

Transforming

UNIVERSITY OF WASHINGTON

ANNUAL REPORT 2005

Lives



Facts

	2004–2005	1999–2000	1994–1995
STUDENTS			
Autumn Enrollment			
Undergraduate	30,790	28,125	25,890
Graduate	10,309	8,606	7,967
Professional	1,808	1,709	1,312
TOTAL	42,907	38,440	35,169
Extension ¹	41,550	26,277	23,661
Number of Degrees Awarded			
Bachelor's	8,517	6,923	6,564
Master's	2,797	2,151	1,936
Doctoral	530	486	482
Professional	475	428	371
TOTAL	12,319	9,988	9,353
INSTRUCTIONAL FACULTY	3,623	3,271	3,053
FACULTY AND STAFF ²	27,695	22,646	20,871
RESEARCH FUNDING – ALL SOURCES (in thousands of dollars)	\$ 996,000	\$ 652,000	\$ 477,000
SELECTED REVENUES (in thousands of dollars)			
Gifts, Grants, and Contracts	\$ 1,021,565	\$ 643,545	\$ 478,028
Auxiliary Enterprises ³ and Other Revenues	1,230,813	775,518	513,036
State Appropriations (Operating)	323,417	322,079	257,176
Tuition and Fees ⁴	331,978	246,895	176,861
SELECTED EXPENSES (in thousands of dollars)			
Instruction, Academic Support, and Student Services	\$ 888,499	\$ 596,317	\$ 443,634
Research and Public Service	605,433	456,040	328,509
Auxiliary Enterprises ³	755,959	621,354	385,719
Institutional Support and Physical Plant	261,174	168,287	150,678
CONSOLIDATED ENDOWMENT FUNDS ⁵ (in thousands of dollars)	\$ 1,366,000	\$ 859,000	\$ 319,000
SQUARE FOOTAGE ⁶ (in thousands of square feet)	17,504	15,800	14,500

¹ Course registrations

² Full-time equivalents

³ Includes medical related

⁴ Net of scholarship allowances of \$48,123,000 in 2004-2005

⁵ Stated at fair value

⁶ Gross square footage, all campuses



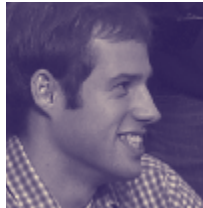
Tarek Holmes – “The GEAR UP academy boosted my confidence through the roof.”



Mary Larson – “Parting with these paintings just tears at my heart. But you can't buy them with cash. You can buy them with donations.”



David R. Flum, M.D. – “The question is, can we make this robotic system better than traditional surgery for a full range of procedures?”



Dane McCartney – “We had 15 real world cases to practice on, covering a host of different problems in applied ethics.”

Transforming Lives

Kathleen Belew – “On a colectivo, all the barriers are down. It's a very intimate space — really extraordinary.”



Linda Buck – “You want to do something you're obsessed with, that you just have to understand, because that's where the joy comes from.”



Jared Silvia – “They turned me on to being a professor, and I want to be versed in as many things as possible.”



Loyce Mbewa – “Look at your neighbor. What will make a difference to the largest number of lives in this community?”



CONTENTS

	2
MESSAGE FROM THE PRESIDENT	
	4
TRANSFORMING LIVES	
	16
FINANCIAL HIGHLIGHTS	
	26
FINANCIAL STATEMENTS AND REQUIRED SUPPLEMENTARY INFORMATION	
INSIDE BACK COVER	
BOARD OF REGENTS AND ADMINISTRATIVE OFFICERS	



Message from the President

The first thing to say about 2005 is that it was a banner year for University of Washington students. Some of them appear in this report—the undergraduates who won Truman and Javits and Churchill scholarships, the team that brought home a first-place trophy from the National Ethics Bowl, and the alumna who was named a Nobel laureate. But we could fill another annual report with similar stories. Three UW students won Goldwater scholarships. Two won Gates Cambridge scholarships. One was named a Udall Scholar for the second year in a row—almost unprecedented. Another won an NIH Oxford scholarship. These are all intensely competitive national awards. And farther afield, a UW math team placed in the highest category (Outstanding Winner) of the international Mathematics Modeling Contest, an honor earned by five UW teams in the last four years.



We are immensely proud of these students. Their honors and awards open doors for them beyond the UW and bring joy to the teachers and mentors who helped them on their way. But these achievements, however remarkable, are just a special case of the prize we want all UW graduates to take away: an education that transforms their lives. That is what the University of Washington gave me thirty years ago, and that is what every student and family today has a right to expect.

What does that kind of education require? First, brilliant and dedicated faculty and staff members, and enough of them. Second, the right facilities and technologies. We need spaces and technologies for a new kind of student-driven learning—active, collaborative, hands-on, and engaged with the outside world. Increasingly, even our research labs are sites of undergraduate learning, as more and more students join faculty research teams.

All this takes money. Fortunately, 2005 brought some real progress on the funding front. Led by Governor Gregoire, the state legislature, in response to growing public awareness of higher education's critical importance, gave us the best budget we have seen in at least a decade. With increases in both state appropriations and authorized tuition levels (as well as financial aid), we gained 10 percent in core educational resources for the 2005-07 biennium. That means more dollars to educate every student. We will be able to provide much-needed salary increases for faculty and staff, add new enrollments to all three campuses, and fund a number of new educational offerings. On the capital side, unfortunately, the budgetary news was not so good, but we will continue to press for the facilities support we need.

The governor and legislators took two other important steps: they authorized our Bothell and Tacoma campuses to begin admitting freshmen and sophomores, and they created the Life Sciences Discovery Fund, the first major state investment in scientific research. Both will significantly expand the UW's ability to serve the state.

In other realms as well, 2005 was a year of forward motion and striking achievement. A few highlights among many:

our research funding increased once more, to just shy of a billion dollars. Jiao Tong University, in Shanghai, ranked the UW number 20 on its list of leading universities worldwide, a ranking that was widely publicized by *The Economist* a few months later and has since risen to 17th. Our Business School rose to 18th in America, while our programs in international business (21st) and accounting (22nd) did well in the specialty rankings. Many other schools and departments also displayed excellence in the rankings, including our School of Nursing, which continued its long reign as the nation's top nursing school, a position it has held each year since 1984. We began development of an ambitious new global health department, a joint undertaking of the School of Medicine and the School of Public Health and Community Medicine. And, we initiated a campus-wide study to address how we can best strengthen and improve the undergraduate educational experience for our students.

UW faculty continued to blaze trails and win recognition. Psychology professor Geraldine Dawson, whose work on understanding, diagnosing, and treating autism was widely covered during the year, gave the keynote speech at the International Meeting for Autism Research. Professor Richard Ladner, of Computer Science & Engineering, won a Presidential Award for Excellence in Science, Mathematics, and Engineering Mentoring. Professor Adrian Raftery, of Statistics and Sociology, was recognized as the most-cited mathematical researcher in the world during the past decade. Three UW faculty members (Qiang Fu of Atmospheric Sciences, Donald Brownlee of Astronomy, and Joseph Sisneros of Psychology) appeared on *Discover* magazine's list of the 100 most important discoveries and developments of 2004; Professor Fu's work on climate change headed the list. And on and on...

This is the rich environment in which University of Washington students learn. The knowledge and opportunities they can find here are almost limitless. When all goes well, they also discover the people they will become, the ideas that will animate their lives, and the work they will contribute to society.

Mark A. Emmert



Transforming

Lives

6
BEYOND THE COMFORT ZONE



8
WELL VERSED



10
WINNING ON MORAL GROUNDS



12
A SEAT AT THE TABLE



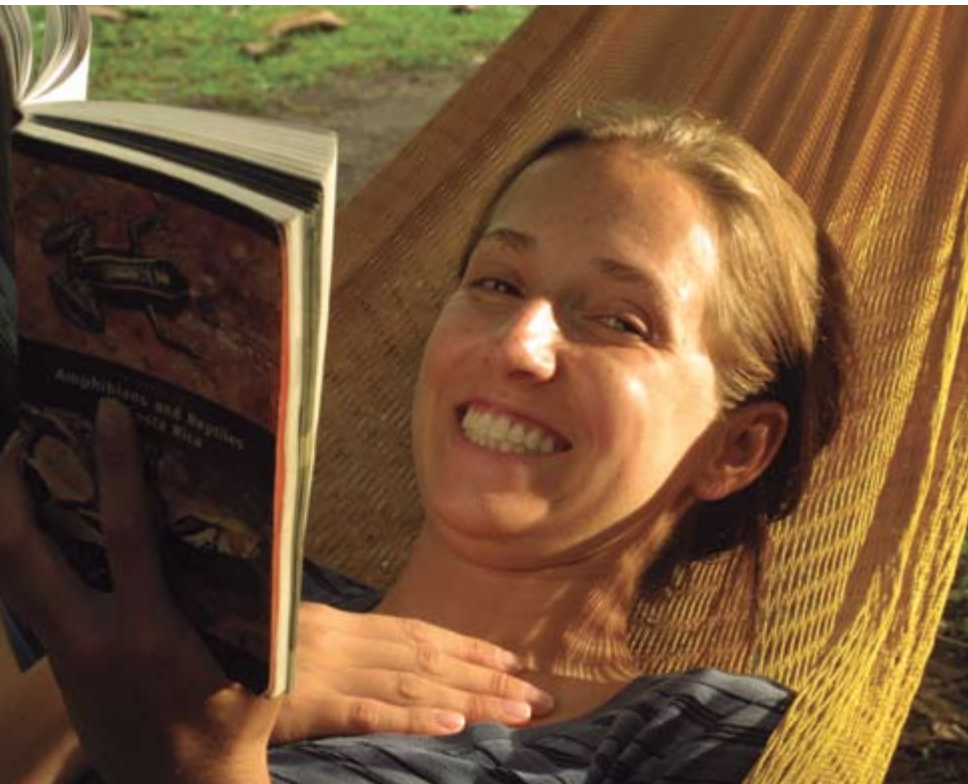
14
DECIPHERING AN ENIGMA



K

KATHLEEN BELEW HAS BEEN A HUNTER AND GATHERER of education. When she talks about her years at the UW, she talks about journeys to Prague and to Chiapas, Mexico, with the Comparative History of Ideas (CHID) program. She talks about roaming Central America for four months in colectivos—local buses with circular seating—on a Bonderman Travel Fellowship. (These fellowships support independent international travel by UW students and recent graduates.) On a colectivo, she says, “all the barriers are down. It’s a very, very intimate space—really extraordinary.” Her own extraordinary encounters with people, landscape, and history were e-mailed back to campus as vivid travel journals. >

Beyond the Comfort Zone



WANDERING CENTRAL AMERICA ON A BONDERMAN FELLOWSHIP GAVE KATHLEEN BELEW THE FREEDOM TO CHALLENGE HER THINKING ABOUT PEOPLE AND THEIR INTERACTION WITH THE LANDSCAPE AND EACH OTHER. SHE WILL PUT THE EXPERIENCE TO GOOD USE AS SHE BEGINS A FOUR-YEAR JAVITS FELLOWSHIP IN AMERICAN STUDIES.





PUBLIC LECTURES

At the UW not all learning takes place in the classroom. Hundreds of evening lectures, musical performances, and art exhibitions take place every year. They have broad appeal to alumni and the greater community. The History Lecture series, now 30 years old, is one such example of connecting community and faculty, and in the process, enriching both.

Most intensely, Kathleen talks about the summer in Tennessee when she gathered material for her CHID honors thesis. It was an oral history project about white sharecroppers, exploring their hard transitions from cotton fields to factories to the widespread unemployment that followed the factories' departure. But these sharecroppers happened to be members of her own extended family. "It was a pivotal moment," she says, "my first time asking family the questions you're not supposed to ask. I thought there would be racism and evangelical disputes. Instead, I found the strength of the human spirit—love, loyalty, humility. It changed me." The outcome, says her adviser, was "the most ambitious undergraduate thesis I have ever supervised."

Kathleen traces this rich, off-campus learning back to its campus source: the CHID program itself and its guiding spirit, the late Jim Clowes. "He's the person who woke me up academically," she says. "He encouraged people to push beyond the ordinary, to question themselves. He made CHID a really exceptional space. It's very project-oriented—the courses are tools to pursue the things that are important to you. And CHID does international study in a unique way—it sends you outside your comfort zone. There's a very intuitive piece in both travel and a CHID liberal education. You are following your interests even to a scary point. It's a risk-loving strategy."

“I thought there would be racism and evangelical disputes. Instead, I found the strength of the human spirit—love, loyalty, humility. It changed me.”

For Kathleen, the risks paid off. She graduated with distinction, was named the 2005 Dean's Medalist in the Humanities, and won a Jacob K. Javits Fellowship (one of only 53 in the nation) for four years of graduate study. Her next stop is the Yale Ph.D. program in American Studies. She then sees three roads opening ahead: as a teacher, creating the kind of space she loved in CHID; pursuing the political implications of her work on rural poverty; and, eventually, writing "a big fiction book." She concludes, like the inveterate traveler she is, "I like all the possibilities."

JJARED SILVIA ARRIVED AT THE UNIVERSITY OF WASHINGTON with a diploma from Hanford High School, an interest in science, a thirst for new opportunities, and his alto sax. Four years later, in June 2005, he graduated with degrees in chemistry and biochemistry, extensive research experience, a year's worth of clips as a *Daily* opinion columnist, memories of good times in the UW concert band, the Dean's Medal in the Natural Sciences, and a Winston Churchill Scholarship for graduate study in science at Cambridge University—one of only 12 awarded in the U.S. >

Well Versed



JARED SILVIA WANTS TO MAKE MOLECULES TO IMPROVE INDUSTRIAL CHEMICAL PROCESSES. LIKE MOST SCIENTISTS TODAY, HE'LL NEED TO CALL ON HIS ACADEMIC PREPARATION IN A VARIETY OF AREAS TO SOLVE THE DIFFICULT PROBLEMS. IT'S SIMILAR TO READING THE SHEET MUSIC AND IMPROVISING, AND HIS SAXOPHONE TRAINING WILL COME IN HANDY.





