2002-2003 Financial Report

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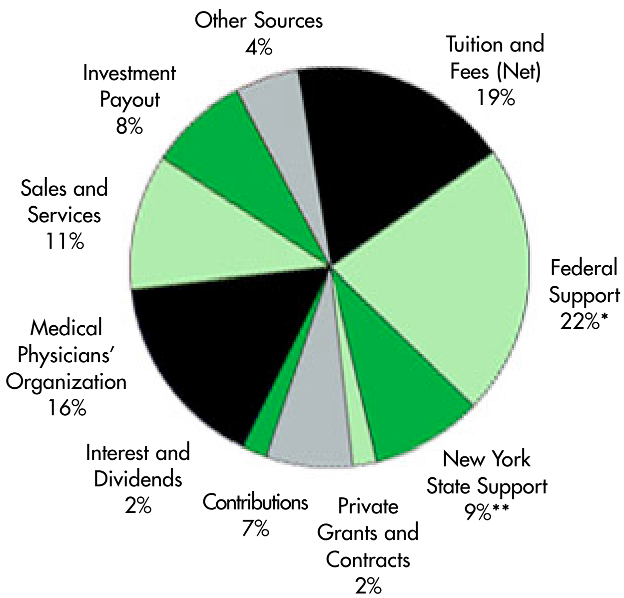
CORNELL UNIVERSITY HIGHLIGHTS

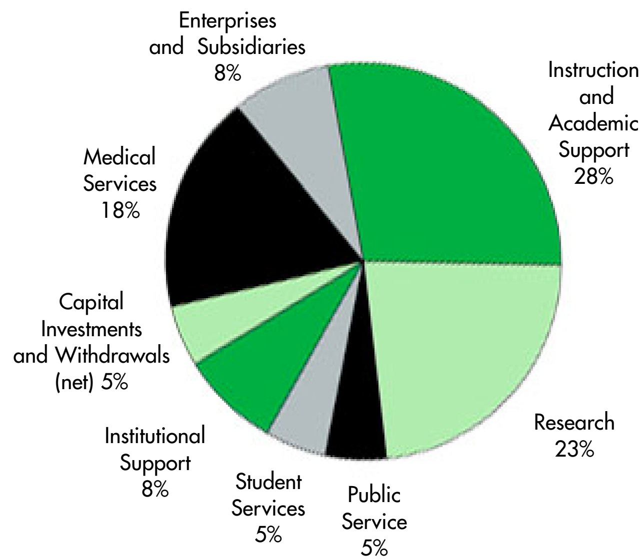
	2002-03	2001-02	2000-01
Fall enrollment (excluding *in absentia*)			
Undergraduate	13,725	13,801	13,590
Graduate	4,534	4,435	4,153
Professional	1,978	1,905	1,877
Total fall enrollment	20,237	20,141	19,620
Degrees granted			
Baccalaureate degrees	3,630	3,565	3,585
Masters degrees	1,550	1,572	1,485
Ph.D. degrees	434	418	459
Other doctoral degrees (J.D., M.D., D.V.M.)	352	361	355
Total degrees granted	5,966	5,916	5,884
Tuition rates			
Endowed Ithaca	$27,270	$25,970	$24,760
Contract Colleges			
Resident	$13,150	$11,970	$10,830
Nonresident	$23,500	$22,200	$20,900
Medical Campus	$29,200	$28,500	$27,650
Business	$30,975	$29,500	$27,600
Law	$31,250	$29,200	$27,300
Veterinary medicine	$18,200	$16,540	$15,400
Volumes in library (in thousands)	7,298	7,136	6,965
Academic workforce			
Full-time employees			
Faculty	2,839	2,821	2,813
Nonfaculty	989	1,008	995
Part-time employees			
Faculty	150	152	144
Nonfaculty	201	176	182
Total academic workforce	4,179	4,157	4,134
Nonacademic workforce			
Full-time employees	8,557	8,413	7,992
Part-time employees	781	749	740
Total nonacademic workforce	9,338	9,162	8,732

	2002-03	2001-02	2000-01
Selected financial capital—net assets			
Book value of total university endowment (in millions)	$2,528.0	$2,771.5	$2,857.3
Market value of total university endowment (in millions)	$2,914.6	$2,920.1	$3,210.4
Unit value of Long-Term Investment Pool	$ 42.65	$ 44.95	$ 51.85
Gifts received, excluding pledges (in millions)	$ 317.0	$ 363.0	$ 309.5
New York State appropriations through SUNY (in millions)	$ 129.5	$ 142.2	$ 136.5
Medical Physicians' Organization fees (in millions)	$ 306.5	$ 283.1	$ 260.0
Sponsored research volume (in millions)			
Direct expenditures	$ 319.3	$ 270.0	$ 232.6
Indirect-cost recovery	$ 97.4	$ 93.5	$ 82.7
Selected physical capital items			
Additions to land, buildings, and equipment (in millions)	$ 300.3	$ 305.1	$ 300.7
Cost of land, buildings, and equipment (in millions)	$2,837.7	$2,696.4	$2,580.8
Outstanding bonds, mortgages, and notes payable (in millions)	$ 494.7	$ 518.6	$ 532.6

GENERAL OPERATIONS REVENUES 2002-03



GENERAL OPERATIONS EXPENSES 2002-03



*	*Appropriations*	*1%*
	Grants	*21%*

**	*Appropriations*	*8%*
	Grants	*1%*

The beginning of the twenty-first century has presented challenges for higher education. Far different from the buoyant decades of the 1980's and 1990's, the new century has been marked by threats to our personal and national security, brought into focus by the events of September 11, 2001, and by a decrease in confidence in the ethics or truthfulness of the leaders of some of our major corporations caused by corporate scandals or examples of outright fraud. All of these have shaken financial markets and caused ripples of many kinds that have significantly changed the environment in which universities like Cornell operate.

More specifically, colleges and universities in general have had to adjust to substantially reduced returns on investments, much greater caution and conservatism on the part of donors, increased financial needs of students, and, for Cornell, severe budget constraints from the State of New York. Adding to these financial pressures on Cornell is the cost of embarking on new and necessary research initiatives, particularly in the physical, biological, and medical sciences. Finally, new regulations (or new interpretations of old regulations), most resulting from increased concern about national security, are creating new procedures and practices, some causing substantial adjustments, for our students, faculty, and research staff.

While the challenges mentioned are broad-ranging and serious, Cornell has responded with energy, imagination, and responsible planning. The Cornell that welcomed its eleventh president, Jeffrey Lehman, in July 2003 is sound, healthy, and vibrant. As this report shows, the assets of the university have increased during the last year, and the university continues to operate with a balanced budget. Not so obvious from this report, however, is the strength of the student body (the quality of applicants remains very strong, and the fraction of the individuals accepted who choose to matriculate at Cornell has increased); the strength and depth of the faculty; and the energy of the instructional and research activities in Ithaca and at the Joan and Sanford I. Weill Medical College (Medical College) in New York City and Qatar.

Of the societal changes noted above, those that have the greatest potential for changing university procedures, policies, and costs revolve around security, privacy, and institutional controls and financial transparency. Regarding security and privacy, significant steps have been taken since September 2001 to review and adjust security procedures on campus, our policies on campus access, and the ways by which we monitor certain activities. But, of course, the very nature of a research university requires that such changes be made carefully and thoughtfully so as not to intrude on the basic freedoms of access and inquiry that define the university.

Adjustments must be, and have been, made to respond to the requirements of the recently-passed *Student and Exchange Visitor Information System* (SEVIS), which requires us to update a federal database for foreign students and exchange visitors. We have also made appropriate adjustments to accommodate the *Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism* (USA PATRIOT) *Act*, which rewrites the rules on protected student data and other information when issues of national security are involved. Still unknown are the implications of a recent interpretation of the *International Traffic in Arms Regulations* (ITAR) that have been long-standing but that now, in the interest of national security, may be applied to certain research activities at universities with the consequence that the traditional free exchange of research results may be diminished.

Personal privacy issues are brought to the fore through the university's compliance with the *Health Insurance Portability and Accountability Act* (HIPAA) and the *Gramm-Leach-Bliley Act*. The former applies to private health care information, of particular importance to the Medical College and to the on-campus Health Center. The latter act establishes privacy standards for financial information. Both acts contain privacy and security requirements for all institutions.

"While the challenges...are broad-ranging and serious, Cornell has responded with energy, imagination, and responsible planning. The Cornell that welcomed its eleventh president, Jeffrey Lehman...is sound, healthy, and vibrant."

Matters of institutional control and financial transparency relate directly to this document and to the university's governance system. Cornell's controls are robust, provide accurate information to the leaders of the institution, and assure the accuracy of this financial report. The nature of this university, with its diverse and participatory centers of authority and basic instincts for inquiry, minimizes the opportunities for distortion of information. To confirm that information is accurate, however, the university turns to an internal auditor and audit staff with the freedom to ask anyone any question about almost any subject. The University Auditor can report findings directly to the President, the Audit Committee of the Board of Trustees, or to the full Board.

"Cornell's controls are robust, provide accurate information...and assure the accuracy of this financial report."

