KPMG

BRANDEIS UNIVERSITY

Financial Statements

June 30, 2004 and 2003

(With Independent Auditors' Report Thereon)

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Independent Auditors' Report

The Board of Trustees
Brandeis University:

We have audited the accompanying statement of financial position of Brandeis University (the University) as of June 30, 2004, and the related statements of activities and cash flows for the year then ended. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the University as of and for the year ended June 30, 2003 were audited by other auditors whose report thereon, dated September 17, 2003, expressed an unqualified opinion.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2004 financial statements referred to above present fairly, in all material respects, the financial position of the University as of June 30, 2004 and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

September 17, 2004

BRANDEIS UNIVERSITY

Statements of Financial Position

June 30, 2004 and 2003

(In thousands)

Assets		**2004**	**2003**
Cash and cash equivalents	$	50,950	59,465
Accounts receivable, net (note 2)		9,560	9,063
Notes receivable, net (note 3)		12,876	12,705
Other assets		5,636	5,097
Pledges receivable, net (note 4)		51,653	46,611
Funds held under bond agreement		22,354	248
Investments, at fair value (note 5)		495,404	419,890
Funds held in trust by others		9,508	9,020
Property, plant and equipment, net (note 6)		169,307	162,057
Total assets	$	827,248	724,156
Liabilities			
Accounts payable and other accrued liabilities (note 5)	$	28,543	26,243
Sponsored program advances and deferred income		8,942	9,267
Accrued interest payable – capital appreciation bonds (note 7)		17,350	18,159
Long-term debt, net (note 7)		137,893	115,571
Refundable advances for student loans (note 3)		6,385	6,394
Total liabilities		199,113	175,634
Net assets (note 8):			
Unrestricted		96,923	78,762
Temporarily restricted		177,213	133,750
Permanently restricted		353,999	336,010
Total net assets		628,135	548,522
Total liabilities and net assets	$	827,248	724,156

See accompanying notes to financial statements.

BRANDEIS UNIVERSITY

Statements of Activities

Years ended June 30, 2004 and 2003

(In thousands)

	2004	2003
Changes in unrestricted net assets:		
Revenues and gains:		
Tuition and fees	$ 122,249	109,100
Residence hall and dining	22,015	18,804
Total tuition, fees, residence hall and dining	144,264	127,904
Less scholarships and financial aid to students	(44,643)	(39,769)
Net student fees	99,621	88,135
Contributions	6,202	7,594
Sponsored programs, grants and contracts	50,350	48,068
Investment earnings (note 5)	7,997	5,352
Investment income from funds held in trust by others	297	319
Other	6,145	6,101
Total revenues and gains	170,612	155,569
Net assets released from restrictions	46,851	50,846
Total unrestricted revenues, gains and other support	217,463	206,415
Expenses and losses:		
Instructional and sponsored programs	118,912	116,897
Libraries	11,504	10,538
Student services	16,109	15,006
General and administrative	19,369	17,272
Development	10,201	10,089
Auxiliary enterprises	24,818	22,647
Other	984	287
Net transfer to record market value decline in donor restricted endowments (notes 5 and 8)	(2,595)	(2,182)
Total expenses and losses	199,302	190,554
Increase in unrestricted net assets	18,161	15,861
Changes in temporarily restricted net assets:		
Contributions	37,188	35,746
Investment earnings (note 5)	56,740	17,318
Change in value of split interest agreements	(637)	(337)
Net assets released from restrictions	(47,233)	(48,424)
Net transfer to record market value decline in donor restricted endowments (notes 5 and 8)	(2,595)	(2,182)
Increase in temporarily restricted net assets	43,463	2,121
Changes in permanently restricted net assets:		
Contributions	15,735	25,370
Investment earnings (note 5)	2,224	3,705
Change in value of funds held in trust by others	492	(188)
Change in value of split interest agreements	(746)	104
Donors’ clarification of intent	284	(2,764)
Increase in permanently restricted net assets	17,989	26,227
Change in net assets	79,613	44,209
Net assets at beginning of year	548,522	504,313
Net assets at end of year	$ 628,135	548,522

See accompanying notes to financial statements.

