foundation have been blended with those of the University. Other related foundations and similar non-profit corporations for which the University is not financially accountable are not part of the accompanying financial statements. The University of North Carolina at Chapel Hill is a constituent institution of the 16-campus University of North Carolina System, which is a component unit of the State of North Carolina and an integral part of the State's Comprehensive Annual Financial Report.

Economic Condition and Outlook

The best once can say about the North Carolina economy for the fiscal year ended June 30, 2003, is that the situation improved as the year progressed. Instead of dramatically outperforming the national average — as has been the case for most economic measures of North Carolina since 1929 — the state struggled to avoid losing ground.

Considerable evidence shows that situation continues to improve. On October 23, 2003, the Bureau of Economic Analysis (BEA) of the U.S. Department of Commerce reported that total personal income for North Carolina in the second quarter of 2003 was running at an annual level of $237.3 billion. That is an all-time record and is up 3.7 percent from the second quarter of 2002. The national increase was 2.8 percent. The increase of the second quarter over the first quarter of 2003 was 1.2 percent, the ninth-fastest growth rate among all 50 states.

According to the Bureau of Labor Statistics of the U.S. Department of Labor, total employment in North Carolina peaked in September 2000 at 4,026,837 people. The unemployment rate was 3.8 percent that month, but it had hit recent lows of 3.0 percent in February, April, and June of 1999. By June 2003, total employment in North Carolina was 3,872,187 people. That was a loss of 154,650 people employed. In September, total employment was back up to 3,913,297 people. Total non-farm payroll employment in North Carolina only grew by 0.3 percent in the year ended June 2003. Since manufacturing jobs declined by 4.5 percent in that period (to 613,000 jobs), other sectors had to grow more in order to eke out that tiny overall increase.

Per capita personal income in North Carolina in 2002 was $27,566. That ranked 34th among the states, a drop of two places from 2001. North Carolina was just ahead of Tennessee ($27,378) and just behind Maine ($27,804). Connecticut remained in first place at $42,829 and Mississippi was last at $22,370. The national average was $30,832, so North Carolina was only 89.4 percent of the national average.

2004, an election year, is quite likely to see the highest national growth rate of any year since 1984. If that occurs and if North Carolina can perform at least at the national average, the economic environment will improve dramatically next year. The state budget could see a healthy surplus and that should benefit the University. The last three years have been economically difficult ones in North Carolina, so better results will be welcomed by all.

Progress and Major Initiatives

Carolina's progress and major initiatives during fiscal year 2002-2003 reflected the University's vision of becoming the leading public university in the United States. Following this letter are highlights from among a few of the major campus-wide areas of focus during the year.

Financial Information

INTERNAL CONTROL STRUCTURE

The Finance and Administration Division of the University is responsible for establishing and maintaining an effective system of internal control. The objectives of an internal control structure are to provide management with reasonable, although not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with appropriate authorization and recorded properly in the financial records to permit the preparation of financial statements in accordance with generally accepted accounting principles. Organizational structure, policies, and procedures have been established to safeguard assets, ensure the reliability of accounting data, promote efficient operations, and ensure compliance with established governmental laws, regulations and policies, University policies, and other requirements of sponsors to whom the University is accountable.

As a recipient of federal financial awards, the University is responsible for ensuring compliance with all applicable laws and regulations. A combination of state and University policies and procedures, integrated with the University's system of internal controls, provides for this compliance. As an integral part of the State of North Carolina's Single Audit, the University is subject to an annual examination by the Office of the State Auditor of its federal financial assistance programs and federal cost-reimbursement contracts in accordance with U. S. Office of Management and Budget Circular A-133, *Audits of State and Local Governments, and Non-Profit Organizations*.

BUDGETARY CONTROLS

The University is responsible for controlling its budget and using the funds to fulfill its educational and other missions. It is also responsible for planning, developing, and controlling budgets and expenditures within authorized allocations in accordance with University, state, and federal policies and procedures. The University maintains budgetary controls to ensure compliance with provisions embodied in the annual appropriated budget approved by the North Carolina General Assembly. Project-length financial plans are adopted for capital projects.

After the budget has been approved by the chancellor and the Board of Governors, the University follows an established system of budgetary controls. Finance and Administration issues periodic interim budget statements to department heads to guide them in managing their budget allocations. Monthly financial reports are provided on each fund to individual managers responsible for the fund. Financial reports are also provided to the state. When actual conditions require changes to the budget, revisions are prepared, and these revisions are appropriately approved and communicated to those affected. Changes to the budget are approved at the university level and/or the state level as required. Based on the state's management flexibility legislation, the University has received delegated authority for designated budget changes. The University maintains an encumbrance accounting system as another method to ensure that imposed expenditure constraints are observed.

DEBT ADMINISTRATION

To ensure the appropriate mix of funding sources is utilized, the University established a debt policy, which is continuously used by management as a tool to evaluate the University's organizational and capital funding structure, the appropriate use of leverage, and internal lending mechanisms.

To fulfill its mission, the University will need to make capital investments, driving capital decisions that impact the University's credit. Appropriate financial leverage serves a useful role and should be considered a long-term component of the University's balance sheet. Just as investments represent an integral component of the University's assets, debt is viewed to be a continuing component of the University's liabilities. Debt, especially tax-exempt debt, provides a low-cost source of capital for the University to fund capital investments and achieve its mission and strategic objectives.

The debt strategies, combined with management judgment, provide the framework by which decisions will be made regarding the use and management of debt. The objectives of the debt policy are:

Identify projects eligible for debt financing. Using debt to fund mission critical projects will ensure that debt capacity is optimally used to fulfill Carolina's mission. Projects that relate to the core mission will be given priority for debt financing; projects with associated revenues will receive priority consideration as well.

Maintain Carolina's favorable access to capital. Management's determination of the timing of capital projects will not be compromised by the University's access to capital sources, including debt. Management will use and issue debt to ensure timely access to capital.

Limit risk of University debt portfolio. The University will manage debt on a portfolio basis. The University's continuing objective to achieve the lowest cost of capital will be balanced with the goal of limiting exposure to market shifts.

Manage the University's credit to maintain the highest acceptable credit. This practice will permit the University to continue to issue debt and finance capital projects at favorable interest rates while meeting strategic objectives. The University will limit its overall debt to a level that will maintain an acceptable credit with the bond rating agencies.

For Carolina to achieve these objectives, it will adopt strategies and procedures relating to both the external and the internal management of debt and interest. The strategies include the following:

Mission-Based Capital Planning. Provide framework with a link to mission to evaluate and prioritize debt-eligible projects.

Core Ratios. Adopt a set of core ratios to guide capital planning and ensure central oversight of University-wide leverage levels.

Financial Instruments. Provide management with appropriate debt vehicles based on borrowing needs.

External and Internal Debt Repayment. Delink external and internal debt repayment, including adoption of internal lending policies.

The University had $373.5 million of revenue bonds outstanding at June 30, 2003. The bonds were issued to finance the construction and/or renovation of many facilities including essential new research buildings, major new cultural facilities that will benefit the local community and state, undergraduate residence halls, student family housing, and parking facilities. The bonds are payable both as to principal and interest from the general revenues of the University and net revenues generated by the operations of those facilities.

CASH MANAGEMENT

The cash management plan of the University addresses control of receipts, management of disbursements and investment of funds to maximize earnings on the investment of cash. State law requires that state-appropriated funds be deposited with the State Treasurer with investment earnings accruing to the state. Other resources, such as gifts, contract and grant awards, auxiliary revenues, and student activity fees are not appropriated by the state. Some of these funds must be deposited with the State Treasurer with investment earnings accruing to the University. Endowment, debt service, and other designated funds are invested by the University in accordance with its investment policies.

The University administers a short-term investment pool for funds not required to be on deposit with the State Treasurer. The investment pool is administered in conjunction with cash receipts and disbursing requirements to minimize idle cash and to generate current income without loss of capital at a rate of return comparable to the State Treasurer. The University uses the state's cash management control system to improve cash flow by electronically recording cash receipts and disbursements for funds deposited with the State Treasurer.

RISK MANAGEMENT

The University is exposed to various risks of loss related to property and employees. These risks are addressed in several ways, including participation in various state-administered risk pools, purchase of commercial insurance, and self-retention of certain risks. Refer to Note 14 of the Notes to the Financial Statements for more detailed information concerning the University's risk management program.

OTHER INFORMATION

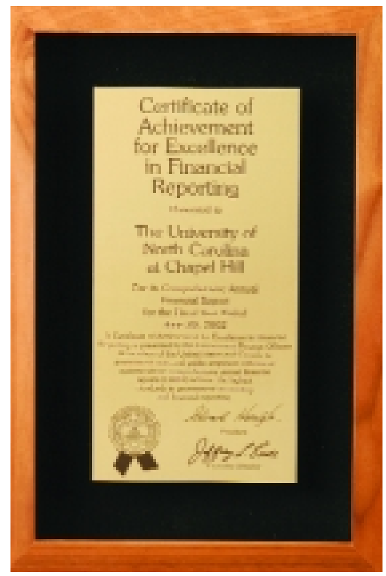
AUDITS

State law, federal guidelines, and certain bond covenants require that the University's accounting and financial records be audited by the Office of the State Auditor each year. Additionally, the University's Internal Auditors perform fiscal, compliance and performance audits. The reports resulting from these audits are shared with University management.

The audit of the University's federal financial assistance programs is performed by the Office of the State Auditor in conjunction with the statewide Single Audit. The accounting and financial records of The University of North Carolina at Chapel Hill Foundation Investment Fund, Inc., The University of North Carolina at Chapel Hill Foundation, Inc., UNC Investment Fund, LLC, UNC Management Company, Inc., The Kenan-Flagler Business School Foundation, The School of Social Work Foundation, Inc., U.N.C. Law Foundation, Inc., WUNC Radio, and the Athletic Department are each audited by a public accounting firm in addition to the State Auditor review. All of the audit reports are available for public inspection.

CERTIFICATE OF ACHIEVEMENT

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to The University of North Carolina at Chapel Hill for its comprehensive annual financial report for the fiscal year ended June 30, 2002. This was the eighth consecutive year that the University has been honored with this prestigious award. In order to be awarded a Certificate of Achievement a government unit must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.



A Certificate of Achievement is valid for a period of one year only. We believe our current comprehensive annual financial report continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

ACKNOWLEDGMENTS

Preparation of this Comprehensive Annual Financial Report in a timely manner would not have been possible without the coordinated efforts of the University community, with special assistance from the Chancellor's Office, the Provost's Office, Academic Affairs, Health Affairs, Research and Economic Development, Student Affairs, Information Technology Services, University Advancement, University Relations, Institutional Research, the Office of Scholarships and Student Aid, the Department of Athletics, and Dr. James F. Smith, Adjunct Professor of Business Administration in the Kenan-Flagler Business School. In addition, the Office of the State Auditor provided invaluable assistance.

Nancy D. Suttenfield
Vice Chancellor for Finance and Administration

Progress and Major Initiatives
Fiscal 2002-2003

Carolina's progress and major initiatives during fiscal 2002-2003 reflected the University's vision of becoming the leading public university in the United States. Following are a sampling of key recent highlights that help illustrate such progress across many areas of the University:

LAUNCHING THE CAROLINA COVENANT

Carolina took a major stand on a key national higher education issue with the Carolina Covenant, a groundbreaking initiative to give the children of low-income families an opportunity to attend the University without borrowing money.

Starting in fall 2004, the Carolina Covenant will enable qualified low-income students to come to Carolina and graduate debt-free if they work on campus 10 to 12 hours weekly in a federal work-study job throughout their four years in Chapel Hill, instead of borrowing. The University will meet the rest of students' needs through a combination of federal, state, university, and private grants and scholarships.

This is the first program of its kind to be launched by a public university in the United States. Several major public campuses, including the University of Virginia, are exploring the possibility of creating similar programs. Reaction in North Carolina and across the nation has been overwhelmingly positive.

Carolina's initiative comes at time when the cost of college is rising steadily for low-income families. Nationally, the average student loan debt has nearly doubled to $17,000 over the past decade. About one-fifth of the full-time students work 35 or more hours a week. As a result, many low-income youth abandon plans for college — or drop out — because the burden of that debt and workload is too much. The patterns are even stronger among minority students. Research also shows that low-income families need more information — and greater predictability — about the availability of financial aid.

The Carolina Covenant responds to such concerns. The University already meets 100 percent of the documented financial need of all students who apply for aid on time, but about a third of that need is being met through loans. To fund the Carolina Covenant, the University will make modest reallocations of existing funds in the Office of Scholarships and Student Aid and pledge growing private gifts dedicated to low-income students.

Eligible students must be at or below 150 percent of the federal poverty level. Under current federal poverty levels, a family of four with an annual income of about $28,000 would qualify. For a single parent with one child, the eligible income would be about $18,000.

The state of the economy and the rising number of families living in poverty demonstrate the need for the Carolina Covenant. Since one in four North Carolina children now live in poverty, the need for an accessibility initiative like the Carolina Covenant will remain strong. According to the North Carolina Children's Index of 2002, more than one-third of North Carolina's families made less than $28,000 a year in 1999, the last year data were available.

In fall 2003, 281 of Carolina's freshmen, or 8 percent of the freshman class, came from low-income families. Most of those — 89 percent — were from North Carolina. More than half were minorities. Federal and state financial aid covered about 60 percent of the college costs for those students.

Photo by Dan Sears

Shirley Ort, associate provost and director of the Office of Scholarships and Student Aid, has long been highly regarded on the national higher education scene and played a key role in developing the proposal for the Carolina Covenant.

The Carolina Covenant will supplement the University's long-standing program of providing generous financial assistance to needy students and need-blind admissions — the practice of granting admission to qualified applicants without consideration of their family's ability to pay.

As the first public university in America, Carolina has always been committed to access. With the Carolina Covenant, the University is strengthening its commitment to ensure that families from all income levels can afford a Carolina education.

The Carolina Covenant is the second major national initiative the University has recently launched to benefit students. Starting with freshmen applying for admission in fall 2003, Carolina became the nation's first major American public university to eliminate its binding early decision admissions plan.

Earning National Rankings and Praise

Several national publications and reports published rankings in 2002 and 2003 that list Carolina prominently in categories ranging from academic quality to affordability to diversity to international presence. Some coverage appearing in these high-profile sources continued to cite Chancellor James Moeser's decision to end early decision admissions, making Carolina the first major highly selective public university to do so.

> "College should be possible for everyone who can make the grade, regardless of family income. A covenant is a promise. With the Carolina Covenant, we are telling students that college is affordable, no matter how much money your family makes."
> *Chancellor James Moeser*

The magazines, journals, guidebooks, newspapers and other sources included *U.S. News & World Report; Kiplinger's Personal Finance; The Wall Street Journal; Business Week; Forbes; "The Top American Research Universities,"* published by the Lombardi Program on Measuring University Performance at the University of Florida; *Black Enterprise; The Journal of Blacks in Higher Education; "The Fiske Guide to Colleges;" Technology Review, MIT's Magazine of Innovation; and "Open Doors 2002"* published by the Institute of International Education.

Highlights included the following:

Carolina ranked as the nation's fifth best public university in *U.S. News & World Report* magazine's annual *"Best Colleges"* guidebook. Carolina is among five schools — along with Berkeley, Virginia, Michigan and UCLA — that have traded or tied for the top slots in the U.S. News public campus rankings of undergraduate programs for the past several years. Such rankings are just one indication of a university's quality. Carolina has been developing its own measures of excellence, including comparisons with these four public peers.

U.S. News & World Report included Carolina in a category called "programs to look for" — highlighting outstanding examples of academic programs that lead to student success. Carolina was listed among 33 public and private campuses for their first-year experiences programs, which include first-year seminars and other programs bringing small groups of students together with faculty and staff on a regular basis. Carolina was one of 17 public campuses selected.

Carolina was listed fifth among public universities appearing in *"The Top American Research Universities,"* produced by TheCenter, part of the Lombardi Program on Measuring University Performance, at the University of Florida. These rankings draw from data covering areas such as research, private support, faculty, and advanced training.

For the fourth consecutive time, *Kiplinger's Personal Finance* magazine listed Carolina first among the nation's 100 best public colleges combining great academics and affordable tuitions. These rankings are based on cost, quality, and financial aid practices.

The *"2003 Fiske Guide to Colleges"* edited by former *New York Times* Education Editor Ted Fiske, listed Carolina among 21 of the very best public universities in the United States and Canada that are a "best buy university" based on the quality of the academic offerings in relation to the cost of attendance.

The Journal of Blacks in Higher Education ranked Carolina first among public campuses and sixth overall in a ranking assessing the success of America's leading universities in integrating African-Americans. The evaluation rated the nation's 26 highest academically ranked universities in 13 categories or factors of racial diversity. For the fourth consecutive year, Carolina topped *The Journal's* list of the nation's top campuses for the highest percentage of black freshmen — 12.5 percent in fall 2002. That was up from 11.6 percent in 2001.

Carolina ranked sixth among all U.S. research universities for the total number of students receiving academic credit for studying abroad during 2000-2001. The ranking comes from *"Open Doors 2002,"* an annual report published by the Institute of International Education. When measuring the percentage of students going abroad, the institute ranked Carolina third among major public research universities and 13th among all major research universities. The Kenan-Flagler Business School appeared in several lists of the nation's best MBA programs. *Forbes* magazine ranked Kenan-Flagler eighth for the return on investment to its graduates. *The Wall Street Journal* listed Kenan-Flagler 10th using results from its survey of corporate recruiters. *U.S. News & World Report* also ranked Kenan-Flagler the fifth-best undergraduate business program. Carolina ranked 12th in a scorecard assessing the licensing and patenting prowess of leading research universities compiled by *Technology Review, MIT's magazine of Innovation*. In the University Research Scorecard 2002, analysts ranked universities by their technological strength — a calculation based on the number of U.S. patents multiplied by the "current impact index" (a measure of how often patents over five years are cited in the current year, relative to all U.S. patents).

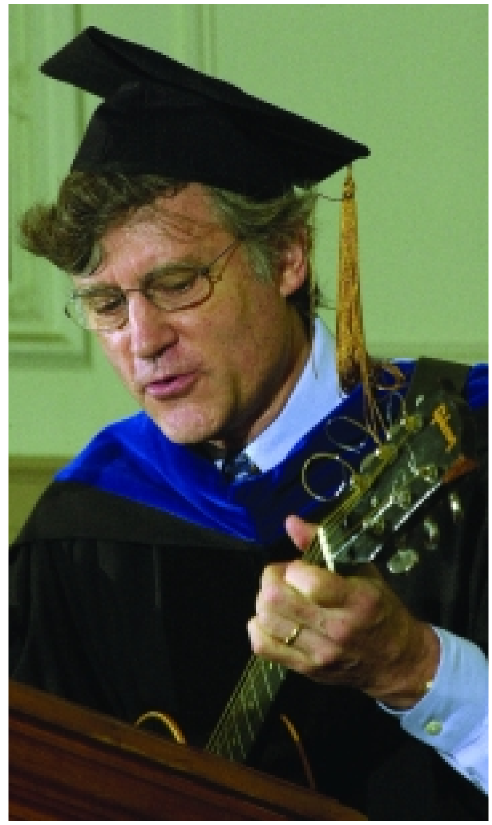


Photo by Dan Sears

Bill Ferris, Joel Williamson Distinguished Professor of History, shown here performing at University Day 2002, is a prime example of how the Carolina First campaign helps successfully recruit leading national teachers and scholars to Chapel Hill. Ferris is former chairman of the National Endowment for the Humanities.

Sustaining Success of Carolina First

The Carolina First Campaign is a comprehensive, multi-year private fund-raising campaign — the largest in the University's history — to support the vision of Carolina becoming the nation's leading public university. The ultimate beneficiaries of reaching that goal will be the people of North Carolina, whom Carolina is dedicated to serve.

The University exceeded the $1 billion mark for the campaign during fiscal 2002-2003. In all, the campaign has raised more than $1.1 billion toward its $1.8 billion goal, the second largest ever announced by a U.S. public university. During the quiet phase of the campaign, which began July 1, 1999, the University raised $866 million. The public kick-off came October 11, 2002.

With 55 percent of the campaign over, the University has raised 62 percent of its total goal. The campaign is scheduled to conclude in 2007. In January and February of 2003 alone, Carolina raised more than any of the other 21 U.S. institutions involved in billion-dollar campaigns, with $23 million in January and $34 million in February.

In recognition of the University's critical need to recruit and retain outstanding faculty, the chancellor and the campaign leadership are focusing additional time and energy on faculty support. Already, with the exception of a broad "strategic initiatives" category, faculty support has been the campaign's most successful category to date. The campaign has secured nearly $165 million (55 percent) toward a total goal for faculty support of $300 million. Those funds have created 107 endowed professorships, which recognize excellence in teaching and research, toward a goal of 200. Thirty-five of these professorships are already fully funded — 29 through a state matching program and six without that match. The University has appointed 23 faculty to professorships created during the campaign.

Of the $165 million raised for faculty support, $76 million is expendable and being put to work immediately for the benefit of the faculty. Funds raised for other campaign goals — especially for research and buildings — also support the faculty.

Other campaign priorities include student support, with a goal of raising $300 million and creating 1,000 new undergraduate scholarships and graduate fellowships. The campaign has raised reached half of its total goal in this category.

The University also made excellent progress toward the campaign's other priorities, which include providing the means to pursue strategic initiatives to enrich the academic experience; conduct research that improves the health and the economic, social, and cultural well being of citizens; redouble the commitment to public service and engagement; and implement a campus master plan to create 21st Century teaching and learning environments.

Total giving in fiscal 2003 was $163.5 million, and the University received the 2003 Council for the Advancement and Support of Education/Wealth ID Award for superior fund-raising performance for the seventh time in 10 years. The award recognized results achieved in fiscal 2002. Only Harvard University has won as many CASE awards in the same decade-long period. Carolina exceeded all other public research/doctoral universities in this category.

Major gifts and pledges announced in fiscal 2002-2003 included:

A $20 million commitment to the School of Pharmacy by Fred Eshelman, a 1972 graduate from Wilmington, N.C. His gift will be used for scholarships, fellowships, faculty development, and the creation of innovative community practice sites. Eshelman's gift was the largest ever to a U.S. pharmacy school and the third largest single gift from an individual in the University's history.

A $5 million gift from Vaughn and Nancy Bryson established a clinical genetics center to explore the relationship between genetics and disease. The gift helps extend the reach of the campus-wide genome sciences initiative.

A $4 million gift from Gatorade created a partnership with the School of Public Health and the Department of Athletics to launch "Get Kids in Action," a four-year program to engage physicians, communities, and families in reducing and preventing childhood obesity.

To advance the study of the use and effects of drugs, GlaxoSmithKline committed $3 million to create the Center for Excellence in Pharmacoepidemiology in the School of Public Health.

Will and Donna Biles announced a $2.5 million gift to the School of Medicine for the study of Sudden Infant Death Syndrome (SIDS). The gift was made on Biles' behalf by an anonymous trust in memory of their daughter, Samantha, a 1997 victim of SIDS.

The BB&T Charitable Foundation awarded $1 million to the Department of Philosophy to inspire discussion and study that merge ancient philosophical theories with modern business principles.

The Elizabeth "Pepper" Dowd Carolina Scholars Fund, established with a $1 million gift from the Dowd Foundation, created six new academic scholarships in the Carolina Scholars Program. The fund honors Dowd's service to Carolina over the years.

A gift from Van and Kay Weatherspoon enabled the University library to purchase one of the world's largest collections of rare Russian books, serials, manuscripts, and photographs from Paris booksellers Andre and Svetlana Savine.

Photo by Dan Sears

Chancellor James Moeser applauds as Fred Eshelman displays a plaque proclaiming "Fred Eshelman Day" at Carolina. Eshelman's $20 million commitment to the School of Pharmacy was the largest ever to a U.S. pharmacy school and the third largest by an individual in University history.

Carolina First is the private complement to the generous public support that North Carolina's voters and legislators have shown for the University. In 2000, North Carolina voters approved $510 million in bond funding for repair, renovations, utilities, infrastructure, and new buildings at Carolina. Carolina First is helping leverage that bond money by making good on the chancellor's pledge to state citizens to triple it through private gifts. In all, the University plans to invest another $600 million in non-state funds for additional buildings essential to continued excellence. The current capital construction program is valued at about $1.2 billion.

Since its beginning, Carolina has benefited from a public-private partnership. With continued support from both the state and from private sources, the University will return to its partners, the people, great teaching, path-breaking research, and inspired public service.

Bringing the Master Plan to Life

The campus master plan will guide the next several decades of an aggressive renovation and building program at Carolina. The plan shows where and how to place future buildings. It identifies transportation and utility corridors and suggests ways to protect open space and meet important environmental standards including no net increase in storm water runoff. The plan also recognizes the importance of enhancing the intellectual climate and the valuable University culture of collegiality and collaboration.

Fiscal 2002-2003 marked the second year in which the University began implementing the master plan. The Board of Trustees approved the plan in 2001 after three years of work involving the University, consultants, and Town of Chapel Hill representatives. Later joint town-gown discussions helped create a new zoning ordinance and category as well as the rezoning of the main campus. A development plan approved by the town in 2001 included details for an initial phase of new construction on proposed development and strategies to mitigate community impacts in areas such as traffic, storm water, and noise.

Overall highlights of the current $1.2 billion capital construction program now being guided by the master plan include the following achievements:

- Seventeen projects, representing 18 percent of the total capital program, have been completed on time and within their budgets. Total value of these projects is $220 million.
- Twenty-four projects, or 33 percent of the total, are under construction. All are within budget and 21 are either ahead or on schedule. These projects are worth approximately $400 million.
- Fifty-three projects, or 48 percent of the program, are currently in the design phase. Those projects will cost an estimated $580 million.
- All but one of the 48 projects supported by $510 million in funds from the Higher Education Bond Referendum of 2000 have progressed to at least the design phase of construction after only three years. The remaining project, Steele Building renovation, is scheduled to be under design soon.

Progress on these specific projects was particularly noteworthy:

- Completing two major new research buildings that are linchpins in Carolina's genome sciences research initiative: the Medical Biomolecular Research Building, which houses the Department of Genetics and the Genomic Science Center, and the Bioinformatics Building.
- Completing a new addition, Kerr Hall, to the School of Pharmacy, as well as a complete classroom building renovation to 79-year-old Murphey Hall, home of the highly regarded classics department.
- Breaking ground for a major addition to the School of Public Health that will expand much-needed laboratory space for researchers.
- Starting a major renovation of Memorial Hall, a key component of a long-range plan for an arts common. Renovating Memorial is the first step in reinvigorating the University as a venue for the performing and visual arts.
- Bringing the first phase of the Carolina Physical Science Complex completely under contract and breaking ground for its first two buildings. This public-private partnership represents the largest construction project in the University's history. It received the single largest allocation in the UNC system's portion of the statewide Higher Education Bond Referendum. When completed, the project will enhance longtime interdisciplinary strengths in the sciences, including emerging fields such as nanotechnology.

Accomplishments directly related to the campus master plan included:

- Dramatic success resulting from the work of the Historically Underutilized Business Resource Center, which aims to increase participation of minority-owned businesses in the University's building program. Carolina accounts for nearly half of the total African-American participation in the 16-campus UNC System's bond referendum construction program.
- Designation as a 2003 Best Workplace for Commuters by the Environmental Protection Agency and the U.S. Department of Transportation. The honor recognized efforts to implement a transportation philosophy to support the master plan. In fall 2002, the University launched a commuter alternatives program, which provides

Photo by Dan Sears

Medical School Dean Jeff Houpt, front left, watches as Trustee Tim Burnett, center, and Chancellor James Moeser, right, cut the ribbon to dedicate the Medical Biomolecular Research Building. The new facility is helping anchor a campus-wide genome sciences initiative.

Photos by Dan Sears

Murphey Hall, home of the classics department, was among the first classroom buildings completely renovated as part of the historic Higher Education Bond Referendum approved by North Carolina voters in 2000. These before and after views of a major lecture hall illustrate the transformation.

incentives to commuters to use transit, park and ride, bike or walk. The goal was 750 participants; the University exceeded that mark by 250 percent.

Recognition with a 2003 Sustainability Award for leadership in sustainable development from Save Our State. The non-profit organization cited the University for using cutting-edge sustainable development practices from the master plan including replacing asphalt with green space, using green building strategies, promoting fare-free transit, and running a recycling program that saved $400,000 in 2002.

Completing the Academic Plan

The University marked a milestone in its strategic planning efforts with the completion of an academic plan. The plan, developed through a campus task force, will guide the University's future decisions about investments in the academic enterprise over the next five years. It is tied with parallel efforts to develop a rolling five-year financial plan that will make possible execution of the academic plan as well as other non-academic strategic goals.

The academic plan's six key priorities are:

Provide the strongest possible academic experiences for undergraduate, graduate, and professional students.

Further integrate interdisciplinary research, education, and public service.

Improve faculty recruitment, retention, and development.

Increase diversity among faculty, students, and staff.

Enhance public engagement.

Extend Carolina's global presence, research, and teaching.

The plan is dynamic and will be reviewed and revised as new opportunities and challenges emerge.

Revising the Undergraduate Curriculum

The Faculty Council voted to approve recommendations resulting from the first comprehensive undergraduate curriculum review since 1980. To better prepare undergraduates for the interconnected world in which they live, the University will be asking them to learn much more about the history, culture, and economies of nations outside the United States.

Specific changes include adding a social sciences course, stipulating that a required philosophy course must deal with moral reasoning, changing a cultural diversity requirement to comprise several categories of work for students including experiential education, internships, field research, study abroad, U.S. diversity, world history and culture, and study of a period before 1750, among others. The new requirements take effect in the fall of 2006.

Continue Growth in Research Funding

Carolina contributes significantly to the North Carolina economy with the sponsored research grants awarded to faculty by the federal government

Photo by Dan Sears

A major renovation continues to take shape at Memorial Hall, where a public-private partnership is refurbishing a campus landmark that will anchor plans for a new arts common.

Photo by Dan Sears

Morehead Scholar Karine Dubè of Canada was chosen in 2002 for a Rhodes Scholarship, becoming the 36th winner from Carolina selected since 1902. Carolina ranks second among U.S. public universities in numbers of Rhodes Scholars produced.

and other sources. The faculty recorded a remarkable 10 percent increase in sponsored research funding for 2003 to $537 million — up from $488 million in 2002.

Such funding supports research vital to the public. For example, Carolina will contribute world-class faculty expertise in emerging and infectious diseases as well as immunology to a new $45-million biodefense initiative. The Southeast Regional Centers of Excellence for Biodefense and Emerging Infectious Disease will develop vaccines, drugs and diagnostic tests against emerging infections and organisms such as Severe Acute Respiratory Syndrome and smallpox. Carolina is among six universities selected for the federally funded research consortium.

The University again recorded research funding gains from a key source: the National Institutes of Health. Carolina ranked 13th overall for total funding awarded by the NIH in fiscal 2002 — a 12 percent increase. That made Carolina the top public university in the South and one of only five Southern universities, public or private, cited in the NIH's top 20. NIH, part of the U.S. Department of Health and Human Services, is the principal biomedical research arm of the federal government. NIH research institutes are fighting diseases including AIDS, alcoholism, arthritis, cancer, diabetes and stroke, as well as tackling health topics related to aging, women and children, drug abuse, the environment and rapidly emerging multidisciplinary fields such as genomics and proteomics.

