

THE UNIVERSITY OF SOUTH DAKOTA

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the University of South Dakota ("University") annual financial report presents management's discussion and analysis of the financial performance of the University during the fiscal year ended June 30, 2004. This discussion should be read in conjunction with the accompanying financial statements and footnotes. The financial statements, footnotes, and this discussion are the responsibility of University management.

Using the Annual Financial Report

This annual report consists of financial statements, prepared in accordance with Governmental Accounting Standards Board ("GASB") Statement No. 35, *Basic Financial Statements and Management's Discussion and Analysis for Public Colleges and Universities*. These financial statements differ significantly, in both the form and the accounting principles utilized, from financial statements prior to FY03. The financial statements presented in prior years focused on the accountability of fund groups, 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 prescribed by GASB Statement No. 35 (the Statement of Net Assets, Statement of Revenues, Expenses and Changes in Net Assets, and the Statement of Cash Flows) present financial information in a form similar to that used by corporations. They are prepared under the accrual basis of accounting, whereby revenues and assets are recognized when the service is provided and expenses and liabilities are recognized when others provide the service, regardless of when cash is exchanged.

The Statement of Net Assets includes all assets and liabilities:

The Statement of Net Assets includes all assets and liabilities. Over time, increases or decreases in net assets (the difference between assets and liabilities) is one indicator 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 facilities.

**Condensed Statement of Net Assets
For Fiscal Year Ending June 30, 2004**

Assets	
Cash or equivalent	\$16,435,125.36
Other Current Assets	4,475,535.45
Non-Current Assets	<u>95,369,454.48</u>
Total Assets	\$116,280,115.29
Liabilities	
Current Liabilities (due within one year)	\$8,297,550.02
Non-Current Liabilities	<u>42,293,383.32</u>
Total Liabilities	\$50,590,933.34
Net Assets	\$65,689,181.95

Noteworthy Financial Activity

As of June 30, 2004, the University's total assets were \$116,280,115. Physical plant of \$73,090,075 is the largest and includes Buildings, Equipment and Library books less depreciation. The remaining non current assets were non-current cash of \$12,395,963.69, which is designated for dorm renovation, and notes receivable of \$9,883,415.29.

In fiscal 2004, the University's current assets of \$20,910,661 were sufficient to cover current liabilities of \$8,297,550 (current ratio of 2.52).

The University's Change in Net Assets showed an increase of \$5,187,858 to \$65,689,182 for FY04, of which \$61,233,039 is invested in capital assets. This was due to capitalized improvements in the AI Neuharth Center for 4.8 Million and other various buildings over depreciated amount.

University liabilities total \$50,590,933 at June 30, 2004. Long-term debt of \$35,638,778 is the largest liability. Dakota Dome, Old Main, Resident Hall Renovation, & Federal Capital Contribution all total the \$35,638,778.

Total liabilities increased by \$1,686,617. The increase is due to increase of various liability accounts and offset by any decrease in any liability accounts. Some of the accounts that increased were Accounts Payable, Compensated Absences, and Agency Funds Held for Others, while some of the accounts that were decreased were Due to Other Component Units, Bonds Payable, and Obligations under Capital Leases.

The Statement of Revenues, Expenses and Changes in Net Assets:

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. A public university's dependency on state aid and gifts could result in operating deficits because the financial reporting model classifies state appropriations and gifts as nonoperating revenues. The utilization of capital assets is reflected in the financial statements as depreciation, which amortizes the cost of an asset over its expected useful life.

**Condensed Statement of Revenues, Expenses, and Changes in Net Assets
For Fiscal Year Ending June 30, 2004**

Total operating Revenues	\$ 74,750,094
Total operating Expenses	\$ 114,013,181
Operating loss	\$ (39,263,087)
Non-operating revenues (expenses)	\$ 41,398,731
Income before other revenues, expenses, gains, or losses	\$ 2,135,644
Capital appropriations and gifts	\$ 3,120,494
Total increase in net assets	\$ 5,256,139
Net assets, beginning of year	\$ 60,501,324
Net assets, beginning of year adjustments	\$ (68,281)
Net assets, end of year	\$ 65,689,182

Noteworthy Financial Activity

The most significant sources of operating revenues for the University are tuition and fees of \$26,114,533, auxiliary services of \$6,103,215, and grants and contracts of \$32,523,659.

Operating expenditures equaled \$114,013.81, of which \$6,020,644.00 is depreciation expense.

State appropriations were the most significant non-operating revenue, totaling \$41,669,741. State appropriations are funds appropriated each year by the state legislatures to the University as part of the University's total budget. However due to GASB reporting requirements it is reported as non-operating income, therefore it offsets the operating loss.

The Statement of Cash Flows:

The Statement of Cash Flows presents information related to cash inflows and outflows summarized by operating, noncapital financing, capital financing, and related investing activities, and helps measure the ability to meet financial obligations as they mature.

**Condensed Statements of Cash Flows
 For the Year Ended June 30, 2004**

Cash provided/(used)by:	
Operating activities	\$ (32,954,018)
Noncapital financing activities	\$ 42,673,506
Capital and related financing activities	\$ (8,296,641)
Investing activities	\$ 877,807
Net increase in cash	\$ 2,300,653
Cash and cash equivalents, beginning of year	\$ 26,530,436
Cash and cash equivalents, end of year	\$ 28,831,089

Looking Ahead

The University maintains a positive outlook for FY04 and beyond. The University continues to be well positioned for the future, both academically and financially. A strategic plan is in place that will enable the University to monitor and achieve academic goals. The University also has a facility plan to insure that campus buildings and infrastructure will be maintained in excellent condition for many years to come. Major Projects that are being completed, in process now, and in the planning process are the Neuharth Media Center, Belbas Building Project which will serve as the Student Services Building, Medical Science Building, the new Business School, and the remodeling of all of the Univeristy's Dorms. The University has begun a study for renovation and expansion of the Coyote Student Center.

