Rhode Island School of Design

Financial Statements
June 30, 2006 and 2005

PRICEWATERHOUSECOOPERS

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Report of Independent Auditors

To the 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 "College") at June 30, 2006 and 2005, and the 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 College'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.

As further discussed in Note 1 to the accompanying financial statements, the College adopted FASB Interpretation No. 47 *Accounting for Conditional Asset Retirement Obligations* as of June 30, 2006.

PricewaterhouseCoopers LLP

October 4, 2006

Rhode Island School of Design
Statements of Financial Position
June 30, 2006 and 2005

ASSETS	2006	2005
Cash and cash equivalents	$ 5,310,624	$ 8,727,233
Deposits with trustee	2,826,935	68,710,966
Accounts receivable (net)	2,281,638	2,205,630
Student loans receivable (net)	5,275,004	5,708,398
Pledges receivable (net)	13,131,948	12,269,858
Funds held in trust by others	13,022,682	12,392,349
Inventories	1,996,643	1,449,492
Prepaid expenses and deferred charges	3,004,324	3,110,176
Other investments	38,530,924	33,011,162
Investment in interest rate swap	185,933	-
Long-term investments	293,293,069	262,104,319
Property, plant and equipment (net)	141,954,101	71,502,957
	$ 520,813,825	$ 481,192,540
LIABILITIES		
Accounts payable and accrued liabilities	$ 9,088,725	$ 7,444,192
Deferred income	5,705,082	4,904,587
Agency accounts and other liabilities	87,956	71,190
U.S. Government loan funds	3,602,638	3,444,543
Liability for interest rate swap	-	5,118,276
Bonds payable	151,898,943	153,399,348
Asset retirement obligation	2,868,610	-
	173,251,954	174,382,136
NET ASSETS		
Unrestricted net assets		
Board designated funds	20,433,636	11,720,131
Designated for endowment	202,204,837	187,514,627
Other funds	13,156,663	12,438,395
	235,795,136	211,673,153
Temporarily restricted net assets	74,956,615	60,641,127
Permanently restricted net assets	36,810,120	34,496,124
	347,561,871	306,810,404
	$ 520,813,825	$ 481,192,540

The accompanying notes are an integral part of the financial statements

Rhode Island School of Design
Statements of Activities
for the year ended June 30,2006
(with comparative totals for 2005)

	Unrestricted	Temporarily Restricted	Permanently Restricted	2006 Total	2005 Total
Revenues:					
Tuition and fees	$ 71,693,541			$ 71,693,541	$ 68,059,577
Less: School sponsored financial aid	9,072,397			9,072,397	8,715,282
Donor sponsored financial aid	1,414,185			1,414,185	1,499,735
Net tuition	61,206,959			61,206,959	57,844,560
Campus support services	15,909,649			15,909,649	11,994,787
Total return income and gain used for operations	7,996,382			7,996,382	7,225,757
Gifts,Grants and pledges	958,862			958,862	933,765
Museum services	1,201,621			1,201,621	1,139,668
Other income	945,441			945,441	500,680
Net assets released from restrictions	7,462,947			7,462,947	3,870,075
	95,681,861			95,681,861	83,509,292
Operating expenses:					
Instruction	33,580,288 ✓			33,580,288	32,146,407
Academic support	6,218,975 ✓			6,218,975	5,791,138
Campus support services	10,215,203			10,215,203	8,827,854
Institutional support	14,473,668			14,473,668	12,671,323
Museum services	5,922,414			5,922,414	5,135,261
Student services	2,959,483			2,959,483	3,157,110
Plant maintenance	8,415,165			8,415,165	6,600,131
Interest	5,478,182			5,478,182	5,029,500
Depreciation	7,369,814			7,369,814	6,241,588
Research	626,280			626,280	516,265
	95,259,472			95,259,472	86,116,577
(Deficit) Surplus before budgetary designations	422,389			422,389	(2,607,285)
Net budgetary designations (Note 1)	(383,518)			(383,518)	3,309,939
Operating surplus	$ 38,871			$ 38,871	$ 702,654
Non operating:					
Investment income	$ 252,800	$ 517,106		$ 769,906	$ 2,448,777
Other investment income	421,421			421,421	1,868,786
Net realized and unrealized income/(loss) on interest rate swap	4,855,304			4,855,304	(5,259,454)
Gain on sale of assets	537,702			537,702	
Realized and unrealized gain on investments	18,518,186	4,228,284	1,052,291	23,798,761	15,997,824
Gifts and grants for capital purposes	1,478,968	17,033,045	1,261,705	19,773,718	7,830,318
Non operating assets allocated for budgetary designations	383,518			383,518	(3,309,939)
Net assets released from restrictions		(7,462,947)		(7,462,947)	(3,870,075)
Increase in net assets from nonoperating activities	26,447,899	14,315,488	2,313,996	43,077,383	15,706,237
Cumulative effect of change in accounting principle (Note 1)	(2,364,787)			(2,364,787)	
Total increase in net assets	24,121,983	14,315,488	2,313,996	40,751,467	16,408,891
Total net assets at the beginning of the year	211,673,153	60,641,127	34,496,124	306,810,404	290,401,513
Total	$ 235,795,136	$ 74,956,615	$ 36,810,120	$ 347,561,871	$ 306,810,404

