



UNIVERSITY OF THE PACIFIC

Consolidated Financial Statements

June 30, 2002

(With Independent Auditors' Report Thereon)



Three Embarcadero Center
San Francisco, CA 94111

Independent Auditors' Report

The Board of Regents
University of the Pacific:

We have audited the accompanying consolidated balance sheet of the University of the Pacific as of June 30, 2002, and the related consolidated statements of activities and cash flows for the year then ended. These consolidated financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. The prior year summarized comparative information has been derived from the University's 2001 financial statements and, in our report dated September 25, 2001, 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of the University of the Pacific as of June 30, 2002, 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.

September 27, 2002



UNIVERSITY OF THE PACIFIC

Consolidated Balance Sheet

June 30, 2002

(With comparative financial information as of June 30, 2001)

(In thousands)

Assets	2002	2001
Cash and cash equivalents	\$ 21,470	22,531
Accounts receivable, net	12,886	12,497
Pledges receivable, net	17,023	18,253
Inventories, prepaid expenses, and other assets	5,614	5,902
Student loans receivable, net	26,083	24,409
Investments	202,553	192,281
Fixed assets, net	146,731	129,084
Total assets	\$ 432,360	404,957
Liabilities and Net Assets		
Liabilities:		
Accounts payable and accrued liabilities	\$ 15,497	16,388
Advance deposits and deferred revenue	5,225	4,752
Self-insurance reserves	2,673	2,568
Early retirement reserves	2,381	2,391
Capital lease obligations	1,463	1,518
Notes and bonds payable	85,568	60,898
Trust and annuity obligations	10,815	10,217
Federal student loan funds	23,819	22,891
Total liabilities	147,441	121,623
Contingencies		
Net assets:		
Unrestricted	163,348	167,324
Temporarily restricted	30,138	29,783
Permanently restricted	91,433	86,227
Total net assets	284,919	283,334
Total liabilities and net assets	\$ 432,360	404,957

See accompanying notes to consolidated financial statements.

UNIVERSITY OF THE PACIFIC
Consolidated Statement of Activities
Year ended June 30, 2002
(With summarized financial information for the year ended June 30, 2001)
(In thousands)

	2002			Total	2001 Totals
	Unrestricted	Temporarily restricted	Permanently restricted		
Revenues, gains, and other support:					
Tuition and student fees	\$ 138,550	—	—	138,550	129,426
University-sponsored financial aid	(29,198)	—	—	(29,198)	(27,687)
Donor-sponsored financial aid	(3,186)	—	—	(3,186)	(2,880)
Net tuition and fees	106,166	—	—	106,166	98,859
Sales and services of auxiliary enterprises	19,000	—	—	19,000	17,284
Government grants and contracts	17,494	—	—	17,494	14,682
Private grants, gifts, and bequests	7,720	1,693	5,501	14,914	38,583
Investment return distributed	8,689	340	(23)	9,006	10,330
Dental clinic fees	7,792	—	—	7,792	7,097
Other	7,979	347	146	8,472	6,898
Actuarial gain (loss) on annuity and trust obligations	73	131	(418)	(214)	830
Net assets released from restrictions	2,156	(2,156)	—	—	—
Total revenues, gains, and other support	177,069	355	5,206	182,630	194,563
Expenses:					
Instructional and departmental research	83,770	—	—	83,770	78,722
Auxiliary enterprises	20,183	—	—	20,183	18,121
Sponsored programs	10,283	—	—	10,283	8,444
Academic support	7,024	—	—	7,024	7,075
Student services	10,363	—	—	10,363	9,416
Student aid	2,361	—	—	2,361	1,852
General administration	5,179	—	—	5,179	4,749
Fund-raising activities	5,661	—	—	5,661	4,947
Operations and maintenance at plant	12,313	—	—	12,313	9,483
Depreciation and amortization	9,720	—	—	9,720	8,768
Interest	3,758	—	—	3,758	3,519
Total expenses	170,615	—	—	170,615	155,096
Increase in net assets from operations	6,454	355	5,206	12,015	39,467
Other changes:					
Investment (loss) income, net of distributions	(10,286)	—	—	(10,286)	(2,413)
Other	(144)	—	—	(144)	—
(Decrease) increase in net assets	(3,976)	355	5,206	1,585	37,054
Net assets, beginning of year (restated)	167,324	29,783	86,227	283,334	246,280
Net assets, end of year	\$ 163,348	30,138	91,433	284,919	283,334

See accompanying notes to consolidated financial statements.

