

# **Rhode Island School of Design**

**Financial Statements  
June 30, 2011 and 2010**

# Rhode Island School of Design

## Index

June 30, 2011 and 2010

---

|   | <b>Page(s)</b> |
|---|----------------|
| <b>Report of Independent Auditors</b> ..... | 1              |
| <b>Financial Statements</b>                 |                |
| Statements of Financial Position.....       | 2              |
| Statements of Activities .....              | 3-4            |
| Statements of Cash Flows .....              | 5              |
| Notes to Financial Statements .....         | 6-26           |



## Report of Independent Auditors

To Board of Trustees of  
Rhode Island School of Design

In our opinion, the accompanying statements of financial position and the related statements of activities and cash flows present fairly, in all material respects, the financial position of Rhode Island School of Design (the "School") at June 30, 2011 and 2010, and the results of its operations, changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the School's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

*PricewaterhouseCoopers LLP*

October 24, 2011

**Rhode Island School of Design**  
**Statements of Financial Position**  
**June 30, 2011 and 2010**

|  | <u>2011</u>                  | <u>2010</u>                  |
|--|------------------------------|------------------------------|
| <b>Assets</b>  |                              |                              |
| Cash and cash equivalents ( <i>Note 1</i> )              | \$ 23,326,239                | \$ 23,374,795                |
| Short-term investments ( <i>Note 1</i> )                 | 4,850,000                    | 5,050,000                    |
| Accounts receivable, net ( <i>Note 5</i> )               | 3,705,098                    | 2,509,709                    |
| Student loans receivable, net ( <i>Note 7</i> )          | 5,582,435                    | 6,113,513                    |
| Pledges receivable, net ( <i>Notes 2, 6</i> )            | 3,733,695                    | 5,185,918                    |
| Funds held in trust by others ( <i>Notes 1, 2</i> )      | 14,982,282                   | 13,100,584                   |
| Inventories ( <i>Note 1</i> )                            | 2,078,567                    | 1,853,788                    |
| Prepaid expenses and deferred charges                    | 2,001,633                    | 2,094,135                    |
| Other investments ( <i>Notes 2, 14</i> )                 | 5,455,959                    | 4,574,108                    |
| Long-term investments ( <i>Note 2</i> )                  | 304,478,341                  | 274,542,669                  |
| Property, plant and equipment, net ( <i>Note 10</i> )    | <u>191,530,276</u>           | <u>192,473,605</u>           |
| <b>Total Assets</b>                                      | <b><u>\$ 561,724,525</u></b> | <b><u>\$ 530,872,824</u></b> |
| <b>Liabilities</b>                                       |                              |                              |
| Accounts payable and accrued liabilities                 | \$ 8,156,324                 | \$ 9,165,501                 |
| Deferred income ( <i>Note 1</i> )                        | 6,442,474                    | 6,079,152                    |
| Agency accounts and other liabilities                    | 159,592                      | 109,901                      |
| Obligations under long-term agreements ( <i>Note 9</i> ) | 12,625,623                   | 13,307,495                   |
| U.S. Government loan funds                               | 3,989,741                    | 3,890,790                    |
| Liability for interest rate swap ( <i>Notes 2, 8</i> )   | 7,518,436                    | 9,031,255                    |
| Bonds payable ( <i>Note 8</i> )                          | 170,928,717                  | 173,843,609                  |
| Asset retirement obligation ( <i>Note 16</i> )           | <u>3,749,159</u>             | <u>3,553,705</u>             |
| <b>Total Liabilities</b>                                 | <b><u>213,570,066</u></b>    | <b><u>218,981,408</u></b>    |
| <b>Net Assets</b>  |                              |                              |
| Unrestricted net assets ( <i>Note 4</i> )                |                              |                              |
| Board designated funds                                   | 9,862,461                    | 9,960,943                    |
| Designated for endowment                                 | 213,098,224                  | 189,712,978                  |
| Other funds  | <u>38,168,833</u>            | <u>30,509,144</u>            |
| <b>Total Unrestricted Net Assets</b>                     | <b>261,129,518</b>           | <b>230,183,065</b>           |
| Temporarily restricted net assets ( <i>Note 4</i> )      | 56,526,636                   | 52,956,920                   |
| Permanently restricted net assets ( <i>Note 4</i> )      | <u>30,498,305</u>            | <u>28,751,431</u>            |
| <b>Total Net Assets</b>                                  | <b><u>348,154,459</u></b>    | <b><u>311,891,416</u></b>    |
| <b>Total Liabilities and Net Assets</b>                  | <b><u>\$ 561,724,525</u></b> | <b><u>\$ 530,872,824</u></b> |

The accompanying notes are an integral part of these financial statements.

**Rhode Island School of Design**  
**Statements of Activities**  
**Year Ended June 30, 2011**  
**(with summarized financial information for the year ended June 30, 2010)**

|  | Unrestricted         | Temporarily Restricted | Permanently Restricted | 2011 Total           | 2010 Total           |
|--|----------------------|------------------------|------------------------|----------------------|----------------------|
| <b>Operating revenues</b>  |                      |                        |                        |                      |                      |
| Tuition and fees   | \$ 96,691,383        | \$ -                   | \$ -                   | \$ 96,691,383        | \$ 92,029,808        |
| Less: School sponsored financial aid                             | 14,173,978           |                        |                        | 14,173,978           | 12,115,694           |
| Donor sponsored financial aid                                    | 1,613,951            |                        |                        | 1,613,951            | 2,014,876            |
| Net tuition  | 80,903,454           | -                      | -                      | 80,903,454           | 77,899,238           |
| Campus support services  | 21,859,815           |                        |                        | 21,859,815           | 21,311,125           |
| Endowment returns made available for operations                  | 9,100,847            |                        |                        | 9,100,847            | 7,250,632            |
| Gifts, grants and pledges  | 1,026,712            |                        |                        | 1,026,712            | 975,110              |
| Museum services  | 1,411,624            |                        |                        | 1,411,624            | 1,703,324            |
| Other income   | 329,338              |                        |                        | 329,338              | 492,686              |
| Net assets released from restrictions                            | 6,385,607            |                        |                        | 6,385,607            | 6,854,851            |
|  | <u>121,017,397</u>   | <u>-</u>               | <u>-</u>               | <u>121,017,397</u>   | <u>116,486,966</u>   |
| <b>Operating expenses</b>  |                      |                        |                        |                      |                      |
| Instruction  | 38,722,397           |                        |                        | 38,722,397           | 37,503,345           |
| Academic support   | 4,402,224            |                        |                        | 4,402,224            | 4,020,501            |
| Campus support services  | 10,657,671           |                        |                        | 10,657,671           | 9,115,475            |
| Institutional support  | 18,204,966           |                        |                        | 18,204,966           | 16,620,928           |
| Museum services  | 6,778,883            |                        |                        | 6,778,883            | 6,733,838            |
| Student services   | 5,893,291            |                        |                        | 5,893,291            | 4,846,942            |
| Plant maintenance  | 11,233,568           |                        |                        | 11,233,568           | 12,625,331           |
| Interest   | 5,244,435            |                        |                        | 5,244,435            | 5,322,130            |
| Depreciation   | 9,860,235            |                        |                        | 9,860,235            | 10,644,494           |
| Research   | 792,435              |                        |                        | 792,435              | 682,753              |
|  | <u>111,790,105</u>   | <u>-</u>               | <u>-</u>               | <u>111,790,105</u>   | <u>108,115,737</u>   |
| Operating net income before budgetary designations               | 9,227,292            | -                      | -                      | 9,227,292            | 8,371,229            |
| Net budgetary designations (Note 1)                              | (5,508,757)          |                        |                        | (5,508,757)          | (3,026,090)          |
| Operating net income   | <u>3,718,535</u>     | <u>-</u>               | <u>-</u>               | <u>3,718,535</u>     | <u>5,345,139</u>     |
| <b>Nonoperating</b>  |                      |                        |                        |                      |                      |
| Investment income  | 73,100               | 304,068                |                        | 377,168              | 2,096,818            |
| Realized and unrealized loss on interest rate swap               | (933,652)            |                        |                        | (933,652)            | (5,133,217)          |
| Realized and unrealized gain on investments, net                 | 20,972,733           | 8,222,615              |                        | 29,195,348           | 13,941,359           |
| Gifts and grants   | 1,109,734            | 1,925,886              | 1,746,874              | 4,782,494            | 6,876,341            |
| Recovery of amounts transferred to restore underwater endowments | 497,246              | (497,246)              |                        | -                    | -                    |
| Nonoperating assets allocated for budgetary designations         | 5,508,757            |                        |                        | 5,508,757            | 3,026,090            |
| Net assets released from restrictions                            |                      | (6,385,607)            |                        | (6,385,607)          | (6,854,851)          |
| Increase in net assets from nonoperating activities              | 27,227,918           | 3,569,716              | 1,746,874              | 32,544,508           | 13,952,540           |
| Increase in net assets   | 30,946,453           | 3,569,716              | 1,746,874              | 36,263,043           | 19,297,679           |
| <b>Total net assets</b>  |                      |                        |                        |                      |                      |
| Beginning of year  | 230,183,065          | 52,956,920             | 28,751,431             | 311,891,416          | 292,593,737          |
| End of year  | <u>\$261,129,518</u> | <u>\$ 56,526,636</u>   | <u>\$ 30,498,305</u>   | <u>\$348,154,459</u> | <u>\$311,891,416</u> |

The accompanying notes are an integral part of these financial statements.