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

Rhode Island School of Design
Statements of Activities
for the year ended June 30, 2005

	Unrestricted	Temporarily Restricted	Permanently Restricted	2005 Total
Revenues:				
Tuition and fees	$ 68,059,577			$ 68,059,577
Less: University sponsored financial aid	8,715,282			8,715,282
Donor sponsored financial aid	1,499,735			1,499,735
Net tuition	57,844,560			57,844,560
Campus support services	11,994,787			11,994,787
Total return income and gain used for operations	7,225,757			7,225,757
Gifts,Grants and pledges	933,765			933,765
Museum services	1,139,668			1,139,668
Other income	500,680			500,680
Net assets released from restrictions	3,870,075			3,870,075
	83,509,292			83,509,292
Operating expenses:				
Instruction	32,146,407			32,146,407
Campus support services	8,827,854			8,827,854
Institutional support	12,671,323			12,671,323
Museum services	5,135,261			5,135,261
Academic support	5,791,138			5,791,138
Student services	3,157,110			3,157,110
Plant maintenance	6,600,131			6,600,131
Interest	5,029,500			5,029,500
Depreciation	6,241,588			6,241,588
Research	516,265			516,265
	86,116,577			86,116,577
(Deficit) Surplus before budgetary designations	(2,607,285)			(2,607,285)
Net budgetary designations (Note 1)	3,309,939			3,309,939
Operating surplus	$ 702,654			$ 702,654
Non operating:				
Investment income	$ 1,807,932	$ 640,845		$ 2,448,777
Other investment income	1,868,786			1,868,786
Net realized and unrealized loss on interest rate swap	(5,259,454)			(5,259,454)
Gain on sale of assets				
Realized and unrealized gain on investments	11,423,565	3,108,299	1,465,960	15,997,824
Loss on early extinguishment of debt				
Gifts and grants for capital purposes	476,089	5,954,966	1,399,263	7,830,318
Non operating assets allocated for budgetary designations	(3,309,939)			(3,309,939)
Net assets released from restrictions		(3,870,075)		(3,870,075)
Increase in net assets from nonoperating activities	7,006,979	5,834,035	2,865,223	15,706,237
Total increase in net assets	7,709,633	5,834,035	2,865,223	16,408,891
Total net assets at the beginning of the year	203,963,520	54,807,092	31,630,901	290,401,513
Total net assets at the end of the year	$ 211,673,153	$ 60,641,127	$ 34,496,124	$ 306,810,404

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

Rhode Island School of Design
Statements of Cash Flows
for the years ended June 30, 2006 and 2005

