

**William Marsh Rice
University**
Consolidated Financial Statements
June 30, 2004 and 2003

William Marsh Rice University

Index

June 30, 2004 and 2003

	Page(s)
Report of Independent Auditors	1
Consolidated Financial Statements	
Statements of Financial Position	2
Statement of Activities	3
Statements of Cash Flows	4
Notes to Financial Statements	5–14

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Report of Independent Auditors

To the Board of Trustees of
William Marsh Rice University

In our opinion, the accompanying statement of financial position and the related statements of activities and cash flows present fairly, in all material respects, the financial position of William Marsh Rice University (the "University") at June 30, 2004, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the University's 2003 financial statements, and in our report dated October 3, 2003, we expressed an unqualified opinion on those financial statements. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

September 30, 2004

William Marsh Rice University
Consolidated Statements of Financial Position
As of June 30, 2004 and 2003

(in thousands of dollars)

	<u>2004</u>	<u>2003</u>
Assets		
Cash and cash equivalents	\$ 2,696	\$ 2,065
Accounts receivable and other assets	49,439	63,193
Pledges receivable, net	67,606	68,133
Investments	3,572,516	3,171,471
Property and equipment, net	580,421	569,966
Total assets	<u>\$ 4,272,678</u>	<u>\$ 3,874,828</u>
Liabilities		
Accounts payable and other liabilities	\$ 58,495	\$ 54,655
Notes and bonds payable	210,000	203,000
Actuarial liability for annuities payable	87,873	78,507
Refundable advances and amounts held in trust	7,151	8,512
Total liabilities	<u>363,519</u>	<u>344,674</u>
Net assets		
Unrestricted net assets	2,958,353	2,603,347
Temporarily restricted net assets	203,654	203,323
Permanently restricted net assets	747,152	723,484
Total net assets	<u>3,909,159</u>	<u>3,530,154</u>
Total liabilities and net assets	<u>\$ 4,272,678</u>	<u>\$ 3,874,828</u>

The accompanying notes are an integral part of these consolidated financial statements.

William Marsh Rice University
Consolidated Statement of Activities
For the Year Ended June 30, 2004 with Summarized Financial Information
for the Year Ended June 30, 2003

<i>(in thousands of dollars)</i>	2004			2003	
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Total
Operating revenues					
Investment returns distributed for operations	\$ 151,722	\$ 9,005	\$ -	\$ 160,727	\$ 153,387
Student tuition and fees, net	61,812	-	-	61,812	59,168
Grants and contracts	69,515	1,533	-	71,048	59,450
Gifts and pledges	15,575	13,002	-	28,577	22,767
Gifts and trusts released from restrictions	19,370	(19,370)	-	-	-
Auxiliary enterprises	29,058	-	-	29,058	26,612
Other revenues	7,498	-	-	7,498	4,069
Total operating revenues	<u>354,550</u>	<u>4,170</u>	<u>-</u>	<u>358,720</u>	<u>325,453</u>
Operating expenses					
Educational and general activities	284,355	-	-	284,355	270,221
Auxiliary enterprises expenditures	49,759	-	-	49,759	45,482
Total operating expenses	<u>334,114</u>	<u>-</u>	<u>-</u>	<u>334,114</u>	<u>315,703</u>
Net operating income	<u>20,436</u>	<u>4,170</u>	<u>-</u>	<u>24,606</u>	<u>9,750</u>
Nonoperating changes					
Gifts and pledges for property and endowment	-	4,322	14,157	18,479	24,417
Investment returns, reduced by operating distribution above	298,781	28,667	16,290	343,738	(21,677)
Net assets released from restrictions	36,300	(35,860)	(440)	-	-
Change in liabilities due under life-income agreements	-	(968)	(6,417)	(7,385)	6,651
Other nonoperating changes	(511)	-	78	(433)	(2,367)
Net nonoperating changes	<u>334,570</u>	<u>(3,839)</u>	<u>23,668</u>	<u>354,399</u>	<u>7,024</u>
Change in net assets before cumulative effect of change in accounting principle	355,006	331	23,668	379,005	16,774
Cumulative effect of change in accounting principle	-	-	-	-	180,890
Net increase in net assets	<u>355,006</u>	<u>331</u>	<u>23,668</u>	<u>379,005</u>	<u>197,664</u>
Net assets					
Beginning of year	2,603,347	203,323	723,484	3,530,154	3,332,490
End of year	<u>\$2,958,353</u>	<u>\$ 203,654</u>	<u>\$ 747,152</u>	<u>\$3,909,159</u>	<u>\$3,530,154</u>

The accompanying notes are an integral part of these consolidated financial statements.

