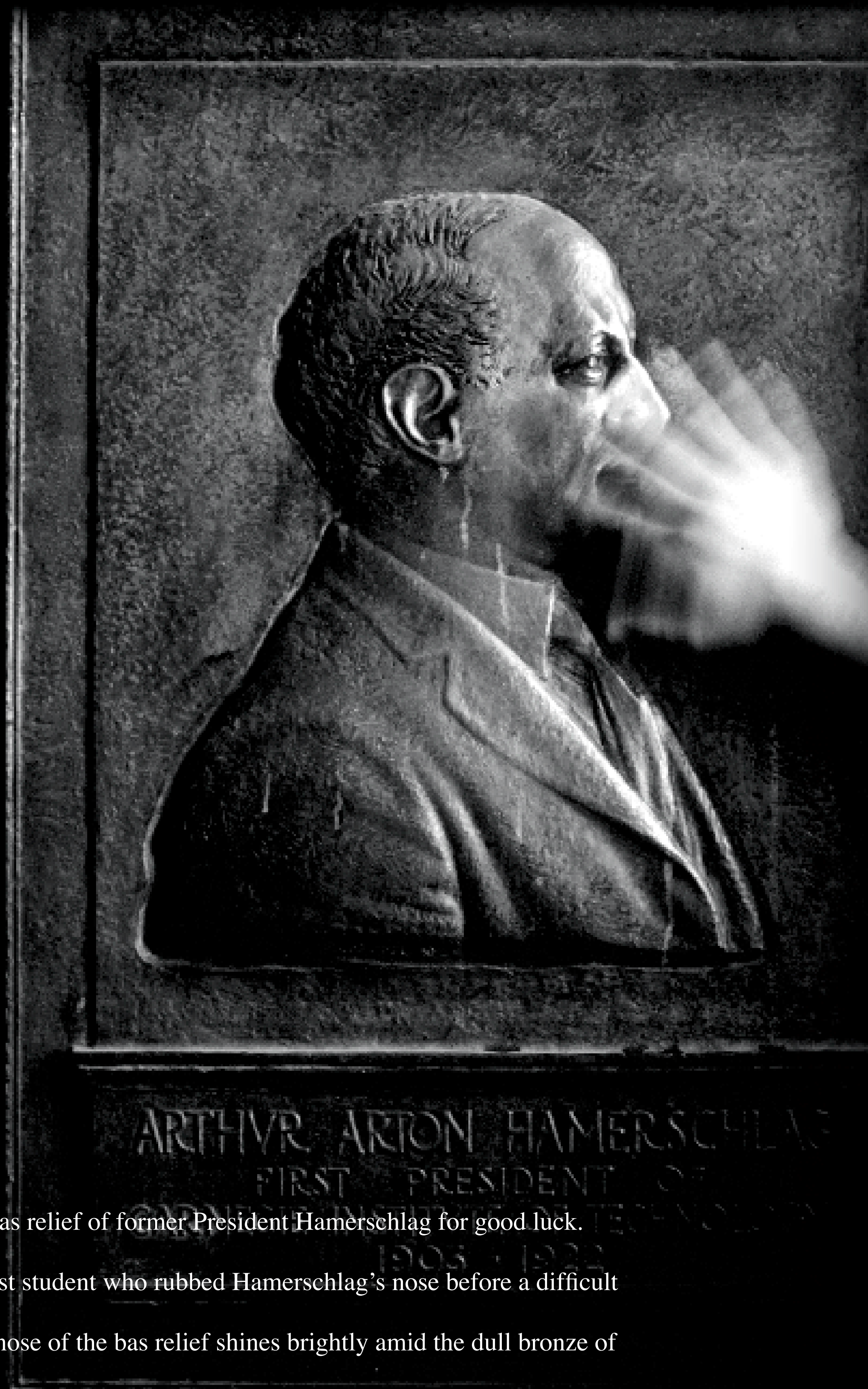
2003 ANNUAL REPORT

Carnegie Mellon

TABLE OF CONTENTS



A Carnegie Mellon tradition;

Students rub the nose of this 1928 bas relief of former President Hamerschlag for good luck. According to campus legend, the first student who rubbed Hamerschlag’s nose before a difficult exam aced the test. To this day, the nose of the bas relief shines brightly amid the dull bronze of the rest of the sculpture.

On the cover:
An engraved rendering of Hamerschlag Hall, named for Arthur A. Hamerschlag, first president of Carnegie Institute of Technology, and Dante, one of Carnegie Mellon's historic robots. Dante opened a new era in field techniques by enabling scientists to remotely and safely conduct research in dangerous terrains, such as active volcanoes.

Innovative Visionary Global Diverse Relevant

This year at Carnegie Mellon we made these concepts come alive once again. What's more, we did it our way. Our distinctive, multi-disciplinary and collaborative style transcends the traditional barriers between technology and the arts, while balancing innovation and research with a deep concern for its impact on people.

We remain a highly focused institution consistently ranked among the nation's top universities. Although we ranked 23rd in the *U.S. News and World Report* Annual Survey of "America's Best Colleges," Carnegie Mellon isn't 23rd in anything. We don't do everything, but all that we do is ranked among the very best programs. Our undergraduate programs in engineering and business were ranked among the ten best in the country. Carnegie Mellon continues to make a strong showing in another of the magazine's "best" categories — that of "undergraduate research/creative projects." I am particularly pleased that our creative efforts in undergraduate education and our vibrant, undergraduate research program continue to be recognized as trendsetters. And, our business school was ranked by *The Wall Street Journal* as sixth best in the world and number one in technology and operations management.

We remain a highly focused institution consistently ranked among the nation's top universities.

Only at Carnegie Mellon will you find computer scientists and public policy specialists, drama students and roboticists, astrophysicists and biologists, psychologists and engineers working together, asking the right questions and solving some of the world's greatest problems. Only at Carnegie

JARED L. COHON

Mellon will you find academically gifted musicians drawn to a world-class conservatory, while simultaneously pursuing studies in physics, history or business.

As a result, our students experience a rich environment, grounded in our commitment to diversity. That's why in February we supported the University of Michigan in our *amicus curiae* brief, and its practice of considering an applicant's race in admissions decisions. I am proud to say that 38 other private, selective colleges and universities joined us in that effort. Diverse perspectives and backgrounds breed the intellectual vitality essential for the health and progress of the university. Simply put, students who learn in a socially and intellectually diverse environment are better prepared for success in a diverse world. Our young people deserve nothing less.

But diversity, by Carnegie Mellon's definition, transcends race and gender to include interdisciplinary research and educational opportunities reflecting an increasingly interconnected world. To that end, we have developed partnerships with institutions in India, China, Germany, Greece, Italy, Latin America and South Africa. Recently, we extended our global boundaries even further with collaborations in Singapore and Taiwan. Our exploration of undergraduate computer science and business programs in Education City in the nation of Qatar has the potential to break new ground in cross-cultural communications between Islamic countries and the West.

Diversity, by Carnegie Mellon's definition, transcends race and gender to include interdisciplinary research and educational opportunities...

In addition, the university's Institute for Strategic Development earned two prestigious awards this year for providing on-campus students with a global learning experience. The "ACE/AT&T Award for Technology as a Tool for Internationalization," presented by the American Council on Education (ACE), recognizes the innovative use of technology to promote international learning at U.S. colleges and universities. Using advanced communications technology, we linked our students, in real time, with their peers at the Delft University of Technology in the Netherlands and at Monterrey Tech in Monterrey, Mexico in virtual team-based class projects that facilitated educational dialogue and collaborative problem solving. The Institute of International Education for Technology-Enhanced Global Learning also recognized this same program for its impact.

I am proud to share a few more examples of how Carnegie Mellon made a difference this year — from a rural town in Appalachia to the nation and the world.