As required by the university's Bylaws, and in accordance with standards generally accepted in the United States, the university's financial statements are audited by independent auditors. The most recently issued opinion of our auditors, KPMG, can be found on page 10 of this report. In addition, as is also required for our peer research institutions, Cornell is audited regularly by federal and state contracting agencies, other entities that provide funding to the university, and federal and state taxing authorities. These audits may be narrow or broad in scope, and may be focused on one or many grants, contracts, or sponsors. In short, on any given day there are likely to be external auditors at work on the Cornell campus examining almost any transaction or procedure.

Some corporate experience within the last few years has shown, however, that internal controls can still be compromised purposefully or through inattention. To reduce these opportunities, the *Sarbanes-Oxley Act* was enacted by Congress to provide financial oversight to publicly traded companies. While this act does not apply to a non-profit organization such as Cornell, New York State's attorney general has introduced similar legislation that would apply the act's principles to the university. Irrespective of the fate of the New York State legislation, Cornell's Board of Trustees is currently comparing Cornell's practices with the tenets of the *Sarbanes-Oxley Act*, and contemplating what changes, if any, should be made to assure rigorous financial oversight.

In conclusion, the report that follows is an accurate representation of the university's financial activity and health. Further, we believe that the report reflects a healthy, energetic university with an extraordinary faculty, strong student body, and a dedicated, skilled staff.

Harold D. Craft Jr.
Vice President for Administration
and Chief Financial Officer

Joanne M. DeStefano
Vice President for Financial Affairs
and University Controller

FINANCIAL REVIEW BY THE VICE PRESIDENT FOR FINANCIAL AFFAIRS AND UNIVERSITY CONTROLLER

The new regulatory environment has proven the soundness of Cornell's governance and control structures. And we expect that there will be continued pressure on our operations from regulations that will establish even higher standards for financial reporting and fiscal responsibility. Therefore, to further strengthen our foundation of governance and controls, we have undertaken initiatives to enhance resource stewardship at the university, not merely as a response to the past but as a central focus taking us into the future.

To achieve this goal, we have conducted reviews of our major administrative functions. The objectives of these reviews were to:

- Clearly define roles, responsibilities, standards of performance, and accountability within each major administrative area
- Realize substantial and ongoing savings, as well as increased effectiveness and efficiency in support services across campus
- Improve staff compensation based on market data

Our reviews and initiatives will lead us to greater integration and consolidation of effort and resources between primary university functions and operating units throughout the university. Toward that end, financial reporting lines are being restructured. Business service centers are being developed within large organizational units to handle financial transactions, and one institutional business service center has been established to be shared by smaller units. This model allows for more focused training, processing, and expertise. It also supports more explicit definition of roles and responsibilities, consistent operations within units, and a first level of review to control risk.

Other initiatives have complemented the above organizational changes. They focus on enhancing systems that support processes that can be conducted without regard to physical location. For example, during the past year, we have delivered systems that provide the campus with access to initiate, review, and authorize financial transactions using web technology. In addition, units now have desktop access to detailed information regarding labor costs, student financial transactions (tuition and fees, financial aid, graduate support), and vendor payments. Future enhancements include online travel reimbursement requests, cash receipts processes, and desktop access to capital inventories. We will continue to pursue innovations that will improve the delivery of financial services to the university and will maximize the value derived from all university assets.

To incorporate best practices, existing requirements, and new regulations into daily procedures, the university employs extensive stakeholder review and wide promulgation in its comprehensive policy creation process. Within the past year, policies related to reporting financial irregularities, recording capital assets, paying for services, and research administration have been issued or revised to respond to current conditions.

Assisted by a strong foundation of governance and accountability, we will continue to improve our practices and policies to address an ever-changing environment and the critical need for relevant, reliable, and timely financial information. These efforts will ensure that Cornell remains a leader in higher education, and maintains its standing as an international treasure for many generations to come.

"...to further strengthen our foundation of governance and controls, we have undertaken initiatives to enhance resource stewardship at the university, not merely as a response to the past but as a central focus taking us into the future."

THE YEAR IN REVIEW

During fiscal year 2002-03, the university's wealth increased, albeit slightly. We believe this is a cause for cautious optimism, and that we have "turned the corner" on the financial declines of the last few years.

Cornell ended the fiscal year at June 30, 2003 with total assets of $6.3 billion, total liabilities of $1.3 billion, and net assets of $5.0 billion. Total assets grew by $169 million, or 2.8 percent, from the prior year. Total liabilities increased by $166 million, or 14.9 percent, from fiscal year 2001–02, and net assets rose by nearly $3 million, or 0.05 percent.

The most significant increase in the university's assets was in Collateral for Securities Loaned, which at June 30, 2003 was over $205 million. This is compared to $87 million at June 30, 2002, an increase of

$118 million, or 137 percent. The amount of collateral held at any one time is temporary, because it must be returned. Consequently, the *Statement of Financial Position* also includes a corresponding liability of $205 million.

The Securities Lending program was approved by the Investment Committee of the Board of Trustees, which authorized lending up to 25 percent of the market value of the university's intermediate term funds and Long Term Investment Pool. At June 30, 2003, the amount available for lending was nearly $836 million, and $199 million was on loan. These securities never leave the university's possession. The lending program is managed by the university's custodian, and monitored by the university Investment Office, to ensure that the loaned securities are collateralized at 103 percent. During fiscal year 2002-03, the program generated $305 thousand in income.

The single largest component of the university's assets is investments, comprising $3.6 billion, or nearly 58 percent of total assets. The largest portion of the investments are held in the Long Term Investment Pool (LTIP), which returned 1.9 percent for the year ended June 30, 2003, reflecting a rebound in global stock markets during the last three months of the fiscal year. The LTIP is a highly diversified investment vehicle, and, over full market cycles, should continue to produce significant growth in the university's financial assets.

At year-end, the market value per unit was $42.65, down 5.1 percent from the prior-year unit value of $44.95. The table on the following pages shows the value of the LTIP over the last ten years. The growth over that period, from $28.01 to $42.65 per share, represents an annual compound rate of 4.3 percent. This return is net of the distributions from the pool, which have averaged 4.6 percent per year over the same ten-year period.

Cornell's policy on distributions from the LTIP is based on total return, rather than annual cash yield. Note 2 in *Notes to the Financial Statements* (page 18) explains this policy. In fiscal years 2002–03 and 2001–02, the payout rate was $2.70 per share. This rate resulted in distributions of $167.5 million and $160.5 million, for fiscal years 2002–03 and 2001-02, respectively.

The dividend for 2002-03 was 6.3 percent of the unit share value at year-end and 5.1 percent of the average unit share value for the 12 quarters ending June 30, 2002. The sources of the payout for fiscal year 2002–03 were $35.6 million in net investment income and $131.9 million in capital appreciation, all of which came from accumulated gains of prior years. Equivalent amounts for fiscal year 2001–02 were $48.9 million from investment income and $111.6 million in capital appreciation, again provided by previously accumulated gains. Therefore, the savings from the years in which we enjoyed positive double-digit returns sustained us during the past two years, allowing withdrawals of $243.5 million in gains to meet current program needs. The payout rate for fiscal year 2003-04 has been lowered by 10 percent to $2.43 per share.

"We will continue to pursue innovations that will improve the delivery of financial services to the university and will maximize the value derived from all university assets."

Table 2, on page 17, shows the value of Cornell's endowment based on Generally Accepted Accounting Principles. As indicated on the table's subtotal line 4, "Total university endowment" is $2.915 billion and corresponds to the numbers in the Net Assets section of the *Statement of Financial Position* (page 11). Purists would probably remove the $60 million of contributions receivable to obtain the value of the university endowment net assets that are actively managed. In fact, the figure reported to the National Association of College and University Business Officers for its longitudinal survey of endowments from all colleges and universities will be $2.855 billion, calculated in this way (net of $60 million contributions receivable).

Contributions receivable decreased $86 million, or 18.4 percent, from $468 million at June 30, 2002 to $382 million at June 30, 2003. These numbers represent the present value of the unconditional promises to donate to the university in the future.

One of the unintended consequences of Financial Accounting Standard 116, *Accounting for Contributions Received and Contributions Made,* is the variability in revenue and receivables caused by recording large one-time "out of the ordinary" pledges when they are made. The present value of these pledges can be sizable and cause significant swings in revenue and receivables from year to year. The decrease in contributions receivable is due to the fact that payments are being collected on existing pledges, and there were few new sizable pledges received this year. Contrast this year with fiscal year 2001-02, when the university received substantial new commitments as a result of the Weill Medical College campaign. These are significant remarkable events that do not occur every year. Table 5 in *Notes to the Financial Statements* (page 21) shows the anticipated payment schedule of the receivables at June 30, 2003, and June 30, 2002. Payments received on existing pledges during fiscal year 2002-03 totaled $131 million.

Student loans receivable decreased slightly from $73 million at June 30, 2002 to $70 million at the end of

2003. Cornell has an excellent loan collection experience. For the fiscal year ending June 30, 2003, our Perkins loan cohort default rate was 2.5 percent compared to the national rate as of June 30, 2000 of 10.6 percent (the most current rate available). Similarly, our cohort default rate on the Federal Direct Lending Program was 1.3 percent for fiscal year 2000-01, versus the national rate of 5.4 percent.