	2006	2005
Cash flows from operating activities:		
Change in net assets	$ 40,751,467	$ 16,408,891
Adjustments to reconcile change in net assets to net cash used by operating activities:		
Gain on investments	(29,962,881)	(21,104,576)
Net realized and unrealized loss on interest rate swap	(5,304,209)	3,919,103
Depreciation and amortization	7,519,409	6,204,324
Gift in kind	(7,120,000)	-
Gain on the sale of asset	(537,702)	-
Cumulative effect of change in accounting principle (Note 1)	2,364,787	-
Changes in working capital:		
Increase in accounts receivable	(76,008)	(267,450)
Increase in pledges receivable	(862,090)	(1,346,503)
Increase in funds held in trust by others	(630,333)	(340,104)
Increase in inventories	(547,151)	(84,100)
Decrease in prepaid expenses and deferred charges	105,852	465,343
Increase (Decrease) in accounts payable and accrued expenses	(260,700)	955,742
Increase in agency accounts and other liabilities	16,766	5
Increase in deferred income	800,495	517,890
Reclassification of contributions for long-term purposes	(6,827,666)	(1,749,263)
Net cash (used for) provided by operating activities	(569,964)	3,579,302
Cash flows for investing activities:		
Purchase of buildings and equipment	(68,773,288)	(9,946,620)
Proceeds from sale of building	1,019,088	-
Decrease in deposits with trustee	65,884,031	9,026,644
Student loans granted	(1,873,360)	(1,994,296)
Collection of student loans	2,306,754	2,064,264
Purchase of investments	(184,760,299)	(76,465,651)
Sale of investments	178,014,668	74,537,579
Net cash used in investing activities	(8,182,406)	(2,778,080)
Cash flows from financing activities:		
Increase in U.S. Government loan funds	158,095	59,424
Payments on long-term debt	(1,650,000)	(45,000)
Reclassification of contributions for long-term purposes	6,827,666	1,749,263
Net cash provided by financing activities	5,335,761	1,763,687
Net increase in cash and cash equivalents	(3,416,609)	2,564,909
Cash and cash equivalents at beginning of the year	8,727,233	6,162,324
Cash and cash equivalents at end of the year	$ 5,310,624	$ 8,727,233

The accompanying notes are an integral part of the financial statements

1. **Summary of Significant Accounting Policies:**

The financial statements of the Rhode Island School of Design (the "School") have been prepared on the accrual basis of accounting and in accordance with the reporting principles of not-for-profit accounting. Certain amounts presented in the prior year financial statements have been reclassified to conform with current year presentation.

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

- 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. Pursuant to Rhode Island General Law, the School has added sufficient net appreciation to the historical gift amounts based on inflation in order to maintain the purchasing power of the original dollar value of the funds.

- Temporarily restricted net assets include gifts, pledges, trusts and remainder interests, 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).

- Unrestricted net assets are not subject to donor imposed stipulations, may be designated for specific purpose by action of the Board of Trustees and include realized and unrealized gains on permanently restricted funds not otherwise subject to donor restrictions or to the extent they exceed amounts added to historical gifts pursuant to the Rhode Island General Law.

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 surpluses/deficits 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 non-expense 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 non-operating 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 2006 and 2005 are as follows:

	2006	2005
Facilities Use Fee	$ (6,461,723)	$ (6,241,588)
Depreciation	7,369,814	6,241,588
Contribution to Principal payments on debt	(1,650,000)	(45,000)
Board Designated or Department Funds availed of	4,590,578	2,821,484
Board Designated Funds availed of for Campaign expenses	(4,232,187)	553,455
Student Loans	0	(20,000)
Net Budgetary Designation	$ (383,518)	$ 3,309,939

Non Operating

Non operating revenue includes 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, 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 market 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, 2006 and 2005. Alternative investments include limited partnerships, limited liability corporations 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 market.

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 market 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 market 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 store.

Spending Policy

The School operates on a total return concept. Under this concept, income from long-term investments is available for expenditure based on a rate of 5% of the twelve-quarter moving average of the market value of the endowment portfolio. Since the spending formula is based on the total return concept, earnings from realized gains may be utilized when current year income from interest and dividends is less than the authorized spending amount.

Property, Plant and Equipment

Property, plant and equipment is stated at acquisition cost or the fair market value as of the date of the gift, net of accumulated depreciation (See Note 7). 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 (see Note 12) 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 operations.

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 permanently 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.

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.