Glenville, West Virginia, is a small community located in the central part of the state in the heart of Appalachia. Overlooked by commercial Internet providers, residents, businesses and schools were forced to depend on slow, costly dial-up service to connect to the Internet. Now, thanks to Carnegie Mellon's Center for Appalachian Network Access (CANA) and a $250,000 grant from the Claude Worthington Benedum Foundation, Glenville will go "wireless" and join the rest of the world via high speed Internet connectivity. This project, which involves Carnegie Mellon students, faculty and alumni from a variety of disciplines, including computer science, mathematics, business and public policy, will raise both the economic and literacy profile of the region.

Technology and relevance are common threads that weave these wonderful stories together *and* permeate the university's culture. In fact, government and industry leaders frequently tell us they rely on Carnegie Mellon "to get things done."

Recently, the U.S. Department of Homeland Security (DHS) tapped Carnegie Mellon's CERT® Coordination Center (CERT/CC), formed in 1988 within the Software Engineering Institute (SEI), to create US-CERT, the national coordination point for

In fact, government and industry leaders frequently tell us they rely on Carnegie Mellon "to get things done."

prevention, protection and response to cyberattacks across the Internet. This honor follows a $35.5 million grant to our Center for Computer and Communications

Security (C3S) from the Department of Defense to create a cybersecurity laboratory, a new network security paradigm to tackle challenges related to Internet security, data storage and privacy issues stemming from America's ongoing war against terrorism. U.S. Secretary of Homeland Security Tom Ridge called US-CERT "a key element to our national strategy to combat terrorism and protect our critical infrastructure." There is no question that Carnegie Mellon remains the national and international leader in cybersecurity. In this critical space, we combine our outstanding people and programs in computer science, robotics, software engineering, artificial intelligence, information technology (IT), public policy and business to ensure that our country is safe and the privacy of our fellow citizens secure.

Our West Coast Campus, in Silicon Valley, is a natural outgrowth of our leadership in technology. This year,

There is no question that Carnegie Mellon remains the national and international leader in cybersecurity.

we celebrated our first graduating class, composed of 17 students who received master's degrees in information technology with specializations in software engineering, e-business technology and the learning sciences. Established in September 2001, the West Coast Campus is the university's first branch, stressing programs that closely simulate real-world workplace experience.

Carnegie Mellon chemists also did their part this year to protect our world — and our environment. Our Institute for Green Chemistry developed a powerful, yet environmentally friendly catalyst called Fe-TAML®, that has the potential to kill the lethal strain of anthrax, a possible biological weapon in the hands of terrorists, and to control water-borne infectious diseases that account for significant death and disability worldwide. Dubbed "green peroxide" by *USA Today*, Fe-TAML also can break down toxic agricultural pesticides and clean up water polluted by textile, pulp and paper mills.

Co-Lab is just one of the many initiatives we have undertaken to support the economic growth of Pittsburgh and southwest Pennsylvania.

The Virtual Chemistry Laboratory, a networked computing environment in which students can select from hundreds of standard chemical reagents and safely combine them to create virtual experiments, won the MERLOT Classic and Editors' Choice Awards for Exemplary Online Resources. The Editor's Choice Award is the highest honor given by the Multimedia Educational Resource for Learning and Online Teaching (MERLOT). More than 7,000 students from Carnegie Mellon and four other universities in Canada, the United States and Mexico have used the virtual lab with great success.

Other noteworthy achievements this year include:

- The opening of our new dormitory, one of the healthiest and most energy-efficient residence halls in the country, as well as the first dormitory to be certified at the Silver Level by the Leadership in Energy and Environmental Design Green Building Rating System.

- Ground breaking for the Collaborative Innovation Center (Co-Lab), a state-of-the-art research facility located on campus, which can provide our corporate partners, involved in technology research access to the world's most talented faculty and students. Co-Lab is just one of many initiatives we have undertaken to support the economic growth of Pittsburgh and southwest Pennsylvania.

- Continued support and steadfast partnership with the Pittsburgh Public Schools, including a myriad of activities offered on our campus and in neighborhood schools. An excellent example of this support is a program developed by an instructor in the School of Music that employs Hip Hop to teach inner-city youngsters basic math.

- Ground breaking of the Posner Center, a building to house a collection of rare books and artifacts, made possible by a gift from Henry and Helen Posner.

- Planning for the rooftop garden, featuring the work of renowned artist and alumnus, Mel Bochner, A'62, made possible by trustee and alumna, Jill Kraus, A'74, and her husband, Peter.

> We will maintain our tremendous momentum by remaining committed to leveraging our core strengths in technology, the arts, business and public policy...

We also celebrated the successes of our alumni who continue to garner recognition and awards for their achievements, including John Wells, A'79, who won his fourth Emmy for the acclaimed television program *The West Wing,* and Rob Marshall, A'82, whose directorial debut, *Chicago,* captured six Oscars.

With all of this success this year, what do we have planned as an encore?

We will maintain our tremendous momentum by remaining committed to leveraging our core strengths in technology, the arts, business and public policy, celebrating our diversity and preparing for the 100th

> Most important, we remain committed to educating young men and women who are both visionaries and doers — that is: leaders for the 21st century.

Anniversary of the College of Fine Arts, the 25th Anniversary of our Robotics Institute and the launch of the world's first Robot Hall of Fame. Most important, we remain committed to educating young men and women who are both visionaries and doers – that is: leaders for the 21st century.

JARED L. COHON
President
Carnegie Mellon University
October 8, 2003

Hamerschlag Hall

FINANCIAL HIGHLIGHTS

A great research university requires excellence in multiple dimensions. In the preceding pages, President Cohon focused on the splendid academic achievements of the past year. Here we present an overview of the financial dimension critical to the university's continued expansion.

In this context, I am pleased to report Carnegie Mellon's positive operating results for fiscal year 2003, leading to a strong balance sheet and an increase in net assets.

2003 Summarized Results (in thousands)

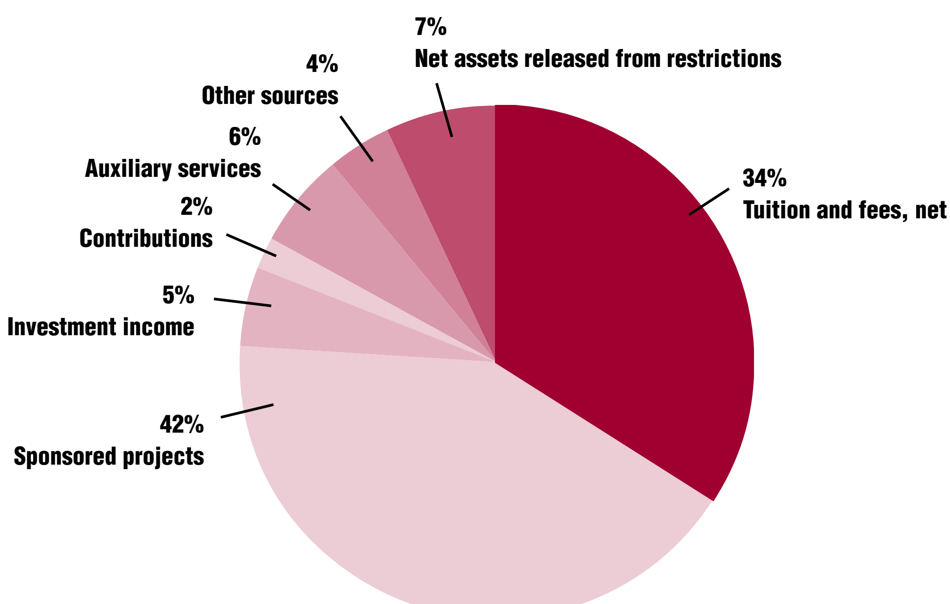
Unrestricted operating revenue and support	$ 576,993
Unrestricted operating expenses	559,755
Change in unrestricted net assets from operations	**17,238**
Decrease in unrestricted net assets from non-operating activities	(5,634)
Change in temporarily restricted net assets	(22,528)
Change in permanently restricted net assets	12,141
Increase in net assets	**1,217**

These results are particularly significant because they were accomplished despite a continuing weak economy and a turbulent equity market (see the Treasurer's Report on Investments following).

