

Rhode Island School of Design

Financial Statements

For the Year Ended June 30, 2005

**(with comparative totals for the
Year Ended June 30, 2004)**

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 changes in net assets and cash flows, present fairly, in all material respects, the financial position of Rhode Island School of Design (the "School") at June 30, 2005 and 2004, 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 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

September 26, 2005

**Rhode Island School of Design
Statements of Financial Position
June 30, 2005 and 2004**

ASSETS	2005	2004
Cash and cash equivalents	\$ 8,727,233	\$ 6,162,324
Other investments	33,011,162	29,540,203
Deposits with trustee	68,710,966	77,737,610
Accounts receivable (net)	2,205,630	1,938,180
Student loans receivable (net)	5,708,398	5,778,366
Pledges receivable (net)	12,269,858	10,923,355
Funds held in trust by others	12,392,349	12,052,245
Inventories	1,449,492	1,365,392
Prepaid expenses and deferred charges	3,110,176	3,575,519
Long-term investments	262,104,319	242,542,630
Property, plant and equipment (net)	71,502,957	67,797,925
	\$ 481,192,540	\$ 459,413,749
 LIABILITIES		
Accounts payable and accrued liabilities	\$ 7,444,192	\$ 6,488,450
Deferred income	4,904,587	4,386,697
Agency accounts and other liabilities	71,190	71,185
U.S. Government loan funds	3,444,543	3,385,119
Liability for interest rate swap	5,118,276	1,199,173
Bonds payable	153,399,348	153,481,612
	174,382,136	169,012,236
 NET ASSETS		
Unrestricted net assets		
Designated for departmental purposes	1,176,199	1,192,241
Board designated funds	11,720,131	8,403,725
Student loans	3,241,824	3,100,455
Plant funds	8,020,372	14,039,363
Designated for endowment	187,514,627	177,227,736
	211,673,153	203,963,520
Temporarily restricted net assets	60,641,127	54,807,092
Permanently restricted net assets	34,496,124	31,630,901
	306,810,404	290,401,513
	\$ 481,192,540	\$ 459,413,749

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
(with comparative totals for 2004)

	Unrestricted	Temporarily Restricted	Permanently Restricted	2005 Total	2004 Total
Revenues:					
Tuition and fees	\$ 68,059,577			\$ 68,059,577	63,883,354
Less: University sponsored financial aid	8,715,282			8,715,282	8,035,277
Donor sponsored financial aid	1,499,735			1,499,735	1,401,818
Net tuition	57,844,560			57,844,560	54,446,259
Campus support services	11,994,787			11,994,787	11,566,485
Total return income and gain used for operations	7,225,757			7,225,757	7,890,587
Gifts, Grants and pledges	933,765			933,765	846,590
Museum services	1,139,668			1,139,668	1,028,465
Other interest income	230,364			230,364	172,282
Other income	270,316			270,316	439,366
Net assets released from restrictions	3,870,075			3,870,075	4,448,251
	<u>83,509,292</u>			<u>83,509,292</u>	<u>80,838,285</u>
Operating expenses:					
Instruction	32,148,407			32,148,407	30,682,480
Campus support services	8,827,854			8,827,854	8,624,791
Institutional support	12,671,323			12,671,323	12,231,757
Museum services	5,135,261			5,135,261	5,114,403
Academic support	5,791,138			5,791,138	5,860,102
Student services	3,157,110			3,157,110	3,112,037
Plant maintenance	6,600,131			6,600,131	6,074,264
Interest	5,029,500			5,029,500	2,309,808
Depreciation	6,241,588			6,241,588	6,059,977
Research	516,265			516,265	394,498
	<u>86,116,577</u>			<u>86,116,577</u>	<u>80,464,117</u>
(Deficit) Surplus before budgetary designations	(2,607,285)			(2,607,285)	374,168
Net budgetary designations (Note 1)	3,309,939			3,309,939	(309,998)
Operating surplus	\$ 702,654			\$ 702,654	64,170
Non operating:					
Investment income	\$ 1,807,932	\$ 640,845		\$ 2,448,777	1,493,979
Other investment income	1,868,786			1,868,786	(1,442,285)
Net realized and unrealized loss on interest rate swap	(5,259,454)			(5,259,454)	2,064,630
Gain on sale of assets					
Realized and unrealized gain on investments	11,423,565	3,108,299	1,465,960	15,997,824	28,206,732
Loss on early extinguishment of debt					(5,003,071)
Gifts and grants for capital purposes	476,089	5,954,966	1,399,263	7,830,318	11,748,205
Non operating assets allocated for budgetary designations	(3,309,939)			(3,309,939)	309,998
Net assets released from restrictions		(3,870,075)		(3,870,075)	(4,448,251)
Increase in net assets from nonoperating activities	7,006,979	5,834,035	2,865,223	15,706,237	32,929,937
Total increase in net assets	7,709,633	5,834,035	2,865,223	16,408,891	32,994,107
Total net assets at the beginning of the year	203,963,520	54,807,092	31,630,901	290,401,513	257,407,406
Total net assets at the end of the year	<u>\$ 211,673,153</u>	<u>\$ 60,641,127</u>	<u>\$ 34,496,124</u>	<u>\$ 306,810,404</u>	<u>290,401,513</u>