**Rhode Island School of Design**  
**Statements of Activities**  
**Year Ended June 30, 2010**

|  | <u>Unrestricted</u>  | <u>Temporarily<br/>Restricted</u> | <u>Permanently<br/>Restricted</u> | <u>2010<br/>Total</u> |
|--|----------------------|-----------------------------------|-----------------------------------|-----------------------|
| <b>Operating revenues</b>  |                      |                                   |                                   |                       |
| Tuition and fees   | \$ 92,029,808        | \$ -                              | \$ -                              | \$ 92,029,808         |
| Less: School sponsored financial aid                             | 12,115,694           |                                   |                                   | 12,115,694            |
| Donor sponsored financial aid                                    | <u>2,014,876</u>     |                                   |                                   | <u>2,014,876</u>      |
| Net tuition  | 77,899,238           | -                                 | -                                 | 77,899,238            |
| Campus support services  | 21,311,125           |                                   |                                   | 21,311,125            |
| Endowment returns made available for operations                  | 7,250,632            |                                   |                                   | 7,250,632             |
| Gifts, grants and pledges  | 975,110              |                                   |                                   | 975,110               |
| Museum services  | 1,703,324            |                                   |                                   | 1,703,324             |
| Other income   | 492,686              |                                   |                                   | 492,686               |
| Net assets released from restrictions                            | <u>6,854,851</u>     |                                   |                                   | <u>6,854,851</u>      |
|  | <u>116,486,966</u>   | <u>-</u>                          | <u>-</u>                          | <u>116,486,966</u>    |
| <b>Operating expenses</b>  |                      |                                   |                                   |                       |
| Instruction  | 37,503,345           |                                   |                                   | 37,503,345            |
| Academic support   | 4,020,501            |                                   |                                   | 4,020,501             |
| Campus support services  | 9,115,475            |                                   |                                   | 9,115,475             |
| Institutional support  | 16,620,928           |                                   |                                   | 16,620,928            |
| Museum services  | 6,733,838            |                                   |                                   | 6,733,838             |
| Student services   | 4,846,942            |                                   |                                   | 4,846,942             |
| Plant maintenance  | 12,625,331           |                                   |                                   | 12,625,331            |
| Interest   | 5,322,130            |                                   |                                   | 5,322,130             |
| Depreciation   | 10,644,494           |                                   |                                   | 10,644,494            |
| Research   | <u>682,753</u>       |                                   |                                   | <u>682,753</u>        |
|  | <u>108,115,737</u>   | <u>-</u>                          | <u>-</u>                          | <u>108,115,737</u>    |
| Operating net income before budgetary designations               | 8,371,229            | -                                 | -                                 | 8,371,229             |
| Net budgetary designations (Note 1)                              | <u>(3,026,090)</u>   |                                   |                                   | <u>(3,026,090)</u>    |
| Operating net income   | <u>5,345,139</u>     | <u>-</u>                          | <u>-</u>                          | <u>5,345,139</u>      |
| <b>Nonoperating</b>  |                      |                                   |                                   |                       |
| Investment income  | 415,658              | 1,681,160                         |                                   | 2,096,818             |
| Realized and unrealized loss on interest rate swap               | (5,133,217)          |                                   |                                   | (5,133,217)           |
| Realized and unrealized gain on investments, net                 | 8,878,896            | 5,062,463                         |                                   | 13,941,359            |
| Gifts and grants   | 286,596              | 4,332,747                         | 2,256,998                         | 6,876,341             |
| Recovery of amounts transferred to restore underwater endowments | 856,460              | (856,460)                         |                                   | -                     |
| Nonoperating assets allocated for budgetary designations         | 3,026,090            |                                   |                                   | 3,026,090             |
| Net assets released from restrictions                            |                      | <u>(6,854,851)</u>                |                                   | <u>(6,854,851)</u>    |
| Increase in net assets from nonoperating activities              | <u>8,330,483</u>     | <u>3,365,059</u>                  | <u>2,256,998</u>                  | <u>13,952,540</u>     |
| Increase in net assets   | 13,675,622           | 3,365,059                         | 2,256,998                         | 19,297,679            |
| <b>Total net assets</b>  |                      |                                   |                                   |                       |
| Beginning of year  | <u>216,507,443</u>   | <u>49,591,861</u>                 | <u>26,494,433</u>                 | <u>292,593,737</u>    |
| End of year  | <u>\$230,183,065</u> | <u>\$ 52,956,920</u>              | <u>\$ 28,751,431</u>              | <u>\$311,891,416</u>  |

The accompanying notes are an integral part of these financial statements.

**Rhode Island School of Design**  
**Statements of Cash Flows**  
**Years Ended June 30, 2011 and 2010**

|  | <u>2011</u>          | <u>2010</u>          |
|--|----------------------|----------------------|
| <b>Cash flows from operating activities</b>  |                      |                      |
| Change in net assets   | \$ 36,263,043        | \$ 19,297,679        |
| Adjustments to reconcile change in net assets to net cash used by operating activities |                      |                      |
| Gain on investments  | (37,062,365)         | (17,038,315)         |
| Unrealized (gain)/loss on interest rate swap   | (1,512,819)          | 2,504,411            |
| Change in funds held in trust by others  | (1,881,698)          | (1,456,130)          |
| Depreciation and amortization  | 9,689,889            | 10,500,864           |
| Contributions restricted for long-term purposes  | (2,334,993)          | (1,337,157)          |
| Contributions of securities  | (586,761)            | (174,396)            |
| Change in asset retirement obligation  | 195,454              | 185,264              |
| Increase in U.S. Government loan funds   | 98,951               | 70,004               |
| Amortization of long-term agreements   | 587,298              | 202,526              |
| Changes in operating assets and liabilities that provide (use) cash                    |                      |                      |
| Accounts receivable  | (1,195,389)          | 1,048,679            |
| Pledges receivable   | 1,452,223            | 61,939               |
| Inventories  | (224,779)            | (49,905)             |
| Prepaid expenses and deferred charges and other assets                                 | 92,502               | (6,379)              |
| Accounts payable and accrued expenses  | (1,167,829)          | 1,048,705            |
| Agency accounts and other liabilities  | 49,691               | 12,050               |
| Deferred income  | 363,322              | (155,795)            |
| Net cash provided by operating activities  | <u>2,825,740</u>     | <u>14,714,044</u>    |
| <b>Cash flows from investing activities</b>  |                      |                      |
| Purchases of buildings and equipment   | (8,562,815)          | (6,816,113)          |
| Student loans issued   | (391,718)            | (759,894)            |
| Student loans repaid   | 922,796              | 1,014,892            |
| Change in short-term investments   | 200,000              | (3,028,046)          |
| Purchases of investments   | (352,845,430)        | (241,744,277)        |
| Sales of investments   | 359,677,048          | 248,291,826          |
| Net cash used in investing activities  | <u>(1,000,119)</u>   | <u>(3,041,612)</u>   |
| <b>Cash flows from financing activities</b>  |                      |                      |
| Payments on long-term debt   | (2,940,000)          | (2,855,000)          |
| Payments on obligations under long-term agreements                                     | (1,269,170)          | (1,200,655)          |
| Contributions restricted for long-term purposes  | 2,334,993            | 1,337,157            |
| Net cash used in financing activities  | <u>(1,874,177)</u>   | <u>(2,718,498)</u>   |
| Net decrease/increase in cash and cash equivalents                                     | (48,556)             | 8,953,934            |
| <b>Cash and cash equivalents</b>   |                      |                      |
| Beginning of year  | <u>23,374,795</u>    | <u>14,420,861</u>    |
| End of year  | <u>\$ 23,326,239</u> | <u>\$ 23,374,795</u> |
| <b>Noncash activity</b>  |                      |                      |
| Assets acquired through long-term arrangements   |                      |                      |
| Property, plant and equipment  | \$ -                 | \$ 6,387,509         |
| Obligations under long-term arrangements   | -                    | 6,387,509            |
| Costs accrued for capital expenditures   | 353,396              | 194,761              |
| Cash paid for interest   | 7,472,090            | 7,740,061            |

The accompanying notes are an integral part of these financial statements.

