



CALIFORNIA STATE UNIVERSITY, STANISLAUS

Financial Statements

June 30, 2004

(With Independent Auditors' Report Thereon)

CALIFORNIA STATE UNIVERSITY, STANISLAUS

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Independent Auditors' Report

Dr. Marvalene Hughes, President
California State University, Stanislaus:

We have audited the accompanying financial statements of California State University, Stanislaus (the University) and its aggregate discretely presented component units as of and for the year ended June 30, 2004, as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express opinions on these financial statements based upon our audit. We did not audit the financial statements of the aggregate discretely presented component units. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the aggregate discretely presented component units, is based on the reports of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of the other auditors provide a reasonable basis for our opinion.

As discussed in note 2, the financial statements present only the statement of net assets, statement of revenues, expenses, and changes in net assets, and statement of cash flows of the University and do not purport to, and do not, present fairly the financial position of the California State University System as of June 30, 2004, 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.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the University and of its aggregate discretely presented component units as of June 30, 2004, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Management's Discussion and Analysis on pages 3 through 7 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 required supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

October 8, 2004

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Management's Discussion and Analysis

June 30, 2004

The following section of California State University, Stanislaus' (the University) annual financial report includes an overview and analysis of the University's financial position and activities for the year ended June 30, 2004. This discussion and analysis, as well as the financial statements that it accompanies, are the responsibility of the management of the University.

Introduction to the Financial Statements

This annual report consists of a series of financial statements, prepared in accordance with the Governmental Accounting Standards Board Statements No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*, No. 37, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments; Omnibus*, and No. 38, *Certain Financial Statement Note Disclosures*. For reporting purposes, the University is considered a special purpose government engaged in business-type activities, which best represents the activities of the University.

The financial statements include a statement of net assets; a statement of revenues, expenses and changes in net assets; and a statement of cash flows. Notes to the financial statements and this section, required supplementary information, support the information contained in these statements. All sections must be considered together to obtain a complete understanding of the financial position and results of operations of the University.

Statement of Net Assets – The statement of net assets includes all assets and liabilities with the difference between the two reported as net assets. Assets and liabilities are reported at their book value, on an accrual basis, as of the statement date. This statement also identifies major categories of restrictions on the net assets of the University.

Statement of Revenues, Expenses and Changes in Net Assets – The statement of revenues, expenses and changes in net assets presents the revenues earned and expenses incurred during the year on an accrual basis.

Statement of Cash Flows – The statement of cash flows presents the changes in the University's cash and cash equivalents, summarized by operating, capital and noncapital financing, and investing activities. The statement is prepared using the direct method of cash flows, and therefore, presents gross rather than net amounts for the year's activities.

Analytical Overview

The following discussion highlights the University's financial activities. Included is a comparative analysis of current and prior year activities and balances; a discussion of restrictions of University net assets; a discussion of capital assets and long-term debt; and factors impacting future reporting periods.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Management's Discussion and Analysis

June 30, 2004

Comparative Analysis of Current and Prior Year Balances

The following condensed summaries of key financial statement information are presented as a basis for reviewing current year results in comparison with the prior year:

Condensed Summary of Net Assets

	<u>FY 2003/2004</u>	<u>FY 2002/2003</u>
Assets:		
Current assets	\$ 24,355,933	20,555,968
Capital assets	91,309,494	79,631,567
Other noncurrent assets	<u>52,217,254</u>	<u>20,808,394</u>
Total assets	<u>167,882,681</u>	<u>120,995,929</u>
Liabilities:		
Current liabilities	22,191,260	14,511,657
Long term liabilities, net of current portion	19,697,577	19,554,806
Other noncurrent liabilities	<u>1,009,226</u>	<u>2,017,050</u>
Total liabilities	<u>42,898,063</u>	<u>36,083,513</u>
Net assets:		
Invested in capital assets, net of related debt	89,124,688	77,086,068
Restricted	28,781,314	1,417,897
Unrestricted	<u>7,078,616</u>	<u>6,408,451</u>
Total net assets	<u>\$ 124,984,618</u>	<u>84,912,416</u>

Current assets, capital assets, and other noncurrent assets increased by 18.5%, 14.7%, and 150.9%, respectively, comparing the June 30, 2004 ending balances to June 30, 2003 ending balances. Current liabilities increased \$7.7 million or 52.9% over prior year. The main causes for these differences are explained below:

- Current assets increased by \$3.8 million largely due to a \$2.5 million increase in the campus state appropriation receivable. As of June 30, 2003, several large campus obligations were prepaid. This was not the case at June 30, 2004.
- Capital assets increased with the near completion of the Residential Life Village addition.
- Other noncurrent assets increased \$31.4 million as of year-end due to the receipt of \$45.8 million for construction of a new science building to begin in Winter 2005.
- The increase in current liabilities is due in part to costs related to the Residential Life construction project which have been incurred and not paid as of June 30, 2004, as well as the timing of other payments.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Management's Discussion and Analysis

June 30, 2004

Restricted Net Assets

Net assets of the University include funds that are restricted by donor or law. Restricted net assets may be expendable for a specific purpose or they may be nonexpendable. The following table describes the type of restriction and respective net asset balances:

	<u>FY 2003/2004</u>	<u>FY 2002/2003</u>
Expendable:		
Scholarships and fellowships	\$ 52,555	101,043
Capital projects	28,319,937	141,539
Debt service	408,822	1,175,315
Total restricted net assets	<u>\$ 28,781,314</u>	<u>1,417,897</u>

There was a significant fluctuation, \$28.2 million, in restricted net assets – capital projects due to the near completion of phase III of the Residential Life Village funded through the Dormitory Revenue Fund. In addition, this balance increased due to funds received for a new science building, which is to be completed in 2007.