FARM WORKER OUTREACH

At a migrant worker camp in the Skagit valley, students from the Health Sciences minority medical education program volunteer with members of the SeaMar Clinic to provide basic health care (blood pressure, diabetes, and TB testing) to migrant workers and their families.

Jared also took away from the UW an image of the life he wants to lead. Two of his earliest professors showed him that life in action.

Kannan Krishnan, professor of materials science and engineering, taught Jared's freshman seminar in nanotechnology. "He was a great professor," says Jared, "one of the most influential for me at the UW. He offered to help me with independent study spring quarter, and then invited me to do research with him my sophomore year. He was very interested in getting one-on-one with the students in his lab. He showed me that university teaching was a field where you could have a lot of personal interaction and do science."

D. Michael Heinekey, who taught Jared honors chemistry in the spring of his freshman year, was the second model and mentor. "He was such a good teacher," Jared remembers, "reaching out to me and teaching me what I needed to know. He got me really excited about chemistry. When I decided that would be my focus, I joined his research group for my last two years. That's where I found out what I wanted to do in my own research."

At Cambridge, Jared will pursue his interest in the reactivity of metals, with the ultimate goal of "making molecules" that can improve chemical processes used in industry. But the career he wants is the one he admired in his two UW mentors, where teaching and research

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flow into each other. "They turned me on to being a professor," he says. "And I want to be versed in as many things as possible," he adds, recalling the pleasure he took in "getting away from science" in the UW concert band.

Jared, says Michael Heinekey, is "a young man of extraordinary gifts and unlimited potential." Just listen for the alto sax in the chemistry lab.

E

ETHICS DOES NOT APPEAR ON MANY LISTS of team sports. But for philosophy students, the National Ethics Bowl involves the same kind of canny recruiting, rigorous team training, and competitive high that others find on the athletic field. And on February 24th, 2005, the UW ethics team came in first in the nation. >

Winning on Moral Grounds



A WINNING TEAM IS A BLEND OF THE TALENTS OF ITS MEMBERS, THEIR TRAINING FOR THE COMPETITION AND A BURNING DESIRE TO SUCCEED. ARGUING CASES FROM TRANSPORTATION PLANNING TO STEM CELL RESEARCH, THE 2005 UW ETHICS BOWL TEAM BECAME THE SECOND UW TEAM IN FIVE YEARS TO WIN THE NATIONAL CHAMPIONSHIP. GO SOCRATES!





ROBOTIC SURGERY

Dr. Lily Chang leads a surgical team in performing a robotic gall bladder operation. By using the Zeus robotic system, Dr. Chang is one of several UW physicians able to perform surgeries that are much more precise and less invasive than more traditional methods.

The team—six undergraduate philosophy majors—was shaped and coached by graduate students David Alexander and Ali Hasan. “We recruited for range,” says Alexander, citing the students on the team with second majors, from political science to comparative literature to biology. “We had 15 real-world cases to practice on, covering a host of different problems in applied ethics, and each team member was assigned to be the expert on certain cases. So our biology student, for example, really helped us on the stem-cell case.”

The youngest team member, Dane McCartney, had just arrived from Peninsula College in Port Angeles, where, as a Running Start student, he had already earned an associate’s degree during his last two years of high school. As a pure philosophy major, he says, “I was by far the least diversified person on the team.” But for coach Alexander, Dane had other credentials: an impressive philosophical mind and extensive experience in debate.

After weeks of ethical calisthenics, the team flew off to San Antonio for the competition. A very late plane and lost luggage, as well as general Northwest style, meant “we were by far the most underdressed team there,” says Dane. Nevertheless, in one intense day that went from Sweet Sixteen (actually 36 teams total) to National Championship, the UW team went undefeated in contest after contest. During the final evening round, says Alexander, “I was a wreck. I felt like a soccer dad.” Then the team he and Hasan had so carefully crafted and coached argued one last case and won the trophy.

“Working with these incredibly bright, motivated kids was so much fun. They evolved so much—to watch that made me really proud.”

Coaching the team, says Alexander, will make him a better teacher of ethics. But beyond that, “working with these incredibly bright, motivated kids was so much fun. They evolved so much—to watch that made me really proud.”

Dane will re-up for the team in 2006. “I learned a lot about ethics,” he says. “It helped me develop my own opinions.” That is good training for either of the future paths he imagines: an academic career in philosophy, or military intelligence work. The latter, he points out, “will use the same skills I’ve developed as a philosophy major: collecting data and forming opinions; figuring out what you know and what you don’t know. It requires epistemic honesty.”

L

LOYCE MBEWA GREW UP IN THE VILLAGE OF RABUOR in western Kenya. It was a place, she remembers, of extraordinary happiness and community: “Everyone was your mother.” So her shock was profound when she returned, after five years in the U.S., to find the village devastated by AIDS and its consequences—poverty, endless funerals, and scores of orphaned children. >

A Seat at the Table



photos on this page: www.amandakoster.com

IMAGINE FINDING YOUR HOMETOWN DEVASTATED—BY NATURAL DISASTER, OR DISEASE, OR ECONOMIC DECLINE. THEN IMAGINE FORMING AN ORGANIZATION TO DO SOMETHING ABOUT IT. FOR LOYCE MBEWA, THIS IS JUST THE FIRST STEP IN PREPARING HERSELF TO BRING CHANGE TO THE DEVELOPING WORLD, BY HELPING TO MAKE COMMUNITIES SELF SUSTAINING.





GEAR-UP

When Henry Foss High School student Tarek Holmes was asked about his experience this past summer attending the UW State GEAR UP Project Honors Academy, his response was unequivocal. “The Academy boosted my confidence through the roof! If I can do college work and live in a college environment as a freshman in high school, I can accomplish anything I put my mind to.”

Inspired by a women’s group her mother had started in the village, Loyce began recruiting partners and volunteers for the Rabuor Village Project (RVP), which she runs from her home in Seattle. Money and other kinds of support began to flow into the village through RVP. But the key, Loyce insists, is the ideas and energy of the villagers themselves. “My starting point,” she says, recalling her childhood in Rabuor, “was this: for generations, they did something right. They’re on weaker ground now, because of AIDS, so we need to give them hands up. Then they can lift themselves and go.” So far, RVP has helped the village open a nursery school and feeding program for orphaned children, drill a well, buy oxen, open a local pharmacy, and start a brick-making business.

With her life now redirected, Loyce went back to school. She wanted both the knowledge and the credibility—the “seat at the table”—that education could give her. She first earned an associate’s degree at Seattle Central Community College and then transferred to the UW in the fall of 2004.

“It was overwhelming, intimidating,” she remembers. But Loyce is not a woman to be overwhelmed for long. She knocked on doors and walked into offices, trying to find the courses and contacts she needed. “I wanted subjects where my learned experience could be enhanced,” she says, “but I didn’t even have the language to ask the right questions.” Fortunately, everyone she talked to, from faculty to counselors to administrative staff, helped her find the right path and take the next step. “I have had an extraordinary experience with staff and community here,” she says. “There’s so much support.”

“I would like to be a person who bridges the gap, ...who helps local communities make themselves sustainable. I like to get my hands dirty and see change as it happens.”

In the spring of 2005, Loyce won another kind of support: a Truman Scholarship for both her senior year and graduate school. The award goes to only 70 or so students nationally, based on “leadership potential, intellectual ability, and the likelihood of making a difference.” When Loyce graduates from the UW in 2006, she will go on to a master’s degree in public health.

“My dream,” she says, “is to work with organizations in the developing world. I would like to be a person who bridges the gap, who translates projects and identifies priorities, who helps local communities make themselves sustainable. I like to get my hands dirty and see change as it happens. To be part of that is a great joy for me.”

T

THROUGH THE SENSE OF SMELL, human beings can perceive more than 10,000 chemicals as distinct odors. With one whiff, we recognize roses or coffee or barnyard manure. How do we do it? For answering that question, Dr. Linda Buck (UW '75) and Dr. Richard Axel were awarded the Nobel Prize for Physiology or Medicine in October 2004. In joint and parallel research, they had deciphered the “most enigmatic of our senses,” in the words of the Nobel committee. >

Deciphering an Enigma



photo by Todd McNaught/Fred Hutchinson Cancer Research Center

FLANKED HERE BY NOBEL PRIZE WINNERS E. DONNAL THOMAS AND LELAND HARTWELL, LINDA BUCK HAS BECOME THE SIXTH UW AFFILIATED NOBEL LAUREATE. DR. BUCK'S SUCCESS, LIKE THAT OF HER PREDECESSORS, REFLECTS A POWERFUL SCIENTIFIC MIND, AN ALL-ABSORBING QUESTION, AND THE RESOURCES OF GREAT INSTITUTIONS.



photo by Roland Morgan



photo by Keith Lazelle



photo by Todd McNaught/Fred Hutchinson Cancer Research Center



PIONEER SQUARE CLINIC

Mary Larson is a nurse at the Pioneer Square Clinic, run by Harborview Medical Center. She has another passion—painting. Her subjects are patients at the clinic, many of them homeless. For several years now, her paintings have added color and cheer to the clinic, and to the lives of those who see them. They are for sale, but the medium of exchange is often pairs of socks or donations of food that are then shared with patients at the clinic.

Dr. Buck remembers the exact moment in 1985 when she became “totally obsessed” with that enigma. She was nearing the end of her postdoctoral work on the nervous system of a sea snail in Dr. Axel’s Columbia University lab. “I read a paper that changed my life,” she writes in her autobiography. “It discussed potential mechanisms underlying odor detection. This was the first time I had ever thought about olfaction, and I was fascinated. It was a monumental puzzle.”

There were two related questions: How can we detect so many odors? And how does the brain translate chemicals in the environment into perceptions of odor? The picture that gradually emerged, teased out by years of ingenious research, was one of astonishing complexity. The first discovery, made at Columbia: a very large family of genes (350 in human beings) produces, in the nose, an equal number of types of odor receptors, each type specialized to recognize a few specific “odorants” (chemical molecules). In Dr. Buck’s subsequent work at Harvard, she traced the complicated route from nose to brain, where the neurological signals sent by odorants finally combine in various patterns to generate different scents. The best analogy, she says, is the way the 26 letters of our alphabet combine to form an almost unlimited number of words.

Dr. Buck grew up in Seattle. Her life as a biologist began, after several years of undergraduate “angst,” in a UW immunology class. “I loved it,” she recalls. “I had finally found the right thing.” Next came a Ph.D. at the University of Texas and her groundbreaking years at

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Columbia and Harvard. In 2002 she returned to the Northwest as an investigator of the Howard Hughes Medical Institute at the Fred Hutchinson Cancer Research Center and an affiliate professor at the UW.

Dr. Buck’s lab at the Hutch is still working out the mysteries of smell. But she has also taken on a new subject: aging. “For many years,” she says, “I’ve wondered why human beings and mice, with quite similar genomes, have such different life spans. Is there a master control, like a clock? Is there a small set of cells that controls aging in all parts of the organism? Are they neurons? How do you study it?” Dr. Buck has found her next enigma.



Financial
Highlights



18
FUNDING AND OPERATIONS

20
INVESTMENTS

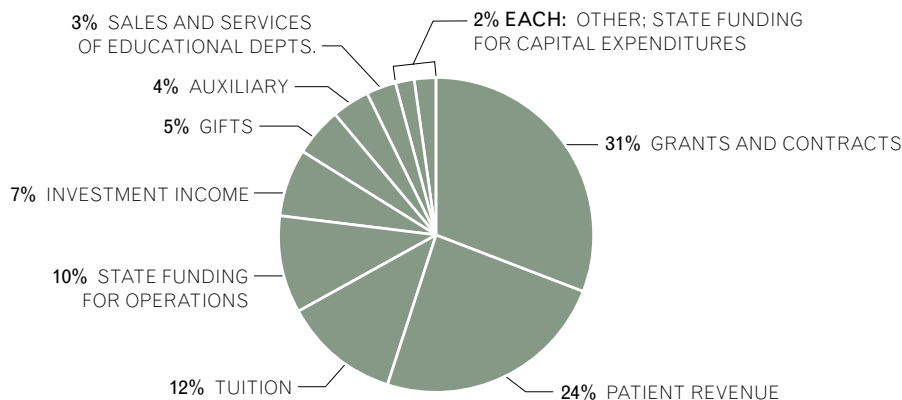
22
DEBT FINANCING

24
CAPITAL BUDGET AND CAMPUS CONSTRUCTION

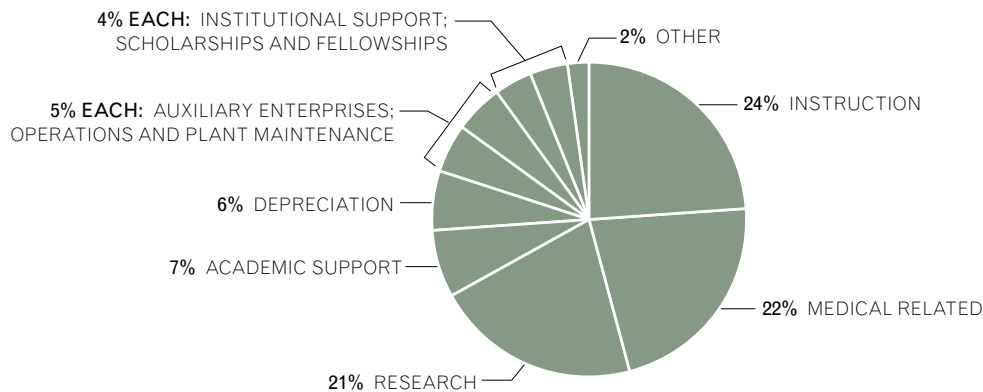
Funding and Operations

- The University has a diversified revenue base. No single source generated more than 31 percent of the total fiscal year 2005 revenues of \$3.1 billion.
- State operating appropriations were \$323 million, or ten percent of total revenues. The University relies heavily on such funding for instructional activities.
- Grants and contracts (31 percent) generated \$954 million of current year revenue, a seven percent increase over fiscal year 2004. These funds provided the opportunity for graduate and undergraduate students to work with nationally recognized faculty in research, as part of their educational experience.
- Income from gifts totaled \$172 million (five percent). This is an increase of \$50 million from the prior year.
- Two primary functions of the University, instruction and research, comprised 45 percent of total operating expenses. These dollars provided instruction to more than 42,000 students and funded 5,200 research awards.
- The University provided students with scholarships and fellowships, (including scholarship allowances of \$50 million), totaling \$107 million. This represented four percent of operating expenditures.