BRANDEIS UNIVERSITY

Statements of Cash Flows

Years ended June 30, 2004 and 2003

(In thousands)

		2004	2003
Cash flows from operating activities:			
Change in net assets	$	79,613	44,209
Adjustments to reconcile change in net assets to cash provided by (used in) operating activities:			
Depreciation and amortization		12,606	11,155
Net realized and unrealized investment gain		(54,270)	(13,288)
Net change from funds held in trust by others		(488)	188
Loss on the disposal and impairment of property, plant, and equipment		13	108
Contributions restricted for long-term investment		(29,021)	(40,115)
Change in other assets		(6,078)	(6,920)
Change in other liabilities		1,157	1,051
Net cash provided by (used in) operating activities		3,532	(3,612)
Cash flows from investing activities:			
Acquisitions of buildings and equipment		(19,759)	(36,245)
Purchases of investments		(182,374)	(247,716)
Proceeds from sale and maturities of investments		161,130	259,921
Change in notes receivable, net		(171)	327
Net cash used in investing activities		(41,174)	(23,713)
Cash flows from financing activities:			
Repayments of bonds, notes and leases		(3,347)	(1,488)
Proceeds from issuance of bonds, notes, and leases		25,559	1,746
Decrease in funds held under bond agreement		(22,106)	13
Contributions restricted for long-term investment		29,021	40,115
Net cash provided by financing activities		29,127	40,386
Change in cash and cash equivalents		(8,515)	13,061
Cash and cash equivalents as of beginning of year		59,465	46,404
Cash and cash equivalents as of end of year	$	50,950	59,465
Supplemental data:			
Interest paid	$	8,096	5,242

See accompanying notes to financial statements.

(1) Significant Accounting Policies

Brandeis University (the University) is a private, coeducational institution of higher learning and research. Founded in 1948 and located in Waltham, Massachusetts, the University is a tax-exempt organization as described in Section (501)(c)(3) of the Internal Revenue Code (the Code) and is generally exempt from income taxes pursuant to Section 501(a) of the Code.

(a) Basis of Accounting

The University's financial statements are prepared on the accrual basis of accounting and in accordance with accounting principles generally accepted in the United States of America.

Depreciation, interest and operation of plant expenses are allocated to functional expense categories on the basis of square feet utilized.

The classification of net assets, revenues, expenses, gains and losses into three categories is based on the existence or absence of donor-imposed restrictions. The three categories are defined as follows:

Unrestricted – Net assets not subject to donor-imposed restrictions.

Temporarily restricted – Net assets with use limited by law or by donor-imposed restrictions as to purpose or time. Life income trusts and pledges receivable for which the ultimate use is not permanently restricted are reported as temporarily restricted.

Permanently restricted – Net assets subject to donor-imposed restrictions that require the assets to be invested in perpetuity.

(b) Revenue Recognition

Revenues are reported as an increase in unrestricted net assets, unless the use of the related assets is limited by donor-imposed restrictions or by law. Expenses are reported as a decrease in unrestricted net assets. Expiration of temporary restrictions are reflected in the accompanying Statements of Activities as net assets released from restrictions. Net realized gains (losses) from the sale or other disposition of investments and the change in unrealized appreciation (depreciation) of investments are reported as revenue in unrestricted net assets, unless use of these gains is restricted by donor-imposed stipulations or by law. Realized gains (losses) are computed using the average cost basis of securities sold.

Revenues associated with research and other grants and contracts are recognized when the related expenses are incurred. Indirect cost recovery by the University on federal grants and contracts is based upon a predetermined negotiated rate and is recorded as unrestricted revenue.