Carolina placed 17th in the National Science Foundation's most recent report on federal academic science and engineering obligations for fiscal 2001 — advancing three spots from the fiscal 2000 funding totals. Overall, the University ranked as the top public university in the South and one of only two North Carolina campuses featured in the top 20 for fiscal 2001, the latest year of funding in the NSF's report on total federal academic science and engineering obligations.

The University ranked third in the NSF's funding for social sciences research during fiscal 2001, the highest level achieved by Carolina in the various science and engineering fields included in the NSF's research and development expenditures. About half of the University's total federal social science funding was in the area of sociology, including research projects addressing aging, adolescent achievement and problem behaviors, and rural health, among others. The department of sociology is the leading department in the nation for such NSF funding.

Positive growth in research funding corresponds with a decision made in mid-1998 by the North Carolina General Assembly to permit the University to retain all overhead receipts generated by research.

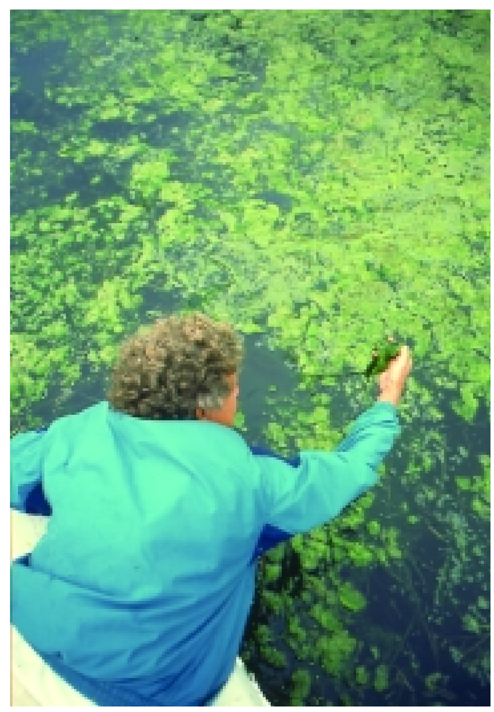
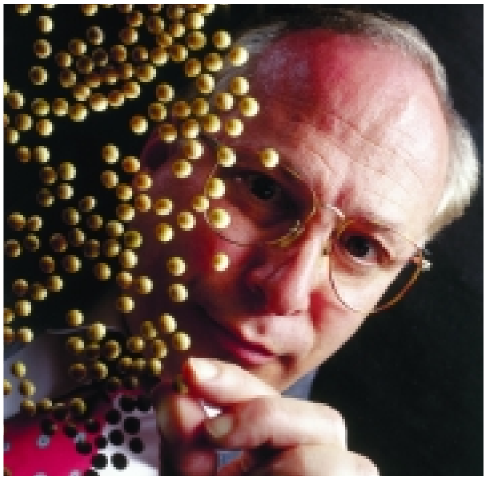


Photo by Dan Sears

Hans Paerl, William R. Kenan professor, documenting the long-term impact of Hurricane Floyd on the water quality of the Pamlico Sound in North Carolina. The sound is the nation's largest lagoonal estuary. Paerl is based at the University's Institute of Marine Sciences. Since the 1940s, institute scientists have served North Carolina by addressing important questions related to the nature, use, development, protection and enhancement of coastal marine resources.



Steven Zeisel, professor of nutrition and pediatrics, studies the safety and effectiveness of using nutritional supplements to treat and prevent disease. He is internationally known for his work on the nutrient choline and served on the National Academy of Sciences panel that named the vitamin-B-like substance an essential nutrient for good health. He chairs the department of nutrition, based in the schools of public health and medicine.

NURTURE TECHNOLOGY-TRANSFER EFFORTS AND SPIN-OFF COMPANIES

Among the University's goals in the research arena are to transfer new technologies into the consumer marketplace, resulting in increased economic value for North Carolinians as well as income for inventors and the University.

Key accomplishments included the following:

- Faculty filed 86 inventions with the Office of Technology Development.
- 83 patent applications were filed, and 34 new U.S. patents were issued to the University. That brought the total of U.S. and foreign patents held by the University to 861.
- 53 inventions were licensed.
- Licensing income to the University totaled $1.08 million.

Such work also has helped make possible the discoveries and innovations to create 25 UNC spin-off companies now employing state residents in the Triangle, Triad, and in eastern North Carolina.

Examples of commercialization include therapeutic agents for Parkinson's Disease, technologies for drug delivery to treat cancer, contrast media for medical imaging, industrial applications for carbon nanotubes, and gene therapy treatment for diseases like muscular dystrophy.

Two spin-offs achieved noteworthy distinctions in 2003. Oriel Therapeutics Inc. and Inspire Pharmaceuticals. Oriel received the 2003 Spin-Off of the Year and 2003 Capital Connection Company of the Year from the Council for Entrepreneurial Development. Oriel produces drug delivery systems, including a dry-powder inhaler, for respiratory and pulmonary diseases. Inspire was recognized in The Scientist as "number 1 among businesses with less than 500 employees as the best place to work for scientists in industry." Inspire discovers new drugs to treat dry eye, respiratory disorders, and cystic fibrosis. NASDAQ also invited Inspire officials to ring the bell to open the trading session in New York City. Inspire was the first North Carolina biotechnology company invited to have that honor.

In addition, Hemocellular Therapeutics, expected to produce the first platelet-based therapeutic available to doctors for the immediate treatment of active bleeding, established an exclusive licensing agreement with Carolina to advance a decade of cutting-edge research at UNC-Chapel Hill and at East Carolina University.

ADVANCE PLANNING FOR CAROLINA NORTH

Vice Chancellor for Research and Economic Development Tony Waldrop continued guiding planning for the potential mixed-use development of Carolina North, a 900-plus acre tract of University-owned property one mile north of the main campus. That property, previously called the Horace Williams tract, was part of a bequest by an esteemed Carolina philosopher years ago.

Waldrop's team developed a draft conceptual plan for development with input from University advisory groups that included campus and community representatives. The draft plan described the University's 50-year to 70-year vision for Carolina North. Potential benefits Carolina North will bring include a vibrant new setting for living and learning, for business innovation and economic development, for cultural exchange, for service, and for engaging citizens of all ages in the life of the University. The draft conceptual plan is currently under review.

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Tony G. Waldrop
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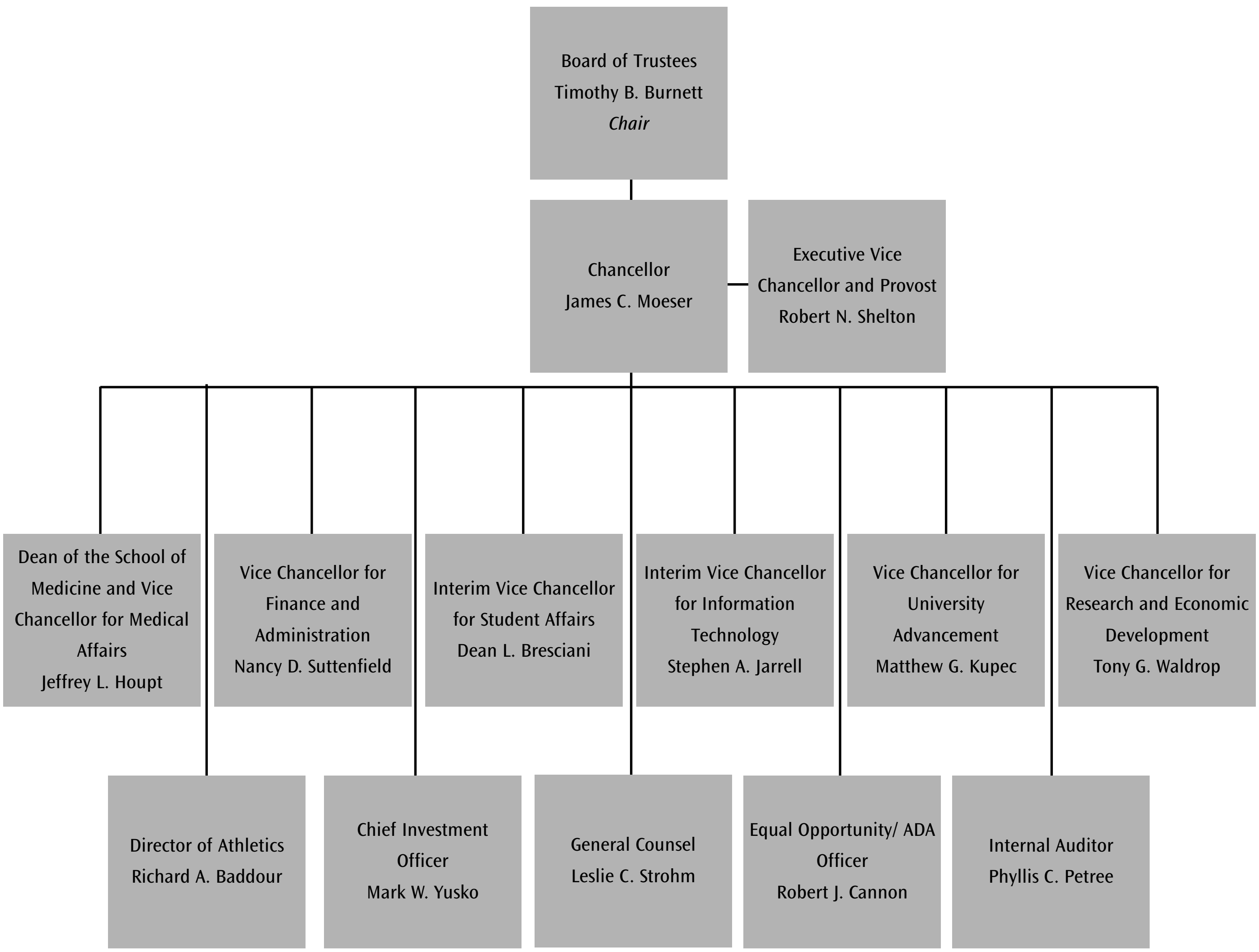
and Economic Development

Organization Chart

The University of North Carolina at Chapel Hill



Financial Section

Chapel Hill, North Carolina
Fiscal Year Ended June 30, 2003

THE UNIVERSITY *of* NORTH CAROLINA *at* CHAPEL HILL

STATE OF NORTH CAROLINA
Office of the State Auditor

Ralph Campbell, Jr.
State Auditor

2 S. Salisbury Street
20601 Mail Service Center
Raleigh, NC 27699-0601
Telephone: (919) 807-7500
Fax: (919) 807-7647
Internet http://www.osa.state.nc.us

INDEPENDENT AUDITOR'S REPORT

Board of Trustees
The University of North Carolina at Chapel Hill
Chapel Hill, North Carolina

We have audited the accompanying basic financial statements of The University of North Carolina at Chapel Hill, a constituent institution of the sixteen-campus University of North Carolina System, which is a component unit of the State of North Carolina, as of and for the year ended June 30, 2003, as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with 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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The University of North Carolina at Chapel Hill as of June 30, 2003, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 17 to the financial statements, the University implemented Governmental Accounting Standards Board Technical Bulletin No. 2003-1, *Disclosure Requirements for Derivatives Not Reported at Fair Value on the Statement of Net Assets,* during the year ended June 30, 2003.

INDEPENDENT AUDITOR'S REPORT (CONCLUDED)

In accordance with *Government Auditing Standards*, we have also issued our report dated November 21, 2003 on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit. The report on compliance and internal control will be issued under separate cover in the Financial Statement Audit Report of The University of North Carolina at Chapel Hill published by this Office.

The Management's Discussion and Analysis (MD&A), as listed in the table of contents, is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

The introductory and statistical sections, identified in the table of contents, were not audited by us, and accordingly, we do not express an opinion thereon.

Ralph Campbell, Jr.

Ralph Campbell, Jr.
State Auditor

November 21, 2003

Management's Discussion and Analysis (unaudited)

INTRODUCTION

This discussion and analysis provides an introduction and overview of the financial position and activities of The University of North Carolina at Chapel Hill (the University) for the fiscal year ended June 30, 2003, with comparative information for the fiscal year ended June 30, 2002. Certain prior year amounts have been reclassified to conform to current year presentations. Management has prepared the discussion and analysis to be read in conjunction with the financial statements and accompanying note disclosures.

The University is a constituent institution of the 16-campus University of North Carolina System (UNC System), a component unit of the State of North Carolina and an integral part of the State's *Comprehensive Annual Financial Report*. The University of North Carolina at Chapel Hill has been built by the people of the state and has existed for more than two centuries as the nation's first state university. Through its excellent undergraduate, graduate, and professional programs it has provided higher education to generations of students, many of whom have become leaders of the state and the nation.

FINANCIAL HIGHLIGHTS

The University's financial position remained strong at June 30, 2003 with total assets of $3.1 billion. Net assets, which represent the residual interest in the University's assets after deducting liabilities, were $2 billion at June 30, 2003. Overall, the University's net assets increased by $60.8 million in fiscal year 2002-2003 when private gifts, grants and endowment additions are included. Changes in net assets and total assets are summarized below:

	2003	2002	% Change
Net assets – July 1	$1,964,418,046	$1,919,024,460	2.4
Increase in net assets	60,767,554	45,393,586	33.9
Net assets – June 30	2,025,185,600	1,964,418,046	3.1
Total liabilities	1,112,017,605	925,114,193	20.2
Total assets	$3,137,203,205	$2,889,532,239	8.6

The increase in net assets was achieved despite a slight decrease in state appropriations due to statewide budget reductions and revenue shortfalls. State appropriations continue to provide essential resources in support of the University's mission. Capital funding resulting from the North Carolina higher education bond referendum, controlled enrollment growth, a robust research program, the continuing success of the Carolina First fund-raising campaign, and the sound investment management program were among the other factors resulting in positive financial results for the fiscal year.

USING THE FINANCIAL STATEMENTS

The University's Comprehensive Annual Financial Report includes the following three financial statements.

Statement of Net Assets
Statement of Revenues, Expenses, and Changes in Net Assets
Statement of Cash Flows

These financial statements have been prepared in accordance with Governmental Accounting Standards Board (GASB) statements. The GASB sets standards for external financial reporting for public colleges and universities and requires that financial statements be presented on a consolidated basis to focus on the University as a whole. GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*, and GASB Statement No. 38, *Certain Financial Statement Note Disclosures*, were effective for fiscal year 2001-2002 and later years. Prior to these standards, the financial statements focused on the accountability of individual fund groups rather than reporting the University's financial information in a single-column format. Other important characteristics of the financial statements include the following:

Net assets represent the excess of total assets over total liabilities. There are three classes of net assets – unrestricted, restricted (nonexpendable and expendable), and invested in capital assets net of related debt.

Assets and liabilities are categorized as either current or non-current. Current liabilities are due within one year, and current assets are those assets available to pay current liabilities.
Revenues and expenses are categorized as either operating or non-operating, and a net income or loss from operations is displayed. State appropriations, noncapital gifts and grants, and investment income are non-operating revenues, which results in a net loss from operations.
Tuition and fees revenues are reported net of scholarships and fellowships that are applied to student accounts. The "scholarship discounts" reduce the tuition and fees revenues and the scholarship and fellowship expenses by equal amounts. Scholarships and fellowships paid directly to students continue to be reported as expenses.
Expenses are reported in the financial statements by natural classification such as salaries and benefits, supplies and materials, and other categories. Presentation by program classification such as instruction, research, and public service are disclosed in the notes to the financial statements.
Purchases of capital assets are expensed over the asset's useful life by the recognition of depreciation expense on the capital assets.
A Statement of Cash Flows using the direct method is reported.

Condensed Statement of Net Assets

The Statement of Net Assets presents the financial position of the University at the end of the fiscal year, includes all assets and liabilities of the University, and segregates the assets and liabilities into current and non-current components. Net assets represent the difference between total assets and total liabilities, and are one indicator of the University's current financial condition.

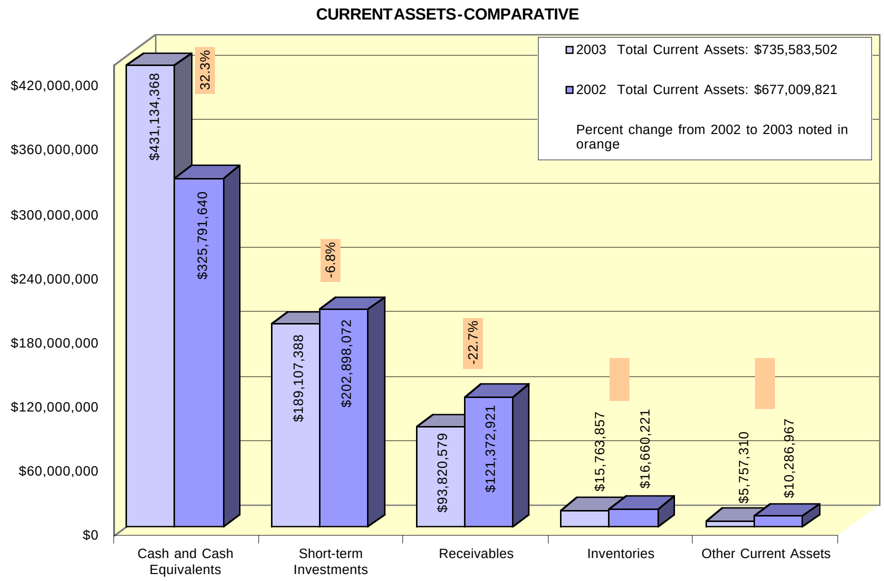
The following table summarizes the University's assets, liabilities and net assets at June 30, 2003, and 2002.

	2003	2002	% Change
Assets:			
Current assets	$735,583,502	$677,009,821	8.7
Non-current assets:			
Endowment investments	754,623,099	758,987,497	-0.6
Other long-term investments	377,744,985	300,226,736	25.8
Capital assets, net	1,134,221,485	1,027,884,988	10.4
Other non-current assets	135,030,134	125,423,197	7.7
Total Assets	3,137,203,205	2,889,532,239	8.6
Liabilities:			
Current liabilities	367,955,960	280,246,736	31.3
Non-current liabilities:			
Funds held in trust for pool participants	345,883,384	291,899,328	18.5
Long-term liabilities	366,628,262	321,843,654	13.9
Other non-current liabilities	31,549,999	31,124,475	1.4
Total Liabilities	1,112,017,605	925,114,193	20.2
Net Assets			
Invested in capital assets, net of related debt	771,280,637	668,385,897	15.4
Restricted:			
Nonexpendable	323,961,205	304,096,632	6.5
Expendable	559,127,937	645,389,715	-13.4
Unrestricted	370,815,821	346,545,802	7.0
	$2,025,185,600	$1,964,418,046	3.1

Current Assets and Liabilities

The Statement of Net Assets shows the University had total assets of $3.1 billion at June 30, 2003, an increase of 8.6% over the prior year. Working capital, which is current assets less current liabilities, was $367.6 million, a decrease of 7.3% from the prior year. Factors causing the working capital decrease include temporary financing for capital construction through the commercial paper program, a decrease in patient accounts receivables resulting from adjustments for uncollectible billings, continued use of the long-term investment pool for a limited portion of working capital to maximize investment returns, and authorization of two weeks of bonus leave to faculty and staff.

Current assets are represented graphically below:



Cash and cash equivalents include cash in bank accounts, cash with fiscal agents, and cash invested through the State Treasurer of North Carolina.

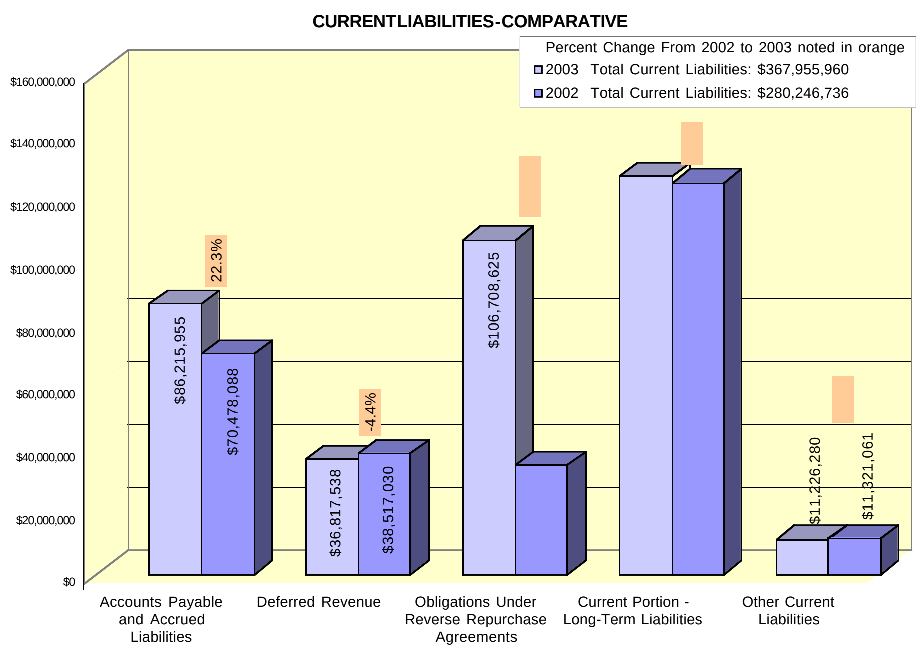
Short-term investments include funds invested through an investment pool administered by the University.

Receivables include amounts due from students of the University, patients of the professional health-care clinics, governmental and private entities for contract and grant awards, donors for pledges of gifts as well as accrued investment earnings.

Inventories represent goods for resale by auxiliary operations of the University.

Other current assets include student loans and amounts due from the State of North Carolina or its component units.

Current liabilities are represented graphically below:



Accounts payable and accrued liabilities include payables to vendors, accrued payroll costs, retainage on construction contracts, and commercial paper.

Deferred revenue is primarily gifts through the planned giving program and represents the calculated remainder after annuity obligations to beneficiaries are determined based on the terms of the gift annuity, charitable trust, or other planned giving arrangement.

Obligations under reverse repurchase agreements are liabilities incurred as part of the University's investment management program.

The current portion of long-term liabilities includes bonds payable, notes payable, capital leases payable, and compensated absences (accrued vacation leave).

Other current liabilities include amounts due to the State of North Carolina or its component units, deposits and interest payable, and funds held for others.

Endowment and Other Long-term Investments

Endowment investments were $754.6 million at June 30, 2003, and include permanent endowments, funds internally designated as endowments, and similar funds such as gift annuities and charitable trusts. Net assets of endowment and similar funds were $710.1 million at June 30, 2003.

The endowment assets are invested with The University of North Carolina at Chapel Hill Foundation Investment Fund, Inc. (the Investment Fund), which is reported as a governmental external investment pool in the financial statements. The Investment Fund is a 501(c)(3) nonprofit corporation established to support the University by operating an investment pool for charitable, nonprofit foundations, associations, trusts, endowments, and funds that are organized and operated primarily to support the University.

Effective January 1, 2003, the assets of the Investment Fund were contributed to the UNC Investment Fund, LLC (System Fund), a North Carolina limited liability company organized and operated to invest assets contributed to it from time to time by the Investment Fund and by The University of North Carolina and its constituent institutions and their related endowments and tax-exempt foundations. All, or substantially all, of the assets of the Investment Fund are expected to be invested in the System Fund. Separate, audited financial statements for the Investment Fund and System Fund are available. The investment returns noted below refer to the pooled investment fund in existence for that time period.

The net assets of the endowment are categorized as restricted nonexpendable, restricted expendable, or unrestricted.

Restricted nonexpendable net assets include permanent endowments for which the donor has stipulated that the principal shall remain inviolate and be invested in perpetuity to generate earnings that can be expended consistent with the purposes specified in the gift instrument.

Restricted expendable net assets include internally designated endowments established by the University with restricted gifts and the undistributed earnings of permanent endowments.

Unrestricted net assets include internally designated endowments established by the University with unrestricted funds.

The investment objective is to earn an average real total return of at least 5.5% per year, net of all fees, over rolling five and 10 year periods. The earnings distribution policy is to provide a stable source of spending support that is sustainable over the long term while preserving the purchasing power of the endowment. The earnings distribution rate was established at 5% of the previous year's market value, with annual increases based on inflationary factors. Each year's distribution is subject to a 4% floor and a 7% cap based on estimated fiscal year-end market value.

Other long-term investments of $377.7 million include funds of $326 million of affiliated entities that are not part of the University's financial reporting entity but do invest through the System Fund, and bond reserves and related funds of $51.7 million.

Most of the University's endowment assets are managed within the System Fund, a pooled investment fund vehicle. The System Fund is designed to provide long-term, stable rates of return on the invested assets through the use of a highly diversified portfolio strategy. The return on the endowment assets invested in the System Fund for the fiscal year was a positive 3.3%. The System Fund return was marginally below the 70/30 S&P 500/Lehman Brothers Government/Corporate Bond Index return of 3.7% for the year, however the System Fund materially outperformed the index over the three and five year periods, -0.1% vs. –4.9% and 6.1% vs. 1.5% respectively. Over the longer term, the System Fund has performed quite well, in both absolute and relative terms, increasing 9.9% for 10 years and 11.6% for 20 years versus the long term-benchmark of inflation plus 5.5% return of 8.6% and 8.8% respectively. Overall, the System Fund is very well positioned in the current environment, given the broad diversification, strong manager roster and conservative structure.

Capital Assets and Debt Management

Capital assets, net of accumulated depreciation, at June 30, 2003 and June 30, 2002 were as follows:

	2003	2002	% Change
Capital Assets:			
Construction in progress	$226,958,080	$225,022,791	0.9
Land and other non-depreciable assets	81,080,269	75,465,273	7.4
Buildings	546,453,143	491,322,542	11.2
General infrastructure	198,911,507	162,460,694	22.4
Machinery and equipment	80,818,486	73,613,688	9.8
Total	$1,134,221,485	$1,027,884,988	10.4

The University's method of capital planning is a long-term process that is continuously reevaluated. The University previously adopted a *Facilities Profile and 10-Year Capital Plan*, recognizing the need for additional academic and student life facilities to keep pace with programmatic expansion. This capital construction program includes major capital renewal of existing buildings and infrastructure to address both deferred maintenance and programmatic needs. Additionally, expansion of campus facilities will allow the University to accommodate the enrollment growth projections over the next decade. One critical factor for the University in fulfilling its mission of teaching, research, and public service and for providing a satisfying residential life for its students is investment in its facilities. Maintenance and renewal of its facilities and infrastructure is an important priority for the University, as evidenced by its $1.3 billion capital construction program.

Major projects completed in fiscal year 2002-2003 include:

New Construction	
Medical Biomolecular Research Building	$64,763,500
Bioinformatics Building	33,677,000
Banks D. Kerr Hall (School of Pharmacy) Addition	22,139,800
Major Renovations of Academic Buildings	
Murphey Hall renovation	6,723,500
Hanes Hall renovation to second floor	2,150,200
Infrastructure Improvements	
Replacement of boiler	15,000,000
Cogeneration Facility repairs to coal silos	12,000,000
Hot water heating system upgrade	8,387,700
Steam distribution system replacement	6,000,000
Expansion of commuter parking lot	1,890,000

Completed projects represent 16% of the $1.3 billion capital construction program, 27% of the projects are under construction, and 57% are in the design phase.

The Higher Education Bond Referendum, overwhelmingly approved in 2000 by North Carolina's voters, is providing nearly $510 million for this program. The University is investing in its capital construction program using a variety of other funding sources including University-issued bonds, cost reimbursements from research grants, internal reserves, and private gifts. Previous changes in state legislation allowed the University to pledge a broader stream of revenues as security for its debt obligations, and general revenue bonds were initially issued in fiscal year 2000-2001. The general revenue pledge results in a stronger, more flexible security that captures the strengths of not only the University's auxiliary and student-related revenues, but also its research programs.

The University launched a commercial paper program during the prior fiscal year that provides low-cost bridge financing for capital projects until gifts are received or in anticipation of an external bond issue. Commercial paper debt was $19 million at June 30, 2003. The commercial paper program and the general revenue bonds allow the University to use a central bank concept for funding capital projects. The University issues fixed and variable rate debt externally, and blends the average borrowing rate to allocate debt costs to individual capital projects and campus divisions. This concept provides a stable and flexible debt-funding source for capital projects. The interest rate on the commercial paper program since its inception has averaged 1.29%. Interest rates on the University's variable rate, long-term bonds were less than one percent for fiscal year 2002-2003. Interest rates on fixed rate, long-term bonds are disclosed in Note 8B of the financial statements.

The University's financial strength allowed it to achieve ratings of AA+/Aa1 by the national rating agencies. The University debt burden ratio, a measure of an entity's dependence on borrowed funds, was only 2.1% at June 30, 2003 and 2.4% for the prior year.

Other Non-current Assets

Other non-current assets were $135 million at June 30, 2003, a 7.7% increase over the prior year. Included in this category are restricted cash and cash equivalents of $66.6 million, receivables for pledged gifts of $27.4 million, notes receivable for student loans of $25.2 million, and restricted resources due from the primary government of $15.8 million from statewide higher education bond referendum proceeds.

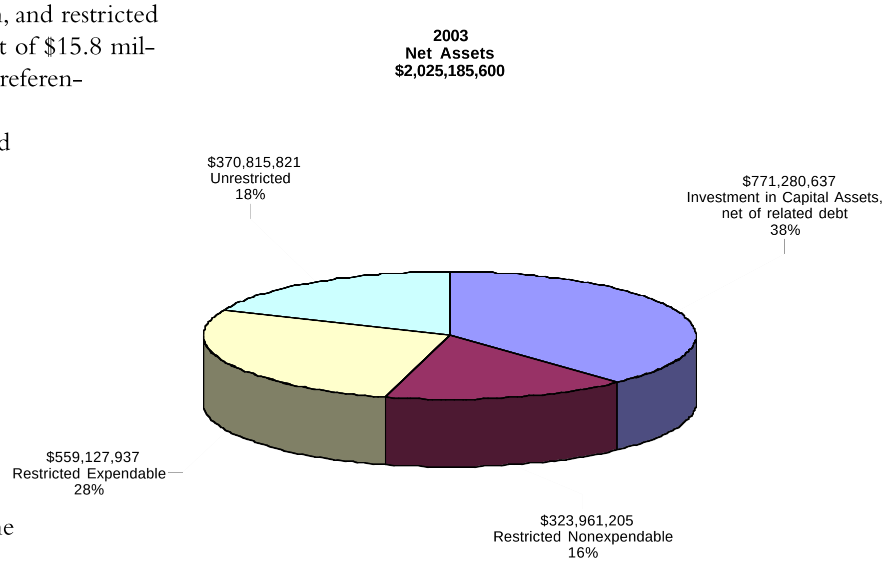
The increase over the prior year resulted from an increase in non-current, restricted cash and cash equivalents. An affiliated foundation, blended as part of the University financial reporting entity, obtained financing in the amount of $35 million to fund the costs of acquisition, construction, and equipping of a student family housing facility. This project, part of the University's master plan, involves building 306 apartments to house University students and their families. The two-bedroom units will replace the existing student family housing, known as Odum Village. The foundation will sell the facility to the University. The University will finance the approved purchase with self-liquidating debt funded by housing revenues.

