



CORNELL UNIVERSITY

OMB Circular A-133 Audit Reports

June 30, 2004

(With Independent Auditors' Report Thereon)

CORNELL UNIVERSITY

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KPMG LLP
265 Clinton Square
Rochester, NY 14604

Independent Auditors' Report on Financial Statements and Supplementary Schedule of Expenditures of Federal Awards

The Board of Trustees
Cornell University:

We have audited the accompanying statement of financial position of Cornell University as of June 30, 2004, 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 2003 financial statements and, in our report dated September 9, 2003, 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the 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, 2004, 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 7, 2004, on our consideration of Cornell University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance, and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.



Our audit was performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

KPMG LLP

September 7, 2004
Rochester, New York

STATEMENT OF FINANCIAL POSITION AS OF JUNE 30, 2004 (IN THOUSANDS)
(WITH COMPARATIVE INFORMATION FOR THE YEAR ENDED JUNE 30, 2003)

	General Operations	Physical Capital	Financial Capital	2004 Total	2003 Total
Assets					
1 Cash and cash equivalents (note 2)	\$ 4,501	\$ 22,164	\$ 33,090	\$ 59,755	\$ 99,858
2 Collateral for securities loaned (note 2B)			235,681	235,681	205,238
3 Investments (note 2)	600,806	129,961	3,419,982	4,150,749	3,622,966
4 Accounts receivable, net (note 3)					
5 Government	54,772			54,772	45,295
6 Patient	57,276			57,276	57,065
7 Contributions	195,327	88,530	75,879	359,736	382,070
8 Other	128,629	5,202	1,430	135,261	85,674
9 Inventories and deferred charges	35,203	6,293		41,496	38,859
10 Student loans receivable (note 3C)	49,423		17,482	66,905	69,750
11 Land, buildings, and equipment, net (note 5)		1,728,844		1,728,844	1,583,491
12 Funds held in trust by others (note 1D)			100,384	100,384	93,818
13 Total assets	<u>\$ 1,125,937</u>	<u>\$ 1,980,994</u>	<u>\$ 3,883,928</u>	<u>\$ 6,990,859</u>	<u>\$ 6,284,084</u>
Liabilities					
14 Accounts payable and accrued expenses	\$ 208,145	\$ 16,697		\$ 224,842	\$ 190,259
15 Securities loan agreements payable (note 2B)			\$ 235,681	235,681	205,238
16 Deposits and deferred revenues	62,612	1,262		63,874	58,740
17 Deferred benefits (note 7)	116,539		47,102	163,641	154,885
18 Funds held in trust for others (note 1E)			86,540	86,540	62,107
19 Living trust obligations (note 1C)			86,327	86,327	71,692
20 Bonds, mortgages, & notes payable (note 6)	16,018	589,937		605,955	494,748
21 Refundable government grants	43,577			43,577	43,477
22 Total liabilities	<u>446,891</u>	<u>607,896</u>	<u>455,650</u>	<u>1,510,437</u>	<u>1,281,146</u>
Net Assets (note 1B)					
23 Unrestricted					
24 Available for operations	336,713			336,713	319,705
25 Designated for student loans	3,734			3,734	5,091
26 Designated for plant		188,251		188,251	155,659
27 Net investment in plant		1,013,003		1,013,003	956,311
28 Appreciation on true endowments			1,044,965	1,044,965	874,127
29 Funds functioning as endowments			848,341	848,341	736,099
30 Temporarily restricted					
31 Available for operations	338,599			338,599	349,296
32 Designated for plant		171,844		171,844	186,954
33 Funds functioning as endowments			96,506	96,506	81,323
34 Funds subject to living trust agreements			47,962	47,962	51,916
35 Funds held in trust			39,556	39,556	35,681
36 Permanently restricted					
37 Student loan funds			30,639	30,639	29,995
38 True endowments			1,177,340	1,177,340	1,077,313
39 Funds subject to living trust agreements			35,449	35,449	33,370
40 Funds held in trust			107,520	107,520	110,098
41 Total net assets	<u>679,046</u>	<u>1,373,098</u>	<u>3,428,278</u>	<u>5,480,422</u>	<u>5,002,938</u>
42 Total liabilities and net assets	<u>\$ 1,125,937</u>	<u>\$ 1,980,994</u>	<u>\$ 3,883,928</u>	<u>\$ 6,990,859</u>	<u>\$ 6,284,084</u>

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

STATEMENT OF ACTIVITIES FOR THE YEAR ENDED JUNE 30, 2004 (IN THOUSANDS)

(WITH SUMMARIZED INFORMATION FOR THE YEAR ENDED JUNE 30, 2003)

	General Operations		Physical Capital	
	Unrestricted	Temporarily Restricted	Unrestricted	Temporarily Restricted
Revenues and other additions				
1 Tuition and fees	\$ 532,645			
2 Scholarship allowance	(158,187)			
3 Net tuition and fees	374,458			
4 State appropriations	140,127		\$ 10,487	
5 Federal appropriations	17,048			
6 Federal grants and contracts	409,514			
7 State and local grants and contracts	24,373			
8 Private grants and contracts	21,398			
9 Contributions	83,926	\$ 65,198	14,680	\$ 26,313
10 Interest and dividends	38,217	3,245	808	732
11 Net realized gain (loss) on investments	25,919	2		
12 Net unrealized gain on investments	42,141	347	13,300	
13 Medical Physicians' Organization	341,289			
14 Enterprises and subsidiaries	149,251			
15 Educational departments	60,694		6	
16 Other sources	61,488	2,341	(93)	1,255
17 Total revenues	1,789,843	71,133	39,188	28,300
18 Investment payout	110,793	26,953	46	
19 Net assets released from restrictions	79,698	(79,698)	1,782	(1,782)
20 Capital investments (withdrawals)	(77,971)	(29,085)	194,016	(41,628)
21 Total revenues and other additions	1,902,363	(10,697)	235,032	(15,110)
Expenses (Note 8)				
22 Salaries and wages	1,024,843			
23 Employee benefits	237,238			
24 Purchased services	138,977			
25 Supplies and general	365,273			
26 Utilities, rents, and taxes	99,134			
27 Interest expense	21,247			
28 Depreciation			136,414	
29 Other			9,334	
30 Total expenses	1,886,712		145,748	
31 Change in net assets	15,651	(10,697)	89,284	(15,110)
32 Total net assets, beginning of year	324,796	349,296	1,111,970	186,954
33 Total net assets, end of year	\$ 340,447	\$ 338,599	\$1,201,254	\$ 171,844

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

Financial Capital			2004	2003
Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Total
			\$ 532,645	\$ 493,217
			(158,187)	(144,017)
			374,458	349,200
			150,614	158,708
			17,048	18,770
			409,514	397,244
			24,373	23,979
			21,398	35,672
\$ 61,137	\$ 17,426	\$ 81,387	350,067	222,606
21,144	21,816	906	86,868	91,155
145,722	10,129	3,808	185,580	(84,713)
221,050	2,092	829	279,759	126,059
			341,289	306,469
			149,251	143,358
			60,700	60,553
374	(6,249)	(91)	59,025	54,295
449,427	45,214	86,839	2,509,944	1,903,355
(110,839)	(26,953)			
(55,508)	(3,157)	13,333		
283,080	15,104	100,172	2,509,944	1,903,355
			1,024,843	973,240
			237,238	217,535
			138,977	129,258
			365,273	335,959
			99,134	94,154
			21,247	21,999
			136,414	123,261
			9,334	5,236
			2,032,460	1,900,642
283,080	15,104	100,172	477,484	2,713
1,610,226	168,920	1,250,776	5,002,938	5,000,225
\$1,893,306	\$ 184,024	\$1,350,948	\$5,480,422	\$5,002,938

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED JUNE 30, 2004 (IN THOUSANDS)
(WITH COMPARATIVE INFORMATION FOR THE YEAR ENDED JUNE 30, 2003)

	2004	2003
Cash flows from operating activities		
1 Increase in net assets	\$ 477,484	\$ 2,713
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Nonoperating items		
2 Contributions for physical and financial capital	(192,253)	(90,228)
3 Net realized (gains)/losses on physical and financial capital investments	(159,659)	84,713
4 Income restricted for financial capital	(815)	(13,067)
Noncash items		
5 Depreciation	136,414	123,261
6 Net unrealized (gains)/losses on investments	(279,759)	(126,059)
7 Loss on equipment disposals	6,228	2,628
8 Provision for receivable allowances	26,267	1,213
9 Accretion of bond discount	939	973
10 Other noncash items	(2,810)	1,705
Change in assets and liabilities		
11 Accounts receivable	(61,893)	85,750
12 Inventories and deferred charges	163	(3,113)
13 Accounts payable and accrued expenses	34,583	30,879
14 Deposits and deferred revenues	5,134	22,774
15 Deferred benefits	8,756	24,911
16 Refundable government grants	100	(41)
17 Net cash provided/(used) by operating activities	<u>(1,121)</u>	<u>149,012</u>
Cash flows from investing activities		
18 Proceeds from the sale and maturities of investments	2,823,346	2,929,806
19 Purchase of investments	(2,911,711)	(2,961,662)
20 Acquisition of land, buildings, and equipment (net)	(273,621)	(194,555)
21 Student loans granted	(13,777)	(13,888)
22 Student loans repaid	15,317	15,608
23 Change in funds held in trust for others	24,433	(12,058)
24 Net cash used by investing activities	<u>(336,013)</u>	<u>(236,749)</u>
Cash flows from financing activities		
Resources for long-term purposes		
Contributions restricted to		
25 Investment in true endowment	76,925	37,642
26 Investment in physical capital	18,268	8,894
27 Investment subject to living trust agreements	8,674	4,097
28 Income restricted for financial capital	815	13,067
29 Contributions designated for funds functioning as endowments	74,012	37,239
Other financing activities		
30 Principal payments of bonds, mortgages, and notes payable	(26,851)	(25,146)
31 Proceeds from issuance of bonds, mortgages, and notes payable	137,119	274
32 Change in obligations under living trust agreements	8,069	4,106
33 Net cash provided by financing activities	<u>297,031</u>	<u>80,173</u>
34 Net change in cash and cash equivalents	(40,103)	(7,564)
35 Cash and cash equivalents, beginning of year	99,858	107,422
36 Cash and cash equivalents, end of year	<u>\$ 59,755</u>	<u>\$ 99,858</u>

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

NOTES TO
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, eight 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 stan-

dards 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, 2004 and June 30, 2003.

