FINANCIAL STATEMENTS

2003–2004

UNIVERSITY OF ROCHESTER

University of Rochester

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December 10, 2004

To: The President and the Board of Trustees

The 2003-04 financial statements that follow indicate that the University of Rochester and its related entities completed the fiscal year in sound financial condition. With an increase of approximately $142 million, the University's total net assets exceeded $2 billion at year-end. The continuing outstanding performance of the University's healthcare system and the positive returns on the University's investment portfolio were determining factors in the University's financial results for the year. A detailed analysis of the financial statements is found in the Controller's commentary on page 2.

While the University achieved positive financial results for the year, it is important to make note of the following evidence of the institution's vitality:

- Advances in the quality of the undergraduate student population made under the Renaissance Plan for the College were maintained;
- External research funding continued to increase with total sponsored project activity exceeding $300 million for the first time;
- The institution continued to invest in facilities and technological infrastructure in order to maintain its competitive position.

The success of the University, including its successful financial performance, is attributable in large measure to the quality of its instructional, research and service programs. In support of those programs, the administrative side of the house continued its efforts to reduce costs and improve efficiency. Examples over the past year include:

1. The Series 2003 bond issue through the Dormitory Authority of the State of New York, along with the related interest rate swap transaction, produced significant savings through the refinancing of approximately $89 million of existing debt and provided cost effective financing for capital projects to be undertaken by the University.
2. A detailed proposal was approved by the University's trustees in March of 2004 for a 25-megawatt cogeneration facility. That facility will significantly reduce the institution's energy costs while renewing the University's energy infrastructure.
3. Execution of major purchasing contracts has resulted in immediate cost reductions for goods and services purchased by the University.

The University and its related entities continue to focus on financial management and stewardship of resources with added emphasis on risk assessment and compliance activities. At the senior management level, a university-wide compliance group is charged with the responsibility of inventorying and monitoring compliance issues ranging from financial reporting to environmental health and safety. Insuring institutional compliance and effectively managing risks will remain top management priorities into the future and will ultimately contribute to the University's financial strength.

Ronald J. Paprocki
Senior Vice President for Administration and
Finance and Chief Financial Officer

Financial Statements Highlights

Summary

The combined financial activities of the University of Rochester and Related Entities concluded with an increase to consolidated total net assets of approximately $142 million for the fiscal year ending June 30, 2004. Overall, the University's financial results demonstrate consistent and steady operating activities with fluctuating but improving non-operating activities dominated by endowment performance. During this past fiscal year, a number of financial "milestones" were reached. On the balance sheet, combined cash and cash equivalents (including operating investments) were above $200 million and our total net assets topped $2 billion for the first time in our financial history. From the statement of activities, our annual revenues from sponsored grants and contracts surpassed $300 million. The increase to net assets from operations of over $34 million was driven in large part by the continued stalwart operating results of Strong Memorial Hospital (4% operating margin) and the University of Rochester Medical Faculty Group (URMFG) as well as improvements in the operating results of Highland Hospital. The increase to consolidated net assets from non-operating activities approached $142 million and was generated primarily from the 17.4% return on the University's endowment investment portfolio.

Results of Operations

A review of the consolidated financial results over the last three years demonstrates the continued and significant growth in the combined activities of the organization. The following table provides trend information regarding key financial statement indicators:

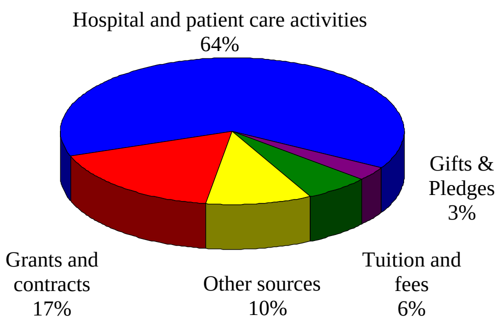
Selected Financial Trends
($'s in millions)

	FY04	FY03	FY02
Consolidated operating revenues	**$** 1,808.9	$ $1,652.9	$ 1,569.9
Consolidated operating expenses	**$** 1,774.6	$ 1,632.9	$ 1,526.8
Consolidated cash position (including operating investments)	$ 212.8	$ 154.4	$ 138.6
Consolidated investments held for long-term purposes	$ 1,429.0	$ 1,274.9	$ 1,269.0
Positive/(negative) return on endowment investment portfolio	17.4%	4.7%	(3.8%)
Consolidated changes in net assets:			
From operating activities	$ 34.3	$ 20.1	$ 43.1
From non-operating activities	107.6	(31.4)	(103.3)
Cumulative effects	-	-	21.2
Total increase/(decrease) to net assets	**$** 141.9	$ (11.3)	$ (39.0)
Consolidated total net assets	$ 2,031.0	$ 1,889.1	$ 1,900.5

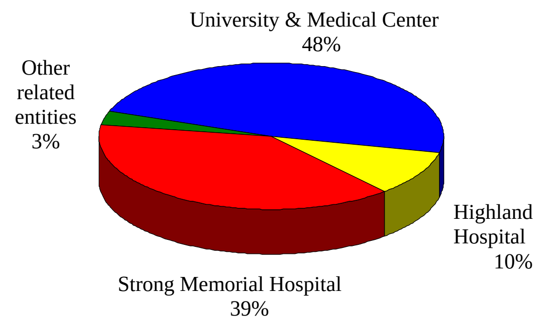
Revenues:

Consolidated operating revenues increased by 9.4% over the prior year to over $1.8 billion for FY2004. Net tuition and fee revenue increased via an average rate increase of 5% while the composite financial aid rate increased slightly to 40.9%. Consistent revenue growth patterns have been dominated by the categories of hospital and faculty practice patient care activities and grants and contracts revenues. Combined patient care revenues are reflective of continued expansion of patient volumes at both our flagship Strong Memorial Hospital (SMH) and Highland Hospital with increased revenues of 7% and 9%, respectively. The URMFG reported an increase in revenues of over 23% due to hospital patient volume increases and also to the acquisition of a new clinical practice group and the relocation of another to a better-situated facility. Revenues from all sources in hospital and faculty practice patient care activities increased by 10.5% and totaled over $1.1 billion by year's end. FY2004 grants and contracts revenues totaled $310 million, or an increase of approximately 12% compared to last year. This increase was achieved by the continued growth in sponsor awards, particularly funding from the National Institutes of Health (NIH) in our School of Medicine and Dentistry and from the Department of Energy in our Laboratory for Laser Energetics. Research expenditures incurred under awards from the Department of Health and Human Services increased by over 11% to $152 million compared to $136 million a year ago. Likewise, expenditures under Department of Energy grants increased by 12% to $47 million compared to $42 million the year before. Royalty revenues derived from licensing activities spawned by our research activities totaled $32 million for FY2004, or a slight increase over last year. Gift and pledge revenues were ahead of last year's pace by about $5 million or a 10.5% increase.

FY 2004 Operating Revenues by Source
$1.8 billion

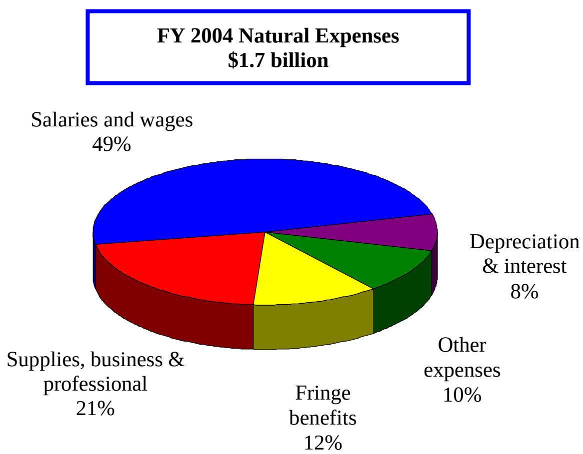


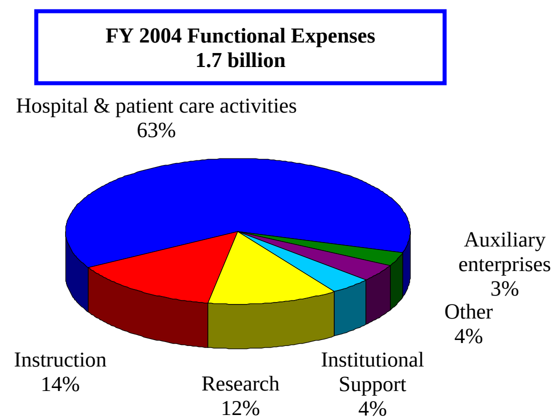
FY 2004 Operating Revenues by Entity
$1.8 billion



Expenses:

Consolidated operating expenses increased by 8.7% over the prior year to $1.7 billion and have had levels of growth similar to those noted in operating revenues. Compensation expenses were about $1.1 billion for the year and represented a 7.4% increase over FY 2003. The increase in the salaries and wages components was reflective of the annual wage and salary program increases, increases in volume and activities in both the health care and research components, and the effects from continued shortages in nurse staffing. We also experienced increases to fringe benefits of approximately 8% over last year. This increase was comprised of not only benefits tied to increased salaries and wages but also to increases to our post-retirement and post-employment benefit obligations due to reductions in the discount rates utilized in projecting future benefit obligations. Supplies expenses are driven heavily by hospital and patient care activities and FY 2004 was no different. Supplies expense (including pharmaceuticals) increased by 11.5% over FY 2003. Business and professional expenses increased to $145.6 million during FY 2004 or 33.5% over last year. This increase was comprised primarily of the University's election to take a one-time write-off of deferred legal fees related to litigation of certain University patent rights. Without the write-off, business and professional fees would have been 9.2% over the prior year. Functional classifications of our expenses are displayed in the footnotes (note 17) of our consolidated financial statements. Instruction expenses increased slightly by just over 1% while research expenses grew by 11.8%. Hospital and patient care activities expenses rose by over 9.5%.





Related entities and affiliates:

This section describes in summary fashion the highlights of the operations of those institutions (without the University and SMH) that consolidate into the financial statements that represent collectively about 13% of consolidated total revenues. Highland Hospital and its subsidiaries generated revenues of about $183 million followed by the Visiting Nurse Service of Rochester and Monroe County, Inc. whose revenues were $40 million for the year ending June 30, 2004. The increase to net assets from operating activities for the combined affiliates was $2.9 million and represented an improvement over the prior year's breakeven results. Highland Hospital and VNS improved on their operating activities by $2 million and $2.8 million, respectively, over FY 2003 figures while the Highlands at Brighton saw its operating margin decrease by approximately $2 million.