Student deposits, along with advance payments for tuition, room, and board for fall and certain summer sessions are deferred and will be recorded as revenues in the year in which the sessions are completed.

(c) Contributions and Pledges

Contributions are nonreciprocal unconditional transfers of assets or cancellations of liabilities. Contributions received without donor-imposed restrictions are recorded as unrestricted revenue. Contributions received with donor-imposed restrictions are reported as revenue in the temporarily restricted or permanently restricted net asset category according to donors' restrictions. Contributions of noncash assets are recorded at fair market value on the date of the contribution.

Unconditional promises to give are recognized as temporarily or permanently restricted revenues in the year the pledges are received. Pledges are recorded as assets at the present value of the expected cash flow using discount rates of 2.3% to 6.0%, net of an allowance for unfulfilled pledges based upon collection experience and other relevant factors. Conditional pledges are not recognized until the stated conditions are met.

(d) Cash and Cash Equivalents

The University records all liquid investments purchased with an original maturity of three months or less as cash equivalents.

(e) Investments and Funds Held under Bond Agreements

Investments and funds held under bond agreements are stated at market value as determined by the investment custodians using market quotations. Real estate participation and securities and alternative investments with no readily available market quotations, totaling $10,093 in 2004 and $11,436 in 2003, are stated at cost (note 5).

(f) Funds Held in Trust by Others

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

(g) Property, Plant and Equipment

Property, plant, and equipment are stated at cost or, if contributed, the fair market value on the date of contribution, less accumulated depreciation. Depreciation is computed on a straight-line basis over the estimated useful lives of land improvements (18 years), buildings (35-60 years), building systems and improvements (18-25 years) and equipment and furnishings (3-15 years). Equipment purchased with grant funds is expensed; disposition of grant-funded equipment follows the applicable agency or foundation guidelines.

(h) Sponsored Programs, Grants and Contracts

Sponsored activities include various research and instructional programs funded by external parties including the federal government, foreign and state governments and private foundations and corporations. Revenues associated with sponsored programs, grants, and contracts are recognized when related costs are incurred. Under the terms of federal grants, periodic audits are required and costs may be questioned and subject to reimbursement. It is believed that the outcome of such audits will not have a material effect on the financial position of the University.

(In thousands)

(i) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(j) Other Assets

Other assets include unamortized debt issuance costs, other prepayments, and inventories.

(k) Reclassification

Certain 2003 balances have been reclassified to conform to the 2004 presentation.

(2) Accounts Receivable

The composition of accounts receivable as of June 30 is as follows:

		2004	2003
Student receivables	$	1,250	1,601
Sponsored programs grants receivable		6,185	6,099
Investment income receivable		1,452	1,266
Other		1,106	841
		9,993	9,807
Less allowance for doubtful accounts		(433)	(744)
Accounts receivable, net	$	9,560	9,063

(3) Notes Receivable

The composition of the notes receivable as of June 30 is as follows:

		2004	2003
Federal Perkins Loan Program	$	6,831	6,684
University loan programs		7,119	7,008
		13,950	13,692
Less allowance for doubtful loans		(1,074)	(987)
Notes receivable, net	$	12,876	12,705

(In thousands)

Notes receivable include funds advanced to the University by the U.S. government under the Federal Perkins Loan Program (the Program). Notes receivable under the Program are subject to significant restrictions. Such funds are reloaned by the University after collection, but in the event that the University no longer participates in the Program, the amounts are generally refundable to the U.S. government. Accordingly, it is not practicable to determine the fair value of such amounts.

(4) Pledges Receivable

The composition of pledges receivable as of June 30 is as follows:

		2004	2003
Amounts due in:			
One year or less	$	27,848	21,948
Between one and five years		27,687	27,315
More than five years		5,758	6,891
Gross pledges receivable		61,293	56,154
Less:			
Discount		(3,270)	(3,741)
Allowance for unfulfilled pledges		(6,370)	(5,802)
Pledges receivable, net	$	51,653	46,611

Pledges receivable have been discounted at rates ranging from 2.3% to 6.0%.