# Rhode Island School of Design

## Notes to the Financial Statements

### June 30, 2011 and 2010

---

#### 1. Summary of Significant Accounting Policies

The financial statements of the Rhode Island School of Design (the "School") have been prepared in accordance with Generally Accepted Accounting Principles in the United States of America ("US GAAP") and with the reporting principles of not-for-profit accounting.

Net assets and current activity are classified into three categories; unrestricted, temporarily restricted and permanently restricted. The categories are based on the existence, absence or expiration of donor-imposed restrictions.

- Unrestricted net assets are not subject to donor-imposed stipulations, but may be designated for specific purpose by action of the Board of Trustees.
- Temporarily restricted net assets include gifts, pledges, trusts and remainder interests, and income and gains which can be expended but for which restrictions have not yet been met. Such restrictions include purpose restrictions where donors have specified the purpose for which the net assets are to be spent, or time restrictions imposed by donors or implied by the nature of the gift (capital projects, pledges to be paid in the future and certain life income funds).
- Permanently restricted net assets include the original amounts of gifts, including pledges, trusts, and remainder interests, which are required by donors to be permanently retained.

#### Operations

Revenues earned and expenses incurred in conducting the programs and services of the School are presented in the financial statements as operating activities. Net revenues and other resources from operating activities are not restricted by donors or other external sources and are, therefore, classified as unrestricted net assets. At the discretion of the School, all or a portion of net assets from operating income/loss may be designated for budgetary purposes, for capital acquisitions, for student loan funds, for principal payments on debt, or for future use by the Board of Trustees.

#### Net Budgetary Designations

Net budgetary designations reconcile operating net income or loss to management's internal net operating statement. Adjustments are made for nonexpense items such as principal payments on debt and depreciation in excess of funds allocated for capital expenditures. Net budgetary designations also reflect management's decision to utilize or defer a portion of nonoperating income to match expenses that are included in operating expenses. This income may be in the form of unrestricted gifts in the current year or from a prior year. It may also include utilization of funds designated by the Board of Trustees in prior years. Net budgetary designations for 2011 and 2010 are as follows:



**Rhode Island School of Design**  
**Notes to the Financial Statements**  
**June 30, 2011 and 2010**

---

|   | <u>2011</u>           | <u>2010</u>           |
|---|-----------------------|-----------------------|
| Capital expenditures  | \$ (6,475,000)        | \$ (5,700,000)        |
| Depreciation  | 9,860,235             | 10,644,494            |
| Debt service adjustment   | (5,539,122)           | (5,318,054)           |
| Reclassification of operating expenses<br>associated with long-term agreement | (675,600)             | (1,376,539)           |
| Reclassification of expenses related<br>to non-operating income               | <u>(2,679,270)</u>    | <u>(1,275,991)</u>    |
| Net Budgetary Designation   | <u>\$ (5,508,757)</u> | <u>\$ (3,026,090)</u> |

**Nonoperating**

Nonoperating revenue and expenses include all gifts, with the exception of those received in the annual fund, change in the value of interest rate swaps, other gains on sales of assets, loss on extinguishment of debt, investment income and realized and unrealized gains on investments to the extent not utilized in operations based on the School's spending policy, as described below, and amounts designated at the discretion of the School for budgetary purposes.

**Gifts and Pledges**

Gifts and pledges are recognized as revenue when received. Gifts specified for the acquisition or construction of long-lived assets are released to unrestricted from temporarily restricted net assets when the assets are placed in service.

Unconditional promises to contribute to the School in the future (pledges) are recorded as receivables at the present value of their expected cash flows less an allowance for uncollectibles. The related revenue is assigned to temporarily restricted net assets until collected and any other restrictions are met, or permanently restricted net assets, if so restricted by the donor.

**Investments**

The fair values of publicly traded investments are determined based upon quoted market prices. The School's alternative investment funds are carried at estimated fair value determined by management, based upon valuations provided by management of the privately held investment funds as of June 30, 2011 and 2010. Alternative investments include limited partnerships, limited liability corporations, real estate and offshore investment funds. Because investments in alternative investment funds are not marketable, the estimated value is subject to uncertainty and therefore, may differ significantly from the value that would have been used had a market for such investments existed and such differences could be material.

**Cash and Cash Equivalents**

The School considers highly liquid investments with maturities of three-months or less when purchased to be cash equivalents. Cash equivalents are stated at cost, which approximates fair value.

**Short-term Investments**

Operating cash invested with original maturities greater than three months at the date of purchase are classified as short-term investments. At June 30, 2011, the majority of the balance represents a \$4,600,000 six-month CD. At June 30, 2010, the majority of the balance represented a \$4,800,000 six-month CD.

# Rhode Island School of Design

## Notes to the Financial Statements

### June 30, 2011 and 2010

---

#### **Split Interest Agreements**

The School is party to various split interest agreements with regards to irrevocable trusts and other agreements. These agreements include: perpetual trusts, charitable remainder trusts, charitable gift annuities and pooled life income funds. The assets of gift annuities and pooled income funds are included at fair value in Other investments on the Statement of Financial Position. The obligations associated with these arrangements are recorded at present value of the aggregate liability to beneficiaries based upon life expectancy. Assets held by an outside trustee are classified as Funds held in trust by others or as Pledges receivable. These assets represent the School's share of the fair value of the trust assets as of the balance sheet date net of a liability for the present value of estimated future payments to the donors or other beneficiaries, where applicable. Distributions of income from the trusts to the School are recorded as revenue. Split interest agreements and annuity obligations are based on certain assumptions regarding life expectancy, discount rate and rate of return. Circumstances affecting these assumptions can change the estimate of the liabilities in future periods.

#### **Inventories**

Inventories are stated at the lower of cost or market. The School uses the first-in, first-out method of accounting for inventory. Inventory consists primarily of items held for resale by the School's stores.

#### **Property, Plant and Equipment**

Property, plant and equipment is stated at acquisition cost or the fair value as of the date of the gift, net of accumulated depreciation (Note 10). Depreciation is computed on a straight-line basis over the following estimated useful lives:

|                            |             |
|----------------------------|-------------|
| Buildings and improvements | 15–45 years |
| Machinery and equipment    | 5–8 years   |
| Furniture and fixtures     | 5–8 years   |

Expenditures for maintenance, repairs, interest and depreciation are expensed as incurred and allocated to functional classifications of expense (Note 15) based on actual expenditures or relative square footage. Upon sale or retirement, the cost of the property and the related accumulated depreciation are removed from the respective accounts, and any resulting gains or losses are reflected in Statement of Activities.

#### **Collections**

The School does not capitalize or assign a value to the museum collections. Collections that are acquired through purchases and contributions are not recognized as assets on the Statement of Financial Position. Purchases of collection items are recorded as decreases in unrestricted net assets in the year in which the items are acquired or in temporarily restricted net assets if the asset used to purchase items is restricted by donors.

Contributed collection items are not reflected in the financial statements. Proceeds from deaccessions or insurance recoveries are reflected as increases in the appropriate net asset classes.

#### **Campus Support Services**

Campus support services include the RISD Store, dining halls, residence halls and other on-campus undertakings that provide services to students, faculty and staff for fees directly related but not necessarily equivalent to the costs of the services.

# Rhode Island School of Design

## Notes to the Financial Statements

### June 30, 2011 and 2010

---

#### **Deferred Income**

Deferred income represents tuition and fees received for programs and services to be conducted predominantly in the next fiscal year.

#### **Tax Status**

The School is qualified for exemption from Federal income tax under Section 501(c)(3) of the Internal Revenue Code.

#### **Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States 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 those estimates.

#### **Fair Value Measurements**

The School complies with accounting guidance for *Fair Value Measurements*, which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. Such guidance applies to reported balances that are required or permitted to be measured at fair value under existing accounting pronouncements.

The *Fair Value Measurements* standard emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement is determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, the guidance establishes a hierarchy of valuation inputs based on the extent to which the inputs are observable in the marketplace, as follows:

- Level 1      Quoted prices in active markets for identical assets or liabilities.
  
- Level 2      Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities in active markets; quoted prices for identical assets or liabilities in markets that are not active; or inputs other than quoted prices that are observable or can be corroborated by observable market data by correlation or other means.
  
- Level 3      Unobservable inputs for an asset or liability that are supported by little or no market activity.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

The School is permitted under US GAAP to estimate the fair value of an investment at the measurement date using the reported net asset value (NAV) without further adjustment unless the entity expects to sell the investment at a value other than NAV or if the NAV is not calculated in accordance with US GAAP. The School's investments in private equity, mutual funds, hedge funds and other securities are fair valued based on the most current NAV.