William Marsh Rice University
Consolidated Statements of Cash Flows
For the Years Ended June 30, 2004 and 2003

(in thousands of dollars)

	<u>2004</u>	<u>2003</u>
Cash flows from operating activities		
Increase in net assets	\$ 379,005	\$ 197,664
Adjustment to reconcile increase in net assets to net cash used in operating activities		
Depreciation	34,735	31,810
Loss on disposal of property and equipment	384	2,276
Net realized and unrealized investment gains	(453,641)	(77,689)
Equipment gifts in-kind	(511)	(1,444)
Contributions restricted for long-term purposes	(27,112)	(23,913)
Actuarial decrease (increase) in life-income agreements	7,385	(6,651)
Cumulative effect of change in accounting principle	-	(180,890)
Changes in		
Accounts receivable and other assets	3,964	4,119
Pledges receivable for current purposes	(6,260)	366
Accounts payable and accrued liabilities	6,604	(7,765)
Net cash used in operating activities	<u>(55,447)</u>	<u>(62,117)</u>
Cash flows from investing activities		
Proceeds from sales of investments	1,505,539	889,614
Purchases of investments	(1,428,158)	(801,172)
Purchases of property and equipment	(46,630)	(64,498)
Net cash provided by investing activities	<u>30,751</u>	<u>23,944</u>
Cash flows from financing activities		
Contributions restricted for long-term purposes		
Endowment	11,553	13,993
Trusts and other	667	257
Property	7,468	8,420
Proceeds from commercial paper	10,500	13,800
Repayment of commercial paper	(3,500)	-
Net change in amounts held for others	(1,361)	2,060
Net cash provided by financing activities	<u>25,327</u>	<u>38,530</u>
Net increase in cash and cash equivalents	631	357
Cash and cash equivalents		
Beginning of year	2,065	1,708
End of year	<u>\$ 2,696</u>	<u>\$ 2,065</u>

The accompanying notes are an integral part of these consolidated financial statements.

William Marsh Rice University
Notes to Consolidated Financial Statements
June 30, 2004 and 2003

1. Basis of Presentation and Summary of Significant Accounting Policies

Basis of Presentation

William Marsh Rice University (the "University") is a Texas not-for-profit corporation that operates a private research university in Houston, Texas. The University is exempt from federal income tax to the extent provided under Section 501(c)(3) of the Internal Revenue Code. The consolidated financial statements of the University as of June 30, 2004, and for the year then ended, have been prepared in accordance with accounting principles generally accepted in the United States of America. Accordingly, the accompanying consolidated financial statements have been prepared on the accrual basis of accounting and include the accounts of the University and all wholly-owned subsidiaries. All material transactions between the University and its subsidiaries have been eliminated.

The financial statements include certain prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the organization's financial statements for the year ended June 30, 2003, from which the summarized information was derived. Certain reclassifications of 2003 information have been made to conform to the 2004 presentation.

Net Asset Categories

Standards for external financial reporting by not-for-profit organizations require that resources be classified for reporting purposes into three net asset categories according to donor-imposed restrictions. A description of the University's three net asset categories follows:

- a. Unrestricted net assets and related activity include the following:
 - (1) All revenues traditionally classified as unrestricted resources of the University, including tuition and fees, unrestricted gifts and income on unrestricted endowments, recovery of facility and administrative costs from grants and contracts, and auxiliary enterprise revenues.
 - (2) Revenues related to sponsored research agreements that are considered exchange transactions.
 - (3) Gifts and endowment income with donor-imposed restrictions, if the restriction is met within the current fiscal year of the University.
 - (4) Investments in plant assets stated at cost or fair value at the date of gift, less accumulated depreciation computed on a straight-line basis over the estimated useful lives of the assets. Equipment is removed from the records at the time of disposal.
 - (5) All expenses of the University.
- b. Temporarily restricted net assets include income from restricted endowments and gifts for which donor-imposed restrictions have not been met. The category also includes pledges receivable and life-income gifts for which the ultimate purpose of the proceeds is not permanently restricted.

