Highlights

Fiscal years ended June 30	2001	2000
	(dollars in thousands)	
Financial		
Principal sources of revenues		
Tuition and fees (net)	$ 88,156	$ 85,751
Government grants and contracts	165,951	153,272
Private gifts, grants, and contracts	61,590	58,052
Investment earnings	151,156	2,086,645
Principal purposes of expenditures		
Educational and general	529,649	482,373
Auxiliary	88,958	81,800
Summary of financial position		
Assets	10,426,426	10,410,285
Liabilities	930,312	873,612
Net assets	9,496,114	9,536,673
Net assets		
Unrestricted/designated	7,743,630	7,733,942
Temporarily restricted	788,513	871,866
Permanently restricted	963,971	930,865
Total	9,496,114	9,536,673
Students		
Enrollment		
Undergraduate students	4,554	4,556
Graduate students	1,884	1,768
Degrees conferred		
Bachelor degrees	1,099	1,122
Advanced and all other degrees	648	618
Annual tuition rate		
Undergraduate	$ 25,430	$ 24,630
Graduate	25,430	24,630
Faculty		
Full-time equivalent	835	828

Report of the Treasurer

Financial Overview

Despite the downturn in the economy, the University ended the fiscal year 2001 in remarkably good financial condition. While the amount of income distributed under the endowment spending rule slightly exceeded the total return on our investments, our overall investment performance for the year of 2.4 percent for the managed portfolio was both positive and among the best of our peers. Other revenue and expenditures were within expectation and our balance sheet continues to be exceptionally strong. We finance our major maintenance, renovation and capital equipment requirements through the use of tax-exempt financing, including variable rate debt. A commercial paper program continues to provide partial financing for capital projects during their construction phase. Each of our debt instruments has received the highest credit ratings from Moody's and Standard & Poor's agencies.

Report

This report describes the financial position of Princeton University on two separate but related bases. Pages 4 and 5 describe the University's annual operating budget and reflect the basis on which the budget decisions are made and executed. The operating budget includes unrestricted and restricted income utilized to cover expenses. The second method (pages 6 through 8) constitutes the basis for preparing the audited financial statements in accordance with generally accepted accounting principles (GAAP). This approach focuses on total income and total expenditures as defined by GAAP. Because the data in the two presentations are prepared with somewhat different objectives and are based on differing rules and conventions, it is not always obvious how they are related. In some cases, similar descriptions are used in both sections of this report even though the precise definitions—and thus the specific amounts—are not identical. However, both sets of figures are accurate, and both are drawn from the University's general ledger.

The schedule from the audited financial statements that most closely relates to the format used for the annual operating budget is the Consolidated Statement of Activities. The lower half of the statement deals with nonoperating activities and reflects realized and unrealized appreciation on the endowment, pledges from donors, changes in the principal value of outside trusts, and gifts for capital projects. All of these deal with factors affecting the long-term value of our assets. The upper sections of the statement focus on basically the same set of revenue and expense items as the annual operating budget. However, this presentation differs from the operating budget in both the gross numbers and in the calculation of a surplus or deficit. Thus, a reconciliation would focus on a comparison between the total column of the upper section of the Consolidated Statement of Activities from our audited financial statements (page 11) and our operating budget, which appears in the Priorities Committee Report and pages 4–5 of this document.

On a gross basis, expenses on the two presentation bases differ by roughly $59 million ($640 million on the Consolidated Statement of Activities and $699 million as total operating budget expenditures). As discussed further below, there are numerous factors that would affect these two totals. However, the single most important factor on a gross basis is the GAAP accounting rule that requires $72 million of certain scholarship and fellowship expenses to be treated as reductions from tuition and fee income amounts on the Consolidated Statement of Activities. The operating budget continues to show tuition and fees as gross income and the full amount of all student aid as an expense.

The surplus or deficit as calculated by these two presentations also differs; the total column of the Consolidated Statement of Activities shows a decrease of roughly $1 million on the line *Increase (Decrease) from Revenues, Gains, and Other Support over Expenses and Losses,* while the operating budget reports a balance of revenues and expenses. There are many factors that cause variances on both income and expense lines. While there is no prescribed formula for reconciling these differences, the following examples illustrate why the numbers would vary, showing estimated GAAP impact as compared to the operating budget presentation.

- Depreciation versus transfer to reserves — In the GAAP financial statements we assign a cost for the depreciation of all buildings, equipment, and library books to the expense lines for academic, administrative, and auxiliary items. These reflect estimated useful lives that range from 10 to 40 years. The total amount of depreciation is some $58 million. The operating budget treats these costs differently. We expense all library books in the year they are purchased. We normally amortize equipment over shorter periods of time, and we show as an expense monies transferred to our Renewal and Replacement Reserve. This reserve funds the annual debt service charges for major maintenance and equipment programs, certain capital renovation projects, and monies for laboratory renovation, equipment, and other expenses associated with the appointment of new faculty members. Most of these items, which total some $81 million, are capitalized for GAAP reporting purposes. Thus, the differing treatment of these items on the expense side produces an improvement to the GAAP surplus of about $23 million.

• The recognition of restricted income to fund capital equipment — As mentioned above, the operating budget includes a general funds transfer to reserves for renewal and replacement of the physical plant. The operating budget does not include either income or expenditures for nongeneral funds equipment. However, since the Consolidated Statement of Activities shows depreciation expense for equipment funded from all sources, these statements must also reflect restricted income given for such purposes. Generally accepted accounting principles provide for all income associated with equipment to be recognized in the year the initial expenditure is made. This results in net additional income of $17 million, which increases the GAAP surplus.

