Tufts University

Consolidated Financial Statements for the Year Ended June 30, 2005, with Comparative Totals for the Year Ended June 30, 2004, and Independent Auditors' Report

TUFTS UNIVERSITY

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INDEPENDENT AUDITORS' REPORT

To the Board of Trustees of
Tufts University:

We have audited the accompanying consolidated statement of financial position of Tufts University (the "University") as of June 30, 2005 and the related consolidated statements of activities and changes in net assets and cash flows 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 financial statements; and in our report dated September 9, 2004, 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 also 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, such consolidated financial statements present fairly, in all material respects, the financial position of the University at June 30, 2005, and the changes in its net assets and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

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 consolidated financial statements for the year ended June 30, 2004, from which the summarized information was derived.

Deloitte & Touche LLP

September 16, 2005

TUFTS UNIVERSITY

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
AS OF JUNE 30, 2005 WITH COMPARATIVE TOTALS AT JUNE 30, 2004
(In thousands)

	2005	2004
ASSETS		
Cash and cash equivalents	$ 48,230	$ 37,117
Receivables—net and other assets	27,239	23,652
Contributions receivable—net	57,074	39,501
Note and student loans receivables—net	36,529	37,259
Funds held under bond agreements	6,515	3,588
Investments	1,132,129	1,023,276
Land, buildings, and equipment—net	491,474	435,566
TOTAL ASSETS	$1,799,190	$1,599,959
LIABILITIES AND NET ASSETS		
LIABILITIES:		
Accounts payable and accrued expenses	$ 95,899	$ 90,919
Deferred revenue and deposits	42,220	41,288
Government advances for student loans	24,478	24,197
Bonds and notes payable	276,615	228,602
Interest rate agreements	31,683	2,880
Total liabilities	470,895	387,886
NET ASSETS:		
Unrestricted	719,798	673,243
Temporarily restricted	300,786	262,108
Permanently restricted	307,711	276,722
Total net assets	1,328,295	1,212,073
TOTAL LIABILITIES AND NET ASSETS	$1,799,190	$1,599,959

See notes to consolidated financial statements.

TUFTS UNIVERSITY

CONSOLIDATED STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS FOR THE YEAR ENDED JUNE 30, 2005 WITH COMPARATIVE TOTALS FOR 2004 (In thousands)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total 2005	Total 2004
OPERATIONS:					
REVENUE:					
Tuition and fees	$269,352	$ -	$ -	$ 269,352	$ 255,576
Less scholarships and fellowships	(63,402)			(63,402)	(59,509)
Tuition and fees—net	205,950			205,950	196,067
Government grants and contracts	117,697			117,697	110,018
Clinical and other educational activities	70,857			70,857	63,477
Auxiliary enterprises	40,445			40,445	38,778
Contributions and grants	45,655	15,005		60,660	42,609
Investment return utilized	50,386			50,386	44,423
Net assets released from restrictions due to investment return utilized	3,583	(3,583)			
Total revenue	534,573	11,422	-	545,995	495,372
EXPENSES:					
Instruction	151,341			151,341	142,209
Sponsored programs	111,757			111,757	105,719
Clinical and other educational activities	78,523			78,523	75,311
Academic and student services	70,569			70,569	65,583
Auxiliary enterprises	39,008			39,008	37,025
Institutional support	52,797			52,797	51,690
Total expenses	503,995	-	-	503,995	477,537
INCREASE IN NET ASSETS FROM OPERATING ACTIVITIES	30,578	11,422		42,000	17,835
NONOPERATING ACTIVITIES:					
Investment return reinvested	24,410	25,295	1,582	51,287	74,236
Contributions and grants	6,294	7,037	29,407	42,738	15,912
Net assets released from restrictions for capital and other nonoperating purposes	5,076	(5,076)			
Change in fair value of interest rate agreements	(19,803)			(19,803)	(2,880)
Other nonoperating activities					(2,731)
Increase in net assets from nonoperating activities	15,977	27,256	30,989	74,222	84,537
INCREASE IN NET ASSETS	46,555	38,678	30,989	116,222	102,372
NET ASSETS—Beginning of year	673,243	262,108	276,722	1,212,073	1,109,701
NET ASSETS—Ending of year	$719,798	$300,786	$307,711	$1,328,295	$1,212,073

See notes to consolidated financial statements.

