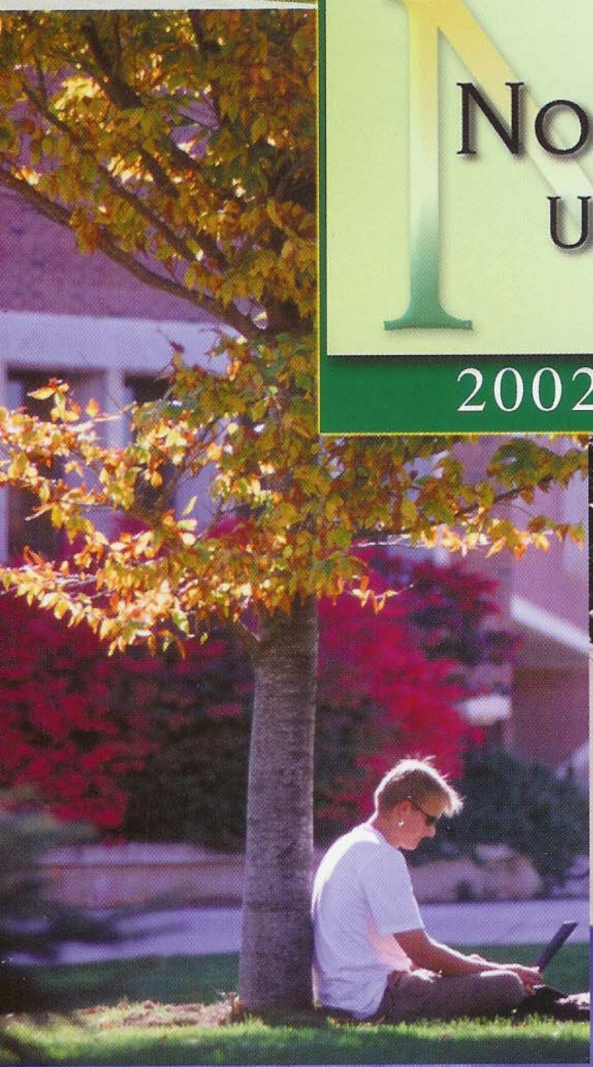
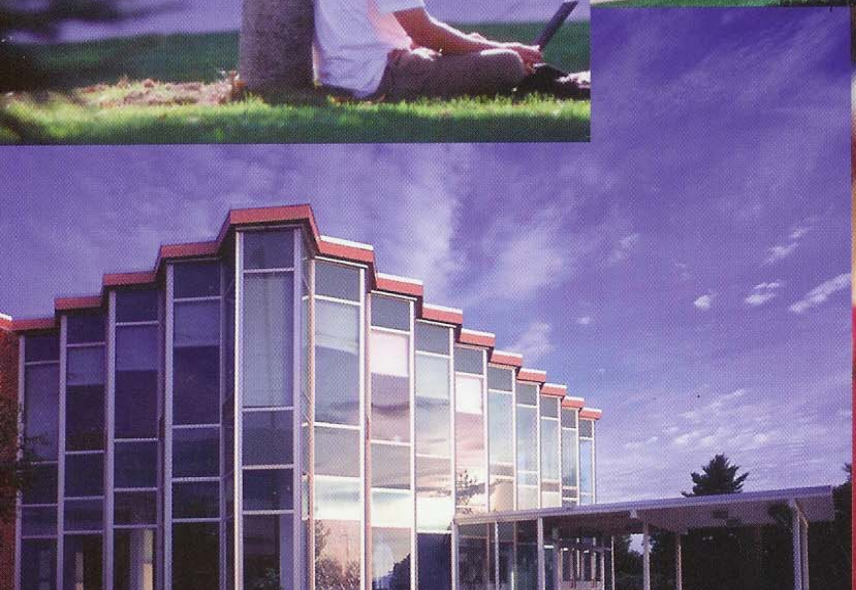



Northern Michigan UNIVERSITY

2002 - 2003 Financial Report



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Provost and Vice President for Academic Affairs

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This section of Northern Michigan University's (the "University") annual financial report presents our discussion and analysis of the financial performance of the University during the fiscal years ended June 30, 2003 and 2002. This discussion has been prepared by management along with the financial statements and related footnote disclosures and should be read in conjunction with and is qualified in its entirety by the financial statements and footnotes. The financial statements, footnotes and this discussion are the responsibility of management.

Reporting Entity

Northern Michigan University is an institution of higher education and is considered to be a component unit of the State of Michigan because its Board of Trustees is appointed by the Governor of the State of Michigan. Accordingly, the University is included in the State's financial statements as a discrete component unit. Transactions with the State of Michigan relate primarily to appropriations for operations, grants from various state agencies, payments to State retirement programs for University employees, and reimbursements for capital outlay projects.

Using the Annual Report

This annual report consists of a series of financial statements, prepared in accordance with the Governmental Accounting Standards Board (GASB) Statement No. 35, Basic Financial Statements - and Management's Discussion and Analysis - for Public Colleges and Universities. The financial statements presented focus on the financial condition of the University, the results of operations, and cash flows of the University as a whole.

The Statement of Net Assets includes all assets and liabilities. It is prepared under the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service, regardless of when cash is exchanged.

The Statement of Revenues, Expenses and Changes in Net Assets presents the revenues earned and expenses incurred during the year. Activities are reported as either operating or non-operating. Under the new reporting model, State appropriations and gifts are reported as non-operating revenues and results in the University showing an operating loss of $50,877,000 for the year ended June 30, 2003, and $50,177,000 for the year ended June 30, 2002. The utilization of long-lived assets, referred to as Capital Assets, is reflected in the financial statements as depreciation, which amortizes the cost of an asset over its expected useful life.

The Statement of Cash Flows presents information related to cash inflows and outflows summarized by operating, capital, financing and investing activities.

Financial Highlights

Operating and non-operating revenue of $128.0 million exceeded operating and non-operating expenses by $1.1 million for the year ended June 30, 2003. The increase in Net Assets, or the overall financial position of the University, primarily resulted from Northern's continued increase in enrollment and increases in tuition and fees that helped offset a $1.8 million decrease in state appropriations.

Operating revenue of $73.2 million increased by $7.7 million over the prior year as the result of a $3.8 million increase in student tuition and fees and a $2.8 million increase in federal and state revenues for scholarships, $0.5 million increase in grant and contract revenues, and $0.6 million increase in other revenue areas. Non-operating revenues of $54.8 million decreased by $3.5 million from the prior year. The University's state appropriation is considered non-operating revenue and decreased by $1.8 million this fiscal year due to budget reductions in the State of Michigan. In addition, capital appropriations decreased by $2.7 million reflecting the completion of the Seaborg Science Complex in fiscal year 2002. A combined increase of $1.0 million was seen in the areas of gifts, investment income, and capital grants and gifts.

Financial Highlights (Continued)

Operating expenses of $124.1 million increased by $8.4 million over the prior year and included an increase of $4.6 million for compensation, $1.3 million increase for additional notebook computers, $1.4 million increase in scholarships, $0.8 million for implementation costs for new administrative software, $0.5 million increase in depreciation expense, and $0.2 million decrease in various support costs. The University made reductions in its workforce that impacted 73 positions, including 20 layoffs, effective July 1, 2003, as the result of reduced state appropriations. Post-separation benefits of $457,000 are included in compensation for employees whose positions were eliminated and signed severance agreements prior to June 30, 2003. Non-operating expenses totaled $2.7 million for interest on capital asset-related debt.

For the year ended June 30, 2003, the University changed its method of classifying the Federal Capital Contribution of its federal Perkins Loan program from restricted expendable net assets to a long-term liability. This represents a change from one generally accepted accounting principle to another generally accepted accounting principle that is the current preferred industry practice. The effect of the change was to reduce beginning net assets by $6,612,615 for the year ended June 30, 2003, and $6,296,285 for the year ended June 30, 2002.