• Postretirement health costs — The operating budget treats all qualified retiree medical expenses, which are primarily self-insured, on a cash basis. However, according to GAAP, the Consolidated Statement of Activities includes an amount that amortizes the potential future medical costs for past and present employees. That net charge on the Consolidated Statement of Activities is roughly $13 million and reduces the GAAP surplus.

• Interest on external debt — Under GAAP, all interest paid on external debt shows as an expense of unrestricted funds. While the operating budget provides for some interest on debt in its amortization schedules and transfers to reserves, it excludes interest amounts associated with capital projects that have been assigned to and funded from capital gifts. The Consolidated Statement of Activities also includes earnings on the reserve funds from which much of the debt is paid, while the operating budget does not. The net of these factors is increased expense, which reduces the GAAP surplus by $17 million.

• All other items — Most of these differences have to do with the recognition of unrestricted revenue and expense. While the operating budget typically covers transactions for a single fiscal year only, there are some instances where small items might carry forward from year to year. Examples would be an annual transfer to an insurance reserve or an agreement to allow a department to retain certain budget savings. In these cases, the operating budget recognizes the liability, and we actually move the amounts on our books into funds functioning as endowment until the expenditures are made. However, GAAP does not count such transfers and recognizes the expenses only when they are actually incurred. On the income side, if unrestricted income has been received but designated for a particular purpose, the operating budget does not recognize the monies until the expenditures occur. A recent example was when unrestricted gifts were set aside to fund the conversion of the library catalog into an electronically readable form. However, GAAP recognizes the unrestricted income when it is received and does not reflect internal restrictions that may have assigned funds to a particular project. Rather, it shows the expenditures when they occur without any income offset. While in any given year these conventions could cancel each other out, in fiscal year 2001 the operating budget recognized a combination of fewer expenses and more income than appear in the Financial Statements. This accounts for the balance of the difference in the two calculations and decreases the GAAP surplus by approximately $9 million.

All these varying factors result in a $1 million difference compared to the operating budget when restated in the form of the Consolidated Statement of Activities. Each of the differing accounting treatments helps in its own way to focus on issues that need to be considered in managing annual operations in the context of our longer-term responsibilities for future years.

Operating Budget

Objectives and Policies

The Priorities Committee of the Council of the Princeton University Community (CPUC) is the faculty-student-administration group that makes recommendations to the president concerning the annual operating budget. The president, after approving these recommendations, submits them to the trustees for their approval in the January preceding the start of each fiscal year. All major budgetary items are reviewed by the Priorities Committee to make sure that both immediate needs and long-range plans for resource allocation are considered and evaluated.

The objective of the operating budget is to accomplish current University goals while ensuring that our physical and financial resources in the future are appropriately preserved for the longer term. Under these general guidelines, the president and the trustees have adopted a set of rules for determining the prudent division of resources between current spending and reinvestment for the future. It is the responsibility of the Priorities Committee and the president to propose annual plans which keep expenditures and revenues in balance.

Fiscal Year 2000-2001 Results

In January 2000 the trustees approved an operating budget for 2000-2001 that anticipated a small surplus of $8,000. The actual results were essentially unchanged, although there were naturally some larger swings in various items of income and expense which offset each other.

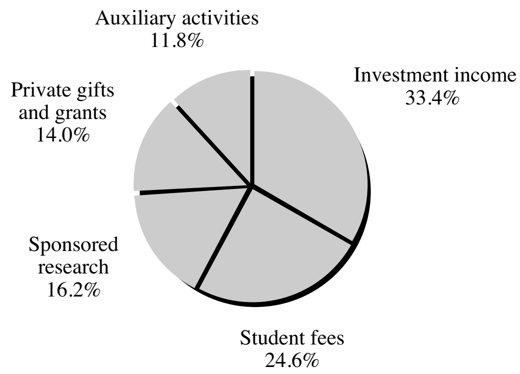
	(in thousands)
Operating Budget Revenues	$ 698,504
Operating Budget Expenditures	698,504
Operating Surplus	$ 0

A balanced budget for 2001-02 was adopted in January, 2001. While the current economic climate is now more unsettled, we believe the University has sufficient resources to sustain financial equilibrium in the foreseeable future.

Princeton Plasma Physics Laboratory

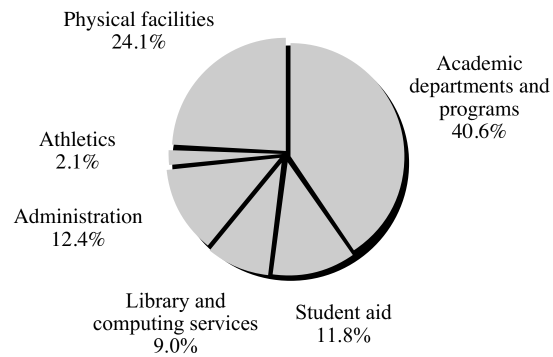
Sponsored revenues and expenditures associated with the Princeton Plasma Physics Laboratory (PPPL), funded primarily by the U.S. Department of Energy, have been excluded from the charts on the facing page. We believe this makes the presentation more meaningful because PPPL is relatively self-contained and would thus tend to distort the other numbers. PPPL activity represents approximately one-tenth of the operating budget.

Operating Budget Revenues



(1) **Investment Income.** Primarily endowment earnings distributed in accordance with a spending formula approved by the trustees (normally amounting to spending between 4 and 5 percent of market value annually). Unlike the general financial statement treatment, income dedicated to the use of a particular department or program is counted in the operating budget only as it is spent.
(2) **Student Fees.** Undergraduate and graduate tuition, in addition to medical and application fees and other miscellaneous charges. All tuition payments are counted here even if they are paid using University-provided student aid funds.
(3) **Sponsored Research.** Support for organized research projects sponsored by the federal government and by corporations and foundations.
(4) **Private Gifts and Grants.** Spendable gifts from outside groups such as corporations, foundations, and individuals, and federal support for financial aid. The largest single component is the amount provided by Annual Giving, which provides unrestricted operating funds to the University. Capital gifts are excluded and restricted gifts are recognized only as they are spent.
(5) **Auxiliary Activities.** Income from athletics, dormitory and food services, rental housing, computing, and miscellaneous support activities.

