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## KANSAS BOARD OF REGENTS

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Donna L. Shank	Nelson D. Galle
Janice B. DeBauge	Franklin D. Gaines
Richard L. Bond	James R. Grier, III
Lewis L. Ferguson	Deryl W. Wynn
William R. Docking	

## EXECUTIVE OFFICERS

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Robert E. Hemenway  
*Chancellor*

Paul Carttar  
*Executive Vice Chancellor for External Affairs*

Theresa Klinkenberg  
*Chief Business and Financial Planning Officer*

### Lawrence Campus

David E. Shulenburger  
*Executive Vice Chancellor / Provost*

Kathleen McCluskey-Fawcett  
*Senior Vice Provost for Academic Affairs*

William L. (Lindy) Eakin  
*Vice Provost for Administration and Finance*

### Medical Center Campus

Dr. Barbara Atkinson, M.D.  
*Executive Vice Chancellor*

Harold E. Phillips  
*Vice Chancellor for Administration*

R. Michael Keeble  
*Associate Vice Chancellor of Finance*

### Financial Officers

Diane H. Goddard  
*Assistant Vice Provost / Comptroller, Lawrence*

Robert W. Weseloh  
*Controller, Medical Center*

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# THE UNIVERSITY OF KANSAS

## MANAGEMENT'S DISCUSSION AND ANALYSIS

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The following discussion and analysis provides an overview of the financial performance of the University based on currently known facts, decisions and conditions and is designed to assist readers in understanding the accompanying financial statements. These financial statements are prepared in accordance with Government Accounting Standards Board (GASB) principles, with the exception of GASB Statement No. 39, Determining Whether Certain Organizations Are Component Units. The University has made the decision not to include the Kansas University Endowment Association within its unaudited financial statements. This discussion – along with the financial statements and related footnote disclosures – has been prepared by management and should be read in conjunction with the statements and footnotes. The financial statements, footnotes, and this discussion are the responsibility of management.

### STATEMENT OF NET ASSETS

The Statement of Net Assets presents the assets, liabilities, and net assets of the University at a point in time (at the end of the fiscal year). Its purpose is to present a financial snapshot of the University. The statement of net assets includes all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector institutions. Under the accrual basis of accounting all of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

Within the Statement of Net Assets, assets and liabilities are further classified as current or non-current. Current classification distinguishes those assets that are highly liquid and available for immediate and unrestricted use by the University, and those liabilities likely to be settled in the next 12 months.

Net assets are divided into three categories:

1. **Invested in capital assets, net of debt**, indicates the university's equity in property, plant, and equipment owned by the University.
2. **Restricted net assets** are further divided into two subcategories, non-expendable and expendable. The corpus of non-expendable restricted resources is only available for investment purposes. Expendable restricted net assets are available for expenditure by the University but must be spent for purposes as determined by donors and/or external entities who have placed time or purpose restrictions on the use of the assets.
3. **Unrestricted net assets** are available to the University for any lawful purpose of the institution.

Total Assets at June 30, 2005 were \$1,133.0 million, an increase of \$155 million (16%). Capital net assets comprised 57%, or \$641.7 million of the assets.

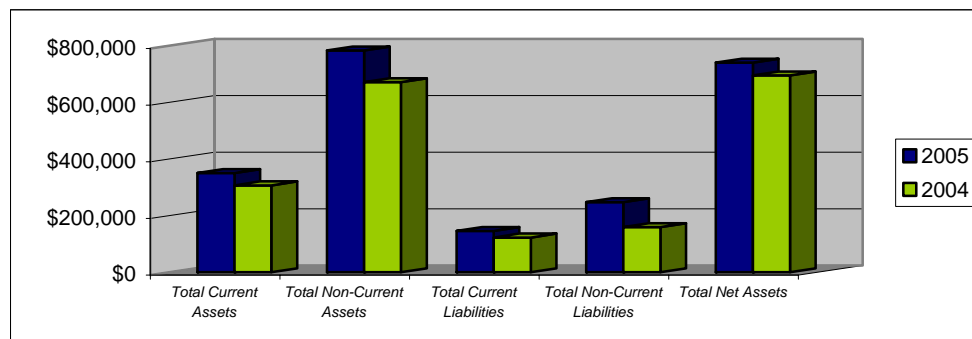
Total liabilities were \$393.0 million at June 30, 2005, an increase of \$109.9 million (39%) compared to \$283.0 million at June 30, 2004. Long-term liabilities comprised 63%, or \$247.4 million of the liabilities.

Total net assets at June 30, 2005 were \$740.0 million, a \$44.9 million increase over the prior year, or a 6% increase in net assets. The breakout of net assets is shown below:

Capital Assets, net of related debt.....	\$432,915,933
Restricted net assets .....	168,992,586
Unrestricted net assets .....	138,120,639
<b>Total net assets.....</b>	<b>\$740,029,158</b>

## MANAGEMENT'S DISCUSSION AND ANALYSIS

The composition of current and non-current assets and liabilities and net assets is displayed below for both the 2005 and 2004 fiscal year-ends (in thousands):



## STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

The Statement of Revenues, Expenses and Changes in Net Assets presents the total revenues earned and expenses incurred by the University for operating, non-operating and other related activities during a period of time. Its purpose is to assess the University's operating results.

### Revenues

Total revenues increased by \$24.3 million, from \$911.0 million to \$935.3 million, an overall increase of 3%.

Operating revenues at the University as of June 30, 2005 increased by 5% over the previous fiscal year. The following is a brief summary of the significant changes:

- Student tuition and fee revenues, after scholarship allowances, were \$160.2 million in 2005, compared to \$136.4 million in 2004, an overall increase of 17%. This increase is a direct result of a tuition increase approved by the Kansas Board of Regents for fiscal year 2005. The goal of the tuition increase, which was the result of collaboration between University Administration and University students, was to provide additional funds to the University to enhance student education. The tuition increase is the third year of a five year plan submitted to the Board of Regents and is composed of two components: a maintenance increase and an enhancement increase. The maintenance component is scheduled to increase at the rate of inflation, estimated by using the Higher Education Price Index (HEPI) over the next five years. The maintenance component for fiscal year 2005 also included a \$6.00 per semester credit hour increase for non-resident tuition. The enhancement component increased all categories of tuition, resident/non-resident, graduate/undergraduate, by \$16.50 per semester credit hour, or approximately \$500 per year for a full-time student. The increase will be used to improve the University in many ways. Funds will be targeted for technology, new faculty positions, salary increases, operating expenses, new staff and programs, and other investments to enhance the University. Additionally several academic schools implemented new differential tuition fees during fiscal year 2005. The Schools of Journalism, Fine Arts, Education, and Business all implemented differential fees that ranged from \$12 to \$75 per credit hour.
- Medical service revenue, net, increased \$5.8 million (7%) from the previous fiscal year. Two component units of the University, the Kansas University Physicians Inc. (KUPI) and Kansas University HealthPartners, Inc. generate medical service revenue. Kansas University Physicians, Inc. (KUPI) was incorporated in 1995 as a not-for-profit organization. KUPI operates at the University of Kansas Medical Center under a contract with the University. KUPI contracts with the various clinical foundations at KUMC who provide physician and other health care services to patients. Revenues generated for these professional physician services are received by KUPI who incurs expenses associated with delivering these services. KUPI also reimburses the clinical departments for physician services. KU HealthPartners, Inc. is a non-profit corporation affiliated with the University of Kansas Medical Center. KU HealthPartners provides clinical services that are non-physician in nature to individuals and

## MANAGEMENT'S DISCUSSION AND ANALYSIS

other entities. KU HealthPartners provides professional clinical services from physical therapists, occupational therapists, hearing and speech pathologists, nurse practitioners, and other ancillary non-physician health care specialists. KU HealthPartners contracts with the School of Nursing and the School of Allied Health for the health care professionals who provide specific clinical services.

- Auxiliary Enterprises – Athletics revenues decreased by \$8.1 million (14%) to \$48.6 million in 2005. This decrease is primarily attributed to a significant decrease in temporarily restricted and unrestricted contributions in comparison to the prior year. In late 2004 the KU Athletics Corporation implemented a new points system for men's basketball season tickets. In conjunction with the implementation, current season ticket holders were given the opportunity to receive double points for any contributions received prior to June 30, 2004. The result of this program was approximately \$12.0 million in contributions. Additionally the KU Athletics Corporation also received significant pledges from donors towards the construction of the Hall of Athletics and Allen Field House Renovations in 2004. Similar sized contributions were not received during the current fiscal year.

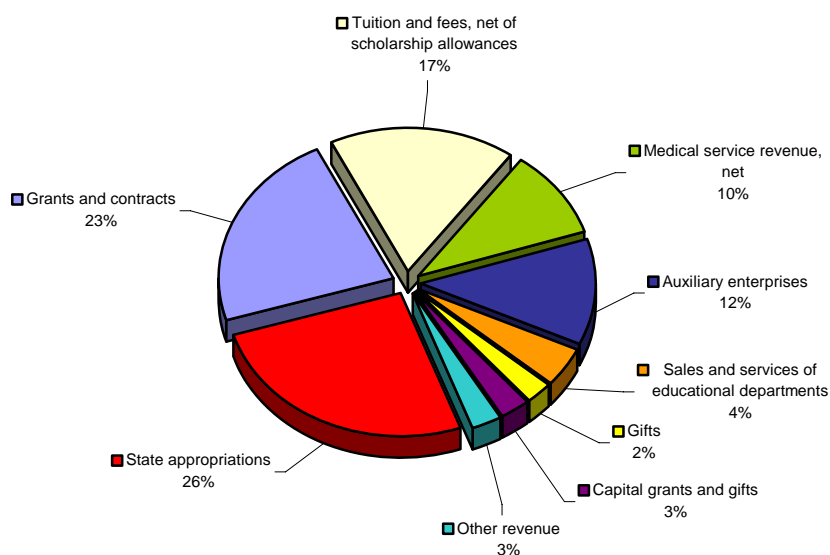
Total non-operating revenues were up 4% from the prior year from \$264.6 million to \$275.1 million. The following is a brief summary of the significant changes:

- State appropriations, the largest single source of revenue at the University, increased from \$232.0 million to \$240.7 million, or 4% as the State has slowly begun to recover economically.
- Gifts decreased 9% to \$21.3 million in 2005. Gifts received consisted primarily of support provided by the Kansas University Endowment Association (KUEA) in the form of reimbursement to the University for salaries and other operating expenses.
- Other non-operating revenues (expenses) increased from (\$.6) million to \$3.6 million in 2005, an increase of over 100%. The increase was primarily attributed to a \$4.0 million payment received by the University in connection with a royalty buyout agreement executed between the University and another entity in July 2004. In connection with the buyout agreement, the University received \$4,000,000 and 2,000,000 shares of Preferred Stock in the other entity.

Other revenues included the following:

- Capital appropriations and capital gifts decreased from \$45.1 million to \$26.4 million, or 42%. In 2004, the University received private donations via KUEA for the construction of several larger projects such as the Dole Institute of Politics, Eaton Hall, the Anderson Family Strength and Conditioning Center, and the Hogle Brain Imaging Center. The majority of construction activity in 2005 was primarily funded via revenue bonds rather than private donations.

The composition of these revenues are displayed in the following graph:



# MANAGEMENT'S DISCUSSION AND ANALYSIS

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## Expenses

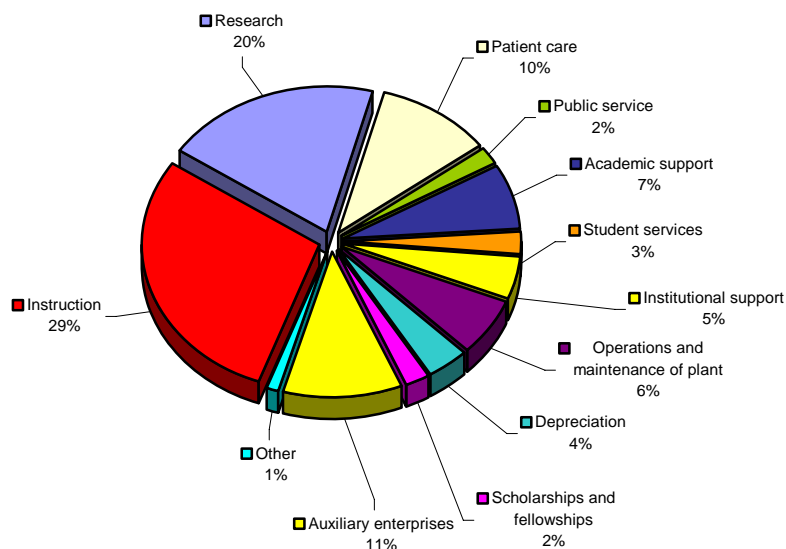
Operating expenses were \$883.0 million for the 2005 fiscal year. This was an increase over the prior year of \$55.9 million, or 7%. The following is a brief summary of the significant changes:

- Instruction increased \$17.8 million (7%) to \$258.1 million in 2005. As noted above the University increased tuition & fees in fiscal year 2005 as part of a five-year tuition enhancement plan. Funds generated from the increase were specifically targeted at instructional and student support functions, specifically technology, new faculty positions, salary increases, operating expenses, new staff and programs, and other investments to enhance the University.
- Research increased from \$158.9 million to \$174.5 million in 2005 (10%). Research expenses include activities specifically organized to produce research whether commissioned by an agency external to the University or separately budgeted by an organizational unit within the University. Increasing sponsored research is a primary focus for the University as it works toward becoming a top 25-public research institution. In addition to obtaining several significant sponsored research grants this past year, the University also had several large grants that reached their peak in expenses during 2005. In recent years the University has also focused on reinvesting its overhead reimbursement funds back into its research mission.
- Public service decreased by 23% in 2005 to \$17.2 million. Public service expenses include funds expended for activities beneficial to individuals and groups external to the University. Activities include programs provided through the University's Continuing Education department, various public lecture series, KANU public radio programs, and various medical clinics. The decrease in expenses can be attributed to several large public service grants administered by the KU Center for Research (KUCR) ending during 2004. Additionally KUCR received several large public service grants during 2004, including two USDE grants that were subcontracted out to KATCO, Kansas Assistive Technology Cooperative. The program is designed to review, approve and grant loans to disabled persons or families for equipment that allows them to be employed or to work from home (wheelchairs, vans, computers, etc.).
- Auxiliary Enterprises – Athletics increased by 17% in 2005 to \$38.1 million. The increase is primarily the result of an increase in staff member numbers as well as increases in compensation packages for existing staff members. Additionally the Corporation held several large promotional events during fiscal year 2005 including the 50<sup>th</sup> anniversary of Allen Field House.
- Auxiliary Enterprises – Parking increased \$1.0 million (36%) from the previous fiscal year. The increase is attributed to increased lease costs for additional parking spaces as well as increased maintenance expenses related to the Medical Center parking garage.
- Auxiliary Enterprises – University health services on the Lawrence Campus increased \$1.1 million (16%) in 2005. This increase in expenses is attributed to a variety of sources including increases in staff compensation, increases in professional liability insurance premiums and increases in pharmaceutical costs. The increase in pharmaceutical costs can be directly attributed to the University's new mandate that all students living in university housing obtain the meningitis vaccination. This mandate officially took effect for the fall of 2005, however the Health Center increased its vaccine inventory near the end of the year as part of its preparation process.
- Auxiliary Enterprises – Other expenses increased from \$3.6 million to \$5.0 million in 2005. Other auxiliary enterprises include a variety of smaller programs across the Lawrence and Edwards campuses such as the Midwestern Music Camps, Hilltop Child Development Center, Printing Services, Network & Telecommunications Services, and the University Press. The majority of this year's increase is attributed to increased program expenses to maintain and expand the University's Network & Telecommunications Services.

Non-operating expenses are represented primarily by interest expense. Interest expense increased by 21% from the prior year from \$6.1 million in 2004 to \$7.4 million in 2005 as the result of the increased debt the University has incurred over the past few years.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

The composition of total expenses, including operating and non-operating are displayed below:



## Extraordinary Items

As noted above under “other non-operating revenues (expenses)”, the University executed a royalty buyout agreement with another entity in July 2004. In connection with the buyout agreement, the University received \$4,000,000 and 2,000,000 shares of Preferred Stock in the other entity. The University did not have any special and/or extraordinary items in 2004.

## Endowment Expenses Paid On Behalf of University

The Kansas University Endowment Association (KUEA), an independent, not-for-profit organization whose primary mission is to raise funds for the University, provides direct and indirect support to the University that is not entirely reflected in the University’s Statement of Revenues, Expenses and Changes in Net Assets. Expense items paid on behalf of the University by KUEA include expenses such as scholarships and fellowships, salaries, construction, equipment, books, works of art, and travel. Total University support provided by KUEA equaled approximately \$103.9 million and \$76.6 million in 2005 and 2004, respectively.

The following support items totaling \$36.6 million are reflected in the University’s statements for 2005.

- **Capital Projects.** KUEA sponsored many capital projects throughout the year with a combined approximate value of \$17.3 million. Major capital projects that benefited from KUEA’s fundraising efforts included the Hall Center for Humanities at \$2.3 million, Rieger Scholarship Hall at \$2.4 million, and the Medical Center Parking Garage #3 at \$8.0 million. Note - amounts represent current year expenses and not the total cost of the capital projects.
- **Salaries and other operating expenses.** KUEA reimbursed the University approximately \$19.3 million for various faculty and staff member salaries and other minor operating expenses including the University’s distinguished professors. The salary expense is reflected in the University’s statements as it represents a more accurate reflection of the University’s operating expenses. KUEA’s reimbursement is reflected as a gift to the University within non-operating revenues.



# MANAGEMENT'S DISCUSSION AND ANALYSIS

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## Net Assets

Net assets increased by \$44.9 million over the previous fiscal year. This significant increase in net assets can be attributed to the increased level of capital and non-capital gifts received by the University during 2005.

## STATEMENT OF CASH FLOWS

The Statement of Cash Flows presents cash receipts and payments of the University during a period of time. Its purpose is to assess the University's ability to generate future net cash flows and meet its obligations as they come due. The following is a condensed statement of cash flows for the years ended June 30, 2005 and 2004:

### CASH FLOWS FOR THE PERIOD

(in thousands of dollars)

	<u>June 30, 2005</u>	<u>June 30, 2004</u>
Net cash provided (used) by:		
Operating activities	(220,261)	(223,487)
Non-capital financing activities	279,363	267,206
Capital and related financing activities	16,225	(41,732)
Investing activities	<u>(55,543)</u>	<u>1,694</u>
Net increase in cash	19,784	3,681
Beginning cash and cash equivalent balances	144,102	140,421
<b>Ending cash and cash equivalent balances</b>	<b>163,886</b>	<b>144,102</b>

Cash flows from operating activities will always be negative since GASB requires state appropriations to be reported as cash flows from noncapital financing activities. Cash flows from capital financing activities include all plant funds and related long-term debt activities. Cash flows from investing activities show all uses of cash and cash equivalents to purchase investments, and all increases in cash and cash equivalents as a result of selling investments or earning income on cash and investments.

Cash used by operating activities decreased \$3.2 million (1%). This decrease in the use of cash is the result of a combination of operating revenues (tuition and fees, grants and contracts, auxiliary income) increasing slightly more than the University's operating expenses.

Cash flows from non-capital financing activities increased by \$12.2 million (5%). This increase was primarily the result of the University's 4% increase in state appropriations, as well as the University's \$4.0 million cash receipt related to the royalty buyout agreement executed in fiscal year 2005 noted above.

Cash flows from capital and related debt increased by \$58.0 million. This increase was primarily the result of a several revenue bond issuances in fiscal year 2005 (See Notes 9 and 10 for further details).

Cash used by investing activities increased \$57.2 million. In conjunction with the revenue bond issuances completed this fiscal year, the University invested any required bond reserves as well as the portion of bond proceeds not immediately needed for construction activity. As of the June 30, 2005, the University had approximately \$109.1 million in investments related to revenue bond activity.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

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## CAPITAL ASSETS

The University made significant investments in capital during the 2004-2005 fiscal year. Detailed information regarding capital asset additions, retirements, and depreciation is available in Note 7 to the financial statements.

The following is a brief summary of the construction projects that were completed during the current fiscal year:

- In November 2001, the University of Kansas, Lawrence campus, engaged Viron Energy Services (purchased by Chevron in 2003) to conduct an investment grade energy audit of the campus for the purpose of identifying energy conservation projects. The audit identified over 100 energy savings measures that will result in an annual utility and maintenance savings of \$1.7 million. These projects include energy savings measures such as solar window film, lighting retrofits, insulation, building automated control systems, programmable thermostats, and many others. The \$19.6 million (including capitalized interest) 18-month project was over 90% completed as of June 30, 2004. The remaining energy saving projects were completed in early fiscal year 2005. The project was funded through a Master Lease Purchase Agreement between the State of Kansas and Citibank, N.A. The University is responsible for repaying the State, via our annual utility and maintenance savings, for the 20-year term of the lease.
- Construction was completed on the second campus building at the University's Edwards Campus in Overland Park, Kansas. Construction of the approximately \$15.6 million building was funded through revenue bonds secured by student fees as well as private donations from the Hall Family Foundation and the Victor and Helen Regnier Charitable Foundation. The 82,000-square-foot building was named the Victor and Helen Regnier Hall. Regnier Hall is expected to allow enrollment at Edwards Campus to nearly double again. Currently 2,100 working adults attend campus programs at the graduate and undergraduate levels.
- In 2002 the State of Kansas Legislature passed the University Research and Development Enhancement Act (URDEA), which included \$5 million bonding authority for research equipment at the University's Lawrence Campus. The equipment included a Nuclear Magnetic Resonance Spectrometer (NMR), a Proteomics Core Lab Suite, and a Proteomics Structures Lab. Bonds were sold in February 2003 for this project. The bonds will be repaid with a combination of State General Funds and University Sponsored Research Overhead. The equipment is housed in a new structural biology center facility. The new \$2.9 million facility was funded via research overhead revenues provided by the Kansas University Research Center, Inc. and the University Provost office. The dedication for the new facility and equipment was held on October 15, 2004.
- The Hall Center for Humanities was built within the existing stonewalls of the oldest standing building on the campus, which was originally constructed as the power plant. The stonewalls are both the "envelope" of the project and the predominant architectural element. The construction of this space preserves a valued historic artifact of the campus, and enhances the entry to this area of campus. This \$5.2 million project was funded predominately through private donations.
- Rieger Scholarship Hall is the third scholarship hall to be built in the last decade through the receipt of gift funds to the Student Housing Department at the Lawrence campus. The new hall provides affordable housing for 50 women in a cooperative living environment. Common areas include a courtyard, living room, kitchen/dining area, recreational room and several multi-purpose rooms. The \$3.1 million project was funded predominately through private donations, and opened its doors to its new residents in August 2005.
- The Medical Center completed its renovation of the 5<sup>th</sup> and 6<sup>th</sup> floors of Wahl Hall East for the new Kidney Foundation. The completed project cost was \$2.7 million.
- The Research Support Facility expansion was completed with a finished total cost of \$5.7 million. Funding for the completed project was provided by revenue bonds issued by the Medical Center in 2001.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

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Additionally, the University was involved in several construction projects that were under construction or in planning and design phases at year-end:

- In 2004, the University received 50% matching grant from the National Institute of Health grant to renovate several labs within Malott Hall that are used by Medicinal Chemistry. The remodeled labs will be used as synthetic chemistry facilities and will be primarily occupied by those faculty members with the most pressing need for space for these types of activities. The final cost of the project is estimated at \$2.6 million.
- Hashinger Hall closed for renovations in May 2005, the day after commencement. Hashinger is the fourth residential hall to be renovated in recent years. The renovation project funded via revenue bond proceeds of \$11.8 million and Student Housing revenue funds is estimated to have a final cost of approximately \$12.6 million. Also known as the Residence Center for the Creative Arts, Hashinger has a performing-arts focus and after renovations will offer expanded studio, rehearsal and performance space for artists as well as updated suites and dorm rooms. Incorporated into its food service area, the renovated residence hall will also have a coffee house including space for open mic nights.
- In late Fall 2004, the KU Center for Research, Inc. and Lawrence Campus administration began the process of constructing a new Multidisciplinary Research Building (MRB). Among the initial occupants of the MRB will be the KU Bioinformatics Program and components of bioanalytical chemistry, drug discovery, stable isotope geology and nanoscience. Ultimately, about 200 people will use the 106,000-square-foot MRB at any time, including 20 faculty, nearly 170 students and post-docs, and a core technical support staff. The \$40 million project includes laboratory spaces on the outside of the building wrapped around a shared core of research equipment and facilities, including bio-safety level 3 labs, a mass spectrometry lab and "clean" rooms. The expected completion date of this "fast-track" project is December 15, 2005. The project is funded via revenue bonds secured with a pledge of KUCR revenues.
- In February 2004, the family of the late Gilbert and Betty Booth committed more than \$4 million for a Hall of Athletics at Allen Field House. The Hall of Athletics will be an addition to be built on the east side of Allen Field House and will feature memorabilia spanning more than a century of KU athletics programs, a ticket office and a store. Construction is expected to be completed in Winter 2005.
- The Medical Center continued its construction of its state-of-the-art biomedical research building. As of June 30, 2005, more than \$22 million had been spent on construction. The five-story building will feature state-of-the-art equipment, administrative areas, support space and laboratories that can be configured into flexible suites that can accommodate current and future research requirements. It will house scientists in KU research programs such as neuroscience, reproductive biology and proteomics. Each research group in the facility will have between 15,000 and 20,000 square feet of office, research-support and laboratory space. The building will include laboratories for researchers in biochemistry, molecular biology, toxicology and pharmacology. It also will have patient interview space for the schools of allied health and nursing. Researchers will integrate information from the study of proteomics; genes and chromosomes, or genomics; and biological systems. The research also will focus on female reproduction and applied neuroscience to answer questions about diseases such as infertility, Alzheimer's disease, Parkinson's disease, stroke, epilepsy, deafness and communication disorders. The total construction cost of the project is estimated to be in excess of \$57 million. Funding has been provided by the issuance of revenue bonds as well as private donations. Construction is expected to be completed by 2006.
- More than \$11 million has been spent on energy conservation measures at the Medical Center. This construction is being performed by Chevron Energy Corporation and is funded by a \$13.3 million K DFA bond issue.
- Construction has begun on a third parking garage at the Medical Center. As of June 30, 2005, more than \$600 thousand had been spent on architectural design costs. The completed project cost is estimated at \$12.5 million. Funding for the project is a combination of revenue bonds secured by future parking revenues as well as private donations.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

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## DEBT ADMINISTRATION

At June 30, 2005, the University had \$220.2 million in debt outstanding. In 2005, the Lawrence Campus issued new debt in the amount of \$11.8 million to finance a portion of the cost to renovate its fourth residence hall. The KU Center for Research, Inc. issued \$45.6 million in new debt to finance the cost to construct, to furnish, and to equip the University's new Multidisciplinary Research Building. Additionally the KU Athletic Corporation issued new debt in the amount of \$17.8 million for the purpose of refinancing and defeasing its series 1998A revenue bonds. Finally the Medical Center issued new debt to finance the continued construction of its new biomedical research facility (\$27.1 million) as well as the construction of its third parking garage (\$3.3 million). The University paid \$35.0 million in principal and interest payments related to all outstanding revenue bonds.

Moody's Investor Service currently rates the University "Aa2". More detailed information about the University's long-term liabilities is available in Notes 9 and 10 to the financial statements.

## ECONOMIC OUTLOOK

The State of Kansas revenues continue to remain stable, and state general fund collections for fiscal year 2006 are estimated to increase by approximately 7% above fiscal year 2005 receipts. Budget cuts similar to those experienced in fiscal years 2002 and 2003 were avoided in fiscal years 2004 and 2005 and are not expected in fiscal year 2006. Fiscal year 2006 will have a least one unique economic twist for both the State and University. Due to the State and University's bi-weekly payroll process, both entities will incur a 27<sup>th</sup> pay period in fiscal year 2006. Funding for this additional pay period will be provided by the state general fund with the expectation that the University will reimburse the State over a set period of time. Pressing issues with K-12 education and one-time funding mechanisms used to balance the budget in the past few years will continue to prevent significant increases in State funding for higher education without significant new sources of funds. The near term for State funding appears to be one of steady state with marginal increases. The State of Kansas is expected to provide approximately 25% of the general operating resources for the University during fiscal year 2006. Appropriations for fiscal year 2006 are currently set at \$249.9 million, an increase of 4% from fiscal year 2005.

The University is not aware of any additional currently known facts, decisions, or conditions that are expected to have significant effect on the financial position or results of operations during this fiscal year beyond those unknown variations having a global effect on virtually all types of business operations.

Overall, the financial position of the University continues to be strong. Enrollment for the academic 2005-2006 year is expected to set another record high. The fourth year of a five-year plan to double undergraduate resident tuition is providing a significant infusion of new tuition funds to help advance the University. The University also continues to move forward towards its goal of increasing federally funded research. A number of major awards and the completed construction of the new Multidisciplinary Research Building and the Biomedical Research Building in fiscal year 2006 will help continue the University's progress in this area.

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*Financial  
Statements*

THE UNIVERSITY OF KANSAS  
STATEMENT OF NET ASSETS  
AS OF JUNE 30, 2005 AND 2004

	<u>2005</u>	<u>Restated 2004</u>
<b><u>ASSETS</u></b>		
Current assets:		
Cash and cash equivalents	\$ 156,547,374	\$ 140,952,558
Investments	130,060,380	103,463,568
Accounts receivable, net	43,442,636	40,875,098
Pledges receivable, net	4,803,421	6,869,494
Loans to students, net	4,111,244	4,013,191
Inventories	7,283,094	7,285,013
Prepaid expenses and other assets	4,186,526	3,381,278
Total current assets	<u>350,434,675</u>	<u>306,840,200</u>
Non-current assets:		
Restricted cash and cash equivalents	7,338,412	3,149,207
Accounts receivable, net	110,770	157,295
Pledges receivable, net	5,959,930	7,164,688
Endowment investments	62,781,454	57,424,515
Other investments	43,663,233	8,942,724
Loans to students, net	17,904,052	17,703,031
Prepaid expenses and other assets	3,161,585	1,805,353
Capital assets, net	641,663,165	574,937,569
Total non-current assets	<u>782,582,601</u>	<u>671,284,382</u>
Total assets	<u>1,133,017,276</u>	<u>978,124,582</u>
<b><u>LIABILITIES</u></b>		
Current liabilities:		
Accounts payable and accrued expenses	57,760,775	42,586,572
Due to Foundations	10,402,048	11,499,243
Deferred revenue	38,445,517	29,388,336
Deposits held in custody for others	7,083,130	7,646,414
Accrued compensated absences – current portion	21,868,454	22,596,865
Capital leases payable - current portion	4,529,391	1,880,800
Revenue bonds payable - current portion	5,440,000	7,290,000
Other liabilities	90,551	81,140
Total current liabilities	<u>145,619,866</u>	<u>122,969,370</u>
Non-current liabilities:		
Accrued compensated absences	5,013,136	2,796,020
Capital leases payable	26,429,790	24,240,972
Revenue bonds payable	214,755,000	132,335,000
Other non-current liabilities	1,170,326	698,555
Total non-current liabilities	<u>247,368,252</u>	<u>160,070,547</u>
Total liabilities	<u>392,988,118</u>	<u>283,039,917</u>
<b><u>NET ASSETS</u></b>		
Invested in capital assets, net of related debt	432,915,933	414,020,578
Restricted for:		
Nonexpendable	60,693,458	57,465,712
Expendable:		
Scholarships, research, instruction and other	17,368,666	12,788,602
Loans	20,496,260	25,013,821
Capital projects	61,673,284	60,520,906
Debt service	8,760,918	6,045,521
Unrestricted	138,120,639	119,229,525
Total net assets	<u>\$ 740,029,158</u>	<u>\$ 695,084,665</u>

See accompanying notes to financial statements.

THE UNIVERSITY OF KANSAS  
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS  
FOR THE YEARS ENDED JUNE 30, 2005 AND 2004

	<u>2005</u>	<u>Restated 2004</u>
<b><u>OPERATING REVENUES</u></b>		
Tuition and fees (net of scholarship allowances of \$12,610,160 in '05 and 9,910,338 in '04)	\$ 160,216,624	\$ 136,428,613
Net Patient service revenue	86,287,422	80,513,857
Foundation, Contractual & Hospital Fee Assessments	6,927,006	6,317,420
Federal grants and contracts	167,089,318	156,117,625
State and local grants and contracts	23,649,613	25,908,687
Nongovernmental grants and contracts	21,083,654	22,494,323
Sales and services of educational departments	41,326,670	40,816,084
Auxiliary enterprises:		
Housing	25,007,416	23,312,318
Athletics	48,611,860	56,669,912
Parking	5,533,413	5,269,259
Student unions	22,383,433	20,078,034
University health services	7,578,725	7,214,583
Other auxiliary enterprises	4,060,285	4,162,324
Other operating revenues	13,604,742	15,284,104
Total operating revenues	<u>633,360,181</u>	<u>600,587,143</u>
<b><u>OPERATING EXPENSES</u></b>		
Instruction	258,085,462	240,247,293
Research	174,524,529	158,906,271
Patient care	93,378,843	87,851,847
Public service	17,217,792	22,488,244
Academic support	64,011,152	60,043,753
Student services	23,141,745	21,592,710
Institutional support	42,846,951	39,575,735
Operations and maintenance of plant	55,556,069	51,999,352
Depreciation	36,480,274	37,169,435
Scholarships and fellowships	19,047,784	19,481,772
Auxiliary enterprises:		
Housing	21,666,865	20,285,592
Athletics	38,127,910	32,722,984
Parking	3,815,984	2,796,533
Student unions	20,462,959	19,797,851
University health services	7,973,438	6,866,532
Other auxiliary enterprises	5,046,113	3,572,329
Other operating expenses	1,590,769	1,663,255
Total operating expenses	<u>882,974,639</u>	<u>827,061,488</u>
Operating income (loss)	<u>(249,614,458)</u>	<u>(226,474,345)</u>
<b><u>NON-OPERATING REVENUES (EXPENSES)</u></b>		
State appropriations	240,669,047	232,021,785
Gifts	21,348,659	23,498,368
Investment income	9,499,599	9,129,562
Interest expense	(7,366,653)	(6,083,549)
Other non-operating revenues (expenses)	3,554,333	(629,431)
Net non-operating revenues (expenses)	<u>267,704,985</u>	<u>257,936,735</u>
Income before other revenues, expenses, gains, or losses	18,090,527	31,462,390
Capital appropriations	4,018,479	4,686,258
Capital grants and gifts (expense)	22,354,048	40,435,608
Additions to permanent endowments	481,439	592,237
Increase (decrease) in net assets	<u>44,944,493</u>	<u>77,176,493</u>
<b><u>NET ASSETS</u></b>		
Net assets - beginning of year	695,084,665	617,908,172
Net assets - end of year	<u>\$ 740,029,158</u>	<u>\$ 695,084,665</u>

See accompanying notes to financial statements



THE UNIVERSITY OF KANSAS  
STATEMENT OF CASH FLOWS  
FOR THE YEARS ENDED JUNE 30, 2005 AND 2004

	<u>2005</u>	<u>Restated 2004</u>
<b><u>CASH FLOWS FROM OPERATING ACTIVITIES</u></b>		
Tuition and fees	\$ 159,986,459	\$ 138,034,534
Sales and services of educational activities	42,386,114	41,513,134
Patient services revenue, net	90,428,315	81,360,273
Auxiliary enterprises:		
Housing	3,192,116	2,644,235
Athletics	3,329,963	(1,307,964)
Parking	1,730,220	2,388,660
Student unions	1,988,559	783,714
University health services	(309,374)	712,782
KU Healthpartners, Inc.	83,528	188,049
Other auxiliary enterprises	(985,828)	589,995
Grants and contracts	209,918,838	197,031,678
Payments to suppliers	(192,280,673)	(182,509,918)
Payments to utilities	(18,913,399)	(16,719,144)
Compensation and benefits	(472,352,811)	(442,198,266)
Payments to Foundations under PSA's	(43,663,910)	(40,660,314)
Payments for scholarships and fellowships	(12,827,269)	(17,170,047)
Loans issued to students and employees	(5,156,199)	(4,199,681)
Collection of loans to students and employees	4,652,542	4,791,204
Other receipts (payments)	8,531,962	11,240,203
Net cash provided (used) by operating activities	<u>(220,260,847)</u>	<u>(223,486,873)</u>
<b><u>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</u></b>		
State appropriations	240,669,047	232,021,785
Gifts	34,518,584	35,436,931
Student organization agency transactions	164,200	(236,345)
Federal family education loan receipts	89,167,347	80,761,000
Federal family education loan disbursements	(89,155,990)	(80,774,723)
Other	4,000,000	(2,314)
Net cash provided by noncapital financing activities	<u>279,363,188</u>	<u>267,206,334</u>
<b><u>CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES</u></b>		
Proceeds from capital debt	110,395,000	13,080,000
Capital appropriations	4,018,479	4,686,258
Capital grants and gifts		
Purchases of capital assets	(57,900,368)	(47,268,135)
Proceeds from sale of capital assets	120,746	124,335
Principal paid on capital debt and leases	(32,135,402)	(6,311,074)
Interest paid on capital debt and leases	(6,706,742)	(6,043,721)
Other	(1,567,107)	
Net cash used by capital financing activities	<u>16,224,606</u>	<u>(41,732,337)</u>
<b><u>CASH FLOWS FROM INVESTING ACTIVITIES</u></b>		
Proceeds from sales and maturities of investments	87,186,643	43,185,714
Interest on investments	5,085,406	3,417,937
Purchase of investments	(147,814,975)	(44,909,680)
Other		
Net cash provided by investing activities	<u>(55,542,926)</u>	<u>1,693,971</u>
Net increase (decrease) in cash	19,784,021	3,681,095
Cash - beginning of the year	<u>144,101,765</u>	<u>140,420,670</u>
Cash - end of year	<u>\$ 163,885,786</u>	<u>\$ 144,101,765</u>

STATEMENT OF CASH FLOWS  
 FOR THE YEARS ENDED JUNE 30, 2005 AND 2004  
 (CONTINUED)

	<u>2005</u>	<u>Restated 2004</u>
<b><u>RECONCILIATION OF NET OPERATING REVENUES (EXPENSES) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES:</u></b>		
Operating income	\$ (249,614,458)	\$ (226,474,345)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:		
Non-cash revenue	(13,814,503)	(11,572,656)
Depreciation expense	36,480,274	37,169,435
Other non-cash expenses	99,298	(932,654)
Changes in assets and liabilities:		
Accounts receivables, net	(1,840,433)	(5,342,383)
Pledges receivable, net	3,456,286	(10,994,771)
Loans to students, net	(299,074)	749,891
Inventories	(5,919)	443,704
Prepaid expenses and other assets	(308,027)	(151,691)
Accounts payable and accrued liabilities	(3,138,709)	(7,678,517)
Due to Foundations	(1,097,195)	335,603
Deferred revenue	8,306,491	(1,272,348)
Accrued compensated absences	1,515,122	2,233,859
Net cash provided (used) by operating activities:	<u>\$ (220,260,847)</u>	<u>\$ (223,486,873)</u>
Non-cash Investing, Capital and Financing Activities		
Capital Leases (Initial Year):		
Fair Market Value	\$ 2,679,762	\$ 41,778
Current Year Cash Payments		(14,178)
Gifts-In-Kind	22,354,048	40,435,608
Net Change in Unrealized Gains and Losses	8,320,605	7,027,772

See accompanying notes to financial statements

# NOTES TO THE FINANCIAL STATEMENTS

## For the Years Ended June 30, 2005 and 2004

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### NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America, with the exception of GASB Statement No. 39, Determining Whether Certain Organizations Are Component Units. The University has made the decision not to include the Kansas University Endowment Association within its financial statements. The financial statements have not been audited.

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amount of assets and liabilities, the 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.

**Organization.** The University of Kansas (the "University") is a comprehensive institution providing undergraduate, graduate, and professional education in a variety of academic programs. The University is a Public Doctoral/Research University - Extensive and is accredited by the North Central Association of Colleges and Schools. The University is governed by the Kansas Board of Regents and is an agency of the State of Kansas. As an agency of the State of Kansas, the University is included in the audited financial report of the State of Kansas.

The University conducts education, research, public service, and related activities at four campuses: the campus in Lawrence, Kansas, the medical center campuses in Kansas City, Kansas and Wichita, Kansas, and the Edwards Campus in Overland Park, Kansas.

For fall 2004, the Lawrence and Edwards campuses had an undergraduate enrollment of 20,887 and a graduate/first professional enrollment of 6,093. The Medical Center had an undergraduate enrollment of 456 and a graduate/first professional (including medical residents, fellows and trainees) enrollment of 2,154.

**Financial Reporting Entity.** As required by accounting principles generally accepted in the United States of America, these financial statements present the combined financial position and financial activities of the University's four campuses and the following blended component units for which the University is financially accountable: the University of Kansas Center for Research, Inc., the University of Kansas Athletic Corporation, the University of Kansas Memorial Corporation, the University of Kansas Medical Center Research Institute, the Student Union Corporation of the University of Kansas Medical Center, Kansas University Physicians, Inc. (KUPI), and Kansas University Health Partners, Inc.

The financial activity and balances of the Kansas University Endowment Association, the Alumni Association of the University of Kansas, and the University of Kansas Hospital Authority are not included in the financial statements of the University as they are legally separate entities and the University does not appoint a voting majority of their governing bodies.

In preparing the financial statements, all significant transactions and balances between campuses and blended component units have been eliminated to avoid overstatement of 1) revenues and expenses on the Statement of Revenues, Expenses, and Changes in Net Assets, and 2) balances on the Statement of Net Assets.

**Basis of Accounting.** For financial reporting purposes, the University is considered a special-purpose government engaged only in business-type activities. Accordingly, the University's financial statements have been presented using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. All significant intra-agency transactions have been eliminated.

The University has the option to apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless FASB conflicts with GASB. The University has elected to not apply FASB pronouncements issued after the applicable date

# NOTES TO THE FINANCIAL STATEMENTS

## For the Years Ended June 30, 2005 and 2004

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**Cash Equivalents.** For purposes of the Statement of Cash Flows, the University considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

**Investments.** The University accounts for its investments at fair value in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. Changes in unrealized gain (loss) on the carrying value of investments are reported as a component of investment income in the Statement of Revenues, Expenses, and Changes in Net Assets.

**Accounts Receivable.** Accounts receivable consists of tuition and fee charges to students and auxiliary enterprise services provided to students, faculty, and staff. Accounts receivable also include amounts due from the Federal government, state and local governments, or private sources, in connection with reimbursement of allowable expenditures made pursuant to the University's grants and contracts. Accounts receivable are recorded net of estimated uncollectible amounts.

**Inventories.** Inventories are carried at cost.

**Prepaid Expenses.** Prepaid expenses consist primarily of deferred charges related to revenue bond issuances as well as deferred summer school expenses.

**Capital Assets.** Capital assets are recorded at cost at the date of acquisition, or fair market value at the date of donation in the case of gifts. For equipment, the University's capitalization policy includes all items with a unit cost \$5,000 or more, and an estimated useful life greater than one year. Renovations to buildings, infrastructure, and land improvements that significantly increase the value or extend the useful life of the structure are capitalized if the related project cost exceeds \$100,000. Routine repairs and maintenance are charged to operating expense in the year in which the expense was incurred.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, 25 years for land improvements, 8 years for equipment, and 5 years for vehicles. Depreciation for buildings and infrastructure is computed using a componentized building and infrastructure depreciation study. Note – The estimated useful lives used by the blended component units for equipment and building improvements vary slightly from the University's policy ranging from 5 to 15 years. The financial impact of the variation is considered to be immaterial to the financials statements as a whole.

Costs incurred during construction of long-lived assets are recorded as construction in progress and are not depreciated until placed in service. The University capitalized \$120,264 and \$1,335,159 in interest during 2005 and 2004, respectively.

**Deferred Revenues.** Deferred revenues include amounts received for tuition and fees and certain auxiliary activities prior to the end of the fiscal year but related to the subsequent accounting period. Deferred revenues also include summer school tuition not earned during the current year and amounts received from grant and contract sponsors that have not yet been earned.

**Compensated Absences.** Employee vacation pay is accrued at year-end for financial statement purposes. The liability and expense incurred are recorded at year-end as accrued compensated absences in the Statement of Net Assets, and as an expense in the Statement of Revenues, Expenses, and Changes in Net Assets.

**Deposits Held In Custody For Others.** Deposits held in custody for others consist primarily of student organizations' moneys administered by the University.

**Noncurrent Liabilities.** Noncurrent liabilities include principal amounts of revenue bonds payable, capital lease obligations with contractual maturities greater than one year, and estimated amounts for accrued compensated absences that will not be paid within the next fiscal year.

# NOTES TO THE FINANCIAL STATEMENTS

## For the Years Ended June 30, 2005 and 2004

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**Net Assets.** The University's net assets are classified as follows:

*Invested in capital assets, net of related debt:* This represents the University's total investment in capital assets, net of outstanding debt obligations related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets such amounts are not included as a component of "invested in capital assets, net of related debt."

*Restricted net assets – expendable:* Restricted expendable net assets include resources in which the University is legally or contractually obligated to spend resources in accordance with restrictions imposed by external third parties.

*Restricted net assets – nonexpendable:* Restricted nonexpendable net assets consist of endowment and similar type funds in which donors or other outside sources have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity, and invested for the purpose of producing present and future income, which may either be expended or added to principal.

*Unrestricted net assets:* Unrestricted net assets represent resources derived from student tuition and fees, state appropriations, and sales and services of educational departments. These resources are used for transactions relating to the educational and general operations of the University, and may be used at the discretion of the governing board to meet current expenses for any purpose. These resources also include auxiliary enterprises, which are substantially self-supporting activities that provide services for students, faculty, and staff.

**Tax Status.** As a state institution of higher education, the income of the University is generally exempt from federal and state income taxes under Section 115(a) of the Internal Revenue Code; however, income generated from activities unrelated to the University's exempt purpose is subject to income taxes under Internal Revenue Code Section 511(a)(2)(B).

**Classification of Revenues.** The University has classified its revenues as either operating or nonoperating revenues according to the following criteria:

*Operating revenues:* Operating revenues include activities that have the characteristics of exchange transactions, such as 1) student tuition and fees, net of scholarship discounts and allowances, 2) sales and services of auxiliary enterprises, 3) most federal, state, and local grants and contracts, and 4) interest on institutional student loans.

*Nonoperating revenues:* Nonoperating revenues include activities that have the characteristics of nonexchange transactions, such as gifts and contributions, and other revenue sources that are defined as nonoperating revenues by GASB Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*, and GASB Statement No. 34, such as state appropriations and investment income.

**Scholarship Discounts and Allowances.** Student tuition and fee revenues, and certain other revenues from students, are reported net of scholarship discounts and allowances in the Statement of Revenues, Expenses, and Changes in Net Assets. Scholarship discounts and allowances are the difference between the stated charge for goods and services provided by the University, and the amount that is paid by students and/or third parties making payments on the students' behalf. Certain governmental grants, such as Pell grants, and other federal, state, or nongovernmental programs, are recorded as either operating or nonoperating revenues in the University's financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees and other student charges, the University has recorded a scholarship discount and allowance.

**Contributions.** Unconditional promises to give cash and other assets are accrued at estimated fair value at the date each promise is received.

**Reclassifications.** Certain reclassifications have been made to the 2004 financial statements to conform to the 2005 financial statement presentation. These reclassifications had no effect on the change in net assets.

# NOTES TO THE FINANCIAL STATEMENTS

## For the Years Ended June 30, 2005 and 2004

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### NOTE 2 – INVESTMENTS

The University of Kansas has the following investments reflected on the Statement of Net Assets as of June 30:

	<u>2005</u>	<u>2004</u>
University of Kansas Lawrence and Edwards Campuses	\$ <b>68,530,902</b>	\$ 52,732,138
University of Kansas Medical Center	<b>63,701,893</b>	51,347,622
University of Kansas Center for Research, Inc.	<b>54,706,036</b>	24,830,800
University of Kansas Athletic Corporation	<b>46,986,544</b>	37,744,895
University of Kansas Memorial Corporation	<b>2,579,692</b>	3,175,352
Total	<u>\$ <b>236,505,067</b></u>	<u>\$ 169,830,807</u>

Of the University of Kansas' total investments of \$236.5 million and \$169.8 million as of June 30, 2005 and 2004, respectively; the University of Kansas Endowment Association administers \$91.0 million and \$77.5 million, respectively. The Kansas Development Finance Authority invests \$65.4 million and \$51.4 million of the total as of June 30, 2005 and 2004, respectively. These monies represent bond proceeds and reserve requirements. The remaining investments consist of \$67.9 million and \$28.8 million invested in short-term investments and \$12.3 million and \$11.8 million of endowment investments administered by trustees not related to the University as of June 30, 2005 and 2004, respectively.

The University of Kansas investments include \$12.3 million and \$11.8 million of investments administered by outside trustees as of June 30, 2005 and 2004, respectively. These investments consist of three accounts: 1) the Gertrude S. Pearson Trust, 2) the Elizabeth M. Watkins Trust for Watkins and Miller Scholarship Halls, and 3) the Elizabeth M. Watkins Trust for Watkins Hospital.

The Gertrude S. Pearson Trust had a reported market value of \$7,026,252 at June 30, 2005 and \$6,745,575 at June 30, 2004. The trustee is Bank of America.

The Elizabeth M. Watkins Trust for Watkins and Miller Scholarship Halls had a reported market value of \$3,376,670 at June 30, 2005 and \$3,304,470 at June 30, 2004. The trustee is Bank of America.

The Elizabeth M. Watkins Trust for Watkins Hospital had a reported market value of \$1,856,211 at June 30, 2005 and \$1,747,636 at June 30, 2004. The trustee is Bank of America.

### NOTE 3 – ACCOUNTS RECEIVABLE

Accounts receivable net of estimated uncollectible amounts, consisted of the following at June 30:

	<u>2005</u>	<u>2004</u>
Tuition and Fees	\$ <b>2,070,790</b>	\$ 2,725,758
Auxiliary	<b>20,453,367</b>	20,558,604
Grants and Contracts	<b>16,567,296</b>	14,717,496
Other	<b>4,461,953</b>	3,030,535
Total	<u>\$ <b>43,553,406</b></u>	<u>\$ 41,032,393</u>

# NOTES TO THE FINANCIAL STATEMENTS

## For the Years Ended June 30, 2005 and 2004

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### NOTE 4 – PLEDGES RECEIVABLE

Pledges receivable consist of the following unconditional promises to give:

	<u>2005</u>	<u>2004</u>
Due in less than one year	\$ 4,973,421	\$ 7,169,494
Due in one to five years	<u>6,990,144</u>	<u>8,508,941</u>
	<b>11,963,565</b>	15,678,435
Less		
Unamortized discount	700,214	944,253
Allowance for uncollectible amounts	<u>500,000</u>	<u>700,000</u>
	<u><b>\$ 10,763,351</b></u>	<u>\$ 14,034,182</u>

Pledges receivable are recorded on the accompanying statements of financial position as follows:

	<u>2005</u>	<u>2004</u>
Pledges receivable - current	\$ 4,803,421	\$ 6,869,494
Pledges receivable - non-current	<u>5,959,930</u>	<u>7,164,688</u>
	<u><b>\$ 10,763,351</b></u>	<u>\$ 14,034,182</u>

### NOTE 5 – INVENTORIES

Inventories consisted of the following at June 30:

	<u>2005</u>	<u>2004</u>
Bookstore	\$ 2,873,905	\$ 2,727,211
Food Service	196,912	117,890
Physical Plant	2,196,620	2,018,917
Professional and Scientific Supplies	948,231	1,259,220
Office Supplies	674,490	534,185
Other	<u>392,936</u>	<u>627,590</u>
	<u><b>\$ 7,283,094</b></u>	<u>\$ 7,285,013</u>

### NOTE 6 – LOANS TO STUDENTS

Student loans made through the Federal Perkins Loan Program comprise substantially all of the loans to students at June 30, 2005 and 2004. The Program provides for cancellation of a loan at rates of 10% to 30% per year up to a maximum of 100% if the participant complies with certain provisions. The federal government reimburses the University for amounts cancelled under these provisions.

As the University determines that loans are uncollectible and not eligible for reimbursement by the federal government, the loans are written off and assigned to the U.S. Department of Education. The University has provided an allowance for uncollectible loans, which, in management's opinion, is sufficient to absorb loans that will ultimately be written off. At June 30, 2005 and 2004, the allowance for uncollectible loans was estimated to be \$464,475 and \$452,894, respectively.

# NOTES TO THE FINANCIAL STATEMENTS

## For the Years Ended June 30, 2005 and 2004

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### NOTE 7 – CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2005 was as follows:

	<b>Restated Beginning Balance</b>	<b>Additions</b>	<b>Retirements</b>	<b>Ending Balance</b>
Land	\$ 7,660,309	\$ 54,386	\$ -	\$ 7,714,695
Land improvements	88,447	16,200	-	104,647
Works of Art	13,428,310	1,559,805	10,000	14,978,115
Infrastructure	36,285,327	2,908,942	-	39,194,269
Buildings	549,505,589	71,484,391	147,605	620,842,375
Equipment	66,286,857	6,025,190	3,616,489	68,695,558
Vehicles	9,809,285	182,280	351,096	9,640,469
Total	<u>683,064,124</u>	<u>82,231,194</u>	<u>4,125,190</u>	<u>761,170,128</u>
Less accumulated depreciation:				
Infrastructure	12,659,535	805,815	-	13,465,350
Buildings	214,045,140	17,459,066	63,528	231,440,678
Equipment	41,132,534	5,773,010	2,970,746	43,934,798
Vehicles	8,815,257	405,515	340,684	8,880,088
Total accumulated depreciation	<u>276,652,466</u>	<u>24,443,406</u>	<u>3,374,958</u>	<u>297,720,914</u>
Capital assets, net	<u>\$ 406,411,658</u>	<u>\$ 57,787,788</u>	<u>\$ 750,232</u>	463,449,214
University of Kansas Medical Center				124,056,841
University of Kansas Center for Research, Inc.				34,732,975
University of Kansas Athletic Corporation				5,723,783
University of Kansas Memorial Corporation				5,639,768
University of Kansas Lawrence and Edwards Campuses Construction In Progress				<u>8,060,584</u>
				<u>\$ 641,663,165</u>

The University elected not to capitalize its library book collections. These collections adhere to the University's policy to (a) maintain them for public exhibition, education, or research; (b) protect, keep encumbered, care for, and preserve them; and (c) require proceeds from their sale to be used to acquire other collection items. Generally accepted accounting principles permit collections maintained in this manner to be charged to operations at the time of purchase rather than be capitalized.



# NOTES TO THE FINANCIAL STATEMENTS

## For the Years Ended June 30, 2005 and 2004

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### NOTE 8 - CHANGES IN LONG-TERM LIABILITIES

Long-term liability activity for the year ended June 30, 2005 was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Current Portion</u>
Revenue bonds payable	\$ 139,625,000	\$ 109,945,000	\$ 29,375,000	\$ 220,195,000	\$ 5,440,000
Lease obligations	26,121,772	6,718,214	1,880,805	30,959,181	4,529,391
Compensated absences	25,392,885	21,444,968	19,956,263	26,881,590	21,868,454
Other long-term liabilities	<u>779,695</u>	<u>572,966</u>	<u>91,784</u>	<u>1,260,877</u>	<u>90,551</u>
Total long-term liabilities	<u>\$ 191,919,352</u>	<u>\$ 138,681,148</u>	<u>\$ 51,303,852</u>	<u>\$ 279,296,648</u>	<u>\$ 31,928,396</u>

### NOTE 9 - REVENUE BONDS OUTSTANDING

Revenue bonds payable consist of the following:

	<u>Principal Outstanding at 6/30/05</u>
Kansas Development Finance Authority Refunding Revenue Bonds – Series C, 1997 (The Board of Regents – University of Kansas Regents Center Refunding Project) \$3,255,000. Due in annual installments of \$170,000 to \$245,000. Issued 3/15/97 with a final maturity on 12/1/10. Interest ranging from 4.70% to 5.30% payable semi-annually. At the time of issuance a rating was not applied for with respect to these bonds, and no insurance was purchased. The underlying revenue stream was assigned a A1 post sale rating by Moody’s Investor Service.	\$ 1,625,000
Kansas Development Finance Authority Revenue Bonds - Series D, 1998 (The Board of Regents - University of Kansas Housing System Renovation Project - Lewis Hall) \$4,290,000. Due in annual installments of \$100,000 to \$690,000. Issued 3/1/98 with a final maturity on 5/1/23. Interest ranging from 3.70% to 5.05% payable semi-annually. A rating of Aa3 was assigned by Moody’s Investor Service. The bonds were upgraded to Aaa with the addition of an insurance policy issued by MBIA Insurance Corporation.	3,580,000
Kansas Development Finance Authority Revenue Bonds - Series H, 1998 (The Board of Regents - University of Kansas Continuing Education Building Purchase Project) \$2,320,000. Due in annual installments of \$105,000 to \$420,000. Issued 6/1/98 with a final maturity on 4/1/13. Interest ranging from 3.75% to 4.80% payable semi-annually. A rating of A2 was assigned by Moody’s Investor Service, and no insurance was purchased. Moody’s upgraded the bonds rating to A1 as of 7/23/04.	1,510,000
Kansas Development Finance Authority Revenue Bonds – Series C, 1999 (The Board of Regents – University of Kansas Child Care Facility Construction Project) \$3,085,000. Due in annual installments of \$100,000 to \$470,000. Issued 6/1/99 with a final maturity on 5/1/19. Interest ranging from 4.00% to 5.10% payable semi-annually. A rating of A1 was assigned by Moody’s Investor Service. The bonds were upgraded to Aaa with the addition of an insurance policy issued by Ambac Assurance Corporation.	2,555,000

# NOTES TO THE FINANCIAL STATEMENTS

## For the Years Ended June 30, 2005 and 2004

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	Principal Outstanding at 6/30/05
Kansas Development Finance Authority Revenue Bonds – Series D, 1999 (The Board of Regents – University of Kansas - Parking Garage #2 Construction Project) \$11,170,000. Due in annual installments of \$560,000 to \$2,085,000. Issued 5/1/99 with final maturity on 4/1/14. Interest ranging from 4.00% to 4.75% payable semi-annually. A rating of Aa3 was assigned by Moody’s Investor Service, and no insurance was purchased.	\$ 8,190,000
Kansas Development Finance Authority Refunding Revenue Bonds - Series 2001 G-4 (The Board of Regents – University of Kansas - Lawrence Campus Parking Facilities) \$2,825,000. Due in annual installments of \$335,000 to \$700,000. Issued 6/15/01 with final maturity on 4/1/08. Interest ranging from 4.25% to 5.00% payable semi-annually. A rating of Aaa was assigned by Moody’s Investor Service based upon an insurance policy issued by Ambac Assurance Corporation. The underlying revenue stream was assigned an Aa3 post sale rating by Moody’s Investor Service.	1,470,000
Kansas Development Finance Authority Revenue Bonds – Series 2001 T-2 (The Board of Regents – University of Kansas Student Union Renovation and Expansion Project) \$4,435,000. Due in annual installments of \$300,000 to \$540,000. Issued 8/1/01 with final maturity on 4/1/13. Interest ranging from 3.10% to 4.75% payable semi-annually. A rating of AAA was assigned by Standard & Poor’s based upon an insurance policy issued by Ambac Assurance Corporation. The underlying revenue stream was assigned an Aa3 post sale rating by Moody’s Investor Service.	3,205,000
Kansas Development Finance Authority Revenue Bonds - Series 2002 A-1 (The Board of Regents – University of Kansas Housing System Renovation Project - Ellsworth Hall) \$11,230,000. Due in annual installments of \$45,000 to \$1,280,000. Issued 4/1/02 with final maturity on 5/1/27. Interest ranging from 3.50% to 5.00% payable semi-annually. A rating of AAA was assigned by Standard & Poor’s based upon an insurance policy issued by Ambac Assurance Corporation. The underlying revenue stream was assigned an Aa3 post sale rating by Moody’s Investor Service.	10,765,000
Kansas Development Finance Authority Revenue Bonds - Series 2002 A-2 (The Board of Regents – University of Kansas Student Recreation and Fitness Center) \$15,330,000. Due in annual installments of \$735,000 to \$1,350,000. Issued 4/1/02 with final maturity on 5/1/17. Interest ranging from 3.50% to 5.00% payable semi-annually. A rating of AAA was assigned by Standard & Poor’s based upon an insurance policy issued by Ambac Assurance Corporation. The underlying revenue stream was assigned a Aa3 post sale rating by Moody’s Investor Service.	12,945,000
Kansas Development Finance Authority Revenue Bonds – Series 2002 K (The Board of Regents – University of Kansas Edwards Campus Project) \$5,120,000. Due in annual installments of \$65,000 to \$540,000. Issued 11/1/02 with a final maturity on 12/1/22. Interest ranging from 4.3% to 5.0% payable semi-annually. A rating of A was assigned by Moody’s Investor Service, and no insurance was purchased. Moody’s Investor Service upgraded the bonds rating to A1 as of 7/23/04.	5,120,000
Kansas Development Finance Authority Revenue Bonds – Series 2003 C (The Board of Regents – Research and Development Facilities Projects) \$4,965,000. Due in annual installments of \$450,000 to \$1,890,000. Issued 2/1/03 with a final maturity on 10/1/10. Interest ranging from 3.3% to 5.0% payable semi-annually. A rating of AAA was assigned by Standard & Poor’s based upon an insurance policy issued by Ambac Assurance Corporation.	3,075,000

# NOTES TO THE FINANCIAL STATEMENTS

## For the Years Ended June 30, 2005 and 2004

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	Principal Outstanding at 6/30/05
<p>Kansas Development Finance Authority Revenue Bonds - Series 2005E-1 (The Board of Regents – University of Kansas Housing System 1996E Templin Hall Refunding Project) \$3,065,000. Due in annual installments of \$155,000 to \$270,000. Issued 5/1/05 with a final maturity on 5/1/21. Interest ranging from 3.0% to 5.0% payable semi-annually. A rating of Aa3 was assigned by Moody’s Investor Service. The bonds were upgraded to Aaa with the addition of an insurance policy issued by Ambac Assurance Corporation.</p>	\$ 3,065,000
<p>Kansas Development Finance Authority Revenue Bonds - Series 2005E-1 (The Board of Regents – University of Kansas Housing System Hashinger Hall Renovation) \$12,965,000. Due in annual installments of \$125,000 to \$2,015,000. Issued 5/1/05 with a final maturity on 5/1/30. Interest ranging from 3.0% to 4.5% payable semi-annually. A rating of Aa3 was assigned by Moody’s Investor Service. The bonds were upgraded to Aaa with the addition of an insurance policy issued by Ambac Assurance Corporation.</p>	12,965,000
<p>Kansas Development Finance Authority Revenue Bonds – Series 1999 B (The Board of Regents – University of Kansas Medical Center for Health in Aging) \$2,920,000. Due in annual installments of \$90,000 to \$440,000. Issued 4/1/99 with final maturity on 4/1/19. Interest ranging from 3.60% to 5.00% payable semi-annually. The bonds were rated at A- by Standard &amp; Poor’s at the time of issuance. The rating was upgraded to AAA with the purchase of insurance.</p>	2,410,000
<p>Kansas Development Finance Authority Revenue Bonds – Series 2001 T-1 (The Board of Regents – University of Kansas Medical Center Research Support Facility) \$5,860,000. Due in annual installments of \$180,000 to \$880,000. Issued 4/1/01 with final maturity on 4/1/21. Interest ranging from 3.10% to 5.00% payable semi-annually. The bonds were rated at A- by Standard &amp; Poor’s at the time of issuance. The rating was upgraded to AAA with the purchase of insurance.</p>	5,280,000
<p>Kansas Development Finance Authority Revenue Bonds – Series 2003 C (The Board of Regents – University of Kansas Medical Center Scientific Research and Development Facilities Projects) \$36,100,000. Due in annual installments ranging from \$3,220,000 to \$5,430,000. Issued 2/1/03 with a final maturity on 4/1/21. Interest ranging from 2.13% to 5.01% payable semi-annually. The bonds were rated at AA by Standard &amp; Poor’s at the time of issuance. A rating of AAA was assigned by Standard &amp; Poor’s based upon an insurance policy issued by Ambac Assurance Corporation.</p>	36,100,000
<p>Kansas Development Finance Authority Revenue Bonds – Series 2003 J-1 (The Board of Regents – University of Kansas Medical Center Energy Conservation Project) \$13,080,000. Due in annual installments ranging from \$350,000 to \$1,060,000. Issued 8/3/03 with a final maturity of 8/1/24. Interest ranging from 2.00% to 4.75% payable semi-annually. The bonds were rated at AA by Standard &amp; Poor’s and Aa2 by Moody’s at the time of issuance. The rating was upgraded to AAA with the purchase of insurance.</p>	13,080,000
<p>Kansas Development Finance Authority Revenue Bonds – Series 2005D (The Board of Regents – University of Kansas Medical Center Scientific Research and Development Facilities Projects) \$27,130,000. Due in annual installments ranging from \$1,170,000 to \$3,935,000. Issued 10/1 with a final maturity on 10/1/15. Interest ranging from 3.90% to 4.80% payable semi-annually. The bonds were rated at AA by Standard &amp; Poor’s at the time of issuance. The rating was upgraded to AAA with the purchase of insurance.</p>	27,130,000

# NOTES TO THE FINANCIAL STATEMENTS

## For the Years Ended June 30, 2005 and 2004

	Principal Outstanding at 6/30/05
Kansas Development Finance Authority Revenue Bonds – Series 2005E-2 (The Board of Regents – University of Kansas Medical Center Parking Garage #3) \$3,330,000. Due in annual installments ranging from \$120,000 to \$225,000. Issued 5/1/05 with a final maturity on 5/1/25. Interest ranging from 3.00% to 5.00% payable semi-annually. The underlying revenue stream was assigned an A1 rating by Moody’s Investor Service. The bonds were upgraded to Aaa with the addition of an insurance policy issued by Ambac Assurance Corporation.	\$ 3,330,000
Kansas Development Finance Authority Revenue Bonds – Series 2004K (The Board of Regents – University of Kansas Athletic Corporation – Restructuring Project) \$17,830,000. Due in annual installments of \$660,000 to \$1,355,000. Issued 11/16/04 with final maturity on 6/1/2023. Interest ranging from 3.3% to 4.5% payable semi-annually. A rating of A was assigned by Standard & Poor’s.	17,170,000
Kansas Development Finance Authority Revenue Bonds – Series 2005B (The Board of Regents – University of Kansas Center for Research, Inc. Project) \$45,625,000. Due in annual installments of \$1,565,000 to \$3,610,000. Issued 2/1/05 with a final maturity on 2/1/25. Interest ranging from 3.6% to 5.3% payable semi-annually. A rating of A1 was assigned by Moody’s. The bonds were upgraded to Aaa with the purchase of a surety bond issued by MBIA Insurance Corporation.	45,625,000

### NOTE 10 - REVENUE BONDS MATURITY SCHEDULE

Maturities of principal and interest requirements on revenue bonds payable are as follows:

Year Ending June 30:	Principal	Interest	Total
2006	\$ 5,440,000	\$ 9,958,453	\$ 15,398,453
2007	11,005,000	9,971,657	20,976,657
2008	10,380,000	9,487,887	19,867,887
2009	10,070,000	9,080,921	19,150,921
2010	10,495,000	8,670,092	19,165,092
2011-2015	52,260,000	36,606,676	88,866,676
2016-2020	55,345,000	24,074,557	79,419,557
2021-2025	55,980,000	9,286,211	65,266,211
2026-2030	9,220,000	1,301,363	10,521,363
Total	<u>\$ 220,195,000</u>	<u>\$ 118,437,817</u>	<u>\$ 338,632,817</u>

The University defeased two separate bond series through advance refunding during fiscal year 2005 and, accordingly, neither series is reflected in the accompanying statements. The amount of bonds that have been defeased as of June 30, 2005 consists of the following:

Series	Outstanding at June 30, 2005
1998 A	\$ 16,635,000
2001 G-5	1,540,000
Total	<u>\$ 18,175,000</u>

# NOTES TO THE FINANCIAL STATEMENTS

## For the Years Ended June 30, 2005 and 2004

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### NOTE 11 - LEASE OBLIGATIONS

The University of Kansas is obligated for the purchase of certain equipment funded through the issuance of blanket financing agreements in the amount of \$30,959,181 and \$26,121,772 as of June 30, 2005 and 2004, respectively. Included in this balance is the \$18.7 million Master Lease Purchase agreement between the University and the State for the University's Energy Performance Contract. The University's Energy Performance Contract consists of approximately 100 energy saving measures that are expected to result in annual utility and maintenance savings of \$1.7 million. The projects are funded through a Master Lease Purchase Agreement between the State of Kansas and Citibank, N.A. The University is responsible for repaying the State for the 20-year term of the lease. Payments to liquidate these obligations are scheduled as follows:

Fiscal Year 2006 Total	\$	4,529,391
Fiscal Year 2007 Total		2,820,138
Fiscal Year 2008 Total		2,861,650
Fiscal Year 2009 Total		2,598,700
Fiscal Year 2010 Total		1,956,319
Fiscal Year 2011 and thereafter Total		<u>16,192,983</u>
Total	\$	<u>30,959,181</u>

### NOTE 12 - RETIREMENT PLANS

University employees participate in two separate retirement programs. Classified employees participate in the "Kansas Public Employees Retirement System" (KPERs). This defined benefit program is funded through contributions by the University and the individual employees. The University contributed \$2,591,810 and \$2,301,012 during fiscal years 2005 and 2004, respectively, and individual employees contributed \$2,100,490 and \$2,022,597. Unclassified employees participate in the "Board of Regents Retirement Program". This defined contribution program is funded through contributions by the University and the individual employees. The University contributed \$22,229,303 and \$21,025,943 during fiscal years 2005 and 2004, respectively, and individual employees contributed \$14,372,430 and \$13,506,773. In addition, the University contributed \$0 and \$718 to KPERs for prior service benefits during fiscal years 2005 and 2004, respectively.

Employees of the University of Kansas Athletic Corporation, the University of Kansas Memorial Corporation, the University of Kansas Medical Center Research Institute, the Student Union Corporation of the University of Kansas Medical Center, and Kansas University Physicians, Inc. participate in defined contribution programs similar to the "Board of Regents Retirement Program". The Corporations contributed \$2,967,393 and \$2,576,541 to their individual plans during fiscal years 2005 and 2004, respectively.

### NOTE 13 - COMMITMENTS AND CONTINGENT LIABILITIES

At June 30, 2005 and 2004 the University had outstanding commitments under construction contracts totaling \$97,071,050 and \$74,505,419, respectively.

The University is a defendant in several lawsuits. However, University officials are of the opinion, based on advice of in-house legal counsel, that the ultimate outcome of all litigation will not have a material effect on the future operations or financial position of the University.

The University maintains specific insurance coverage as allowed by the State of Kansas and as required by outstanding bond issues. To a large extent, the State follows a policy of self-insurance; therefore, most claims against the University require legislative approval (and potential funding) prior to settlement. The University is not aware of any significant outstanding claims as of June 30, 2005.

# NOTES TO THE FINANCIAL STATEMENTS

## For the Years Ended June 30, 2005 and 2004

The State does not insure buildings and contents valued under \$0.5 million and does not insure State-owned automobiles for bodily injury and property damages. State buildings valued over \$0.5 million are insured against catastrophic loss with a \$5.0 million deductible per occurrence and a maximum annual liability of \$100 million per occurrence.

In the normal course of operations, the University receives grants and other forms of reimbursement from various Federal and State agencies. These activities are subject to audit by agents of the funding authority, the purpose of which is to ensure compliance with conditions precedent to providing of such funds. University officials believe that the liability, if any, for any reimbursement that may arise as the result of audits, would not be material.

### NOTE 14 – NATURAL CLASSIFICATIONS WITH FUNCTIONAL CLASSIFICATIONS

The University's operating expenses by functional and natural classification are as follows:

	Compensation & Benefits	Scholarships & Fellowships	Utilities	Supplies & Other Services	Depreciation	Total
Educational and general						
Instruction	\$ 230,662,687	\$	\$ 112,785	\$ 27,309,990	\$	\$ 258,085,462
Research	104,319,573		9,462	70,195,494		174,524,529
Patient care	26,436,434			66,942,409		93,378,843
Public service	9,727,395		1,235	7,489,162		17,217,792
Academic support	46,232,877		3,890	17,774,385		64,011,152
Student services	15,063,566		214,803	7,863,376		23,141,745
Institutional support	33,155,108		22,277	9,669,566		42,846,951
Operations and maintenance of plant	27,712,130		18,857,344	8,986,595		55,556,069
Depreciation					36,480,274	36,480,274
Scholarships and fellowships		19,047,784				19,047,784
Auxiliary enterprises:						
Housing	9,763,312		2,564,634	9,338,919		21,666,865
Athletics	15,673,628	5,730,319	83,092	16,640,871		38,127,910
Parking	1,563,862		127,437	2,124,685		3,815,984
Student unions	6,181,549		531,958	13,749,452		20,462,959
University health services	4,662,626		705	3,310,107		7,973,438
Other auxiliary enterprises	4,546,404		853	498,856		5,046,113
Other	502,122			1,088,647		1,590,769
<b>Total</b>	<b>\$ 536,203,273</b>	<b>\$ 24,778,103</b>	<b>\$ 22,530,475</b>	<b>\$ 262,982,514</b>	<b>\$ 36,480,274</b>	<b>\$ 882,974,639</b>

### NOTE 15 – OTHER NON-OPERATING REVENUE

Through July 2004, the University had received certain royalty payments in connection with a License Agreement that was executed between the University and another entity. In July 2004, the University executed an agreement whereby the other entity bought out the Patent Rights covered by the License Agreement. In connection with the buyout agreement, the University received \$4.0 million, which has been recorded as other non-operating revenue in fiscal year 2005.

# NOTES TO THE FINANCIAL STATEMENTS

## For the Years Ended June 30, 2005 and 2004

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### **NOTE 16 – PRIOR YEAR ADJUSTMENTS**

The June 30, 2004 statements have been restated for the following reasons:

In prior periods, the University of Kansas Medical Center Research Institute accounted for certain liabilities (deferred income and funds held for researchers) as temporarily restricted net assets. The University of Kansas Medical Center Research Institute's beginning net assets have been restated to properly reflect such items as liabilities on the accompanying statement of financial position. The restatement decreased the previously reported July 1, 2004 unrestricted and temporarily restricted net assets by \$2,724,389 and \$7,155,224, respectively.

Additionally net capital assets were improperly recorded as of July 1, 2003. In fiscal year 2005, litigation involving the completed renovation of Memorial Stadium was finally settled, and KUAC transferred the construction costs that it had capitalized as construction-in-progress between 1998-2005 to the University. It was due to this transfer that the University discovered that it had incorrectly capitalized expenses related to this renovation that had flowed through the University's accounting system due to requirements established by the State in 1998. As the University prior to the completion and transfer of the asset from KUAC should not have capitalized the project, the decision was made to correct the error within the University's beginning balances. The effect of this correction was a decrease to capital assets and investment in capital assets, net of debt by \$18,445,241.