The value of land, buildings, and equipment increased by $71 million from $1.512 billion to $1.583 billion, or 4.7 percent. Projects completed during the year included the new Lab of Ornithology Center, additions to the Baker Research Institute, renovations to White Hall, and the rehabilitation and expansion of Martha Van Rensselaer Hall. Construction in progress at June 30, 2003 included Duffield Hall, the West Campus Residential Initiative – Building #1, and an addition to the School of Hotel Administration.

The largest component of the university's liabilities is bonds, mortgages, and notes payable, which totaled $495 million at June 30, 2003, decreasing by $24 million, or 4.6 percent, from the June 30, 2002 balance. This decrease is the result of regularly scheduled principal payments, and no new bonds were issued during the year. The university's rating of AA+ by Standard & Poor's was reconfirmed in June of 2003, Moody's Investors Service rating of Aa1 was last confirmed in February 2002.

The significant increase in liabilities of $166 million relates to the increase in collateral under the securities loan agreements, mentioned above. Also, accounts payable and accrued expenses grew by approximately $31 million, primarily due to the adverse adjustment to market value of the variable-to-fixed debt swaps in the current interest rate environment. The amount held as deposits and deferred revenue grew by nearly $23 million due to advance payments received from the Qatar Foundation to conduct the Weill Medical College of Cornell University in Qatar. Finally, deferred benefits rose $25 million, of which almost $15 million was due to increased obligations for post-retirement medical benefits.

Information detailing the slight increase in net assets of $2.7 million for fiscal year 2002–03, and the decrease of $110 million for fiscal year 2001–02, is shown in the *Statement of Activities* and is also summarized in Table 1 of the *Notes to the Financial Statements* (page 16).

The performance result for unrestricted general operations, which aggregates the activities of the primary and supporting missions of the university, shows a rise in net assets of $27 million. This increase represents 1.5 percent of unrestricted general operations sources of $1.8 billion after transfers out of $101 million for capital investment in physical and financial capital. There was a $12 million decline in restricted net assets used for general operations, essentially the result of higher utilization of donor-restricted funds for program activities. The pie charts on page 3 show the composition of general operations revenues and expenses.

Cornell's investment in plant and equipment was essentially break-even during fiscal year 2002–03. The year's activity resulted in gross additions of $121 million, primarily capital investments in new buildings, equipment, and principal payments on outstanding debt. Deductions for depreciation and disposals were $128 million. Contributions that had been received for construction of Duffield Hall, the Lab of Ornithology Center, and the James Baker Institute were drawn on for those projects.

Net assets in Financial capital fell $4.8 million. This was after the withdrawal of $131.9 million in prior-year accumulated gains to meet the LTIP payout, as mentioned previously. Financial capital realized losses were $84 million; however, that same group's unrealized gains were $108 million. Contributions of $80 million, (both direct payments and pledges receivable) helped to minimize the reduction in financial capital resulting from the withdrawals to meet program expenses.

Total revenue grew by $237 million, or 14 percent, from the prior year—from $1.666 billion in fiscal year 2001–02 to $1.903 billion for fiscal year 2002–03. The largest single gain was in unrealized appreciation on investments, increasing by $350 million, from an unrealized loss in 2001-02 of $224 million to an unrealized gain of $126 million for the current year. Again, this gives rise to cautious optimism as the university's overall wealth is closely linked to its investment performance.

Federal grants and contracts rose by $67 million, or 20 percent, due to increased funding from the Department of Health and Human Services for a project being

LONG-TERM INVESTMENT POOL

Source and applications ***(in millions)***
Beginning market value
Gifts and other additions
Withdrawals
Realized and unrealized gains (losses)
Ending market value
Unit value at year end ***(in dollars)*** *****

* *Unit values adjusted for 2 for 1 unit split on July 1, 1998*

> "One of the unintended consequences of Financial Accounting Standard 116... is.... [that] the present value of these pledges can be sizable and cause significant swings in revenue and receivables from year to year."

conducted at the Fermi National Accelerator Laboratory outside of Chicago. The National Science Foundation also increased its support to the university for programs at the National Astronomy and Ionosphere Center (Arecibo Radio Telescope) and nanoscale biotechnologies and information technologies. This pattern is consistent with the national pattern, with those two federal agencies showing the largest funding growth from 1990 to 2003 in constant dollars.

The largest decline in revenue was in contributions, dropping $215 million from the all-time high recorded last year of $437 million. This is the other side of the phenomenon described above, where revenue was recorded in prior years when a commitment was made. Revenue gains were also posted in the Medical Physicians' Organization ($23 million, 8.2 percent), and net tuition and fees ($19 million, 5.9 percent).

There was modest growth in expenses from the prior year, in the amount of $124 million or 7.0 percent, from $1.776 billion to $1.900 billion. Employee benefit expenses grew $25 million, or 13.3 percent, due partly to the $15 million accrual for unfunded post-retirement benefits. The higher amount is due to higher health care cost trend rates and a drop in the discount rate used to value the current obligation. Purchased services also rose $25 million or 24.5 percent due to the expenses arising from the grants and contracts mentioned above, the activities of the Weill Medical College in Qatar, and increases in the Weill Medical College Physicians' Organization expenses. Table 11 in *Notes to the Financial Statements*, on page 27, shows expenses by functional category, reflecting the increased purchased service expenses in the research, academic support, and medical services functions.

Turning to the *Statement of Cash Flows*, the university's cash and cash equivalents dropped slightly by just over $7 million, from $107 million at June 30, 2002 to almost $100 million at June 30, 2003. Net cash provided by operating activities was $149 million and Net cash provided by financing activities was $80 million. Investing activities used $236 million, to achieve the goal of being as fully invested as possible. These figures indicate a pattern somewhat similar to the prior year, in which $85 million was generated from operating activities, $148 million was added from financing activities, and $202 million was used for investing activities.

In summary, fiscal year 2002-03 was one of modestly positive results. The declines in the university's overall wealth of the previous two years appear to have been weathered adequately, with no erosion in programs or services. And with positive signs from the investment markets, it appears we are poised for a strong fiscal year 2003-04.

Joanne M. DeStefano
Vice President for Financial Affairs
and University Controller

1992–93	1993–94	1994–95	1995–96	1996–97	1997–98	1998-99	1999-00	2000–01	2001–02	2002-03
$1,027.5	$1,178.5	$1,213.2	$1,424.2	$1,748.4	$2,043.4	$2,427.6	$2,760.3	$3,288.0	$3,043.9	$2,750.4
56.1	50.6	59.2	77.4	72.8	98.9	147.8	146.4	135.4	132.5	124.3
(28.2)	(2.6)	(8.7)	(23.2)	(25.9)	(32.1)	(40.5)	(55.5)	(84.6)	(110.5)	(128.1)
123.1	(13.3)	160.5	270.0	248.1	317.4	225.4	436.8	(294.9)	(315.5)	(25.8)
$1,178.5	$1,213.2	$1,424.2	$1,748.4	$2,043.4	$2,427.6	$2,760.3	$3,288.0	$3,043.9	$2,750.4	$2,720.8
$ 28.01	$ 27.70	$ 31.28	$ 36.71	$ 41.51	$ 47.65	$ 51.16	$ 58.16	$ 51.85	$ 44.95	$ 42.65

Independent Auditor's Report

To the Board of Trustees
Cornell University

We have audited the accompanying statement of financial position of Cornell University as of June 30, 2003, and the related statements of activities and cash flows for the year then ended. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the University's 2002 financial statements and, in our report dated September 10, 2002, we expressed an unqualified opinion on those financial statements.

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 significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

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

KPMG LLP

September 9, 2003
Rochester, New York

STATEMENT OF FINANCIAL POSITION AS OF JUNE 30, 2003 (*IN THOUSANDS*)

(WITH COMPARATIVE INFORMATION FOR THE YEAR ENDED JUNE 30, 2002)