For the year ended June 30, 2002, the University's net assets increased by $5.4 million to $156.5 million, as restated, primarily due to the State of Michigan capital outlay appropriations totaling $3.4 million for completion of the Glenn T. Seaborg Science Complex buildings. Excluding the capital appropriations, net assets increased by $2.0 million.

Condensed Financial Information

Condensed Statement of Net Assets

	June 30	
	2003	2002
ASSETS		
Current Assets	$ 46,484,583	$ 53,116,579
Noncurrent Assets:		
Capital	181,412,624	176,269,502
Other	27,924,581	27,842,844
Total Noncurrent Assets	209,337,205	204,112,346
Total Assets	255,821,788	257,228,925
LIABILITIES		
Current Liabilities	18,226,830	19,112,137
Noncurrent Liabilities	79,947,718	81,602,305
Total Liabilities	98,174,548	100,714,442
NET ASSETS		
Invested in Capital Assets Net of Related Debt	122,437,622	123,522,313
Restricted		
Nonexpendable	744,832	739,189
Expendable	3,306,270	3,146,741
Unrestricted	31,158,516	29,106,240
Total Net Assets	$157,647,240	$156,514,483

Condensed Financial Information (Continued)

Total current assets of $46.5 million at June 30, 2003, included $10.7 million in unspent bond proceeds that will be used for construction projects. At June 30, 2002, total current assets of $53.1 million included $18.8 million in unspent bond proceeds. After adjusting for unspent bond proceeds, the current ratio of current assets to current liabilities is 1.97 for the year ended June 30, 2003, and 1.80 for the year ended June 30, 2002.

The University's largest non-current asset is its investment in physical plant of $181.4 million at June 30, 2003. Net capital assets increased $5.1 million over the prior year after recognition of $7.6 million in depreciation expense.

The state appropriations receivable totaled $9.0 million at June 30, 2003 and included $0.1 million in construction receivables. The state appropriation receivable at June 30, 2002, totaled $9.8 million and included $0.3 million in construction receivables.

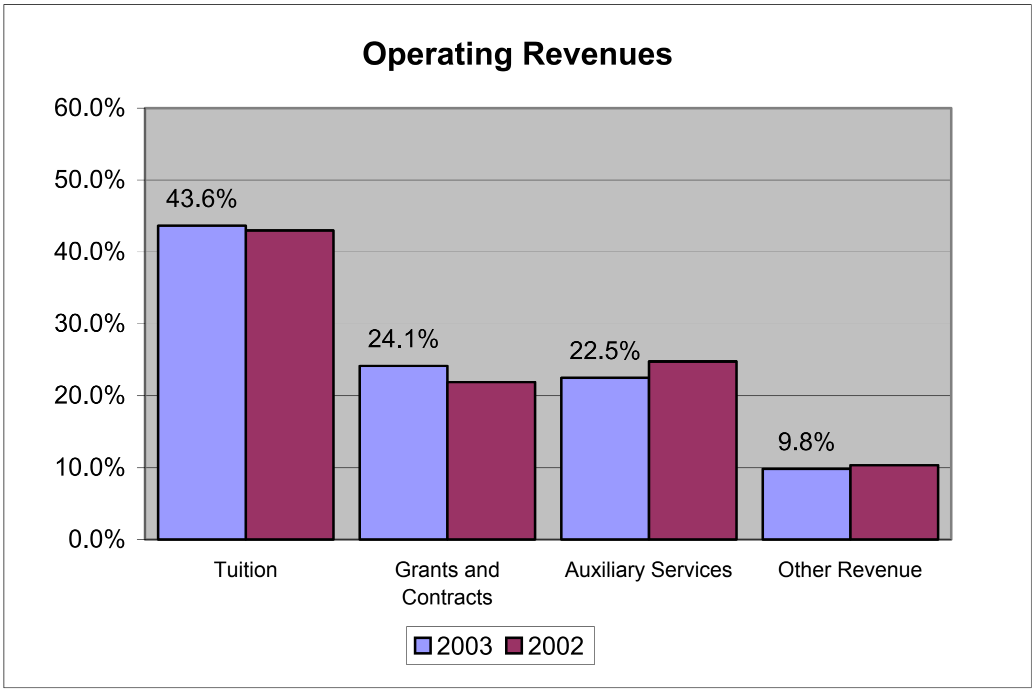
University liabilities totaled $98.2 million at June 30, 2003 and $100.7 million at June 30, 2002. Long-term debt, the largest liability, totaled $69.6 million at June 30, 2003 and $71.4 million at June 30, 2002, consisted of notes and bonds payable.

Condensed Statement of Revenues, Expenses and Changes in Net Assets

	June 30	
	2003	2002
Operating Revenues		
Tuition and Fees	$ 31,963,965	$ 28,169,400
Grants and Contracts	17,687,048	14,355,331
Auxiliary Enterprises	16,475,116	16,233,258
Other Operating Revenues	7,131,069	6,781,821
Total Operating Revenues	73,257,198	65,539,810
Operating Expenses	124,134,226	115,716,752
Operating Income/(Loss)	(50,877,028)	(50,176,942)
Non-operating Revenues (Expenses)		
State Appropriations	50,192,382	52,012,900
Other Non-operating Income and Expenses	379,365	(349,042)
Net Non-operating Revenues and Expenses	50,571,747	51,663,858
Income Before Other Revenues	(305,281)	1,486,916
Capital Appropriations	727,642	3,431,328
Capital Grants and Gifts	710,396	485,639
Total Other Revenues	1,438,038	3,916,967
Total Increase in Net Assets	1,132,757	5,403,883
Net Assets		
Net assets—beginning of year	163,127,098	157,406,885
Cumulative effect of change in accounting principle	(6,612,615)	(6,296,285)
Net assets—balance at beginning of year, as restated	156,514,483	151,110,600
Net assets – end of year	$157,647,240	$156,514,483

Condensed Financial Information (Continued)

Total operating revenues were $73.3 million for fiscal 2003 and $65.5 million for fiscal 2002. The most significant sources of operating revenue for the University are tuition and fees, auxiliary services, and grants and contracts, as shown below:



Tuition and Fees

The University currently has the second lowest annual tuition and fees out of the 15 state universities in Michigan. As part of tuition and fees, each full-time undergraduate student is provided the use of a laptop computer. A full-time undergraduate student normally takes 15 credit hours per semester and a full-time graduate student 12 credit hours per semester. The following table sets forth the average annual student fees for full-time on-campus students, plus the registration fees for the academic year indicated.

Average Annual Full-Time Student Tuition and Fees

	2002-2003	2001-2002
Undergraduate, resident	$4,780	$4,357
Undergraduate, nonresident	$7,732	7,141
Graduate, resident	$5,404	4,187
Graduate, nonresident	$8,092	6,635