TUFTS UNIVERSITY

CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2005 WITH COMPARATIVE TOTALS FOR 2004
(In thousands)

	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES:		
Total increase in net assets	$ 116,222	$ 102,372
Adjustments to reconcile total increase in net assets to net cash provided by operating activities:		
Net realized investment gains	(35,086)	(30,145)
Net unrealized investment gains	(35,899)	(60,404)
Depreciation and amortization of bond premium	30,357	27,550
Loss on disposal of fixed assets	582	1,231
Gifts of property and equipment	(93)	(77)
Decline in value of interest rate agreements	19,803	2,880
Contributions and investment income restricted for long-term investment	(41,571)	(17,842)
Changes in operating assets and liabilities:		
Receivables and other assets—net	(3,587)	(638)
Contributions receivable—net	(17,573)	(1,488)
Note receivable	317	299
Accounts payable and accrued expenses	4,981	3,673
Deferred revenue and deposits	932	1,872
Net cash provided by operating activities	39,385	29,283
CASH FLOWS FROM INVESTING ACTIVITIES:		
Student loans granted	(6,682)	(5,082)
Student loans repaid—net of reserve	7,094	7,160
Purchases of investments	(819,368)	(575,377)
Proceeds from sale of investments	781,500	549,817
Changes in funds held under bond agreements	(2,927)	48
Additions to land, buildings and equipment	(86,854)	(46,733)
Net cash used in investing activities	(127,237)	(70,167)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Increase in government advances for student loans	280	195
Proceeds from issuance of bonds and notes	54,000	273
Repayments of bonds and notes	(5,886)	(7,993)
Proceeds from swaption agreements	9,000	
Proceeds from contributions and investment income restricted for long-term investment	41,571	17,842
Net cash provided by financing activities	98,965	10,317
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	11,113	(30,567)
CASH AND CASH EQUIVALENTS—Beginning of year	37,117	67,684
CASH AND CASH EQUIVALENTS—End of year	$ 48,230	$ 37,117
SUPPLEMENTAL DATA—Cash paid for interest	$ 12,862	$ 10,587

See notes to consolidated financial statements.

1. ORGANIZATION

Tufts University (the "University"), founded in 1852, is a not-for-profit institution committed to education and research. The University is a complex independent nonsectarian university, with approximately 9,100 students and three campuses in Boston, Medford/Somerville and Grafton, Massachusetts. The University provides degree programs at both undergraduate and graduate levels in a variety of liberal arts and professional areas. The University has been granted a tax-exemption as described in Section 501(c)(3) of the Internal Revenue Code (the "Code") and is generally exempt from income taxes pursuant to Section 501(a) of the Code.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation—The accompanying consolidated financial statements have been prepared on the accrual basis with net assets and revenues, expenses, gains and losses classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the University are classified and reported as follows:

Permanently restricted—Net assets subject to donor-imposed stipulations that they be maintained in perpetuity by the University. Such net assets consist primarily of donor-restricted endowment funds.

Temporarily restricted—Net assets subject to donor-imposed stipulations that may be satisfied by actions of the University that expire with the passage of time or the occurrence of specific events.

Unrestricted—Net assets not subject to donor-imposed stipulations. Unrestricted net assets may be designated for specific purposes by the Board of Trustees.

Consolidation—The consolidated financial statements include the accounts of the University and its wholly owned subsidiaries. Intercompany accounts and transactions have been eliminated.

Classifications—Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulations or by law. Contributions and investment return for operating activities subject to donor-imposed stipulations that are met in the same period are reported as unrestricted revenue. Investment return subject to donor-imposed stipulations not utilized in the current period are released from temporarily restricted net assets when spent and shown as investment return utilized. Expirations of all other temporarily restricted net assets are reported as reclassifications between the applicable classes of net assets.

Contributions—Contributions, including unconditional promises to give, are recognized as revenue in the period received. Contributions restricted for the acquisition of land, buildings and equipment are reported as increases in temporarily restricted net assets. These contributions are reclassified to unrestricted net assets as the funds are expended. Promises to give subject to donor-imposed stipulations that the corpus be maintained in perpetuity are recognized as increases in permanently restricted net assets.

Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Contributions of assets other than cash are reported at their estimated fair value at the date of gift. Contributions scheduled to be received after one year are discounted at a rate commensurate with the risk involved. Amortization of the discount is recorded as additional contributions in the appropriate net asset class.

