



**BROWN UNIVERSITY**

Financial Statements

June 30, 2006

(With Independent Auditors' Report Thereon)



**KPMG LLP**  
600 Fleet Center  
50 Kennedy Plaza  
Providence, RI 02903-2321

## **Independent Auditors' Report**

The President and Corporation  
Brown University:

We have audited the accompanying statement of financial position of Brown University (the University) as of June 30, 2006, and the related statements of activities, cash flows and expenses by function for the year then ended. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the University's 2005 financial statements and, in our report dated September 27, 2005, we expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the University as of June 30, 2006, and the changes in its net assets and its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

**KPMG LLP**

October 20, 2006

**BROWN UNIVERSITY**

## Statement of Financial Position

June 30, 2006

(with comparative information as of June 30, 2005)

(Thousands of dollars)

<b>Assets</b>	<b>2006</b>	<b>2005</b>
Cash and cash equivalents	\$ 37,427	\$ 9,662
Accounts receivable and other assets	46,692	54,636
Notes receivable	31,526	33,170
Contributions receivable, net	226,103	173,266
Investments, at fair value	2,392,684	2,133,207
Funds held in trust by others	43,425	17,308
Bond proceeds held in refunding trust	—	21,377
Land, buildings and equipment, net	582,813	492,384
Total assets	<u>\$ 3,360,670</u>	<u>\$ 2,935,010</u>
<b>Liabilities</b>		
Accounts payable and accrued liabilities	\$ 72,532	\$ 73,077
Annuity and other split interest obligations	21,996	75,797
Deferred revenues and student deposits	19,302	15,388
Refundable advances	38,194	37,293
Asset retirement obligations	12,535	—
Bonds payable through refunding trust	—	21,377
Bonds, loans and notes payable	365,553	249,636
Total liabilities	<u>530,112</u>	<u>472,568</u>
Net assets:		
Unrestricted	1,419,890	1,271,563
Temporarily restricted	190,915	148,539
Permanently restricted	1,219,753	1,042,340
Total net assets	<u>2,830,558</u>	<u>2,462,442</u>
Total liabilities and net assets	<u>\$ 3,360,670</u>	<u>\$ 2,935,010</u>

See accompanying notes to financial statements.

**BROWN UNIVERSITY**  
Statement of Activities  
Year ended June 30, 2006  
(with comparative totals for the year ended June 30, 2005)  
(Thousands of dollars)

	2006			2005	
	Unrestricted	Temporarily restricted	Permanently restricted	Total	Total
Operating revenues:					
Tuition and fees	\$ 257,496			\$ 257,496	\$ 235,458
Less University scholarships	(71,040)			(71,040)	(63,716)
	<u>186,456</u>	<u>—</u>	<u>—</u>	<u>186,456</u>	<u>171,742</u>
Grants and contracts – direct	104,387			104,387	106,412
Grants and contracts – indirect	29,288			29,288	28,443
Contributions for current use	43,762	12,358		56,120	43,972
Endowment income distributed	79,247	6,579		85,826	77,819
Sales and services of auxiliary enterprises	70,738			70,738	65,787
Other income	29,506	692		30,198	28,456
Net assets released from restrictions	10,938	(10,938)		—	—
<b>Total operating revenues</b>	<u>554,322</u>	<u>8,691</u>	<u>—</u>	<u>563,013</u>	<u>522,631</u>
Operating expenses:					
Instruction and departmental research	189,928			189,928	174,910
Sponsored programs	99,569			99,569	104,543
Academic and student support	102,413			102,413	95,888
Institutional support	90,070			90,070	82,043
Auxiliary services	72,155			72,155	66,060
<b>Total operating expenses</b>	<u>554,135</u>	<u>—</u>	<u>—</u>	<u>554,135</u>	<u>523,444</u>
<b>Change in net assets from operating activities</b>	<u>187</u>	<u>8,691</u>	<u>—</u>	<u>8,878</u>	<u>(813)</u>
Nonoperating activities:					
Contributions to long-term assets	13,722	30,218	76,885	120,825	113,267
Net investment earnings	220,861	12,134	38,458	271,453	220,385
Endowment income distributed	(79,247)	(6,579)		(85,826)	(77,819)
Change in value of split interest agreements	106	548	56,787	57,441	(9,884)
Other net asset changes	3,568	(1,596)	5,283	7,255	(1,697)
Net assets released from restrictions	1,040	(1,040)		—	—
<b>Change in net assets from nonoperating activities</b>	<u>160,050</u>	<u>33,685</u>	<u>177,413</u>	<u>371,148</u>	<u>244,252</u>
Cumulative effect of change in accounting principle	(11,910)			(11,910)	—
<b>Change in net assets</b>	<u>148,327</u>	<u>42,376</u>	<u>177,413</u>	<u>368,116</u>	<u>243,439</u>
Net assets, beginning of year	1,271,563	148,539	1,042,340	2,462,442	2,219,003
Net assets, end of year	<u>\$ 1,419,890</u>	<u>\$ 190,915</u>	<u>\$ 1,219,753</u>	<u>\$ 2,830,558</u>	<u>\$ 2,462,442</u>