Operating Budget Expenses



(1) **Academic Departments and Programs.** Instructional costs (such as faculty and graduate teaching assistants) and all other operating costs of academic departments. Also included here are all the direct costs of carrying out sponsored research within these departments and programs.
(2) **Student Aid.** Undergraduate scholarships and graduate fellowships, most of which are funded from either endowment funds or general University funds.
(3) **Library and Computing Services.** Costs associated with the Library and with the Office of Information Technology.
(4) **Administration.** The cost of all central administrative functions, including the offices of the provost and deans, Health Services, Admissions, Registrar, Religious Life, and Public Safety. Other "business" offices such as the Treasurer, Human Resources, Development, and Public Affairs are also included in this category.
(5) **Athletics.** Expenses of intercollegiate competition, intramural sports, and physical education.
(6) **Physical Facilities.** Operation, maintenance, and energy expenses for all campus buildings, as well as the costs of food services and other facilities-related service units. Also included are transfers to reserves to fund debt service related to major maintenance, renovation, and central capitalequipment expenditures.

Financial Statements

Accounting Principles

Princeton University's financial statements are presented in accordance with generally accepted accounting principles set forth by the Financial Accounting Standards Board (FASB) as supplemented by the audit guide of the American Institute of Certified Public Accountants (AICPA). In addition to general accounting guidance, the statements reflect the impact of specific reporting requirements of not-for-profit organizations prescribed by FASB Statements 116 and 117 on the subjects of accounting for contributions and the format of general purpose external financial statements, respectively. Compliance with AICPA guidance includes the consolidation of wholly owned subsidiaries and significant trusts in which the University is a beneficiary, as well as reporting tuition discounts, primarily fellowships and scholarships, as reductions of tuition revenue. The financial statements are fully comparable, including prior year data on the Consolidated Statement of Activities.

Financial Reports

The principal objectives of FASB Statement 117 are to provide consistency among the financial statements of not-for-profit organizations and to make them more comparable to those of the for-profit sector. Statement 117 requires not-for-profit organizations to provide, for their external financial reports, a statement of financial position, a statement of activities, and a statement of cash flows. The organization's resources are classified among three categories of net assets, that is, gross assets less related liabilities, based solely on the existence or absence of donor-imposed restrictions. Amounts for each of the three classes of net assets—permanently restricted, temporarily restricted, and unrestricted—are displayed in a statement of financial position, and the amounts of change in each category are displayed in a statement of activities.

Permanently restricted net assets are those resources that may never be spent, mainly endowment funds. They are generally the results of gifts and bequests with donor stipulations that they be invested to provide a permanent source of income. They may also include gifts in kind such as works of art or real property. *Temporarily restricted* net assets include those that, again by donor stipulation, must be invested only for a certain period of time or may be used in a specified future period. *Unrestricted* net assets may be expended for any purpose and result from investment income, including net gains, and from gifts.

Statement of Financial Position

The statement of financial position is a snapshot of the University's resources and obligations at the close of the fiscal year and is comparable to the document sometimes referred to as the balance sheet. Assets on the statement are presented in decreasing order of liquidity, from cash to property and equipment, the least liquid of its assets. A significant item is the amount for contributions receivable, a requirement under FASB Statement 116.

Liabilities are also presented in order of anticipated time of liquidation. Included is the liability under unitrust agreements, which represents the estimated amount payable to donors under the University's planned giving programs. The accounting rules require donees to record a liability for the present value of the expected lifetime payments to donors and to recognize the net amount received as a contribution in the year of receipt.

In accordance with the accounting rules, certain unrestricted net assets have been partially earmarked, or designated, according to their intended use by the University. A significant portion of unrestricted net assets, realized gains on endowment assets, has been reinvested and is not treated as available for spending. Temporarily restricted net assets include promises to give that are receivable in future years as well as donor-restricted contributions, the purpose of which has not yet been fulfilled. Permanently restricted net assets include endowment gifts that cannot be spent and funds held in perpetual trust by others.

Statement of Activities

The statement of activities is a summary of the income and expenditures for the year, classified according to the existence or absence of the restrictions described above. Sources such as tuition, sponsored research, and auxiliary activities are normally shown as unrestricted income, although income from certain gifts or sponsored agreements may be includible in any of the three classes of income depending upon the donor's specifications. Gifts to endowment, for example, are permanently restricted.

Income from temporarily restricted sources is reclassified to unrestricted income when the circumstances of the restriction have been fulfilled. All expenditures are made from unrestricted net assets, since an amount cannot be spent until all restrictions on its use have been removed.

The statement of activities is presented in two sections, operating and nonoperating, which attempt to reflect the principles of the University's operating budget. Items of income shown in the operating section include all unrestricted receipts as well as the endowment earnings made available for spending under the spending rule. Virtually all expenditures are considered to be associated with operating activity. Major items of income that are considered nonoperating include unrealized appreciation on investments and endowment income earned in the current year to be used in the succeeding year in accordance with operating budget policy. Unrestricted gift income, primarily from Annual Giving, is shown as operating income, while income from promises to give (pledges) is considered a nonoperating source of income.

The statement of activities concludes with a reconciliation of the change in each class of net assets for the year to the balance of net assets shown on the statement of financial position.