UNIVERSITY OF THE PACIFIC
Consolidated Statement of Cash Flows
Year ended June 30, 2002
(With comparative financial information as of June 30, 2001)
(In thousands)

	<u>2002</u>	<u>2001</u>
Cash flows from operating activities:		
Increase in net assets	\$ 1,585	37,054
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation and amortization	9,720	8,768
Noncash contributions	(1,596)	(10,231)
Other noncash items	144	—
Changes in assets and liabilities, net of effect of Feather River:		
Accounts receivable	(387)	620
Pledges receivable	1,230	(12,007)
Inventories, prepaid expenses, and other assets	343	(414)
Accounts payable and accrued liabilities	(1,277)	1,759
Advance deposits and deferred revenue	426	(1,225)
Self-insurance reserves	105	(179)
Early retirement services	(10)	(10)
Trust and annuity obligations	598	753
Federal student loan funds	928	711
Net realized and unrealized gains (losses) on investments	7,335	(93)
Interest and dividends restricted for long-term investment	23	(201)
Contributions restricted for long-term investment	(7,562)	(10,946)
Net cash provided by operating activities	<u>11,605</u>	<u>14,359</u>
Cash flows from investing activities:		
Proceeds from sale of investments	173,638	103,619
Purchase of investments	(189,649)	(97,891)
Purchase of fixed assets	(25,395)	(25,179)
Proceeds from student loans collections	5,078	4,304
Student loans issued	(6,752)	(4,156)
Feather River cash acquired	9	—
Net cash used in investing activities	<u>(43,071)</u>	<u>(19,303)</u>
Cash flows from financing activities:		
Contributions restricted for long-term investment	7,562	10,946
Other financing activities:		
Proceeds from issuance of bonds	24,789	—
Increase in notes payable	—	176
Payment on notes payable, bonds payable, and capital leases	(1,923)	(1,367)
Interest and dividends restricted for reinvestment	(23)	201
Net cash provided by financing activities	<u>30,405</u>	<u>9,956</u>
Net (decrease) increase in cash and cash equivalents	(1,061)	5,012
Cash and cash equivalents, beginning of year	<u>22,531</u>	<u>17,519</u>
Cash and cash equivalents, end of year	<u>\$ 21,470</u>	<u>22,531</u>
Supplemental disclosure of cash flow information:		
Interest paid	\$ 3,216	3,021
Supplemental disclosure of noncash investing and financing activities:		
Equipment acquired under capital leases	\$ 766	782

See accompanying notes to consolidated financial statements.

UNIVERSITY OF THE PACIFIC

Notes to Consolidated Financial Statements

June 30, 2002

(With comparative 2001 financial information)

(1) Significant Accounting Policies

(a) *Nature of Operations*

The University of the Pacific (University) was founded in 1851 and offers undergraduate and graduate programs of higher education through three campuses located in Northern California. Funding sources generally include tuition and fees charged to students, income of auxiliary enterprises, grants, contracts, gifts, and bequests.

(b) *Basis of Presentation*

The financial statements of the University have been prepared on the accrual basis of accounting.

The financial statements include the accounts of the University as of and for the 12 months ended June 30, 2002 and Feather River Inn, Inc. (Feather River) as of and for the three months ended March 31, 2002. The University has had a controlling financial interest in Feather River since January 1, 2002.

The University classifies net assets and revenues, expenses, gains and losses into three categories, based on the existence or absence of donor-imposed restrictions. The categories are permanently restricted, restricted, and unrestricted net assets.

- Permanently restricted net assets are comprised of the historical dollar amount of gifts, including pledges, trusts, and remainder interests, which are required by donors to be permanently retained. Pledges, trusts, and remainder interests are reported at their estimated present values. Endowments are reported at the original amount of the gift plus the portion, if any, of earnings explicitly stipulated by the donor to be added to corpus.
- Temporarily restricted net assets include gifts, pledges, trusts, remainder interests, and income and gains on restricted contributions which can be expended but for which 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 (capital projects, pledges to be paid in the future, life income funds, etc.)
- Unrestricted net assets are all the remaining net assets of the University. Unrestricted net assets are, in part, designated for specific purposes by action of the board of regents and may otherwise be limited by contractual agreements with outside parties.

