VIRGINIA COMMONWEALTH UNIVERSITY

RICHMOND, VIRGINIA

REPORT ON AUDIT

FOR THE YEAR ENDED

JUNE 30, 2002

APA
Auditor of
Public Accounts
COMMONWEALTH OF VIRGINIA

AUDIT SUMMARY

Our audit of Virginia Commonwealth University for the year ended June 30, 2002, found the following:

- the financial statements are presented fairly, in all material respects;
- internal control matters that we consider to be a reportable conditions; however, we do not consider these to be material weaknesses;
- an instance of noncompliance that is required to be reported under Government Auditing Standards; and
- the University has not taken adequate corrective action with respect to the previously reported finding "Improve Controls Over Cash Collections." Adequate corrective action was taken with respect to audit findings reported in the prior year that are not repeated in this report.

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UNIVERSITY OFFICIALS

Commonwealth of Virginia

Auditor of Public Accounts
P.O. Box 1295
Richmond, Virginia 23218

Walter J. Kucharski, Auditor

December 11, 2002

The Honorable Mark R. Warner
Governor of Virginia

The Honorable Kevin G. Miller
Chairman, Joint Legislative Audit
and Review Commission

The Board of Visitors
Virginia Commonwealth University

We have audited the accounts and records of **Virginia Commonwealth University** and its discretely presented component unit, as of and for the year ended June 30, 2002, and submit herewith our complete reports on financial statements and compliance and internal control over financial reporting.

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

We have audited the accompanying basic financial statements of Virginia Commonwealth University, a component unit of the Commonwealth of Virginia, and its discretely presented component unit as of and for the year ended June 30, 2002, as listed in the table of contents. 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. We did not audit the financial statements of the Virginia Commonwealth University Health System Authority, a discretely presented component unit, which statements reflect total assets and revenues of $578,179,879 and $678,896,710, respectively, as of and for the year ended June 30, 2002. Those statements were audited by other auditors whose report has been furnished to us and our opinion, insofar as it relates to the amounts included for the Virginia Commonwealth University Health System Authority is based solely upon the report of the other auditors.

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 and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of Virginia Commonwealth

University and of its discretely presented component unit as of June 30, 2002, and the respecitve changes in financial position and cash flows thereof for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

As described in Note 1 in the Notes to Financial Statements, the University has implemented a new financial reporting model as required by the provisions of Governmental Accounting Standards Board Statement 34, *Basic Financial Statements – and Management's and Analysis – for State and Local Governments,* and Statement 35, *Basic Financial Statements Discussion – and Management's Discussion and Analysis – for Public Colleges and Universities* as of June 30, 2002.

The Management's Discussion and Analysis presented on pages 7 through 13 is not a required part of the basic financial statements, but is supplemental information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplemental information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements. The accompanying Schedule of Auxiliary Enterprises – Revenues and Expenditures is presented for the purpose of additional analysis and is not a required part of the financial statements. The information in that schedule has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, such information is fairly presented in all material respects in relation to the financial statements taken as a whole.

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements of Virginia Commonwealth University as of and for the year ended June 30, 2002, we considered internal controls over financial reporting and tested compliance with certain provisions of laws, regulations, contracts, and grants 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.

Compliance

As part of obtaining reasonable assurance about whether the University's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance 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 an instance of noncompliance that is required to be reported under Government Auditing Standards.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the 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 assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the University's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. These reportable conditions are described in the section titled "Internal Control Finding and Recommendations."

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 misstatements 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. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. However, we believe that the reportable conditions described above are not material weaknesses.

Status of Prior Findings

Virginia Commonwealth University has not taken adequate corrective action with respect to the previously reported finding "Improve Controls Over Cash Collections." Accordingly, we included this finding in the section entitled "Internal Control Findings and Recommendations." Virginia Commonwealth University has taken adequate corrective action with respect to audit findings reported in the prior year that are not repeated in this report.

The "Independent Auditor's Report on Compliance and on Internal Control over Financial Reporting" is intended solely for the information and use of the Governor and General Assembly of Virginia, Board of Visitors and management, and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

EXIT CONFERENCE

We discussed this report with management at an exit conference held on January 16, 2003.

AUDITOR OF PUBLIC ACCOUNTS

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INTERNAL CONTROL FINDINGS AND RECOMMENDATIONS

Ensure Proper Stewardship and Control Over Fixed Assets

The University did not adequately maintain and safeguard fixed assets in accordance with the University's fixed asset policies and procedures and the Commonwealth's Accounting Policies and Procedures. Exceptions noted in our test work included being unable to locate fixed assets, assets having unreadable or non-visible identification tags, assets without identification tags, assets with incorrect location or other description data in the fixed asset system, and assets not appearing on the department's inventory verification listing. These exceptions arose from individual department custodians not following procedures for properly maintaining and tracking fixed assets.

Management should ensure that each department follows the requirements and guidelines in the University's fixed asset policies and procedures and properly conducts an annual inventory of its fixed assets. Management should establish a uniform procedure of tagging fixed assets so tags are visible for tracking purposes, and update the policies and procedures to reflect changes caused by the new online fixed asset system.

Improve Controls over Cash Collection

University policy requires the deposit of cash receipts over $100 by the next business day. Our review of five cash collections points found two departments that did not consistently comply with this policy. The University has written policies and procedures regarding the handling of cash transactions and provides employee training. However, departmental management has the responsibility for ensuring employee awareness and commitment to strong internal controls over cash receipts. These controls are necessary to prevent mishandling of funds and safeguard against loss.

Improve Construction Project Management

The University did not clearly document the authority and responsibilities of all persons involved in the contract administration, project management, and oversight of construction projects. For the West Hospital Fire/Safety Renovation project, the project inspector was one month behind in completing required daily inspection reports, and the reports did not include the inspector's signature and project number. The Construction and Professional Services Manual requires these reports to show the progress of and changes in a project during construction, and provide useful information for the University in case the need arises to enforce contractor performance. In addition, the project files did not clearly designate the department responsible for the administration of the contract and we could not determine whether it was the Construction Management Department or the Planning and Design Department. The University should improve its project management by clearly designating responsible departments and ensuring project inspectors complete required reports timely to protect the University in the event of a dispute with the contractor.

Improve Controls Over Small Purchase Charge Card Program

The University has received certain exemptions from the Department of Accounts on how it may operate and use the small purchase charge cards. The exemptions allow the University to set rules, policies, and procedures that best meet its operating environment. However, none of the exemptions allow the University to bypass fundamental internal controls and more importantly, the exemptions require the University to enforce its own rules, policies, and procedures.

One of the key internal controls with the small purchase charge card is ensuring that the University only pays for authorized and approved purchases and has a procedure to detect statement errors and misbillings. The Department of Accounts has allowed the University to establish its procedures and documentation standards for this process. The University has not clearly communicated its standards to the departments resulting in inconsistencies in documentation. Our review found departments do not clearly identify discrepancies. Not following University purchasing and usage guidelines could allow improper payments. The University should enforce its policies and procedures to reduce the risk of improper payments.

MANAGEMENT'S DISCUSSION AND ANALYSIS

New Accounting Standards

In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement 34, *Basic Financial Statements and Management's Discussion and Analysis – for State and Local Governments*, which established new financial reporting requirements. In November 1999, GASB issued Statement 35, *Basic Financial Statements and Management's Discussion and Analysis for Public Colleges and Universities – an Amendment of GASB Statement 34*, which applies the new reporting standards to public higher education institutions.

The new financial reporting standards significantly change the appearance and nature of the required financial information. The major changes are: (1) financial statements are presented on an entity-wide basis and not by major fund groups; (2) depreciation expense is recognized, previously it was not; (3) expenses rather than expenditures are reported; and (4) the basic financial statements are preceded by this Management's Discussion and Analysis.

As required by the new accounting pronouncements, the basic financial statements are: the Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; and the Statement of Cash Flows. The following analysis discusses elements from each of these statements, as well as provides an overview of University activities. Since this is a transition year for the new reporting format, only one year of information is presented in the audited financial statements.

Virginia Commonwealth University's Management Discussion and Analysis (MD&A) of its financial condition provides an overview of financial activity, identifies changes in financial position, and assists the reader in focusing on significant financial issues. While maintaining financial health is crucial to the long-term viability of a university, the primary mission of a public institution of higher education is to provide education, research, and public service. Therefore, net assets are accumulated only as required to ensure that there are sufficient reserve funds for future operations and implementation of new programs.

The MD&A provides summary level financial information; therefore, it should be read in conjunction with the accompanying financial statements.

Financial Highlights – Operating

University:

- The University's income before other revenues and expenses was $ 7.6 million.

- State appropriations decreased $6.6 million of which $2.3 million was offset by reductions in the contribution to state employee benefit plans, and $1.6 million was applied to the budget reduction for fiscal year 2003.

- State appropriations receivable decreased $9.1 million as the University accumulated its reserves in non-general fund sources.

- The University negotiated a Federal facilities and administrative (indirect) cost rate of 50 percent effective for fiscal years 2002-2004.

Authority:

- Patient service revenues comprise the majority of the Authority revenues. Net patient services revenue increased 3.3 percent from the prior year due to an increase in selected hospital services and revenue improvement processes. The premium revenue of Virginia Premier increased by $64 million as a result of participation in the Department of Medical Assistance Medallion II managed care expansion throughout the state.

- During the year, the Authority's expenses increased by $75.8 million from prior year. The majority of the increase is the result of the medical claims expense increase of $58 million, which resulted from Virginia Premier's network expansion.

<u>Financial Highlights – Capital</u>

University:

- The University acquired the Capitol Medical Center in fiscal year 2002 to provide additional student housing. Construction was also substantially completed on the Bowe Street Parking Deck.

- VCU Real Estate Foundation started construction of the second student apartment complex, which will be managed by the University.

Authority:

- The major capital expenditure was the completion and opening of the Gateway Building.

<u>Using the Annual Report</u>

This annual report consists of a series of financial statements, prepared in accordance with the Governmental Accounting Standards Board Statement 34, *Basic Financial Statements-and Management's Discussion and Analysis - for State and Local Governments*. The financial statements presented in prior years focused on the accountability of funds, while these statements focus on the financial condition of the University, the results of operations, and cash flows of the University as a whole. The financial statements presented have been prepared using the most current implementation guidelines of the Governmental Accounting Standards Board.

One of the most important questions asked about University finances is, "Is the University as a whole better or worse as a result of the year's activities?" The key to understanding that question is the Statement of Net Assets, the Statement of Revenues, Expenses and Changes in Net Assets, and the Statement of Cash Flows. These statements present financial information in a form similar to that used by corporations. The University's net assets (the difference between assets and liabilities) is one indicator of the University's financial health. Over time, increases or decreases in net assets are indicators of the improvement or erosion of the University's financial health when considered with non-financial facts such as enrollment levels and the condition of the facilities.

The Statement of Net Assets includes all assets (property that we own and what we are owed by others) and liabilities (what we owe to others and have collected from others before we have provided the service). It is prepared under the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided, and expenses and liabilities are recognized when others provide the service to us, regardless of when cash is exchanged.