Operating Revenue

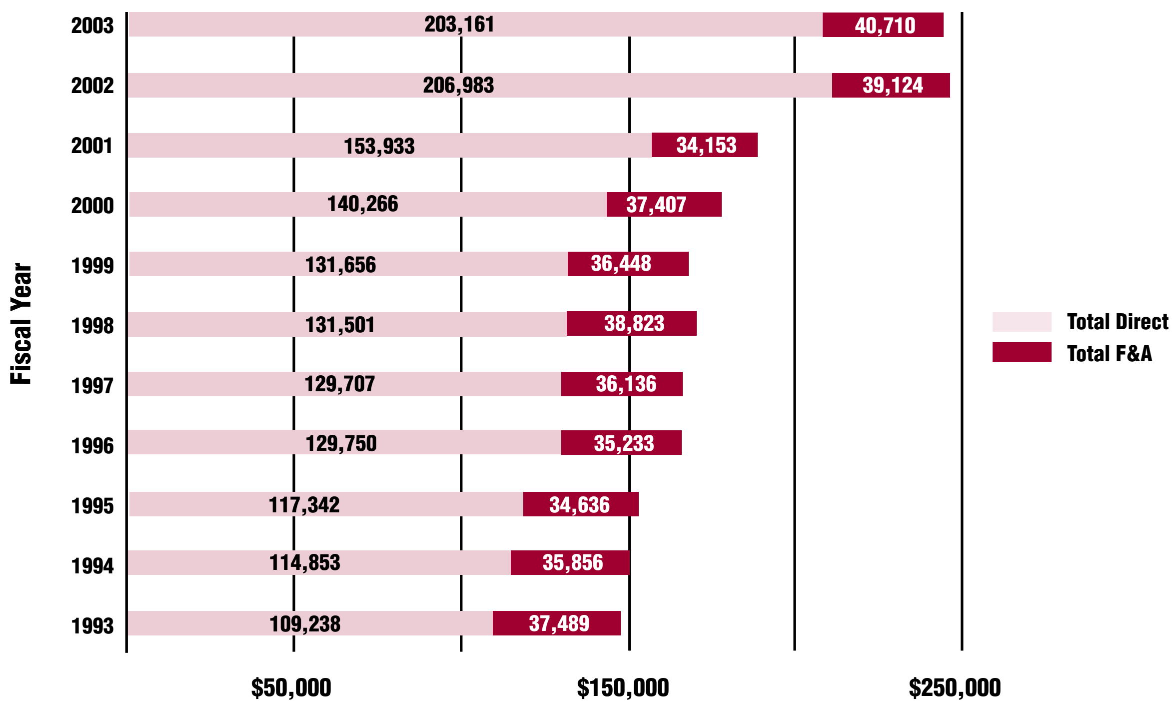
Carnegie Mellon, like its peer institutions, remains dependent on four major categories of revenue: tuition (net of financial aid), research (more precisely defined as sponsored activities), private support (composed of investment income and contributions) and revenue generated by sales of auxiliary services, such as housing and meals. The fiscal 2003 results continue to reflect strong performance in our core education and research activities, leaving the relative proportions of the four revenue streams fundamentally unchanged.

Fiscal 2003 Operating Revenue



The sponsored activities revenue trend is especially notable. As shown in the chart below, over the past 10 years this revenue stream has grown 66%, from $147 million to $244 million[1]: Very few other universities have gone so far so fast.

Sponsored Projects Revenue



The growth in tuition and other educational fees, net of financial aid, was consistent with increases in tuition rates, the number of graduate students and the increased demand for executive education. These figures represent the tangible impact of our flourishing educational and research programs. The following tables show enrolled students in the fall semester of 2002 by school and other enrollment data.

2002 Fall Semester Enrollment

School	Percentage	Number of Students
Carnegie Institute of Technology	24%	2,233
Graduate School of Industrial Administration	16%	1,496
College of Humanities & Social Sciences	14%	1,311
College of Fine Arts	13%	1,220
School of Computer Science	12%	1,104
Mellon College of Science	8%	803
Interdisciplinary	7%	688
H. John Heinz III School of Public Policy and Management	5%	518
Non-Degree & Other	1%	128
Total	100%	9,501

[1] A small decrease in fiscal 2003 is explained by the impact of a non-recurring, equipment-related project in the prior year.

Fall Enrollment Headcount by Class

	1998	1999	2000	2001	2002
Undergraduate	5,050	5,136	5,106	5,194	5,347
Graduate	3,013	3,174	3,290	3,278	4,026
Non-Degree	122	126	118	116	128
Total Headcount	8,185	8,436	8,514	8,588	9,501

Undergraduate Admissions - Fall Semester

	1998	1999	2000	2001	2002
Applications	13,202	14,130	14,621	16,696	14,271
Acceptances	5,598	5,358	5,241	5,211	5,440
Matriculations	1,308	1,254	1,329	1,318	1,365

Philanthropic support for our unrestricted operations remained strong at $9.1 million, despite the current unfavorable conditions in financial markets. Carnegie Mellon remains deeply appreciative of this support.

Operating Expenses

Operating expenses increased by 1.6%, totaling $559.8 million due principally to the growth in sponsored research programs and related research expenses. By far the largest operating expenses are salaries and benefits, where growth is driven by increases in number of employees, as well as rate of pay. Expense growth in all categories is consistent with the growth of the university and our objectives for cost containment.

Overview of Balance Sheet

Total assets at June 30, 2003 were $1,498 million, 1% higher than a year ago. Investments, which represent 55% of total assets, declined by $14.1 million, or 1.7%. This reduction in assets was primarily due to a decrease in the endowment from the excess of distributions over positive investment returns and new gifts and other additions. Cash and cash equivalents increased by $14 million, principally from operating activities.

During fiscal year 2002, Carnegie Mellon issued $44.7 million of tax-exempt bonds to fund capital projects, and at June 30, 2003, the unspent proceeds of $7.5 million were held in trust to pay for the completion of the projects.

Overall net assets increased $1.2 million in the year ended June 30, 2003. Though small in absolute terms, this number represents an important and desirable reversal of the decreasing trend of the two prior fiscal years.

Additions to Buildings and Equipment

The university completed two major projects and broke ground on two more, continuing construction on the main campus within guidelines of a Master Plan approved by the Pittsburgh City Council in May 2002.

Construction was completed on an 8-story addition to Doherty Hall for chemistry labs, where $5 million was expended in fiscal year 2003. This addition significantly expands and enhances interdisciplinary laboratories supporting science education. The university also completed construction of a new freshman dormitory. This dormitory was first occupied by students in the fall of 2003. These projects have been funded through an amalgam of fundraising, debt financing and future cash flows through the auxiliary operation of the new dormitory. In addition to these major building projects, significant investments were made to renovate and upgrade research laboratories, classrooms and physical infrastructure of the university.

We also broke ground on these new campus construction projects. They are:

- Collaborative Innovation Center, a state-of-the-art research facility that will provide our corporate partners access to the world's most talented faculty and students, funded with the help of the Regional Industrial Development Corporation of Southwestern Pennsylvania.

- Posner Center, a new building that will house the Posner collection of rare books and artifacts, made possible by a gift from Henry and Helen Posner.

- A rooftop garden, featuring the work of renowned artist and alumnus Mel Bochner, made possible by trustee and alumna Jill Kraus and her husband, Peter.

Expenditures for buildings and equipment were $56.0 million in fiscal year 2003, including movable equipment of $21.1 million, and buildings and construction of $34.9 million. These additions are offset by $38.8 million in depreciation expense.

Long-Term Debt

External debt outstanding at June 30, 2003 was $308.4 million, representing 68% of total liabilities. Long-term debt decreased by $2.1 million from $310.5 million at June 30, 2002, principally due to a decrease in capital lease obligations. Virtually all of the university's outstanding debt matures in 2025 and beyond.