In accordance with the American Institute of Certified Public Accountants *Audit and Accounting Guide*, (i) tuition and fees are reflected net of financial aid provided in the form of institutional scholarships; (ii) expenses include vested benefits of employees for future compensated absences; and (iii) funds administered as an intermediary for others, including student loan funds provided by federal agencies, are accounted for as liabilities rather than as net assets of the University.

UNIVERSITY OF THE PACIFIC

Notes to Consolidated Financial Statements

June 30, 2002

(With comparative 2001 financial information)

(c) Cash and Cash Equivalents

Cash and cash equivalents include all cash balances and highly liquid investments with a maturity of three months or less other than cash equivalents included in the University's investment pool.

The University maintains its operating cash accounts in several commercial banks. The accounts at the banks are guaranteed by the Federal Deposit Insurance Corporation up to \$100,000 for each financial institution. The University has not experienced losses on these deposits to date.

(d) Inventories

Inventories, consisting principally of clinic supplies, are valued at the lower of average cost or market.

(e) Investments

Investments in equity securities with readily determinable fair values and all investments in debt securities are carried at fair value based on published market values. Investments in real estate and securities for which fair value is not readily determinable are carried at cost, if purchased, or at fair value at the date of receipt, if acquired by donation. These investment securities are exposed to various risks, such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investments securities will occur in the near term and that such changes could materially affect total net assets and the amounts reported in the statement of financial position.

Net appreciation (depreciation) in the fair value of those investments that are accounted for at fair value, including realized gains or losses and unrealized appreciation (depreciation) on those investments, as well as all dividends, interest, and other investment income, is shown in the statement of activities. Gains and investment income that are limited to specific uses by donor-imposed restrictions are reported as increases in unrestricted net assets if the restrictions are met in the same reporting period that the gains and income are recognized. Losses on investments related to gifts that the donor required to be invested in perpetuity (i.e., endowment funds) are classified as decreases in unrestricted net assets; subsequent gains that restore the fair value of the assets of the endowment funds to the required level are classified as increases in unrestricted net assets.

UNIVERSITY OF THE PACIFIC

Notes to Consolidated Financial Statements

June 30, 2002

(With comparative 2001 financial information)

(f) *Endowment Investment Return Spending Policy*

The University invests certain assets on a pooled basis under a methodology wherein the investment returns of the pool are allocated proportionately among the individual funds and activities participating in the pool. Board policy allows the board of regents to appropriate portions of the net appreciation resulting from investment of endowment corpus and from investment of amounts set aside by the board of regents as quasi-endowment investments as is prudent considering the University's long- and short-term needs, present and anticipated financial requirements, expected total return on its investments, price level trends and general economic conditions. Under the University's endowment spending policy, 5.5% of the average fair value at the end of the previous three years of endowment and quasi-endowment investments is appropriated to support current operations.

(g) *Fixed Assets*

Fixed assets are recorded at cost, if purchased, or at fair market value at the date of gift, if acquired by donation. Depreciation is computed using the straight-line method over the assets' estimated useful lives ranging from 7 to 40 years.

Repairs and maintenance are expensed as incurred. The cost and accumulated depreciation of assets retired or sold are removed from the accounts and a gain or loss is recognized in the year of disposal.

(h) *Contributions*

Unconditional contributions received, including unconditional promises or pledges, are recognized as revenue when the donors' unconditional commitment is received. Conditional promises and gifts are recorded as revenue when donor's conditions are substantially met. Pledges in excess of \$5,000 are recorded at the estimated present value of the future cash flows, net of an allowance for nonfulfillment. Promises made that are designated for future periods or are restricted by the donor for specific purposes are reported as temporarily restricted or permanently restricted support, depending on the nature of the restriction. Donor-restricted gifts, including investment return on endowments, which are received and either spent or deemed spent within the same year are reported as unrestricted revenues. Gifts of long-lived assets are reported as temporarily restricted net assets until expensed, at which time the restrictions are released and net asset amount is reclassified to the unrestricted category.