Sources of Funds



Uses of Funds





MyFinancial.desktop Launched

In May 2005, the University of Washington launched a new financial reporting tool to the campus community. The tool, MyFinancial.desktop, was developed using an incremental, phased approach that enables users to have up-to-date access to financial information needed to make informed business decisions. The tool was developed by campus-wide user task groups, led by the University Services Renewal (USER) Project. One of the keys to success of a USER-led project is the involvement of campus units, central offices, and key business owners in the planning, design, development, and implementation of the product.

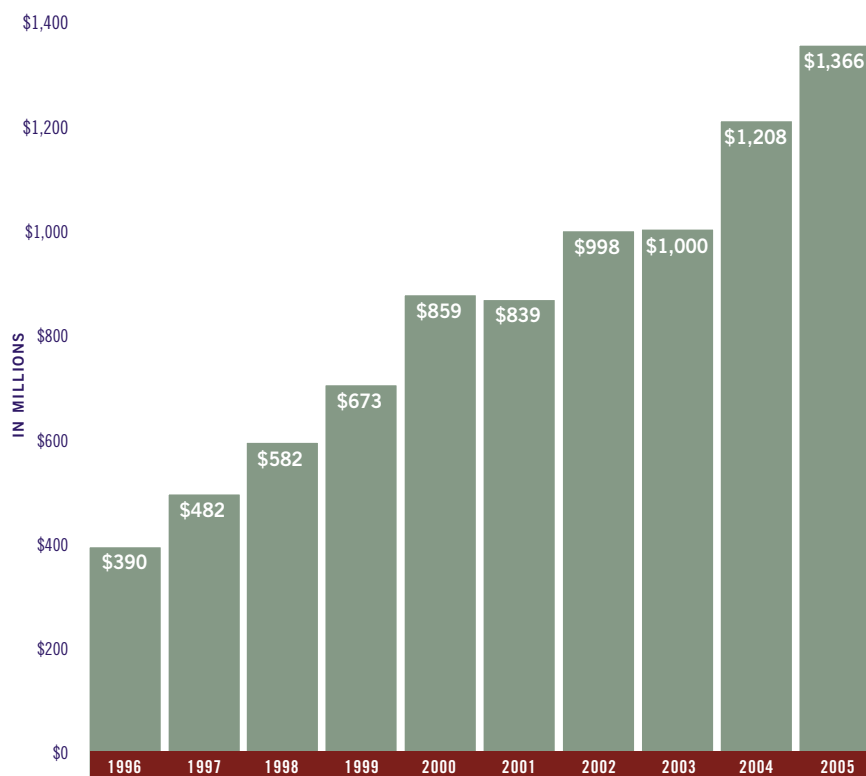
The launch of the new reporting application is a large step in moving the University closer to a vision where financial information and tools are available to users on any desktop, at any time. Prior to MyFinancial.desktop, expense reports, for example, were only available on a monthly basis, several weeks after the end of a month. Thus, information was dated, incomplete, and the format was inadequate to meet today's complex business needs. In addition, with the University's expanding global activities, researchers and staff are traveling the world as far as Australia, the former Soviet Union, Africa, Italy, and elsewhere. MyFinancial.desktop makes possible easy access to critical financial information anywhere an internet connection is available. Data is updated daily, displayed in a more user-friendly format, and can be queried and downloaded into user-tailored reports.

The University can look forward to using MyFinancial.desktop and its future enhancements to even more effectively and efficiently support the financial and stewardship responsibilities critical to achieving the University's research, teaching, and public service missions.

Investments

- Investment returns provide an important source of revenue for the University’s programs. Among the funds invested by the University are endowments, life income trusts and annuities, outright gifts, reserve balances, and excess cash.
- Endowed gifts for current use provide permanent capital and an ongoing stream of current earnings to the University. Programs supported by the endowment include undergraduate scholarships, graduate fellowships, professorships and chairs, and research activities.
- Most endowments are commingled in the Consolidated Endowment Fund (CEF), a balanced investment fund. As in a mutual fund, each individual endowment maintains a separate identity and owns units in the fund. On June 30, 2005, the fair market value of the CEF was \$1.4 billion, representing the investments of 2,036 individual endowments.
- During fiscal year 2002, the Board of Regents approved the investment of a portion of the University’s operating funds to establish an endowment. These funds currently comprise \$338 million of the CEF market value.
- Endowed program support over the last five years totaled \$269 million. During that period, the average annual total return on the CEF was 4 percent.
- Non-endowed gifts, reserve balances, and cash are commingled for investment purposes although accounted for separately. The fair market value of these investments at the end of the fiscal year was \$646 million. The total return has averaged 6.0 percent annually over the last five years.

Growth of Consolidated Endowment Fund: 1996-2005





Professorship opens doors to better futures

A recurring theme—giving people the tools they need to be successful—runs through University of Washington Computer Science & Engineering professor Richard Ladner’s research and his interactions with his students. One of his current research interests, the Tactile Graphics Project, grew out of his desire to help a blind graduate student named Sangyun Hahn read the charts and graphs in his textbooks. Since 2003, this effort to create a system for translating scientific illustrations into Braille has involved more than a dozen UW students, including Hahn and a variety of undergraduates, in addressing real research problems in need of workable solutions.

“There’s a benefit for the project because the students contribute,” says Ladner, who has taught at the UW since 1971, “and then the students of course get a benefit. That’s the way it should happen, right? They both benefit.”

Matt Renzelmann ('05), who worked on the project for more than a year before earning his bachelor’s degree last summer, says the research and the professor helped confirm his plans to go on to graduate school. “It really has been a life-changing experience, doing research with faculty. It has introduced me to professional literature and exposed to me all these advanced topics. Professor Ladner has done a lot for me.”

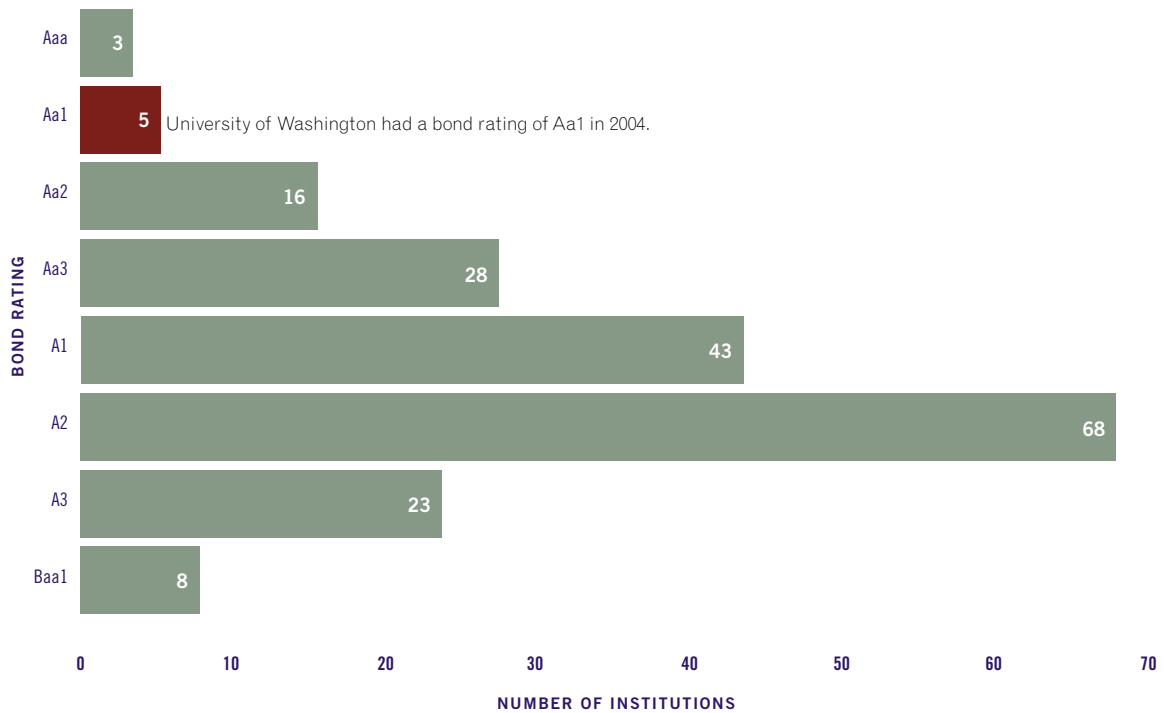
Ladner says he is able to do even more for students now that he’s the Boeing Endowed Professor in Computer Science & Engineering, an appointment he has held since 2004. “It gives me this freedom I’ve never had before where I had to think about ‘how can I fund that’ or ‘how can I get that student to work with me.’ Suddenly I have that ability to just move on a dime. I think it’s really increased my productivity.”

Richard Ladner was honored at the White House last May when he received the Presidential Award for Excellence in Science, Mathematics, and Engineering Mentoring.

Debt Financing

- The University’s General Revenue borrowing platform, established in 2003, has been used to fund research facilities on campus and at South Lake Union. Both Standard and Poor’s and Moody’s have recognized the financial strength of the General Revenue platform with their second highest bond rating, Aa1 from Moody’s and AA+ from Standard & Poor’s. These ratings put the UW in elite company; only three other public universities have a higher rating and just four others have the same rating.
- Strong ratings carry substantial advantages for the UW: continued and better access to capital markets when the University issues debt, lower interest rates on bonds, and the ability to negotiate favorable bond terms.
- The University takes seriously its role of financial stewardship and works hard to manage its financial resources effectively. Continued high debt ratings are important indicators of the University’s success in this area.

Moody’s 2004 Public College and University Ratings





General Revenue Bonds — Funding the Future

The University's local authority to finance research buildings was put to its first use in fiscal year 2005 with the sale of UW General Revenue Bonds for the William H. Foege Bioengineering/Genome Sciences and Research & Technology Buildings. Both facilities will be used for basic and applied research in the sciences. They were funded through a combination of gifts, capital grants, and tax exempt borrowing. The tax-exempt borrowing utilized the University's strongest credit to achieve the lowest cost of funds for the buildings.

Aside from the Aa1 rated General Revenue borrowing platform, the University utilized an interest rate "swap" to further reduce borrowing costs. An interest rate swap agreement is a contract between the University and a counterparty where the University pays a fixed rate of interest in exchange for a variable rate of interest. By entering into this agreement, the University has been able to reduce overall interest costs by over \$300,000 in just the first 12 months after the bonds were sold.

Looking forward, the University is evaluating ways to broaden the General Revenue platform to reduce borrowing costs to support campus capital needs beyond research. By viewing the University's outstanding debt holistically, it is possible to minimize the cost of borrowing on an institutional basis.

Capital Budget and Campus Construction

The University's capital projects continue the overall strategy to balance the need to restore and renew aging facilities with the need to grow by providing modern facilities for world-class excellence in research and teaching.

Major projects in progress in 2005 include the following:

William H. Foege BioEngineering/ Genome Sciences Building

Construction of this building will provide 265,000 square feet of modern facilities for research and teaching, leading the world in transforming healthcare and blazing paths into uncharted territories of science and medicine and addressing leading edge questions in biology and medicine.

The Educational Outreach Building

Construction of 55,000 square feet will provide a single point of contact for the public for Educational Outreach, and the Visitors Information and Welcome Centers. Educational Outreach, housed in a leased building until it was destroyed by fire in December 2002, will consolidate operations currently located in multiple leased buildings. The Visitor's Information and Welcome Centers will be located on the first floor of this building. The project cost of approximately \$18 million is funded by Educational Outreach, Parking, and other University revenue sources.

Architecture Hall Renovation

Constructed in 1909 for the Alaska-Yukon Pacific Exposition, Architecture Hall is the only surviving major Exposition building that has maintained its original appearance. Improvements include seismic, life safety and accessibility upgrades, hazardous materials abatement, and replacement of all major infrastructure systems. This

47,500 square foot renovation of approximately \$24 million was state funded and will continue to house Construction Management, Architecture, general assignment classrooms, architecture studios, and a 310 seat auditorium. This building, along with Guggenheim Hall, is part of the second phase of a series of renovation projects to restore critical facilities at the Seattle campus.

Guggenheim Hall Renovation

Renovation of 56,200 square feet will upgrade all major building systems, address seismic and accessibility deficiencies, correct life-safety conditions, abate asbestos, and provide updated facilities for Aeronautics and Astronautics, Applied Math, and general assignment classrooms including a 300 seat auditorium. State funding of approximately \$28 million was provided for this renovation.

Warren G. Magnuson Health Sciences Center H-Wing Renovation

The phased renovation of the original H-Wing coordinates several projects funded from state, National Institute of Health federal facilities grants, and University sources. The building structure and major systems will be upgraded to provide updated space for School of Medicine departments such as the Department of Physiology and Biophysics and the Department of Biological Structure.