The Statement of Revenues, Expenses and Changes in Net Assets presents the revenues earned and expenses incurred during the year. Activities are reported as either operating or nonoperating. Because the financial reporting model classifies State appropriations and gifts as nonoperating revenues, a public university's dependency on state aid and gifts will generally result in operating deficits. The utilization of long-lived assets, referred to as Capital Assets, is reflected in the financial statements as depreciation, which amortizes the cost of an asset over its expected useful life.

Another important factor to consider when evaluating financial viability is the University's ability to meet financial obligations as they mature. The Statement of Cash Flows presents information related to cash inflows and outflows summarized by operating, capital, financing, and investing activities.

Statement of Net Assets

The following table reflects the condensed Statement of Net Assets of the University and the Authority.

	University	VCU Health System Authority
Current and other assets	$ 197,542,523	$ 330,741,422
Capital assets - net	369,020,513	247,438,457
Total assets	566,563,036	578,179,879
Current and other liabilities	101,972,146	118,598,631
Long term liabilities	150,707,826	102,930,339
Total liabilities	252,679,972	221,528,970
Net assets:		
Invested in capital assets, net of related debt	235,774,513	165,435,381
Restricted	44,513,529	16,487,808
Unrestricted	33,595,022	174,646,720
Total net assets	$ 313,883,064	$ 356,569,909

For more detailed information see the accompanying Statement of Net Assets.

Six basic transactions affect the Statement of Net Assets:

- The issuance of notes or bonds will increase current assets and increase long-term liabilities.

- Spending note or bond proceeds on capital acquisitions will change the composition of the assets: current assets will decrease and capital assets will increase. Likewise, the classification of net assets changes: Restricted Net Assets will decrease and Invested in Capital Assets, Net of Debt will increase.

- Spending other resources on capital acquisitions will decrease current assets and increase capital assets. A second effect will be the decrease of Unrestricted Net Assets and the increase of Invested in Capital Assets, Net of Debt.
- Principal payments on liabilities will decrease current assets and decrease long-term liabilities. These payments will also increase Invested in Capital Assets, Net of Debt and decrease Unrestricted Net Assets.
- Depreciation expense, which is reflected as an operating expense, will reduce capital assets and Invested in Capital Assets, Net of Debt.
- Operating results, excluding depreciation expense, will affect (increase or decrease) all of the categories other than capital assets and Invested in Capital Assets, Net of Debt.

During fiscal year 2002, University net assets increased $12.3 million. Buildings and equipment, capital assets increased while other assets decreased, as the result of the expenditure of cash converted from investments and capital appropriations on land.

Statement of Revenues, Expenses and Changes in Net Assets

The following is a schedule of the revenues and expenses for the University and the Authority for the current year:

	University	VCU Health System Authority
Operating revenues:		
Student tuition and fees	$ 73,603,341	$ -
Grants and contracts	137,185,745	-
Sales and services of educational departments	7,949,171	-
Auxiliary enterprises	45,674,175	-
Hospital services	17,638,834	678,896,710
Other revenues	30,301,385	-
Total operating revenues	312,352,651	678,896,710
Operating expenses:		
Program activities:		
Instruction	195,292,359	-
Research	92,026,054	-
Public service	6,040,423	-
Supporting services:		
Academic support	47,252,643	-
Student services	9,071,480	-
Institutional support	38,257,610	-
Operations and maintenance of plant	26,565,981	-
Student aid	11,317,322	-
Auxiliary enterprises	33,749,319	-
Hospital services	16,676,470	652,473,785
Depreciation expense	26,169,077	23,644,150
Other expenses	674,682	-
Total operating expenses	503,093,420	676,117,935
Operating gain/(loss)	(190,740,769)	2,778,775

Nonoperating revenues(expenses):		
State appropriations	188,057,625	-
Gifts	16,634,974	-
Investment income (net of investment expense)	626,660	3,553,343
Interest on capital asset-related debt	(6,978,351)	(2,447,228)
Other	-	100,665
Total nonoperating revenues	198,340,908	1,206,780
Income before other revenues and expenses	7,600,139	3,985,555
Additions to permanent endowments	11,614	-
Capital appropriations	1,879,092	-
Capital gifts	1,750,718	78,000
Decrease in beneficial interest in trusts	-	(3,053,196)
Increase in net assets	11,241,563	1,010,359
Net assets – beginning of year	302,641,501	355,559,550
Net assets - end of year	$313,883,064	$356,569,909

Nine basic transactions affect the levels of revenues and expenses.

Revenues:

- Enrollment levels directly affect tuition and fee revenues and auxiliary enterprise sales, services, and fee revenues. The number of potential students, overall economic condition, and acceptance levels at other institutions affect enrollment levels. The mix of on-campus and off-campus students will affect auxiliary enterprise sales and services.

- The Commonwealth of Virginia contributes a significant portion of University revenues through state appropriations and also directs the tuition policy for Virginia undergraduate resident students. Thus, the economic health and budget priorities of the Commonwealth may directly affect revenues.

- The University derives the majority of grant and contract revenues and student financial aid from the Federal Government. As such, changes in Federal budget priorities and award levels may affect sponsored program activities and enrollment levels.

- Investment income is affected by changes in interest rates and the stock market, as well as by the funds available for investing.

Expenses:

- Enrollment levels may directly affect expenses by increasing or decreasing the resources required to support the students.

- The implementation of new programs or additional services within the existing functional expense categories directly affects the level of services.

- The Commonwealth of Virginia establishes salary increases for cost of living and merit pay for classified staff as well as overall increase levels for faculty. Generally, the portion of the increase attributable to state supported activities is funded through state appropriations.

- Federal laws and regulations regarding research activities can require the University to increase the level of support to maintain grant and contract funding.

- Changes in prices caused by inflation or changes in energy prices affect the non-personnel costs of the University. Significant changes in energy prices can require the reallocation of resources from the maintenance of facilities to support increased operating costs during a fiscal year.

Overall operating revenues for the University increased by $20.8 million primarily from increases in Federal grants and contracts. The student head count increased by 994 to 24,915 for the fall semester and credit hours increased 3.9 percent in fiscal year 2002.

The Authority's total revenues increased by 13.5 percent or $80.5 million. This significant increase in revenues resulted from new services, such as the expansion of Virginia Premier, pricing and the mix of hospital services.

While total operating costs of the University increased by less than two percent, the Authority costs increased approximately 12.6 percent or $75.8 million. This is primarily attributable to a $58.0 million increase in medical claims expenses associated with the expansion of Virginia Premier's network. Additional personnel costs of $10 million required to meet market demands and the reduction in selected segments of the workforce contributed to the increase. Depreciation increased as the result of additional investment in capital assets.

Capital Assets

The University has started construction of the Bowe Street Parking Deck and continued the renovation projects in Sanger Hall, West Hospital, and student housing. The projects are either fully funded by state appropriations or will be financed through the Virginia College Building Authority's Pooled Bond Program, which is not dependent on the bond rating of the University. The Authority completed the Gateway Building ($58.0 million), which was funded through the 1998 revenue bond debt issue.

Future Financial Effects

The following are known facts and circumstances that will affect future financial results.

- The Governor of the Commonwealth of Virginia has reduced the state appropriation by 9.8 percent or $15.3 million in fiscal year 2003, and 12 percent or $18.1 million in fiscal year 2004.

- University employees will not receive base salary increases in fiscal year 2003.

- Employees received a one-time 2.5 percent bonus based on their annual salary in fiscal year 2003. In lieu of receiving their bonus in cash, some classified employees may have elected to receive all or part of their bonus as additional paid time-off.

- The Board of Visitors approved a 6.6 percent increase in resident tuition and mandatory fee rates, a 7.5 percent increase in nonresident tuition, and mandatory fees for the fiscal year 2003 and approved a surcharge of $600 per year per student effective with the Spring 2003 semester.

- On November 6, 2002, the University issued a note to the Virginia College Building Authority (VCBA) in the amount of $32,945,000. The proceeds of the note will be used to finance the academic housing project, the Bowe Street Deck project, the renovation of Gladding Residence Hall, and Student Commons Phase III. The note bears interest at rates ranging from 3 percent to 5.25 percent.

VIRGINIA COMMONWEALTH UNIVERSITY
STATEMENT OF NET ASSETS
As of June 30, 2002

	University	VCU Health System Authority
ASSETS		
Current assets:		
Cash and cash equivalents (Note 2)	$ 78,427,124	$ 30,495,045
Short-term investments (Note 2)	12,078,156	13,946,651
Accounts receivable:		
Student, Net of allowance of $1,766,728	5,567,678	-
Sponsors, Net of allowance of $200,000	11,965,099	-
Patient, Net of allowance of $23,050,000	-	72,916,774
Third-party and non-patient	-	44,612,041
Due from VCU Health System Authority	1,264,112	-
Due from Commonwealth of Virginia	1,832,898	-
Appropriations receivable	4,136,868	-
Student loans receivable, current portion	4,121,106	-
Other assets	1,810,552	8,475,074
Total current assets	121,203,593	170,445,585
Noncurrent assets:		
Endowment investments (Note 2)	2,572,230	-
Other investments (Note 2)	50,689,591	148,365,571
Student loans receivable, Net of allowance of $3,587,644	19,312,374	-
Due from VCU Health System Authority	3,007,876	-
Other long-term assets	756,859	11,930,266
Capital assets, Net (Note 4)	369,020,513	247,438,457
Total noncurrrent assets	445,359,443	407,734,294
Total assets	$ 566,563,036	$ 578,179,879
LIABILITIES		
Current liabilities:		
Accounts payable and accrued liabilities	42,879,065	98,439,198
Deferred revenue	23,883,656	-
Due to Virginia Commonwealth University	-	1,264,112
Long-term liabilities - current portion (Note 6)	11,924,192	15,887,445
Total current liabilities	78,686,913	115,590,755
Noncurrent liabilities:		
Deposits	23,285,233	-
Due to Virginia Commonwealth University	-	3,007,876
Long-term liabilities (Note 6)	150,707,826	102,930,339
Total noncurrent liabilities	173,993,059	105,938,215
Total liabilities	252,679,972	221,528,970
NET ASSETS		
Invested in capital assets, net of related debt	235,774,513	165,435,381
Restricted for:		
Nonexpendable:		
Scholarships and fellowships	2,018,526	-
Departmental uses	553,703	16,487,808
Expendable:		
Scholarships and fellowships	7,225,183	-
Research	11,969,213	-
Departmental uses	14,923,791	-
Loans	4,392,619	-
Capital projects	3,430,494	-
Unrestricted	33,595,022	174,646,720
Total net assets	$ 313,883,064	$ 356,569,909

The accompanying Notes to Financial Statements are an integral part of this statement.