Overview of Investment Results by Treasurer John Mazur

The performance of the university's long-term investments for the fiscal year ending June 30, 2003 was 2.3%. This positive result, while modest, was a welcome change after two consecutive years of negative returns.

Markets during the fiscal year continued to be volatile, with equities showing declines for the first half of the year until reversing at mid-year. Good equity returns since then have continued through the end of the fiscal year.

The university's endowment value as of June 30, 2003 was $654.7 million compared to $667.8 million at the end of the prior fiscal year. Positive investment performance of $16.2 million and gifts and other additions of $12.4 million partially offset distributions made under the university's spending policy. The endowment's distributions of $41.7 million in 2003 provided key support to the university's operations.

Financial Outlook

Carnegie Mellon has never been stronger. With 14,271 applications for the 2003 freshman class of 1,365, education remains the foundation upon which we build our future. And this foundation is poised to become even more diverse, even more multicultural, as we contemplate a major new effort in a foreign land. At the same time, with a unique spectrum of strengths in areas of national priority, the pace of growth of our research, already fast in the year just past, will accelerate again, as our faculty mobilizes to coordinate sponsored activities across the university.

Both dimensions have important financial implications. On the education side of the house, we anticipate the need to enhance financial aid allocations to address reduced capabilities of students and parents to pay the full cost of attendance in an unsettled economic environment. On the research side, our unprecedented growth will require additional resources, not the least of which pertain to operating space.

While we do not underestimate these demands, we face them from the vantage point of a strong balance sheet. The university also has an ingrained habit of allocating financial resources rapidly and efficiently. These assets will enable us to make excellent use of the opportunities inherent in the fiscal challenges.

Stefano Falconi

STEFANO FALCONI
Vice President for Administration and Chief Financial Officer
Carnegie Mellon University
October 8, 2003

AUDITED CONSOLIDATED FINANCIAL STATEMENTS

Margaret Morrison Carnegie Hall

To the Board of Trustees
Carnegie Mellon University and Subsidiaries
Pittsburgh, Pennsylvania

We have audited the accompanying consolidated statements of financial position of Carnegie Mellon University and subsidiaries as of June 30, 2003 and 2002, and the related consolidated statements of activities and cash flows for the years then ended. These consolidated financial statements are the responsibility of the university's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Carnegie Mellon University and subsidiaries as of June 30, 2003 and 2002, and the changes in their net assets and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

Pittsburgh, Pennsylvania
October 8, 2003

Consolidated Statements of Financial Position

June 30, 2003 and 2002
($ in Thousands)

	2003	2002
Assets		
Cash and cash equivalents	$ 69,889	$ 55,886
Accrued interest and dividends	2,650	3,184
Accounts receivable, net (Note C)	64,956	45,987
Pledges receivable (Note D)	36,950	37,907
Loans receivable (Note C)	15,119	14,216
Investments (Note E)	832,138	846,242
Assets held in trust by others	12,238	33,780
Other assets	11,354	10,420
Land, buildings and equipment, net (Note H)	453,053	436,366
Total assets	**$1,498,347**	**$1,483,988**
Liabilities		
Accounts payable and other liabilities	$ 58,644	$ 56,775
Deferred revenue	51,478	36,076
Federal loan programs	14,077	14,266
Present value of future annuities payable	18,360	20,194
Long-term debt (Note I)	308,385	310,491
Total liabilities	**450,944**	**437,802**
Net assets		
Unrestricted	540,858	529,254
Temporarily restricted	206,526	229,054
Permanently restricted	300,019	287,878
Total net assets	**1,047,403**	**1,046,186**
Total liabilities and net assets	**$1,498,347**	**$1,483,988**

See notes to consolidated financial statements.

Consolidated Statements of Activities

For the Years Ended June 30, 2003 and 2002
($ in Thousands)

	2003	2002
Changes in unrestricted net assets:		
Operating revenue and support:		
Tuition and other educational fees, net of financial aid	$196,153	$177,299
Sponsored projects (Note G)	243,871	246,107
Investment income	31,306	32,890
Contributions (Note D)	9,149	10,520
Auxiliary services	32,950	31,423
Other sources	25,689	24,470
Net assets released from restrictions	37,875	30,723
Total operating revenue and support	**576,993**	**553,432**
Operating expenses:		
Salaries	296,635	273,808
Benefits	55,233	51,525
Supplies and services	99,010	120,461
Occupancy and related expenses	35,994	34,957
Other operating expenses	28,247	23,309
Depreciation and amortization	38,819	41,539
Interest expense	5,817	5,407
Total operating expenses	**559,755**	**551,006**
Increase in unrestricted net assets from operations	**17,238**	**2,426**
Nonoperating activities:		
Net realized loss on investments	(25,120)	(28,728)
Unrealized gain (loss) on investments	7,498	(28,061)
Other sources	(1,179)	(11,176)
Net assets released from restrictions	13,167	—
Decrease in unrestricted net assets from nonoperating activities	**(5,634)**	**(67,965)**
Increase (decrease) in unrestricted net assets	**11,604**	**(65,539)**
Changes in temporarily restricted net assets:		
Contributions (Note D)	14,521	10,404
Investment income	5,690	8,733
Net realized loss on investments	(7,792)	(15,282)
Unrealized gain (loss) on investments	10,316	(31,843)
Other sources	5,779	1,238
Net assets released from restrictions	(51,042)	(30,723)
Decrease in temporarily restricted net assets	**(22,528)**	**(57,473)**
Changes in permanently restricted net assets:		
Contributions (Note D)	12,413	14,595
Investment income and other	(272)	981
Increase in permanently restricted net assets	**12,141**	**15,576**
Increase (decrease) in net assets	**$ 1,217**	**$ (107,436)**

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

For the Years Ended June 30, 2003 and 2002
($ in Thousands)

	2003	2002
Cash flows from operating activities:		
Increase (decrease) in net assets	$ 1,217	$(107,436)
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities:		
Realized losses on investment sales	13,537	28,103
Unrealized (gains) losses on investments	(17,432)	59,904
Depreciation and amortization	38,819	41,539
Gifts in kind	(1,529)	(3,311)
Loss on asset dispositions	1,898	5,372
Contributions for land, buildings, equipment and permanent endowment	(12,429)	(14,304)
Contributions held in perpetual trusts	—	(5,152)
Changes in assets and liabilities:		
Decrease (increase) in:		
Accrued interest and dividends	534	2,012
Accounts receivable	(18,969)	2,128
Pledges receivable	957	1,224
Other assets	(934)	3,094
Increase (decrease) in:		
Accounts payable and other liabilities	1,869	7,476
Deferred revenue	15,402	(3,340)
Federal loan programs	(189)	(1,359)
Present value of future annuities payable	(1,834)	(478)
Other, net	355	1,503
Net cash provided by operating activities	**21,272**	**16,975**
Cash flows from investing activities:		
Proceeds from sale and maturity of investments	2,822,273	1,928,147
Purchases of investments	(2,804,274)	(1,913,640)
Purchases of land, buildings and equipment	(55,984)	(48,535)
Proceeds from sale of land, buildings and equipment	122	820
Disbursements of loans to students	(4,640)	(2,556)
Repayments of loans from students	3,705	2,733
Net cash used for investing activities	**(38,798)**	**(33,031)**
Cash flows from financing activities:		
Proceeds from long-term debt issuance	—	43,779
Deposit of proceeds with trustee	—	(43,469)
Payment of debt issuance costs	—	(493)
Withdrawal of trusteed bond funds for construction	21,260	14,947
Repayments of long-term debt	(2,160)	(2,152)
Contributions for land, buildings, equipment and permanent endowment	12,429	14,304
Net cash provided by financing activities	**31,529**	**26,916**
Net increase in cash and cash equivalents	**14,003**	**10,860**
Cash and cash equivalents at beginning of year	**55,886**	**45,026**
Cash and cash equivalents at end of year	**$ 69,889**	**$ 55,886**

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

June 30, 2003 and 2002

Note A—Carnegie Mellon

Carnegie Mellon University ("Carnegie Mellon") is a private, not-for-profit educational and research institution. Carnegie Mellon currently enrolls about 9,500 students and grants approximately 2,700 bachelor's, master's and doctor's degrees each year. (Approximately 90% of undergraduate students are from the United States. International students comprise approximately 10% of undergraduate, 36% of master's and 60% of Ph.D. students.)