Non-current Liabilities

Non-current liabilities were $744.1 million at June 30, 2003, and include funds of $345.9 million held for the University's affiliated foundations and other UNC System campuses and their affiliates. These entities are not part of the University's financial reporting entity but do invest through the System Fund. Other non-current liabilities of $31.5 million are refundable U.S. government grants that provide resources for student loan programs. Long-term liabilities of $366.6 million are the non-current portion of bonds payable, notes payable, capital leases payable, compensated absences, and annuities payable.

Net Assets

Net assets represent the value of the University's assets after liabilities are deducted. The University's net assets at June 30, 2003, were $2 billion and are presented graphically below:



The invested in capital assets, net of related debt category represents the University's land, buildings, general infrastructure, equipment, and other capital assets net of accumulated depreciation and net of the outstanding bonds and other indebtedness on the facilities. The restricted nonexpendable category includes the University's permanent endowments funds. The restricted expendable category primarily includes restricted internally-designated endowments, gifts, contract and grant awards, and distributed endowment earnings. The unrestricted category includes unrestricted internally designated endowments, gifts, auxiliary operations, facilities and administrative funds (overhead receipts), and other unrestricted funds. While there are no externally imposed restrictions on unrestricted funds, the funds are generally designated by the University for specific academic programs or capital needs.

Condensed Statement of Revenues, Expenses, and Changes in Net Assets

The Statement of Revenues, Expenses, and Changes in Net Assets presents the University's results of operations. The statement for the fiscal year ended June 30, 2003, and the prior year is summarized as follows:

	2003	2002	% Change
Operating Revenues:			
Student tuition and fees, net	$146,961,417	$124,661,145	17.9
Grants and contracts	455,680,436	444,451,049	2.5
Sales and services, net	393,361,966	383,603,214	2.5
Other	7,563,970	14,749,606	-48.7
Total Operating Revenues	1,003,567,789	967,465,014	3.7
Operating Expenses:			
Salaries and benefits	876,265,477	829,473,249	5.6
Supplies and materials	146,986,272	148,324,265	-.9
Services	364,456,573	364,831,514	-.1
Scholarships and fellowships	45,618,092	40,414,555	12.9
Utilities	57,314,345	45,452,167	26.1
Depreciation	53,075,830	48,517,249	9.4
	1,543,716,589	1,477,012,999	4.5
Operating Loss	(540,148,800)	(509,547,985)	6.0
Non-operating Revenues (Expenses):			
State appropriations	368,024,036	368,504,553	-0.1
Noncapital grants	40,994,829	34,768,925	17.9
Noncapital gifts, net	60,887,596	62,403,802	-2.4
Investment income, net	47,398,174	52,956,614	-10.5
Interest and fees on capital asset-related debt	(15,680,788)	(15,031,104)	4.3
Other non-operating revenues (expenses)	(1,899,072)	(7,661,489)	-75.2
Loss Before Other Changes	(40,424,025)	(13,606,684)	197.1
Capital grants	72,486,349	27,479,400	163.8
Capital gifts, net	7,552,718	8,238,379	-8.3
Additions to permanent endowments	21,152,512	23,282,491	-9.2
Increase in Net Assets	60,767,554	45,393,586	33.9
Net Assets – July 1	1,964,418,046	1,919,024,460	2.4
Net Assets – June 30	$2,025,185,600	$1,964,418,046	3.1

Operating Revenues

The operating revenues represent resources generated by the University in fulfilling its instruction, research, and public service missions. Student tuition and fees are reported net of the scholarship discount, which was $31.5 million for fiscal year 2002-2003 and $25.9 million for the prior year. Total revenues from student tuition and fees increased 17.9% over the prior year. An approved rate increase of $300 per student, inflationary rate increases of 4% for resident students and 12% for nonresident students, additional rate increases for the professional schools, and controlled enrollment growth contributed to the increase in revenues from tuition and fees in fiscal year 2002-2003.

Revenues from contracts and grants (including non-operating grants) increased 3.6% over the prior year. Discussion of contracts and grants in terms of awards also provides a useful perspective. Research grant funding from the National Institutes of Health (NIH) increased 14%. The University is among the nation's leading public research universities, with a diversified portfolio of research that attracted more than $537 million in sponsored program awards during fiscal year 2002-2003, a 10% increase over the prior year. During the same period, NIH funding increased more than 13% to $308 million. During the federal fiscal year 2001-2002 (the latest available information), the University placed 13th nationally in overall NIH research support. The University continues to rank in the top 20 institutions nationally in federal support for science and technology.

The University's standing among the nation's top research universities depends upon the excellence of the faculty and the reputation of the University. During the fiscal year, these strengths have continued to come under pressure as state funding has decreased. The key challenge remains for the administration to preserve or enhance the University's competitive position in the marketplace, not only to sustain external grant funding but also to retain and attract top faculty, staff, and students. To meet these challenges, a five-year strategic plan for research services was developed, and elements of the plan have been included in a newly approved academic plan. A new federal-relations position established in the prior year has allowed expansion of the influence of the faculty in the national policy arena and improves the University's ability to leverage federal funds.

Sales and services revenues of $393.4 million represent an increase of 2.5% over the prior year and include the revenues of campus auxiliary or similar operations such as student housing, student stores, student health services, the utilities system, parking and transportation, the professional health-care clinics, and others. Other revenues of $7.6 million represent operating resources not separately identified and include, as examples, an assessment to the Investment Fund to support administrative services, library fines, and interest income from student loans.

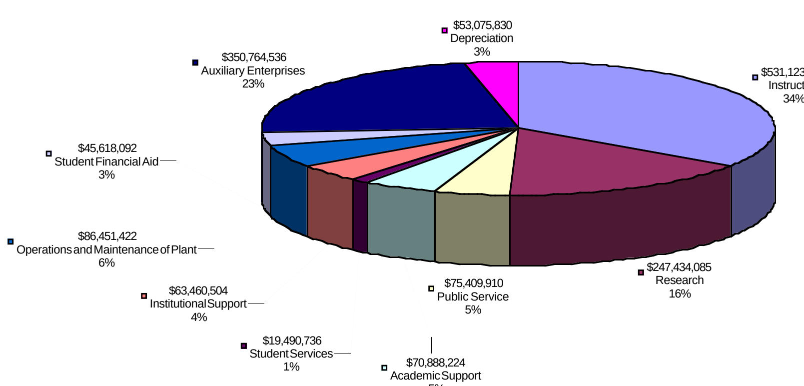
OPERATING EXPENSES

The University's operating expenses were $1.5 billion for the fiscal year ended June 30, 2003, an increase of 4.5% over the prior year. The operating expenses are reported by natural classification in the financial statements and by functional classification in the note disclosures.

The following table illustrates the University's operating expenses by the functional classification:

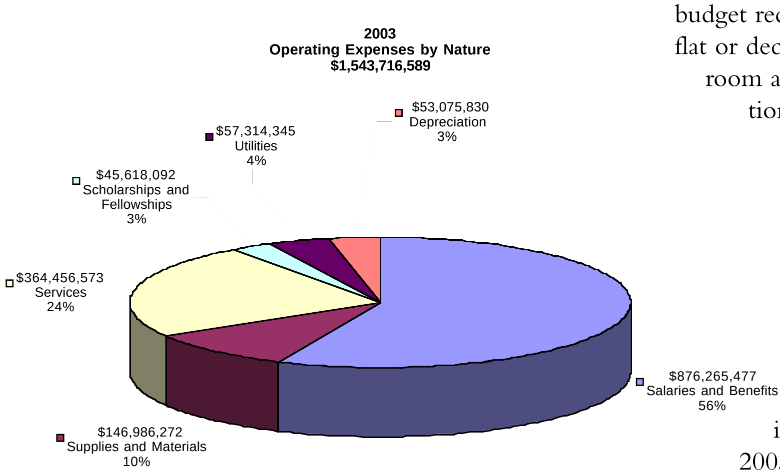
	2003	2002	% Change
Operating Expenses by Function:			
Instruction	$531,123,250	$497,770,880	6.7
Research	247,434,085	237,275,464	4.3
Public Service	75,409,910	76,896,238	-1.9
Academic Support	70,888,224	67,617,814	4.8
Student Services	19,490,736	18,224,875	6.9
Institutional Support	63,460,504	58,560,098	8.4
Operations and Maintenance of Plant	86,451,422	90,941,785	-4.9
Student Financial Aid	45,618,092	40,414,555	12.9
Auxiliary Enterprises	350,764,536	340,794,041	2.9
Depreciation	53,075,830	48,517,249	9.4
Total Operating Expenses by Function:	$1,543,716,589	$1,477,012,999	4.5

2003
Operating Expenses by Function
$1,543,716,589



Some operating expense categories increased at a higher rate than the total. Scholarships and fellowships increased 12.9% over the prior year. A portion of the revenues from tuition increases provides resources for need-based financial aid to enable students to pay the tuition increases. The University strengthened its commitment to merit-based aid as well. During fiscal year 2002-2003, about half of the student body received some form of financial assistance. Utilities expenses increased 26.1% over the prior year. The increase in utilities expenses resulted from growth in research and other facilities on campus due to the ongoing capital construction program, rate increases of both external providers of utilities and the campus utilities operation, and a change in billing protocol for chilled water operations. Depreciation expenses increased 9.4% over the prior year, an expected event given the ongoing, major capital construction activity.

The following graph illustrates the University's operating expenses by the natural classification.



NON-OPERATING REVENUES AND EXPENSES

State appropriations of $368 million, noncapital grants of $41 million, noncapital gifts of $60.9 million, investment income of $47.4 million, interest and fees on capital asset-related debt of -$15.7 million, and other revenues and expenses of -$1.9 million comprise non-operating revenues and expenses. Net non-operating revenues and expenses were relatively unchanged for fiscal year 2002-2003 when compared to the prior year. These revenues are considered non-operating because they were not generated by the University's principal, ongoing operations. For example, state appropriations were not generated by the University but were provided to help fund operating expenses.

The University's initial budget for state appropriations was $398.6 million for fiscal year 2002-2003. Budget increases of $4.4 million to fund enrollment increases including distance learning and other program enhancements as well as reductions in budgeted state appropriations of -$15.2 million resulted in an operating budget for state appropriations of $387.8 million. During the fiscal year 2002-2003, the University was required to reserve $17.2 million in appropriations for reversion at the end of the year. Additionally, the carry forward and use of certain revenues was not approved at the state level, which resulted in reversion of state appropriations of an additional $2.6 million.

National and state economic conditions have significantly affected the level of state appropriations. The University has proactively addressed this issue. Considering that enrollment growth funding was provided and therefore support for continuing operations declined more significantly, it is important to discuss actions taken by the University.

The University restructured the annual budget planning and hearing process with all deans and vice chancellors. The review process provides a framework to implement differential budget reductions, the across-the-board approach for budget reductions is not used. The approach in administering flat or declining state appropriations is to protect the classroom as much as possible, while streamlining administration and eliminating programs. The University has increased its reliance on alternative funding sources, such as clinical income, research awards, indirect cost reimbursements of facilities and administrative expenses, and gifts.

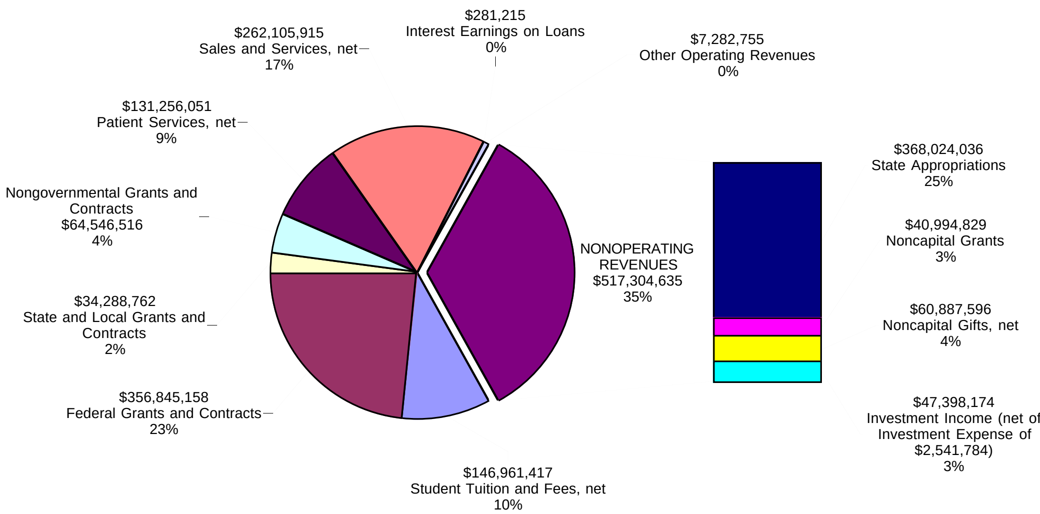
The management approach also includes protecting activities that are central to the University's mission, add value, or are required by law or for internal control purposes. Efficiency improvements are continuously sought in order to save resources. During fiscal year 2002-2003, specific programs as well as instructional and administrative positions were eliminated to address the reductions in state appropriations and to allow funding for enrollment growth to be used for the purposes allocated.

Noncapital grants increased by 17.9% to $40.1 million in fiscal year 2002-2003 and represent federal awards that are not considered to be exchange transactions. Net noncapital gifts of $60.9 million represent expendable gifts received and pledges made and are net of an allowance for uncollectible pledges. Net investment income of $47.4 million includes income and realized and unrealized gains and is net of realized and unrealized losses and investment management fees. Interest and fees on capital asset-related debt were -$15.7 million. Other non-operating expenses total -$1.9 million and include capital asset disposals.

TOTAL OPERATING AND NON-OPERATING REVENUES

Operating and non-operating revenues such as state appropriations, noncapital grants, noncapital gifts, and investment income are used to fund University operations.

The following chart illustrates the University's operating and non-operating revenues which total $1.5 billion for fiscal year 2002-2003.



Other Changes in Net Assets

Capital grants of $72.5 million came from statewide higher education bond proceeds for capital construction projects. Net capital gifts of $7.6 million also provided funding for construction projects. Nonexpendable gifts and funds from the state's program to match gifts for distinguished professorship endowments resulted in additions to permanent endowments of $21.2 million during fiscal year 2002-2003.

Condensed Statement of Cash Flows

The Statement of Cash Flows provides additional information about the University's financial results by reporting the major sources and uses of cash. Cash increased by $115.5 million during the fiscal year 2002-2003. Many factors affect the changes in cash and the cash position of the University. One significant factor that resulted in a $90 million increase in the cash position at June 30, 2003 was the additional use of the State Treasurer's short-term investment fund, which is classified as a cash equivalent, for the University's temporary investment pool.

The statements for the fiscal year ended June 30, 2003, and the prior year are summarized as follows:

	2003	2002
Cash Flows Provided (Used):		
Operating activities	($382,265,470)	($440,098,807)
Noncapital financing activities	488,584,930	482,880,498
Capital and related financing activities	(55,707,534)	(171,429,157)
Investing activities	64,860,649	90,827,088
Net Increase (Decrease) in Cash	115,472,575	(37,820,378)
Cash – July 1	382,265,905	420,086,283
Cash – June 30	$497,738,480	$382,265,905

Cash flows from operating activities include, as examples, cash received for tuition and fees or research grants and salaries paid to faculty or payments of invoices to vendors. Since state appropriations, gifts, and certain other revenues are not considered operating revenue, operating activities had a net cash outflow for both fiscal years.

Noncapital financing activities include state appropriations received for operations and noncapital gifts, and had a net cash inflow for both fiscal years.

The cash flows from capital and related financing activities include the proceeds received from short-term and long-term debt obligations, the repayment of debt, and the acquisition of capital assets. Due to the increase in the level of capital grants provided as part of the capital construction program and a decrease in debt principal payments, capital and related financing activities had a lower net cash outflow in fiscal year 2002-2003. The use of cash was significantly more in fiscal year 2001-2002 due to the issuance of general revenue bonds to defease $69.9 million of outstanding utility system revenue bonds.

The net cash inflows from investing activities include purchases and sales of equity securities and other investments as well as interest and dividends received.

ECONOMIC OUTLOOK

Management's view is that the University is well positioned to continue demonstrating excellence in teaching, research, and public service. Management believes that, although national and state economic conditions have affected resources, the University will maintain its solid financial foundation and enhance its financial outlook. The University's strong debt credit rating allows it to obtain competitive financing for capital construction. The University's comparatively low tuition levels enhance its appeal to prospective students and provide a possible source of additional resources, should tuition increases be enacted. The University's academic standing allows it to continuously attract top students. Student application levels, enrollment levels of students including cross admits, applicants' exam scores and other admission criteria, and other factors illustrate the substantial appeal of the University to prospective students.

Tuition rates increased for fiscal year 2003-2004 by 5% with a $500 increase cap for nonresident graduate students. There were also limited tuition increases for professional schools. Consideration is being given at the federal level regarding use of price controls to control tuition increases of both private and public universities. Other changes related to affordability in higher education are also under consideration. Carolina's tuition levels remain low in comparison to its national peer group of institutions, and these very competitive tuition levels place the University in a stronger financial position as this national debate on rising educational costs for students continues.

Starting next fall, the University will launch the Carolina Covenant, a new initiative that will give children of low income families the opportunity to attend the University debt-free. This is the first program of its kind to be offered by a public university in the United States. The University will meet 100% of a qualified student's financial need through a combination of federal, state, campus-based, privately funded grants and scholarships, as well as his or her participation in the federal work-study job program.

The University's relationship with the State of North Carolina is a critical success factor. Given the recent economic conditions, the state has continued to demonstrate strong financial support for higher education in North Carolina. The budgeted funding level for state appropriations for 2003-2004 totals $384.7 million, which represents an increase of 4.5% over fiscal year 2002-2003 actual state appropriations. Based on communications from state officials, 2% of the state appropriations budget is being held in reserve for possible reversion. Given the recent economic volatility and in the event budgeted state revenue targets are not realized, this action was required by state officials. While additional reversions or budget reductions are not anticipated for fiscal year 2003-2004, it is not certain.

While the overall financial strength of the University remains solid both currently and prospectively, some appropriated support has stagnated. The cumulative impact of reduced state appropriations includes elimination of some academic and support programs, loss of faculty and staff positions, diminished classroom experience caused by an increase in class size and other factors, reduction in academic and administrative support services, impairment to the libraries, and organizational restructuring. The University must continue to address competitive pressures related to recruiting and retaining faculty and staff. The University's programs for health, retirement, and other benefits have cost and coverage issues that are of concern and require resolution, working in conjunction with UNC System and state officials. The University is progressing on these benefits issues by pursuing additional flexibility in allowing benefits and other enhancements to the benefits programs. However, the University's diverse revenue base, its strategic planning processes, and its proactive approach in addressing budgetary issues help alleviate the significance of the impacts. For example, completion of an academic plan to guide future investments over the next five years was a major step forward for the University.

Research efforts will continue to provide impetus to the financial condition of the University and the state. The research enterprise creates jobs for the North Carolina economy. The University continues its commitment to transfer new technologies developed by faculty to the market place, which translates into higher quality and better paying careers for the citizens of North Carolina. Planning for Carolina North, a 900-acre tract of University-owned land proposed for mixed-use development, is in its early stages. The living-learning community that is envisioned as a public-private partnership would significantly enhance the research, teaching, and public service mission of the University and benefit the people of North Carolina and beyond.

The University believes the investment performance of its endowment fund will continue to provide important resources for University operations. Although the investment performance record has been impressive, recent major changes are expected to strengthen investment management. The University's investment management operation was separately organized as the UNC Management Company, Inc. (UNC-MC), a nonprofit corporation organized and operated as a 501(c)(3) entity, to provide investment management services and administrative services to the University and to the other campuses of the UNC System and their affiliated, nonprofit foundations as appropriate. The UNC-MC was also organized to manage real estate, promote the dissemination and commercialization of technology development at the University, and to participate in joint ventures, limited partnerships, limited liability companies, and similar entities for the purpose of providing investment opportunities. Management believes this new structure will enhance the ability to attract and retain investment professionals and increase the number of entities that may invest in the pooled investment fund. It is anticipated that these factors will contribute to enhanced investment performance.

The $1.8 billion Carolina First fund-raising campaign continues to succeed, providing critical resources for the present and for future generations. The campaign began its quiet phase on July 1, 1999. As of September 30, 2003, gifts, pledges, and deferred commitments of $1.1 billion had been received. With 53% of the campaign's time period elapsed, 60% of the total goal has been reached through gifts and commitments. Of the $1.8 billion goal, $850 million will provide expendable resources, $700 million will be used to increase endowment assets, and $250 million will support the capital construction program. The campaign will conclude on June 30, 2007.

The capital planning process continues to benefit the University as the construction program has and will continue to improve the academic and administrative facilities of the University. The new and renovated facilities will enhance the teaching environment, improve research opportunities, and provide a better infrastructure. The operational planning process is a critical success factor too. The current environment demanded that the University move away from a short-term, marginal focus to more strategic, mission-driven financial decision processes. Without the framework of an academic plan that considers mission-critical goals and resource needs, the University was not likely to achieve its full potential. An academic plan was developed, and a five-year financial planning process was undertaken. The purpose and desired outcomes of the Five-Year Financial Plan include the following:

Serves as the "enabling" means to implement long-range plans for programs, facilities, and other initiatives.

Aligning resources optimally to accomplish the mission and the strategic goals of the University.

Relying upon quantitative as well as qualitative analyses of critical issues that will affect the University's successful advancement and financial stability during the next five years.

Providing ongoing mechanism for evaluating the extent that resources are being used to meet fundamental goals.

Highlighting the links between the institutional values that drive our policies and ultimately determine the revenue and cost structures of the University.

Enhancing flexibility to redirect or retain funds and strengthen the University's ability to react to change and cope with short- and long-term fiscal stress.

Management believes the improved academic and financial planning process will result in a more strategic use of resources.

The University's solid support from the state in difficult economic times, its widespread appeal to top prospective students, its diversified portfolio of research funding, its strong investment performance, its capital construction program, and its outstanding fundraising capabilities are among the factors indicating a positive and successful future for the University. The University's commitment to strategic and balanced operating budgets, protection and enhancement of its endowed and physical assets, and adherence to compliance and control standards all support a continuing strong financial position for the University.

Statement of Net Assets
June 30, 2003

ASSETS	
Current Assets	
Cash and cash equivalents	$214,800,699
Restricted cash and cash equivalents	216,333,669
Short-term investments	122,067,058
Restricted short-term investments	67,040,330
Receivables, net (Note 4)	93,820,579
Due from State of North Carolina component units	1,861,427
Inventories (Note 1G)	15,763,857
Notes receivable, net (Note 4)	3,895,883
Total current assets	$735,583,502
Non-current Assets	
Restricted cash and cash equivalents	66,604,112
Receivables, net (Note 4)	27,427,006
Restricted due from primary government	15,787,019
Endowment investments	754,623,099
Other long-term investments	377,744,985
Notes receivable, net (Note 4)	25,211,997
Capital assets, nondepreciable (Note 5)	308,038,349
Capital assets, depreciable, net (Note 5)	826,183,136
Total non-current assets	2,401,619,703
Total assets	$3,137,203,205
LIABILITIES	
Current Liabilities	
Accounts payable and accrued liabilities (Note 6)	$67,215,955
Due to primary government	82,676
Due to State of North Carolina component units	1,033,245
Deposits payable	2,160,444
Funds held for others	6,081,682
Deferred revenue	36,817,538
Interest payable	1,868,233
Obligations under reverse repurchase agreements	106,708,625
Short-term debt (Note 7)	19,000,000
Long-term liabilities-current portion (Note 8)	126,987,562
Total current liabilities	$367,955,960
Non-current Liabilities	
US government grants refundable	31,549,999
Funds held in trust for pool participants	345,883,384
Long-term liabilities (Note 8)	366,628,262
Total non-current liabilities	744,061,645
Total liabilities	$1,112,017,605
Total assets less liabilities	$2,025,185,600

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

Statement of Net Assets *(continued)*
June 30, 2003

NET ASSETS	
Invested in capital assets, net of related debt	$771,280,637
Restricted for	
Nonexpendable	
Professorships and lectureships	120,856,256
Scholarships and fellowships	79,955,407
Research	10,035,203
Library acquisitions	20,017,539
Departmental uses	49,543,457
Loans	13,533,012
Other	30,020,331
Expendable	
Professorships and lectureships	188,740,918
Scholarships and fellowships	110,132,665
Research	17,153,443
Library acquisitions	16,278,810
Departmental uses	165,334,114
Instruction and educational service agreements	16,438,938
Plant improvements	13,361,072
Capital projects	21,517,527
Debt service	10,170,450
Unrestricted	370,815,821
Total net assets	$2,025,185,600

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

Statement of Revenues, Expenses, and Changes in Net Assets
For the Year Ended June 30, 2003

REVENUES	
Operating Revenues	
Student tuition and fees, net (Note 10)	$146,961,417
Federal grants and contracts	356,845,158
State and local grants and contracts	34,288,762
Nongovernmental grants and contracts	64,546,516
Patient services, net (Note 10)	131,256,051
Sales and services, net (Note 10)	262,105,915
Interest earnings on loans	281,215
Other operating revenues	7,282,755
Total operating revenues	$1,003,567,789
EXPENSES	
Operating Expenses	
Salaries and benefits	876,265,477
Supplies and materials	146,986,272
Services	364,456,573
Scholarships and fellowships	45,618,092
Utilities	57,314,345
Depreciation	53,075,830
Total operating expenses	1,543,716,589
Operating loss	($540,148,800)
NON-OPERATING REVENUES (EXPENSES)	
State appropriations	368,024,036
Noncapital grants	40,994,829
Noncapital gifts, net (Note 10)	60,887,596
Investment income (net of investment expense of $2,541,784)	47,398,174
Interest and fees on capital asset-related debt	(15,680,788)
Other non-operating revenues (expenses)	(1,899,072)
Net non-operating revenues	499,724,775
Loss before other revenues, expenses, gains, or losses	($40,424,025)
Capital grants	72,486,349
Capital gifts, net (Note 10)	7,552,718
Additions to permanent endowments	21,152,512
Increase in net assets	60,767,554
NET ASSETS	
Net assets July 1, 2002	1,964,418,046
Net assets June 30, 2003	$2,025,185,600

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

Statement of Cash Flows
For the Year Ended June 30, 2003

Cash Flows from Operating Activities	
Received from customers	$1,017,533,913
Payments to employees and fringe benefits	(854,699,876)
Payments to vendors and suppliers	(569,581,149)
Payments for scholarships and fellowships	(45,618,092)
Loans issued to students	(5,879,203)
Collection of loans to students	6,680,902
Other receipts (payments)	69,298,035
Net cash used by operating activities	(382,265,470)
Cash Flows from Noncapital Financing Activities	
State appropriations	368,024,036
Noncapital grants received	45,785,818
Noncapital gifts	53,165,391
Additions to permanent endowments	21,152,512
Related activity agency receipts	2,405,224
Related activity agency disbursements	(1,948,051)
Net cash provided by noncapital financing activities	488,584,930
Cash Flows from Capital Financing and Related Financing Activities	
Proceeds from capital debt	53,532,276
Capital grants	74,148,014
Capital gifts	10,384,493
Acquisition and construction of capital assets	(161,425,139)
Principal paid on capital debt and leases	(14,044,252)
Interest and fees paid on capital debt and leases	(18,302,926)
Net cash used by capital financing activities	(55,707,534)
Cash Flows from Investing Activities	
Proceeds from sales and maturities of investments	481,404,506
Purchase of investments and related fees	(523,612,081)
Interest on investments	35,354,598
Obligations under reverse repurchase agreements	71,713,626
Net cash provided by investing activities	64,860,649
Net increase in cash	115,472,575
Cash July 1, 2002	382,265,905
Cash June 30, 2003	$497,738,480

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

Statement of Cash Flows *(continued)*
For the Year Ended June 30, 2003

Reconciliation of Net operating Revenues (Expenses) to Net Cash Used by Operating Activities:	
Operating (loss)	($540,148,800)
Adjustments to reconcile operating loss to net cash Used by operating activities:	
Depreciation expense	53,075,830
Allowances, write-offs and amortizations	340,915
Nonoperating other income (expense)	330,235
Changes in assets and liabilities:	
Receivables, net	29,607,181
Notes receivable, net	(574,076)
Inventories	896,365
Accounts payable & accrued liabilities	(493,025)
Due to primary government	(115,508)
Deferred revenue	(879,063)
Compensated absences	20,112,895
U.S. government grants refundable	425,524
Funds held for others	55,156,057
Net cash used by operating activities:	($382,265,470)
Noncash Investing, Capital, and Financiang Activities:	
Assets acquired through a gift	765,916
Change in fair value of investments	(9,564,883)
Increase in receivable related to nonoperating income	4,124,514
Reconciliation of Cash and Cash Equivalent:	
Current assets:	
Cash and cash equivalents	$214,800,699
Restricted cash and cash equivalents	216,333,669
Non-current assets:	
Restricted cash and cash equivalents	66,604,112
Total cash and cash equivalent - June 30, 2003	$497,738,480

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

NOTES TO THE FINANCIAL STATEMENTS

June 30, 2003

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NOTE 1 SIGNIFICANT ACCOUNTING POLICIES

A. Financial Reporting Entity

The concept underlying the definition of the financial reporting entity is that elected officials are accountable to their constituents for their actions. As required by accounting principles generally accepted in the United States of America, the financial reporting entity includes both the primary government and all of its component units. An organization other than a primary government may serve as a nucleus for a reporting entity when it issues separate financial statements. The University of North Carolina at Chapel Hill is a constituent institution of the 16-campus University of North Carolina System, which is a component unit of the State of North Carolina and an integral part of the State's *Comprehensive Annual Financial Report*.

The accompanying financial statements present all funds belonging to the University and its component units. While the Board of Governors of the University of North Carolina System has ultimate responsibility, the chancellor, the Board of Trustees, and the Board of Trustees of the Endowment Fund have both delegated and statutory responsibilities for financial accountability of the University's funds. Although legally separate, The University of North Carolina at Chapel Hill Foundation Investment Fund, Inc. (Investment Fund), UNC Investment Fund, LLC (System Fund), UNC Management Company, Inc. (Management Company), The University of North Carolina at Chapel Hill Foundation, Inc. (UNC-CH Foundation), The Kenan-Flagler Business School Foundation (Business School Foundation), The School of Social Work Foundation Inc. (Social Work Foundation), and U.N.C. Law Foundation Inc. (Law Foundation), are reported as if they were part of the University.

The Investment Fund is governed by a board consisting of 11 ex-officio directors and one or two elected directors. Ex-officio directors include all of the members of the Board of Trustees of the Endowment Fund of The University of North Carolina at Chapel Hill, the vice chancellor for finance and administration, and the vice chancellor for university advancement. The UNC-CH Foundation Board may, in its discretion, elect one or two of its at-large members to the Investment Fund Board. The Investment Fund supports the University by operating an investment fund for charitable, non-profit foundations, associations, trusts, endowments and funds that are organized and operated primarily to support the University. Because members of the Board of Directors of the Investment Fund are officials or appointed by officials of the University and the Investment Fund's primary purpose is to benefit UNC-Chapel Hill and other organizations operated primarily to support the University, its financial statements have been blended with those of the University.