VIRGINIA COMMONWEALTH UNIVERSITY
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
As of June 30, 2002

	University	VCU Health System Authority
Operating revenues:		
Student tuition and fees, Net of scholarship allowances of $18,707,315	$ 73,603,341	$ -
Federal grants and contracts	108,075,566	-
State grants and contracts	7,718,179	-
Local grants and contracts	1,336,804	-
Nongovernmental grants and contracts	20,055,196	-
Sales and services of educational departments	7,949,171	-
Auxiliary enterprises:		
Sales and services	28,303,357	-
Student fees, Net of scholarship allowances of $943,022	17,370,818	-
Hospital services	17,638,834	678,896,710
Other revenues	30,301,385	-
Total operating revenues	312,352,651	678,896,710
Operating expenses:		
Instruction	195,292,359	-
Research	92,026,054	-
Public service	6,040,423	-
Supporting services:		
Academic support	47,252,643	-
Student services	9,071,480	-
Institutional support	38,257,610	-
Operations and maintenance of plant	26,565,981	-
Student aid	11,317,322	-
Auxiliary enterprises	33,749,319	-
Hospital services	16,676,470	652,473,785
Depreciation expense	26,169,077	23,644,150
Other expenses	674,682	-
Total operating expenses	503,093,420	676,117,935
Operating gain/(loss)	(190,740,769)	2,778,775
Nonoperating revenues (expenses):		
State appropriations (Note 18)	188,057,625	-
Gifts	16,634,974	-
Investment income, Net of investment expense of $115,465	626,660	3,553,343
Interest on capital asset-related debt	6,978,351)	(2,447,228)
Other	-	100,665
Net nonoperating revenues	198,340,908	1,206,780
Income before other revenues and expenses	7,600,139	3,985,555
Other revenues:		
Additions to permanent endowments	11,614	-
Capital appropriations	1,879,092	-
Capital gifts	1,750,718	78,000
Decrease in beneficial interest in trusts	-	(3,053,196)
Increase in net assets	11,241,563	1,010,359
Net assets - beginning of year	302,641,501	355,559,550
Net assets - end of year	$ 313,883,064	$ 356,569,909

The accompanying Notes to Financial Statements are an integral part of this statement.

VIRGINIA COMMONWEALTH UNIVERSITY
STATEMENT OF CASH FLOWS
For the Year Ended June 30, 2002

	University	VCU Health System Authority
Cash flows from operating activities:		
Tuition and fees	$ 73,317,098	$ -
Grants and contracts	139,295,750	-
Auxiliary enterprise charges	45,578,760	-
Hospital services charges	17,638,834	666,998,612
Payments to suppliers	(135,036,233)	(276,361,687)
Payments to employees	(343,961,688)	(333,481,153)
Loans issued to students	(4,454,795)	-
Collection of loans to students	4,021,693	-
Other receipts (payments)	39,249,396	(3,887,934)
Net cash used by operating activities	(164,351,185)	53,267,838
Cash flows from noncapital financing activities:		
State appropriations	188,057,625	-
Direct lending receipts	89,559,540	-
Direct lending disbursements	(89,559,540)	-
Gifts	16,646,588	-
Virginia Commonwealth University Health System Authority loan repayment	272,246	-
Noncapital long term-debt	(322,830)	-
Net cash provided by noncapital financing activities	204,653,629	-
Cash flows from capital financing activities:		
Proceeds from issuance of note payable	-	23,000,000
State appropriations for capital assets	11,036,637	
Gifts for capital assets	1,750,718	78,000
Purchase of capital assets	(47,251,103)	(54,915,303)
Principal paid on capital-related debt	3,361,726	(5,454,936)
Interest paid on capital-related debt	(6,978,351)	(2,447,228)
Decrease in accrued interest payable	-	(116,239)
Net cash used by capital financing activities	(38,080,373)	(39,855,706)
Cash flows from investing activities:		
Proceeds from sales and maturities of investments	120,015,648	219,126,899
Investment income	3,899,065	3,141,362
Purchases of investments	(123,032,495)	(240,801,621)
Payments received on notes receivable	-	176,512
Other	-	19,667
Net cash provided by investing activities	882,218	(18,337,181)
Net increase (decrease) in cash	3,104,289	(4,925,049)
Cash and cash equivalents - Beginning of year	75,322,835	35,420,094
Cash and cash equivalents - End of year	$ 78,427,124	$ 30,495,045

VIRGINIA COMMONWEALTH UNIVERSITY
STATEMENT OF CASH FLOWS, cont.
For the Year Ended June 30, 2002

RECONCILIATION OF NET OPERATING EXPENSES TO NET CASH USED BY OPERATING ACTIVITIES:		
Operating gain/(loss)	$ (190,740,769)	$ 2,778,775.00
Adjustments to reconcile net gain/(loss) to net cash used by operating activities:		
Depreciation expense	26,169,077	23,644,150
Loss on asset disposition	634,800	-
Provision for uncollectible accounts	(484,676)	42,972,099
Changes in assets and liabilities:		
Receivables	(1,913,206)	(47,612,195)
Other assets	(148,307)	1,128,238
Accounts payable	(3,176,038)	30,963,903
Deferred revenue	3,522,209	-
Compensated absences and deferred compensation	638,578	(607,132)
Deposits	1,147,147	-
Net cash used by operating activities	$ (164,351,185)	$ 53,267,838
Noncash financing transactions:		
Terminated of capital lease, reduction in long-term liabilities	$ 321,999	$ -

The accompanying Notes to Financial Statements are an integral part of this statement.

VIRGINIA COMMONWEALTH UNIVERSITY

NOTES TO FINANCIAL STATEMENTS

AS OF JUNE 30, 2002

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

As one of only three Carnegie Doctoral/Research University-Extensive Universities in Virginia, Virginia Commonwealth University plays a significant role in providing a college-trained workforce, high quality health care, and cultural enrichment for the Richmond area and the Commonwealth.

More than 25,400 undergraduate, graduate, and professional students pursue 162 degree programs on VCU's two campuses: the Academic Campus, situated in the historic Fan District, and the MCV Campus, located two miles east in the commercial and governmental district of downtown Richmond. VCU's one college and eleven schools include the School of Engineering, one of the largest School of Arts in the country, as well as the South's oldest School of Social Work. The University also is the site for the VCU Health System, one of the most comprehensive academic health centers in the nation.

The University's accounting policies conform with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB), including all applicable GASB pronouncements, as well as applicable Financial Accounting Standards Board (FASB) statements and interpretations, Accounting Principles Board opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. The Authority applies all FASB statements and interpretations, Accounting Principles Board opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure issued, unless those pronouncements conflict with or contradict GASB pronouncements. The accompanying financial statements of the University are prepared in accordance with generally accepted accounting principles as prescribed by GASB Statement 34 Basic Financial Statements - and *Management's Discussion and Analysis - for State and Local Governments* and GASB Statement 35, *Basic Financial Statements and Management's Discussion and Analysis of Public College and Universities*. Since the University is a component unit of the Commonwealth of Virginia, it is included in the Comprehensive Annual Financial Report of the Commonwealth.

A. Reporting Entity

The accompanying financial statements include the accounts of all organizational units of Virginia Commonwealth University (University) and the Virginia Commonwealth University Intellectual Property Foundation, a component unit, which is blended (consolidated) with University operations. These statements are presented as stand-alone statements of the University. The Virginia Commonwealth University Health System Authority (VCUHSA) is a discretely presented component unit.

The Virginia Commonwealth University Health System Authority (the Authority) is a public corporate body and political subdivision of the Commonwealth of Virginia created and established by an Act of the General Assembly of the Commonwealth of Virginia during 1996. The Authority is a tax-exempt, not-for-profit organization under the provisions of Internal Revenue Code Section 115.

The Authority's principal activity is the operation of the Medical College of Virginia Hospitals (the Hospitals), University Health Services, Inc. and Subsidiaries (UHS), and MCV Associated Physicians (MCVAP). The Hospitals, a division of the Authority, is an approximately 900-bed teaching hospital, which provides inpatient and outpatient services primarily to patients in the Commonwealth of Virginia. MCVAP, formed in 1991 as a non-stock, not-for-profit charitable educational organization, functions as the group practice plan for those physicians and health care professionals who have faculty appointments in Virginia Commonwealth University (VCU) School of Medicine. Separate financial statements for MCVAP may be obtained from MCVAP's corporate office. The Hospitals, UHS, and MCVAP are included in the enterprise funds of the Authority.

UHS, a component unit of the Authority, is a not-for-profit, non-stock, tax-exempt corporation which was incorporated on January 26, 1995 to support the educational, scientific, and charitable purposes and activities of the University and, in particular, the activities of the Medical College of Virginia/Virginia Commonwealth University (MCV/VCU) and the Hospitals. These activities include, but are not limited to, activities undertaken pursuant to Section 23-50.16B of the Code of Virginia. UHS is a blended component unit of the Authority due to the significance of the operational and financial relationship between the two entities. Virginia Premier Health Plan, Inc. (VA Premier) is a wholly owned subsidiary of UHS. VA Premier is a for-profit health maintenance organization (HMO) whose primary purpose is to provide quality health care within a managed care framework. The accounts of VA Premier are included in the consolidated financial statements of UHS. Separate consolidated financial statements for UHS may be obtained from UHS's corporate office.

The University also benefits from a number of organizations that exist mainly to support the various purposes and activities of the University and Authority. The assets of these affiliated organizations, which are separately incorporated and managed by their own Boards, are not included in these statements. The affiliated organizations are listed below and are described in Note 8:

VCU Foundation	Medical College of Virginia Foundation
VCU Real Estate Foundation	MCV/VCU Dental Faculty Practice Association
Virginia Biotechnology Research Park Authority	Virginia Commonwealth University School of Engineering Foundation
Virginia Commonwealth University Alumni Association	Medical College of Virginia Alumni Association of VCU

B. Basis of Accounting

The financial statements of the University have been prepared on the accrual basis. Under the accrual basis, revenues are recognized when earned, expenses are recorded when a liability is incurred, regardless of the timing of related cash flows, and depreciation expense relating to capitalized fixed assets is included. Revenues for the summer term are prorated on the basis of student class days occurring before and after June 30.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

C. Investments

Investments are reported at market, if purchased, or fair value (market) at the date of receipt, if received as a gift. Investments held in the liquidity fund (securities with a maturity of less than one year) of the University are reported as current assets with the remaining investments reported as noncurrent assets.

D. Inventories

Inventories are valued at the lower of cost (generally determined on the first-in, first-out method) or market.

E. Restricted Resources

The Authority's investment balances include resources restricted for debt service under a bond indenture agreement, resources restricted under malpractice trust agreement, resources restricted by insurance regulations of the Commonwealth of Virginia, and resources restricted under the pension plan agreement.

Restricted resources limited by donors to a specific period or purpose are reported as restricted net assets. The Authority restricted net assets consist principally of beneficial interests in perpetual trust funds established by split interest agreements. Split interest agreements are trust agreements established by donors under which the Authority receives benefits that are shared with other beneficiaries. The trust agreements established by donors provide for a third party to hold the trust assets. These trusts do not permit donors to revoke their charitable contributions. Trust assets of $16,466,000, which are restricted by donors for the Authority in perpetuity, are reported at fair value, which approximates the present value of the future cash receipts from the trust assets.