William Marsh Rice University
Notes to Consolidated Financial Statements
June 30, 2004 and 2003

- c. Permanently restricted net assets include gifts, trusts and pledges on which donors have imposed the restriction that the corpus be maintained in perpetuity and only the investment return be made available for program operations. Those gifts specified by donors to provide loans to students are also included in permanently restricted net assets.

Expirations of temporary restrictions on net assets or subsequent donor release of restrictions are reported as reclassifications between the applicable classes of net assets.

Contributions

Contributions, including unconditional promises to give and irrevocable trusts held by others under which the University is the beneficiary, are recognized as revenues in the period received or promised. Contributions restricted for the acquisition of land, buildings and equipment are reported as temporarily restricted revenues. These contributions are reclassified to unrestricted net assets when the assets are placed in service. Promises to give that are subject to donor-imposed stipulations that the corpus be maintained in perpetuity are recognized as increases in permanently restricted net assets.

Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Contributions of assets other than cash are reported at their estimated fair value at the date of gift. Contributions scheduled to be received after one year are discounted at a rate commensurate with the risk. Amortization of the discount is recorded as contribution revenue.

Operating and Nonoperating Activities

The consolidated statement of activities reports the change in net assets from the University's operating and non-operating activities. Operating activities exclude (a) gifts and pledges for property and endowment (including annuity and life-income trusts), (b) release from restrictions of contributions restricted for the acquisition of property and equipment, (c) donor release of restrictions from permanently restricted net assets, (d) endowment return net of the University's operating needs as defined by University spending policy (Note 4) and (e) actuarial adjustments of annuities payable.

Cash and Cash Equivalents

The University considers all highly liquid financial instruments with an original maturity of 90 days or less to be cash and cash equivalents, except those amounts assigned to its investment managers and unspent commercial paper proceeds, which are classified as investments.

Investments

Investments are made within guidelines authorized by the University's Board of Trustees. Investments are initially recorded at cost at date of acquisition or fair market value at date of donation in the case of gifts. Investments are stated at market value. Ownership of marketable securities is recognized as of the trade date. Marketable securities transactions that have not settled are recognized as accounts receivable or accounts payable until the settlement date. Endowment return is calculated net of investment management expenses.

William Marsh Rice University
Notes to Consolidated Financial Statements
June 30, 2004 and 2003

Limited Partnership Investments

Diversified limited partnership interests are invested in both publicly and privately owned securities. The fair values of private investments are based on estimates and assumptions of the general partners or partnership valuation committees in the absence of readily determinable market values. Such valuations generally reflect discounts for illiquidity and consider variables such as financial performance of investments, recent sale prices of similar investments and other pertinent information. The private investments have a high concentration of pre-initial public offering securities, subjecting these investments to market value volatility.

Other Investments

Real estate, timber, oil and gas and other investments are valued at fair value. The fair value is estimated by professional appraisers or University management.

The terms of certain gifts of real property by the founder of the University provided that all returns realized from these properties were to be invested to generate income to be used for University purposes. Changes in the market value of these specific properties are recorded as permanently restricted as required by the donor.

Change in Accounting Principle

As of July 1, 2002, the University changed its method of accounting for other investments, including primarily real estate, timber, and oil and gas properties, from cost to fair value to more accurately reflect the University's financial position. This change is shown as a cumulative effect of change in accounting principle in fiscal year 2003 on the statement of activities and resulted in an increase in unrestricted net assets of \$64,900,000 and in permanently restricted net assets of \$115,990,000.

Property and Equipment

Educational property is stated at cost for purchased assets and fair market value at the date of donation in the case of gifts. The University depreciates its educational property assets (excluding works of art) using the straight-line method over their estimated useful lives. Repairs and maintenance of property and equipment are expensed as incurred.

Life-Income Agreements and Agency Arrangements

Life-income agreements include charitable remainder trusts and gift annuities. Charitable remainder trusts hold donated assets for which the University's subsidiary acts as trustee and periodically pays specified amounts to the designated beneficiaries. Generally, beneficiary payments are a fixed amount for annuity trusts and a fixed percentage of the fair market value of the trust assets or based on income earned for other charitable remainder trusts. At a date specified in each gift instrument, usually the beneficiary's date of death, ownership of the trust assets will transfer to the University and the beneficiary payments will cease. The University also enters into gift annuity agreements, which require that the University take ownership of the assets at the date of gift with an obligation to periodically pay specified amounts to designated beneficiaries for their lifetimes. Assets held in life-income trusts and those assets associated with gift annuities are included in investments. Contribution revenues are recognized at the date the trusts or gift annuities are established. Liabilities are recorded at the same time in accordance with actuarial tables established by the Internal Revenue Service and discounted according to the risk-free rate at the time of the gift. The liability represents the present value of the estimated future payments to be made to the donors and/or other beneficiaries. The liabilities are adjusted annually for changes in the value of the assets and actuarial changes that impact the estimates of future payments.