The School performs additional procedures including due diligence reviews on its investments in investment companies and other procedures with respect to the capital account or NAV provided to ensure conformity with US GAAP. The School has assessed factors including, but not limited to,

# Rhode Island School of Design

## Notes to the Financial Statements

### June 30, 2011 and 2010

---

managers' compliance with *Fair Value Measurements* standard, price transparency and valuation procedures in place, the ability to redeem at NAV at the measurement date, and existence of certain redemption restrictions at the measurement date.

The guidance also requires additional disclosures to enable users of the financial statements to understand the nature and risk of the School's investments. Furthermore, investments which can be redeemed at NAV by the School on the measurement date or in the near term (defined as 90 days) are classified as Level 2. Investments which cannot be redeemed on the measurement date or in the near term are classified as Level 3.

#### **Reclassifications**

Certain June 30, 2010 balances and amounts previously reported related to program expenditures have been reclassified to conform to the June 30, 2011 presentation, which was adjusted to reflect best practice NACUBO (National Association of College and University Business Officers) program definitions.

#### **Subsequent Events**

The FASB establishes standards of accounting for and disclosure of events that occur after the balance sheet date, but before financial statements are issued or are available to be issued. The School has evaluated subsequent events through October 24, 2011, the date of financial statements' issuance. There were no subsequent events that occurred after the balance sheet date that have a material impact on the School's financial statements.

#### **Recently Adopted Accounting Standards**

On July 1, 2010, the School adopted new guidance enhancing the *Fair Value Measurement* standard. This standard requires further disclosure of significant transfers in and out of Level 1 and Level 2 fair value measurements, including the reasons for the transfers, and requires discussions of their fair value measurement disclosures on a disaggregated basis. Please see Note 2 for further details.

## **2. Fair Value of Financial Instruments**

In accordance with accounting guidance for *Fair Value Measurements*, the following table summarizes the financial instruments carried at fair value on a recurring basis as of June 30, 2011 and 2010, aggregated by the level in the fair value hierarchy within which those measurements fall:

**Rhode Island School of Design**  
**Notes to the Financial Statements**  
**June 30, 2011 and 2010**

|   | Quoted Prices<br>in Active<br>Markets<br>(Level 1) | Significant Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | 2011<br>Total<br>Fair Value |
|---|--|--|--|-----------------------------|
| <b>Assets</b>                               |  |  |  |                             |
| Short-term investments                      | \$ 4,850,000                                       | \$ -   | \$ -   | \$ 4,850,000                |
| Investments                                 |  |  |  |                             |
| Cash and cash equivalents                   | 68,649,062   |  |  | 68,649,062                  |
| Receivable from fund managers               | a 71,912,374                                       |  |  | 71,912,374                  |
| Fixed income securities                     | b -  |  |  | -                           |
| Common and preferred stocks                 | c  |  |  |                             |
| Domestic Large Cap Growth Equities          | 9,165  |  |  | 9,165                       |
| Domestic Large Cap Value Equities           | 26,937,198   |  |  | 26,937,198                  |
| Domestic Small/Mid Cap Growth Equities      | 17,617,149   |  |  | 17,617,149                  |
| Mutual funds                                | d 15,170,637                                       |  |  | 15,170,637                  |
| International securities                    | e  | 16,306,246   |  | 16,306,246                  |
| Hedge funds                                 |  |  |  |                             |
| Multi-Strategy Hedge Fund of Funds          | f  | 3,047,683  | 41,248,947   | 44,296,630                  |
| Equity Long/Short                           | g  | 4,934,321  | 1,104,179  | 6,038,500                   |
| Private equity                              | h  |  | 36,139,343   | 36,139,343                  |
| Real estate                                 | i  |  | 5,675,170  | 5,675,170                   |
| Total investments*                          | 200,295,585  | 24,288,250   | 84,167,639   | 308,751,474                 |
| Beneficial interests held by third parties* |  |  | 15,763,668   | 15,763,668                  |
| Total assets at fair value                  | \$ 205,145,585                                     | \$ 24,288,250  | \$ 99,931,307                                      | \$ 329,365,142              |
| <b>Liabilities</b>                          |  |  |  |                             |
| Interest rate swap                          | \$ -   | \$ -   | \$ (7,518,436)                                     | \$ (7,518,436)              |
| Total liabilities at fair value             | \$ -   | \$ -   | \$ (7,518,436)                                     | \$ (7,518,436)              |

\* Total investments and beneficial interests held in trust by others vary in relation to the Statement of Financial Position because certain accounts thereon are reported in Pledges Receivable, Other Investments and Funds Held in Trust by Others.

- a. Receivable from fund managers includes redemptions on June 30, 2011 for which cash was received after June 30, 2011.
- b. Fixed income securities include investments in government or municipal bonds, which pay a fixed rate.
- c. Common and preferred stocks typically have a daily redemption frequency and a 3-day notification period. Domestic Large Cap Growth equities typically have a capitalization of \$5.0 billion or more and generate significantly positive cash flows or earnings, which increase at significantly faster rates than the overall economy. This category is made up of one type of investment that has a daily redemption frequency and a 3-day notice period.
- d. Mutual funds consist of a long-only strategy which invests in international securities. This category is made up of one type of investment that has a daily redemption frequency and a 3-day notice period.
- e. International securities are equity securities whose primary tracking markets are outside of the United States. This category is made up of two types of investments: one has a monthly

**Rhode Island School of Design**  
**Notes to the Financial Statements**  
**June 30, 2011 and 2010**

---

- redemption frequency with a 2-day notice period and the other has a quarterly redemption frequency with a 60-day notice period.
- f. Multi-Strategy Fund of Funds invest with multiple managers who choose investment strategies and provide the investor with the advantage of diversification among managers and styles. This category is made up of five types of investments: two have a quarterly redemption frequency with a 65-day notice period (in Level 2), one has an annual redemption frequency with a 90-day notice period (in Level 3), one is in liquidation so any ability to redeem is at the manager's discretion (in Level 3), and one essentially has no liquidation rights at this time (in Level 3).
  - g. Equity Long/Short investing consists of a core holding of long equities hedged at all times with short sales of stocks and/or stock index options. This category is made up of two types of investments: one is fully redeemed but with a side pocket remaining so any redemption is at the manager's discretion (in Level 3) and the other has a quarterly redemption frequency with a 25% limit and a 60-day notice period (in Level 2).
  - h. Private equity is money invested in companies that are not publicly traded on a stock exchange. They are illiquid long-term investments whose goals are to provide a meaningful return premium over public equity markets. Any ability to redeem these securities is at the manager's discretion.
  - i. This category includes directly held real estate which is reported at appraised value which approximates fair value.

**Rhode Island School of Design**  
**Notes to the Financial Statements**  
**June 30, 2011 and 2010**

|   | Quoted Prices<br>in Active<br>Markets<br>(Level 1) | Significant Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | 2010<br>Total<br>Fair Value |
|---|--|--|--|-----------------------------|
| <b>Assets</b>                               |  |  |  |                             |
| Short-term investments                      | \$ 5,050,000                                       | \$ -   | \$ -   | \$ 5,050,000                |
| Investments                                 |  |  |  |                             |
| Cash and cash equivalents                   | 8,449,361  |  |  | 8,449,361                   |
| Fixed income securities                     | 37,928,495   |  |  | 37,928,495                  |
| Common and preferred stocks                 |  |  |  |                             |
| Domestic Large Cap Growth Equities          | 19,608,793   |  |  | 19,608,793                  |
| Domestic Large Cap Value Equities           | 20,974,742   |  |  | 20,974,742                  |
| Domestic Small/Mid Cap Growth Equities      | 11,406,594   |  |  | 11,406,594                  |
| Mutual funds                                | 12,599,545   |  |  | 12,599,545                  |
| International securities                    |  | 11,457,280   |  | 11,457,280                  |
| Hedge funds                                 |  |  |  |                             |
| Multi-Strategy Hedge Fund of Funds          |  | 34,101,453   | 44,756,536   | 78,857,989                  |
| Equity Long/Short                           |  | 27,826,444   | 11,913,051   | 39,739,495                  |
| Private equity                              |  |  | 31,030,705   | 31,030,705                  |
| Real estate                                 |  |  | 5,918,043  | 5,918,043                   |
| Total investments*                          | <u>110,967,530</u>                                 | <u>73,385,177</u>                                      | <u>93,618,335</u>                                  | <u>277,971,042</u>          |
| Beneficial interests held by third parties* |  |  | 13,821,487   | 13,821,487                  |
| Total assets at fair value                  | <u>\$ 116,017,530</u>                              | <u>\$ 73,385,177</u>                                   | <u>\$ 107,439,822</u>                              | <u>\$ 296,842,529</u>       |
| <b>Liabilities</b>                          |  |  |  |                             |
| Interest rate swap                          | \$ -   | \$ -   | \$ (9,031,255)                                     | \$ (9,031,255)              |
| Total liabilities at fair value             | <u>\$ -</u>  | <u>\$ -</u>  | <u>\$ (9,031,255)</u>                              | <u>\$ (9,031,255)</u>       |

The School's policy for allocation to Levels 1, 2, and 3 in the tables above are described in Note 1.