Statement of Cash Flows

The statement of cash flows is intended to be the bridge from the increase or decrease in net assets for the year to the change in cash balances from one year-end to the next. Several items shown as expenditures in the statement of activities, such as depreciation, do not require an outlay of cash, whereas the purchase of capital assets, which does require the expenditure of cash, is added directly to the statement of financial position and only shows on the statement of activities on a depreciation basis. Other items that affect cash balances but are not required to be included in the statement of activities include the purchase and sale of investment securities, borrowing proceeds and the repayment of loan principal, and the net change in accounts receivable and payable.

The reconciling items on the statement of cash flows are grouped into three categories. *Operating activities* are those items of income and expenditure that occur during the normal course of providing services as an educational institution. *Investing activities* include the acquisition of capital assets such as buildings and equipment, purchase and sale of investment securities, disbursing funds for new student and employee loans, and the collection of principal payments on such loans. *Financing activities* are those transactions that provide permanent capital for the organization, such as endowment gifts, as well as the proceeds from long-term borrowing to finance capital additions and the repayment of principal on such indebtedness.

Contributions

In accordance with FASB Statement 116, donors' unconditional promises to give are required to be recorded as revenue and as amounts receivable by donees in the year received. Prior practice was to recognize contributions only as collected, on a cash basis. Where collection is not expected within one year, the amount recorded is determined on a present-value basis. Conditional promises to give are recognized when they become unconditional, that is, when the conditions imposed by the donor have been substantially met.

Contributions must be classified among those that are permanently restricted, temporarily restricted, or unrestricted, as determined solely by the donor. The classification of contributions is essential for the proper presentation of revenue in the Statement of Activities and of net assets in the Statement of Financial Position, previously discussed.

Endowment Management

A significant portion of the operating budget is financed from endowment earnings. Consequently, the University's investment portfolio is professionally managed for total return that is accounted for under a consistently applied formula.

Most invested funds participate in the Primary Pool, which is operated on a market-value basis. Long-term growth of principal and increase of future earnings are the University's objectives in the investment of these funds. Funds participating in the Primary Pool are assigned units on a market-value basis. Funds withdrawn from the Primary

Pool receive appreciation or depreciation based on the change in unit market values. After deducting investment management fees, the earnings are allocated on the basis of units owned by participating funds.

The University follows an endowment spending rule that provides for an annual increase in the amount of Primary Pool earnings allocated for spending. For the Primary Pool's year ended May 31, 2001, the interest and dividends per unit (net of investment management fees) were $32.61. The unit earnings allocated for spending, including gains, were $211.00. The market value of a unit was $5,034.48 at June 30, 2001 and $5,150.07 at June 30, 2000.

A Secondary Pool is maintained for funds expected to be disbursed within five years. The University guarantees the principal of these funds and makes annual distributions at money market rates. Distributions to the participating funds for the Secondary Pool's year ended May 31, 2001 equaled 6.18 percent of the average market value.

The Balanced Fund and the Income Fund have been established for funds subject to the donor's reservation of life income. The fiscal year-end for each pool is December 31. These pools are operated on a market-value basis in a manner similar to the Primary Pool. After deducting investment management fees, earnings are distributed quarterly to the beneficiaries. For the year ended December 31, 2000, the earnings distribution from the Balanced Fund was $118.47 per unit, and the average market value of a unit was $2,630.51; the earnings distribution from the Income Fund was $12.38 per unit, and the average market value of a unit was $178.60.

The University also maintains a group of separately invested funds. Included therein are funds established from gifts of investments restricted as to sale by donors, funds where the University acts as custodian or fiscal agent for others, and the University's investments in real estate.

Conclusion

In summary, we hope that readers find the presentations and explanations helpful in interpreting the financial state of the University. Princeton is blessed with significant financial resources and is committed to utilizing them in support of our current institutional and research programs while simultaneously preserving their value for future generations.

Christopher McCrudden
Treasurer

Henry J. Murphy
Controller

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Deloitte & Touche

INDEPENDENT AUDITORS' REPORT

To the Board of Trustees
of Princeton University

We have audited the accompanying Consolidated Statements of Financial Position of Princeton University (the "University") as of June 30, 2001 and 2000 and the related Consolidated Statements of Activities and Cash Flows for the year ended June 30, 2001. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audits. The financial statements include certain prior-year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the University's financial statements for the year ended June 30, 2000, from which the summarized information was derived.

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 the University at June 30, 2001 and 2000, and the changes in its net assets and its cash flows for the year ended June 30, 2001 in conformity with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

October 26 2001

Deloitte
Touche
Tohmatsu

Princeton University
Consolidated Statements of Financial Position

June 30, 2001 and 2000

(dollars in thousands)	*2001*	*2000*
Assets		
Cash	$ 2,997	$ 6,326
Accounts and accrued interest receivable	71,474	75,154
Contributions receivable	201,011	249,395
Inventories and deferred charges	43,424	34,987
Investments at market value	8,750,100	8,777,100
Assets held in trust by others	88,999	103,341
Property:		
Land	40,107	40,476
Buildings and improvements	1,220,230	1,063,646
Construction in Progress	48,165	90,043
Other property	490,602	467,724
Accumulated depreciation	(530,683)	(497,907)
Total assets	$10,426,426	$10,410,285
Liabilities		
Accounts payable	$ 60,131	$ 53,565
Deposits, advance receipts, and accrued liabilities	33,415	31,284
Deposits held in custody for others	126,552	124,139
Deferred revenues	42,532	42,627
Liability under planned giving agreements	83,445	85,829
Federal loan programs	11,288	10,941
Indebtedness to third parties	464,373	429,232
Accrued postretirement benefits	108,576	95,995
Total liabilities	930,312	873,612
Net Assets		
Unrestricted	7,743,630	7,733,942
Temporarily restricted	788,513	871,866
Permanently restricted	963,971	930,865
Total net assets	9,496,114	9,536,673
Total Liabilities and Net Assets	$10,426,426	$10,410,285

See notes to consolidated financial statements.