Reliance on state support remains an important non-operating revenue source for the University. The level of State General Fund Appropriations is expected to remain stable. The University has relied on Grants and Contracts for a major source of revenue and will continued to seek more revenue from outside entities for Grants and Contracts in the future.

The University's Research program has grown significantly over the last few years and the University will continue to promote excellence in the research area along with increased outside funding. Below is a comparative chart on the growth in our research area.

Grants & Contracts

Fiscal Year	Private	State	Federal	Total
USD				
FY98	\$1,422,618.00	\$792,096.00	\$3,970,388.00	\$6,185,102.00
FY99	\$1,310,697.00	\$634,178.00	\$4,722,210.00	\$6,667,085.00
FY00	\$1,510,382.00	\$484,689.00	\$3,934,189.00	\$5,929,260.00
FY01	\$1,140,501.00	\$537,639.00	\$4,769,316.00	\$6,447,456.00
FY02	\$1,742,180.00	\$432,924.00	\$6,073,966.00	\$8,249,070.00
FY03	\$2,167,869.00	\$472,987.00	\$7,345,363.00	\$9,986,219.00
FY04	\$1,676,370.00	\$229,505.00	\$7,319,760.00	\$9,225,635.00
MED				
FY98	\$926,978.00	\$457,804.00	\$3,787,105.00	\$5,171,887.00
FY99	\$947,127.00	\$180,900.00	\$4,455,459.00	\$5,583,486.00
FY00	\$1,174,747.00	\$158,729.00	\$4,227,465.00	\$5,560,941.00
FY01	\$877,215.00	\$125,727.00	\$5,880,491.00	\$6,883,433.00
FY02	\$1,034,436.00	\$127,998.00	\$8,766,602.00	\$9,929,036.00
FY03	\$825,912.00	\$128,816.00	\$12,134,625.00	\$13,089,353.00
FY04	\$825,559.00	\$127,731.00	\$15,212,456.00	\$16,165,746.00
Total USD & MED				
FY98	\$2,349,596.00	\$1,249,900.00	\$7,757,493.00	\$11,356,989.00
FY99	\$2,257,824.00	\$815,078.00	\$9,177,669.00	\$12,250,571.00
FY00	\$2,685,129.00	\$643,418.00	\$8,161,654.00	\$11,490,201.00
FY01	\$2,017,716.00	\$663,366.00	\$10,649,807.00	\$13,330,889.00
FY02	\$2,776,616.00	\$560,922.00	\$14,840,568.00	\$18,178,106.00
FY03	\$2,993,781.00	\$601,803.00	\$19,479,988.00	\$23,075,572.00
FY04	\$2,501,929.00	\$357,236.00	\$22,532,216.00	\$25,391,381.00

The University has implemented a new marketing plan, increased scholarships, and increased enrollment requirements to 24 ACT and above. The University will continue to strive to be the best, small, publicly funded institution of higher education in the country.

THE UNIVERSITY OF SOUTH DAKOTA
STATEMENT OF NET ASSETS
June 30, 2004

ASSETS

	June 30, 2004	June 30, 2003
CURRENT ASSETS		
CASH ON DEPOSIT-STATE TREASURER	\$ 6,369,649.44	\$ 5,628,979.84
OTHER CASH & TEMPORARY INVESTMENTS	\$ 10,065,475.92	\$ 7,803,715.64
ACCTS REC - STUDENTS	\$ 1,089,483.20	\$ 963,072.12
(NET OF ALLOWANCE OF \$92,854.13)		
ACCOUNTS RECEIVABLE - DEPT SALES	\$ 28,886.54	\$ 93,911.28
NOTES RECEIVABLE	\$ 2,376,326.00	\$ 2,666,188.31
INTEREST RECEIVABLE	\$ 147,472.64	\$ 133,738.94
PREPAID EXPENSES & DEFERRED CHARGES	\$ -	\$ -
INVENTORY	\$ 536,371.38	\$ 428,467.47
DUE FROM FEDERAL SOURCES	\$ 197,139.00	\$ 197,139.00
DUE FROM PRIMARY GOVERNMENT	\$ 57,761.55	\$ 25,923.30
DUE FROM OTHER COMPONENT UNIT	\$ 42,095.14	\$ 172,526.73
TOTAL CURRENT ASSETS	\$ 20,910,660.81	\$ 18,113,662.63
NON-CURRENT ASSETS		
CASH NON-CURRENT	\$ 12,395,963.69	\$ 13,097,740.34
NOTES RECEIVABLE	\$ 9,883,415.29	\$ 8,959,676.03
WORKS OF ARTS & HISTORICAL TREASURES	\$ 379,085.00	\$ 379,085.00
CONSTRUCTION IN PROGRESS	\$ 2,828,750.86	\$ 5,571,445.61
BUILDINGS & BUILD IMPROVE	\$ 48,736,246.56	\$ 44,831,186.41
(NET OF ACCUM DEPR \$38,264,239.80)		
LAND	\$ 945,215.41	\$ 945,215.41
LAND IMPROVEMENTS	\$ 3,322,624.72	\$ 2,918,314.49
(NET OF ACCUM DEPREC \$604,995.39)		
INFRASTRUCTURE	\$ 1,479,780.26	\$ 1,624,168.40
(NET OF ACCUM DEPREC \$3,243,768.29)		
EQUIPMENT & OTHER PROPERTY	\$ 15,398,372.69	\$ 12,965,146.41
(NET ACCUM DEPREC \$43,433,394.83)		
TOTAL NON-CURRENT ASSETS	\$ 95,369,454.48	\$ 91,291,978.10
TOTAL ASSETS	\$ 116,280,115.29	\$ 109,405,640.73
LIABILITIES		
CURRENT LIABILITIES		
ACCOUNTS PAYABLE - CURRENT	\$ 2,582,005.64	\$ 2,193,418.86
ACCRUED WAGES & BENEFITS	\$ 315,752.57	\$ 253,020.41
ACCRUED INTEREST PAYABLE	\$ 561,838.07	\$ 345,555.74
COMPENSATED ABSENCES PAYABLE - CURRENT	\$ 2,315,515.97	\$ 2,101,284.69
NOTES PAYABLE - CURRENT PORTION	\$ -	\$ -
BONDS PAYABLE - CURRENT	\$ 325,000.00	\$ 290,000.00
OBLIGATIONS UNDER CAPITAL LEASES - CURRENT	\$ 230,000.00	\$ 220,000.00
DEFERRED REVENUE	\$ -	\$ -
OTHER ACCRUED LIABILITIES	\$ 630,142.98	\$ 424,253.97
STUDENT DEPOSITS	\$ 18,100.00	\$ 24,800.00
DUE TO FEDERAL SOURCES	\$ -	\$ -
DUE TO PRIMARY GOVERNMENT	\$ 181,612.67	\$ 150,396.34
DUE TO OTHER COMPONENT UNIT	\$ 44,811.17	\$ 160,961.69
AGENCY FUNDS-FUNDS HELD FOR OTHERS	\$ 1,092,770.95	\$ 519,158.97
TOTAL CURRENT LIABILITIES	\$ 8,297,550.02	\$ 6,682,850.67