(i) *Funds Held in Trust by Others*

Funds held in trust by others represent assets irrevocably held and administered by trustees other than the University with the University named as a beneficiary to derive income or a residual interest from the assets of such funds after the passage of time or occurrence of specified events. When the University is notified that funds have been put in a trust held by others with the University designated as beneficiary, contribution income is recognized as an increase in temporarily or permanently restricted net assets, depending on the nature of restriction imposed by the donor, at the estimated present value of the future cash flows to be received by the University. Under the terms of a trust agreement that has been classified as permanently restricted, the University can appropriate up to \$925,000 from funds held in this trust if it suffers an occurrence of severe financial hardship.

UNIVERSITY OF THE PACIFIC

Notes to Consolidated Financial Statements

June 30, 2002

(With comparative 2001 financial information)

(j) *Undistributed Estates*

Bequests are recorded as contribution income when the court orders distribution.

(k) *Expenses*

Expenses are reported as decreases in unrestricted net assets.

(l) *Use of Estimates in the Preparation of Financial Statements*

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 and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(m) *Self-Insurance*

The University is self-insured for workers' compensation, unemployment, dental, and disability benefits. Annual provisions to adjust reserves for claims are recorded as expenses of unrestricted net assets. Reserves for unpaid claims are estimated using actuarial methods. The University maintains stop-loss coverage for workers' compensation benefits with an independent insurance company to reduce its exposure to loss. It is possible that the amounts paid in connection with self-insured risks will vary from amounts accrued as self-insurance reserves.

(n) *Measure of Operations*

The statement of activities reports the change in net assets from operations, the excess of revenues, gains and support over expenses and losses exclusive of the portion of investment return designated by the University's board of regents for future years' operations and exclusive of revenues or expenses related to unusual or nonrecurring items. As to investment return, the board of regents designates only a portion of the University's cumulative investment return for support of current operations; the remainder is retained to function as endowment funds (i.e., quasi-endowment funds) in support of operations of future years and to offset potential market declines. The amount computed under the endowment spending policy of the investment pool (note 1) and all investment income earned by investing cash in excess of daily requirements are used to support current operations and such amount is reported as a component of the change in net assets from operations. The balance of investment return, consisting of the excess of investment return on endowment and quasi-endowment funds over the spending rate, is reported in other changes in net assets.

(o) *Income Taxes*

The University is exempt from income taxes on its activities as a University under Section 501(c)(3) of the Internal Revenue Code and similar state statutes. Activities unrelated to those of a University are subject to tax at corporate rates.

UNIVERSITY OF THE PACIFIC

Notes to Consolidated Financial Statements

June 30, 2002

(With comparative 2001 financial information)

(p) Comparative Totals

The statement of activities includes certain prior-year summarized information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation 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 year ended June 30, 2001 from which the summarized information was derived.

(q) Restatements and Reclassifications

The 2001 financial statements have been restated in order to reflect \$2.7 million of contributions receivable as of June 30, 2001 which were not previously reported. Certain reclassifications have been made to the 2001 financial statements and summarized information to conform to the 2002 presentation.

(2) Receivables

(a) Accounts Receivable

Accounts receivable as of June 30, 2002 and 2001 are without collateral and consist of (in thousands):

	2002	2001
Student accounts	\$ 2,372	3,794
Dental clinic	3,879	3,854
Government contracts and other	8,179	6,424
Total	14,430	14,072
Less allowance for doubtful accounts	(1,544)	(1,575)
Accounts receivable, net	\$ 12,886	12,497

(b) Student Loans Receivable

Student loans receivable as of June 30, 2002 and 2001 are without collateral and consist of (in thousands):

	2002	2001
Federal government programs	\$ 25,854	24,292
Institutional programs	1,102	990
	26,956	25,282
Less allowance for doubtful loans	(873)	(873)
Student loans receivable, net	\$ 26,083	24,409

UNIVERSITY OF THE PACIFIC

Notes to Consolidated Financial Statements

June 30, 2002

(With comparative 2001 financial information)

(c) Pledges Receivable

Pledges receivable as of June 30, 2002 and 2001 are without collateral and consist of (in thousands):

	2002	2001
Pledges to be collected:		
In one year or less	\$ 6,164	5,564
Between one year and five years	11,763	14,443
In more than five years	891	835
Total pledges	18,818	20,842
Less allowance for nonfulfillment	(783)	(874)
Less discount to present value at 3.22% to 4.64%	(1,012)	(1,715)
	\$ 17,023	18,253

The pledges receivable as of June 30, 2002 and 2001 will, when collected, have the following restrictions (in thousands):