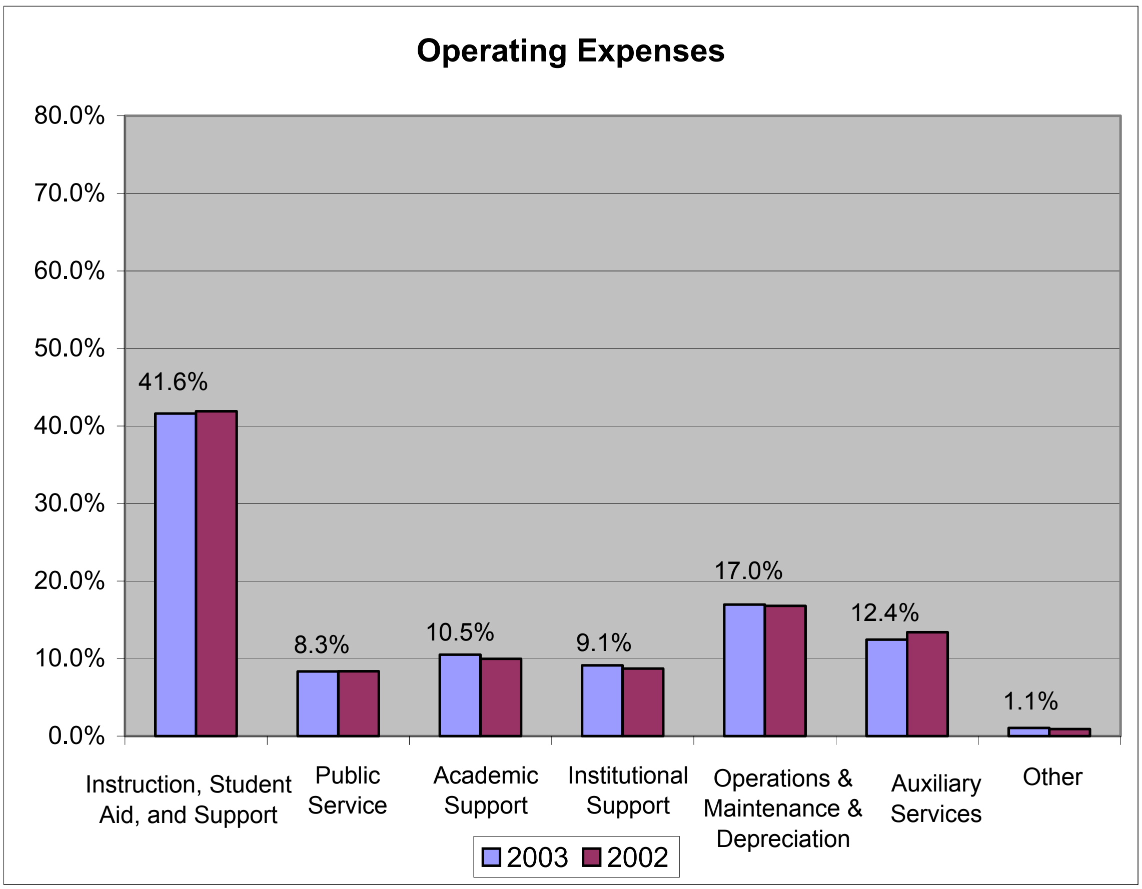
Room and Board

The annual cost of room and board, which includes laundry and other miscellaneous residence fees, was $5,630 for 2002-2003 and $5,436 for 2001-2002. The University provides on-campus residence hall and apartment facilities for students. Most students who are not living at home with their parents must live on campus through their first four semesters. Nine residence halls currently have a mean occupancy of 2,179 and are at a 95 percent capacity. Campus apartments total 278 units with occupancy varying depending on the ratio of single students to student families and the size of the household. Approximately 90 percent of apartments are rented during the academic year. A constant pass meal plan is available which can be used at two on-campus dining facilities.

Operating Expenses

Operating expenses for June 30, 2003, including depreciation of $7.6 million, totaled $124.1 million. Of this total, $51.6 million, or 41.6 percent, was used for instruction, student aid, and student support, and $15.4 million, or 12.4 percent, was used for auxiliary services. Operating expenses for June 30, 2002, including depreciation of $7.1 million, totaled $115.7 million. Of this total, $48.5 million, or 41.9 percent, was used for instruction, student aid, and student support, and $15.5 million, or 13.4 percent, was used for auxiliary services.

The breakout by functional expense is highlighted below:



Other

The State appropriation of $50.2 million for June 30, 2003 and $52.0 million for June 30, 2002, is the largest source of non-operating revenues. The appropriation is recognized in the period for which it is appropriated.

Interest expense on outstanding debt was $2.7 million for June 30, 2003 and $2.6 million for June 30, 2002.

The Statement of Cash Flows

The Statement of Cash Flows provides relevant information about the cash receipts and cash payments of the University during the period.

Condensed Statement of Cash Flows

	June 30 2003	June 30 2002
Cash Provided (Used) By:		
Operating Activities	$(43,929,874)	$(46,149,434)
Non-capital Financing Activities	52,172,802	54,020,242
Capital and Related Financing Activities	(15,911,400)	15,565,778
Investing Activities	1,144,293	(1,026,568)
Net Increase (Decrease) in Cash and Cash Equivalents	(6,524,179)	22,410,018
Cash and Cash Equivalents – Beginning of Year	33,383,439	10,973,421
Cash and Cash Equivalents – End of Year	$ 26,859,260	$ 33,383,439

Major sources of funds included in operating activities are student tuition and fees of $32.2 million, grants and contracts of $17.5 million, and auxiliary sales of $16.5 million for June 30, 2003; and student tuition and fees of $27.7 million, auxiliary sales of $16.5 million, and grants and contracts of $13.9 million for June 30, 2002. The major source of funds included in non-capital financing activities is state appropriations of $50.7 million for June 30, 2003, and $51.9 million for June 20, 2002.

Factors Impacting Future Periods

Enrollment

The University projects that total enrollment will continue to grow as we move toward our goal of 10,400 students by 2005. The following table indicates the total fall headcount enrollment of undergraduate and graduate students. Also indicated are the fiscal year equated students and total annual credit hours for all students attending the University.

	Fall Headcount Enrollment				
Academic Year	Undergraduate Students	Graduate Students	Total	Fiscal Year Equated Students	Annual Total Credit Hours Taken
1998	6,983	843	7,826	6,799	201,138
1999	7,070	797	7,867	6,999	206,881
2000	7,257	887	8,144	7,134	211,060
2001	7,575	853	8,428	7,396	219,017
2002	7,724	853	8,577	7,718	228,551
2003	8,113	903	9,016	8,047	238,345

For the 2003 academic year, fifty-nine percent (59%) of the University's students represents Upper Peninsula Michigan residents, twenty-five percent (25%) of the University's students come from Michigan's Lower Peninsula, and the remaining sixteen percent (16%) comes from other states and foreign countries.

For the 2002 academic year, sixty-one percent (61%) of the University's students represents Upper Peninsula Michigan residents, twenty-four percent (24%) of the University's students come from Michigan's Lower Peninsula, and the remaining fifteen percent (15%) comes from other states and foreign countries.

Admissions

Given the projected decline in Upper Peninsula high school enrollments, NMU is expanding its recruiting in the Lower Peninsula of Michigan, as well as in targeted regions of Illinois and Wisconsin, which have relatively large population densities. While the potential for more student enrollments is high, we convert a lower percentage of admitted students to enrolled students the farther away we recruit from Marquette. Thus, we are likely to see an increase in enrollment despite a drop in the admitted to enrolled conversion rate.

The tables below set forth the total number of first year (including associate degree and vocational and one-year certificate students) and transfer applications received and accepted and the number of students enrolled for the fall semesters indicated.

First Year Student Admissions

Fall Semester	Applications Received	Applications Accepted	Percent Accepted	Total New Freshmen Enrolled	Percent Enrolled
1998	3,192	2,828	88.5	1,417	50.1
1999	3,619	3,098	85.6	1,593	51.4
2000	4,179	3,543	84.8	1,771	50.0
2001	4,473	3,776	84.4	1,818	48.1
2002	4,421	3,780	85.5	1,801	47.6

Transfer Student Admissions

Fall Semester	Applications Received	Applications Accepted	Percent Accepted	Students Enrolled	Percent Enrolled
1998	1,051	868	82.6	476	54.8
1999	1,118	874	78.1	493	56.4
2000	1,243	948	76.3	512	54.0
2001	1,186	878	74.0	494	56.3
2002	1,070	780	72.9	474	60.8

By June 20, 2003, the University had received 4,262 freshman applications (as compared to 4,268 as of June 21, 2002) and had granted 3,529 acceptances (as compared to 3,583 as of June 20, 2002).

By June 20, 2003, the University had received 945 transfer applications (as compared to 905 as of June 21 2002) and had granted 656 acceptances (as compared to 600 as of June 20, 2002).

Capital Plan

The University has in place a five-year strategic capital plan focusing on renovation and transformation of existing facilities to provide state-of-the-art learning environments. A connected learning environment requires that we continue to improve our support systems, technology infrastructure, and facilities.