THE UNIVERSITY OF SOUTH DAKOTA
STATEMENT OF NET ASSETS
June 30, 2004

	June 30, 2004	June 30, 2003
NON-CURRENT LIABILITIES		
COMPENSATED ABSENCES PAYABLE - NON-CURRENT	\$ 6,654,605.76	\$ 6,643,960.39
NOTES PAYABLE - NON-CURRENT		\$ -
BONDS PAYABLE - NON-CURRENT	\$ 15,820,000.00	\$ 16,145,000.00
OBLIGATIONS UNDER CAPITAL LEASES - NON-CURRENT	\$ 7,878,000.00	\$ 8,108,000.00
FEDERAL CAPITAL CONTRIBUTION ADVANCE	\$ 11,940,777.56	\$ 11,324,505.34
TOTAL NON-CURRENT LIABILITIES	<u>\$ 42,293,383.32</u>	<u>\$ 42,221,465.73</u>
TOTAL LIABILITIES	<u><u>\$ 50,590,933.34</u></u>	<u><u>\$ 48,904,316.40</u></u>
NET ASSETS		
INVESTED IN CAPITAL, NET OF RELATED DEBT	\$ 61,233,039.19	\$ 57,569,302.07
RESTRICTED		
NONEXPENDABLE		
SCHOLARSHIPS AND FELLOWSHIPS		\$ -
RESEARCH		\$ -
LOANS	\$ 1,511,082.24	\$ 1,344,416.29
EXPENDABLE		
SCHOLARSHIPS AND FELLOWSHIPS		\$ -
RESEARCH		\$ -
INSTRUCTIONAL DEPARTMENT USES		\$ -
OTHER	\$ 675,777.09	\$ 1,015,646.59
DEBT & M&E RESERVED	\$ 1,155,887.85	\$ 1,154,786.26
UNRESTRICTED	<u>\$ 1,113,395.58</u>	<u>\$ (582,826.88)</u>
TOTAL NET ASSETS	<u><u>\$ 65,689,181.95</u></u>	<u><u>\$ 60,501,324.33</u></u>

THE UNIVERSITY OF SOUTH DAKOTA
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
June 30, 2004

	June 30, 2004	June 30, 2003
OPERATING REVENUES		
Tuition		
State support	\$ 13,349,393.67	\$ 12,899,188.58
Self support	\$ 4,349,026.14	\$ 4,056,006.57
HEFF	\$ -	\$ -
Total Tuition	\$ 17,698,419.81	\$ 16,955,195.15
Fees		
University support fee	\$ 5,092,835.16	\$ 4,995,982.71
Salary Competitiveness Fee	\$ 2,899,740.00	\$ 2,477,682.00
General Activity Fee	\$ 2,256,563.29	\$ 1,679,516.82
Salary Enhancement Fees (business, law, etc.)	\$ 407,338.22	\$ 228,159.15
Special Discipline Fees (nursing, law, med, etc.)	\$ 905,693.97	\$ 769,683.47
Lab Fees	\$ 148,230.00	\$ 152,070.97
Vehicle Registration	\$ 249,388.02	\$ 231,018.81
Delivery Fees	\$ 458,880.09	\$ 309,739.04
Technology Fee	\$ -	\$ -
Other Fees (application, transcript, exam for credit & international student fees)	\$ 182,167.38	\$ 619,761.81
Total Fees	\$ 12,600,836.13	\$ 11,463,614.78
Total Tuition and Fees	\$ 30,299,255.94	\$ 28,418,809.93
Student Financial Assistance	\$ (4,184,722.63)	\$ (3,644,928.89)
Tuition and Fees net of student financial assistance	\$ 26,114,533.31	\$ 24,773,881.04
Auxiliaries (net of scholarship allowances of \$866,306.56)	\$ 6,103,214.76	\$ 5,734,037.28
General Sales & Services	\$ 9,651,853.58	\$ 8,448,236.21
Loan Cancellation Reimbursement	\$ 188,017.00	\$ 180,095.00
Contracts & Grants		
Federal	\$ 25,840,745.77	\$ 22,687,899.36
State	\$ 453,709.29	\$ 756,762.14
Private	\$ 6,229,204.03	\$ 5,544,151.09
Student Loan Interest	\$ 168,816.66	\$ 178,427.92
Transfers In from Other Component Units/Other Additions	\$ -	\$ 242,824.00
TOTAL OPERATING REVENUES	\$ 74,750,094.40	\$ 68,546,314.04
OPERATING EXPENSES		
Personal Services (salaries & benefits)	\$ (73,371,512.16)	\$ (69,908,481.03)
Travel	\$ (2,543,909.13)	\$ (2,327,023.88)
Contractual	\$ (17,139,055.46)	\$ (13,670,421.74)
Supplies & Materials	\$ (9,403,070.87)	\$ (12,310,895.67)
Capital Outlay	\$ -	\$ -
Other	\$ (288,981.85)	\$ (403,912.67)
Grants	\$ (5,246,008.16)	\$ (4,350,247.83)
Interest	\$ -	\$ -
Bad Debt	\$ -	\$ -
Depreciation	\$ (6,020,643.66)	\$ (5,757,698.04)
TOTAL OPERATING EXPENSES	\$ (114,013,181.29)	\$ (108,728,680.86)
OPERATING INCOME/(LOSS)	\$ (39,263,086.89)	\$ (40,182,366.82)