Princeton University
Consolidated Statement of Activities

Year ended June 30, 2001 (with comparative totals for 2000)

(dollars in thousands)	*Unrestricted*	*Temporarily Restricted*	*Permanently Restricted*	*2001 Total*	*2000 Total*
Revenues, gains, and other support					
Tuition and fees	$ 160,266			$ 160,266	$ 152,955
Less scholarships and fellowships	(72,110)			(72,110)	(67,384)
Net tuition and fees	88,156			88,156	85,751
Government grants and contracts	165,951			165,951	153,272
Private gifts, grants, and contracts	61,590			61,590	58,052
Sales and services of auxiliary activities	56,404			56,404	51,140
Other sources	19,839			19,839	15,813
Investment earnings distributed	221,145	$ 25,625		246,770	229,942
Total revenues, gains, and other support	613,085	25,625		638,710	593,790
Net assets released from restrictions	74,499	(74,499)			
Total revenues, gains, and other support	687,584	(48,874)		638,710	593,790
Expenses and losses					
Educational and general:					
Academic departments and programs	310,619			310,619	283,449
Academic support	16,378			16,378	15,182
Student services	21,354			21,354	15,774
Library	34,761			34,761	33,814
General administration and general institutional support	67,212			67,212	59,158
Other student aid	11,853			11,853	9,956
Plasma Physics Laboratory	67,472			67,472	65,040
Total educational and general	529,649			529,649	482,373
Auxiliary activities	88,958			88,958	81,800
Interest on indebtedness	21,057			21,057	17,493
Total expenses and losses	639,664			639,664	581,666
Increase (decrease) from revenues, gains, and other support over expenses and losses	47,920	(48,874)		(954)	12,124
Nonoperating activities					
Adjustments to planned giving agreements		(1,549)	$ 1,305	(244)	470
Increase (decrease) in value of assets held in trust by others			(14,342)	(14,342)	14,722
Private gifts, noncurrent	21,842	11,184	37,569	70,595	178,635
Net unrealized appreciation (depreciation) on investments	(666,372)	(46,250)	1,017	(711,605)	437,216
Investment earnings	827,443	27,761	7,557	862,761	1,649,429
Distribution of prior year investment earnings for spending	(221,145)	(25,625)		(246,770)	(229,942)
Increase (decrease) from nonoperating activity	(38,232)	(34,479)	33,106	(39,605)	2,050,530
Increase (decrease) in net assets	9,688	(83,353)	33,106	(40,559)	2,062,654
Net assets at the beginning of the year	7,733,942	871,866	930,865	9,536,673	7,474,019
Net assets at the end of the year	$7,743,630	$788,513	$963,971	$9,496,114	$9,536,673

See notes to consolidated financial statements.

Princeton University
Consolidated Statements of Cash Flows

Years ended June 30, 2001and 2000

(dollars in thousands)	*2001*	*2000*
Cash flows from operating activities:		
Change in net assets	$ (40,559)	$ 2,062,654
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation expense	58,000	54,480
Property gifts-in-kind	(3,805)	(2,659)
Adjustments to planned giving agreements	244	(470)
Realized gain on investments	(656,020)	(1,547,232)
Unrealized depreciation (appreciation) on investments	711,605	(437,216)
Gain on disposal of fixed assets	(1,764)	(1,470)
Contributions received for long-term investment	(41,918)	(87,103)
Changes in operating assets and liabilities:		
Increase (decrease) in operating assets	57,970	(113,033)
Increase in operating liabilities	23,596	46,995
Net cash provided by (used by) operating activities	107,349	(25,054)
Cash flows from investing activities:		
Purchases of property, plant, and equipment	(154,345)	(152,005)
Proceeds from disposal of property, plant, and equipment	6,213	3,625
Purchases of investments	(9,275,823)	(8,012,556)
Proceeds from maturities/sales of investments	9,283,815	7,976,504
Net cash used by investing activities	(140,140)	(184,432)
Cash flows from financing activities:		
Issuance of indebtedness to third parties	63,765	159,463
Payment of debt principal	(35,381)	(40,219)
Contributions received for long-term investment	41,918	87,103
Transactions on planned giving agreements	(628)	5,429
Government advances for loan funds	347	305
Net cash provided by financing activities	70,021	212,081
Net increase (decrease) in cash	(3,329)	2,595
Cash at beginning of year	6,326	3,731
Cash at end of year	$ 2,997	$ 6,326
Supplemental disclosures:		
Interest paid	$ 21,057	$ 17,493

See notes to consolidated financial statements.

Princeton University
Notes to Consolidated Financial Statements

Year ended June 30, 2001

Nature of operations

Princeton University (the "University") is a privately endowed, nonsectarian institution of higher learning. When the University was chartered in 1746 as the College of New Jersey, it became the fourth college in British North America. It was renamed Princeton University in 1896. Originally located in Elizabeth, New Jersey, and later located in Newark, New Jersey, the school was moved to Princeton, New Jersey, in 1756.

The student body numbers approximately 4,600 undergraduates and 1,800 graduate students in more than 60 departments and programs. The University offers instruction in the liberal arts and sciences and in professional programs of the School of Architecture, the School of Engineering and Applied Science, and the Woodrow Wilson School of Public and International Affairs. The faculty numbers more than 1,000, including visitors and part-time appointments.

Summary of significant accounting policies

The financial statements of the University are prepared on the accrual basis and include the accounts of its wholly owned subsidiaries and two foundations controlled by the University. Financial information conforms to the statements of accounting principles of the Financial Accounting Standards Board (FASB) and to the American Institute of Certified Public Accountants *Audit and Accounting Guide for Not-for-Profit Organizations*. Recent pronouncements of the FASB include Statements of Financial Accounting Standards ("SFAS") No. 116, *Accounting for Contributions Received and Contributions Made*, and SFAS No. 117, *Financial Statements of Not-for-Profit Organizations*, issued by the Financial Accounting Standards Board.