	2002	2001
Endowment with earnings expendable for departmental programs and activities	\$ 5,571	3,743
Endowments with earnings expendable for scholarships	330	500
Building construction	7,852	11,300
Departmental programs and activities	3,270	2,710
Pledges receivable, net	\$ 17,023	18,253

(3) Investments

Investments as of June 30, 2002 and 2001 consist of (in thousands):

	2002	2001
Treasury mutual funds and other short-term investments	\$ 15,852	27,842
Long-term government and corporate bonds	89,625	67,359
Corporate stocks and mutual funds	85,148	84,100
Assets held by other trustees	1,513	1,513
Real and personal properties	10,415	11,467
Total	\$ 202,553	192,281

UNIVERSITY OF THE PACIFIC

Notes to Consolidated Financial Statements

June 30, 2002

(With comparative 2001 financial information)

Investments include \$15,254,055 and \$15,437,000 held under split-interest trust agreements as of June 30, 2002 and 2001, respectively. Bond proceeds included in investments and restricted for construction were \$31,416,000 and \$15,938,000 as of June 30, 2002 and 2001, respectively.

The following summarizes the investment return during the year ended June 30, 2002 and its classification in the statement of activities (in thousands):

	<u>Total</u>	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>
Dividends and interest	\$ 6,055	5,738	340	(23)
Realized and unrealized loss on investments accounted for at fair value	<u>(7,335)</u>	<u>(7,335)</u>	<u>—</u>	<u>—</u>
Total investment return, net	<u>\$ (1,280)</u>	<u>(1,597)</u>	<u>340</u>	<u>(23)</u>
Investment return distributed	\$ 9,006	8,689	340	(23)
Investment loss, net of distributions	<u>(10,286)</u>	<u>(10,286)</u>	<u>—</u>	<u>—</u>
Total investment return, net	<u>\$ (1,280)</u>	<u>(1,597)</u>	<u>340</u>	<u>(23)</u>

UNIVERSITY OF THE PACIFIC

Notes to Consolidated Financial Statements

June 30, 2002

(With comparative 2001 financial information)

The following summarizes the investment return during the year ended June 30, 2001 and its classification in the statement of activities (in thousands):

	<u>Total</u>	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>
Dividends and interest	\$ 7,824	7,375	248	201
Realized and unrealized gain on investments accounted for at fair value	<u>93</u>	<u>93</u>	<u>—</u>	<u>—</u>
Total investment return, net	<u>\$ 7,917</u>	<u>7,468</u>	<u>248</u>	<u>201</u>
Investment return distributed	\$ 10,330	9,881	248	201
Investment loss, net of distributions	<u>(2,413)</u>	<u>(2,413)</u>	<u>—</u>	<u>—</u>
Total investment return, net	<u>\$ 7,917</u>	<u>7,468</u>	<u>248</u>	<u>201</u>

Pooled Funds

Endowment and similar funds assets are generally pooled on a unit-market-value basis. Funds are added to or withdrawn from the pool at the unit-market value at the beginning of the six-month period after which the transaction takes place. Pooled funds as of June 30, 2002 and 2001 consisted of:

	<u>2002</u>	<u>2001</u>
Investments in pooled funds, at market value	\$ 112,195,000	118,520,000
Total number of units	70,502	68,697
Market value per unit	\$ 1,591	1,725
Average annual investment earnings per unit, inclusive of net realized and unrealized gains	77	103

Professional fees for management of the pooled investments are recorded against investment returns and amounted to approximately \$366,000 and \$369,000 for the years ended June 30, 2002 and 2001, respectively.

UNIVERSITY OF THE PACIFIC

Notes to Consolidated Financial Statements

June 30, 2002

(With comparative 2001 financial information)

(4) Fixed Assets

Fixed assets as of June 30, 2002 and 2001 consist of (in thousands):

	2002	2001
Land	\$ 6,998	6,998
Buildings	164,105	145,438
Equipment	33,605	60,885
Library books and collections	19,962	18,309
Construction in progress	21,020	20,529
Leasehold improvements	1,331	—
	247,021	252,159
Less accumulated depreciation	(100,290)	(123,075)
	\$ 146,731	129,084

(5) Notes and Bonds Payable

Notes and bonds payable as of June 30, 2002 and 2001 consist of (in thousands):