THE UNIVERSITY OF SOUTH DAKOTA
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
June 30, 2004

	June 30, 2004	June 30, 2003
NON-OPERATING REVENUES		
General Fund Appropriations	\$ 41,669,740.96	\$ 40,454,050.17
School & Public Lands	\$ 126,570.00	\$ 133,440.93
Federal Fund Appropriations	\$ -	\$ -
HEFF	\$ 87,983.00	\$ 87,983.00
Endo/Ecto Tax	\$ -	\$ -
Investment Income	\$ 455,879.04	\$ 197,028.13
Loan Cancellation Reimbursement	\$ -	\$ -
Other Revenue & Additions	\$ 440,890.65	\$ -
NON-OPERATING EXPENSES		
Personal Services (salaries & benefits)	\$ -	\$ -
Travel	\$ -	\$ -
Contractual	\$ -	\$ -
Supplies & Materials	\$ -	\$ -
Capital Outlay		
Other	\$ (1,218,385.29)	\$ (879,097.17)
Depreciation	\$ -	\$ -
Unrealized Gain/Loss on investment		
Gain/Loss on Sale of investment	\$ -	\$ -
Gain/Loss on Disposal of Asset	\$ (163,947.20)	\$ (132,015.47)
TOTAL NON-OPERATING REVENUES/(EXPENSES)	\$ 41,398,731.16	\$ 39,861,389.59
INCOME BEFORE OTHER REVENUES, EXPENSES, GAINS OR LOSSES		
CAPITAL		
Capital Appropriations (state)	\$ -	\$ -
HEFF	\$ 1,872,087.20	\$ 1,352,664.07
Capital Grants & Contracts	\$ 1,248,407.04	\$ 4,228,924.77
NET INCREASE (DECREASE) IN NET ASSETS	\$ 5,256,138.51	\$ 5,260,611.61
NET ASSETS		
Net Assets - Beginning of the year - restated	\$ 60,501,324.33	\$ 54,970,532.48
Net Assets - Beginning of the year adjustments	\$ (68,280.89)	\$ 270,180.24
Net Assets - End of the year	\$ 65,689,181.95	\$ 60,501,324.33

**UNIVERSITY OF SOUTH DAKOTA
STATEMENT OF CASH FLOWS
June 30, 2004**

CASH FLOWS FROM OPERATING ACTIVITIES

Tuition, Fees, (Net of Scholarship allowance & discounts)	\$ 30,435,481.97
General Sales & Services	\$ 7,214,202.42
Federal Grants & Contracts	\$ 29,311,043.16
State Grants & Contracts	\$ 565,464.93
Private Grants & Contracts	\$ 5,438,581.96
Auxiliary Enterprise	\$ 7,068,515.64
Collection on Loan Funds to Students	\$ 2,260,679.67
Disbursements on Loan Funds to Students	\$ (3,010,202.95)
Other (Net Change in Clearing Accounts)	\$ (372,564.06)
Personal Services (salaries & benefits)	\$ (73,098,276.30)
Travel	\$ (2,562,492.99)
Contractual	\$ (17,178,422.41)
Supplies & Materials	\$ (9,429,156.52)
Payments for Scholarships	\$ (9,783,836.29)
Other	\$ (1,053.28)
Loan Cancellation Reimbursement	\$ 188,017.00
Net cash provided (used) by operating activities	\$(32,954,018.05)

CASH FLOWS FROM NONCAPITAL FINANCIAL ACTIVITIES

General Fund Appropriations	\$ 41,669,740.96
School & Public Lands	\$ 126,570.00
Agency Funds (Net Change)	\$ 789,211.81
HEFF	\$ 87,983.00
Stafford Direct Lending Receipts	\$ 38,251,482.00
Stafford Direct Lending Disbursements	\$ (38,251,482.00)
Net cash flows provided by noncapital financing activities	\$ 42,673,505.77

CASH FLOWS FROM CAPITAL RELATED FINANCING ACTIVITIES

Capital Appropriations (state)	\$ -
HEFF	\$ 1,872,087.20
Federal Capital Contribution	\$ 619,983.03
Bond Proceeds	\$ -
Net Purchase of Capital Assets	\$ (10,543,978.49)
Capital Gifts	\$ 1,233,837.79
Principal Paid on Capital Debt and Leases	\$ (510,000.00)
Interest Paid on Capital Debt and Leases	\$ (968,570.60)
Net cash used by capital and related financing activities	\$ (8,296,641.07)

CASH FLOWS FROM INVESTING ACTIVITIES

Net cash provided (used) by investing activities	\$ 877,806.58
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Net Increase (Decrease) in Cash	\$ 2,300,653.23
Cash - Beginning of the year	\$ 26,530,435.82
Cash - End of the year	\$ 28,831,089.05