Under SFAS No. 116, unconditional promises to give are recognized as revenues in the year made, not in the year in which the cash is received. The amounts are present-valued based on expected collections. Amounts received from donors to planned giving programs are shown in part as a liability for the present value of annuity payments to the donor and the balance as a gift of either temporarily or permanently restricted net assets.

SFAS No. 117 prescribes the standards for external financial statements and requires not-for-profit organizations to prepare a statement of financial position (balance sheet), statement of activities, and statement of cash flows. It requires the classification of the organization's net assets and its revenues and expenses into three categories according to the existence or absence of donor-imposed restrictions—permanently restricted, temporarily restricted, or unrestricted. Changes in each category are reflected in the statement of activities, certain of which are further categorized as nonoperating. Such activities primarily reflect transactions of a long-term investment or capital nature, including contributions receivable in future periods, contributions subject to donor-imposed restrictions, and gains and losses on investments in excess of the University's spending rule. Other significant accounting policies are described elsewhere in these notes.

SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended by SFAS Nos. 137 and 138, establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts (collectively referred to as "derivatives"), and for hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. This statement is effective for fiscal years beginning after June 15, 2000. Its adoption did not have a significant effect on the University's financial statements.

The preparation of the University's financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the consolidated statements of financial position and the reported amounts of revenue and expense included in the consolidated statement of activities. Actual results could differ from such estimates.

The prior year financial statements of the University include certain reclassifications to conform to the current year presentation.

Investments

All investments in equity securities with readily determinable fair values and all investments in debt securities are reported at fair values. In addition, the University utilizes fair values for reporting other investments, primarily limited partnerships and derivatives.

The fair value of marketable equity, debt, and certain derivative securities (which includes both domestic and foreign issues) is generally based upon a combination of published current market prices and exchange rates. The fair value of restricted securities and other investments, where published market prices are not available, is based on estimated values when practicable, or at a nominal value. The fair values of limited partnerships have been based on estimates and assumptions determined by the respective general partners or a valuation committee in the absence of readily ascertainable market values. A summary of investments at fair value at June 30, 2001 and 2000 is as follows (in millions):

	2001	*2000*
Managed portfolio:		
Equity accounts	$ 5,486.8	$ 4,489.5
Fixed income accounts	1,073.8	1,091.0
Limited partnerships	1,822.6	2,771.9
Educational loans and mortgages	233.0	234.2
Miscellaneous assets	133.9	190.5
Gross investments	8,750.1	8,777.1
Planned Giving investments	(190.8)	(198.7)
Bond proceeds awaiting drawdown	(13.8)	(68.7)
Government funding for student loans	(15.0)	(14.4)
Working capital	(171.5)	(97.2)
Net University investment portfolio	$ 8,359.0	$ 8,398.1

The composition of net investment return for the years ended June 30, 2001 and 2000 were as follows (in thousands):

	2001	*2000*
Realized and unrealized gains and (losses)	$ (55,586)	$ 1,984,448
Interest, dividends, and other income	206,742	102,197
Total	$ 151,156	$ 2,086,645

The University follows a spending rule for its endowment funds, including funds functioning as endowment, that provides for regular increases in spending while preserving the long-term purchasing power of the endowment. Earnings available for spending are shown in the Consolidated Statement of Activities as operating income, and the balance as nonoperating income.

As of June 30, 2001 and 2000, the University had loaned certain securities, returnable on demand, with a market value of $199 and $180 million, respectively, to several financial institutions that have deposited collateral with respect to such securities of $204 and $186 million, respectively. The University receives income on the invested collateral, and also continues to receive interest and dividends from the securities on loan. The collateral received in connection with the securities lending program is reduced by the liability to borrowers for financial statement purposes.

As part of its investment strategy, the University enters into a variety of financial instruments and strategies, including futures, swaps, options, short sales, and forward foreign currency exchange contracts. In all cases except forward foreign currency exchange and swap contracts, these transactions are traded through securities and commodities exchanges. The forward foreign currency exchange and swap contracts are executed with creditworthy banks and brokerage firms.

During the year a hedge program was continued to maintain the value of certain volatile securities in the private equity sector. The program uses a series of customized derivative contracts to, in effect, sell forward a portion of the equity exposure. At June 30, 2001 the program had the net effect of reducing the University's exposure to private equity investments by $32 million, and resulted in approximately $26 million of net unrealized gains.

A swap program in real estate investment trusts (REITs) is in effect. Under the terms of the program the University receives the return on an approximately $100 million basket of REITs. At June 30 the market value of the basket was approximately $2.6 million less than the notional value, and is reflected in the market value of the portfolio.

At June 30, 2001 and 2000 approximately $30.0 million of a controlled foundation's equity holdings have been hedged through a series of put-and-call options.

Property

Land additions subsequent to June 30, 1973 are reported at estimated market value at the date of gift, in the case of gifts, and at cost in all other cases. Land acquired through June 30, 1973 is carried at estimated value at that date, computed using municipal tax assessments because it was not practicable to determine historical cost or the market value at the date of gift.

Buildings and improvements are stated at cost. Expenditures for operation and maintenance of physical plant are expensed as incurred.