A substantial portion of Carnegie Mellon's revenues is from sponsored research and other projects under federal, state, industrial and other contracts.

Note B—Summary of Significant Accounting Policies

Basis of Accounting and Reporting

The accompanying consolidated financial statements have been prepared on the accrual basis and include the accounts of Carnegie Mellon and its wholly owned subsidiaries. The accounts of the wholly owned subsidiaries are not significant; intercompany transactions have been eliminated in consolidation.

Carnegie Mellon's net assets and revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified and reported as follows:

Unrestricted net assets — Net assets that are not subject to donor-imposed stipulations.

Temporarily restricted net assets — Net assets subject to donor-imposed or legal stipulations that may or will be met either by actions of Carnegie Mellon and/or the passage of time.

Permanently restricted net assets — Net assets subject to donor-imposed stipulations that the assets be maintained permanently. Generally, the donors of these assets permit Carnegie Mellon to use all or part of the income earned on the related investments for general or specific purposes.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions on net assets are reported as net assets released from restrictions between applicable classes of net assets.

Income and realized net gains and losses on investments are reported as follows:

- As changes in permanently restricted net assets if so restricted by the donor;
- As changes in temporarily restricted net assets if the terms of the gift or relevant state law impose restrictions on the use of the income or gains and losses; and
- As changes in unrestricted net assets in all other cases.

Equity securities with readily determinable fair values and all debt securities are measured at fair value with gains and losses reported in the statement of activities.

Carrying values of accounts and loans receivable approximate their fair values.

Fund Accounting

In order to ensure observance of limitations and restrictions placed on the use of the resources available to Carnegie Mellon, the internal operating accounts are maintained in accordance with the principles of fund accounting. This is the procedure by which resources for various purposes are classified into funds that are in accordance with activities or objectives specified. These financial statements, however, have been prepared to focus on the entity as a whole and to present transactions according to the existence or absence of donor-imposed restrictions.

Student Financial Aid

Tuition and other educational fees are reported net of student financial aid of $57.6 million and $50.3 million in the years ended June 30, 2003 and 2002, respectively.

Sponsored Project Revenues

Sponsored project revenues include research and other programs sponsored by government and private sources. Direct sponsored project revenues represent reimbursement of costs incurred in direct support of sponsored projects. Such revenue is recognized when the direct costs are incurred. In addition, sponsored projects normally provide for the recovery of indirect costs supporting the project. Indirect sponsored project revenues are recorded at rates established in advance by Carnegie Mellon through negotiations with the United States Government and other sponsors. Amounts received from sponsors under agreements that require the exchange of assets, rights or other privileges between Carnegie Mellon and the sponsor are recorded as deferred revenue until the contract terms are fulfilled.

Contributions with Restrictions Met in the Same Year

Contributions received with donor-imposed restrictions that are met in the same year as received are reported as revenues of the temporarily restricted net asset class, and a release of restriction is made to unrestricted net assets to reflect the satisfaction or expiration of such restrictions.

Contributions for Plant Activities

Donors' contributions to fund construction projects are classified as temporarily restricted net assets until the facility is placed in service. At that time, the temporarily restricted net assets are released from restriction and replenish unrestricted net asset balances designated for plant activities.

Operations

Revenues received and expenses incurred in conducting the programs and services of Carnegie Mellon are presented in the financial statements as operating activities. Nonoperating results include realized and unrealized gains and losses due to investment results, certain investee operating results, and non-recurring or unusual expenses and additions. In addition, net assets released from donor restrictions for buildings are released into nonoperating activities when the building is put into service.

Cash Equivalents

Cash equivalents include U.S. treasury obligations, commercial paper and corporate notes with maturities of three months or less, except that such instruments purchased with endowment and annuity and life income assets on deposit with trustees are classified as investments.

Investments

Debt and equity securities held by Carnegie Mellon are carried at market values as established by the major securities markets. Diversified, non-liquid holdings are carried at market values based upon financial information provided by the portfolio managers. Investments received as a gift are reflected as contributions at their fair market value at the date of the gift. Carnegie Mellon utilizes various investment instruments. Investment securities, in general, are exposed to various risks, such as interest rate, credit and overall market volatility. Due to the level of risk associated with certain investment securities, changes in the values of investment securities will occur in the near term and it is reasonably possible that such changes could materially affect the amounts reported in the statements of financial position.

Endowment

Investment policy for endowment assets is the responsibility of the Investment Committee of the Board of Trustees. Substantially all endowment assets are managed by outside investment managers and held in custody by an outside trustee.

Endowment net assets classified as unrestricted include Carnegie Mellon funds and unrestricted gifts from donors, and any accumulated income and appreciation thereon, which is intended to remain in the endowment for the long-term support of Carnegie Mellon activities but may be expended under Trustee authorization.

Temporarily restricted endowment net assets include certain expendable gifts, and any retained income and appreciation thereon, that are restricted by the donor to a specific purpose. When the temporary restrictions on these funds have been met, the gifts ordinarily remain in the endowment to continue supporting the same activities as those specified by the donors; however, by Trustee designation, the funds are reclassified to unrestricted endowment net assets.

This classification also includes all expendable, accumulated appreciation of $153 million and $164 million on permanent endowment assets as of June 30, 2003 and 2002, respectively. The Trustees of Carnegie Mellon must authorize release of endowment gains from temporarily restricted to unrestricted net assets according to Pennsylvania law.

Permanently restricted endowment net assets include those assets that must be invested in perpetuity to provide a permanent source of income.

All endowment funds participate in a Carnegie Mellon investment pool. The investment pool provides income to its respective participants. Such income is used for the specific purpose prescribed by the donor or, if the purpose was not prescribed by the donor, the income is deemed unrestricted and used for general purposes. New endowment funds or additions to existing funds are assigned shares in the investment pool based upon the per share market value at the end of the previous month. Income distributions from the investment pool are based upon the number of shares held by each participant and the approved spending rate (See Note F). Income distributions from the investment pool are based upon the "total return concept." The annual income distributed from the investment pool includes interest and dividends and could include a portion of the accumulated capital gains. Any capital gains not distributed currently are reinvested in the investment pool and are available for distribution from the endowment assets in future years.

Land, Buildings and Equipment

Land, buildings and equipment are recorded at cost at the date of acquisition or, if acquired by gift, at the estimated fair market value as of the date of the gift. Additions to plant assets are capitalized while scheduled maintenance and minor renovations are charged to operations. Buildings and equipment are reflected net of accumulated depreciation calculated on a straight-line basis over the estimated economic lives.

Assets Held In Trust By Others

Assets Held In Trust By Others includes proceeds from the issuance of bonds in 2002 (see Note I), which are held by a trustee under the bond indenture for future capital expenditures, and the value of Carnegie Mellon's beneficial interest in perpetual trusts held by outside trustees.

Reclassifications

Certain 2002 amounts have been reclassified to conform with the 2003 presentation, including a reclassification for certain financial aid that had previously been included in operating expenses and is currently reported in net tuition and other educational fees.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Note C—Accounts and Loans Receivable

Accounts receivable at June 30, 2003 and 2002, consist of the following:

$ in thousands	**2003**	**2002**
Sponsored project grants and contracts:		
Federal	$35,748	$20,110
Other	26,043	20,394
Total sponsored projects	61,791	40,504
Student accounts	5,975	5,746
Other	4,528	5,357
	72,294	51,607
Allowance for doubtful accounts	(7,338)	(5,620)
Net accounts receivable	**$64,956**	**$45,987**

Loans receivable are primarily student loans made under a Federal loan program, and are reported net of an allowance for doubtful accounts of approximately $1.6 million as of June 30, 2003 and 2002.