Financial Condition

Total assets of the combined institutions grew to close to $3 billion as of June 30, 2004, or 7.5% over last year's ending balance. The University has continued to improve upon its cash position (inclusive of cash and cash equivalents and operating investments) so that by year end, approximately $213 million were held by accounts of the combined entities, or an increase of $58 million over the prior year. By year-end, accounts receivable had increased by $17.6 million due almost entirely to the acquisition of a new clinical practice plan and increased hospital patient volume on URMFG receivables. Inventories, prepaid expenses, and deferred charges decreased from $60.2 million to $39.3 million due to the write-off of deferred legal fees. The year-over-year increase in the market value of investments held for long-term purposes of $154 million was attributable to the 17.4% rate of return on the University's endowment portfolio and unspent funds invested from the proceeds of the Series 2003 bonds; net of endowment income/gains used in operations.

Total liabilities increased by $117.8 million to $941.5 million as of June 30, 2004. Accounts payable and accrued expenses increased by $27 million to $176.7 million at year end and reflective of increases in accrued payroll, post-retirement and post-employment obligations, and the mark-to-market adjustment for the interest rate swap contracts related to the Series 2003 borrowing. Long-term debt increased by $60.1 million primarily the result of the issuance of Series 2003 bonds that refinanced about $86 million of previous debt and provided an additional $79 million of new capital; net of scheduled debt principal payments.

Capital spending for FY2004 totaled $145.2 million compared to $65.6 million for FY2003. The combined additions for FY2004 included $60.2 million for major moveable equipment, $78.3 million for building and renewal/replacement projects, and $6.7 million for library and museum collections. Distribution of total capital expenditures by entity was $84.7 million for the University (including the School of Medicine and Dentistry), $43.6 million for Strong Memorial Hospital, and $16.9 million for all of the related entities.

Consolidated total net assets increased by $141.9 million from $1.89 billion at the end of last year to $2.03 billion at June 30, 2004.

Into FY2005, we will continue to face numerous challenges in maintaining and improving financial performance. Clearly, the performance of the endowment portfolio, fund-raising, and to maintain and improve our physical plant will continue as leading financial priorities for all of the combined institutions.

Douglas W. Wylie
University Controller

KPMG LLP
265 Clinton Square
Rochester, NY 14604

Independent Auditors' Report

The Board of Trustees
University of Rochester:

We have audited the accompanying consolidated balance sheets of the University of Rochester and related entities as of June 30, 2004 and 2003, and the related consolidated statements of activities and cash flows for the years then ended. These consolidated financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the University of Rochester and related entities as of June 30, 2004 and 2003, and the changes in their net assets and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

September 22, 2004

CONSOLIDATED BALANCE SHEETS

As of June 30
(dollars in thousands)

Assets	**2004**	**2003**
Cash and cash equivalents	$ 124,086	$ 93,267
Operating investments	88,746	61,120
Accounts receivable, net	224,489	206,869
Inventories, prepaid expenses and deferred charges	39,296	60,218
Contributions receivable, net	40,922	37,610
Notes receivable, net	21,297	21,034
Other assets	2,637	2,814
Investments held for long-term purposes	1,429,040	1,274,957
Property, plant and equipment, net	934,421	896,154
Interest in net assets of foundation	16,920	15,572
Investments in perpetual trusts held by others	50,622	43,158
Total assets	$ 2,972,476	$ 2,712,773
Liabilities and Net Assets		
Liabilities:		
Accounts payable and accrued expenses	$ 176,748	$ 149,584
Advance receipt of sponsored research revenues	31,141	26,835
Deferred revenue	40,520	38,205
Third-party settlements payable, net	59,360	49,374
Accrued pension, post-retirement, and post-employment obligations	113,602	98,786
Long-term debt	504,240	444,097
Refundable U.S. Government grants for student loans	15,848	16,776
Total liabilities	941,459	823,657
Net Assets:		
Unrestricted	1,587,176	1,485,275
Temporarily restricted	207,447	185,099
Permanently restricted	236,394	218,742
Total net assets	2,031,017	1,889,116
Total liabilities and net assets	$ 2,972,476	$ 2,712,773

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF ACTIVITIES

For The Year Ended June 30, 2004
(dollars in thousands)

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Operating revenues:				
Tuition and fees	$ 198,901	$ -	$ -	$ 198,901
Less: scholarships and fellowships	(81,422)	-	-	(81,422)
Net tuition and fees	117,479	-	-	117,479
State and local appropriations	1,942	-	-	1,942
Gifts and pledges	22,740	12,889	14,092	49,721
Grants and contracts	310,460	-	-	310,460
Hospital and faculty practice patient care activities	1,149,961	-	-	1,149,961
Auxiliary enterprises	38,090	-	-	38,090
Interest income on cash equivalents	4,322	627	-	4,949
Educational activities	26,880	-	-	26,880
Royalty income	31,846	-	-	31,846
Other sources	3,790	-	-	3,790
Long-term investment income and gains allocated to operations	73,798	-	-	73,798
Net assets released from restrictions	22,934	(22,934)	-	-
Total operating revenues	1,804,242	(9,418)	14,092	1,808,916
Operating expenses:				
Salaries and wages	867,555	-	-	867,555
Fringe benefits	221,046	-	-	221,046
Total compensation	1,088,601	-	-	1,088,601
Supplies	228,558	-	-	228,558
Business and professional	145,632	-	-	145,632
Utilities	20,133	-	-	20,133
Maintenance and facilities costs	51,127	-	-	51,127
Depreciation expense	109,437	-	-	109,437
Interest expense	23,811	-	-	23,811
Other	107,321	-	-	107,321
Total operating expenses	1,774,620	-	-	1,774,620
Change in net assets from operating activities	29,622	(9,418)	14,092	34,296
Non-operating activities:				
Long-term investment activities:				
Investment income	19,950	1,634	-	21,584
Net appreciation	123,455	31,469	3,560	158,484
Total long-term investment activities	143,405	33,103	3,560	180,068
Long-term investment income and gains allocated for operations	(73,798)	-	-	(73,798)
Loss on extinguishment of debt	(4,746)	-	-	(4,746)
Other changes, net	7,418	-	-	7,418
Change in valuation of annuities	-	(1,337)	-	(1,337)
Change in net assets from non-operating activities	72,279	31,766	3,560	107,605
Change in net assets	101,901	22,348	17,652	141,901
Beginning net assets	1,485,275	185,099	218,742	1,889,116
Ending net assets	$ 1,587,176	$ 207,447	$ 236,394	$ 2,031,017

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF ACTIVITIES

For The Year Ended June 30, 2003

(dollars in thousands)

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Operating revenues:				
Tuition and fees	$ 190,037	$ -	$ -	$ 190,037
Less: scholarships and fellowships	(76,491)	-	-	(76,491)
Net tuition and fees	113,546	-	-	113,546
State and local appropriations	1,937	-	-	1,937
Gifts and pledges	19,953	19,404	5,532	44,889
Grants and contracts	278,005	-	-	278,005
Hospital and faculty practice patient care activities	1,040,185	-	-	1,040,185
Auxiliary enterprises	38,777	-	-	38,777
Interest income on cash equivalents	3,989	-	-	3,989
Educational activities	24,581	-	-	24,581
Royalty income	31,364	-	-	31,364
Other sources	4,521	-	-	4,521
Long-term investment income and gains allocated to operations	71,176	-	-	71,176
Net assets released from restrictions	19,302	(19,302)	-	-
Total operating revenues	1,647,336	102	5,532	1,652,970
Operating expenses:				
Salaries and wages	808,318	-	-	808,318
Fringe benefits	204,977	-	-	204,977
Total compensation	1,013,295	-	-	1,013,295
Supplies	205,003	-	-	205,003
Business and professional	109,057	-	-	109,057
Utilities	24,966	-	-	24,966
Maintenance and facilities costs	42,827	-	-	42,827
Depreciation expense	107,697	-	-	107,697
Interest expense	24,455	-	-	24,455
Other	105,619	-	-	105,619
Total operating expenses	1,632,919	-	-	1,632,919
Change in net assets from operating activities	14,417	102	5,532	20,051
Non-operating activities:				
Long-term investment activities:				
Investment income	24,009	1,244	4	25,257
Net appreciation	27,963	2,014	1,095	31,072
Total long-term investment activities	51,972	3,258	1,099	56,329
Long-term investment income and gains allocated for operations	(71,176)	-	-	(71,176)
Other changes, net	(14,781)	-	-	(14,781)
Change in valuation of annuities	-	(1,768)	-	(1,768)
Change in net assets from non-operating activities	(33,985)	1,490	1,099	(31,396)
Change in net assets	(19,568)	1,592	6,631	(11,345)
Beginning net assets	1,504,843	183,507	212,111	1,900,461
Ending net assets	$ 1,485,275	$ 185,099	$ 218,742	$ 1,889,116

See accompanying notes to consolidated financial statements

CONSOLIDATED STATEMENTS OF CASH FLOWS

For The Years Ended June 30

(dollars in thousands)

	2004	2003
Cash flows from operating activities:		
Change in net assets	$ 141,901	$ (11,345)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization expense	102,256	105,240
Net appreciation of investments	(158,044)	(35,135)
Gifts of property, plant and equipment	(6,514)	(5,910)
(Appreciation)/depreciation in interest in net assets of foundation	(1,348)	2,474
(Appreciation)/depreciation of investments in perpetual trusts held by others	(4,276)	203
Bond premium amortization	1,490	103
Loss on disposals of property, plant and equipment	7,181	2,457
(Increases)/decreases in:		
Operating investments	(27,626)	(61,120)
Accounts receivable	(17,620)	(9,536)
Inventories, prepaid expenses and deferred charges	20,568	(11,898)
Contributions receivable	(3,312)	2,719
Other assets	(1,954)	(166)
Increases/(decreases) in:		
Accounts payable and accrued expenses	27,164	15,387
Advance receipt of sponsored research revenues	4,306	(298)
Deferred revenues	2,315	4,529
Third-party settlements, net	9,986	(5,970)
Accrued post-employment and post-retirement benefits	14,816	23,928
Contributions for long-term investment, net	(10,559)	(17,836)
Investment income restricted for long-term purposes	365	(1,153)
Net cash provided by/(used in) operating activities	101,095	(3,327)
Cash flows from investing activities:		
Purchases of property, plant and equipment, net	(138,705)	(65,553)
Purchases of investments	(978,189)	(918,953)
Proceeds from the sale and maturity of investments	982,150	948,126
Increase/(decrease) in notes receivable, net of activities and other reductions	(263)	146
Net cash used in investing activities	(135,007)	(36,234)
Cash flows from financing activities:		
Principal repayments of indebtedness	(30,409)	(34,636)
Proceeds from issuance of long-term debt	89,062	9,652
Increase in investments held in perpetuity by others	(3,188)	-
Increase/(decrease) in refundable U.S. Government grants for student loans	(928)	183
Contributions for long-term investment, net	10,559	17,836
Investment income restricted for long-term purposes	(365)	1,153
Net cash provided by/(used in) financing activities	64,731	(5,812)
Net increase/(decrease) in cash and cash equivalents	30,819	(45,373)
Cash and cash equivalents - beginning of year	93,267	138,640
Cash and cash equivalents - end of year	$ 124,086	$ 93,267
Supplemental disclosure of cash flow information - Cash paid during the year for interest on long-term debt	$ 24,528	$ 22,620

See accompanying notes to consolidated financial statements.

