APPENDIX E

UNIVERSITY OF RHODE ISLAND
(A Component Unit of the State of Rhode Island
and Providence Plantations)

Financial Statements

June 30, 2006 and 2005

(With Independent Auditors' Report Thereon)

UNIVERSITY OF RHODE ISLAND
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June 30, 2006 and 2005

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KPMG LLP
600 Fleet Center
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Providence, RI 02903-2321

September 1, 2006

Independent Auditors' Report

Board of Governors for Higher Education
State of Rhode Island and Providence Plantations:

We have audited the accompanying financial statements of the business-type activities and the discretely presented component units of the University of Rhode Island (the University) (a component unit of the State of Rhode Island and Providence Plantations) as of and for the years ended June 30, 2006 and 2005, which collectively comprise the University's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the University's management. Our responsibility is to express opinions on these financial statements based on our audits. We did not audit the financial statements of the discretely presented component units. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the discretely presented component units, is based on the reports of the other auditors.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we express no such opinion. 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 audits and the reports of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audits and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and the discretely presented component units of the University as of June 30, 2006 and 2005, and the respective changes in financial position, and, where applicable, cash flows thereof for the years then ended in conformity with U.S. generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 1, 2006 on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The Management's Discussion and Analysis (MD&A) is not a required part of the financial statements but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the supplementary information and express no opinion on it.

KPMG LLP

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Management's Discussion and Analysis

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Introduction

The following management's discussion and analysis (MD&A) provides management's view of the financial position of the University of Rhode Island (the University) as of June 30, 2006 and the results of operations for the year then ended, with selected comparative information for the years ended June 30, 2005 and 2004. The purpose of the MD&A is to assist readers in understanding the accompanying financial statements by providing an objective and understandable analysis of the University's financial activities based on currently known facts, decisions, and conditions. This analysis has been prepared by management, which is responsible for the completeness and fairness of the information contained therein. The MD&A consists of highly summarized information, and it should be read in conjunction with the University's financial statements and notes thereto that follow this section.

The University is the only publicly supported research institution in the State of Rhode Island (the State) and is charged with providing state residents an opportunity for undergraduate and graduate studies at a Land Grant, Urban Grant and Sea Grant research university. As such, the University receives federal funding for land and sea research. The University had its beginning as the State Agricultural School chartered in 1888. The Morrill Act of 1862 provided the framework within which the school became the State's land-grant institution, and in 1892 the school became the Rhode Island College of Agriculture and Mechanic Arts. In 1909, the name of the College was changed to Rhode Island State College, and the program of study was revised and expanded. In 1951, the College became known as the University of Rhode Island by an act of the State's General Assembly. The Board of Governors for Higher Education became the governing body for the University in 1981.

The mission of the University is to be committed to enriching the lives of its students through its land, sea and urban grant traditions. Students, faculty, staff and alumni are united in one common purpose; to learn and lead together. The University values (1) creativity and scholarship, (2) diversity, fairness and respect, (3) engaged learning and civic involvement, and (4) intellectual and ethical leadership. As set forth in its Vision Statement, the University is building a new culture for learning. The University will share in the power of discovery through collaborative teaching, learning and research and through independent inquiry and free speech. This culture generates a spirited public life for our students, who will become engaged and productive leaders. This Vision Statement will serve as a guideline for the University's commitment to continuous improvement and high quality.

The University has a combined enrollment of about 15,000 students and offers undergraduate and graduate degree programs through the doctoral level. Its main campus is located in Kingston, Rhode Island, 30 miles south of Providence in the northeastern metropolitan corridor between New York and Boston. In addition to the Kingston Campus, the University has three other campuses – the 165-acre Narragansett Bay Campus, which is the site of the Graduate School of Oceanography; the Alan Shawn Feinstein College of Continuing Education located in downtown Providence; and the W. Alton Jones Campus located in the western Section of the State, 20 miles from Kingston. The 2,300 acres of woods, fields, streams and ponds of W. Alton Jones Campus is the site of the environmental education research programs and contains conference facilities for both public and private use.

The University has adopted a new Three-Year Strategic Plan, which seeks to: (1) enhance student recruitment, retention, involvement, and graduation rates; (2) improve the fiscal health of the University; (3) create a more

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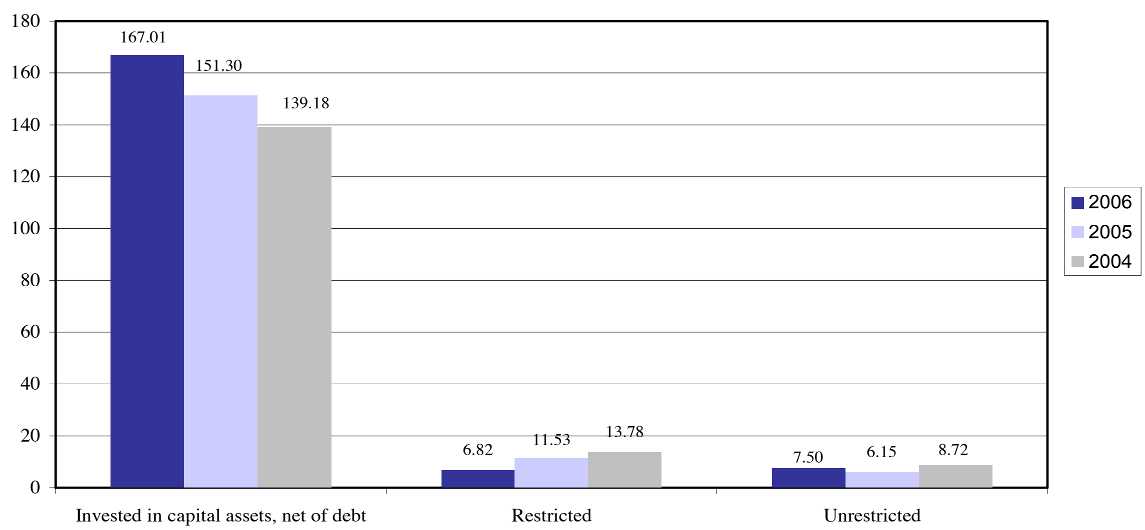
inclusive environment; and (4) improve the efficiency and effectiveness of research and outreach support. These strategic initiatives are being facilitated by community members, including the University's senior management, the Joint Strategic Planning Committee and each of the on-campus divisions. Collectively, these initiatives should help guide the decision-making at all levels in order to align limited resources with University priorities.

Financial Highlights

The University's financial position for the year ended June 30, 2006 showed a net loss before capital appropriations and gifts of $10.39 million for the year, after nonoperating revenues and expenses, compared with a net loss of $4.09 million and $2.10 million for fiscal 2005 and 2004, respectively. The $10.39 million net loss in fiscal 2006 resulted from the increase in operating expenses of $20.4 million over fiscal year 2005. The majority of the increases, $15.4 million is related to faculty and staff salaries, fringe benefits, health insurance, utilities, architect/engineering services and depreciation. Net assets increased by $12.35 million during fiscal 2006 and $7.30 million during fiscal year 2005 with the infusion of state capital appropriations and private funds totaling $22.73 million in fiscal 2006 and $11.39 million in fiscal 2005.

The following chart displays the components of the University's net assets for the fiscal years ended June 30, 2006, 2005, and 2004.

Net Assets
(Dollars in millions)



On June 30, 2006, 2005, and 2004, the University's total assets of $448.56 million, $423.60 million, and $337.76 million, exceeded its total liabilities of $267.23 million, $254.62 million, and $176.08 million by

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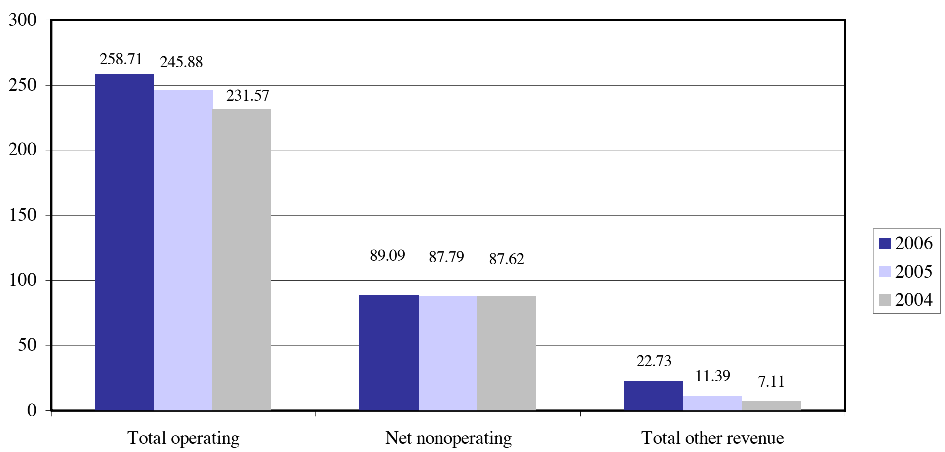
$181.33 million, $168.98 million, and $161.68 million, respectively. The resulting net assets are summarized in the following categories (dollars in millions):

		2006	2005	2004
Invested in capital assets, net of related debt	$	167.01	151.30	139.18
Restricted expendable		6.82	11.53	13.78
Unrestricted		7.50	6.15	8.72
Total net assets	$	181.33	168.98	161.68

The following chart provides a graphical breakdown of total revenues by category for the fiscal years ending June 30, 2006, 2005, and 2004:

Revenues
(Dollars in millions)



Overview of the Financial Statements

The University's financial statements have two primary components: 1) the financial statements and 2) the notes to the financial statements. Additionally, the financial statements focus on the University as a whole, rather than upon individual funds or activities.

The University of Rhode Island Foundation (the Foundation) and the University of Rhode Island Alumni Association (the Alumni Association) are legally separate tax-exempt component units of the University of Rhode Island. The Foundation and the Alumni Association act primarily as fund-raising organizations to supplement the resources that are available to the University in support of its programs. The Boards of the Foundation and the Alumni Association are self-perpetuating and primarily consist of graduates and friends of

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the University. Although the University does not control the timing or the amount of receipts from the Foundation and the Alumni Association, the majority of resources received or held by the Foundation and the Alumni Association are restricted to the activities of the University by the donors. Because these resources held by the Foundation and the Alumni Association can only be used by or are for the benefit of the University, the Foundation and the Alumni Association are considered component units of the University and are discretely presented in the University's financial statements.

Management's Discussion and Analysis is required to focus on the University, and not on its component units.

The Financial Statements. The financial statements are designed to provide readers with a broad overview of the University's finances and are comprised of three basic statements.

The *Statement of Net Assets* presents information on all of the University's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the University is improving or deteriorating.

The *Statement of Revenues, Expenses, and Changes in Net Assets* presents information showing how the University's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows only in future fiscal periods (e.g. the payment for accrued compensated absences, or the receipt of amounts due from students and others for services rendered).

The *Statement of Cash Flows* is reported on the direct method. The direct method of cash flow reporting portrays net cash flows from operations as major classes of operating receipts (e.g. tuition and fees) and disbursements (e.g. cash paid to employees for services).

The financial statements can be found on pages 22 to 24 of this report.

The University reports its operations as a business – type activity using the economic measurement focus and full accrual basis of accounting. As a component unit of the State of Rhode Island and Providence Plantations, the results of the University's operations, its net assets and cash flows are also summarized in the State's Comprehensive Annual Financial Report derived from its government-wide financial statements.

Notes to the Financial Statements. The notes provide additional information that is essential to a full understanding of the data provided in the financial statements. They also provide information regarding both the accounting policies and procedures the University has adopted as well as additional detail of certain amounts contained in the financial statements. The notes to the financial statements can be found on pages 25 to 51 of this report.

Financial Analysis

As mentioned earlier, net assets may serve over time as a useful indicator of the University's financial position. In the case of the University, total assets exceeded total liabilities by $181.33 million, $168.98 million, and $161.68 million at the close of fiscal years 2006, 2005, and 2004, respectively.

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The University's condensed net assets are presented below.