Investments included in Level 3 primarily consist of the school's ownership in alternative investments (principally limited partnership interests in hedge, private equity, and other similar funds). The value of alternative investments represents the ownership interest in the NAV of the respective partnership as reported by the general partner. The School has performed due diligence around its alternative investments to ensure that they are recorded at fair value, which is based on the NAV. At June 30, 2011, approximately 22.2% of investments held by the partnerships consist of marketable securities and investments with observable inputs and 77.8% are securities that are subject to the judgment of the general partner as reflected in the NAVs. At June 30, 2010, these percentages were 13.7% and 86.3%, respectively.

Interest rate swaps are valued using both observable and unobservable inputs, such as quotations received from the counterparty, dealers or brokers, whenever available and considered reliable.

**Rhode Island School of Design**  
**Notes to the Financial Statements**  
**June 30, 2011 and 2010**

The following table is a rollforward of the Statement of Financial Position amounts for financial instruments classified by the School within Level 3 of the fair value hierarchy defined above:

|  | Fair Value<br>July 1, 2010 | Realized<br>Gains (Losses) | Unrealized<br>Gains (Losses) | Purchases           | Sales                  | Fair Value<br>June 30, 2011 |
|--|----------------------------|----------------------------|------------------------------|---------------------|------------------------|-----------------------------|
| Investments                                |                            |                            |                              |                     |                        |                             |
| Hedge funds                                |                            |                            |                              |                     |                        |                             |
| Multi-Strategy Hedge Fund of Funds         | \$ 44,756,536              | \$ 2,027,149               | \$ 3,261,563                 | \$ -                | \$ (8,796,301)         | \$ 41,248,947               |
| Equity Long/Short                          | 11,913,051                 | (7,425,370)                | 6,923,686                    |                     | (10,307,188)           | 1,104,179                   |
| Private equity                             | 31,030,705                 | 8,307,199                  | (4,252,975)                  | 3,932,389           | (2,877,975)            | 36,139,343                  |
| Real estate                                | 5,918,043                  |                            | (718,043)                    | 475,170             |                        | 5,675,170                   |
| Total investments                          | <u>\$ 93,618,335</u>       | <u>\$ 2,908,978</u>        | <u>\$ 5,214,231</u>          | <u>\$ 4,407,559</u> | <u>\$ (21,981,464)</u> | <u>\$ 84,167,639</u>        |
| Beneficial interests held by third parties | \$ 13,821,487              | \$ -                       | \$ 2,445,157                 | \$ 10,000           | \$ (512,976)           | \$ 15,763,668               |
| Interest rate sw ap                        | \$ (9,031,255)             | \$ -                       | \$ 1,512,819                 | \$ -                | \$ -                   | \$ (7,518,436)              |

|  | Fair Value<br>July 1, 2009 | Realized<br>Gains (Losses) | Unrealized<br>Gains (Losses) | Purchases            | Sales          | Transfers<br>Out       | Fair Value<br>June 30, 2010 |
|--|----------------------------|----------------------------|------------------------------|----------------------|----------------|------------------------|-----------------------------|
| Short term investments                     | \$ 1,771,954               | \$ -                       | \$ -                         | \$ -                 | \$ (1,771,954) | \$ -                   | \$ -                        |
| Investments                                |                            |                            |                              |                      |                |                        |                             |
| International securities                   | 8,127,958                  | (667,507)                  | 1,073,495                    | 2,923,333            |                | (11,457,279)           | -                           |
| Hedge funds                                |                            |                            |                              |                      |                |                        |                             |
| Multi-Strategy Hedge Fund of Funds         | 68,788,666                 | 18,928,854                 | (14,109,999)                 | 11,356,064           |                | (40,207,049)           | 44,756,536                  |
| Equity Long/Short                          | 39,599,660                 | (56,210)                   | 2,997,815                    | -                    |                | (30,628,214)           | 11,913,051                  |
| Private equity                             | 23,285,094                 | 190,251                    | 672,303                      | 6,883,057            |                |                        | 31,030,705                  |
| Real estate                                | 9,109,422                  |                            | (3,482,872)                  | 291,493              |                |                        | 5,918,043                   |
| Total investments                          | <u>\$ 148,910,800</u>      | <u>\$ 18,395,388</u>       | <u>\$ (12,849,258)</u>       | <u>\$ 21,453,947</u> | <u>\$ -</u>    | <u>\$ (82,292,542)</u> | <u>\$ 93,618,335</u>        |
| Beneficial interests held by third parties | \$ 12,278,252              | \$ -                       | \$ 882,027                   | \$ 661,208           | \$ -           | \$ -                   | \$ 13,821,487               |
| Interest rate sw ap                        | \$ (6,526,844)             | \$ -                       | \$ (2,504,411)               | \$ -                 | \$ -           | \$ -                   | \$ (9,031,255)              |

For the year ended June 30, 2010, Transfers Out represent transfers from Level 3 to Level 2 due to the change in redemption periods to less than or equal to 90 days.

All net realized and unrealized gains (losses) in the tables above are reflected in the accompanying Statement of Activities. Net unrealized gains (losses) relate to those financial instruments held by the School at June 30, 2011.



**Rhode Island School of Design**  
**Notes to the Financial Statements**  
**June 30, 2011 and 2010**

The following table represents the transfers between levels for the year ended June 30, 2011:

|                                    | Level 1              | Level 2                |
|------------------------------------|----------------------|------------------------|
| Transfers in and/or (out)          |                      |                        |
| Receivable from fund managers      | \$ 61,359,686        | \$ -                   |
| International securities           |                      | (2,768,323)            |
| Hedge funds                        |                      |                        |
| Multi-Strategy Hedge Fund of Funds |                      | (33,478,121)           |
| Equity Long/Short                  |                      | (25,113,242)           |
| Total                              | <u>\$ 61,359,686</u> | <u>\$ (61,359,686)</u> |

Please note that the School has changed investment advisors. As a result, it is in the process of realigning investment managers and asset allocation.

Transfers in are shown separately from Transfers out. The investments in Level 2 above were all redeemed on June 30, 2011; however, the cash was not received until after June 30, 2011. This is represented by the Receivable from fund managers in Level 1 above. Therefore, the significant transfer from Level 2 to Level 1 is simply a matter of the timing of when the cash is invested.

**3. Investments**

Investment income for the years ended June 30, 2011 and 2010 was as follows:

|   | 2011                 |                        |                        |                      |
|---|----------------------|------------------------|------------------------|----------------------|
|   | Unrestricted         | Temporarily Restricted | Permanently Restricted | Total                |
| Interest and dividend income            | \$ 1,306,930         | \$ 304,068             | \$ -                   | \$ 1,610,998         |
| Realized gains                          | 12,818,663           | 1,934,860              |                        | 14,753,523           |
| Increase in net unrealized appreciation | 16,021,087           | 6,287,755              |                        | 22,308,842           |
| Total investment return                 | <u>\$ 30,146,680</u> | <u>\$ 8,526,683</u>    | <u>\$ -</u>            | <u>\$ 38,673,363</u> |

|  | 2010                 |                        |                        |                      |
|--|----------------------|------------------------|------------------------|----------------------|
|  | Unrestricted         | Temporarily Restricted | Permanently Restricted | Total                |
| Interest and dividend income                           | \$ 4,569,334         | \$ 1,681,160           | \$ -                   | \$ 6,250,494         |
| Realized gains   | 21,050,403           | 2,743,243              |                        | 23,793,646           |
| Increase in net unrealized appreciation (depreciation) | (9,074,551)          | 2,319,220              |                        | (6,755,331)          |
| Total investment return                                | <u>\$ 16,545,186</u> | <u>\$ 6,743,623</u>    | <u>\$ -</u>            | <u>\$ 23,288,809</u> |

# Rhode Island School of Design

## Notes to the Financial Statements

### June 30, 2011 and 2010

---

Investment management fees and other expenses (netted from interest and dividend income) totaled \$1,161,776 and \$73,329 in 2011 and 2010, respectively. In 2010, \$954,845 of management fees were partially offset by an \$881,516 tax refund for unrelated business income from one of the School's alternative investments.