William Marsh Rice University
Notes to Consolidated Financial Statements
June 30, 2004 and 2003

The University has also received certain agency funds for which the University serves as custodian. Agency funds are recorded as investments with a corresponding liability (amounts held in trust for others) in the accompanying consolidated financial statements.

Use of Estimates

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

2. Accounts Receivable and Other Assets

Accounts receivable and other assets of the University at June 30, 2004 and 2003, were as follows:

(in thousands of dollars)

	<u>2004</u>	<u>2003</u>
Unsettled investment sales	\$ 16,254	\$ 25,571
Investment income receivable	4,027	7,393
Student loans receivable	7,208	6,672
Other accounts receivable	2,569	7,152
Inventory, prepaid expenses and other assets	6,683	6,019
Sponsored programs receivable	12,698	10,386
Total accounts receivable and other assets	<u>\$ 49,439</u>	<u>\$ 63,193</u>

3. Pledges

Unconditional promises to give are included in the consolidated financial statements as pledges receivable and revenue of the appropriate net asset category. Multi-year pledges are recorded after discounting to the present value of expected future cash flows. Unconditional promises to give at June 30, 2004 and 2003, are expected to be realized in the following periods:

(in thousands of dollars)

	<u>2004</u>	<u>2003</u>
In one year or less	\$ 25,490	\$ 23,542
Between one year and five years	32,802	31,934
More than five years	17,219	19,508
Less: Discount to net present value	(6,541)	(5,421)
Less: Allowance for uncollectible pledges	(1,364)	(1,430)
	<u>\$ 67,606</u>	<u>\$ 68,133</u>

William Marsh Rice University
Notes to Consolidated Financial Statements
June 30, 2004 and 2003

Pledges receivable at June 30, 2004 and 2003, had the following restrictions:

(in thousands of dollars)

	<u>2004</u>	<u>2003</u>
Permanently invested	\$ 19,230	\$ 25,064
Buildings	19,825	21,141
Support of University programs and activities	36,456	28,779
Less: Discount to net present value	(6,541)	(5,421)
Less: Allowance for uncollectible pledges	(1,364)	(1,430)
	<u>\$ 67,606</u>	<u>\$ 68,133</u>

A discount rate of 3% was used to discount pledges made on or after July 1, 2001, and a discount rate of 6% was used to discount all pledges made prior to July 1, 2001.

A conditional pledge of \$2,000,000 has been made to the University. Conditional pledges are recorded on the books when the conditions set by the donor are met.

4. Investments

Investments at June 30, 2004 and 2003, were as follows:

(in thousands of dollars)

	<u>2004</u>	<u>2003</u>
Fixed income securities	\$ 629,933	\$ 597,370
Equity securities	1,807,789	1,614,401
Limited partnerships	888,585	719,773
Other investments	246,209	239,927
	<u>\$ 3,572,516</u>	<u>\$ 3,171,471</u>

The table above includes annuity and life income fund assets of \$133,232,000 and \$117,926,000 as of June 30, 2004 and 2003, respectively.

William Marsh Rice University
Notes to Consolidated Financial Statements
June 30, 2004 and 2003

The following table summarizes investment income and net gains (losses) for the years ended June 30, 2004 and 2003, by net asset classification:

<i>(in thousands of dollars)</i>	2004			2003	
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Total
Investment earnings	\$ 42,788	\$ 1,652	\$ 6,384	\$ 50,824	\$ 54,021
Net gains on investments	407,715	36,020	9,906	453,641	77,689
Total investment gains and earnings	450,503	37,672	16,290	504,465	131,710
Less: Investment returns distributed for operations	(151,722)	(9,005)	-	(160,727)	(153,387)
Investment returns, reduced by operating distribution	\$ 298,781	\$ 28,667	\$ 16,290	\$343,738	\$(21,677)

Investment earnings are presented net of internal and external investment management expenses of \$18,602,000 and \$16,520,000 in fiscal 2004 and 2003, respectively.