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, 2004**

	Unrestricted	Temporarily Restricted	Permanently Restricted	2004 Total
Revenues:				\$ 63,883,354
Tuition and fees	\$ 63,883,354			8,035,277
Less: University sponsored financial aid	8,035,277			1,401,818
Donor sponsored financial aid	1,401,818			54,446,259
Net tuition	54,446,259			11,566,485
Campus support services	11,566,485			7,890,587
Total return income and gain used for operations	7,890,587			846,590
Gifts, Grants and pledges	846,590			1,028,465
Museum services	1,028,465			172,282
Other interest income	172,282			439,366
Other income	439,366			4,448,251
Net assets released from restrictions	4,448,251			80,838,285
	80,838,285			30,682,480
Operating expenses:				30,682,480
Instruction	30,682,480			8,624,791
Campus support services	8,624,791			12,231,757
Institutional support	12,231,757			5,114,403
Museum services	5,114,403			5,860,102
Academic support	5,860,102			3,112,037
Student services	3,112,037			6,074,264
Plant maintenance	6,074,264			2,309,808
Interest	2,309,808			6,059,977
Depreciation	6,059,977			394,498
Research	394,498			80,464,117
	80,464,117			374,168
Surplus before budgetary designations	374,168			(309,998)
Net budgetary designations (Note 1)	(309,998)			64,170
Operating surplus	\$ 64,170			\$ 1,493,979
Non operating:				\$ 1,493,979
Investment income	\$ 972,975	\$ 521,004		(1,442,285)
Net realized and unrealized loss on interest rate swap	(1,442,285)			2,064,630
Gain on sale of assets	2,064,630			28,206,732
Realized and unrealized (loss) gain on investments	22,540,898	3,699,868	1,965,966	(5,003,071)
Loss on early extinguishment of debt	(5,003,071)			11,748,205
Gifts and grants for capital purposes	1,208,378	8,550,685	1,989,142	309,998
Non operating assets allocated from budgetary designations	309,998			(4,448,251)
Net assets released from restrictions		(4,448,251)		32,929,937
Increase in net assets from nonoperating activities	20,651,523	8,323,306	3,955,108	32,994,107
Total increase in net assets	20,715,693	8,323,306	3,955,108	257,407,406
Total net assets at the beginning of the year	183,247,827	46,483,786	27,675,793	290,401,513
Total net assets at the end of the year	\$ 203,963,520	\$ 54,807,092	\$ 31,630,901	\$ 290,401,513

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

**Rhode Island School of Design
Statements of Cash Flows
for the years ended June 30, 2005 and 2004**

	2005	2004
<u>Cash flows from operating activities:</u>		
Change in net assets	\$ 16,408,891	\$ 32,994,107
Adjustments to reconcile change in net assets to net cash used by operating activities:		
Gain on investments	(21,104,576)	(33,653,423)
Net realized and unrealized loss on interest rate swap	3,919,103	1,199,173
Depreciation and amortization	6,204,324	6,914,497
Changes in working capital:		
Increase in accounts receivable	(267,450)	(559,886)
(Increase) Decrease in pledges receivable	(1,346,503)	916,962
Increase in funds held in trust by others	(340,104)	(1,727,314)
(Increase) Decrease in inventories	(84,100)	387,815
Decrease (Increase) in prepaid expenses and deferred charges and other assets	465,343	(1,857,158)
Increase (Decrease) in accounts payable and accrued expenses	955,742	(1,432,919)
Increase (Decrease) in agency	5	(92,303)
Increase in deferred income	517,890	430,787
Reclassification of contributions for long-term purposes	(1,749,263)	(1,989,142)
 Net cash provided by operating activities	 3,579,302	 1,531,196
 <u>Cash flows for investing activities:</u>		
Purchase of buildings and equipment	(9,946,620)	(13,076,711)
Decrease(increase) in deposits with trustee	9,026,644	(73,196,928)
 Student loans granted	(1,994,296)	(1,896,124)
Collection of student loans	2,064,264	1,575,172
Purchase of investments	(76,465,651)	(196,026,618)
Sale of investments	74,537,579	188,018,786
 Net cash used in investing activities	 (2,778,080)	 (94,602,423)
 <u>Cash flows from financing activities:</u>		
Increase in U.S. Government loan funds	59,424	59,438
Payments on long-term debt	(45,000)	(34,340,000)
Proceeds from issuance of long term debt	-	125,689,359
Reclassification of contributions for long-term purposes	1,749,263	1,989,142
 Net cash provided by financing activities	 1,763,687	 93,397,939
 Net increase in cash and cash equivalents	2,564,909	326,712
Cash and cash equivalents at beginning of the year	6,162,324	5,835,612
Cash and cash equivalents at end of the year	\$ 8,727,233	\$ 6,162,324

The accompanying notes are an integral part of the financial statements

Rhode Island School of Design

Notes to the Financial Statements for the Year Ended June 30, 2005 and 2004

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.

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.

Tuition revenue per student, as defined by the School, was \$27,510 and \$25,734 for fiscal year 2005 and 2004, respectively.

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 funds allocated for capital expenditures in excess of depreciation. 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 2005 and 2004 are as follows:

Rhode Island School of Design
Notes to the Financial Statements for the Year Ended June 30, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Facilities Use Fee	\$(6,241,588)	\$(6,059,977)
Depreciation	6,241,588	6,059,977
Contribution to Principal payments on debt	(45,000)	(1,015,000)
Board Designated or Department Funds availed of (deferred)	2,821,484	(634,397)
Board Designated Funds availed of for Campaign expenses	553,455	1,359,399
Student Loans	(20,000)	(20,000)
Net Budgetary Designation	<u>\$ 3,309,939</u>	<u>\$ (309,998)</u>

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 privately held 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, 2005 and 2004. Because investments in privately held 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 all highly liquid investments of maturities with three-months or less when purchased to be cash equivalents. Cash equivalents are stated at cost, which approximates market.

Rhode Island School of Design

Notes to the Financial Statements for the Year Ended June 30, 2005 and 2004

Funds Held in Trust by Others

Funds held in trust by others are held by external trustees, as specified by the donor and are recorded by the School at net present value. Trust income is distributed at least annually to the School in accordance with the terms of the trust and is recorded as investment income. Changes in net present values of the funds held in trust are recorded as restricted gains or losses.

Inventories

Inventories are stated at the lower of cost or market. The School principally uses the retail method for valuing inventories on the first-in, first-out method. Inventory consists primarily of items held for resale by the School's Bookstore.

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 or library book 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 as 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 bookstore, 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 for the Year Ended June 30, 2005 and 2004

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.

2. Investments:

The cost and market value of investments at June 30, 2005 and 2004 were as follows:

	<u>Cost</u>	<u>Market</u>
<u>2005</u>		
Pooled and mutual funds	\$36,548,630	\$36,548,630
Common and preferred stocks	106,122,143	127,378,204
Fixed income securities	38,046,208	37,875,764
Alternative investments	66,597,140	92,037,072
Split interest	1,275,811	1,275,811
	<u>\$248,589,932</u>	<u>\$295,115,481</u>
	<u>Cost</u>	<u>Market</u>
<u>2004</u>		
Pooled and mutual funds	\$20,389,810	\$20,389,810
Common and preferred stocks	91,044,893	110,353,382
Fixed income securities	37,364,333	36,705,392
Alternative investments	86,229,882	103,654,239
Split interest	980,010	980,010
	<u>\$236,008,928</u>	<u>\$272,082,833</u>

Rhode Island School of Design

Notes to the Financial Statements for the Year Ended June 30, 2005 and 2004

Reclassification

Certain amounts related to other investment income in the financial statements for 2004 have been reclassified to conform to the 2005 presentation.

Investment income for the years ended June 30, 2005 and 2004 was as follows:

<u>2005</u>	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	<u>\$20,457,254</u>	<u>\$3,749,144</u>	<u>\$1,465,960</u>	<u>\$25,672,358</u>
<u>2004</u>	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Interest and dividend income	\$3,589,153	\$521,004		\$4,110,157
Realized losses	13,905,882	2,245,275		16,151,157
Increase in net unrealized gains	14,081,707	1,454,593	\$1,965,966	17,502,266
Total investment return	<u>\$31,576,742</u>	<u>\$4,220,872</u>	<u>\$1,965,966</u>	<u>\$37,763,580</u>

The School earned \$21,104,576 of realized and unrealized gains during fiscal year 2005 of which \$5,106,752 was utilized in order to meet the spending formula used in operations. In 2004 the School earned \$33,653,423 of realized and unrealized gains of which \$5,446,691 was utilized to meet the spending formula.