University of Rhode Island's Net Assets

(Dollars in millions)

		2006	2005	2004
Current assets	$	58.89	76.39	66.04
Noncurrent assets		389.67	347.21	271.72
Total assets		448.56	423.60	337.76
Current liabilities		41.28	48.68	38.81
Noncurrent liabilities		225.95	205.94	137.27
Total liabilities		267.23	254.62	176.08
Net assets:				
Invested in capital assets, net of related debt		167.01	151.30	139.18
Restricted, expendable		6.82	11.53	13.78
Unrestricted		7.50	6.15	8.72
Total net assets	$	181.33	168.98	161.68

By far the largest portion of the University's net assets, $167.01 million, $151.30 million, and $139.18 million, respectively, reflects its investment in capital assets (such as land, buildings, machinery, and equipment), net of any related outstanding debts, including capital leases, used to acquire, construct, improve, or rehabilitate those assets. The University uses these capital assets to provide services to students, faculty and administration; consequently, these assets are not available for future spending. Although the University's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate the related debt. In addition to the debts noted above, which are reflected in the University's financial statements, the State of Rhode Island regularly provides financing for certain capital projects through the issuance of general obligation bonds and appropriations from the Rhode Island Capital Plan Fund. Borrowings by the State are not reflected in these financial statements. Additional financing for certain capital projects is also provided by the issuance of revenue bonds by the Rhode Island Health and Educational Building Corporation, a quasi-public state agency.

The University's current assets include cash and cash equivalents, cash held by the State Treasurer, accounts receivable, inventories, and prepayments, while current liabilities consist of accounts payable and accrued expenses, deferred revenues, funds held for others, and the current portion of compensated absences and long-term debts. Compensated absences represent accumulated vacation and sick leave and deferred compensation that will be used or paid in future years. The current ratio (current assets divided by current liabilities), which measures the University's liquidity, has remained positive: 1.43 to 1, 1.57 to 1 and 1.70 to 1 as of June 30, 2006, 2005, and 2004, respectively.

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One of the major components of the University's noncurrent assets are the funds on deposit with the bond trustee totaling $58.83 million as of June 30, 2006. This amount includes $50.93 million of unspent proceeds of Series 2004 and 2005 Bonds, which are being used to finance the construction of a 440-bed apartment unit, a 360-suite-style residence hall, and a two-story dinning hall. These additional housing facilities, which are scheduled to go online in September 2006 and January 2007, will have a positive impact on student enrollment especially among transfer students who seek on-campus housing.

During fiscal years 2006, 2005, and 2004, the University's net assets increased by $12.35 million, $7.30 million, and $5.02 million, respectively, which is largely due to capital and private funds received. The University closed fiscal 2006, 2005, and 2004 with positive unrestricted net assets of $7.50 million, $6.15 million, and $8.72 million, respectively.

Net assets that are not subject to restrictions imposed by creditors, grantors, contributors, laws, regulations or enabling legislation are classified as unrestricted net assets. As of June 30, 2006, 2005, and 2004, the University's unrestricted net assets represent 4%, 4%, and 5%, respectively, of the net assets. At year end, these net assets are designated or committed for goods and services that have not yet been received and normal working capital for auxiliary enterprise and departmental activities.

The restricted expendable net assets consist of resources that are subject to external restrictions on how they must be used, and they represent 4%, 7%, and 9% of the University's net assets at June 30, 2006, 2005, and 2004, respectively.

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The University's condensed revenues, expenses and changes in net assets are presented below.

University of Rhode Island's Condensed Revenues, Expenses and Changes in Net Assets

(Dollars in millions)

	2006	2005	2004
Operating revenues:			
Tuition and fees, net of tuition waivers and remissions	$ 155.43	145.59	131.42
Operating grants and contributions	65.76	65.00	66.17
Other sources	37.52	35.29	33.97
Total operating revenues	258.71	245.88	231.56
Operating expenses:			
Salaries and benefits	230.70	221.82	212.78
Operating expenses	47.73	41.38	36.35
Scholarships, grants and contracts	10.41	9.60	9.11
Auxiliaries	53.04	49.51	48.45
Depreciation and amortization	16.31	15.44	14.59
Total operating expenses	358.19	337.75	321.28
Net operating loss	$ (99.48)	(91.87)	(89.72)

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**University of Rhode Island's Condensed Revenues,
Expenses and Changes in Net Assets**

(Dollars in millions)

		2006	2005	2004
Nonoperating revenues (expenses):				
State appropriation	$	83.19	82.91	82.82
Net investment income		2.50	1.49	0.39
Private gifts		7.72	9.00	10.59
Interest expense		(4.32)	(5.62)	(6.17)
Total nonoperating revenues		89.09	87.78	87.63
Loss before other revenues, expenses, gains or losses		(10.39)	(4.09)	(2.09)
Capital appropriations		9.31	6.21	4.57
State contributed capital		12.44	3.20	2.11
Capital gifts		0.99	1.98	0.43
Increase in net assets		12.35	7.30	5.02
Net assets – beginning of year		168.98	161.68	156.66
Net assets – end of year	$	181.33	168.98	161.68

Operating Revenues

The total operating revenues were up $12.83 million or 5% in fiscal 2006 ($14.31 million or 6% in fiscal 2005 and $16.92 million or 8% in fiscal 2004) as compared with those of the preceding year. This increase is largely attributable to the tuition and fee rate increase as well as the increase in enrollment as envisioned in the University's Three-Year Strategic Plan. Revenues from tuition and fees, net of waivers and remissions, contributed 60% of the total operating revenue stream of fiscal 2006 as opposed to 59% of fiscal 2005.

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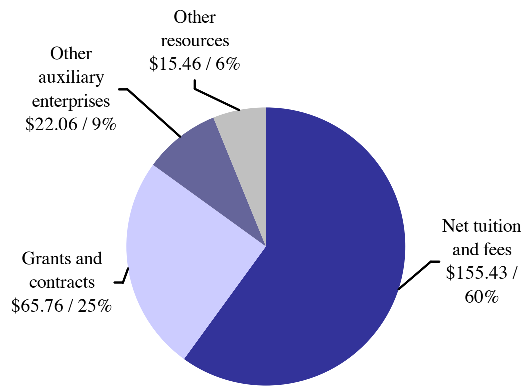
The following provides a graphical breakdown of operating revenues by category for the year ended June 30, 2006.

Operating Revenues by Category
(Dollars in millions)



Total = $258.71

Consistent with the goal of the University's 2003-2006 strategic plan, the benefits derived from tuition and fees rate and student enrollment increases became evident at the close of fiscal 2006. They have funded many aspects of the University that have been long under-funded such as libraries and information technologies. Such revenues also gave the University the capacity to fund salary increases to faculty and staff, as well as medical and insurance costs. However, the need for financial support of students, both need-based and merit-based scholarships, has become more critical in order to increase, if not stabilize, the current student enrollment at the University.

During fiscal years ended June 30, 2006, 2005 and 2004, the revenues from operating grants and contracts contributed 25%, 26%, and 29% respectively, of the total operating revenues.

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Tuition and fees received by the University included the following (dollars in millions):

		2006	2005	2004
Tuition	$	126.90	116.42	101.16
Student service fees		14.85	15.18	15.48
Health service fees		4.26	4.02	3.89
Housing fees		18.15	17.67	17.20
Dining service fees		12.61	12.88	12.73
Miscellaneous student fees		8.87	6.96	6.09
Total		185.64	173.13	156.55
Tuition waived or remitted		(30.21)	(27.54)	(25.13)
Net	$	155.43	145.59	131.42

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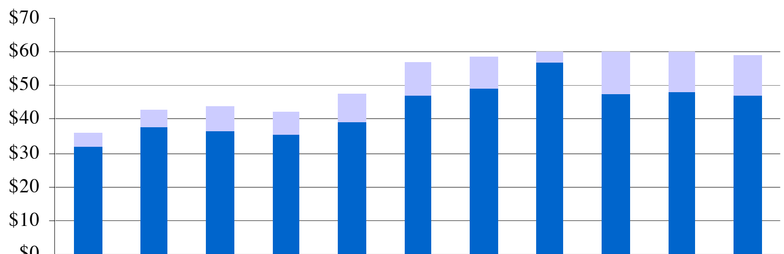
Grant and Contract Revenue

The recognition of revenue from grants and contracts is deferred until services have been performed to fulfill the requirements of the grants and contracts. Hence, awards received are not reflected in the statement of net assets.

The bar chart below shows a steady growth in the amount of grants and contracts awarded to the University during the last ten years, from a total of $36.1 million in 1995 to $59.08 million in 2006 or a 64% increase. This positive development is a reflection of the University's vision to pursue research and to enhance creative and entrepreneurial activities on campus.

Awards for Competitive Sponsored Programs



	95-96	96-97	97-98	98-99	99-00	00-01	01-02	02-03	03-04	04-05	05-06
Total	36.1	42.7	43.8	42.5	47.7	57.1	58.3	60	60.2	60.3	59.08
Nonfederal	4.3	5.2	7.0	7.2	8.5	10.2	9.0	3.1	12.6	12.4	11.9
Federal	31.8	37.5	36.8	35.3	39.2	46.9	49.3	56.9	47.6	47.9	47.2

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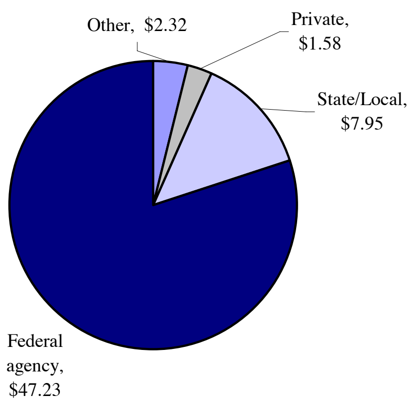
The following summary shows the breakdown of federal awards received from sponsoring agencies during fiscal 2006, with a pie chart for federal and nonfederal awards (dollars in millions).



Agency		Award
Department of Health and Human Services	$	9.58
National Science Foundation		10.88
Department of Defense		5.27
Department of Commerce		5.21
Department of Agriculture		2.98
Agency for International Development		2.38
Department of Education		1.46
National Aeronautic and Space Administration		1.98
Department of Interior		1.13
Environmental Protection Agency		1.10
Other agencies		5.26
Federal agency		47.23
State/Local		7.95
Private		1.58
Other agencies		2.32
Total	$	59.08

The University has been awarded close to $25 million in federal grants for biomedical research in Rhode Island. The award for $16.5 million is a five-year grant to continue the University's work as a catalyst for biomedical research in the State. With funding from the previous $8 million grant, the University has completed the fifth year of Biomedical Research Infrastructure Network (BRIN) award, which resulted in increased collaboration among researchers from the University and other colleges and universities in the State. The new grant cements such relationships and focuses researchers' attention to the University's strength in molecular toxicology. In addition, a core research instrumentation laboratory was established at the University's Kingston campus with the funding from a previous grant. This facility is open to all biomedical researchers in the State, and provides the latest analytical equipment to investigate cancer generation, the effect of toxic chemicals on reproductive, nervous and cardiovascular systems, organs, and drug metabolism.

Operating Expenses

The operating expenses for fiscal 2006, 2005, and 2004 totaled $358.18 million, $337.75 million, and $321.28 million, respectively, an increase of $20.43 million, $16.47 million and $10.72 million or 6.05%, 5.12% and 3.46% over those of fiscal 2005, 2004 and 2003. The increase in fiscal 2006 operating expenses is accounted for by the increase in health insurance premiums, faculty and staff salaries and associated fringe benefits, consulting fees related to systems implementation, ground maintenance, utilities, and depreciation expense.