		General Operations	Physical Capital	Financial Capital	**2003** Total	**2002** Total
	Assets					
1	Cash and cash equivalents (note 2)	$ 36,546	$ 37,609	$ 25,703	$ 99,858	$ 107,422
2	Collateral for securities loaned (note 2)			205,238	205,238	86,599
3	Investments (note 2)	529,958	81,004	3,012,004	3,622,966	3,549,764
4	Accounts receivable, net (note 3)					
5	Government	45,295			45,295	43,925
6	Patient	57,065			57,065	60,035
7	Contributions	207,541	114,659	59,870	382,070	468,220
8	Other	79,113	4,702	1,859	85,674	83,368
9	Inventories and deferred charges	35,096	3,763		38,859	37,443
10	Student loans receivable (note 3C)	52,005		17,745	69,750	72,998
11	Land, buildings, and equipment, net (note 5)		1,583,491		1,583,491	1,512,469
12	Funds held in trust by others (note 1D)			93,818	93,818	92,681
13	Advances for capital investment	22,628	(22,628)			
14	Total assets	$1,065,247	$1,802,600	$3,416,237	$6,284,084	$6,114,924
	Liabilities					
15	Accounts payable and accrued expenses	$ 163,259	$ 27,000		$ 190,259	$ 159,380
16	Securities loan agreements payable (note 2)			$ 205,238	205,238	86,599
17	Deposits and deferred revenues	57,639	1,101		58,740	35,966
18	Deferred benefits (note 7)	107,607		47,278	154,885	129,974
19	Funds held in trust for others (note 1E)			62,107	62,107	74,165
20	Living trust obligations (note 1C)			71,692	71,692	66,449
21	Bonds, mortgages, & notes payable (note 6)	19,173	475,575		494,748	518,648
22	Refundable government grants	43,477			43,477	43,518
23	Total liabilities	391,155	503,676	386,315	1,281,146	1,114,699
	Net Assets (note 1B)					
24	Unrestricted					
25	Available for operations	319,705			319,705	292,438
26	Designated for student loans	5,091			5,091	4,822
27	Designated for plant		155,659		155,659	165,986
28	Net investment in plant		956,311		956,311	923,075
29	Appreciation on true endowments			874,127	874,127	970,199
30	Funds functioning as endowments			736,099	736,099	724,311
31	Temporarily restricted					
32	Available for operations	349,296			349,296	361,583
33	Designated for plant		186,954		186,954	217,552
34	Funds functioning as endowments			81,323	81,323	67,197
35	Funds subject to living trust agreements			51,916	51,916	51,281
36	Funds held in trust			35,681	35,681	33,570
37	Permanently restricted					
38	Student loan funds			29,995	29,995	28,545
39	True endowments			1,077,313	1,077,313	1,024,567
40	Funds subject to living trust agreements			33,370	33,370	34,789
41	Funds held in trust			110,098	110,098	100,310
42	Total net assets	674,092	1,298,924	3,029,922	5,002,938	5,000,225
43	Total liabilities and net assets	$1,065,247	$1,802,600	$3,416,237	$6,284,084	$6,114,924

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

STATEMENT OF ACTIVITIES FOR THE YEAR ENDED JUNE 30, 2003 (*IN THOUSANDS*)

(WITH SUMMARIZED INFORMATION FOR THE YEAR ENDED JUNE 30, 2002)

		General Operations		Physical Capital	
		Unrestricted	Temporarily Restricted	Unrestricted	Temporarily Restricted
	Revenues and other additions				
1	Tuition and fees	$ 493,217			
2	Scholarship allowance	(144,017)			
3	Net tuition and fees	349,200			
4	State appropriations	145,747		$ 12,961	
5	Federal appropriations	18,770			
6	Federal grants and contracts	397,244			
7	State and local grants and contracts	23,979			
8	Private grants and contracts	35,672			
9	Contributions	95,549	$ 35,669	3,206	$ 8,044
10	Interest and dividends	36,733	3,678	1,597	1,231
11	Net realized gain (loss) on investments	(407)	5		
12	Net unrealized gain (loss) on investments	33,792		(15,700)	
13	Medical Physicians' Organization	306,469			
14	Enterprises and subsidiaries	143,358			
15	Educational departments	60,549		4	
16	Other sources	55,945	(1,475)	2,598	448
17	Total revenues	1,702,600	37,877	4,666	9,723
18	Investment payout	131,323	14,268	553	127
19	Net assets released from restrictions	67,178	(67,178)	920	(920)
20	Capital investments (withdrawals)	(101,420)	2,746	145,267	(39,528)
21	Total revenues and other additions	1,799,681	(12,287)	151,406	(30,598)
	Expenses (Note 8)				
22	Salaries and wages	973,240			
23	Employee benefits	217,535			
24	Purchased services	129,258			
25	Supplies and general	335,959			
26	Utilities, rents, and taxes	94,154			
27	Interest expense	21,999			
28	Depreciation			123,261	
29	Other			5,236	
30	Total expenses	1,772,145		128,497	
31	Change in net assets	27,536	(12,287)	22,909	(30,598)
32	Total net assets, beginning of year	297,260	361,583	1,089,061	217,552
33	Total net assets, end of year	$ 324,796	$ 349,296	$1,111,970	$ 186,954

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

		Financial Capital			
Unrestricted	Temporarily Restricted	Permanently Restricted	**2003** Total	**2002** Total	
			$ 493,217	$ 462,830	1
			(144,017)	(133,166)	2
			349,200	329,664	3
			158,708	165,857	4
			18,770	19,495	5
			397,244	329,884	6
			23,979	22,560	7
			35,672	33,976	8
$ 21,593	$ 18,043	$ 40,502	222,606	437,373	9
15,556	16,887	15,473	91,155	119,065	10
(90,896)	1,444	5,141	(84,713)	(109,531)	11
107,261	1,157	(451)	126,059	(224,222)	12
			306,469	283,090	13
			143,358	137,075	14
			60,553	59,696	15
503	(1,318)	(2,406)	54,295	62,124	16
54,017	36,213	58,259	1,903,355	1,666,106	17
(131,876)	(14,395)				18
					19
(6,425)	(4,946)	4,306			20
(84,284)	16,872	62,565	1,903,355	1,666,106	21
			973,240	906,138	22
			217,535	192,029	23
			129,258	103,845	24
			335,959	326,907	25
			94,154	88,573	26
			21,999	23,088	27
			123,261	120,329	28
			5,236	15,465	29
			1,900,642	1,776,374	30
(84,284)	16,872	62,565	2,713	(110,268)	31
1,694,510	152,048	1,188,211	5,000,225	5,110,493	32
$1,610,226	$ 168,920	$1,250,776	$5,002,938	$5,000,225	33

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED JUNE 30, 2003 (*IN THOUSANDS*)

(WITH COMPARATIVE INFORMATION FOR THE YEAR ENDED JUNE 30, 2002)

		2003	2002
	Cash flows from operating activities		
1	Increase/(decrease) in net assets	$ 2,713	($ 110,268)
2	Adjustments to reconcile change in net assets to net cash provided by operating activities		
3	Nonoperating items		
4	Contributions for physical and financial capital	(90,228)	(184,085)
5	Net realized (gains)/losses on investments	84,713	109,531
6	Income restricted for financial capital	(13,067)	(22,453)
7	Noncash items		
8	Depreciation	123,261	120,329
9	Net unrealized (gains)/losses on investments	(126,059)	224,222
10	Loss on equipment disposals	2,628	9,853
11	Provision for receivable allowances	1,213	21,422
12	Accretion of bond discount	973	914
13	Other noncash items	1,705	1,167
14	Change in assets and liabilities		
15	Accounts receivable	85,750	(113,206)
16	Inventories and deferred charges	(3,113)	3,750
17	Accounts payable and accrued expenses	30,879	8,384
18	Deposits and deferred revenues	22,774	4,801
19	Deferred benefits	24,911	9,897
20	Refundable government grants	(41)	1,044
21	Net cash provided by operating activities	149,012	85,302
	Cash flows from investing activities		
22	Proceeds from the sale of investments	2,929,806	3,635,651
23	Purchase of investments	(2,961,662)	(3,629,058)
24	Acquisition of land, buildings, and equipment (net)	(194,555)	(180,892)
25	Student loans granted	(13,888)	(11,596)
26	Student loans repaid	15,608	13,766
27	Change in funds held in trust for others	(12,058)	(29,751)
28	Net cash used by investing activities	(236,749)	(201,880)
	Cash flow from financing activities		
29	Resources for long-term purposes		
30	Contributions restricted to		
31	Investment in true endowment	37,642	84,642
32	Investment in physical capital	8,894	54,507
33	Investment subject to living trust agreements	4,097	7,246
34	Income restricted for financial capital	13,067	22,453
35	Contributions designated for funds functioning as endowments	37,239	28,282
36	Other financing activities		
37	Principal payments of bonds, mortgages, and notes payable	(25,146)	(90,597)
38	Proceeds from issuance of bonds, mortgages, and notes payable	274	75,730
39	Change in obligations under living trust agreements	4,106	(33,909)
40	Net cash provided by financing activities	80,173	148,354
41	Net change in cash and cash equivalents	(7,564)	31,776
42	Cash and cash equivalents, beginning of year	107,422	75,646
43	Cash and cash equivalents, end of year	$ 99,858	$ 107,422

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

1. SIGNIFICANT ACCOUNTING POLICIES

A. Description of the Organization

From a fiscal viewpoint, Cornell University consists of three major organizational units: Endowed Ithaca, which includes the endowed colleges, the central university administration, and the enterprise and service operations for the Ithaca campus; Contract Colleges at Ithaca (colleges operated by Cornell on behalf of New York State); and the Joan and Sanford I. Weill Medical College and Graduate School of Medical Sciences (Medical College) in New York City. All three units are subject to the common administrative authority and control of the Cornell University Board of Trustees and operate as self-supporting entities (net assets relating to one of the units are generally not available to the other units); the only legal limitations pertain to certain donor-restricted funds and funds of the contract colleges. Specifically, the laws establishing the contract colleges at Ithaca prohibit other segments of the university from using funds attributable to those colleges. Except as specifically required by law, the contract and endowed colleges at Ithaca are, to the extent practicable, governed by common management principles and policies determined within the private discretion of Cornell University. In addition to the three major organizational units, seven subsidiary corporations are included in the financial statements. All significant intercompany transactions and balances are eliminated in the accompanying consolidated financial statements.

B. Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis in accordance with accounting principles generally accepted in the United States of America, and presented in accordance with the AICPA Audit and Accounting Guide for Not-for-Profit Organizations. The standards for general purpose external financial statements of not-for-profit organizations require a statement of financial position, a statement of activities, and a statement of cash flows, and are displayed based on the concept of "net assets." The audit guide requires presentation of net assets and revenues, expenses, gains, and losses in three categories, based on the presence or absence of donor-imposed restrictions. The categories are Permanently Restricted, Temporarily Restricted, and Unrestricted Net Assets.

Permanently restricted net assets include the historical dollar amount of gifts, including pledges and trusts, as well as gains, all of which are explicitly required by donors to be permanently retained. Pledges and trusts are reported at their estimated fair value on the date of donation.

Temporarily restricted net assets include gifts, pledges, trusts, income, and gains that can be expended, but for which the use and purpose restrictions have not yet been met. Such restrictions include purpose restrictions where donors have specified the purpose for which the net assets are to be spent, or time restrictions imposed by donors or implied by the nature of the gift (e.g., capital projects, pledges to be paid in the future, and life income funds.)

Unrestricted net assets are the remaining net assets of the university, including appreciation on true endowments where the donor restrictions are deemed to have been met.

Temporarily restricted net assets are reported as reclassifications from temporarily restricted to unrestricted when the donor purpose has been fulfilled or when the stipulated time period has elapsed. Contributions that are released from restriction within the current fiscal year are classified as increases in unrestricted net assets in the year the contribution is received.

Table 1 shows a summary of the balances and changes in net assets by restriction class for the years ended June 30, 2003 and June 30, 2002.

Classifying and aggregating items with similar characteristics into reasonably homogeneous groups and separating items with differing characteristics is a basic reporting practice that increases the usefulness of the information. Cornell has chosen to separate financial statement activity into three primary groups: general operations, physical capital, and financial capital.

General operations includes the financial activities and balances that are the result of carrying on the primary and supporting missions of the university.

Physical capital includes the activities and balances related to the acquisition, renewal, and replacement of investment in the university's infrastructure.

Financial capital includes balances or activity related to amounts set aside for the long-term economic stability of the university. Table 2 shows the composition of financial capital net assets.

As of June 30, 2003, the university's true endowment net assets consisted of approximately 15 percent for unrestricted purposes, 24 percent for student aid, 41 percent for instruction, and 20 percent for other donor-specified purposes. On June 30, 2002, the breakdown was 15 percent for unrestricted purposes, 21 percent for student aid, 42 percent for instruction, and 22 percent for other donor-specified purposes.

C. Living Trust Agreements

The university's living trust agreements with donors consist primarily of charitable gift annuities, charitable remainder trusts, and pooled income funds for which the university serves as trustee. Assets held in trust are either separately invested or included in the university's investment pools in accordance with trust instruments. Contribution revenue and the assets related to living trust agreements, net of related liabilities, are classified as increases in temporarily restricted net assets or permanently restricted net assets. Liabilities associated with charitable gift annuities and charitable remainder trusts represent the present value of the expected payments to the beneficiaries over the term of the agreement. Pooled income funds are recognized at the net present value expected to be received at a future date. Gains or losses resulting from changes in actuarial assumptions and accretion of the discount are recorded as increases or decreases in the respective net asset categories in the *Statement of Activities*.

TABLE 1. SUMMARY OF CHANGE IN NET ASSETS *(IN THOUSANDS)*

		Unrestricted	Temporarily Restricted	Permanently Restricted	Total
1	Net assets at June 30, 2001	$3,389,220	$ 643,428	$1,077,845	$5,110,493
	2002 change in net assets:				
2	General operations	25,230	45,989		71,219
3	Physical capital	62,093	26,595		88,688
4	Financial capital	(395,712)	15,171	110,366	(270,175)
5	Total change in net assets	(308,389)	87,755	110,366	(110,268)
6	Net assets at June 30, 2002	$3,080,831	$ 731,183	$1,188,211	$5,000,225
	2003 change in net assets:				
7	General operations	27,536	(12,287)		15,249
8	Physical capital	22,909	(30,598)		(7,689)
9	Financial capital	(84,284)	16,872	62,565	(4,847)
10	Total change in net assets	(33,839)	(26,013)	62,565	2,713
11	Net assets at June 30, 2003	$3,046,992	$ 705,170	$1,250,776	$5,002,938

TABLE 2. COMPOSITION OF FINANCIAL CAPITAL NET ASSETS AT JUNE 30, 2003 *(IN THOUSANDS)*
(WITH SUMMARIZED COMPARATIVE FINANCIAL INFORMATION AS OF JUNE 30, 2002)

		Net Asset Classification				
		Unrestricted	Temporarily Restricted	Permanently Restricted	**2003**	**2002**
1	True endowment and unspent earnings, including contributions receivable of $59,870	$ 874,127		$1,077,313	$1,951,440	$1,994,766
2	Functioning as endowment	736,099	$ 81,323		817,422	791,508
3	Funds held in trust		35,681	110,098	145,779	133,880
4	Total university endowment	1,610,226	117,004	1,187,411	2,914,641	2,920,154
5	Living trust funds		51,916	33,370	85,286	86,070
6	Loan funds			29,995	29,995	28,545
7	Total	$1,610,226	$ 168,920	$1,250,776	$3,029,922	$3,034,769

D. Funds Held in Trust by Others

Funds held in trust represent resources neither in the possession nor under the control of the university. These funds are administered by outside trustees, with the university deriving income or residual interest from the assets of the funds. Funds held in trust by others are recognized at the estimated fair value of the assets or the present value of the future cash flows when the irrevocable trust is established or the university is notified of its existence. Contribution revenues related to these trusts for the fiscal years 2002-03 and 2001-02 were $276,396 and $7,299,457, respectively.

E. Funds Held in Trust for Others

Financial capital includes funds invested by the university as custodian for others. Independent trustees are responsible for the funds and for the designation of income distribution. The Center Fund, which benefits the New York Cornell Weill Center of the New York Presbyterian Hospital, is one of those organizations, with assets having a market value of $72,862,624, and $75,575,880 at June 30, 2003 and June 30, 2002, respectively. Of these investments, a portion of the future income stream has been directed in perpetuity to benefit the Medical College. As such, the present value of the income stream, calculated to be $51,960,992 and $41,199,000 at June 30, 2003 and June 30, 2002, respectively, has been recorded in Net assets of financial capital.

F. Medical Physicians' Organization

The Medical Physicians' Organization provides the management structure for the practice of medicine in an academic medical center. Physician members generate clinical-practice income from their professional services to patients, in addition to conducting instructional and research activities. Medical Physicians' Organization fees are reflected as university revenues. Expenses of the clinical practice, including physician compensation, administrative operations, and provision for uncollectible accounts, are reflected as university expenses. Net assets resulting from the activities of the Medical Physicians' Organization are set aside for the respective clinical departments of the Medical College.

G. Collections

Cornell's collections, which have been acquired through purchases and contributions since the university's inception, are recognized as capital assets in the *Statement of Financial Position*. Gifts of collection items are recorded as increases in net assets in the year in which the items are acquired.

TABLE 3A. INVESTMENTS AT FAIR VALUE *(IN THOUSANDS)*

		2003	2002
1	Cash and cash equivalent holdings	($ 22,912)	$ 78,421
	Equity Securities		
2	Domestic	1,306,519	1,337,219
3	International	274,975	201,243
	Debt Securities		
4	Domestic - government	614,328	389,836
5	Domestic - corporate debt securities	275,032	355,138
6	International - governments	55,195	44,163
7	International - corporate	29,775	67,451
8	Mortgages and other asset-backed securities	78,540	156,169
	Other Investments		
9	Limited partnerships	951,058	860,440
10	Real Estate	27,217	24,510
11	Other	33,239	35,174
12	Total Investments	$3,622,966	$3,549,764

H. Derivative Instruments and Hedging Activities

The university records the fair value of its derivatives related to its investment securities within the applicable portfolio. The change in the fair value of those derivatives is included in Net unrealized gain (loss) on investments in the *Statement of Activities*.

Derivative instruments related to the university's long-term debt are included in Physical Capital, Accounts payable and accrued expenses on the *Statement of Financial Position*. The change in the fair value of the derivative instruments is also included in Net unrealized gain (loss) on investments in the *Statement of Activities*, in the Physical Capital category.

I. Use of 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 of assets, liabilities, revenues, and expenses during the reporting period. Actual results may differ from those estimates.

J. Comparative Financial Information

The *Statement of Activities* includes prior-year summarized information in total rather than by net asset class. Such information does not include sufficient detail to constitute a presentation of prior-year data in conformity with accounting principles generally accepted in the United States of America.

Accordingly, such information should be read in conjunction with the university's financial statements for the fiscal year ended June 30, 2002 from which the summarized information was derived.

K. Reclassifications

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

L. Income Taxes

The university is a not-for-profit organization as described in section 501(c) (3) of the Internal Revenue Code and is exempt from income taxes on related income pursuant to the appropriate sections of the Internal Revenue Code.

2. CASH AND INVESTMENTS

A. General Information

Investment policy of the university is established by the Investment Committee of the Board of Trustees. University investments are stated at fair value. The value of fixed-income and publicly traded equity securities is based upon quoted market prices and exchange rates, if applicable. Private equities, real estate partnerships, and certain other nonmarketable securities are valued using current information obtained from the general partner or investment manager for the respective funds. Fees paid to managers in fiscal years 2002-03 and 2001-02 for investing the university's portfolios amounted to approximately $5,900,000 and $6,900,000, respectively. The composition of investments at June 30, 2003 and June 30, 2002 are shown in Table 3A.

TABLE 3B. INVESTMENT POOLS/CATEGORIES AT FAIR VALUE *(IN THOUSANDS)*

		2003	2002
1	Working capital	$ 11,827	1,531
2	Intermediate-term (resources for spending in less than 3 years)	508,790	418,228
3	Long-term investment pool (resources held for 3 years or longer)	2,720,790	2,750,401
4	Separately invested securities	317,349	287,843
5	Life income fund pools	20,900	21,435
6	DASNY holdings	39,923	66,585
7	Other purposes of investment	3,387	3,741
8	Total Investments	$3,622,966	$3,549,764

Investment income is recorded on the accrual basis, and purchases and sales of investment securities are reflected on a trade-date basis.

Realized and unrealized gains and losses on investments are accounted for in the group (General Operations, Physical Capital, or Financial Capital) holding the assets. Realized gains and losses are calculated on the average-cost basis. Income earned from investments or from services rendered is accounted for in the same group as the assets or service provider.

The university considers all instruments that bear an original maturity date of ninety days or less to be cash or a cash equivalent. The carrying amount of cash and cash equivalents approximates fair value because of the short maturity of those instruments.

B. Collateral Held for Investments Lent to Brokerage Firms

Investment securities having a fair value of $199,323,136 and $82,780,566 at June 30, 2003 and June 30, 2002, respectively, were lent to various brokerage firms. The loaned securities are returnable on demand and are collateralized by cash deposits. The university has recorded the fair value of the collateral received of $205,238,322 and $86,598,488 and an offsetting liability for the return of the collateral in Financial Capital on the *Statement of Financial Position* at June 30, 2003 and June 30, 2002, respectively. The collateral is invested in short-term securities and income earned is credited as additional income to the investment pools.

C. Investment Pools and Separately Invested Portfolios

The university maintains a number of investment pools, and invests the principal of certain funds separately. Table 3B shows the investments by university category or pool.

The university's working capital and intermediate-term funds are invested for the production of income and capital appreciation on principal anticipated to be expended within three years.

The long-term investment pool is a mutual fund-like vehicle used for investing the university's true endowment funds, funds functioning as endowment, and other funds that are not expected to be expended for at least three years.

The pool is divided into units that represent ownership. These units are determined based on the date of purchase and market value per unit. At June 30, 2003 and June 30, 2002, the market prices per unit were $42.65 and $44.95, respectively.

The long-term investment pool was invested, as of June 30, 2003, as a balanced fund consisting of 61 percent marketable-equity securities, 11 percent real estate and private-equity investments, and 28 percent bonds and fixed-income investments. At June 30, 2002, the pool consisted of 57 percent marketable-equity securities, 12 percent real estate and private-equity investments, and 31 percent bonds and fixed-income investments. The objective is to achieve a total return, net of expenses, of at least 5 percent in excess of inflation, as measured by the Consumer Price Index, over rolling five-year periods. Table 4 summarizes certain information about the long-term investment pool.

TABLE 4. SUMMARY INFORMATION—LONG-TERM INVESTMENT POOL

		Fair Value (*in thousands*)	Cost (*in thousands*)	Net Change (*in thousands*)	Fair Value Per Unit	Number of Units
	Long-Term Investment Pool					
1	End of year	$2,720,790	$2,502,861	$ 217,929	$42.65	63,791,217
2	Beginning of year	$2,750,401	$2,604,569	$ 145,832	$44.95	61,184,733
3	Unrealized net gain for year			$ 72,097		
4	Change in interest receivable for year			2,292		
5	Realized net gain/(loss) for year			(97,909)		
6	Net gain/(loss) for year			($ 23,520)		

The university has a total return policy. Under this policy, a distribution is provided from the pool that is independent of the cash yield and investment changes occurring in a given year. This insulates investment policy from budgetary pressures, and insulates the distribution from fluctuations in capital markets. The total return of the long-term investment pool was a gain of $29,593,620 (1.90 percent) for fiscal year 2002-03. The total return consisted of $53,113,715 (3.41 percent) of income and $23,520,095 (-1.51 percent) of depreciation.

Distributions from the pool are approved by the Board of Trustees as part of the financial planning process. The annual distribution is set so that over time, a sufficient portion of the return is reinvested to maintain the purchasing power of the endowment, and to provide reasonable growth in support of program budgets.

For the year ended June 30, 2003, distributions for investment payout were $167,553,378 ($2.70 per unit), of which $146,271,647 supported general operations and physical capital. The remaining distribution of $21,281,731 was returned to principal, or went to funds held in trust for others, shown in the accompanying *Statement of Financial Position*. The distribution for 2003 was comprised of $35,634,933 in net investment income and $131,918,445 paid from prior year accumulated gains. For the fiscal year ended June 30, 2002, the investment payout was $160,549,571 ($2.70 per unit). The distribution for 2002 was comprised of $48,908,006 in net investment income and $111,641,565 paid from prior year accumulated gains.

At June 30, 2003, 1,469 of 4,680 true endowment funds invested in the long-term investment pool had market values below book values by $47,840,796, on a total book value of $387,644,017. The university holds significant unrestricted appreciation on endowments to offset this temporary decrease in value. The university has maintained these true endowment funds at their historical dollar values.

Separately invested securities consist of several types of funds that—for legal or other reasons, or by request of the donor—could not participate in any of the investment pools.

Life income fund pools consist of donated funds, the income from which is payable to one or more beneficiaries during their lifetime. On the termination of life interests, the principal becomes available for university purposes, which may or may not have been restricted by the donor.

D. Other Investments

Under the terms of certain limited partnership agreements, the university is obligated to periodically advance additional funding for private-equity and real estate investments. At June 30, 2003 and June 30, 2002, the university had commitments of approximately $335,806,000 and $394,147,000, respectively, for which capital calls had not been exercised. Such commitments generally have fixed expiration dates or other termination clauses. The university maintains sufficient liquidity in its investment portfolio to cover such calls.

The university engages in limited use of derivative instruments, including futures, options, and other similar vehicles to manage market exposure and to enhance the total return of the investment portfolio. These financial instruments and certain other investments necessarily involve market risk and counterparty credit exposure.

3. ACCOUNTS AND LOANS RECEIVABLE

A. Patient Accounts and Other

Patient accounts receivable at June 30, 2003 and June 30, 2002, are net of provisions for allowances and doubtful accounts of $58,866,618 and $60,257,246, respectively. Other accounts receivable, including student accounts, at June 30, 2003 and June 30, 2002 are

TABLE 5. CONTRIBUTIONS RECEIVABLE (*IN THOUSANDS*)

		2003	2002
	Contributions expected to be realized		
1	In one year or less	$ 92,735	$ 111,432
2	Between one year and five years	288,196	393,747
3	More than five years	138,335	131,075
4	Gross contributions receivable	519,266	636,254
5	Discount	(117,087)	(143,391)
6	Allowance	(20,109)	(24,643)
7	Total discount and allowance	(137,196)	(168,034)
8	Net contributions receivable	$ 382,070	$ 468,220

net of allowances for doubtful accounts of $1,701,680 and $1,565,779, respectively.

B. Contributions

Contributions, which include unconditional written or oral promises to donate to the university in the future, are recognized when received. Contributions of approximately $382,070,000 and $468,220,000, representing the present value of future cash flows, are recorded as receivables at June 30, 2003 and June 30, 2002, respectively. The corresponding revenue is assigned to the appropriate net asset category in the year the promise is received. The face value, discount (7.00 percent for both fiscal years 2002-03 and 2001-02), and allowance for contributions receivable are shown in Table 5. Conditional promises are recorded when donor stipulations are substantially met. At June 30, 2003 and 2002, conditional promises and donor intentions not reflected in the financial statements were approximately $114,060,000 and $107,042,000, respectively. Expenses related to fund-raising activities amounted to approximately $24,667,000 and $21,425,000 for fiscal years 2002-03 and 2001-02, respectively.

C. Student Loans

Student loans receivable at June 30, 2003 and June 30, 2002, are reported net of allowances for doubtful loans of $8,439,983 and $7,332,306, respectively. The allowance is intended to provide for loans, both in repayment status and not yet in repayment status (borrowers are still in school or in the grace period following graduation), that may not be collected.

Determination of the fair value of student loans receivable could not be made without incurring excessive costs. These loans include donor-restricted and federally sponsored student loans that bear mandated interest rates and repayment terms, and are subject to significant restrictions on their transfer and disposition.

4. PLEDGED ASSETS AND FUNDS ON DEPOSIT

The Dormitory Authority of the State of New York (DASNY) and others hold investments in lieu of various required reserves as follows: $10,138,715 and $10,256,099 at June 30, 2003 and June 30, 2002, respectively, of financial capital; and $389,541 and $1,079,935, respectively, of general operations. Escrow held by the Workers' Compensation Board of New York includes investment securities of financial capital comprised of United States government obligations of $106,281 and $105,000 at June 30, 2003 and June 30, 2002, respectively.