F. Investment Income

Investment income, including net realized and unrealized gains or losses on investment transactions, is recorded as nonoperating revenue, and investment transactions of restricted funds are added to the fund that owns the investment. This income is restricted primarily for indigent care.

G. Accrued Compensated Absences

University full-time classified, part-time classified, and faculty employed on or after January 1, 1999 who are also active members of the Virginia Retirement System (VRS) are covered under the "Virginia Sickness and Disability Program" (VSDP). The plan provides for sick leave, family and personal leave, short-term disability benefits, and long-term disability benefits. Full-time classified, part-time classified, and faculty employed prior to January 1, 1999, who are active members of VRS, participate in VSDP under one of two options or remain under the traditional sick leave program in which classified employees and twelve month faculty earn five hours of leave each pay period regardless of the length of state service and nine month faculty accrue 48 hours per semester. One VSDP option permitted eligible employees to convert accumulated sick leave balances to short-term disability credits. The other allowed for the conversion of sick leave balances to VRS service credit. The University was not required to currently fund the cost of conversion to VRS service credit. Enrollment in the VSDP is irrevocable, and no additional enrollments are planned. Under VSDP, unused VSDP sick leave and family and personal leave balances do not carry forward from one year to the next, and employees are not paid for unused balances upon termination. The converted short-term disability credits of classified employees are payable upon termination in accordance with the Commonwealth of Virginia's sick leave payout policy discussed below. Faculty who converted sick leave balances to short-term disability credits are not compensated for these balances at termination.

Full-time and part-time twelve-month faculty and classified employees earn annual leave based upon the number of years of continuous state service. Faculty may carry forward up to 384 hours of annual leave from one year to the next and classified employees may carry forward up to 432 hours of annual leave. Upon termination, unused annual leave balances of up to 288 hours for faculty and up to 336 hours for classified staff are paid in full. The liability recorded in the financial statements is limited to the amount of payment received at termination.

Employees who are not subject to the overtime provisions of the Fair Labor Standards Act may be eligible to earn compensatory leave. Leave is earned on an hour-for-hour basis for having worked additional hours in a workweek, holidays, or scheduled days off. Compensatory leave may be used for paid time off and is payable upon termination. Accrued compensatory leave lapses within 12 months from the date it is earned and once lapsed may not be used or paid upon termination.

The University records a liability for all unused annual, non-VSDP sick, and compensatory leave and unused short-term disability credits as well as related fringe benefits. Annual and compensatory leave balances are paid in full upon termination. Non-VSDP sick leave and short-term disability credits are payable upon employment termination and are limited to 25 percent of the value accumulated or $5,000, whichever is less, under the Commonwealth of Virginia's sick leave pay-out policy for employees with 5 or more years of service.

The Authority records a liability for all paid time off and related FICA taxes expected to be paid.

H. Capital Assets

Capital assets are stated at cost or, if donated, at fair market value on the date of acquisition. Equipment costing $5,000 or more with a useful life of two or more years is capitalized, except for assets acquired under the Higher Education Equipment Trust Fund, which are capitalized at $500 as required by the State Council of Higher Education. Infrastructure assets are included in the financial statements and are depreciated. The

University and the Authority record depreciation on property, plant and equipment, including capital leases and excluding land and construction in progress, computed over the estimated useful lives of the assets based on the straight-line method. The general range of estimated useful lives for the University and the Authority is 10 to 40 years for buildings and fixtures, 5 to 20 years for equipment, 5 years for library books, and 10 to 25 years for land improvements and infrastructure. Expenditures for construction in progress are capitalized as incurred and reflected in net investment in plant. Interest expense relating to construction is capitalized net of interest income earned on resources set aside for this purpose. Capital assets at the time of disposal revert to the Commonwealth of Virginia for disposition.

I. Hospital Services

In addition to the services provided by the Authority to patients, the University provides facilities, graduate medical education, clinical support, and administrative support to hospitals. The revenues and expenditures necessary to provide the services are classified as hospital services.

J. Charity Care

The Authority provides care to patients who meet certain criteria under its indigent care policy without charge or at amounts less than its established rates. Because the Authority does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. The costs and expenses incurred in providing these services are included in operating expenses. Charges written off to charity care for the year ended June 30, 2002, measured at established rates, approximated $154,171,000 (see Note 16).

K. Net Patient Service Revenue

Net patient service revenue is reported in hospital services at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, and includes estimated retroactive adjustments due to future audits, reviews, and investigations.

Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered, and such amounts are adjusted in future periods as adjustments become known or as years are no longer subject to such audits, reviews, and investigations.

A summary of the payment arrangements with major third-party payors follows:

- *Trigon*. Inpatient acute care services rendered to Trigon subscribers are paid at a per diem rate or discounted rate. Outpatient services rendered to Trigon subscribers are reimbursed at discounted rates or applicable fee schedule. The rates are not subject to retroactive adjustment.

- *Medicare*. Inpatient acute care services and defined capital costs rendered to Medicare program beneficiaries are paid at prospectively determined rates per discharge. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors. Inpatient nonacute services, certain outpatient services, and education related to Medicare beneficiaries are paid based on prospectively determined rates and a discounted cost reimbursement methodology. The Authority is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the Authority and audits thereof by the Medicare fiscal intermediary. The Authority's Medicare cost reports have been audited by the Medicare fiscal intermediary through June 30, 2000.

- *Medicaid*. Inpatient acute care services rendered to Medicaid program beneficiaries are paid at a per diem rate. Outpatient services rendered to Medicaid program beneficiaries are reimbursed on prospectively determined rates and a cost reimbursement methodology. In addition to inpatient and outpatient services provided to Medicaid program beneficiaries, Medicaid reimburses the Authority for services provided to indigent patients up to an amount which results in total Medicaid and indigent reimbursement to the Authority of $180 million in 2002. The Authority's Medicaid cost reports have been audited by the Medicaid program representative through June 30, 2000.

In accordance with the third-party payor agreements, the difference between payment for services and the Authority's standard billing rates results in contractual adjustments. Contractual adjustments are recorded as deductions from patient service revenue in the period in which the related services are rendered. The annual settlements of reimbursement for patients' services covered by third parties are determined through cost reports for Medicare (for outpatient and educational costs) and Medicaid. The settlements are subject to audit and retroactive adjustment by these third parties.

Provisions for possible adjustments of cost reports have been estimated and reflected in the accompanying financial statements as considered appropriate. The difference in any year between the originally estimated amount and the final determination is reported in the year of determination as an adjustment to net patient service revenue. Net patient service revenue was decreased by approximately $7,200,000 in 2002, as a result of such settlements.

L. Premiums Earned

VA Premier has contracts with the Virginia Department of Medical Assistance Services (DMAS) wherein VA Premier provides health care services to the Aid for Families with Dependent Children (AFDC), the Children's Medical Services Insurance Plan (CMSIP) and Aged, Blind, and Disabled (ABD) residents of Virginia through a health maintenance organization (HMO). VA Premier recognizes premiums received from DMAS for members in the period to which health care coverage relates. All of VA Premier's premiums were earned from contracts with DMAS.

M. Uncollectible Accounts

A provision for uncollectible accounts is recorded during the period in which collection is considered doubtful.

N. Estimated Medical Claims Payable

VA Premier provides for the liability arising from services rendered to HMO members, but unpaid at year-end based upon the experience of VA Premier and cost-per-member trends. Although considerable variability is inherent in such estimates, management believes that the liability is adequate. Any required revisions to these estimates are reflected in operations of the period in which such revisions are determined.

O. Net Assets

GASB Statement 34 requires that the Statement of Net Assets report the difference between assets and liabilities as net assets, not fund balances. Net assets are classified according to external donor restrictions or availability of assets for satisfaction of obligations. Invested in capital assets net of related debt represents the net value of capital assets (property, plant and equipment) less the debt incurred to acquire or construct the asset. Nonexpendable restricted net assets are gifts that have been received for endowment purposes, the corpus of which cannot be expended. Expendable restricted net assets represent gifts that have been received for specific purposes. Unexpended appropriations for capital projects are included in expendable restricted net assets as they are not available for general operating purposes.

In connection with the implementation of GASB Statements 34 and 35, the following adjustment was made to reflect the cumulative effect of this accounting change:

Fund Balances reported at June 30, 2001	$599,249,712
Accumulated depreciation on capital assets at June 30, 2001, not previously recorded	(264,995,690)
Reclassification of grant and contract review	(13,841,186)
Reclassification of Federal Loan Programs	(20,939,980)
Summer school adjustment	3,168,645
Net Assets at July 1, 2001	$302,641,501

P. Scholarship Allowances and Student Aid

Financial aid to students is reported in the financial statements under the alternative method as prescribed by the National Association of College and University Business Officers (NACUBO). Certain aid (loans, funds provided to students as awarded by third parties and Federal Direct Lending) is accounted for as third party payments (credited to the student's account as if the student made the payment). All other aid is reflected in the financial statements as operating expenses or scholarship allowances, which reduce revenues. The amount reported as operating expense represents the portion of aid that was provided to the student in the form of cash. Scholarship allowances represent the portion of aid provided to the student in the form of reduced tuition. Under the alternative method, these amounts are computed on a total university basis by allocating the cash payments to students, excluding payments for services, on the ratio of all aid to the aid not considered to be third party aid.

Q. Intangibles

The Authority's prepaid expenses and other assets include $4,424,899 of goodwill. On January 1, 2002, (beginning of VA Premier's fiscal year) the Authority early adopted Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets*, which requires that goodwill is no longer amortized, but is reviewed annually for impairment.

R. Revenue and Expense Classifications

Operating revenues include activities that have the characteristics of exchange transactions, such as: (1) student tuition and fees, net of scholarship discounts and allowances; (2) sales and services of auxiliary enterprises, net of scholarship allowances; and (3) federal, state, and nongovernmental grants and contracts.

Nonoperating revenues include activities that have the characteristics of nonexchange transactions, such as gifts, and other revenue sources that are defined as nonoperating revenues by GASB Statement 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*, and GASB Statement 34, such as state appropriations and investment and interest income.

Nonoperating expenses include interest on debt related to the purchase of capital assets and losses on the disposal of capital assets. All other expenses are classified as operating expenses.

2. CASH AND INVESTMENTS

Cash

All cash is maintained in accounts collateralized in accordance with the Virginia Security for Public Deposits Act, Section 2.1-359 et seq. of the Code of Virginia or covered by federal depository insurance.

Investments

The University's non-state funds, other than endowment and funds internally designated to function as an endowment, are managed by professional investment managers. The University's investment objective is to ensure the preservation of capital with sufficient liquidity to meet operating expenditure requirements. The investment policy of the University is established by the Board of Visitors and is monitored by its Finance, Investment, and Property Committee. Investment managers may invest in the following types of investments: direct obligations of the United States, obligations unconditionally guaranteed by the United States, collateralized mortgage obligations, obligations of any agency or instrumentality of the United States, certificates of deposit and bank notes of domestic banks, banker's acceptances, commercial paper issued by domestic corporations, money market funds, corporate notes of domestic corporations, fully hedged debt obligations of sovereign governments and companies, obligations of the Commonwealth of Virginia, asset backed securities with AAA ratings, and negotiable certificates of deposit and negotiable bank notes of domestic banks. The allocation of assets at June 30, 2002, is three percent high-quality cash equivalents with maturities of less than one year and 97 percent high quality fixed income securities.