The University has adopted an endowment earnings distribution policy based on total investment returns, as permitted by the Texas Uniform Management of Institutional Funds Act. Under this policy, the Board of Trustees approves an endowment earnings distribution, which is based on the earnings distribution of the preceding year and the market value of endowment assets. Sources of this distribution for each restricted endowment, in the order utilized, are (a) earned income as traditionally defined (interest, dividends, and rents), (b) reinvested earned income from prior years and (c) capital gains where not prohibited by the gift document. Sources of this distribution for the unrestricted general endowment, in the order utilized, are (a) earned income as traditionally defined (interest, dividends, and rents) and (b) capital gains. Endowment return, net of operating distributions, is reinvested under the University's endowment earnings distribution policy in the investment pool as net assets functioning as endowment.

5. Educational Plant

Property and equipment of educational plant at June 30, 2004 and 2003, were as follows:

<i>(in thousands of dollars)</i>	Estimated Useful Lives (Years)	2004	2003
Land	-	\$ 17,597	\$ 17,597
Buildings and improvements	20 - 50	559,848	526,229
Equipment, furniture and library books	2 - 20	265,658	250,894
Construction in progress	-	4,630	9,640
Less: Accumulated depreciation	-	(267,312)	(234,394)
		<u>\$ 580,421</u>	<u>\$ 569,966</u>

William Marsh Rice University
Notes to Consolidated Financial Statements
June 30, 2004 and 2003

6. Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities of the University at June 30, 2004 and 2003, were as follows:

<i>(in thousands of dollars)</i>	<u>2004</u>	<u>2003</u>
Unsettled investment purchases	\$ 18,381	\$ 20,603
Vendor accounts payable	14,847	12,315
Accrued payroll and employee benefits	12,423	7,906
Sponsored programs unearned income	7,716	8,571
Other accrued liabilities	5,128	5,260
Total accounts payable and accrued liabilities	<u>\$ 58,495</u>	<u>\$ 54,655</u>

7. Notes and Bonds Payable

Notes and bonds payable of the University at June 30, 2004 and 2003, were as follows:

<i>(in thousands of dollars)</i>	<u>2004</u>	<u>2003</u>
City of Houston Higher Education Finance Corporation (CHHEFC)		
Tax-exempt revenue bonds, Series 1999A, maturing 2023 through 2029, with fixed interest at 5.375% per annum payable semiannually	\$ 120,000	\$ 120,000
Tax-exempt commercial paper notes, Series A, with interest ranging from 0.98% to 1.13% at June 30, 2004 (1.05% to 1.10% at June 30, 2003) per annum payable upon maturity	90,000	83,000
	<u>\$ 210,000</u>	<u>\$ 203,000</u>

The University incurred interest expense of approximately \$7,359,000 and \$7,403,000 in 2004 and 2003, respectively, and paid interest expense of approximately \$7,371,000 in 2004 and \$7,281,000 in 2003. Interest expense of \$7,305,000 and \$7,201,000 was charged to operations in 2004 and 2003, respectively.

Tax-Exempt Revenue Bonds

Scheduled interest payments on the bonds are \$6,450,000 per year. Principal payments commence on November 15, 2023. No collateral is pledged on these bonds.

The estimated fair value of the CHHEFC Series 1999A bonds is 103.2% and 109.9% of face value at June 30, 2004 and 2003. The fair value is estimated based on quoted market prices for the same or similar issues.

Tax-Exempt Commercial Paper Notes

The University has a tax-exempt commercial paper credit facility that provides for borrowings in the form of individual notes up to an aggregate of \$100,000,000. The notes bear a fixed rate of interest, established on the borrowing date, over their individual terms, not to exceed 270 days.

William Marsh Rice University
Notes to Consolidated Financial Statements
June 30, 2004 and 2003

The outstanding balance under the facility was \$90,000,000 and \$83,000,000 with an average interest rate of 1.05% and 1.07% and an average maturity of 69 days and 55 days as of June 30, 2004 and 2003, respectively. In July 2004, the University paid down \$1,100,000 on the commercial paper program.

The estimated fair value of the Series A Notes is considered to be the same as the face value in view of their maturity dates.