Beginning in January 2003, the University made a commitment to move its current mainframe administrative software system to a web accessible relational database system. Consulting costs of $0.5 million were included in current operations for this conversion. The new software consists of six integrated modules that include finance, alumni, student, financial aid, human resources, and general shared data. Finance went live on July 1, 2003, and the remaining modules will phase into operation throughout this upcoming fiscal year with the final completion date of June 30, 2004.

Campus facilities continued to be renovated through the use of internal resources and funds from bonds issued during the 2002 fiscal year. The largest on-going project is the Renovation and Adaptive Re-Use of East Campus Facilities. The Fine and Practical Arts section totals $21.2 million and includes an addition to the Art & Design Studios North building, the renovation of the Thomas Fine Arts facility, and a new pedestrian link to the Student Services building. The Student Services section totals $15.8 million and includes the adaptive re-use of the C.B. Hedgcock Fieldhouse to a student service building. All departments in direct support of students will be consolidated into a one-stop service center.

The University has in place a plan to grow our enrollment to 10,400 by 2005. In support of our enrollment growth, future renovation projects include conversion of space vacated in the Cohodas Administrative Center by student service departments into faculty offices, general purpose classrooms, and a conference center, conversion of Magers Hall from faculty offices back to a student residence hall, and construction of new student apartments.

Teaching, Learning, and Communication (TLC) Initiative

The University believes that providing high-quality technology to students as part of full-time enrollment will assist in preparing our graduates to easily move into the increasingly technology driven, global workplace. The NMU campus is a connected learning community with a total of 8,200 notebook computers distributed to students. Wireless technology throughout campus provides improved student access in an out-of-the classroom while reducing renovation costs for University facilities and enabling greater efficiency in the delivery of student services via the internet. The Teaching, Learning, and Communications (TLC) program is one of many steps the University has made toward its vision and goal of students becoming independent lifelong learners.

NMU's plan to keep current in technology has all student and staff notebook and desktop computers replaced on a two-year cycle. Subsequent to June 30, 2003, the University anticipates signing a $3,672,000 lease with IBM for 2,800 computers.

ANDREWS HOOPER & PAVLIK P.L.C.
Certified Public Accountants

Report of Independent Auditors

Board of Trustees
Northern Michigan University
Marquette, Michigan

We have audited the accompanying basic financial statements of Northern Michigan University, a component unit of the State of Michigan, as of and for the years ended June 30, 2003 and 2002. These basic financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these basic financial statements based on our audits.

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

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of Northern Michigan University as of June 30, 2003 and 2002, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note A, the University changed its method of classifying the Federal Capital Contribution of its federal Perkins Loan program from restricted net assets to a long-term liability.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 7, 2003 on our consideration of Northern Michigan University's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The Management's Discussion and Analysis (MD&A) on pages 3 to 10 is not a required part of the basic financial statements but is supplemental information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this supplemental information. However, we did not audit the information and express no opinion on it.

Andrews Hooper & Pavlik P.L.C.

Saginaw, Michigan
August 7, 2003

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NORTHERN MICHIGAN UNIVERSITY
Statements of Net Assets

	June 30	
ASSETS	**2003**	**2002**
Current Assets:		
Cash and cash equivalents	$ 26,859,260	$ 33,383,439
Short-term investments		89,757
State appropriation receivable	9,011,707	9,771,963
Accounts receivable (less allowance 2003--$1,021,970; 2002--$715,042)	6,457,354	6,659,209
Student notes receivable (less allowance 2003--$235,403; 2002--$195,398)	1,748,036	1,497,206
Investment receivable	78,737	120,401
Inventories	1,357,137	1,157,738
Other assets	972,352	436,866
Total current assets	46,484,583	53,116,579
Noncurrent Assets:		
Long-term investments	19,477,866	19,546,090
Student notes receivable (less allowance 2003--$982,935; 2002--$939,974)	7,351,753	7,201,792
Other long-term investments	1,094,962	1,094,962
Capital assets, net	181,412,624	176,269,502
Total noncurrent assets	209,337,205	204,112,346
Total assets	255,821,788	257,228,925
LIABILITIES		
Current Liabilities:		
Accounts payable and accrued liabilities	5,629,966	6,948,690
Accrued payroll and benefits	6,619,239	6,167,299
Deferred revenue (unearned student fees and deposits)	2,972,282	3,006,848
Long-term liabilities-current portion	3,005,343	2,989,300
Total current liabilities	18,226,830	19,112,137
Noncurrent Liabilities:		
Long-term liabilities	79,947,718	81,602,305
Total noncurrent liabilities	79,947,718	81,602,305
Total liabilities	98,174,548	100,714,442
NET ASSETS		
Invested in capital assets, net of related debt	122,437,622	123,522,313
Restricted for		
Nonexpendable		
Scholarships and fellowships	175,540	119,519
Loans	39,602	39,671
Instruction	529,690	579,999
Expendable		
Instruction	421,914	462,389
Scholarships and fellowships	341,135	244,413
Loans	2,466,586	2,405,252
Research	31,711	34,687
Academic support	44,924	
Unrestricted	31,158,516	29,106,240
Total net assets	$157,647,240	$156,514,483

See notes to financial statements.

NORTHERN MICHIGAN UNIVERSITY
Statements of Revenues, Expenses, and Changes in Net Assets

	June 30	
	2003	**2002**
REVENUES		
Operating Revenues		
Student tuition and fees (less allowance 2003--$9,966,545; 2002--$7,921,017)	$ 31,963,965	$ 28,169,400
Federal grants and contracts	10,603,463	9,299,708
State and local grants and contracts	6,579,226	4,732,335
Nongovernmental grants and contracts	504,359	323,288
Sales and services of educational activities	6,883,003	6,572,371
Auxiliary enterprise:		
Residential life (less allowance 2003--$3,257,043; 2002--$2,828,635)	11,262,283	10,855,265
Other auxiliary	5,212,833	5,377,993
Other operating revenues	248,066	209,450
Total operating revenues	73,257,198	65,539,810
EXPENSES		
Operating Expenses		
Educational and general:		
Instruction	32,925,722	31,915,203
Research	1,109,048	923,593
Public Service	10,338,377	9,661,268
Academic support	13,025,847	11,519,651
Student services	11,770,627	10,993,707
Institutional support	11,330,182	10,064,701
Operations and maintenance of plant	13,496,990	12,368,684
Depreciation	7,555,915	7,068,180
Student Aid	6,948,355	5,574,868
Auxiliary enterprise:		
Residential life	9,972,626	9,335,603
Other	5,457,250	6,157,642
Other expenses	203,287	133,652
Total operating expenses	124,134,226	115,716,752
Operating loss	(50,877,028)	(50,176,942)
NON-OPERATING REVENUES (EXPENSES)		
State appropriations	50,192,382	52,012,900
Gifts	2,173,804	1,806,070
Investment income (net of investment expense 2003--$54,699; 2002--$70,000)	953,362	487,710
Interest on capital asset-related debt	(2,747,801)	(2,642,822)
Net non-operating revenues and expenses	50,571,747	51,663,858
Income (loss) before other revenues	(305,281)	1,486,916
Capital appropriations	727,642	3,431,328
Capital grants and gifts	710,396	485,639
Total other revenues	1,438,038	3,916,967
Increase in net assets	1,132,757	5,403,883
NET ASSETS		
Net assets--beginning of year	163,127,098	157,406,885
Cumulative effect of change in accounting principle	(6,612,615)	(6,296,285)
Net assets--balance at beginning of year, as restated	156,514,483	151,110,600
Net assets--end of year	$157,647,240	$156,514,483

See notes to financial statements.