New Accounting Standards

In March 2005, the FASB issued FIN 47, "Accounting for Conditional Asset Retirement Obligations," which clarifies that the term "conditional asset retirement obligation" as used in SFAS 143 refers to a legal obligation to perform an asset retirement activity when the timing and/or method of settlement are conditional on a future event that may or may not be in the control of the entity. This legal obligation is absolute, despite the uncertainty regarding the timing and/or method of settlement. In addition, the fair value of a liability for the conditional asset retirement obligation should be recognized when incurred (generally upon acquisition, construction or development) if the liability's fair value can be reasonably estimated.

The School adopted FIN 47 effective June 30, 2006. Upon adoption, the School recorded asset retirement obligations of $2,868,610 in the statement of financial position and $2,364,787 as the cumulative effect of a change in accounting principle, included in the statement of activities. Had FIN 47 been adopted as of fiscal year 2005, the total depreciation and interest accretion costs for the years ended June 30, 2006 and 2005, would not have been material. The asset retirement obligations will be adjusted on an ongoing basis due to the passage of time, new laws and regulations and revisions to either the timing or amounts of original estimates.

Rhode Island School of Design

Notes to the Financial Statements for the Year Ended June 30, 2006 and 2005

2. Investments:

The cost and market value of investments at June 30, 2006 and 2005 were as follows:

2006	Cost	Market
Pooled and mutual funds	$42,316,056	$42,316,054
Common and preferred stocks	104,182,008	129,979,910
Fixed income securities	32,693,891	31,172,477
Alternative investments	80,406,683	126,394,758
Split interest agreements	1,960,794	1,960,794
	$261,559,432	$331,823,993

2005	Cost	Market
Pooled and mutual funds	$36,548,630	$36,548,630
Common and preferred stocks	106,122,143	127,378,204
Fixed income securities	32,846,208	32,675,754
Alternative investments	65,020,434	97,237,082
Split interest agreements	1,275,811	1,275,811
	$241,813,226	$295,115,481

Investment income for the years ended June 30, 2006 and 2005 was as follows:

2006	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Interest and dividend income	$2,085,062	$517,106	-	$2,602,168
Realized gains	11,620,893	1,379,682	-	13,000,575
Increase in net unrealized gains	13,061,413	2,848,602	$1,052,291	16,962,306
Total investment return	$26,767,368	$4,745,390	$1,052,291	$32,565,049

2005	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Interest and dividend income	$3,926,937	$640,845	-	$4,567,782
Realized gains	8,464,324	2,188,608	-	10,652,932
Increase in net unrealized gains	8,065,993	919,691	$1,465,960	10,451,644
Total investment return	$20,457,254	$3,749,144	$1,465,960	$25,672,358

The School earned $29,962,881 of realized and unrealized gains during fiscal year 2006 of which $6,164,120 was utilized in order to meet the spending formula used in operations. In 2005 the School earned $21,104,576 of realized and unrealized gains of which $5,106,752 was utilized to meet the spending formula.

Investment management fees (netted from interest and dividend income) totaled $1,848,477 and $1,304,866 in 2006 and 2005, respectively.

Certain net assets are pooled for investment income purposes. The unit market value at June 30, 2006 and 2005 was $264.56 and $239.58 respectively. The market value of long-term investments as stated in the Statement of Financial Position represents the value of pooled endowment at June 30, 2006 and 2005.

3. Accounts Receivable:

Accounts receivable consisted of the following at June 30:

	2006	2005
Government grants	$ 10,949	$ 32,121
Computer loan programs	1,139,638	1,209,287
Student tutition and fees	794,095	805,174
Notes receivable from related party	300,000	300,000
Interest receivable	33,850	11,772
Other	359,499	152,641
Total	$ 2,638,031	$ 2,510,995
Less: allowance for uncollectible accounts	(356,393)	(305,365)
Total	$ 2,281,638	$ 2,205,630

4. Pledges Receivable:

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

	2006	2005
In one year or less	$ 4,099,684	$ 4,056,210
Between one year and five years, net of discount	6,834,722	5,878,442
Five years and over, net of discount	3,299,923	3,330,910
Total	$ 14,234,329	$ 13,265,562
Less: allowance for uncollectible pledges	(1,102,381)	(995,704)
Pledges receivable, net	$ 13,131,948	$ 12,269,858

Discount to present value was calculated using a discount factor based on US Treasury note rates for the respective pledges. The discount was $623,269 and $479,280 for 2006 and 2005 respectively.