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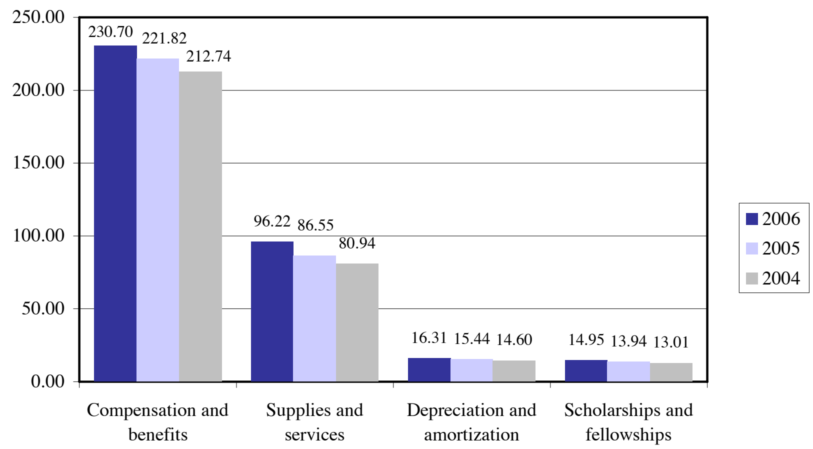
The bar chart below illustrates the University's operating expenses by function for the fiscal years ended June 30, 2006, 2005, and 2004, excluding scholarship allowances applied against tuition and fees.

Operating Expenses
(Dollars in millions)



The following summary shows where major grant and contract expenditures, including indirect cost charges, occurred during 2006, 2005, and 2004 (dollars in millions).

Agency		Amount 2006	2005	2004
National Science Foundation	$	11.38	10.62	10.81
Department of Health and Human Services		10.52	9.43	10.54
Department of Agriculture		5.76	5.50	6.56
Department of Defense		4.99	6.35	7.39
Department of Commerce		4.98	4.42	4.60
National Aeronautic and Space Administration		1.98	1.75	1.61
Department of Education		1.53	0.44	1.22
Environmental Protection Agency		1.26	1.25	1.35
Department of Transportation		1.23	1.48	1.49
Department of Interior		1.03	1.23	1.16
Agency for International Development		0.20	1.50	2.37

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Nonoperating Revenues and Expenses

The State's unrestricted appropriation is the largest component of the University's nonoperating revenues. The amount requested for fiscal 2006 was $85.75 million. However, the amount appropriated by the State was $83.19 million resulting in an appropriation for fiscal 2006 that was $2.56 million less than the amount requested. Although the budget request for fiscal 2006 did not fully meet the real needs of the University, it did provide for a balanced budget and an acceptable level of quality in carrying out the University's mission as it currently exists.

The University has a long tradition of using the state appropriation to support its operating expenses. During fiscal years 2006, 2005, and 2004, the University received state appropriations of $83.19 million, $82.91 million, and $82.82 million, respectively, which was not sufficient to cover operating expenses to the extent of $16.29 million, $8.96 million, and $6.9 million, respectively, as the schedule below indicates. Because operating costs have increased over the years and the state appropriations have not risen enough to cover operating expenses, the student tuition and fees have played an increasingly important role in funding (43% in fiscal 2006, 43% in fiscal 2005, and 41% in fiscal 2004) the University's operations. It is important to note that the Rhode Island General Assembly presets tuition and fees after reviewing recommendations from the Board of Governors for Higher Education and the University.

		2006	2005	2004
			(Dollars in millions)	
Net student fees	$	155.43	145.59	131.42
Other operating revenue		103.28	100.29	100.14
Operating expenses		(358.19)	(337.75)	(321.28)
Operating loss		(99.48)	(91.87)	(89.72)
State direct appropriations		83.19	82.91	82.82
Net loss after state appropriation	$	(16.29)	(8.96)	(6.90)

Investment income was up $1.0 million or 67% (compared with an increase of $1.1 million or 282% in fiscal 2005) due to increased short-term rates of return and to the major increase in funds available for investment by the bond trustee during the year. Interest expense was down $1.3 million or 23% (compared with a decrease of $0.55 million or 8.9% in fiscal 2005) due to the interest that was capitalized in regard to capital projects that were under construction during the year and refinancing of 1999 and 2003 Bond Series at lower interest rates.

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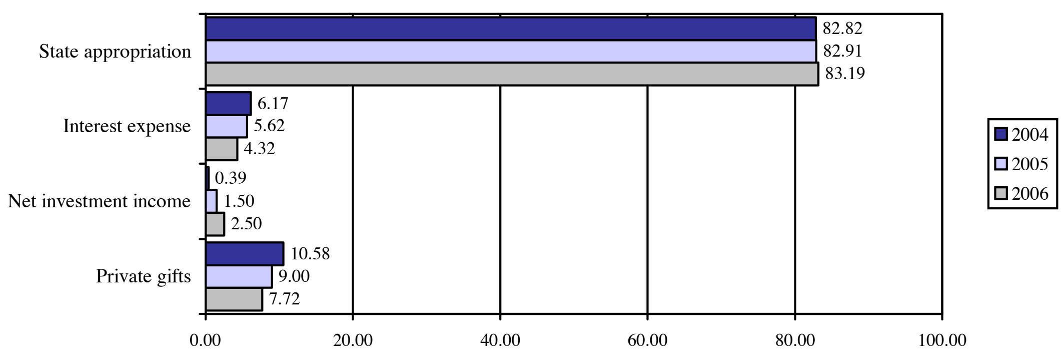
The following chart provides a graphical breakdown of the University's nonoperating revenues and expenses.

Nonoperating Revenue and Expenses
(Dollars in millions)



	Private gifts	Net investment income	Interest expense	State appropriation
2004	10.58	0.39	6.17	82.82
2005	9.00	1.50	5.62	82.91
2006	7.72	2.50	4.32	83.19

Capital Assets and Debt Administration

Capital Plan

The University generally has funded its capital plans through a combination of funds received from University operations, bonds issued by the Rhode Island Health and Educational Building Corporation, state appropriations, general obligation bonds, federal appropriations, and private fund raising. The execution of the University's capital improvement plan is contingent upon approval and sufficient funding from the State.

The Board of Governors for Higher Education submits a running five-fiscal-year capital improvement plan to the General Assembly and State Executive each year. The plan for the proposed capital projects for the entire system of public higher education in Rhode Island includes the University. The fiscal year 2008-2012 plan for the University totals $580.32 million, and it includes all continuing and planned projects, whether funded or not. This plan forms the basis for discussions on funding the various projects from all available funding sources.

UNIVERSITY OF RHODE ISLAND
(A Component Unit of the State of Rhode Island
and Providence Plantations)

Management's Discussion and Analysis

June 30, 2006 and 2005

Capital Assets

The University's investment in capital assets as of June 30, 2006, 2005, and 2004 net of accumulated depreciation, amounts to $313.30 million, $261.87 million, and $252.61 million, respectively. This investment in capital assets includes land, buildings (including improvements), and furnishings and equipment (including the cost of capital leases). Capital assets increased during fiscal 2006 by $51.43 million and $9.26 million during fiscal 2005. Legal title to all land and real estate assets is vested in the Rhode Island Board of Governors for Higher Education or the State of Rhode Island. A summary of capital asset balances as of June 30, 2006, 2005, and 2004 is presented below.

Summary Schedule of Net Capital Assets

(Dollars in millions)

		2006	2005	2004
Land and improvements	$	32.79	29.24	27.79
Building and improvements		198.73	196.37	196.90
Furnishings and equipment		21.96	21.45	21.34
Construction in progress		59.82	14.81	6.58
Total	$	313.30	261.87	252.61

Capital additions in fiscal 2006 included Surge II and Heathman with total costs of $3 million and $6.78 million, respectively. The major capital additions are in construction in progress, which includes the new student housing and new dining hall with total costs of $30.66 million and $6.2 million, respectively, both of which are expected to be completed in January 2007. In addition, the renovation of Independence Hall, with a total cost of $5.54 million, has a completion date of September 2006.

Additional information about the University's capital assets can be found in note 6 to the financial statements.

UNIVERSITY OF RHODE ISLAND
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Management's Discussion and Analysis

June 30, 2006 and 2005

Debt

As of June 30, 2006, 2005 and 2004, the University had $202.09 million, $183.19 million, and $113.42 million respectively, in outstanding debt, an increase of $18.90 million, $69.76 million, and $0.58 million over that of the prior years. The table below summarizes the types of debt instruments.

Summary Schedule of Debt

(Dollars in millions)

		2006	2005	2004
Loans payable	$	1.94	0.25	0.32
Capital lease obligations		14.63	15.51	16.16
Revenue bonds		185.52	167.43	96.95
Total	$	202.09	183.19	113.43

In fiscal year 2006, additional revenue bonds were issued; (a) University of Rhode Island Auxiliary Enterprise Revenue Issue, Series 2005 C Bonds, $13.84 million for the construction of a two story dining hall and (b) University of Rhode Island Educational and General Revenue Issue, Series 2005 F Bonds, $3.24 million for the acquisition and demolition of Theta Delta Chi House and the construction of an addition to Tyler Hall.

In fiscal year 2006 refunding bonds were issued (a) University of Rhode Island Auxiliary Enterprise Revenue Issue, Series 2005 D Bonds, $19.63 million for the refunding of Series 1999 A Bonds which resulted in a net present value savings of $1.13 million and (b) University of Rhode Island Educational and General Revenue Issue, Series 2005 G Bonds, $44.81 million for the refunding of Series 1999 B and Series 2000 B Bonds, a net present value savings of $2.19 million.

The additions to revenue bonds payable during fiscal 2005 consisted of: (a) University of Rhode Island Auxiliary Enterprise Revenue Issue, Series 2004 A and B Bonds for $66.93 million and (b) University of Rhode Island Educational and General Revenue Issue, Series 2005 A and B Bonds for $4.74 million. The proceeds of Series 2004 Bonds are primarily used for the construction of a 440-bed apartment unit and 360 suite-style residence hall. Currently, these projects are under construction and are scheduled to go online in the fall of fiscal 2006. The proceeds of Series 2005 Bonds are primarily used for the construction of a 2nd level above the Surge Modular Building to provide interim classroom space during the Independence Hall construction and for the construction and rebuilding of parking facilities, roadways, sidewalks, curbing, drainage and landscape amenities on the Kingston Campus.

The University has no independent bonding authority. All bonds must be approved by and arranged through the Board of Governors for Higher Education. All general obligation and revenue bond related indebtedness is reflected on the financial accounts of the entity issuing the bonds. Both Moody's and Standard and Poor's rating services have given the Board of Governors for Higher Education general revenue bonds a rating of AAA. The State of Rhode Island general obligation bonds are rated by Moody's at Aa3, Fitch's at AA, and Standard and Poor's at AA.

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As a means to lower debt service costs, the University, acting through the Board of Governors for Higher Education entered into a swap agreement in connection with the issuance of its $33 million Series 2004 B revenue bonds in December 2004.

More detailed information about the University's long-term liabilities is presented in notes 7 and 8 to the financial statements.

Economic Factors That Will Affect the Future

The seasonally adjusted unemployment rate for the State of Rhode Island, from which the University draws a majority of its students, increased from 5.0% in June of 2005 to 5.5% in June of 2006, according to the U.S. Bureau of Labor Statistics. This compares to a decrease from 5.0% to 4.6%, respectively, on a national level. Rhode Island's job growth rate for the first six months of 2005 of 1.4% trailed the national average of 1.6% for the period. Rhode Island was one of only four states to record an increased rate of unemployment during this period. Historically, in times of economic slowdowns, public colleges/universities have experienced increases in their enrollment as unemployed and underemployed workers seek to update and upgrade their skills. The University cannot predict the extent to which enrollment may vary in this current environment.

Rhode Island faced a state budget deficit in fiscal year 2006, and as part of a state-wide program to balance the budget, reduced the annual state appropriation to the University by $2 million at mid-year. The state projects a significant budget short fall in fiscal year 2007 and has proposed reductions in the state appropriation that will result in an operating short fall of $6.6 million for the University in fiscal year 2007.

To support their strategic priorities in this financially challenging environment, the University and the Board of Governors for Higher Education took the following actions during fiscal 2006.

- Fiscal 2006 tuition and mandatory fees increased by 8% for in-state students 8.7% of out-of-state students, 8.7% for in-state graduate students, and 11% for out-of state graduate students
- Fiscal 2007 tuition and fees were increased by 6% for in-state students 7.5% for out-of-state students, and 7.5% for all graduate students
- A hiring freeze was imposed on all but critical positions, which were reviewed on a case-by-case basis
- All discretionary expenses were closely reviewed by senior management
- Gained State approval to carry forward unrestricted funds annually
- Developed an energy performance contract to use energy savings to pay for necessary equipment and facility upgrades with no negative impact on current operating budgets
- Eliminated department of Professional Development and Training

Despite the reductions in state funding per student and the change in budget allocation authority, the University's current financial and capital plans indicate that the infusion of additional financial resources from the foregoing Board and management actions will enable it to maintain its present level of services at all campuses.