In December, 2002 the System Fund was organized to allow the University, the University of North Carolina and its constituent institutions (UNC System), affiliated foundations, associations, trusts and endowments that support the University and the UNC System, to pool their resources and invest collectively in investment opportunities identified, structured and arranged by the Management Company (formerly University Investment Office). The membership interests are offered only to government entities or tax-exempt organizations that are controlled by or support the UNC System. The Investment Fund contributed and assigned all of its assets to the System Fund effective January 1, 2003 in exchange for its membership interest in the System Fund. Upon such contribution and assignment, and in consideration thereof, the System Fund has assumed all liabilities and obligations of the Investment Fund in respect of such contributed assets. At June 30, 2003 the Investment Fund membership interest was approximately 97% of the System Fund total membership interests. Because the Investment Fund is the predominant member of the System Fund, the financial statements of the System Fund have been blended with those of the University.

The Management Company is a North Carolina non-profit corporation organized and operated exclusively to support the educational mission of the University. The Management Company will also provide investment management services to the University, UNC System, and institutions and affiliated tax-exempt organizations, and perform other functions for and generally carry out the purposes of the University. The Management Company is governed by five ex-officio directors and one or two additional directors as fixed or changed from time to time by the board, elected by the ex-officio directors. The ex-officio directors consist of the chancellor of the University, the vice chancellor for finance and administration of the University, the chairman of the University's Board of Trustees of the University, the chairman of the Board of Directors of the Investment Fund, and the president of the Management Company. Because members of the Board of Directors of the Management Company are officials or appointed by officials of the University and the Management Company's primary purpose is to benefit UNC-Chapel Hill and other organizations operated primarily to support the University, its financial statements have been blended with those of the University. Effective January 1, 2003, the Management Company entered into an investment services agreement with the System Fund pursuant to which it will provide investment management and administrative services to the System Fund.

The UNC-CH Foundation is governed by a 17-member board consisting of nine ex-officio directors and eight elected directors. Ex-officio directors include the chairman of the UNC-Chapel Hill Board of Trustees, the chancellor, the vice chancellor for finance and administration, and the vice chancellor for university advancement (nonvoting). In addition, the Board of Trustees elects two ex-officio directors from among its own members as well as three ex-officio directors from the membership of the Board of Trustees of the Endowment Fund who have not otherwise been selected. The eight remaining directors are elected as members of the UNC-CH Foundation Board of Directors by action of the ex-officio directors. The UNC-CH Foundation aids, supports, and promotes teaching, research and service in the various educational, scientific, scholarly, professional, artistic and creative endeavors of the University. Because members of the Board of Directors of the UNC-CH Foundation are officials or appointed by officials of the University and the UNC-CH Foundation's sole purpose is to benefit UNC-Chapel Hill, its financial statements have been blended with those of the University.

The Business School Foundation is governed by a board consisting of four ex-officio directors and four or more elected directors. Ex-officio directors include the dean of the Kenan-Flagler Business School (Business School), as well as the school's chief financial officer, associate dean of academic affairs, and associate dean for MBA Programs. The remaining directors are elected to the Business School Foundation Board of Directors by action of the ex-officio directors. The Business School Foundation aids, promotes and supports the Kenan-Flagler Business School at UNC-Chapel Hill. Because members of the Board of Directors of the Business School Foundation are officials or appointed by officials of the University, the financial statements of the Business School Foundation have been blended with those of the University.

The Social Work Foundation is governed by a board consisting of three ex-officio directors and 10 elected directors. Ex-officio directors include the dean of the School of Social Work as well as the school's Chairman of the Board of Advisors and the assistant dean for external affairs. The remaining 10 directors are elected to the Social Work Foundation Board of Directors by action of the ex-officio directors. The Social Work Foundation fosters and promotes the growth, progress, and general welfare of social work practice and research at the School of Social Work of UNC-Chapel Hill. Because members of the Board of Directors of the Social Work Foundation are officials or appointed by officials of the University, the financial statements of the Social Work Foundation have been blended with those of the University.

The Law Foundation is governed by a board consisting of one ex-officio director, six appointed directors and six elected directors. The ex-officio director is the dean of the School of Law of UNC-Chapel Hill. The ex-officio director appoints six directors and the Board of Directors of the Law Alumni Association of the UNC, Inc. elects the other six directors. The Law Foundation provides support, fosters, and encourages the study and teaching of law at the UNC-Chapel Hill Law School. Because a majority of the members of the Board of Directors of the Law Foundation are officials or appointed by officials of the University, the financial statements of the Law Foundation have been blended with those of the University.

Separate financial statements for the Investment Fund, System Fund, the Management Company and blended foundations may be obtained from the University Controller's Office, Campus Box 1270, Chapel Hill, NC 27599-1270, or by calling (919) 962-1370. Other related foundations and similar non-profit corporations for which the University is not financially accountable are not part of the accompanying financial statements except for their participation in the Investment Fund and Temporary Pool as presented in the accompanying financial statements as Funds Held in Trust for Pool Participants. The University's financial statements include the financial activities of the clinical patient care programs. These clinical patient care programs established or maintained by the School of Medicine of The University of North Carolina at Chapel Hill are a component unit of The University of North Carolina Health Care System, which is a component unit of the University of North Carolina System.

B. Basis of Presentation

The accompanying financial statements are presented in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

Pursuant to the provisions of GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – For Public Colleges and Universities* effective for the University's year ended June 30, 2003, the full scope of the University's activities is considered to be a single business-type activity (BTA) and accordingly, is reported within a single column in the basic financial statements.

In accordance with GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the University does not apply Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless the GASB amends its pronouncements to specifically adopt FASB pronouncements issued after that date.

C. Basis of Accounting

The financial statements of the University have been prepared using the economic resource management focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred.

Nonexchange transactions, in which the University receives value without directly giving equal value in exchange, includes state appropriations, certain grants, and donations. Revenues are recognized, net of estimated uncollectible amounts, as soon as all eligibility requirements imposed by the provider have been met, and collection is probable.

D. Cash and Cash Equivalents

This classification includes cash on deposit with private bank accounts, petty cash, undeposited receipts, savings accounts, cash on deposit with fiscal agents, and deposits held by the State Treasurer in the short-term investment portfolio. The short-term investment portfolio maintained by the State Treasurer has the general characteristics of a demand deposit account in that participants may deposit and withdraw cash at any time without prior notice or penalty.

E. Investments

This classification includes long-term fixed income investments, repurchase agreements, equity investments, mutual funds, money market funds, certificates of deposit, limited partnerships, real estate investment trusts, real estate, and other asset holdings by the University. Except for money market funds, certificates of deposit, real estate not held by a governmental external investment pool, and other asset holdings, these investments are reported at fair value for year-end financial reporting purposes. Fair value is the amount at which an investment could be exchanged between two willing parties. Fair value for financial reporting purposes is based on quoted market prices. The net increase (decrease) in the fair value of investments is recognized as a component of investment income.

Money market funds, certificates of deposit, real estate not held by a governmental external investment pool, and other asset holdings are reported at cost, if purchased, or at fair value or appraised value at date of gift, if donated.

Short-term investments include marketable securities representing the investment of cash that is available for current operations. A majority of this available cash is invested in the University's Temporary Pool, a governmental external investment pool.

F. Receivables

The receivables consist of tuition and fees charges to students, and charges to patients for services provided by the UNC Physicians & Associates and the Dental Faculty Practices. Receivables also include amounts due from the federal government, state and local governments, private sources in connection with reimbursement of allowable expenditures made pursuant to contracts and grants, pledges that are verifiable, measurable, and expected to be collected and available for expenditures for which the resource provider's conditions have been satisfied, and notes receivable from loans to students. Patients, pledges and notes receivables are recorded net of the allowance for doubtful accounts. The accounts and other receivables are shown at book value with no provision for doubtful accounts considered necessary.

G. Inventories

Inventories held by the University are priced at cost or average cost except for the Student Stores inventory, which is valued at the lower of cost or market. The inventories consist of expendable supplies, postage, fuel held for consumption, textbooks, and other merchandise for resale.

H. Capital Assets

Capital assets are stated at cost at date of acquisition or fair value at date of donation in the case of gifts. The value of assets constructed includes all material direct and indirect construction costs. Interest costs incurred are capitalized during the period of construction.

The University capitalizes assets that have a value or cost in excess of $5,000 at the date of acquisition and an expected useful life of more than one year. Library books are generally not considered to have a useful life of more than one year unless part of a collection and are expensed in the year of acquisition.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 10 to 40 years for infrastructure, 10 to 50 years for buildings and two to 10 years for equipment.

The University's historic property, artworks and literary collections are capitalized at cost or fair value at the date of donation. These property and collections are considered inexhaustible and are therefore not depreciated.

I. Restricted Assets

Restricted assets represent assets whose use is restricted by external parties or by law through constitutional provisions or enabling legislation. Unexpended proceeds of revenue bonds and unexpended capital contributions are classified as restricted assets because their use is limited by applicable bond covenants or donor/grantor agreements.

J. Funds Held in Trust for Pool Participants

Funds held in trust for pool participants represent the external portion of the University's governmental external investment pool more fully described in Note 2.

K. Funds Held in Trust by Others

Funds held in trust by others are resources neither in the possession nor the control of the University, but held and administered by an outside organization, with the University deriving income from such funds. Such funds established under irrevocable trusts where the University has legally enforceable rights or claims have not been recorded on the accompanying financial statements. The value of these assets at June 30, 2003, is approximately $31,726,073.

L. Non-current Long-term Liabilities

Non-current long-term liabilities include principal amounts of bonds payable, notes payable, capital lease obligations, annuity payable and compensated absences that are not scheduled to be paid within the next fiscal year.

Bonds payable are reported net of unamortized premiums or discounts and deferred losses on refundings. The University amortizes bond premiums/discounts over the life of the bonds using the straight-line method. The deferred losses on refundings are amortized over the life of the old debt or new debt (whichever is shorter) using the straight-line method. Issuance costs paid from the debt proceeds are expensed.

M. Compensated Absences

The University's policy is to record the cost of vacation leave when earned. The policy provides for a maximum accumulation of unused vacation leave of 30 days which can be carried forward each January 1st or for which an employee can be paid upon termination of employment. Also, any accumulated vacation leave in excess of 30 days at year-end is converted to sick leave. Under this policy, the accumulated vacation leave for each employee at June 30th equals the leave carried forward at the previous December 31st plus the leave earned, less the leave taken between January 1st and June 30th.

In addition to the vacation leave described above, compensated absences includes the accumulated unused portion of the special annual leave bonus awarded by the North Carolina General Assembly to all full-time permanent employees as of September 30, 2002. The unused portion of this leave remains available until used, notwithstanding the limitation on annual leave carried forward described above.

When classifying compensated absences into current and non-current, leave is considered taken using a last in, first out method.

There is no liability for unpaid accumulated sick leave because the University has no obligation to pay sick leave upon termination or retirement. However, additional service credit for retirement pension benefits is given for accumulated sick leave upon retirement.

N. Net Assets

The University's net assets are classified as follows:

Invested in Capital Assets, Net of Related Debt – This represents the University's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of invested in capital assets, net of related debt.

Restricted Net Assets – Nonexpendable – Nonexpendable restricted net assets include endowments and similar type assets whose use is limited by donors or other outside sources, and as a condition of the gift the principal is to be maintained in perpetuity.

Restricted Net Assets – Expendable – Expendable restricted net assets include resources which the University is legally or contractually obligated to spend in accordance with restrictions imposed by external parties.

Unrestricted Net Assets – Unrestricted net assets include resources derived from student tuition and fees, sales and services, unrestricted gifts, royalties, and interest income.

Restricted and unrestricted resources are recorded using a fund accounting system and are spent in accordance with established fund authorities. Fund authorities provide rules for the fund activity and are separately established for restricted and unrestricted activities. When both restricted and unrestricted funds are available for expenditure, the University would generally first apply restricted funds; although individual departments have authority to use either restricted or unrestricted funds as appropriate.

O. Scholarship Discounts

Student tuition and fees revenues and certain other revenues from University charges are reported net of scholarship discounts in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. The scholarship discount is the difference between the actual charge for goods and services provided by the University and the amount that is paid by students or by third parties on the students' behalf. Student financial assistance grants, such as Pell grants, and other federal, state or nongovernmental programs, are recorded as either operating or non-operating revenues in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. To the extent that revenues from these programs are used to satisfy tuition, fees, and other charges, the University has recorded a scholarship discount.

P. Revenue and Expense Recognition

The University classifies its revenues and expenses as operating or non-operating in the accompanying Statement of Revenues, Expenses, and Changes in Net Assets. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the University's principal ongoing operations. Operating revenues include activities that have characteristics of exchange transactions, such as student tuition and fees, sales and services of auxiliary enterprises, certain federal, state and local grants and contracts that are essentially contracts for services, and interest earned on loans. Operating expenses are all expense transactions incurred other than those related to capital and noncapital financing or investing activities as defined by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*.

Non-operating revenues include activities that have the characteristics of nonexchange transactions. Revenues from nonexchange transactions such as state appropriations that represent subsidies, gifts to the University and certain grants, as well as investment income, are considered non-operating since these are either investing, capital or noncapital financing activities. Capital contributions and additions to endowment are presented separately after non-operating revenues and expenses.

Q. Internal Sales Activities

Certain institutional auxiliary operations provide goods and services to University departments as well as to its customers. These institutional auxiliary operations include activities such as utility services, telecommunications, central stores, printing and copy centers, postal services, repairs and maintenance services. In addition, the University has other miscellaneous sales and service units that operated either on a reimbursement or charge basis. All internal sales activities to University departments from auxiliary operations and sales and service units have been eliminated in the accompanying financial statements. These eliminations are recorded by removing the revenue and expense in the auxiliary operations and sales and service units and, if significant, allocating any residual balances to those departments receiving the goods and services during the year.

R. Related Parties

Related parties are non-profit organizations established to assist and provide support to University programs by funding scholarships, fellowships, professorships, and other needs of specific schools as well as the University's overall academic endeavors. The University's financial statements do not include the assets, liabilities, net assets or operational transactions of these organizations except for support from each organization to the University.

NOTE 2
DEPOSITS AND INVESTMENTS

A. Deposits

Unless specifically exempt, the University is required by General Statute 147-77 to deposit moneys received with the State Treasurer or with a depository institution in the name of the State Treasurer. General Statute 116-36.1 requires the University to deposit its institutional trust funds, except for funds received for services rendered by health-care professionals, with the State Treasurer. Although specifically exempted, the University may voluntarily deposit endowment funds, special funds, revenue bond proceeds, debt service funds, and funds received for services rendered by health-care professionals with the State Treasurer. Special funds consist of moneys for intercollegiate athletics and agency funds held directly by the University.

Deposits include cash and cash equivalents and certificates of deposit totaling $498,534,217. At year-end, cash on hand was $204,263. The University's portion of the State Treasurer's short term Investment Pool was $453,461,438. It is the State Treasurer's policy and practice for deposits not covered by federal depository insurance to be covered by collateral held by the State of North Carolina's agent in the name of the state and for his investments to be held by the state's agent in the state's name. The carrying amount of the University's deposits not with the State Treasurer was $44,277,042 and the bank balance was $7,097,583. Of the bank balance, $2,173,739 was covered by federal depository insurance or by collateral held by the University's agent in the University's name, and $4,923,844 was uninsured and uncollateralized.

North Carolina General Statutes 147-69.1(c), applicable to the state's General Fund and 147-69.2, applicable to institutional trust funds, authorize the State Treasurer to invest in the following: obligations of or fully guaranteed by the United States; obligations of certain federal agencies; repurchase agreements; obligations of the State of North Carolina; time deposits of specified institutions; prime quality commercial paper, asset-backed securities with specified ratings. General Statute 147-69.1(c) also authorizes the following: specified bills of exchange or time drafts and corporate bonds and notes with specified ratings. General Statue 147-69.2 also authorizes the following: general obligations of other states; general obligations of North Carolina local governments; and obligations of certain entities with specified ratings.

The financial statements and disclosures for the State Treasurer's short-term Investment Pool are included in the State of North Carolina's Comprehensive Annual Financial Report. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's internet home page http://www.osc.state.nc.us/ and clicking on "Financial Reports", or by calling the state controller's financial reporting section at (919) 981-5454.

B. Investments

The University is authorized by The University of North Carolina Board of Governors pursuant to General Statute 116-36.2 to invest its special funds and funds received for services rendered by health care professionals pursuant to General Statute 116-36.1(h) in the same manner as the State Treasurer is required to invest, as previously discussed.

In accordance with the bond resolutions, bond proceeds and debt service funds are invested in obligations that will by their terms mature on or before the date funds are expected to be required for expenditure or withdrawal.

General Statute 116-36(e) provides that the trustees of the Endowment Fund shall be responsible for the prudent investment of the Endowment Fund in the exercise of their sound discretion, without regard to any statute or rule of law relating to the investment of funds by fiduciaries but in compliance with any lawful condition placed by the donor upon that part of the Endowment Fund to be invested.

Investments of the University's component units, the UNC-CH Foundation, the Investment Fund, the System Fund, the Management Company, the Business School Foundation, the Social Work Foundation and the Law Foundation are subject to General Statute 36B *"Uniform Management of Institutional Funds Act"* (UMIFA) and any requirements placed on them by contract or donor agreements.

Investments of various funds may be pooled unless prohibited by statute or by terms of the gift or contract. The University utilizes investment pools to manage investments and distribute investment income. The University utilizes the following investment pools:

Temporary Investment Pool (Temporary Pool) - This is a fixed income portfolio managed by UNC Management Co., Inc. (Management Company) and Tanglewood Asset Management LLC. It operates in conjunction with the University's Bank of America disbursing account for all special funds, funds received for services rendered by health care professionals and endowment revenue funds (internal portion) and funds of affiliated foundations (external portion). Because of the participation in the Temporary Pool by affiliated foundations, it is considered a governmental external investment pool. The external portion of the Temporary Pool is presented in the accompanying financial statements as Funds Held in Trust for Pool Participants. The Temporary Pool is not registered with the SEC and the University has not provided legally binding guarantees during the period to support the value of the pool's investments. There are no involuntary participants in the Temporary Pool.

The Northern Trust Company is the custodian for the Temporary Pool and provides the University's director of accounting services with monthly statements defining income and market value information. Investments of the Temporary Pool are highly liquid and generally include U.S. government securities, collateralized mortgage obligations, corporate bonds, mutual funds and money market funds. The University has elected to invest a portion of the Temporary Pool assets in the University's Investment Fund.

Through written request to accounting services, participants may purchase and sell shares in the Temporary Pool at a fixed value of $1 per share. Generally, the purchase and sale of participation shares occur only at the beginning of the month. Income distribution is determined each quarter by multiplying the distribution rate by the average of the invested fund balance. Statements are sent to each participating account or group of accounts on a quarterly basis reflecting the participants' balance and income distribution. The rate earned by an account is dependent upon its account classification and investable fund balance. The rates are set in coordination between the Management Company and the vice chancellor for finance and administration.

UNC-CH Foundation Investment Fund Inc. (Investment Fund) - This is a North Carolina nonprofit corporation exempt from income tax pursuant to Section 501(c)3. It began operations in January 1997 by the University and is classified as a governmental external investment pool. The pool is utilized to manage the investments for charitable, nonprofit foundations, associations, trusts, endowments and funds that are organized and operated primarily to support the University. The University's Endowment, the UNC-CH Foundation, the Business School Foundation, the Social Work Foundation, and the Law Foundation are participants in the Investment Fund and are included in the University's reporting entity (internal portion). Other affiliated organizations (external portion) in the Investment Fund are not included in the University's reporting entity. Fund ownership of the University's Investment Fund is measured using the unit value method. Under this method, each participant's investment balance is determined on a market value basis. The external portion of the Investment Fund is presented in the accompanying financial statements as Funds Held in Trust for Pool Participants.

The Investment Fund is not registered with the SEC and is not subject to any formal oversight other than that provided by the Investment Fund Board of Directors (See Note 1 A).

The Northern Trust Company is the custodian for the Investment Fund and provides the University with monthly statements defining income and market value information. The Investment Fund uses a unit basis to determine each participant's market value and to distribute the Fund's earnings according to the Fund's spending policy. There are no involuntary participants in the Investment Fund pool. The University has not provided or obtained any legally binding guarantees during the period to support the value for the pool's investments. The audited financial statements for the Investment Fund pool may be obtained from the University Controller's Office, Campus Box 1270, Chapel Hill, NC 27599-1270, or by calling (919) 962-1370.

UNC Investment Fund, LLC (System Fund) - This is a limited liability company organized under the laws of the State of North Carolina. It was established in

December 2002 by the University and is classified as a governmental external investment pool. The pool is utilized to manage the investments for The University of North Carolina, its constituent institutions, and affiliates of the constituent institutions. This includes charitable, nonprofit foundations, associations, trusts, endowments and funds that are organized and operated primarily to support these institutions. The Investment Fund, with an approximately 97% membership interest as of June 30, 2003, is a predominant member of the System Fund. The University's reporting entity portion of the Investment Fund is characterized as the internal portion. Other affiliated organizations in the Investment Fund in addition to other members of the System Fund not included in the University's reporting entity are characterized as the external portion. The external portion of the System Fund is presented in the accompanying financial statements as Funds Held in Trust for Pool Participants. Membership interests of the System Fund are measured using the unit value method. Under this method, each member's investment balance is determined on a market value basis.

The System Fund is not registered with the SEC and is not subject to any formal oversight other than that provided by the Members and the Management Company (See Note 1 A). Effective January 1, 2003, the Management Company entered into an investment management services agreement with the System Fund and will provide investment management and administrative services.

The Northern Trust Company is the custodian for the System Fund and provides the University with monthly statements defining income and market value information. The System Fund uses a unit basis to determine each member's market value and to distribute the Fund's earnings. There are no involuntary participants in the System Fund pool. The University has not provided or obtained any legally binding guarantees during the period to support the value for the pool's investments. The audited financial statements for the System Fund pool may be obtained from the University Controller's Office, Campus Box 1270, Chapel Hill, NC 27599-1270, or by calling (919) 962-1370.

Credit Risk Categories - The University's investments (pooled and non-pooled) are categorized below to give an indication of the level of risk assumed by the entity at year-end. The credit risk categories are concerned with custodial credit risk, which is the risk that a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party if the counterparty to the investment transaction fails. There are three categories of credit risk. Category 1 includes investments that are insured or registered or for which the securities are held by the University or its agent in the University's name. Category 2 includes uninsured and unregistered investments for which the securities are held by counterparty's trust department or agent in the University's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the broker or dealer, or by counterparty's trust department or agent but not in the University's name.

A summary of the University's investments at June 30, 2003 is presented below.

TEMPORARY POOL INVESTMENTS

	Fair Value			
	Risk Category			
	1	2	3	Total
Categorized Investments:				
U.S. Government Securities	$41,562,034	$0	$0	$41,562,034
Collateralized Mortgage Obligations	53,172,386			53,172,386
State and Municipal Securities	4,330,691			4,330,691
Corporate Bonds	23,836,009			23,836,009
Corporate Stock	30,000			30,000
Total Categorized Investments	$122,931,120	$0	$0	$122,931,120
Investments Not Categorized:				
Investments Held by Broker-Dealers				
Under Reverse Repurchase Agreements:				
U.S. Government Securities				$84,126,559
Certificates of Deposit				1,000,000
Money Market Funds				7,422,071
Mutual Funds				20,827,220
Total Investments Not Categorized				$113,375,850
Total Temporary Pool Investments (a)				$236,306,970

(a) The Temporary Pool also has $29,983,646 of equity in the Investment Fund categorized below.

INVESTMENT FUND POOL INVESTMENTS

The Investment Fund consists of an approximately 97% membership interest in the System Fund categorized below.

SYSTEM FUND POOL INVESTMENTS

	Fair Value			
	Risk Category			
	1	2	3	Total
Categorized Investments:				
U.S. Government Securities	$2,173,104	$0	$0	$2,173,104
Collateralized Mortgage Obligations	4,497,979			4,497,979
Corporate Bonds	12,137,915			12,137,915
Corporate Stocks	33,651,924			33,651,924
International Bonds - Corporate	5,000,000			5,000,000
International Stocks	2,884,439			2,884,439
Total Categorized Investments	$60,345,361	$0	$0	$60,345,361
Investments Not Categorized:				
Investments Held by Broker-Dealers				
Under Reverse Repurchase Agreements:				
U.S. Government Securities				$24,326,240
Money Market Funds				3,668,659
Mutual Funds				394,394,266
Limited Partnerships				474,402,803
Total Investments Not Categorized				$896,791,968
Total System Fund Pool Investments				$957,137,329

NON POOLED INVESTMENTS

	Fair Value Risk Category 1	2	3	Total
Categorized Investments:				
U.S. Government Securities	$ 3,723,478	$768,911	$0	$4,492,389
Collateralized Mortgage Obligations	141,612			141,612
State and Municipal Securities	163,999			163,999
Corporate Bonds	7,621,474			7,621,474
Corporate Stocks	13,058,815	722,273		13,781,088
Total Categorized Investments	$24,709,378	$1,491,184	$0	$26,200,562
Investments Not Categorized:				
Money Market Funds				$35,235,582
Mutual Funds				43,287,131
Real Estate				15,956,225
Other Investments				7,351,672
Total Investments Not Categorized				$101,830,610
Total Non Pooled Investments				$128,031,172

TOTAL INVESTMENTS

	Fair Value Risk Category 1	2	3	Total
Total Categorized Investments	$207,985,859	$1,491,184	$0	$209,477,043
Total Investments Not Categorized				1,111,998,429
Total Investments				$1,321,475,472

Since a separate annual financial report of the Temporary Investment Pool has not and is not planned to be issued, the following additional disclosures are being provided in the University's financial statements.

The Temporary Investment Pool's Statement of Net Assets and Statement of Operations and Changes in Net Assets as of and for the period ended June 30, 2003 are as follows:

STATEMENT OF NET ASSETS
JUNE 30, 2003

Assets:	
State Treasurer Investment Fund	$112,000,000
Accrued Investment Income	2,200,631
Investment Fund Equity	29,983,646
Investments	236,306,970
Total Assets	$380,491,247
Liabilities:	
Obligations Under Reverse Repurchase Agreements	$82,285,000
Deferred Income	1,441,185
Total Liabilities	$ 83,726,185
Net Assets:	
Internal Portion	$159,036,397
External Portion	137,728,665
Total Net Assets	$296,765,062
Total Liabilities and Net Assets	$380,491,247

STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS
FOR THE FISCAL YEAR ENDED JUNE 30, 2003

Increase in Net Assets From Operations:	
Revenues:	
Investment Income	$17,709,598
Expenses:	
Investment Management	338,216
Net Increase in Net Assets Resulting from Operations	$17,371,382
Distributions to Participants:	
Distributions Paid and Payable	17,371,382
Share Transactions:	
Net Share Purchases	35,235,074
Total Increase in Net Assets	$35,235,074
Net Assets:	
Beginning of Year	261,529,988
End of Year	$296,765,062

The major investment classifications of the Temporary Pool had the following attributes at June 30, 2003:

Investment Classification	Fair Value	Principal Amount	Yield to Maturity	Range of Maturities
U.S. Government Securities:	$41,562,034	$39,572,905	1.2% - 7.0%	2005 - 2030
Collateralized Mortgage Obligations	53,172,386	52,806,965	1.4% - 19.0%	2005 - 2033
State and Municipal Securities	4,330,691	3,918,505	2.3%	2009
Corporate Bonds	23,836,009	22,994,878	1.7% - 5.5%	2004 - 2026
Corporate Stocks	30,000	30,000	N/A	N/A
Certificate of Deposit	1,000,000	1,000,000	3.5%	2004
Mutual Funds	20,827,220	19,195,083	N/A	N/A
Money Market Funds	7,422,071	7,422,071	0.9%	1 day
Reverse Repurchase Agreements	84,126,559	81,835,972	1.2% - 1.4%	1 - 15 days
Total Temporary Pool Investments	$236,306,970	$228,776,379		

C. Reverse Repurchase Agreements

Under the University's authority to purchase and sell securities, it has entered into fixed coupon reverse repurchase (reverse repurchase) agreements, that is, a sale of securities with a simultaneous agreement to repurchase them in the future at the same price plus a contract rate of interest. The fair value of the securities underlying reverse repurchase agreements normally exceeds the cash received, providing the dealers a margin against a decline in fair value of the securities. If the dealers default on their obligations to resell these securities to the University or provide securities or cash of equal value, the University would suffer an economic loss equal to the difference between the fair value plus accrued interest of the underlying securities and the agreement obligation, including accrued interest. This credit exposure at year end was $2,747,646.

At June 30, 2003, reverse repurchase agreements are both fixed term and open (on-demand) agreements. The amount and interest rate of the open agreements may be changed daily and either party may terminate the transaction at any time. In investing the proceeds of reverse repurchase agreements, the University's practice is for the term to maturity of the investment to be the same as the term of the reverse repurchase agreement. The University's investments in the underlying securities and the securities purchased with proceeds from the reverse repurchase agreements are in accordance with the statutory requirements as noted. The interest earnings and interest cost arising from reverse repurchase agreement transactions are reported at gross amounts on the accompanying financial statements.

D. Derivative and Similar Transactions

A derivative is a financial instrument created from, or whose value depends on (is derived from), the value of one or more underlying assets, reference rates, or indexes of asset values. These instruments may include forwards, futures, currency and interest rate swaps, options, floaters/inverse floaters and caps/floors/collars. Investment transactions similar to a derivative may include securitized assets, such as mortgage-backed securities and other asset-backed securities. As required by accounting principles generally accepted in the United States of America, the nature of derivative or similar transactions entered into by the University, and the reasons for entering into those transactions follow:

Mortgage-Backed Securities - The University invests in mortgage-backed securities issued by the Government National Mortgage Association (GNMA), an agency of the United States government, government-sponsored enterprises including the Federal Home Loan Mortgage Corporation (FHLMC) or the Federal National Mortgage Association (FNMA), and private trusts or corporations. The University invests in these securities to increase the yield and return on its investment portfolio given the available alternative investment opportunities.

The values of mortgage-backed securities are generally based on the cash flows from principal and interest receipts on the underlying mortgage pools. These securities may include mortgage pass-through securities and collateralized mortgage obligations (CMOs). Mortgage pass-through securities pay the holder of the security the principal and interest amounts received from the underlying pool of mortgages as these amounts are collected from the mortgage holders. In a CMO, the cash flows from principal and interest payments from one or more mortgage pass-through securities or a pool of mortgages may be reallocated to multiple security classes with different priority claims and payment streams (commonly referred to as tranches.) A holder of the CMO security thus chooses the class of security that best meet its risk and return objectives. Both pass-through securities and CMOs are subject to significant market risk due to fluctuations in interest rates, prepayment rates, and various liquidity factors related to their specific markets.

The mortgage pass-through securities issued by GNMA, FNMA, and FHLMC are classified by the University as U.S. government securities. The mortgage pools underlying the GNMA pass-through securities are backed by the full faith and credit of the U.S. government by the Federal Housing Administration (FHA), Veterans Administration (VA), and the Farmers Home Administration (FHA). The FNMA and FHLMC securities are collateralized by underlying pools of mortgages primarily issued by GNMA, FNMA or FHLMC that guarantee full and timely payment of principal and interest.

