

Middle Tennessee State University

FINANCIAL REPORT

For the Year Ended June 30, 2003



Office of the President

Middle Tennessee State University
110 Cope Administration Building
Murfreesboro, Tennessee 37132
615-898-2622
FAX: 615-898-2507



September 15, 2003

Dr. Charles Manning, Chancellor
The State University and Community
College System of Tennessee
1415 Murfreesboro Road, Suite 350
Nashville, TN 37217

Dear Chancellor Manning:

Enclosed is the annual Financial Report for the fiscal year ended June 30, 2003.
This report has been prepared in accordance with the Generally Accepted
Accounting Principles.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Sidney A. McPhee", written over a horizontal line.

Sidney A. McPhee
President



Vice President for Business and Finance
Middle Tennessee State University
211 Cope Administration Building
Murfreesboro, Tennessee 37132
615-898-2852
FAX: 615-898-5906



September 15, 2003

Dr. Sidney A. McPhee
President
Middle Tennessee State University
Murfreesboro, TN 37132

Dear Dr. McPhee:

I am transmitting the annual Financial Report for the fiscal year ended June 30, 2003.

This report has been prepared in accordance with Generally Accepted Accounting Principles. The Financial Report has not been audited. The last audit by the State Comptroller's Office was completed as of June 30, 2002. An audit is currently in progress for fiscal year ended June 30, 2003.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "John W. Cothem".

John W. Cothem
Vice President for
Business and Finance



MIDDLE TENNESSEE STATE UNIVERSITY

FINANCIAL REPORT

For the Year Ended June 30, 2003

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A Tennessee Board of Regents University

MTSU is an equal opportunity, non-racially identifiable, educational institution that does not discriminate against individuals with disabilities. BF012-0803

MIDDLE TENNESSEE STATE UNIVERSITY
Management's Discussion and Analysis
For the Year Ended June 30, 2003

This section of Middle Tennessee State University's annual financial report presents a discussion and analysis of the financial performance of the University during the fiscal year ended June 30, 2003, with comparative information presented for the fiscal year ended June 30, 2002. This discussion has been prepared by management along with the financial statements and related note disclosures and should be read in conjunction with the financial statements and notes. The financial statements, notes, and this discussion are the responsibility of management.

Using This Annual Report

This report consists of three basic financial statements. The Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; and the Statement of Cash Flows provide information on Middle Tennessee State University as a whole and present a long-term view of the University's finances.

The Statement of Net Assets

The Statement of Net Assets presents the financial position of the University at the end of the fiscal year and includes all assets and liabilities of the University. The difference between total assets and total liabilities—net assets—is an indicator of the current financial condition of the University. Assets and liabilities are generally measured using current values. A notable exception occurs with capital assets, which are stated at historical cost less an allowance for depreciation.

Net assets are divided into three major categories. The first category is Invested in Capital Assets, Net of Debt. It provides the University's equity in property, plant, and equipment owned by the University. The next asset category is Restricted Net Assets, which is divided into two subcategories, Nonexpendable and Expendable. The corpus of nonexpendable restricted resources is only available for investment purposes. Expendable restricted net assets are available for expenditure by the University but must be spent for purposes as determined by donors and/or external entities that have placed time or purpose restrictions on the use of the assets. The final category is Unrestricted Net Assets. Unrestricted assets are available for any lawful purpose of the institution.

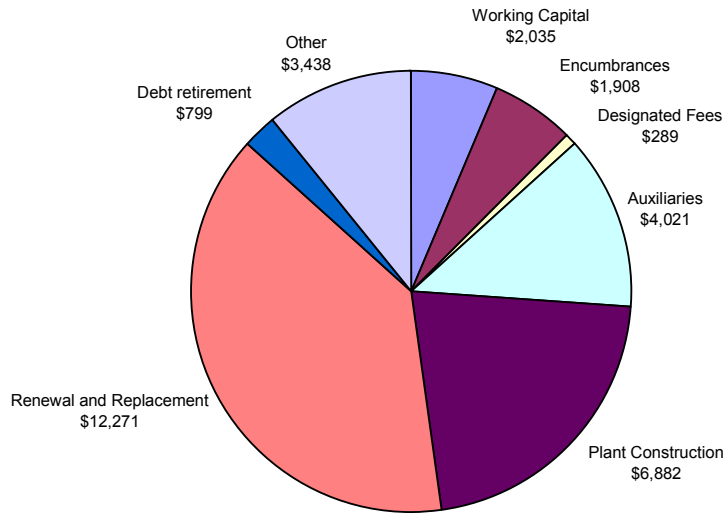
Statement of Net Assets
(in thousands of dollars)

	2003	2002
Assets		
Current assets	\$ 90,793	\$ 82,655
Capital assets, net	170,627	165,702
Other assets	25,848	27,340
Total Assets	\$ 287,268	\$ 275,697
Liabilities		
Current liabilities	\$ 75,210	\$ 69,340
Noncurrent liabilities	84,878	80,177
Total Liabilities	\$ 160,088	\$ 149,517
Net Assets		
Invested in capital assets, net of debt	\$ 89,235	\$ 87,837
Restricted - expendable	5,585	6,871
Restricted - nonexpendable	716	626
Unrestricted	31,643	30,846
Total Net Assets	\$ 127,179	\$ 126,180

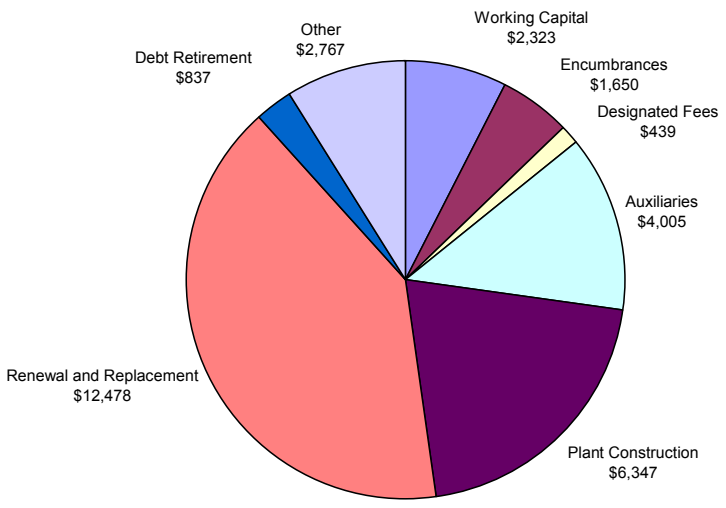
- ◆ Current assets increased by \$8,137,526. This increase is partially due to an increase in the Other Assets category, which is made up of the MTSU Foundation's capital assets. This was primarily the result of the addition of the Tennessee Miller Coliseum. Short-term investments also increased significantly, the result of donations to the MTSU Foundation.
- ◆ Current liabilities increased by \$5,870,318. This increase in current liabilities is primarily the result of an increase in deposits held in custody for others. The increase is attributed to the construction of the Tennessee Miller Coliseum by the MTSU Foundation, along with additions of current year donations.
- ◆ Noncurrent liabilities increased by \$4,701,355. The most significant cause for the increase was the issuance of commercial paper by the Tennessee State School Bond Authority (TSSBA) on behalf of the University for the following projects: purchase of Steinway pianos for the School of Music, purchase of a new fleet of airplanes for the Aerospace Department, property acquisitions around the perimeter of the campus, and renovation of the Smith Hall Complex for student housing.

Many of the University's unrestricted net assets have been designated or reserved for specific purposes such as repairs and replacement of equipment, future debt service, quasi-endowments, capital projects, and student loans. The following graphs show the allocations (in thousands of dollars).

Allocations of Unrestricted Net Assets 2003



Allocations of Unrestricted Net Assets 2002



- ◆ Plant construction increased by \$534,855. This is the result of increases in various capital project balances, which are funded by both appropriations and local funds, netted with decreases in other capital project balances.
- ◆ The Other category increased by \$670,427. Factors contributing to this increase were an increase in the allocation for the 2003–2004 budget and an increase in unrestricted net assets.