Certain net assets are pooled for investment income purposes. The unit market value at June 30, 2011 and 2010 was \$290.06 and \$261.60, respectively. The market value of long-term investments, as stated in the Statement of Financial Position, represents the value of pooled endowment plus other nonpooled investments at June 30, 2011 and 2010.

#### 4. Endowment Funds

The School's endowment consists of approximately 220 individual donor-restricted endowment funds and 55 board-designated endowment funds for a variety of purposes plus the following where the assets have been designated for endowment: pledges receivable, split interest agreements, and other net assets. The endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. The net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

The School's Board of Trustees has interpreted the UPMIFA as requiring the preservation of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the School classifies as permanently restricted net assets, (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure of the School in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the School considers the following factors in making a determination to appropriate or accumulate endowment funds:

1. The duration and preservation of the fund
2. The purposes of the School and the donor-restricted endowment fund
3. General economic conditions
4. The possible effect of inflation and deflation
5. The expected total return from income and appreciation of investments
6. Other resources of the School
7. The investment policies of the School

**Rhode Island School of Design**  
**Notes to the Financial Statements**  
**June 30, 2011 and 2010**

Endowment net asset composition by type of fund as of June 30, 2011 and 2010 were as follows:

**2011**

|   | <b>Unrestricted</b>  | <b>Temporarily<br/>Restricted</b> | <b>Permanently<br/>Restricted</b> | <b>Total</b>         |
|---|----------------------|-----------------------------------|-----------------------------------|----------------------|
| <b>Board-designated</b>                 |                      |                                   |                                   |                      |
| For scholarships                        | \$ 11,128,586        | \$ -                              | \$ -                              | \$ 11,128,586        |
| For academic and institutional purposes | 200,156,159          |                                   |                                   | 200,156,159          |
| For museum support                      | 2,213,744            |                                   |                                   | 2,213,744            |
| For underwater endowments               | (400,265)            |                                   |                                   | (400,265)            |
| Total board designated                  | <u>213,098,224</u>   | <u>-</u>                          | <u>-</u>                          | <u>213,098,224</u>   |
| <b>Donor-restricted</b>                 |                      |                                   |                                   |                      |
| For scholarships                        |                      | 12,649,518                        | 16,048,659                        | 28,698,177           |
| For academic and institutional purposes |                      | 5,719,457                         | 4,503,698                         | 10,223,155           |
| For museum support                      |                      | 15,668,346                        | 9,945,948                         | 25,614,294           |
| Total donor restricted                  | <u>-</u>             | <u>34,037,321</u>                 | <u>30,498,305</u>                 | <u>64,535,626</u>    |
| Total endowment funds                   | <u>\$213,098,224</u> | <u>\$ 34,037,321</u>              | <u>\$ 30,498,305</u>              | <u>\$277,633,850</u> |

**2010**

|   | <b>Unrestricted</b>  | <b>Temporarily<br/>Restricted</b> | <b>Permanently<br/>Restricted</b> | <b>Total</b>         |
|---|----------------------|-----------------------------------|-----------------------------------|----------------------|
| <b>Board-designated</b>                 |                      |                                   |                                   |                      |
| For scholarships                        | \$ 7,573,495         | \$ -                              | \$ -                              | \$ 7,573,495         |
| For academic and institutional purposes | 181,233,079          |                                   |                                   | 181,233,079          |
| For museum support                      | 1,803,915            |                                   |                                   | 1,803,915            |
| For underwater endowments               | (897,511)            |                                   |                                   | (897,511)            |
| Total board designated                  | <u>189,712,978</u>   | <u>-</u>                          | <u>-</u>                          | <u>189,712,978</u>   |
| <b>Donor-restricted</b>                 |                      |                                   |                                   |                      |
| For scholarships                        |                      | 10,482,626                        | 14,109,517                        | 24,592,143           |
| For academic and institutional purposes |                      | 5,985,948                         | 5,351,469                         | 11,337,417           |
| For museum support                      |                      | 13,590,500                        | 9,290,445                         | 22,880,945           |
| Total donor restricted                  | <u>-</u>             | <u>30,059,074</u>                 | <u>28,751,431</u>                 | <u>58,810,505</u>    |
| Total endowment funds                   | <u>\$189,712,978</u> | <u>\$ 30,059,074</u>              | <u>\$ 28,751,431</u>              | <u>\$248,523,483</u> |

**Rhode Island School of Design**  
**Notes to the Financial Statements**  
**June 30, 2011 and 2010**

Changes in endowment net assets for the years ended June 30, 2011 and 2010 were as follows:

|   | <u>Unrestricted</u>  | <u>Temporarily<br/>Restricted</u> | <u>Permanently<br/>Restricted</u> | <u>Total</u>         |
|---|----------------------|-----------------------------------|-----------------------------------|----------------------|
| <b>Endowment net assets at June 30, 2010</b>                        | \$189,712,978        | \$ 30,059,074                     | \$ 28,751,431                     | \$248,523,483        |
| Investment return   |                      |                                   |                                   |                      |
| Investment income   | 1,306,930            | 304,068                           |                                   | 1,610,998            |
| Net appreciation (realized and unrealized)                          | <u>28,528,553</u>    | <u>6,365,614</u>                  |                                   | <u>34,894,167</u>    |
| Total investment return   | 29,835,483           | 6,669,682                         | -                                 | 36,505,165           |
| Gifts   | 2,692,559            |                                   | 1,746,874                         | 4,439,433            |
| Endowment return allocated for spending                             | (9,640,042)          | (2,242,834)                       |                                   | (11,882,876)         |
| Unspent current year revenue allocation                             |                      | 48,645                            |                                   | 48,645               |
| Recovery of amounts transferred to restore<br>underwater endowments | <u>497,246</u>       | <u>(497,246)</u>                  |                                   | <u>-</u>             |
| <b>Endowment net assets at June 30, 2011</b>                        | 213,098,224          | 34,037,321                        | 30,498,305                        | 277,633,850          |
| Nonendowment net assets   | <u>48,031,294</u>    | <u>22,489,315</u>                 | -                                 | <u>70,520,609</u>    |
| Total net assets at June 30, 2011                                   | <u>\$261,129,518</u> | <u>\$ 56,526,636</u>              | <u>\$ 30,498,305</u>              | <u>\$348,154,459</u> |

|   | <u>Unrestricted</u>  | <u>Temporarily<br/>Restricted</u> | <u>Permanently<br/>Restricted</u> | <u>Total</u>         |
|---|----------------------|-----------------------------------|-----------------------------------|----------------------|
| <b>Endowment net assets at June 30, 2009</b>                        | \$176,973,847        | \$ 28,025,133                     | \$ 26,494,433                     | \$231,493,413        |
| Investment return   |                      |                                   |                                   |                      |
| Investment income   | 4,569,334            | 1,681,160                         |                                   | 6,250,494            |
| Net appreciation (realized and unrealized)                          | <u>14,786,785</u>    | <u>4,018,083</u>                  |                                   | <u>18,804,868</u>    |
| Total investment return   | 19,356,119           | 5,699,243                         | -                                 | 25,055,362           |
| Gifts   | 502,754              |                                   | 2,256,998                         | 2,759,752            |
| Endowment return allocated for spending                             | (7,976,202)          | (2,934,623)                       |                                   | (10,910,825)         |
| Unspent current year revenue allocation                             |                      | 125,781                           |                                   | 125,781              |
| Recovery of amounts transferred to restore<br>underwater endowments | <u>856,460</u>       | <u>(856,460)</u>                  |                                   | <u>-</u>             |
| <b>Endowment net assets at June 30, 2010</b>                        | 189,712,978          | 30,059,074                        | 28,751,431                        | 248,523,483          |
| Nonendowment net assets   | <u>40,470,087</u>    | <u>22,897,846</u>                 | -                                 | <u>63,367,933</u>    |
| Total net assets at June 30, 2010                                   | <u>\$230,183,065</u> | <u>\$ 52,956,920</u>              | <u>\$ 28,751,431</u>              | <u>\$311,891,416</u> |

# Rhode Island School of Design

## Notes to the Financial Statements

### June 30, 2011 and 2010

---

The following provides additional information about the School's policies regarding the management of its endowment assets.

#### **Endowment Funds with Deficits**

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the value of the initial and subsequent donor gift amounts ("underwater"). When donor endowment deficits exist, they are classified as a reduction of unrestricted net assets. The total amount of endowment funds underwater was \$400,265 and \$897,511 as of June 30, 2011 and June 30, 2010, respectively. As the restricted endowment funds begin to recover, the School records income for the amounts originally transferred to restore the underwater endowments. Nonoperating Income of \$497,246 and \$856,460 was recorded in unrestricted net assets as of June 30, 2011 and June 30, 2010, respectively. These results are directly driven by market fluctuations.