Investment management fees (netted from interest and dividend income) totaled \$1,304,866 and \$1,045,427 in 2005 and 2004, respectively.

Certain net assets are pooled for investment income purposes. The unit market value at June 30, 2005 and 2004 was \$239.58 and \$224.52 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, 2005 and 2004.

Rhode Island School of Design

Notes to the Financial Statements for the Year Ended June 30, 2005 and 2004

3. Accounts Receivable:

Accounts receivable consisted of the following at June 30:

	<u>2005</u>	<u>2004</u>
Government grants	\$ 32,121	\$ 27,830
Computer loan programs	1,209,287	917,970
Student tuition and fees	805,174	649,805
Note receivable from related party	300,000	-
Interest receivable	11,772	3,456
Other	152,641	596,609
Total	<u>\$ 2,510,995</u>	<u>\$ 2,195,670</u>
Less: allowance for uncollectible accounts	(305,365)	(257,490)
Total	<u>\$ 2,205,630</u>	<u>\$ 1,938,180</u>

4. Pledges Receivable:

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

	<u>2005</u>	<u>2004</u>
In one year or less	\$ 4,056,210	\$ 3,935,933
Between one year and five years, net of discount	5,878,442	4,562,368
Five years and over, net of discount	3,330,910	3,288,439
Total	<u>\$ 13,265,562</u>	<u>\$ 11,786,740</u>
Less: allowance for uncollectible pledges	(995,704)	(863,385)
Pledges receivable, net	<u>\$ 12,269,858</u>	<u>\$ 10,923,355</u>

Discount to present value was calculated using a discount factor based on US Treasury note rates for the respective pledges. The discount was \$479,280 and \$419,770 for 2005 and 2004 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.

During 2005, the School made a contribution to the Federal Perkins Loan Fund totaling \$20,000 to increase aid to qualifying students.

Student loans receivable is shown net of an allowance for uncollectible accounts of \$422,275 and \$443,572 at June 30, 2005, and 2004, respectively.

Rhode Island School of Design

Notes to the Financial Statements for the Year Ended June 30, 2005 and 2004

6. Bonds Payable:

	<u>2005</u>	<u>2004</u>
Rhode Island Health and Education Building Corporation Series 2001, Range 3%-5%, original issue \$27,890,000	\$27,752,097	\$27,793,524
Rhode Island Health and Education Building Corporation Series 2004A, variable interest rates range from 1.02%-2.90%, original issue \$28,500,000	28,500,000	28,500,000
Rhode Island Health and Education Building Corporation Series 2004B, variable interest rates range from 1.02%-2.90%, original issue \$27,000,000	27,000,000	27,000,000
Rhode Island Health and Education Building Corporation Series 2004C, variable interest rates range from 1.46%-3.11%, original issue \$10,675,000	10,675,000	10,675,000
Rhode Island Health and Education Building Corporation Series 2004D, Range 2.5%-5.625%, original issue \$58,435,000	<u>59,472,251</u>	<u>59,513,088</u>
Total	<u>\$153,399,348</u>	<u>\$153,481,612</u>

As of June 30, 2005 and 2004 the unamortized discount on 2001 Bonds amounted to \$92,903 and \$96,476 respectively, which is being amortized over the life of the bond using the effective interest basis.

As of June 30, 2005 and 2004 the unaccreted premium on 2004D Bonds amounted to \$1,037,251 and \$1,078,088 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 2006 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 2032 to \$8,750,000 in 2035 for tax-exempt term bonds. RIHEBC Bonds (Series 2004B) are due in principal amounts and sinking fund requirements ranging from \$175,000 in 2006 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 \$1,425,000 in 2006 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 \$890,000 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

Rhode Island School of Design

Notes to the Financial Statements for the Year Ended June 30, 2005 and 2004

interest through the date of redemption. Series 2004A, 2004B, and 2004C Bonds maturing on and after August 15, 2005 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:

	<u>RIHEBC Bonds</u>
2006	\$ 1,650,000
2007	2,515,000
2008	2,605,000
2009	2,700,000
2010 - 2035	<u>142,985,000</u>
	<u>\$ 152,455,000</u>

At June 30, 2005 estimated fair value of debt was approximately \$158,696,790 and at June 30, 2004 carrying value of debt approximated fair value.