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

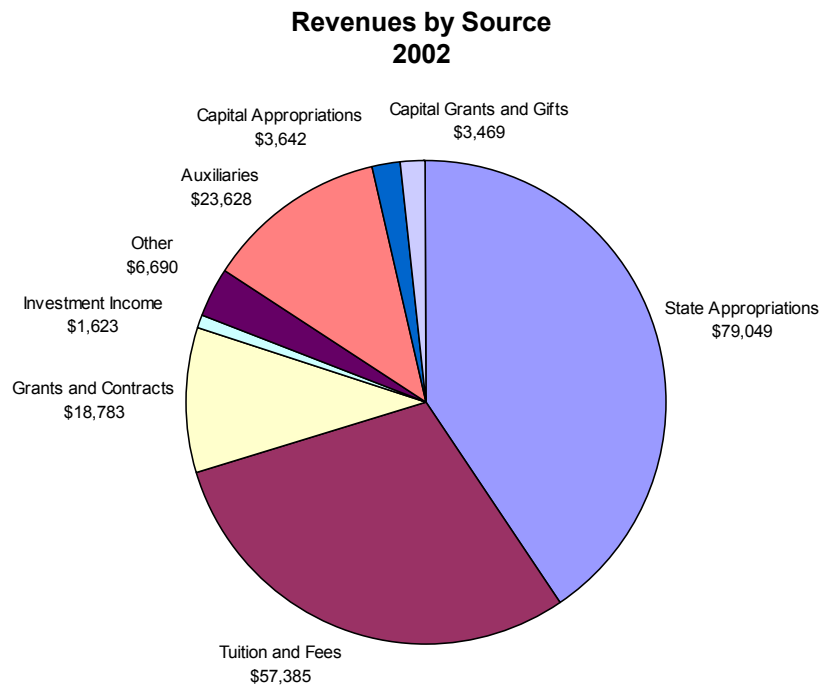
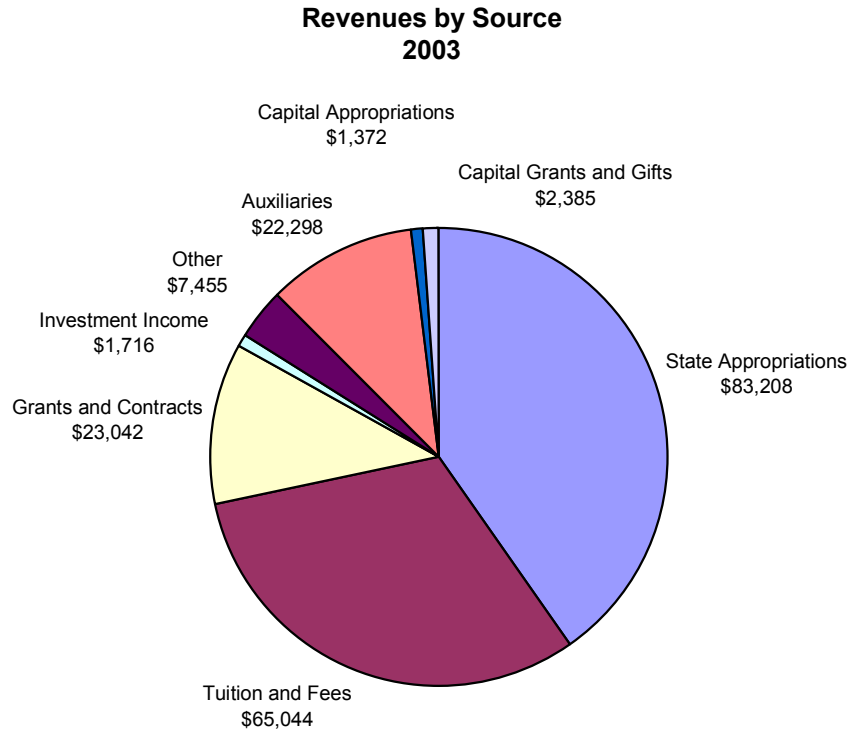
The Statement of Revenues, Expenses, and Changes in Net Assets presents the operating results of the University and the nonoperating revenues and expenses. Annual state appropriations, while budgeted for operations, are considered nonoperating revenues according to generally accepted accounting principles.

Statement of Revenues, Expenses, and Changes In Net Assets (in thousands of dollars)

	2003	2002
Operating revenues		
Net tuition and fees	\$ 65,044	\$ 57,385
Auxiliaries	22,298	23,627
Grants and contracts	23,042	18,783
Other	5,956	4,975
Total operating revenues	\$ 116,340	\$ 104,770
Operating expenses	\$ 201,150	\$ 188,710
Operating loss	\$ (84,810)	\$ (83,940)
Nonoperating revenues and expenses		
State appropriations	\$ 83,208	\$ 79,049
Gifts	929	901
Investment income	1,716	1,623
Other revenues and expenses	(3,597)	(3,112)
Total nonoperating revenues and expenses	\$ 82,256	\$ 78,461
Income (loss) before other revenues, expenses, gains, or losses	\$ (2,554)	\$ (5,479)
Other revenues, expenses, gains, or losses		
Capital appropriations	\$ 1,372	\$ 3,642
Capital grants and gifts	2,385	3,469
Other	(52)	
Total revenues, expenses, gains, or losses	\$ 3,705	\$ 7,111
Increase (decrease) in net assets	\$ 1,151	\$ 1,632
Net assets at beginning of year, as originally reported	\$ 126,180	\$ 258,152
Cumulative effect of changes in accounting principle		(131,675)
	\$ 126,180	\$ 126,477
Net assets at beginning of period, restated		
Prior period adjustment	\$ (152)	\$ (1,929)
Net assets at end of year	\$ 127,179	\$ 126,180

Revenues

The following is a graphic illustration of revenues, operating and nonoperating, used to fund the University's operating activities for the year ended June 30, 2003, and the year ended June 30, 2002 (in thousands of dollars).



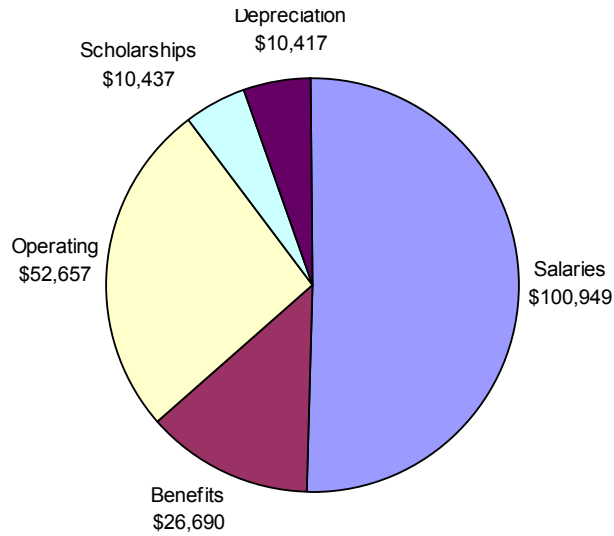
- ◆ Tuition and fees increased by \$7,658,425. Student enrollment increased approximately 5% from fall 2001 to fall 2002. Across-the-board fee increases were approved for 2002–2003 by the Tennessee Board of Regents, thus increasing student fees by 8%.
- ◆ Grants and contracts increased by \$4,258,983. This increase was due to an increase in the University’s Pell Grant award of approximately \$1,800,000, significant increases in existing grant program revenues, and the addition of several new grant programs.
- ◆ Capital appropriations decreased by \$2,270,184. This decrease in capital appropriations was the result of fewer capital projects being approved by the Tennessee State Building Commission for 2002–2003.