UNIVERSITY OF RHODE ISLAND
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In accordance with its strategic plan, the University continues to increase its enrollment gradually each year, consistent with its efforts to effectively manage student housing and class enrollment. The University has also attempted to maintain affordability by limiting the size of tuition and fee increases. Increases in in-state undergraduate student charges have been held to an average of 7% for academic years 2003-2007. Out-of-state undergraduate student charges have been held to an average of 9% over the same period. Based on in-state undergraduate mandatory tuition and fees during the 2005-2006 academic year, the University ranks fifth lowest among the six New England public flagship universities.

Fiscal Planning

The University will continue to control expenses in accordance with available resources and established priorities by increasing resources through retention programs as well as increasing efficiencies throughout the organization. The Academic Investment and Improvement Model along with other financial and program assessment tools continue to be utilized to balance mission and resources. The University has established plans to increase revenue over the next three years as reflected in the University's Three-Year Strategic Plan, for the fiscal years 2007 to 2009.

Information System

The University has implemented PeopleSoft's Student Administration, Human Resources, and Financial Systems. The PeopleSoft e-Campus system is stable. After several years of hard work implementing the fundamental pieces of these systems, the University still continues to reassess the progress of the actual implementation on a regular basis and refocus efforts on the PeopleSoft systems to yield the most effective outcome for students, faculty and staff. The PeopleSoft Financial system was upgraded to version 8.9 in fiscal 2006. The PeopleSoft Student Administration and Human Resources system is in the process of implementing an upgrade to version 8.9 and is expected to be completed prior to the end of fiscal year 2007.

In addition, the University has initiated a plan to upgrade the University's Advancement software (Sungard BSR) in order to facilitate fundraising efforts. The new software uses state-of-the-art fundraising technology and telecommunications that will aid in future gift/pledge drives, events, and capital campaign. The University started the upgrade or migration of the BSR fundraising system in August 2005 and is expected to go online in fall of 2006.

Requests for Information

This financial report is designed to provide a general overview of the University's finances for all those with an interest in the University's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to: Mr. Robert Weygand, Vice President for Administration, University of Rhode Island, 108 Carlotti Administration Building, 75 Lower College Road, Room 108, Kingston, RI 02881.

UNIVERSITY OF RHODE ISLAND
(A Component Unit of the State of Rhode Island
and Providence Plantations)

Statements of Net Assets

June 30, 2006 and 2005

Assets		2006 University of Rhode Island	2005 University of Rhode Island	2006 Component units	2005 Component units
Current assets:					
Cash and cash equivalents (note 2)	$	33,592,715	33,451,421	6,548,784	4,462,999
Cash held by State Treasurer – capital projects (note 3)		934,899	4,007,506	—	—
Cash held by State Treasurer – other (note 3)		1,903,763	1,704,400	—	—
Accounts receivable, net (note 4)		19,131,227	32,422,171	—	—
Current portion of pledges receivable (note 4)		—	—	1,857,530	2,329,836
Current portion of notes receivable		—	—	24,910	39,297
Current portion of net investment in sales types leases		—	—	—	33,237
Inventory and other current assets		3,324,830	4,799,511	795,649	962,608
Total current assets		58,887,434	76,385,009	9,226,873	7,827,977
Noncurrent assets:					
Cash and cash equivalents – restricted (note 2)		22,618	18,197	—	—
Funds on deposit with bond trustee – restricted		58,832,246	72,666,479	—	—
Investments (note 2)		—	—	84,834,535	75,903,594
Pledges receivable (note 4)		—	—	879,756	1,901,144
Loans receivable, net (note 5)		12,302,665	11,312,154	116,910	133,349
Charitable remainder trusts		—	—	979,415	1,028,415
Other deferred assets		5,214,204	1,342,489	—	—
Capital assets, net of accumulated depreciation (notes 6 and 7)		313,300,690	261,874,693	2,139,068	2,215,241
Total noncurrent assets		389,672,423	347,214,012	88,949,684	81,181,743
Total assets	$	448,559,857	423,599,021	98,176,557	89,009,720
Liabilities					
Current liabilities:					
Accounts payable and accrued liabilities (note 3)	$	25,092,952	31,377,919	224,569	217,956
Current portion of contributions payable to University		—	—	—	374,428
Compensated absences (note 7)		1,061,579	1,300,450	—	—
Funds held for others		358,144	207,064	—	—
Deferred revenues		11,047,918	11,824,695	—	—
Current portion of capital lease obligations (note 7)		1,283,742	1,202,816	—	—
Current portion of bonds and loans payable (note 7)		2,434,637	2,762,909	—	—
Current portion of gift annuity payable		—	—	79,541	70,280
Total current liabilities		41,278,972	48,675,853	304,110	662,664
Noncurrent liabilities:					
Compensated absences (note 7)		16,631,400	15,910,533	—	—
Pledges payable		—	—	200,000	225,000
Contributions payable to University		—	—	—	80,000
Capital lease obligations (note 7)		13,344,744	14,307,386	—	—
Bonds and loans payable (note 7)		185,022,859	164,914,197	—	—
Gift annuity payable		—	—	721,438	505,511
Grant refundable (note 9)		10,955,725	10,810,453	—	—
Total noncurrent liabilities		225,954,728	205,942,569	921,438	810,511
Total liabilities	$	267,233,700	254,618,422	1,225,548	1,473,175
Net Assets					
Invested in capital assets, net of related debt	$	167,006,038	151,306,098	6,098,722	4,762,620
Restricted:					
Expendable (note 10)		6,816,893	11,527,252	24,482,876	19,754,841
Nonexpendable		—	—	61,356,149	58,142,003
Unrestricted (note 11)		7,503,226	6,147,249	5,013,262	4,877,081
Total net assets	$	181,326,157	168,980,599	96,951,009	87,536,545

See accompanying notes to financial statements.

UNIVERSITY OF RHODE ISLAND
(A Component Unit of the State of Rhode Island
and Providence Plantations)

Statements of Revenues, Expenses, and Changes in Net Assets

Years ended June 30, 2006 and 2005

	2006 University of Rhode Island	2005 University of Rhode Island	2006 Component units	2005 Component units
Operating revenues:				
Tuition and fees	$ 144,135,660	132,968,906	—	—
Residence, dining, student union, and health fees	41,501,586	40,164,381	—	—
Less scholarship allowances	(30,210,074)	(27,544,907)	—	—
Net student fees	155,427,172	145,588,380	—	—
Federal, State, local, and private grants and contracts	65,759,533	65,003,960	—	—
Other auxiliary enterprises	22,055,351	20,468,823	—	—
Other sources	15,464,097	14,815,870	3,147,842	2,637,548
Total operating revenues	258,706,153	245,877,033	3,147,842	2,637,548
Operating expenses (note 13):				
Instruction	86,203,232	84,308,997	—	—
Research	57,308,073	53,300,260	—	—
Academic support	35,530,848	36,319,051	—	—
Student services	23,107,465	22,126,405	2,170,829	2,189,174
Scholarships and fellowships	10,414,491	9,585,186	—	—
Public service	4,996,060	5,198,606	—	—
Operation and maintenance of plant	35,219,123	28,134,680	322,948	205,238
Depreciation and amortization	16,309,085	15,439,135	133,688	75,937
Institutional support	36,053,687	33,825,673	5,226,208	3,838,881
Auxiliary operations	53,041,664	49,513,845	—	—
Total operating expenses	358,183,728	337,751,838	7,853,673	6,309,230
Operating loss	(99,477,575)	(91,874,805)	(4,705,831)	(3,671,682)
Nonoperating revenues (expenses):				
State appropriation (note 14)	83,187,769	82,910,362	—	—
Net investment income	2,498,587	1,496,959	751,946	135,254
Endowment income	—	—	8,690,234	2,701,125
Private gifts and contributions	—	—	6,139,647	6,298,792
Payments between the University and component units	7,722,977	8,996,801	(6,816,377)	(8,304,239)
Additions to permanent endowments	—	—	4,295,289	3,975,642
Patent receipts	—	—	966,319	1,107,244
Miscellaneous receipts	—	—	1,078,443	2,260,232
Interest expense	(4,318,315)	(5,618,976)	—	—
Net nonoperating revenues	89,091,018	87,785,146	15,105,501	8,174,050
Income (loss) income before capital activities	(10,386,557)	(4,089,659)	10,399,670	4,502,368
Capital appropriations (note 14)	21,746,909	9,414,901	—	—
Capital gifts	985,206	1,978,701	(985,206)	(1,978,701)
Increase in net assets	12,345,558	7,303,943	9,414,464	2,523,667
Net assets, at beginning of year	168,980,599	161,676,656	87,536,545	85,012,878
Net assets, at end of year	$ 181,326,157	168,980,599	96,951,009	87,536,545

See accompanying notes to financial statements.

UNIVERSITY OF RHODE ISLAND
(A Component Unit of the State of Rhode Island
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Statements of Cash Flows

Years ended June 30, 2006 and 2005

		2006 University of Rhode Island	2005 University of Rhode Island
Cash flows from operating activities:			
Tuition and fees	$	158,394,830	144,580,185
Grants and contracts		73,771,138	62,289,849
Payments to suppliers		(90,467,757)	(84,226,173)
Payments to employees		(240,784,503)	(217,066,684)
Payments for scholarships, fellowships, and sponsored programs		(14,950,673)	(13,940,038)
Auxiliary enterprises		22,182,893	20,386,388
Other receipts		16,026,220	18,248,223
Net cash used by operating activities		(75,827,852)	(69,728,250)
Cash flows from noncapital financing activities:			
State appropriations		83,187,769	82,910,362
Cash overdraft implicitly financed		—	(100,492)
Gifts from component units		7,722,977	8,996,801
Funds held for others		151,080	(717,867)
Net cash provided by noncapital financing activities		91,061,826	91,088,804
Cash flows from capital and related financing activities:			
Proceeds from capital debt		79,361,247	70,332,511
Capital appropriations		21,746,909	9,414,901
Capital gifts		985,206	1,978,701
Net loss on disposal of capital assets		337,863	296,294
Purchase of capital assets		(67,353,599)	(24,418,575)
Principal paid on capital debt and leases		(65,053,634)	(2,502,782)
Interest paid on capital debt and leases		(4,318,315)	(5,618,976)
Deposit with trustee		13,834,233	(64,230,013)
Net cash used by capital and related financing activities		(20,460,090)	(14,747,939)
Cash flows from investing activities:			
Interest on investments		2,498,587	1,496,959
Net cash provided by investing activities		2,498,587	1,496,959
Net increase in cash, restricted cash and cash equivalents		(2,727,529)	8,109,574
Cash, restricted cash and cash equivalents – beginning of year		39,181,524	31,071,950
Cash, restricted cash and cash equivalents – end of year	$	36,453,995	39,181,524
Reconciliation of net operating revenues (expenses) to net cash used by operating activities:			
Operating loss	$	(99,477,575)	(91,874,805)
Adjustments to reconcile net loss to net cash used by operating activities:			
Depreciation and amortization		16,309,085	15,439,135
Changes in assets and liabilities:			
Accounts receivable		13,290,944	(667,674)
Inventory and other current assets		1,474,681	(1,584,515)
Loans receivable		(990,511)	(642,738)
Accounts payable and accrued liabilities		(6,284,967)	7,751,452
Deferred revenues		(776,777)	814,833
Compensated absences		481,996	832,491
Refundable grant		145,272	203,571
Net cash used by operating activities	$	(75,827,852)	(69,728,250)
Supplemental disclosure of cash flows information:			
New capital leases	$	507,618	583,568

See accompanying notes to financial statements.