Comparative Analysis of Current and Prior Year Activities

The University's net assets increased by \$40.1 million or 47.2%, as reflected below:

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

	<u>FY 2003/2004</u>	<u>FY 2002/2003</u>
Operating revenues:		
Student tuition and fees	\$ 11,598,138	11,082,183
Grants and contracts	13,416,549	12,837,705
Auxiliary enterprises, net	2,613,840	1,747,911
Total operating revenues	<u>27,628,527</u>	<u>25,667,799</u>
Operating expenses	90,502,737	91,105,497
Nonoperating revenues:		
State appropriations, noncapital	53,540,259	57,768,963
Investment income, net	255,266	452,495
Other nonoperating revenue	3,149,981	3,884,418
Total nonoperating revenue	<u>56,945,506</u>	<u>62,105,876</u>
Other capital related revenues	<u>46,000,906</u>	<u>5,020,996</u>
Increase in net assets	40,072,202	1,689,174
Beginning net assets	<u>84,912,416</u>	<u>83,223,242</u>
Ending net assets	<u>\$ 124,984,618</u>	<u>84,912,416</u>

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Management's Discussion and Analysis

June 30, 2004

The University's financial position, as a whole, improved slightly during the fiscal year ended June 30, 2004. Significant revenue and expense changes from fiscal year 2003 to 2004 are a result of the following:

- Student fees increased 30% from fiscal year 2003 to fiscal year 2004 and enrollment remained relatively consistent from 2003 to 2004.
- The campus general fund budget was reduced over \$4 million in fiscal year 2004 due to the state of California fiscal crisis.
- Total expenses slightly decreased; however, this does not reflect the true operational changes due to budget reductions. Salary costs decreased and benefit costs significantly increased largely due to the increase in the percentage contribution to the state retirement fund.
- The significant increase in capital state appropriations is related to receiving capital outlay funding for the new campus science building scheduled for completion and occupancy in 2007.

Capital Assets

The University had \$91.3 million invested in capital assets, net of accumulated depreciation of \$74.3 million as of June 30, 2004 and \$79.6 million invested in capital assets, net of accumulated depreciation of \$69.8 million as of June 30, 2003. Depreciation expense increased \$284,000, a change of 6% from the prior fiscal year. Current and prior year details of these assets are shown below:

Capital Assets, Net

	<u>FY 2003/2004</u>	<u>FY 2002/2003</u>
Land and land improvements	\$ 714,150	714,150
Works of art and historical treasures	212,318	226,715
CWIP	14,442,951	7,089,720
Buildings	53,949,445	55,008,163
Improvements other than buildings	4,123,148	4,784,178
Infrastructure	14,537,300	8,147,319
Leasehold improvements	132,803	70,990
Personal property	2,982,665	3,313,093
Intangible assets	214,714	277,239
Total capital assets, net	<u>\$ 91,309,494</u>	<u>79,631,567</u>

The \$5.7 million telecommunications infrastructure project was completed during the year. The third phase of the Residential Life Village was near completion at June 30, 2004 and was ready for occupancy at the beginning of the Fall 2004 term. Bed capacity was increased from 356 beds to 656 beds. The cost of the project at June 30, 2004 is included in the CWIP figure above.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Management's Discussion and Analysis

June 30, 2004

Long-Term Debt

The University had \$19.6 million in debt outstanding at June 30, 2004, a decrease of \$0.4 million over the prior year. Interest rates on outstanding debt range from 2.5% to 7.5%. Below is a summary of current and prior year outstanding debt by type of debt instrument:

	<u>FY 2003/2004</u>	<u>FY 2002/2003</u>
Revenue bonds	\$ 18,110,000	18,135,000
Capital leases	<u>1,444,806</u>	<u>1,814,631</u>
Total debt outstanding	<u>\$ 19,554,806</u>	<u>19,949,631</u>

Factors Impacting Future Periods

The legislative process has approved the State General Fund allocation to the California State University for fiscal year 2005. CSU Stanislaus received \$1.4 million for enrollment growth; however, because of the state fiscal crisis, the budget was reduced by \$4.8 million. To help offset the reduction, undergraduate student fees were increased an additional 14% and graduate fees were increased by 20%. The net effect of the budget changes is estimated to be a budget reduction of \$1.3 million. In addition, unfunded mandatory costs of \$1.6 million will have to be covered from existing funds.

The planned FTE enrollment target for 2004/2005 is 6,462, a decrease from the previous year of 3%. The increase in student fees will generate approximated \$1.7 million in additional revenue. A growth of 2% to 3% is currently budgeted for 2005/2006.

CSU Stanislaus received a \$45.8 million allocation from the state capital outlay bond fund for a new science building. Construction is to begin in Winter 2005 and is projected to be completed in 2007. This project will replace an existing building that was built in 1972 and is in need of major seismic and programmatic renovations involving extensive destructive and reconstructive work.

CSU Stanislaus began its CMS/PeopleSoft implementation in Fall 2002. Human Resources went live in July 2003 and phase I of Financials is scheduled for January 2005. Phase II of Financials will begin Spring 2005 and be completed in July 2005. Estimated expenditures for the 2004/2005 through 2008/2009 fiscal years range from \$600,000 to \$2.2 million per year. The campus will be implementing the baseline product with no campus specific modifications.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Statement of Net Assets

June 30, 2004

Assets	University	Discretely presented component units	Total
	<u> </u>	<u> </u>	<u> </u>
Current assets:			
Cash and cash equivalents	\$ 1,366,859	727,820	2,094,679
Short-term investments	10,674,201	5,624,495	16,298,696
Accounts receivable, net	11,537,074	2,072,259	13,609,333
Pledges receivable, net	—	307,142	307,142
Prepaid expenses and other assets	777,799	1,180,353	1,958,152
Total current assets	<u>24,355,933</u>	<u>9,912,069</u>	<u>34,268,002</u>
Noncurrent assets:			
Restricted cash and cash equivalents	559,439	—	559,439
Accounts receivable, net	50,273,944	101,031	50,374,975
Student loans receivable, net	1,012,307	—	1,012,307
Pledges receivable, net	—	4,561,200	4,561,200
Endowment investments	—	4,589,033	4,589,033
Other long-term investments	—	2,771,679	2,771,679
Capital assets, net	91,309,494	5,621,952	96,931,446
Other assets	371,564	482,205	853,769
Total noncurrent assets	<u>143,526,748</u>	<u>18,127,100</u>	<u>161,653,848</u>
Total assets	<u>167,882,681</u>	<u>28,039,169</u>	<u>195,921,850</u>
Liabilities and Net Assets			
Current liabilities:			
Accounts payable	11,815,905	996,804	12,812,709
Accrued salaries and benefits payable	5,917,327	357,969	6,275,296
Deferred revenue	1,482,178	39,345	1,521,523
Accrued compensated absences – current portion	2,189,693	56,308	2,246,001
Capitalized lease obligations – current portion	333,349	—	333,349
Long-term debt obligations – current portion	30,000	191,000	221,000
Other liabilities	422,808	3,362,389	3,785,197
Total current liabilities	<u>22,191,260</u>	<u>5,003,815</u>	<u>27,195,075</u>
Noncurrent liabilities:			
Accrued compensated absences, net of current portion	506,120	—	506,120
Grants refundable	1,009,226	85,975	1,095,201
Capitalized lease obligations, net of current portion	1,111,457	—	1,111,457
Long-term debt obligations, net of current portion	18,080,000	4,672,989	22,752,989
Other liabilities	—	1,384,918	1,384,918
Total noncurrent liabilities	<u>20,706,803</u>	<u>6,143,882</u>	<u>26,850,685</u>
Total liabilities	<u>42,898,063</u>	<u>11,147,697</u>	<u>54,045,760</u>
Net assets:			
Invested in capital assets, net of related debt	89,124,688	158,020	89,282,708
Restricted for:			
Nonexpendable – endowments	—	7,264,979	7,264,979
Expendable:			
Scholarships and fellowships	52,555	2,320,589	2,373,144
Capital projects	28,319,937	—	28,319,937
Debt service	408,822	—	408,822
Other	—	2,726,733	2,726,733
Unrestricted	7,078,616	4,421,151	11,499,767
Total net assets	<u>\$ 124,984,618</u>	<u>16,891,472</u>	<u>141,876,090</u>