Tacoma Campus Garage and Housing

This new construction is a public/private partnership project that will provide apartments and parking for students, faculty, staff, and the public. The housing is privately owned and funded.



Research and Technology Building

New construction of approximately 153,000 square feet (a five story building and 24,000 square feet parking garage) will provide flexible, cost-effective facilities for expanding multi-disciplinary research initiatives that need to be located on the Seattle campus. The project cost for the basic building structure is approximately \$30 million and is funded by \$10 million of University funds, debt (to be

repaid from indirect cost recovery generated from grant and contract projects occupying the building), and parking revenues. The building construction will be completed in the spring of 2006. Researchers occupying space in this building participate in the design and build-out of specialized laboratories and equipment to be funded by their research projects.





Financial Statements

AND REQUIRED SUPPLEMENTARY INFORMATION

28

MANAGEMENT'S DISCUSSION AND ANALYSIS

33

INDEPENDENT AUDITORS' REPORT

FINANCIAL STATEMENTS:

34

BALANCE SHEETS

35

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

36

STATEMENTS OF CASH FLOWS

37

NOTES TO FINANCIAL STATEMENTS



Management's Discussion and Analysis

The following discussion and analysis provides an overview of the financial position and activities of the University of Washington ("University") for the years ended June 30, 2005 and 2004. This discussion has been prepared by management and should be read in conjunction with the financial statements and accompanying notes which follow this section.

Using the Financial Statements

The University's financial statements include the Balance Sheets, the Statements of Revenues, Expenses, and Changes in Net Assets, the Statements of Cash Flows, and the Notes to Financial Statements. These financial statements are prepared in accordance with Governmental Accounting Standards Board (GASB) principles, which establish standards for external financial reporting for public colleges and universities. GASB standards require that financial statements be presented on a consolidated basis in order to focus on the University as a whole.

Financial Health

BALANCE SHEETS

The Balance Sheets present the financial condition of the University at the end of the last two fiscal years and report all assets and liabilities of the University. A summarized comparison of the University's assets, liabilities, and net assets as of June 30, 2005, 2004, and 2003 follows:

	2005	2004 (in millions)	2003
Current assets	\$ 985	\$ 916	\$ 1,055
Noncurrent assets:			
Capital assets, net	2,309	2,182	2,110
Other	2,408	2,192	1,998
Total assets	5,702	5,290	5,163
Current liabilities	822	787	889
Noncurrent liabilities	857	759	734
Total liabilities	1,679	1,546	1,623
Net assets	\$ 4,023	\$ 3,744	\$ 3,540

Current assets consist primarily of cash, short-term investments, collateral from securities lending, and accounts receivable.

Total current assets increased by \$69 million, to \$985 million at June 30, 2005. The June 30, 2004 balance of \$916 million was a decrease of \$139 million from 2003. The current asset balance fluctuates primarily due to changes in the collateral from securities lending and short-term investments. The short-term portion of the University's investment portfolio can fluctuate based upon changes in investment mix and the expected short term needs for University funds. The excess of current assets over current liabilities of \$163 million in 2005 reflects the University's ability to meet its short-term obligations.

The difference between total assets and total liabilities—net assets, or "equity"—is one indicator of the current financial

condition of the University. The change in net assets measures whether the overall financial condition has improved or deteriorated during the year.

The University reports its "equity" in the following categories:

- **Invested in Capital Assets, net of related debt** – This is the University's total investment in property, plant, equipment and infrastructure, net of accumulated depreciation and outstanding debt obligations related to those capital assets;
- **Restricted Net Assets:**
 - Nonexpendable net assets consist of funds on which the donor or external party has imposed the restriction that the corpus is not available for expenditures but rather for investment purposes only;
 - Expendable net assets are resources which the University is legally or contractually obligated to spend in accordance with time or purpose restrictions placed by donors and/or other external parties;
- **Unrestricted Net Assets** – are all other funds available to the institution for any purpose. Unrestricted assets are often internally designated for specific purposes.

The University's net assets at June 30, 2005, 2004, and 2003 are summarized as follows:

	2005	2004 (in millions)	2003
Invested in capital assets, net of related debt	\$ 1,609	\$ 1,539	\$ 1,512
Restricted:			
Nonexpendable	628	544	498
Expendable	990	933	833
Unrestricted	796	728	697
Total net assets	\$ 4,023	\$ 3,744	\$ 3,540

Net investment in capital assets increased \$70 million in 2005 and \$27 million in 2004. This balance increases as debt is paid off or when the University funds fixed asset purchases without financing. This balance decreases as assets are depreciated. The increase each year demonstrates that the University continues to invest in its buildings and plant, and represents a continuing investment in facilities for education and research.

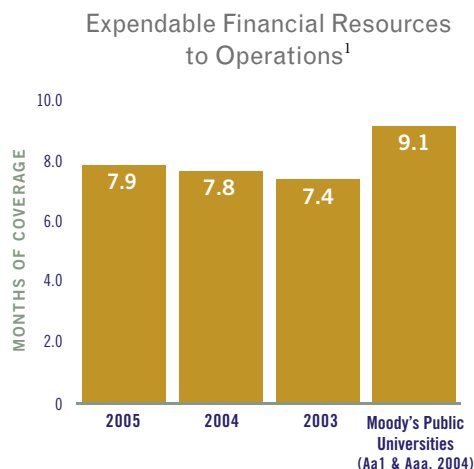
Restricted nonexpendable net assets increase as additional permanent endowment gifts are received. Increases in 2005 and 2004 are a result of new endowment gifts as well as recoveries of prior period decreases in original corpus value.

Restricted expendable net assets grew \$57 million, or 6% in 2005, and \$100 million, or 12% in 2004 as a result of new operating and capital gifts and earnings on endowments.

Unrestricted Net Assets in 2005 increased by \$68 million, or an increase of 9% over 2004. The Unrestricted Net Asset growth in 2004 over 2003 was \$31 million, or 4%. The increase in 2005 was due to continuing tuition increases, indirect cost recoveries on grant expenditures, and a strong investment return, offset by

capital expenditures. The increase in 2004 was driven by the same factors; however, the growth was reduced by a significant settlement payment of \$26 million.

The ratio of expendable financial resources to operations (as defined by Moody's) measures the strength of Net Assets. This ratio, illustrated in the chart below, shows that as of June 30, 2005, 2004, and 2003 the University had enough expendable resources from various sources to fund operations for over seven months.



Endowment and Other Investments

The Consolidated Endowment Fund (CEF) returned 12.5%, ending the year at \$1.4 billion, compared to a return of 17.8% in the prior year. In fiscal year 2002, the Board of Regents approved the investment of a portion of the University's operating funds into the CEF. These funds comprise \$338 million of the CEF market value. Over the past ten years, the CEF averaged an 11.4% return and stands in the top half of the Cambridge Associates College and University peer group.

The Invested Funds (IF), or operating monies of the University, returned 3.7% for fiscal year 2005 and 0.1% in 2004, ending the 2005 fiscal year with a market value of \$646 million.

Capital Improvements and Related Debt

In 2005, total long-term debt associated with capital assets increased to \$753 million, an increase of \$98 million over 2004. The largest bond issues in 2005 were: \$60 million in bonds to finance the construction of the new Research and Technology Building, and to finance the completion of the William H. Foege BioEngineering/Genome Sciences Building; a \$38 million issuance to finance Phase I of the South Lake Union Blue Flame construction; and a \$16 million bond issue to finance the expansion of the West Campus Garage.

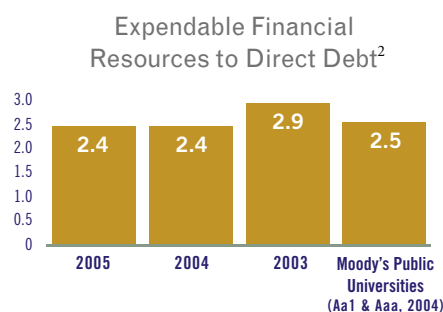
In 2004, total long-term debt associated with capital assets increased to \$655 million, a \$34 million increase over 2003. New debt in 2004 provided funding to begin construction of the new

William H. Foege BioEngineering/Genome Sciences Building and renovations to student residence halls.

Expenditures on capital construction were \$184 million in 2005; the largest of these were \$70 million for the new Bioengineering Building/Genome building, \$32 million for the renovation of Johnson Hall, and \$13 million on the new Research & Technology Building.

Expenditures on capital construction in 2004 were almost \$150 million and included costs associated with the William H. Foege BioEngineering/Genome Sciences Building, student hall renovations, Tacoma campus reconstruction, UWMC Surgery Pavilion, William Gates Hall, and expansion of the Intramural Activities (IMA) facility.

The expendable financial resources to direct debt ratio (as defined by Moody's) shows that the University has sufficient expendable resources to pay its long-term debt obligations.



STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

The Statements of Revenues, Expenses, and Changes in Net Assets present the University's results of operations and non-operating items that result in the changes in Net Assets for the year. In accordance with GASB reporting principles, revenues and expenses are classified as either operating or nonoperating. A condensed comparison of the University's revenues, expenses, and changes in net assets for the years ended June 30, 2005, 2004, and 2003 follows:

	2005	2004 (in millions)	2003
Total operating revenues	\$ 2,298	\$ 2,155	\$ 2,025
Operating expenses	2,747	2,573	2,418
Operating loss	(449)	(418)	(393)
Nonoperating revenues, net of expenses	567	529	521
Other revenues	161	93	106
Increase in net assets	279	204	234
Net assets, beginning of year	3,744	3,540	3,306
Net assets, end of year	\$ 4,023	\$ 3,744	\$ 3,540

¹ The sum of Unrestricted Net Assets and Restricted Expendable Net Assets, divided by Total Operating Expenses (Operating Expenses less scholarship expense plus interest expense). The result is multiplied by 12 to arrive at months of coverage.

² The sum of Unrestricted Net Assets and Restricted Expendable Net Assets, divided by total capital leases, bonds, and notes payable outstanding.

The University has a diversified revenue base. No single source generated more than 31% of the total fiscal 2005 revenues of \$3.1 billion. The following table summarizes revenues from all sources for the years ended June 30, 2005, 2004, and 2003:

	2005	2004 (in millions)	2003
Tuition	\$ 332	\$ 304	\$ 282
Patient Services	747	689	636
Grants and Contracts	954	896	843
Sales and Services of Educational Departments	90	89	85
Auxiliary	117	126	119
State Funding for Operations	323	310	333
Gifts	172	122	170
Investment income	219	220	88
State Funding for Capital Projects	56	33	61
Other	59	52	59
Total revenue – all sources	\$ 3,069	\$ 2,841	\$ 2,676

Grant Revenue

The largest source of revenues has been from grants and contracts. This revenue has increased 6% in both 2005 and 2004. The University receives more dollar awards of federal grants and contracts than any other public institution in the country. This revenue is earned only when direct expenditures (such as researchers' compensation or purchases of goods and services) are made; therefore, there is little effect to the University's operating margin as a result of this direct expense reimbursement process.

Facility and administrative expenses necessary to support grants and contracts are reimbursed by an indirect cost recovery. The current federal indirect cost recovery is approximately 30 cents on every direct expenditure dollar on these grants and contracts.

Primary Non-Grant Funding Sources

The University relies primarily on student tuition and fees and state appropriations as revenue sources to support its non-grant funded educational operating expenses. Tuition revenue, net of scholarship allowances, has continued to grow, increasing from \$304 million in fiscal year 2004 to \$332 million in the 2005 fiscal year, an increase of 9%. The impact to students as a result of this tuition rate increase was partially offset by the increase in scholarships (including scholarship allowances) of \$5 million in 2005. The University has flexibility in its ability to set non-undergraduate resident tuition rates, which helps to compensate for shortfalls in state funding.

State appropriations are considered nonoperating revenue under GASB 35 standards and are reflected in the nonoperating section of the income statement; however, they are used solely for operating purposes.

Patient Services

Revenues from patient services increased \$58 million, or 8%, from \$689 million in 2004 to \$747 million in 2005. In 2004,

patient revenues increased \$53 million, or 8% over the previous year. Revenues increased due to both patient volume and price increases during both years. Volume increases were primarily in surgery, oncology, and other tertiary care service areas.

Gifts and Endowments and Other Investments

Investment income and gifts continue to provide the University with an added margin of excellence and the flexibility to respond to special opportunities. Income from these two sources was the difference between growth and loss in net assets.

Net investment returns for the years ended June 30, 2005, 2004, and 2003 consisted of the following components:

	2005	2004 (in millions)	2003
Interest and dividends	\$ 59	\$ 56	\$ 65
Metropolitan Tract operating income	9	9	12
Net appreciation (depreciation) of fair value of investments	158	162	18
Investment expenses	(7)	(7)	(7)
Net investment income	\$ 219	\$ 220	\$ 88

Net appreciation includes both realized and unrealized gains and losses. Net investment income remained relatively strong in 2005. In 2004, net investment income increased by \$132 million over 2003, or 150%, due primarily to the \$162 million net appreciation in the fair value of the investments.

The University continues to receive strong support from its donors. Gift revenue in 2005 amounted to \$172 million. This is an increase of \$50 million from the prior year. In 2004, gift revenue decreased by \$48 million from 2003; however, there was an individual gift in 2003 of over \$70 million. Gifts are used to support a variety of purposes, including capital improvements, scholarships, research, and endowments for various academic and research chairs.