5. 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 $383,630 and $422,275 at June 30, 2006, and 2005, respectively.

6. Bonds Payable:

	2006	2005
Rhode Island Health and Education Building Corporation Series 2001, Range 3.3%-5%, original issue $27,890,000	$27,705,670	$27,752,097
Rhode Island Health and Education Building Corporation Series 2004A, Range 2.%-3.85% original issue $28,500,000	28,500,000	28,500,000
Rhode Island Health and Education Building Corporation Series 2004B, Range 2.%-3.85% original issue $27,000,000	26,825,000	27,000,000
Rhode Island Health and Education Building Corporation Series 2004C, Range 3.11%-4.95% original issue $10,675,000	9,250,000	10,675,000
Rhode Island Health and Education Building Corporation Series 2004D, Range 2.5%-5.625% original issue $58,435,000	59,618,273	59,472,251
Total	$151,898,943	$153,399,348

As of June 30, 2006 and 2005 the unamortized discount on 2001 Bonds amounted to $89,329 and $92,903 respectively, which is being amortized over the life of the bond using the effective interest basis.

As of June 30, 2006 and 2005 the unaccreted premium on 2004D Bonds amounted to $1,183,272 and $1,037,251 respectively, which is being accreted over the life of the bond 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 $50,000 in 2007 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 2004A) are due in principal amounts and sinking fund requirements ranging from $3,300,000 in 2031 to $8,750,000 in 2034 for tax-exempt term bonds. RIHEBC Bonds (Series 2004B) are due in principal amounts and sinking fund requirements ranging from

$200,000 in 2007 to $2,375,000 in 2026 for tax-exempt term bonds. RIHEBC Bonds (Series 2004C) are due in principal amounts and sinking fund requirements ranging from $1,450,000 in 2007 to $1,700,000 in 2012 for taxable term bonds. 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. The Municipal Bond Assurance Association insures redemption of Series 2001 bonds. XL Capital Assurance insures redemption of all the 2004 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 2004A, 2004B, and 2004C Bonds maturing on and after August 15, 2015 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 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.

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 payment due for the next five years and thereafter are as follows:

	RIHEBC
2007	$ 2,515,000
2008	2,605,000
2009	2,700,000
2010	2,805,000
2011-2035	140,180,000
	$ 150,805,000

At June 30, 2006 estimated fair value of debt was approximately $153,635,220 and at June 30, 2005 carrying value of debt approximated fair value. Cash paid for interest on long-term debt for the years ended June 20, 2006 and 2005 was $5,672,372 and $6,555,034, respectively.

The School capitalizes the interest cost related to outstanding debt on qualifying assets. Interest costs capitalized for the years ended June 30, 2006 and 2005 totaled $1,083,363 and $597,760, respectively.

Bond issuance costs are capitalized and amortized over the life of the bond. Unamortized bond issuance costs were $2,724,478 and $2,839,783 for the years ended June 30, 2006 and 2005, respectively.

During 2004 the School entered into various interest 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. 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 swaps at the estimated value at which the swaps could be settled as of June 30, 2006 and 2005. The unrealized (appreciation) and depreciation that was recognized for the swaps was ($5,304,647) and $3,919,103 for the years ending June 30, 2006 and 2005, respectively. Net payments or receipts under the swap agreements along with the change in fair value of the swaps are included in non-operating revenues on the statement of activities. During 2006 and 2005 the School incurred a realized loss on the swaps of $449,343 and $1,340,351, respectively.

The estimated fair value of the interest rate swaps was computed by a third-party. The 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.

The following schedule presents the notional principal amounts of the School's interest swaps at June 30, 2006.

Bond Issue	Maturity	Original Notional Amount	Fair Value at June 30, 2006
Series 2004C	Aug. 15, 2011	$ 9,250,000	$ 1,790
Series 2004B	Aug. 15, 2025	27,000,000	109,509
Series 2004A	Aug. 15, 2034	28,500,000	(1,028,210)
Series 2004A	Aug. 15, 2034	28,500,000	1,102,844
Total Asset			$ 185,933

7. Property, Plant and Equipment

Property, plant and equipment included the following at June 30, 2006.

	2006	2005
Land and buildings:		
Educational plant	63,090,729	$ 60,390,330
Dormitories and refectory	83,079,587	29,584,499
Administrative and other	17,552,173	17,291,142
Residences	884,426	879,680
Construction in progress	25,006,309	8,851,216
Land	6,130,556	3,176,060
Total	195,743,780	120,172,927
Furniture, fixtures and equipment	32,059,343	29,483,389
Total	$ 227,803,123	$ 149,656,316
Less: accumulated depreciation	(85,849,022)	(78,153,359)
	$ 141,954,101	$ 71,502,957

$1,905,233 was accrued for capital expenditures at June 30, 2006.

8. Museum:

Revenues

The Museum realized service revenue of $1,201,621 and $1,139,668 as well as $1,059,217and $1,048,433 of total return income and gain and $276,692 and $164,186 of gifts and grants for the years ended June 30, 2006, and 2005 respectively.

Collections

The majority of the School's collection 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 $677,332 and $394,997 for acquisitions during 2006 and 2005 respectively.

9. Retirement and Pension Plans:

The School participates in the Teachers Insurance and Annuity Association (TIAA) and College Retirement Equities Fund (CREF) 403(b) retirement plan for eligible faculty, administrative and staff employees. The School made contributions to the TIAA-CREF retirement plan of approximately $3,185,582 and $3,123,546 for the years ended June 30, 2006 and 2005, respectively.

10. Commitments and Contingencies:

During fiscal year 2003, the School entered into an agreement with the City of Providence to provide a financial contribution in lieu of taxes on newly acquired properties as specified by the agreement. As of June 30, 2006 the School had no outstanding commitment related to the acquisition of new property, and $3,133,160 over the next seventeen years as payments in lieu of taxes. Payments of $3,204,000 and $1,602,000 were made in fiscal year 2006 and fiscal year 2005, respectfully.

Certain of the School's investments in privately held funds included unfunded commitments. As of June 30, 2006, unfunded commitments totaled $12,215,323.

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.

The school has four established employee bargaining units (Full-Time Faculty, Part-Time Faculty, Public Safety Officers and Museum Guards) and is currently negotiating a contract renewal with one of them.

11. Related Party Note:

During fiscal 2005, the School issued a secured note in the amount of $300,000 to a related party in accordance with IRS Regulation 1.7872.5T(c)(1)(i).

Certain members of the School's Board are executives with institutions which provide services to the School. A small portion of the School's cash balances are held at a bank at which a member of the School's Board serves as President. A member of the School's Board is an Executive at the counterparty to the School's investment in interest rate swaps to which net (receipts) and payments of ($4,855,304) and $5,259,454 were made during the years ended June 30, 2006 and 2005, respectively. The procurement of these services is performed in accordance with the School's established policies and procedures. Management and the Board of Trustees report and monitor related party transactions in accordance with the School's conflict of interest policy.

12. <u>Functional Expenses:</u> Total expenses of the School by functional classification are as follows:

	2006	**2005**
Instruction	$42,984,912	$40,455,980
Campus Support Services	16,917,243	14,770,990
Institutional Support	16,183,731	13,244,187
Museum Servcies	7,791,770	6,789,989
Academic Support	7,370,790	6,806,026
Student Support	3,384,746	3,533,140
Research	626,280	516,265
Total	$95,259,472	$86,116,577

13. Subsequent Events:

On July 6, 2006 the School issued two new series of variable rate debt totaling $39.5 million, as follows:

Series	Title	Principal
2006 A	Higher Education Facility Revenue Bonds	$31,550,000
2006 B	Higher Education Facility Revenue Refunding Bonds	$ 7,950,000

A portion of the proceeds of the issuance was used to repay the $9,250,000 of Series 2004C Rhode Island Health and Education Building Corporation Bonds outstanding at June 30, 2006. The remainder will be used to finance the acquisition, construction, conversion, renovation, expansion, equipping, replacement and furnishing of various capital improvements to the School.

In connection with the debt issuance of Series 2006 B, the School entered into an interest rate swap agreement to manage the interest cost and variable rate risk. Under the terms of the agreement, the School pays a fixed rate to a third party who in turn pays a variable rate on this notional principal amount to the bondholders.