Investments—Investments are reported at fair value. Dividends, interest, and net gains on investments are reported as follows:

- as increases in permanently restricted net assets if the terms of the gift require that they be added to the principal of a permanent endowment or loan fund;

- as increases in temporarily restricted net assets if the terms of the gift or relevant state law impose restrictions on the current use of the income or net gains. The University has relied on the Massachusetts Attorney General's interpretation of relevant state law that unappropriated endowment gains should generally be classified as temporarily restricted; and

- as increases in unrestricted net assets in all other cases.

Investments are comprised of the assets of the University's endowment and nonendowment funds. The majority of these assets are invested in the University's Total Return Pool. The Total Return Pool assets are owned by participating funds based on shares acquired by each fund when it entered the pool. The fair value of the pooled assets is determined each month and the resulting value per share is used to account for funds entering or leaving the pool. The University has established spending policies for endowment and nonendowment investments in the Total Return Pool as follows:

Endowment Spending Policy—The objective of the policy is to ensure that endowment income available to support operations is stable and predictable, while at the same time increases over time to offset the effects of inflation. The endowment spending rate for the Total Return Pool is adjusted annually, based on a percentage increase over the previous year's spending rate. The policy provides that management will adjust the spending rate as necessary if it does not remain within a specified range of the pool's market value calculated as of December 31 of the previous year.

Nonendowment Spending Policy—The nonendowment investments in the Total Return Pool consists of operating and capital funds. These long-term funds, while invested in a similar manner as the endowment, are not intended to be held in perpetuity. As of April 1, 2005, the University adopted a fixed annual spending rate equivalent to 6% of the market value calculated as of December 31 of the previous year.

The spending rate increases and market value ranges for the Total Return Pool as outlined in the University's Spending Policy are summarized as follows:

	Endowment Funds		Nonendowment Funds	
	Spending rate increase over prior year	Spending as a percentage of market value	Spending rate increase over prior year	Spending percentage of market value
July 1, 2003–June 30, 2004	5.0 %	3.5–4.5%	5.0 %	3.5–4.5%
July 1, 2004–March 31, 2005	4.0	4.5–5.5	4.0	4.5–5.5
April 1, 2005–June 30, 2005	4.0	4.5–5.5	-	6.0

Certain nonendowment hedge fund investments are held outside of the Total Return Pool. The University has established spending rates between 6% and 7.5% for these investments. Spending on all other investments held outside the Total Return Pool represents the yield earned, unless otherwise prescribed by donor restrictions.

Operations and Nonoperating Activities—The statement of activities and changes in net assets reports changes in unrestricted, temporarily restricted, and permanently restricted net assets from operations and nonoperating activities. Operations does not include the release from restrictions of contributions restricted to the acquisition of land, buildings, and equipment; investment return in excess of the University's operating needs as defined by its spending policy; unrealized gain or loss on interest rate agreements; or unrestricted bequests and gifts of property.

Tuition revenue is reported in the period earned net of the discount attributable to reductions in amounts charged to students, whether as unrestricted University financial aid, distributions from endowment funds, or government aid awarded to students by the University. Revenue associated with research and other grants and contracts is recognized when related expenses are incurred. Indirect cost recovery by the University is recorded as unrestricted revenue of $29,451,000 in 2005 and $27,661,000 in 2004. Revenue from all other sources is recognized in the period earned.

Interest, depreciation, operations, and maintenance expenses have been allocated to functional expense classifications based on square footage utilized.

Cash and Cash Equivalents—For purposes of the statements of cash flows, short-term investments with maturities at the dates of purchase of three months or less are classified as cash and cash equivalents.

Financial Instruments—The University has estimated, where practicable, the fair values of its financial instruments by using appropriate valuation methodologies. Except where otherwise noted, the University determined that the differences between the carrying values and the estimated fair values of its other financial assets and liabilities are not material.

Land, Buildings, and Equipment—Land, buildings, and equipment are stated at cost at date of purchase or fair value at date of donation in the case of gifts. Depreciation is provided using the straight-line method over the assets' estimated useful lives, which range from 20 years for land improvements, 5 to 50 years for buildings and 3 to 25 years for equipment and furnishings.