NORTHERN MICHIGAN UNIVERSITY
Statements of Cash Flows

	June 30	
	2003	**2002**
Cash Flows from Operating Activities		
Tuition and fees	$ 32,150,387	$ 27,714,177
Grants and contracts	17,524,061	13,925,968
Payments to suppliers	(37,599,855)	(36,712,204)
Payments to employees	(72,269,153)	(67,471,162)
Payments for scholarships and fellowships	(6,948,355)	(5,574,868)
Loans issued to students and employees	(2,147,270)	(2,217,959)
Collection of loans to students and employees	1,642,800	1,470,950
Auxiliary enterprise:		
Residential Life	11,289,241	10,818,100
Other	5,171,954	5,650,704
Other receipts	7,256,316	6,246,860
Net cash used by operating activities	(43,929,874)	(46,149,434)
Cash Flows from Noncapital Financing Activities		
State appropriations	50,712,528	51,875,893
William D. Ford direct lending receipts	22,351,880	18,214,473
William D. Ford direct lending disbursements	(22,349,847)	(18,209,153)
Gifts and grants received for other than capital purpose	227,890	1,653,746
Other	1,230,351	485,283
Net cash provided by noncapital financing activities	52,172,802	54,020,242
Cash Flows from Capital and Related Financing Activities		
Bonds issued		30,000,000
Capital appropriations	967,752	6,395,030
Capital grants and gifts received	457,948	686,969
Purchases of capital assets	(12,841,692)	(17,196,510)
Principal paid on capital debt	(1,750,000)	(1,845,000)
Interest paid on capital debt	(2,745,408)	(2,474,711)
Net cash provided (used) by capital and related financing activities	(15,911,400)	15,565,778
Cash Flows from Investing Activities		
Proceeds from sales and maturities of investments	14,553,574	12,155,342
Interest on investments	(1,730,029)	1,862,980
Purchase of investments	(11,679,252)	(15,044,890)
Net cash provided (used) by investing activities	1,144,293	(1,026,568)
Net increase (decrease) in cash and cash equivalents	(6,524,179)	22,410,018
Cash and cash equivalents - beginning of the year	33,383,439	10,973,421
Cash and cash equivalents - end of year	$ 26,859,260	$ 33,383,439
Reconciliation of Operating Loss to Net Cash Used by Operating Activities		
Operating loss	$(50,877,028)	$(50,176,942)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Gifts of capital assets		115,000
Depreciation expense	7,555,915	7,068,180
Loss on equipment disposal	575,975	58,279
Change in assets and liabilities:		
Receivables, net	(296,611)	(2,443,361)
Inventories	(199,399)	210,286
Other assets	(535,287)	148,724
Accounts payable	(1,025,973)	(1,060,239)
Deferred revenue	(75,507)	(130,383)
Compensated absences/Accrued payroll	948,041	61,022
Net cash used by operating activities	$(43,929,874)	$(46,149,434)

See notes to financial statements.

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NOTE A--BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). The University follows the "business-type" activities requirements of GASB Statement No. 34. rather than issuing fund-type financial statements and has the following components of the financial statements:

- Management's discussion and analysis
- Basic financial statements including statements of net assets, statements of revenues, expenses and changes in net assets, and statements of cash flows for the University as a whole
- Notes to the financial statements

The University is required to report revenues net of discounts and allowances. Discounts and allowances previously reported as scholarship expenditures are now reported as an allowance against tuition and related revenues.

CHANGES IN ACCOUNTING PRINCIPLES

For the year ended June 30, 2003, the University changed its method of classifying the Federal Capital Contribution of its federal Perkins Loan program from restricted expendable net assets to a long-term liability. This represents a change from one generally accepted accounting principle to another generally accepted accounting principle that is the current preferred industry practice. The liability (refundable advance) method is preferable because the amounts received from the federal government would ultimately be returned to the federal government if the University were to cease making loans or have excess cash as determined under the loan program. The 2002 financial statements have been restated to reflect retroactive application of this change in accounting principle.

The effect of the change was to reduce beginning net assets by the following amounts:

	2003	**2002**
Beginning net assets, as originally reported	**$163,127,098**	$157,406,885
Effect of change in accounting principle	**(6,612,615)**	(6,296,285)
Beginning net assets, as restated	**$156,514,483**	$151,110,600

The above change also reflects restatement of the 2002 change in net assets to record the 75 percent Federal Capital Contribution portion of the net loan increase for the year ended June 30, 2002, in the amount of $316,330. This amount is reflected as a reduction to revenue from federal capital contributions of $240,748 and other operating revenues of $75,582.

REPORTING ENTITY

Northern Michigan University is an institution of higher education and is considered to be a component unit of the State of Michigan because its Board of Trustees is appointed by the Governor of the State of Michigan. Accordingly, the University is included in the State's financial statements as a discrete component unit. Transactions with the State of Michigan relate primarily to appropriations for operations, grants from various state agencies, payments to State retirement programs for University employees, and reimbursements for capital outlay projects.

NOTE A--BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The accompanying financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting.

In accordance with GASB Statement No. 20, the University is required to follow all applicable GASB pronouncements. In addition, the University should apply all applicable Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board (APB) Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. The University has elected not to apply FASB pronouncements issued after November 30, 1989.

Operating revenues of the University consist of tuition and fees, grants and contracts, sales and services of educational activities and auxiliary enterprise revenues. Transactions related to capital and financing activities, noncapital financing activities, investing activities and State appropriations are components of nonoperating income. Restricted and unrestricted resources are spent and tracked at the University level within the guidelines of donor restrictions.

Cash Equivalents

Cash equivalents are all investments with original maturity dates of 90 days or less.

Investments

Investments are stated at fair market value.

Institutional Physical Properties

Institutional physical properties are stated at cost when purchased and at appraised value for other acquisitions.

Depreciation is provided for physical properties on a straight line basis over the estimated useful lives, 50 years for buildings and 5 to 20 years for equipment.

Depreciation expense for 2003 and 2002 is approximately $7,556,000 and $7,068,000 respectively. The University capitalizes assets with a cost of $5,000 and greater.

Inventories

Inventories are stated at the lower of cost or market value as follows: office supplies, first-in, first-out method; and bookstore books and supplies, retail method.

State Appropriations

State appropriation revenue is recognized in the period for which it is appropriated.

Non-Exchange Transactions

In accordance with GASB Statement No. 33, gifts and grants are recognized at the later of the date pledged or when the eligibility requirements of the gifts and grants are met.

NOTE A--BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Reclassifications

Certain 2002 balances have been reclassified to conform to the 2003 presentation.

NOTE B--CASH AND INVESTMENTS

General Policies

University cash and investments are managed in accordance with the Michigan Compiled Laws.

The Board of Trustees established an Investment Policy for cash and investments which authorized the University to invest in various types of funds. Securities are to be highly liquid and convertible into cash at any time. All bonds shall have a quality rating of "A" or better at the time of purchase and the average quality of the short fixed income portfolio shall be between "AA" and "AAA".

Short Fixed Income funds are defined as investments with maturities of one year and no more than seven years with an average maturity portfolio between one and three years. It is expected that the total return over a three year moving period shall exceed the return of the Merrill Lynch 1-3 Year Bond Index.

Intermediate Fixed Income funds are defined as investments with maturities of three years and no more than fifteen years with an average maturity portfolio between three and six years. Securities are to be highly liquid and convertible to cash at any time. It is expected that the total return over a three year moving period shall exceed the return of the Lehman Intermediate Government/Corporate Bond Index.

The yields on the cash and investments were as follows:

	2003	2002
Short Term	**1.60%**	2.65%
Short Fixed Income	**5.55%**	6.65%
Intermediate Fixed Income	**9.39%**	9.13%
Endowment Funds	**1.10%**	1.30%

Investments and Deposits

GASB Statement No. 3 requires certain disclosures regarding policies and practices with respect to deposits, investments, and the custodial credit risk associated with them.