UNIVERSITY OF RHODE ISLAND
(A Component Unit of the State of Rhode Island
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Notes to Financial Statements

June 30, 2006 and 2005

(1) Summary of Significant Accounting Policies

(a) Organization

The University is a State Land-Sea-and-Urban-Grant University. Chartered in 1951, the University offers undergraduate and graduate degree programs of study and also confers doctoral degrees. The University has three campuses throughout Rhode Island in addition to the main campus located in Kingston, Rhode Island. The University is accredited by the New England Association of Schools and Colleges. In addition, certain courses and programs of study have been approved by national accrediting agencies.

The University is supported by the State of Rhode Island, as part of the system of public higher education that includes the Community College of Rhode Island (CCRI) and Rhode Island College (RIC), with which articulation agreements exist for student transfer within the system.

The University, a component unit of the State of Rhode Island and Providence Plantations, is governed by the Rhode Island Board of Governors for Higher Education (the Board), a body politic and corporate established under Chapter 59 of Title 16 of the General Laws of Rhode Island. The Board consists of public members appointed by the Governor, as well as the Chair of the Board of Regents for Elementary and Secondary Education, and the Chairs or designees of the Finance Committees of the House and Senate of the Rhode Island General Assembly.

(b) Basis of Presentation

The accompanying financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting in accordance with U.S. generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements have been met. The University has determined that it functions as a Business Type Activity, as defined by GASB. The effect of interfund activity has been eliminated from these financial statements.

The University's policies for defining operating activities in the statements of revenues, expenses, and changes in net assets are those that generally result from exchange transactions such as the payment received for services and payment made for the purchase of goods and services. Certain other transactions are reported as nonoperating activities. These nonoperating activities include the University's operating and capital appropriations from the State of Rhode Island, net investment income, gifts, and interest expense.

The University has elected not to adopt the pronouncements issued by the Financial Accounting Standards Board (FASB) and related standards after November 30, 1989.

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Notes to Financial Statements

June 30, 2006 and 2005

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UNIVERSITY OF RHODE ISLAND
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Notes to Financial Statements

June 30, 2006 and 2005

The condensed statements of net assets of the Foundation as of March 31 and the Alumni Association as of June 30 are as follows:

	2006		
	Foundation	**Alumni Association**	**Total**
Current assets	$ 8,946,357	280,516	9,226,873
Noncurrent assets	85,922,711	3,026,973	88,949,684
Total assets	94,869,068	3,307,489	98,176,557
Current liabilities	142,455	161,655	304,110
Noncurrent liabilities	921,438	—	921,438
Total liabilities	1,063,893	161,655	1,225,548
Net assets:			
Invested in capital assets, net of related debt	6,098,722	—	6,098,722
Restricted:			
Expendable	23,417,401	1,065,475	24,482,876
Nonexpendable	61,356,149	—	61,356,149
Unrestricted	2,932,903	2,080,359	5,013,262
Total net assets	$ 93,805,175	3,145,834	96,951,009

UNIVERSITY OF RHODE ISLAND
(A Component Unit of the State of Rhode Island and Providence Plantations)

Notes to Financial Statements

June 30, 2006 and 2005

	2005		
	Foundation	**Alumni Association**	**Total**
Current assets	$ 7,531,081	296,896	7,827,977
Noncurrent assets	78,393,085	2,788,658	81,181,743
Total assets	85,924,166	3,085,554	89,009,720
Current liabilities	417,688	244,976	662,664
Noncurrent liabilities	730,511	80,000	810,511
Total liabilities	1,148,199	324,976	1,473,175
Net assets:			
Invested in capital assets, net of related debt	4,762,620	—	4,762,620
Restricted:			
Expendable	18,768,767	986,074	19,754,841
Nonexpendable	58,142,003	—	58,142,003
Unrestricted	3,102,577	1,774,504	4,877,081
Total net assets	$ 84,775,967	2,760,578	87,536,545

UNIVERSITY OF RHODE ISLAND
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Notes to Financial Statements

June 30, 2006 and 2005

The condensed statements of revenues, expenses and changes in net assets of the Foundation for the years ended March 31 and the Alumni Association for the years ended March 31 are as follows:

	2006		
	Foundation	**Alumni Association**	**Total**
Operating revenues:			
Endowment income	$ 8,690,234	—	8,690,234
Other sources	—	3,147,842	3,147,842
Total operating revenue	8,690,234	3,147,842	11,838,076
Operating expenses:			
Student services	—	2,170,829	2,170,829
Operation and maintenance in plant	—	322,948	322,948
Depreciation and amortization	133,688		133,688
Institutional support	3,483,353	1,742,855	5,226,208
Total operating expenses	3,617,041	4,236,632	7,853,673
Operating loss	5,073,193	(1,088,790)	3,984,403
Nonoperating revenues (expenses):			
Net investment income	708,450	43,496	751,946
Private gifts	4,709,097	1,430,550	6,139,647
Gifts to University	(6,816,377)	—	(6,816,377)
Additions to permanent endowments	4,295,289	—	4,295,289
Patent receipts	966,319	—	966,319
Miscellaneous receipts	1,078,443	—	1,078,443
Net nonoperating revenues	4,941,221	1,474,046	6,415,267
Income before other revenues, expenses, gains or losses	10,014,414	385,256	10,399,670
Capital gifts to the University	(985,206)	—	(985,206)
Increase in net assets	9,029,208	385,256	9,414,464
Net assets, beginning of year	84,775,967	2,760,578	87,536,545
Net assets, end of year	$ 93,805,175	3,145,834	96,951,009

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		2005	
	Foundation	Alumni Association	Total
Operating revenues:			
Endowment income	$ 2,701,125	—	2,701,125
Other sources	—	2,637,548	2,637,548
Total operating revenue	2,701,125	2,637,548	5,338,673
Operating expenses:			
Student services	—	2,189,174	2,189,174
Operation and maintenance in plant	—	205,238	205,238
Depreciation and amortization	75,937	—	75,937
Institutional support	2,204,015	1,634,866	3,838,881
Total operating expenses	2,279,952	4,029,278	6,309,230
Operating loss	421,173	(1,391,730)	(970,557)
Nonoperating revenues (expenses):			
Net investment income	135,254	—	135,254
Private gifts	4,723,760	1,575,032	6,298,792
Gifts to University	(8,304,239)	—	(8,304,239)
Additions to permanent endowments	3,975,642	—	3,975,642
Patent receipts	1,107,244	—	1,107,244
Miscellaneous receipts	2,260,232	—	2,260,232
Net nonoperating revenues	3,897,893	1,575,032	5,472,925
Income before other revenues, expenses, gains or losses	4,319,066	183,302	4,502,368
Capital gifts to the University	(1,830,854)	(147,847)	(1,978,701)
Increase in net assets	2,488,212	35,455	2,523,667
Net assets, beginning of year	82,287,755	2,725,123	85,012,878
Net assets, end of year	$ 84,775,967	2,760,578	87,536,545

Complete financial statements for the Foundation can be obtained from: 79 Upper College Road, Kingston, RI 02881.

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Complete financial statements for the Alumni Association can be obtained from: Alumni Relations, Room 105, 73 Upper College Road, Kingston, RI 02881.

(c) ***Net Assets***

Resources are classified for accounting purposes into the following three net asset categories:

Invested in capital assets, net of related debt: Capital assets, net of accumulated depreciation and of outstanding principal balances of debt attributable to the acquisition, construction, repair, or improvement of those assets.

Restricted – nonexpendable: Net assets subject to externally imposed conditions that the University must maintain them in perpetuity.

Restricted – expendable: Net assets whose use is subject to externally imposed conditions that can be fulfilled by the actions of the University or by the passage of time.

Unrestricted: All other categories of net assets. Unrestricted net assets may be designated by the University.

The University has adopted a policy of generally utilizing restricted – expendable funds, when available, prior to unrestricted funds.

(d) ***Cash Equivalents***

Cash equivalents consist entirely of highly liquid financial instruments with an original maturity date of three months or less.

(e) ***Inventories***

Inventories are stated at the lower of cost (first-in, first-out, and retail inventory method) or market, and consist primarily of bookstore, dining, health, and residential life services items.

(f) ***Capital Assets***

Real estate assets, including improvements, are generally stated at cost. Furnishings and equipment are stated at cost at date of acquisition or, in the case of gifts, at fair value at date of donation. In accordance with the Rhode Island Board of Governors for Higher Education's capitalization policy, all land is capitalized, regardless of value. Vehicles, equipment, computer software for internal use, and works of art and historical treasures with a unit cost of $5,000 or more are capitalized. Building, leasehold, and infrastructure improvements with a unit cost of $50,000 or more are capitalized. Interest costs on debt related to capital assets are capitalized during the construction period and then depreciated over the life of the asset. University capital assets, with the exception of land and construction in progress are depreciated on a straight-line basis over their estimated useful lives, which range from 5 to 50 years.

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The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

(g) Compensated Absences and Salary Reduction Plan

University employees are granted vacation and sick leave in varying amounts. The University is committed to separate union contracts which contain different policies for the employees covered under the specific contract. In the event of termination, an employee is paid for those accumulated vacation and sick days allowable under the union contract or in the case of nonunion personnel, according to State or University policy.

Amounts of vested and accumulated vacation and sick leave are reported as accrued compensation and benefits. Amounts are determined based upon the personal service rates in effect as of the balance sheet date. No liability is recorded for nonvesting accumulating rights to receive vacation and sick pay benefits.

Also reported as noncurrent liabilities are the remaining balances of employee salaries deferred under a Comprehensive Salary Reduction Plan adopted by the Board during fiscal years 1991 and 1992. Minor amounts attributable to a voluntary salary reduction program for fiscal 1993, approved by the Board, are also included. These expenditures can be in the form of paid leave on a day-to-day basis, payment at the time of employee termination or retirement, or payment to an employee's estate in the event of death.

(h) Health

The State offers one state paid health plan to each of its participating agencies, including the University. The premiums for these plans are divided among the sixteen participants based upon their number of lives (eligible employees). Certain nonunion employees (classified and nonclassified) contribute between 4% to 8% of the cost of their health plans. The University pays the remaining balance of their health care costs for those employees who do not contribute to their health plans and is required to budget for these costs based on the estimated number of lives. The costs are automatically deducted through the payroll system on a biweekly basis. Amounts paid by the University to the State for the 2006 and 2005 health premiums were $24,442,819 and $25,393,363, respectively.

(i) Assessed Fringe Benefit Administrative Fund

In July 2000, the State established the Assessed Fringe Benefit Administrative Fund. This fund is used to make all payments relating to workers' compensation charges, unemployment payments, and payments to employees for unused vacation and sick leave at the time of retirement or termination from State service. The State funds this account by assessing a charge against the biweekly payrolls of all State agencies, including the University. The fringe benefit assessment rate for fiscal 2006 was 3.8% and for 2005 was 4.1%. The assessed fringe benefit cost for the University was $5,035,709 for fiscal year 2006 and $4,950,120 for fiscal year 2005.

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(j) Students' Deposits and Unearned Revenues

Deposits and advance payments received for tuition and fees related to certain summer programs and tuition received for the following academic year are deferred and are recorded as revenues as earned.

(k) Student Fees

Student tuition, dining, residence, health, and other fees are presented net of scholarships and fellowships applied to students' accounts. Certain other scholarship amounts are paid directly to, or refunded to, the student and are generally reflected as expenses.

(l) Tax Status

The University is a component unit of the State of Rhode Island and Providence Plantations and is therefore generally exempt from income taxes under Section 115 of the Internal Revenue Code.

(m) Use of Estimates

The presentation 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.

(n) Risk Management

The University is exposed to various risks of loss related to general liability, property and casualty, workers' compensation, unemployment, and employee health and life insurance claims.

The University is insured for general liability with policy limits of $1 million per claim and $3 million in the aggregate with a $25,000 deductible. Coverage under the General Liability Policy extends to faculty, staff, students, and volunteers acting within scope of their duties on behalf of the University. Employed health care providers, are covered under an institutional medical malpractice policy excluding physicians who have separate coverage. This policy does not apply to actions relating to federal/civil rights, eminent domain, and breach of contract. Such claims are insured under a separate policy with limits of $4 million per claim and $4 million for the annual aggregate with a $150,000 deductible. Crime coverage for University employees is carried with a limit of $1 million and a deductible of $100,000. The University also maintains an excess liability insurance policy with a limit of $25 million.