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, 2004, the university's true endowment net assets consisted of approximately 16 percent for unrestricted purposes, 25 percent for student aid, 40 percent for instruction, and 19 percent for other donor-specified purposes. On June 30, 2003, the breakdown was 15 percent for unrestricted purposes, 24 percent for student aid, 41 percent for instruction, and 20 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*. The discount rates for the fiscal years 2003-04 and 2002-03 were 5.75% and 7.00%, respectively.

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

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

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
1 Net assets at June 30, 2002	\$ 3,080,831	\$ 731,183	\$ 1,188,211	\$ 5,000,225
2003 change in net assets:				
2 General operations	27,536	(12,287)		15,249
3 Physical capital	22,909	(30,598)		(7,689)
4 Financial capital	(84,284)	16,872	62,565	(4,847)
5 Total change in net assets	(33,839)	(26,013)	62,565	2,713
6 Net assets at June 30, 2003	3,046,992	705,170	1,250,776	5,002,938
2004 change in net assets:				
7 General operations	15,651	(10,697)		4,954
8 Physical capital	89,284	(15,110)		74,174
9 Financial capital	283,080	15,104	100,172	398,356
10 Total change in net assets	388,015	(10,703)	100,172	477,484
11 Net assets at June 30, 2004	<u>\$ 3,435,007</u>	<u>\$ 694,467</u>	<u>\$ 1,350,948</u>	<u>\$ 5,480,422</u>

TABLE 2. COMPOSITION OF FINANCIAL CAPITAL NET ASSETS AT JUNE 30, 2004 (IN THOUSANDS)
(WITH SUMMARIZED COMPARATIVE FINANCIAL INFORMATION AS OF JUNE 30, 2003)

	Net Asset Classification			2004	2003
	Unrestricted	Temporarily Restricted	Permanently Restricted		
1 True endowment and unspent earnings, including contributions receivable of \$75,878.	\$ 1,044,965		\$ 1,177,340	\$ 2,222,305	\$ 1,951,440
2 Functioning as endowment	848,341	\$ 96,506		944,847	817,422
3 Funds held in trust		39,556	107,520	147,076	145,779
4 Total university endowment	1,893,306	136,062	1,284,860	3,314,228	2,914,641
5 Living trust funds		47,962	35,449	83,411	85,286
6 Loan funds			30,639	30,639	29,995
7 Total	<u>\$ 1,893,306</u>	<u>\$ 184,024</u>	<u>\$ 1,350,948</u>	<u>\$ 3,428,278</u>	<u>\$ 3,029,922</u>

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 2003-04 and 2002-03 were \$2,332,678 and \$276,396, 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 \$79,987,568, and \$72,862,624 at June 30, 2004 and June 30, 2003, 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 \$46,691,861 and \$51,960,992 at June 30, 2004 and June 30, 2003, 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.

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 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, 2003 from which the summarized information was derived.

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

	2004	2003
1 Cash and cash equivalent holdings	\$ 267,277	\$ (22,912)
Equity securities		
2 Domestic	1,149,743	1,306,519
3 International	575,734	274,975
Debt securities		
4 Domestic - government	338,149	614,328
5 Domestic - corporate debt securities	197,252	275,032
6 International - governments	66,700	55,195
7 International - corporate	26,482	29,775
8 Mortgages and other asset-backed securities	30,751	78,540
Other investments		
9 Limited partnerships	1,458,963	951,058
10 Real estate	6,189	27,217
11 Other	33,509	33,239
12 Total investments	<u>\$ 4,150,749</u>	<u>\$ 3,622,966</u>

K. Reclassifications

In previous years certain prior-year amounts were reclassified to conform to the current-year's presentation. However, for fiscal year 2003-04, no reclassifications were required.

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 non-marketable 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 2003-04 and 2002-03 for investing the university's portfolios amounted to approximately \$7,000,000 and \$5,900,000, respectively. The composition of investments at June 30, 2004 and June 30, 2003 are shown in Table 3A.

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 \$228,609,221 and \$199,323,136 at June 30, 2004 and June 30, 2003, 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 \$235,681,598 and \$205,238,322 and an offsetting liability for the return of the collateral in Financial Capital on the *Statement of Financial Position* at June 30, 2004 and June 30, 2003, 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 Long Term Investment Pool (LTIP) 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 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 3B. INVESTMENT POOLS/CATEGORIES AT FAIR VALUE (IN THOUSANDS)

	2004	2003
1 Working capital	\$ 8,159	\$ 11,827
2 Intermediate-term (resources for spending in less than 3 years)	646,936	508,790
3 Long-term investment pool (resources held for 3 years or longer)	3,070,235	2,720,790
4 Separately invested securities	333,282	317,349
5 Life income fund pools	20,633	20,900
6 DASNY holdings	66,934	39,923
7 Other purposes of investment	4,570	3,387
8 Total investments	<u>\$ 4,150,749</u>	<u>\$ 3,622,966</u>

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, 2004 and June 30, 2003, the market prices per unit were \$46.51 and \$42.65, respectively. The total return on the university's long-term investments, of which the LTIP is a component, was 16.1 percent for fiscal year 2003-04.

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. 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, 2004, distributions for investment payout were \$157,090,152 (\$2.43 per unit), of which \$137,791,523 supported general operations and physical capital. The remaining distribution of \$19,298,629 was returned to principal, or went to funds held in trust for

others, shown in the accompanying *Statement of Financial Position*. The distribution for 2004 was comprised of \$42,749,256 in net investment income and \$114,340,896 paid from accumulated gains. For the fiscal year ended June 30, 2003, the investment payout was \$167,553,378 (\$2.70 per unit). The distribution for 2003 was comprised of \$35,634,933 in net investment income and \$131,918,445 paid from prior year accumulated gains.

At June 30, 2004, 1,128 of 4,832 true endowment funds invested in the LTIP had market values below book values by \$20,325,748, on a total book value of \$310,549,366 for those funds. 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.

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	\$ 3,070,235	\$ 2,612,901	\$ 457,334	\$ 46.51	66,016,562
2 Beginning of year	\$ 2,720,790	\$ 2,502,861	<u>\$ 217,929</u>	\$ 42.65	63,791,217
3 Unrealized net gain for year			<u>\$ 239,405</u>		
4 Realized net gain/(loss) for year			<u>\$ 137,455</u>		
5 Net gain/(loss) for year			<u>\$ 376,860</u>		

D. Other Investments

Under the terms of certain limited partnership agreements, the university is obligated to advance additional funding for private-equity and real estate investments periodically. At June 30, 2004 and June 30, 2003, the university had commitments of approximately \$567,006,000 and \$335,806,000, 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 has approved the use of derivatives by outside investment managers, based on investment guidelines negotiated at the time the manager was appointed. The derivatives in the investment portfolio at June 30, 2004 are used for three purposes: to adjust fixed income duration and rates, to create "synthetic exposures" to certain types of investments, and to hedge foreign currency fluctuations.

Derivatives are used as fixed income substitutes when the investment manager determines that using a derivative contract provides the least expensive, and therefore potentially more profitable way of "exposing" the portfolio to opportunities for increased returns, rather than buying underlying securities directly. These transactions typically involve buying futures or swap contracts on U.S. Treasury securities or on foreign government securities. Commodity investments are used by the university to diversify the investment portfolio and as a general hedge against an inflationary economic environment that might reduce the value of the traditional stock and bond holdings in the portfolio. The most efficient means of creating these investments is through derivative contracts that rise or fall in price in direct correlation to the value of an underlying commodity index. In addition, derivative instruments are used to adjust the foreign currency exposure of the investment portfolio for securities whose prices are denominated in foreign currencies.

The university's investment guidelines require that the investment managers only use counterparties with very strong credit ratings for these derivatives. The notional amount of the exposures at June 30, 2004 was approximately

\$554,756,000, with the largest portion, \$499,344,000, going to the creation of synthetic exposures in fixed income substitutes and commodities. The notional amount of the exposures as of June 30, 2003 was approximately \$38,535,000. As a result of this activity, the university has recorded unrealized losses of \$696,300 and unrealized gains of \$61,897 for fiscal years 2003-04 and 2002-03, respectively.