(1) Summary of Significant Accounting Policies

(a) General

The University of Rochester (the University) is a private, nonprofit institution of higher education based in Rochester, New York. The University provides education and training services, primarily for students at the undergraduate, graduate and postdoctoral levels. It also performs research, training and other services under grants, contracts and similar agreements with sponsoring organizations, primarily departments and agencies of the United States Government; and provides health care services through Strong Memorial Hospital, Strong Home Care Group and the various entities included in Strong Partners Health System, Inc. (SPHS).

(b) Basis of Presentation

The accompanying consolidated financial statements include all of the integrated divisions of the University – The College, Margaret Warner Graduate School of Education and Human Development, William E. Simon Graduate School of Business Administration, Eastman School of Music, Memorial Art Gallery, School of Medicine and Dentistry, Strong Memorial Hospital, School of Nursing, Eastman Dental Center, Health Affairs and the University of Rochester Medical Faculty Group (URMFG). Included also are Strong Partners Health System, Inc. (and its affiliates), Eastman Dental Center Foundation, Inc., Strong Home Care Group (and its subsidiaries) and the Research Foundation of the University of Rochester. All significant interorganizational balances and transactions have been eliminated.

The University is the sole member of SPHS, which has affiliation agreements with Highland Hospital of Rochester (including its subsidiaries Highland Foundation, Inc., Highland Facilities Development Corp. and the Medical Administrative Associates, Inc.); The Highlands Living Center, Inc.; Highland Community Development Corp.; and The Meadows at Westfall, Inc. Highland Hospital and its subsidiaries have debt outstanding which has been included in the University's consolidated financial statements; however, under the terms of the affiliation agreement with SPHS, the University has no legal obligation for the debt of Highland Hospital and affiliates.

The Eastman Dental Center Foundation (the Foundation) was formed to hold and manage the investment assets of the former Eastman Dental Center, which was merged into the University during 1998. Income and assets of the Foundation are used to support oral health, education and research projects at the University.

The University is the sole corporate member of Strong Home Care Group doing business as Visiting Nurse Service of Rochester and Monroe County, Inc. and Community Care of Rochester.

The University is the sole corporate member of the Research Foundation of the University of Rochester. The Research Foundation manages certain intellectual property created by the University of Rochester and investments based on such intellectual property.

The University, through SPHS, Strong Memorial Hospital and URMFG, formed a Managed Care Organization (MCO) in October 1997 together with two community physician organizations: the Highland Physician Organization and the Rochester Community Physician Organization. The MCO has ceased operations related to member contracting activities and is in the process of winding down its activities.

(c) Basis of Accounting

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

Certain amounts as of and for the year ended June 30, 2003 have been reclassified for comparative purposes.

Classification of Net Assets

The University reports its net assets and changes therein according to three classifications: unrestricted, temporarily restricted and permanently restricted, based upon the existence or absence of donor-imposed restrictions.

Permanently restricted – Net assets subject to donor-imposed stipulations that they be maintained permanently by the University. Generally, the University may use the income and gains derived from the donated assets, restricted only by the donors' stipulations.

Temporarily restricted – Net assets subject to donor-imposed stipulations that may or will be met either by actions of the University and/or the passage of time. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Unrestricted – Net assets that are not subject to donor-imposed stipulations and that are generally available for support of the University's activities, with certain limitations, as follows:

- Uses of certain unrestricted net assets are committed through contractual agreements. Such amounts primarily consist of required trusteed balances under long-term debt agreements and matching funds under student loan programs of the Federal Government. In addition, grants and contracts for the performances of certain services or functions are reported in the unrestricted net asset category.

- Many of the funds, which are unrestricted for accounting purposes, carry internal designations to specific divisions of the University, and therefore are not treated operationally as unrestricted funds.

- Certain accumulated net investment gains earned on permanently restricted net assets are included within unrestricted net assets. In accordance with New York State law, the appropriation and spending of such gains, absent donor directives, is subject to a standard of prudence, as more fully discussed under the accounting policy note on investments, note 1(i).

- The Board of Trustees, through voluntary resolutions, has set aside portions of the University's unrestricted net assets to function as endowment, for property, plant and equipment purposes and for other specific operating purposes.

Revenues from sources other than contributions are generally reported as increases in unrestricted net assets. Contributions are reported as increases in the appropriate category of net assets, except those contributions whose imposed restrictions are met in the same fiscal year they are received are included in unrestricted revenues.

Investment income and gains and losses on investments are reported as increases or decreases in the unrestricted net assets unless their use is restricted by explicit donor stipulations or by law. When such restrictions exist, investment income, gains or losses are reported as temporarily or permanently restricted, except when the restrictions are met in the same fiscal year in which the income or gains are earned, in which case the income and gains are reported within the unrestricted category.

Expenses are reported as decreases in unrestricted net assets. Expiration of temporary restrictions recognized on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) that do not occur within the same period as revenue recognition are reported as reclassifications from temporarily restricted net assets to unrestricted net assets. Temporary restrictions on gifts to acquire long-lived assets are considered met in the period in which the assets are acquired or placed in service.

(d) Income Taxes

The University is a not-for-profit organization as described in section 501(c)(3) of the Internal Revenue Code and is generally exempt from income taxes on related income pursuant to Section 501(a) of the Code.

(e) Operations

The statements of activities present the changes in net assets of the University from operating activities and from nonoperating activities. Operating revenues and expenses relate primarily to educational and training programs, research activities and hospital and patient care activities provided by the University and its related entities. Utilization of investment income and gains on long-term investments held for endowment and similar purposes under the University's total return spending policy, as discussed in note 1(i), is considered operating revenue.

Nonoperating activities consist primarily of investment income and appreciation from long-term investments in excess of amounts utilized for operations.

(f) Cash Equivalents and Operating Investments

Cash equivalents include amounts on deposit with financial institutions, short-term investments with maturities of three months or less at the time of purchase and other highly liquid investments, primarily cash management funds.

Operating investments include all other current investments with original maturities greater than three months. These current investments include obligations of the US Treasury, US Government and other government agencies and corporate & foreign bonds. These items are reported at fair value.

(g) Inventories

Inventories, primarily medical supplies, are valued at the lower of cost, which is determined by the first-in, first-out method, or market.

(h) Contributions

Contributions, including unconditional promises, or pledges, are recognized as revenues in the period received. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value at the date of gift. Contributions to be received after one year are discounted, at a range of 2% to 6%, to their present value. Amortization of the discount is recorded as additional contribution revenue and used in accordance with donor-imposed restrictions, if any, on the contributions. Allowance is made for uncollectible contributions based upon management's judgement and analysis of the creditworthiness of the donors, past collection experience and other relevant factors.

(i) Investments

The University's investments are comprised of the assets of the University's endowment and other investments held for general operating purposes. The University reports those investments at their fair value. The fair value of debt and equity securities is based on quoted market prices of public securities markets. Fair value for certain venture investments is based on transactions involving similar issues or on quoted prices of registered securities, although the University's holdings are restricted with respect to disposition in the ordinary manner.

New York State law generally allows the spending of income and gains on investments of permanently restricted net assets, absent explicit donor stipulations that all or a portion of such gains be maintained in perpetuity. State law allows the University to appropriate and spend such income and gains as is prudent, considering such factors as the University's long- and short-term needs, present and anticipated financial requirements, expected total return on investments, price level trends and general economic conditions.

In accordance with accounting requirements, realized and unrealized gains and losses, as well as gains and losses on temporarily restricted and unrestricted net assets, are reported as temporarily restricted or unrestricted, based upon the presence or absence of donor stipulations as to their use. The University's policy regarding spending of gains thus classified, however, is to spend no more than a stated percentage of market value of its investment portfolio over time, as described in the following paragraph.

Investment of the University's net assets held for endowment and similar purposes is based upon a total return policy, and the utilization of its endowment resources for current operating and capital needs is related to this policy. Accordingly, during 2004 and 2003, University Trustees authorized the use of total return (income and appreciation) from its endowment resources at a rate of 6.5% and 6.4%, respectively, of the average market value of its consolidated investment portfolio for the most recent five years. To the extent that the total return requirement for the current year is not fulfilled by interest, dividends and royalties, the University utilizes the appreciation of its endowment and similar net assets for operating purposes. To the extent that the total return requirement for the current year is exceeded by interest, dividends and royalties, the University reinvests the excess in its net assets held for endowment and similar purposes.

Investment securities are exposed to various risks, such as interest rates, market, economic conditions, world affairs and credit risks. Due to the level of risk associated with certain investment securities, it is possible that changes in their value could occur in the near term and such changes could materially affect the amounts reported in the investments and investment activity of the University.

(j) Property, Plant and Equipment

Property, plant and equipment are stated at cost or at estimated fair value if acquired by gift, less accumulated depreciation and amortization. Buildings used for research activities are componentized as site improvements, buildings, building services and fixed equipment. Depreciation of the building components is calculated using the straight-line method over the useful lives of the components ranging from five to fifty years. Depreciation of non-research buildings, equipment and library books and amortization of leasehold and land improvements are computed using the straight-line method over the estimated useful lives of the assets. Land and museum collections are not subject to depreciation. Estimated useful lives for non-research assets are as follows:

	Years
Building	40
Building and leasehold improvements	20
Land improvements	20
Equipment	4 to 15
Library books	10

The University reports gifts of property, plant and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the University reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

(k) Collections

The University capitalizes its collections. If purchased, collection items are capitalized at cost, and if donated at their appraised or fair value on the accession date (the date on which the item is accepted by the Board of Trustees). There is no depreciation recorded on collection items.