8. Net Assets

The University's unrestricted, temporarily restricted and permanently restricted net assets for the years ended June 30, 2004 and 2003, are summarized as follows:

	2004			2003	
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Total
<i>(in thousands of dollars)</i>					
Internally designated for specific programs or ongoing activities	\$ 72,757	\$ -	\$ -	\$ 72,757	\$ 56,694
Designated or restricted by donor, including pledges	39,947	67,084	-	107,031	109,428
Net investment in plant	368,203	432	-	368,635	362,575
Endowment and designated for long-term investment including pledges	2,475,043	124,468	719,865	3,319,376	2,964,794
Life-income trusts	-	11,670	25,172	36,842	32,053
Loans	2,403	-	2,115	4,518	4,610
	<u>\$2,958,353</u>	<u>\$ 203,654</u>	<u>\$ 747,152</u>	<u>\$3,909,159</u>	<u>\$3,530,154</u>

The Board of Trustees has designated certain unrestricted and temporarily restricted net assets for long-term investment. Most net assets designated for long-term investment and endowment assets participate in one common investment pool of marketable securities (Note 4).

9. Student Financial Aid

Gross student tuition and fees of \$94,854,000 and \$88,128,000 in 2004 and 2003, respectively, are presented in the consolidated financial statements net of scholarship and fellowship awards of \$33,042,000 and \$28,960,000, respectively. Auxiliary enterprises revenue was reduced by scholarship awards applied to room and board charges of \$1,356,000 and \$1,772,000 in 2004 and 2003, respectively.

William Marsh Rice University
Notes to Consolidated Financial Statements
June 30, 2004 and 2003

10. Functional Expenses

Educational and general expenses of the University by major functional category for the year ended June 30, 2004 and 2003, were as follows:

<i>(in thousands of dollars)</i>	<u>2004</u>	<u>2003</u>
Instruction and department research	\$ 148,920	\$ 141,021
Sponsored programs	56,656	50,637
Library	20,934	20,398
Scholarships and fellowships	9,049	10,284
Student services	12,706	12,352
General administration	21,438	21,233
Institutional development and other activities	14,652	14,296
Total educational and general	<u>\$ 284,355</u>	<u>\$ 270,221</u>

The above table includes depreciation expense of \$17,501,000 and \$16,865,000 and operations and maintenance expense of \$25,785,000 and \$26,002,000 for the years ended June 30, 2004 and 2003, respectively, which were allocated to the major functional categories based on space usage. Depreciation of library books of \$6,356,000 and \$5,991,000 was recognized as library expense in 2004 and 2003, respectively. In addition, depreciation expense of \$10,878,000 and \$8,954,000 was allocated to auxiliary enterprises in 2004 and 2003, respectively.

11. Retirement Plans

Substantially all employees are eligible to participate in a defined contribution retirement plan, which is administered by an outside agency. The plan operates in accordance with Section 401(a) of the Internal Revenue Code. All University contributions are made to this plan. In addition, employees may elect to participate in plans created under Section 403(b) of the Internal Revenue Code. The contributions of the University and the employees are applied to annuity contracts. The University's contributions to the plan of \$12,556,000 and \$11,958,000 were recorded as expenses in the appropriate functional categories in 2004 and 2003, respectively.

12. Commitments and Contingencies

A number of suits and claims are pending against the University. While final outcomes cannot be determined at this time, management believes that uninsured liability, if any, resulting from these suits and claims will not have a material adverse effect on the University's financial position.

The University receives funding from federal government agencies for activities conducted under government grants and contracts. The grants and contracts provide for reimbursement of direct and indirect costs. The costs recovered by the University in support of sponsored programs are subject to audit and adjustment.

In connection with its private equity investment program (Note 4), the University is obligated under certain limited partnership agreements to advance additional funding up to specified levels upon the request of the general partner. At June 30, 2004 and 2003, the University had unfunded commitments of \$379,033,000 and \$269,526,000, respectively, which are expected to be called primarily over the next five to seven years.

William Marsh Rice University
Notes to Consolidated Financial Statements
June 30, 2004 and 2003

Additionally, the University was committed under contracts at June 30, 2004 and 2003, for capital construction and improvements and major maintenance of approximately \$6,284,000 and \$17,954,000, respectively, to be financed primarily from gifts and net assets designated for long-term investments. Other commitments of \$5,793,000 and \$5,396,000 were also outstanding at June 30, 2004 and 2003, respectively.