3. ACCOUNTS AND LOANS RECEIVABLE

A. Patient Accounts and Other

Patient accounts receivable at June 30, 2004 and June 30, 2003, are net of provisions for allowances and doubtful accounts of \$78,059,422 and \$58,866,618, respectively. Other accounts receivable, including student accounts, at June 30, 2004 and June 30, 2003 are net of allowances for doubtful accounts of \$1,975,833 and \$1,701,680, 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 \$359,736,000 and \$382,070,000, representing the present value of future cash flows, are recorded as receivables at June 30, 2004 and June 30, 2003, respectively. The corresponding revenue is assigned to the appropriate net asset category in the year the promise is received. The face value, discount, and allowance for contributions receivable are shown in Table 5. Conditional promises are recorded when donor stipulations are substantially met. At June 30, 2004 and 2003, conditional promises and donor intentions not reflected in the financial statements were approximately \$98,815,000 and \$114,060,000, respectively. Expenses related to fund-raising activities amounted to approximately \$25,570,000 and \$24,667,000 for fiscal years 2003-04 and 2002-03, respectively.

TABLE 5. CONTRIBUTIONS RECEIVABLE (IN THOUSANDS)

	2004	2003
Contributions expected to be realized		
1 In one year or less	\$ 98,062	\$ 92,735
2 Between one year and five years	291,774	288,196
3 More than five years	72,793	138,335
4 Gross contributions receivable	462,629	519,266
5 Discount	(83,960)	(117,087)
6 Allowance	(18,933)	(20,109)
7 Total discount and allowance	(102,893)	(137,196)
8 Net contributions receivable	\$ 359,736	\$ 382,070

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

	Book value at June 30, 2003	Additions	Disposals and Closed Projects	Book value at June 30, 2004
1 Land, buildings, and improvements	\$ 1,797,141	\$ 160,461	\$ 4,820	\$ 1,952,782
2 Furniture, equipment, books, and collections	887,873	82,475	210,227	760,121
3 Construction in progress	152,712	165,474	120,415	197,771
4 Total before accumulated depreciation	2,837,726	<u>\$ 408,410</u>	<u>\$ 335,462</u>	2,910,674
5 Accumulated depreciation	<u>(1,254,235)</u>			<u>(1,181,830)</u>
6 Land, buildings and equipment, net	<u>\$ 1,583,491</u>			<u>\$ 1,728,844</u>

C. Student Loans

Student loans receivable at June 30, 2004 and June 30, 2003, are reported net of allowances for doubtful loans of \$9,553,578 and \$8,439,983, 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: \$10,104,930 and \$10,138,715 at June 30, 2004 and June 30, 2003, respectively, of financial capital; and \$389,793, and \$389,541, 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 \$124,950 and \$106,281 at June 30, 2004 and June 30, 2003, respectively.

Physical capital assets include cash and United States government obligations of \$32,670,096, and \$36,682,363 at June 30, 2004 and June 30, 2003, respectively. These assets are held by DASNY to be used primarily for the retirement of debt at a future time. In addition, \$30,999,585 and \$14,586 of bond proceeds were on deposit for future project expenditures at June 30, 2004 and 2003, respectively.

Assets in general operations for student loans include \$3,264,783 and \$3,225,883 at June 30, 2004 and June 30, 2003, respectively, on deposit with DASNY that are available for the retirement of debt at a future time.

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 \$14,374,000 and \$2,356,000 for fiscal years 2003-04 and 2002-03, 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 \$317,198,000 and \$317,759,000 at June 30, 2004 and June 30, 2003, 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 \$24,299,000 and \$23,417,000 at June 30, 2004 and June 30, 2003, respectively.

Effective July 1, 2003, the university changed the capitalization threshold for moveable and fixed equipment from \$1,500 (\$500 for computers and related equipment) to \$5,000. As a result of that change, during fiscal year 2003-04, the remaining depreciation of approximately \$19,178,000 for the items under the capital threshold has been included in the Statement of Activities.

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, 2004 and June 30, 2003, 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 2003-04 and 2002-03 was approximately \$20,308,000 and \$21,027,000, 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 \$614,952,000 and \$509,817,000 at June 30, 2004 and June 30, 2003, 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, 2004, 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 \$81,300,000 (expiring July 1, 2030); 2.99 percent on a notional amount of \$83,055,000 (expiring October 1, 2004); 4.52 percent on a notional amount of \$42,905,000 (expiring July 1, 2030); and 4.33 percent on a notional amount of \$15,390,000 (expiring July 1, 2010). Net payments or receipts under the swap agreement are recorded as an adjustment to interest expense.

The university continues to issue tax-exempt 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.

In fiscal year 2003-04, the university established a program to issue \$100,000,000 of taxable commercial paper to

finance working capital, capital projects and equipment purchases for the Ithaca and Medical College campuses. As of June 30, 2004, the par amount outstanding was \$42,589,000. In addition, the university issued \$92,100,000 of auction rate bonds through DASNY. The proceeds were used to redeem approximately \$41 million of tax-exempt commercial paper outstanding and to finance approximately \$51 million of new construction projects and renovations.

In October 2003, the university entered into a capital lease for the Southtown residential building on Roosevelt Island in New York City. The present value of the 30-year obligation is estimated at \$40,140,000 and is included in the *Statement of Financial Position*. Payments under the lease are scheduled to begin October 2004. Please refer to Note 9 for additional information.

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 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 fund annually 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. No employer or employee contributions were made during fiscal years 2003-04 or 2002-03.

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

	Balance June 30, 2004	Balance June 30, 2003	Interest Rates	Maturity Date	
Plant Funds					
1	Dormitory Authority of the State of New York (DASNY)				
2	Revenue Bond Series				
3	1990B	\$ 58,700	\$ 59,000	0.40 to 1.27*	2025
4	1993	660	1,290	5.00 to 5.10	2005
5	1996	82,550	91,795	5.00 to 5.40	2014
6	2000A	63,055	64,505	2.99	2029
7	2000B	82,085	83,695	4.63	2030
8	2004	92,100	0	1.00 to 1.07*	2033
9	Bond Series 1987B	14,135	15,150	11.11	2012
10	DASNY 1993 Pooled Loan Program	1,554	1,696	1.10 to 1.20*	2012
11	Tax-Exempt Commercial Paper	21,480	68,760	0.85* to 2.99	2028
12	Taxable Commercial Paper	42,589	0	1.07 to 1.25*	-
13	Industrial Development Agency				
14	2000	7,070	7,900	4.75 to 5.25	2011
15	2002A	42,905	43,070	4.52	2030
16	2002B	15,390	15,390	4.33	2015
17	Student Loan Marketing Association	6,180	6,430	5.75 to 6.50	2019
18	Urban Development Corporation	3,125	3,250	zero	2029
19	Capitalized leases				
20	312 College Ave	12,791	13,213	various	2020
21	WMC-Southtown #2	40,140	0	5.80	2034
22	Other	3,428	431	various	2006-2028
23	Total Physical Capital	<u>589,937</u>	<u>475,575</u>		
Student Loan Funds					
24	DASNY Bond 1992 Capital Appreciation	2,963	4,083	6.70 to 6.80	2009
25	DASNY Bond 1993 Capital Appreciation	2,463	3,089	5.25 to 5.50	2007
26	DASNY Bond 1995 Serial	1,995	3,890	5.35 to 5.45	2005
27	DASNY Bond 1995 Capital Appreciation	8,597	8,111	5.70 to 6.15	2011
28	Total General Operations—Student Loans	<u>16,018</u>	<u>19,173</u>		
29	Total Bonds, Mortgages, and Notes Payable	<u>\$ 605,955</u>	<u>\$ 494,748</u>		

* Rates presented are the actual rates paid during fiscal year 2003-04. These rates are variable based on market conditions.

TABLE 8. ANNUAL DEBT SERVICE REQUIREMENTS (IN THOUSANDS)

Year	Principal	Interest	Total
1 2005	\$ 20,119	\$ 27,385	\$ 47,504
2 2006	19,573	27,558	47,131
3 2007	21,740	26,470	48,210
4 2008	21,141	25,312	46,453
5 2009	22,741	24,041	46,782
6 Thereafter	500,641	277,580	778,221
7 Total	<u>\$ 605,955</u>	<u>\$ 408,346</u>	<u>\$ 1,014,301</u>

The defined benefit plans' funded status, amounts recognized in the university's *Statement of Financial Position*, asset allocations, calculation assumptions, and anticipated benefit payments are shown in Tables 9A and 9B.

The assets are invested for the sole benefit of the plan's beneficiaries. Consistent with that objective, investments are managed to maximize total return while maintaining a prudent limitation on risk. Risk mitigation is achieved by diversifying investments across multiple asset classes, by investing in high quality securities and by permitting flexibility in the balance of investments in the permitted asset classes. The expected return on assets was derived based on long-term assumptions of inflation, real returns (which are

primarily historically based), anticipated value added by the investment managers, and expected average asset class allocations.

Total pension costs of the Endowed Ithaca and Medical College plans for the year ended June 30, 2004 and June 30, 2003 amounted to \$56,217,192 and \$51,247,423, respectively.