#### **Return Objectives and Risk Parameters**

The School has adopted endowment investment and spending policies that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of endowment assets. Under this policy, the return objective for the endowment assets, measured over a full market cycle of approximately five years, is to maximize the return against various market indexes across the investment portfolio as determined by the Investment Committee while minimizing risk. The goal of each investment manager over the investment horizon is to exceed the appropriate market index. The overall portfolio is intended to embody no greater risk than the risk of a blend of the indexes assigned to the managers. Further, to achieve a prudent level of portfolio diversification, the securities of any one company or governmental agency does not exceed 5% of the total fund, and no more than 10% of the total fund is invested in any one industry.

#### **Strategies Employed for Achieving Investment Objectives**

To achieve its long-term rate of return objectives, the School relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized gains) and current yield (interest and dividends).

#### **Endowment Spending Allocation and Relationship of Spending Policy to Investment Objectives**

The Board of Trustees of the School determines the method to be used to appropriate endowment funds for expenditure. In 2011, the spending policy was to spend the amount equal to the debt service plus an additional \$975,000 to be used for strategic needs in enrollment and institutional engagement. In 2010, the spending policy was suspended by the Board of Trustees and the endowment draw was set to an amount equal to debt service. The Board of Trustees plans to return to a formulaic spending policy in 2012.

**Rhode Island School of Design**  
**Notes to the Financial Statements**  
**June 30, 2011 and 2010**

---

**5. Accounts Receivable**

Accounts receivable consisted of the following at June 30:

|  | <b>2011</b>         | <b>2010</b>         |
|--|---------------------|---------------------|
| Student tuition and fees                   | \$ 943,869          | \$ 1,033,207        |
| Computer loan programs                     | 1,043,803           | 1,196,389           |
| Government grants                          | 1,430,236           | 146,840             |
| Other                                      | 614,253             | 580,775             |
|  | <u>4,032,161</u>    | <u>2,957,211</u>    |
| Less: Allowance for uncollectible accounts | <u>(327,063)</u>    | <u>(447,502)</u>    |
|  | <u>\$ 3,705,098</u> | <u>\$ 2,509,709</u> |

**6. Pledges Receivable**

Pledges receivable at June 30 are expected to be realized in the following periods:

|  | <b>2011</b>         | <b>2010</b>         |
|--|---------------------|---------------------|
| In one year or less                              | \$ 1,490,440        | \$ 2,879,839        |
| Between one year and five years, net of discount | 3,386,773           | 3,892,232           |
| Five years and over, net of discount             | 1,884,586           | 1,600,197           |
|  | <u>6,761,799</u>    | <u>8,372,268</u>    |
| Less: Allowance for uncollectible pledges        | <u>(3,028,104)</u>  | <u>(3,186,350)</u>  |
| Pledges receivable, net                          | <u>\$ 3,733,695</u> | <u>\$ 5,185,918</u> |

Discounts of \$305,268 and \$360,831 for the years ended June 30, 2011 and June 30, 2010, respectively, were calculated using discount factors based on the appropriate U.S. Treasury Bill rates for pledges received prior to the adoption of accounting guidance for *Fair Value Measurements* and using the School's taxable unsecured borrowing rate for pledges received beginning in fiscal 2009.

**7. Student Loan Funds**

The School participates in the Federal Perkins Loan Program. Under existing laws, Perkins loan funds of the United States Government are ultimately refundable to the extent funds are available from the program and are, therefore, shown as a liability on the Statement of Financial Position. Due to the significant restrictions of this program, it is not practical to determine the fair value of such amounts.

Student loans receivable is shown net of an allowance for uncollectible accounts of \$498,747 and \$575,407 at June 30, 2011, and 2010, respectively.

**Rhode Island School of Design**  
**Notes to the Financial Statements**  
**June 30, 2011 and 2010**

---

**8. Bonds Payable and Other Debt**

|  | 2011                  | 2010                  |
|--|-----------------------|-----------------------|
| Rhode Island Health and Education Building Corporation Series 2001, Range 3.5%-5%, original issue \$27,890,000     | \$ 27,443,536         | \$ 27,499,963         |
| Rhode Island Health and Education Building Corporation Series 2004D, Range 3.0%-5.625% original issue \$58,435,000 | 55,180,181            | 56,188,646            |
| Rhode Island Health and Education Building Corporation Series 2008A, Range 1.25%-2.60% original issue \$61,930,000 | 56,455,000            | 58,305,000            |
| Rhode Island Health and Education Building Corporation Series 2008B, Range 1.25%-2.60% original issue \$31,850,000 | 31,850,000            | 31,850,000            |
|  | <u>\$ 170,928,717</u> | <u>\$ 173,843,609</u> |

As of June 30, 2011 and 2010, the unamortized discount on 2001 Bonds amounted to \$71,464 and \$75,037, respectively, which is being amortized over the life of the bonds using the effective interest basis.

As of June 30, 2011 and 2010, the unaccrued premium on 2004D Bonds amounted to \$1,480,181 and \$1,458,646, respectively, which is being accreted over the life of the bonds using the effective interest basis.

**Rhode Island Health and Educational Building Corporation (RIHEBC)**

RIHEBC Bonds (Series 2001) are due in principal amounts and sinking fund requirements ranging from \$60,000 in 2011 to \$645,000 in 2020 for serial bonds and a payment of \$4,445,000 for term bonds due in 2026 and a final payment of \$18,280,000 for term bonds due in 2031. RIHEBC Bonds (Series 2004D) are due in principal amounts and sinking fund requirements ranging from \$900,000 in 2007 to \$9,155,000 in 2035 for serial bonds and a payment of \$10,510,000 for term bonds due in 2028 and a final payment of \$7,555,000 for term bonds due in 2031. RIHEBC Bonds (Series 2008A and Series 2008B) are due in principal amounts and mandatory redemption requirements ranging from \$1,800,000 in 2008 to \$13,945,000 in 2036.

The Municipal Bond Assurance Association insures redemption of Series 2001 bonds. XL Capital Assurance insures redemption of the Series 2004D bonds. Series 2001 Bonds maturing on and after June 1, 2011 are subject to redemption prior to maturity at a redemption price of 100% to 102% of the principal amounts plus accrued interest through the date of redemption. Series 2004D Bonds maturing on and after August 15, 2014 are subject to redemption prior to maturity at a redemption price of 100% of the principal amounts plus accrued interest through the date of redemption.

Series 2008A and Series 2008B Bonds can be optionally redeemed on any interest payment date (the first business day of each month) at par plus accrued interest. In the event that the School receives notice of any optional redemption on its Series 2008A and 2008B variable-rate bonds, the purchase price of the bonds will be paid from the remarketing of such bonds. However, if the

**Rhode Island School of Design**  
**Notes to the Financial Statements**  
**June 30, 2011 and 2010**

---

remarketing proceeds are insufficient, the School will be obligated to purchase the bonds redeemed. On April 29, 2011, the School secured a \$56,455,000 letter of credit with Bank of America to cover an amount up to the outstanding balance of the 2008A bonds at the time of redemption. On June 1, 2011, the School secured a \$31,850,000 letter of credit with TD Bank to cover an amount up to the outstanding balance of the 2008B bonds at the time of redemption. For both Bank of America and TD Bank, any payout is to be repaid immediately or accrue interest. If payout is not made in 90 days, the payout will convert to a term loan, due in five semi-annual installments beginning six months after the conversion date. The original letters of credit expire on June 1, 2016. The College is required to comply with debt covenants from Bank of America and TD Bank to support its Letter of Credit. The debt service ratio must be at least 1.25 to 1 and the liquidity ratio must be at least 0.85 to 1. The School is in compliance with its debt covenant requirements.

The School has pledged as collateral all revenue received in each fiscal year up to an amount equal to the debt service on the bonds due during the fiscal year.

Mandatory annual principal payments due for the next five years and thereafter are as follows:

|                                   | <b>RIHEBC</b>                |
|-----------------------------------|------------------------------|
| 2012                              | \$ 3,055,000                 |
| 2013                              | 3,140,000                    |
| 2014                              | 3,275,000                    |
| 2015                              | 3,420,000                    |
| 2016–2037                         | <u>156,630,000</u>           |
| Annual principal payments         | <u>\$ 169,520,000</u>        |
| Unamortized discount/premium      | <u>1,408,717</u>             |
| Bonds payable as of June 30, 2011 | <u><u>\$ 170,928,717</u></u> |

Estimated fair value of debt was approximately \$172,108,289 and \$175,258,678 at June 30, 2011 and 2010, respectively. Cash paid for interest on long-term debt for the years ended June 30, 2011 and 2010, was \$4,425,835 and \$4,480,277, respectively.

Bond issuance costs are capitalized and amortized over the life of the bond. Unamortized bond issuance costs were \$1,764,769 and \$1,839,767 for the years ended June 30, 2011 and 2010, respectively.