	2002	2001
Bonds payable:		
California Educational Facilities Authority (CEFA) Project Revenue Bonds:		
Series 1997A, 4.350-5.450%, due in 2013	\$ 7,140	7,820
Series 1998, 3.650-5.000%, due 2018 to 2023	11,910	12,115
Series 2000, 5.750-5.875%, due 2020 to 2030	41,000	41,000
Series 2002, 2.200-5.375%, due 2003 to 2032	24,500	—
	84,550	60,935
Less net unamortized discount on bonds	(30)	(328)
Total bonds payable	84,520	60,607
Notes payable	1,048	291
	\$ 85,568	60,898

UNIVERSITY OF THE PACIFIC

Notes to Consolidated Financial Statements

June 30, 2002

(With comparative 2001 financial information)

Scheduled maturities of bonds and notes payable are (in thousands):

	Bonds	Notes	Total
Year ending June 30:			
2003	\$ 1,260	100	1,360
2004	1,315	99	1,414
2005	1,370	103	1,473
2006	1,425	72	1,497
2007	1,330	70	1,400
Thereafter	77,850	604	78,454
	\$ 84,550	1,048	85,598
Less net unamortized discount			(30)
			\$ 85,568

The University has a \$4,000,000 line of credit with a bank due on demand or in June 2003. Such line of credit is without collateral. The interest rate is at prime (4.75% as of June 30, 2002) plus 0.25%. There were no borrowings under the line of credit as of June 30, 2002.

California Educational Facilities Authority (CEFA) Project Revenue Bonds

In May 2002, the University issued CEFA Revenue Bonds, Series 2002 amounting to \$24,500,000. Such bonds are payable in varying annual installments through 2032 with interest paid semiannually at rates ranging from 2.200% – 5.375%. Net proceeds of \$24,375,000 will be utilized for various construction projects.

In June 2000, the University issued CEFA Revenue Bonds, Series 2000 amounting to \$41,000,000. Such bonds are payable in varying annual installments through 2030 with interest paid semiannually at rates ranging from 5.750% – 5.875%. Net proceeds of \$14,723,000 were placed in an irrevocable trust for the sole purpose of funding payments of principal and interest on the Series 1993 B Bonds.

In June 1998, the University issued CEFA Revenue Bonds, Series 1998 amounting to \$12,500,000. Such bonds are payable in varying annual installments through 2023, with interest paid semiannually at rates ranging from 3.65% to 5.00%. The net proceeds, after deducting issuance costs, amounted to approximately \$11,926,000.

In April 1997, the University participated in the issuance of CEFA Revenue Bonds, 1997 Series A and B. The University's portion of the bonds amounted to \$9,570,000 of Series A bonds. Upon issuance of the CEFA 1997 Series A bonds, the net proceeds were used to purchase U.S. government securities, which securities were placed into an irrevocable trust for the sole purpose of funding payments of principal and interest on the University's CEFA Series 1986 and 1987 bonds.

UNIVERSITY OF THE PACIFIC

Notes to Consolidated Financial Statements

June 30, 2002

(With comparative 2001 financial information)

The University must maintain a ratio of available assets (as defined in the Indentures) to general liabilities (as defined in the Indentures) of at least 2:0 under the Series 1997A and 1998 bonds. The applicable agreements place certain other restrictions on the University, including cash reserve requirements for sinking funds. In the opinion of management, the University complied with the applicable requirements for the year ended June 30, 2002.

The University has pledged as collateral a portion of its gross revenues equal to the annual payments on its CEFA bonds as they become due. Obligations under the 1997 Series A (Series B and A) loan agreements are several with other Series B and A borrowers, and no Series B and A borrower will be responsible for the default of another Series B and A borrower except to the extent of amounts in a borrower's Bond Reserve Fund (approximately \$476,000 for the University as of June 30, 2002). The University is not aware of any default by any Series B and A borrower.

(6) Retirement Benefits

Defined contribution retirement benefits are provided for University employees principally through the Teachers Insurance and Annuity Association (TIAA-CREF), a national organization used to fund retirement benefits for educational institutions. Under this arrangement, the University and plan participants make monthly contributions to TIAA-CREF to fund retirement benefits. The University's share of the cost of these benefits for the years ended June 30, 2002 and 2001 was approximately \$4,741,000 and \$4,462,000, respectively.

(7) Contingencies

The University is involved in various items of litigation, most of which involve employment matters. Management believes each of these matters has meritorious defenses and intends to defend these cases vigorously and believes the ultimate liability, if any, will not be material to the financial position of the University.

The University receives funding or reimbursement from governmental agencies for various activities which are subject to numerous laws and regulations of federal, state, and local governments. Compliance with these laws and regulations can be subject to government review and interpretation, as well as regulatory actions. Recently, government activity has increased with respect to investigations and allegations concerning possible violations by university healthcare providers of regulations which could result in the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. The University is subject to such regulatory reviews and, while these reviews may result in repayments and/or civil remedies, management believes based on its current knowledge and information, that such repayments and/or civil remedies would not have a material effect on the University's financial position.

UNIVERSITY OF THE PACIFIC

Notes to Consolidated Financial Statements

June 30, 2002

(With comparative 2001 financial information)

(8) Fair Value of Financial Instruments

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

(a) Cash and Cash Equivalents

The carrying amount approximates fair value, based on the short maturity of those instruments.

(b) Loans Receivable

The fair value of student loans receivable approximates their carrying value, based on current comparable loan rates.

(c) Investments

The fair value of investments is estimated based on quoted market prices for those investments that are invested in actively traded securities. For other investments for which there are no quoted market prices, an estimate of the amount that could be realized in a sale was made by management. As of June 30, 2002, management believes the fair value of all investments for which there are no quoted market prices approximates the carrying value.

(d) Notes and Bonds Payable

The fair value of the University's long-term debt is estimated based on the current rates available to the University for debt of the same remaining maturities. As of June 30, 2002, the fair value of the University's notes and bonds approximates \$87,816,000.

(9) Leases

The University is obligated under various capital leases for equipment that expire at various dates during the next five years. As of June 30, 2002 and 2001, the gross amount of equipment recorded under capital leases was as follows:

	<u>2002</u>	<u>2001</u>
Equipment	\$ 3,068	2,295
Less accumulated depreciation	<u>(1,605)</u>	<u>(777)</u>
	<u>\$ 1,463</u>	<u>1,518</u>

UNIVERSITY OF THE PACIFIC

Notes to Consolidated Financial Statements

June 30, 2002

(With comparative 2001 financial information)

Future minimum capital lease payments as of June 30, 2002 are as follows:

	Capital leases
Fiscal year ending June 30:	
2003	\$ 733
2004	503
2005	183
2006	182
Total minimum lease payments	1,601
Less amounts representing interest	(138)
Present value of net minimum capital lease payments	\$ 1,463

(10) Composition of Net Assets

The composition of the categories of net asset as of June 30, 2002 and 2001 consists of (in thousands):

	2002	2001
Unrestricted net assets:		
Undesignated net assets	\$ 4,579	1,978
Designated for specific purposes	53,731	51,010
Quasi-endowment and accumulated gains on permanent endowments whose income is unrestricted	42,827	45,859
Investment in fixed assets, net of long-term debt	62,211	68,477
	163,348	167,324
Temporarily restricted net assets:		
Amounts restricted by donors for specific purposes	19,016	15,773
Pledges receivable for specific purposes	11,122	14,010
	30,138	29,783
Permanently restricted net assets:		
Permanent endowment and similar funds	85,532	81,701
Pledges for permanent endowment	5,901	4,526
	91,433	86,227
	\$ 284,919	283,334

UNIVERSITY OF THE PACIFIC

Notes to Consolidated Financial Statements

June 30, 2002

(With comparative 2001 financial information)

(11) Expenses by Function

Expenses by functional classification after allocating operations and maintenance of plant, depreciation expense, and interest expense are as follows for the years ended June 30, 2002 and 2001:

	<u>2002</u>	<u>2001</u>
Instruction and departmental research	\$ 101,438	93,842
Auxiliary enterprises	20,183	18,121
Sponsored programs	12,452	10,066
Academic support	8,506	8,433
Student services	12,548	11,224
Student aid	2,362	1,852
General administration	6,271	5,661
Fundraising activities	6,855	5,897
Expenses by function	<u>\$ 170,615</u>	<u>155,096</u>

(12) Related Party Transactions

Included in revenues for the years ended June 30, 2002 and 2001, are contributions from board of regents members totaling \$1,487,000 and \$566,000, respectively.