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, 2005 and 2004. The unrealized depreciation that was recognized for the swaps was \$3,919,103 and \$1,199,173 for the years ending June 30, 2005 and 2004, 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 2005 and 2004 the School incurred a realized loss on the swaps of \$1,340,351 and \$243,112, respectively.

The estimated fair value of the interest rate swaps was computed by a third-party evaluator. 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, 2005.

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Notes to the Financial Statements for the Year Ended June 30, 2005 and 2004

Bond Issue	Maturity	Original Notional Amount	Fair Value at June 30, 2005
Series 2004C	Aug. 15, 2011	\$9,250,000	\$ 208,375
Series 2004C	June 1, 2006	10,675,000	(73,335)
Series 2004B	Aug. 15, 2025	27,000,000	2,119,213
Series 2004A	Aug. 15, 2034	28,500,000	4,583,084
Series 2004A	Aug. 15, 2034	28,500,000	(1,719,061)
Total Liability			<u>\$ 5,118,276</u>

7. Property, Plant and Equipment

Property, plant and equipment included the following at June 30, 2005.

	<u>2005</u>	<u>2004</u>
Land and buildings:		
Educational plant	\$ 60,390,330	\$ 58,703,693
Dormitories and refectory	29,584,499	28,075,290
Administrative and other	17,291,142	16,885,904
Residences	879,680	876,529
Construction in progress	8,851,216	5,375,404
Land	3,176,060	3,176,060
Total	<u>120,172,927</u>	<u>113,092,880</u>
Furniture, fixtures and equipment	<u>29,483,389</u>	<u>26,616,816</u>
Total	\$ 149,656,316	\$ 139,709,696
Less: accumulated depreciation	(78,153,359)	(71,911,771)
	<u>\$ 71,502,957</u>	<u>\$ 67,797,925</u>

8. Museum:

Revenues

Included in the Statement of Activities, the Museum realized service revenue as well as \$1,048,433 and \$1,099,859 of investment income and \$164,186 and \$816,358 of gifts and grants for the years ended June 30, 2005, and 2004 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 \$394,997 and \$583,115 for acquisitions during 2005 and 2004 respectively.

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Notes to the Financial Statements for the Year Ended June 30, 2005 and 2004

9. Retirement and Pension Plans:

The School participates in the Teachers Insurance and Annuity Association (TIAA) and College Retirement Equities Fund (CREF) retirement plan for eligible faculty, administrative and staff employees. The School made contributions to the TIAA-CREF retirement plan of approximately \$3,123,546 and \$3,022,154 for the years ended June 30, 2005 and 2004, 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. In the agreement the School agreed to make voluntary payments relating to the acquisition of a specific property with an option to cancel payment fourteen months prior to the applicable fiscal year. As of June 2005 the School had a commitment of \$1,602,000 for 2005 and 2006 or \$3,204,000 over the next two years, related to the acquisition of new property, and \$3,293,923 over the next eighteen years as payments in lieu of taxes. Payments of \$1,602,000 were made in fiscal year 2004 and fiscal year 2005, respectfully. A certain portion of the payment was made by a third party for which the School is liable.

Certain of the School's investments in privately held funds included unfunded commitments. As of June 30, 2005, unfunded commitments totaled \$17,100,429.

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 three established employee bargaining units (Full-Time Faculty, Part-Time Faculty, and Public Safety Officers) and is currently negotiating contract renewals with two of them; the contract for the third expires on June 30, 2006. The school is also currently negotiating a first contract with a fourth group (Museum Guards).

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 payments of \$5,259,454 and \$1,442,285 were made during the years ended June 30, 2005 and 2004, 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.

Rhode Island School of Design**Notes to the Financial Statements for the Year Ended June 30, 2005 and 2004**

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

	<u>2005</u>	<u>2004</u>
Instruction	\$40,455,980	\$37,455,726
Campus support Services	14,770,990	13,429,578
Institutional Support	13,244,187	12,892,293
Museum Services	6,789,989	6,434,225
Academic Support	6,806,026	6,641,055
Student Support	3,533,140	3,409,480
Research	516,265	394,498
Total	<u>\$86,116,577</u>	<u>\$80,656,855</u>

13. Subsequent Events:

On August 12, 2005 the School consummated its commitment to purchase 15 Westminster Street for \$47,573,040. This building known as the Living and Learning Center will include the Library and dormitory space. Funding for this acquisition came from proceeds of Series 2004D Bonds, which were included in deposits with trustee.