**UNIVERSITY OF SOUTH DAKOTA
STATEMENT OF CASH FLOWS
June 30, 2004**

**RECONCILIATION OF NET OPERATING REVENUES/(EXPENSES) TO
NET CASH PROVIDED/(USED) BY OPERATING ACTIVITIES**

OPERATING INCOME (LOSS)	\$ (39,263,086.89)
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities:	
Depreciation expense	\$ 6,020,643.66
CHANGES IN ASSETS AND LIABILITIES:	
Increase in Accounts Receivable	\$ (61,386.34)
Increase in Notes Receivable	\$ (633,876.95)
Decrease in Due from Component Units	\$ 130,431.59
Increase in Interest Receivable	\$ (13,733.70)
Increase in Inventory	\$ (107,903.91)
Increase in Due from Primary Government Entities	\$ (31,838.25)
Increase in Accounts Payable - Current	\$ 388,586.78
Increase in Accrued Wages & Benefits	\$ 62,732.16
Decrease in Compensated Absences Payable - Current	\$ 214,231.28
Decrease in Due to Primary Government Entities	\$ 31,216.33
Decrease in Student Deposits	\$ (6,700.00)
Increase in Accrued Interest Payable	\$ 216,282.33
Increase in Other Accrued Liabilities	\$ 205,889.01
Decrease in Deposits held in Trust	\$ -
Increase in Compensated Absences Payable - Non-current	\$ 10,645.37
Decrease in Due to Other Component Units	\$ (116,150.52)
NET CASH PROVIDED/(USED) BY OPERATING ACTIVITIES	<u>\$ (32,954,018.05)</u>

NON CASH TRANSACTIONS:

Gains/Loss on disposal of Assets	\$ (132,015.47)
FY04 Loan Principal Cancelled	\$ 223,179.68

Notes to the Financial Statements

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The University of South Dakota, the state's flagship university, is a growing, thriving university committed to excellence in education, research, and service. Accredited by the North Central Association of College and Schools since 1913, the University is a comprehensive, doctorate granting institution with a liberal arts undergraduate emphasis.

Founded in 1862 by the Dakota Territorial Legislature, USD is the state's oldest university. USD is an institution that recognizes the value of its past, even as it extends and expands its high quality programs and services to meet the challenges of tomorrow. USD is one of six public universities under the governance of the South Dakota Board of Regents, a nine-member board. Dr. Robert T. "Tad" Perry is executive director of the Board of Regents.

In December 1998 GASB released Statement No. 33, "Accounting and Financial Reporting For Non-exchange Transactions." In June 1999 GASB approved Statement No. 34, "Basic Financial Statements and Management Discussion and Analysis for State and Local Governments," followed by Statement No. 35, "Basic Financial Statements and Management's Discussion and Analysis for Public College and Universities." These statements were implemented for the fiscal year ended June 30, 2002. The change in financial statement presentation provides a comprehensive one-line look at the total university and requires capitalization of assets and the recording of depreciation. The recording of scholarship credit reduces Tuition & Fee income that has already been recorded.

A. Basis of Accounting:

The University is considered to be a special-purpose government engaged only in business-type activities. The University has adopted the accrual basis of accounting as required by generally accepted accounting principles in preparing its annual financial statements. Under the accrual basis of accounting, revenue is recognized when earned and expenditures when an obligation is incurred. The University is a component unit of the State of South Dakota. A separate Financial Statement will be issued for the University as well as included as a component unit in the State of South Dakota's Financial Statements.

B. Fund Accounting:

In order to ensure observance of the limitations and restrictions placed on the use of resources available to the University, the accounts of the institution are maintained in accordance with the principles of fund accounting. Fund accounting is the procedure by which resources are classified for accounting and reporting purposes into funds that are maintained in accordance with activities or objectives specified by donors, governmental appropriations, granting agencies, and other sources or regulations.

Separate accounts are maintained for each fund; however, in the accompanying statements, all funds are combined for reporting purposes.

C. Accounts Receivable:

Accounts Receivable consists of funds owed to various University departments at June 30, 2004 from external sources. Accounts Receivable would include funds owed from students for outstanding tuition & fee charges as well as funds owed to University departments from external sources for various sales & services. The University uses the direct write-off method for uncollectible receivables.

D. Interest Receivable:

The interest receivable consists of monies pooled together with the state's investment council monies that earn interest during the fiscal year. The earnings are prorated annually to the participating funds. The amounts included in the statements represent the actual interest earned by the Investment Council for FY04. The interest receivable also includes interest receivable on student loans.

E. Inventories:

Inventories of supplies are reported using the FIFO method or last invoice price.

F. Capital Assets:

Equipment includes \$15,398,373 which includes library books and films less depreciation. Library books and films are depreciated by the group method of depreciation at a straight-line depreciation over a 10-year period. Library books and films are assumed to be fully depreciated when they are deleted. The University has capitalized equipment in accordance with the Board of Regents policy. Primary criteria for capitalization include a useful life of one year or more and a unit cost in excess of \$5,000. The University uses the state's policy on useful life on equipment.

The building and other improvements total includes the total cost of \$16,002,037 less depreciation for the Law School, DakotaDome, Telecommunications Center Phase II, and the Akeley Science Center Addition. These buildings are totally or partially financed through the South Dakota Building Authority and are leased to the Board of Regents of the State of South Dakota. The Building Authority issued bonds to finance the cost of the construction and the lease payments made by the Board of Regents are in sufficient amounts to repay the principal and interest payments on the bonds. When the last payments have been made on the bonds, the Building Authority will transfer title to this property to the Board of Regents. Buildings of Major Structures have a useful life of 50 years, Buildings-Pole Type and Storage have a useful life of 25 years, and Buildings-Small will have a useful life of 10 years. Building improvements to all Buildings except Small Buildings would have a useful life of 20 years and Small Buildings would be 10 years.