Deposits:

In accord with the GASB Statement No. 3, deposits are classified into three categories of custodial credit risk, as follows:

Category 1: Insured or collateralized with securities held by the University or by its agent in the University’s name

Category 2: Collateralized with securities held by the pledging financial institution's trust department or agent in the University’s name

Category 3: Uncollateralized. (This includes any bank balance that is collateralized with securities held by the pledging financial institution, or by its trust department or agent, but not in the University’s name.)

NOTE B--CASH AND INVESTMENTS (Continued)

Investments:

In accord with GASB Statement No. 3, investments are classified into three categories of custodial credit risk, as follows:

Category 1: Insured or registered, or securities held by the University or its agent in the University's name

Category 2: Uninsured and unregistered, with securities held by the counterparty's trust department or agent in the University's name

Category 3: Uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent but not in the University's name. (This includes the portion of the carrying amount of any repurchase agreement that exceeds the market value of the underlying securities.)

Certain types of investments are not categorized because they are not evidenced by securities that exist in physical or book entry form. Deposits classified as investments on the balance sheet are included in the investment table following and are categorized using the deposit risk category definitions.

The following table shows the market values of investments, including deposits classified as investments on the Statement of Net Assets, by investment type and in total.

	GASB Category #3	Not Categorized	Market Value
Investments:			
Money market funds	$12,058,726		$12,058,726
Commercial paper	1,200,000		1,200,000
Government agencies	54,935		54,935
Preferred stock	10,696	$ 900,000	910,696
Mutual funds		19,423,153	19,423,153
Real estate		194,962	194,962
Total Investments	$13,324,357	$20,518,115	33,842,472
Less Investments Reported as “Cash Equivalents” on Statement of Net Assets			(13,269,644)
Total Investment per Statement of Net Assets			$20,572,828

At June 30, 2003, the carrying amount of deposits, excluding those classified as investments above, was $13,589,616. The deposits were reflected in the accounts of the banks at $17,049,596. For the deposits at the bank, $100,000 was Category 1 custodial credit risk and $16,949,596 was Category 3 custodial credit risk.

Endowment Funds

According to the law of the State of Michigan, the governing board may appropriate for expenditure for the uses and purposes for which an endowment is established so much of the net appreciation, realized and unrealized, in the fair value of the assets of an endowment over the historic dollar value as is prudent under the facts and circumstances prevailing at the time of the action or decision.

NOTE B--CASH AND INVESTMENTS (Continued)

Investments in the Endowment Fund and their related beneficiary accounts are managed by trustees. Policies regarding investments and marketable securities, which are set forth by the Board of Trustees, authorize the trustee to invest in bonds rated A or better, common stock rated B or better, and cash equivalents. The bond and common stock components of investments are each to be kept between 20 and 60 percent of Endowment Fund assets.

The Board has established a Spending Policy for endowed funds to provide for stability in income growth together with preservation of purchasing power. Current operations for which the endowment was established shall have funds made available for spending using a payout factor of 5 percent applied to the weighted average market value for the last twelve quarters as of June 30 each year. The earliest four quarters market value is given a 25 percent weighting, the middle four quarters market value a 35 percent weighting and the latest four quarters a 40 percent weighting. Any gifts or additional deposits received during the last valuation period will be added to the prior quarter's market values in order to be given full weight in the payout calculation. Payments will be made from income to the extent available and capital appreciation to make up any shortfall. Due to the inevitability of short-term market fluctuations, it is intended that the performance objectives will be achieved by the investment manager(s) over a five-year moving period, net of investment management fees. At June 30, 2003, net appreciation of $19,311 (2002--$85,488) was available to be spent and was restricted to specific purposes.

NOTE C--INVESTMENT IN COMMUNITY DEVELOPMENT

The other investments in the Endowment Fund include $900,000, 5% Cumulative Convertible Non-Voting Preferred Stock in the Shorebank Corporation (Shorebank). The proceeds of the Units were used by Shorebank, among other purposes, to capitalize and incorporate North Coast BIDCO, Inc. ("North Coast"), a rural business and industrial development corporation ("BIDCO") in the Upper Peninsula, and to develop a loan production office ("LPO") of South Shore Bank of Chicago ("South Shore"), Shorebank's wholly-owned banking subsidiary in the Upper Peninsula. All dividends have been paid to date.

NOTE D--RECEIVABLES

Receivables at June 30 were as follows:

	2003	**2002**
State appropriations	**$ 8,936,744**	$ 9,456,890
State capital appropriations	**74,963**	315,073
Student loans – net	**9,099,789**	8,698,998
Charter schools	**2,154,040**	2,440,072
NMU Development Fund	**354,263**	146,927
State and federal grants	**1,986,372**	1,985,902
Students, employees, and vendors	**1,962,679**	2,086,308
Investment receivable	**78,737**	120,401
Total	**$24,647,587**	$25,250,571

During the fiscal year, the University recorded revenue of $11,918,418 ($13,515,437 in 2002) for charter schools which was forwarded, net an administration fee, to five (six in 2002) charter schools.

NOTE E--FIXED ASSETS

The following table summarizes, by major class of asset, the recorded costs of fixed assets as of June 30, 2003:

	Beginning Balance	Additions and Reclassifications	Retirements	Ending Balance
Land	$ 4,535,640			$ 4,535,640
Land improvements	7,581,930	$ 332,342		7,914,272
Buildings and improvements	185,554,458	11,624,750		197,179,208
Infrastructure	14,690,412	2,227,954		16,918,366
Equipment	24,639,772	1,459,547	$103,774	25,995,545
Books	12,426,583	745,413	659,103	12,512,893
Construction in progress	10,483,317	(3,114,994)		7,368,323
Totals at historical cost	259,912,112	13,275,012	762,877	272,424,247
Less accumulated depreciation for:				
Land improvements	1,828,724	385,875		2,214,599
Buildings and improvements	52,735,739	3,990,864		56,726,603
Infrastructure	4,975,042	639,576		5,614,618
Equipment	14,546,891	1,978,793	68,263	16,457,421
Books	9,556,214	560,807	118,639	9,998,382
Total accumulated depreciation	83,642,610	7,555,915	186,902	91,011,623
Capital assets, net	$176,269,502	$5,719,097	$575,975	$181,412,624

The following table summarizes, by major class of asset, the recorded costs of fixed assets as of June 30, 2002:

	Beginning Balance	Additions and Reclassifications	Retirements	Ending Balance
Land	$ 3,761,805	$ 773,835		$ 4,535,640
Land improvements	6,636,255	945,675		7,581,930
Buildings and improvements	164,633,365	20,921,093		185,554,458
Infrastructure	14,223,916	466,496		14,690,412
Equipment	21,804,984	3,085,401	$250,613	24,639,772
Books	11,171,896	1,261,655	6,968	12,426,583
Construction in progress	20,588,638	(10,105,321)		10,483,317
Totals at historical cost	242,820,859	17,348,834	257,581	259,912,112
Less accumulated depreciation for:				
Land improvements	1,415,675	413,049		1,828,724
Buildings and improvements	49,026,288	3,709,451		52,735,739
Infrastructure	4,444,917	530,350	225	4,975,042
Equipment	12,974,795	1,764,902	192,806	14,546,891
Books	8,912,057	650,428	6,271	9,556,214
Total accumulated depreciation	76,773,732	7,068,180	199,302	83,642,610
Capital assets, net	$166,047,127	$ 10,280,654	$ 58,279	$176,269,502

Fixed assets are capitalized at cost including ancillary charges necessary to place the asset into use. Interest expense, on debt incurred for construction, is included in the asset cost for the period of construction.

NOTE F--COLLECTIONS

The University has the Moses Coit Tyler Collection that has not been capitalized. This collection is maintained for public exhibition and education.