Expenses

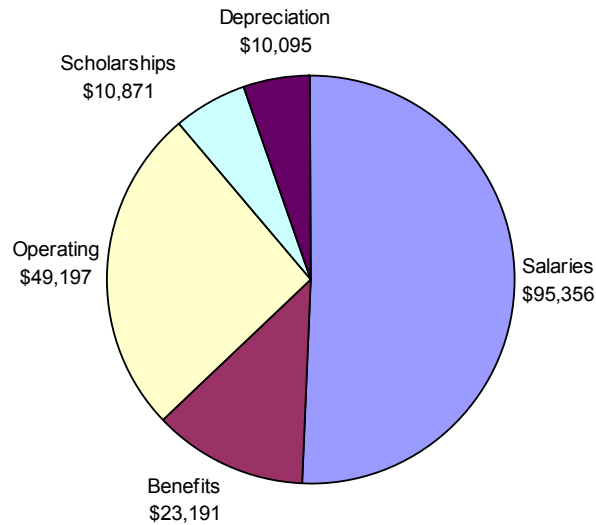
Operating expenses can be displayed in two formats, natural classification and program classification. Both formats are displayed below in thousands.

Natural Classification (in thousands)		
	2003	2002
Salaries	\$ 100,949	\$ 95,356
Benefits	26,690	23,191
Operating	52,657	49,197
Scholarships	10,437	10,871
Depreciation	10,417	10,095
TOTAL	\$ 201,150	\$ 188,710

**Expenses by Natural Classification
2003**



**Expenses by Natural Classification
2002**

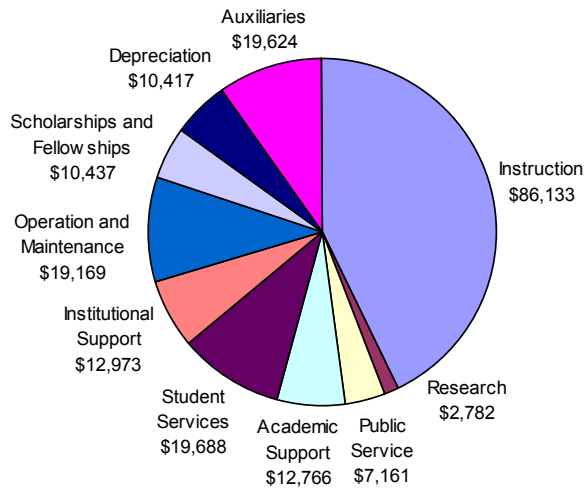


- ◆ Salaries increased by \$5,592,235. This increase in salary expenses is primarily due to salary increases given to employees in January 2002 (2% for faculty and 1% for administrative and classified) and January 2003 (5% for faculty and 4% for administrative and classified). Other factors contributing to this increase are faculty promotions, new faculty positions, and new Public Safety officer positions.
- ◆ Benefits increased by \$3,498,740. The increase is due to increases in the state's group insurance premiums in January 2002 and January 2003, an increase in TCRS rates, and added benefits for new positions.

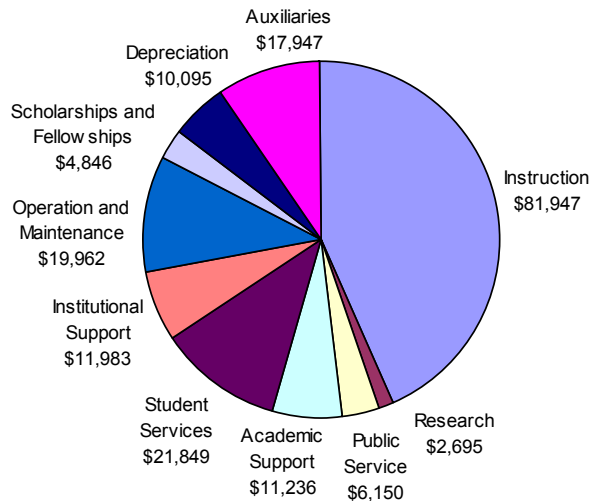
Program Classification
(in thousands)

	2003	2002
Instruction	\$ 86,133	\$ 81,947
Research	2,782	2,695
Public Service	7,161	6,150
Academic Support	12,766	11,236
Student Services	19,688	21,849
Institutional Support	12,973	11,983
Operation and Maintenance	19,169	19,962
Scholarships and Fellowships	10,437	4,846
Auxiliaries	19,624	17,947
Depreciation	10,417	10,095
TOTAL	\$201,150	\$188,710

Expenses by Program Classification
2003



Expenses by Program Classification
2002



- ◆ The Instruction function increased by \$4,185,885. This increase is primarily the result of faculty salary increases in January 2002 and January 2003, faculty promotions, and new faculty positions.
- ◆ The Scholarship function increased by \$5,591,145. Starting in 2002–2003, all scholarship expenses are shown in the Scholarship function rather than reported as part of each other function. The result of this reporting is a significant increase in expenses in the Scholarship function for 2002–2003.

The Statement of Cash Flows

The Statement of Cash Flows provides information about cash receipts and cash payments during the year. This statement also assists users in assessing the University's ability to generate net cash flows, its ability to meet its obligations as they come due, and its need for external financing.

	2003	2002
Cash provided (used) by		
Operating activities	\$(72,668)	\$(70,155)
Noncapital financing activities	83,469	77,653
Capital and related financing activities	(11,659)	(5,868)
Investing activities	1,684	1,666
Net increase (decrease) in cash	\$ 826	\$ 3,296
Cash, beginning of year	58,901	55,605
Cash, end of year	\$ 59,727	\$ 58,901

- ◆ In the noncapital financing activities section of the Statement of Cash Flows, state appropriations increased by \$5,330,100 over the previous year.
- ◆ In the capital and related financing activities section, capital appropriations decreased by \$2,270,184. Capital grants and gifts received also decreased by \$3,260,352, primarily the result of gifts received in 2001–2002 for the construction of the Paul W. Martin, Sr., Honors College Building.
- ◆ The University's cash position for the year increased by \$825,960.

Capital Asset and Debt Administration

Capital Assets

At June 30, 2003, Middle Tennessee State University had \$170,627,179 invested in capital assets, net of accumulated depreciation of \$113,865,683. Depreciation charges totaled \$10,416,727 for the current fiscal year. Details of these assets are shown below.

**Schedule of Capital Assets, Net of Depreciation
(in thousands of dollars)**

	2003	2002
Land	\$ 4,527	\$ 4,449
Land improvements and infrastructure	13,195	14,142
Buildings	124,449	128,186
Equipment	12,438	9,182
Library holdings	8,323	7,851
Projects in progress	7,695	1,891
Total	\$170,627	\$165,701

Some highlights of the information presented on the Schedule of Capital Assets, Net of Depreciation are as follows:

- ◆ Buildings decreased by \$3,736,813. This decrease is the result of the recording of the current year building depreciation of \$4,819,861 and the completion of only one building. The Development Facility amount of \$1,146,773 was transferred in from Projects in Progress.
- ◆ Equipment increased by \$3,255,955 primarily from the purchase of Steinway pianos in the amount of \$1,226,646 from donated funds to the School of Music and the purchase of a new fleet of airplanes for the Aerospace Department totaling \$1,987,024 for the fiscal year.
- ◆ Projects in Progress increased by \$5,803,909. Major projects under construction during the year included the construction of the Paul W. Martin, Sr., Honors College Building; construction of a pad to mount a donated 727 jet; improvements to several parking areas throughout campus; renovations to several housing facilities; renovations to the Keathley University Center; and the planning phase for the renovation of the Todd Building.

The following projects will be underway during the next fiscal year:

- ◆ The Todd Building, formerly the Todd Library, is being renovated to house the Art Department and the Albert Gore Research Center. The project will be substantially complete the beginning of fiscal year 2004–2005. The total project cost is \$9,355,000 and is funded by state capital funds.
- ◆ University housing facilities are in the initial phase of a 10-year renovation plan that includes major renovation of most of the housing facilities. Renovation plans for fiscal year 2003–2004 include major renovations of Beasley, Sims, Judd, and Gracy and minor renovations in Family Housing, Rutledge, and Monohan. These renovation projects are funded through TSSBA bond funds supported by housing auxiliary fees.
- ◆ The Paul W. Martin, Sr., Honors College Building, a 19,000 gross square foot structure is under construction. Substantial completion is expected during fiscal year 2003–2004. The project is funded through a \$2,000,000 gift by Paul W. Martin, Jr., and Lee Martin and \$2,000,000 matching gift funds by other generous donors.