Buildings and contents are insured against fire, theft, and natural disaster to the extent that losses exceed $100,000 per incident and do not exceed $500 million. A separate inland marine policy insures specifically listed property items such as computer equipment, valuable papers, fine arts, contractors equipment, and miscellaneous property at various limits of insurance and deductibles. The University also maintains Hull and Property & Indemnity coverage on a specific schedule of watercraft. This policy has a $300,000 policy limit with a $1,000 deductible over which there is an

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excess coverage bringing the limit to $1 million. A separate policy insures the University's 184-foot research vessel.

All vehicles are owned by the State, which insures them for liability through an outside carrier. The policy is a loss retrospective program where premiums can be adjusted for claims incurred. Worker's compensation, unemployment, and employee health and life insurance claims are self-insured and managed by the State.

(o) Reclassifications

Certain 2005 balances have been reclassified to conform to the 2006 presentation.

(2) Cash, Cash Equivalents, and Investments

(a) Cash and Cash Equivalents

At June 30, 2006 and 2005, the carrying amount of the University's cash deposits was $33,615,333 and $33,469,618 and the bank balance was $32,379,978 and $38,117,655, respectively. Deposits are exposed to custodial credit risk if they are not covered by depositary insurance and the deposits are:

a) Uncollateralized

b) Collateralized with securities held by the pledging financial institution, or

c) Collateralized with securities held by the pledging financial institution's trust department or agent but not in the depositor-government's name.

Of the bank balance $270,704 was covered by federal depository insurance and $27,996,382 was collateralized with securities held by the pledging financial institution, in the University's name. The remaining amount, $4,112,892 was uninsured and uncollateralized. None of the University's cash deposits were required to be collateralized by law since the deposits are not time deposits. In addition, the three financial institutions doing business with the University exceed the minimum capital standards prescribed by their federal regulator.

The University's policy is in accordance with Chapter 35-10.1 of the Rhode Island General Laws dealing with the Public Finance any depository institutions holding public deposits shall insure or pledge eligible collateral equal to one hundred percent (100%) with any time deposit with maturities greater than sixty (60) days. If any depository institution does not meet its minimum capital standards as prescribed by its federal regulator they shall insure or pledge eligible collateral equal to one hundred percent (100%) of all public deposits.

The University does not have a policy for custodial credit risk associated with deposits.

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(b) Investments

The Rhode Island Board of Governors for Higher Education has a policy stressing preservation of principal and limiting deposits to federally insured and other financially secured accounts. The University predominantly invests in short to medium term cash and similar vehicles.

The Foundation investments at March 31, 2006 and 2005 and the Alumni Association investments at June 30, 2006 and 2005 are reported at fair market value and are composed of the following:

	2006		
	Foundation	**Alumni Association**	**Total**
Government securities	$ 14,972,646	—	14,972,646
Corporate bonds	6,274,990	1,055,811	7,330,801
Common stock	60,595,079	1,936,009	62,531,088
	$ 81,842,715	2,991,820	84,834,535

	2005		
	Foundation	**Alumni association**	**Total**
Government securities	$ 15,293,620	—	15,293,620
Corporate bonds	3,910,992	1,760,227	5,671,219
Common stock	53,910,324	1,028,431	54,938,755
	$ 73,114,936	2,788,658	75,903,594

(3) Cash Held by State Treasurer

Accounts payable and accrued salaries to be funded from state-appropriated funds totaled $2,838,662 and $5,711,906 at June 30, 2006 and 2005, respectively. The University has recorded a comparable dollar amount of cash held by the State Treasurer for the benefit of the University which was subsequently utilized to pay for such liabilities.

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(4) Accounts and Pledges Receivable

Accounts receivable include the following at June 30:

		2006	2005
Student accounts receivable	$	6,661,072	8,413,959
Grants receivable		4,562,025	6,310,759
Unbilled grants receivable		8,262,075	15,303,770
Other receivables		4,390,625	7,734,145
		23,875,797	37,762,633
Less allowance for doubtful accounts		(4,744,570)	(5,340,462)
	$	19,131,227	32,422,171

The University has determined that the net amount of accounts receivable will be collected within one year's time.

(5) Loans Receivable

Loans receivable include the following at June 30:

		2006	2005
Perkins loans receivable	$	9,628,119	8,595,190
Nursing loans receivable		1,155,039	1,107,914
Health profession loans receivable		1,498,620	1,394,832
Other		445,835	639,733
		12,727,613	11,737,669
Less allowance for doubtful accounts		(424,948)	(425,515)
	$	12,302,665	11,312,154

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(6) Capital Assets

Capital assets of the University consist of the following at June 30:

	2006					
	Estimated lives (in years)	Beginning balance	Additions	Retirements	Reclassifi-cations	Ending balance
Capital assets not being depreciated:						
Land	—	$ 888,172	—	—	—	888,172
Construction in progress	—	14,811,483	61,924,054	—	(16,919,473)	59,816,064
Total not being depreciated		15,699,655	61,924,054	—	(16,919,473)	60,704,236
Capital assets being depreciated:						
Land improvements	15-25	35,573,890	—	—	5,157,649	40,731,539
Buildings, including improvements	10-50	316,704,007	—	(559,011)	11,761,824	327,906,820
Furnishings and equipment (including cost of capital leases)	5-15	59,874,100	5,937,163	(1,789,847)	—	64,021,416
Total being depreciated		412,151,997	5,937,163	(2,348,858)	16,919,473	432,659,775
Less accumulated depreciation:						
Land improvements		7,219,281	1,612,765	—	—	8,832,046
Building, including improvements		120,336,086	9,268,908	(437,929)	—	129,167,065
Furnishings and equipment		38,421,592	5,215,684	(1,573,066)	—	42,064,210
Total accumulated depreciation		165,976,959	16,097,357	(2,010,995)	—	180,063,321
Capital assets, net		$ 261,874,693	51,763,860	(337,863)	—	313,300,690

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	2005					
	Estimated lives (in years)	**Beginning balance**	**Additions**	**Reductions**	**Reclassifi-cations**	**Ending balance**
Capital assets not being depreciated:						
Land	—	$ 888,172	—	—	—	888,172
Construction in progress	—	6,576,407	13,549,257	—	(5,314,181)	14,811,483
Total not being depreciated		7,464,579	13,549,257	—	(5,314,181)	15,699,655
Capital assets being depreciated:						
Land improvements	15-25	32,664,418	2,909,472	—	—	35,573,890
Buildings, including improvements	10-50	308,160,913	3,228,913	—	5,314,181	316,704,007
Furnishings and equipment (including cost of capital leases)	5-15	55,761,097	5,314,501	(1,201,498)	—	59,874,100
Total being depreciated		396,586,428	11,452,886	(1,201,498)	5,314,181	412,151,997
Less accumulated depreciation:						
Land improvements		5,767,859	1,451,422	—	—	7,219,281
Building, including improvements		111,257,829	9,078,257	—	—	120,336,086
Furnishings and equipment		34,417,340	4,909,456	(905,204)	—	38,421,592
Total accumulated depreciation		151,443,028	15,439,135	(905,204)	—	165,976,959
Capital assets, net		$ 252,607,979	9,563,008	(296,294)	—	261,874,693

(7) Long-Term Liabilities

Long-term liabilities consist of the following at June 30:

	2006				
	Beginning balance	**Additions**	**Reductions**	**Ending balance**	**Current portion**
Leases and bonds payable:					
Lease obligations	$ 15,510,202	507,618	1,389,334	14,628,486	1,283,742
Revenue bonds payable	167,433,622	81,515,000	63,427,532	185,521,090	2,055,626
Loans payable	243,484	1,929,690	236,768	1,936,406	379,010
Total leases and bonds payable	183,187,308	83,952,308	65,053,634	202,085,982	3,718,378
Other long-term liabilities:					
Compensated absences	17,210,983	1,392,384	910,388	17,692,979	1,061,579
Total long-term liabilities	$ 200,398,291	85,344,692	65,964,022	219,778,961	4,779,957

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	2005				
	Beginning balance	**Additions**	**Reductions**	**Ending balance**	**Current portion**
Leases and bonds payable:					
Lease obligations	$ 16,162,039	583,568	1,235,405	15,510,202	1,202,816
Revenue bonds payable	96,952,155	71,675,000	1,193,533	167,433,622	2,687,533
Loans payable	317,328	—	73,844	243,484	75,376
Total leases and bonds payable	113,431,522	72,258,568	2,502,782	183,187,308	3,965,725
Other long-term liabilities:					
Compensated absences	16,378,492	1,986,135	1,153,644	17,210,983	1,300,450
Total long-term liabilities	$ 129,810,014	74,244,703	3,656,426	200,398,291	5,266,175

Bonds Payable

The revenue bonds payable totaling $185,521,090 and $167,433,622 as of June 30, respectively, consist of the following:

	2006	**2005**
Revenue Bonds payable to U.S. Government:		
1972 Graduate Housing Revenue Bonds, 5.75%, due semiannually through 2007	$ 260,000	375,000
Series 1993 B Facility Revenue and Refunding Bonds – Various Purpose Educational Facilities, 4.60% to 5.50%, due semiannually through 2023	260,040	403,660
Series 1997 Higher Education Revenue Bonds – University of Rhode Island Issue, 4% to 5.3%, due semiannually through 2023	1,720,000	1,780,000
Series 1999 A University of Rhode Island Auxiliary Enterprise Revenue Issue, 4.75% to 5.875%, due semiannually through 2029. The bonds were paid in fiscal 2006 from the proceeds of the Series 2005 D	—	18,390,000
Series 1999 B University of Rhode Island Educational and General Issue, 4.75% to 5.8%, due semiannually through 2029. The bonds were paid in fiscal 2006 from the proceeds of the Series 2005 G	—	3,500,000
Series 2000 B University of Rhode Island Educational and General Issue, 4.50% to 5.70%, due semiannually through 2030. The bonds were paid in fiscal 2006 from the proceeds of Series 2005 G	—	40,045,000

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	2006	2005
Series 2002 University of Rhode Island Educational and General Revenue Issue, 3% to 5.0% due semiannually through 2022	$ 7,660,000	7,975,000
Series 2003 A University of Rhode Island Educational and General Revenue Issue, 2% to 5%, due semiannually through 2013	2,790,000	3,100,000
Series 2003 B Facility Revenue Refunding Bonds, Auxiliary Enterprise Revenue Issue, 2% to 5%, due semiannually through 2023	12,152,600	12,640,959
Series 2003 C Facility Revenue Refunding Bonds, Educational and General Revenue Issue, 2% to 5%, due semiannually through 2023	7,488,450	7,549,003
Series 2004 A University of Rhode Island Auxiliary Enterprise Revenue Issue, 2.5% to 5.5%, due semiannually through 2024	33,935,000	33,935,000
Series 2004 B University of Rhode Island Auxiliary Enterprise Revenue Issue, 4% due semiannually through 2034	33,000,000	33,000,000
Series 2005 A University of Rhode Island Educational and General Revenue Issue, 3% to 4.25%, due semiannually through 2020	2,740,000	2,740,000
Series 2005 B University of Rhode Island Educational and General Revenue Issue, 3% to 4.25%, due semiannually through 2025	2,000,000	2,000,000
Series 2005 C University of Rhode Island Auxiliary Enterprise Revenue Issue, 3% to 4.625%, due semiannually through 2035	13,840,000	—
Series 2005 D University of Rhode Island Auxiliary Enterprise Revenue Refunding Issues, 3% to 4.625%, due semiannually through 2029	19,625,000	—
Series 2005 F University of Rhode Island Educational and General Revenue Issue 3% to 4.50%, due semiannually through 2025	3,245,000	—
Series 2005 G University of Rhode Island Educational and General Revenue Issue 4% to 5%, due semiannually through 2030	44,805,000	—
	$ 185,521,090	167,433,622

The 1972 Graduate Housing Revenue Bond was issued under trust indentures and is collateralized by a pledge of revenues from the facilities financed. The facilities include University housing, dining and student union operations. Under the terms of the trust indentures, certain net revenues from the pledged facilities must be transferred to the trustees for payment of interest, retirement of bonds and maintenance of facilities.