NOTE G--PAYABLES

Payables at June 30 were as follows:

	2003	2002
Accrued payroll and benefits	**$ 6,619,239**	$ 6,167,299
Construction contractors	**1,650,423**	2,460,441
Charter Schools	**2,154,040**	2,440,072
Vendors	**1,659,784**	1,880,066
Interest payable	**165,719**	168,111
Total	**$12,249,205**	$13,115,989

NOTE H--NONCANCELABLE LEASES

The University has entered into noncancelable leases for computers. The following table is a summary of the noncancelable operating lease payments:

Year ended June 30	Operating Leases
2004	$3,458,238
2005	485,268
Total	$3,943,506

NOTE I--BONDS AND NOTES PAYABLE

In 2001, the University sold a $30,000,000 General Revenue Bond issue for various renovations and construction needs on campus. The principal and interest on the 2001 Revenue Bonds are primarily payable from general University revenues, bear interest based on a daily rate, and mature in varying amounts through 2031. The interest rate at June 30, 2003 was 1.05%.

As a means to lower its borrowing costs, when compared against fixed-rate bonds at the time of issuance in 2001, the University entered into an interest rate swap for $20,000,000 of the Series 2001, General Revenue Variable Rate Demand Bonds. The intention of the swap was to effectively change the University's variable interest rate on the bonds to a synthetic fixed rate.

Under the swap, the University pays the counterparty a fixed payment of 4.015 percent and receives a variable payment computed as 67 percent of the U.S. Dollar – London Interbank Offered Rate (USD-LIBOR-BBA). The swap has a notional amount of $20 million and the associated variable-rate bond has a $30 million principal amount. The swap was entered into at the same time the bonds were issued (2001). The bonds mature on June 1, 2031. The related swap agreement matures on June 1, 2025, when the first $20,000,000 of the associated debt is repaid. As of June 30, 2003, rates were as follows:

	Terms	Rates
Interest rate swap:		
Fixed payment to counterparty	Fixed	4.015%
Variable payment from counterparty	67% of USD-LIBOR-BBA	(0.688%)
Net interest rate swap payments		3.327%
Variable rate bond coupon payments	Actual daily tax-exempt variable rate	1.050%
Synthetic interest rates on bonds		4.377%

NOTE I--BONDS AND NOTES PAYABLE (Continued)

The University has not calculated the fair value of the swap agreement. As of June 30, 2003, and as long as the variable rate portion of the swap being received by the University is less than the fixed rate being paid, the University will be in a negative position on the swap. That is, the University will be paying more in interest expense than they would had they not entered into the swap agreement. The University believes that the variable rate they receive on the swap agreement will eventually exceed the 4.015 percent fixed rate they pay and the swap agreement will reduce its overall interest expense in the future.

The University is exposed to credit risk, which is the risk that the counterparty will not fulfill its obligations, when the swap has a positive fair value. Since the University did not calculate the fair value of the swap, it is not known if there is any potential credit risk. However, as of June 30, 2003, the counterparty to the swap agreement was rated AAA by Standard & Poors.

As noted above, the swap exposes the University to basis risk should the relationship between LIBOR and the University's actual daily tax-exempt variable rate converge, changing the synthetic rate on the bonds. If a change occurs that results in the rates moving to convergence, the expected cost savings may not be realized.

The swap agreement uses the International Swap Dealers Association Master Agreement, which includes standard termination events, such as failure to pay and bankruptcy. The Schedule to the Master Agreement includes an "optional termination rights." The University has the right to terminate the swap transaction at any time upon receipt of notice by the counterparty at least 20 calendar days and no more than 30 calendar days, prior to the specified date. The optional termination amount with respect to this transaction shall equal the present value of the difference on a monthly basis between the cash flows generated at the Settlement Rate and the Fixed Rate of a swap with the then remaining schedule for the notional amounts, discounted monthly to the date the optional termination amount shall be paid using a LIBOR curve of yields calculated under then prevailing industry standards subject to approval by the University and such approval is not to be unreasonably withheld.

In 1998, the University sold a $17,600,000 General Revenue Bond issue for various renovations and construction needs on campus, and to defease in substance $8,020,000 of outstanding 1993 bonds by depositing funds in an irrevocable trust with an escrow agent. All defeased 1993 bonds were called on June 1, 2003; therefore, the outstanding balance for these defeased bonds as of June 30, 2003 and 2002, was $0 and $8,020,000, respectively. The principal and interest on the 1998 Revenue Bonds are primarily payable from general University revenues, bear interest at rates from 4.25% to 5.00%, and mature in varying amounts through 2026. Also in 1998, the University sold a $24,560,000 General Revenue Bond issue for a portion of the University's 25% match of the $47 million State of Michigan funding for the Glenn T. Seaborg Center, and various other renovations and construction needs on campus, and to defease in substance $6,175,000 of outstanding 1992 bonds by depositing funds in an irrevocable trust with an escrow agent. All defeased 1992 bonds were called on June 1, 2002; therefore, there was no outstanding balance for these defeased bonds as of June 30, 2003 and 2002. The principal and interest on the 1997 Revenue Bonds are primarily payable from general University revenues, bear interest at rates from 4.25% to 5.13%, and mature in varying amounts through 2021.

In 1997, the University issued a $1,000,000 term note payable to construct a cable system for residence halls on campus. The note payable bears interest of 5.34% computed on a 360-day year with twelve 30-day months. Principal and interest payments were due annually through fiscal year 2003. This note was paid in full during fiscal year 2003.

NOTE I--BONDS AND NOTES PAYABLE (Continued)

In 1993, the University sold a $12,000,000 General Revenue Bond Issue for the renovation of various campus buildings. The principal and interest on revenue bonds were primarily payable from general University revenues. The bonds bore interest at 2.85% to 5.60% and matured at various dates through 2014. However, during fiscal year 2003, all remaining outstanding bonds either matured or were called; therefore, the outstanding balance due on the 1993 bonds was $0 at June 30, 2003.

In 1992, the University sold an $8,500,000 General Revenue Bond Issue for the renovation of the Don H. Bottum University Center and residence halls and to defease in substance $1,860,000 of outstanding bonds by depositing funds in an irrevocable trust with an escrow agent of which there were no defeased bonds outstanding at June 30, 2002. The principal and interest on revenue bonds were primarily payable from general University revenues, bore interest at rates ranging from 3.25% to 6.55%, and matured in varying amounts through 2015. However, during fiscal year 2002, all remaining outstanding bonds either matured or were called; therefore, the outstanding balance due on the 1992 bonds was $0 at June 30, 2002.

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

		Interest		
Fiscal Year	**Principal**	**Bonds**	**Interest Rate Swap**	**Total**
2003-2004	$ 1,730,000	$ 2,268,091	$ 633,235	$ 4,631,326
2004-2005	1,810,000	2,209,531	612,852	4,632,383
2005-2006	1,890,000	2,148,548	593,379	4,631,927
2006-2007	1,955,000	2,084,162	573,077	4,612,239
2007-2008	2,055,000	2,017,197	553,465	4,625,662
Total five years	9,440,000	10,727,529	2,966,008	23,133,537
Thereafter				
2008-2013	11,725,000	8,911,690	2,411,444	23,048,134
2013-2018	14,615,000	6,490,932	1,730,749	22,836,681
2018-2023	17,035,000	3,403,713	892,729	21,331,442
2023-2028	11,860,000	782,718	82,414	12,725,132
2028-2031	4,955,000	101,050	-	5,056,050
Total	$69,630,000	$30,417,632	$8,083,344	$108,130,976

NOTE I--BONDS AND NOTES PAYABLE (Continued)

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

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Leases and bonds payable:					
Note payable	$ 170,000		$ 170,000		
Bonds payable	71,210,000		1,580,000	$69,630,000	$1,730,000
Total notes and bonds payable	71,380,000		1,750,000	69,630,000	1,730,000
Other liabilities:					
Severance benefits	4,500,281	$457,244	628,638	4,328,887	1,021,541
Compensated absences	2,098,709	269,956	167,978	2,200,687	253,802
Federal portion of Perkins Loan Program	6,612,615	180,872		6,793,487	
Total other liabilities	13,211,605	908,072	796,616	13,323,061	1,275,343
Total long-term liabilities	$84,591,605	$908,072	$2,546,616	$82,953,061	$3,005,343