(l) Split Interest Agreements and Perpetual Trusts

The University's split interest agreements with donors consist primarily of gift annuities, unitrusts, lead trusts, charitable remainder annuity trusts and life income agreements. Assets held under these agreements are included in investments. Generally, contribution revenues are recognized at the dates the agreements are established after recording liabilities for the present value of the estimated future payments to be made to the beneficiaries. The liabilities are adjusted during the term of the trusts for changes in the value of the assets, accretion of the discount and other changes in the estimates of future benefits. The University is also the beneficiary of certain perpetual trusts held and administered by others. The present values of the estimated future cash receipts, which are measured by the fair value of the assets contributed to the trust, are recognized as assets and contribution revenues at the dates the trusts are established. Distributions from the trusts are recorded as contributions and the carrying value of the assets is adjusted for changes in the fair value of the trust assets.

(m) Refundable U.S. Government Grants for Student Loans

Funds provided by the United States Government under the Federal Perkins, Nursing and Health Professions Student Loan programs are loaned to qualified students and may be reloaned after cash collections. These funds are ultimately refundable to the government and are recognized as a liability in the accompanying consolidated balance sheets.

(n) Grants and Contracts

Revenue from grants and contracts, primarily for research and training programs, is generally recognized as earned, that is, as the related costs are incurred under the grant or contract agreements. Amounts received in advance are reported as advance receipt of sponsored research revenues.

Grants and contracts awarded to the University are subject to audit by the various sponsoring agencies. Indirect costs recovered on grants and contracts are recorded at rates established by the University with the Federal Government, or predetermined by the non-Federal sponsor. Indirect cost rates for government grants and contracts are subject to audit, and subsequent final settlements are recorded as current period adjustments. Management believes the impact of any future settlements to be immaterial to the consolidated financial statements.

(o) Benefits Plans

The University provides certain health care and life insurance benefits to retired employees and spouses under a defined benefit plan. Benefits include basic medical and major medical coverage. Certain categories of retirees receive dental coverage and group life insurance. Such post-retirement benefits are accounted for as a form of deferred compensation over the estimated service lives of employees.

Post-employment benefits include benefits provided to former or inactive employees after employment but before retirement. For the University, such benefits include workers' compensation benefits, short-term disability benefits and benefits provided under various other programs.

(p) Patient Service Revenues

Patient service revenues for the hospitals are recorded at established rates, with provisions for third-party contractual adjustments to arrive at net patient service revenue. Estimated contractual adjustments, including prospective rate adjustments arising under third-party reimbursement programs, are accrued in the period the services are rendered to the patients. Differences between estimated retroactive third-party reimbursement settlements for prior years and subsequent final settlements are recorded in the year of settlement as contractual adjustments. Estimated settlements at June 30, 2004 have been accrued for services provided during the years ended June 30, 1999 through 2004. Final settlements have been made for all years prior to 1999.

Patient service revenues for the faculty practice are recorded at the established physician fee schedules with provisions for third-party contractual adjustments deducted to arrive at net patient service revenue. Estimated contractual adjustments are accrued in the period the services are rendered to the patients. Estimates are based on historical and current gross collection ratios.

(q) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and judgements that affect the reported amounts of assets and liabilities and disclosures of contingencies at the date of the financial statements and revenues and expenses recognized during the reporting period. Actual results could differ from those estimates.

(r) Investment in Net Assets of Foundation

The University follows the provisions of Statement of Financial Accounting Standards (SFAS) No. 136, *Transfers of Assets to a Not-for-Profit Organization or Charitable Trust That Raises or Holds Contributions for Others* in accounting for its interest in the net assets of the James P. Wilmot Foundation, Inc. ("Foundation"). SFAS No. 136 establishes standards for transactions in which a donor transfers assets to a not-for-profit organization or charitable trust, which then agrees to transfer those assets, the return on investment of those assets, or both to a beneficiary specified by the donor. Under the provisions of SFAS No. 136, the University is required to recognize the net assets and its share of the change in the net assets of the Foundation. The Foundation was established for the support of cancer research at the University's School of Medicine and Dentistry.

(s) Derivative Instruments and Hedging Activities

Derivative instruments related to the University's long-term debt are included in accounts payable and accrued expenses on the consolidated balance sheet. The change in the fair value of the derivative instruments is also included in the net appreciation in the statement of activities. The University selected the combination of a variable rate bond issue and a thirty year interest rate swap agreement to obtain fixed rate financing at the lowest available cost at the time of the transaction. The University is exposed to credit loss in the event of nonperformance by the counterparty to its long term rate swap. The interest rate swap does not qualify for cash flow hedge accounting.

(2) Net Assets

Unrestricted net assets consist of the following at June 30:

	2004	2003
Designated:		
For long-term purposes to support scholarships and other programs:		
Funds functioning as endowment	$ 732,285	$ 663,191
Accumulated appreciation resulting from investment of permanently restricted net assets	201,697	171,909
For property, plant and equipment purposes and debt service reserves held by trustees under debt agreements	23,058	22,701
For student loan programs, including required matching funds under Federal Government loan programs	3,693	3,870
For other specific operating purposes	46,476	46,045
For Highland Hospital and affiliates	51,641	48,992
For Eastman Dental Center Foundation	42,531	40,130
For other related entities	(17,531)	(16,011)
Total designated	1,083,850	980,827
Net investment in property, plant and equipment	437,919	421,532
Undesignated	65,407	82,916
Total unrestricted net assets	$ 1,587,176	$ 1,485,275

Temporarily restricted net assets consist of the following at June 30:

	2004	2003
Accumulated appreciation on permanently restricted net assets subject to purpose restrictions:		
Scholarships and grants	$ 21,858	$ 19,176
Instruction	59,926	49,672
Other	23,601	19,360
Subtotal	105,385	88,208
Interest in net assets of foundation	16,920	15,572
Related entities	2,499	1,475
Other gifts and income subject to:		
Purpose restrictions	20,369	21,956
Time restrictions:		
Contributions receivable	36,576	34,835
Split-interest agreements	25,698	23,053
Total temporarily restricted net assets	$ 207,447	$ 185,099

Permanently restricted net assets consist of the following at June 30:

	2004	2003
Perpetual endowment funds:		
Restricted income purposes:		
Scholarships and grants	$ 11,802	$ 12,148
Instruction	38,873	36,258
Other	14,973	12,996
Unrestricted income purposes	109,675	103,466
Subtotal	175,323	164,868
Interests in perpetual trusts held by others:		
Restricted income purposes:		
Instruction	33,575	30,404
Student loans	1,420	1,395
Unrestricted income purposes	14,005	11,359
Subtotal	49,000	43,158
Related entities	3,001	2,943
Split-interest agreements	763	1,132
Perpetual loan funds	3,961	3,866
Contributions receivable	4,346	2,775
Total permanently restricted net assets	$ 236,394	$ 218,742

(3) Accounts Receivable

Accounts receivable at June 30 consist of the following:

	2004	2003
Patient care and related activities, net of allowances for doubtful accounts of $16,052 and $16,005	$ 145,030	$ 132,103
Federal, state and local governments, foundations and companies, net of allowances for doubtful accounts of $400 and $630	35,711	29,495
Student receivables, net of allowances for doubtful accounts of $1,839 and $1,744	8,462	8,971
Other	35,286	36,300
Total accounts receivable	$ 224,489	$ 206,869

(4) Contributions

Contributions receivable, net, are summarized as follows at June 30:

	2004	2003
Unconditional promises expected to be collected in:		
Less than one year	$ 26,202	$ 19,051
One year to five years	18,977	23,091
Over five years	1,203	1,440
Subtotal	46,382	43,582
Less unamortized discount and allowance for uncollectible amounts	(5,460)	(5,972)
Total contributions receivable, net	$ 40,922	$ 37,610

At June 30, 2004, the University had also received bequest intentions of $23,758 and certain other conditional promises to give. These intentions and conditional promises to give are not recognized as assets. If they are received, they will generally be restricted for specific purposes stipulated by the donor, primarily endowments for faculty support, scholarships or general operating support of a particular department or division of the University.

The University expended $17,832 and $18,266, for University relations and development for the years ended June 30, 2004 and 2003, respectively.

(5) Notes Receivable

Student loans receivable at June 30, 2004 and 2003 respectively are reported net of allowances for doubtful loans of $1,377 and 1,040 respectively. The allowance is intended to provide for loans, both in repayment status and not yet in repayment status (borrowers are still in school or in the grace period following graduation), that may not be collected.

(6) Investments Held for Long-Term Purposes

Investments were held for the following long-term purposes at June 30:

	2004	2003
Endowment and similar purposes	$ 1,287,173	$ 1,147,299
Property, plant and equipment purposes:		
Debt service reserve held by trustees under debt agreements	14,175	13,416
Other	42,957	12,864
Total property, plant and equipment purposes	57,132	26,280
Other purposes	84,735	101,378
Total investments held for long-term purposes	$ 1,429,040	$ 1,274,957

Investments held for long-term purposes consist of the following at June 30:

	2004	2003
Cash and cash equivalents	$ 94,016	$ 128,707
Debt securities	188,475	143,784
Common and preferred stocks	695,616	540,012
Limited partnerships and similar interests	395,516	392,437
Oil royalties	11,700	8,200
Other investments	43,717	61,817
Total market value	$ 1,429,040	$ 1,274,957

Included in the investments held for long-term purposes above are $261,313 and $195,089 of international investments at June 30, 2004 and 2003, respectively.

Under the terms of certain limited partnership agreements, the University is obligated to periodically advance additional funding for private-equity and real estate investments. At June 30, 2004 and 2003, respectively, the University had commitments of $132,383 and $83,990 for which capital calls had not been exercised. Such commitments generally have fixed expiration dates or other termination clauses. The University maintains sufficient liquidity in its investment portfolio to cover such calls.

For investment purposes, substantially all investments held for endowment and similar purposes participate in one of several pools, each with its own investment policy and objectives. The investment pool assets are owned by the separate funds based on shares purchased by each fund and fund addition when it entered the pool. The pooled assets are valued on a monthly basis and a "market value per share" is determined and used to calculate the number of shares applicable to funds entering or leaving the pool.