Items classified as other property at June 30, 2001 and 2000 consist of the following (in thousands):

	2001	*2000*
Equipment	$ 233,966	$ 225,383
Rare books	41,451	37,829
Library books, periodicals, and bindings	147,682	137,531
Fine arts objects	67,503	66,981
Total	$ 490,602	$ 467,724

Equipment, rare books, and library books, periodicals, and bindings are stated at cost. Equipment includes items purchased with federal government funds; an indeterminate portion of those items are expected to be transferred to the University at the termination of the respective grant or contract. In addition to purchases with University funds, the University, since its inception, has received a substantial number of fine arts objects from individual gifts and bequests. Art objects acquired through June 30, 1973 are carried at insurable values at that date because it is not practicable to determine the historical cost or market value at the date of gift. Art objects acquired subsequent to June 30, 1973 are recorded at cost or fair value at the date of gift.

Annual depreciation is calculated on the straight-line method over 30 and 40-year lives for buildings and improvements, 30 years for library books, and 10 and 15 years for equipment.

Funds held in trust by others

The University is the income beneficiary of various trusts that are held and controlled by independent trustees. In addition, the University is the income beneficiary of entities that qualify as supporting organizations under Section 509(a)(3) of the U.S. Internal Revenue Code. Funds held in trust by others are recognized at the estimated fair value of the assets or the present value of the future cash flows when the irrevocable trust is established or the University is notified of its existence. Funds held in trust by others, stated at fair value, amounted to $89.0 million in 2001 and $103.3 million in 2000.

Deferred revenues

Deferred revenues represent advance receipts relating to the University's real estate leasing activities. Such amounts are amortized over the term of the related leases.

Indebtedness to third parties

The debt consists of loans through the New Jersey Educational Facilities Authority (NJEFA), taxable revenue bonds, commercial paper, various parental loans with the Student Loan Marketing Association (Sallie Mae) and a local bank, and various mortgages as follows (in thousands):

NJEFA Revenue Bonds	
Dated July 1, 1992, Series F, 5.08%, due in installments through July 2002, net of unamortized discount of $7	2,138
Dated August 1, 1993, Series B, 4.17%, due in installments through July 2003, net of unamortized discount of $21	4,039
Dated July 1, 1994, Series A, 5.84%, due in installments through July 2012, net of unamortized discount of $167	13,203
Dated July 1, 1995, Series C, 5.08%, due in installments through July 2025, net of unamortized discount of $259	17,321
Dated July 1, 1996, Series C, 4.86% due in installments through July 2006, net of unamortized discount of $36	13,694
Dated July 1, 1997, Series E, 4.42%, due in installments through July 2007, net of unamortized discount of $39	14,466
Dated July 1, 1998, Series E, 4.87%, due in installments through July 2024, net of unamortized discount of $79	17,681
Dated July 1, 1998, Series F, 4.44%, due in installments through July 2018, net of unamortized discount of $147	30,423
Dated February 15, 1999, Series A, 4.80%, due in installments through July 2029, net of unamortized discount of $361	43,354
Dated July 15, 1999, Series B, 4.98%, due in installments through July 2019, net of unamortized discount of $458	46,552
Dated June 15, 2000, Series E, 5.35%, due in installments through July 2020, net of unamortized discount of $438	48,137
Dated October 15, 2000, Series H, 5.34%, due in installments through July 2030, net of unamortized discount of $1,447	98,213
NJEFA Capital Improvement Fund	
Dated August 1, 2000, Series A, 5.72% due in installments through August 2020	2,065
Taxable Revenue Bonds	
Dated March 15, 1994, Series 1994B, 6.41%, due in installments through July 2002, net of unamortized discount of $28	9,592
Dated March 15, 1994, Series 1994C, 6.48%, due in installments through July 2003, net of unamortized discount of $18	4,227
Commercial Paper	51,700
Parental Loans	47,272
Mortgages	296
Total	$ 464,373

The proceeds of NJEFA loans were used primarily for renovation and rehabilitation of University facilities and purchases of capital equipment. The proceeds of the Taxable Revenue Bonds were used to advance refund certain NJEFA loans and to reimburse the University for the cost of renovation and rehabilitation of University facilities and purchases of capital equipment in recent years that, due to statutory limitation, could not be financed with tax-exempt debt.

Subsequent to June 30, 2001 the University issued bonds of $100 million through the NJEFA. The purpose of the bonds was to provide funding for the annual major maintenance, capital equipment and renovation budgets, and is a 20 year, variable rate issue. The University intends to issue additional bonds in the future.

The NJEFA loan agreements entered into through 1998 contain certain restrictive covenants with which the University must comply. Specifically, the ratio of available assets to general liabilities, as defined in the loan agreements, shall be equal to at least two to one. Also, the University pledges tuition and fees received from all students up to an amount equal to one and one half times the maximum annual debt service on all outstanding NJEFA bonds, in addition to the full faith and credit of the University. The University was in compliance with these covenants at June 30, 2001.

Loans with the Student Loan Marketing Association (Sallie Mae) are used for the parental loan program. As of June 30, 2001, the amount outstanding was $25.2 million, at rates ranging from 5.2 percent to 9.9 percent. As collateral, the University pledges these parent loans and additional student loans for which Sallie Mae provides a second market. In fiscal 1999 the University entered into a loan facility with a local bank to provide funding up to $40 million for the parental loan program. Terms to the borrowers are similar to the Sallie Mae program in that fixed or variable rates may be selected on a pass-through basis; terms may be as long as 14 years. At June 30, 2001 the balance outstanding was $22.0 million at rates ranging from 5.8 percent to 7.4 percent.

In fiscal year 1998 a commercial paper program was authorized as an initial step of a financing proposal to provide construction funds for several approved capital projects. The proceeds have permitted construction to proceed until permanent financing from gifts or other sources has been made available. The program has been authorized to a maximum level of $120 million for a period of up to five years. At June 30, 2001 $51.7 million was issued through the NJEFA on a tax-exempt basis to the investors. Maturities of the debt were from 32 to 127 days, and the nominal interest rate was 2.68 percent.

Principal payments for each of the next five years and thereafter on debt outstanding at June 30, 2001, excluding commercial paper, are as follows (in thousands):

	Principal payments
2002	$ 34,520
2003	33,749
2004	27,642
2005	24,545
2006	25,109
Thereafter	270,613
Subtotal	416,178
Unamortized discount	(3,505)
Net long-term debt	$ 412,673

The fair value of the University's long-term debt is estimated based on current notes offered for the same or similar issues with similar security, terms, and maturities. At June 30, 2001, the carrying value and the estimated fair value of the University's long-term debt, excluding commercial paper, were $412.7 million and $423.5 million, respectively.

Commitments and contingencies

At June 30, 2001, the University had authorized major renovation and capital construction projects for more than $500 million including the Genomics Institute ($45 million), new graduate and undergraduate housing ($66 million) and a dormitory renovation program ($65 million). Of the total, approximately $300 million had not yet been expended. Also, the University is obligated under certain limited partnership agreements to advance additional funding periodically up to specified levels. At June 30, 2001, the University had unfunded commitments of $1.095 billion that are likely to be called through 2006.

Employee benefit plans

Effective January 1, 1994, all faculty and staff who meet specific employment requirements participate in a defined contribution plan, which participates in the Teachers Insurance and Annuity Association (TIAA) and College Retirement Equities Fund (CREF). Prior to this date, the University participated in a TIAA and CREF defined contribution plan for faculty and certain administrative employees, while all other employees participated in a noncontributory defined benefit plan. The University's contributions were $26.2 million for the year ended June 30, 2001. The defined contribution plan permits employee contributions.

Postretirement benefits other than pensions

Effective July 1, 1993, the University adopted the provisions of SFAS No. 106, *Accounting for Postretirement Benefits Other Than Pensions*. SFAS 106 requires employers to recognize the cost of providing postretirement benefits for employees over the period of their working years. The University has calculated its Accumulated Postretirement Benefits Obligation ("APBO") and elected to amortize it over 20 years.

The University provides single coverage health insurance to its retirees who meet certain eligibility requirements. Participants may purchase additional dependent or premium coverage. The accounting for the plan anticipates future cost-sharing changes to the written plan that are consistent with the University's expressed intent to increase retiree contributions in line with medical costs.

The benefits cost for the year consists of the following (in thousands):

Service cost	$ 4,274
Interest cost	9,846
Net amortization of transition amount	6,361
Other	(2,272)
Total	$ 18,209

The APBO at June 30, 2001 consisted of actuarially determined obligations to the following categories of employees (in thousands):

Retirees	$ 63,674
Fully eligible active employees	38,804
Other active participants	41,660
Total	$ 144,138

Reconciliation of funded status (in thousands):

Accumulated postretirement benefit obligation and funded status	$ 144,138
Unrecognized transition obligation existing at June 30, 2001	(76,335)
Unrecognized net gain	40,773
Accrued expense at June 30, 2001	$ 108,576

An assumed discount rate of 7.5 percent was used to calculate the APBO. The assumed health care cost trend rate to be used to calculate the University's cost of benefits for fiscal 2001 is an increase of 10 percent over the costs for fiscal 2000. The cost trend used to calculate the APBO ranges downward to 5.25 percent in the year 2006 and thereafter. An increase of 1 percent in the cost trend rate would raise the APBO to $160.9 million and cause the service and interest cost components of the net periodic cost to be increased by $3.9 million.

Promises to give

At June 30, 2001 and 2000 the University had received from donors unconditional promises to give contributions of amounts receivable in the following periods (in thousands):

	2001	*2000*
Less than one year	$ 61,842	$ 75,501
One to five years	138,184	180,443
More than five years	43,437	47,428
Total	243,463	303,372
Less unamortized discount	42,452	53,977
Net amount	$ 201,011	$ 249,395

The amounts promised have been discounted at a rate for intermediate-term funds to take into account the time value of money. Current year promises are included in revenue as additions to temporarily or permanently restricted net assets, as determined by the donors.

In addition, the University has received from donors promises to give $9.4 million, which are conditioned upon the raising of matching gifts from other sources and other criteria. These amounts will be recognized as income in the periods in which the conditions have been fulfilled.

Net assets

Net assets are categorized as unrestricted, temporarily restricted, and permanently restricted. The unrestricted category contains, in addition to expendable funds, amounts dedicated to special programs, invested in plant and equipment, and designated for other related purposes. Temporarily restricted net assets are those that may be spent after the occurrence of an event or time certain, and permanently restricted net assets cannot be spent.

Fair value of financial instruments

Except as set forth elsewhere in these notes, the University's other financial instruments are carried in the balance sheet at amounts that approximate their fair values.

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*As of 9/30/01

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*As of 9/30/01

PrincetonUniversity

Report of the Treasurer

Princeton University 2000-01

Cover and inside front cover photographs:

The Friend Center for Engineering Education, a monument to a long-standing friendship between two Princeton students, was dedicated in October, 2001. University Charter Trustee Dennis Keller '63, chair and chief executive officer of DeVry Inc., provided a generous gift to establish the center in memory of Peter Friend '63. The two, acquainted since childhood in Hinsdale, Ill., were roommates at Princeton. Friend died while an undergraduate, just before his 21st birthday.

At the dedication ceremony President Tilghman said, "In the enduring connection between Dennis Keller and Peter Friend, this new center symbolizes the bonds of friendship and devotion that are woven so strongly into the fabric of our University community. The Friend Center will serve as a wonderful new resource for engineering students, and also as an important academic gateway, introducing undergraduates from other disciplines to the vastly interesting and vital study of technology and applied science."

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In the Nation's Service and in the Service of All Nations