Twenty percent of the tuition and fees deposited with the State Treasurer from all state-supported universities in South Dakota are allocated to the Higher Education Facilities Fund. This money is then used to make the lease payments as previously described, among other uses. Total HEFF revenue was \$3,320,483.15. The total allocation back to USD was \$1,872,087.20.

Capital Asset Activity for the Year Ended June 30, 2004				
	Beginning Balances	Increases	Decreases	Ending Balances
Capital assets not being depreciated:				
Land	\$ 945,215.41	\$ -	\$ -	\$ 945,215.41
Works of Arts & Historical Treasures	\$ 379,085.00	\$ -	\$ -	\$ 379,085.00
Construction in Progress	\$ 5,571,445.61	\$ 2,451,412.48	\$(5,194,107.23)	\$ 2,828,750.86
Total capital assets not being depreciated:	<u>\$ 6,895,746.02</u>	<u>\$ 2,451,412.48</u>	<u>\$(5,194,107.23)</u>	<u>\$ 4,153,051.27</u>
Capital assets being depreciated:				
Land Improvements	\$ 3,387,055.51	\$ 540,564.60	\$ -	\$ 3,927,620.11
Buildings and Improvements	\$ 83,095,426.21	\$ 6,709,079.84	\$ (656,941.00)	\$ 89,147,565.05
Machinery and Equipment	\$ 54,108,334.36	\$ 5,677,702.84	\$ (954,269.68)	\$ 58,831,767.52
Infrastructure	\$ 4,723,548.55	\$ -	\$ -	\$ 4,723,548.55
Total capital assets being depreciated	<u>\$145,314,364.63</u>	<u>\$12,927,347.28</u>	<u>\$(1,611,210.68)</u>	<u>\$156,630,501.23</u>
Less accumulated depreciation for:				
Land Improvements	\$ 468,741.02	\$ 136,254.37	\$ -	\$ 604,995.39
Buildings and Improvements	\$ 38,264,239.80	\$ 2,659,471.79	\$(512,393.10)	\$ 40,411,318.49
Machinery and Equipment	\$ 41,143,187.95	\$ 2,839,374.36	\$(549,167.48)	\$ 43,433,394.83
Infrastructure	\$ 3,099,380.15	\$ 144,388.14	\$ -	\$ 3,243,768.29
Total accumulated depreciation	<u>\$ 82,975,548.92</u>	<u>\$ 5,779,488.66</u>	<u>\$(1,061,560.58)</u>	<u>\$ 87,693,477.00</u>
Total capital assets being depreciated, net	<u>\$ 62,338,815.71</u>	<u>\$ 7,147,858.62</u>	<u>\$(549,650.10)</u>	<u>\$ 68,937,024.23</u>
Capital Assets, Net	<u>\$ 69,234,561.73</u>	<u>\$ 9,599,271.10</u>	<u>\$(5,743,757.33)</u>	<u>\$ 73,090,075.50</u>

G. Long Term Liabilities:

Summary of Changes in Long-term Liabilities for Year Ended June 30, 2004

	Interest Rate	Maturity Date	Balance 07/01/2003	Additions	Reductions	Balance 06/30/2004	Due within one year
Housing and Auxiliary Facilities Revenue Bonds, Series 2003	2-5%	04/01/28	\$16,435,000.00	--	\$(290,000.00)	\$16,145,000.00	\$325,000.00
2000 Dakota Dome Roof Long-Term Lease	4.5- 6.5%	09/01/24	\$6,260,000.00	--	(150,000.00)	6,110,000.00	155,000.00
1997 Old Main Long-term Lease	5.5%	07/01/21	2,068,000.00	--	(70,000.00)	1,998,000.00	75,000.00
TOTAL			\$24,763,000.00	--	\$(510,000.00)	\$24,253,000.00	\$555,000.00

Compensated Absences:					
Sick Leave Liability	\$5,482,189.34	\$875,678.16	(\$727,679.02)	\$5,630,188.48	\$750,419.27
Annual Leave Liability	3,236,040.03	1,572,565.92	(1,500,085.29)	3,308,520.66	1,533,684.11
Comp Time Liability	27,015.71	4,396.88	--	31,412.59	31,412.59
Federal Portion of Loan Programs	11,324,505.34	616,272.22	--	11,940,777.56	--
TOTAL	\$44,832,750.42	\$3,068,913.18	\$(2,737,764.31)	\$45,163,899.29	\$2,870,515.97

Liabilities payable at 6/30/2004 is comprised of the following:

Revenue Bonds:

Housing and Auxiliary Facilities Revenue Bonds, Series 2003,
2 to 5 percent interest, Final Maturity Date of April 1, 2028. \$16,145,000.00

Long-Term Leases:

2000 Long-term Lease Obligation with South Dakota Building Authority (Dome Roof)
4.5 to 6.5 percent interest, Final Maturity Date of September 1, 2024. \$1,998,000.00

1997 Long-term Lease Obligation with South Dakota Building Authority (Old Main)
5.5 percent interest, Final Maturity Date of July 1, 2021. \$6,110,000.00

Other Obligations:

Compensated Absences:

Amount owed by USD to employees for their accrued annual leave, sick leave,
And comp time balances, including benefits, to be paid from various accounts \$8,970,121.73

Federal Loans:

Cumulative federal capital contributions for Federal Perkins/Direct, Health Profession,
Nursing Student, and Disadvantage Student loan programs \$11,940,777.56

Federal loans to students and compensated absences have been determined to be long-term liabilities.

Annual leave is earned by state of South Dakota employees. Upon termination, employees are eligible to receive compensation for their accrued leave balance.