See accompanying notes to financial statements.

**BROWN UNIVERSITY**  
Statement of Cash Flows  
Year ended June 30, 2006  
(with comparative information for the year ended June 30, 2005)  
(Thousands of dollars)

	<b>2006</b>	<b>2005</b>
Cash flows from operating activities:		
Change in net assets	\$ 368,116	\$ 243,439
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:		
Cumulative effect of change in accounting principle	11,910	—
Depreciation	32,552	32,641
Net realized and unrealized gains on investments	(279,266)	(229,956)
Contributions of property and securities	(33,567)	(18,415)
Contributions restricted for long-term investment	(42,117)	(49,694)
Changes in assets and liabilities:		
Accounts receivable and other assets	7,944	(8,412)
Contributions receivable, net	(52,837)	3,697
Accounts payable and accrued liabilities	(2,968)	21,721
Deferred revenues and student deposits	3,914	(103)
Refundable advances	901	(4,670)
Net cash provided by (used in) operating activities	14,582	(9,752)
Cash flows from investing activities:		
Purchase of land, buildings and equipment	(121,600)	(69,202)
Purchases of investments	(2,562,129)	(1,972,297)
Sales of investments	2,617,152	1,865,733
Loans issued	(32,723)	(32,300)
Loans repaid	34,367	32,660
Change in funds held in trust, net	(26,117)	40,929
Net cash used in investing activities	(91,050)	(134,477)
Cash flows from financing activities:		
Contributions restricted for long-term investment	42,117	49,694
Payments of long-term debt	(18,598)	(2,240)
Proceeds from issuance of bonds	134,515	—
Change in annuity and other split interest obligations	(53,801)	56,595
Net cash provided by financing activities	104,233	104,049
Change in cash and cash equivalents	27,765	(40,180)
Cash and cash equivalents, beginning of year	9,662	49,842
Cash and cash equivalents, end of year	\$ 37,427	\$ 9,662

See accompanying notes to financial statements.

**BROWN UNIVERSITY**

Statement of Expenses by Function

Year ended June 30, 2006

(with summarized comparative information for the year ended June 30, 2005)

(Thousands of dollars)

	2006										2005
	Instruction and Departmental Research	Sponsored Programs	Academic and Student Support			Institutional Support			Operation and Maintenance of Plant	Total	Total
			Libraries and Acad Support	Computing and Info Services	Student Services	General and Administrative	Advancement and Univ Relations	Auxiliary Services			
Expenses:											
Salaries and wages	\$ 110,872	\$ 46,965	\$ 9,169	\$ 9,000	\$ 20,372	\$ 27,810	\$ 13,234	\$ 13,655	\$ 11,361	\$ 262,438	\$ 245,534
Employee benefits	25,921	10,976	2,715	2,739	4,316	11,004	4,002	3,492	4,938	70,103	68,300
Purchased services	7,640	17,070	273	234	766	14,674	1,293	3,479	4,863	50,292	50,983
Supplies and general Utilities	10,938	6,706	9,042	4,291	9,729	2,686	2,440	14,692	2,936	63,460	62,165
Travel	3,186	3,667	132	237	2,887	1,286	589	382	17,101	17,101	12,490
Other expenses	8,116	3,573	472	407	5,402	4,402	3,396	2,932	66	12,432	11,371
Subtotal	166,673	88,957	21,803	16,908	43,472	61,862	24,954	38,632	45,019	508,280	481,109
Interest expense	3,420	1,561	1,449	195	1,281	336	143	4,918		13,303	9,695
Plant expense allocation	11,575	5,282	4,905	659	4,335	1,136	484	16,643	(45,019)	—	—
Depreciation	8,260	3,769	3,843	470	3,093	810	345	11,962	—	32,552	32,640
2006 total	\$ 189,928	\$ 99,569	\$ 32,000	\$ 18,232	\$ 52,181	\$ 64,144	\$ 25,926	\$ 72,155	\$ —	\$ 554,135	
2005 total	\$ 174,910	\$ 104,543	\$ 30,830	\$ 17,269	\$ 47,789	\$ 59,195	\$ 22,848	\$ 66,060	\$ —	\$ —	\$ 523,444

See accompanying notes to financial statements.