Employees of the contract colleges are covered under the New York State pension plans. Contributions to the state retirement system and other employee benefit costs are paid directly by the state. The amounts of the direct payments applicable to the university as revenue and expenditures are not currently determinable and are not included in the financial statements. The university reimburses the state for

TABLE 9A. DEFINED BENEFIT PENSION PLANS - BENEFIT OBLIGATIONS, PLAN ASSETS AND COST (IN THOUSANDS)

	2004			2003
	Endowed Ithaca*	Medical College	Combined	Combined
1 Accumulated benefit obligation at end of year	\$ 19,907	\$ 31,491	\$ 51,398	\$ 50,435
Change in benefit obligation				
2 Projected benefit obligation at beginning of year	\$ 21,177	\$ 36,427	\$ 57,604	\$ 50,290
3 Service cost (benefits earned during the period)		2,477	2,477	1,858
4 Interest cost on projected benefit obligation	1,160	2,279	3,439	3,420
5 Actuarial (gain)/loss	(457)	2,472	2,015	5,954
6 Benefits paid	(1,972)	(2,249)	(4,221)	(3,918)
7 Projected benefit obligation at end of year	19,908	41,406	61,314	57,604
Change in plan assets				
8 Fair value of plan assets at beginning of year	27,435	30,327	57,762	59,977
9 Actual return on plan assets	3,605	4,358	7,963	1,703
10 Benefits paid	(1,972)	(2,249)	(4,221)	(3,918)
11 Fair value of plan assets at end of year	29,068	32,436	61,504	57,762
12 Funded status	9,160	(8,970)	190	158
13 Unrecognized prior service cost				7
14 Unrecognized net actuarial loss/(gain) from past experience different than assumed	6,660	6,295	12,955	15,805
15 Net amount recognized - prepaid/(accrued) benefit cost	\$ 15,820	\$ (2,675)	\$ 13,145	\$ 15,970
Components of net periodic benefit cost				
16 Service cost (benefits earned during the period)		\$ 2,477	\$ 2,477	\$ 1,858
17 Interest cost	\$ 1,160	2,279	3,439	3,420
18 Expected return on plan assets	(2,119)	(2,184)	(4,303)	(5,082)
19 Amortization of prior service cost		7	7	108
20 Amortization of net (gain)/loss	657	548	1,205	274
21 Net periodic benefit cost /(income)	\$ (302)	\$ 3,127	\$ 2,825	\$ 578

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

TABLE 9B. DEFINED BENEFIT PENSION PLANS - BENEFIT OBLIGATIONS, PLAN ASSETS AND COST

Estimated future benefit payments from the trust (in thousands)				
	Endowed Ithaca*	Medical College	Combined	
1 2005	\$ 1,877	\$ 2,122	\$ 3,999	
2 2006	1,825	2,237	4,062	
3 2007	1,774	2,275	4,049	
4 2008	1,738	2,257	3,995	
5 2009	1,705	2,424	4,129	
6 2010-2014	7,850	16,541	24,391	
	2004		2003	
	Endowed Ithaca	Medical College	Endowed Ithaca	Medical College
Weighted-average assumptions used to determine net periodic benefit cost as of July 1				
7 Discount rate	5.75%	5.75%	7.00%	7.00%
8 Expected return on plan assets	8.00%	8.00%	9.00%	9.00%
9 Rate of compensation increase	4.00%	6.10%	4.00%	6.10%
Weighted-average assumptions used to determine benefit obligations at end of year				
10 Discount rate	6.00%	6.00%	5.75%	5.75%
11 Rate of compensation increase	4.00%	6.10%	4.00%	6.10%
Combined plan assets				
	Target Allocation	Percentage of Plan Assets at June 30		
Asset category	2005	2004	2003	
12 Equity securities	39-85%	62.1%	62.8%	
13 Debt securities	15-55%	33.1%	32.6%	
14 Real estate	1-5%	4.8%	4.6%	
15 Total		100.0%	100.0%	

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

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, 2004 and June 30, 2003, was \$12,806,510 and \$10,949,189, 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. The trusts are invested with the objective of maximizing return, subject to tolerance of reasonable risk.

Risk is reduced through the use of multiple asset classes, high-quality securities and flexible permitted asset allocation within the authorized asset classes. The expected return on assets was derived based on long-term assumptions of inflation, real returns (which are primarily historically based), anticipated value added by the investment manager, and expected average asset class allocations.

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

	2004			2003
	Endowed Ithaca	Medical College	Combined	Combined
Change in benefit obligation				
1 Benefit obligation at beginning of year	\$ 240,411	\$ 54,176	\$ 294,587	\$ 233,412
2 Service cost (benefits earned during the period)	8,397	3,694	12,091	8,716
3 Interest cost	12,548	3,068	15,616	15,512
4 Plan amendments		1,153	1,153	
5 Actuarial (gain)/loss	(36,296)	(5,367)	(41,663)	44,419
6 Benefits paid (outside of trust)	(6,065)	(1,863)	(7,928)	(7,472)
7 Benefit obligation at end of year	<u>218,995</u>	<u>54,861</u>	<u>273,856</u>	<u>294,587</u>
Change in plan assets				
8 Fair value of plan assets at beginning of year	41,975	15,762	57,737	52,594
9 Actual return on plan assets	7,006	2,858	9,864	12
10 Employer contribution	4,432	1,755	6,187	5,131
11 Fair value of plan assets at end of year	<u>53,413</u>	<u>20,375</u>	<u>73,788</u>	<u>57,737</u>
12 Funded status	(165,582)	(34,486)	(200,068)	(236,850)
13 Unrecognized net transition obligation	24,011	8,787	32,798	36,443
14 Unrecognized prior service cost		1,528	1,528	687
15 Unrecognized net actuarial loss from past experience different than assumed	74,241	15,474	89,715	142,020
16 Prepaid/(accrued) postretirement benefit cost	<u>\$ (67,330)</u>	<u>\$ (8,697)</u>	<u>\$ (76,027)</u>	<u>\$ (57,700)</u>
Components of net periodic postretirement benefit cost				
17 Service cost (benefits earned during the period)	\$ 8,397	\$ 3,694	\$ 12,091	\$ 8,716
18 Interest cost	12,548	3,068	15,616	15,512
19 Expected return on plan assets	(3,500)	(1,295)	(4,795)	(4,733)
20 Amortization of initial transition obligation	2,668	976	3,644	3,644
21 Amortization of prior service cost		313	313	184
22 Amortization of net (gain)/loss	4,432	1,141	5,573	3,867
23 Net periodic postretirement benefit cost /(income)	<u>\$ 24,545</u>	<u>\$ 7,897</u>	<u>\$ 32,442</u>	<u>\$ 27,190</u>
Participant contributions (retiree health insurance premiums)				
24 2003	\$ 1,284	\$ 112	\$ 1,396	
25 2004	1,422	120	1,542	
Estimated future benefit payments (employer paid)				
26 2005	\$ 6,927	\$ 2,183	\$ 9,110	
27 2006	7,611	2,396	10,007	
28 2007	8,323	2,616	10,939	
29 2008	9,023	2,776	11,799	
30 2009	9,637	2,952	12,589	
31 2010-2014	58,968	19,260	78,228	

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

	2004		2003	
	Endowed Ithaca	Medical College	Endowed Ithaca	Medical College
Weighted-average assumptions used to determine net periodic postretirement benefit cost as of July 1				
1 Discount rate	5.75%	5.75%	7.00%	7.00%
2 Expected return on plan assets	8.00%	8.00%	9.00%	9.00%
Weighted-average assumptions used to determine benefit obligations at end of year				
3 Discount rate	6.00%	6.00%	5.75%	5.75%
Assumed health care cost trend rates at end of year				
4 Health care cost trend rate assumed for next year	9.00%	9.00%	10.00%	10.00%
5 Ultimate trend rate	5.00%	5.00%	5.00%	5.00%
6 Years to reach ultimate trend rate	4	4	5	5

	2004		2003	
	Endowed Ithaca	Medical College	Endowed Ithaca	Medical College
Effect of 1 percentage point change in assumption of health care cost trend rate				
1-Percentage point increase				
7 Effect on total service cost and interest cost	\$ 4,823	\$ 1,313	\$ 3,875	\$ 963
8 Effect on accumulated postretirement benefit obligation as of June 30	\$ 39,178	\$ 7,620	\$ 39,268	\$ 6,952
1-Percentage point decrease				
9 Effect on total of service and interest cost	\$ (3,714)	\$ (1,087)	\$ (3,036)	\$ (781)
10 Effect on accumulated postretirement benefit obligation as of June 30	\$ (31,241)	\$ (6,615)	\$ (31,732)	\$ (5,827)

Asset category	Target Allocation	Percentage of Plan Assets at June 30	
	2005	2004	2003
1 Equity securities	39-85%	72.4%	68.0%
2 Debt securities	15-55%	27.6%	32.0%
3 Real estate	0-5%	0.0%	0.0%
4 Total		100.0%	100.0%

Tables 10A and 10B set forth the funded status and asset allocations of the plans as of June 30, 2004 and June 30, 2003, the components of net periodic postretirement benefit costs, and the assumptions used in accounting for the plans during 2004 and 2003. The accrued postretirement benefit cost shown in Table 10A is \$18,327,000 of current-year unfunded cost plus \$57,700,000 of accumulated prior-year unfunded cost.

In December 2003, the Medicare Prescription Drug Improvement and Modernization Act of 2003 (the Act) was passed. The Act introduces a prescription drug benefit under Medicare (Medicare Part D) as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit at least actuarially equivalent to Medicare Part D. Due to uncertainties in determining the impact of the Act on the accumulated postretirement obligation and net

periodic postretirement benefit cost, the consolidated financial statements do not reflect the Act's effect on the university's postretirement plans. Upon resolution of such uncertainties, the postretirement plans will recognize the effects of the Act.

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.

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 \$136,909,000 for fiscal year 2003-04, and \$132,085,000 for fiscal year 2002-03.

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 \$22,432,772 and \$18,860,379 for fiscal years 2003-04 and 2002-03, respectively, is classified as Instruction expense.