Expenses

A comparative summary of the University's expenses by functional classification for the years ended June 30, 2005, 2004, and 2003 is as follows:

	2005	2004 (in millions)	2003
Operating expenses:			
Instruction	\$ 670	\$ 595	\$ 594
Research	575	553	501
Public service	30	23	21
Academic support	192	186	166
Student services	27	26	25
Institutional support	113	103	97
Operation and maintenance of plant	148	146	155
Scholarships and fellowships	57	54	51
Auxiliary enterprises	132	124	128
Medical related	624	590	527
Depreciation	179	173	153
Total operating expenses	\$ 2,747	\$ 2,573	\$ 2,418

The University's operating expenses increased \$174 million in 2005 and \$155 million in 2004. Consistent with the increase in tuition revenues and operating state appropriation dollars, instruction and academic support expenses increased \$81 million or 10% in 2005 over the prior year. Departmental research, which is classified as instructional, also increased in the current year. Research expenditures, which represent sponsored research, increased \$22 million or 4% from the prior year.

Of the \$174 million increase in operating expenses, \$101 million related to salaries and benefits. Salaries and benefits increased approximately 6%, versus a \$102 million, or 7% increase in the prior year. The increase is due to both additional employees as well as increased salary levels.

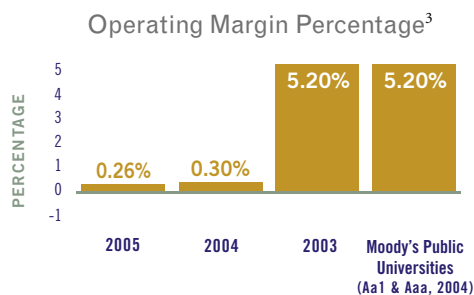
Supplies, materials, and services increased \$63 million or 11%, versus an increase of \$22 million or 4% in the prior year. The growth in these categories is heavily impacted by the growth in grant and contract revenues, especially international research and training. Increases in service expense in particular reflect the growth in international activities and subcontracting of awards as well as increases in the Medical Center.

Depreciation expense increased \$6 million in 2005, compared to a \$20 million increase in 2004. In 2005, \$70 million in buildings were placed into service, versus \$458 million in 2004.

OPERATING LOSS

The University's operating loss increased to \$449 million in 2005 from \$418 million in 2004 and from \$393 million in 2003. As discussed above, GASB standards require that state appropriations, which are used solely for operations, be classified as nonoperating, thus creating the significant loss. If state appropriations were classified as operating, the operating loss would be as follows for 2005, 2004, and 2003, respectively: \$125 million, \$108 million, and \$60 million. Thus, of the \$31 million increase in operating loss from 2004 to 2005, all but \$17 million was funded by increases in state appropriations. The University continues to rely upon nonoperating revenues other than operating state appropriations to fund its operations, including operating gift revenues and investment income.

The net result of revenue and expense activity is measured by the operating margin (as defined by Moody's, which considers several nonoperating revenue categories in determining the margin). The margin remained relatively consistent in 2005 versus 2004. The operating margin includes an estimated spending rate of the University's investments rather than actual investment income. Therefore, strong investment performance in a given year will not necessarily increase the operating margin.



Economic Factors That Will Affect the Future

The University's funding comes primarily from four general sources: research grants and contracts, revenues from patient services, state appropriations, and tuition and fees.

State funding levels continue to put pressure on the instructional function of the University. However, the ability to increase certain tuition rates, along with continued strong demand for services, offsets much of that pressure.

³ Operating loss, (including interest expense, operating appropriations, an assumed 4.5% spending rate on investments, and non-permanent endowment gifts), divided by operating revenues (less scholarship expenses, and including operating appropriations, an assumed 4.5% spending rate on investments, and non-permanent endowment gifts).





INDEPENDENT AUDITORS' REPORT

The Board of Regents
University of Washington:

We have audited the accompanying financial statements of the University of Washington, an agency of the State of Washington, as of and for the years ended June 30, 2005 and 2004, as listed in the table of contents. 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 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we express no such opinion. An audit also 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, 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 financial statements referred to above present fairly, in all material respects, the financial position of the University of Washington as of June 30, 2005 and 2004, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 28 through 31 and the supplemental component pension information on page 44 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

Seattle, Washington
November 4, 2005

Balance Sheets

	June 30,	
ASSETS	2005	2004
CURRENT ASSETS:		
CASH AND CASH EQUIVALENTS (NOTE 2)	\$ 45,759	\$ 35,880
COLLATERAL FROM SECURITIES LENDING (NOTE 6)	339,231	318,277
SHORT-TERM INVESTMENTS (NOTE 6)	201,845	211,026
ACCOUNTS RECEIVABLE (NET OF \$72,936 AND \$74,516 ALLOWANCE) (NOTE 5)	367,794	324,907
INVENTORIES	23,639	22,014
OTHER CURRENT ASSETS	6,865	3,653
TOTAL CURRENT ASSETS	985,133	915,757
NONCURRENT ASSETS:		
DEPOSIT WITH STATE OF WASHINGTON (NOTE 3)	54,784	58,500
LONG-TERM INVESTMENTS (NOTE 6)	2,127,451	1,914,293
METROPOLITAN TRACT (NOTE 7)	118,331	117,454
STUDENT LOANS RECEIVABLE (NET OF \$8,135 AND \$7,935 ALLOWANCE) (NOTE 4)	60,755	59,668
OTHER NONCURRENT ASSETS	47,198	42,479
CAPITAL ASSETS (NET OF \$1,752,581 AND \$1,620,094 ACCUMULATED DEPRECIATION) (NOTE 8)	2,308,665	2,182,077
TOTAL NONCURRENT ASSETS	4,717,184	4,374,471
TOTAL ASSETS	\$ 5,702,317	\$ 5,290,228
LIABILITIES		
CURRENT LIABILITIES:		
ACCOUNTS PAYABLE	\$ 112,841	\$ 92,600
ACCRUED LIABILITIES	193,551	184,551
PAYABLES: SECURITIES LENDING TRANSACTIONS (NOTE 6)	339,231	318,277
DEFERRED REVENUE	113,729	102,109
FUNDS HELD FOR OTHERS	19,803	11,295
SHORT-TERM NOTES PAYABLE	-	27,488
LONG-TERM LIABILITIES – CURRENT PORTION (NOTES 9,10, AND 11)	42,921	50,828
TOTAL CURRENT LIABILITIES	822,076	787,148
NONCURRENT LIABILITIES:		
DEFERRED REVENUE	4,373	4,685
U.S. GOVERNMENT GRANTS REFUNDABLE	50,173	49,720
LONG-TERM LIABILITIES, NET OF CURRENT PORTION (NOTES 9,10, AND 11)	803,016	704,348
TOTAL NONCURRENT LIABILITIES	857,562	758,753
TOTAL LIABILITIES	1,679,638	1,545,901
NET ASSETS		
INVESTED IN CAPITAL ASSETS, NET OF RELATED DEBT	1,608,876	1,538,941
RESTRICTED FOR:		
NONEXPENDABLE – SCHOLARSHIPS, RESEARCH, AND DEPARTMENT USES	628,356	543,679
EXPENDABLE – SCHOLARSHIPS, RESEARCH, AND DEPARTMENT USES	989,261	933,198
UNRESTRICTED	796,186	728,509
TOTAL NET ASSETS	4,022,679	3,744,327
TOTAL LIABILITIES AND NET ASSETS	\$ 5,702,317	\$ 5,290,228

See accompanying Notes to Financial Statements

Dollars in thousands

Statements of Revenues, Expenses, and Changes in Net Assets

	For the Year Ended June 30,	
	2005	2004
REVENUES		
OPERATING REVENUES:		
STUDENT TUITION AND FEES (NET OF SCHOLARSHIP ALLOWANCES OF \$48,123 AND \$46,519)	\$ 331,978	\$ 304,189
PATIENT SERVICES (NET OF CHARITY CARE AND UNCOLLECTIBLE ACCOUNTS OF \$21,115 AND \$18,089)	746,675	688,521
FEDERAL GRANTS AND CONTRACTS	813,643	758,427
STATE AND LOCAL GRANTS AND CONTRACTS	47,807	49,139
NONGOVERNMENTAL GRANTS AND CONTRACTS	92,737	87,986
SALES AND SERVICES OF EDUCATIONAL DEPARTMENTS	89,617	88,579
AUXILIARY ENTERPRISES:		
HOUSING AND FOOD SERVICES	41,176	40,921
PARKING SERVICES	7,012	7,282
SPORTS PROGRAMS (NET OF SCHOLARSHIP ALLOWANCES OF \$1,996 AND \$1,905)	28,783	34,574
OTHER AUXILIARY ENTERPRISES	39,886	43,088
OTHER MEDICAL CENTER REVENUE	36,949	32,171
OTHER OPERATING REVENUE	21,646	19,876
TOTAL OPERATING REVENUES	2,297,909	2,154,753
EXPENSES		
OPERATING EXPENSES:		
SALARIES	1,385,085	1,311,585
BENEFITS	361,104	333,908
SCHOLARSHIPS AND FELLOWSHIPS	56,647	53,566
UTILITIES	47,777	41,354
SUPPLIES AND MATERIALS	270,300	266,699
PURCHASED SERVICES	362,367	302,475
DEPRECIATION	178,704	172,567
OTHER	84,433	90,716
TOTAL OPERATING EXPENSES	2,746,417	2,572,870
OPERATING LOSS	(448,508)	(418,117)
NONOPERATING REVENUES (EXPENSES)		
STATE APPROPRIATIONS	323,417	309,618
GIFTS	67,378	62,311
INVESTMENT INCOME (NET OF INVESTMENT EXPENSE OF \$6,971 AND \$6,873)	219,069	219,831
INTEREST ON CAPITAL ASSET-RELATED DEBT	(35,060)	(27,624)
OTHER NONOPERATING REVENUES AND EXPENSES	(8,402)	(35,370)
NET NONOPERATING REVENUES	566,402	528,766
INCOME BEFORE OTHER REVENUES, EXPENSES, GAINS, OR LOSSES	117,894	110,649
CAPITAL APPROPRIATIONS	56,149	33,395
CAPITAL GRANTS AND GIFTS	35,658	26,986
GIFTS TO PERMANENT ENDOWMENTS	68,651	33,112
TOTAL OTHER REVENUE	160,458	93,493
INCREASE IN NET ASSETS	278,352	204,142
NET ASSETS		
NET ASSETS-BEGINNING OF YEAR	3,744,327	3,540,185
NET ASSETS-END OF YEAR	\$ 4,022,679	\$ 3,744,327

See accompanying Notes to Financial Statements

Dollars in thousands

Statements of Cash Flows

	For the Year Ended June 30,		For the Year Ended June 30,	
	2005	2004	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES				
STUDENT TUITION AND FEES	\$ 319,671	\$ 292,071		
PATIENT SERVICES	733,090	696,934		
GRANTS AND CONTRACTS	940,836	894,242		
PAYMENTS TO SUPPLIERS	(263,556)	(288,373)		
PAYMENTS FOR UTILITIES	(46,206)	(40,582)		
PURCHASED SERVICES	(356,788)	(313,008)		
OTHER OPERATING DISBURSEMENTS	(84,713)	(91,874)		
PAYMENTS TO EMPLOYEES	(1,381,813)	(1,308,502)		
PAYMENTS FOR BENEFITS	(344,818)	(313,074)		
PAYMENTS FOR SCHOLARSHIPS AND FELLOWSHIPS	(56,647)	(53,566)		
LOANS ISSUED TO STUDENTS	(30,224)	(29,356)		
COLLECTION OF STUDENT LOANS	28,684	28,613		
SALES AND SERVICES OF THE MEDICAL CENTER	36,949	32,171		
AUXILIARY ENTERPRISE RECEIPTS	116,268	122,228		
SALES AND SERVICES OF EDUCATIONAL DEPARTMENTS	91,514	87,251		
OTHER RECEIPTS	12,899	13,797		
NET CASH USED BY OPERATING ACTIVITIES	(284,854)	(271,028)		
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
STATE APPROPRIATIONS	321,679	308,920		
GIFTS, EXCLUDING PERMANENT ENDOWMENT AND CAPITAL	67,378	62,311		
ADDITIONS TO PERMANENT ENDOWMENTS	68,651	33,112		
DIRECT LENDING RECEIPTS	155,986	123,558		
DIRECT LENDING DISBURSEMENTS	(142,123)	(137,482)		
RECEIPTS FROM OUTSIDE AFFILIATED AGENCIES	387,003	377,737		
DISBURSEMENTS TO OUTSIDE AFFILIATED AGENCIES	(393,700)	(364,914)		
OTHER	(47,041)	(23,304)		
NET CASH PROVIDED BY NONCAPITAL FINANCING ACTIVITIES	417,833	379,938		
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES				
PROCEEDS FROM CAPITAL DEBT	174,889	75,170		
CAPITAL APPROPRIATIONS	52,297	31,101		
CAPITAL GRANTS AND GIFTS RECEIVED	35,658	26,986		
PURCHASES OF CAPITAL ASSETS	(310,036)	(265,056)		
PRINCIPAL PAID ON CAPITAL DEBT AND LEASES	(76,462)	(28,716)		
INTEREST PAID ON CAPITAL DEBT AND LEASES	(38,299)	(32,094)		
OTHER	5,107	(11,398)		
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	(156,846)	(204,007)		
CASH FLOWS FROM INVESTING ACTIVITIES				
PROCEEDS FROM SALES OF INVESTMENTS	2,256,225	2,486,309		
PURCHASES OF INVESTMENTS	(2,284,336)	(2,444,302)		
INVESTMENT INCOME	61,857	58,171		
NET CASH PROVIDED BY INVESTING ACTIVITIES	33,746	100,178		
NET INCREASE IN CASH AND CASH EQUIVALENTS	9,879	5,081		
CASH AND CASH EQUIVALENTS – BEGINNING OF THE YEAR	35,880	30,799		
CASH AND CASH EQUIVALENTS – END OF THE YEAR	\$ 45,759	\$ 35,880		
RECONCILIATION OF OPERATING LOSS TO NET CASH USED BY OPERATING ACTIVITIES				
OPERATING LOSS	\$ (448,508)	\$ (418,117)		
ADJUSTMENTS TO RECONCILE OPERATING LOSS TO NET CASH USED BY OPERATING ACTIVITIES:				
DEPRECIATION EXPENSE	178,704	172,567		
CHANGES IN ASSETS AND LIABILITIES:				
RECEIVABLES	(33,764)	16,454		
INVENTORIES	(1,625)	(732)		
OTHER ASSETS	(7,931)	(6,797)		
ACCOUNTS PAYABLE	21,988	(11,509)		
DEFERRED REVENUE	11,308	(13,523)		
OTHER LONG-TERM LIABILITIES	(3,486)	(8,628)		
U.S. GOVERNMENT GRANTS REFUNDABLE	(453)	(961)		
LOANS TO STUDENTS	(1,087)	218		
NET CASH USED BY OPERATING ACTIVITIES	\$ (284,854)	\$ (271,028)		

See accompanying Notes to Financial Statements

Dollars in thousands

NOTE 1:

Summary of Significant Accounting Policies**FINANCIAL REPORTING ENTITY**

The University of Washington (University), an agency of the State of Washington, is governed by a ten-member Board of Regents, appointed by the Governor and confirmed by the state Senate.