(5) Investments

The University's investments are comprised of the following:

		2004	2003
Cash and cash equivalents	$	11,111	21,292
Fixed income		111,370	108,046
Equities		212,729	169,801
Real estate		5,218	6,754
Alternative investments		154,976	113,997
Investments, at fair value	$	495,404	419,890

The majority of permanently restricted net assets is true endowment and is pooled for investment purposes. Income earned is allocated to the appropriate net asset category, based upon the unit share method. At June 30, 2004 and 2003, additional pooled endowment cash of $8,548 and $21,206, respectively, is classified as cash and cash equivalents not as investments.

Investments include gift annuities and charitable remainder trusts. These funds are held in trust for one or more beneficiaries, and generally pay lifetime income to those beneficiaries, after which the principal is

(Continued)

(In thousands)

made available to the University in accordance with donor intentions. The assets are recorded at fair market value and liabilities are recorded to recognize the present value of estimated future payments due to beneficiaries. The liabilities of $13,480 in 2004 and $9,664 in 2003 are included in accounts payable and other liabilities in the Statements of Financial Position.

Alternative investments consist primarily of privately-held equity and hedge funds that follow primarily event driven, absolute return and long-short equity investment strategies. Alternative investments of $148,294 in 2004 and $105,972 in 2003 are carried at their estimated fair market value, based on valuations provided by external investment managers. Since these investments are not readily marketable, their estimated value is subject to uncertainty and therefore may differ from the value that would have been used had a ready market for such investments existed. The University's Investment Committee approves and monitors these estimated values. The remaining alternative investments of $6,682 in 2004 and $8,025 in 2003 are carried at cost, which approximates fair value. Alternative investments represent approximately 30% of total investments.

The University has agreed to make additional capital contributions of up to $2,150 in a private equity fund and up to $5,000 in a private timber fund. The timing and amounts of the contributions will be determined by the general partners.

The following summarizes the investment return for all investments for the years ended June 30:

		2004	2003
Investment income	$	12,691	13,088
Net realized gain (loss)		14,468	(4,031)
		27,159	9,057
Less management fees		(1,455)	(1,325)
		25,704	7,732
Net change in unrealized appreciation		39,802	17,319
Investment earnings	$	65,506	25,051

The Board of Trustees approved a spending policy, which authorizes the use of a prudent amount of capital appreciation in accordance with provisions of the Massachusetts Uniform Management of Institutional Funds Act. Accumulated capital gains spent in 2004 and 2003 amount to $14,794 and $6,389, respectively. The funds are utilized principally for financial aid and support of faculty chairs. Future utilization of gains is dependent on market performance. Deficiencies in donor-restricted endowment funds, resulting from declines in market value, have been offset by transfers from unrestricted net assets to temporarily restricted net assets. These deficiencies totaled $0 and $2,595 at June 30, 2004 and 2003, respectively. As the market value of the portfolio increases, the deficiency is reduced. The allocation of deficiencies is recorded in accordance with FAS 124, *Accounting for Certain Investments Held by Not-for-Profit Organizations*. In the opinion of counsel, the University is under no obligation to fund this allocation.

(In thousands)

The University has relied upon the Massachusetts Attorney General's interpretation of relevant state law as generally permitting the spending of gains on permanently restricted net assets over a stipulated period of time. State law allows the Board of Trustees to appropriate all of the income and a specified percentage of the net appreciation as is prudent considering the University's long-term and short-term needs, present and anticipated financial requirements, expected total return on its investments, price level trends, and general economic conditions. Under the University's spending policy, which is deemed to be within the guidelines specified under state law, a percentage of permanently restricted long-term investments is appropriated annually as determined by the University's Board of Trustees.