9. SUBSEQUENT EVENTS AND CONTINGENT LIABILITIES

On August 18, 2004, the university formalized its intention to purchase the Southtown residential building on Roosevelt

Island in New York City (referred to in Note 6). The purchase price is equal to the present value of the lease obligation and will be financed with tax-exempt commercial paper and gifts to the university.

On July 22, 2004, the university signed a letter of intent to purchase four floors in a second Southtown building on Roosevelt Island, yet to be constructed. The letter of intent details the plan to purchase the four floors of the building for approximately \$23 million. Construction began in August 2004, with occupancy expected in September 2006.

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 be determined currently, 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 11. FUNCTIONAL EXPENSES (IN THOUSANDS)

	General Operations	Physical Capital	2004	2003
1 Instruction	\$ 423,480	\$ 27,754	\$ 451,234	\$ 422,742
2 Research	438,687	29,130	467,817	448,060
3 Public service	100,539	3,112	103,651	100,376
4 Academic support	150,182	33,456	183,638	162,341
5 Student services	86,354	10,027	96,381	93,326
6 Medical services	350,567	3,426	353,993	333,841
7 Institutional support	178,002	14,601	192,603	169,670
8 Enterprises and subsidiaries	158,901	24,242	183,143	170,286
9 Total expenses and deductions	<u>\$ 1,886,712</u>	<u>\$ 145,748</u>	<u>\$ 2,032,460</u>	<u>\$ 1,900,642</u>

CORNELL UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2004

Federal grantor/pass-through grantor/program title	Federal CFDA number	Direct awards	Pass-through awards	Total expenditures
Research and Development:				
Department of Agriculture:				
Department of Agriculture	10.000	\$ 423,442	216,780	640,222
Agricultural Research_Basic and Applied Research	10.001	3,688,363	125,908	3,814,271
Plant and Animal Disease, Pest Control, and Animal Care	10.025	70,005	115,368	185,373
Commodity Loans and Loan Deficiency Payments	10.051	—	23,086	23,086
Forestry Incentives Program	10.064	9,312	—	9,312
Inspection Grading and Standardization	10.162	129,455	—	129,455
Grants for Agricultural Research, Special Research Grants	10.200	5,683,588	806,001	6,489,589
Cooperative Forestry Research	10.202	115,212	—	115,212
Payments to Agricultural Experiment Stations Under the Hatch Act	10.203	4,752,729	—	4,752,729
Payments to 1890 Land-Grant Colleges and Tuskegee University	10.205	—	76,500	76,500
Grants for Agricultural Research_Competitive Research Grants	10.206	4,743,840	98,254	4,842,094
Animal Health and Disease Research	10.207	80,781	—	80,781
Sustainable Agriculture Research and Education	10.215	—	51,987	51,987
Higher Education Challenge Grants	10.217	—	69	69
Biotechnology Risk Assessment Research	10.219	67,816	—	67,816
Higher Education Multicultural Scholars Program	10.220	24,061	—	24,061
Fund for Rural America Research, Education, and Extension Activities	10.224	959,442	66,433	1,025,875
Agricultural and Rural Economic Research	10.250	47,016	24,786	71,802
Initiative for Future Agriculture and Food Systems	10.302	1,097,085	602,291	1,699,376
Integrated Programs	10.303	1,156,042	251,220	1,407,262
Homeland Security Agricultural	10.304	105,099	—	105,099
Cooperative Extension Service	10.500	—	25,795	25,795
Emergency Food Assistance Program (Administrative Costs)	10.568	—	4,070	4,070
Emergency Food Assistance Program (Food Commodities)	10.569	—	45,993	45,993
Forestry Research	10.652	4,569	36,778	41,347
Cooperative Forestry Assistance	10.664	189,364	7,914	197,278
Soil Survey	10.903	3,300	—	3,300
Farm and Ranch Lands Protection Program	10.913	(1,563)	—	(1,563)
Scientific Cooperation and Research	10.961	109,118	—	109,118
Department of Agriculture Total		23,458,076	2,579,233	26,037,309
Department of Commerce:				
Department of Commerce	11.000	269,496	530	270,026
Census Geography	11.003	134,670	—	134,670
Census Intergovernmental Services	11.004	(6,005)	—	(6,005)
ITA Special Projects	11.113	—	766,441	766,441
Grants for Public Works and Economic Development Facilities	11.300	1,044,274	—	1,044,274
Sea Grant Support	11.417	—	305,557	305,557
Coastal Zone Management Administration Awards	11.419	—	94,017	94,017
Fisheries Development and Utilization Research and Development Grants and Cooperative Agreements Program	11.427	81,568	—	81,568
Climate and Atmospheric Research	11.431	108,309	139,175	247,484
Office of Oceanic and Atmospheric Research (OAR) Joint and Cooperative Institutes	11.432	—	152,362	152,362
Marine Fisheries Initiative	11.433	64,021	—	64,021
Cooperative Fishery Statistics	11.434	10,724	—	10,724
Applied Meteorological Research	11.468	274,355	—	274,355
Unallied Science Program	11.472	234,894	254,155	489,049
Coastal Services Center	11.473	—	27,750	27,750

CORNELL UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2004

<u>Federal grantor/pass-through grantor/program title</u>	<u>Federal CFDA number</u>	<u>Direct awards</u>	<u>Pass-through awards</u>	<u>Total expenditures</u>
Center for Sponsored Coastal Ocean Research				
Coastal Ocean Program	11.478	\$ 124,016	—	124,016
Measurement and Engineering Research and Standards	11.609	23,641	—	23,641
Department of Commerce Total		<u>2,363,963</u>	<u>1,739,987</u>	<u>4,103,950</u>
Department of Defense:				
Department of Defense	12.000	37,424	1,177,514	1,214,938
Aquatic Plant Control	12.100	—	25,260	25,260
Collaborative Research and Development	12.114	—	(2)	(2)
Basic and Applied Scientific Research	12.300	5,880,819	349,580	6,230,399
Military Medical Research and Development	12.420	476,603	—	476,603
Basic Scientific Research	12.431	1,308,767	422,369	1,731,136
Basic, Applied, and Advanced Research in Science and Engineering	12.630	1,585,909	105,138	1,691,047
Air Force Defense Research Sciences Program	12.800	6,126,279	761,858	6,888,137
Mathematical Sciences Grants Program	12.901	80,665	—	80,665
Research and Technology Development	12.910	3,565,127	1,757,513	5,322,640
Department of Defense Total		<u>19,061,593</u>	<u>4,599,230</u>	<u>23,660,823</u>
Department of Housing and Urban Development:				
Department of Housing and Urban Development	14.000	8,625	—	8,625
Community Outreach Partnership Center Program	14.511	2,683	—	2,683
Department of Housing and Urban Development Total		<u>11,308</u>	<u>—</u>	<u>11,308</u>
Department of the Interior:				
Department of Interior	15.000	18,464	464,786	483,250
Fish and Wildlife Management Assistance	15.608	69,810	—	69,810
Cooperative Endangered Species Conservation Fund	15.615	—	130,859	130,859
Wildlife Conservation and Appreciation	15.617	—	22,280	22,280
Administrative Grants for Federal Aid in Sport				
Fish and Wildlife Restoration	15.618	36,100	—	36,100
African Elephant Conservation	15.620	55,073	—	55,073
Assistance to State Water Resources Research Institute	15.805	182,723	—	182,723
U.S. Geological Survey_ Research and Data Collector	15.808	425,962	—	425,962
Technical Preservation Services	15.915	—	(1,065)	(1,065)
Rivers, Trails, and Conservation Assistance	15.921	81,343	—	81,343
Migratory Bird Banding and Data Analysis	15.976	11,640	—	11,640
Department of the Interior Total		<u>881,115</u>	<u>616,860</u>	<u>1,497,975</u>
Department of Justice:				
Criminal Justice Research and Development - Graduate Research Fellowships	16.562	19,982	—	19,982
Department of Justice Total		<u>19,982</u>	<u>—</u>	<u>19,982</u>
Department of Labor:				
Employee Benefits Security Administrator	17.150	7,783	—	7,783
Department of Labor Total		<u>7,783</u>	<u>—</u>	<u>7,783</u>
Department of State:				
Department of State	19.000	4,163,054	1,081,790	5,244,844
Department of State Total		<u>4,163,054</u>	<u>1,081,790</u>	<u>5,244,844</u>

CORNELL UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2004

Federal grantor/pass-through grantor/program title	Federal CFDA number	Direct awards	Pass-through awards	Total expenditures
Department of Transportation:				
Department of Transportation	20.000	\$ —	51,142	51,142
Highway Planning and Construction	20.205	8,220	3,024,878	3,033,098
University Transportation Centers Program:	20.701	—	167,952	167,952
Department of Transportation Total		8,220	3,243,972	3,252,192
National Aeronautics and Space Administration:				
Aerospace Education Services Program:	43.001	5,751,532	13,754,659	19,506,191
National Aeronautics and Space Administration Total		5,751,532	13,754,659	19,506,191
National Foundation on the Arts and the Humanities:				
Promotion of the Humanities – Research:	45.161	39,714	—	39,714
National Foundation on the Arts and the Humanities Total		39,714	—	39,714
National Science Foundation:				
Engineering Grants	47.041	19,696,067	498,491	20,194,558
Mathematical and Physical Sciences	47.049	54,946,832	262,066	55,208,898
Geosciences	47.050	3,951,107	140,032	4,091,139
Computer and Information Science and Engineering	47.070	7,940,642	458,983	8,399,625
Biological Sciences	47.074	10,632,581	2,593,415	13,225,996
Social, Behavioral, and Economic Sciences	47.075	2,391,641	120	2,391,761
Education and Human Resources	47.076	4,435,127	68,869	4,503,996
Polar Programs	47.078	118,879	—	118,879
National Science Foundation Total		104,112,876	4,021,976	108,134,852
Environmental Protection Agency:				
Environmental Protection Agency	66.000	—	1,451	1,451
Water Pollution Control State and Interstate Program Support	66.419	—	5,938	5,938
Nonpoint Source Implementation Grants	66.460	89,991	136,126	226,117
Water Quality Cooperative Agreements	66.463	12,265	—	12,265
Environmental Protection_Consolidated Research	66.500	127,820	114,071	241,891
Safe Drinking Water Research and Demonstrator	66.506	12,855	—	12,855
Science To Achieve Results (STAR) Program	66.509	327,845	25,631	353,476
Surveys, Studies, Investigations, and Special Purpose Grants	66.606	290,020	(50,119)	239,901
Solid Waste Management Assistance	66.808	3,664	—	3,664
Environmental Protection Agency Total		864,460	233,098	1,097,558
Department of Energy:				
Department of Energy	81.000	405,079	721,552	1,126,631
Office of Science Financial Assistance Program	81.049	3,820,162	586,276	4,406,438
Regional Biomass Energy Program:	81.079	—	(2,145)	(2,145)
Conservation Research and Development	81.086	140,356	—	140,356
Renewable Energy Research and Development	81.087	—	18,094	18,094
University Reactor Infrastructure and Education Support	81.114	2,562,145	—	2,562,145
Department of Energy Total		6,927,742	1,323,777	8,251,519

CORNELL UNIVERSITY
Schedule of Expenditures of Federal Awards
Year ended June 30, 2004

<u>Federal grantor/pass-through grantor/program title</u>	<u>Federal CFDA number</u>	<u>Direct awards</u>	<u>Pass-through awards</u>	<u>Total expenditures</u>
Department of Education:				
Department of Education	84.000	\$ 29,496	—	29,496
National Resource Centers and Fellowships Program for Language and Area or Language and International Studies	84.015	478,357	—	478,357
International Research and Studies	84.017	263,918	—	263,918
Overseas – Faculty Research Abroad	84.019	59,528	—	59,528
National Institute on Disability and Rehabilitation Research Goals 2000: State & Local Education Systemic Improvement Grants	84.133	314,787	—	314,787
International Education Technological Innovation and Cooperation for Foreign Information Access	84.276	—	(9,880)	(9,880)
	84.337	—	33,697	33,697
Department of Education Total		1,146,086	23,817	1,169,903
United States Institute of Peace:				
Unsolicited Grant Program	91.001	—	21,604	21,604
United States Institute of Peace Total		—	21,604	21,604
Department of Health and Human Services:				
Department of Health and Human Services	93.000	2,526,170	18,035,793	20,561,963
Food and Drug Administration_Research	93.103	115,525	—	115,525
Maternal and Child Health Federal Consolidated Programs	93.110	133,600	—	133,600
Biological Response to Environmental Health Hazards	93.113	275,488	32,816	308,304
Applied Toxicological Research and Testing	93.114	343,969	—	343,969
Biometry and Risk Estimation – Health Risks from Environmental Exposures	93.115	—	52,530	52,530
Oral Diseases and Disorders Research	93.121	543,879	153,862	697,741
AIDS Education and Training Centers	93.145	—	224,621	224,621
Coordinated Services and Access to Research for Women, Infants, Children, and Youth	93.153	282,408	—	282,408
Human Genome Research	93.172	6,561	232,144	238,705
Research Related to Deafness and Communication Disorders	93.173	1,445,773	—	1,445,773
Research and Training in Complementary and Alternative Medicine	93.213	1,318	—	1,318
National Research Service Awards_Health Services Research Training	93.225	31,668	—	31,668
Research on Healthcare Costs, Quality, and Outcomes	93.226	633,348	—	633,348
Mental Health Research Grants	93.242	9,890,114	39,001	9,929,115
Alcohol Research Programs	93.273	778,434	—	778,434
Drug Abuse Scientist Development Awards, Research Scientist Development Awards, and Research Scientist Awards	93.277	290,079	—	290,079
Drug Abuse National Research Service Award for Research Training	93.278	325,579	—	325,579
Drug Abuse Research Programs	93.279	5,667,225	105,642	5,772,867
Mental Health Research Career/Scientist Development Awards	93.281	1,502,121	173,830	1,675,951
Mental Health National Research Service Awards for Research Training	93.282	378,327	—	378,327
Centers for Disease Control and Prevention – Investigations and Technical Assistance	93.283	386,479	—	386,479
Discovery and Applied Research	93.286	1,241,396	—	1,241,396
Bioengineering Research	93.287	—	1,051	1,051
Comparative Medicine Program	93.306	421,464	—	421,464
General Clinical Research Centers	93.333	6,319,514	—	6,319,514
Nursing Research	93.361	—	2,048	2,048
Biomedical Research Technology	93.371	5,859,525	285,275	6,144,800

CORNELL UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2004

Federal grantor/pass-through grantor/program title	Federal CFDA number	Direct awards	Pass-through awards	Total expenditures
National Center for Research Resources	93.389	\$ 3,620,368	—	3,620,368
Cancer Cause and Prevention Research	93.393	2,381,891	144,626	2,526,517
Cancer Detection and Diagnosis Research	93.394	3,992,626	—	3,992,626
Cancer Treatment Research	93.395	2,213,802	142,638	2,356,440
Cancer Biology Research	93.396	3,135,125	161,759	3,296,884
Cancer Centers Support Grants	93.397	—	23,336	23,336
Cancer Research Manpower	93.398	1,243,225	30,743	1,273,968
Cancer Control	93.399	716,350	141,406	857,756
Temporary Assistance for Needy Families and Development Fund	93.558	—	7,651	7,651
Child Care Mandatory and Matching Funds of the Child Care	93.596	286,352	—	286,352
Social Services Research and Demonstrator	93.647	21,948	—	21,948
Adoption Opportunities	93.652	—	60,120	60,120
Child Abuse and Neglect Discretionary Activities	93.670	505,463	—	505,463
Medicaid Infrastructure Grants To Support the Competitive Employment of People with Disabilities	93.768	—	378,517	378,517
Cell Biology and Biophysics Research	93.821	9,968,607	315,046	10,283,653
Heart and Vascular Diseases Research	93.837	16,249,834	109,493	16,359,327
Lung Diseases Research	93.838	5,391,524	—	5,391,524
Blood Diseases and Resources Research	93.839	4,834,446	—	4,834,446
Arthritis, Musculoskeletal, and Skin Diseases Research	93.846	2,078,602	130,391	2,208,993
Diabetes, Endocrinology, and Metabolism Research	93.847	4,439,920	17,125	4,457,045
Digestive Diseases and Nutrition Research	93.848	1,907,071	597	1,907,668
Kidney Diseases, Urology, and Hematology Research	93.849	3,860,095	—	3,860,095
Extramural Research Programs in the Neurosciences and Neurological Disorders	93.853	5,953,209	259,485	6,212,694
Biological Basis Research in the Neurosciences	93.854	3,033,661	50,017	3,083,678
Allergy, Immunology, and Transplantation Research	93.855	3,512,585	—	3,512,585
Microbiology and Infectious Diseases Research	93.856	12,804,826	433,794	13,238,620
Biomedical Research and Research Training	93.859	7,540,994	41,293	7,582,287
Genetics and Developmental Biology Research	93.862	6,386,171	211,187	6,597,358
Population Research	93.864	3,230,312	81,108	3,311,420
Child Health and Human Development Extramural Research	93.865	2,167,418	166,138	2,333,556
Aging Research	93.866	5,596,810	32,644	5,629,454
Vision Research	93.867	4,056,135	372,051	4,428,186
Minority Access to Research Careers	93.880	87,350	—	87,350
Grants for Physician Assistant Training Program	93.886	1,191	—	1,191
Special Projects of National Significance	93.928	354,060	—	354,060
Fogarty International Research Collaboration Award	93.934	81,315	—	81,315
International Research and Research Training	93.989	1,296,716	—	1,296,716
Department of Health and Human Services Total		162,349,966	22,649,778	184,999,744
Social Security Administration:				
Social Security – Research and Demonstration	96.007	—	(79,293)	(79,293)
Social Security Administration Total		—	(79,293)	(79,293)
Research and Development Total		331,167,470	55,810,488	386,977,958
Student Financial Aid:				
Department of Education:				
Federal Supplemental Educational Opportunity Grants	84.007	4,412,569	—	4,412,569
Federal Family Education Loans	84.032	11,688,262	—	11,688,262
Federal Work-Study Program	84.033	3,800,531	—	3,800,531
Federal Perkins Loan Program – Federal Capital Contributions	84.038	10,889,439	—	10,889,439
Federal Pell Grant Program	84.063	6,394,613	—	6,394,613
Federal Direct Student Loans	84.268	55,519,378	—	55,519,378
Department of Education Total		92,704,792	—	92,704,792

CORNELL UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2004

<u>Federal grantor/pass-through grantor/program title</u>	<u>Federal CFDA number</u>	<u>Direct awards</u>	<u>Pass-through awards</u>	<u>Total expenditures</u>
Department of Health and Human Services:				
Health Professions Student Loans, Including Primary Care Loans/Loans for Disadvantaged Students	93.342	\$ 524,692	—	524,692
Scholarships for Health Professions Students from Disadvantaged Backgrounds	93.925	162,223	—	162,223
Department of Health and Human Services Total		686,915	—	686,915
Student Financial Aid Total		93,391,707	—	93,391,707
Department of Agriculture:				
Department of Agriculture	10.000	284,802	349,778	634,580
Plant and Animal Disease, Pest Control, and Animal Care	10.025	86,352	58,125	144,477
Minority Research and Teaching Grants	10.140	40,540	—	40,540
Grants for Agricultural Research, Special Research Grants	10.200	236,061	71,625	307,686
Payments to Agricultural Experiment Stations Under the Ac	10.203	291,701	—	291,701
Grants for Agricultural Research – Competitive Research Grants	10.206	135,849	96,743	232,592
Animal Health and Disease Research	10.207	337,819	—	337,819
Food and Agricultural Sciences National Needs Graduate Fellowship Grants	10.210	166,152	—	166,152
Sustainable Agriculture Research and Education	10.215	13,721	15,953	29,674
Higher Education Challenge Grants	10.217	73,835	—	73,835
Higher Education Multicultural Scholars Program	10.220	77,276	—	77,276
Fund for Rural America – Research, Education, and Extension Activities	10.224	—	7,617	7,617
Initiative for Future Agriculture and Food Systems	10.302	467,455	50,181	517,636
Integrated Programs	10.303	—	366,196	366,196
Technical Assistance to Cooperatives	10.350	15,588	—	15,588
Human Nutrition Information Service	10.375	—	23,118	23,118
Crop Insurance	10.450	156,963	213,626	370,589
Cooperative Extension Service	10.500	12,888,004	114,495	13,002,499
Food Stamps	10.551	—	588,319	588,319
Emergency Food Assistance Program (Administrative Costs)	10.568	—	2,659	2,659
Cooperative Forestry Assistance	10.664	86,020	—	86,020
National Agricultural Library	10.700	3,334	—	3,334
Environmental Quality Incentives Program	10.912	—	6,270	6,270
Technical Agricultural Assistance	10.960	1,305	—	1,305
Scientific Cooperation and Research	10.961	35,866	—	35,866
International Training – Foreign Participant	10.962	44,569	—	44,569
Department of Agriculture Total		15,443,212	1,964,705	17,407,917
Department of Commerce:				
Department of Commerce	11.000	9,454	—	9,454
Census Intergovernmental Services	11.004	65,139	—	65,139
Economic Development – Technical Assistance	11.303	75,510	—	75,510
Sea Grant Support	11.417	73,891	886,301	960,192
Unallied Science Program	11.472	—	12,110	12,110
Calibration Program	11.601	86,975	—	86,975
Department of Commerce Total		310,969	898,411	1,209,380
Department of Defense:				
Department of Defense	12.000	31,287	—	31,287
Military Medical Research and Development	12.420	30,224	—	30,224
Mathematical Sciences Grants Program	12.901	98,705	—	98,705
Department of Defense Total		160,216	—	160,216

CORNELL UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2004

<u>Federal grantor/pass-through grantor/program title</u>	<u>Federal CFDA number</u>	<u>Direct awards</u>	<u>Pass-through awards</u>	<u>Total expenditures</u>
Department of Housing and Urban Development: Community Outreach Partnership Center Program:	14.511	\$ 30,966	—	30,966
Department of Housing and Urban Development Total		30,966	—	30,966
Department of the Interior: Wildlife Conservation and Appreciation	15.617	2,393	—	2,393
Assistance to State Water Resources Research Institute:	15.805	7,974	—	7,974
Historic Preservation Fund Grants-In-Aid	15.904	476	—	476
Department of the Interior Total		10,843	—	10,843
Department of Labor: Department of Labor	17.000	(133,499)	—	(133,499)
Work Incentives Grant	17.266	—	220,910	220,910
Department of Labor Total		(133,499)	220,910	87,411
Department of State: Department of State	19.000	21,534	880,511	902,045
Professional Development – International Educators/Administrators	19.404	—	204	204
Educational Partnerships Program	19.424	25,225	—	25,225
Department of State Total		46,759	880,715	927,474
Department of Transportation: Highway Planning and Construction	20.205	—	6,735	6,735
Highway Training and Education	20.215	(6,000)	—	(6,000)
Federal Transit_Capital Investment Grants	20.500	275	—	275
State and Community Highway Safety	20.600	—	53,649	53,649
Department of Transportation Total		(5,725)	60,384	54,659
Department of the Treasury: Community Development Financial Institutions Program	21.020	—	426,628	426,628
Department of the Treasury Total		—	426,628	426,628
Office of Personnel Management: Intergovernmental Personnel Act (IPA) Mobility Program	27.011	85,844	—	85,844
Office of Personnel Management Total		85,844	—	85,844
National Aeronautics and Space Administration: Aerospace Education Services Program:	43.001	435,050	36,948	471,998
National Aeronautics and Space Administration Total		435,050	36,948	471,998
National Foundation on the Arts and the Humanities: National Foundation on the Arts and the Humanities Promotion of the Humanities_Division of Preservation and Access	45.000	25,000	—	25,000
Promotion of the Humanities_Public Programs	45.149	397,665	—	397,665
Museum for America Grants	45.164	182,177	—	182,177
National Leadership Grants	45.301	15,094	—	15,094
	45.312	377,652	—	377,652
National Foundation on the Arts and the Humanities Total		997,588	—	997,588
National Science Foundation: Engineering Grants	47.041	34,338	103,368	137,706
Mathematical and Physical Sciences	47.049	61,310	—	61,310
Geosciences	47.050	56,597	—	56,597
Computer and Information Science and Engineering	47.070	321,905	6,947	328,852
Biological Sciences	47.074	142,777	—	142,777

CORNELL UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2004

<u>Federal grantor/pass-through grantor/program title</u>	<u>Federal CFDA number</u>	<u>Direct awards</u>	<u>Pass-through awards</u>	<u>Total expenditures</u>
Education and Human Resources	47.076	\$ 3,975,281	87,766	4,063,047
National Science Foundation Total		4,592,208	198,081	4,790,289
Environmental Protection Agency:				
Environmental Protection Agency	66.000	20,726	—	20,726
Water Quality Management Planning	66.454	—	2,316	2,316
National Estuary Program	66.456	206,517	4,400	210,917
Nonpoint Source Implementation Grants	66.460	—	197,387	197,387
Great Lakes Program	66.469	866	—	866
Environmental Protection – Consolidated Research	66.500	24,031	—	24,031
Surveys, Studies, Investigations, and Special Purpose Grants	66.606	256,627	—	256,627
Environmental Protection Agency Total		508,767	204,103	712,870
Department of Education:				
Migrant Education – State Grant Program	84.011	—	182,218	182,218
National Resource Centers and Fellowships Program for				
Language and Area or Language and International Studies	84.015	1,680,554	260,249	1,940,803
Overseas – Doctoral Dissertation	84.022	153,110	—	153,110
Special Education – Grants to States	84.027	—	397,405	397,405
National Institute on Disability and Rehabilitation Research	84.133	1,784,035	—	1,784,035
Migrant Education – Coordination Program	84.144	—	4,071	4,071
Javits Fellowships	84.170	315,269	—	315,269
Graduate Assistance in Areas of National Need	84.200	724,269	—	724,269
Early Childhood Educator Professional Development	84.349	—	82,278	82,278
Department of Education Total		4,657,237	926,221	5,583,458
United States Institute of Peace:				
Unsolicited Grant Program	91.001	—	70	70
United States Institute of Peace Total		—	70	70
Department of Health and Human Services:				
Department of Health and Human Services	93.000	—	540,186	540,186
Applied Toxicological Research and Testing	93.114	—	9,104	9,104
Occupational Safety and Health Research Projects	93.262	—	49,141	49,141
Mental Health National Research Service Awards for				
Research Training	93.282	121,089	—	121,089
Comparative Medicine Program	93.306	362,570	—	362,570
Cancer Research Manpower	93.398	165,104	—	165,104
Temporary Assistance for Needy Families	93.558	—	54,667	54,667
Community Services Block Grant Discretionary Awards				
Community Food and Nutrition	93.571	—	75,604	75,604
Refugee and Entrant Assistance – Discretionary Grants	93.576	—	13,546	13,546
Child Care Mandatory and Matching Funds of the Child				
Care and Development Fund	93.596	—	499,531	499,531
Head Start	93.600	—	42,418	42,418
Developmental Disabilities Basic Support and				
Advocacy Grants	93.630	—	128,099	128,099
Foster Care Title IV-E	93.658	—	890,454	890,454
Cell Biology and Biophysics Research	93.821	1,450,841	—	1,450,841
Digestive Diseases and Nutrition Research	93.848	428,976	—	428,976
Microbiology and Infectious Diseases Research	93.856	197,319	—	197,319
Biomedical Research and Research Training	93.859	259,325	—	259,325
Genetics and Developmental Biology Research	93.862	304,408	—	304,408
Population Research	93.864	33,864	—	33,864
Vision Research	93.867	5,193	—	5,193
Strabismus, Amblyopia, and Visual Processing	93.871	2,212	—	2,212
Minority Access to Research Careers	93.880	31,286	—	31,286
Resource and Manpower Development in the				
Environmental Health Sciences	93.894	164,528	—	164,528

CORNELL UNIVERSITY

Schedule of Expenditures of Federal Awards

Year ended June 30, 2004

Federal grantor/pass-through grantor/program title	Federal CFDA number	Direct awards	Pass-through awards	Total expenditures
Fogarty International Research Collaboration Award	93.934	\$ 4,897	—	4,897
Health Administration Traineeships and Special Projects Program	93.962	4,500	—	4,500
International Research and Research Training	93.989	478,286	—	478,286
Department of Health and Human Services Total		4,014,398	2,302,750	6,317,148
Social Security Administration:				
Social Security Agency	96.000	890,123	—	890,123
Social Security – Research and Demonstration	96.007	—	20,151	20,151
Social Security Administration Total		890,123	20,151	910,274
Department of Homeland Security:				
Crisis Counseling	97.032	—	233,999	233,999
Department of Homeland Security Total		—	233,999	233,999
Total Federal Financial Assistance		\$ 456,604,133	64,184,564	520,788,697

See accompanying notes to Schedule of Expenditures of Federal Awards

CORNELL UNIVERSITY

Notes to Schedule of Expenditures of Federal Awards

Year ended June 30, 2004

(1) Basis of Presentation

The accompanying schedule of expenditures of Federal awards includes the Federal grant activity of Cornell University and is presented on the accrual basis of accounting. The information in the schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of the basic financial statements.