The financial statements include the individual schools, colleges, and departments of the University, the University of Washington Medical Center, Portage Bay Insurance (a wholly owned subsidiary of the University), and certain affiliated operations determined to be a part of the University's financial reporting entity. Affiliated organizations are evaluated for inclusion in the reporting entity as component units based on the significance of their relationship with the University.

The University of Washington Alumni Association, University of Washington Physicians, University of Washington Physicians Network, Community Development Properties C-D, Educational Research Properties, Radford Court Properties, Twenty-Fifth Avenue Properties, and Washington Biomedical Research Properties I are included in the reporting entity as blended component units. These legally separate entities are included in the University's financial reporting entity because of the nature of their relationship to the University. Financial information for these affiliated organizations may be obtained from their respective administrative offices.

BASIS OF ACCOUNTING

The financial statements of the University have been prepared in accordance with Governmental Accounting Standards Board (GASB) Statement No. 34, Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments, as amended by GASB Statement No. 35, Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities; No. 37, Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments: Omnibus (an amendment of GASB Statements No. 21 and No. 34); and No. 38, Certain Financial Statement Note Disclosures. The University is reporting as a special purpose government engaged in business type activities (BTA). In accordance

with BTA reporting, the University presents a management's discussion and analysis, balance sheets, statements of revenues, expenses, and changes in net assets, statements of cash flows, and notes to the financial statements. The financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting.

Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred. All intra-agency transactions have been eliminated. The University has elected not to apply any FASB pronouncements after November 30, 1989. The University reports capital assets net of accumulated depreciation, and reports depreciation expense in the Statements of Revenues, Expenses, and Changes in Net Assets.

OTHER ACCOUNTING POLICIES

Investments. Investments other than real estate and miscellaneous investments are stated at fair value. Real estate and miscellaneous investments are stated at cost or, in the case of gifts, at fair values at the date of donation. Limited partnership investments are valued based upon the valuations provided by the respective general partners. Securities are valued at the last sale price on the last business day of the fiscal year, as quoted on a recognized exchange or an industry standard pricing service. Securities for which no sale was reported on the last day of business of the fiscal year are valued at the quoted market price of a dealer who regularly trades in the security.

Investments under long-term strategies are considered noncurrent. Short-term investments consist primarily of cash equivalents and fixed income vehicles with maturities of less than one year.

Securities Lending Transactions. Cash collateral received from borrowers through securities lending transactions is recorded as an asset with an offsetting liability.

Inventories. Inventories are carried at the lower of cost or market value. Consumable inventories, consisting of expendable materials and supplies held for consumption, are generally valued using the weighted average method. Merchandise inventories are generally valued using the first-in, first-out method.

Capital Assets. Land, buildings, equipment, and library books are stated at cost or, if acquired by gift, at fair market value at the date of the gift. Additions, replacements, major repairs, and renovations are capitalized.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 15 to 50 years for building components, 20 to 50 years for infrastructure and land improvements, 15 years for library books, and five to seven years for equipment.

Capitalized construction-related interest was \$905,000 and \$4,950,000 during 2005 and 2004, respectively.

Deferred Revenues. Deferred revenues occur when funds have been collected in advance of an event, such as advance ticket sales, summer quarter tuition, and unspent cash advances on certain grants.

Deferred Giving – Split Interest Agreements. Under these agreements, donors make initial gifts to trusts or directly to the University. The University has beneficial interests but is not the sole beneficiary. The University records an asset related to these agreements at fair market value at year end. The University also records a liability related to the split-interest agreements equal to the present value of expected future distributions; the discount rates applied range from 4.4% to 8.0%.

Compensated Absences. University employees accrue annual leave at rates based on length of service, and for sick leave at the rate of one day per month. Annual leave accrued as of June 30, 2005 and 2004 of \$51,461,000 and \$49,214,000, respectively, was included in accrued liabilities. Sick leave accrued as of June 30, 2005 and 2004 was \$21,255,000 and \$20,751,000, respectively.

In fiscal year 2004, the University changed its method of estimating annual leave and sick leave. This resulted in additional employee benefits expense of \$7,134,000 of annual leave and \$5,461,000 of sick leave. These amounts are included in the fiscal year 2004 statement of revenues, expenses, and changes in net assets.

Tuition and Fees. Tuition and Fees are reported net of scholarship allowances applied to students' accounts, while student aid paid directly to students is reported as scholarship and fellowship expenses.

State Appropriations. The State of Washington appropriates funds to the University on both annual and biennial bases. These revenues are reported as nonoperating revenues in the Statements of Revenues, Expenses, and Changes in Net Assets. The University of Washington Medical Center received \$8,293,000 and \$8,306,000 in operating state appropriations in 2005

and 2004, respectively. These amounts are included in other Medical Center revenue in the Statements of Revenues, Expenses, and Changes in Net Assets.

Operating Activities. The University’s policy for reporting operating activities in the Statements of Revenues, Expenses, and Changes in Net Assets is to include activities that generally result from exchange transactions. Examples of exchange transactions are payments received or made for an exchange of goods or services. Certain other significant revenue streams used for operations, such as state appropriations, gifts and investment income are recorded as nonoperating revenues, as prescribed by GASB 35.

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

Invested in capital assets, net of related debt: The University’s investments in capital assets, less accumulated depreciation, net of outstanding debt obligations related to capital assets;

Restricted net assets – nonexpendable: Net assets subject to externally-imposed requirements that they be maintained permanently by the University, including permanent endowment funds;

Restricted net assets – expendable: Net assets which the University is obligated to spend in accordance with restrictions imposed by external parties;

Unrestricted net assets: Net assets not subject to externally imposed restrictions, but which may be designated for specific purposes by management, or the Board of Regents.

Tax Exemption. The University is exempt from tax under Section 115 of the Internal Revenue Code on income related to the University’s mission.

Reclassifications. Certain amounts in the 2004 financial statements have been reclassified for comparative purposes to conform to the presentation in the 2005 financial statements.

NOTE 2:

Cash and Cash Equivalents

Cash includes petty cash, bank deposits, cash held by fiscal agents, and cash held by escrow agents. Amounts held by escrow agents were \$17,620,000 and \$10,530,000 in 2005 and 2004, respectively. Most cash, except for cash held at the University, is covered by federal depository insurance (FDIC) or by collateral

held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (PDPC). At June 30, 2005 and 2004, bank balances of \$1,341,000 and \$764,000, respectively, were insured by the FDIC and balances of \$62,766,000 and \$22,037,000, respectively, were collateralized under the PDPC.

NOTE 3:

Deposit with State of Washington

State law requires the University to deposit certain funds with the state treasurer, who holds and invests the funds. The deposits include: amounts held for the University’s permanent land grant funds, the University of Washington building fee, and certain general obligation bonds reserve funds. The fair value of these funds approximates the carrying value.

NOTE 4:

Student Loans Receivable

Net student loans of \$60,755,000 and \$59,668,000 at June 30, 2005 and 2004, respectively, consist of \$50,173,000 and \$49,720,000 from federal programs and \$10,582,000 and \$9,948,000 from University programs. Interest income from student loans for the years ended June 30, 2005 and 2004, was \$967,000 and \$1,244,000, respectively. Loans are made primarily to students who reside in the state of Washington. The loans are unsecured and are expected to be repaid from earnings of the borrowers.

NOTE 5:

Accounts Receivable

The major components of accounts receivable as of June 30, 2005 and 2004, were:

	(Dollars in thousands)	
	2005	2004
PATIENT SERVICES	\$ 202,086	\$ 189,519
GRANTS AND CONTRACTS	140,835	118,038
PENDING INVESTMENT SALES	18,376	15,341
SALES AND SERVICES	7,166	9,064
TUITION	15,399	16,427
STATE APPROPRIATIONS	9,868	4,279
OTHER	47,000	46,755
TOTAL	440,730	399,423
LESS ALLOWANCE FOR DOUBTFUL ACCOUNTS	(72,936)	(74,516)
ACCOUNTS RECEIVABLE, NET	\$ 367,794	\$ 324,907

NOTE 6:

Investments

INVESTMENTS – GENERAL

The Board of Regents of the University of Washington is responsible for the management of the University’s investments. The Board establishes investment policy which is carried out by the Chief Investment Officer. The University of Washington Investment Committee (UWINCO), comprised of Board members and investment professionals, advise on matters relating to the management of the University’s investment portfolios.

The majority of the University’s investments are insured, registered, and held by the University’s custodial bank as an agent for the University. Investments not held by the custodian include lent securities, mutual funds, venture capital, private equity, distressed, marketable alternatives, mortgages, real estate, and miscellaneous investments.

INVESTMENT POOLS

The University combines most short-term cash balances into the Invested Funds Pool. At June 30, 2005, the Invested Funds Pool totaled \$646,428,000 compared to \$681,015,000 at June 30, 2004. The fund also owns units in the Consolidated Endowment Fund valued at \$337,787,000 on June 30, 2005 and \$289,859,000 on June 30, 2004. By University policy, departments with qualifying funds in the Invested Funds Pool receive income based on their average balances. The income rates are set by management based on the type of balance held and the realized return of the portfolio. Long-term deposits received 3.5% and 3.1% for fiscal years 2005 and 2004

respectively. Operating and plant fund balances of self-sustaining units received 3.2% and 2.8% for the years ending June 30, 2005 and 2004, respectively. Royalty accounts received 1.0% in 2004 and 2005, and gift accounts received 3.0% for both fiscal years. The difference between the actual earnings of the Invested Funds Pool and the calculated distributions is used to support activities benefiting all University departments.

The composition of the carrying amounts of investments by type at June 30, 2005 and 2004 are listed in Table 1.

The majority of the endowed funds are invested in a pooled fund called the Consolidated Endowment Fund (CEF). Individual endowments subscribe to or dispose of units in the pool on the basis of a per unit valuation of the CEF at fair value on the last business day of the calendar quarter. Income is distributed based on the number of units held. The CEF annual income distribution is 5% of the average fair value of the CEF for the previous three years. RCW 24.44.050 of the Washington State Code allows for the spending of appreciation in the CEF.

The University records its permanent endowments at the lower of original value or current market value in the Restricted Nonexpendable Net Assets category. Of the total of approximately \$775,000,000 and \$700,000,000 permanent endowment funds (at market value) as of June 30, 2005 and 2004, the aggregate amount of the deficiencies for all endowments where the fair value of the assets is less than the original gifts is \$2,849,000 and \$6,167,000 at June 30, 2005 and 2004, respectively.

Funds in irrevocable trusts managed by trustees other than the University are not reported in the financial statements. The fair value of these funds was approximately \$52,030,000 at June 30, 2005 compared to \$50,000,000 at June 30, 2004. Income received from these trusts was \$2,091,000 for the year ended June 30, 2005 and \$2,075,000 for the year ended June 30, 2004.

Net appreciation in the fair value of investments includes both realized and unrealized gains and losses on investments. During the fiscal years ended June 30, 2005 and 2004, the University realized net gains of \$117,406,000 and \$68,162,000, respectively, from the sale of investments. The calculation of realized gains and losses is independent of the net appreciation of the fair value of investments. Realized gains and losses on investments that have

been held in more than one fiscal year and are sold in the current year, include the net appreciation of these investments reported in the prior year(s). The net appreciation in the fair value of investments during the years ended June 30, 2005 and 2004, was \$158,229,000 and \$161,660,000, respectively.

SECURITIES LENDING

The University's investment policies permit it to lend its securities to broker dealers and other entities. The University's custodian lends securities for collateral in the form of cash or other securities, with the simultaneous agreement to return the collateral for the same securities in the future. U.S. securities are loaned and secured by collateral valued at 102% of the fair value of the securities plus any accrued interest. Non-U.S. securities are loaned and secured by collateral valued at 105% of the fair value of the securities plus any accrued interest. At year-end, the University had no credit risk exposure to borrowers because the amounts the University owed the borrowers exceeded the amounts the borrowers owed the University.

The contract with the custodian requires it to indemnify the University if the borrowers fail to return the securities (and if the collateral is inadequate to replace the securities lent) or fail to pay the University for income distributions by the securities' issuers while the securities are on loan.

Either the University or the borrower can terminate all securities loans on demand,

although the average term of overall loans is 87 days. Cash collateral is invested in a short-term investment pool which had an average weighted maturity of 28 days as of June 30, 2005. The relationship between the maturities of the investment pool and the University's loans is affected by the maturities of the securities loaned by other entities that use the custodian's pool. The University cannot determine the maturities of these loaned securities. The University cannot sell or pledge non-cash collateral unless the borrower defaults. Non-cash collateral at June 30, 2005 and 2004 was \$35,689,000 and \$54,524,000, respectively.