See accompanying notes to financial statements.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Statement of Revenues, Expenses, and Changes in Net Assets

Year ended June 30, 2004

	<u>University</u>	<u>Discretely presented component units</u>	<u>Total</u>
Revenues:			
Operating revenues:			
Student tuition and fees (net of scholarship allowances of \$9,202,610)	\$ 11,598,138	1,133,845	12,731,983
Grants and contracts, noncapital:			
Federal	9,171,849	4,042,383	13,214,232
State and local	4,003,152	1,107,654	5,110,806
Nongovernmental	241,548	211,637	453,185
Sales and services of auxiliary enterprises (net of scholarship allowances of \$685,173)	2,613,840	1,190,498	3,804,338
Other operating revenues	—	1,020,912	1,020,912
Total operating revenues	<u>27,628,527</u>	<u>8,706,929</u>	<u>36,335,456</u>
Expenses:			
Operating expenses:			
Instruction	34,071,827	2,239,223	36,311,050
Research	397,203	2,852,202	3,249,405
Public service	201,849	142,284	344,133
Academic support	13,492,970	1,835	13,494,805
Student services	7,681,447	1,084,602	8,766,049
Institutional support	12,021,221	2,062,063	14,083,284
Operation and maintenance of plant	7,166,939	108,228	7,275,167
Student grants and scholarships	6,925,061	927,298	7,852,359
Auxiliary enterprise expenses	3,121,015	2,060,568	5,181,583
Depreciation and amortization	5,423,205	296,085	5,719,290
Total operating expenses	<u>90,502,737</u>	<u>11,774,388</u>	<u>102,277,125</u>
Operating loss	<u>(62,874,210)</u>	<u>(3,067,459)</u>	<u>(65,941,669)</u>
Nonoperating revenues (expenses):			
State appropriations, noncapital	53,540,259	—	53,540,259
Gifts, noncapital	—	1,996,011	1,996,011
Investment income, net	255,266	140,007	395,273
Endowment income	—	500,885	500,885
Interest on capital-related debt	(949,704)	—	(949,704)
Other nonoperating revenues (expenses)	4,099,685	(33,927)	4,065,758
Net nonoperating revenues	<u>56,945,506</u>	<u>2,602,976</u>	<u>59,548,482</u>
Loss before other additions	<u>(5,928,704)</u>	<u>(464,483)</u>	<u>(6,393,187)</u>
State appropriations, capital	45,809,000	—	45,809,000
Grants and gifts, capital	191,906	412,934	604,840
Additions to permanent endowments	—	247,604	247,604
Increase in net assets	<u>40,072,202</u>	<u>196,055</u>	<u>40,268,257</u>
Net assets:			
Net assets at beginning of year	<u>84,912,416</u>	<u>16,695,417</u>	<u>101,607,833</u>
Net assets at end of year	<u>\$ 124,984,618</u>	<u>16,891,472</u>	<u>141,876,090</u>

See accompanying notes to financial statements.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Statement of Cash Flows

Year ended June 30, 2004

	<u>University</u>
Cash flows from operating activities:	
Tuition and fees	\$ 11,495,695
Federal grants and contracts	9,506,539
State and local grants and contracts	3,984,993
Nongovernmental grants and contracts	241,548
Payments to suppliers	(17,355,697)
Payments to employees	(58,829,961)
Payments to students	(6,941,546)
Collections of student loans	(112,631)
Sales and services of auxiliary enterprises	2,085,833
Other payments	(9,907,468)
	<hr/>
Net cash used in operating activities	(65,832,695)
	<hr/>
Cash flows from noncapital financing activities:	
State appropriations	51,050,661
Federal loan program receipts	(171,905)
Federal loan program disbursements	287,901
Monies received on behalf of others	13,393,560
Monies disbursed on behalf of others	(13,057,421)
Other	4,420,451
	<hr/>
Net cash provided by noncapital financing activities	55,923,247
	<hr/>
Cash flows from capital and related financing activities:	
State appropriations	4,080,707
Capital grants and gifts	30,694
Proceeds from sale of capital assets	400
Acquisition of capital assets	(11,737,596)
Principal paid on capital debt and leases	(394,825)
Interest paid on capital debt and leases	(949,704)
	<hr/>
Net cash used in capital and related financing activities	(8,970,324)
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Cash flows from investing activities:	
Proceeds from sales and maturities of investments	774,000
Purchases of investments	(1,304,000)
Investment income received	255,266
	<hr/>
Net cash used in investing activities	(274,734)
	<hr/>
Net decrease in cash and cash equivalents	(19,154,506)
	<hr/>
Cash and cash equivalents at beginning of year	21,080,804
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Cash and cash equivalents at end of year (including restricted cash and cash equivalents of \$559,439)	\$ <u>1,926,298</u>