In accordance with Bond Resolutions adopted by its Board of Directors, the Authority can invest assets held with trustees in the following instruments: obligations of federal agencies or those guaranteed by the United States of America, savings accounts, certificates of deposit, time deposits, and obligations of the Commonwealth of Virginia.

The University's investments that are represented by specific identifiable investment securities are classified as to the level of risk assumed at year-end. Category 1 includes investments that are insured or registered or for which the securities are held by the University or its agents in the University's name. Category 2 includes uninsured and unregistered investments for which the securities are held in the broker or dealer's trust department or safekeeping agent in the University's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the broker or dealer, or by its trust department or safekeeping agent, but not in the University's name. All of the University's investments are categorized as Category 1.

For management purposes, endowment funds and funds internally designated to function as an endowment, are held in the investment pools of the VCU Foundation, the VCU Real Estate Foundation, or the MCV Foundation. These funds remain the property of the University. The investment pools consist of cash equivalents, bonds, preferred and common stocks, and real estate. The University's equity in the investment pools is based on units or shares in the investment pools. Consequently, funds held by the foundations are not categorized as to the level of risk.

Investments are reported at fair value (market). Categorization of investments is as follows:

	Category 1	Fair Value	Cost
University Investments:			
U.S. Government and U.S. Government Agency securities	$ 22,975,581	$ 22,975,581	$ 22,732,148
Corporate bonds	12,646,566	12,646,566	12,345,439
Commercial paper	199,864	199,864	199,075
Municipal bonds	123,206	123,206	111,808
Subtotal	35,945,217	35,945,217	35,388,470
Mutual and money market funds	-	2,893,446	2,893,446
Investments held by the Treasurer of Virginia - Securities Loans	-	707,377	707,377
Investments held by the VCU Intellectual Property Foundation	-	774,676	171,645
Investment pools held by:			
VCU Foundation	-	19,571,741	18,752,611
VCU Real Estate Foundation	-	1,000,000	1,000,000
MCV Foundation	-	4,447,520	3,133,144
Total University investments	$ 35,945,217	$ 65,339,977	$ 62,046,693

Authority Investments:			
Cash and cash equivalents	$ 16,567,827	$ 16,567,827	$ 16,533,560
Money Market instruments	2,101,872	2,101,872	2,081,249
U.S. Government and U.S. Government			
Agency securities:	52,647,691	52,647,691	51,661,076
Corporate bonds	19,019,591	19,019,591	18,602,658
Commercial paper	12,462,646	12,462,646	12,404,163
Interest receivable	624,109	624,109	624,109
Mutual funds	4,559,362	4,559,362	5,614,500
Equity securities	13,674,643	13,674,643	14,138,502
Total	121,657,741	102,988,042	103,045,008
Externally restricted:			
Cash and cash equivalents	23,567,468	23,567,468	23,567,468
U.S. Government and U.S. Government			
Agency securities	599,295	599,295	599,420
Commercial paper	21,705	21,705	21,705
Total	24,188,468	24,188,468	24,188,593
Beneficial interest in trust	-	16,466,013	16,466,013
Total Authority investments	$181,791,426	$162,312,222	$162,314,423

3. JOINT VENTURES AND EQUITY INVESTMENTS

UHS has become a joint venture partner with several organizations with net investments totaling approximately $4,910,000. Individual financial statements for each of the investments are available from UHS's corporate office. The investments are noted below.

Investment in Ownership Interest in Land and Buildings.

Included in other long term assets on the accompanying statement of net assets is a $978,000 investment representing a 25 percent interest in land and buildings owned by the VCU Real Estate Foundation (VCUREF). VCUREF is leasing the property in its entirety to VCU and the Hospitals to allow for consolidation of off-campus leases to a site closer to the VCU campus. A portion of the lease payments earned on the property are paid to UHS as a return on its investment. UHS accounts for this investment using the cost method of accounting. When the buildings are needed in the future for the Virginia Biotechnology Research Park, they will be sold to the Virginia Biotechnology Research Park Authority. The purchase price will be determined at the time of sale based upon appraisals received for the properties and negotiations between the VCU Real Estate Foundation and the purchaser.

Investment in Richmond Medical Commons, L.L.C.

UHS and the Richmond Eye & Ear Healthcare Alliance (REEH) entered into a joint venture agreement on July 31, 1995 for the purpose of constructing and operating an ambulatory surgery center and related facility. As part of the joint venture agreement, UHS invested $100,000 in Richmond Medical Commons, L.L.C. (RMC), a Virginia limited liability company. On August 27, 1996, UHS's investment in RMC was reduced to $40,000 when UHS sold three-fifths of its interest in RMC to an outside third party. On September 30, 1999, UHS purchased an additional 30 percent interest in RMC. UHS's interest is included in other long term assets on the accompanying statement of net assets. UHS contributed $3,240,000 to RMC in 2002. The investment in RMC of approximately $3,500,000 is accounted for under the equity method of accounting. UHS is a guarantor, along with REEH, of a six-year lease for RMC with aggregate payments totaling approximately $4,770,000.

Investment in 7th and Marshall Corporation

Included in other long term assets on the accompanying statement of net assets is a capital contribution to 7th and Marshall Corporation of $500,000. UHS and Hospital Hospitality House, Inc. are the sole members of the 7th and Marshall Corporation, a not-for-profit corporation formed to support the charitable, educational and scientific activities of UHS and Hospital Hospitality House, Inc. The investment in 7th and Marshall Corporation is accounted for under the equity method of accounting. The investment is carried at $409,000.

Investment in Commonwealth Care of Virginia LLC

On September 25, 1997, Commonwealth Care of Virginia LLC (CCV), an independent practice association, amended and restated its operating agreement for the purpose of permitting the admission of UHS as a Class P member. Under the terms of the agreement, as of September 25, 1997, the notes receivable from CCV of $458,511, the related accrued interest receivable of $76,447, and an additional investment of $194,042 by UHS on September 25, 1997 in CCV were converted into 729 shares of Class P membership interests of $729,000. The Class P membership interest is entitled to a quarterly preferred distribution of an amount equal to the prime rate of interest plus one percent times UHS's membership interests. The preferred distribution is deferred under certain conditions and is required to be paid before any bonus, withhold, holdback or similar pool distribution. The agreement also has provisions for sharing 20 percent of sales proceeds with UHS in the event CCV experiences a change in control and options to buy back UHS membership interests if certain levels of income are achieved. The investment in CCV is accounted for under the cost method of accounting. A valuation allowance of $729,000 is recorded for the investment in CCV.

4. CAPITAL ASSETS

Capital asset activity for the year was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance
University:				
Land	$ 21,413,359	$ 1,772,782	$ -	$ 23,186,141
Land improvements and infrastructure	11,008,732	2,144,589	-	13,153,321
Buildings	369,767,334	55,474,303	517,190	424,724,447
Equipment	99,176,435	12,111,388	6,554,468	104,733,355
Library books	70,788,753	4,313,388	-	75,102,141
Construction in progress	41,736,363	29,127,270	57,693,803	13,169,830
Total cost of capital assets	613,890,976	104,943,720	64,765,461	654,069,235
Less accumulated depreciation for:				
Land improvements and infrastructure	6,059,877	810,257	-	6,870,134
Buildings	134,127,327	11,468,088	299,644	145,295,771
Equipment	66,000,128	9,115,604	5,816,402	69,299,330
Library books	58,808,359	4,775,128	-	63,583,487
Total accumulated depreciation	264,995,691	26,169,077	6,116,046	285,048,722
Total University capital assets - net	$348,895,285	$ 78,774,643	$ 58,649,415	$369,020,513
Authority:				
Land	$ 4,150,782	$ -	$ 1,467,534	$ 2,683,248
Buildings	198,935,665	79,827,597	20,851,135	257,912,127
Equipment	173,990,405	8,690,640	835,465	181,845,580
Construction in progress	67,271,235	47,457,801	79,986,882	34,742,154
Total cost of capital assets	444,348,087	135,976,038	103,141,016	477,183,109
Less accumulated depreciation for:				
Buildings	103,006,342	9,169,961	21,261,455	90,914,848
Equipment	125,752,460	13,896,169	818,825	138,829,804
Total accumulated depreciation	228,758,802	23,066,130	22,080,280	229,744,652
Total Authority capital assets - net	$215,589,285	$112,909,908	$ 81,060,736	$247,438,457

5. VIRGINIA COMMONWEALTH UNIVERSITY FACULTY EARLY RETIREMENT INCENTIVE PLAN

The University established the Virginia Commonwealth University Faculty Supplemental Retirement Plan for Faculty (Plan) to provide a financial early retirement incentive for certain tenured faculty that will facilitate the release of tenured faculty resources for budget reallocation or reduction in accordance with the University Strategic Plan goals, changes in enrollment, and other University needs. Tenure is a permanent appointment granted to associate professors and professors, which continues until the faculty member leaves the University, is dismissed for cause, or is terminated due to a financial crisis.

The Plan provides an annuity for five years from the date of retirement equal to 20 percent of the average University salary of the faculty members eligible to participate in the Plan, not to exceed 30 percent of the participant's base annual salary from University resources at the time the agreement was signed. In addition, the University provides a health care benefit supplement until the participant becomes Medicare eligible (currently age 65) if the participant retires, or up to 18 months of COBRA benefits if the participant does not retire.

Thirty-one faculty members were enrolled in the Plan. Payments during the fiscal year were $421,989. The present values of future Plan payments included in long-term liabilities are as follows:

Fiscal Year	Plan Obligations
2003	$ 496,558
2004	534,092
2005	520,251
2006	353,231
2007	164,500
Later Years	19,651
Total	$2,088,283

6. LONG-TERM LIABILITIES

Long-term liabilities of the University consist of bonds, notes payable, capital leases, installment purchases, deferred compensation, and compensated absences.

Commonwealth Revenue Bonds

The Commonwealth of Virginia issues bonds for agencies and institutions of the Commonwealth. The University has received a portion of the proceeds to fund capital construction. The University recognizes a liability associated with its share of the bonds and remits principal and interest payments related to this liability to the Treasurer of Virginia. The General Revenue Pledge Bonds (Section 9d Bonds) carry interest rates of 4.25 percent - 5.75 percent and are due through 2021. The Commonwealth of Virginia Revenue Bonds (Section 9c Bonds) carry interest rates of three percent to eight percent and are payable through 2017. Of the total Commonwealth of Virginia Revenue Bonds, outstanding bonds payable in the amount of $3,356,397, which will be repaid by the Authority as described in Note 12, are not considered capital asset related debt.