Note D—Pledges Receivable and Contributions

Pledges and outside trusts as of June 30, 2003 and 2002, are discounted to the present value of future cash flows and are due as follows:

$ in thousands	2003			
	Discount Rate	Temporarily Restricted	Permanently Restricted	Total
In one year or less	1.0%	$ 9,379	$ 4,785	$14,164
Between one year and five years	1.7%	6,974	10,028	17,002
More than five years	2.8%	2,985	4,331	7,316
Present value of pledges		19,338	19,144	38,482
Less allowance for unfulfilled pledges		(773)	(759)	(1,532)
Pledges receivable, net of allowance		**$18,565**	**$18,385**	**$36,950**

$ in thousands	2002			
	Discount Rate	Temporarily Restricted	Permanently Restricted	Total
In one year or less	2.1%	$ 4,236	$ 5,632	$ 9,868
Between one year and five years	3.5%	9,153	6,562	15,715
More than five years	4.5%	9,023	4,643	13,666
Present value of pledges		22,412	16,837	39,249
Less allowance for unfulfilled pledges		(667)	(675)	(1,342)
Pledges receivable, net of allowance		**$21,745**	**$16,162**	**$37,907**

Pledges receivable as of June 30, 2003 and 2002, net of allowances, are intended for the endowment in the amounts of $18.4 million and $16.2 million, respectively, capital projects in the amounts of $6.3 million and $4.5 million, respectively, and other donor restricted purposes in the amounts of $12.2 million and $17.2 million, respectively.

Contribution revenue includes gifts, unconditional pledges to give and grants. Contributions are recorded in the appropriate net asset category based upon the intent of the donor or grantor. Contributions for the years ended June 30, 2003 and 2002 are as follows:

$ in thousands	2003		
	Gifts/Grants	Change in Pledges Receivable	Total
Unrestricted	$ 9,149		$ 9,149
Temporarily restricted	17,701	$(3,180)	14,521
Permanently restricted	10,190	2,223	12,413
Total	**$37,040**	**$ (957)**	**$36,083**

$ in thousands	2002		
	Gifts/Grants	Change in Pledges Receivable	Total
Unrestricted	$10,520		$10,520
Temporarily restricted	10,863	$ (459)	10,404
Permanently restricted	15,360	(765)	14,595
Total	**$36,743**	**$ (1,224)**	**$35,519**

Carnegie Mellon generally reports foundation grants as exchange contracts and accordingly, reports such revenues as sponsored project revenue in the accompanying Consolidated Statements of Activities. These revenues were $5.8 million and $6.1 million in the years ended June 30, 2003 and 2002, respectively.

Note E—Investments

Investments by major category at June 30, 2003 and 2002, are as follows:

$ in thousands	2003	2002
Restricted cash and equivalents	$ 50,388	$ 45,759
Fixed income	234,029	237,187
Common stock	424,040	454,345
Other investments	123,681	108,951
Total investments	**$832,138**	**$846,242**

Investments are held for the following purposes:

$ in thousands	2003	2002
Endowment	$651,413	$664,648
Reserves for debt service	114,227	119,395
Life income trusts	26,694	27,043
Other	39,804	35,156
Total investments	**$832,138**	**$846,242**

Nearly all fixed income securities are U.S. investment grade and high yield bonds, asset backed securities and United States Treasury and Agency obligations at June 30, 2003 and 2002. Common stock investments are composed of approximately 69% domestic equities and 31% international and emerging market equities at June 30, 2003. At June 30, 2002 approximately 63% of common stock investments consisted of domestic equities while the remaining 37% included international and emerging market equities. Other investments are largely investments in domestic buyout funds, venture capital, hedge funds and real estate.

The allocation to each major category represents the actual allocation of all investment pools on a combined basis. Each investment pool maintains a unique investment strategy. Actual allocations on a combined basis should not be interpreted as an investment allocation policy for a particular investment pool. In addition, the above asset category allocations do not reflect the effective allocation exposures resulting from investment strategies that include derivatives. The following schedule summarizes the investment return for the years ended June 30, 2003 and 2002:

$ in thousands	2003	2002
Dividends and interest	$ 17,730	$ 26,095
Net realized losses on sale of securities	(13,537)	(28,103)
Unrealized gain (loss)	17,432	(59,904)
Total return on investments	**$ 21,625**	**$(61,912)**

Operating investment income includes dividends and interest earned on unrestricted funds, and unrestricted accumulated gains utilized for current operations in the amount of $19.4 million and $15.9 million in the years ended June 30, 2003 and 2002, respectively.

Carnegie Mellon and certain of its outside investment managers purchase and sell derivative instruments in order to manage interest rate and foreign currency risk and market positions.

Carnegie Mellon's international portfolios maintain market benchmarks, for performance evaluation and risk control purposes, that are unhedged with respect to foreign currencies. Unhedged benchmarks reflect the full impact of foreign currency fluctuations stemming from the benchmarks' foreign currency positions. Investment managers of these international portfolios have the discretion to manage the portfolios' foreign currencies, relative to the currency exposures in their unhedged benchmarks, to protect the portfolios from potential foreign currency losses and to benefit from potential foreign currency gains. Carnegie Mellon's investment managers understand that they are assuming active management risks to the extent that they assume foreign currency exposures that differ from the foreign currency exposures in their relevant market benchmarks (as documented in the formal investment guidelines for each manager). Carnegie Mellon had foreign exchange contracts totaling $5.9 million and $10.8 million at June 30, 2003 and 2002, respectively. Certain of these foreign exchange contracts are entered into with respect to pending settlements of foreign securities transactions.

Investment managers purchase and sell interest rate futures to control the risk of fluctuations in market interest rates, relative to portfolio benchmarks, on the university's fixed income investments. At June 30, 2003 and 2002, the notional value of interest rate futures was $0.1 million and $(19.4) million, respectively. (Parentheses denote net short positions.)

Certain domestic equity investment managers purchase S&P 500 futures contracts to obtain cost-efficient exposure to the S&P 500 Index when the S&P 500 Index is the portfolio benchmark. At June 30, 2003 and 2002, the notional value of S&P 500 futures contracts was $54.5 million and $53.2 million, respectively.

Gains or losses from derivative instruments are reported as realized and unrealized gains or losses in the statement of activities. The market value of all derivative instruments is included in the market value of the investments.

Note F—Endowment

The following table provides a summary of the changes in value of the endowment assets excluding pledges for the years ended June 30:

$ in thousands	**2003**	**2002**
Beginning of year endowment value	**$667,807**	**$756,930**
Gifts and other additions:		
Contributions (excluding pledges)	11,459	10,844
Terminated life income trusts and income and gains reinvested	946	630
Other transfers	—	305
Total gifts and other additions	12,405	11,779
Investment income:		
Interest and dividends	12,200	18,735
Realized loss on sale of securities	(12,268)	(24,387)
Unrealized gain (loss)	16,271	(52,480)
Total investment income	16,203	(58,132)
Income distributed for operating purposes:		
Cash and accrued interest and dividends	(12,071)	(18,518)
Accumulated realized investment gains	(29,666)	(24,252)
Total income distributed	(41,737)	(42,770)
End of year endowment value	**$654,678**	**$667,807**

Endowment net assets at June 30 are classified as follows:

$ in thousands	**2003**	**2002**
Unrestricted	$230,792	$244,646
Temporarily restricted	153,273	164,397
Permanently restricted	270,613	258,764
Total	**$654,678**	**$667,807**

Carnegie Mellon maintains a total return spending policy. Endowment income distributions can consist of dividend and interest income and a withdrawal of accumulated capital gains when necessary. The main objective of the total return spending policy is to separate spending policy from investment policy. Separating spending policy from investment policy permits asset allocation decisions to be made independently of the need for current income. The spending rate for endowment is determined annually as a percentage of the trailing three year average of December 31 endowment market values. For fiscal 2003 and 2002, the spending rate was set at 5.1% and 5.2%, respectively. The actual spending rate based on average annual endowment market value for the year was 6.3% in fiscal 2003, compared to 6.0% in fiscal 2002.