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Statement of Cash Flows

Year ended June 30, 2004

	<u>University</u>
Reconciliation of net operating loss to net cash used in operating activities:	
Operating loss	\$ (62,874,210)
Adjustments to reconcile net operating loss to net cash used in operating activities:	
Depreciation and amortization expense	5,423,205
Change in assets and liabilities:	
Accounts receivable, net	(10,395,023)
Student loans receivable, net	(45,660)
Prepaid expenses and other assets	(940,791)
Accounts payable	1,339,499
Accrued salaries and benefits	1,780,133
Accrued compensated absences	(210,028)
Deferred revenue	(35,444)
Depository accounts	6,046
Other liabilities	119,578
Net cash used in operating activities	\$ <u><u>(65,832,695)</u></u>

See accompanying notes to financial statements.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Notes to Financial Statements

June 30, 2004

(1) Organization

California State University, Stanislaus (the University) was established as a campus of the California State University under the state of California Education Code to offer undergraduate and graduate instruction for professional and occupational goals emphasizing a broad liberal arts education. As one of 23 campuses in the California State University system (the System), the University is included in the financial statements of the System. Responsibility for the University is vested in the Trustees of the System (the Trustees) who, in turn, appoint the Chancellor, the chief executive officer of the System, and the University president, the chief executive officer of the University.

The University provides instruction for baccalaureate and masters' degrees, and certificate programs, and operates various auxiliary enterprises such as student dormitories, student unions, and parking facilities. In addition, the University administers a variety of financial aid programs which are funded primarily through state and federal programs.

(2) Summary of Significant Accounting Policies

(a) *Financial Reporting Entity*

In accordance with Governmental Accounting Standards Board (GASB) Statements No. 34, *Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, and No. 35, *Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*, the accompanying financial statements include the accounts of the University and the University's four recognized auxiliary organizations. These auxiliary organizations are legally separate entities that provide services primarily to the University's students and faculty. Separate financial statements are issued for each of the recognized auxiliary organizations and may be obtained from the University.

The discretely presented auxiliary organizations are as follows:

- California State University, Stanislaus Foundation
- Associated Students Incorporated of California State University, Stanislaus
- University Student Union of California State University, Stanislaus
- California State University, Stanislaus Auxiliary, and Business Services.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Notes to Financial Statements

June 30, 2004

Summary information for the discretely presented auxiliary organizations is as follows:

June 30, 2004	California State University, Stanislaus Foundation	Other auxiliary organizations	Total
Current assets	\$ 5,449,359	4,462,710	9,912,069
Capital assets, net	—	5,621,952	5,621,952
Other noncurrent assets	11,769,262	735,886	12,505,148
Total assets	17,218,621	10,820,548	28,039,169
Current liabilities	4,366,828	636,987	5,003,815
Noncurrent liabilities	36,000	6,107,882	6,143,882
Total liabilities	4,402,828	6,744,869	11,147,697
Invested in capital assets, net of related debt	—	158,020	158,020
Restricted	11,878,928	433,373	12,312,301
Unrestricted	936,865	3,484,286	4,421,151
Total net assets	\$ 12,815,793	4,075,679	16,891,472

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Notes to Financial Statements

June 30, 2004

<u>June 30, 2004</u>	<u>California State University, Stanislaus Foundation</u>	<u>Other auxiliary organizations</u>	<u>Total</u>
Revenues:			
Student tuition and fees	\$ —	1,133,845	1,133,845
Grants and contracts, noncapital	4,806,807	554,867	5,361,674
Sales and services of auxiliary enterprises, net	—	1,190,498	1,190,498
Other	758,616	262,296	1,020,912
Total operating revenues	<u>5,565,423</u>	<u>3,141,506</u>	<u>8,706,929</u>
Expenses:			
Instruction	1,464,469	774,754	2,239,223
Research	2,852,202	—	2,852,202
Public service	142,284	—	142,284
Academic support	1,835	—	1,835
Student services	346,017	738,585	1,084,602
Institutional support	2,062,063	—	2,062,063
Operation and maintenance of plant	—	108,228	108,228
Student grants and scholarships	927,298	—	927,298
Auxiliary enterprise expenses	509,554	1,551,014	2,060,568
Depreciation	—	296,085	296,085
Total operating expenses	<u>8,305,722</u>	<u>3,468,666</u>	<u>11,774,388</u>
Operating loss	(2,740,299)	(327,160)	(3,067,459)
Net nonoperating revenues	<u>2,560,129</u>	<u>42,847</u>	<u>2,602,976</u>
Loss before other additions	(180,170)	(284,313)	(464,483)
Grants and gifts, capital	412,934	—	412,934
Additions to permanent endowments	247,604	—	247,604
Change in net assets	480,368	(284,313)	196,055
Beginning net assets, July 1, 2003	<u>12,335,425</u>	<u>4,359,992</u>	<u>16,695,417</u>
Ending net assets, June 30, 2004	<u>\$ 12,815,793</u>	<u>4,075,679</u>	<u>16,891,472</u>

The auxiliary organizations are presented in the accompanying financial statements as component units due to the nature and significance of their relationship with the University. The relationships are such that exclusion of these organizations from the reporting entity would render the financial statements incomplete, primarily due to the activities that the organizations carry out on behalf of the University, such as research, grant administration, foodservice, and academic support. The auxiliary organizations are discretely presented to allow the financial statement users to distinguish them from the University.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Notes to Financial Statements

June 30, 2004

The financial statements present only the statement of net assets, statement of revenues, expenses, and changes in net assets, and statement of cash flows of the University and do not purport to, and do not, present fairly the financial position of the California State University System as of June 30, 2004, and 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.

(b) Basis of Presentation

The accompanying financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America, as prescribed by the GASB. 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 have been met.

The financial statements required by GASB Statements Nos. 34 and 35 include a statement of net assets, a statement of revenues, expenses, and changes in net assets, and a statement of cash flows. As a public institution, the University is considered a special-purpose government under the provisions of GASB Statement No. 35. The University records revenue in part from fees and other charges for services to external users, and accordingly has chosen to present its financial statements using the reporting model for special-purpose governments engaged only in business-type activities. This model allows all financial information for the University to be reported in a single column in each of the financial statements, accompanied by aggregated financial information for the auxiliary organizations. In accordance with the business-type activities reporting model, the University prepares its statement of cash flows using the direct method.