Securities on loan at June 30, 2005 and 2004, totaled \$360,879,000 and \$365,579,000, respectively, and are listed by investment type in Table 1. The securities lending program resulted in net revenues of \$651,000 for the year ended June 30, 2005 and \$615,000 for the year ended June 30, 2004.

INTEREST RATE RISK

The University manages interest rate risk through its investment policies and the investment guidelines established with each manager. Each fixed income manager is assigned a maximum boundary for duration as compared to the manager's relevant benchmark index. The goal is to allow ample freedom for the manager to perform, while controlling the interest rate risk in the portfolio. Modified duration, which estimates the sensitivity of a bond's price to interest rate changes, is based on Macaulay duration. Macaulay duration is the basic calculation developed for a portfolio

TABLE 1—UNIVERSITY INVESTMENTS AND COLLATERAL FROM SECURITIES LENDING (Dollars in thousands)

Investment Type	Carrying Value	
	June 30, 2005	June 30, 2004
CASH EQUIVALENTS	\$ 76,919	\$ 25,701
DOMESTIC FIXED INCOME	604,305	593,275
DOMESTIC FIXED INCOME – LOANED	294,567	307,024
FOREIGN FIXED INCOME	48,358	31,890
DOMESTIC EQUITY	518,615	503,512
DOMESTIC EQUITY – LOANED	38,500	36,443
FOREIGN EQUITY	277,122	241,804
FOREIGN EQUITY – LOANED	27,812	22,112
NON-MARKETABLE ALTERNATIVES	170,383	161,685
MARKETABLE ALTERNATIVES	243,350	194,173
REAL ESTATE	29,341	7,679
MISCELLANEOUS	24	21
TOTAL INVESTMENTS	2,329,296	2,125,319
COLLATERAL FROM SECURITIES LENDING – CASH	339,231	318,277
TOTAL INVESTMENTS AND COLLATERAL	\$ 2,668,527	\$ 2,443,596

of bonds assembled to fund a fixed liability. Macaulay duration is calculated as follows: sum of discounted time-weighted cash flows divided by the bond price. Modified duration is calculated using the following formula: Macaulay duration divided by (1 + yield-to-maturity divided by the number of coupon payments per year).

As of June 30, 2005, modified duration of the University's investments for which duration is measured is as follows:

FOREIGN CURRENCY RISK

The University's Investment Policies permit investments in international equity and other asset classes which can include foreign currency exposure.

The University's investment strategy within the Invested Funds Pool is to hedge exposure to foreign currency. Within this pool, the University enters into foreign currency forward contracts, futures contracts, and options to hedge the foreign currency exposure.

NOTE 7

Metropolitan Tract

The Metropolitan Tract, located in downtown Seattle, is comprised of approximately 11 acres of developed property, including office space, retail space, parking, and a luxury hotel. This land was the original site of the University from 1861 until 1895 when the University moved to its present location. Since the early 1900s, the Metropolitan Tract has been leased

TABLE 2 – INVESTMENTS MANAGED BY THE UNIVERSITY (Dollars in thousands, modified duration in years)

Duration as of June 30, 2005	Consolidated Endowment Funds		Invested Funds		Insurance Funds	
	Asset Value	Duration	Asset Value	Duration	Asset Value	Duration
DOMESTIC FIXED INCOME						
ASSET BACKED	\$ 7,029	1.73	\$ 127,909	1.29	\$ 2,525	1.36
CASH EQUIVALENTS (SHORT-TERM MONEY MARKET)	2,689	0.05	10,481	0.05	1,668	0.04
CORPORATE BONDS	12,420	4.44	20,249	2.22	13,841	6.08
GOVERNMENT AND AGENCIES	42,921	6.15	296,738	3.92	9,218	5.83
MORTGAGE RELATED	26,167	2.87	153,790	1.83	4,727	2.85
SUBTOTAL	91,226	4.46	609,167	2.72	31,979	4.84
FOREIGN FIXED INCOME						
INTERNATIONAL FIXED	37,367	6.09	1,201	4.35	2,891	5.69
TOTAL	\$ 128,593	4.93	\$ 610,368	2.72	\$ 34,870	4.91

Approximately \$166,500,000 of additional domestic fixed income securities (including loaned) and \$6,899,000 of additional foreign fixed income securities, which in total make up 7.4% of the University's investments, are not included in the duration figures above. These investments, which are managed by the University or by the University's affiliates, are not invested under the same investment strategy or with the same custodian as those detailed in Table 2.

CREDIT RISK

The University Investment Policies limit fixed income exposure to investment grade assets. The Investment Policy for the operating fund's cash and liquidity pools requires each manager to maintain an average AA rating as issued by a nationally recognized rating organization. By policy, these managers hold 50% of their portfolios in government and government agency issues. The Investment Policy for the CEF reflects its long-term nature by specifying average quality rating levels by individual manager, but still restricting investment to investment grade credits.

At June 30, 2005 and 2004, the University had net outstanding forward commitments to sell foreign currency with a total fair value of \$32,654,000 and \$25,060,000, respectively, which equals 1.4% and 1.2% of the total portfolio.

As part of the investment strategy, the University does not hedge foreign currency exposure within the equity portion of the Consolidated Endowment Fund.

The following table details the market value of foreign denominated securities by currency type in the Consolidated Endowment Fund.

(Dollars in thousands)	June 30, 2005	
Foreign Currency	Market Value	%
EURO	\$ 63,907	18%
BRITISH – POUND	43,280	12%
JAPAN – YEN	37,641	10%
SWITZERLAND – FRANC	15,832	4%
SOUTH KOREAN – WON	14,232	4%
HONG KONG DOLLAR	12,811	4%
CHINA – RENMINBI	11,412	3%
TAIWAN – NTD	11,221	3%
MEXICO – PESO	10,634	3%
OTHER (LESS THAN 3% EACH)	139,935	39%
TOTAL	\$ 360,905	100%

by the University to entities responsible for developing and operating the property. On July 18, 1953, the Board of Regents of the University and the entity now known as Unico Properties, Inc. entered into a lease agreement for office, retail, and parking facilities, which will expire in 2014. On January 19, 1980, the Board of Regents of the University entered into a lease with the Urban/Four Seasons Hotel Venture for the Olympic Hotel property, which will expire in 2040. The hotel was operated as the Four Seasons Olympic Hotel until July 31, 2003. On August 1, 2003, the remaining lease term was assigned to LHCS Hotel Holding (2002) LLC. The hotel was renamed the Fairmont Olympic Hotel and is now managed by Fairmont Hotels & Resorts.

The balances as of June 30, 2005 and 2004, represent operating assets, net of liabilities, and land, buildings, and improvements stated at appraised value as of November 1, 1954, plus all subsequent capital additions and improvements at cost, less buildings retired or demolished and accumulated depreciation of \$88,018,000 and \$82,269,000, respectively.

NOTES TO FINANCIAL STATEMENTS

NOTE 8:

Capital Assets

Capital asset activity for the two year period ended June 30, 2005 is summarized as follows:

CAPITAL ASSETS (Dollars in thousands)							
	Balance at June 30, 2003	Additions/ Transfers	Retirements	Balance at June 30, 2004	Additions/ Transfers	Retirements	Balance at June 30, 2005
LAND	\$ 59,129	\$ -	\$ -	\$ 59,129	\$ -	\$ -	\$ 59,129
INFRASTRUCTURE	159,984	-	-	159,984	2,501	-	162,485
BUILDINGS	2,005,945	457,680	319	2,463,306	69,632	-	2,532,938
FURNITURE, FIXTURES, AND EQUIPMENT	759,907	87,344	46,558	800,693	89,075	48,690	841,078
LIBRARY MATERIALS	194,260	13,354	1,033	206,581	14,799	1,100	220,280
CAPITALIZED COLLECTIONS	4,409	-	-	4,409	1,092	-	5,501
CONSTRUCTION IN PROGRESS	417,190	(309,121)	-	108,069	131,766	-	239,835
TOTAL	3,600,824	249,257	47,910	3,802,171	308,865	49,790	4,061,246
LESS ACCUMULATED DEPRECIATION:							
INFRASTRUCTURE	50,403	4,243	-	54,646	2,958	-	57,604
BUILDINGS	759,193	74,359	145	833,407	78,246	-	911,653
FURNITURE, FIXTURES, AND EQUIPMENT	561,492	84,213	42,711	602,994	87,178	45,512	644,660
LIBRARY MATERIALS	119,949	9,752	654	129,047	10,322	705	138,664
TOTAL ACCUMULATED DEPRECIATION	1,491,037	172,567	43,510	1,620,094	178,704	46,217	1,752,581
CAPITAL ASSETS, NET	\$2,109,787	\$ 76,690	\$ 4,400	\$2,182,077	\$ 130,161	\$ 3,573	\$2,308,665

NOTE 9:

Long-Term Liabilities:

Long-term liability activity for the two year period ended June 30, 2005 is summarized as follows:

LONG-TERM LIABILITIES (Dollars in thousands)									
	Balance at June 30, 2003	Additions	Reductions	Balance at June 30, 2004	Additions	Reductions	Balance at June 30, 2005	Current Portion 2004	Current Portion 2005
LEASES AND BONDS PAYABLE:									
CAPITAL LEASE OBLIGATIONS	\$ 21,180	\$ 17,651	\$ 4,485	\$ 34,346	\$ 11,747	\$ 8,712	\$ 37,381	\$ 7,651	\$ 9,654
GENERAL OBLIGATION BONDS PAYABLE	294,041	27,070	11,466	309,645	-	12,478	297,167	12,478	12,618
REVENUE BONDS PAYABLE	264,110	16,985	10,175	270,920	162,965	52,335	381,550	6,490	8,090
TOTAL LEASES AND BONDS PAYABLE	579,331	61,706	26,126	614,911	174,712	73,525	716,098	26,619	30,362
OTHER LIABILITIES:									
NOTES PAYABLE AND OTHER CAPITAL ASSET RELATED	41,685	767	2,590	39,862	177	2,937	37,102	2,894	2,945
NOTES PAYABLE AND OTHER NON-CAPITAL ASSET RELATED	13,052	120	55	13,117	659	11,811	1,965	10,002	2
CHARITABLE AND DEFERRED GIFT ANNUITY LIABILITY	29,262	7,586	4,173	32,675	7,153	4,683	35,145	-	-
SICK LEAVE	14,324	10,002	3,575	20,751	2,999	2,495	21,255	900	1,036
SELF INSURANCE RESERVE	35,072	6,563	10,526	31,109	2,730	4,626	29,213	9,413	7,576
NET PENSION OBLIGATION	-	3,775	1,024	2,751	3,363	955	5,159	1,000	1,000
TOTAL OTHER LIABILITIES	133,395	28,813	21,943	140,265	17,081	27,507	129,839	24,209	12,559
TOTAL LONG-TERM LIABILITIES	\$ 712,726	\$ 90,519	\$ 48,069	\$ 755,176	\$ 191,793	\$ 101,032	\$ 845,937	\$ 50,828	\$ 42,921

NOTE 10:

Leases

CAPITAL LEASES

The University has certain lease agreements in effect that are considered capital leases. As of June 30, 2005 and 2004, the University had buildings in the amounts of \$9,987,000 and \$9,987,000 and equipment in the amounts of \$47,198,000, and \$36,693,000, respectively, related to capital leases. These assets were recorded net of accumulated depreciation of \$5,992,000 and \$4,994,000, respectively, for buildings, and \$22,716,000 and \$14,271,000, respectively, for equipment. The University recorded depreciation expense of \$999,000 and \$999,000 for buildings, and \$9,440,000 and \$7,194,000 for equipment in the respective years. Future minimum lease payments under capital leases, and the present value of the net minimum lease payments, as of June 30, 2005, are as follows:

Year	(Dollars in thousands)
2006	\$ 10,821
2007	8,919
2008	6,676
2009	6,656
2010	3,748
2011-2015	4,045
TOTAL MINIMUM LEASE PAYMENTS	40,865
LESS: AMOUNT REPRESENTING INTEREST COSTS	(3,484)
PRESENT VALUE OF MINIMUM LEASE PAYMENTS	\$ 37,381

OPERATING LEASES

The University has certain lease agreements in effect that are considered operating leases, primarily for leased building space. During the years ended June 30, 2005 and 2004, the University recorded expenses of \$30,016,000 and \$30,327,000, respectively, for these leases. Future lease payments under these leases as of June 30, 2005, are as follows:

Year	(Dollars in thousands)
2006	\$ 28,738
2007	20,619
2008	17,147
2009	15,614
2010	14,203
2011-2015	52,504
2016-2020	17,536
2021-2025	13,557
2026-2030	1,345
2031-2051	24
TOTAL MINIMUM LEASE PAYMENTS	\$ 181,287

NOTE 11:

Bonds and Notes Payable

The bonds and notes payable at June 30, 2005, consist of State of Washington General Obligation and Refunding Bonds, University Revenue Bonds, and Notes Payable. These obligations have fixed interest rates ranging from 2.00% to 7.38%, except for debt totaling \$60,720,000, which has variable rates.