Effective July 1, 1979, any employee who had been continuously employed by the State of South Dakota for at least seven years prior to the dates of their retirement, voluntary resignation, or death shall receive payment for one-fourth of their accumulated sick leave balance. Such payment is not to exceed the sum of twelve weeks of the employee's annual compensation.

Net pledged revenue of \$1,138,907.32 consists of revenues from Auxiliary Services and is available as security for debt service.

The accrued annual and sick leave is reflected as an expense for FY04 for all accrued leave through June 30, 2004 in the appropriate fund group.

Principal and interest on long-term debt are payable from operating revenues, allocated student fees and the excess of revenues over expenditures of specific auxiliary activities. The future amounts of principal and interest payments required by the debt agreements (excluding federal loans and compensated absences) are as follows:

Year Ending June 30.	<u>Revenue Bonds</u>		<u>Long-Term Leases</u>		<u>TOTAL</u>
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	
2005	325,000.00	646,286.26	230,000.00	449,082.51	1,650,368.77
2006	515,000.00	639,786.26	245,000.00	437,476.26	1,837,262.52
2007	525,000.00	629,486.26	255,000.00	423,511.26	1,832,997.52
2008	535,000.00	618,198.76	270,000.00	407,411.26	1,830,610.02
2009	545,000.00	604,823.76	285,000.00	390,386.26	1,825,210.02
2010-2014	2,905,000.00	2,763,743.78	1,710,000.00	1,710,000.00	9,088,743.78
2015-2019	3,110,000.00	2,226,512.52	2,245,000.00	2,110,000.00	9,691,512.52
2020-2024	3,870,000.00	1,465,531.30	2,383,000.00	609,652.50	8,328,183.80
2025-2029	3,815,000.00	451,168.78	485,000.00	54,435.00	4,805,603.78
TOTAL	\$16,145,000.00	\$10,045,537.68	\$8,108,000.00	\$6,591,955.05	\$40,890,492.73

H. Operating Leases

A summary of changes in operating leases follows:

	<u>Balance</u> <u>7/1/2003</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>6/30/2004</u>
Xerox Operating Lease – Copiers	\$2,468,784.76	\$0.00	\$(615,852.76)	\$1,852,932.00
Panasonic Lease – Copiers	3,096.72	0.00	(2,185.92)	910.80
Lab. Facilities & Equipment Lease	2,176,721.00	0.00	(504,034.00)	1,672,687.00
TOTAL	\$4,648,602.48	\$0.00	(\$1,122,072.68)	\$3,526,529.80

The University has entered into operating leases with Xerox and Panasonic for copier services. Payments are payable from auxiliary Services operating revenues. The University also entered into an operating lease with The South Dakota Health Research Foundation (SDHRF) for laboratory facilities, equipment, and related operating support services specific to the Cardiovascular Research Institute (CRI) operated under the auspices of SDHRF. Payments to SDHRF are payable from indirect cost recovery received for personnel associated with CRI.

The following is a schedule of the University's aggregate minimum payments for existing operating leases:

For Year Ended June 30, 2005	\$1,046,644.40
2006	1,048,691.60
2007	977,187.60
2008	454,006.20
2009	0.00
Total	\$3,526,529.80

I. Net Assets:

Net assets are classified according to external donor restrictions or availability of assets for satisfaction of University obligations. The “Invested in Capital, 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. Expendable Restricted Net Assets represents funds that have been received for specific purposes.

J. Scholarship Allowance and Student Aid:

Allocating Scholarship Allowances

		Percent	Scholarship Allowance Allocation \$4,511,235.45	Expense Allowance
Institutional Resources Provided as Financial Aid				
Supplemental Educational Opportunity Grant SEOG	\$432,821.81	4.58	\$235,647.29	\$197,174.52
Pell Grants	4,808,208.77	50.83	2,617,800.97	2,190,407.80
Other Fed Scholarships	80,641.27	0.85	43,904.66	36,736.61
Institutional Scholarships	3,270,856.72	34.58	1,780,798.69	1,490,058.03
Athletic Scholarships	866,703.99	9.16	471,871.89	394,832.10
Non-monetary Institutional waivers				
Institutional	0.00	0.00%	0.00	0.00
Residential Life	0.00			0.00
Bookstore	0.00			0.00
Total	<u>\$9,459,232.56</u>	<u>100.00%</u>	<u>\$5,150,023.51</u>	<u>\$4,309,209.05</u>

Allocation Ratio for Tuition Discount & Student Aid Expense:

Tuition & Fee Allocation & Tuition & Fees Local (Schedule C in Management Report)	\$30,643,064.65	81.26%	\$4,184,722.63
Auxiliary Revenue (Schedule C in Management Report)	\$7,068,515.64	18.74%	\$965,300.88

K. Operating and Non-Operating Revenues:

Operating – Revenue Transactions that result from the everyday activity of the University.

Non-Operating – Revenue Transactions that result from non-capital financing, capital and related financing, investing activities and any other revenues that are not considered operating.

L. Cash and Cash Equivalents:

For reporting purposes, cash includes cash on hand, cash in local banks, and cash in the State Treasury. Cash equivalents include short-term investments with original maturities of three months or less.

M. Related Parties:

The financial statements do not include the assets, liabilities, or fund balances of affiliated organizations, whose financial statements are separately audited. The USD Foundation is the only related party of the University of South Dakota.

N. Investments:

Investments consist of funds on deposit with the State Treasurer which are pooled by the State Investment Council for investment purposes. Interest earnings on Current Funds investments are not received by the University but are credited to the State of South Dakota's General Fund. In addition, interest earnings are received for Investments in the Renewals and Replacements Fund, Retirement of Indebtedness Fund, and Unexpended Plant Fund.

Interest earnings are credited to the Perkins Student Loan Program, Nursing Student Loan Program, and Health Professions Student Loan Program based upon the State Investment Council prorated rate of return.