# BROWN UNIVERSITY

## Notes to Financial Statements

June 30, 2006

(with comparative information as of and for the Year Ended June 30, 2005)

(Thousands of dollars)

### (1) Summary of Significant Accounting Policies

#### (a) *Basis of Presentation*

The financial statements of Brown University are prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles (GAAP). The financial statements include the accounts of the John Nicholas Brown Center for the Study of American Civilization and Farview Incorporated, a real estate holding company, both of which are wholly owned subsidiaries. Brown University and these consolidated entities are collectively referred to herein as the University.

University resources are reported for accounting purposes in separate classes of net assets based upon the existence or absence of donor-imposed restrictions. The net assets are classified as permanently restricted, temporarily restricted, or unrestricted.

Permanently restricted net assets include gifts of cash and other assets that are required to be retained permanently by the University. Generally the donors of these assets permit the University to use all or part of the investment return on these assets. Such assets are primarily included in the University's endowment funds. Pursuant to Rhode Island General Law, these funds include sufficient net appreciation in order to maintain the purchasing power of the original dollar value of the funds.

Temporarily restricted net assets carry specific donor-imposed restrictions on the expenditure or other use of the contributed funds. Temporary restrictions may expire either due to the passage of time or through actions of the University pursuant to stipulations indicated by the donor.

Unrestricted net assets are those not subject to donor-imposed restrictions. Unrestricted net assets may be designated for specific purposes by action of the Corporation or may otherwise be limited by contractual agreements with outside parties.

Expenses are reported as decreases in unrestricted net assets. Expirations of donor-imposed restrictions that simultaneously increase one class of net assets and decrease another are reported as net assets released from restrictions.

The Statement of Activities reports the change in net assets from operating and nonoperating activities separately. Operating revenues include tuition and fees, gifts and net assets released from restrictions for current use, grants and contracts, and the allocation of endowment spending in support of the University's educational programs or research conducted by the academic departments. Operating expenses include the costs of providing University programs and other activities, and are reported by functional categories, after allocating, on a square footage basis, expenses for operation and maintenance of plant, interest on indebtedness and depreciation. Nonoperating activities primarily consist of the excess of long-term investment earnings over amounts utilized in operating activities, contributions and net assets released from restrictions for endowment and facilities, and other activities not in direct support of the University's annual operations.

# BROWN UNIVERSITY

## Notes to Financial Statements

June 30, 2006

(with comparative information as of and for the Year Ended June 30, 2005)

(Thousands of dollars)

**(b) *Cash and Cash Equivalents***

Cash equivalents may consist of money market funds and investments with maturity dates when purchased of less than 90 days, and are carried at cost, which approximates fair value.

The University has transferred certain amounts of operating fund working capital to the long-term investment pool in order to enhance earnings on these funds. These funds are now included in the investments at fair value.

**(c) *Accounts and Notes Receivable and Other Assets***

Accounts receivable and other assets include amounts due from students, reimbursements due from sponsors of externally funded research, accrued income on investments, inventory and prepaid expenses. Notes receivable consist primarily of loans to students. Accounts receivable and notes receivable are carried at cost, which approximates fair value. The balances for accounts receivable and notes receivable are presented net of allowances for uncollectibles of \$727 and \$594, respectively, at June 30, 2006, and \$765 and \$406, respectively, at June 30, 2005.

**(d) *Investments***

Investments are stated at fair value in the case of marketable securities and at estimated fair value for certain nonmarketable securities. Fair value is determined on the following basis: equity and fixed-income investments are valued at the last sale price (if quotations are readily available) or at the closing bid price in the principal market in which such securities are normally traded (if no sale price is available). Nonmarketable securities include alternative investments such as private equity, venture capital, and real estate, which are valued using current estimates of fair value obtained from the investment manager in the absence of readily determinable public market values. Such valuations generally reflect discounts for liquidity and consider variables such as financial performance of investments, including comparison of comparable companies' earning multiples, cash flow analysis, recent sales prices of investments, and other pertinent information. Because of the inherent uncertainty of valuation for these investments, the investment manager's estimate may differ from the values that would have been used had a ready market existed. The University believes the carrying amount of these financial instruments is a reasonable estimate of fair value.

Certain of the University's investment funds and partnerships use derivative instruments to hedge against market risk and to enhance investment returns. At any point during the year, the University may have exposure to derivatives primarily through limited liability vehicles such as limited partnerships and commingled investment funds. In addition, the University maintains certain directly held derivative financial instruments to hedge its portfolio, including exchange contracts, futures, options, and swap agreements. The portfolio is exposed to certain counterparty credit risks associated with these instruments. These risks are controlled by considering the credit rating, business risk, and reputation of any counterparty before entering into a transaction, diversifying across a number of counterparties, executing standardized contracts among all parties to the transaction, and monitoring for any change in the credit standing of its counterparty during the life of the transaction.

# **BROWN UNIVERSITY**

## Notes to Financial Statements

June 30, 2006

(with comparative information as of and for the Year Ended June 30, 2005)

(Thousands of dollars)

Investments also include gift annuities and charitable remainder trusts. These funds are held in trust for one or more beneficiaries, and generally pay lifetime income to those beneficiaries, after which the principal is made available to the University in accordance with donor intentions. The assets are recorded at fair value and liabilities, which are included in accounts payable and accrued liabilities, are recorded to recognize the present value of estimated future payments due to beneficiaries.

**(e) Endowment**

The University invests its endowment funds and allocates the related earnings for expenditure in accordance with the total return concept. The endowment usage is determined in accordance with the policy adopted by the Corporation. This policy fixes the spending range of endowment total return between 4.5% and 5.5% of the average fair value of applicable endowment for the three calendar years proceeding the budget year, with the objective being to hold the spending rate to no more than 5% average over time. Applicable endowments include pooled quasi-endowment and true endowment funds, as well as separately invested funds and funds held in trust by others, the income of which accrues to the University. Excluded are funds where the income accrues to others (life income funds) and funds where the income must be added to principal.

**(f) Grants and Contracts**

Government grants and contracts normally provide for the recovery of direct and indirect costs, subject to audit. The University recognizes revenue associated with direct and indirect costs as direct costs are incurred. The recovery of indirect costs is pursuant to an agreement, which provides for a predetermined fixed indirect cost rate.

**(g) Tax Exempt Status**

The University is a not-for-profit organization as described in Section 501 c(3) of the Internal Revenue Code (the Code) and is exempt from income taxes on related income pursuant to the appropriate sections of the Code.

**(h) Contributions**

Contributions, including unconditional promises to give, are recognized as revenues or gains in the period received. Contributions received are measured at their fair values and are reported as restricted or unrestricted support based upon the existence or absence of donor-imposed restrictions. Contributions made towards long-lived assets are reported as temporarily restricted until expended. Contributions that are expected to be released from restrictions within the year are classified as increases in unrestricted net assets.

Contributions received in the form of bequest intentions are generally conditional and therefore not recorded in the University's financial statements. Such gifts are identified as conditional pledges until the passage of time or events take place.

# BROWN UNIVERSITY

## Notes to Financial Statements

June 30, 2006

(with comparative information as of and for the Year Ended June 30, 2005)

(Thousands of dollars)

The University has recorded unconditional contributions receivable of \$226,103 and \$173,266 as of June 30, 2006 and 2005, respectively. These amounts are presented net of an allowance for uncollectible contributions and a discount to reduce the receivables to present value. Contributions receivable of less than fifty thousand dollars are not recorded in the statement of financial position, as they are not material to the overall financial statements of the University. Conditional contributions, due to uncertainties with regard to their realizability and valuation, are not estimated by management and are recognized as assets if and when the specific conditions are met.

The following summary represents the unconditional contributions receivable recorded as of June 30:

	<u>2006</u>	<u>2005</u>
Contributions expected to be received:		
In one year or less	\$ 109,489	\$ 78,667
Between one and five years	130,881	102,053
In more than five years	<u>17,471</u>	<u>18,279</u>
Gross contributions receivable	257,841	198,999
Discount	(10,135)	(7,692)
Allowance	<u>(21,603)</u>	<u>(18,041)</u>
Contributions receivable, net	<u>\$ 226,103</u>	<u>\$ 173,266</u>

(i) ***Funds Held in Trust by Others***

Funds held in trust by others represent funds that are held and administered by outside trustees. The administration of endowment funds held in trust in perpetuity of \$12,940 and \$12,207 at June 30, 2006 and 2005, respectively, is at the direction of the donor; the income from these funds inures to the benefit of the University. The plant funds held in trust of \$30,485 and \$5,101 at June 30, 2006 and 2005, respectively, are bond proceeds which will be utilized for construction projects in accordance with provisions contained within the respective bond indentures.

(j) ***Land, Buildings and Equipment***

Land, buildings and equipment are stated at cost of acquisition or construction (including construction financing) or, if received as a gift, at the appraised value at the time of receipt, net of accumulated depreciation. All other expenditures for maintenance, repairs, and library books are charged to operating net assets as incurred.

(k) ***Depreciation***

Depreciation is calculated using the straight-line method with estimated useful lives of 30 years for buildings, 20 years for building improvements made since 1987, and 10 years for building

# BROWN UNIVERSITY

## Notes to Financial Statements

June 30, 2006

(with comparative information as of and for the Year Ended June 30, 2005)

(Thousands of dollars)

equipment. Moveable equipment is depreciated over a range of 3 to 15 years, depending upon asset class.

Land, buildings and equipment include the following at June 30:

	<u>2006</u>	<u>2005</u>
Land	\$ 26,564	\$ 23,600
Buildings and improvements	725,640	683,472
Equipment	71,125	58,996
Construction in progress	<u>152,433</u>	<u>87,673</u>
	975,762	853,741
Accumulated depreciation	<u>(392,949)</u>	<u>(361,357)</u>
Land, buildings and equipment, net	<u>\$ 582,813</u>	<u>\$ 492,384</u>

**(l) Collections**

The University's collections include works of art, historical treasures, and artifacts that are maintained in the University's libraries and museums. These collections are protected and preserved for education and research purposes. The collections are not recognized as assets in the financial statements of the University.

**(m) Use of Estimates**

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during this period. Actual results could differ from those estimates.

**(n) Change in Accounting Principle**

In March 2005, the Financial Accounting Standards Board issued Interpretation No. 47 (FIN 47), *Accounting for Conditional Asset Retirement Obligations*. Under FIN 47, costs related to the legal obligations to perform certain activities in connection with the retirement, disposal or abandonment of assets is required to be accrued. The University identified asbestos abatement as a conditional asset retirement obligation and calculated the liability using a per square foot estimate based on historical experience. Accordingly, the University adopted FIN 47 effective July 1, 2005, recorded a liability of \$11,910, and recorded as a reduction of unrestricted net assets a cumulative effect of change in accounting principle.

# BROWN UNIVERSITY

## Notes to Financial Statements

June 30, 2006

(with comparative information as of and for the Year Ended June 30, 2005)

(Thousands of dollars)

### (o) *Prior Year Financial Statements*

While comparative information is not required under GAAP, the University believes that this information is useful and has included comparative financial information from the financial statements for 2005. This summarized information is not intended to be a full presentation in conformity with GAAP, which would require certain additional information. Accordingly, such information should be read in conjunction with the University's audited financial statements for the year ended June 30, 2005. In addition, certain 2005 comparative financial information has been reclassified to conform to the 2006 presentation.

### (2) **Investments**

The fair value of investments held as of June 30 are as follows:

	<u>2006</u>	<u>2005</u>
Cash and short-term investments	\$ 82,240	\$ 93,527
Limited liability corporations and partnerships	1,186,950	994,953
Common and preferred stock	233,091	236,084
Bonds	2,919	3,410
Government issues	7,082	77,844
Mutual funds	531,033	511,732
Private equities	166,668	90,227
Real assets	182,236	124,893
Other	465	537
Total investments, at fair value	<u>\$ 2,392,684</u>	<u>\$ 2,133,207</u>

Limited liability corporations and partnerships in which the University invests are commingled limited partnership and trust entities primarily investing in publicly traded securities.

The University is obligated, under certain limited partnership agreements, to make additional capital contributions up to contractual levels. The timing and amounts of the contributions will be determined by the general partners. As of June 30, 2006, the University has unfunded commitments of \$519,400.

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Notes to Financial Statements

June 30, 2006

(with comparative information as of and for the Year Ended June 30, 2005)

(Thousands of dollars)

***Long-Term Pooled Investments***

Certain endowment and other investments are pooled on a fair value basis with each participating fund owning shares in the pool. Additions or withdrawals are based on the fair value of the pooled investments. The nominal fair value per share was \$16.1538 and \$14.7132 at June 30, 2006 and 2005, respectively. The investment activity for the pooled investments is summarized as follows for the years ended June 30:

	<u>2006</u>	<u>2005</u>
Investment income, net of fees	\$ 19,183	\$ 12,122
Net realized gains	130,150	120,356
Net unrealized appreciation	124,939	82,430
Total	<u>\$ 274,272</u>	<u>\$ 214,908</u>

The change in the fair value of the long-term pooled funds is shown below:

Fair value at June 30, 2005	\$ 1,928,618
Amount distributed for operations	(85,826)
Investment income, net of fees	19,183
Net gains and unrealized appreciation on investments	255,089
Expired split interest agreement	99,634
New gifts	45,562
Operating funds invested in long-term pool	25,000
Net transfers	3,982
Fair value at June 30, 2006	<u>\$ 2,291,242</u>

**BROWN UNIVERSITY**

## Notes to Financial Statements

June 30, 2006

(with comparative information as of and for the Year Ended June 30, 2005)

(Thousands of dollars)

**(3) Bonds, Loans and Notes Payable**

The University has entered into various agreements for the purpose of financing the acquisition, renovation, and improvement of its facilities. The bonds, loans and notes payable outstanding for this purpose as of June 30 are as follows:

	<u>2006</u>	<u>2005</u>
Taxable Standard Commercial Paper Notes, Series A, with rates of 5.06% to 5.07%, maturing July 3 to July 7, 2006	\$ 16,000	\$ —
Rhode Island Health and Educational Building Corporation (RIHEBC) Higher Education Facilities Bonds:		
Series 1975 Facility Building Bonds, 8.00% final maturity 2005 (effective rate of 3.00% resulting from a HUD subsidy)	—	160
Series 1995 Facilities Revenue Bonds at a rate of 5.20% with maturities through 2005. All other outstanding 1995 Bonds were advance refunded by Series 2004 Revenue Refunding Bonds with final redemption in 2005	—	545
Series 1998 Facilities Revenue Bonds, at rates ranging from 4.75% to 5.00%, with various maturity dates through 2028	46,485	47,575
Series 2001A Facilities Revenue Refunding Bonds, at rates ranging from 3.375% to 5.25%, with various maturity dates through 2023	29,755	30,250
Series 2001B Facilities Revenue Bonds, at a variable rate (3.90% at June 30, 2006), with mandatory sinking fund redemption payments annually through 2032 final maturity	55,340	55,340
Series 2003A Facilities Revenue Bonds, at rates ranging from 2.00% to 4.85%, with various maturity dates through 2037	46,200	46,200
Series 2003B Facilities Revenue Bonds, at a variable rate (3.97% at June 30, 2006), with mandatory sinking fund redemption payments annually through 2043 final maturity	45,225	45,225
Series 2004 Facilities Revenue Refunding Bonds, at rates ranging from 2.00% to 4.75%, with various maturity dates through 2025	22,605	22,835

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Notes to Financial Statements

June 30, 2006

(with comparative information as of and for the Year Ended June 30, 2005)

(Thousands of dollars)

	<b>2006</b>	<b>2005</b>
Series A 2005 Facilities Revenue Bonds, at a variable rate (3.97% at June 30, 2006), maturing on May 31, 2035	\$ 85,500	\$ —
Brown University Taxable Bonds Series 2005, at a fixed rate of 5.09%, maturing on November 1, 2015	17,000	—
Loan payable – U.S. Department of Education loan, 5.50%, due in semiannual payments through 2021	1,443	1,506
Total bonds, loans and notes payable	\$ 365,553	\$ 249,636

***Tax Exempt Bonds:***

The RIHEBC series bonds represent obligations under various agreements pursuant to which the University is required to make payments to this state agency sufficient to liquidate the debt. The University is required under certain of its financing agreements to appropriate funds from operating and other net assets for payment of principal and interest and for maintenance of the properties.

In October 2005, the Series A Facilities Revenue Bonds were issued to finance work on a variety of new and ongoing capital projects for research, academic and administrative buildings, and infrastructure throughout the University. The bonds currently bear interest at a variable rate determined weekly and paid to bondholders on a monthly basis.

In conjunction with the issuance of the 2005 Series A Bonds, the University entered into an interest rate swap agreement to convert the variable rate on these bonds to a fixed rate without exchanging the underlying principal amount. Under the terms of the agreement, the counterparty pays the University a variable interest rate indexed to the USD-BMA Municipal Swap Index. The University pays the counterparty a fixed rate of 3.979% on a notional amount of \$85,500. The agreement terminates on May 1, 2035, which is the maturity date of the bonds.

In April 2004, the University issued Facilities Revenue Refunding Bonds to advance refund \$20,535 of the University's 1995 Series Bonds. Proceeds from the refunding bonds were deposited into a refunding trust account to be used to pay interest on the refunded 1995 Bonds through September 1, 2005, and to redeem the bonds on that date at a redemption price of 102%. The transaction resulted in a loss on advance refunding of debt of \$2,041. The trust assets and corresponding amounts payable through the trust are reported on the statement of financial position as of June 30, 2005.

In October 2003, the Series A and B Facilities Revenue Bonds were issued to finance capital projects in a variety of research, academic and administrative buildings, and infrastructure upgrades throughout the University. The Series A Bonds are comprised of both serial and term fixed-rate bonds. The Series B Bonds currently bear interest at a variable rate determined weekly and paid to bondholders on a monthly basis.

# BROWN UNIVERSITY

## Notes to Financial Statements

June 30, 2006

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(Thousands of dollars)

In conjunction with the issuance of the Series B Bonds, the University entered into an interest rate swap agreement to convert the variable rate on these bonds to a fixed rate without exchanging the underlying principal amount. Under the terms of the agreement, the counterparty pays the University a variable interest rate indexed to LIBOR. The University pays the counterparty a fixed rate of 3.732% on a notional amount of \$45,225. The fair value of the swap at June 30, 2006 was a net receivable of \$187, which is included in accounts receivable and other assets, and the fair value of the swap at June 30, 2005 was a net payable of \$5,088, which is included in accounts payable and accrued liabilities. The change in fair value of the swap has been included in nonoperating activities as an unrestricted other net asset change. The agreement terminates on September 1, 2043, which is the final maturity date of the bonds.

### ***Taxable Bonds and Other Debt:***

In November 2005, the Brown University Taxable Bonds, Series 2005 were issued to finance a portion of the acquisition cost of an office building. In addition, the University implemented a Taxable Commercial Paper Program in November 2005. The program enables the University to issue up to \$50,000 in Notes with \$16,000 currently authorized by the University Corporation. The program provides for the issuance of Taxable Standard Commercial Paper Notes, Series A, and Taxable Extendible Commercial Paper Notes, Series B. As of June 30, 2006, all of the outstanding commercial paper is Taxable Standard Commercial Paper Notes, Series A.

Interest paid in 2006 was \$13,302. Principal payments of bonds and loan payable for the succeeding five fiscal years ending June 30 are as follows:

2007	\$	2,529
2008		3,758
2009		3,891
2010		4,035
2011		4,185

The University's bonds, loans and notes payable are stated at cost. The fair value has been calculated by determining the net present values of future cash outlays using an interest rate of 4.3%. This rate is based upon market conditions as of June 30. The total estimated fair values at June 30, 2006 and 2005 are \$377,788 and \$239,858, respectively.

The University has a line of credit available of up to \$40,000. As of June 30, 2006, the full amount of \$40,000 was available.

## BROWN UNIVERSITY

### Notes to Financial Statements

June 30, 2006

(with comparative information as of and for the Year Ended June 30, 2005)

(Thousands of dollars)

#### (4) Pensions

The University participates in several different contributory retirement plans. The plans provide for the purchase of annuities on a compulsory basis by full-time faculty and administrative staff. The expense to the University, representing its contributions to the accounts of faculty and staff, was \$17,953 and \$17,313 for the years ended June 30, 2006 and 2005, respectively. The University has no liability for unfunded pension costs under these plans.

The Brown University Food Services and Plant Operations Employees' Pension Plan is a noncontributory defined benefit plan which provides pensions for certain full-time weekly paid employees. The policy of the University is to fund pension costs in accordance with the Employee Retirement Income Security Act of 1974. Information regarding the defined benefit pension plan as of June 30 is as follows:

	<b>2006</b>	<b>2005</b>
Change in projected benefit obligation:		
Projected benefit obligation at beginning of year	\$ 37,064	31,260
Service cost	1,792	1,443
Interest cost	1,901	1,827
Benefits paid	(1,147)	(1,129)
Changes in actuarial assumptions	(6,421)	3,663
Projected benefit obligation at end of year	\$ 33,189	37,064

The projected benefit obligation was determined using the following assumptions for the years ended:

	<b>2006</b>	<b>2005</b>
Discount rate	6.41%	5.25%
Rate of compensation increase	4.50	4.50
Change in plan assets:		
Fair value of plan assets at beginning of year	\$ 26,397	\$ 24,351
Actual return on plan assets	2,266	2,175
Contributions	1,070	1,000
Benefits paid	(1,147)	(1,129)
Fair value of plan assets at end of year	\$ 28,586	\$ 26,397
Funded status	\$ (4,603)	(10,667)
Unrecognized prior service cost	879	1,106
Unrecognized net loss	672	7,653
Accrued pension cost	\$ (3,052)	\$ (1,908)