Virginia College Building Authority

The Virginia College Building Authority (VCBA) issues Educational Facilities Revenue Bonds (Public Higher Education Financing Program). As a participating institution in this program, the University issued a note payable to the VCBA. This note, along with the notes of other institutions, is held by the VCBA as security for the Educational Facilities Revenue Bonds. For accounting purposes, the financing arrangement is considered to represent a note payable. The notes have interest rates of 3.15 percent to 6 percent.

The University participates in the Higher Education Equipment Trust Fund of the VCBA, an agency of the Commonwealth of Virginia. The Higher Education Equipment Trust Fund provides funds to public colleges and universities for equipment acquisition. Prior to 1999, funds were provided in the form of a lease. For accounting purposes, the financing arrangement for the outstanding debt is considered to represent a capital lease with imputed interest rates of 7.26 percent to 8.39 percent.

The University participates in a temporary financing program with the Department of Treasury to fund the construction of various capital projects prior to the issuance of bonds payable or notes payable to the VCBA. The amount outstanding at the end of the year is classified as a long-term liability in anticipation of the issuance of long-term notes to the VCBA.

Virginia Public Building Authority

The University participates in a financing arrangement with the Virginia Public Building Authority for the construction of a steam plant adjacent to the MCV campus. The University considers this financing arrangement to be a capital lease with imputed interest rates of 2.25 percent to 5.85 percent.

Virginia Biotechnology Research Park Authority

As more fully described in Note 8, the University occupies space owned by the Virginia Biotechnology Research Park Authority. For accounting purposes, this arrangement is considered to be a capital lease with an imputed interest rate of 9 percent.

Defeasance of Debt

In prior fiscal years, a portion of the Commonwealth of Virginia Revenue Bonds, of which the University has a share, has been defeased. Details relating to the prior years' defeasances are reported in the Comprehensive Annual Financial Report of the Commonwealth.

Changes in Long-Term Liabilities

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
University:					
Bonds payable:					
General Revenue Pledge Bonds	$ 51,240,000	$ -	$ 1,945,000	$ 49,295,000	$ 2,039,999
Commonwealth of Virginia Revenue Bonds	31,637,955	-	3,075,254	28,562,701	2,712,674
Total bonds payable	82,877,955	-	5,020,254	77,857,701	4,752,673
Notes payable:					
Virginia College Building Authority	25,730,000	-	790,000	24,940,000	920,000
Capital leases:					
Virginia College Building Authority	3,180,347	-	2,216,049	964,298	964,298
Virginia Public Building Authority	14,299,471	-	758,844	13,540,627	798,359
Virginia Biotechnology Research Park Authority	4,881,825	-	448,548	4,433,277	170,046
Total capital leases	22,361,643	-	3,423,441	18,938,202	1,932,703
Installment purchases	2,943,270	-	1,912,185	1,031,085	281,082
Total long-term debt	133,912,868	-	11,145,880	122,766,988	7,886,458
Compensated absences	23,520,631	18,500,000	18,106,663	23,913,968	3,541,176
Treasury Loans	516,481	13,346,298	-	13,862,779	-
Deferred compensation	1,843,042	586,334	341,093	2,088,283	496,558
Total University	$159,793,022	$32,432,632	$29,593,636	$162,632,018	$11,924,192
Authority:					
General Revenue Pledge Bonds	$ 82,260,000	$ -	$ 5,470,000	$ 76,790,000	$ 5,695,000
Capital leases	972,818	-	517,256	455,562	175,773
Installment purchases	545,969	1,220,813	365,664	1,401,118	499,486
Total long-term debt	83,778,787	1,220,813	6,352,920	78,646,680	6,370,259
Estimated losses on malpractice claims	27,212,052	1,272,620	2,421,905	26,062,767	1,000,000
Compensated absences	14,715,470	1,066,838	1,673,971	14,108,337	8,517,186
Total Authority	$125,706,309	$ 3,560,271	$10,448,796	$118,817,784	$15,887,445

Long-term debt matures as follows:

Fiscal Year	Revenue Bonds	Notes Payable	Capital Leases	Installment Purchases	Total
University:					
2003	$ 4,752,674	$ 920,000	$ 1,932,702	$ 281,082	$ 7,886,458
2004	5,054,389	945,000	1,027,367	281,880	7,308,636
2005	4,254,832	990,000	1,090,781	231,469	6,567,082
2006	4,216,745	1,030,000	1,159,195	235,218	6,641,158
2007	4,438,349	1,075,000	1,233,426	1,436	6,748,211
Later Years	55,140,712	19,980,000	12,494,731	-	87,615,443
Total	$77,857,701	$24,940,000	$18,938,202	$1,031,085	$122,766,988
Authority:					
2003	$ 5,695,000	$ -	$ 175,773	$ 499,486	$ 6,370,259
2004	8,010,000	-	279,789	507,041	8,796,830
2005	2,080,000	-	-	223,472	2,303,472
2006	2,175,000	-	-	67,757	2,242,757
2007	2,270,000	-	-	68,088	2,338,088
Later Years	56,560,000	-	-	35,274	56,595,274
Total	$76,790,000	$ -	$ 455,562	$1,401,118	$ 78,646,680

7. RETIREMENT, PENSION PLANS, AND POST EMPLOYMENT BENEFITS OTHER THAN PENSION BENEFITS

University

Substantially all full-time classified salaried and certain full-time faculty employees of the University participate in the defined benefit retirement plan administered by the Virginia Retirement System (VRS). The VRS is an agent multiple-employer public employee retirement system (PERS) that acts as a common investment and administrative agency for the Commonwealth of Virginia and its political subdivisions.

The long-term disability benefit provided by the "Virginia Sickness and Disability Program" (VSDP) is administered by VRS. Funding for this benefit has been incorporated into the VRS contribution shown below.

The University's payroll costs for the year, excluding accrued payroll, for employees covered by the VRS were $131,266,522. The University's total payroll costs for the year were $275,815,754.

Information regarding types of employees covered, benefit provisions, employee eligibility requirements including eligibility for vesting, and the authority under which benefit provisions as well as employer and employee obligations to contribute is established and disclosed in the Comprehensive Annual Financial Report of the Commonwealth of Virginia.

The University's total VRS contributions were $9,766,502 for the year, which included the 5 percent employee contribution assumed by the employer. These contributions represent 7.4 percent of covered payroll.

The VRS does not measure assets and pension benefit obligations separately for individual state institutions. The Comprehensive Annual Financial Report of the Commonwealth of Virginia provides disclosure of the Commonwealth's unfunded pension benefit obligation. The same report contains historical trend information showing VRS's progress in accumulating sufficient assets to pay benefits when due.

Full-time faculty and certain administrative staff are eligible to participate in other retirement plans. These are fixed-contribution programs where the retirement benefits received are based upon the employer, 5.4 percent, and employee, 5 percent, contributions (all of which are paid by the University) plus interest and dividends.

Individual contracts issued under the plans provide for full and immediate vesting of both the University's and the employee’s contributions. Total pension costs under these plans were $9,727,352 for the year. Contributions to other retirement plans were calculated using the base salary $93,532,235 for the year.

The state participates in the VRS administered statewide group life insurance program, which provides post employment life insurance benefits to eligible retired and terminated employees. The state also provides health care credits against the monthly health insurance premiums of its retirees who have at least 15 years of state service and participate in the state health plan. Information related to these plans is available at the statewide level in the Comprehensive Annual Financial Report of the Commonwealth.

The Deferred Compensation Program (DCP) gives eligible Participants (employees with at least 12 consecutive months of salaried state service and who are making continuous deferrals of at least $20 per pay period to a 403(b) retirement plan) a maximum of $20 per pay period in matching Deferring Compensation savings.

Authority

Prior to July 1, 1997, employees of the Authority were employees of the Commonwealth of Virginia (the Commonwealth). These employees are eligible to participate in a defined benefit pension plan administered by the Virginia Retirement System (VRS). The VRS also administers life insurance and health-related plans for retired employees. Information relating to these plans is available at the statewide level only in the Commonwealth of Virginia’s Comprehensive Annual Financial Report. The Commonwealth, not the Authority, has overall responsibility for these plans. Total pension costs for the year were approximately $3,880,000.

Effective July 1, 1997, the Authority established the Virginia Commonwealth University Health System Authority Defined Contribution Plan (the Plan). All employees working at least 35 hours of service per week are eligible to participate in the Plan. Per the Plan document, as approved by the Authority’s Board of Directors, the Authority contributes up to eight percent of the participant’s salary to the Plan, up to a maximum of $30,000. Total contributions to the Plan for the year were approximately $6,319,000. The Authority shall have the right at anytime, and without the consent of any party, to terminate the Plan in its entirety. Any changes to the provisions of the Plan, including the contribution requirements, must be approved in writing by the Authority's Board of Directors.

The Authority has also established the Virginia Commonwealth University Health System Authority Health Care Providers Defined Contribution Plan (the HCP Plan). All persons hired as a health care provider on or after July 1, 1993 and prior to July 1, 1997 and working at least 35 hours of service per week are eligible to participate in the HCP Plan. All significant provisions of the HCP Plan, including the contribution requirements, are similar to the Plan. Total contributions to the HCP Plan for the year were approximately $116,000.

The Plan and the HCP Plan use the accrual basis of accounting and the Plan assets, which consist of mutual funds, are carried at fair market value. The fair market values of the mutual funds are based on quoted market prices, if available, or estimated using quoted market prices for similar securities. Individual organizations that hold 5 percent or more of the assets are:

Fidelity Investments	$14,970,527
TIAA/CREF	11,687,388
VALIC (Variable Annuity Life Insurance Co.)	3,553,733
Net assets available for plan benefits	30,211,648
Beginning net assets available for plan benefits	29,770,863
Pension contributions	5,604,113
Investment loss	(1,477,759)
Pension benefit payments	(3,685,569)
Ending net assets available for plan benefits	$30,211,648

MCVAP sponsors the MCVAP 403(b) Retirement Fund (the 403(b) Plan), which includes a defined contribution plan covering substantially all non-medical employees of MCVP and a salary reduction plan, which represents employee contributions. MCVAP's contribution to the 403(b) Plan (7.5 percent of participant's compensation) combined with the employee's salary reduction amounts approximated $1,764,000 for the year.

MCVAP sponsors the MCVAP 401(a) Retirement Plan (the 401(a) Plan), a noncontributory, defined contribution plan which covers substantially all full-time clinical provider employees of MCVAP. Contributions to the 401(a) Plan by MCVAP, as determined annually at the discretion of the Board of Directors, were approximately $3,850,000 for the year.

MCVAP sponsors the VCUHS 401(a) Retirement Plan (the VCUHS 401(a) Plan), a defined contribution plan which covers all non-medical employees of MCVP and the VCUHS 457(b) Retirement Plan (VCUHS 457(b) Plan), a salary reduction plan that represents employee contributions. These plans became effective on January 1, 2002 and replaced the MCVAP 403(b) plan for all non-medical staff. The 401(a) Plan contributions are a function of the employee's age plus years of service per the table below. MCVAP employees may contribute to the VCUHS 457(b) Salary Reduction Plan. Employees may also receive a two percent matching contribution in their VCUHS 401(a) Plan based on their 457(b) salary reduction contribution.