Physical capital assets include cash and United States government obligations of $36,682,363, and $26,854,200 at June 30, 2003 and June 30, 2002, respectively, held by DASNY, that will be used primarily for the retirement of debt at a future time. In addition, $14,586 and $36,436,510 of bond proceeds were on deposit for future project expenditures at June 30, 2003 and 2002, respectively.

Student loan assets in general operations include $3,225,883 and $3,294,315 at June 30, 2003 and June 30, 2002, respectively, on deposit with DASNY that are available for the retirement of debt at a future time.

TABLE 6. LAND, BUILDINGS, AND EQUIPMENT *(IN THOUSANDS)*

		Book value at June 30, 2002	Additions	Disposals and Closed Projects	Book value at June 30, 2003
1	Land, buildings, and improvements	$1,700,180	$ 97,850	$ 889	$1,797,141
2	Furniture, equipment, books, and collections	858,891	83,642	54,660	887,873
3	Construction in progress	137,292	118,805	103,385	152,712
4	Total before accumulated depreciation	2,696,363	$ 300,297	$ 158,934	2,837,726
5	Accumulated depreciation	(1,183,894)			(1,254,235)
6	Land, buildings and equipment, net	$1,512,469			$1,583,491

5. PHYSICAL CAPITAL

Physical plant and equipment are stated principally at cost at date of acquisition or at fair value on the date of donation, net of accumulated depreciation. Depreciation is computed on a straight-line basis over the useful lives of the buildings (30–100 years) and equipment (3–15 years). A full year of depreciation is taken in the year of acquisition, and no depreciation is taken in the year of disposal. Depreciation expense is reflected as a cost of physical capital.

Capital investments and withdrawals consist of net transfers to physical capital for principal payments on debt and the acquisition of capital assets.

Expenditures associated with the construction of new facilities are shown as construction in progress until the projects are completed. Land, buildings, and equipment are detailed in Table 6.

Gifts-in-kind of capital assets were approximately $2,356,000 and $9,408,000 for fiscal years 2002-03 and 2001-02, respectively.

Certain properties to which the university does not have title are included in physical capital at net book value as follows: (1) land, buildings, and equipment of the contract colleges aggregating $317,759,000 and $300,545,000 at June 30, 2003 and June 30, 2002, respectively, the acquisition cost of which was borne primarily by New York State; and (2) land, buildings, and equipment for which title rests with government and corporate agencies aggregating $23,417,000 and $25,652,000 at June 30, 2003 and June 30, 2002, respectively.

The university is planning to decommission and retire the Ward Center's nuclear reactor. A decommissioning plan will be submitted to the Nuclear Regulatory Commission to begin the process of fuel removal and contractor bids. Retirement costs are not available at this time.

6. BONDS, MORTGAGES, AND NOTES PAYABLE

The balance outstanding, interest rates, and final maturity dates of the bonds and other debt as of June 30, 2003 and June 30, 2002, are summarized in Table 7.

The total annual debt service requirements for the next five fiscal years and thereafter are shown in Table 8. Interest expense paid during fiscal year 2002-03 and 2001-02 was approximately $21,027,000 and $22,174,000, respectively. Debt and debt service related to borrowings by New York State for the construction and renovation of facilities of the contract colleges are not included in the *Financial Statements* because they are not liabilities of the university.

Under agreement with DASNY, certain revenues, principally rental income from facilities financed by bond proceeds plus a portion of tuition, are pledged by the university to meet debt service requirements (see note 4). Also, certain revenue bonds require compliance with an asset-to-liability ratio and an unencumbered securities-to-operating-expense ratio.

The fair value of the university's bonds, mortgages, and notes payable is approximately $509,817,000 and $528,875,000 at June 30, 2003 and June 30, 2002, respectively. The estimated fair value of bonds is based on quoted market prices for the same or similar issues. The market prices utilized reflect the amount a third party would pay to purchase the bonds; they do not reflect an additional liability to the university.

The university has interest rate swap agreements to exchange variable rate debt for a fixed rate obligation without the exchange of the underlying principal amount. Under these arrangements, in effect at June 30, 2003, the counter party pays the university a variable interest rate equal to the BMA index. The university will pay the counter party a fixed interest rate of 4.63 percent on a notional amount of $83,695,000; 2.99 percent on a notional amount of $84,505,000; 4.52 percent on a notional amount of $43,070,000; and 4.33 percent on a notional amount of $15,390,000. Net payments or receipts under the swap agreement are recorded as an

TABLE 7. BONDS, MORTGAGES, AND NOTES PAYABLE (*IN THOUSANDS*)

		Balance June 30, 2003	Balance June 30, 2002	Interest Rates	Maturity Date
	Plant Funds				
1	Dormitory Authority of the State of New York (DASNY)				
2	Revenue Bond Series				
3	1990B	59,000	59,300	2.26 to 2.57*	2025
4	1993	1,290	1,895	4.90 to 5.10	2005
5	1996	91,795	101,215	4.80 to 5.40	2014
6	2000A	64,505	65,905	2.99	2029
7	2000B	83,695	85,240	4.63	2030
8	Bond Series 1987B	15,150	16,065	11.11	2012
9	DASNY 1993 Pooled Loan Program	1,696	1,828	1.40 to 2.00*	2012
10	Commercial Paper	68,760	68,760	1.00 to 2.99*	2028
11	Industrial Development Agency				
12	2000	7,900	8,695	4.65 to 5.25	2011
13	2002A	43,070	43,225	4.52	2030
14	2002B	15,390	15,390	4.33	2015
15	Student Loan Marketing Association	6,430	6,665	5.75 to 6.50	2019
16	Urban Development Corporation	3,250	3,375	zero	2029
17	Capitalized Leases	13,213	13,600	various	2020
18	Private Foundation Line of Credit	0	5,000	zero	2003
19	Other	431	330	various	2004
20	Total Physical Capital	475,575	496,488		
	Student Loan Funds				
21	DASNY Bond 1992 Capital Appreciation	$ 4,083	$ 5,129	6.60 to 6.80	2009
22	DASNY Bond 1993 Serial	0	755	4.90	2003
23	DASNY Bond 1993 Capital Appreciation	3,089	2,929	5.25 to 5.50	2007
24	DASNY Bond 1995 Serial	3,890	5,695	5.25 to 5.45	2005
25	DASNY Bond 1995 Capital Appreciation	8,111	7,652	5.70 to 6.15	2011
26	Total General Operations—Student Loans	19,173	22,160		
27	Total Bonds, Mortgages, and Notes Payable	$ 494,748	$ 518,648		

** Rates presented are the actual rates paid during fiscal year 2002-03. These rates are variable based on market conditions.*

TABLE 8. ANNUAL DEBT SERVICE REQUIREMENTS *(IN THOUSANDS)*

	Year	Principal	Interest	Annual Installment Total
1	2004	$ 19,447	$ 22,810	$ 42,257
2	2005	19,708	21,691	41,399
3	2006	18,946	21,140	40,086
4	2007	19,108	20,112	39,220
5	2008	18,468	19,038	37,506
6	Thereafter	399,071	179,340	578,411
7	Total	$ 494,748	$ 284,131	$ 778,879

adjustment to interest expense. The contractual relationship under these agreements will last until July 1, 2030.

The university continues to issue commercial paper under an agreement entered into in fiscal year 1998-99 for $100,000,000. Under the agreement, a total of $490,000,000 of principal may be issued, with a maximum of $100,000,000 outstanding at any one time. The funds may be used for new capital projects, and to refinance earlier projects.

7. BENEFIT PLANS

A. Pension Plans

The university's employee pension plan coverage for Endowed Ithaca and the Medical College is provided by two basic types of plan: that based on a predetermined level of funding (defined contribution) and that based on a level of benefit to be provided (defined benefit). The primary plans for Endowed Ithaca and for exempt employees (those not subject to the overtime provisions of the Fair Labor Standards Act) at the Medical College are carried by the Teachers Insurance and Annuity Association and the College Retirement Equities Fund, which also permit employee contributions. Medical College non-exempt employees and certain non-exempt employees of Endowed Ithaca are covered by defined benefit plans. Certain accrued benefits and an appropriate amount of the university's pension reserves are frozen in connection with plan reorganizations.

The pension liabilities recognized by the university in connection with the frozen plans were established by charges to expenses in prior years, to meet future retirement costs for current employees. Although the liabilities are considered internally funded, they are not intended to create a trust or fund in which any employee or former employee has any right or interest of any kind.

In accordance with ERISA requirements for the defined benefit plans, the university must annually fund with an independent trustee an actuarially determined amount that represents normal costs plus amortization of prior service costs over a forty-year-period that began on July 1, 1976.

The defined benefit plans' funded status, amounts recognized in the university's *Statement of Financial Position* at June 30, 2003, and assumptions used for calculations are shown in Table 9.

Total pension costs of the Endowed Ithaca and Medical College plans for the year ended June 30, 2003 and June 30, 2002, amounted to $51,247,423 and $47,121,663, respectively.

Employees of the contract colleges are covered under the New York State pension plan. Contributions to the state retirement system and other employee benefit costs are paid directly by the state. The amount of the direct payments applicable to the university as revenue and expenditures is not currently determinable and is not included in the *Financial Statements*. The university reimburses the state for employee benefit costs on certain salaries, principally those associated with externally sponsored programs. The amount reimbursed to the state during the years ended June 30, 2003 and June 30, 2002, was $10,949,189 and $9,893,852, respectively, which are included in the expenses of general operations.