Significant categories of awards for the University are as follows:

Research and development – Includes awards for research and development work of the University under grants and contracts primarily funded by the Department of Health and Human Services, the National Science Foundation, the Department of Agriculture, the Department of Defense, the National Aeronautics Space Administration, and the Department of Energy.

Student financial assistance – Includes certain awards to provide financial assistance to students, under the Federal Work-Study (FWS), Federal Pell Grant (Pell), and Federal Supplemental Educational Opportunity Grant (FSEOG) programs. Student financial assistance also includes the Federal Perkins, Federal Family Education, Federal Direct, and Health Professions Student guaranteed loan programs of the Department of Education or Department of Health and Human Services. The University receives awards to make loans to eligible students under certain Federal student loan programs and federally-guaranteed loans are issued to students of the University either by various financial institutions or directly by the University.

Cooperative extension service – Includes awards issued by the Department of Agriculture under the Smith-Lever Act for public services and education provided by cooperative extension locations in each county of New York and New York City.

(2) Facilities and Administrative Costs

Certain expenditures include a portion of costs associated with general university activities (Facilities and Administrative Costs), which are allocated to awards under negotiated formulas commonly referred to as Facilities and Administrative (F&A) cost rates (formerly known as indirect cost rates).

Federal F&A cost recoveries for the fiscal year ended June 30, 2004 totaled \$114,001,287 including \$70,298,429 for the Ithaca campus and \$43,702,858 for Weill Medical College (WMC).

Ithaca Campus

F&A cost rates for the Ithaca Campus have been finalized through fiscal year 2005 as predetermined rates pursuant to the Department of Health and Human Services (DHHS) rate agreement dated June 28, 2004. Provisional rates have been established for fiscal year 2006 and beyond.

CORNELL UNIVERSITY

Notes to Schedule of Expenditures of Federal Awards

Year ended June 30, 2004

Weill Medical College

F&A cost rates for the WMC have been finalized through fiscal year 2006 as predetermined rates pursuant to the Department of Health and Human Services (DHHS) rate agreement dated June 17, 2003. Provisional rates have been established for fiscal year 2007 and beyond.

(3) Student Loan Programs

The University had the following loan balances outstanding at June 30, 2004. These balances are not included in the Federal expenditures presented in the Schedule.

	<u>CFDA number</u>		<u>Amount outstanding</u>
Federal Perkins Loan Program	84.038	\$	45,142,467
Health Professions Student Loan Program, including Primary Care Loans and Loans for Disadvantaged Students	93.342		<u>3,619,473</u>
		\$	<u><u>48,761,940</u></u>

The loan programs noted above are administered directly by the University and balances and transactions relating to these programs are included in the University's basic financial statements. The schedule of expenditures of federal awards includes loan expenditures and disbursements to students and administrative costs of the loan programs for the year ended June 30, 2004.

The University issued the following amounts of new loans under the Federal Direct Loan and Federal Family Education Loan Programs to students of the University during the year ended June 30, 2004:

Federal Direct Loan Program (FDLP):	
Federal Subsidized	\$ 36,306,907
Federal Unsubsidized	<u>19,212,471</u>
Total FDLP	<u>\$ 55,519,378</u>
Federal Family Education Loan Program	<u>\$ 11,688,262</u>

The University is responsible only for the performance of certain administrative duties with respect to the Federal Family Education Loan and the Federal Direct Loan programs and, accordingly, these loans are not included in the University's basic financial statements. It is not practical to determine the balance of loans outstanding under these programs at June 30, 2004.

(4) Pass-Through Awards and Subrecipients

The University receives pass-through awards from approximately 500 not-for-profit organizations. Accordingly, it is not practical to identify in the schedule of expenditures of federal awards each organization from which the University receives such pass-through awards. In addition, the University has approximately 540 subrecipients of its federal funds. Due to the large number of programs and sponsors, it is not practical to disclose the amount of payments to subrecipients.



KPMG LLP
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Rochester, NY 14604

**Independent Auditors' Report on Internal Control over
Financial Reporting and Compliance and Other Matters
Based on an Audit of Financial Statements Performed in
Accordance with *Government Auditing Standards***

The Board of Trustees
Cornell University:

We have audited the financial statements of Cornell University as of and for the year ended June 30, 2004, and have issued our report thereon dated September 7, 2004. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing our audit, we considered Cornell University's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Cornell University's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of Cornell University in a separate letter dated September 7, 2004.



This report is intended solely for the information and use of the Audit Committee, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

September 7, 2004
Rochester, New York



KPMG LLP
265 Clinton Square
Rochester, NY 14604

Independent Auditors' Report on Compliance with Requirements Applicable to each Major Program and Internal Control over Compliance in Accordance with OMB Circular A-133

The Board of Trustees
Cornell University:

Compliance

We have audited the compliance of Cornell University with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major Federal programs for the year ended June 30, 2004. Cornell University's major Federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major Federal programs is the responsibility of Cornell University's management. Our responsibility is to express an opinion on Cornell University's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major Federal program occurred. An audit includes examining, on a test basis, evidence about Cornell University's compliance with those requirements and performing such other procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Cornell University's compliance with those requirements.

In our opinion, Cornell University complied, in all material respects, with the requirements referred to above that are applicable to each of its major Federal programs for the year ended June 30, 2004.

Internal Control over Compliance

The management of Cornell University is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to Federal programs. In planning and performing our audit, we considered Cornell University's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.



We noted a matter involving the internal control over compliance and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect Cornell University's ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. The reportable condition is described in the accompanying schedule of findings and questioned costs as item 2004-1.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable condition described above is not a material weakness.

This report is intended solely for the information and use of the Audit Committee, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

January 4, 2005
Rochester, New York

CORNELL UNIVERSITY

Schedule of Findings and Questioned Costs

Year ended June 30, 2004

I. Summary of Auditors' Results:

Financial Statements

Type of auditors' report issued: unqualified

Internal control over financial reporting:

- Material weakness(es) identified? yes no
- Reportable condition(s) identified that are not considered to be material weaknesses? yes none reported

Noncompliance material to financial statements noted? yes no

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? yes no
- Reportable condition(s) identified that are not considered to be material weaknesses? yes none reported

Type of auditors' report issued on compliance for major programs: unqualified

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133? yes no

Identification of major programs:

<u>CFDA Number(s)</u>	<u>Name of Federal Programs or Clusters</u>
Various	Research and Development Cluster
84.007, 84.032, 84.033, 84.038, 84.063, 84.268, 93.342, and 93.925	Student Financial Assistance Cluster
Dollar threshold used to distinguish between type A and type B programs:	\$3,000,000

Auditee qualified as low-risk auditee? yes no

II. Findings Relating to the Financial Statements Reported in Accordance with *Government Auditing Standards*:

None Reported

CORNELL UNIVERSITY

Schedule of Findings and Questioned Costs

Year ended June 30, 2004

III. Findings and Questioned Costs Relating to Federal Awards:

Finding: 2004-1

Program: Student Financial Assistance Cluster

Condition Found:

It was noted during an audit performed by the University's internal audit department that Student Financial Aid counselors have the ability to change parameters within the student profiles. Such parameters might include cost of attendance, student resources, income, family data, and other items affecting the calculation of the aid amounts. Once the counselors prepare the initial award information and check the packaging based on the initial stated parameters, there is no additional review.

Questioned Costs:

None.

Recommendation:

We recommend that the University establish and maintain appropriate internal controls to review the validity of changes made to student profiles after the initial review is performed.

University's Response:

While controls exist for the review of student financial aid applications, the Office of Financial Aid and Student Employment recognizes the concern being expressed about the adequacy of this process. The Office has already begun to strengthen the system.

The Office of Financial Aid and Student Employment will review a random sample of financial aid files each semester. We will begin with a sample size of 50 to 75 students. As we review the files and learn more about the error rate, we will revise the sample size accordingly. The writing of procedures to govern file reviews is expected to be completed by January 15, 2005, with file review beginning in February 2005.

In addition, management is developing a written approval process for large adjustments to parameters of student profiles, and will develop an exception report to support this oversight. The process will be written and the exception checking will begin by March 2005.