The following table summarizes changes in relationships between cost and market values of investments held for endowment and similar purposes:

	2004		
	Market	**Cost**	**Net Gains**
End of year	$ 1,287,173	$ 1,077,281	$ 209,892
Beginning of year	$ 1,147,299	$ 1,056,672	90,627
Unrealized appreciation			119,265
Realized net gains for year			36,830
Net increase for year			$ 156,095

	2003		
	Market	**Cost**	**Net Gains**
End of year	$ 1,147,299	$ 1,056,672	$ 90,627
Beginning of year	$ 1,132,014	$ 1,044,269	87,745
Unrealized appreciation			2,882
Realized net gains for year			42,587
Net increase for year			$ 45,469

The University permits several of its investment managers to utilize forward contracts, currency options and futures with the specific authorization of the investment committee of the Board of Trustees. These financial instruments involve, to varying degrees, elements of market risk in excess of the amounts recorded in the consolidated financial statements.

Interest rate futures contracts are held as hedges against changes in market value of fixed income securities due to market interest rate fluctuations. The University is subject to market risk associated with the changes in the value of these futures contracts. The University held long and short-term U.S. Treasury and municipal bond futures contracts at June 30, 2004 and 2003, at a notational amount of $1,413 and $3,053, respectively. These amounts, however, may differ from the University's future cash requirements as the University may close out futures positions prior to settlement and thus be subject only to the change in value of the futures contracts since the contracts are valued daily using the mark-to-market method. The margin requirements on deposits with a third party for futures contracts were $368 at June 30, 2004 and $301 at June 30, 2003.

Management does not anticipate that losses, if any, resulting from its market or credit risks would materially affect the consolidated financial position of the University.

Investment fees for the two years ended June 30, 2004 and 2003 were $12,478 and $11,533, respectively.

(7) Property, Plant and Equipment

As of June 30, 2004 and 2003, the University's investment in property, plant and equipment is as follows:

	2004	2003
Buildings and improvements	$ 1,171,896	$ 1,146,840
Land improvements	27,586	27,319
Completed projects under leasehold agreements	46,202	46,600
Equipment owned	543,448	516,819
Library books	89,581	83,554
Subtotal	1,878,713	1,821,132
Less accumulated depreciation	1,045,020	979,111
Subtotal	833,693	842,021
Land	5,177	5,177
Museum collections	25,717	25,231
Construction in progress	69,834	23,725
Total property, plant and equipment, net	$ 934,421	$ 896,154

(8) Long-Term Debt

The following is a summary of the University's long-term indebtedness at June 30, 2004 and 2003:

	2004	2003
Obligations under capital leases, 0% to 9.164%, (a)	$ 11,366	$ 6,006
Urban Development Corporation loan, (b)	2,833	3,000
Term note payable, LIBOR rate plus 0.40%, (c)	4,400	6,150
Term note payable, LIBOR rate plus 1.25% (d)	-	592
Term note payable, LIBOR rate plus 0.75% (e)	1,288	1,632
Line of credit, LIBOR rate plus 0.20% (f)	-	7,812
Settlement note payable, 6.00% (g)	219	-
Direct Note Obligation, Series 2003, 5.40% to 5.75% (net of unamortized discount of $33 in 2004), (h)	8,567	-
Bonds Payable – COMIDA, 10.00% (i)	698	-
Bonds payable – DASNY Series 1987, 3.60% to 6.50%, (j)	-	1,620
Bonds payable – DASNY Series 1993A, 2.50% to 5.30% (net of unamortized discount of $40 in 2003), (k)	-	8,855
Bonds payable – DASNY Series 1994, 3.90% to 5.90% (net of unamortized discount of $1,468 in 2003), (l)	-	76,452
Bonds payable – DASNY Series 1994A, 4.50% to 6.50% (net of unamortized discount of $18 in 2004 and $20 in 2003), (m)	2,322	3,390
Bonds payable – DASNY Series 1994, 7.625%, (n)	9,303	9,469
Bonds payable – DASNY Series 1994B, 5.50% (o)	11,745	12,030
Bonds payable – DASNY Series 1996, 3.85% to 5.30% (net of unamortized discount of $11 in 2004 and $16 in 2003), (p)	5,119	7,489
Bonds payable – DASNY Series 1997A, 3.75% to 5.00% (net of unamortized premium of $810 in 2004 and $845 in 2003), (q)	46,845	54,600
Bonds payable – DASNY Series 1997A and B, 5.70% to 8.25%, (r)	27,320	28,195
Bonds payable – DASNY Series 1998A, 3.50% to 5.00% (net of unamortized discount of $291 in 2004 and $304 in 2003), (s)	108,569	113,171
Bonds payable – DASNY Series 1999A, 5.00% (net of unamortized discount of $136 in 2004 and $147 in 2003), (t)	17,329	17,318
Bonds payable – DASNY Series 1999B, 3.70% to 5.72% (net of unamortized discount of $247 in 2004 and $259 in 2003), (u)	22,714	23,356
Bonds payable – DASNY Series 2000A, 4.50% to 6.05% (net of unamortized discount of $1 in 2003), (v)	39,139	40,699
Bonds payable – DASNY Series 2001A, 2.90% to 5.00% (net of unamortized discount of $126 in 2004 and $134 in 2003), (w)	22,089	22,261
Bonds payable – DASNY Series 2003 A, B and C, 3.97%, (x)	162,375	-
Total long-term debt	$ 504,240	$ 444,097

The following is a description of the University's long term debt.

(a) Obligations Under Capital Leases

Strong Memorial Hospital entered into a tax-exempt capital equipment lease program in October 2000 for $4,719. The lease is being repaid with quarterly payments of $208, including interest at 5.50% through May 2007. The leased equipment includes CT Radio Surgery, Ultrasound and linear accelerator equipment.

In 1986, the University entered into a lease on a facility used partly to house activities of its Eastman School of Music. During 1992, the University exercised an option to acquire the interests of its lessor in that facility. As part of the exercise of its option, the University has assumed mortgages amounting to $796, bearing interest at 4.75% and payable in monthly installments through December 2011. In October 2003, the University refinanced these mortgages by drawing on a line of credit with JPMorgan Chase Bank. During fiscal 2004, proceeds from the sale of the University's Direct Note Obligations, Series 2003 were in turn used to refinance the amount drawn on the line of credit.

In addition to the arrangements discussed above, the University and its related entities have entered into several other capital leases for equipment.

(b) Urban Development Corporation Loan

In March 1992, the New York State Urban Development Corporation (UDC) entered into an agreement with the University to partially fund the construction of the University's Center for Optoelectronics and Imaging (COI) with a loan of $5,000. The agreement requires the University to pay an amount equal to the debt service on the $6,320 tax-exempt bond issued by which UDC financed the loan and the associated reserve funds and costs of issuance. The loan is secured by a mortgage on the property.

Pursuant to an agreement authorized by statute, the State of New York leases the COI from the University for the 30-year term of the loan, paying, as rent, an amount sufficient to cover the University's obligations to UDC. These rents have been assigned to UDC as further security for the loan. The University retains possession of the property under a sub-lease from the State at an annual rent equivalent to one-thirtieth of the sum of the loan principal and the cost of issuance of the UDC bonds.

(c) Term Note Payable – JPMorgan Chase Bank

Pursuant to an agreement between the University and JPMorgan Chase Bank dated June 30, 2000, JPMorgan Chase Bank issued a term note of $7,000 to finance the renovation of the Goergen Athletic Center. The note is being repaid at an interest rate of LIBOR plus 0.40% on the unpaid principal balance through September 2005.

(d) Term Note Payable – HSBC Bank, USA

A University related entity entered into a $1,939 term note agreement with HSBC Bank, USA. The note was being repaid with monthly payments of $54, including interest at the bank's prime rate of LIBOR plus 1.25% through May 2004. This note was guaranteed by the University through June 1, 2004 and was collateralized by the assets of the related entity.

(e) Term Note Payable – HSBC Bank, USA

A University related entity entered into a $1,718 term note agreement with HSBC Bank, USA. The note is currently being repaid at an interest rate of LIBOR plus 0.75% on the unpaid balance through January 2008. This note is guaranteed by the University and is collateralized by the assets of the related entity.

(f) Line of Credit – JPMorgan Chase Bank

Pursuant to an agreement between the University and JPMorgan Chase Bank dated June 2, 2003, the University drew on its available revolving line of credit, in the amount of $7,812 to refinance the COMIDA lease related to Eastman Place. The rate of interest on the line was the bank's prime rate of LIBOR plus 0.20%. During fiscal 2004, proceeds from the sale of the University's Direct Note Obligations, Series 2003, were in turn used to refinance the amount drawn on the line of credit.

(g) Settlement Note Payable – Siemens

A University related entity entered into a settlement agreement with Siemens Medical Solutions Health Services Corporation regarding amounts due for maintenance that relate to the years 2000 through 2002. As part of the settlement, arrangements were made to repay the remaining amount owed, $300, over 18 months, commencing in February 2004 through July 2005, at an interest rate of 6.00%.

(h) Direct Note Obligation – The Bank of New York

Pursuant to an agreement between the University and the Bank of New York dated November 25, 2003, the Bank of New York issued $8,600 of notes known as the University of Rochester Direct Note Obligations, Series 2003. The Series 2003 notes were issued to refinance drawings under the University's revolving line of credit with JPMorgan Chase Bank. The line of credit had been used to refinance indebtedness and certain other mortgages related to Eastman Place. Eastman Place is a facility used partly to house activities of the Eastman School of Music.

The Series 2003 notes are general, unsecured obligations of the University.

(i) Bond Payable – COMIDA

Pursuant to an agreement between the University and the County of Monroe Industrial Development Agency (COMIDA) dated January 6, 2004, COMIDA issued a replacement bond in the amount of $698. The 2004 COMIDA Replacement bond is for the purchase of property at 10 Gibbs Street, Rochester, New York and will become part of the Eastman School of Music campus.

(j) Bonds Payable – Dormitory Authority of the State of New York (DASNY) Series 1987

Pursuant to an agreement between the University and DASNY dated April 1, 1987, DASNY issued and sold $150,000 of bonds known as University of Rochester, Series 1987. The Series 1987 bonds were issued to refund outstanding DASNY Revenue Bonds; to fund the Debt Service Reserve Fund in an amount equal to its requirement; and to pay certain costs of issuance of the Series 1987 bonds.

During fiscal 1998, $65,930 of the Series 1987 bonds were refunded as a result of the issuance of the Series 1997A bonds. Another $20,655 of the Series 1987 bonds were refunded during fiscal 1999 as a result of the issuance of the Series 1998A bonds. During fiscal 2004, the remaining outstanding Series 1987 bonds, totaling $1,620, were refinanced as a result of the issuance of the Series 2003A bonds.