Debt service requirements at June 30, 2005 were as follows:

BONDS AND NOTES PAYABLE (Dollars in thousands)						
Year	STATE OF WASHINGTON GENERAL OBLIGATION BONDS		REVENUE BONDS		NOTES PAYABLE AND OTHER	
	Principal	Interest	Principal	Interest	Principal	Interest
2006	\$ 12,618	\$ 15,116	\$ 8,090	\$ 18,415	\$ 2,947	\$ 1,712
2007	12,929	14,529	8,525	18,050	4,409	1,587
2008	13,720	13,872	11,740	17,614	2,851	1,463
2009	14,373	13,149	12,350	17,076	2,826	1,340
2010	11,674	12,470	13,035	16,513	2,457	1,232
2011-2015	72,908	51,900	79,065	72,541	10,450	4,519
2016-2020	79,850	30,516	87,450	54,125	8,800	2,376
2021-2025	62,270	12,706	75,495	36,722	4,327	338
2026-2030	16,825	1,345	62,365	18,659	-	-
2031-2035	-	-	21,270	3,212	-	-
2036-2040	-	-	2,165	82	-	-
TOTAL	\$ 297,167	\$ 165,603	\$ 381,550	\$ 273,009	\$ 39,067	\$ 14,567

State law requires that the University reimburse the state for debt service payments relating to its portion of the State of Washington General Obligation and Refunding Bonds from Medical Center patient revenues, tuition, timber sales, and other revenues. The University has pledged the net revenues from the Housing and Dining System, the Intercollegiate Athletics Department, the Parking System, and a special student fee to retire the related revenue and facilities bonds.

REFUNDING ACTIVITY

On June 7, 2005, \$41,630,000 of Student Fee Construction Revenue Bonds, Series 2000 with an average interest rate of 5.769% were refunded through the issuance of \$43,610,000 Student Facilities Fee Refunding Revenue Bonds, Series 2005 with an average interest rate of 4.815%. The partial refunding of the bonds decreased the University's total debt service payments to be made over the next 25 years by \$3,560,000. The refunding resulted in an economic gain (difference between the present values of debt service payments on the old and new debt) of \$2,112,000. The remaining \$5,060,000 of original bonds was not refunded and are payable over the next

five years.

On September 29, 2004, \$3,960,000 of Parking System Revenue Bonds, Series, 1995 with an average interest rate of 6.1341% were refunded through the issuance of \$4,570,000 Parking System Revenue and Refunding Bonds, Series 2004 with an average interest rate of 3.429%. The decrease in the total debt service payments over the next 11 years and the resulting economic effect were not significant.

On April 6, 2004, \$4,160,000 of Housing and Dining System Revenue Bonds with an aver-

age interest rate of 5.912% were refunded through the issuance of a \$4,375,000 portion of \$16,985,000 Housing and Dining System Revenue and Refunding Bonds, Series 2004 with an average interest rate of 2.789% on the refunding portion. The refunding of the bonds decreased the University's total debt service payments to be made over the next nine years by \$457,000. The refunding resulted in an economic gain of \$413,000.

SUBSEQUENT DEBT OFFERINGS

The following State of Washington General Obligation Bond issues were refunded after June 30, 2005:

On July 26, 2005, \$15,000,000 of Education Bonds, Series 1994A-UW with an average interest rate of 4.4671%, were refunded through a State of Washington General Obligation Bond issue of \$13,955,000, Series R2006A(1994A-UW) with an average interest rate of 4.965%. The refunding of the bonds decreased the University's total debt service payments to be made over the next 14 years by \$1,527,000. The refunding resulted in an economic gain of \$955,000.

On July 26, 2005, \$13,330,000 of Education

Bonds, Series 1994A-HE-UW, with an average interest rate of 4.4670%, were refunded through a State of Washington General Obligation Bond issue of \$12,400,000, Series R2006A(1994A-HE-UW) with an average interest rate of 4.963%. The refunding of the bonds decreased the University's total debt service payments to be made over the next 14 years by \$1,360,000. The refunding resulted in an economic gain of \$850,000.

On July 26, 2005, \$50,550,000 of Medical Center Bonds, Series 2000A-UW, with an average interest rate of 5.579%, were refunded through a State of Washington General Obligation Bond issue of \$49,880,000, Series R2006A(2001A) with an average interest rate of 4.994%. The refunding of the bonds decreased the University's total debt service payments to be made over the next 19 years by \$5,662,000. The refunding resulted in an economic gain of \$3,932,000.

INTEREST RATE SWAP AGREEMENT

In October 2004, the University issued General Revenue Bonds in the amount of \$60,720,000 to fund construction of two research buildings. In connection with this issuance of the Series 2004A and the Series 2004B variable-rate bonds, the University entered into an interest rate swap agreement with a notional amount of \$60,720,000. The intention of the swap was to effectively change the variable rate debt to a synthetic fixed rate of 3.268% as of the closing date of the bonds.

Beginning in December of 2007, the notional amount of the swap and the principal amount of the associated debt declines over time and terminates on June 30, 2037 (the final maturity date of the underlying bonds). The University is currently making fixed rate interest payments to Goldman Sachs and Bank of New York, the two swap counterparties, and receives a variable rate payment computed as 67% of the London Interbank Offered Rate (LIBOR). The variable rate bonds re-price weekly based on market conditions.

The estimated fair value of the interest rate swap was a liability of \$1,737,000 at June 30, 2005. The fair value represents the estimated amount that the University would pay to terminate the swap agreement at the Balance Sheet date, taking into account current interest rates and the creditworthiness of the underlying counterparties. In accordance with governmental accounting standards, this amount is not included in the accompanying financial statements.

The University is exposed to credit risk, which is the risk that the counterparty will not fulfill its obligations. As of June 30, 2005, Goldman Sachs credit ratings were AA+ from S&P and Aaa from Moody's. Bank of New York was rated AA- from S&P and Aa2 from Moody's. Additionally, the swap exposes the University to basis risk, which is the risk that arises when the relationship between the rates on the variable rate bonds and the swap formula of 67% of one-month LIBOR varies from historical norms. If this occurs, swap payments received by the University would not fully offset its bond interest payments. As these rates change, the effective synthetic rate on the bonds will change.

The University or the counterparties may terminate the swap if the other party fails to perform under the terms of the contract.

NOTE 12:

Operating Expenses by Function

Operating expenses by functional classification for the years ended June 30, 2005 and 2004 are summarized as follows:

Operating Expenses	<i>(Dollars in thousands)</i>	
	2005	2004
EDUCATIONAL AND GENERAL		
INSTRUCTION	\$ 670,068	\$ 594,837
RESEARCH	575,410	553,240
PUBLIC SERVICE	30,023	23,367
ACADEMIC SUPPORT	191,827	186,316
STUDENT SERVICES	26,604	25,596
INSTITUTIONAL SUPPORT	113,042	103,059
OPERATION AND MAINTENANCE OF PLANT	148,133	145,928
SCHOLARSHIPS AND FELLOWSHIPS	56,647	53,566
AUXILIARY ENTERPRISES	131,885	124,020
MEDICAL RELATED	624,074	590,374
DEPRECIATION	178,704	172,567
TOTAL OPERATING EXPENSES	\$ 2,746,417	\$ 2,572,870

NOTE 13:

Pension Plans

The University offers two contributory plans: the Washington State Public Employees Retirement System (PERS) plan, a defined benefit retirement plan; and the University of Washington Retirement Plan (UWRP), a

defined contribution plan with supplemental payments, when required.

PUBLIC EMPLOYEES RETIREMENT SYSTEM

Plan Description. The University of Washington contributes to PERS, a cost-sharing, multiple-employer, defined benefit pension plan administered by the State of Washington Department of Retirement Systems. PERS Plan 1 provides retirement and disability benefits and minimum benefit increases beginning at age 66 to eligible non-academic plan members hired prior to October 1, 1977. PERS Plans 2 and 3 provide retirement and disability benefits and a cost-of-living allowance to eligible non-academic plan members hired on or after October 1, 1977. In addition, PERS Plan 3 has a defined contribution component, which is fully funded by employee contributions. The authority to establish and amend benefit provisions resides with the legislature. The Washington State Public Employees Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for PERS. The report may be obtained by writing to the Department of Retirement Systems, P.O. Box 48380, Olympia, Washington 98504-8380, or visiting <http://www.drs.wa.gov/administration>.

Funding Policy. The Office of the State Actuary, using funding methods prescribed by statute, determines actuarially required contribution rates for PERS. Plan 1 members are required to contribute 6% of their annual covered salary. Contributions for Plan 2 members are determined by the aggregate method, and may vary over time. The contribution rate for Plan 2 employees at June 30, 2005 and 2004 was 1.18% and 1.18%, respectively. PERS 3 members can choose contributions ranging from 5% to 15% of salary, based on the age of the member. The defined contribution benefit for PERS 3 will depend on the member's contributions, the investment earnings on those contributions, and if an annuity is taken, the age at which the member receives payment. The contribution rate for the University at June 30, 2005 and 2004, for each of PERS Plans 1, 2, and 3 was 1.38% and 1.40%, respectively.

The University's contributions to PERS for the years ended June 30, 2005, 2004, and 2003 were \$8,651,000, \$8,120,000, and \$7,969,000 respectively, which were equal to the required contributions for each year.

**UNIVERSITY OF WASHINGTON
RETIREMENT PLAN**

Plan Description. Faculty, librarians, professional staff, and certain other salaried employees are eligible to participate in the University of Washington Retirement Plan, a defined contribution plan administered by the University. Contributions to the Plan are invested in annuity contracts or mutual fund accounts offered by one or more fund sponsors. Employees have at all times a 100% vested interest in their accumulations.

Benefits from fund sponsors are available upon separation or retirement at the member's option. RCW 28B.10.400 et. seq. assigns the authority to the University of Washington Board of Regents to establish and amend benefit provisions.

The Plan has a supplemental payment component which guarantees a minimum retirement benefit based upon a one-time calculation at each employee's retirement date. The University makes direct payments to qualifying retirees when the retirement benefits provided by the fund sponsors do not meet the benefit goals.

Funding Policy. Employee contribution rates, based on age, are 5%, 7.5%, or 10% of salary. The University matches the contributions of employees. Within parameters established by the legislature, contribution requirements may be established or amended by the University of Washington Board of Regents. Employee and employer contributions for the year ended June 30, 2005 were each \$55,080,000 compared to \$50,294,000 for the year ended June 30, 2004. The supplemental component of the UWRP is financed on a pay-as-you go basis.

Supplemental Component (Unaudited). The University received an actuarial evaluation of the supplemental component of the UWRP during fiscal year 2004. The previous evaluation was performed in 1999. The Unfunded Actuarial accrued Liability (UAL) calculated as of June 30, 2004 and 1999 was \$32,454,000 and \$13,786,000, respectively, and is amortized over a 19.5 year period. The Annual Required Contribution (ARC) of \$3,363,000 consists of amortization of the UAL, including interest expense, (\$1,993,000) and normal cost (or current cost) (\$1,370,000). The UAL and ARC were established using the entry age normal cost method. The actuarial assumptions included an investment rate of return of 7% and projected salary increases ranging from 2% to 4%. Approximately \$640,000,000 and \$302,000,000 of the UW's payroll was

covered under this plan during 2004 and 1999, respectively. The following table reflects the activity in the Net Pension Obligation for the years ended June 30, 2005 and 2004:

<i>(Dollars in thousands)</i>	2005	2004
BALANCE AT BEGINNING OF FISCAL YEAR	\$ 2,751	\$ -
ANNUAL REQUIRED CONTRIBUTION	3,363	3,775
PAYMENTS TO BENEFICIARIES	(955)	(1,024)
BALANCE AT END OF FISCAL YEAR	\$ 5,159	\$ 2,751

The annual payment for fiscal year 2003 was \$1,109,000 and approximated the ARC.

NOTE 14:

Commitments and Contingencies

Authorized expenditures for construction projects unexpended as of June 30, 2005, were \$110,736,000. These expenditures will be funded from local funds and state appropriations.

The University receives and expends substantial amounts under federal and state grants and contracts. This funding is used for research, student aid, Medical Center operations, and other programs, and is subject to audit by governmental granting agencies. Certain grant and contract costs billed to the federal government are subject to audit under OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. The University is also involved in various other claims and legal actions arising in the ordinary course of business. University management believes that any liabilities arising from these matters will not have a material effect on the University's financial statements.

The University is a defendant in a suit filed by a faculty member alleging wrongful denial of a salary increase. The case seeks retroac-

tive award of the increase for faculty members included in the class. On October 25, 2005, the trial court granted the plaintiff summary judgement on liability but there are numerous judicial proceedings remaining in the case and at this time, the University and its legal counsel are unable to provide a meaningful assessment of the legal or financial risk associated with this case. Potential costs include the two percent increase dating back to 2002-03, the consequent additional salary cost for all subsequent years, interest, and litigation costs. The amount could be substantial.

The University is exposed to risk of loss related to tort liability, injuries to employees, and loss of property. The University purchases insurance protection for workers' compensation as well as marine, aviation, and certain other risks. The University also purchases insurance protection for loss of property at self-sustaining units, bond-financed buildings, and where otherwise required by contract; otherwise, the risk of property loss is retained, unfunded. For professional, general, employment, and automobile liability, the University maintains a program of self-insurance reserves and excess insurance coverage. The self insurance reserve represents the estimated ultimate cost of settling claims resulting from events that have occurred on or before the balance sheet date. The reserve includes the amount that will be required for future payments of claims that have been reported and claims related to events that have occurred but have not been reported.

The self insurance reserve is estimated through an actuarial calculation using individual case-basis valuations and statistical analyses. Although considerable variability is inherent in such estimates, management believes that the self-insurance reserve is adequate. Changes in the self-insurance reserve for the years ended June 30, 2005, 2004, and 2003 are noted below.

Self Insurance Reserve	<i>(Dollars in thousands)</i>		
	2005	2004	2003
RESERVE AT BEGINNING OF FISCAL YEAR	\$ 31,109	\$ 35,072	\$ 32,440
INCURRED CLAIMS AND CHANGES IN ESTIMATES	2,730	6,563	7,080
CLAIM PAYMENTS	(4,626)	(10,526)	(4,448)
RESERVE AT END OF FISCAL YEAR	\$ 29,213	\$ 31,109	\$ 35,072

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