Age + Years of Service	Employer Contribution (401(a) Plan)
65+	10%
55 – 65	8%
45 – 55	6%
35 – 45	4%
<35	2%

The contributions to the VCUHS 401(a) Plan and the VCUHS 457(b) Plan for the period January 1, 2002 through June 30, 2002 were approximately $1,312,000.

Effective August 1, 1999, VA Premier adopted a 401(k) plan sponsored by Prudential Mutual Fund Management, Inc. Employees may enter into the plan on the first day of the month coinciding with or following the date on which the employee begins employment. There is no minimum service or age requirement to be in the 401(k) plan. Employees may contribute 1 percent to 15 percent of their compensation. VA Premier will match 50 percent of the employees' contributions up to 4 percent of the employees' compensation. Matching will occur based on the bi-weekly pay periods. In addition, VA Premier contributes 3 percent of the employee's compensation after each bi-weekly payroll, effective when the employee begins employment. Employees are fully vested after four years of service in which the employees have at least 1,000 hours of service each year. The total expense to VA Premier was approximately $218,000.

8. RELATED PARTIES

The financial statements do not include the assets, liabilities, or fund balances of affiliated organizations. All of these organizations are separately incorporated entities managed by their own Boards and audited by other independent certified public accounting firms. Each organization is described below.

Medical College of Virginia Foundation

The foundation is organized to aid, strengthen, and extend the work, services, and objectives of the Virginia Commonwealth University Health System Authority and the Health Sciences Campus of Virginia Commonwealth University. This is achieved through the receipt of contributions, investment and management of funds, and the disbursement of current funds and a portion of the total return on endowment. Foundation transfers and expenditures to support University programs were $20,366,000.

VCU Foundation

The foundation functions solely to assist and support the University. In that capacity, the foundation holds and manages selected investments for the University. The University received $4,434,865 from the foundation.

VCU Real Estate Foundation

The foundation functions solely to assist and support the University. The sole purpose of the foundation is to hold and manage real estate for the University. The University received $348,648 from the foundation and has an operating lease liability of $1,396,303.

Virginia Commonwealth University School of Engineering Foundation

The foundation is organized exclusively for educational, scientific and charitable purposes, and to provide financial and other support to the University's School of Engineering. The University has issued $26,895,000 of General Revenue Pledge Bonds for the purpose of constructing a School of Engineering Foundation building. The proceeds were advanced to the School of Engineering Foundation, which, as owner of the property, constructed the building. The School of Engineering Foundation solicits contributions and remits funds to the University sufficient to retire the indebtedness including interest. The funds received from the School of Engineering Foundation will be recorded as contributions received. For accounting purposes, the University records a leasehold interest equal to the funds advanced. The University received $2,689,802 in 2002.

The following summarizes selected financial data, excluding data included in the University's financial statements, of the fund raising foundations which support the University, the Medical College of Virginia Foundation, the VCU Foundation, the VCU Real Estate Foundation and its controlled affiliate, and the Virginia Commonwealth University School of Engineering Foundation.

Assets:	
Cash and investments	$223,759,556
Other assets	51,625,730
Total assets	$275,385,286
Liabilities and fund balances:	
Accounts and loans payable	$ 30,737,416
Fund balances	244,647,870
Total liabilities and fund balances	$275,385,286
Revenues and other fund additions	$ 22,457,660
Expenditures and other fund deductions	$ 32,455,800

Medical College of Virginia Alumni Association of VCU

The purpose of the Medical College of Virginia Alumni Association of VCU is to organize alumni activities for Virginia Commonwealth University. The University provided funding of $234,861 for the Association's operation.

Virginia Commonwealth University Alumni Association

The Association was formed for educational purposes to further the best interests of the University, its alumni, and students. The University provided funding of $113,765 for the Association's operation.

Virginia Biotechnology Research Park Authority

The primary purpose of the Virginia Biotechnology Research Park Authority is to expand knowledge pertaining to scientific and technological research and development among public and private entities and promote the economic and industrial development of the City of Richmond and the Commonwealth of Virginia. The University currently occupies 41,847 square feet of Biotech One under a capital lease as shown in Note 6. In addition, the University is committed to a twenty year Master Lease with the Authority, which guarantees monthly rent equal to the principal and interest necessary to amortize the outstanding debt associated with the construction of the facilities and any additional rent required. The maximum amount payable under this Lease for space not occupied by the University is $543,235 annually during the first ten years of the Lease and $1,278,200 annually for the remainder of the lease term.

M.C.V./V.C.U. Dental Faculty Practice Association

The Association was established to support the education, research, service and patient care mission of the School of Dentistry (School) of Virginia Commonwealth University. The Association promotes and coordinates the delivery of superior patient care at the School.

9. FUNDS HELD IN TRUST BY OTHERS

Under the provisions of the wills of certain benefactors, the University's portion of principal sums with market values of $14,190,298 was held in trust by others. These assets are not included in the University's statement of net assets.

10. COMMITMENTS

The University and the Authority are party to various construction commitments. At June 30, 2002, the remaining commitments were $10,311,063 for the University and approximately $58,900,000 for the Authority.

The University also is committed under various operating leases (for buildings, computer equipment, business equipment, etc.). The University has renewal options on certain of the leased assets. In most cases, the University expects that, in the normal course of business, these leases will be replaced by similar leases. Rental expense for the fiscal year ended June 30, 2002, was $2,429,639 for the University and $6,668,000 for the Authority. In addition, the University reimburses the Commonwealth of Virginia $153,703 annually for the use of space in a facility owned by the Commonwealth.

The University has, as of June 30, 2002, the following total future minimum rental payments due under the above leases.

Fiscal Year	University	Authority
2003	$1,713,136	$ 5,667,119
2004	940,488	2,977,256
2005	698,903	2,245,159
2006	554,327	818,211
2007	183,714	577,509
2008 - 2011	359,216	-
Total future minimum rental payments	$4,449,784	$12,285,254

Of the total minimum rental payments for the University, $1,396,303 is to the VCU Real Estate Foundation, a related party.

11. LITIGATION

The University and Authority have been named as a defendant in a number of lawsuits. The final outcome of any of these lawsuits cannot be determined at this time. However, management is of the opinion that any ultimate liability to which the University and Authority may be exposed will not have a material effect upon the University's financial position.

12. TRANSACTIONS BETWEEN COMPONENT UNITS

Effective July 1, 1997, the Authority and the University, concurrently, entered into an affiliation agreement, which provides that each will support the mission of the other. The University will provide graduate medical education, clinical support, administrative support, and medical care of indigent patients to the Authority. The Authority will provide operation and maintenance support for certain buildings included in a five-year lease agreement, residents for the Blackstone Family Practice Residency Training Program, and be the primary teaching hospital for the University.

The University leased the patient care facilities to the Authority under a ninety-nine year lease for the greater of the annual debt service on the facilities or $1 per year. Additionally, the Authority leased space in other buildings from the University under a five-year lease with two renewal options, except the West Hospital, which is not included in the renewal options.

Payments under the agreement with the University for the year was as follows:

By the University to the Authority:	
Operation and maintenance – buildings (5 year lease)	$ 3,006,821
Blackstone Family Practice Residency Training Program	583,155
Total paid by the University to the Authority	$ 3,589,976

By the Authority to the University:	
Graduate education services	$ 579,180
Non-physician clinical support	2,518,211
Administrative support	4,612,004
Rent on the short-term space	2,712,927
Principal and interest on parking deck debt	523,909
Use of steam plant	588,276
Total paid by the Authority to the University	$ 11,534,507

13. SUBSEQUENT EVENT

On November 6, 2002, the University issued a note to the Virginia College Building Authority (VCBA) in the amount of $32,945,000. The proceeds of the note will be used to finance the academic housing project, the Bowe Street Deck project, the renovation of Gladding Residence Hall, and Student Commons Phase III. The note bears interest at rates ranging from 3 percent to 5.25 percent payable in the years 2004 through 2023.

14. CONTINGENCIES

Through June 30, 1990, the Hospitals were insured under a claims-made policy with respect to institutional and professional liability, each with liability limits of $1 million per incident and an aggregate annual liability limit of $3 million in each policy year. Either the PHICO Insurance Company, or The Virginia Insurance Reciprocal provided insurance.

Effective July 1, 1990 and through June 30, 1998, the Hospitals and the Authority were insured under a risk management plan for the Commonwealth of Virginia. This plan was also claims-made with institutional and professional liability limits of $1 million per incident, but no aggregate limit.

Effective July 1, 1998, the Authority insured itself under a self-insured professional liability, self-administered plan. This plan is claims-made with professional liability limits of $1 million per incident and $3 million in aggregate with excess insurance coverage up to $10 million, which is provided by The Reciprocal of America (the Reciprocal), a multiprovider reciprocal insurance company. A revocable trust has been established and is funded based on actuarially determined reserves. At June 30, 2002, the medical malpractice trust fund includes approximately $4,230,000 for claims and related legal expenses for reported and unreported incidents occurring since July 1, 1998. There have been malpractice claims asserted against the Authority by various claimants. The claims are in various stages of processing and some may ultimately be brought to trial. There are also known incidents that have occurred through June 30, 2002 that may result in the assertion of additional claims. In addition, there may be other claims from unreported incidents arising from services provided to patients through June 30, 2002. At June 30, 2002, the Authority's management accrued professional liability losses to the extent they fall within the limits of the Authority's self-insurance program or exceed the limits of the excess insurance coverage. The liability for medical malpractice at June 30, 2002 includes approximately $5,463,000 for claims and related legal expenses for reported and unreported incidents occurring since July 1, 1998. The liability was actuarially determined combining industry data and the Authority's historical experience.

MCVAP's professional liability coverage is provided through a claims-made policy obtained from Universal Re-Insurance Company (URIC), a Bermuda insurance corporation. At June 30, 2001, the policy provided coverage of $1,550,000 per occurrence and $5,000,000 in the aggregate. In response to recent legislative changes in the Commonwealth of Virginia regarding malpractice insurance liability limitations, MCVAP has increased its coverage with URIC effective July 1, 2002 to $1,650,000 per occurrence and $8,000,000 in the aggregate. Premiums paid by MCVAP to URIC are recorded as an expense by MCVAP. There were no premiums paid during 2002. Such premiums, aggregating approximately $11.8 million from inception to date, are maintained in an irrevocable trust fund administered by SunTrust Bank. Under the terms of the agreement with URIC, no risk has been transferred by MCVAP to URIC. As a result, the premiums paid to URIC have been recorded as a deposit in assets, whose use is limited and as a liability for estimated losses for malpractice claims.

Through June 30, 2002, an excess professional liability policy was written by The Reciprocal of America. This policy covers losses in excess of the URIC limits for an additional aggregate amount of $10 million.

Effective July 1, 2002, an excess professional liability policy was written by Columbia Casualty Group of the CNA Insurance Group. This policy covers losses in excess of the URIC limits for an additional aggregate amount of $5 million.