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In July 1993, Rhode Island Health and Education Building Corporation (the Corporation) issued the Facility Revenue and Refunding Bonds which included the $14,281,069 Various Purpose Educational Facilities Issue – Series 1993 B. The proceeds from this issue were used to defease the outstanding obligations of the University, Rhode Island College (RIC) and the Community College of Rhode Island (CCRI) relative to previous Series A and B issues of 1990 and 1992, respectively, and to fund the acquisition of library capital, and various capital renovations to existing buildings at the three institutions.

On September 1, 1997 the Corporation issued the $2,125,000 University of Rhode Island Issue, Series 1997. The proceeds of the Series 1997 Bonds, including accrued interest to the date of delivery, were used for the construction of an addition of the University's Social Science Center and for the renovations to the University's Multicultural Center.

On September 15, 1999, the Corporation issued the $20,000,000 University of Rhode Island Auxiliary Enterprise Revenue Issue, Series 1999 A and the $3,800,000 University of Rhode Island Educational and General Reserve Issue, Series 1999 B. The proceeds of the Series 1999 A Bonds were used for the renovations and improvements to the University's residence halls and surrounding landscaping on the Kingston Campus, while the proceeds of the Series 1999 B Bonds were used for the acquisition of buildings on the University's Kingston Campus for general administrative use and for the reconstruction of paved surfaces on the Kingston Campus including roads, walkways, and parking lots.

On November 1, 2000, the Board completed a second amendment to the Loan and Trust Agreement dated as of September 1, 1997 authorizing the issuance of the University of Rhode Island Educational and General Issue Series 2000 B Bonds, par amount $40,160,000. The proceeds of Series 2000 B Bonds were used to finance capital improvements at the University consisting of the Athletic Complex Convocation Center, the Athletic Complex Ice Rink Facility, and a modular building.

On November 15, 2002, the Corporation issued the University of Rhode Island Educational and General Reserve Issue, Series 2002 Bonds. The proceeds of these bonds were used to finance the construction and equipping of 1,000 parking spaces, transit shelters, parking meters, and shuttle services. In addition, part of the proceeds were deposited in a capitalized interest fund to finance the interest due until 2005.

On May 1, 2003, the Corporation issued the University of Rhode Island Educational and General Revenue Issue, Series 2003 A Bonds, par amount $3,100,000. The proceeds of the Series 2003 A Bonds were used for the construction, equipping and furnishing of the Alumni Center, which provides meeting and reception space as well as office suites for staff members serving the University of Rhode Island Alumni Association and the Division of University Advancement.

On July 17, 2003, the Corporation issued the Facility Revenue Refunding Bonds, Auxiliary Enterprise Revenue Issue, Series 2003 B Bonds, par amount $20,785,000, and the Facility Revenue Refunding Bonds, Educational and General Revenue Issue, Series 2003 C Bonds, par amount $13,165,000. The proceeds of these bonds were used to defease the outstanding obligations of the University, RIC and CCRI relative to the previous Series A and Series B issues of 1993.

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In December 2004, the Corporation issued the University of Rhode Island Auxiliary Enterprise Revenue Issue, Series 2004 A, Fixed Rate Revenue Bonds with a par amount of $33,935,000 and the University of Rhode Island Auxiliary Enterprise Revenue Issue, Series 2004 B, Variable Rate Revenue Bonds with a par amount of $33,000,000. The proceeds of the 2004 Bonds are being used for the construction of a 440-bed apartment unit and a 360-suite-style residence hall. In addition, part of the proceeds were deposited in a capitalized interest fund to finance the interest due until 2007.

On April 1, 2005, the Corporation issued the University of Rhode Island Educational and General Revenue Issue, Series 2005 A Bonds, par amount $2,740,000. The proceeds were used to construct the 2nd level of an existing facility, Surge Modular Building I, located at 210 Flag Road on the Kingston Campus.

On June 30, 2005, the Corporation issued the University of Rhode Island Educational and General Revenue Issue, Series 2005 B, with a par amount of $2,000,000. The proceeds of this bond were used for the construction and rebuilding of parking facilities, roadways, sidewalks, curbing, drainage and landscape amenities on the Kingston Campus.

On October 14, 2005, the Corporation issued the University of Rhode Island Auxiliary Enterprise Revenue Issue, Series 2005 C Bonds with a par amount of $13,840,000. The proceeds of the 2005 C Bonds were used for the demolition and construction of a two story dining hall. The Corporation also issued the University of Rhode Island Education and General Revenue Issue, Series 2005 F Bonds with a par amount of $3,245,000. The proceeds of the 2005 F Bonds were used to acquire and demolish the former Delta Chi House.

On October 14, 2005, the Corporation issued the Auxiliary Enterprise Revenue Refunding Issue, Series 2005 D Bonds with a par amount of $19,625,000. The proceeds of the 2005 D Bonds were used to advance refund the outstanding Series 1999 A principal of $18,020,000. The net present value savings from refunding is $1,127,401. The Corporation also issued the Educational and General Revenue Issue, Series 2005 G Bonds with a par amount of $44,805,000. The proceeds of the 2005 G Bonds were used to advance refund the outstanding Series 1999 B principal of $3,430,000 and Series 2000 B principal of $39,290,000. The net present value of savings of this refunding is $2,185,245 in total.

In addition to specific project costs, bond proceeds were also used to fund debt service reserve funds and costs of bond issuance.

The bonds issued by the Corporation are special limited obligations of the Board of Governors acting on behalf of the University. The refunding and general and educational bonds are secured by all available revenues of the Board of Governors derived by the University and State appropriations for the University. The auxiliary enterprise revenue bonds are secured by all auxiliary enterprise revenue of the University.

The bond agreements covering the above-mentioned bond issues contain redemption provisions and various restrictive covenants. The University complied with such covenants at June 30, 2006 and 2005.

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Principal and interest on bonds payable for the next five years and in subsequent five-year periods are as follows:

	Principal	Interest	Total
Year ending June 30:			
2007	$ 2,055,624	8,126,537	10,182,161
2008	3,864,309	8,048,238	11,912,547
2009	5,310,930	7,752,790	13,063,720
2010	5,488,117	7,571,080	13,059,197
2011	5,695,303	7,372,170	13,067,473
2012-2016	30,966,949	33,477,504	64,444,453
2017-2021	36,862,874	26,178,598	63,041,472
2022-2026	39,501,984	16,588,848	56,090,832
2027-2031	37,325,000	7,981,100	45,306,100
2032-2036	18,450,000	1,651,306	20,101,306
	$ 185,521,090	124,748,171	310,269,261

In conjunction with its 2004 B issuance of fixed-rate revenue bonds, the University entered into an interest rate Swap agreement with a financial institution counter party. See note 8 for details.

Interest costs for the years ended June 30, 2006 and 2005 were $5,014,055 and $7,331,214, respectively. Of these amounts, $695,740 and $1,712,238 were capitalized in 2006 and 2005, respectively.

Loans Payable

Principal and interest in loans payable for the next five years are as follows:

	Principal	Interest	Total
Year ending June 30:			
2007	$ 379,010	43,707	422,717
2008	440,229	38,851	479,080
2009	299,912	33,729	333,641
2010	305,312	28,328	333,640
2011	511,943	75,203	587,146
	$ 1,936,406	219,818	2,156,224

Lease Obligations

On May 21, 1998, the Board and the University (individually and collectively called University) entered into a Development and a Steam Service Agreement with ERI Services, Inc., the Seller, a Delaware corporation. Noresco, LLC, (a company subsidiary) was the Seller's contract service provider. On December 30, 2005, Noresco was sold to ERI (including the University's contract) to a fund managed by

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GFI Energy Ventures, LLC, a California corporation. Under this agreement, the Seller is required to deliver and the University is required to purchase certain quantities of acceptable steam required by the University in connection with its operation. The Seller's commitment for steam service to the University is for a duration of twenty years from the initial delivery date, which corresponds to the completion of the construction of the new steam plant.

The Seller assumed the construction costs of this facility, which is located on the University's property. In addition, the Seller is responsible for the costs of operating this facility and for making such additional repairs to the steam/condensate distribution system as directed by the University at a cost of up to $1.5 million.

The Seller is required to supply the University with 320,000,000 pounds of steam annually until 2019. If the Seller is unable to supply this requirement, the University may purchase steam in excess of that produced by the Seller from any other source. Additionally, the Seller cannot sell steam produced at the facility to any party other than the University without prior consent from the University. Each year, the actual consumption of steam is recorded and a year-end adjustment is effectuated to assure that all operation and maintenance costs are addressed.

The monthly charges for services under the contract consist of a capacity charge and a variable charge for acceptable steam delivered. For contract years 1 through 20, the capacity charged is fixed at $108,000 per month. The variable charge for the same period is calculated as the sum of commodity charges for gas and fuel oil consumed at the plant plus gas transportation and delivery charge, including operation and maintenance charge for acceptable steam delivered per thousand pounds. The O & M charge is adjusted for the current consumer price index.

On May 15, 1999, the Rhode Island Economic Development Corporation (EDC) issued the $16,395,000 Rhode Island Economic Development Corporation Revenue Bonds (University of Rhode Island Steam Facility Project) Series 1999 and made the proceeds available to ERI to fund the construction of the steam plant. On June 3, 1999, the University, ERI, EDC, and the Chase Manhattan Bank, as Trustee, entered into a Consent, Amendment, and Assignment Agreement to ensure the continued payment of the capacity charge. The agreement requires the University to include in each annual budget a specific line item request for the capacity charge. This includes a specific reference to the capacity charge as the source of payment of the debt service on the Rhode Island Economic Development Corporation Revenue Bonds (University of Rhode Island Steam Facility Project) Series 1999. During the term of the Indenture Agreement covering this bond issue, the University is obligated to make payments of the capacity charge directly to the Trustee.

The construction of the facility was completed in November 1999, and the University owns the facility throughout the term of the Steam Agreement and thereafter.

The University accounted for the amounts due under the above steam agreement as a capital lease and recorded the steam plant at $16,395,000, the present value of the minimum lease payments.

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The following schedule summarizes future minimum payments under all noncancelable leases at June 30, 2006:

	Principal	Interest	Total
Year ending June 30:			
2007	$ 1,283,741	664,059	1,947,800
2008	1,306,944	616,343	1,923,287
2009	861,299	566,086	1,427,385
2010	897,370	526,459	1,423,829
2011	938,732	483,820	1,422,552
2012-2016	4,755,400	1,726,833	6,482,233
2017-2020	4,585,000	453,271	5,038,271
	$ 14,628,486	5,036,871	19,665,357

(8) Interest Rate Swap

(a) Objective of the Interest Rate Swap

The intent of the Swap was to lower the cost of funds relating to the University's currently outstanding Auxiliary Enterprise Revenue Issue, Series 2004 B.

(b) Terms

The University pays the bondholders a variable rate set weekly. Based on the Swap agreement, the University pays interest at a variable rate based on the Bonds and I) a Fixed Rate on the Swap equal to 3.691% and II) in return the University receives the sum of (i) 67.0% of the one month USD-LIBOR-BBA plus (ii) 0.12%. The one month USD-LIBOR-BBA plus 0.12% is a variable rate designed to offset the variable rate paid to the bondholders, thereby establishing a synthetic fixed rate for the bonds.

All payments under the Swap agreement are netted and paid on a monthly basis each on the fifteenth (15th), commencing on January 15, 2005. As further defined in the Confirmation to the Swap agreement, the Board of Governors of Higher Education is acting for the University. Subject to cash settlement, the University has the right to terminate the agreement, in whole or in part, on the Effective Date and on any Business Day thereafter. The Swap is scheduled to terminate on September 15, 2034.

(c) Fair Value

Because interest rates have declined and tax-exempt and taxable ratios have remained high since execution of the Swap, the Swap, if it were to be terminated, had a fair market value of $1,215,250 and a negative fair market value of $2,530,725 as of June 30, 2006 and June 30 2005, respectively. Swaps are not normally valued through exchange-type markets with easily accessible quotation systems and procedures. The fair market value was calculated using the zero coupon method.