Long-term liability activity for the year ended June 30, 2002, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Current Portion
Leases and bonds payable:					
Note payable	$ 325,000		$ 155,000	$ 170,000	$ 170,000
Bonds payable	42,900,000	$30,000,000	1,690,000	71,210,000	1,580,000
Total notes and bonds payable	43,225,000	30,000,000	1,845,000	71,380,000	1,750,000
Other liabilities:					
Severance benefits	5,382,195		881,914	4,500,281	980,670
Compensated absences	1,949,879	488,455	339,625	2,098,709	258,630
Federal portion of Perkins Loan Program	6,296,285	316,330		6,612,615	
Total other liabilities	13,628,359	804,785	1,221,539	13,211,605	1,239,300
Total long-term liabilities	$56,853,359	$30,804,785	$3,066,539	$84,591,605	$2,989,300

NOTE J--OPERATING EXPENSES

Operating expenses by natural classification for the year ended June 30 were as follows:

	2003	2002
Salaries, wages and benefits	**$ 72,614,750**	$ 68,042,422
Supplies and support services	**32,582,320**	30,721,916
Utilities	**4,432,886**	4,309,366
Depreciation expense	**7,555,915**	7,068,180
Scholarships	**6,948,355**	5,574,868
Total	**$124,134,226**	$115,716,752

NOTE K--RETIREMENT PLANS

The University has two retirement plans: the Michigan Public School Employees' Retirement System (MPSERS) and the Teachers Insurance and Annuities Association - College Retirement Equities Fund (TIAA-CREF).

The following represents the employer’s share of retirement contributions for MPSERS liability:

- Pension Normal Cost: This contribution rate is determined each year by the retirement system’s actuary and is charged to the seven universities formally participating in MPSERS as a percentage due on their covered MPSERS payroll. For the State’s fiscal year 2003, this rate is 6.47%, and is applied to payrolls occurring on or after October 1, 2002. For the State’s fiscal year 2002, this rate is 6.46%, and is applied to payrolls occurring on or after October 1, 2001.

- Pension Unfunded Liability: This contribution rate is determined each year by the retirement system’s actuary, and is charged to the covered universities as a percentage on their combined member and non-member/non-optional retirement programs payrolls. For the State’s fiscal year 2003, this rate is 0.88% and is applied to payrolls occurring on or after October 1, 2002. For the State’s fiscal year 2002, this rate is 0.0%, and is applied to payrolls occurring on or after October 1, 2001.

- Retiree Health Insurance: This payment is computed annually, and each university is charged a portion of the total requirement due based on the number of retirees each university has, compared to the total number of all university retirees. For the State’s fiscal year 2003, the total amount due for the University’s retiree’s health insurance is $2,107,033. For the State’s fiscal year 2002, the total amount due for the University’s retiree’s health insurance was $1,872,369.

The TIAA-CREF plan is a defined contribution retirement plan. Substantially all full-time employees of the University are eligible to participate in the TIAA-CREF plan. Employee benefits vest immediately. The University contributes a specified percentage of employee wages, as defined by the appropriate labor contract, and has no liability beyond its own contribution.

The University contributed to the plans as follows for the year ended June 30, 2003:

	TIAA-CREF	MPSERS	University Total
University Contributions	$ 4,624,440	$ 3,099,951	$ 7,724,391
Employee Contributions		330,676	330,676
Covered Payroll	30,493,467	14,510,496	45,003,963

The University contributed to the plans as follows for the year ended June 30, 2002

	TIAA-CREF	MPSERS	University Total
University Contributions	$ 4,350,537	$ 2,861,055	$ 7,211,592
Employee Contributions		334,057	334,057
Covered Payroll	28,665,516	14,616,701	43,282,217

NOTE L--EARLY RETIREMENT INCENTIVES

The University has in place a Severance Incentive Program (SIP) available to all active full-time salaried employees who have completed ten years of service. The enrollment period for the first SIP was December 15, 1995 through August 30, 1996. Approved employees were eligible for post-separation benefits consisting of health insurance benefits, if needed, and/or cash severance benefits in varying amounts based on years of service and separation date, but not to exceed 100 percent of annual salary. The remaining SIP liability as of June 30, 2003 and 2002, was $1,041,000 and $1,380,000, respectively.

The University established a second Severance Incentive Program (SIP) available to all active full-time salaried and clerical/technical employees who have completed ten years of service. The employee had to enroll and sever employment between July 1, 2000 and June 30, 2001. Approved employees were eligible for post-separation benefits consisting of health insurance benefits, if needed, and/or cash severance benefits. The remaining SIP liability as of June 30, 2003 and 2002, was $2,831,000 and $3,120,000, respectively. The SIP is expected to be paid over a ten-year period beginning in fiscal year 2000-01.

During fiscal year 2003, the University established a Reduction in Force (RIF) plan for those full-time employees whose positions were eliminated due to budget cuts by July 1, 2003. The employees could not exercise their bumping rights in accordance with their applicable collective bargaining agreement. Employees were eligible for post-separation benefits consisting of health insurance benefits and/or cash severance benefits. The remaining RIF liability as of June 30, 2003, was $457,000.

NOTE M--NORTHERN MICHIGAN UNIVERSITY DEVELOPMENT FUND

Northern Michigan University Development Fund (not included in the University financial statements) is an independent corporation formed for the purpose of receiving funds for the sole benefit of the University. Unaudited financial information of the Northern Michigan University Development Fund at June 30, 2003, includes net assets of approximately $17,540,000 (2002–$16,534,000) and revenues for the year ended June 30, 2003, of approximately $4,462,000 (2002–$2,702,000). Accounts receivable from the Northern Michigan University Development Fund at June 30, 2003, was $354,000 (2002–$147,000).

NOTE N--LIABILITY INSURANCE

The University participates in the Michigan Universities Self-Insurance Corporation (M.U.S.I.C.), which provides indemnity to members against comprehensive general liability, property and casualty, and errors and omissions losses commonly covered by insurance and provides risk management and loss control services and programs. M.U.S.I.C. provides coverage for claims in excess of agreed upon deductibles.

Loss coverages are structured on a three layer basis with each member retaining a portion of its losses, M.U.S.I.C. covering the second layer and commercial carriers covering the third layer. Comprehensive general liability coverage is provided on an occurrence basis; errors and omissions coverage is provided on a claims made basis.

M.U.S.I.C. was established on May 28, 1987, pursuant to the State of Michigan Constitution of 1963, Article 8, Sections 5 and 6. Eleven Michigan Public universities participate in M.U.S.I.C. All members have signed a participation agreement. Participant contributions are assessed on an annual basis to cover insurance risks retained as a group, costs related to excess coverage and general and administrative expenses. Members equity totaled $11,772,000 at June 30, 2002, based on the last published financial statements.

NOTE O--CONTINGENCIES

The University is in the process of renovating various campus buildings. Contractual commitments relating to renovations were approximately $12,816,000 and $2,660,000 at June 30, 2003 and 2002, respectively.

University facilities including the Heating Plant, the Service Building, the Art Annex, and the Seaborg Center Complex, have been or are scheduled to be financed in whole or in part by State Building Authority bond issues which are secured by a pledge of rentals to be received from the State of Michigan pursuant to lease agreements between the SBA, the State of Michigan, and the University. During the lease terms the SBA will hold title to the respective buildings and the University will pay all operating and maintenance costs. At the expiration of the individual leases, the SBA has agreed to sell each building to the University for one dollar. The cost and accumulated depreciation for these assets are recorded in the Statement of Net Assets.

In the normal course of its activities, the University is a party in various legal actions. The University and its legal counsel are of the opinion that the outcome of asserted and unasserted claims outstanding will not have a material effect on the financial statements.

NOTE P--SUBSEQUENT EVENTS

Subsequent to year end, the University anticipated signing a $3,672,000 lease commitment with IBM for laptop computers.

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