(6) Property, Plant and Equipment

The composition of property, plant and equipment as of June 30 is as follows:

		2004	2003
Land and land improvements	$	14,044	12,943
Buildings		81,520	71,065
Building systems and improvements		180,998	155,481
Equipment and furnishings		63,540	59,444
		340,102	298,933
Less accumulated depreciation		(175,054)	(163,001)
Construction in progress		4,259	26,125
Property, plant and equipment, net	$	169,307	162,057

Depreciation expense amounted to $12,496 in 2004 and $11,050 in 2003. Operation and maintenance expenses amounted to $22,940 in 2004 and $21,683 in 2003.

Expenses for the repairs and maintenance of facilities are recorded during the period incurred; betterments, which add to the value of the related assets or materially extend the life of the assets, are capitalized. At the time of disposition, the cost and associated accumulated depreciation are removed from the related accounts and gains or losses are reported as unrestricted revenue or expense.

The University has commitments to expend approximately $4,600 to complete various construction projects as of June 30, 2004.

(Continued)

(In thousands)

(7) Indebtedness

Outstanding debt as of June 30 consists of the following:

		2004	2003
Commonwealth of Massachusetts Health and Educational Facilities Authority (MHEFA) Brandeis University Issue Series J Revenue Bonds at an interest rate of 5%, maturing October 1, 2024 through October 1, 2026.	$	19,120	19,120
Commonwealth of Massachusetts Health and Educational Facilities Authority (MHEFA) Brandeis University Issue Series I Revenue Bonds at effective interest rates from 4.67% to 5.125%, maturing October 1, 2012 through October 1, 2028		82,380	82,380
Commonwealth of Massachusetts Industrial Finance Agency (MIFA) Revenue Bonds, Brandeis University Issue 1989 Series C, at interest rates from 6.40% to 6.85%, maturing in annual installments from October 1, 2003 through October 1, 2011.		10,000	11,688
Commonwealth of Massachusetts Development Finance Agency (MDFA) Revenue Bonds, Brandeis University Issue 2004 Series K, at interest rates from 2.0% to 4.94%, maturing in annual installments from October, 2004 through October 1, 2033.		25,385	—
Capital lease with a financial services corporation as lessor, Massachusetts Health and Education Facilities Authority (MHEFA) as lessee, and Brandeis University as sub-lessee, with semiannual payments at an interest rate of 5.065% through October 1, 2005.		738	1,200
Various capital lease agreements with a financial services corporation with quarterly lease payments at interest rates from 2.57% to 10.25% through January 2006.		1,360	1,596
Various mortgage notes payable at interest rates from 0% to 8.50%, maturing in various years through November 1, 2011. See note (1)		1,622	2,024
Long-term debt before discount		140,605	118,008
Less unamortized discount		(2,712)	(2,437)
Long-term debt, net	$	137,893	115,571

(Continued)

(In thousands)

In January 2004, the University issued Massachusetts Development Finance Agency (MDFA) Revenue Bonds, Brandeis University Issue, Series K, in the amount of $25,385. The proceeds of the Series K Bonds are being used to finance a major infrastructure renewal project on the University's campus over the next two to three years.

During fiscal years 2004 and 2003 the University obtained lease financing through financial services corporations in the amount of $560 and $481, respectively, for the installation of network wiring and acquisition of computer equipment.

Dining facilities renovations have been financed by loans from a University vendor. The outstanding balance of $1,181 at June 30, 2004 is included in notes payable and will be repaid in installments through January, 2009.

MIFA 1989 Series C capital appreciation bonds require interest to be paid when the principal on the bonds is due. The capital appreciation bonds mature in 2003 through 2011. The University accrues for the capital appreciation interest currently, the balance at June 30, 2004 and 2003 was $17,350 and $18,159 respectively.

The University has a $25,000 line of credit, with a variable rate of interest at prime or a fixed rate at LIBOR plus 1% that is redetermined on a 30 to 90 day basis. There was no amount outstanding as of June 30, 2004 and 2003.

The fair market value of the external debt is estimated to be approximately $2,000 more than the aggregate carrying value at June 30, 2004. The University's payments for debt and lease obligations are as follows:

		Debt	**Leases**
Year ending June 30:			
2005	$	2,398	1,152
2006		2,300	675
2007		2,207	189
2008		2,085	82
2009		1,878	—
Thereafter		127,639	—
	$	138,507	2,098

Interest expense for the years ended June 30, 2004 and 2003 was $7,547 and $7,184, respectively. $17 of the interest costs in association with the Series K Bond were capitalized in 2004, and will be amortized over the useful lives of the related assets. The bond agreements contain covenants, which among other restrictions include the maintenance of a specific amount of cash and investments not subject to legal restrictions. The University was compliant with these covenants as of June 30, 2004.

Indebtedness is collateralized as noted below:

Residence facilities with a book value of $2,129 are pledged as collateral for certain of these notes.

(Continued)

(In thousands)

In June 2003, the University contracted to lease a telephone system. The initial lease term is 36 months with options to renew for two consecutive periods of 24 and 12 months. Future minimum operating lease payments under this agreement are as follows:

		Amount
Fiscal year:		
2005	$	819
2006		819
2007		819
2008		819
2009		819
	$	4,095

(8) Net Assets

(a) Unrestricted Net Assets

Unrestricted net assets are comprised principally of internally designated reserves and investment in plant offset by the deficiencies in donor-restricted endowments.

The composition of unrestricted net assets as of June 30 is as follows:

		2004	2003
Unrestricted net assets before allocation of deficiency	$	96,923	81,357
Deficiencies in donor-restricted endowments recorded in unrestricted net assets		—	(2,595)
	$	96,923	78,762

(b) Temporarily Restricted Net Assets

Temporarily restricted net assets are gifts and income received with donor stipulations and the realized and unrealized gains on endowment assets. These assets are expendable principally for instruction or financial aid.

(In thousands)

The composition of the temporarily restricted net assets as of June 30 is as follows:

		2004	2003
Restricted gifts	$	16,202	16,465
Unexpended endowment income		4,334	3,927
Restricted gifts invested in endowment		36,422	35,426
Net realized and unrealized gain on endowment		65,964	33,511
Deficiencies in donor-restricted endowments recorded in unrestricted net assets		—	2,595
Life income and annuity funds		8,941	6,892
Pledges receivable, net		35,879	28,475
Physical plant and other		9,471	6,459
Total temporarily restricted net assets	$	177,213	133,750

(c) *Permanently Restricted Net Assets*

The composition of the permanently restricted net assets as of June 30 is as follows:

		2004	2003
Endowment funds	$	318,155	300,366
Student loan funds		4,624	4,361
Life income and annuity funds		5,936	4,127
Pledges receivable, net		15,775	18,136
Funds held in trust by others		9,509	9,020
Total permanently restricted net assets	$	353,999	336,010

(9) Retirement Programs

The University participates in defined contribution pension programs providing retirement benefits for substantially all full-time and regular part-time employees. Under the programs, the University makes monthly contributions, currently limited to 3–10% of the annual eligible wages of participants, up to defined limits. Voluntary contributions by participants are made subject to IRS defined limits. Retirement program expenses amounted to $5,559 in 2004 and $5,488 in 2003.

In addition, the University has implemented a supplemental executive retirement plan for certain senior management employees. Benefits are based on the employees' service and earnings. The Plan is a nonqualified plan under the Code and currently has no advanced funding.

(10) Related Party Transactions

The University has invested $6,682 and $8,026 as of June 30, 2004 and 2003, respectively, in a limited partnership for which a former University Trustee is a general partner. The University is committed to make additional investments of up to $1,974. The University's Investment Committee approved and continues to monitor this investment.

(11) Contingencies

The University is engaged in legal cases that have arisen in the normal course of its operations. The University believes that the outcome of these cases will not have a material adverse effect on the financial position of the University.