Perpetual Trusts, Life Income, and Annuity Agreements—The University has an interest in various perpetual trusts, irrevocable charitable remainder trusts, and life income and annuity agreements. Assets held in these trusts and agreements, which are administered by the University or third-party trustees, are included in investments, and totaled approximately $75,100,000 and $60,300,000 for 2005 and 2004, respectively. Contributions are recognized at the date the trusts or annuity agreements are established. Liabilities associated with life income and annuity agreements are recorded at the present value of the estimated future payments to be made to the donors and/or other beneficiaries by the University. The liabilities associated with life income and annuity agreements are adjusted during the term of the life income agreement or annuity for changes in the value of the assets, accretion of the discount and other changes in the estimates of future payments. The liabilities are included in accounts payable and accrued expenses and totaled approximately $11,500,000 and $9,700,000 for 2005 and 2004, respectively.

Use of Estimates—The preparation of 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 date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Prior Year Summarized Information—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 generally accepted accounting principles. Accordingly, such information should be read in conjunction with the University's consolidated financial statements for the year ended June 30, 2004, from which the summarized information was derived.

2004 Presentation—Certain 2004 amounts have been reclassified to conform with the 2005 presentation.

3. RECEIVABLES AND OTHER ASSETS

Receivables represent amounts due from students, grants, and contracts, clinic billings and other sources. Other assets include deferred charges, prepaid expenses, and inventories. The components at June 30, are as follows (in thousands):

	2005	2004
Gross receivables	$ 21,657	$ 19,107
Less allowance for uncollectible amounts	(2,506)	(2,452)
Receivables—net	19,151	16,655
Other assets	8,088	6,997
Total	$ 27,239	$ 23,652

4. CONTRIBUTIONS RECEIVABLE

Contributions receivable consisted of the following at June 30, (in thousands):

	2005	2004
Unconditional promises scheduled to be collected in:		
Less than one year	$ 31,985	$ 23,858
One year to five years	29,105	18,500
More than five years	4,587	3,993
Less allowance for uncollectible amounts	(5,724)	(4,471)
Less discount to present value	(2,879)	(2,379)
Total	$ 57,074	$ 39,501

Contributions receivable were intended for the following purposes at June 30, (in thousands):

	2005	2004
Endowment for educational and general purposes	$ 23,002	$ 16,788
Construction and modernization of plant	16,880	15,194
Support of current operations	17,192	7,519
Total	$ 57,074	$ 39,501

5. NOTE AND STUDENT LOANS RECEIVABLES

Note and student loans receivables consisted of the following components at June 30, (in thousands):

	2005	2004
Student loans receivable	$ 37,399	$ 37,853
Less allowance for uncollectible amounts	(1,948)	(1,989)
Student receivables—net	35,451	35,864
T-NEMC note receivable (Note 12)	1,078	1,395
Total	$ 36,529	$ 37,259

Generally, payment commences on student loans receivable upon graduation and can extend up to 20 years. Interest rates range from 2% to 18%.

6. INVESTMENTS

Investments consisted of the following at June 30, (in thousands):

	2005	2004
Cash and cash equivalents	$ 38,103	$ 35,443
Equity securities	408,091	342,271
Fixed income securities	182,762	217,285
Hedge funds and alternative investments	470,844	411,634
Private equities	24,204	16,622
Real estate	12,144	
Receivable for unsettled trades	494	21
Payable for unsettled trades	(4,513)	
Total	$1,132,129	$1,023,276

Fair values for equity securities and fixed income securities are generally based on published market values. At June 30, 2005 and 2004, approximately $34,300,000 and $21,200,000 of equity securities are not readily marketable and are valued at management's estimate of fair value, and $2,400,000 and $3,600,000 are stated at cost. The University invests in hedge funds, alternative investments, and private equity investments through various limited partnerships and similar vehicles. Hedge funds and alternative investments utilize a variety of investment strategies incorporating marketable securities and, in some cases, derivative instruments, all of which are reported at estimated fair value by the fund managers. Private equity investments consist of long-term private investment securities and have been valued based on estimates reported by fund managers. Estimates of fair value may differ significantly from values that would have been used had a ready market for the investments existed. Real estate consists of investments in privately held and publicly traded REITs and other privately held entities. The University is obligated under certain limited partnership agreements and other alternative investment arrangements to advance additional funding periodically up to specified levels. At June 30, 2005, the University had unfunded commitments of approximately $62,233,000, which can be called through 2011.

The total return on investments is as follows for the years ended at June 30, (in thousands):

	2005			2004		
	Endowment	Non-Endowment	Total	Endowment	Non-Endowment	Total
Dividends and interest	$ 15,476	$ 15,212	$ 30,688	$ 14,393	$ 13,717	$ 28,110
Net realized and unrealized gains (losses)	68,747	2,238	70,985	91,551	(1,002)	90,549
Total return on investments	84,223	17,450	101,673	105,944	12,715	118,659
Investment return utilized	(35,813)	(14,573)	(50,386)	(31,603)	(12,820)	(44,423)
Investment return reinvested	$ 48,410	$ 2,877	$ 51,287	$ 74,341	$ (105)	$ 74,236

Endowment and nonendowment funds are described in Note 9.

7. LAND, BUILDINGS, AND EQUIPMENT

Land, buildings, and equipment consisted of the following at June 30, (in thousands):

	2005	2004
Land and land improvements	$ 30,462	$ 28,237
Buildings	600,529	553,667
Construction in progress	56,242	29,861
Equipment and furnishings	139,751	130,105
	826,984	741,870
Less accumulated depreciation	(335,510)	(306,304)
Total	$ 491,474	$ 435,566

Depreciation expense charged to operations was $30,458,000 and $27,651,000 in 2005 and 2004, respectively. Net interest cost capitalized in fiscal 2005 and 2004 was $1,864,000 and $223,000, respectively.

Equipment and furnishings includes $667,000 in assets recorded under capital leases in 2005 and 2004 with depreciation expense amounting to $86,220 in each year. Accumulated depreciation on the assets amounted to $172,440 and $86,220 in 2005 and 2004, respectively.

8. BONDS AND NOTES PAYABLE

Bonds and notes payable consisted of the following at June 30, (in thousands):

	2005	2004
Massachusetts Industrial Finance Agency ("MIFA")—Series H, fixed rate bonds at 4.75%-5.50%, due through 2028	$ 90,900	$ 93,600
Massachusetts Health and Educational Facilities Authority ("MHEFA"):		
Series G, variable rate bonds, 2.23% average rate for 2005, due 2024-2026	33,100	35,400
Series I, fixed rate bonds at 5.25%-5.50%, due 2029-2036	50,000	50,000
Series J, fixed rate bonds at 3.00%-5.50%, due 2003-2018	32,855	33,070
Series K, variable rate bonds at 2.14% average rate for 2005, due 2022-2034	54,000	
United States Department of Education ("DOE"):		
Fixed rate bonds, 3.00%-3.625%, due through 2018	3,613	3,929
Fixed rate bonds, 3.00%, due through 2021	2,077	2,195
Secured note, 5.50%, due through 2020	1,360	1,415
Citizens Bank—Note—Rate fixed at 6.135% until 2005; rate at 7-year Eurodollar rate plus 1.00% from 2005 to maturity in 2006	7,500	7,500
Capital Leases—various imputed interest rates up to 4.63%, due through 2006	255	437
	275,660	227,546
Net unamortized bond premium	955	1,056
Total bonds and notes payable	$ 276,615	$ 228,602

The DOE fixed rate bonds are collateralized by certain dormitories and other buildings. The DOE secured note is collateralized with amounts included in funds held under bond agreements.

Scheduled aggregate principal repayments on bonds and notes payable are as follows (in thousands):

Fiscal Year	
2006	$ 4,331
2007	11,326
2008	3,828
2009	4,166
2010	4,386
Thereafter	247,623
Total	$ 275,660

A refunding trust was established in 1989 to retire Series A bonds. Trust funds will be applied to outstanding principal and interest through 2008. Because the refunded bonds are no longer deemed to be outstanding for financial reporting purposes, neither the debt nor the irrevocable trust assets are included in the consolidated statements of financial position.

The University's debt is stated at cost. The fair value has been calculated by determining the net present value of future cash outlays using an appropriate interest rate based on the length of time to maturity. The rates were based upon market conditions as of June 30, 2005 and 2004. The estimated fair value at June 30, 2005 and 2004, is $294,409,000 and $230,822,000, respectively.

In May 2004, the University entered into two interest rate swap agreements, in order to manage the risk associated with its Series K variable rate debt. Under the terms of the first agreement, the University pays a fixed rate of 4.069% on a principal amount of $54,000,000. The second agreement covers the anticipated issuance in January 2006 of $34,000,000 in variable rate bonds and calls for a fixed payment rate of 4.292%. The counterparty is obligated to pay the University 69% of LIBOR which will approximate the interest rate on the bonds. The reduction in the notional amounts of the agreements coincides with the maturity dates of the bonds through 2034 and 2036, respectively. At June 30, 2005 and 2004, the fair value of the swap agreements are reflected on the balance sheet as liabilities of $13,828,000 and $2,880,000, respectively.

In October 2004, the University entered into two interest rate swaption agreements associated with certain outstanding fixed rate debt. In return for the option to exercise the swaption agreements, the counterparty paid the University a premium of $9,000,000. The first swaption relates to the Series H bonds and is exercisable on the issue's initial call date of January 15, 2008. The underlying swap carries a fixed interest rate of 4.32% on a notional amount of $65,950,000 and has a maturity schedule terminating on February 15, 2028. The second agreement relates to the Series I bonds and is exercisable on the issue's initial call date of January 13, 2011. The underlying swap carries a fixed interest rate of 5.11% on a notional amount of $50,500,000 and has a maturity schedule terminating on February 15, 2036. If these options are exercised by the counterparty, the University will call the bonds covered under the agreements, issue new variable rate debt and enter into the swap agreements described above. At June 30, 2005 the fair value of the swaptions are reflected on the balance sheet as liabilities of $17,855,000.

Any gain or loss associated with the interest rate agreements, including the swaption agreements is reflected as a nonoperating item in the accompanying statement of activities and changes in net assets.

9. NET ASSETS

Net assets consisted of the following at June 30, (in thousands):

	Unrestricted	Temporarily Restricted	Permanently Restricted	2005 Total	2004 Total
Endowment	$ 340,169	$ 249,049	$ 291,320	$ 880,538	$ 778,915
Invested in physical plant	218,019			218,019	206,749
Operating	115,894	17,076		132,970	135,779
Building projects	28,565	34,661		63,226	58,464
Student loans	17,151		16,391	33,542	32,166
Total	$ 719,798	$ 300,786	$ 307,711	$ 1,328,295	$ 1,212,073

Endowment consists of resources that have been restricted by the donor, trust, split interest agreement, or designated by the Board of Trustees for investment to provide future resources to support the University's activities. Temporarily restricted endowment includes unapproriated gains of approximately $193 million and $181 million in 2005 and 2004, respectively. Unrestricted operating includes funds that have been internally designated for use by various schools, departments, and programs throughout the University.

10. NATURAL CLASSIFICATION OF EXPENSES

The University reports operating expenses in its consolidated statement of activities and changes in net assets by functional category. Operating expenses by natural category consisted of the following for the years ended June 30, (in thousands):

	2005	2004
Compensation:		
Staff, student, and other	$ 165,111	$ 158,874
Faculty	83,062	78,474
Benefits	53,132	51,881
Total compensation	301,305	289,229
Materials, supplies, and other	85,423	80,416
Purchased services	36,171	33,134
Depreciation and loss on disposals	31,039	28,882
Maintenance and facilities costs	29,181	25,781
Interest	10,919	10,180
Travel	9,957	9,915
Total expense	$ 503,995	$ 477,537

11. BENEFIT PLANS

Defined Contribution Plan—The University sponsors a defined contribution retirement plan under Section 401(a) of the Code, which is available to eligible faculty and administrative staff. All retirement benefits are funded by the University and are subject to a vesting schedule. The University's contributions to the plan amounted to approximately $17,225,000 and $16,482,000 in 2005 and 2004, respectively.

The University also offers a supplemental retirement plan under Section 403(b) of the Code, which is fully funded by voluntary employee contributions.

Deferred Compensation Plans—The University maintains two separate plans under Section 457(b) of the Code for eligible officers, faculty and administrative staff. The University funded the Officers' Plan with approximately $53,000 and $47,000 in 2005 and 2004, respectively. Under the terms of the Faculty and Administrative Staff Plan, no contributions are made by the University but are fully funded by voluntary employee contributions. The assets and related liabilities of these plans are recorded in the consolidated financial statements and total approximately $1,751,000 and $970,000 in 2005 and 2004, respectively. The University also maintains a plan under Section 457(b) of the Code for eligible faculty and administrative staff that was closed to future participants in 1989. The University funded this plan with approximately $19,000 and $13,000 in 2005 and 2004, respectively. The investment assets and related liabilities of these plans, which total approximately $9,785,000 and $9,921,000 in 2005 and 2004, respectively, are recorded in the consolidated financial statements.

Health and Welfare Benefit Plan—The University provides postretirement health care benefits to eligible retired employees and their eligible spouses. Retirees share in the cost of their health care benefits through co-payments and deductibles related to years of service and date of retirement. Employees who were hired after December 31, 1993, must pay for the entire cost of their benefit when they retire. The University has established a trust to fund the postretirement health care benefits for most of the eligible employees. The trust qualifies as a "voluntary employees beneficiary association" under the provisions of Section 501(c)(9) of the Code in order that the trust be exempt from certain taxes. The University funded the trust with $818,000 and $2,283,000 in 2005 and 2004, respectively.

Following is the change in the University's postretirement health care benefit obligation for the years ended June 30, (in thousands):

	2005	2004
Benefit obligation—beginning of year	$ 34,470	$ 42,398
Service cost	237	475
Interest cost	2,019	2,269
Benefits paid	(2,589)	(2,652)
Participants' contributions	743	572
Actuarial (gain) loss	4,266	(4,539)
Amendments		(4,053)
Benefit obligation—end of year	$ 39,146	$ 34,470

The funded status of the University's postretirement health care plan and the amounts recognized in the consolidated statements of financial position at June 30, were as follows (in thousands):

	2005	2004
Fair value of plan assets—beginning of year	$ 27,475	$ 22,493
Actual return on plan assets	4,046	4,779
Employer contributions	818	2,283
Plan participant contributions	743	572
Benefits paid	(2,589)	(2,652)
Fair value of plan assets—end of year	$ 30,493	$ 27,475
Funded status	$ (8,653)	$ (6,995)
Unrecognized transition obligation	6,525	7,341
Unrecognized actuarial (gain) loss	1,956	(396)
Accrued liability recognized	$ (172)	$ (50)

The postretirement health care benefit expense included the following components (in thousands):

	2005	2004
Interest cost	$ 2,019	$ 2,269
Service cost	237	475
Amortization of transition obligation over 20 years	816	1,186
Expected return on plan assets	(2,132)	(1,818)
Net periodic benefit cost	$ 940	$ 2,112

The 2005 and 2004 postretirement benefit obligation amounts were measured at the end of the year using a weighted-average discount rate of 5.25%and 6.25%, respectively. For 2005, medical and drug costs were assumed to increase 9.5% and 13.5%, respectively, grading down to 5.0% for both costs in year 2012 and thereafter. For 2004, medical and drug costs were assumed to increase 11%, grading down to 5.5% in year 2009 and thereafter. The medical and drug cost trend rates have a significant effect on the amounts reported. A 1.0% increase in the medical and drug cost trend would have increased the expense and the accumulated postretirement benefit obligation for 2005 by $74,000 and $1,409,000, respectively. A 1.0% decrease in the medical and drug cost trend would have decreased the expense and the accumulated postretirement benefit obligation for 2005 by $67,000 and $1,272,000, respectively.

The expected return on plan assets was assumed to be 8.0 % per year for 2005 and 2004.

Effective May 1, 2004, the plan was amended to eliminate pre-65 subsidy for all participants who retire after May 31, 2005. In 2004, this change was recognized on a pro-rated basis.

The expected future benefit payments, net of participant contributions, for the next five years and thereafter are as follows:

2006	$ 2,478,000
2007	2,595,000
2008	2,724,000
2009	2,811,000
2010	2,881,000
2011 through 2015	14,735,000

The estimated expected contribution for fiscal 2006 is $639,000.

The weighted-average investment allocation of plan assets by category is as follows:

	2005	2004	Target Allocation
Equity securities	55 %	57 %	56 %
Debt securities	29	25	29
Real estate securities	16	15	15
Other		3	
Total	100 %	100 %	100 %

The Health and Welfare Benefit Plan fiduciaries set the investment policy and strategy for investment of plan assets, including selecting investment managers and setting long-term risk and return objectives. The asset allocations are broadly diversified among asset category and within each category, which lowers the expected volatility of the portfolio's return and may protect against negative market environments.

To determine the expected long-term rate of return on plan assets, the University considers the target asset allocations, as well as expected returns on assets by category.

On December 8, 2003, the Medicare Prescription Drug Improvement and Modernization Act of 2003 was signed into law. The Act introduces a prescription drug benefit beginning in 2006 under Medicare (Medicare Part D) as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. Financial Accounting Standards Board Staff Position No. 106-2, issued in May 2004, provided accounting and disclosure requirements relating to the Act. Based on an actuarial analysis of the levels of benefits provided under the Tufts University retiree health care plans, the plan's actuary has concluded that pre-1993 retirees receive drug coverage at least actuarially equivalent to Medicare Part D. Effective July 1, 2004, the 28% federal subsidy was reflected in costs, reducing the Accumulated Postretirement benefit obligation by $1,709,000 and expense by $103,000.