In addition, MCVAP insures itself under a self-insured liability self-administered plan for any claims in excess of its insurance coverage. The Board annually sets aside funds to be used to fund estimated losses based on actuarially determined reserves. At June 30, 2002, assets whose use is limited includes approximately $11,533,000 that has been designated by the Board to fund malpractice claims. In addition, MCVAP's management accrued professional liability losses of approximately $8,856,000 at June 30, 2002, in addition to the $11.8 million insured by URIC.

Should MCVAP not renew its policies or replace them with equivalent insurance, occurrences during its term, but asserted after its term will be uninsured, unless MCVAP obtains tail coverage. MCVAP management is of the opinion that its financial position would not be materially affected by the ultimate cost related to unasserted claims, if any, at June 30, 2002.

VA Premier maintains general and professional liability policies. The general liability policy in force is occurrence-based. The coverage under the professional liability policy is made on a claims-made basis and must be renewed or replaced with the equivalent insurance if claims incurred during its terms, but asserted after its expiration, are to be insured. Coverage limits for the general liability policy are $1 million per occurrence and $3 million annual aggregate. The coverage limits for the professional liability policy are $6 million per medical incident and $8 million annual aggregate.

In management's opinion, the claims-made insurance coverage is adequate to cover the estimated ultimate liability, which could result upon settlement of claims currently asserted against the Authority, and the ultimate liability for medical incidents of which the Authority has knowledge, but for which no claim has been asserted against the Authority. Based upon current historical data, management is of the opinion that the liability, if any, for unreported medical incidents would not have a material effect on the Authority's financial position.

During fiscal 1996, the Department of Health and Human Services ("HHS") announced its intention to audit Medicare billings submitted by teaching physicians at all of the major teaching hospitals in the United States. During fiscal 1998, MCVAP received notification from the Department of Justice ("DOJ") stating that it was the subject of investigations relating to CHAMPUS and Medicare billing practices. MCVAP has cooperated fully with this notification from the DOJ. At the present time, management does not have sufficient information to determine if MCVAP will have any liability related to these issues or what the potential liability, if any, might be.

15. STOP-LOSS COVERAGE

Effective February 1, 2001, VA Premier entered into a stop-loss arrangement to limit its losses on individual claims. This contract provides stop-loss coverage for all VA Premier enrollee claims. This contract provides coverage for 100 percent of certain hospital claims in excess of $100,000 subject to certain limitations and an annual limit of $1,000,000 per enrollee and a lifetime limit of $2,000,000 per enrollee. Stop-loss premiums of approximately $307,000 are included in medical claims expense in the year.

16. NET PATIENT SERVICE REVENUE

The Authority's patient service revenue is as follows for the year ended June 30, 2002:

Gross Patient Revenue:	
Inpatient:	
Routine services	$144,879,165
Ancillary services	478,892,480
Outpatient:	
Emergency	26,768,853
Special medical	231,423,003
Total gross patient service revenue	881,963,501
Provision for indigent care and contractual adjustments	(400,683,538)
Provision for bad debts	(31,826,568)
Net patient service revenue (Hospitals)	449,453,395
MCVAP's net patient service revenue	84,550,370
Net patient service revenue (Authority)	$534,003,765

The Authority received approximately $102,500,000 for disproportionate share payments from the Department of Medical Assistance Services that were funded by the Commonwealth of Virginia for patients that are indigent. These payments are included in net patient service revenue as an adjustment of allowances for indigent care and contractual adjustments.

Amounts written off for indigent care, net of the disproportionate share payments, were approximately $51,671,000.

17. ESTIMATED MEDICAL CLAIMS PAYABLE

Claims expenses and liabilities arising from services rendered to VA Premier's HMO members are reported when it is probable that services have been provided and the amount of the claim can be reasonably estimated. The claims payable includes an estimate of claims that have been incurred, but not reported. At June 30, the amount of these liabilities included in accounts payable and accrued liabilities was $21,754,704. This liability is VA Premier's best estimate based on available information.

18. STATE APPROPRIATIONS – UNRESTRICTED FUNDS

The University receives state appropriations from the General Fund of the Commonwealth. The Appropriation Act specifies that such unexpended appropriations shall revert at the end of the biennium, as specifically provided by the General Assembly, unless the University meets management standards.

The following is a summary of state appropriations by the University for the year ended June 30, 2002 including all reversions.

Original legislative appropriation per Chapter 1073:	
Educational and general programs	$176,739,022
Higher Education Student Financial Assistance	9,671,840
Financial assistance for educational and general services	150,000
Supplemental adjustments:	
Non-general fund budget reduction	(985,731)
General fund budget reduction	(5,328,604)
Pre-pay of FY03 reduction	(1,633,000)
Higher education equipment trust fund	4,990,209
Other adjustments	4,519,305
Reversion to the General Fund of the Commonwealth	(65,416)
Adjusted appropriation	$188,057,625

19. RISK MANAGEMENT

The University is exposed to various risks of loss related to torts; theft or, damage to, and destruction of assets; errors and omissions; non-performance of duty; injuries to employees; and natural disasters. The University participates in insurance plans maintained by the Commonwealth of Virginia. The state employee health care and worker's compensation plans are administered by the Department of Human Resource Management and the risk management insurance plans are administered by the Department of Treasury, Division of Risk Management. Risk management insurance includes property, general liability, medical malpractice, faithful performance of duty bond, automobile, and air and watercraft plans. The University pays premiums to each of these Departments for its insurance coverage. Information relating to the Commonwealth's insurance plans is available at the statewide level in the Commonwealth of Virginia's Comprehensive Annual Financial Report. Information relating to the Authority's risk management is included in Note 14.

VIRGINIA COMMONWEALTH UNIVERSITY
SCHEDULE OF AUXILIARY ENTERPRISES - REVENUE
EXPENDITURES AND CHANGES IN FUND BALANCE
For The Period Ended June 30, 2002

	Athletics	Siegel Center	Food Services	Gyms	Larrick Student Center	Parking and Transportation	Residence Halls
Revenue:							
Student fees	$ -	$ -	$ 4,628,057	$ -	$ -	$ -	$ 8,379,091
University fee	5,784,751	2,473,578	-	2,017,907	192,874	1,946,494	-
Sales and services	1,210,978	1,203,049	1,551,194	235,849	-	6,263,869	434,227
Auxiliary interest earnings	-	-	-	-	-	-	-
Total revenue	6,995,729	3,676,627	6,179,251	2,253,756	192,874	8,210,363	8,813,318
Cost of sales	-	-	-	-	-	-	-
Net revenue	6,995,729	3,676,627	6,179,251	2,253,756	192,874	8,210,363	8,813,318
Expenditures:							
Personal services	2,274,102	326,862	192,130	1,057,132	133,699	1,234,130	2,790,643
Employee benefits	577,402	69,368	69,330	172,039	21,328	289,915	581,993
Contractual services	995,214	995,705	3,652,503	162,034	12,315	1,350,430	1,077,808
Supplies and materials	123,052	147,579	89,275	138,254	3,320	139,076	388,533
Equipment	133,068	223,453	322,640	65,437	1,961	251,548	64,827
Current charges and obligations	2,618,466	857,426	557,135	269,508	23,046	1,756,856	2,385,691
Miscellaneous	192,990	168,813	230,643	149,712	6,274	290,436	383,312
Operating expenditures	6,914,294	2,789,206	5,113,656	2,014,116	201,943	5,312,391	7,672,807
Interdepartmental recoveries and charges	(57,237)	(3,364)	-	-	(100)	(32,157)	(34,123)
Net operating expenditures	6,857,057	2,785,842	5,113,656	2,014,116	201,843	5,280,234	7,638,684
Excess (deficiency) of revenues over (under) operating expenditures before transfers	138,672	890,785	1,065,595	239,640	(8,969)	2,930,129	1,174,634
Transfers:							
Mandatory	275,815	2,046,608	6,491	-	-	2,674,334	1,453,505
Nonmandatory	(228,004)	(1,820,193)	508,986	(49,724)	(4,704)	119,129	(233,532)
Excess (deficiency) of revenues over/(under) expenditures and transfers	90,861	664,370	550,118	289,364	(4,265)	136,666	(45,339)
Beginning fund balance	(287,846)	842,930	2,620,298	2,556,952	(857)	4,920,607	(1,269,735)
Ending fund balance	$ (196,985)	$ 1,507,300	$ 3,170,416	$ 2,846,316	$ (5,122)	$ 5,057,273	$ (1,315,074)

Note: This schedule is prepared on a modified accrual basis of accounting and does not support the basic financial statements.

Stores and Shops	Student Commons	Student Health	Business Services Administration	Development Programs	Unassigned	Dental Programs	Steam Plant	Total
$ -	$ -	$ 2,450,955	$ -	$ -	$ 17,051,905	$ -	$ -	$ 32,510,008
-	2,653,887	198,356	-	230,891	(15,498,738)	-	-	-
2,719,882	92,286	323,816	30,422	41,620	1,261,461	-	2,223,455	17,592,108
-	-	-	-	-	-	-	-	-
2,719,882	2,746,173	2,973,127	30,422	272,511	2,814,628	-	2,223,455	50,102,116
1,463,635	-	-	-	-	-	-	-	1,463,635
1,256,247	2,746,173	2,973,127	30,422	272,511	2,814,628	-	2,223,455	48,638,481
166,237	849,004	1,365,851	235,289	87,062	4,828	-	380,741	11,097,710
40,395	192,986	334,054	34,123	27,070	394	-	100,979	2,511,376
237,331	150,558	257,434	38,453	57,787	1,689,440	-	512,051	11,189,063
28,283	50,341	346,343	(128,778)	58,124	2,736	-	406,305	1,792,443
-	(119,217)	104,838	51,672	10,131	2,141	-	38	1,112,537
34,737	373,479	77,081	34,922	7,183	82,193	-	385,441	9,463,164
16,474	48,740	92,081	13,591	49,441	160,088	-	825	1,803,420
523,457	1,545,891	2,577,682	279,272	296,798	1,941,820	-	1,786,380	38,969,713
-	(86,921)	36	(420,662)	(45,724)	(1,251,285)	-	-	(1,931,537)
523,457	1,458,970	2,577,718	(141,390)	251,074	690,535	-	1,786,380	37,038,176
732,790	1,287,203	395,409	171,812	21,437	2,124,093	-	437,075	11,600,305
-	643,508	85,301	-	-	224,944	-	-	7,410,506
604,762	(39,374)	2,967	-	(3,595)	1,492,773	-	-	349,491
128,028	683,069	307,141	171,812	25,032	406,376	-	437,075	3,840,308
1,828,829	396,781	228,816	33,471	(16,655)	3,264,965	-	(291,615)	14,826,941
$ 1,956,857	$ 1,079,850	$ 535,957	$ 205,283	$ 8,377	$ 3,671,341	$ -	$ 145,460	$ 18,667,249

VIRGINIA COMMONWEALTH UNIVERSITY
Richmond, Virginia

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