B. Postretirement Benefits Other Than Pensions

The university provides health and life insurance benefits for eligible retired employees and their dependents. Although there is no legal obligation for future benefits, the cost of postretirement benefits must be accrued during the service lives of employees. The university elected the prospective-transition approach and is amortizing the transition obligation over twenty years, through fiscal year 2012-13.

The plan assets for Endowed Ithaca and the Medical College are invested with an outside trustee.

Tables 10A and 10B set forth the funded status of the plans as of June 30, 2003 and June 30, 2002, the components of net periodic postretirement benefit costs for 2003 and 2002, and the assumptions used in accounting for the plans during 2003 and 2002. The accrued postretirement benefit cost shown in Table 10A is $14,587,000 of current-year unfunded cost plus $43,113,000 of accumulated prior-year unfunded cost.

C. Postemployment Benefits

The university provides various benefits to former or inactive employees after employment, but before retirement. The expected costs of these benefits are recognized when they are earned, even though there may not be any legal requirement to continue the programs. Current-year estimated costs are allocated among the expenses of general operations.

TABLE 9. DEFINED BENEFIT PENSION PLANS – BENEFIT OBLIGATIONS, NET ASSETS AND COST (*IN THOUSANDS*)

				2003	2002
		Endowed Ithaca*	Medical College	Combined	Combined
	Change in benefit obligation				
1	Benefit obligation at beginning of year	$ 20,032	$ 30,258	$ 50,290	$ 50,951
2	Service costs (benefits earned during the period)		1,858	1,858	1,654
3	Interest cost on projected benefit obligation	1,321	2,099	3,420	3,426
4	Actuarial (gain)/loss	1,870	4,084	5,954	(1,205)
5	Benefits paid	(2,046)	(1,872)	(3,918)	(4,536)
6	Benefit obligation at end of year	21,177	36,427	57,604	50,290
	Change in plan assets				
7	Fair value of plan assets at beginning of year	28,798	31,179	59,977	70,279
8	Return on plan assets	683	1,020	1,703	(5,766)
9	Benefits paid	(2,046)	(1,872)	(3,918)	(4,536)
10	Fair value of plan assets at end of year	27,435	30,327	57,762	59,977
11	Excess/(deficiency) of plan assets over projected benefit obligation	6,258	(6,100)	158	9,687
12	Unrecognized prior service costs		7	7	115
13	Unrecognized net loss from past experience different than assumed	9,261	6,544	15,805	6,746
14	Prepaid pension cost	$ 15,519	$ 451	$ 15,970	$ 16,548
	Net periodic pension cost components				
15	Prepaid service cost		$ 1,858	$ 1,858	$ 1,654
16	Interest cost on projected benefit obligation	$ 1,321	2,099	3,420	3,427
17	Expected return on plan assets	(2,505)	(2,577)	(5,082)	(6,017)
18	Net amortization and deferral of:				
19	Initial transition obligation				206
20	Prior service cost		108	108	108
21	Net (gain) loss	274		274	(154)
22	Net periodic pension cost (income)	($ 910)	$ 1,488	$ 578	($ 776)

			2003		2002
		Endowed Ithaca	Medical College	Endowed Ithaca	Medical College
	Assumptions used in accounting for the plans as of June 30				
23	Discount rate	5.75%	5.75%	7.00%	7.00%
24	Expected return on plan assets	9.00%	9.00%	9.00%	9.00%
25	Rate of compensation increase	4.00%	6.10%	4.00%	6.10%

** A frozen retirement plan for the non-exempt employees of the endowed colleges at Ithaca*

TABLE 10A. POSTRETIREMENT BENEFITS OTHER THAN PENSIONS BENEFIT OBLIGATIONS, NET ASSETS AND COST *(IN THOUSANDS)*

				2003	2002
		Endowed Ithaca	Medical College	Combined	Combined
	Change in benefit obligation				
1	Benefit obligation at beginning of year	$ 194,413	$ 38,999	$ 233,412	$ 187,826
2	Service costs (benefits earned during the period)	6,206	2,510	8,716	6,908
3	Interest cost on projected benefit obligation	12,565	2,947	15,512	13,806
4	Actuarial loss	32,987	11,432	44,419	31,909
5	Benefits paid (outside of trust)	(5,760)	(1,712)	(7,472)	(7,037)
6	Benefit obligation at end of year	240,411	54,176	294,587	233,412
	Change in plan assets				
7	Fair value of plan assets at beginning of year	37,809	14,785	52,594	52,814
8	Return on plan assets	(65)	77	12	(5,109)
9	Employer contribution	4,231	900	5,131	4,889
10	Fair value of plan assets at end of year	41,975	15,762	57,737	52,594
11	Excess/(deficiency) of plan assets over projected benefit obligation	(198,436)	(38,414)	(236,850)	(180,818)
12	Unrecognized obligation	26,679	9,764	36,443	40,088
13	Unrecognized prior service costs		687	687	871
14	Unrecognized net loss from past experience different than assumed	118,475	23,545	142,020	96,746
15	Prepaid/(accrued) postretirement benefit cost	($ 53,282)	($ 4,418)	($ 57,700)	($ 43,113)
	Net periodic postretirement benefit cost components				
16	Service costs (benefits during the period)	$ 6,206	$ 2,510	$ 8,716	$ 6,908
17	Interest cost on projected benefit obligation	12,565	2,947	15,512	13,806
18	Expected return on plan assets	(3,403)	(1,330)	(4,733)	(4,753)
19	Net amortization and deferral of:				
20	Initial transition obligation	2,668	976	3,644	3,644
21	Prior service cost		184	184	184
22	Net loss	3,115	752	3,867	2,550
23	Net periodic postretirement benefit cost	$ 21,151	$ 6,039	$ 27,190	$ 22,339

8. FUNCTIONAL EXPENSES AND STUDENT AID

Table 11 shows expenses by functional category for General Operations and Physical Capital. Expenses for operations and maintenance of facilities, depreciation, and interest have been allocated to functional categories using square-footage statistics. The amount allocated for operations and maintenance was approximately $132,085,000 for fiscal year 2002-03, and $133,890,000 for fiscal year 2001-02.

Institutionally provided student financial assistance that is not given in exchange for services is shown as a discount against revenue rather than as an expense. Aid in excess of the institution's actual tuition and fees, of $18,860,379 and $16,891,196 for fiscal years 2002-03 and 2001-02, respectively, is classified as Instruction expense.

9. SUBSEQUENT EVENTS AND CONTINGENT LIABILITIES

The university is a defendant in various legal actions, some of which are for substantial monetary amounts, that arise out of the normal course of its operations. Although the final outcome of the actions cannot currently be determined, the university's administration is of the opinion that eventual liability, if any, will not have a material effect on the university's financial position.

The university retains self insurance for property, general liability, and certain health benefits, and has an equity interest in a multiprovider captive insurance company.

TABLE 10B. POSTRETIREMENT BENEFITS OTHER THAN PENSIONS BENEFIT OBLIGATIONS, NET ASSETS AND COST *(IN THOUSANDS)*

CONTINUED

		2003		2002	
		Endowed Ithaca	Medical College	Endowed Ithaca	Medical College
	Assumptions used in accounting for the plans as of July 1				
1	Discount rate	5.75%	5.75%	7.00%	7.00%
2	Expected return on plan assets	9.00%	9.00%	9.00%	9.00%
3	Health care cost trend rate - initial	10.00%	10.00%	10.00%	10.00%
4	Health care cost trend rate - final	5.00%	5.00%	5.00%	5.00%
5	Years to reach final	5	5	6	6

		2003		2002	
		Endowed Ithaca	Medical College	Endowed Ithaca	Medical College
	Effect of 1 percentage point change in assumption of Health Care Cost trend rate				
6	1-Percentage point increase				
7	Effect on total service cost and interest cost components	$ 3,875	$ 963	$ 3,514	$ 592
8	Effect on accumulated postretirement benefit obligation as of June 30	$ 39,268	$ 6,952	$ 31,594	$ 4,776
9	1-Percentage point decrease				
10	Effect on total service cost and interest cost components	($ 3,036)	($ 781)	($ 2,755)	($ 484)
11	Effect on accumulated postretirement benefit obligation as of June 30	($ 31,732)	($ 5,827)	($ 25,541)	($ 4,013)

TABLE 11. FUNCTIONAL EXPENSES (IN THOUSANDS)

		General Operations	Physical Capital	2003	2002
1	Instruction	$ 398,191	$ 24,551	$ 422,742	$ 396,872
2	Research	422,533	25,527	448,060	414,674
3	Public service	97,802	2,574	100,376	99,134
4	Academic support	133,195	29,146	162,341	149,979
5	Student services	84,107	9,219	93,326	93,702
6	Medical services	330,780	3,061	333,841	294,078
7	Institutional support	156,925	12,745	169,670	168,778
8	Enterprises and subsidiaries	148,612	21,674	170,286	159,157
9	Total expenses and deductions	$1,772,145	$ 128,497	$1,900,642	$1,776,374

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JULY 1, 2003

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