(k) Bonds Payable – DASNY Series 1993A

Pursuant to an agreement between the University and DASNY dated April 1, 1993, DASNY issued and sold $21,245 of bonds to finance various physical plant projects and equipment related to Strong Memorial Hospital. The bonds were issued at a discount of $84, resulting in net proceeds to the University of $21,161. The bonds are a general obligation of the University and require the University to pay principal, sinking fund installments and interest on all bonds issued as such payments become due.

During fiscal 2004, the outstanding Series 1993A bonds, totaling $8,895, were refinanced with proceeds from the sale of the Series 2003B bonds.

(l) Bonds Payable – DASNY Series 1994

Pursuant to an agreement between the University and DASNY dated March 1, 1994, DASNY issued and sold $94,985 of bonds known as University of Rochester, Strong Memorial Hospital Revenue Bonds, Series 1994. The Series 1994 bonds were issued at a discount of $2,229, resulting in proceeds of $92,756 to finance the construction of an ambulatory care facility, access center and parking garage for the Hospital and the renovation of the Hospital's obstetrical unit. The bonds are a general obligation of the University and require the University to pay principal, sinking fund installments and interest on all bonds issued as such payments become due.

During fiscal 2004, the outstanding Series 1994 bonds, totaling $77,920, were refinanced with proceeds from the sale of Series 2003B bonds and Series 2003C bonds.

(m) Bonds Payable – DASNY Series 1994A

Pursuant to an agreement between the University and DASNY dated October 1, 1994, DASNY issued and sold $30,575 of bonds known as University of Rochester Revenue Bonds, Series 1994A. The Series 1994A bonds were issued at a net discount of $30, resulting in proceeds of $30,545 to finance the renovation of a dormitory, two academic buildings and an administration building on the University's River Campus; the repair and improvement of the exterior and utility infrastructure of the buildings of the Eastman School of Music and the refinancing of the University's maturing $20,000 repurchase agreement with the Student Loan Marketing Association (SLMA). The bonds are a general obligation of the University and require the University to pay principal, sinking fund installments and interest on all bonds issued as such payments become due. During fiscal 2002, the Series 1994A bonds maturing on and after July 1, 2007 were refinanced as a result of the issuance of Series 2001A. The bondholders were paid on July 1, 2004.

The obligation of the University is secured by a pledge of certain revenues of the University. These pledged revenues include all tuition, room and board and mandatory fees charged to students. The pledged revenues are subordinate to the prior pledges securing certain other outstanding indebtedness of the University.

(n) Bonds Payable – DASNY Series 1994

Pursuant to an agreement with a University related entity (Highland Hospital and affiliates) and DASNY dated July 1, 1994, DASNY issued and sold $11,790 of FHA-Insured Mortgage Revenue Bonds, Series 1994. The related entity is repaying the bonds that are due December 1, 2025 at a fixed rate of 7.625%. The Series 1994 bonds are collateralized by buildings.

(o) Bonds Payable – DASNY Series 1994B

Pursuant to an agreement with a University related entity (Highland Hospital and affiliates) and DASNY, $13,000 of Series 1994B Revenue Bonds were issued and sold by DASNY. The related entity is repaying the indebtedness at a fixed rate of 5.50%, maturing July 1, 2023. The bond issue is secured by an irrevocable direct pay letter that is held by the trustee, JPMorgan Chase Bank. The Series 1994B Revenue Bonds are secured by a parity mortgage and a security interest in certain buildings and equipment.

(p) Bonds Payable – DASNY Series 1996

Pursuant to an agreement between the University and DASNY dated July 1, 1996, DASNY issued and sold $21,375 of bonds known as University of Rochester, Strong Memorial Hospital Revenue Bonds, Series 1996. The Series 1996 bonds were issued at a discount of $54, resulting in proceeds of $21,321 to finance (1) the implementation of an automated clinical information system; (2) the expansion and renovation of the Hospital's basement area to enlarge and consolidate the pre and post anesthesia units and (3) the purchase and installation of a nuclear cardiology gamma camera at the Hospital's ambulatory care facility.

The bonds are a general obligation of the University and require the University to pay principal, sinking fund installments and interest on all bonds issued as such payments become due. As security for its obligation under the agreement, the University has granted to the Authority a security interest in pledged revenues consisting of any moneys, income rents, or revenues received or receivable by the Hospital.

(q) Bonds Payable – DASNY Series 1997A

Pursuant to an agreement between the University and DASNY dated November 7, 1997, DASNY issued and sold $78,280 of bonds known as University of Rochester Revenue Bonds, Series 1997A. The Series 1997A bonds were issued at a premium of $1,041 resulting in proceeds of $79,321 to finance (1) interior and exterior building renewal for major buildings at the Eastman School of Music as part of a multi-year project; (2) installation of a local area network for all River Campus and Eastman School of Music residence halls to provide high speed data access to undergraduate students; (3) reconstruction of an existing pedestrian bridge connecting Hill Court Residence Complex with the River Campus and (4) major renewal and replacement projects for various buildings, structures, roadways and other facilities on the River Campus, on Mt. Hope Avenue and at the Mees Observatory in South Bristol, New York as part of a multi-year project. Series 1997A also refunded a portion of the University of Rochester Revenue Bonds, Series 1987.

The bonds are secured by the pledge and assignment of certain revenues of the University. These pledged revenues include all tuition, room and board and mandatory fees charged to students. The pledged revenues are subordinate to the prior pledges securing outstanding indebtedness of the University.

(r) Bonds Payable – DASNY Series 1997 A and B

Pursuant to an agreement with a University related entity (Highland Hospital and affiliates) and DASNY dated December 11, 1997, DASNY issued and sold $26,635 of the Series 1997A tax-exempt FHA-Insured Mortgage Hospital Revenue Bonds and $5,250 of Series 1997B taxable FHA-Insured Mortgage Hospital Revenue Bonds.

The Series 1997A and B bonds were issued at par value. The proceeds of these bond issues were used to finance (1) the expansion and modernization of selected clinical and support areas of the Highland Hospital; (2) the construction of the main parking garage and (3) to refinance the Marine Midland Bank, N.A. construction mortgage note payable. The bonds are secured by a pledge of collateral for letters of credit and cash.

(s) Bonds Payable – DASNY Series 1998A

Pursuant to an agreement between the University and DASNY dated March 18, 1998, DASNY issued and sold $131,615 of bonds known as University of Rochester Revenue Bonds, Series 1998A. The Series 1998A bonds were issued at a discount of $370 resulting in proceeds of $131,245 to finance (1) design and construction of a new biomedical research facility of approximately 240,000 square feet; (2) construction of a new entrance to the School of Medicine and Dentistry of approximately 55,000 square feet; (3) renovations for laboratory space of approximately 65,000 square feet; (4) the acquisition of scientific equipment and furnishings for the new facility and renovated laboratory space; (5) the University-wide telecommunications system and (6) replacement of the chiller at the central utilities plant. Series 1998A also refunded a portion of the University of Rochester Revenue Bonds, Series 1987.

The bonds are secured by the pledge and assignment of certain revenues of the University. These pledged revenues include all tuition, room and board and mandatory fees charged to students. The pledged revenues are subordinate to the prior pledges securing certain other outstanding indebtedness of the University.

(t) Bonds Payable – DASNY Series 1999A

Pursuant to an agreement between the University and DASNY dated August 15, 1999, DASNY issued and sold $17,465 of bonds known as University of Rochester Revenue Bonds, Series 1999A. The Series 1999A bonds were issued at a discount of $190 resulting in proceeds of $17,275 to finance (1) the implementation of a new Human Resource information system to serve payroll and personnel functions University wide; (2) renovations of existing space for various uses in the School of Medicine and Dentistry and (3) various projects throughout the University designed to improve the accessibility of facilities and to accomplish deferred maintenance items. The Loan Agreement and the obligation of the University to make payments under the Loan Agreement are general obligations of the University.

No security interest in any revenues or assets of the University has been granted by the University to the Authority under the Loan Agreement.

(u) Bonds Payable – DASNY Series 1999B

Pursuant to an agreement between the University and DASNY dated August 15, 1999, DASNY issued and sold $25,860 of bonds known as the University of Rochester, Strong Memorial Hospital Revenue Bonds, Series 1999B. The Series 1999B bonds were issued at a discount of $306 resulting in proceeds of $25,554 to finance (1) the design and construction of a new emergency room at the Hospital; (2) relocation and expansion of the cardiac catheterization laboratory and (3) expansion of existing space for the Hospital clinical laboratories.

The Loan Agreement and the obligation of the University to make payments under the Loan Agreement are general obligations of the University. No security interest in any revenues or assets of the University has been granted by the University to the Authority under the Loan Agreement.

(v) Bonds Payable – DASNY Series 2000A

Pursuant to an agreement between the University and DASNY dated June 1, 2000, DASNY issued and sold $45,764 of bonds known as the University of Rochester Revenue Bonds, Series 2000A. The Series 2000A bonds were issued at a discount of $2 resulting in proceeds of $45,762 to finance (1) the construction of an addition to the Medical Research Building to expand research space for core programs in the School of Medicine and Dentistry; (2) the renovation of faculty office space and the expansion of instructional facilities of the William E. Simon Graduate School of Business Administration; (3) the upgrading of chilled water supply infrastructure; (4) improvements to faculty office and laboratory space at the University's River Campus and (5) infrastructure repairs at the Eastman School of Music and other facility improvements on the River Campus including the continuation of general deferred maintenance items. Series 2000A also refinanced a portion of the University of Rochester Revenue Bond, Series 1972C.

The Loan Agreement and the obligation of the University to make payments under the Loan Agreement are general obligations of the University. No security interest in any revenues or assets of the University has been granted by the University to the Authority under the Loan Agreement.

(w) Bonds Payable – DASNY Series 2001A

Pursuant to an agreement between the University and DASNY dated July 10, 2001, DASNY issued and sold $22,920 of bonds known as the University of Rochester Revenue Bonds, Series 2001A. The Series 2001A bonds were issued at a discount of $152 resulting in net proceeds of $22,768 to refinance (1) all the outstanding $184 University's Dormitory (Apartment) bonds of 1962, HUD Series D and all the outstanding $840 University's Dormitory (Apartment) bonds of 1966, HUD Series E and (2) a portion of the University of Rochester Revenue Bond, Series 1994A, maturing on and after July 1, 2007. HUD Series D and E were paid on October 1, 2001. DASNY Series 1994A bondholders were paid on July 1, 2004 in the amount of $19,640.

The Loan Agreement and the obligation of the University to make payments under the Loan Agreement are general obligations of the University. No security interest in any revenues or assets of the University has been granted by the University to the Authority under the Loan Agreement.