# BROWN UNIVERSITY

## Notes to Financial Statements

June 30, 2006

(with comparative information as of and for the Year Ended June 30, 2005)

(Thousands of dollars)

	<u>2006</u>	<u>2005</u>
Net periodic pension cost:		
Service cost	\$ 1,792	\$ 1,443
Interest cost	1,901	1,827
Expected return on assets	(1,988)	(1,829)
Amortization of unrecognized loss	281	79
Amortization of unrecognized prior service cost	227	229
Net periodic pension cost	<u>\$ 2,213</u>	<u>\$ 1,749</u>

The net periodic pension cost was determined using the following assumptions for the years ended:

	<u>2006</u>	<u>2005</u>
Discount rate	5.25%	6.00%
Rate of compensation increase	4.50	4.50
Expected long term rate of return	7.50	7.50

The expected rate of return on assets was derived based upon assumptions of inflation, real returns, anticipated value added by the investment manager and expected asset class allocations.

For the year ended June 30, 2006, the accumulated benefit obligation was \$26,746. For the year ended June 30, 2005, the accumulated benefit obligation of \$29,165 exceeded the fair value of the plan assets by \$2,768. As required by FAS No. 87, the University recorded, as of June 30, 2005, an intangible asset to the extent of the unrecognized prior service cost of \$1,106. The resulting asset and accrued liability are reflected in the statement of financial position.

The investment strategy for the Plan takes into account several factors consistent with the characteristics of an employee pension plan. As such, the strategy recognizes a long-term time horizon where a substantial allocation to equities is appropriate and will help to maximize returns; broad diversification in order to increase return and reduce risk; and investment in institutional retirement annuities that serve to reduce administrative costs.

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Notes to Financial Statements

June 30, 2006

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(Thousands of dollars)

The actual asset allocation target for the pension plan as of June 30, 2006 and 2005, and the weighted average asset target allocation for 2006 by asset category are as follows:

	<b>Target 2006</b>	<b>Actual</b>	
		<b>2006</b>	<b>2005</b>
Equity securities	55%	57%	55%
Fixed income securities	33	31	34
Real estate	10	11	10
Cash and cash equivalents	2	1	1
Total	<u>100%</u>	<u>100%</u>	<u>100%</u>

Information about the expected cash flows for the Plan follows:

Estimated employer contributions:

2007 \$ 1,200

Estimated future benefit payments are as follows:

2007 \$ 1,484  
 2008 1,515  
 2009 1,554  
 2010 1,622  
 2011 1,705  
 2012 and beyond 10,212

**(5) Net Assets**

The University's net assets as of June 30 are as follows:

	<b>2006</b>			<b>2005 Total</b>
	<b>Unrestricted</b>	<b>Temporarily restricted</b>	<b>Permanently restricted</b>	
Operating:				
Undesignated, departmental funds	\$ 52,867			\$ 52,867
University designated	68,096			68,096
Donor restricted		\$ 48,872		48,872
Facilities and equipment	262,409	57,239		319,648
Student loans	8,364		\$ 7,684	16,048
Endowment and life income	1,028,154	84,804	1,212,069	2,325,027
Total net assets	<u>\$ 1,419,890</u>	<u>\$ 190,915</u>	<u>\$ 1,219,753</u>	<u>\$ 2,830,558</u>

**BROWN UNIVERSITY**

Notes to Financial Statements

June 30, 2006

(with comparative information as of and for the Year Ended June 30, 2005)

(Thousands of dollars)

**(6) Commitments and Contingencies**

Outstanding commitments on uncompleted construction contracts total \$42,317 at June 30, 2006.

All funds expended in conjunction with government grants and contracts are subject to audit by governmental agencies. In the opinion of management, any liability resulting from these audits will not have a material effect on the University's financial position.

The University is a defendant in various legal actions arising out of the normal course of its operations. Although the final outcome of such actions cannot currently be determined, the University believes that eventual liability, if any, will not have a material effect on the University's financial position.

The University and the City of Providence (the City) have entered into an agreement whereby the University will make certain payments to the City. Such payments are voluntary and may be discontinued at any time with prior notice as described in the agreement. The amount expected to be paid in fiscal year 2007 is approximately \$1,440.