The School has entered into various interest rate swap agreements to manage the interest cost and variable rate risk associated with its outstanding debt. The interest rate swap agreements were not entered into for trading or speculative purposes. The risks associated with interest rate swaps are primarily market risk. Under the terms of these agreements, the School pays a fixed rate, determined at inception, to a third party who in turn pays a variable rate on these respective notional principal amounts to the bondholders.

The School records interest rate swaps at the estimated value at which the swaps could be settled as of June 30, 2011 and 2010. The unrealized appreciation that was recognized for the swaps was \$1,512,819 and unrealized depreciation of \$2,504,411 for the years ending June 30, 2011 and 2010, respectively. The interest rate swap balances are classified as liabilities on the Statement of Financial Position. Net payments or receipts under the swap agreements, along with the change in



**Rhode Island School of Design**  
**Notes to the Financial Statements**  
**June 30, 2011 and 2010**

---

fair value of the swaps, are included in nonoperating revenues on the Statement of Activities and in the cash flows from operating activities on the Statement of Cash Flows.

The estimated fair value of the swap instruments represents the estimated cost to the School to cancel the agreements at the reporting date, which is based on option pricing models that consider risks and market factors. During 2011 and 2010, the School incurred realized losses of \$2,446,471 and \$2,628,806, respectively.

The following schedule presents the notional principal amounts of the School's interest swaps at June 30, 2011.

| <b>Maturity</b>  | <b>Original<br/>Notional</b> | <b>Fair Value at<br/>June 30, 2011</b> |
|------------------|------------------------------|--|
| August 15, 2011  | \$ 9,250,000                 | \$ (9,739)                             |
| February 1, 2020 | 18,000,000                   | (773,136)                              |
| August 15, 2025  | 27,000,000                   | (3,173,616)                            |
| August 15, 2034  | 28,500,000                   | (3,561,945)                            |
|                  |                              | <u>\$ (7,518,436)</u>                  |

In May 2011, the School renewed its 2008 line of credit agreement with Bank of America that expires in June 2012. Under the terms of the agreement the School may borrow up to \$5,000,000. Interest on borrowings under the line of credit was based on the London Inter-Bank Offered (LIBOR) rate plus 0.85%. There was no balance outstanding at the years ended June 30, 2011 and 2010.

**9. Obligations Under Long-Term Agreements**

In June 2007, the School entered into a capital lease for the Charles Landing building. The original lease term was 119 months with an initial obligation of \$7,809,235. Interest is computed using the incremental borrowing rate of 4.27%. The amount outstanding on the capital lease was \$6,370,688 at June 30, 2011.

Minimum annual lease payments due for building over the next five years and thereafter are as follows:

|                              |                     |
|------------------------------|---------------------|
| 2012                         | \$ 1,073,128        |
| 2013                         | 1,122,852           |
| 2014                         | 1,168,832           |
| 2015                         | 1,221,415           |
| 2016-2017                    | <u>3,179,843</u>    |
| Total Minimum Lease Payments | 7,766,070           |
| Interest Expense             | <u>(1,395,382)</u>  |
| Total Obligation             | <u>\$ 6,370,688</u> |

**Rhode Island School of Design**  
**Notes to the Financial Statements**  
**June 30, 2011 and 2010**

---

During fiscal year 2004, the School entered into a long-term agreement with a third party in order to purchase the Center for Integrative Technology building. Prior to June 30, 2010, this agreement was accounted for as period expenses. At June 30, 2010, the School recorded the full amount of the obligation of \$6,387,509. The amount outstanding on the capital lease was \$6,254,935 at June 30, 2011. Based on a variety of assumptions, the current estimation is that the lease will term on or about 2031.

Minimum annual lease payments due for the building over the next five years and thereafter are as follows:

|                              |                     |
|------------------------------|---------------------|
| 2012                         | \$ 363,072          |
| 2013                         | 363,072             |
| 2014                         | 399,379             |
| 2015                         | 399,379             |
| 2016-2031                    | <u>7,405,689</u>    |
| Total Minimum Lease Payments | 8,930,591           |
| Interest Expense             | <u>(2,675,656)</u>  |
| Total Obligation             | <u>\$ 6,254,935</u> |

**10. Property, Plant and Equipment**

|                                   | <b>2011</b>           | <b>2010</b>           |
|-----------------------------------|-----------------------|-----------------------|
| Land and buildings                |                       |                       |
| Educational plant                 | \$ 154,465,794        | \$ 150,956,573        |
| Dormitories and refectory         | 86,541,236            | 85,813,583            |
| Capital lease                     | 7,809,235             | 7,809,235             |
| Administrative and other          | 19,315,170            | 18,704,014            |
| Residences                        | 1,108,088             | 1,046,945             |
| Construction in Progress          | 1,109,724             |                       |
| Land                              | <u>7,911,598</u>      | <u>7,921,618</u>      |
|                                   | 278,260,845           | 272,251,968           |
| Furniture, fixtures and equipment | <u>45,675,064</u>     | <u>42,962,479</u>     |
|                                   | 323,935,909           | 315,214,447           |
| Less: Accumulated depreciation    | <u>(132,405,633)</u>  | <u>(122,740,842)</u>  |
|                                   | <u>\$ 191,530,276</u> | <u>\$ 192,473,605</u> |

**11. Museum**

**Revenues**

The Museum realized service revenue of \$1,411,624 and \$1,703,324, as well as \$920,965 and \$1,204,295 of total return income and gain, and \$1,156,691 and \$1,100,922 of gifts and grants for the years ended June 30, 2011 and 2010, respectively.

# Rhode Island School of Design

## Notes to the Financial Statements

### June 30, 2011 and 2010

---

#### **Collections**

The majority of the School's collections resides in the Museum and consists of artifacts of historical significance, art objects and books that are held for educational, research and curatorial purposes. Each of the items are cataloged, preserved and cared for and activities verifying their existence and assessing their condition are performed periodically. The collections are subject to a policy that requires proceeds from their sales to be used to acquire other items for collections. The School expended \$656,163 and \$683,417 for acquisitions during 2011 and 2010, respectively.

#### **12. Retirement and Pension Plans**

The School participates in the Teachers Insurance and Annuity Association (TIAA), College Retirement Equities Fund (CREF) and Fidelity 403(b) retirement plan for eligible faculty, administrative and staff employees. The School made contributions to the TIAA-CREF retirement plan of approximately \$3,395,362 and \$3,377,214 for the years ended June 30, 2011 and 2010, respectively.

#### **13. Commitments and Contingencies**

Certain of the School's investments in privately held funds included unfunded commitments from private equity. Unfunded commitments totaled \$1,913,143 and \$6,503,261 as of June 30, 2011 and June 30, 2010, respectively. The School expects these funds to be called currently and for a period not to exceed the time limit outlined in each respective investment's Private Placement Memorandum.

In conducting its activities, the School from time to time is the subject of various claims and also has claims against others. In management's opinion, the ultimate resolution of such claims would not have a material adverse or favorable effect on the financial position of the School.

#### **14. Related Parties**

During the year ended June 30, 2011, the School purchased real estate in Ohio in the amount of \$475,170 in order to assist the move of one of its new executives to the Rhode Island area. The School intends to sell the real estate at a future date.

During the years ended June 30, 2011 and June 30, 2010, a small portion of the School's cash balances were held at a bank at which a member of the School's Board served as President.

Additionally, during the years ended June 30, 2011 and June 30, 2010, a member of the School's Board was an executive at an investment management company at which the School held one alternative investment.

Management and the Board of Trustees report and monitor related party transactions in accordance with the School's conflict of interest policy.

**Rhode Island School of Design**  
**Notes to the Financial Statements**  
**June 30, 2011 and 2010**

---

**15. Functional Expenses**

Total expenses of the School by functional classification are as follows:

|                         | <b>2011</b>           | <b>2010</b>           |
|-------------------------|-----------------------|-----------------------|
| Instruction             | \$ 48,634,982         | \$ 48,274,241         |
| Campus support services | 24,448,172            | 24,071,139            |
| Institutional support   | 18,369,746            | 16,800,403            |
| Museum services         | 8,161,973             | 8,236,465             |
| Academic support        | 5,226,124             | 4,917,874             |
| Student support         | 6,156,673             | 5,132,862             |
| Research                | 792,435               | 682,753               |
|                         | <u>\$ 111,790,105</u> | <u>\$ 108,115,737</u> |

**16. Asset Retirement Obligation**

The College presents an asset retirement obligation on its statement of financial position that represents the probability and projected cost to remedy certain environmental hazards in relation to its buildings and boiler systems. The asset retirement obligation was \$3,749,159 and \$3,553,705, at June 30, 2011 and June 30, 2010, respectively.