The auxiliary organizations included in these financial statements apply the accounting and reporting standards promulgated by the Financial Accounting Standards Board (FASB).

(c) Election of Applicable FASB Statements

The University has elected not to adopt the pronouncements issued by the Financial Accounting Standards Board (FASB) after November 30, 1989.

(d) Classification of Current and Noncurrent Assets and Liabilities

The University considers assets to be current that can reasonably be expected, as part of its normal business operations, to be converted to cash and be available for liquidation of current liabilities within 12 months of the statement of net assets date. Liabilities that reasonably can be expected, as part of normal University business operations, to be liquidated within 12 months of the statement of net assets date are considered to be current. All other assets and liabilities are considered to be noncurrent.

(e) Cash Equivalents

The University considers all highly liquid investments with an original maturity date of three months or less to be cash equivalents.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Notes to Financial Statements

June 30, 2004

(f) Investments

Investments are reflected at fair value using quoted market prices. Realized and unrealized gains and losses are included in the accompanying statement of revenues, expenses, and changes in net assets as investment income, net.

(g) Capital Assets

Capital assets are stated at cost or estimated historical cost if purchased, or if donated at estimated fair value at date of donation. Capital assets, including infrastructure, with a value of \$5,000 or more and with a useful life of one year or more are capitalized. Title to all assets, whether purchased, constructed, or donated, is held by the state of California. Although title is not with the University for land and buildings, the University has exclusive use of these assets and is responsible for the maintenance of these assets and thus has recorded the cost of these assets on the accompanying financial statements. Capital assets, with the exception of land and land improvements, works of art and historical treasures, and construction work in progress, are depreciated on a straight-line basis over their estimated useful lives, which range from 3 to 45 years. Library books, unless considered rare collections, are capitalized and depreciated over a ten-year period. Periodicals and subscriptions are expensed as purchased. Works of art and historical treasures are valued at cost if purchased or the fair market value at the date of donation if contributed. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend its life are expensed as incurred

Depreciation expense is shown separately in the statement of revenues, expenses, and changes in net assets rather than being allocated among other categories of operating expenses.

(h) Deferred Revenue

Deferred revenue consists primarily of fees collected in advance for summer- and fall-terms and continuing education programs.

(i) Compensated Absences

University employees accrue annual leave at rates based on length of service and job classification.

(j) Grants Refundable

The University periodically receives contributions from the federal government in support of its operation of the Federal Perkins and Nursing Loan programs, approved Title IV loan programs. The federal government has the ability to terminate its support of these programs at any time and to request the University to return those contributions that it has made on a cumulative basis. Accordingly, the federal contributions received and retained by the University at year-end are considered to be liabilities of the University, and are reflected as such in the accompanying statement of net assets.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Notes to Financial Statements

June 30, 2004

(k) Net Assets

The University's net assets are classified into the following net asset categories:

Invested in capital assets, net of related debt: Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction, or improvement of those assets.

Restricted – nonexpendable: Net assets subject to externally imposed conditions that the University retain them in perpetuity. Net assets in this category consist of endowments held by the University or its related auxiliaries.

Restricted – expendable: Net assets subject to externally imposed conditions that can be fulfilled by the actions of the University or by the passage of time.

Unrestricted: All other categories of net assets. In addition, unrestricted net assets may be designated for use by management of the University or have legislative or bond indenture requirements associated with their use. These requirements limit the area of operations for which expenditures of net assets may be made, and require that unrestricted net assets be designated to support future operations in these areas. Campus housing programs are a primary example of operations that have unrestricted net assets with designated uses.

The University has adopted a policy of generally utilizing restricted – expendable funds, prior to unrestricted funds, when an expense is incurred for purposes for which both are available.

(l) Classification of Revenues and Expenses

The University considers operating revenues and expenses in the statement of revenues, expenses, and changes in net assets to be those revenues and expenses that result from exchange transactions or from other activities that are connected directly to the University's primary functions. Exchange transactions include charges for services rendered and the acquisition of goods and services. Certain other transactions are reported as nonoperating revenues and expenses or capital contributions in accordance with GASB Statement 35. These nonoperating activities include the University's operating and capital appropriations from the state of California, net investment income, gifts, and interest expense.

The state of California appropriates funds to the System on an annual basis. The appropriations are, in turn, allocated among the campuses by the Office of the Chancellor. Appropriations are recognized as revenue when authorization is received, and are reported as either noncapital appropriations when used to support general operations or capital appropriations when used for capital projects.

Student tuition and fee revenue, and sales and services of auxiliary enterprises, including revenues from student housing programs, are presented net of scholarships and fellowships applied to student accounts. Certain other scholarship amounts are paid directly to, or refunded to, the student and are reflected as expenses.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Notes to Financial Statements

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(m) Income Taxes

The System was established under the state of California Education Code as an agency of the State of California. As a campus of the System, the University is generally not subject to federal or state income taxes. However, the University remains subject to income taxes on any net income that is derived from a trade or business, regularly carried on, and not in furtherance of the purpose for which it was granted exemption. No income tax provision has been recorded as the net income, if any, from any unrelated trade or business, in the opinion of management, is not material to the financial statements taken as a whole.

The University has not undergone any recent Internal Revenue Service or other state income tax audits and no taxes have been provided for any assessments that may result from such audits. In the opinion of management, any such possible assessments would not be material to the financial statements taken as a whole.

(n) Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts in the accompanying financial statements. Actual results could differ from those estimates.

(3) Cash, Cash Equivalents, and Investments

The deposits of the University that are maintained at financial institutions are fully insured or collateralized as required by state law. At June 30, 2004, cash consisted of demand deposits held at the state Treasury and petty cash. This cash of \$1,366,859 had a bank balance of \$622,768. The differences are related to deposits in transit and outstanding checks. Restricted cash and cash equivalents of \$559,439 represent unexpended bond proceeds held at the Chancellor's Office and invested in the State of California Surplus Money Investment Fund.

State law and regulations require that surplus monies of the University must be invested. The University's investment policy authorizes excess funds to be invested in obligations of the federal and California state governments, certificates of deposit, and certain other investment instruments.

At June 30, 2004 the investment portfolio consists primarily of investments held in the California State University investment pool, as well as interest-bearing accounts held in the state Treasury.