(x) Bonds Payable – DASNY Series 2003 A, B and C

Pursuant to an agreement with the University and DASNY dated October 29, 2003, DASNY issued and sold $164,425 of Series 2003 bonds, consisting of $32,550 Series 2003A bonds, $49,650 Series 2003B bonds and $82,225 Series 2003C bonds.

Series 2003A bonds were issued to finance (1) an expansion of the Laboratory for Laser Energetics building to accommodate the construction of a federally funded laser expansion; (2) renovation of space to house a functional MRI; (3) deferred maintenance remediation in various buildings and (4) renovation and information technology upgrades in various faculty offices, laboratory space and student residential buildings. A portion of the proceeds from Series 2003A also refinanced the remaining portion of the University of Rochester Revenue Bonds, Series 1987, which was paid to bondholders on December 10, 2003.

Series 2003B bonds were issued to finance (1) equipment acquisitions for the Hospital; (2) the expansion of an existing garage and (3) laboratory relocations at the Hospital. Series 2003B bonds also refinanced University of Rochester Series 1993A bonds, which was paid to bondholders on December 10, 2003 and a portion of the University of Rochester Series 1994 bonds, in the amount of $22,145, which was paid to bondholders on July 1, 2004.

Series 2003C bonds were issued to finance (1) construction of an Adult Intensive Care Unit; (2) renovations of the Cancer Center and (3) deferred maintenance, renovations and improvements to faculty offices, laboratory and clinical spaces for various departments and areas within the Hospital and School of Medicine and Dentistry. Series 2003C also refinanced a portion of the University of Rochester Series 1994 bonds, in the amount of $53,155, which was paid to bondholders on July 1, 2004.

On July 31, 2003, the University executed $164,425 of interest rate swaps with third parties. The University entered into the interest rate swap agreement to exchange variable rate debt for a fixed rate obligation without the exchange of the underlying principal amount. Under this agreement the counter party pays the University a variable interest rate equal to 61.5% of one-month LIBOR plus 56 basis points. The University will pay the counter party a fixed interest rate of 3.97%. Net payments or receipts under the swap agreements are recorded as an adjustment to interest expense. As of June 30, 2004, the fair value of the interest rate swap was a liability of $2,779, and was included in accounts payable and accrued expenses on the consolidated balance sheet. The contractual relationship under this agreement will last until July 1, 2033.

The Loan Agreement and the obligation of the University to make payments under the Loan Agreement are general obligations of the University.

(y) Required Principal Payments

Required composite principal payments for long-term debt, net of unamortized discount, for each of the years in the five-year period ending June 30, 2009 and thereafter are as follows:

Maturity		Principal portions of lease payments		Principal payments of debt		Total principal payments
2005	$	3,518	$	27,191	$	30,709
2006		3,075		28,037		31,112
2007		2,477		23,046		25,523
2008		1,698		23,281		24,979
2009		598		23,654		24,252
Thereafter		-		367,665		367,665
Total	$	11,366	$	492,874	$	504,240

The University expended $23,811 and $24,455 for interest for the years ended June 30, 2004 and 2003, respectively, net of interest capitalization of $893 and $167 for the years ended June 30, 2004 and 2003, respectively.

(9) Benefits Plans

Self-insurance Plans – University

The University is self-insured for workers' compensation and medical benefits. Liabilities for asserted and unasserted claims under the workers' compensation program at June 30, 2004 were discounted by 4.50% and amounted to $23,177 (6.00% and $15,123 in 2003). The University has a $16.8 million standby letter of credit with JPMorgan Chase Bank to cover potential liabilities under the University's self-insured workers' compensation program.

Effective July 1, 2002, the University converted to a self-insured plan for health care benefits. Based on estimates provided by actuaries, the University's obligation for incurred but not reported claims was $8,631 as of June 30, 2004 ($8,307 in 2003). This amount has not been discounted.

Retirement Plan – University

Most full-time University employees participate in the retirement plans administered by TIAA-CREF, or in a defined contributions plan sponsored by the University. Under these plans, the University made contributions of $43,888 in 2004 ($40,268 in 2003), which were vested for the benefit of the participants.

Post-retirement Benefit Plan – University

The University's post-retirement benefit plan includes basic medical, major medical, dental coverage and life insurance. Benefit levels differ for current retirees, current employees eligible to retire and current employees not eligible to retire. The accumulated post-retirement benefit obligation of $70,623, created as of January 1, 1996 by the enactment of the plan, is being amortized over 16 years, the average estimated service lives of plan participants.

The University incurred retirement plan expense of $13,503 and $13,690 for the years ended June 30, 2004 and 2003, respectively, that is recorded in fringe benefits expense on the consolidated statement of activities.

The impact on retiree liabilities as a result of the conversion to a self-funded plan for health care benefits is reflected as an amendment to the change in benefit obligation.

Benefit expense for this plan for the years ended June 30, 2004 and 2003 includes the following components:

	2004	2003
Change in benefit obligation:		
Benefit obligation at beginning of year	$ 112,193	$ 101,857
Service cost	1,513	1,331
Interest cost	6,806	7,254
Estimated plan participants' contributions	1,411	1,206
Actuarial (gain)/loss	10,336	(2,833)
Benefits paid	(7,993)	(7,490)
Amendments	-	10,868
Benefit obligation at end of year	$ 124,266	$ 112,193
Change in plan:		
Fair value of plan assets at beginning of year	$ -	$ -
Employer contributions	6,582	6,284
Participant contributions	1,411	1,206
Benefits paid	(7,993)	(7,490)
Fair value of plan assets at end of year	$ -	$ -
Components of accrued benefit:		
Funded status	$ (124,266)	$ (112,193)
Unrecognized net actuarial loss	22,752	12,495
Unrecognized prior service cost	42,711	47,816
Accrued benefits	$ (58,803)	$ (51,882)
Amounts recognized in the balance sheet consist of:		
Accrued post-retirement benefit cost	$ (51,881)	$ (44,474)
Net post-retirement benefit income	(13,504)	(13,691)
Net benefits paid	6,582	6,283
Accrued benefits	$ (58,803)	$ (51,882)
Components of net periodic benefit cost:		
Service cost	$ 1,513	$ 1,331
Interest cost	6,806	7,254
Amortization of prior service cost	5,105	5,105
Net loss	80	-
Net periodic benefit cost	$ 13,504	$ 13,690

Estimated future contribution and benefit payments for the years ending June 30:

2005	$ 6,990
2006	7,525
2007	8,034
2008	8,388
2009	8,668
2010 to 2014	46,826
Total estimated future payments	$ 86,431

Benefits are valued based upon the projected unit cost method. The weighted average assumption used at the measurement date, April 1, are as follows:

	2004	**2003**
Discount rate for obligation	5.75%	6.25%
Expected return on plan assets	N/A	N/A
Rate of compensation increase	N/A	N/A
Health care cost trend rate – initial	12.00%	12.00%
Health care cost trend rate – final	4.00%	4.00%

The rate increase in health care costs was assumed to decrease to 4% in 2011 and to remain at that level thereafter.

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one percentage-point change in the health care cost trend rate would have the following effects:

	One percentage point increase	**One percentage point decrease**
Effect on total of service and interest cost components	$ 450	$ (412)
Effect on post-retirement benefit obligation	$ 4,935	$ (4,817)

In December 2003, the Medicare Prescription Drug Improvement and Modernization Act of 2003 (the Act) was passed. The Act introduces a prescription drug benefit under Medicare (Medicare Part D) as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit at least actuarially equivalent to Medicare Part D. Due to uncertainties in determining the impact of the Act on the accumulated post-retirement obligation and net periodic post-retirement benefit cost, the consolidated financial statements do not reflect the Act's effect on the University's post-retirement plans. Upon resolution of such uncertainties, the post-retirement plan will recognize the effects of the Act.

Post-employment Benefits – University

Accrued post-employment benefits of the University amounted to $35,545 and $27,209 at June 30, 2004 and 2003, respectively.

Retirement Plan – Related Entity (Highland Hospital and Affiliates)

The retirement plan of a related entity covers all employees who have completed one full year of continuous employment. The benefits for this plan are based primarily on years of service and employees' pay near retirement. The related entity's funding policy is to contribute annually, an amount consistent with the requirement of the Employee Retirement Income Security Act. Plan assets consist principally of cash equivalents, common stocks and fixed income investments.

Retirement plan expense of $4,136 and $1,835 was incurred for the years ended December 31, 2003 and 2002, respectively, and is recorded in fringe benefits expense in the consolidated statement of activities. In addition, a reduction in minimum pension liability of $1,730 was recorded in 2003. In 2002 a minimum liability of $10,266 was recorded, primarily due to the market performance of the plan's assets as well as a change in the weighted average discount rate. These amounts are included as other health care costs in the consolidated statement of activities.

Pension expense for this plan for the years ended December 31, 2003 and 2002 (the most recent data available) includes the following components:

	2003	**2002**
Change in benefit obligation:		
Benefit obligation at beginning of year	$ 53,446	$ 41,697
Service cost	2,323	1,838
Interest cost	3,294	2,979
Amendment	(359)	-
Actuarial loss	1,493	8,265
Benefits paid	(1,515)	(1,333)
Benefit obligation at end of year	$ 58,682	$ 53,446
Change in plan assets:		
Fair value of assets at beginning of year	$ 28,258	$ 32,124
Actual return on plan assets	5,155	(2,533)
Employer contribution	2,665	-
Benefits paid	(1,515)	(1,333)
Fair value of assets at end of year	$ 34,563	$ 28,258

	2003	2002
Components of accrued pension liability:		
Funded status	$ (24,119)	$ (25,188)
Unrecognized net actuarial loss	15,648	18,419
Unrecognized net asset in transition	(645)	(960)
Unrecognized prior service cost	66	158
Accumulated comprehensive pension expense	(8,536)	(10,266)
Intangible asset	(66)	(158)
Accrued pension liability	$ (17,652)	$ (17,995)
Amounts recognized in the balance sheet consist of:		
Accrued benefits cost	$ (17,718)	$ (18,153)
Intangible assets	66	158
Net amount recognized	$ (17,652)	$ (17,995)
Projected benefit obligation	58,682	53,445
Accumulated benefit obligation	52,216	45,253
Fair value of plan assets	34,563	28,258
Components of net periodic benefit cost:		
Service cost	$ 2,323	$ 1,838
Interest cost	3,294	2,979
Expected return on plan assets	(2,510)	(2,836)
Amortization of prior service cost	84	84
Amortization of transition asset	(315)	(315)
Amortization gain	1,260	85
Net periodic benefit cost	$ 4,136	$ 1,835
Weighted-average assumptions as of December 31:		
Discount rate for obligation	6.00%	6.50%
Discount rate for pension expense	6.50%	7.25%
Investment return assumption (regular)	9.00%	9.00%
Future compensation increase rate	3.00%	4.50%

Negative financial market returns during 2002 were offset by positive market returns in 2003. The combination of declining discount rate assumptions and market trends has resulted in a decline in the plan's funded status.