O. Due to/Due From:

Due from Federal Sources represents federal monies owed the University but has not been received yet.

Due from Primary Government represents funds owed from various state agencies of South Dakota, outside of Higher Education. Due to Primary Government represents funds owed to various state agencies of South Dakota, outside of Higher Education.

Due From Other Component Units represent funds owed from other South Dakota public universities or the South Dakota Board of Regents. Due to Other Component Units represents funds owed to other South Dakota public universities or the South Dakota Board of Regents.

All funds owed to or from other university funds have been eliminated for financial reporting purposes.

2. RETIREMENT PLAN

The institution participates in a mandatory retirement program administered by the South Dakota Retirement System. Expenditures under this program for the year ended June 30, 2004 were \$3,296,591.45.

3. ANNUAL AND SICK LEAVE ACCRUAL

Annual leave is earned by State of South Dakota employees. Upon termination, employees are eligible to receive compensation for their accrued annual leave balance.

Effective July 1, 1979, any employee who had been continuously employed by the State of South Dakota for at least seven years prior to the date of their retirement, voluntary resignation, or death shall receive payment for one-fourth of their accumulated sick leave balance. Such payment is not to exceed the sum of twelve weeks of the employee's annual compensation.

The accrued annual and sick leave is reflected as an expense for FY04 for all accrued leave through June 30, 2004.

4. STATE APPROPRIATIONS/TUITION AND FEES

State appropriations totaled \$41,884,293.96. The University collected and remitted \$20,298,286.40 of tuition and fees to the Tuition and Fee Fund maintained by the Board of Regents Office. Of that amount, \$3,320,483.15 was transferred to the Higher Education Facilities Fund. The tuition and fees collected and remitted to the Tuition and Fee Fund are not reported as revenue in the University's financial statements. Only the amount returned to the University as a tuition allocation from the fund is reported as revenue. The allocation received in FY04 was \$13,545,715.00.

5. ENDOWMENT AND SIMILAR FUNDS

The assets of the endowment and similar funds administered by the Department of School and Public Lands have not been included in the financial statements. For the year ended June 30, 2004, the assets within the funds, based upon unaudited information provided by the Department of School and Public Lands, consisted of (1) receivables recorded at \$1,866,000 and (2) cash and securities with a cost of \$131,342,000 and (3) 9,628.25 acres of undeveloped land.

6. CASH AND CASH EQUIVALENTS

Cash includes deposits held at banks, both the University's bank and the State of South Dakota's bank, plus small amounts maintained for change funds.

7. OPERATING AND NON-OPERATING REVENUE

Simply stated, operating transactions that are to be used to determine operating income:

- Sales of goods or services (including accounts receivable from these sales (students)).
- Grant receipts for activities that are a part of operations.
- Quasi-external operating transactions with outside agencies.
- Reimbursement of operating transactions.
- All other cash receipts that do not result from transactions defined as capital and related financing, noncapital financing, or investing activities.
- All other that does not fit above are considered non-operating.

8. FUNDS HELD FOR OTHERS

Funds held for others consist of federal loan program balances and funds held for other students. Assets of the federal loan program are student loans receivable and the funds held for students, including student organizations, are principally cash.

Student Receivable	\$1,089,483.20
Cash held for others	\$1,092,770.95

9. CONSTRUCTION IN PROGRESS

Schedule of Changes in Construction in Progress

Balance 6/30/03	Net Change		Balance 6/30/04
	<u>Increases</u>	<u>Decreases</u>	
\$5,571,446	2,451,412	(5,194,107)	\$2,828,751

10. INVESTED IN CAPITAL, NET OF RELATED DEBT

Capital Investment	\$73,090,075.50
Plus Bond Proceeds that remain unspent	\$12,395,963.69
Related Debt	<u>(\$ 24,253,000.00)</u>
Invested in Capital, Net of Related Debt	\$61,233,039.19

11. PRIOR PERIOD ADJUSTMENTS

The University had prior period adjustments which decrease the beginning Net Assets by \$68,280.89. This was done to adjust cash on deposit state treasurer and to decrease Net Assets per adjustment.

**FUNCTIONAL CLASSIFICATION OF EXPENSES AND DEPRECIATION
06/30/2004**

	Personal Services	Travel	Contractual	Supplies & Non- Capitalized Equipment	Grants & Subsidies	Other	Depreciation	Total
Instruction	\$37,078,388.34	\$670,944.69	\$4,561,229.51	\$1,540,127.25	\$72,276.82	\$2,760.22		\$43,925,726.83
Research	5,269,262.14	319,008.38	2,496,011.96	1,716,237.84	338,490.09	11,006.85		10,150,017.26
Public Service	5,922,738.83	412,970.58	3,367,603.15	646,595.68	109,063.59	20,333.74		10,479,305.57
Academic Support	10,299,618.89	308,256.63	1,687,308.33	1,220,240.07	11,309.74	12,921.03		13,539,654.69
Student Services	4,188,931.51	599,601.57	1,147,917.76	7,,2642.03	2,051.25	241,259.98		6,925,404.10
Institutional Support	4,901,405.37	135,597.61	435,548.16	221,926.69	78,373.89	542.50		5,773,394.22
Operations & Maint	3,535,626.00	71,994.19	95,801.65	2,474,988.73	630.00	22.00		6,179,062.57
Scholarships & Fellow	7.00		(28.01)	958.27	4,633,812.78			4,634,750.04
Auxiliary Enterprises Depreciation (Unallocated)	2,175,534.08	25,535.48	3,346,662.95	837,354.31		135.53	6,020,643.66	6,385,222.35
TOTAL	\$73,371,512.16	\$2,543,909.13	\$17,139,055.46	\$9,403,070.87	\$5,246,008.16	\$288,981.85	\$6,020,643.66	\$114,013,181.29