The CMOs held by the University include mortgage-backed securities issued by FNMA, FHLMC, certain trusts and private corporations (including Real Estate Mortgage Investment Conduit issuers). In addition, non-traditional mortgage pass-through securities, such "interest-only strips" and "principal-only strips," if held by the University, are classified as CMOs. The University held non-traditional pass-through securities during the year.

As of June 30, 2003, the University was holding $136,441,395 in mortgage-backed securities valued at fair value representing approximately 10.3% of its total investments. Of this amount, $57,811,977 represent investments in CMOs.

Other Asset-Backed Securities - The University invests in various asset-backed securities such as automobile loan securitizations, credit card securitizations, and home equity loans. The University invests in the various asset-backed securities to increase the yield and return on its investment portfolio given the available alternative investment opportunities.

The values of these other asset-backed securities are generally based on the cash flows to be received from the underlying pools of assets. Accordingly, these securities are subject to market risk due to fluctuations in interest rates, prepayment rates, and various liquidity factors related to their specific markets. The market risk is reduced by the University's preference to invest in the shorter average life securities.

These security holdings are subject to credit-related losses in the event of non-performance by the issuers or counterparties to these instruments. However, the University does not expect any issuers or counterparties to fail to meet their obligation given their high credit ratings. The assets that collateralize these securities, which could be liquidated at market values at the time of non-performance, reduce the credit risk.

As of June 30, 2003, the University was holding $11,220,025 in asset-backed securities valued at fair value representing approximately 0.9% of its total investments.

Futures - The University purchases and sells equity index futures and futures on domestic and foreign securities and currencies. The University uses the futures market to securitize excess cash holdings, to gain exposure to non-U.S. markets, to exploit foreign interest rate yield opportunities, to diversify its overall investment portfolio, to lower its transaction costs and to improve its liquidity.

Futures contracts are traded on margin on various futures and options exchanges. Since there is no direct cost in establishing any given futures position, the book value of these securities is recorded at $0. The margin amounts remitted by the University to the brokerage houses are reflected in the University's cash and cash equivalent or government securities holdings. Gains or losses from trading the futures are recognized in income when the futures positions are closed or liquidated. Unlike most securities investments, the losses on futures contracts can exceed their cost (of $0).

The market value of a futures contract is dependent on the value of its underlying cash market security or securities. Accordingly, the futures contracts held by the University are sensitive to changes in their respective foreign currency rates or security values. They are also sensitive to changes in the level of interest rates. The University trades futures on organized exchanges, which mitigates its credit risk of default by a counterparty.

As of June 30, 2003, the futures contracts held by the University had expiration dates not exceeding September 2003.

Options - The University purchases and sells options on futures of U.S. and foreign securities. All options are traded through domestic and foreign exchanges.

The University uses the options to hedge certain of its futures positions, to gain exposure to non-U.S. markets, to exploit foreign interest rate yield opportunities, and to further diversify its overall investment portfolio.

The University records the book values of long and short call and put option contracts at the option premium paid (if the option is purchased) or collected (if the option is written.) The University records the book value of the options in an investment account at an amount equal to the quantity of contracts purchased (sold) at the respective option premium price paid (collected.) When the option contract expires, or is repurchased or is exercised, the University records any resulting gain or loss in related income accounts. Unlike purchased options and most securities investments, losses on written options can exceed their cost.

During the year ending June 30, 2003, the option contracts held by the University vary with changes in the market price of their underlying futures contracts and accordingly also fluctuate with changes in their respective foreign currency rates or security values. The University's option contracts are traded on organized exchanges which mitigate its credit risk of default by a counterparty.

As of June 30, 2003, the University had no outstanding option transactions.

Indirect Derivative Holdings – The University identifies various external investment funds (mutual funds, external investment pools, and limited partnerships) that meet asset allocation and investment management objectives. The University invests in these funds to increase the yield and return on its investment portfolio given the available alternative investment opportunities and to diversify its asset holdings. Fund investments generally include equity and bond funds. Certain funds expose the University to significant amounts of market risk by trading or holding derivative instruments and by leveraging the securities in the fund.

The University limits the amount of funds managed by any single asset manager and also limits the amount of funds to be invested in particular security classes. The asset classes of the System Fund that utilized derivative securities for the fiscal year ending June 30, 2003 are summarized in the chart below. The amounts shown in the chart represent the market value of the System Fund's investment in the various asset classes and the market value and percent of holdings held in derivatives in those classifications. The University's reporting entity comprises 71.01% of the System Fund.

The market values reported for each asset class do not include accrued income, reverse repurchase liabilities, investments in the State Treasurer's Investment Fund, cash with a fiscal agent, accounts receivable, or accounts payable.

The UNC Investment Fund, LLC (System Fund) Indirect Derivative Analysis for Fiscal Year Ending June 30, 2003:

Asset Class	Total Market Value	% Invested Derivatives	Amount
Domestic Equity	$ 159,133,148	7.35 %	$11,702,497
International Equity	141,705,565	4.74 %	6,711,357
Global Equity	75,940,304	18.79 %	14,267,461
Private Equity	157,935,300	0.57 %	906,640
Absolute Return	100,896,577	4.24 %	4,274,249
Fixed Income			
Domestic Fixed Income	55,895,914	7.48 %	4,183,268
Enhanced Fixed Income	152,716,894	1.31 %	1,997,804
Real Estate	61,434,683	1.29 %	795,560
Energy	50,640,848	30.90 %	15,647,358
Total			$60,486,194
Total Market Value of Investments in the System Fund			$957,137,329
Total % of Market Value for Indirect Derivative Exposure			6.32 %

The market risk associated with these indirect derivative holdings by fund type follows:

Domestic Equity – From time-to-time domestic equity managers will utilize equity index futures, options on equity index futures, and specific stock options. These are used mainly to hedge their portfolio or to take advantage of an options mispricing on a security they own.

International Equity – International equity managers will utilize foreign equity index futures and options to hedge their exposure to their respective markets.

Global Equity – Global equity managers will utilize a wide range of currency, equity, and fixed income futures and options. These are used to gain exposure to specific markets in the most cost-effective and liquid manner possible.

Private Equity – By serving as substitutes for domestic and global common stocks, the role of these investments is to provide high real returns and control volatility. The private equity allocation is expected to be approximately one-half in traditional venture capital and one-half in buyout strategies.

Absolute Return – Absolute return managers utilize fixed income and equity futures both as a hedging tool and to gain exposure to specific markets.

Fixed Income – Fixed income funds utilize futures and options on global fixed income and currency markets. These vehicles are used purely to hedge exposure to a given market or to gain exposure to an illiquid market. Domestic and Enhanced are two subasset classes of this fund type.

Domestic Fixed Income focuses upon U.S. Treasury securities, quasi-government securities, and high-grade U.S. corporate bonds. Enhanced Fixed Income can include non-U.S. investments and non high-grade securities, and are generally intended to provide a higher total return than traditional fixed income.

Real Estate – Primarily serves as a hedge against high-unanticipated general price inflation, but is also a source of current income. Investments in this area include private portfolio investments, which focus on specific niche markets within the real estate sector or public Real Estate Investment Trust (REIT) investments, which provide a more liquid means of gaining exposure to the asset class.

Energy – Principally included to hedge against unanticipated inflation. These strategies include direct energy investments, energy security investments, commodity-linked notes and direct investments in commodity indices or the futures markets. The principal attraction of these investments is the lack of correlation with the balance of the portfolio.

The System Fund's holdings in indirect derivatives (i.e., derivatives held by external investment managers) are primarily used to decrease risk. This is because the indirect derivatives are used by the fund's hedge fund managers primarily to hedge underlying positions, or to gain exposure to specific markets in an efficient, inexpensive, liquid, and diversified manner. In the former case, risk is actually reduced by the use of derivatives because the derivative is directly offsetting market exposure. In the latter case, the derivatives are merely substituting for what would otherwise be a more traditional (individual security) array. Hence there would be no greater risk and often less risk than the traditional array that would exist in place of such derivatives. In limited cases, select managers are allowed to use derivatives to lever specific holdings or market positions. In aggregate, the fund's 6.32% exposure to indirect derivative holdings reflects a smaller degree of risk than there would be without such derivatives in the portfolio. The University considers the risk associated with these holdings to be prudent and within acceptable bounds.

NOTE 3
ENDOWMENT INVESTMENTS RETURN

Substantially all of the investments of the University's endowment funds are pooled in the Investment Fund. Investment return of the University's pooled endowment funds is predicated on the total return concept (yield plus appreciation). Annual distributions from the Investment Fund to the University's pooled endowment funds are based on an adopted spending policy. Under this policy, the prior year distribution is increased by the rate of inflation as measured by the Consumer Price Index (CPI). Each year's distribution, however, is subject to a minimum of 4% and a maximum of 7% of the pooled endowment fund's average market value for the previous year.

To the extent that the total return for the current year exceeds the distribution, the excess is added to principal. If current year earnings do not meet the distribution requirements, the University uses accumulated income and appreciation to make up the difference. At June 30, 2003, accumulated income and appreciation of $274,403,227 was available in the University's pooled endowment funds of which $243,771,348 was restricted to specific purposes.

NOTE 4
RECEIVABLES

Receivables at June 30, 2003 were as follows:

	Gross Receivables	Allowance for Doubtful Accounts	Net Receivables
Current Receivables:			
Students	$2,532,008		$2,532,008
Patients	69,359,847	($62,737,770)	6,622,077
Accounts	31,163,058		31,163,058
Intergovernmental	33,210,870		33,210,870
Pledges	15,949,393	(239,241)	15,710,152
Investment Earnings	3,910,475		3,910,475
Interest on Loans	671,939		671,939
Total Current Receivables	$156,797,590	($62,977,011)	$93,820,579
Noncurrent Receivables:			
Pledges	$27,844,676	($417,670)	$27,427,006
Notes Receivable - Current			
Federal Loan Programs	$2,515,106	($254,202)	$2,260,904
Institutional Student Loan Programs	485,604	(10,625)	474,979
Other Notes Receivable	1,160,000		1,160,000
Total Notes Receivable Current	$4,160,710	($264,827)	$3,895,883
Notes Receivable - Non-current:			
Federal Loan Programs	$23,197,541	($2,355,707)	$20,841,834
Institutional Student Loan Programs	4,470,682	(100,519)	4,370,163
Total Notes Receivable Non-current	$27,668,223	($2,456,226)	$25,211,997

Pledges are receivable over varying time periods ranging from one to 10 years, and have been discounted based on a projected interest rate of 3.58% for the outstanding periods, and allowances are provided for the amounts estimated to be uncollectible.

Scheduled receipts, the discounted amount under these pledge commitments, and allowances for uncollectible pledges are as follows:

Fiscal Year	Amount
2004	$15,975,771
2005	12,059,174
2006	10,449,751
2007	4,035,848
2008	1,865,829
2009-2012	2,502,317
Total Pledge Receipts Expected	46,888,690
Discount Amount Representing Interest (3.58% Rate of Interest)	(3,094,621)
Present Value of Pledge Receipts Expected	43,794,069
Less Allowance for Uncollectible	(656,911)
Pledges Receivable	$43,137,158

NOTE 5
CAPITAL ASSETS

A summary of changes in the capital assets for the year ended June 30, 2003 is presented as follows:

	Balance July 1, 2002	Adjustments	Increases	Decreases	Balance June 30, 2003
Capital Assets, Non-Depreciable:					
Land	$22,093,860	$2,372,320	$1,145,785		$25,611,965
Art, Literature, and Artifacts	52,371,413		2,097,314	$423	54,468,304
Construction in Progress	225,022,791	(89,847,692)	93,807,851	2,024,870	226,958,080
Intangible assets	1,000,000				1,000,000
Total Capital Assets, Non-Depreciable	300,488,064	(87,475,372)	97,050,950	2,025,293	308,038,349
Capital Assets, Depreciable:					
Buildings	823,740,406	52,191,980	27,613,285		903,545,671
Machinery and Equipment	193,199,053		25,091,725	12,779,657	205,511,121
General Infrastructure	285,337,256	35,283,392	13,910,544		334,531,192
Total Capital Assets, Depreciable	1,302,276,715	87,475,372	66,615,554	12,779,657	1,443,587,984
Less Accumulated Depreciation/ Amortization for:					
Buildings	332,417,864		24,674,664		357,092,528
Machinery and Equipment	119,585,365		15,658,043	10,550,773	124,692,635
General Infrastructure	122,876,562		12,743,123		135,619,685
Total Accumulated Depreciation/Amortization	574,879,791		53,075,830	10,550,773	617,404,848
Total Capital Assets, Depreciable, net	727,396,924	87,475,372	13,539,724	2,228,884	826,183,136
Capital Assets, net	$1,027,884,988	$0	$110,590,674	$4,254,177	$1,134,221,485

NOTE 6
ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities at June 30, 2003 were as follows:

	Totals
Accounts Payable	$41,338,853
Accrued Payroll	19,181,776
Contract Retainage	6,425,301
Other	270,025
Total accounts payable and accrued liabilities	$67,215,955

NOTE 7
SHORT-TERM DEBT

Short-term debt activity for the year ended June 30, 2003 is as follows:

	Balance July 1, 2002	Issued	Redeemed	Balance June 30, 2003
Commercial Paper	$1,000,000	$18,000,000	$0	$19,000,000

The July 1, 2002, balance of $1,000,000 issued from the University of North Carolina General Revenue Bonds, Series 2002A had a maturity date of November 12, 2002, and has been extended to November 2003. The $18,000,000 issued during the fiscal year also matures in November 2003. These new proceeds were used to provide interim financing for the construction of capital projects.

NOTE 8
LONG-TERM LIABILITIES

A. Changes in Long-term Liabilities

A summary of changes in the long-term liabilities for the year ended June 30, 2003 is presented as follows:

	Balance July 1, 2002	Additions	Reductions	Balance June 30, 2003	Current Portion
Notes, Bonds and Capital Leases Payable					
Notes Payable	$3,800,229 (A)	$35,532,276 (B)		$39,332,505	$4,326,788
Bonds Payable	442,430,000		$13,570,000	428,860,000	117,201,497
Add/Deduct Premium/ Discount	(55,218,108)	4,028,023	1,190,835	(52,380,920)	
Deduct Deferred Charge on Refunding	(3,257,254)		(325,725)	(2,931,529)	
Total Bonds Payable	383,954,638	4,028,023	14,435,110	373,547,551	117,201,497
Capital Leases Payable	605,700	795,180	474,252	926,628	424,537
Total Notes, Bonds, and Capital Leases Payable	388,360,567	40,355,479	14,909,362	413,806,684	121,952,822
Compensated Absences	52,475,420	59,006,480	38,893,586	72,588,314	4,268,038
Annuity Payable	5,943,224	2,405,224	1,127,622	7,220,826	766,702
Total Long-term Liabilities	$446,779,211	$101,767,183	$54,930,570	$493,615,824	$126,987,562

Additional information regarding capital lease obligations is included in Note 9.

(A)The July 1, 2002 balance of $3,800,229 for the Promisory note with Wachovia Bank had a maturity date of January 7, 2003 and has been extended to December 9, 2003.

(B)On December 20, 2002, the UNC-CH Foundation (which is part of the University's financial reporting entity) signed a promissory note with Wachovia Bank in the amount of $318,960. On January 8, 2003, a second advance was received in the amount of $213,316 for a total note amount of $532,276. The final maturity date is December 31, 2003. The proceeds were used to acquire property.

The University plans to repay the note maturing on December 31, 2003, after the state purchases the property using the state general obligation bond funding.

On April 7, 2003, the UNC-CH Foundation (which is part of the University's financial reporting entity) entered into a loan agreement with Bank of America in the amount of $35,000,000. The final maturity date is April 1, 2005. The proceeds will be used to finance the costs of acquisition, construction, and equipping a student housing facility for students and their families.

The student housing facility will be purchased by the University upon completion at which time the UNC-CH Foundation will repay the loan. The University plans to finance the purchase with other long term University financing.

B. Bonds Payable

The University was indebted for bonds payable for the purposes shown in the following table:

Purpose	Series	Interest Rate/ Ranges	Final Maturity Date	Original Amount of Issue plus Capital Appreciation	Principal Paid Through 6/30/2003	Discount on Capital Appreciation Bonds	Principal Outstanding 6/30/2003
Housing System							
	1997A	4.500%-5.100%	1-Nov-17	$9,170,000	$1,315,000		$7,855,000
	1997B	4.000%-5.000%	1-Nov-17	7,210,000	810,000		6,400,000
Total Housing System				16,380,000	2,125,000		14,255,000
Utility System							
	1997	5.250%-5.500%	1-Aug-21	84,135,000	0	$(43,009,099)	41,125,901
	1992	3.000%-6.000%	1-Aug-07	3,490,000	3,490,000		0
Total Utility System				87,625,000	3,490,000	(43,009,099)	41,125,901
Parking System							
	1997A	4.350%-5.700%	15-May-27	11,750,000	840,000		10,910,000
	1997B	3.900%-5.150%	15-May-09	8,245,000	3,495,000		4,750,000
Total Parking System				19,995,000	4,335,000		15,660,000
General Revenue 2001							
	2001A	2.900%-5.125%	1-Dec-25	89,930,000	3,585,000		86,345,000
	2001B	variable	1-Dec-25	54,970,000	3,015,000		51,955,000
	2001C	variable	1-Dec-25	54,970,000	3,015,000		51,955,000
Total General Revenue 2001				199,870,000	9,615,000		190,255,000
General Revenue 2002 Series	2002B	3.500%-5.000%	1-Dec-11	66,555,000	1,595,000		64,960,000
Student Union	2000	4.550%-5.659%	1-Jun-22	12,465,000	690,000		11,775,000
Student Recreation Center	1997	3.900%-5.000%	1-Jun-11	3,545,000	765,000		2,780,000
U.S. EPA Project, Series 1991	1991	8.250%-9.050%	15-Feb-15	58,125,000	13,990,000	(14,064,847)	30,070,153
U.S. EPA Project, Series 1996	1996	6.72%	15-Feb-06	2,400,000	1,495,000		905,000
Total Bonds Payable (principal only)				$466,960,000	$38,100,000	$(57,073,946)	371,786,054
Less: Unamortized Loss on Refunding							(2,931,528)
Less: Unamortized Discount							0
Plus: Unamortized Premium							4,693,025
Total Bonds Payable							$373,547,551

C. Demand Bonds

Included in bonds payable are two variable rate demand bond issues. Demand bonds are securities that contain a "put" feature that allows bondholders to demand payment before the maturity of the debt upon proper notice of the University's remarketing or paying agents.

Regarding the following demand bonds, the University has not entered into legal agreements, which would convert the demand bonds not successfully remarketed into another form of long-term debt.

General Revenue, Series 2001B and 2001C:

In 2001 the University issued two series of variable rate demand bonds in the amount of $54,970,000 (2001B) and $54,970,000 (2001C) that each have a final maturity date of December 1, 2025, and are repaid from available funds. Available funds are defined as any Unrestricted Net Assets remaining after satisfying obligations of the University under trust indentures, trust agreements or bond resolutions (specific revenue bonds), but excluding state appropriations, tuition, restricted gifts and certain special facilities revenues. The bonds are subject to mandatory sinking fund redemption that began on December 1, 2001. The proceeds of these issuances were used to provide funds to refund in advance of their maturity the following issues: Ambulatory Care Clinic, Series 1990; Athletic Facilities, Series 1998; Carolina Inn, Series 1994; School of Dentistry, Series 1995; Housing System, Series 2000; Kenan Stadium, Series 1996; and Parking System, Series 1997C. While bearing interest at a weekly rate, the bonds are subject to purchase on demand with seven days notice and delivery to the University's remarketing agents, Lehman Brothers, Inc (2001B) and UBS Financial Services, Inc (2001C).

Under an irrevocable line of credit issued by The Toronto-Dominion Bank and JP Morgan Chase Bank, the University is entitled to draw up to $54,970,000 from each bank or a maximum aggregate of $109,940,000 which the University would apply to meet its obligation to pay the principal, and, while the bonds are bearing interest at the daily or weekly rate, accrued interest on bonds delivered for purchase. The University is required to pay a quarterly commitment fee for the line of credit of .08% per annum of the amount of bonds then currently outstanding.

Under the letter of credit agreement, the University has promised to repay loans that represent purchase drawings in equal semi-annual payments after termination of the letter of credit. Interest at the rate of prime plus 1.0% (prime plus 2.0% after 60 days) is payable quarterly and upon draw repayment. At June 30, 2003, no purchase drawings had been made under the letter of credit.

The letter of credit terminates on February 4, 2004.

In order to protect against the risk of interest rate changes, effective October 3, 2000, the University entered into an interest rate swap contract agreement with Lehman Brothers Special Financing, Inc. (Lehman Brothers) related to $22,000,000 of The University of North Carolina at Chapel Hill Variable Rate Housing System Revenue Bonds, Series 2000. This series of bonds was refunded in its entirety by the issuance of the University's Variable Rate General Revenue Bonds, Series 2001B, and the interest swap agreement was amended to reflect the refunding.

Under this amended agreement, Lehman Brothers pays the University interest on the notational amount based on the Bond Market Association (BMA) Municipal Bond Index on a quarterly basis. For the fiscal year ended June 30, 2003, Lehman Brothers paid the University $285,962 under this agreement. On a semiannual basis, the University pays Lehman Brothers interest at the fixed rate of 5.24%. For the fiscal year ended June 30, 2003, the University paid Lehman Brothers $1,147,167 under this agreement. The notional amount of the swap reduces annually; the reductions began in November 2002 and end in November 2025. The swap agreement matures November 1, 2025. As of June 30, 2003, rates were as follows:

	Terms	Rates (%)
Fixed payment to Lehman	Fixed	5.24
Variable payment from Lehman	BMA	1.13
Net interest rate swap payments		4.11
Variable rate bond coupon payments		1.00
Synthetic interest rate on bonds		5.11

As of June 30, 2003, the swap had a negative fair value of $5,505,094. The fair value was developed by Lehman Brothers. Their method calculates the future net settlement payments required by the swap assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for London Interbank Offered Rate (LIBOR) due on the date of each future net settlement on the swap.

As of June 30, 2003, the University was not exposed to credit risk because the swap had a negative fair value. However, should interest rates change and the fair value of the swap becomes positive, the University would be exposed to credit risk in the amount of the derivative's positive fair value. Should the swap have a positive fair value of more than $1,000,000, at that point Lehman would be required to collateralize 103% of their exposure. Lehman Brothers Holdings, guarantor of Lehman Brothers Special Financing, Inc., was rated A2 by Moody's Investor's Service, A by Standard and Poor's Corporation, and A+ by Fitch Ratings.

The University receives the BMA Index from Lehman Brothers and pays a floating rate to its bondholders set by the remarketing agent. The University incurs basis risk when its bonds begin to trade at a yield above the BMA. Basis risk also exists since swap payments are made quarterly while bond payments are made monthly. With the alternative tax structure of the swap, a change in tax law would trigger the swap being converted from a BMA swap to a percentage of LIBOR swap. This would introduce basis risk. If the relationship of the University's bonds trade to a percentage of LIBOR greater than 65%, the University will experience an increase in debt service above the fixed rate on the swap.

The derivative contract uses the International Swap Dealers Association Master Agreement, which includes standard termination events, such as failure to pay and bankruptcy. Termination could result in the University being required to make an unanticipated termination payment. The swap terminates if the University or Lehman Brothers fails to perform under terms of the contract.

As rates vary, variable rate bond interest payments and net swap payments will vary. Using rates as of June 30, 2003, debt service requirements of the variable rate debt and net swap payments, assuming current interest rates remain the same for the term, were as follows.

General Revenue Bonds
Series 2001B

Fiscal Year Ending June 30	Principal	Interest	Interest Rate Swaps, Net*	Total
2004	$1,855,000	$510,275	$890,740	$3,256,015
2005	1,925,000	491,375	881,287	3,297,662
2006	2,060,000	471,450	871,423	3,402,873
2007	2,140,000	450,450	861,148	3,451,598
2008	2,175,000	428,875	850,359	3,454,234
2009-2013	12,590,000	1,789,600	4,064,687	18,444,287
2014-2018	11,635,000	1,168,875	3,368,556	16,172,431
2019-2023	10,710,000	599,150	2,086,338	13,395,488
2024-2026	6,865,000	105,125	375,758	7,345,883
Total	$51,955,000	$6,015,175	$14,250,296	$72,220,471

* Computed using (5.24% - 1.13%) x ($22,000,000 – annual reduction)

D. Capital Appreciation Bonds

The University's Series 1997 Utility System and the Series 1991 U. S. Environmental Protection Agency Project bond issues include capital appreciation bonds with an original issue amount of $30,379,142 and $3,828,921, respectively. These bonds are recorded in the amounts of $41,125,901 ($84,135,000 ultimate maturity less $43,009,099 discount) and $11,210,153, ($25,275,000 ultimate maturity less $14,064,847 discount) respectively, which are the accreted values at June 30, 2003. These bonds mature in the years from 2010 to 2021.

E. Annual Requirements

The annual requirements to pay principal and interest on the long-term obligations at June 30, 2003 are as follows:

Annual Requirements

	Bonds Payable		Notes Payable	
Fiscal Year	Principal	Interest	Principal	Interest
2004	$17,080,000	$9,349,585	$4,332,505	$562,203
2005	17,930,000	8,841,269	35,000,000	394,110
2006	18,880,000	8,287,613		
2007	19,635,000	7,719,403		
2008	20,610,000	7,129,841		
2009-2013	113,695,000	27,679,907		
2014-2018	101,725,000	19,194,172		
2019-2023	85,465,000	10,363,010		
2024-2028	33,840,000	1,945,252		
Total Requirements	$428,860,000	$100,510,052	$39,332,505	$956,313

Interest on the variable rate General Revenue Bonds 2001B revenue bonds is calculated at 1.000% at June 30, 2003.
Interest on the variable rate General Revenue Bonds 2001C revenue bonds is calculated at 0.900% at June 30, 2003.

For UNC-CH General Revenue Bonds, Series 2001 B and 2001 C, interest rates change weekly.

F. Bond Defeasance

The University has extinguished long-term debt obligations by the issuance of new long-term debt instruments as follows:

Utilities System: On May 7, 2002, the University defeased $69,895,000 of outstanding Utility System Revenue Bonds, Series 1993. Securities were placed in an irrevocable trust with an escrow agent to provide for all future debt service payments on the defeased bonds. The trust account assets and the liability for the defeased bonds are not included in the University's Statement of Net Assets. At June 30, 2003, the outstanding balance of the defeased Utility System Revenue Bonds was $64,445,000.

Dining System: On February 7, 2001 the University defeased $13,205,000 of outstanding Dining System Revenue Bonds, Series 1997. Securities were deposited into an irrevocable trust with an escrow agent to provide for all future debt service payments on the defeased bonds. The trust assets and the liability for the defeased bonds are not included in the University's Statement of Net Assets. At June 30, 2003 the outstanding balance of the defeased Dining System bonds was $11,595,000.

Dormitory System: On December 1, 1999, the University defeased $1,225,000 of outstanding Dormitory System Revenue Bonds, Series E, F & G (1963). Securities were placed in an irrevocable trust with an escrow agent to provide for all future debt service payments on the defeased bonds. For financial reporting purposes, the trust account assets and the liability for the defeased bonds are not included in the University's Statement of Net Assets. At June 30, 2003, the outstanding balance was $439,000 for the defeased outstanding Dormitory System Revenue Bonds, Series F and Series G (1963).

Student Apartments: On December 1, 1999, the University defeased $128,000 of outstanding Student Apartment Revenue Bonds, Series A (1961). Securities were placed in an irrevocable trust with an escrow agent to provide for all future debt service payments on the defeased bonds. For financial reporting purposes, the trust account assets and the liability for the defeased bonds are not included in the University's Statement of Net Assets. At June 30, 2003, the outstanding balance was $0 for the defeased outstanding Student Apartment Revenue Bonds, Series A (1961).

Student Union: On December 1, 1999, the University defeased $620,000 of outstanding Student Union Revenue Bonds, Series 1967. Securities were placed in an irrevocable trust with an escrow agent to provide for all future debt service payments on the defeased bonds. For financial reporting purposes, the trust account assets and the liability for the defeased bonds are not included in the University's Statement of Net Assets. At June 30, 2003, the outstanding balance was $405,000 for the defeased outstanding Student Union Revenue Bonds, Series 1967.

Utility System: On October 30, 1997, the University defeased $19,337,000 of outstanding Utility System Revenue Bonds, Series 1992. Securities were deposited into an irrevocable trust with an escrow agent to provide for all future debt service payments on the defeased bonds. The trust assets and the liability for the defeased bonds are not included in the University's Statement of Net Assets. At June 30, 2003, the outstanding balance of the defeased Utility System bonds was $0.

NOTE 9
LEASE OBLIGATIONS

A. Capital Lease Obligations

Capital lease obligations relating to medical and research equipment are recorded at the present value of the minimum lease payments. Future minimum lease payments under capital lease obligations consist of the following at June 30, 2003:

Fiscal Year	Amount
2004	$465,649
2005	514,967
2006	10,038
2007	0
Total Minimum Lease Payments	990,654
Amount Representing Interest (4.0% - 14.9% Rate of Interest)	64,026
Present Value of Future Lease Payments	$926,628

Machinery and equipment acquired under capital leases amounted to $2,072,142 at June 30, 2003.

B. Operating Lease Obligations

Future minimum lease payments under non-cancelable operating leases consist of the following at June 30, 2003:

Fiscal Year	Amount
2004	$5,544,826
2005	4,596,029
2006	3,437,730
2007	1,363,553
2008	675,034
Total Minimum Lease Payments	$15,617,172

Rental expense for all operating leases during the year was $11,856,976.

C. Other Lease Obligations

The University of North Carolina at Chapel Hill Foundation, Inc. (UNC-CH Foundation) issued certificates of participation to provide for construction of Alumni Facilities. The University constructed the facilities as an agent for the UNC-CH Foundation. In October 1989, the University entered into a 20-year lease agreement with the UNC-CH Foundation and simultaneously entered into a sublease agreement with the General Alumni Association, an affiliated organization, for the same time period for the use of the alumni facilities.

Payments under the terms of the lease are a limited obligation of the University, payable solely from and secured by the annual rental income derived from the sublease of the alumni facilities. The University has no other obligations for repayment of the certificates of participation; therefore, the certificates are not reported as a liability in the accompanying financial statements. As of June 30, 2003, the aggregate principal amount of the certificates was $9,950,000.

If the University complies with all the terms of the lease agreement, title to the alumni facilities will be conveyed to the University.

NOTE 10
REVENUES

A summary of eliminations and allowances by revenue classification and revenues pledged as security for revenue bonds is presented as follows:

	Gross Revenues	Internal Sales Eliminations	Less Scholarship Discounts	Less Allowance for Uncollectibles	Less Indigent Care and Contractual Adjustments	Net Revenues	Net Revenues Pledged as Security for Debt
Operating revenues:							
Student Tuition and Fees	$178,483,678		$31,522,261			$146,961,417	
Patient Service	336,493,199			$10,314,442	$194,922,706	131,256,051	
Sales and Services:							
Residential Life	24,252,104		4,314,574			19,937,530	$18,464,277 (A)
Dining	16,813,899		238,307			16,575,592	
Student Union Services	2,067,743		406,238			1,661,505	
Health, Physical Education and Recreation Services	14,050,244		2,809,535			11,240,709	11,240,709 (B)
Bookstore	32,075,507	$6,072,533				26,002,974	
Parking	14,287,592					14,287,592	14,287,592 (C)
Athletic	33,187,532		454,184			32,733,348	
Utilities	72,725,243	55,258,490				17,466,753	17,466,753 (D)
Other Professional Income	69,027,595					69,027,595	
Other	136,560,842	83,388,525				53,172,317	4,734,172 (E)
Total Sales and Services	$415,048,301	$144,719,548	$8,222,838			$262,105,915	$66,193,503
Non-operating Noncapital Gifts	$64,639,128			3,751,532*		$60,887,596	
Capital Gifts, Net	$7,552,718					$7,552,718	

(A) Housing System Revenue Bonds, Series 1997 A & B

(B) Student Fee Revenue Bonds. Series 1997 & 2000

(C) Parking System Revenue Bonds, Series 1997 A & B

(D) Utility System Revenue Bonds, Series 1992 & 1997

(E) US EPA Project, Series 1991 & 1996

* Includes $3,094,621 PV discount on pledges receivable

NOTE 11
OPERATING EXPENSES BY FUNCTION

The University's operating expenses by functional classification are presented as follows:

	Salaries and Benefits	Supplies and Materials	Services	Scholarships and Fellowships	Utilities	Depreciation	Total
Instruction	$398,172,611	$27,181,907	$105,734,309		$34,423		$531,123,250
Research	153,709,889	39,445,019	54,254,901		24,276		247,434,085
Public Service	27,232,590	1,454,851	46,689,814		32,655		75,409,910
Academic Support	45,488,859	13,059,982	12,339,383				70,888,224
Student Services	9,786,765	1,056,088	8,645,353		2,530		19,490,736
Institutional Support	41,330,738	4,473,044	17,595,079		61,643		63,460,504
Operations and Maintenance of Plant	27,529,762	7,581,750	11,661,547		39,678,363		86,451,422
Student Financial Aid				$45,618,092			45,618,092
Auxiliary Enterprises	173,014,263	52,733,631	107,536,187		17,480,455		350,764,536
Depreciation						$53,075,830	53,075,830
Total Operating Expenses	$876,265,477	$146,986,272	$364,456,573	$45,618,092	$57,314,345	$53,075,830	$1,543,716,589

NOTE 12
PENSION PLANS

A. Retirement Plans

Each permanent full-time employee, as a condition of employment, is a member of either the Teachers' and State Employees' Retirement System or the Optional Retirement Program. Eligible employees can elect to participate in the Optional Retirement Program at the time of employment; otherwise they are automatically enrolled in the Teacher's and State Employees' Retirement System.

The Teachers' and State Employees' Retirement System is a cost sharing multiple-employer defined benefit pension plan established by the state to provide pension benefits for employees of the state, its component units and local boards of education. The plan is administered by the North Carolina State Treasurer.

After five years of creditable service, members of the Teachers' and State Employees' Retirement System qualify for a vested deferred benefit. Employees who retire on or after age 65 and complete five years of membership service (age 55 and five years of creditable service for law enforcement officers), reach age 60 with 25 years of membership service, or complete 30 years of creditable service receive a retirement allowance of 1.81% of an average final compensation (based on the four consecutive years that produce the highest average) multiplied by the number of years of creditable service. Employees may retire with reduced benefits if they reach age 50 with 20 years of creditable service or reach age 60 with five years of creditable service (age 50 with 15 years creditable service for law enforcement officers).

Benefit and contribution provisions for the Teachers' and State Employees' Retirement System are established by North Carolina General Statutes 135-5 and 135-8 and may be amended only by the North Carolina General Assembly. Employer and member contributions rates are set each year by the North Carolina General Assembly based on annual actuarial valuations. For the year ended June 30, 2003, the General Assembly required no contribution by employers and 6% of covered payroll for members.

For the year ended June 30, 2003, the University had a total payroll of $753,845,168 of which $325,527,079 was covered under the Teachers' and State Employees' Retirement System. Total employee and employer contributions for pension benefits for the year were $19,531,625 and $0, respectively. The University made one hundred percent of its annual required contributions for the years ended June 30, 2003, 2002, and 2001, which were $0, $6,175,101, and $16,111,000, respectively.

The Teachers' and State Employees' Retirement System's financial information is included in the State of North Carolina's *Comprehensive Annual Financial Report*. An electronic version of this report is available by accessing the North Carolina Office of the State Controller's internet home page http://www.osc.state.nc.us/ and clicking on "Financial Reports", or by calling the State Controller's financial reporting section at (919) 981-5454.

The Optional Retirement Program (Program) is a defined contribution retirement plan that provides retirement benefits with options for payments to beneficiaries in the event of the participant's death. Administrators and eligible faculty of the University may join the Program instead of the Teachers' and State Employees' Retirement System. The Board of Governors of The University of North Carolina is responsible for the administration of the Program and designates the companies authorized to offer investment products. The Board has authorized the following carriers: Teachers' Insurance and Annuity Association - College Retirement Equities Fund (TIAA-CREF), Lincoln Life Insurance Company, Variable Annuity Life Insurance Company (VALIC), and Fidelity Investments. Participants may elect to allocate their contributions and the University contributions to the carrier of their choice. Each carrier offers a variety of investment funds, including both fixed and variable account investment options and mutual funds.

Participant eligibility and contributory requirements are established by General Statute 135-5.1. Employer and member contributions rates are set each year by the North Carolina General Assembly. For the year ended June 30, 2003, these rates were set at 6.84% of covered payroll for employers and 6% of covered payroll for members. The University assumes no liability other than its contribution.

Program Participants are immediately vested in the value of employee contributions. The value of employer contributions is vested after five years of participation in the Program. Participants become eligible to receive distributions when they terminate employment or retire.

For the year ended June 30, 2003, the University had a total payroll of $753,845,168, of which $285,195,070 was covered under the Optional Retirement Program. Total employee and employer contributions for pension benefits for the year were $17,111,704 and $19,507,343, respectively.

B. Deferred Compensation and Supplemental Retirement Income Plans IRC Section 457 Plan

The State of North Carolina offers its permanent employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457 through the North Carolina Public Employee Deferred Compensation Plan (Plan). The Plan permits each participating employee to defer a portion of his or her salary until future years. The deferred compensation is available to employees upon separation from service, death, disability, retirement or financial hardships if approved by the Board of Trustees of the Plan. The board, a part of the North Carolina Department of Administration, maintains a separate fund for the exclusive benefit of the participating employees and their beneficiaries, *the North Carolina Public Employee Deferred Compensation Trust Fund*. The board also contracts with an external third party to perform certain administrative requirements and to manage the trust fund's assets. All costs of administering and funding the Plan are the responsibility of Plan participants. No costs are incurred by the University. The voluntary contributions by employees amounted to $2,849,834 for the year ended June 30, 2003.

IRC Section 401(k) Plan - All members of the Teachers' and State Employees' Retirement System and the Optional Retirement Program are eligible to enroll in the Supplemental Retirement Income Plan, a defined contribution plan, created under Internal Revenue Code Section 401(k). All costs of administering the plan are the responsibility of the plan participants. No costs are incurred by the University except for a 5% employer contribution for the University's law enforcement officers, which is mandated under General Statute 143-166.30(e). Total employer contributions on behalf of University law-enforcement officers for the year ended June 30, 2003 were $91,593. The voluntary contributions by employees amounted to $2,328,232 for the year ended June 30, 2003.

IRC Section 403(b) and 403(b)(7) Plans - Eligible University employees can participate in tax sheltered annuity plans created under Internal Revenue Code Sections 403(b) and 403(b)(7). The employee's eligible contributions, made through salary reduction agreements, are exempt from federal and state income taxes until the annuity is received or the contributions are withdrawn. These plans are exclusively for employees of universities and certain charitable and other non-profit institutions. All costs of administering and funding these plans are the responsibility of the plan participants. No costs are incurred by the University. The voluntary contributions by employees amounted to $18,593,463 for the year ended June 30, 2003.

NOTE 13
OTHER POSTEMPLOYMENT BENEFITS

A. Health Care for Long-term Disability Beneficiaries and Retirees

The University participates in state administered programs which provide postemployment health insurance to eligible former employees. Eligible former employees include long-term disability beneficiaries of the Disability Income Plan of North Carolina and retirees of the Teachers' and State Employees' Retirement System or the Optional Retirement Program. These benefits were established by Chapter 135, Article 3, Part 3, of the General Statutes and may be amended only by the North Carolina General Assembly. Funding for the health care benefit for long-term disability beneficiaries and retirees is financed on a pay-as-you-go basis. The University contributed 2.35% of the covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program for these health care benefits. For the fiscal year ended June 30, 2003, the University's total contribution to the Plan was $14,351,971. The University assumes no liability for retiree health care benefits provided by the programs other than its required contribution. Additional detailed information about these programs can be located in the State of North Carolina's *Comprehensive Annual Financial Report*.

B. Long-term Disability

The University participates in the Disability Income Plan of North Carolina (DIPNC). Established by Chapter 135, Article 6, of the General Statutes, DIPNC provides short-term and long-term disability benefits to eligible members of the Teachers' and State Employees' Retirement System and the Optional Retirement Program. Long-term disability income benefits are advance funded on an actuarially determined basis using the one-year term cost method. The University contributes .52% of covered payroll under the Teachers' and State Employees' Retirement System and the Optional Retirement Program to the DIPNC. For the fiscal year ended June 30, 2003, the University's total contribution to the DIPNC was $3,175,755. The University assumes no liability for long-term disability benefits under the plan other than its contribution. Additional detailed information about the DIPNC is disclosed in the State of North Carolina's *Comprehensive Annual Financial Report.*

NOTE 14
RISK MANAGEMENT

The University is exposed to various risks of loss related to torts; theft of, damage to, and the destruction of assets; errors and omissions; injuries to employees; and natural disasters. These exposures to loss are handled via a combination of methods, including participation in various state-administered insurance programs, purchase of commercial insurance, and self-retention of certain risks. There have been no significant reductions in insurance coverage from the previous year and settled claims have not exceeded coverage in any of the past three fiscal years.

Public Officers' and Employees' Liability Insurance - Tort claims of up to $500,000 are self-insured under the authority of the State Tort Claims Act. In addition, the state provides excess public officers' and employees' liability insurance up to $11,000,000 per occurrence via contract with a private insurance company. The University pays the premium, based on a composite rate, directly to the private insurer.

Fire and Other Property Loss - The University is required to maintain fire and lightning coverage on all state-owned buildings and contents through the State Property Fire Insurance Fund (Fund), an internal service fund of the state. Such coverage is provided at no cost to operations supported by the state's General Fund. Other operations not supported by the state's General Fund are charged for the coverage. Losses covered by the Fund are subject to a $500 per occurrence deductible. The University also purchased through the Fund extended coverage and other property coverage such as sprinkler leakage, business interruption, vandalism, theft, and all risk insurance for buildings and contents.

Automobile Liability Insurance – All state-owned vehicles are covered by liability insurance through a retrospective rated plan handled by the North Carolina Department of Insurance and a private insurance company. The liability limits for losses incurring in-state are $500,000 per claim and $5,000,000 per occurrence and out-of-state are $1,000,000 per claim and $5,000,000 per occurrence. The University is charged premiums in accordance with this retrospective rated plan as well as any optional physical damage coverages that may be purchased.

Employee and Computer Fraud - The University is protected for losses from employee dishonesty and computer fraud. The coverage is with a private insurance company and is handled by the North Carolina Department of Insurance with coverage of $5,000,000 per occurrence and a $50,000 deductible and a 10% participation in each loss above the deductible.

Other authorized coverage not handled by the North Carolina Department of Insurance is purchased through the State's insurance agent of record.

Comprehensive Major Medical Plan – University employees and retirees are provided comprehensive major medical care benefits. Coverage is funded by contributions to the State Health Plan (Plan), a pension and other employee benefit trust fund of the State of North Carolina. The Plan has contracted with third parties to process claims.

The North Carolina Workers' Compensation Program provides benefits to workers injured on the job. All employees of the state and its component units are included in the program. When an employee is injured, the University's primary responsibility is to arrange for and provide the necessary treatment for the work related injury. The University is responsible for paying medical benefits and compensation in accordance with the North Carolina Workers' Compensation Act. The University is self-insured for workers' compensation.

Liability Insurance Trust Fund – The University participates in the Liability Insurance Trust Fund (the Fund), a claims-servicing public entity risk pool for healthcare professional liability protection. The Fund services professional liability claims, managing separate accounts for each participant from which the losses of that participant are paid. Although participant assessments are determined on an actuarial basis, ultimate liability for claims remains with the participants and, accordingly, the insurance risks are not transferred to the Fund.

The Fund was created by Chapter 116, Article 26, of the General Statutes and The University of North Carolina Board of Governors Resolution of June 9, 1978, to provide professional liability protection for program participants and individual health care practitioners working as employees, agents, or officers of The University of North Carolina Hospitals at Chapel Hill (the Hospitals) and The University of North Carolina at Chapel Hill Physicians and Associates (University Physicians & Associates). The Fund is exempt from federal and state income taxes, and is not subject to regulation by the North Carolina Department of Insurance.

Participation in the Fund is open to the University of North Carolina, any constituent institution of the University of North Carolina, the Hospitals, and any health-care institution, agency or entity that has an affiliation agreement with the University of North Carolina, with a constituent institution of the University of North Carolina, or with the Hospitals. Only the University Physicians & Associates and the Hospitals have participated in the Fund to date. Participants provide management and administrative services to the Fund at no cost.

The Fund is governed by the Liability Insurance Trust Fund Council (the Council). The Council consists of 13 members as follows: one member each appointed by the state attorney general, the state auditor, the state insurance commissioner, the director of the Office of State Budget and Management, the State Treasurer, (each serving at the pleasure of the appointer); and eight members appointed to three year terms (with no limit on the number of terms) by the UNC System's Board of Governors.

The Fund establishes claim liabilities based on estimates of the ultimate cost of claims (including future expenses and claim adjustment expenses) that have been reported but not settled and of claims incurred but not reported. Claim liabilities are recomputed annually based on an independent actuary study to produce current estimates that reflect recent settlements, claims frequency, inflation and other factors. Participant assessments are determined at a level to fund claim liabilities, discounted for future investment earnings. Each participant is required by statute to maintain a fund balance of $100,000 at all times. Participants are subject to additional premium assessments in the event of deficiencies.

The Fund provides occurrence coverage for participants as a corporate entity, as well as for the employees and professional staff of the participants. From July 1, 2002 through April 30, 2003 the Fund provided coverage on an occurrence basis of $7,000,000 for each and every claim and for the next $10,000,000 per claim/annual aggregate. As of July 1, 2002, the fund purchased an excess policy on a claim made basis for $40,000,000 of coverage above the self-insured retention applicable to that policy year through April 30, 2003. As of May 1, 2003, the fund had no excess of loss reinsurance coverage. As of May 1, 2003, the Fund provided coverage on an occurrence basis of $7,000,000 for each and every claim. The Fund provides coverage of $500,000 per occurrence in accordance with the limited waiver of sovereign immunity afforded by the State Tort Claims Act, for any recovery against the participants for the negligence of its employees. To assure that both existing and future claims will be paid, the UNC System Board of Governors is authorized by law to borrow up to $30,000,000 to replenish the Fund. No borrowings have been made under this line of credit to date. The Council believes adequate funds are on deposit in the Fund to meet estimated losses based upon the results of the independent actuary's report.

The Fund has purchased annuity contracts to settle claims for which the claimant has signed an agreement releasing the Fund from further obligation. The related claim liabilities have been removed from estimated malpractice costs. The likelihood that the Fund will be required to make future payments on these claims is considered remote.

The Council may choose to terminate the Fund, or the respective participants may choose to terminate their participation. In the event of such termination by either the Council or a participant, an updated actuarial study will be performed to determine amounts due to or from the participants based on loss experience up to the date of termination.

At June 30, 2003, University assets in the Fund totaled $23,491,200 while University liabilities totaled $19,447,939 resulting in net assets of $4,043,261.

Additional disclosures relative to the funding status and obligations of the Trust Fund are set forth in the Audited Financial Statements of the Liability Insurance Trust Fund for the years ended June 30, 2003 and 2002. Copies of this report may be obtained from The University of North Carolina Liability Insurance Trust Fund, 6001 East Wing, University of North Carolina Hospitals, 101 Manning Drive, Chapel Hill, North Carolina 27514, or by calling (919) 966-3041.

Term Life Insurance – The Death Benefit Plan is administered by the State Treasurer as part of the Teachers and State Employees Retirement System (TSERS) and funded with employer contributions. The employer contribution rate was .16% for the current fiscal year. The amount payable at death is approximately one times salary for eligible employees. The minimum benefit is $25,000 and the maximum is $50,000.

Additional details on state-administered risk management programs are disclosed in the State of North Carolina *Comprehensive Annual Financial Report*, issued by the Office of State Controller.

NOTE 15 COMMITMENTS AND CONTINGENCIES

A. Commitments

The University had commitments of $48,806,775 for various capital improvements projects that include construction and completion of new buildings, and renovations of existing buildings.

B. Pending Litigation and Claims

A $2.1 million claim related to the construction of the Frank Porter Graham Student Union project has been submitted to the State Construction Office by the contractor. No ruling has been made regarding this claim.

The University is undertaking environmental remediation efforts on the Old Sanitary Landfill. The amount of the liability associated with this site cannot reasonably be estimated at this time.

The University is a party to other litigation and claims in the ordinary course of its operations. Since it is not possible to predict the ultimate outcome of these matters, no provision for any liability has been made in the financial statements. University management is of the opinion that the liability, if any, for any of these matters will not have a material adverse effect on the financial position of the University.

C. University Improvement General Obligation Bonds

The 1999-2000 Session of the General Assembly of North Carolina authorized the issuance of $2.5 billion of general obligation bonds of the state, as subsequently approved by a vote of qualified voters of the state, to provide funds for capital improvements for the University of North Carolina. The funds authorized are to be used solely for capital facilities cost on the University of North Carolina campuses as specified in the legislation. The bond legislation specifies the amount of bond funding for each University campus and the level of bond funding intended for each project. The bonds are authorized to be issued over a six-year period beginning in 2001 at a level not to exceed amounts provided in the legislation. Using a cash flow financing approach, The University of North Carolina – Office of the President (UNC-OP), establishes annual amounts not to exceed for each approved project. The amounts not to exceed are subject to change due to actual cash availability and needs during the year. Subsequent to the bond sales and the availability of bond proceeds, UNC-OP notifies the Office of State Budget and Management (OSBM) of the amounts not to exceed for each approved project. Within these amounts, based on an official request of cash needs from the University, OSBM authorizes allotments. The University records the allotments as revenue on the accompanying financial statements. In addition, amounts not allotted but accrued as expended at year-end are recorded as revenue. The University's remaining authorization $386,815,928 is contingent on future bond sales and OSBM allotment approval. Because of uncertainty and time restrictions the remaining authorization is not recorded as an asset or revenue on the accompanying financial statements.

D. Other Contingent Receivables

The University has received notification of other gifts and grants for which funds have not been disbursed by the resource provider and for which conditions attached to the gift or grant have not been satisfied or, in the case of permanent endowments, cannot begin to be satisfied. In accordance with accounting principles generally accepted in the United States of America these amounts have not been recorded on the accompanying financial statements. The purpose and amount of other contingent receivables at year-end is as follows:

Purpose	Amount
Pledges to Permanent Endowments	$21,618,179

NOTE 16
RELATED PARTIES

There are 14 separately incorporated non-profit organizations associated with the University. These organizations are The Botanical Garden Foundation, Inc., The Dental Alumni Association, Inc., The Dental Foundation of North Carolina, Inc., The Educational Foundation, Inc., The General Alumni Association, The Institute of Government Foundation, Inc., The Law Alumni Association of N.C., Inc., The Medical Foundation of North Carolina, Inc., The Pharmacy Foundation of North Carolina, Inc., The School of Education Foundation, Inc., The School of Journalism and Mass Communication Foundation of North Carolina, Inc., The University of North Carolina at Chapel Hill Arts and Sciences Foundation, Inc., The University of North Carolina at Chapel Hill Public Health Foundation, Inc., and The University of North Carolina at Chapel Hill School of Nursing Foundation, Inc. The support from these organizations to the University approximated $19,065,762 for the year ended June 30, 2003.

NOTE 17
ACCOUNTING CHANGES

For the fiscal year ended June 30, 2003, the University implemented the GASB Technical Bulletin No. 2003-1, *Disclosure Requirements for Derivatives Not Reported at Fair Value on the Statement of Net Assets*. GASB Technical Bulletin No. 2003-1 supercedes Technical Bulletin No. 94-1 and applies to derivatives that are not reported at fair value on the statement of net assets. This standard provides an updated definition of derivatives and also requires disclosure of the government's objective for entering into the derivative and the derivative's terms, fair value, associated debt, and risk exposures.

Statistical Section

Chapel Hill, North Carolina
Fiscal Year Ended June 30, 2003

Effective July 1, 2001, the University implemented GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – For Public Colleges and Universities*. The financial statement presentation required by these Statements is a single-column enterprise activity rather than the fund-group perspective previously reported. Significant accounting changes in order to comply with the new requirements include adopting depreciation on capital assets, reporting revenues net of discounts and allowances, eliminating inter-fund activities, classifying activities as operating or non-operating, classifying assets and liabilities as current or non-current, and prorating summer school activities to periods earned.

In addition, the University implemented GASB Statement No. 38, *Certain Financial Statement Note Disclosures*. Changes in existing disclosures include more detailed information on debt service requirements, obligations under leases, and short-term debt. New disclosures include variable debt interest information and the major components of receivable and payable balances.

Due to these significant changes in financial reporting, the University is presenting only two years of data in this statistical section, except for specific revenue and general revenue bond coverage and demographic data which are not affected by the GASB implementation. For information purposes, selected 10 years of statistical data (Fiscal years 1992 - 2001) are included in the "Historical Statistical Section," reproduced from the prior year CAFR.

THE UNIVERSITY
of NORTH CAROLINA
at CHAPEL HILL

OPERATING AND NON-OPERATING REVENUES BY SOURCE

	For the Year Ended June 30,		
	2003	2002	% Change
Operating Revenues			
Student Tuition and Fees, net	$146,961,417	$124,661,145	17.9%
Federal Grants and Contracts	356,845,158	330,402,676	8.0%
State and Local Grants and Contracts	34,288,762	38,512,136	-11.0%
Nongovernmental Grants and Contracts	64,546,516	75,536,237	-14.5%
Patient Services, net	131,256,051	137,035,225	-4.2%
Sales and Services, net	262,105,915	246,567,989	6.3%
Interest Earnings on Loans	281,215	120,650	133.1%
Other Operating Revenues	7,282,755	14,628,956	-50.2%
Total Operating Revenues	$1,003,567,789	$967,465,014	3.7%
Non-operating Revenues			
State Appropriations	$368,024,036	$368,504,553	-0.1%
Noncapital Grants, net	40,994,829	34,768,925	17.9%
Noncapital Gifts, net	60,887,596	62,403,802	-2.4%
Investment Income, net	47,398,174	52,956,614	-10.5%
Total Non-operating Revenues	$517,304,635	$518,633,894	-0.3%
TOTAL REVENUES	$1,520,872,424	$1,486,098,908	2.3%

	For the Year Ended June 30,	
	2003	2002
Operating Revenues		
Student Tuition and Fees, net	9.7%	8.4%
Federal Grants and Contracts	23.5%	22.2%
State and Local Grants and Contracts	2.3%	2.6%
Nongovernmental Grants and Contracts	4.2%	5.1%
Patient Services, net	8.6%	9.2%
Sales and Services, net	17.2%	16.6%
Interest Earnings on Loans	0.0%	0.0%
Other Operating Revenues	0.5%	1.0%
Total Operating Revenues	66.0%	65.1%
Non-operating Revenues		
State Appropriations	24.2%	24.8%
Noncapital Grants, net	2.7%	2.3%
Noncapital Gifts, net	4.0%	4.2%
Investment Income, net	3.1%	3.6%
Total Non-operating Revenues	34.0%	34.9%
TOTAL REVENUES	100.0%	100.0%

(Percent of total revenues)

Reclassifications: Certain prior year numbers have been reclassified to conform to current year presentations.

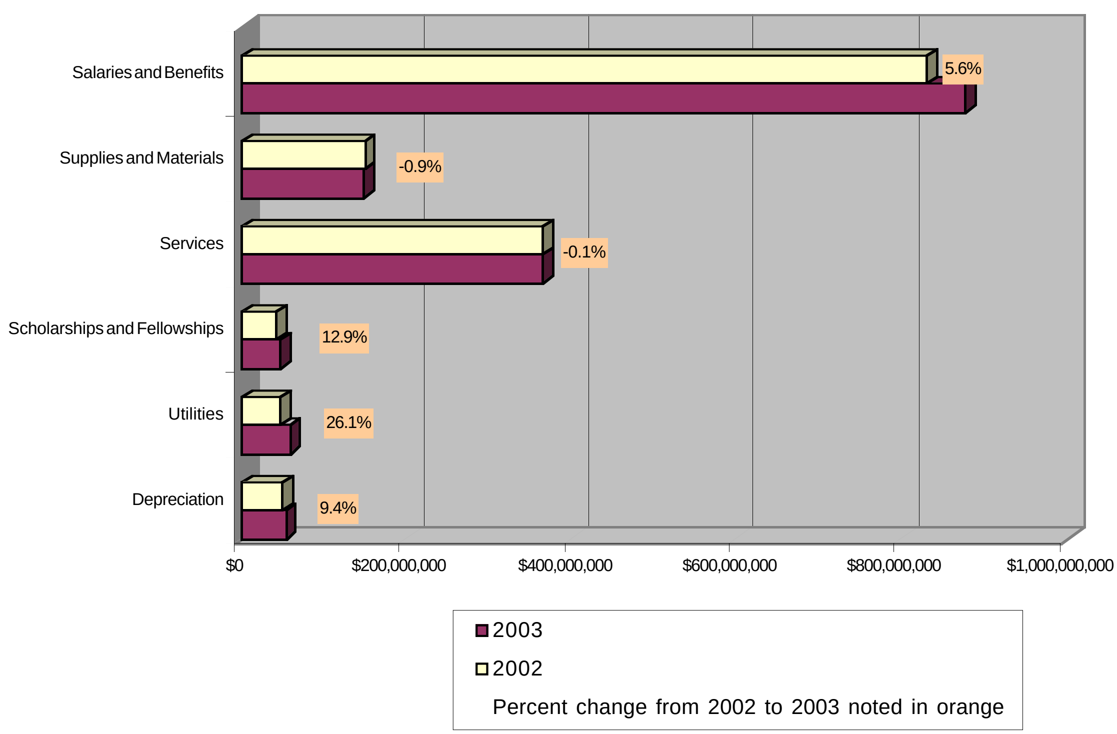
OPERATING EXPENSES BY NATURE

	For the Year Ended June 30, 2003	2002	% Change
Salaries and Benefits	$876,265,477	$829,473,249	5.6%
Supplies and Materials	146,986,272	148,324,265	-0.9%
Services	364,456,573	364,831,514	-0.1%
Scholarships and Fellowships	45,618,092	40,414,555	12.9%
Utilities	57,314,345	45,452,167	26.1%
Depreciation	53,075,830	48,517,249	9.4%
Total Operating Expenses by Nature	$1,543,716,589	$1,477,012,999	4.5%

	For the Year Ended June 30, 2003	2002
Salaries and Benefits	56.8%	56.2%
Supplies and Materials	9.5%	10.0%
Services	23.6%	24.7%
Scholarships and Fellowships	3.0%	2.7%
Utilities	3.7%	3.1%
Depreciation	3.4%	3.3%
Total Operating Expenses by Nature	100.0%	100.0%

(Percent of total operating expenses by nature)

OPERATING EXPENSES BY NATURE



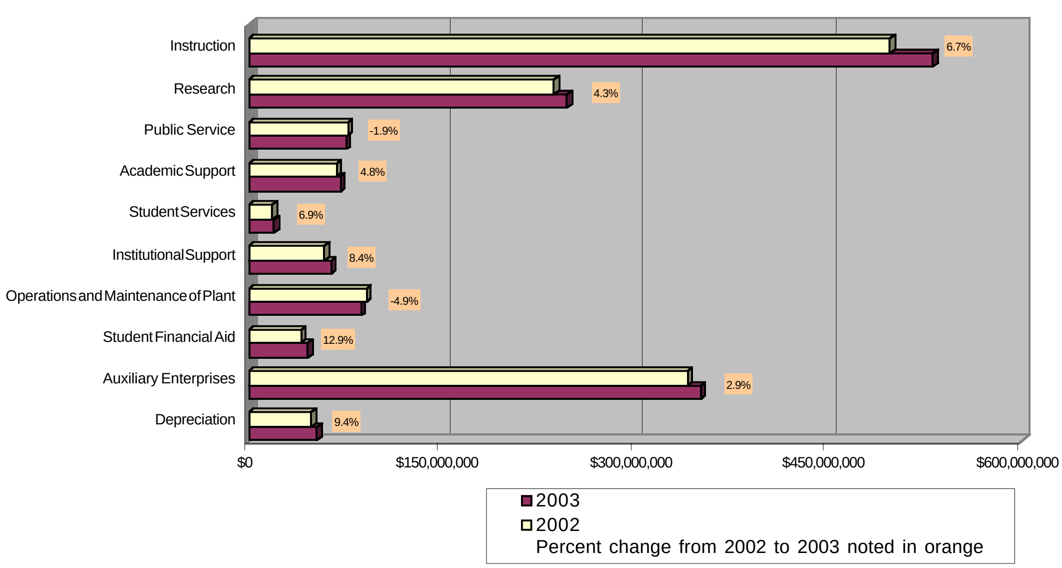
OPERATING EXPENSES BY FUNCTION

	For the Year Ended June 30,		
	2003	2002	% Change
Instruction	$531,123,250	$497,770,880	6.7%
Research	247,434,086	237,275,464	4.3%
Public Service	75,409,910	76,896,238	-1.9%
Academic Support	70,888,224	67,617,814	4.8%
Student Services	19,490,735	18,224,875	6.9%
Institutional Support	63,460,504	58,560,098	8.4%
Operations and Maintenance of Plant	86,451,422	90,941,785	-4.9%
Student Financial Aid	45,618,092	40,414,555	12.9%
Auxiliary Enterprises	350,764,536	340,794,041	2.9%
Depreciation	53,075,830	48,517,249	9.4%
Total Operating Expenses by Function	$1,543,716,589	$1,477,012,999	4.5%

	For the Year Ended June 30,	
	2003	2002
Instruction	34.4%	33.7%
Research	16.0%	16.0%
Public Service	4.9%	5.2%
Academic Support	4.6%	4.6%
Student Services	1.3%	1.2%
Institutional Support	4.1%	4.0%
Operations and Maintenance of Plant	5.6%	6.2%
Student Financial Aid	3.0%	2.7%
Auxiliary Enterprises	22.7%	23.1%
Depreciation	3.4%	3.3%
Total Operating Expenses by Function	100.0%	100.0%

(Percent of total operating expenses by function)

OPERATING EXPENSES BY FUNCTION



SUMMARY OF RATIOS

PRIMARY RESERVE RATIO

	For the Year Ended June 30, 2003	2002
Unrestricted Net Assets	$370,815,821	$346,545,802
Expendable Restricted Net Assets	559,127,937	645,389,715
Less:expendable Restricted for Capital Projects	(21,517,527)	(58,608,182)
Expendable Net Assets	$908,426,231	$933,327,335
Operating Expenses	$1,543,716,589	$1,477,012,999
Interest and Fees on Capital Asset-related Debt	15,680,788	15,031,104
Other Non-operating Expenses	1,899,072	7,661,489
Total Expenses	$1,561,296,449	$1,499,705,592
Expendable Net Assets	$908,426,231	$933,327,335
Total Expenses	$1,561,296,449	$1,499,705,592
Ratio	0.6 x	0.6 x

Measures the financial strength of the institution by indicating how long the institution could function using its expendable reserves to cover operations should additional net assets not be available. A positive ratio and an increasing amount over time denotes strength.

RETURN ON NET ASSETS RATIO

	For the Year Ended June 30, 2003	2002
Change in Net Assets	$60,767,554	$45,393,586
Total Net Assets (Beginning of Year)	$1,964,418,046	$1,919,024,460
Ratio	3.1%	2.4%

Measures total economic return. While a increasing trend reflects strength, a decline may be appropriate and even warranted if it represents a strategy on the part of the institution to fulfill its mission.

SUMMARY OF RATIOS *(cont'd)*

Net Operating Revenues Ratio

	For the Year Ended June 30, 2003	2002
Total Operating Revenues	$1,003,567,789	$967,465,014
State Appropriations	368,024,036	368,504,553
Noncapital Gifts and Grants, net	101,882,425	97,172,727
Investment Income, net	47,398,174	52,956,614
Adjusted Net Operating Revenues	$1,520,872,424	$1,486,098,908
Income Before Other Revenues, Expenses, Gains, or Losses	($40,424,025)	($13,606,684)
Adjusted Net Operating Revenues	$1,520,872,424	$1,486,098,908
Ratio	-2.7%	-0.9%

Measures whether the institution is living within available resources. A positive ratio and an increasing amount over time generally reflects strength.

Operating Margin Excluding Gifts

	For the Year Ended June 30, 2003	2002
Income Before Other Revenues, Expenses, Gains, or Losses	($40,424,025)	($13,606,684)
Less: Noncapital Gifts and Grants, net	(101,882,425)	(97,172,727)
Adjusted Income Before Other Revenues, Expenses, Gains, or Losses	($142,306,450)	($110,779,411)
Total Operating Revenues	$1,003,567,789	$967,465,014
State Appropriations	368,024,036	368,504,553
Investment Income, net	47,398,174	52,956,614
Adjusted Net Operating Revenues less Gifts	$1,418,989,999	$1,388,926,181
Adjusted Income Before Other Revenues, Expenses, Gains, or Losses	($142,306,450)	($110,779,411)
Adjusted Net Operating Revenues less Gifts	$1,418,989,999	$1,388,926,181
Ratio	-10.0%	-8.0%

A more restrictive measure of whether the institution is living within available resources. A positive ratio and an increasing amount over time generally reflects strength.

SUMMARY OF RATIOS *(cont'd)*

Viability Ratio

	For the Year Ended June 30,	
	2003	2002
Unrestricted Net Assets	$370,815,821	$346,545,802
Expendable Restricted Net Assets	559,127,937	645,389,715
Less:Expendable Restricted for Capital Projects	(21,517,527)	(58,608,182)
Expendable Net Assets	$908,426,231	$933,327,335
Expendable Net Assets	$908,426,231	$933,327,335
Total Notes, Bonds, Capital Leases and Commercial Paper	$432,806,684	$389,360,567
Ratio	2.1 x	2.4 x

Measures the ability of the institution to cover its debt as of the balance sheet date, should the institution need to do so. A positive ratio of greater than 1:1 generally denotes strength.

Total Financial Resources to Direct Debt

	For the Year Ended June 30,	
	2003	2002
Unrestricted Net Assets	$370,815,821	$346,545,802
Nonexpendable Restricted Net Assets	323,961,205	304,096,632
Expendable Restricted Net Assets	559,127,937	645,389,715
Total Financial Resources	$1,253,904,963	$1,296,032,149
Total Financial Resources	$1,253,904,963	$1,296,032,149
Total Notes, Bonds, Capital Leases and Commercial Paper	$432,806,684	$389,360,567
Ratio	2.9 x	3.3 x

A broader measure of the ability of the institution to cover its debt as of the balance sheet date.

SUMMARY OF RATIOS *(cont'd)*

Debt Burden Ratio

	For the Year Ended June 30,	
	2003	2002
Interest and Fees Paid on Capital Debt and Leases	$18,302,926	$21,117,301
Principal Paid on Capital Debt and Leases	14,044,252	14,130,000
Debt Service	$32,347,178	$35,247,301
Operating Expenses	1,543,716,589	1,477,012,999
Interest and Fees on Capital Asset-related Debt	15,680,788	15,031,104
Other Non-operating Revenues (Expenses)	1,899,072	7,661,489
Less: Depreciation Expense	(53,075,830)	(48,517,249)
Plus: Principal Paid on Capital Debt and Leases	14,044,252	14,130,000
Total Expenditures	$1,522,264,871	$1,465,318,343
Debt Service	$32,347,178	$35,247,301
Total Expenditures	$1,522,264,871	$1,465,318,343
Ratio	2.1%	2.4%

Measures the financial strength of the institution by indicating how long the institution could function using its expendable reserves to cover operations should additional net assets not be available. A positive ratio and an increasing amount over time denotes strength.

Direct Debt to Adjusted Cash Flow

	For the Year Ended June 30,	
	2003	2002
Net Cash Used by Operating Activities	($382,265,470)	($440,098,807)
State Appropriations	368,024,036	368,504,553
Grants for Other than Capital Purposes	40,994,829	34,768,925
Noncapital Gifts	60,887,596	62,403,802
Adjusted Cash Flow from Operations	$87,640,991	$25,578,473
Total Notes, Bonds, Capital Leases and Commercial Paper	$432,806,684	$389,360,567
Adjusted Cash Flow from Operations	$87,640,991	$25,578,473
Ratio	4.9 x	15.2 x

Measures the financial strength of the institution by indicating how long the institution would take to repay the debt using the cash provided by its operations. A decreasing ratio over time denotes strength.

SUMMARY OF RATIOS *(cont'd)*

Research Expenses to Total Operating Expenses

	For the Year Ended June 30, 2003	2002
Operating Expenses	$1,543,716,589	$1,477,012,999
Interest and Fees on Capital Asset-related Debt	15,680,788	15,031,104
Other Non-operating (Revenues) Expenses	1,899,072	7,661,489
Total Adjusted Operating Expenses	$1,561,296,449	$1,499,705,592
Research Expenses	$247,434,086	$237,275,464
Total Adjusted Operating Expenses	$1,561,296,449	$1,499,705,592
Ratio	15.8%	15.8%

Measures the institution's research expense to the total operating expenses.

Net Tuition per Student

	For the Year Ended June 30, 2003	2002
Student Tuition and Fees, net	$146,961,417	$124,661,145
Less: Scholarships and Fellowships	(45,618,092)	(40,414,555)
Net Tuition and Fees	$101,343,325	$84,246,590
Net Tuition and Fees	$101,343,325	$84,246,590
Undergraduate, Graduate and Professional FTE	24,041	23,517
Net Tuition per Student	$4,215	$3,582

Measures the institution's net student tution and fees received per student.

State Appropriation per Student

	For the Year Ended June 30, 2003	2002
State Appropriations	$368,024,036	$368,504,553
Undergraduate, Graduate and Professional FTE	24,041	23,517
State Appropriation per Student	$15,308	$15,670

Measures institution's dependency on state appropriations.

Specific Revenue and General Revenue Bond Coverage
Last Ten Fiscal Years (in thousands)

On May 7, 2002 and February 7, 2001, The University of North Carolina at Chapel Hill issued General Revenue Bonds, which are repaid from Available Funds. Available Funds are defined as any unrestricted Net Assets remaining after satisfying obligations of the University under trust indentures, trust agreements or bond resolutions (Specific Revenue Bonds), but excluding State Appropriations, Tuition, and certain special facilities revenues. Specific Revenue Bonds have a pledged revenue stream as the repayment source.

	For the Year Ended June 30,				
	2003	**2002**	**2001**	**2000**	**1999**
Specific Revenue Bond Coverage					
Gross Operating Revenues	$116,985	$102,042	$92,977	$250,316	$246,610
Direct Operating Expenses	90,731	73,720	64,808	214,212	208,753
Net Revenue Available for Debt Service	$26,254	$28,322	$28,169	$36,104	$37,857
Principal	$6,420	$10,090	$9,195	$11,601	$10,128
Interest	4,414	8,433	10,203	11,351	11,008
Specific Revenue Debt Service Requirements	$10,834	$18,523	$19,398	$22,952	$21,136
Coverage	**2.42**	**1.53**	**1.45**	**1.57**	**1.79**

	For the Year Ended June 30,				
	2003	**2002 (1)**	**2001**	**2000**	**1999**
Available Funds General Revenue Bonds					
Total Unrestricted Revenue	$1,055,273	$987,708	$1,009,353	$924,667	$877,492
Less:					
State Appropriations	(368,024)	(368,505)	(402,205)	(383,189)	(382,372)
Tuition and Fees	(146,961)	(124,661)	(139,319)	(121,507)	(110,400)
Specific Revenue Debt Service Requirements	(10,834)	(18,523)	(19,398)	(22,952)	(21,136)
Plus:					
Adjusted Beginning Unrestricted Net Assets	346,546	392,613	354,936	347,359	310,896
Total Available Funds	$876,000	$868,632	$803,367	$744,378	$674,480
Annual Increase	$7,368	$65,265	$58,989	$69,898	$32,043
% Increase	0.8%	8.1%	7.9%	10.4%	5.0%

	For the Year Ended June 30,				
	2003	**2002**	**2001**	**2000**	**1999**
General Revenue Bond Coverage					
Total Available Funds	$876,000	$868,632	$803,367	$744,378	$674,480
Principal	$7,150	$4,060	$2,840		
Interest	8,332	7,094	5,012		
General Revenue Debt Service Requirements	$15,482	$11,154	$7,852	n/a	n/a
Coverage	**56.58**	**77.88**	**102.31**		

General Revenue Bond Debt Service includes debt service for specific revenue bonds refunded or defeased by issuance of general revenue debt during the year of refunding.

(1) For fiscal year ended June 30, 2002, the University implemented GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments* as amended by GASB Statement No. 35, *Basic financial Statements - and Management's Discussion and Analysis - for Public Colleges and Universities*. In addition, the University implemented GASB Statement No. 38, *Certain Financial Statement Note Disclosures*. The definition of available funds has not changed as a result of implementing these GASB Statements.
(2) As of July 1, 1997, the fund balances of the various funds as previously reported were restated as a result of the University implementing GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. This statement requires that certain investments be reported at fair value for year-end financial reporting purposes.
(3) As of July 1, 1993, the fund balances of the various funds as previously reported were restated as a result of the University implementing GASB Statement No. 14, *The Financial Reporting Entity*. This statement requires that the financial statements of certain affiliated organizations be blended with those of the University.

	For the Year Ended June 30,				
	1998	**1997**	**1996**	**1995**	**1994**
Specific Revenue Bond Coverage					
Gross Operating Revenues	$226,567	$228,228	$205,387	$189,346	$175,567
Direct Operating Expenses	189,205	177,793	158,584	147,847	140,552
Net Revenue Available for Debt Service	$37,362	$50,435	$46,803	$41,499	$35,015
Principal	$8,913	$8,279	$7,743	$6,217	$5,794
Interest	10,634	11,063	11,610	13,937	13,264
Specific Revenue Debt Service Requirements	$19,547	$19,342	$19,353	$20,154	$19,058
Coverage	**1.91**	**2.61**	**2.42**	**2.06**	**1.84**

	For the Year Ended June 30,				
	1998 (2)	**1997**	**1996**	**1995**	**1994 (3)**
Available Funds General Revenue Bonds					
Total Unrestricted Revenue	$819,645	$776,658	$709,447	$682,180	$641,932
Less:					
State Appropriations	(352,283)	(331,650)	(308,245)	(302,337)	(283,826)
Tuition and Fees	(105,745)	(102,277)	(88,478)	(81,465)	(75,531)
Specific Revenue Debt Service Requirements	(19,547)	(19,342)	(19,353)	(20,154)	(19,058)
Plus:					
Beginning Unrestricted Net Assets	300,367	251,740	225,795	206,190	192,164
Total Available Funds	$642,437	$575,129	$519,166	$484,414	$455,681
Annual Increase	$67,308	$55,963	$34,752	$28,733	$40,089
% Increase	11.7%	10.8%	7.2%	6.3%	9.6%

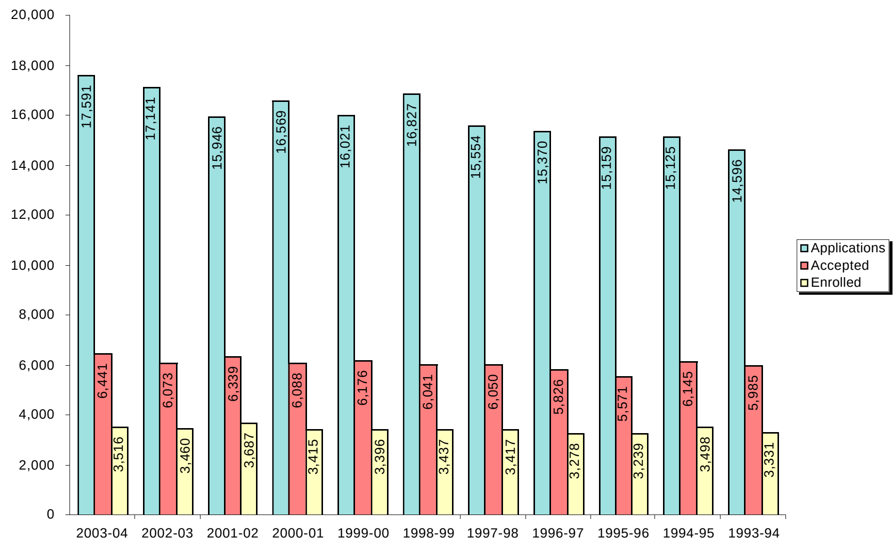
	For the Year Ended June 30,				
	1998	**1997**	**1996**	**1995**	**1994**
General Revenue Bond Coverage					
Total Available Funds	$642,437	$575,129	$519,166	$484,414	$455,681
Principal					
Interest					
General Revenue Debt Service Requirements	n/a	n/a	n/a	n/a	n/a
Coverage					

ADMISSIONS, ENROLLMENT, AND DEGREE STATISTICS
FALL ENROLLMENT 2003-04 AND LAST TEN FISCAL YEARS

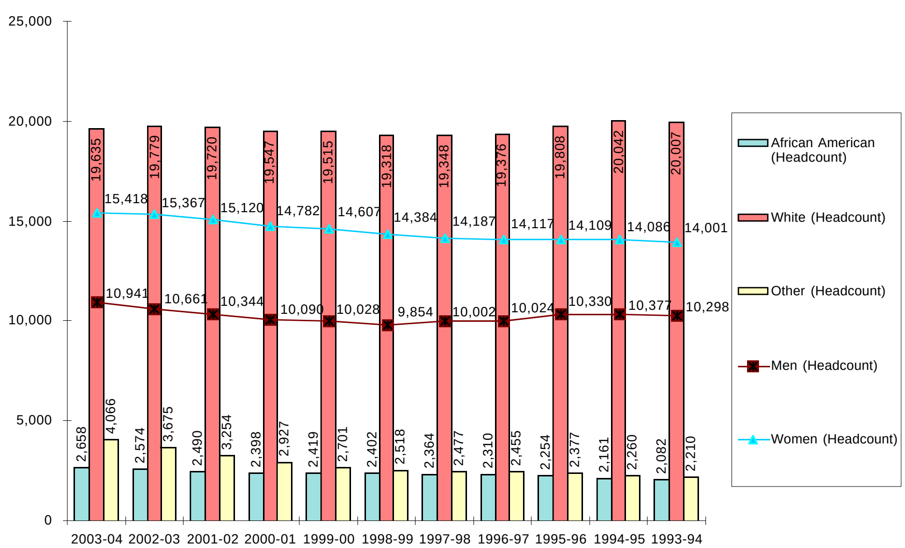
	Fall Enrollment of Fiscal Year										
	2003-04	2002-03	2001-02	2000-01	1999-00	1998-99	1997-98	1996-97	1995-96	1994-95	1993-94
Admissions - Freshmen											
Applications	17,591	17,141	15,946	16,569	16,021	16,827	15,554	15,370	15,159	15,125	14,596
Accepted	6,441	6,073	6,339	6,088	6,176	6,041	6,050	5,826	5,571	6,145	5,985
Enrolled	3,516	3,460	3,687	3,415	3,396	3,437	3,417	3,278	3,239	3,498	3,331
Accepted as a Percentage of Applications	36.6%	35.4%	39.8%	36.7%	38.5%	35.9%	38.9%	37.9%	36.8%	40.6%	41.0%
Enrolled as a Percentage of Accepted	54.6%	57.0%	58.2%	56.1%	55.0%	56.9%	56.5%	56.3%	58.1%	56.9%	55.7%
Average SAT Scores - Total	1,283	1,267	1,257	1,251	1,245	1,230	1,220	1,222	1,142	1,128	1,126
Verbal	634	625	623	622	620	613	609	611	539	529	529
Math	649	642	634	629	625	617	611	611	603	599	597
Enrollment											
Undergraduate, Graduate and Professional FTE	24,314	24,041	23,517	23,000	22,761	21,940	21,794	21,709	21,961	21,918	21,758
Undergraduate, Graduate and Professional Headcount	26,359	26,028	25,464	24,872	24,635	24,238	24,189	24,141	24,439	24,463	24,299
Men (Headcount)	10,941	10,661	10,344	10,090	10,028	9,854	10,002	10,024	10,330	10,377	10,298
Percentage of Total	41.5%	41.0%	40.6%	40.6%	40.7%	40.7%	41.3%	41.5%	42.3%	42.4%	42.4%
Women (Headcount)	15,418	15,367	15,120	14,782	14,607	14,384	14,187	14,117	14,109	14,086	14,001
Percentage of Total	58.5%	59.0%	59.4%	59.4%	59.3%	59.3%	58.7%	58.5%	57.7%	57.6%	57.6%
African American (Headcount)	2,658	2,574	2,490	2,398	2,419	2,402	2,364	2,310	2,254	2,161	2,082
Percentage of Total	10.1%	9.9%	9.7%	9.6%	9.8%	9.9%	9.8%	9.6%	9.2%	8.8%	8.6%
White (Headcount)	19,635	19,779	19,720	19,547	19,515	19,318	19,348	19,376	19,808	20,042	20,007
Percentage of Total	74.4%	76.0%	77.3%	78.5%	79.2%	79.7%	80.0%	80.2%	81.1%	82.0%	82.3%
Other (Headcount)	4,066	3,675	3,254	2,927	2,701	2,518	2,477	2,455	2,377	2,260	2,210
Percentage of Total	15.5%	14.1%	12.9%	11.9%	11.0%	10.4%	10.2%	10.2%	9.7%	9.2%	9.1%
Degrees Granted											
Bachelor's	3,741	3,560	3,477	3,444	3,406	3,669	3,568	3,674	3,542	3,623	3,497
Master's	1,738	1,638	1,679	1,726	1,550	1,464	1,489	1,361	1,465	1,511	1,451
Doctoral	412	390	398	425	374	382	389	366	369	373	388
Professional	672	589	599	588	571	584	476	484	480	464	443

Source: The University of North Carolina at Chapel Hill Fact Book.

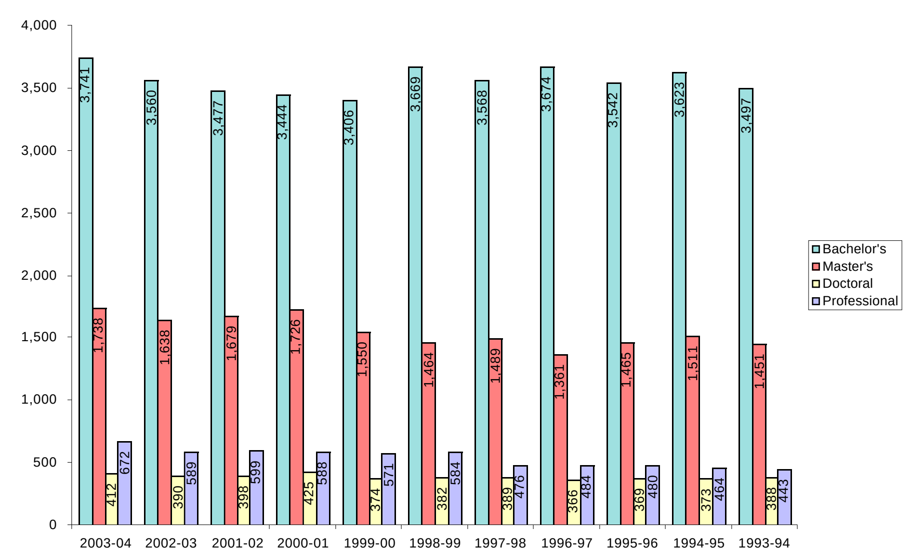
FRESHMEN APPLIED, ACCEPTED, AND ENROLLED



HEADCOUNT TOTAL



DEGREES EARNED



Faculty and Staff Statistics
Fall Employment 2003-04 and Last Ten Fiscal Years

	Fall Employment of Fiscal Year					
	2003-04	**2002-03**	**2001-02**	**2000-01**	**1999-00**	**1998-99**
Faculty						
Full-time	2,744	2,701	2,598	2,488	2,601	2,477
Part-time	313	307	322	294	260	260
Total Faculty	3,057	3,008	2,920	2,782	2,861	2,737
Percentage Tenured	45.9%	50.5%	52.1%	53.9%	51.9%	54.6%
Staff and EPA Non-Faculty						
Full-time	1,227	1,157	1,034	993	784	725
Part-time	128	111	97	92	63	56
EPA Non-Faculty	1,355	1,268	1,131	1,085	847	781
Full-time	5,947	5,915	5,782	5,574	5,996	5,790
Part-time	317	290	278	284	307	311
SPA	6,264	6,205	6,060	5,858	6,303	6,101
Total Full-time	7,174	7,072	6,816	6,567	6,780	6,515
Total Part-time	445	401	375	376	370	367
Total Staff and EPA Non-Faculty	7,619	7,473	7,191	6,943	7,150	6,882

	Fall Employment of Fiscal Year				
	1997-98	**1996-97**	**1995-96**	**1994-95**	**1993-94**
Faculty					
Full-time	2,421	2,417	2,369	2,328	2,297
Part-time	239	223	216	210	204
Total Faculty	2,660	2,640	2,585	2,538	2,501
Percentage Tenured	56.2%	57.9%	58.3%	59.2%	59.6%
Staff and EPA Non-Faculty					
Full-time	674	653	648	627	596
Part-time	53	56	57	51	55
EPA Non-Faculty	727	709	705	678	651
Full-time	5,587	5,236	5,519	5,468	5,405
Part-time	314	298	322	328	360
SPA	5,901	5,534	5,841	5,796	5,765
Total Full-time	6,261	5,889	6,167	6,095	6,001
Total Part-time	367	354	379	379	415
Total Staff and EPA Non-Faculty	6,628	6,243	6,546	6,474	6,416

Note: SPA denotes employees subject to the State Personnel Act
EPA denotes employees exempt from the State Personnel Act

Source: The University of North Carolina at Chapel Hill Fact Book.

Historical Statistical Section

Chapel Hill, North Carolina
Fiscal Year Ended June 30, 2003

THE UNIVERSITY of NORTH CAROLINA at CHAPEL HILL

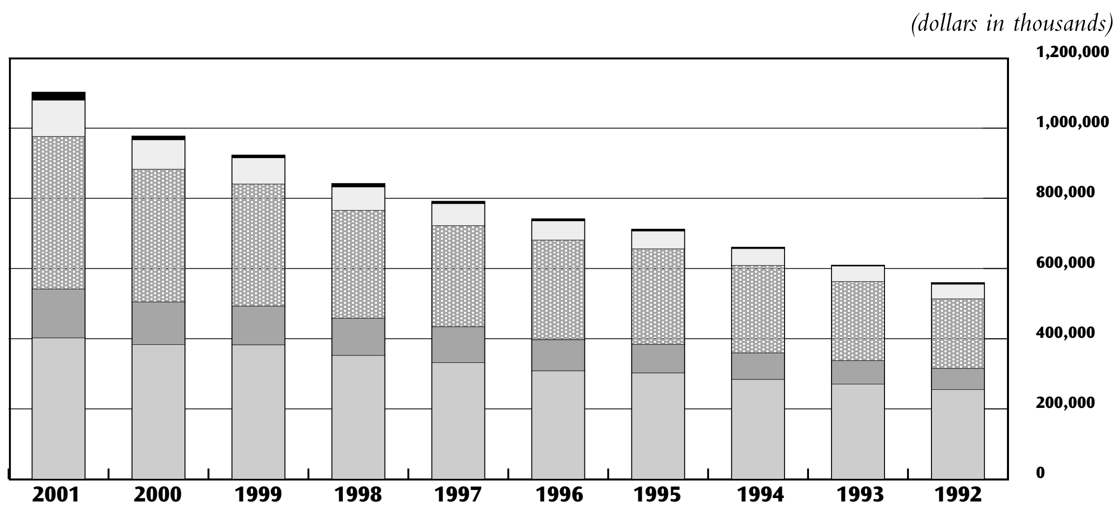
Unrestricted General and Restricted Current Funds Revenues By Source

LAST TEN FISCAL YEARS

(in thousands)

	For the Year Ended June 30,				
	2001	**2000**	**1999**	**1998**	**1997**
Current Funds Revenues					
State Appropriations	$402,205	$383,189	$382,372	$352,283	$331,650
Tuition and Fees	139,319	121,507	110,400	105,745	102,277
Contracts and Grants	434,683	378,094	347,850	307,685	288,042
Gifts, Investment and Endowment Income	103,382	83,459	74,557	66,321	62,720
Sales and Services and Others	23,347	11,797	8,767	10,816	7,317
Total Current Funds Revenues	**$1,102,936**	**$978,046**	**$923,946**	**$842,850**	**$792,006**

Unrestricted General and Restricted Current Funds Revenues By Source for year ended June 30,



(in thousands)

	For the Year Ended June 30,				
	1996	**1995**	**1994**	**1993**	**1992**
Current Funds Revenues					
State Appropriations	$308,245	$302,337	$283,826	$270,700	$255,003
Tuition and Fees	88,478	81,465	75,531	66,718	60,247
Contracts and Grants	284,195	272,176	249,448	225,512	198,095
Gifts, Investment and Endowment Income	54,486	50,429	47,637	43,783	41,676
Sales and Services and Others	6,693	6,043	4,646	3,066	5,310
Total Current Funds Revenues	**$742,097**	**$712,450**	**$661,088**	**$609,779**	**$560,331**

Sales and Services and Others
Gifts, Investment and Endowment Income
Contracts and Grants
Tuition and Fees
State Appropriations

UNRESTRICTED GENERAL AND RESTRICTED CURRENT FUNDS EXPENDITURES AND MANDATORY TRANSFERS BY FUNCTION

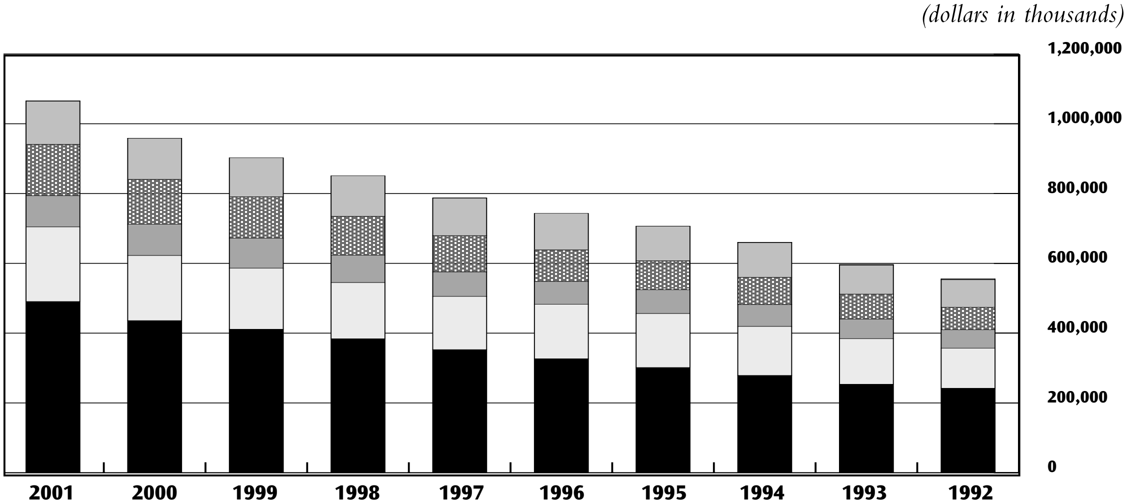
LAST TEN FISCAL YEARS

(in thousands)

	For the Year Ended June 30,				
	2001	**2000**	**1999**	**1998**	**1997**
Current Funds Expenditures					
Instruction	$490,447	$435,839	$411,292	$383,759	$352,711
Organized Research	213,833	186,550	174,973	161,128	152,478
Public Service	89,663	89,906	86,062	78,678	70,106
Academic Support, Student Services, and Financial Aid	146,575	128,107	118,351	110,863	104,051
Institutional Support, Plant Maintenance and Operations	123,867	117,690	122,029	116,583	107,535
Total Current Funds Expenditures	**$1,064,385**	**$958,092**	**$912,707**	**$851,011**	**$786,881**
Current Funds Mandatory Transfers	**1,346**	**502**	**37**	**43**	**689**
Total Current Funds Expenditures and Mandatory Transfers	**$1,065,731**	**$958,594**	**$912,744**	**$851,054**	**$787,570**

Unrestricted General and Restricted Current Funds Expenditures and Madatory Transfers by Function for year ended June 30,

(dollars in thousands)



(in thousands)

	For the Year Ended June 30,				
	1996	**1995**	**1994**	**1993**	**1992**
Current Funds Expenditures					
Instruction	$326,546	$301,323	$278,587	$253,662	$241,956
Organized Research	156,034	154,817	140,586	130,570	115,014
Public Service	65,502	68,317	62,834	56,111	52,952
Academic Support, Student Services and Financial Aid	90,236	83,016	77,728	71,427	64,079
Institutional Support, Plant Maintenance and Operations	104,929	98,751	99,372	82,921	78,970
Total Current Funds Expenditures	**$743,247**	**$706,224**	**$659,107**	**$594,691**	**$552,971**
Current Funds Mandatory Transfers	**57**	**490**	**1,323**	**2,202**	**2,754**
Total Current Funds Expenditures and Mandatory Transfers	**$743,304**	**$706,714**	**$660,430**	**$596,893**	**$555,725**