Note G—Sponsored Project Revenues

The major components of sponsored projects revenue for the years ended June 30, 2003 and 2002, are as follows:

$ in thousands	2003	2002
Federal		
Direct	$144,698	$151,616
Indirect	29,515	27,664
Total Federal	174,213	179,280
State, industrial and other		
Direct	58,463	55,367
Indirect	11,195	11,460
Total state, industrial and other	69,658	66,827
Total sponsored projects revenue	**$243,871**	**$246,107**

Note H—Land, Buildings and Equipment

Land, buildings and equipment at June 30 consist of the following:

$ in thousands	2003	2002
Buildings	$576,487	$526,844
Utilities and building-related assets	50,830	53,695
Moveable equipment	263,593	252,011
Subtotal	890,910	832,550
Accumulated depreciation	(454,956)	(428,625)
Subtotal	435,954	403,925
Land	7,323	7,323
Construction in progress	9,776	25,118
Net land, buildings and equipment	**$453,053**	**$436,366**

Buildings include $22.3 million in 2003 and 2002 representing the present value of minimum lease payments under capital lease arrangements.

Note I—Long-Term Debt

Long-term debt consists of the following as of June 30:

$ in thousands	Interest %	2003	2002
Pennsylvania Higher Education Facilities Authority, Variable Rate Refunding Bonds, Series 1995	Variable	$176,800	$176,800
Allegheny County Higher Education Building Authority, Variable Rate University Revenue Bonds, Series 1998	Variable	78,000	78,000
Allegheny County Higher Education Building Authority, University Revenue Bonds, Series 2002	5.125 - 5.5	43,815	43,786
Dormitory bonds/mortgage notes	2.75 - 3.50	2,904	3,077
Subtotal - bonds and mortgages		301,519	301,663
Capital lease obligations	5.0 - 7.5	6,866	8,828
Total long-term debt		**$308,385**	**$310,491**

On November 1, 1995, Carnegie Mellon issued through the Pennsylvania Higher Education Facilities Authority $176.8 million of Carnegie Mellon University Variable Rate Revenue Refunding Bonds, Series 1995 (the "1995 Bonds"). The proceeds of the 1995 Bonds were used to repay the Washington County Higher Education Pooled Equipment Leasing program debt and the Pennsylvania Higher Education Facilities Authority Variable Rate Option Revenue Bonds, First Series of 1985. The $176.8 million debt issue consists of $50 million Series 1995A due 2025, $50 million Series 1995B due 2027, $50 million Series 1995C due 2029, and $26.8 million Series 1995D due 2030. The 1995 Bonds have certain financial covenants consistent with similar types of financing arrangements. The 1995 Bonds structured as multiple mode obligations currently bear interest at a variable market rate determined daily by the bonds' remarketing agent. Interest was charged at rates ranging from 0.7% to 2.0% during the year.

On December 30, 1998, Carnegie Mellon issued through the Allegheny County Higher Education Building Authority $88.0 million of Carnegie Mellon University Variable Rate Revenue Bonds, Series 1998 (the "1998 Bonds"). The proceeds of the 1998 Bonds were used to fund capital projects. The 1998 Bonds structured as multiple mode obligations currently bear interest at a variable market rate determined daily by the bonds' remarketing agent. Interest was charged at rates ranging from 0.7% to 2.0%.

To provide further security for the 1995 Bonds and 1998 Bonds, Carnegie Mellon and the trustees have entered into 364 day Standby Bond Purchase agreements, which have been renewed annually.

On March 27, 2002, Carnegie Mellon issued through the Allegheny County Higher Education Building Authority, University Revenue Bonds, Series 2002, with a face value of $44,665,000, (the "2002 Bonds"). The proceeds of the 2002 Bonds will be used to fund capital projects. The 2002 Bonds mature $5 million in 2027, $7.665 million in 2028 and $32 million in 2032. The 2002 Bonds bear fixed rates of interest, and the effective interest rate on the 2002 Bonds, including the effect of the original issue discount, is 5.34%.

The dormitory bonds and mortgage notes mature in varying amounts through 2024 and bear interest at fixed rates that range from 2.75% through 3.5%. Facilities of Carnegie Mellon and the revenues thereon are pledged as collateral on the dormitory bonds and mortgage notes.

Carnegie Mellon's investments include $11.7 million required under its various debt agreements to be held until the related debt is retired. An additional $102.5 million has been designated by management as a reserve to meet future debt service requirements.

Carnegie Mellon guarantees the payment of principal and interest due on $19.3 million RIDC Regional Growth Fund Revenue Refunding Bonds (Carnegie Mellon University Software Engineering Institute Facility), Series 1995, issued through the Pennsylvania Higher Educational Facilities Authority. These bonds, which had principal outstanding of $6.8 million as of June 30, 2003, were issued to refinance a prior debt issue used for construction of a building in accordance with the research contract for the Software Engineering Institute. Carnegie Mellon had a capital lease obligation in connection with this transaction in the amount of $5.4 million and $7.4 million at June 30, 2003 and 2002, respectively. The lease concludes in fiscal 2006 and has an interest rate of 5%.

On July 15, 1995, Carnegie Mellon and the Urban Redevelopment Authority of Pittsburgh entered into a capital lease for the land and buildings that are known as the National Robotics Engineering Consortium. The lease term currently extends to fiscal 2005. The lease obligation was $1.4 million as of June 30, 2003 and 2002, respectively. The interest rate on the lease is 7.5%. Contract and grant revenues will support the payments on this lease.

The fair value of Carnegie Mellon's long-term debt obligations as of June 30, 2003 and 2002, is approximately $311.1 million and $310.9 million, respectively.

Interest paid for the years ended June 30, 2003 and 2002, totaled $6.1 million and $5.0 million, respectively. In the year ended June 30, 2003, interest of $318,000 was capitalized as part of the cost of building construction.

Aggregate maturities of bonds and mortgages for each of the five years ending June 30, are as follows:

$ in thousands	
2004	$ 150
2005	159
2006	140
2007	144
2008	148
Thereafter	300,778
Total	**$301,519**

Note J—Expenses by Functional Category

Operating expenses by functional category for the years ended June 30, 2003 and 2002 are as follows:

$ in thousands	2003	2002
Instruction and departmental research	$212,484	$198,712
Sponsored projects	206,336	222,430
Academic support	44,910	45,086
Student services	26,478	25,650
Administration and institutional support	39,232	31,468
Auxiliary services and activities	30,315	27,660
Total	**$559,755**	**$551,006**

Note K—Commitments and Contingencies

Carnegie Mellon is a defendant in a number of legal actions seeking damages and other relief. While the final outcome of each action cannot be determined at this time, legal counsel and management are of the opinion that the liability, if any, in these legal actions will not have a material effect on Carnegie Mellon's financial statements.

Carnegie Mellon and its affiliates receive significant financial assistance from the federal government, including the sponsorship of federal research projects. Research grants and contracts normally provide for the recovery of direct and indirect costs. Entitlement to the recovery of the applicable direct and related indirect costs is generally conditioned upon compliance with the terms and conditions of the grant agreements and applicable federal regulations, including the expenditure of the resources for eligible purposes. Substantially all grants and Carnegie Mellon's indirect cost rate are subject to financial and compliance reviews and audits by the grantors. In management's opinion, the likelihood of an adverse material outcome upon its financial position from those reviews and audits is remote.