Debt

At June 30, 2003, the University had \$81,392,341.95 in debt outstanding. The table below summarizes these amounts by type of debt instrument (in thousands of dollars).

	2003	2002
TSSBA Bonds	\$ 75,490	\$ 75,997
TSSBA Commercial Paper	5,902	1,867
Total Debt	\$ 81,392	\$ 77,864

The Tennessee State School Bond Authority (TSSBA) did not issue any new bonds on behalf of the University during the year; however, commercial paper was issued for the following four projects during the year: purchase of Steinway pianos for the School of Music, purchase of a new fleet of airplanes for the Aerospace Department, property acquisitions around the perimeter of the campus, and renovation of the Smith Hall Complex for student housing. TSSBA earned an “AA” bond rating for the fiscal year. More detailed information about the University’s long-term liabilities is presented in Note 9 to the financial statements.

Economic Factors That Will Affect The Future

The University began receiving notifications of potential reductions in state appropriations early in the second half of the fiscal year. These reductions were realized shortly thereafter and resulted in a 5% decrease, or \$4,284,400, from the original appropriations. State appropriations for the upcoming fiscal year 2003–2004 have also been reduced by approximately 9% or \$7,713,200.

Given the reductions in state appropriations for both fiscal years, the University has developed a budget that contains significant cuts in operating, travel, and capital outlay expenses. Salary and benefit expenses were also reduced by cutting positions across campus, both filled and unfilled. The University has taken measures to help deal with possible future reductions in appropriations.

Across-the-board fee increases have been approved by the Tennessee Board of Regents, which has increased student fees by 14%.

Requests for Information

This report is designed to provide a general overview for all those with an interest in the University’s finances. Questions concerning any of the information provided in this report or requests for additional financial information should be directed to Alan Thomas, Controller, CAB 105, Middle Tennessee State University, 1301 East Main Street, Murfreesboro, TN 37132.

BASIC FINANCIAL STATEMENTS

Middle Tennessee State University
Unaudited Statement of Net Assets
June 30, 2003, with comparative figures at June 30, 2002

ASSETS	<u>2003</u>	<u>2002</u>
Current assets:		
Cash and cash equivalents (Notes 3 and 4)	\$ 37,369,963.77	\$ 35,038,192.63
Short-term investments (Note 5)	20,107,679.91	18,004,475.08
Accounts, notes, and grants receivable (net) (Note 6)	9,320,244.70	9,529,796.75
Inventories (at lower of cost or market)	2,476,787.57	2,702,891.96
Prepaid expenses and deferred charges	730,102.34	389,720.78
Accrued interest receivable	52,806.31	80,236.19
Other assets	<u>20,735,166.96</u>	<u>16,909,912.45</u>
Total current assets	<u>90,792,751.56</u>	<u>82,655,225.84</u>
Noncurrent assets:		
Cash and cash equivalents (Notes 3 and 4)	22,357,293.61	23,863,104.85
Investments (Note 5)	697,319.67	657,880.41
Accounts, notes, and grants receivable (net) (Note 6)	2,793,178.07	2,777,376.26
Deposit with Trustees		41,642.80
Capital assets (net) (Note 7)	<u>170,627,178.98</u>	<u>165,701,661.87</u>
Total noncurrent assets	<u>196,474,970.33</u>	<u>193,041,666.19</u>
Total assets	<u>\$ 287,267,721.89</u>	<u>\$ 275,696,892.03</u>
 LIABILITIES		
Current liabilities:		
Accounts payable	\$ 1,982,611.39	\$ 2,017,414.28
Accrued liabilities	12,259,146.06	11,104,457.94
Student deposits	949,351.30	892,632.81
Deferred revenue	3,925,801.95	3,651,554.27
Compensated absences (Note 8)	1,051,274.65	1,668,834.24
Accrued interest payable	681,890.06	698,974.42
Long-term liabilities, current portion (Note 8)	2,522,927.44	2,390,069.35
Deposits held in custody for others	51,642,150.28	46,816,269.02
Other liabilities	<u>195,022.37</u>	<u>99,651.53</u>
Total current liabilities	<u>75,210,175.50</u>	<u>69,339,857.86</u>
Noncurrent liabilities:		
Compensated absences (Note 8)	3,003,574.85	2,119,002.75
Long-term liabilities (Note 8)	78,869,414.51	75,474,018.42
Due to grantors (Note 8)	<u>3,005,097.53</u>	<u>2,583,710.94</u>
Total noncurrent liabilities	<u>84,878,086.89</u>	<u>80,176,732.11</u>
Total liabilities	<u>\$ 160,088,262.39</u>	<u>\$ 149,516,589.97</u>
 NET ASSETS		
Invested in capital assets, net of related debt	\$ 89,234,837.03	\$ 87,837,574.10
Restricted for:		
Nonexpendable:		
Scholarships and fellowships	10,900.00	10,900.00
Other	704,747.30	614,899.93
Expendable:		
Scholarships and fellowships	98,655.30	59,177.92
Research	271,768.66	139,235.99
Instructional department uses	68,541.09	87,514.73
Loans	1,686,827.12	1,640,845.51
Capital projects	1,390,919.24	3,256,320.62
Debt service	1,360,799.66	908,158.61
Other	708,074.28	779,390.67
Unrestricted (Note 9)	<u>31,643,389.82</u>	<u>30,846,283.98</u>
Total net assets	<u>\$ 127,179,459.50</u>	<u>\$ 126,180,302.06</u>

The notes to the financial statements are an integral part of this statement.

Middle Tennessee State University
Unaudited Statement of Revenues, Expenses, and Changes in Net Assets
for the year ended June 30, 2003, with comparative figures at June 30, 2002

REVENUES	<u>2003</u>	<u>2002</u>
Operating revenues:		
Student tuition and fees (net of scholarship allowances of \$12,391,421.11 for the year ended June 30, 2003, and \$11,966,041.32 for the year ended June 30, 2002)	\$ 65,043,588.14	\$ 57,385,162.99
Governmental grants and contracts	22,414,057.25	18,090,920.19
Nongovernmental grants and contracts	627,451.29	691,605.20
Sales and services of educational departments	5,245,450.63	4,572,127.19
Auxiliary enterprises:		
Residential life (net of scholarship allowances of \$1,703,820.40 for the year ended June 30, 2003, and \$ -0- for the year ended June 30, 2002: all residential life revenues are used as security for revenue bonds, see Note 8)	8,883,196.20	10,635,144.14
Bookstore (net of scholarship allowances of \$1,394,034.88 for the year ended June 30, 2003, and \$ -0- for the year ended June 30, 2002: all bookstore revenues are used as security for revenue bonds, see Note 8)	7,083,866.49	8,187,911.61
Food service	530,126.77	475,246.47
Wellness facility (all wellness facility revenues are used as security for revenue bonds, see Note 8)	1,810,471.86	1,256,838.37
Other auxiliaries	3,990,830.05	3,072,368.11
Interest earned on loans to students	99,081.07	101,509.15
Other operating revenues	611,770.18	301,023.75
Total operating revenues	<u>\$ 116,339,889.93</u>	<u>\$ 104,769,857.17</u>
EXPENSES		
Operating Expenses		
Salaries and wages	\$ 100,948,724.09	\$ 95,356,489.53
Benefits	26,689,905.88	23,191,166.09
Utilities, supplies, and other services	52,657,097.29	49,196,528.07
Scholarships and fellowships	10,437,455.35	10,871,191.29
Depreciation expense	10,416,727.14	10,094,640.50
Total operating expenses	<u>201,149,909.75</u>	<u>188,710,015.48</u>
Operating loss	<u>\$ (84,810,019.82)</u>	<u>\$ (83,940,158.31)</u>
NONOPERATING REVENUES (EXPENSES)		
State appropriations	\$ 83,208,100.00	\$ 79,049,100.00
Gifts	929,155.27	901,142.70
Investment income (net of investment expense of \$73,728.87 for the year ended June 30, 2003, and \$527,095.16 for the year ended June 30, 2002)	1,715,902.70	1,623,221.14
Interest on capital asset-related debt	(4,165,982.47)	(3,926,514.41)
Other nonoperating revenues	569,383.04	814,275.35
Net nonoperating revenues	<u>82,256,558.54</u>	<u>78,461,224.78</u>
Income before other revenues, expenses, gains, or losses	<u>(2,553,461.28)</u>	<u>(5,478,933.53)</u>
Capital appropriations	<u>1,371,984.95</u>	<u>3,642,168.62</u>
Capital grants and gifts	2,385,156.27	3,469,196.77
Other	(52,188.69)	
Total other revenues	<u>3,704,952.53</u>	<u>7,111,365.39</u>
Increase in net assets	<u>\$ 1,151,491.25</u>	<u>\$ 1,632,431.86</u>
NET ASSETS		
Net Assets - beginning of year, as originally reported	\$ 126,180,302.06	\$ 258,152,160.84
Cumulative effect of changes in accounting principle:		
Adoption of capitalization criteria for buildings and additions		(2,234,914.27)
Adoption of depreciation for capital assets		(127,466,383.88)
Deferred revenue recognition		799,665.81
Reclassification of loan fund		(2,773,144.37)
Net assets - beginning of year, as restated	<u>\$ 126,180,302.06</u>	<u>\$ 126,477,384.13</u>
Prior period adjustment	(152,333.81)	(1,929,513.93)
Net Assets - end of year	<u>\$ 127,179,459.50</u>	<u>\$ 126,180,302.06</u>

The notes to the financial statements are an integral part of this statement.

Middle Tennessee State University
Unaudited Statement of Cash Flows
for the year ended June 30, 2003, with comparative figures at June 30, 2002

	2003	2002
CASH FLOWS FROM OPERATING ACTIVITIES		
Tuition and fees	\$ 65,201,861.09	\$ 58,937,540.43
Grants and contracts	22,673,635.27	18,206,771.92
Sales and services of educational activities	5,255,817.62	4,557,156.04
Payments to suppliers and vendors	(52,612,370.12)	(49,689,905.98)
Payments to employees	(101,228,414.24)	(92,551,989.45)
Payments for benefits	(24,917,519.83)	(22,459,781.06)
Payments for scholarships and fellowships	(10,437,455.35)	(10,871,191.29)
Loans issued to students and employees	(261,746.75)	
Collection of loans from students and employees	338,483.29	
Interest earned on loans to students	102,971.77	101,302.16
Auxiliary enterprise charges:		
Residence halls	8,873,249.48	10,675,289.34
Bookstore	7,450,550.97	7,795,352.44
Food services	489,587.63	504,418.88
Wellness facility	1,810,471.86	1,256,838.37
Other auxiliaries	3,980,982.17	3,081,994.42
Other receipts	611,770.18	301,023.75
Net cash flows used by operating activities	\$ (72,668,124.96)	\$ (70,155,180.03)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State appropriations	\$ 83,580,400.00	\$ 78,250,300.00
Gifts and grants received for other than capital or endowment purposes	858,345.67	868,287.86
Federal student loan receipts	49,697,262.36	136,707.54
Federal student loan disbursements	(49,623,102.27)	(154,773.86)
Changes in deposits held for others	(1,613,210.41)	(1,447,191.02)
Other noncapital financing receipts	569,383.04	
Net cash flows provided by noncapital financing activities	\$ 83,469,078.39	\$ 77,653,330.52
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from capital debt	\$ 6,431,620.90	\$ 13,035,264.76
Capital - state appropriation	1,371,984.95	3,642,168.62
Capital grants and gifts received	202,944.36	3,463,296.77
Proceeds from sale of capital assets	(52,188.69)	
Purchase of capital assets and construction	(12,519,718.92)	(11,508,395.79)
Principal paid on capital debt and lease	(2,903,366.72)	(9,760,455.47)
Interest paid on capital debt and lease	(4,190,230.17)	(3,828,777.91)
Deposit with trustee		(1,735,100.84)
Other capital and related financing receipts		823,817.22
Net cash flows used by capital and related financing activities	\$ (11,658,954.29)	\$ (5,868,182.64)

	<u>2003</u>	<u>2002</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments	\$ 12,000.00	\$ 66,449.43
Income on investments	1,723,960.76	1,691,127.32
Purchase of investments	(52,000.00)	(91,500.00)
Net cash provided by investing activities	<u>\$ 1,683,960.76</u>	<u>\$ 1,666,076.75</u>
Net increase in cash and cash equivalents	\$ 825,959.90	\$ 3,296,044.60
Cash and cash equivalents - beginning of year	58,901,297.48	55,605,252.88
Cash and cash equivalents - end of year (Note 3)	<u>\$ 59,727,257.38</u>	<u>\$ 58,901,297.48</u>
 RECONCILIATION OF OPERATING LOSS TO NET CASH USED BY OPERATING ACTIVITIES		
Operating loss	\$ (84,810,019.82)	\$ (83,940,158.31)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation expense	10,416,727.14	10,094,640.50
Change in assets and liabilities:		
Receivables, net	(344,455.19)	(735,107.07)
Inventories	226,104.39	(305,103.10)
Prepaid/deferred items	(298,738.76)	(84,483.82)
Other assets	3,890.70	(206.99)
Accounts payable	731,162.78	(718,575.69)
Accrued liabilities	1,161,851.46	3,222,612.53
Deferred revenues	274,247.68	1,767,634.38
Deposits	56,718.49	152,901.82
Compensated absences	267,012.51	338,105.56
Due to grantors	(371,260.64)	52,560.16
Loans to students and employees	(76,736.54)	
Other	95,370.84	
Net cash used by operating activities	<u>\$ (72,668,124.96)</u>	<u>\$ (70,155,180.03)</u>
 Non-cash transactions		
In-Kind Gifts, equipment	2,182,211.91	
Unrealized gains on investments	11,917.25	

The notes to the financial statements are an integral part of this statement.

MIDDLE TENNESSEE STATE UNIVERSITY

Notes to the Financial Statements

June 30, 2003

1. Summary of Significant Accounting Policies

REPORTING ENTITY

The institution is a part of the State University and Community College System of Tennessee (Tennessee Board of Regents). This system is a component unit of the State of Tennessee because the state appoints a majority of the system's governing body and provides financial support; the system is discretely presented in the **Tennessee Comprehensive Annual Financial Report**.

BASIS OF PRESENTATION

The financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). In June 1999, the GASB issued Statement No. 34, *Basic Financial Statements and Management Discussion and Analysis for State and Local Governments*. This was followed in November 1999 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 GASB No. 34 and No. 35 provides a comprehensive, entity-wide perspective of the institution's assets, liabilities, net assets, revenues, expenses, changes in net assets, and cash flows.

BASIS OF ACCOUNTING

For financial statement purposes, the institution is considered a special-purpose government engaged only in business-type activities. Accordingly, the financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. All significant interfund transactions have been eliminated.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board (GASB). The institution has the option of following private-sector guidance issued subsequent to November 30, 1989, subject to the above limitation. The institution has elected not to follow private-sector guidance issued subsequent to November 30, 1989.

Amounts reported as operating revenues include 1) tuition and fees, net of waivers and discounts; 2) federal, state, local and private grants and contracts; 3) sales and services of auxiliary enterprises; and 4) other sources of revenue. Operating expenses for the institution include 1) salaries and wages; 2) employee benefits; 3) scholarships and fellowships; 4) depreciation; and 5) utilities, supplies, and other services.

All other activity is nonoperating in nature. This activity includes 1) state appropriations for operations, 2) investment income, 3) bond issuance costs, 4) interest on capital asset-related debt, and 5) gifts.

When both restricted and unrestricted resources are available for use, generally it is the institution's policy to use the restricted resources first.

INVENTORIES

Inventories are valued at the lower of cost or market. Textbooks included in the inventory are recorded on a first-in, first-out basis. All other items are maintained on an average cost or first-in, first-out basis.

COMPENSATED ABSENCES

The institution's employees accrue annual leave at varying rates, depending upon length of service or classification. Some employees also earn compensatory time. The amount of these liabilities and their related benefits are reported in the Statement of Net Assets.

CAPITAL ASSETS

Capital assets, which include property, plant, equipment, and library holdings, are reported in the Statement of Net Assets at historical cost or at fair value at date of donation, less accumulated depreciation. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend the assets' useful lives are not capitalized.

A capitalization threshold of \$100,000 is used for buildings and \$50,000 is used for infrastructure. Equipment is capitalized when the unit acquisition cost is \$5,000 or greater. The capitalization threshold for additions and improvements to buildings and land is set at \$50,000.

These assets, with the exception of land, are depreciated using the straight-line method over the estimated useful lives of these assets, which range from 5 to 40 years.

MIDDLE TENNESSEE STATE UNIVERSITY FOUNDATION

The institution is the sole beneficiary of the Middle Tennessee State University Foundation. A board independent of the institution controls this private, nonprofit foundation. The institution handles the financial records, investments, and other financial transactions, and the assets and liabilities of the foundation are included on the institution's Statement of Net Assets.

NET ASSETS

The institution's net assets are classified as follows:

INVESTED IN CAPITAL ASSETS, NET OF RELATED DEBT. This represents the institution'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 consist of endowment and similar type funds in which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity and invested for the purpose of producing present and future income, which may be expendable or added to principal.

RESTRICTED NET ASSETS – EXPENDABLE. Restricted expendable net assets include resources in which the institution is legally or contractually obligated to spend resources in accordance with restrictions imposed by external third parties.

UNRESTRICTED NET ASSETS. Unrestricted net assets represent resources derived from student tuition and fees, state appropriations, and sales and services of educational departments and auxiliary enterprises. These resources are used for transactions relating to the educational and general operations of the institution and may be used at the discretion of the institution to meet current expenses for any purpose. The auxiliary enterprises are substantially self-supporting activities that provide services for students, faculty, and staff.

SCHOLARSHIP DISCOUNTS AND ALLOWANCES

Student tuition and fee revenues and certain other revenues from students are reported net of scholarship discount and allowances in the statement of revenues, expenses, and changes in net assets. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by the institution and the amount that is paid by the student and/or third parties making payments on the students' behalf. Certain governmental grants, such as Pell Grants, and other federal, state, or nongovernmental programs, are recorded as either operating or nonoperating revenues in the institution's financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees and other student charges, the institution has recorded a scholarship discount and allowance.

2. Independent Audit

The financial statements for the year ended June 30, 2003, are unaudited. The most recent audit covered the year ended June 30, 2002, for which an audit report has been issued. The institution received an unqualified opinion in the audit report for the year ended June 30, 2002. There is an audit in progress for the year ended June 30, 2003.

3. Cash and Cash Equivalents

In addition to demand deposits and petty cash on hand, this classification includes instruments which are readily convertible to known amounts of cash and which have original maturities of three months or less. At June 30, 2003, cash and cash equivalents consists of \$18,743,488.76 in bank accounts, \$115,115.00 of petty cash on hand, \$35,989,463.96 in the State of Tennessee Local Government Investment Pool administered by the State Treasurer, \$3,371,395.32 in the LGIP Deposits – Capital Projects account, and \$1,507,794.34 in a money market account.

LGIP Deposits – Capital Projects. Payments related to the institution's capital projects are made by the State of Tennessee's Department of Finance and Administration. The institution's estimated local share of the cost of each project is held in a separate Local

Government Investment Pool (LGIP) account. As expenses are incurred, funds are withdrawn from the LGIP account by the Tennessee Board of Regents and transferred to the Department of Finance and Administration. The funds in the account are not available to the institution for any other purpose until the project is completed and the Tennessee Board of Regents releases any remaining funds.

4. **Deposits**

The institution's bank accounts are in financial institutions that participate in the bank collateral pool administered by the State Treasurer. The securities pledged to protect these accounts are pledged in the aggregate rather than against each individual account. The members of the pool may be required by agreement to pay an assessment to cover any deficiency. Under this additional assessment agreement, public fund accounts covered by the pool are considered to be insured for purposes of credit risk disclosure.

At June 30, 2003, the carrying amount of the institution's deposits was \$20,251,283.10 and the bank balance was \$21,756,953.36. The bank balance was insured.

In accordance with the laws of the State of Tennessee, commercial banks have pledged securities as collateral for institution funds on deposit. The required collateral accepted as security for deposits shall be collateral whose market value is equal to either one hundred fifteen percent (115%), one hundred percent (100%), or ninety percent (90%) of the uninsured deposits. The pledge level is based on financial criteria set by the Collateral Pool Board with the financially strongest institutions being eligible for the lowest pledge level.

The institution also has deposits in the Local Government Investment Pool (LGIP) administered by the State Treasurer. The LGIP is part of the Pooled Investment Fund. The Pooled Investment Fund's investment policy and custodial credit risk are presented in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor, William R. Snodgrass Tennessee Tower, 312 Eighth Avenue North, Nashville, Tennessee 37242-0298 or by calling (615) 741-2140.

5. **Investments**

The institution is authorized by statute to invest funds in accordance with Tennessee Board of Regents policies. Under the current policy, funds other than endowments may be invested only in obligations of the United States or its agencies which are backed by the full faith and credit of the United States, repurchase agreements for United States securities, certificates of deposit in banks and savings and loan associations, banker's acceptances, commercial paper, money market mutual funds, and the State of Tennessee Local Government Investment Pool. The policy requires that investments of endowments in equity securities be limited to funds from private gifts or other sources external to the institution and that endowment investments be prudently diversified. The Middle Tennessee State University Foundation is authorized to invest funds in accordance with its board of directors' policies.

All investments permitted to be reported at fair value under GASB Statement 31 are reported at fair value, including those with a maturity date of one year or less at the time of purchase.

Investments of the Middle Tennessee State University Foundation are categorized below to give an indication of the level of risk assumed by the foundation at year-end. Category 1 consists of investments that are insured or registered or for which the securities are held by the foundation or its agent in the foundation's name. Category 2 consists of uninsured and unregistered investments for which the securities are held by the counter-party's/counter-parties' trust department or agent in the foundation's name. Category 3 consists of uninsured and unregistered investments for which the securities are held by the counter-party or by its trust department or agent but not in the foundation's name.

	Category			Fair Value
	1	2	3	
U.S. Government Securities	\$ -	\$ 339,778.87	\$ -	\$ 339,778.87
Corporate Stocks	-	11,186,087.74	-	11,186,087.74
Corporate Bonds	-	8,541,019.80	-	8,541,019.80
Totals	\$ -	\$ 20,066,886.41	\$ -	\$ 20,066,886.41
Mutual Funds				738,113.17
Total Investments per Statement of Net Assets				<u>\$ 20,804,999.58</u>

All category 2 investments belong to the Middle Tennessee State University Foundation. The foundation's Finance Committee makes all investment decisions of the foundation.

Investments of endowment and similar funds owned by the University are composed of the following:

	Carrying Value	
	FY 2002-03	FY 2001-02
Mutual Funds	\$697,319.67	\$657,880.41

Assets of endowment funds are pooled on a fair value basis with each individual fund subscribing to or disposing of units on the basis of the value per unit market value at the beginning of the calendar quarter within which the transaction takes place. The 133,495.67 units at June 30, 2003, each having a market value of \$5.22, were owned by quasi-endowments.

The following tabulation summarizes changes in relationships between cost and market values of the pooled assets:

	Pooled Assets		Net Gains (Losses)	Market Value Per Unit
	Market	Cost		
End of year	\$ 697,319.67	\$ 747,188.07	\$ (49,868.40)	\$ 5.22
Beginning of year	657,880.41	719,666.06	(61,785.65)	5.06
				<u>\$ 0.16</u>
Unrealized net gains			\$ 11,917.25	
Realized net gains			(2,746.45)	
Total net gains			<u>\$ 9,170.80</u>	

The average annual earnings per unit, exclusive of net gains, were \$.14 for the year.

Investments of endowment and similar funds owned by the foundation are composed of the following:

	Carrying Value	
	FY 2002-03	FY 2001-02
Mutual Funds	\$ 40,793.50	\$ 41,187.72

Assets of endowment funds are pooled on a fair value basis with each individual fund subscribing to or disposing of units on the basis of the value per unit market value at the beginning of the calendar quarter within which the transaction takes place. The 4,029.743 units at June 30, 2003, each having a market value of \$10.12, were owned by quasi-endowments.

The following tabulation summarizes changes in relationships between cost and market values of the pooled assets:

	Pooled Assets		Net Gains (Losses)	Market Value per Unit
	Market	Cost		
End of year	\$ 40,793.50	\$ 48,608.60	\$ (7,815.10)	\$ 10.12
Beginning of year	41,187.72	48,608.60	(7,420.88)	10.22
				<u>(0.10)</u>
Unrealized net gains (losses)			(394.22)	
Realized net gains			-	
Total net gains (losses)			<u>\$ (394.22)</u>	

There were no average annual earnings per unit exclusive of net gain for the year.

6. **Accounts, Notes, and Grants Receivable**

Accounts receivable included the following at June 30, 2003:

Student accounts receivable	\$ 3,413,488.81
Grants receivable	3,697,878.51
Notes receivable	488,685.25
Pledges receivable	747,000.00
State appropriation receivable	426,500.00
Other receivables	2,268,342.68
Subtotal	<u>\$ 11,041,895.25</u>
Less allowance for doubtful accounts	(1,717,107.30)
Total	<u>\$ 9,324,787.95</u>

Pledges receivable are promises of private donations that are reported as accounts receivable and revenue.

Federal Perkins Loan Program funds include the following at June 30, 2003:

Perkins loans receivable	\$ 3,679,943.44
Less allowance for doubtful accounts	(891,308.62)
Total	<u>\$ 2,788,634.82</u>

7. Capital Assets

Capital asset activity for the year ended June 30, 2003, was as follows:

	Beginning Balance	Additions	Transfers	Reductions	Ending Balance
Land	\$ 4,449,224.5	\$ 78,000.00	\$ -	\$ -	\$ 4,527,224.51
Improvements and infrastructure	25,320,600.52	197,925.80	-	-	\$ 25,518,526.32
Buildings	196,375,217.92	-	1,146,773.07	31,576.01	\$ 197,490,414.98
Equipment	28,960,113.47	5,522,097.62	-	841,744.81	\$ 33,640,466.28
Library holdings	14,690,716.33	2,156,377.63	-	1,226,167.73	\$ 15,620,926.23
Projects in progress	1,891,394.70	6,968,288.48	(1,146,773.07)	17,606.00	\$ 7,695,304.11
Total	\$ 271,687,267.45	\$ 14,922,689.53	\$ -	\$ 2,117,094.55	\$284,492,862.43

Less accumulated depreciation:

Improvements and infrastructure	\$ 11,178,519.99	\$ 1,217,582.49		\$ 72,454.25	\$ 12,323,648.23
Buildings	68,188,988.16	4,819,861.21	-	(32,148.44)	\$ 73,040,997.81
Equipment	19,778,581.52	2,694,574.03	-	1,270,175.73	\$ 21,202,979.82
Library holdings	6,839,515.91	1,684,709.41	-	1,226,167.73	\$ 7,298,057.59
Total accumulated depreciation	\$ 105,985,605.58	\$ 10,416,727.14	\$ -	\$ 2,536,649.27	\$ 113,865,683.45
Capital assets, net	\$ 165,701,661.87	\$ 4,505,962.39	\$ -	\$ (419,554.72)	\$ 170,627,178.98

8. Long-term Liabilities

Long-term liability activity for the year ended June 30, 2003, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Payables					
Bonds	\$ 75,996,953.82	\$ 1,882,997.81	\$ 2,390,069.35	\$ 75,489,882.28	\$ 2,522,927.44
Commercial Paper	1,867,133.95	4,548,623.09	513,297.37	5,902,459.67	-
Subtotal	\$ 77,864,087.77	\$ 6,431,620.90	\$ 2,903,366.72	\$ 81,392,341.95	\$ 2,522,927.44
Other Liabilities					
Compensated Absences	\$ 3,787,836.99	\$ 2,208,175.58	\$ 1,941,163.07	\$ 4,054,849.50	\$ 1,051,274.65
Due to Grantors	2,583,710.94	1,840,800.80	1,419,414.21	3,005,097.53	-
Deferred Revenue	3,651,554.27	274,247.86	-	3,925,801.95	3,925,801.95
Subtotal	\$ 10,023,102.20	\$ 4,323,224.24	\$ 3,360,577.28	\$ 10,985,748.98	\$ 4,977,076.60
Total long-term liabilities	\$ 87,887,189.97	\$10,754,845.14	\$ 6,263,944.00	\$ 92,378,090.93	\$ 7,500,004.04

Bonds Payable

Bond issues, with interest rates ranging from 3.65% to 7.75% for Tennessee State School Bond Authority bonds, are due serially to 2030 and are secured by pledges of the facilities' revenues to which they relate and certain other revenues and fees of the University, including state appropriations. The bonded indebtedness with the Tennessee State School Bond Authority reported on the statement of net assets is shown net of assets held by the authority in the debt service reserve and net of unexpended loan proceeds. The reserve amount was \$907,739.11 at June 30, 2003, and \$907,739.11 at June 30, 2002.

Unexpended debt proceeds were \$262,115.04 at June 30, 2003.

Debt service requirements to maturity for all bonds payable at June 30, 2003, are as follows:

For the Year(s) Ending June 30	Principal	Interest	Total
2004	\$ 2,522,927.44	\$ 4,016,615.75	\$ 6,539,543.19
2005	2,418,430.01	3,896,899.10	6,315,329.11
2006	2,446,690.06	3,780,741.54	6,227,431.60
2007	2,570,342.09	3,662,031.22	6,232,373.31
2008	2,695,931.48	3,542,689.74	6,238,621.22
2009 - 2013	14,591,741.66	15,648,759.76	30,240,501.42
2014 - 2018	16,659,187.51	11,659,972.28	28,319,159.79
2019 - 2023	15,312,853.93	7,304,959.86	22,617,813.79
2024 - 2028	14,716,482.03	2,995,730.42	17,712,212.45
2029 - 2030	1,555,296.07	132,466.06	1,687,762.13
Total	\$ 75,489,882.28	\$ 56,640,865.73	\$ 132,130,748.01

Commercial Paper

The Tennessee State School Bond Authority authorized the issuance of commercial paper to finance costs of various capital projects. At June 30, 2003, \$5,902,459.67 had been issued for projects at Middle Tennessee State University.

For the commercial paper program, the Tennessee State School Bond Authority maintains an interest rate reserve fund. The institution contributes amounts to the reserve fund based on the amounts drawn. The principal of the reserve will be contributed to pay off notes or credited back to the University when the notes are converted to bonds. The interest earned on the reserve is used to pay interest due during the month.

9. Unrestricted Net Assets

Unrestricted net assets include funds that have been designated or reserved for specific purposes. These purposes include the following:

	FY 2003
Working capital	\$ 2,034,843.43
Encumbrances	1,907,654.99
Designated fees	288,841.01
Auxiliaries	4,021,406.62
Quasi-endowment	155,100.00
Plant construction	6,881,741.34
Renewal and replacement of equipment	12,271,270.77
Debt retirement	799,267.88
Unreserved/undesigned balance	3,283,263.78
Total	\$ 31,643,389.82

10. Endowments

If a donor has not provided specific instructions to Middle Tennessee State University, state law permits the University to authorize for expenditure the net appreciation (realized and unrealized) of the investments of endowment funds. When administering its power to spend net appreciation, the University is required to consider its long-term and short-term needs, present and anticipated financial requirements, expected total return on its investments, price-level trends, and general economic conditions. Any net appreciation that is spent is required to be spent for the purposes for which the endowment was established.

The University chooses to spend the investment income (including changes in the value of investments) each year. Under the spending plan established by the University, all interest earnings have been authorized for expenditure. At June 30, 2003, net appreciation of \$2,474.39 was available to be spent, none of which was restricted to specific purposes.

11. Pension Plans

Defined Benefit Plan

PLAN DESCRIPTION - The institution contributes to the State Employees, Teachers, and Higher Education Employees Pension Plan (SETHEEPP), a cost-sharing multiple employer defined benefit pension plan administered by the Tennessee Consolidated Retirement System (TCRS). TCRS provides retirement, death, and disability benefits as well as annual cost-of-living adjustments to plan members and their beneficiaries. Title 8, Chapters 34-37, *Tennessee Code Annotated*, establishes benefit provisions. State statutes are amended by the Tennessee General Assembly.

The TCRS issues a publicly available financial report that includes financial statements and required supplementary information for SETHEEPP. That report may be obtained by writing to the Tennessee Treasury Department, Consolidated Retirement System, 10th Floor, Andrew Jackson Building, Nashville, TN 37243-0230 or by calling (615) 741-8202, extension 139.

FUNDING POLICY - Plan members are noncontributory. The institution is required to contribute at an actuarially determined rate. The current rate is 7.29% of annual covered payroll. The contribution requirements of the institution are established and may be amended by the TCRS Board of Trustees. The institution's contributions to TCRS for the years ending June 30, 2003, 2002, and 2001 were \$2,571,010.23, \$2,165,347.75 and \$2,107,764.38, respectively, equal to the required contributions for each year.

Defined Contribution Plans

PLAN DESCRIPTION – The institution contributes to three defined contribution plans: Teachers Insurance and Annuity Association-College Retirement Equities Fund (TIAA-CREF), Aetna Life Insurance and Annuity Company, and Variable Annuity Life Insurance Company (VALIC). These plans are administered by the Tennessee Department of the Treasury. Each plan provides retirement benefits to faculty and staff who are exempt from the overtime provisions of the Fair Labor Standards Act and who waive membership in the TCRS. Benefits depend solely on amounts contributed to the plan plus investment earnings. Plan provisions are established by state statute in Title 8, Chapter 35, Part 4, *Tennessee Code Annotated*. State statutes are amended by the Tennessee General Assembly.

FUNDING POLICY – Plan members are noncontributory. The institution contributes an amount equal to 10% of the employee's base salary up to the social security wage base and 11% above the social security wage base. Contribution requirements are established and amended by state statute. The contribution made by the institution to the plans for the year ended June 30, 2003, was \$5,393,658.17 and for the year ended June 30, 2002, was \$4,977,476.97. Contributions met the requirements for each year.

12. Other Post-Employment Benefits

The State of Tennessee administers a group health insurance program that provides post-employment health insurance benefits to eligible institution retirees. This benefit is provided by and administered by the State of Tennessee. The institution assumes no liability for retiree health care programs. Information related to this plan is available at the statewide level in the *Tennessee Comprehensive Annual Financial Report*. That report may be obtained by writing to the Tennessee Department of Finance and Administration, Division of Accounts, 14th Floor, William R. Snodgrass Tennessee Tower, 312 Eighth Avenue North, Nashville, Tennessee 37242-0298 or by calling (615) 741-2140.

13. Chairs of Excellence

The institution had \$20,812,189.54 on deposit at June 30, 2003, with the State Treasurer for its Chairs of Excellence program. These funds are held in trust by the state and are not included in these financial statements.

14. Insurance-Related Activities

The state purchases commercial insurance for real property losses above \$5 million per year and surety bond coverage on the state's officials and employees. In the past three fiscal years, the state has not had any claims filed with the commercial insurer. A designation for casualty losses in the amount of \$5 million has been established in the state's general fund to provide for any property losses not covered by commercial insurance.

At June 30, 2003, the scheduled coverage was \$353,275,000 for buildings and \$153,389,100 for contents.

The state has set aside assets for claim settlement in an internal service fund, the Claims Award Fund. This fund services all claims for risk of loss to which the state is exposed, including general liability, automobile liability, professional malpractice, and workers' compensation. The institution participates in the Claims Award Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the institution based on a percentage of the institution's expected loss costs, which include both experience and exposures. This charge considers recent trends in actual claims experience of the state as a whole. An actuarial valuation is performed as of fiscal year-end to determine the fund liability and premium allocation. The institution is subject to the liability limitations under the provisions of the Tennessee Claims Commission Act, *Tennessee Code Annotated* 9-8-101 et seq. Liability for the negligence of the institution for bodily injury and property damage is limited to \$300,000 per person and \$1,000,000 per occurrence. The limits of liability under workers' compensation are set forth in *Tennessee Code Annotated* 50-6-101 et seq. Claims are paid through the State's Claims Award Fund.

The state has also set aside assets in the Employee Group Insurance Fund, an internal service fund, to provide a program of health insurance coverage for the employees of the state with the risk retained by the state. The institution participates in the Employee Group Insurance Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the institution based on estimates of the ultimate cost of claims that have been reported but not settled and of claims that have been incurred but not reported. Employees and providers have 13 months to file medical claims.

15. Commitments and Contingencies

SICK LEAVE - The institution records the cost of sick leave when paid. Generally, since sick leave (earned one day per month with unlimited accumulation) is paid only when an employee dies or is absent because of illness, injury, or related family death, there is no liability for sick leave at June 30. The dollar amount of unused sick leave was \$37,344,187.29 at June 30, 2003.

OPERATING LEASES - The institution has entered into various operating leases for buildings and equipment. Such leases will probably continue to be required. Expenditures under operating leases for real and personal property were \$193,645.16 and \$137,998.57 respectively for the year ended June 30, 2003. Comparative amounts for the year ended June 30, 2002, were \$178,581.94 and \$78,591.98 respectively. All operating leases are cancelable at the lessee's option.

CONSTRUCTION IN PROGRESS - At June 30, 2003, outstanding commitments under construction contracts totaled \$8,271,238.80, all of which will be funded by future state capital outlay appropriations. Major projects include the development facility, Todd renovation, housing renovations, several building roof replacements, Keathley University Center, the Honors College Building, life safety renovations, parking improvements, and a new observatory.

LITIGATION - The institution is involved in several lawsuits, none of which are expected to have a material effect on the accompanying financial statements.

16. Natural Classifications with Functional Classifications

The institution's operating expenses by functional classification for the year ended June 30, 2003, are as follows:

Functional Classification	Natural Classification					
	Salaries	Benefits	Operating	Scholarships	Depreciation	Total
Instruction	\$ 60,004,155.04	\$ 14,729,404.38	\$ 11,398,990.94	\$ -	\$ -	\$ 86,132,550.36
Research	1,728,191.56	362,315.80	691,516.27	-	-	2,782,023.63
Public Service	3,061,708.89	860,069.93	3,239,312.31	-	-	7,161,091.13
Academic Support	9,358,123.97	2,647,636.64	760,517.56	-	-	12,766,278.17
Student Services	9,029,689.61	2,499,638.84	8,158,952.19	-	-	19,688,280.64
Institutional Support	7,908,942.01	2,468,801.38	2,595,504.43	-	-	12,973,247.82
Maint. and Operations	4,823,495.53	1,717,882.69	12,627,352.33	-	-	19,168,730.55
Scholarships and Fellowships	-	-	-	10,437,455.35	-	10,437,455.35
Auxiliaries	5,034,417.48	1,404,156.22	13,184,951.26	-	-	19,623,524.96
Depreciation	-	-	-	-	10,416,727.14	10,416,727.14
Total Expenses	\$100,948,724.09	\$ 26,689,905.88	\$ 52,657,097.29	\$10,437,455.35	\$ 10,416,727.14	\$201,149,909.75

17. Prior Period Adjustment

The prior period adjustment relates to the following items: 1) recording of liability due to the U.S. Department of Education for the Settlement Agreement entered into by the University on May 29, 2003, in the amount of \$873,323.80; 2) reductions to accumulated depreciation in the amount of \$657,919.42 from the FY '02 state audit; 3) correction in the reclassification of the loan fund balance in FY '02 totaling \$80,676.57; and 4) reclassification of the sports museum project from the University to the MTSU Foundation in the amount of \$17,606.00.