Institutional Support, Plant Maintenance and Operations

Academic Support, Student Support and Financial Aid

Public Service

Organized Research

Instruction

Current Funds Revenues By Source

LAST TEN FISCAL YEARS

(in thousands)

	For the Year Ended June 30,				
	2001	2000	1999	1998	1997
Current Funds Revenues					
State Appropriations	$402,205	$383,189	$382,372	$352,283	$331,650
Tuition and Fees	139,319	121,507	110,400	105,745	102,277
Federal Contracts and Grants	311,821	276,548	259,152	231,687	221,548
State Contracts and Grants	52,519	44,782	37,570	31,269	26,402
Nongovernmental Contracts and Grants	70,343	56,764	51,128	44,729	40,092
Gifts and Bequests	80,007	53,484	46,657	44,312	38,197
Investment Income	28,679	18,619	20,335	17,045	21,748
Endowment Income	8,727	21,110	19,556	16,176	15,544
Sales and Services	333,262	307,929	280,484	268,455	255,593
Other Revenues	29,790	15,506	13,027	15,547	9,231
Total Current Funds Revenues	**$1,456,672**	**$1,299,438**	**$1,220,681**	**$1,127,248**	**$1,062,282**

	For the Year Ended June 30,				
	2001	2000	1999	1998	1997
	%	%	%	%	%
Current Funds Revenues					
State Appropriations	27.6	29.5	31.3	31.3	31.2
Tuition and Fees	9.6	9.4	9.0	9.4	9.6
Federal Contracts and Grants	21.4	21.3	21.2	20.5	20.8
State Contracts and Grants	3.6	3.4	3.1	2.8	2.5
Nongovernmental Contracts and Grants	4.8	4.4	4.2	4.0	3.8
Gifts and Bequests	5.5	4.1	3.8	3.9	3.6
Investment Income	2.0	1.4	1.7	1.5	2.0
Endowment Income	0.6	1.6	1.6	1.4	1.5
Sales and Services	22.9	23.7	23.0	23.8	24.1
Other Revenues	2.0	1.2	1.1	1.4	0.9
Total Current Funds Revenues	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

(percent of total current funds revenues)

(in thousands)

	For the Year Ended June 30,				
	1996	1995	1994	1993	1992
Current Funds Revenues					
State Appropriations	$308,245	$302,337	$283,826	$270,700	$255,003
Tuition and Fees	88,478	81,465	75,531	66,718	60,247
Federal Contracts and Grants	219,878	208,802	190,534	172,288	147,556
State Contracts and Grants	24,607	26,394	22,696	17,948	15,498
Nongovernmental Contracts and Grants	39,710	36,980	36,218	35,276	35,041
Gifts and Bequests	34,464	30,688	27,928	25,544	23,851
Investment Income	15,274	12,726	13,748	14,534	15,828
Endowment Income	13,599	13,798	11,895	9,212	8,040
Sales and Services	233,888	224,600	210,767	187,390	176,297
Other Revenues	6,526	5,679	4,246	4,632	3,847
Total Current Funds Revenues	**$984,669**	**$943,469**	**$877,389**	**$804,242**	**$741,208**

	For the Year Ended June 30,				
	1996	1995	1994	1993	1992
	%	%	%	%	%
Current Funds Revenues					
State Appropriations	31.3	32.1	32.3	33.7	34.4
Tuition and Fees	9.0	8.6	8.6	8.3	8.1
Federal Contracts and Grants	22.3	22.1	21.7	21.4	19.9
State Contracts and Grants	2.5	2.8	2.6	2.2	2.1
Nongovernmental Contracts and Grants	4.0	3.9	4.1	4.4	4.8
Gifts and Bequests	3.5	3.3	3.2	3.2	3.2
Investment Income	1.5	1.3	1.6	1.8	2.1
Endowment Income	1.4	1.5	1.4	1.1	1.1
Sales and Services	23.8	23.8	24.0	23.3	23.8
Other Revenues	0.7	0.6	0.5	0.6	0.5
Total Current Funds Revenues	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

(percent of total current funds revenues)

Current Funds Revenues by Source

ADJUSTED FOR INFLATION (1992 DOLLARS) LAST TEN FISCAL YEARS

(in thousands)

For the Year Ended June 30,	2001	2000	1999	1998	1997
Current Funds Revenues					
State Appropriations	$316,793	$311,619	$322,554	$303,007	$290,064
Tuition and Fees	109,733	98,813	93,129	90,954	89,452
Federal Contracts and Grants	245,603	224,896	218,611	199,279	193,768
State Contracts and Grants	41,366	36,418	31,693	26,895	23,091
Nongovernmental Contracts and Grants	55,405	46,162	43,130	38,472	35,065
Gifts and Bequests	63,017	43,495	39,358	38,114	33,407
Investment Income	22,589	15,141	17,154	14,661	19,021
Endowment Income	6,874	17,167	16,497	13,913	13,595
Sales and Services	262,491	250,416	236,606	230,904	223,544
Other Revenues	23,464	12,610	10,989	13,372	8,074
Total Current Funds Revenues	**$1,147,335**	**$1,056,737**	**$1,029,721**	**$969,571**	**$929,081**

For the Year Ended June 30,	2001	2000	1999	1998	1997
	%	%	%	%	%
Current Funds Revenues					
State Appropriations	27.6	29.5	31.3	31.3	31.2
Tuition and Fees	9.6	9.4	9.0	9.4	9.6
Federal Contracts and Grants	21.4	21.3	21.2	20.5	20.9
State Contracts and Grants	3.6	3.4	3.1	2.8	2.5
Nongovernmental Contracts and Grants	4.8	4.4	4.2	4.0	3.8
Gifts and Bequests	5.5	4.1	3.8	3.9	3.6
Investment Income	2.0	1.4	1.7	1.5	2.0
Endowment Income	0.6	1.6	1.6	1.4	1.5
Sales and Services	22.9	23.7	23.0	23.8	24.0
Other Revenues	2.0	1.2	1.1	1.4	0.9
Total Current Funds Revenues	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

(percent of total current funds revenues)

	2001	2000	1999	1998	1997
Consumer Price Index	178.0	172.4	166.2	163.0	160.3

(in thousands)

	For the Year Ended June 30,				
	1996	**1995**	**1994**	**1993**	**1992**
Current Funds Revenues					
State Appropriations	$275,788	$277,952	$268,868	$262,826	$255,003
Tuition and Fees	79,162	74,894	71,550	64,777	$60,247
Federal Contracts and Grants	196,726	191,961	180,492	167,277	$147,556
State Contracts and Grants	22,016	24,265	21,500	17,426	$15,498
Nongovernmental Contracts and Grants	35,529	33,997	34,309	34,250	$35,041
Gifts and Bequests	30,835	28,213	26,456	24,801	$23,851
Investment Income	13,666	11,700	13,023	14,111	$15,828
Endowment Income	12,167	12,685	11,268	8,944	$8,040
Sales and Services	209,260	206,485	199,659	181,940	$176,297
Other Revenues	5,839	5,221	4,022	4,497	$3,847
Total Current Funds Revenues	**$880,988**	**$867,373**	**$831,147**	**$780,849**	**$741,208**

	For the Year Ended June 30,				
	1996	**1995**	**1994**	**1993**	**1992**
	%	%	%	%	%
Current Funds Revenues					
State Appropriations	31.2	32.1	32.3	33.7	34.4
Tuition and Fees	9.0	8.6	8.6	8.3	8.1
Federal Contracts and Grants	22.3	22.1	21.7	21.4	19.9
State Contracts and Grants	2.5	2.8	2.6	2.2	2.1
Nongovernmental Contracts and Grants	4.0	3.9	4.1	4.4	4.8
Gifts and Bequests	3.5	3.3	3.2	3.2	3.2
Investment Income	1.6	1.3	1.6	1.8	2.1
Endowment Income	1.4	1.5	1.4	1.1	1.1
Sales and Services	23.8	23.8	24.0	23.3	23.8
Other Revenues	0.7	0.6	0.5	0.6	0.5
Total Current Funds Revenues	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

(percent of total current funds revenues)

Consumer Price Index	156.7	152.5	148.0	144.4	140.2

CURRENT FUNDS EXPENDITURES AND MANDATORY TRANSFERS BY FUNCTION

LAST TEN FISCAL YEARS

(in thousands)

	For the Year Ended June 30,				
	2001	**2000**	**1999**	**1998**	**1997**
Current Funds Expenditures					
Instruction	$490,447	$435,839	$411,292	$383,759	$352,711
Organized Research	213,833	186,550	174,973	161,128	152,478
Public Service	89,663	89,906	86,062	78,678	70,106
Academic Support	75,226	63,528	60,384	56,528	53,663
Student Services	16,679	14,735	13,662	12,661	11,763
Institutional Support	51,122	48,165	58,078	49,309	44,105
Plant Maintenance and Operations	72,745	69,525	65,501	63,359	60,224
Student Financial Aid	54,670	49,844	44,305	41,674	38,625
Auxiliary Enterprises and Internal Services	135,706	127,443	121,148	112,844	101,556
Professional and Clinical Services	167,703	156,522	133,057	135,099	116,393
Other Expenditures and Deductions	0	0	0	5,974	5,669
Total Current Funds Expenditures	**1,367,794**	**1,242,057**	**1,168,462**	**1,101,013**	**1,007,293**
Current Funds Mandatory Transfers	**27,481**	**27,620**	**20,079**	**22,852**	**29,007**
Total Current Funds Expenditures and Mandatory Transfers	**$1,395,275**	**$1,269,677**	**$1,188,541**	**$1,123,865**	**$1,036,301**

	For the Year Ended June 30,				
	2001	**2000**	**1999**	**1998**	**1997**
	%	%	%	%	%
Current Funds Expenditures					
Instruction	35.2	34.3	34.6	34.1	34.0
Organized Research	15.3	14.7	14.7	14.3	14.7
Public Service	6.4	7.1	7.2	7.0	6.8
Academic Support	5.4	5.0	5.1	5.0	5.2
Student Services	1.2	1.2	1.2	1.1	1.1
Institutional Support	3.7	3.8	4.9	4.4	4.3
Plant Maintenance and Operations	5.2	5.5	5.5	5.7	5.8
Student Financial Aid	3.9	3.9	3.7	3.7	3.8
Auxiliary Enterprises and Internal Services	9.7	10.0	10.2	10.1	9.8
Professional and Clinical Services	12.0	12.3	11.2	12.0	11.2
Other Expenditures and Deductions			0.6	0.5	
Total Current Funds Expenditures	**98.0**	**97.8**	**98.3**	**98.0**	**97.2**
Current Funds Mandatory Transfers	**2.0**	**2.2**	**1.7**	**2.0**	**2.8**
Total Current Funds Expenditures and Mandatory Transfers	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

(percent of total current funds expenditures and mandatory transfers)

(in thousands)

	For the Year Ended June 30,				
	1996	**1995**	**1994**	**1993**	**1992**
Current Funds Expenditures					
Instruction	$326,546	$301,323	$278,587	$253,662	$241,956
Organized Research	156,034	154,817	140,586	130,570	115,014
Public Service	65,502	68,317	62,834	56,111	52,952
Academic Support	47,771	43,423	40,507	35,845	32,740
Student Services	10,986	9,998	9,191	8,585	7,624
Institutional Support	41,500	37,698	36,800	32,118	30,097
Plant Maintenance and Operations	62,402	59,662	58,447	49,606	48,552
Student Financial Aid	31,479	29,595	28,030	26,997	23,715
Auxiliary Enterprises and Internal Services	89,946	89,532	80,587	85,774	73,199
Professional and Clinical Services	108,282	99,140	97,265	85,187	74,769
Other Expenditures and Deductions	1,027	1,391	4,125	1,197	345
Total Current Funds Expenditures	**941,475**	**894,896**	**836,959**	**765,652**	**700,963**
Current Funds Mandatory Transfers	**24,084**	**20,758**	**21,158**	**18,140**	**9,066**
Total Current Funds Expenditures and Mandatory Transfers	**$965,559**	**$915,654**	**$858,117**	**$783,792**	**$710,029**

	For the Year Ended June 30,				
	1996	**1995**	**1994**	**1993**	**1992**
	%	%	%	%	%
Current Funds Expenditures					
Instruction	33.8	32.9	32.5	32.4	34.1
Organized Research	16.2	16.9	16.4	16.7	16.2
Public Service	6.8	7.5	7.3	7.2	7.5
Academic Support	4.9	4.7	4.7	4.6	4.6
Student Services	1.1	1.1	1.1	1.1	1.1
Institutional Support	4.3	4.1	4.3	4.1	4.2
Plant Maintenance and Operations	6.5	6.5	6.8	6.3	6.8
Student Financial Aid	3.3	3.2	3.3	3.4	3.3
Auxiliary Enterprises and Internal Services	9.3	9.8	9.4	10.9	10.3
Professional and Clinical Services	11.2	10.8	11.3	10.9	10.5
Other Expenditures and Deductions	0.1	0.2	0.4	0.1	0.1
Total Current Funds Expenditures	**97.5**	**97.7**	**97.5**	**97.7**	**98.7**
Current Funds Mandatory Transfers	**2.5**	**2.3**	**2.5**	**2.3**	**1.3**
Total Current Funds Expenditures and Mandatory Transfers	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

(percent of total current funds expenditures and mandatory transfers)

Ten Year SUMMARY OF RATIOS

LAST TEN FISCAL YEARS

RATIO OF TOTAL CURRENT REVENUES TO TOTAL CURRENT EXPENDITURES

(in thousands)

For the Year Ended June 30,	2001	2000	1999	1998	1997
Total Current Revenues	$1,456,672	$1,299,438	$1,220,681	$1,127,248	$1,062,282
Total Current Expenditures and Mandatory Transfers	1,395,275	1,269,677	1,188,541	1,123,865	1,036,301
Ratio	**104.40%**	**102.34%**	**102.70%**	**100.30%**	**102.51%**

This ratio indicates the percentage of current funds revenues that remain after all current funds expenditures and mandatory transfers are applied. A percentage greater than 100% indicates a surplus for the year. The larger the surplus, the stronger the institution's financial position as a result of the year's operations. Large deficits are usually a bad sign, particularly if they occur in successive years. A pattern of large deficits can reduce an institution's financial strength. Such a pattern is a warning signal that corrective action should be taken.

RATIO OF AVAILABLE FUNDS TO EDUCATIONAL AND GENERAL EXPENDITURES AND MANDATORY TRANSFERS

(in thousands)

For the Year Ended June 30,	2001	2000	1999	1998	1997
Current Fund Balance - General	$115,263	$86,061	$60,828	$54,643	$60,437
Current Fund Balance - Proprietary	170,668	162,193	165,090	157,697	154,264
Quasi Endowment Fund Balance - Unrestricted	106,682	121,441	98,556	85,787	48,704
Total Availability	392,613	369,695	324,474	298,127	263,405
Total Availability	392,613	369,695	324,474	298,127	263,405
Educational and General Expenditures and Mandatory Transfers	1,091,866	985,712	934,336	869,948	812,682
Ratio	**35.96%**	**37.51%**	**34.73%**	**34.27%**	**32.41%**

This ratio measures the size of the institution's financial reserves. Increasing ratios indicate better preparation for financial disruptions. The University receives its state appropriations on a quarterly allotment basis and state appropriations are not accrued at year end to finance accrued expenses.

(in thousands)

	For the Year Ended June 30,				
	1996	**1995**	**1994**	**1993**	**1992**
Total Current Revenues	$984,669	$943,469	$877,389	$804,242	$741,208
Total Current Expenditures and Mandatory Transfers	965,559	915,654	858,117	783,792	710,029
Ratio	**101.98%**	**103.04%**	**102.25%**	**102.61%**	**104.39%**

(in thousands)

	For the Year Ended June 30,				
	1996	**1995**	**1994**	**1993**	**1992**
Current Fund Balance - General	$53,902	$49,726	$44,104	$37,536	$29,681
Current Fund Balance - Proprietary	149,134	140,429	127,098	116,643	111,371
Quasi Endowment Fund Balance - Unrestricted	35,640	34,988	36,656	36,066	33,761
Total Availability	238,676	225,143	207,858	190,245	174,813
Total Availability	238,676	225,143	207,858	190,245	174,813
Educational and General Expenditures and Mandatory Transfers	766,304	725,591	676,140	611,634	561,716
Ratio	**31.15%**	**31.03%**	**30.74%**	**31.10%**	**31.12%**

TEN YEAR SUMMARY OF RATIOS *(continued)*

LAST TEN FISCAL YEARS

RATIO OF EXPENDABLE FUND BALANCE TO TOTAL EXPENDITURES AND MANDATORY TRANSFERS

(in thousands)

For the Year Ended June 30,

	2001	2000	1999	1998	1997
Current Fund Balance - General	$115,263	$86,061	$60,828	$54,643	$60,437
Current Fund Balance - Proprietary	170,668	162,193	165,090	157,697	154,264
Current Fund Balance - Restricted	207,040	147,942	137,437	112,855	94,072
Quasi Endowment Fund Balance	489,126	493,209	161,984	143,043	92,180
Unexpended Plant Fund Balance	63,159	55,581	86,670	72,332	61,063
Debt Service Fund Balance	24,761	28,485	28,628	32,329	26,454
Total Expendable Fund Balance	1,070,017	973,471	640,637	572,899	488,470
Total Expendable Fund Balance	1,070,017	973,471	640,637	572,899	488,470
Total Current Expenditures and Mandatory Transfers	1,395,275	1,269,677	1,188,541	1,123,865	1,036,301
Ratio	**76.69%**	**76.67%**	**53.90%**	**50.98%**	**47.14%**

This ratio is an important measure of financial strength relative to institutional operating size. Expendable fund balances should increase at least proportionally as the rate of growth of operating size. If this is not the case, the same dollar amount of expendable fund balances will provide less margin of protection against adversity as the institution grows in dollar level of expenditure.

RATIO OF INSTRUCTION AND ACADEMIC SUPPORT TO TOTAL EDUCATIONAL AND GENERAL EXPENDITURES LESS RESTRICTED SCHOLARSHIPS

(in thousands)

For the Year Ended June 30,

	2001	2000	1999	1998	1997
Instruction	$490,447	$435,839	$411,292	$383,759	$352,711
Other Academic Support	75,226	63,528	60,384	56,528	53,663
Total Instruction and Academic Support	565,673	499,367	471,676	440,287	406,374
Educational and General Expenditures and Mandatory Transfers	1,065,655	958,594	914,294	847,139	784,364
Less: Restricted Scholarships	25,853	24,953	19,945	21,489	20,705
Total Educational and General Expenditures less Restricted Scholarships	1,039,802	933,641	894,349	825,650	763,659
Total Instruction and Academic Support	565,673	499,367	471,676	440,287	406,374
Total Educational and General Expenditures less Restricted Scholarships	1,039,802	933,641	894,349	825,650	763,659
Ratio	**54.40%**	**53.49%**	**52.74%**	**53.33%**	**53.21%**

This ratio indicates whether the institution has been maintaining the allocation of resources to the academic program. If financial resources are decreasing, the instruction and academic support proportion may also decrease due to greater demands for administrative expenditures, such as admissions or fund raising. A decrease in instruction and academic support expenditures as a proportion of the operating budget may not indicate an absolute decline, specifically when there is an alternative increase in quality; however, such a change in quality is difficult to measure.

(in thousands)

	For the Year Ended June 30,				
	1996	**1995**	**1994**	**1993**	**1992**
Current Fund Balance - General	$53,902	$49,726	$44,104	$37,536	$29,681
Current Fund Balance - Proprietary	149,134	140,429	127,098	116,643	111,371
Current Fund Balance - Restricted	92,510	91,586	77,839	66,205	53,318
Quasi Endowment Fund Balance	71,023	64,935	66,525	63,364	56,024
Unexpended Plant Fund Balance	55,763	48,658	34,830	20,573	9,657
Debt Service Fund Balance	10,833	17,073	16,421	16,244	18,300
Total Expendable Fund Balance	433,165	412,407	366,817	320,565	278,351
Total Expendable Fund Balance	433,165	412,407	366,817	320,565	278,351
Total Current Expenditures and Mandatory Transfers	965,559	915,654	858,117	783,792	710,029
Ratio	**44.86%**	**45.04%**	**42.75%**	**40.90%**	**39.20%**

(in thousands)

	For the Year Ended June 30,				
	1996	**1995**	**1994**	**1993**	**1992**
Instruction	$326,546	$301,323	$278,587	$253,662	$241,956
Other Academic Support	47,771	43,423	40,507	35,845	32,740
Total Instruction and Academic Support	374,317	344,746	319,094	289,507	274,696
Educational and General Expenditures and Mandatory Transfers	742,277	705,323	656,305	595,696	555,404
Less: Restricted Scholarships	19,021	17,713	17,439	17,116	14,940
Total Educational and General Expenditures less Restricted Scholarships	723,256	687,610	638,866	578,580	540,464
Total Instruction and Academic Support	374,317	344,746	319,094	289,507	274,696
Total Educational and General Expenditures less Restricted Scholarships	723,256	687,610	638,866	578,580	540,464
Ratio	**51.75%**	**50.14%**	**49.95%**	**50.04%**	**50.83%**

TEN YEAR SUMMARY OF RATIOS *(continued)*

LAST TEN FISCAL YEARS

EDUCATIONAL EXPENDITURES PER STUDENT

(in thousands)

	For the Year Ended June 30,				
	2001	**2000**	**1999**	**1998**	**1997**
Total Current Fund Expenditures	$1,367,794	$1,242,057	$1,168,462	$1,101,013	$1,007,293
Plus: Current Fund Mandatory Transfers	27,481	27,620	20,079	22,852	29,007
Less: Student Financial Aid	54,670	49,844	44,305	41,674	38,625
Less: Auxiliary Enterprises Expenditures	127,425	121,969	115,280	106,837	96,674
Less: Professional Clinical Services	167,703	156,522	133,057	135,099	116,393
Total Educational Expenditures	1,045,477	941,342	895,899	840,255	784,608
Total Educational Expenditures	1,045,477	941,342	895,899	840,255	784,608
Undergraduate, Graduate and Professional FTE	23,000	22,761	21,940	21,794	21,709
Educational Expenditures per Student (in thousands)	**$45.5**	**$41.4**	**$40.8**	**$38.6**	**$36.1**

This ratio measures average educational expenditures incurred per student FTE.

RATIO OF NET GAIN IN ENDOWMENT ASSETS

(in thousands)

	For the Year Ended June 30,				
	2001	**2000**	**1999**	**1998**	**1997**
Year - End Endowment Assets (Market Value)	$768,816	$750,321	$593,373	$554,029	$465,152
Year - Begin Endowment Assets (Market Value)	750,321	593,373	554,029	465,152	390,146
Yearly Change	18,495	156,948	39,344	88,877	75,006
Yearly Change	18,495	156,948	39,344	88,877	75,006
Year - Begin Endowment Assets (Market Value)	750,321	593,373	554,029	465,152	390,146
Ratio	**2.46%**	**26.45%**	**7.10%**	**19.11%**	**19.23%**

This ratio measures the growth of endowment assets resulting directly from investment policies and/or gifts. If the ratios are increasing, the endowment assets are growing through efficient investment of the endowment funds and/or additional gifts and transfers to the endowment funds.

(in thousands)

	For the Year Ended June 30,				
	1996	**1995**	**1994**	**1993**	**1992**
Total Current Fund Expenditures	$941,475	$894,896	$836,959	$765,652	$700,963
Plus: Current Fund Mandatory Transfers	24,084	20,758	21,158	18,140	9,066
Less: Student Financial Aid	31,479	29,595	28,030	26,997	23,715
Less: Auxiliary Enterprises Expenditures	88,032	83,823	76,560	81,907	56,996
Less: Professional Clinical Services	108,282	99,140	97,265	85,187	74,769
Total Educational Expenditures	737,766	703,096	656,262	589,701	554,549
Total Educational Expenditures	737,766	703,096	656,262	589,701	554,549
Undergraduate, Graduate and Professional FTE	21,961	21,918	21,758	21,398	21,391
Educational Expenditures per Student (in thousands)	**$33.6**	**$32.1**	**$30.2**	**$27.6**	**$25.9**

(in thousands)

	For the Year Ended June 30,				
	1996	**1995**	**1994**	**1993**	**1992**
Year - End Endowment Assets (Market Value)	$390,146	$335,076	$293,214	$223,948	$209,547
Year - Begin Endowment Assets (Market Value)	335,076	293,214	223,948	209,547	181,413
Yearly Change	55,070	41,862	69,266	14,401	28,134
Yearly Change	55,070	41,862	69,266	14,401	28,134
Year - Begin Endowment Assets (Market Value)	335,076	293,214	223,948	209,547	181,413
Ratio	**16.44%**	**14.28%**	**30.93%**	**6.87%**	**15.51%**

Ten Year SUMMARY OF RATIOS *(continued)*

LAST TEN FISCAL YEARS

RATIO OF UNRESTRICTED OPERATING RESOURCES TO DEBT

(in thousands)

For the Year Ended June 30,

	2001	2000	1999	1998	1997
Current Fund Balance - General	$115,263	$86,061	$60,828	$54,643	$60,437
Current Fund Balance - Proprietary	170,668	162,193	165,090	157,697	154,264
Unrestricted Quasi Endowment Fund Balance	106,682	121,441	98,556	85,787	48,704
Unrestricted Unexpended Plant Fund Balance	1,433	1,828	1,837	6,291	3,112
Unrestricted Debt Service Fund Balance	5,892	6,725	5,211	11,305	7,453
Total Expendable Fund Balance	399,938	378,248	331,522	315,723	273,970
Total Expendable Fund Balance	399,938	378,248	331,522	315,723	273,970
Total Debt Outstanding	396,805	306,603	286,366	279,096	272,965
Ratio	**100.79%**	**123.37%**	**115.77%**	**113.12%**	**100.37%**

This ratio is a conservative measure of resources available to investors from unrestricted expendable reserves that excludes amounts designated for long-term investment.

RATIO OF TOTAL RESOURCES TO DEBT

(in thousands)

For the Year Ended June 30,

	2001	2000	1999	1998	1997
Current Fund Balance - General	$115,263	$86,061	$60,828	$54,643	$60,437
Current Fund Balance - Proprietary	170,668	162,193	165,090	157,697	154,264
Current Fund Balance - Restricted	207,040	147,942	137,437	112,855	94,072
Endowment Fund Balance	731,170	727,798	587,946	547,750	376,052
Unexpended Plant Fund Balance	63,159	55,581	86,670	72,332	61,063
Debt Service Fund Balance	24,761	28,485	28,628	32,329	26,454
Total Expendable Fund Balance	1,312,061	1,208,060	1,066,599	977,606	772,342
Total Expendable Fund Balance	1,312,061	1,208,060	1,066,599	977,606	772,342
Total Debt Outstanding	396,805	306,604	286,366	279,096	272,965
Ratio	**330.66%**	**394.01%**	**372.46%**	**350.28%**	**282.95%**

This ratio is a broad measure of resources to debt that includes the corpus of endowed contributions.

(in thousands)

	For the Year Ended June 30,				
	1996	**1995**	**1994**	**1993**	**1992**
Current Fund Balance - General	$53,902	$49,726	$44,104	$37,536	$29,681
Current Fund Balance - Proprietary	149,134	140,429	127,098	116,643	111,371
Unrestricted Quasi Endowment Fund Balance	35,640	34,988	36,656	36,066	33,761
Unrestricted Unexpended Plant Fund Balance	3,645	4,658	4,366	5,178	1,872
Unrestricted Debt Service Fund Balance	(6,238)	2,298	3,798	7,901	9,327
Total Expendable Fund Balance	236,083	232,099	216,022	203,324	186,012
Total Expendable Fund Balance	236,083	232,099	216,022	203,324	186,012
Total Debt Outstanding	232,028	238,176	225,834	230,825	222,548
Ratio	**101.75%**	**97.45%**	**95.66%**	**88.09%**	**83.58%**

(in thousands)

	For the Year Ended June 30,				
	1996	**1995**	**1994**	**1993**	**1992**
Current Fund Balance - General	$53,902	$49,726	$44,104	$37,536	$29,681
Current Fund Balance - Proprietary	149,134	140,429	127,098	116,643	111,371
Current Fund Balance - Restricted	92,510	91,586	77,839	66,205	53,318
Endowment Fund Balance	303,674	273,448	270,211	212,158	191,497
Unexpended Plant Fund Balance	55,763	48,658	34,830	20,573	9,657
Debt Service Fund Balance	10,833	17,073	16,421	16,244	18,300
Total Expendable Fund Balance	665,816	620,920	570,503	469,359	413,824
Total Expendable Fund Balance	665,816	620,920	570,503	469,359	413,824
Total Debt Outstanding	232,028	238,176	225,834	230,825	222,548
Ratio	**286.96%**	**260.70%**	**252.62%**	**203.34%**	**185.95%**

GROSS DEBT SERVICE COVERAGE

LAST TEN FISCAL YEARS

	For the Year Ended June 30,				(in thousands)
	2001	**2000**	**1999**	**1998**	**1997**
General Fund Increase in Fund Equity	$29,202	n/a	n/a	n/a	n/a
General Fund Mandatory Transfers	1,270	n/a	n/a	n/a	n/a
Proprietary Fund Increase in Fund Equity	8,475	(2,897)	7,393	2,699	5,130
Proprietary Fund Mandatory Transfers	26,135	27,118	20,042	22,809	28,318
Total Resources	**65,082**	**24,221**	**27,435**	**25,508**	**33,448**
Total Debt Service Requirements	27,250	22,952	21,136	19,547	19,342
Total Resources	65,082	24,221	27,435	25,508	33,448
Coverage	**2.39**	**1.06**	**1.30**	**1.30**	**1.73**

RATIO OF DEBT SERVICES TO CURRENT EXPENDITURES

LAST TEN FISCAL YEARS

	For the Year Ended June 30,				(in thousands)
	2001	**2000**	**1999**	**1998**	**1997**
Debt Service Requirements	27,250	22,952	21,136	19,547	19,342
Current Funds Expenditures	1,367,794	1,242,057	1,168,462	1,101,013	1,007,293
Ratio %	**1.99**	**1.85**	**1.81**	**1.78**	**1.92**

For the Year Ended June 30,				(in thousands)
1996	**1995**	**1994**	**1993**	**1992**
n/a	n/a	n/a	n/a	n/a
n/a	n/a	n/a	n/a	n/a
8,705	13,331	10,455	5,272	17,421
24,027	20,268	19,835	15,938	6,312
32,732	**33,599**	**30,290**	**21,210**	**23,733**
19,353	20,154	19,058	15,642	14,719
32,732	33,599	30,290	21,210	23,733
1.69	**1.67**	**1.59**	**1.36**	**1.61**

For the Year Ended June 30,				(in thousands)
1996	**1995**	**1994**	**1993**	**1992**
19,353	20,154	19,058	15,642	14,719
941,475	894,896	836,959	765,652	700,963
2.06	**2.25**	**2.28**	**2.04**	**2.10**

Photo by Dan Sears

THE UNIVERSITY
of NORTH CAROLINA
at CHAPEL HILL

A Constituent Institution of the
University of North Carolina System
and a component unit of the
State of North Carolina

2003

Comprehensive Annual Financial Report

Chapel Hill, North Carolina
Fiscal Year Ended June 30, 2003