Lease expense was $9.2 million and $7.7 million for the years ending June 30, 2003 and 2002, respectively. Future minimum lease payments at June 30, 2003 are as follows:

$ in thousands	Operating Leases	Capital Leases
2004	$3,558	$2,473
2005	1,092	3,885
2006	479	1,007
2007	238	21
2008	238	11
	$5,605	7,397
Less amount representing interest		(531)
Present value of minimum capitalized lease payments		**$6,866**

In 2003, Carnegie Mellon entered into lease agreements with the Regional Industrial Development Corporation of Southwestern Pennsylvania in connection with construction of a new building on the Carnegie Mellon campus. Carnegie Mellon has committed to occupying a minimum amount of space in the new building once completed, although the actual space to be occupied may ultimately be reduced if additional tenants are secured. If Carnegie Mellon were to occupy the full committed amount, lease payments would be $2.4 million annually for ten years commencing July 2004.

Note L—Retirement Plans and Other Post-Employment Benefits

Carnegie Mellon has various pension and retirement programs covering substantially all of its employees. The two principal pension programs are a defined contribution plan sponsored by the university and the SEIU National Industry Pension Fund, a multi-employer plan. Annual contributions are made to the plans equal to amounts accrued for pension expense. Such plans are fully funded on a current basis. Retirement plan expense for the years ended June 30, 2003 and 2002, totaled $17.0 million and $16.0 million, respectively.

Carnegie Mellon provides certain health care benefits for eligible retired employees. The table below sets forth the health care plan's funded status at June 30, 2003 and 2002:

$ in thousands	2003	2002
Benefit obligation	$21,440	$11,979
Unrecognized actuarial loss	(9,865)	(1,839)
Unrecognized net transition obligation	(2,062)	(2,268)
Accrued benefit cost	**$ 9,513**	**$ 7,872**

The net periodic benefit cost for the years ended June 30 is as follows:

$ in thousands	2003	2002
Benefit cost	$2,006	$1,614
Employer contribution	365	305
Plan participants' contributions	150	111
Benefits paid	515	416

The reconciliation of the accumulated benefit obligation at June 30, 2003 and 2002, was as follows:

$ in thousands	2003	2002
Benefit obligation, beginning of year	$11,979	$11,145
Service cost	629	487
Interest cost	1,003	854
Plan amendments	—	(215)
Assumption changes and actuarial loss	8,194	13
Benefit payments	(365)	(305)
Benefit obligation, end of year	**$ 21,440**	**$11,979**

The assumed discount rate used for calculating the benefit obligation was 5.5% for 2003 and 7.0% for 2002. An 11% annual rate of increase in the per capita cost of covered healthcare benefits was assumed for 2003. The rate was assumed to decrease gradually to 5.0% for 2009 and remain at that level thereafter.

The health care cost trend rate assumption has a significant effect on the amounts reported. Increasing the assumed healthcare cost trend rate by 1 percent in each year would increase the benefit obligation as of June 30, 2003, by $3.8 million and increase the aggregrate service cost and interest cost components for 2003 by $0.3 million. Decreasing the assumed health care cost trend rate by 1 percent in each year would decrease the benefit obligation as of June 30, 2003, by $3.1 million and decrease the aggregate service cost and interest cost components for 2003 by $0.2 million.

In conjunction with an agreement made with the federal government, the university has established a separate trust, which is available to general creditors, only in the event of insolvency. The expected return on plan assets for both 2003 and 2002 was 8.75% and was used in determining the benefit cost. Assets in the trust to fund post-retirement health care and other post-employment benefits are $9.5 million and $0.7 million, respectively, at June 30, 2003 and $7.9 million and $0.6 million, respectively, at June 30, 2002. These assets are reflected as investments in the accompanying Consolidated Statements of Financial Position. Total contributions for each of the years ended June 30, 2003 and 2002, to fund the liability, including payments into the trust, totaled $0.5 million.

Note M—Related Party Transactions

Sponsored research revenue for fiscal 2003 and 2002 includes $9.9 million and $39.2 million, respectively, in research funding received from MPC Corporation (“MPC”), a nonprofit corporate joint venture of Carnegie Mellon and the University of Pittsburgh. The funding primarily represents Federal funding under a $54.9 million contract received by MPC, for which MPC has subcontracted to Carnegie Mellon for the construction of a supercomputer and related activities.

In June 2002, Carnegie Mellon sold the net assets of Carnegie Technology Education (“CTE”), a wholly owned subsidiary, to iCarnegie, Inc. (“iCarnegie”) in exchange for stock representing an approximate 41% interest in iCarnegie, approximately $5.8 million in notes, and certain license royalties. Carnegie Mellon’s interest in iCarnegie has a carrying value of $0 as of June 30, 2003 and 2002 and the notes from iCarnegie are fully reserved. Carnegie Mellon’s nonoperating activities for the year ended June 30, 2002 included a $0.6 million gain from CTE operations and the above noted transaction.

Note N—Guarantees

In November 2002, the Financial Accounting Standards Board (“FASB”) issued FASB Interpretation No. 45 (“FIN 45”), “Guarantor’s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others.” FIN 45 elaborates on the disclosure to be made by a guarantor in its financial statements abouts its obligations under certain guarantees that are issued. It also clarifies that an organization is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee.

In the ordinary course of business, Carnegie Mellon enters into contracts with third parties pursuant to which the third parties provide services on behalf of Carnegie Mellon. Such contracts may provide for Carnegie Mellon to indemnify the third party service provider under certain circumstances. The terms of indemnity vary from contract to contract and the amount of the indemnification liability, if any, cannot be determined.

Carnegie Mellon provides indemnification to trustees, officers, and in some cases employees and agents against certain liabilities incurred as a result of their service on behalf of or at the request of Carnegie Mellon and also advances on behalf of covered individuals’ costs incurred in defending against certain claims.

Carnegie Mellon provides indemnification in connection with bond offerings in which it is involved. The indemnifications relate to losses, claims, damages, liabilities, and other expenses incurred by underwriters that would arise as a result of any untrue statements or material omissions made by Carnegie Mellon. Due to the nature of these indemnification provisions, it is not possible to quantify the aggregate exposure to Carnegie Mellon resulting from them.

ADMINISTRATION AND BOARD

Hunt Library

*Alumnus(a)

Type of university:
Private, coeducational, granting about 2,700 bachelor's, master's and doctor's degrees each year.

Number of colleges and schools:
Seven — the Carnegie Institute of Technology (engineering); the College of Fine Arts, the College of Humanities and Social Sciences (liberal arts and professional studies); the Graduate School of Industrial Administration (business); the H. John Heinz III School of Public Policy and Management; the Mellon College of Science; the School of Computer Science.

Physical size:
105-acre main campus; 75 buildings.

Location:
Five miles east of downtown Pittsburgh, bordered by 500-acre Schenley Park and three culturally active residential neighborhoods.

Number of students:
5,347 undergraduates; 2,751 master's and 1,275 doctoral students.

Number of faculty:
1,126 full-time and 189 part-time faculty;
47 administrative faculty.

Athletics:
Team name is "the Tartans"; NCAA Division III classification; founding member of the University Athletic Association; 17 varsity sports; more than 40 intramural sports.

Number of alumni:
57,119

Computers:
There are thousands of high-powered computer work stations and personal computers on campus; all student rooms and apartments and all academic and research facilities are linked to the university's Andrew computing network. Recognized twice as the "Most Wired College" by Yahoo! Internet Life, Carnegie Mellon boasts a university-wide wireless network with access available to all administrative and dormitory buildings on campus.

History:
Founded in 1900 by industrialist and philanthropist Andrew Carnegie as a technical school for working class Pittsburgh; became Carnegie Institute of Technology, or "Tech," in 1912; merged with the Mellon Institute of Research in 1967 to become Carnegie Mellon University.

Founder's motto:
"My Heart Is in the Work," as inscribed by founder Andrew Carnegie in his "contract" to the city of Pittsburgh written in 1900.

For more insight into our vision for the future of Carnegie Mellon:
Please visit our homepage at: www.cmu.edu

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Carnegie Mellon

Produced by The Communications Design Group, October 2003, E027
♻ Printed on recycled paper.