None of the University's investments are represented by specific identifiable investment securities and, accordingly, are not subject to custodial risk categorization as prescribed by GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Notes to Financial Statements

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At June 30, 2004, University investments are pooled; however, separate accounting is maintained as to the amounts allocable to the various funds and programs. Investments at fair value consisted of the following at June 30, 2004:

State of California Surplus Money Investment Fund	\$	2,554,149
Metropolitan West Total Return Fund		1,200,532
Metropolitan West Short-Term Fund		6,910,258
Other		9,262
		<u>9,262</u>
Total	\$	<u><u>10,674,201</u></u>

For information regarding the investments of the individually discretely presented auxiliary organizations, please refer to the separately issued auxiliary organizations' reports.

(4) Accounts Receivable

Accounts receivable at June 30, 2004 consisted of the following:

	<u>Current</u>	<u>Noncurrent</u>	<u>Total</u>
State appropriations	\$ 3,101,153	45,348,774	48,449,927
Auxiliary organizations	577,031	—	577,031
Student accounts	459,825	—	459,825
Other	7,629,295	4,925,170	12,554,465
	<u>11,767,304</u>	<u>50,273,944</u>	<u>62,041,248</u>
Less allowance for doubtful accounts	<u>(230,230)</u>	<u>—</u>	<u>(230,230)</u>
Total	\$ <u><u>11,537,074</u></u>	<u><u>50,273,944</u></u>	<u><u>61,811,018</u></u>

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Notes to Financial Statements

June 30, 2004

(5) Capital Assets

Capital asset activity consisted of the following:

	Balance				Balance
	June 30, 2003	Additions	Retirements	Transfers	June 30, 2004
Nondepreciable capital assets:					
Land and land improvements	\$ 714,150	—	—	—	714,150
Works of art and historical treasures	226,715	—	(14,397)	—	212,318
Construction work in progress	<u>7,089,720</u>	<u>12,566,896</u>	<u>—</u>	<u>(5,213,665)</u>	<u>14,442,951</u>
Total nondepreciable capital assets	<u>8,030,585</u>	<u>12,566,896</u>	<u>(14,397)</u>	<u>(5,213,665)</u>	<u>15,369,419</u>
Depreciable capital assets:					
Buildings and building improvements	89,593,333	1,240,521	—	152,704	90,986,558
Improvements, other than buildings	22,158,864	72,213	—	333,748	22,564,825
Infrastructure	12,633,002	1,978,593	—	4,727,213	19,338,808
Leasehold improvements	70,990	74,467	—	—	145,457
Personal property:					
Equipment	9,808,474	878,422	(826,546)	—	9,860,350
Library books and materials	5,878,380	272,499	—	—	6,150,879
Intangible assets	<u>1,214,016</u>	<u>12,484</u>	<u>(10,522)</u>	<u>—</u>	<u>1,215,978</u>
Total depreciable capital assets	<u>141,357,059</u>	<u>4,529,199</u>	<u>(837,068)</u>	<u>5,213,665</u>	<u>150,262,855</u>
Total cost	<u>149,387,644</u>	<u>17,096,095</u>	<u>(851,465)</u>	<u>—</u>	<u>165,632,274</u>
Less accumulated depreciation:					
Buildings and building improvements	34,585,170	2,451,943	—	—	37,037,113
Improvements, other than buildings	17,374,686	1,066,991	—	—	18,441,677
Infrastructure	4,485,683	315,825	—	—	4,801,508
Leasehold improvements	—	12,654	—	—	12,654
Personal property:					
Equipment	7,060,737	1,315,890	(845,980)	—	7,530,647
Library books and materials	5,313,024	184,893	—	—	5,497,917
Intangible assets	<u>936,777</u>	<u>75,009</u>	<u>(10,522)</u>	<u>—</u>	<u>1,001,264</u>
Total accumulated depreciation	<u>69,756,077</u>	<u>5,423,205</u>	<u>(856,502)</u>	<u>—</u>	<u>74,322,780</u>
Net capital assets	\$ <u>79,631,567</u>	<u>11,672,890</u>	<u>5,037</u>	<u>—</u>	<u>91,309,494</u>

For information regarding the capital assets of the individually discretely presented auxiliary organizations, please refer to the separately issued auxiliary organizations' reports.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Notes to Financial Statements

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(6) Lease Obligations

The University is obligated under various capital and operating leases and installment purchase agreements for the acquisition of equipment and facility rentals.

Capital leases consist primarily of leases of certain facilities and office equipment. Total capital assets related to capital leases have a carrying value of \$3,220,495 at June 30, 2004. Substantially all of these assets are pledged as security for the related leases. The leases bear interest at rates ranging from 4.95% to 7.48% and have terms expiring in various years through January 1, 2008.

Operating leases consist primarily of leases for the use of real property and have terms expiring in various years through fiscal year 2009. The leases can be canceled if the state does not provide adequate funding.

Future minimum lease payments under capital and operating leases having remaining terms in excess of one year are as follows:

	<u>Capital leases</u>	<u>Operating leases</u>
Year ending June 30:		
2005	\$ 407,876	683,436
2006	407,876	647,588
2007	407,876	645,500
2008	407,876	622,400
2009	—	40,000
	<u>1,631,504</u>	<u>\$ 2,638,924</u>
Total minimum lease payments	1,631,504	\$ 2,638,924
Less amount representing interest	<u>(186,698)</u>	
Present value of future minimum lease payments	\$ <u>1,444,806</u>	

Rent expense under operating leases for the year ended June 30, 2004 totaled \$1,227,389.

Lease financing is provided to the System for the construction of various system and campus facilities through its participation with the state of California in the state Public Works Board Lease Revenue Bond Program. Certain capital assets recorded by the University may have been financed under these arrangements. However, since the obligation for the repayment of this financing rests with the System and the proceeds of such financing are not readily identifiable with a campus or project, a substantial portion of such financing is not allocated to the individual campuses of the System. Unallocated Lease Revenue Bonds outstanding for the System as of June 30, 2004 totaled \$577,751,000.

(7) Long-Term Debt Obligations

(a) General Obligation Bond Program

The General Obligation Bond program of the state of California has provided capital outlay funds for the three segments of California Higher Education through voter-approved bonds. Each of the approved bond programs provides a pool of available funds which is allocated on a

CALIFORNIA STATE UNIVERSITY, STANISLAUS

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project-by-project basis among the University of California, the California State University, and the Community Colleges. Financing provided to the University through state of California General Obligation Bonds is not allocated to the System by the state of California. This debt remains the obligation of the state and is funded by state tax revenues. Accordingly, such debt is not reflected in the accompanying financial statements. Total General Obligation Bond debt carried by the state related to California State University projects is approximately \$436,819,000 as of June 30, 2004.

(b) Revenue Bond Programs

The Revenue Bond Act of 1947 provides the board of trustees with the ability to issue revenue bonds to fund six specific self-supporting programs. The statute has enabled the trustees to finance student housing, parking facilities, student unions, health facilities, continuing education, and auxiliary organizations. Outstanding bonds at June 30, 2004 consist of campus student housing and student union.

The housing program provides on-campus housing primarily for students. Housing is a self-supporting program deriving its revenues from fees collected for the use of the residence facilities. Funds are used for current operating expenses, maintenance and repair, improvements to facilities, and interest and principal payments on outstanding bonds. Available balances after payment of all operating expenses and required charges remain available for future program expenses and capital needs.

The student union program provides facilities and programs aimed at creating and enhancing learning experiences outside the classroom by promoting interaction among students, faculty, and staff. The student union program is self-supporting and derives its revenues primarily from student fees and interest income. Funds are used for maintenance and repair, improvements to facilities, and interest and principal payments on outstanding bonds. After payment of all authorized charges, the balances of these funds are available for transfer to the campus auxiliary organization that has contracted with the University to operate the facility. The operating entity may derive additional revenue from facility subrental, recreational and commercial activities, and interest income.

The Systemwide Revenue Bond program, formerly the Housing Revenue Bond program, was approved by the board of trustees in fiscal year 2003. This program provides funding for various construction projects, including student residence and dining halls facilities, continuing education buildings, student unions, parking facilities, and health facilities at designated campuses within the system as specified by the individual bond documents. It is designed to provide lower cost debt and greater flexibility to finance revenue bond projects in the University. Rather than relying on specific pledged revenues to support specific debt obligations, this program pools several sources of revenue as the pledge for the related revenue producing projects.

The net revenues from the University's revenue bond program in place prior to fiscal year 2003, which includes the student union, are recorded as student tuition and fees and sales and services of auxiliary enterprises on the statement of revenue, expenses, and changes in net assets and are pledged to retire the related revenue bonds of that program. The University's total outstanding balance of revenue bond indebtedness under this program was \$740,000 at June 30, 2004 and are senior to the System Revenue Bond.

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Notes to Financial Statements

June 30, 2004

The System's total outstanding balance of revenue bond indebtedness under the Systemwide Revenue Bond Program was \$672,620,000 at June 30, 2004. The University's portion of the total outstanding balance under this program was \$17,370,000 at June 30, 2004

Long-term debt obligations of the University as of June 30, 2004 consist of the following as of June 30:

<u>Description</u>	<u>Interest rate</u>	<u>Fiscal year maturity date</u>	<u>Original issue amount</u>	<u>Amount outstanding</u>
Systemwide Revenue Bonds:				
Housing, Series 2003A	2.5% – 5.25%	2035	\$ 17,370,000	17,370,000
Student Union Revenue Bonds:				
Series 2002A	3.0% – 5.5%	2021	780,000	<u>740,000</u>
Total long-term debt				18,110,000
Less current portion				<u>(30,000)</u>
Long-term debt, net of current portion				<u>\$ 18,080,000</u>

Long-term debt principal obligations and related interest mature in the following fiscal years:

	<u>Principal</u>	<u>Interest</u>
Year ending June 30:		
2005	\$ 30,000	861,969
2006	320,000	857,219
2007	330,000	847,894
2008	345,000	837,444
2009	350,000	827,456
2010 – 2014	1,940,000	3,947,241
2015 – 2019	2,445,000	3,431,019
2020 – 2024	2,955,000	2,719,988
2025 – 2029	3,650,000	1,904,307
2030 – 2034	4,665,000	876,874
2035	1,080,000	27,000
	<u>\$ 18,110,000</u>	<u>17,138,411</u>

Long-term debt obligations of the discretely presented auxiliary organizations have been issued to purchase or construct facilities for University-related uses. For information regarding the long-term debt obligations of the individually discretely presented auxiliary organizations, please refer to the separately issued auxiliary organizations' report.

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Notes to Financial Statements

June 30, 2004

(8) Long-Term Liabilities Activity

Long-term liabilities activity for the year ended June 30, 2004 was as follows:

	<u>Beginning balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending balance</u>	<u>Current portion</u>
Accrued compensated absences	\$ 2,905,841	2,071,743	(2,281,771)	2,695,813	2,189,693
Capitalized lease obligations (note 6)	1,814,631	—	(369,825)	1,444,806	333,349
Long-term debt obligation (note 7):					
Student union revenue bonds	765,000	—	(25,000)	740,000	30,000
Housing revenue bonds	<u>17,370,000</u>	<u>—</u>	<u>—</u>	<u>17,370,000</u>	<u>—</u>
Total long-term liabilities	<u>\$ 22,855,472</u>	<u>2,071,743</u>	<u>(2,676,596)</u>	<u>22,250,619</u>	<u>2,553,042</u>

(9) Pension Plan and Postretirement Benefits

(a) Plan Description

The University, as an agency of the state of California, contributes to the California Public Employees' Retirement System (CalPERS). The state's plan with CalPERS is an agent multiple-employer defined benefit pension plan. For the University, the plan acts as a cost-sharing multiple-employer defined benefit pension plan which provides a defined benefit pension and postretirement benefit program for substantially all eligible University employees. CalPERS functions as an investment and administrative agent for its members. The plan also provides survivor, death, and disability benefits. Eligible employees are covered by the Public Employees' Medical and Hospital Care Act (PEMHCA) for medical benefits.

CalPERS issues a publicly available comprehensive annual financial report that includes financial statements and required supplementary information. Copies of the CalPERS annual financial report may be obtained from the California Public Employees' Retirement System Executive Office – 400 P Street – Sacramento, California 95814.

(b) Funding Policy

University personnel are required to contribute 5% of their monthly earnings in excess of \$513 to CalPERS. The University is required to contribute at an actuarially determined rate; the current rate is approximately 14.843% of annual covered payroll. The contribution requirements of the plan members are established and may be amended by CalPERS.

The University's contributions to CalPERS for the most recent three fiscal years were equal to the required contributions and were as follows:

2002	\$ 1,723,511
2003	3,170,274
2004	6,547,337

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Notes to Financial Statements

June 30, 2004

(c) **Faculty Early Retirement Program**

During the fiscal year ended June 30, 2004, the System implemented the Faculty Early Retirement Program, which was authorized by Executive Order S-8-04 issued by the Governor on May 6, 2004. In order to enroll in the program, participants must meet the CalPERS retirement eligibility requirements of age 50 or more on the date of retirement and have 5 years or more of service credit. Eligible employees who elect to participate in this program will receive two additional years of service credit in their retirement income calculation if their 1) separation date is no earlier than May 5, 2004, and not later than July 28, 2004, and 2) CalPERS retirement date is no earlier than May 6, 2004, and no later than July 28, 2004. In return, the System must contribute to CalPERS an amount representing the actuarial equivalent of the value of this benefit. As the early retirement benefit is not dependent upon future services and has already been earned as of June 30, 2004 by those who have elected to participate in the program, the University's estimated liability of \$1.0 million has been recorded as a component of accrued salaries and benefits payable as of June 30, 2004.

(10) **Self-Insurance Claims Liability**

The System and certain auxiliary organizations have established a public entity risk pool to manage centrally workers' compensation, industrial and nonindustrial disability, and general organizational risks. The self-insurance claims liability reflects the estimated share of the ultimate cost of settling claims relating to events that have occurred on or before June 30, 2004. The liability includes estimated amounts that will be required for future payments of claims that have been reported and claims related to events that have occurred but have not been reported. The estimated liability is actuarially determined using individual-case basis valuations and statistical analyses.

Changes in the System's self-insurance claims liability for the year ended June 30, 2004 are as follows:

Liability at June 30, 2002	\$ 102,523,000
Incurred claims and changes in estimates	42,819,000
Claim payments	<u>(40,971,000)</u>
Liability at June 30, 2003	104,371,000
Incurred claims and changes in estimates	49,591,000
Claim payments	<u>(35,251,000)</u>
Liability at June 30, 2004	118,711,000
Less current portion	<u>(33,652,000)</u>
Long-term liability at June 30, 2004, net of current portion	<u>\$ 85,059,000</u>

CALIFORNIA STATE UNIVERSITY, STANISLAUS

Notes to Financial Statements

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The System maintains excess general liability insurance coverage provided by Schools Excess Liability Fund (SELF), a Joint Powers Authority, with coverage for individual claims between \$1,000,000 and \$24,000,000 per occurrence. The System also maintains excess workers' compensation insurance provided by SELF for individual claims over \$350,000 per occurrence. There have been no settlements in the most recent three fiscal years that have exceeded insurance limits.

The University's allocation of the System's total self-insurance claims liability as of June 30, 2004 was zero due to the University's prepayment through fiscal year 2004/2005.

(11) Commitments and Contingencies

Federal grant programs are subject to review by the grantor agencies, which could result in requests for reimbursement to grantor agencies for disallowed expenditures. Management believes that it has adhered to the terms of its grants and that any disallowed expenditures resulting from such review would not have a material effect on the financial position of the University.

Contractual commitments for construction projects unexpended as of June 30, 2004 totaled \$14,442,951. These expenditures will be funded primarily from state appropriations.

The University is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the University's financial position, changes in net assets, or liquidity.

(12) Classification of Operating Expenses

The University has elected to report operating expenses by functional classification in the statement of revenues, expenses, and changes in net assets, but to provide the natural classification of those expenses as an additional disclosure. For the years ended June 30, 2004, operating expenses by natural classification consisted of the following:

<u>2004</u>	<u>Salaries</u>	<u>Benefits</u>	<u>Scholarships and fellowships</u>	<u>Supplies and other services</u>	<u>Depreciation</u>	<u>Total</u>
Functional classification:						
Instruction	\$ 22,881,568	7,906,964	—	3,283,295	—	34,071,827
Research	239,845	16,392	—	140,966	—	397,203
Public service	79,516	3,014	—	119,319	—	201,849
Academic support	6,991,346	2,151,691	—	4,349,933	—	13,492,970
Student services	4,149,126	1,608,830	—	1,923,491	—	7,681,447
Institutional support	6,055,785	2,639,720	—	3,325,716	—	12,021,221
Operation and maintenance of plant	2,956,330	1,197,013	—	3,013,596	—	7,166,939
Student grants and scholarships	—	—	6,925,061	—	—	6,925,061
Auxiliary enterprise expenses	1,144,077	378,849	—	1,598,089	—	3,121,015
Depreciation	—	—	—	—	5,423,205	5,423,205
Total	\$ <u>44,497,593</u>	<u>15,902,473</u>	<u>6,925,061</u>	<u>17,754,405</u>	<u>5,423,205</u>	<u>90,502,737</u>

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June 30, 2004

(13) Transactions with Related Entities

The System is an agency of the state of California and as such, processes substantially all of its revenue and expenditure activity through the Office of the California State Controller. State appropriations allocated to the University through the Office of the Chancellor aggregated \$99,349,259 for the year ended June 30, 2004. State appropriations receivable aggregated \$48,449,927 at June 30, 2004. The University also received lottery appropriations from the state of California in the amount of \$696,890 for the year ended June 30, 2004, which is included in other nonoperating revenues and expenses.

As headquarters for the System, the Office of the Chancellor administers certain activities centrally for the individual campuses. Primary among these activities are management of capital projects, debt administration, and risk pool administration. The costs associated with the operations of the Office of the Chancellor are not allocated to the individual universities' financial statements.

As discussed in notes 6 and 7, the University has recorded capital assets that have been financed by System or state of California obligations that are not reflected in the accompanying financial statements. For the year ended June 30, 2004, no such additions of capital assets are included in the accompanying financial statements.

The accompanying financial statements also include the following transactions with discretely presented auxiliary organizations and other related parties as of and for the year ended June 30, 2004:

Reimbursements from recognized auxiliary organizations for salaries of		
University employees working on contracts, grants, and other programs	\$	837,177
Amounts payable to the Office of the Chancellor		3,109
Amounts receivable from recognized auxiliary organizations		577,031