12. RELATED ORGANIZATIONS

Walnut Hill Properties Corporation (Walnut Hill)—Walnut Hill is a not-for-profit corporation established by the University to own and manage certain investment and rental properties. The accounts of Walnut Hill are included in the accompanying consolidated financial statements of the University.

TUDC, LLC. (TUDC)—TUDC, formerly TUDC Inc., is a single member limited liability company created by the University to develop the Tufts International Center (the "Center") with the air rights over South Station in Boston. The Center, when completed, will include an office tower, hotel and conference facilities, retail space and a parking facility. In October 1997, TUDC entered into a development partnership agreement with Hines Interests Limited Partnership to co-develop the air rights. This arrangement was approved by the Boston Redevelopment Authority in July 1998. TUDC has a promissory note payable to the Massachusetts Bay Transportation Authority (the "MBTA") in the amount of $10,000,000, which remains the sole responsibility of TUDC. In May 2005, a new term sheet has been entered into which sets forth revised terms with respect to the development of the South Station air rights and the restructuring of the note payable to the MBTA. According to the term sheet, the University continues to have no legal liability for the promissory note. The accounts of TUDC are included in the accompanying consolidated financial statements of the University in investments and accounts payable and accrued expenses.

Tufts Veterinary Emergency Treatment & Specialties (Tufts VETS)—Tufts VETS is a not-for-profit corporation organized by the University to provide emergency and specialty veterinary services in a community environment. It provides post graduate training in its emergency and critical care training program and training to veterinary students on elective rotations. The accounts of Tufts VETS are included in the accompanying consolidated financial statements of the University.

Tufts Media LLC (Tufts Media)—Tufts Media is a single member limited liability company created by the University to operate its consumer publishing and media capability. The accounts of Tufts Media are included in the accompanying consolidated financial statements of the University.

JM Holding Corporation (JM Holdings)—JM Holdings, formerly Tufts Biotechnology Corporation, is a for-profit development corporation created by the University to develop 106 acres designated for commercial use on the veterinary school campus. At this time, there is no development agreement. The accounts of JM Holdings are included in the accompanying consolidated financial statements of the University.

New England Veterinary Conference LLC (NEVC)—NEVC is a single member limited liability company created by the University to operate The Northeast Veterinary Conference, which provides continuing medical education for veterinarians and technicians. The conference is co-hosted by the Cummings School of Veterinary Medicine at Tufts University and is a collaborative effort of organized veterinary medicine and various veterinary teaching hospitals of the Northeast. The accounts of NEVC are included in the accompanying consolidated financial statements of the University.

Tufts-New England Medical Center, Inc. (T-NEMC)—The University and New England Medical Center Hospitals, Inc. (the Medical Center) jointly formed T-NEMC, a service corporation. T-NEMC provides parking, laboratory animal housing, and educational media services to the University and the Medical Center. The costs of these services to the University for the years ended June 30, 2005 and 2004 were approximately $5,042,000 and $6,265,000, respectively. The administrative board of T-NEMC includes equal representation from the University and the Medical Center. The University holds a mortgage note receivable that bears interest at rates varying from 5.9 % to 7 %, with principal and interest payable semiannually. The balance of the note at June 30, 2005 and 2004 was $1,078,000 and $1,395,000, respectively, and is included in note and student loans receivables in the consolidated statements of financial position. The accounts of T-NEMC are not included in the accompanying consolidated financial statements of the University.

The assets of any of the organizations included in the consolidated financial statements may not be available to meet the obligations of the other entities.

13. CONTINGENCIES AND COMMITMENTS

There are currently several cases pending involving labor relations and other matters related to the normal operation of the University. The University believes that the outcome of these cases will have no significant effect on the financial position or results of operations of the University.

Operating Leases—The University has several noncancelable operating lease commitments at June 30, 2005, with terms in excess of one year for equipment and office space. Expenses associated with operating leases totaled approximately $1,103,000 for the year ended June 30, 2005. Future minimum lease payments under operating leases are as follows (in thousands):

Fiscal Year	
2006	$ 1,753
2007	969
2008	735
2009	503
2010	101
Total	$ 4,061

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