The pension plan funds are allocated to two money market managers, each with a balanced portfolio. These money managers monitor financial market funds and adjust inconsistent strategy accordingly.

The weighted-average asset allocation for the pension plan as of December 31, 2003 and 2002 by asset manager categories is as follows:

	2003	2002
Weighted-average assumptions by asset categories:		
Equity securities	65%	59%
Fixed income securities	34%	39%
Cash and other investments	1%	2%
	100%	100%

(10) Investment in Insurance Company

The University, together with other universities and teaching hospitals, has formed a captive insurance company (captive) to insure the medical malpractice risks of the shareholders. The University's investment in the captive represents 20% of the voting rights; however, the dissolution provisions of the captive agreement indicate that the University's financial participation (based on percentage of premiums paid) is approximately 8% of the financial results of the captive.

(11) Professional Liability Insurance

The University's coverage for professional liability insurance is provided under insurance policies obtained jointly with other universities and teaching hospitals. The primary layer of coverage, and 10% of the first layer of excess insurance, were written by MCIC Vermont, Inc. (a Risk Retention Group) formed and directed by the participating insured institutions. Multiple layers of excess insurance were purchased from several different insurance companies. The maximum coverage for the Medical Center is $207,500 per claim. The per claim coverage amount at each of the five participating institutions has been tailored to their own experience and exposures.

Based on estimates provided by the actuaries retained by MCIC Vermont, Inc., the University's obligations for incurred, but not reported claims were $14,491 and $12,341 as of June 30, 2004 and 2003, respectively.

(12) Fair Value of Financial Instruments

The method and assumptions described below were used to estimate the fair value of each class of financial instrument for which it is practicable to estimate that value. Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Cash and Cash Equivalent, Accounts Receivable, Third-Party Settlements Payable and Accounts Payable and Accrued Expenses

The carrying amount approximates fair value because of the short maturities of these instruments.

Contributions Receivable

Contributions receivable are recorded at their net present value. See note 1(h) for accounting policies related to contributions receivable.

Investment

Investments are reported at their fair values. See note 1(i) for accounting policies for determination of fair value of investments.

Notes Receivable

A reasonable estimate of the fair value of notes receivable from students under Federal Government financial assistance programs could not be made because the notes are not salable and can only be assigned to the Federal Government or its designees. The fair value of notes receivable from students under University loan programs approximates carrying value.

Estimated Professional Liability Costs

The carrying amount of this actuarially determined liability approximates fair value.

Long-Term Debt

The fair value of the University's long-term debt is estimated based upon the amount of future cash flows, discounted using the University's current borrowing rate for similar debt instruments of comparable maturities. The fair value of total bonds and notes payable was $591,900 and $508,600 at June 30, 2004 and 2003, respectively.

(13) Lines and Letters of Credit

The University has a $5 million line of credit with JPMorgan Chase Bank that can be used for letters of credit. Of this $5 million, $1,033 is currently committed ($500 for the University's Commercial General Liability Policy deductible and $533 for the repayment of obligations to the Urban Development Corporation).

The University has an additional $40 million line of credit with JPMorgan Chase Bank for emergency purposes. At June 30, 2004, there was no amount outstanding under this line of credit. At June 30, 2003, $7.8 million was committed for the refinancing of Eastman Place COMIDA bonds, which was in turn refinanced with the proceeds from the sale of the University's Direct Note Obligation, Series 2003.

(14) Commitments and Contingencies

In the ordinary course of operations, the University is named as a defendant in various lawsuits, or events occur which could lead to litigation, claims, or assessments. Although the outcome of such matters cannot be predicted with certainty, management believes that insurance coverage is sufficient to cover current or potential claims, or that the final outcomes of such matters will not have a material adverse effect on the consolidated financial position.

At June 30, 2004, the University has entered into construction contracts and commitments aggregating $309,153 ($290,585 at June 30, 2003) of which $263,003 ($263,683 at June 30, 2003) had been incurred.

As of June 30, 2004, the University has been awarded grants and contracts totaling $177,735 ($199,938 at June 30, 2003) for which the funds have not been received. Accordingly, these awards are not reflected in the consolidated financial statements, but represent commitments of sponsors, both government and other, to provide funds for specific research and training programs.

(15) Leases

Future minimum payments by year and in the aggregate, under non-cancelable operating leases, with initial or remaining terms of one year or more are as follows:

Operating Leases

	University	Related Entity
2005	$ 13,809	$ 710
2006	11,301	582
2007	8,715	577
2008	7,084	577
2009	4,404	577
Thereafter	22,036	1,458
Total minimum lease payments	$ 67,349	$ 4,481

(16) Scholarships, Grants and Fellowships

The University awarded a total of $81,422 and $76,491 in scholarships, grants and fellowships during fiscal years 2004 and 2003, respectively. In addition, the University awarded $9,528 and $9,051, respectively, of scholarships, grants and fellowships as compensation to the recipients. $13,316 and $14,181, respectively, of the total scholarships, grants and fellowships awarded were specifically funded by Federal, state or private gifts or grants, or by investment income and gains earned on investments held for endowment and similar purposes and utilized under the University's total return spending policy.

(17) Functional Expenses

The University also records expenses according to major classes of program or functions. Functional expenses for the years ended June 30 consisted of the following:

	2004	2003
Instruction	$ 242,178	$ 239,323
Research	211,734	189,311
Public Service	9,970	8,872
Libraries and other academic support	35,525	35,932
Student services	31,105	36,104
Institutional support	73,987	49,182
Hospital and faculty practice patient care	1,123,244	1,028,278
Auxiliary enterprises	46,877	45,917
Total functional expenses	$ 1,774,620	$ 1,632,919

(18) Subsequent Event

Pursuant to an agreement between the University and the Dormitory Authority of the State of New York, dated August 6, 2004, DASNY issued and sold $45,000 of University of Rochester Revenue Bonds, Series 2004A. The proceeds will be used to finance the construction of a cogeneration facility to provide supplementary heat and/or electricity to the University and will also include an addition to the University's Central Utilities plant. The University will be repaying the indebtedness at rates of interest ranging from 3% to 5.125%, maturing July 1, 2039.

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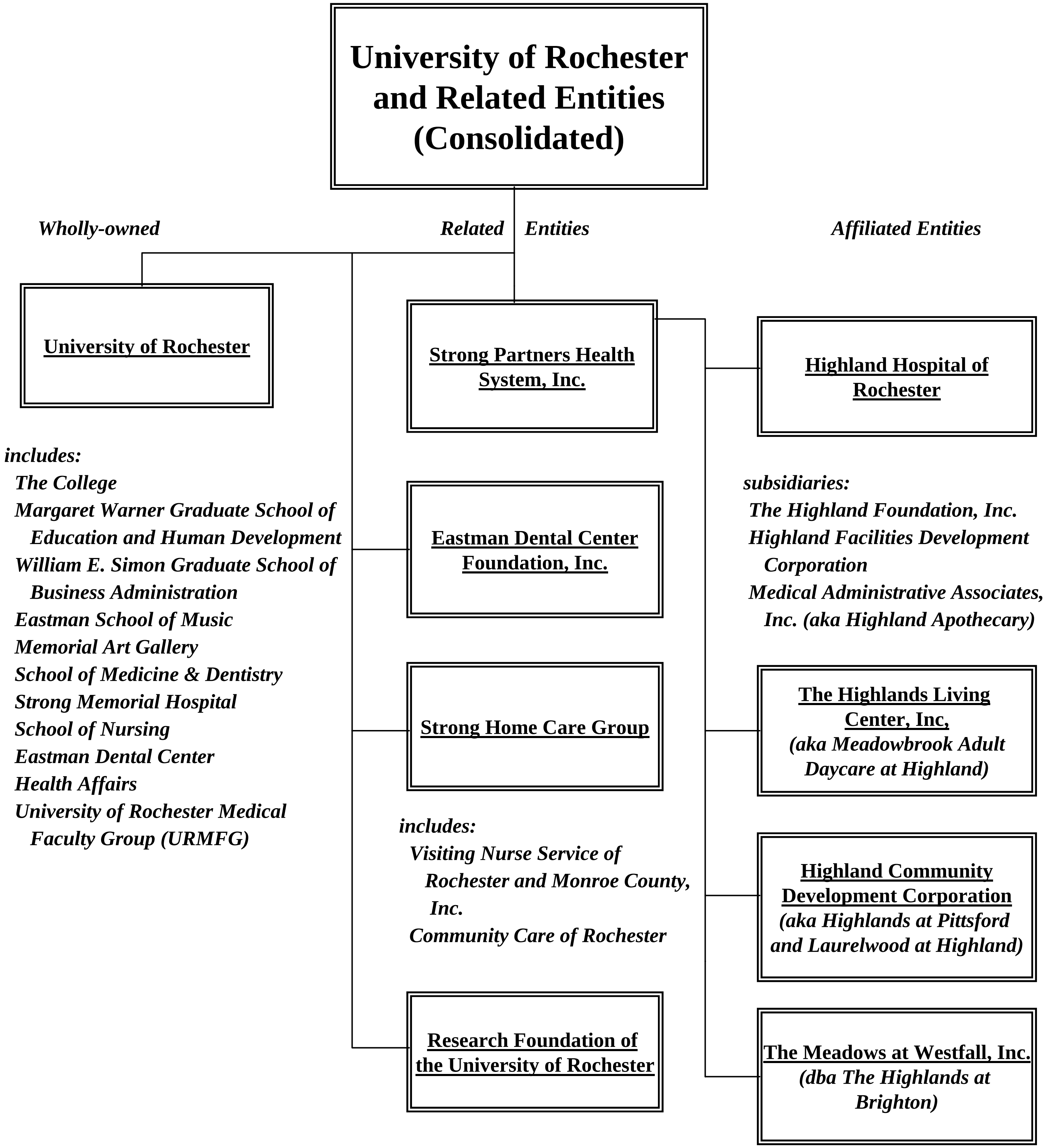

as of June 30, 2004