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Information was obtained from generally recognized sources with respect to quotations, reporting specific transactions and market conditions and based on accepted industry standards and methodology.

(d) Basis and Credit Risk

As the variable rate that the University pays on its Bonds, which approximates the Bond Market Association Municipal Swap Index, differs from the variable percent of LIBOR rate received from MLCS, the Swap exposes the University to basis risk. As of June 30, 2006 and June 30, 2005, the Bond Market Municipal Swap Index was 3.97% and 2.28%, respectively whereas 67.0% of 1 month LIBOR plus 0.12% was 3.58% and 2.35% respectively.

As of June 30, 2006, the University was exposed to credit risk because the Swap had a negative fair value. MLCS is unconditionally guaranteed by Merrill Lynch & Co. and has maintained their ratings since inception of AA3, A+ and AA- by Moody's Investors Service, Standard & Poor's and Fitch Ratings, respectively. Additionally the University has obtained Swap insurance on this transaction from Ambac Assurance Corporation. To mitigate credit risk, if the counterparty's credit quality falls below a threshold level, the counterparty is obligated, on demand of the University, to provide and maintain collateral (cash or U.S. Government and Agency Securities) having certain values required by the Swap in order to provide security for payment of the positive value of the Swap, if any, to the University.

(9) Grant Refundable

The University participates in the Federal Perkins Loan, Nursing Loan, and Health Profession Loan Programs. These programs are funded through a combination of federal and institutional resources. The portion of these programs that has been funded with federal funds is ultimately refundable to the U.S. government upon the termination of the University's participation in the programs.

(10) Restricted Net Assets

The University is the recipient of funds that are subject to various external constraints upon their use, either as to purpose or time. These funds are composed of the following at June 30:

	2006	2005
Restricted – expendable:		
Loans	$ 3,187,037	3,012,534
Capital programs	3,547,142	8,490,033
Sponsored research	82,714	24,685
	$ 6,816,893	11,527,252

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(11) Unrestricted Net Assets

The University's unrestricted net assets at June 30 were internally designated for goods and services that have not yet been received and normal working capital balances maintained for auxiliary enterprise and departmental activities.

(12) Contingencies

Various lawsuits are pending or threatened against the University that arose from the ordinary course of operations. In the opinion of management, no litigation is now pending, or threatened that would materially affect the University's financial position.

At June 30, 2006 and 2005, the University is a guarantor of loans to fraternities and sororities in the amount of $563,532 and $563,782, respectively.

The University receives significant financial assistance from federal and state agencies in the form of grants. Expenditures of funds under these programs require compliance with the grant agreements and are subject to audit. Any disallowed expenditures resulting from such audits become a liability of the University. In the opinion of management such adjustments, if any, are not expected to materially affect the financial condition of the University.

(13) Operating Expenses

The University's operating expenses, on a natural classification basis, are the following for the years ended June 30:

		2006	2005
Compensation and benefits	$	230,700,351	221,823,351
Supplies and services		96,223,619	86,549,314
Depreciation and amortization		16,309,085	15,439,135
Scholarships and fellowships		14,950,673	13,940,038
	$	358,183,728	337,751,838

(14) State Appropriation

(a) Direct Appropriations

Pursuant to the Rhode Island General Law 16-59-9, the legislature-enacted budget reflects the budget passed by the General Assembly and signed by the Governor as well as any re-appropriations made by the Governor for fiscal 2005. The Board reviews and approves the unrestricted and restricted budgets and makes recommendations to the Governor and General Assembly for revisions to the current year's budget and the ensuing year's budget for the University, RIC, CCRI, and the Office of Higher Education.

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The original and supplemental budget requests to the Governor and General Assembly are acted upon by a vote of the Board. As part of the University's annual budget process for unrestricted and restricted funds, the Board allocates specific amounts in the budget which are allocated for the following categories: (1) salaries and wages; (2) operating expenditures; and (3) outlays for personnel costs, utilities, repairs, capital, and student aid, as well as the overall budget allocation.

(b) State Capital Plan Funds

The Rhode Island Capital Plan Fund was modeled on a financial technique originating in the State of Delaware. Each year the State reserves 2% of its general revenues to fund a Budget Reserve and Cash Stabilization Fund. This process continues annually until the fund reaches 3% of total resources. Once that point is achieved, excess revenues are transferred to a Capital Plan Fund. This Capital Fund is used for capital expenditures and for debt reduction. The technique is a "pay-as-you-go" process that avoids increasing the state's debt burden. Higher education has received off-budget allocations through this program since fiscal 1995.

During fiscal years 2006 and 2005, the State allocated \$9.31 million and \$6.21 million, respectively, to the University for asset protection.

(c) State Contributed Capital

In November 1998, the Rhode Island votes approved the issuance of \$21.0 million General Obligation Bonds for higher education facilities. The bond provided the University with \$10.0 million for the renovations of Lippitt and Independence Hall. From the proceeds of these general obligation bonds issues, the University spent \$2.87 and \$0.59 million on the renovations of these two buildings at the Kingston Campus during fiscal years 2006 and 2005, respectively.

In November 2000, the Rhode Island voters approved the issuance of General Obligation Bonds to fund improvements to the University. The bonds provide funding until 2008 with \$22 million to fund the major renovations and upgrades of student residence halls and surrounding landscape at the University. During fiscal years 2006 and 2005, the University spent \$1.17 million and \$1.99 million, respectively.

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In November 2004, Rhode Island voters approved the issuance of $114 million General Obligation Bonds to fund improvements for higher education facilities. The bonds provide the University with $20 million to complete the residence hall renovation project initiated in 1999, $14 million for the construction of an Ocean Exploration and Research Center and rehabilitate the Pell Marine Science Library, and $50 million for the construction of the Center for Biotechnology and Life Sciences. During fiscal years 2006 and 2005, the University spent $8.41 million and $0.57 million, respectively.

The expenditures funded from the proceeds of the above-mentioned general obligation bonds and capitalized during fiscal years 2006 and 2005 totaled $12,433,660 and $3,201,612, respectively.

The University's State appropriations is composed of the following at June 30:

		2006	2005
Direct appropriations	$	83,187,769	82,910,362
State Capital Plan Funds		9,313,249	6,213,289
State contributed capital		12,433,660	3,201,612
	$	104,934,678	92,325,263

(15) Pension, Early, and Post-Retirement Plans

Certain employees of the University, RIC, CCRI, and the Office of Higher Education (principally faculty and administrative personnel) are covered by individual annuity contracts under a defined contribution retirement plan. Eligible employees who have reached the age of 30, and who have two (2) years of service are required to participate in either the Teachers' Insurance and Annuity Association, the Metropolitan Life Insurance Company or Variable Annuity Life Insurance Company retirement plan. Eligible employees must contribute at least 5% of their gross biweekly earnings. These contributions may be made on a pre-tax basis. The University contributes 9% of the employee's gross biweekly earnings. Total expenditures by the University for such 403(b) annuity contracts amounted to $8,311,928 and $7,913,225 during 2006 and 2005, respectively.

Other employees of the University (principally civil service personnel) participate in the Employees' Retirement System of the State of Rhode Island (System), a multiple-employer, cost-sharing, public employee retirement system. The plan provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. The level of benefits provided to state employees is established by Chapter 36-10 of the General Laws which is subject to amendment by the general assembly. The System issues a publicly available financial report that includes financial statements and required supplementary information for plans administered by the system. The report may be obtained by writing to the Employees' Retirement System, 40 Fountain Street, Providence, RI 02903. The payroll expense of University employees covered by the system was $36,954,644 and $34,243,672 for the years ended June 30, 2006 and 2005, respectively. The University's total payroll expense for the years ended June 30, 2006 and 2005 was $174,360,184 and $166,682,017, respectively.

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All full-time employees of the University who have not obtained at least 10 years of contributory service as of July 1, 2005 and are not covered by 403(b) annuity contracts are eligible to retire at or after age 65 with 10 years of credited service, or at age 59 with 29 years of credited service or at age 55 and had completed 20 years of total service provided, that the retirement allowance, as determined according to the formula in the State statute is reduced actuarially for each month that the age of the member is less than 65 years. The retirement benefit is equal to various percentages of annual earnings, ranging from 1.6% to 2.25% for each of the first 38 years of service, to the maximum benefit of 75% of final salary after 38 years of service. Final average salary is the three highest consecutive years of earned salary excluding overtime, bonuses or severance pay. The System also provides certain death and disability benefits. The above information can be found at RIGL 36-10-9 and 36-10-10.

Employer and employee required contributions to the System are established by the State of Rhode Island and are based on percentages established by the State of Rhode Island and are based on percentages of covered employees' gross salaries, which are calculated annually by the fund's actuaries. Covered employees in the System were required to contribute 8.75% of salaries paid while the University was required to pay 14.84% and 11.51% of salaries paid for the years ending June 30, 2006 and 2005, respectively. In addition, the University is required to contribute 2.24% and 1.87% in 2006 and 2005, respectively, for post-retirement health benefits. Employees contributed $3,233,531 and $2,996,321, respectively, and the University's contribution to the System for the years ended June 30, 2006, 2005, and 2004 were $6,312,974, $4,852,572, and $3,653,403, respectively, representing 100% of the required contribution for each of the three years.

In 1998, the Rhode Island Board of Governors for Higher Education established a health care insurance retirement program (medical coverage only), effective July 1, 1998. This health benefit applies to employees who participate in the Rhode Island Board of Governors for Higher Education defined contribution retirement plan noted above. Active employees who are covered by the Board of Governors retiree medical plan contribute 0.25% of their regular salary. To be eligible for coverage the retiree must have worked a minimum of 10 years for the Board of Governors or the University and must be 60 years of age, unless they have 28 years of service. Depending on the years of service and the retiree's age the Board of Governors will pay from 50% to 100% medical insurance premium while the retiree will contribute from 50% to 0%. Employees covered by this program contributed $383,000 and $348,000 during fiscal years 2006 and 2005, respectively.

(16) Joint Venture

Municipal joint ventures pool resources to share the costs, risks, and rewards of providing services to their participants, the general public, or others. The University, in coordination with the Town of South Kingstown and the Town of Narragansett, shares in the maintenance costs of the regional waste water system, which was constructed during the late 1970's. Each is responsible for its share of the net capital and administrative costs of the project. The University's fiscal 2006 and 2005 share of capital expenditures amounted to $45,302 and $20,442, respectively.

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In addition to capital costs, the University is responsible for its proportionate share of the total operating costs of the regional waste water system. Its share of the operating costs is in proportion to its share of the total flow into the common facilities as determined by metering devices and a predetermined percentage of operating costs of certain other facilities. The University's share of operating costs amounted to $456,504 and $397,920 in 2006 and 2005, respectively. Financial information may be obtained at the Town of South Kingstown, 180 High Street, Wakefield, Rhode Island 02879.

(17) Pass Through Grants

The University distributed $49,179,675 and $44,803,628 during fiscal 2006 and 2005, respectively, for student loans through the U.S. Department of Education federal direct lending program. These distributions and related funding sources are not included as expenses and revenues or as cash disbursements and cash receipts in the accompanying financial statements.

KPMG LLP
600 Fleet Center
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Providence, RI 02903

September 1, 2006

Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

The Board of Governors for Higher Education
State of Rhode Island and Providence Plantations:

We have audited the financial statements of the business-type activities and the discretely presented component units of the University of Rhode Island (the University) (a component unit of the State of Rhode Island and Providence Plantations) as of and for the year ended June 30, 2006, which collectively comprise the University's basic financial statements, and have issued our report thereon dated September 1, 2006, which included a reference to the reports of other auditors who audited the discretely presented component units. We did not audit the financial statements of the discretely presented component units. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Our consideration of internal control over financial reporting and our tests of compliance with certain provisions of laws, regulations, contracts and grants, and other matters did not include the discretely presented component units audited by the other auditors referred to in the previous paragraph. The findings, if any, of those other auditors are not included herein.

Internal Control over Financial Reporting

In planning and performing our audit, we considered the University's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the University's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information of the Board of Governors for Higher Education management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP