



INNOVATION FOR THE PUBLIC GOOD
University of Washington 2001 Annual Report

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BOARD OF REGENTS AND ADMINISTRATIVE OFFICERS *inside back cover*



MESSAGE FROM THE PRESIDENT

Research universities are in the business of creating the future. That's where our students will use their education, and that's where our research will prove its value.

Certain moments bring this home. In December 2000, Emma Brunskill, who had graduated from the UW the previous June, was named a Rhodes Scholar—our first in 20 years. So to celebrate, we gave her a party. We also invited other high-achieving UW students, including Emma's younger sister, Amelia.

The talent in that room was inspiring. We could only imagine what those young people might be accomplishing 10 or 20 or 30 years from now. But we were also proud that UW innovations in education had helped them realize their great promise. Emma Brunskill entered the UW at the age of 15, as part of our pioneering Early Entrance Program for young students. While she was here, she worked on six different research projects in the departments of computer science, physics, geophysics, and chemistry—the kinds of opportunities that have been a centerpiece of our work to transform undergraduate education. Emma's future, and the contributions she will undoubtedly make, will carry the imprint of her years at the University of Washington.

Students who can see and seize the possibilities of the future, new knowledge that makes those possibilities real, a society enhanced by both—these are the products of a strong and innovative university. Can we find the resources to remain that kind of university? That was a question, increasingly urgent, that we grappled with throughout the past year.

At the state level, the answer was discouraging. The long legislative session, frustrating for all involved, produced a biennial UW budget with major gaps between our resources and our needs. At a time of rising demand for higher education, the budget funds only a few more students. Despite some improvement in salaries, it leaves our faculty and staff about 15 percent behind their peers at comparable public institutions. (And of course the salary gap between the UW and private universities, with which we also compete for faculty, can be several times that 15 percent.) The budget makes no provision for the escalating costs of energy or library materials. It leaves us with core funding almost \$2,000 per student behind the average of our peers—an aggregate gap of \$70 million a year. It passes over our pressing need for more research space and for renewal of aging and inadequate facilities. It leaves us with a shortfall in our operating budget that will have to be made up

from our reserves. And, as I write, the worsening economic situation makes it likely that even this budget will be cut during the 2002 legislative session.

Clearly, we have to seek alternatives. Tuition will continue to rise (as will financial aid). Our record-setting success in winning federal and corporate research grants will have to reach new heights. We are exploring new possibilities for income from technology transfer and self-sustaining educational programs. And we believe that private philanthropy can play a much larger role here than it has in the past.

These are not steps to “privatize” the University of Washington. We hold fast to our public mission: expanding opportunity for Washington citizens and providing knowledge and expertise to advance the state’s health, economy, and quality of life. But as public funding for higher education declines—a trend in almost every state in the nation—that public mission must depend increasingly on private resources.

The stakes are high. We draw inspiration from students like Emma Brunskill (and others you will read about in this report), from the myriad of University programs that are melding research, education, and service in exciting new ways—and from a long history of UW innovation.

More than 30 years ago, a young scientist came to the UW as a faculty member in our fledgling department of genetics. He was drawn by the chance to work with the department’s founding chairman, Herschel Roman, sometimes called “the father of yeast genetics.” Over the next decades, Leland Hartwell’s patient and brilliant research on yeast led to new understanding of how cells divide and how this process goes wrong in cancer. In 1997 he became director of the Fred Hutchinson Cancer Research Center. Just this October, Lee Hartwell, along with two British scientists whose work built on his, won the 2001 Nobel Prize for medicine.

In uncertain times, the power of knowledge to shape the future remains clear. That’s where the University of Washington will stake its claim to public and private support.

RICHARD L. McCORMICK



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INNOVATION FOR THE PUBLIC GOOD

ANTHONY KELLEY *6*

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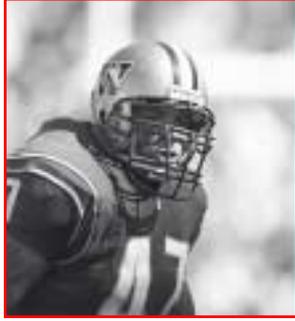
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Seeing through





African eyes

ANTHONY KELLEY Senior, Comparative History of Ideas

On New Year's Day 2001, outside linebacker Anthony Kelley helped the Huskies win the Rose Bowl. The next day, he set off on an experience that would prove even more memorable: winter quarter in Cape Town, South Africa. "It changed my life," he says simply.

Anthony joined a study-abroad term run jointly by the UW's American Ethnic Studies department and Comparative History of Ideas (CHID) program. CHID students study the complex interplay between history and identity, and the quarter in Cape Town (like CHID programs in Prague, Belfast, and elsewhere) gives that study an intense immediacy. Students have to make connections between their classroom learning and their experience in the community. The focus of this particular term was a comparison between African-American literature and experience and that of black South Africa.

For Anthony, the first rush of impressions was overwhelming. "I couldn't take it all in—just being there, talking to people, making friends. I found myself feeling kind of shallow, seeing the real black culture in Africa. But it also made me appreciate the blacks here who fought for our rights. I'd never seen the kind of segregation and racism I saw there. I had a sense it was like this country years ago."

Then, through the Amy Biehl Foundation, Anthony began visiting black townships. "I found a new love: working with the kids." He tutored and set up athletic programs and tried to provide adult care for kids whose parents had to work far away. "They were so enthused just to have something to do. In the townships, they have nothing."

Anthony returned home with a new sense of his own future. "Seeing the things I saw in Africa put football in a different context for me." He's been busy raising funds and support for more work with the children of the townships when he returns to Cape Town his senior year. "I'm going to bring a group of athletes to the squatter camps to work with kids in athletics, to give them something to pursue. But I know it's the lack of education that's keeping people down. I want the kids to see that their future is in those books."

Immersed in research



SAMAR HASSOUNEH Junior, Neurobiology

Sophomore Samar Hassouneh was really enjoying Biology 202, so when Professor Dennis Willows began talking about research apprenticeships at the UW's Friday Harbor Labs, she paid attention. A team of 10 undergraduates, living at Friday Harbor for a whole quarter, would join a multi-disciplinary project called Implantable Electrodes and Computers in the Brain. The brain in question was that of a sea slug, and the project's ultimate goal was to implant a self-contained computer chip that could monitor the neurological activity of a living creature interacting freely with its environment.

Samar was excited by the ambition of the project. "I was trying to decide if I wanted to go into neurobiology, and this seemed like a good way to find out." She signed on.

From March until June 2001, as spring came to San Juan Island, Samar and her fellow students immersed themselves in their research. "We were living in the woods, the weather was really nice, and we had the whole day just to think about our projects." First came intensive coaching in basic concepts and techniques; then students paired up to tackle one small piece of the long-term project. Samar and her partner worked on "brain implantation methods for a silicon interface." By the end of the quarter, they had concrete results—"crucial practical steps in making the project feasible," says Willows.

Willows started the Friday Harbor apprenticeship program in 1999 with funding from the UW's Tools for Transformation. For Samar, the experience was "really, really good. It taught me how to conduct research on my own. You have a problem, you think about it, you find out what other people have done, you come up with new ideas, you find something that works, and you just keep going and going and going."

The quarter also confirmed her interest in neurobiology. Now, with plans for medical school, she's doing research on traumatic brain injury with a professor of neurological surgery. "The first time I approached him, before I went to Friday Harbor, he said to come back when I knew more. After Friday Harbor, I knew a lot."



into new
Venturing



technologies

CHAD LINDHORST Graduate, Computer Science and Engineering

In the winter quarter of his junior year, computer engineering major Chad Lindhorst had a hole in his schedule. A lucky hole, as it turned out. “I looked through the catalog and found Chris Diorio’s Introduction to VLSI Design course. I didn’t know anything about it, but it was the only course that fit my schedule.”

Chad loved the course. “We got to do detailed design of integrated circuits from scratch—from the very bottom, the simplest primitives. It was a totally different level of circuit design from what’s done in other classes, much closer to the physics involved.” It didn’t hurt that Professor Diorio was a master teacher, who would later win one of the UW’s coveted Distinguished Teaching Awards. “We had so much fun,” says Chad, “that three of my classmates and I decided to do an honors project with Chris.” In that project, the students produced a new kind of integrated circuit, from design through testing and fabrication. “It was a very rare opportunity for us as undergraduates. We’re writing up patent applications for one of the techniques we developed.”

In another stroke of luck, Chad graduated from the UW just as Chris Diorio and his own mentor from Caltech, Carver Mead, were putting together a new company called Impinj. Its groundbreaking “Self-Adaptive Silicon” technology, developed by Mead and Diorio, combines analog and digital functions on a single chip, which continuously recalibrates itself as operating conditions change. These “radically new microchips” (*MIT Technology Review*) promise to revolutionize wireless communications.

Diorio invited Chad and a fellow student from the honors group to join Impinj. “I had another job all lined up, but Chris said, ‘Come on, it’ll be fun.’ I think I was actually Impinj’s first employee. And it has been fun. There’s so much interesting work to do here it’s amazing. We’re taking a technology that hasn’t even been proven yet in industry and thinking up a lot of new uses for it. It’s an adventure.”



Building bridges



for world health

ROBERTO ADOR Graduate student, Health Services

Why would a man with important public-policy responsibilities in Manila take extended leave to do graduate work at the University of Washington? “I was looking for new ideas,” says Roberto (Obet) Ador. As Executive Director of the Philippines Legislators’ Committee on Population and Development, Obet wanted to learn from others dealing with health and population issues in developing countries. A staffer in his office, browsing the Internet, alerted him to opportunities at the UW.

In two years here, Obet has found both new colleagues and new ideas. He arrived as one of 10 inaugural Packard-Gates Fellows in the Population Leadership Program at the Daniel J. Evans School of Public Affairs. Then Obet and two other Fellows were invited to join the International Health Program of the School of Public Health and Community Medicine. In both of these highly competitive programs, mid-career professionals from around the world study challenging public-health problems and compare experiences.

“We get an incredibly good group of people,” says Professor Steve Gloyd, who started the International Health Program in 1988. “They’re often here at a transition point, and then go back home to have enormous impact. Really, the faculty here are just traffic directors of conversations—what the students learn from each other is what’s fundamental.”

Obet gives the professors more credit. “I’ve gained a lot from the interactions, but also from the classes and readings. They’ve sharpened my understanding of so many issues—especially the ways in which health in developing countries is linked with poverty, education, and economic structures.”

He stays in close touch with his staff in Manila. “Even while I’m here, our work in the Philippines is being improved by a continual passing on of what I learn. When I go back, I’ll be looking critically at our methods and skills. And I’ll bring much richer detail to our discussions of policy issues and positions we want to advocate. I can be a bridge between all the knowledge and experience I’ve found here and health policy in the Philippines.”

Buenos Señor Stevenson

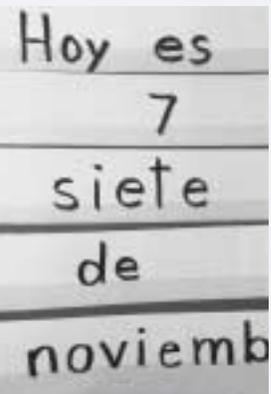
JEFF STEVENSON Graduate student, Linguistics

Once or twice every week, doctoral student Jeff Stevenson goes back to first grade. It's not your garden-variety first grade. In Maria Buceta Miller's classroom at John Stanford International School, students spend half of each day learning math and science entirely in Spanish. To the kids, Jeff is a friendly guy who sometimes lends a helping hand. But mainly he's there to watch and listen intently.

"In a nutshell," he says, "we're looking at how Maria's kids go about learning Spanish verbs." Jeff and the chair of the UW linguistics department are tracing the steps by which young children learn a second language through "immersion," with no explicit language instruction. The research is funded by the UW's multidisciplinary Center for Mind, Brain, and Learning. "One of our main goals," says Jeff, "is to investigate the gap between comprehending a language and actually speaking it. I didn't expect these kids to be talking as much as they are. At this age, they just internalize the rules on their own—even tricky grammatical structures that take UW students a long time to learn. In my opinion, this is really cool stuff."

Jeff's research project is just one of many relationships between the Stanford School and the University. When the late superintendent John Stanford first imagined an international elementary school, he and UW president Dick McCormick agreed on a partnership. Since then, UW faculty and staff have worked closely with Stanford School planners and teachers. They've collaborated on curriculum design, on shaping the "partial [half-day] immersion" model for learning Spanish and Japanese, and on making the Stanford School the first elementary school in the nation with a connection to Internet2. When the school opened in fall 2000, it became a lab school for UW students and faculty. The partnership "has really been a two-way street," says Stanford School principal Karen Kodama. "We're all learning together."

Jeff hopes that his own research will help document the value of the Stanford School's international approach and the need for more such schools. Already, the school has won strong community support. "It's a wonderful thing," says Jeff. "If I had kids, that's where I'd want them to go."



dias





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FINANCIAL HIGHLIGHTS

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Current Operations

- The University has a diversified revenue base. No single source generated more than 32 percent of the total fiscal year 2001 operating revenues of \$2.2 billion.
- State appropriated dollars (16 percent) and student tuition and fees (12 percent) were key sources of funds, providing \$608 million in 2001, primarily for instructional activities.
- Grants and contracts (30 percent) generated \$643 million of current-year revenue, a 7 percent increase over fiscal year 2000. These funds provided the opportunity for graduate and undergraduate students to work with nationally recognized faculty in research as part of their educational experience.
- Operating income from gifts totaled \$52 million (2 percent). This private support gave the University an added margin of excellence and the flexibility to respond to special opportunities.
- Approximately 44 percent of total expenditures supported two primary functions of the University: instruction and research (see figure 2). These dollars provided instruction to more than 39,000 students and funded 4,800 research awards.
- The University provided students with scholarships and fellowships that totaled over \$88 million (4 percent of expenditures).

FIGURE 1
SOURCES OF UW FUNDS
 Current funds for fiscal year 2001

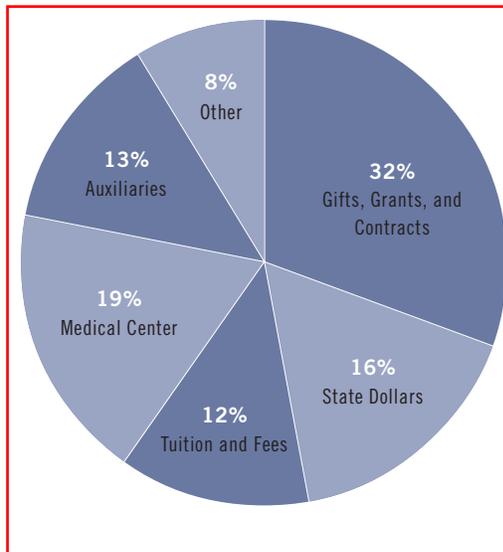
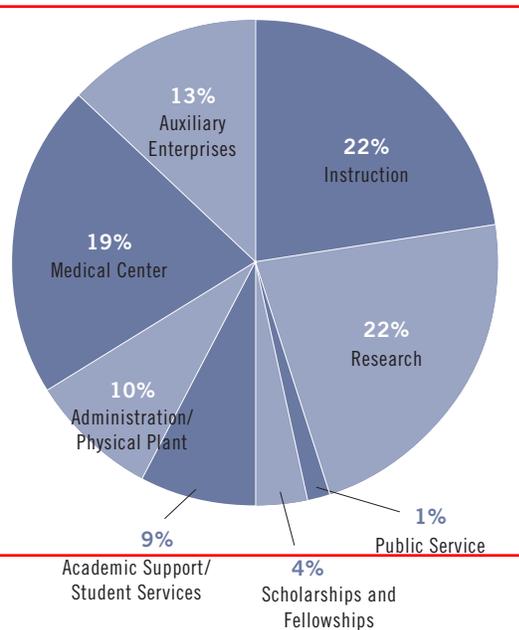


FIGURE 2
USES OF UW FUNDS
 Current funds for fiscal year 2001





Streamlining the Purchasing Process

Credit cards are widely accepted and one of the easiest methods for company employees to make routine purchases as Carolyn Chow, School of Nursing Recruiter, is doing above. They provide portability and straightforward record keeping for complex organizations. But, until a year ago, this option was not available at the University of Washington. During Spring Quarter 2001, after a very successful pilot project and thorough evaluation of several card vendors, the UW Financial Management division launched the procurement card program. To date, more than 1400 cards have been issued to 150 departments on campus.

A purchasing process that used to take several hours and many people across the campus has been reduced to a few steps and even fewer people. This particular solution is well suited to meet the needs of a major higher education research institution with multiple funding sources and a decentralized control structure.

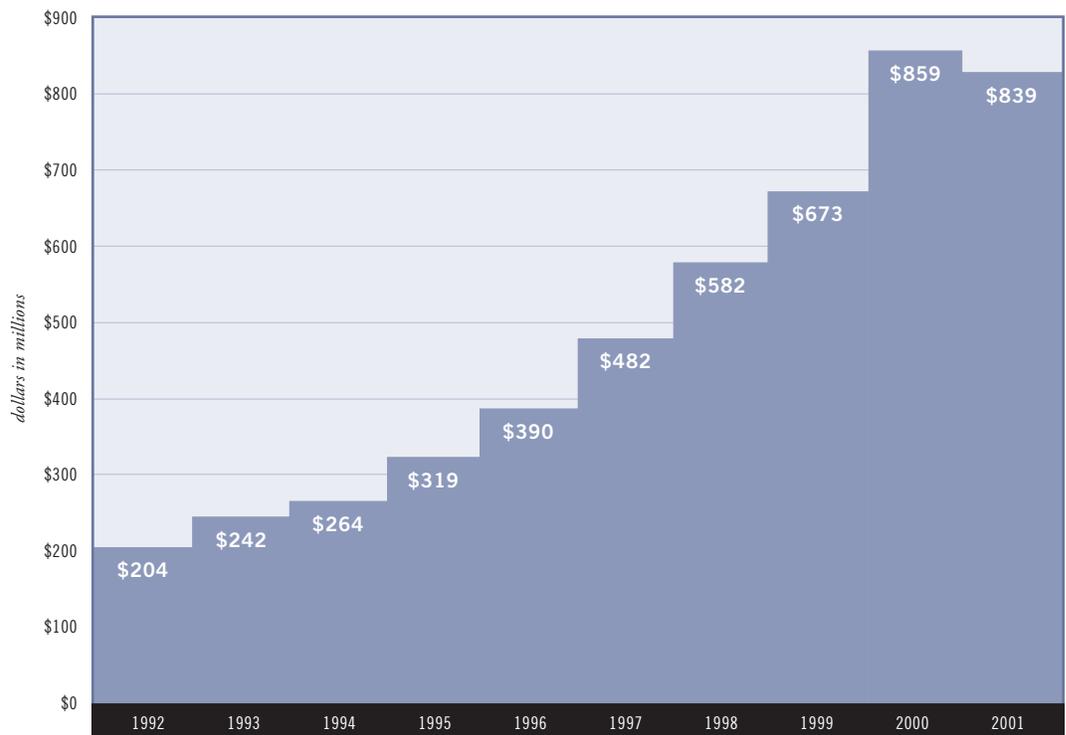
Although the program is still young, procurement cards are being used for more than 14 percent of purchasing transactions, and acceptance has been widespread. One college administrator said, “It (the procurement card) has saved time and paper by eliminating approximately 90 percent or more of our requisitions and petty cash transactions and making it more convenient for staff to make smaller purchases.” Another added, “The procurement card is great for online purchases—once an order, card number, and expiration date have been entered, the item arrives a few days later!”

Campus departments appreciate the technology offered for reconciling and allocating charges as well as the greater degree of control over the purchasing process. And, vendors are paid faster. Everybody wins.

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 cash.
- Endowed gifts 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, 2001, the fair market value of the CEF was \$839 million, representing the investments of 1,628 individual endowments.
- Endowed program support over the last five years totaled \$124.5 million. During that period, the average annual total return on the CEF was 14.5 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 \$792 million. The total return has averaged 9.1 percent annually over the last five years.

**GROWTH OF
CONSOLIDATED
ENDOWMENT FUND:
1992-2001**





Endowed Chair in Women's Sports Medicine and Lifetime Fitness

The number of women involved in high school and college athletics has tripled in the past thirty years—from 840,000 to more than 2.6 million. That's good news because, compared to their inactive peers, active women have higher self-esteem, are better scholars, and are at less risk for diabetes, depression, cancer, heart disease, and osteoporosis. But increased participation in sports has also uncovered the fact that females are more likely than males to suffer sports-related injuries, such as stress fractures and tears in the knee's anterior cruciate ligament.

To increase our understanding of women's fitness, including why women are more prone to sports injuries than men, the department of orthopaedics and sports medicine at the University of Washington School of Medicine recently established the first Endowed Chair in Women's Sports Medicine and Lifetime Fitness.

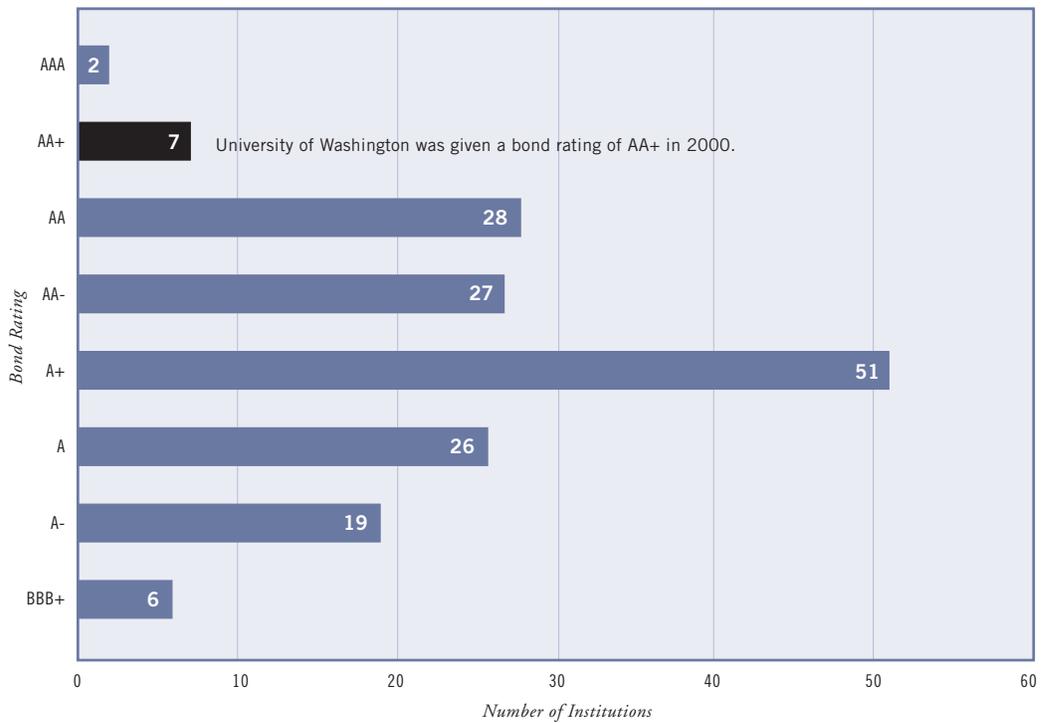
According to 1984 Olympic Skiing gold medalist Debbie Armstrong, the new chair will be a huge help to many women athletes in the future, whether they're into serious competition or simply want to stay in shape throughout their lifetimes. "Sports can be such a positive factor in the lives of women. The endowment of this chair marks a tremendous step forward in the search to understand the special needs of women athletes in terms of injury prevention and recovery," she says.

The chair has been established through \$1.7 million in private gifts from donors from the Seattle community, and will be the catalyst for a \$10 million fundraising effort to establish the United States' first Endowed Center for Women's Sports Medicine and Lifetime Fitness. The goal of this center is to extend the benefits of cutting edge research to individuals at risk for osteoporosis fractures and those at risk from participation in sports.

Debt Financing

- 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.
- 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 has received ratings upgrades from the major rating agencies, Standard & Poor’s and Moody’s, in 1997, 1998, and 2000. These actions from the nation’s premier credit agencies continue to recognize the University’s strong stewardship of financial resources and prudent use of debt to finance capital projects.

STANDARD & POOR’S 2001 PUBLIC COLLEGE AND UNIVERSITY RATINGS





Intramural Activities Building – Making a Good Thing Better

When the original IMA was constructed in 1968, the University had total enrollment of 27,000. The facility was designed to accommodate the needs of this campus population. By 1999, enrollment exceeded 35,000 and the building, while still in good condition, was being pushed to its limits. In addition, the recreational demands of students have changed since the 1960s.

A campus survey was conducted and the Student Activities Committee, in conjunction with the Office of Student Affairs, recommended that a major building renovation and addition be constructed with funds raised from issuing bonds to be repaid with a new student activity fee.

The bonds were issued in late 2000 and the facility began construction in August 2001. When completed in spring 2003, the newly redone IMA will boast an indoor climbing rock, running track, two new basketball courts, and increased space for weight and fitness training. An expanded front entrance and café will add to the appeal of the building. In addition, a night lighting system will be added to an outdoor sports field and, funds permitting, renovations will be made to the golf driving range.

This new state-of-the-art facility will serve UW students, faculty, and staff well into the new century.

Capital Budget and Campus Construction

In recent years, the State of Washington and University resources have provided significant capital funding to modernize and expand University of Washington facilities on all three campuses.

During 2000–2001 a number of major projects were under construction.



UW Tacoma Campus

Renovation of the historic West Coast Grocery and Dougan buildings is now complete, bringing new classroom and office space to accommodate the growing student population. Construction of the Central Complex science lab and classroom buildings began in May 2000 and is scheduled for completion in early 2002.

Suzzallo Library

Structural work is nearing completion in the renovation of this landmark building. Along with the reconstruction work, remodeling and relocations will improve library services and make them more accessible. The library sustained very minor damage during the Nisqually earthquake, primarily from falling bookshelves, but structural work already completed prevented more extensive damage. The library remains open throughout the construction.

UW Medical Center Pacific Tower

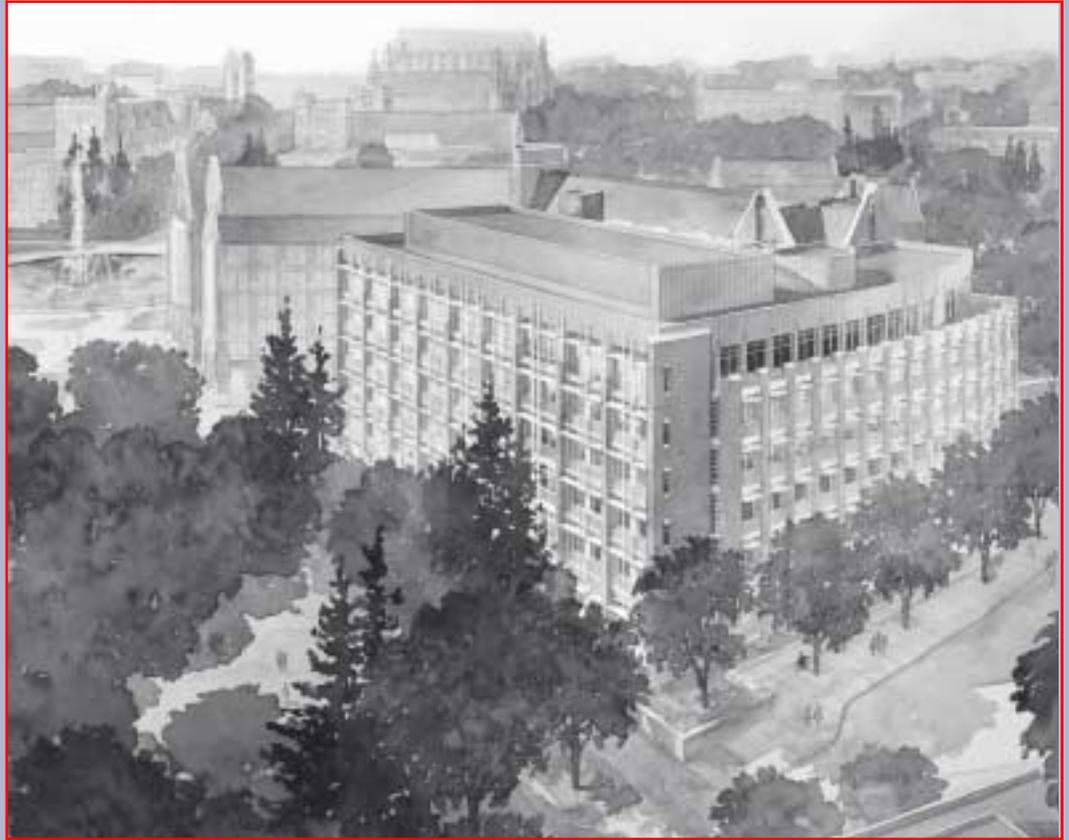
The final phase of this 70,000-square-foot renovation of inpatient and clinical spaces built in the 1950s is nearly finished and will be completed in early 2002. Much of the newly remodeled and rewired space is already occupied.

Intercollegiate Athletics Practice Facility

Construction of the 95,000-square-foot indoor practice facility and adjoining outdoor practice field was completed in fall 2001. The new facilities provide all-weather practice opportunities for men's and women's sports teams as well as recreational use by students, faculty, and staff.

Intramural Activities Building

Renovation and expansion of the Intramural Activities building (IMA) began in August 2001. The project will upgrade the seismic resistance of the existing facility and add a gymnasium, walking/jogging track, weight and cardiovascular rooms, and an indoor climbing facility. Construction is scheduled for completion in 2003.



Computer Science and Engineering

The final phase of a project begun in 1994 to unite and enhance the classroom, laboratory, and staff facilities for Electrical Engineering and Computer Science and Engineering began this year.

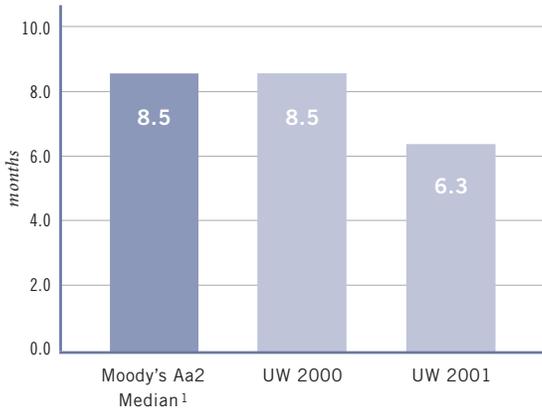
Beginning with the demolition of the old Electrical Engineering building, the project will provide 75,000 square feet of space for research and teaching laboratories, offices for faculty and staff, and meeting spaces. Construction has begun with estimated completion in 2003.

The new building is being constructed as a public/private partnership. State and University resources are providing \$30 million of the \$70 million total cost of the project, with the remaining \$40 million to be raised privately.

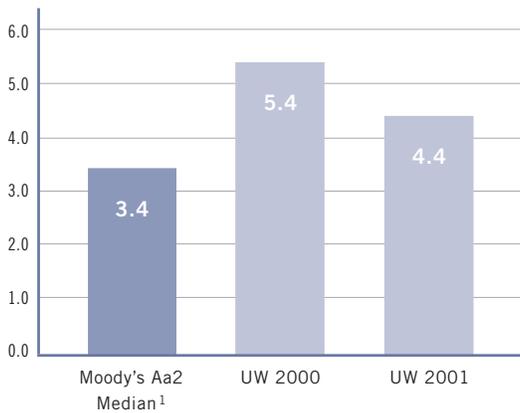
The Department of Computer Science and Engineering has attracted worldwide attention for research at the forefront of areas like intelligent Internet systems, data mining, invisible computing, artificial intelligence, computer graphics, and “active networks”—a technology that will transform the Internet in the next decade.

Financial Health and Flexibility

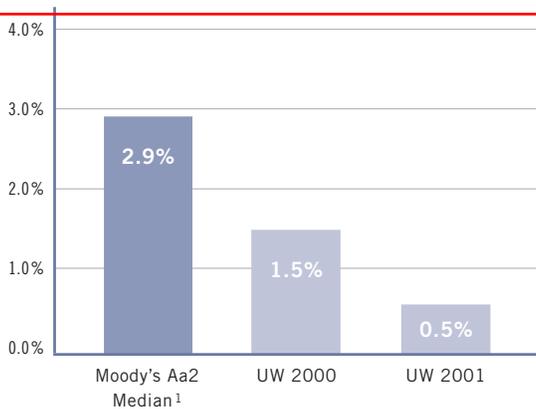
PRIMARY RESERVE RATIO



TOTAL RESOURCES TO DEBT RATIO



OPERATING MARGIN



Prudent stewardship of financial resources is a high priority for the University of Washington and is crucial to meeting the institution's future financial demands. The results are a strong balance sheet and acceptable operating ratios compared to the institution's peers, as shown in the charts at left. It is also reflected in recent credit rating upgrades which help the University borrow money at cost-effective interest rates for important capital projects on campus.

Primary Reserve Ratio

This ratio measures the University's overall financial strength. Today the University has enough expendable resources from various sources to fund operations for more than six months. This is slightly less than the median for public universities with strong "Aa2" credit ratings.

Total Resources to Debt Ratio

The University has been prudent in the issuance of debt to finance capital projects. This is reflected in the University's ratio of available financial resources to current outstanding debt obligations compared to the median for other public universities.

Operating Margin

This ratio measures how much operating revenues² exceed expenses expressed as a percent of total revenues of the University. The substantial decline in operating margin reflects the difficult state funding environment and higher energy costs the University faced in 2001.

¹ Median data as of fiscal year 1999 published in December 2000 for Aa2 rated schools represents most recent information provided by Moody's Investors Service.

² Operating revenues adjusted to exclude the net appreciation in the fair value of investments held in the diversified investment pool. The excluded amounts total (\$13,546,000) and \$33,510,000 for 2001 and 2000, respectively. This adjustment more closely reflects the Moody's universe of public universities that typically do not invest a comparable proportion of operating funds in endowment type strategies. Although not available for current operations, the diversified investment pool gains and losses are reflected in current unrestricted funds in the financial statements.





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FINANCIAL STATEMENTS

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INDEPENDENT AUDITORS' REPORT

The Board of Regents
University of Washington:

We have audited the accompanying balance sheet of the University of Washington as of June 30, 2001, and the related statements of changes in fund balances and current funds revenues, expenditures and other changes for the year then ended. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the financial statements of the University of Washington Medical Center, which statements reflect 17% of current unrestricted fund assets, 15% of investment in plant fund assets and 27% of current unrestricted fund revenues. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for the University of Washington Medical Center, is based solely on the report of the other auditors. The prior year summarized comparative information has been derived from the University of Washington's 2000 financial statements and, in our report dated November 3, 2000, we expressed an unqualified opinion on those financial statements.

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

In our opinion, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of the University of Washington as of June 30, 2001, and the changes in fund balances and the current funds revenues, expenditures and other changes for the year then ended in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

Seattle, Washington
November 2, 2001

Balance Sheet

June 30, 2001, with comparative totals for 2000

	CURRENT FUNDS					PLANT FUNDS			June 30, 2001	June 30, 2000
	Unrestricted	Restricted	Loan Funds	Endowment and Similar Funds	Annuity and Life Income Funds	Unexpended	Retirement of Indebtedness	Investment In Plant		
ASSETS										
CASH	\$ 19,847					4,057	1		23,905	29,750
FUNDS ON DEPOSIT WITH STATE TREASURER	1			22,097		39,803	1,095		62,996	49,619
COLLATERAL FROM SECURITIES LENDING	48,502	40,863	1,386	91,568	1	23,174			205,494	294,814
INVESTMENTS	467,426	271,055	8,996	878,541	65,416	197,616	4,840		1,893,890	1,955,033
METROPOLITAN TRACT				105,252					105,252	99,839
ACCOUNTS RECEIVABLE (NET OF \$66,328 ALLOWANCE)	210,657	109,347	1,164	12,672		1,471	232		335,543	270,499
STUDENT LOANS (NET OF \$7,650 ALLOWANCE)			58,279						58,279	57,027
STORES AND OTHER INVENTORIES	20,232								20,232	20,092
DEFERRED EXPENSES AND OTHER ASSETS	31,782					501	3,755		36,038	27,534
DUE FROM OTHER FUNDS	6,485	1,063					5,550		13,098	18,458
LAND, BUILDINGS, AND IMPROVEMENTS								2,150,488	2,150,488	1,977,956
EQUIPMENT								685,684	685,684	637,040
LIBRARY BOOKS								176,525	176,525	166,220
TOTAL ASSETS	\$ 804,932	422,328	69,825	1,110,130	65,417	266,622	15,473	3,012,697	5,767,424	5,603,881
LIABILITIES AND FUND BALANCES										
ACCOUNTS PAYABLE	\$ 182,513	16,068		8,525	6	17,940			225,052	200,543
ACCRUED LIABILITIES	73,854	35,367					5,550		114,771	114,235
PAYABLES – SECURITIES LENDING TRANSACTIONS	48,502	40,863	1,386	91,568	1	23,174			205,494	294,814
DUE TO OTHER FUNDS	6,613	6,240			245				13,098	18,458
FUNDS HELD FOR OTHERS		4,899							4,899	3,873
DEFERRED REVENUES	48,145								48,145	46,835
ANNUITIES PAYABLE					3,206				3,206	3,140
OBLIGATIONS UNDER CAPITAL LEASES						14,385		41,541	55,926	35,436
BONDS AND NOTES PAYABLE	1,375	1,400			158	53,224	8,092	325,519	389,768	334,493
SELF-INSURANCE RESERVE	36,653								36,653	31,704
FUND BALANCES:										
UNRESTRICTED – GENERAL	227,682								227,682	243,491
UNRESTRICTED – DESIGNATED	179,595								179,595	216,196
RESTRICTED		317,491				157,899	1,831		477,221	442,864
U.S. GOVERNMENT GRANTS REFUNDABLE			44,952						44,952	43,811
UNIVERSITY LOAN FUNDS – RESTRICTED			23,487						23,487	22,712
ENDOWMENT				680,131					680,131	679,346
QUASI-ENDOWMENT – RESTRICTED				329,906					329,906	358,281
ANNUITY					4,722				4,722	4,052
LIFE INCOME					57,079				57,079	60,990
NET INVESTMENT IN PLANT								2,645,637	2,645,637	2,448,607
TOTAL LIABILITIES AND FUND BALANCES	\$ 804,932	422,328	69,825	1,110,130	65,417	266,622	15,473	3,012,697	5,767,424	5,603,881

See accompanying Notes to the Financial Statements

Dollars in thousands

Statement of Changes in Fund Balances

For the year ended June 30, 2001, with comparative totals for 2000

	CURRENT FUNDS					PLANT FUNDS			June 30, 2001	June 30, 2000
	Unrestricted	Restricted	Loan Funds	Endowment and Similar Funds	Annuity and Life Income Funds	Unexpended	Retirement of Indebtedness	Investment in Plant		
REVENUES AND OTHER ADDITIONS										
UNRESTRICTED CURRENT FUND REVENUES	\$ 1,534,050								1,534,050	1,421,414
TUITION AND FEES			6,214			3,323	3,322		12,859	12,302
STATE APPROPRIATIONS						65,938			65,938	77,283
GIFTS, GRANTS, AND CONTRACTS		736,244	872	34,416	1,455	6,341		6,129	785,457	756,374
INVESTMENT INCOME		26,768	2,292	5,004	2,541	8,205	15,446		60,256	58,606
NET APPRECIATION (DEPRECIATION) IN FAIR VALUE OF INVESTMENTS				(48,595)	3,066				(45,529)	142,599
ANNUITY AND LIFE INCOME MATURITIES				454					454	813
EXPENDED FOR PLANT FACILITIES (\$72,549 FROM CURRENT FUNDS)								211,565	211,565	209,385
RETIREMENT OF INDEBTEDNESS								19,760	19,760	17,242
PROCEEDS FROM PROPERTY SALES AND STATE TIMBER SALES							1,145		1,145	281
GAIN ON REFINANCING								828	828	
TOTAL REVENUES AND OTHER ADDITIONS	1,534,050	763,012	9,378	(8,721)	7,062	83,807	19,913	238,282	2,646,783	2,696,299
EXPENDITURES AND OTHER DEDUCTIONS										
EDUCATIONAL AND GENERAL	835,809	614,183							1,449,992	1,300,959
AUXILIARY ENTERPRISES	288,648	2,100							290,748	283,565
MEDICAL CENTER	395,677	578							396,255	337,789
INDIRECT COST RECOVERED		125,806							125,806	119,088
LOAN CANCELLATIONS AND WRITE-OFFS			931						931	452
ADMINISTRATIVE AND COLLECTION COSTS			301						301	328
ACTUARIAL ADJUSTMENT FOR ANNUITIES					66				66	311
DISTRIBUTION TO LIFE BENEFICIARIES					4,163				4,163	4,105
ANNUITY AND LIFE INCOME MATURITIES					454				454	813
RETIREMENT OF INDEBTEDNESS							19,759		19,759	17,242
INTEREST OF INDEBTEDNESS							22,358		22,358	19,595
EXPENDED FOR PLANT FACILITIES						139,016			139,016	129,376
RETIREMENT OF CAPITAL ASSETS								41,252	41,252	36,247
OTHER					5,620				5,620	277
TOTAL EXPENDITURES AND OTHER DEDUCTIONS	1,520,134	742,667	1,232		10,303	139,016	42,117	41,252	2,496,721	2,250,147
TRANSFERS AMONG FUNDS—ADDITIONS (DEDUCTIONS)										
MANDATORY:										
PRINCIPAL AND INTEREST	(35,004)	(1,177)				(6,593)	42,774			
LOAN FUND MATCHING GRANT	(187)		187							
NONMANDATORY	(31,135)	16,518	(6,417)	(18,869)		65,766	(25,863)			
TOTAL TRANSFERS	(66,326)	15,341	(6,230)	(18,869)		59,173	16,911			
NET INCREASE (DECREASE) FOR THE YEAR	(52,410)	35,686	1,916	(27,590)	(3,241)	3,964	(5,293)	197,030	150,062	446,152
FUND BALANCES AT BEGINNING OF YEAR	459,687	281,805	66,523	1,037,627	65,042	153,935	7,124	2,448,607	4,520,350	4,074,198
FUND BALANCES AT END OF YEAR	\$ 407,277	317,491	68,439	1,010,037	61,801	157,899	1,831	2,645,637	4,670,412	4,520,350

See accompanying Notes to the Financial Statements

Dollars in thousands

Statement of Current Funds Revenues, Expenditures and Other Changes

For the year ended June 30, 2001, with comparative totals for 2000

	UNRESTRICTED		RESTRICTED	June 30, 2001	June 30, 2000
	General	Designated			
REVENUES					
TUITION AND FEES	\$ 197,461	63,315	5,447	266,223	246,895
STATE APPROPRIATIONS	341,451			341,451	322,079
GOVERNMENT GRANTS AND CONTRACTS	103	119,592	451,107	570,802	518,143
PRIVATE GIFTS, GRANTS, AND CONTRACTS	739	8,502	115,277	124,518	125,402
INVESTMENT INCOME:					
ENDOWMENT			15,545	15,545	12,631
TRUST INCOME			1,426	1,426	1,184
OTHER	14,609	15,281	12,520	42,410	41,823
NET APPRECIATION (DEPRECIATION) IN FAIR VALUE OF INVESTMENTS	(8,043)	5,379		(2,664)	21,393
SALES AND SERVICES OF EDUCATIONAL DEPARTMENTS	11,551	61,874	(32)	73,393	62,309
SALES AND SERVICES OF AUXILIARY ENTERPRISES	266,713			266,713	253,034
SALES AND SERVICES OF MEDICAL CENTER	416,769			416,769	355,271
OTHER	3,467	15,287	16,421	35,175	27,873
TOTAL REVENUES	1,244,820	289,230	617,711	2,151,761	1,988,037
EXPENDITURES AND MANDATORY TRANSFERS					
EDUCATIONAL AND GENERAL:					
INSTRUCTION	305,052	120,675	43,945	469,672	416,359
RESEARCH	9,766	39,777	420,594	470,137	445,916
PUBLIC SERVICE	913	4,332	8,338	13,583	10,124
ACADEMIC SUPPORT	92,913	28,923	61,857	183,693	159,357
STUDENT SERVICES	15,551	7,783	153	23,487	20,601
INSTITUTIONAL SUPPORT	50,573	51,895	7,072	109,540	89,793
OPERATION AND MAINTENANCE OF PLANT	55,941	35,471	172	91,584	78,494
SCHOLARSHIPS AND FELLOWSHIPS	16,244		72,052	88,296	80,315
EDUCATIONAL AND GENERAL EXPENDITURES	546,953	288,856	614,183	1,449,992	1,300,959
MANDATORY TRANSFERS FOR:					
LOAN FUND MATCHING GRANT	187			187	215
PRINCIPAL AND INTEREST	8,754	10,025	1,177	19,956	17,715
EDUCATIONAL AND GENERAL TRANSFERS	8,941	10,025	1,177	20,143	17,930
TOTAL EDUCATIONAL AND GENERAL	555,894	298,881	615,360	1,470,135	1,318,889
AUXILIARY ENTERPRISES:					
EXPENDITURES	288,648		2,100	290,748	283,565
MANDATORY TRANSFERS FOR PRINCIPAL AND INTEREST	4,951			4,951	3,895
TOTAL AUXILIARY ENTERPRISES	293,599		2,100	295,699	287,460
MEDICAL CENTER:					
EXPENDITURES	395,677		578	396,255	337,789
MANDATORY TRANSFERS FOR PRINCIPAL AND INTEREST	11,274			11,274	7,657
TOTAL MEDICAL CENTER	406,951		578	407,529	345,446
TOTAL EXPENDITURES AND MANDATORY TRANSFERS	1,256,444	298,881	618,038	2,173,363	1,951,795
OTHER TRANSFERS AND ADDITIONS (DEDUCTIONS)					
EXCESS OF RESTRICTED RECEIPTS OVER EXPENDITURES			19,495	19,495	28,575
NONMANDATORY TRANSFERS FROM (TO) OTHER FUNDS	(4,185) ¹	(26,950) ¹	16,518	(14,617) ¹	(33,875) ¹
NET INCREASE (DECREASE) IN FUND BALANCES FROM CURRENT YEAR ACTIVITY	\$ (15,809)¹	(36,601)¹	35,686	(16,724)¹	30,942

See accompanying Notes to the 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 individual schools, colleges, and departments, the University of Washington Medical Center, the Associated Students of the University of Washington, 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, and University of Washington Physicians Network 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 on the accrual basis. Depreciation is recorded only on Metro Tract real estate held for investment. The Statement of Current Funds Revenues, Expenditures, and other Changes is a statement of financial activities of current funds related to the current reporting period. It does not purport to present the results of operations or the net income or loss for the period as would a statement of income or a statement of revenues and expenses.

The University maintains its accounts in accordance with the principles of fund accounting in order to ensure observance of limitations and restrictions placed on the use of various resources. These resources are classified for accounting and reporting purposes into funds that are used for specified activities or objectives. Separate accounts are maintained for each fund. However, in the accompanying financial statements, funds that have similar characteristics have been combined into fund groups.

Within each fund group, fund balances restricted by outside sources are indicated and are distinguished from unrestricted funds that have been internally designated. Externally restricted funds may be utilized only in accordance with the purposes established by the sources of such funds, in contrast to unrestricted funds, which may be used in achieving any purpose of the University.

All gains and losses arising from the sale, collection, or other disposition of investments and other non-cash assets are accounted for in the fund that owns such assets. Ordinary income derived from investments, receivables, and other assets is accounted for in the fund owning such assets, except for income derived from investments of Endowment and Similar Funds, which is accounted for in the fund to which it is restricted.

Fund Classification

Current Unrestricted Funds account for all resources available for current operations that have not been restricted as to use by outside entities. Current operations include the University's educational and general-purpose expenditures, the Medical Center, and self-sustaining auxiliary enterprises.

Current Unrestricted Funds are classified as either general or designated. The purpose of this classification procedure is to separate state appropriation revenues from certain locally generated revenues. Designated funds include certain departmental fees and indirect cost revenues, as well as related expenditures. General funds in-

clude the Medical Center, auxiliary enterprises, and other unrestricted revenues and expenditures not classified as designated.

Current Restricted Funds account for resources made available to the University for operating purposes that have been restricted by outside entities. These resources generally are in the form of grants, contracts, and gifts received by the University in support of research, educational, and public service activities.

Loan Funds account for resources, primarily from the federal government, which provide loans to students.

Endowment and Similar Funds are subject to the restrictions of gift instruments requiring that the principal be invested in perpetuity and only the income be utilized. Also included are quasi-endowments established by the Board of Regents from current funds and expendable at the Board's direction consistent with the funds' restricted purposes.

Annuity and Life Income Funds account for funds received by the University subject to obligations to pay stipulated amounts periodically to the donors or to other beneficiaries. Payments terminate at the time specified in the agreement. Upon termination, principal balances are moved to the appropriate fund group.

Plant Funds account for the resources invested in and available for University land, buildings, and equipment and debt retirement.

Other Accounting Policies

Investments. Investments other than real estate or miscellaneous investments are stated at fair value. Real estate or 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 as of the close of 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 being valued.

Securities Lending Transactions. Cash collateral received from borrowers through securities lending transactions is recorded as both an asset and 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.

Investment in Plant. 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 recorded as additions. Depreciation of plant assets is not recorded.

Deferred Revenues. Deferred revenues occur when unrestricted funds have been collected in advance of an event, such as advance ticket sales and 2001 summer quarter tuition.

Tuition and Fees. A portion of tuition and fees is required by law to fund student aid (recorded in the Current Restricted and Loan Funds) and physical plant facilities (recorded in the Plant Funds). The remaining portion of tuition and fees is reported in the Current Unrestricted Fund.

State Appropriations. The State of Washington appropriates funds to the University on both an annual and biennial basis. Appropriations are recognized as revenue when the related expenditures are made.

These revenues are reported in the Current Unrestricted Fund when used to support general operations and in the Unexpended Plant Fund when used for capital projects.

Compensated Absences. University employees accrue annual leave at rates based on length of service and sick leave at the rate of one day per month. Compensated absences accrued as of June 30, 2001,

were \$36,239,000 for annual leave and \$12,498,000 for sick leave.

Tax Exemption. The University is a tax exempt organization under the provisions of Section 115 of the Internal Revenue Code and is exempt from federal income taxes on related income.

Total Columns. Total columns on the financial statements are presented only to facilitate financial analysis. The prior year summarized information has been derived from the University's 2000 Financial Statements and should be read in conjunction with those statements.

New Accounting Pronouncements

In November, 1999, the Governmental Accounting Standards Board (GASB) issued Statement 35, Basic Financial Statements—and Management's Discussion and Analysis—for Public Colleges and Universities. This pronouncement is effective next year (fiscal year 2002) and thereafter. Under the provisions of the GASB standards, the University will report as a special purpose government engaged only in business type activities (BTA). BTA reporting will require the University to present Management's Discussion and Analysis, a Statement of Net Assets, a Statement of Revenues, Expenses, and Changes in Net Assets, and a Statement of Cash Flows, as well as Notes to the Financial Statements and other required supplementary information. The University will also report capital assets net of accumulated depreciation, and report depreciation expense in the Statement of Revenues, Expenses, and Changes in Net Assets. Under BTA reporting, fund group financial statements will not be presented.

NOTE 2

Cash

Cash includes bank demand deposits, cash held by fiscal agents, \$4,056,000 cash held with escrow agents, and petty cash. All 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, 2001, bank balances of \$1,380,000 were insured by the FDIC and balances of \$20,012,000 were collateralized under the PDPC.

NOTE 3

Funds on Deposit with the State Treasurer

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 in the Endowment and Similar Funds, the University of Washington building fee in the Unexpended Plant Fund, and certain General Obligation bonds reserve funds in the Retirement of Indebtedness Fund. The fair value of these funds approximates the carrying value.

NOTE 4

Student Loans

Net student loans at June 30, 2001, consist of \$48,901,000 from federal programs and \$9,378,000 from University programs. Interest income from student loans for the year ended June 30, 2001, was \$1,529,000. Student loans are made primarily to individuals who reside in the state of Washington. The loans are unsecured and are expected to be repaid from earnings of individual borrowers.

NOTE 5

Accounts Receivable

These receivables primarily consist of patient fees receivable, state and federal grants and contracts receivable, tuition receivables, and receivables arising from the sale of investments.

TABLE 1

UNIVERSITY INVESTMENTS AND COLLATERAL FROM SECURITIES LENDING	
Investment Type	Carrying Value
CASH EQUIVALENTS	\$ 103,926
DOMESTIC FIXED INCOME	540,426
DOMESTIC FIXED INCOME – LOANED	231,070
FOREIGN FIXED INCOME	54,525
FOREIGN FIXED INCOME – LOANED	10,112
DOMESTIC EQUITY	530,492
DOMESTIC EQUITY – LOANED	24,053
FOREIGN EQUITY	104,307
FOREIGN EQUITY – LOANED	20,291
VENTURE CAPITAL	180,590
PRIVATE EQUITY	31,531
BANKRUPTCY	52,808
MORTGAGES	2,942
REAL ESTATE	4,669
MISCELLANEOUS	2,148
TOTAL INVESTMENTS	1,893,890
SHORT TERM COLLATERAL FROM SECURITIES LENDING	205,494
TOTAL INVESTMENTS AND COLLATERAL	\$ 2,099,384

Dollars in thousands

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 and approves the appointment of investment managers. The Board of Regents’ policies are carried out by the Treasurer, Board of Regents. Investment performance is reviewed quarterly.

Categorized investments are insured, registered, or held by the University’s custodial bank as an agent for the University. Investments that are not categorized include lent securities, mutual funds, venture capital, private equity arbitrage, bankruptcy, mortgages, real estate, and miscellaneous investments.

The University’s investments include certain derivative instruments and structured notes that derive their value

from a security, asset, or index. Such investments are governed by the University’s Investment Policies and Guidelines, which effectively constrain their use by establishing (a) duration parameters which limit price sensitivity to interest rate fluctuations (market risk), (b) minimum quality ratings at both the security and portfolio level, and (c) a market index as a performance benchmark.

The University’s investment portfolio includes certain foreign denominated securities. To reduce the exposure to foreign currency fluctuations inherent in such investments, the University enters into foreign currency forward contracts, futures contracts, and options. Under the University’s Investment Policies and Guidelines, such instruments are not permitted for speculative use or to create leverage. The guidelines also specify counterparty exposure limits and credit screens to reduce credit risk.

At June 30, 2001, the University had net outstanding forward commitments to sell foreign currency with a total fair value of

\$43,642,000 which equals 2.3% of the total portfolio. Unrealized and realized gains or losses are reported in the Statement of Changes in Fund Balances and are netted with the hedged securities in Table 1.

Investment Pools

The University combines most short term cash balances into the Invested Funds pool. At June 30, 2001, the Invested Funds pool totaled \$791,891,000. By University policy, departments participating in the Invested Funds pool receive one of three rates of return based on the realized yield of the portfolio. Endowment fund holdings received 7.4% for fiscal year 2001. Operating and plant fund balances of self-sustaining units received 6.7%. Other eligible fund balances received 3.0%. The difference between the actual earnings of the Invested Funds pool and the stated rates is used to support activities benefiting all University departments.

The composition of the carrying amounts of investments by type at June 30, 2001, is listed in Table 1.

Net appreciation in the fair value of investments includes both realized and unrealized gains and losses on investments. During the year ended June 30, 2001, the University realized a net gain of \$87,273,000 from the sale of investments in the two major funds. The calculation of realized gains 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 sold in the current year include the net appreciation (depreciation) of these investments reported in the prior year. The net depreciation in the fair value of investments during the year ended June 30, 2001, was \$48,193,000.

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 income distribution is 5% of the average fair value of the CEF for the previous three years.

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 \$51,000,000 at June 30, 2001. Income received from these trusts was \$1,887,000 for the year ended June 30, 2001.

Securities Lending

The University’s investment policies permit it to lend its securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. The University’s custodian lends securities of the type on loan at year-end for collateral in the form of cash or other securities. U.S. securities are loaned versus collateral valued at 102% of the fair value of the securities plus any accrued interest. Non-U.S. securities are loaned versus collateral valued at 105% of the fair value of the securities plus any accrued interest. At year-end, the University has no credit risk exposure to borrowers because the amounts the University owes the borrowers exceed the amounts the borrowers owe 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 24 days. Cash collateral is invested in a short-term investment pool which had an average weighted maturity of 34 days as of June 30, 2001. The relationship between the maturities of the investment pool and the University’s loans is affected by the maturities of the securities loans made by other entities that use the custodian’s pool, which the University cannot determine.

Non-cash collateral cannot be pledged or sold unless the borrower defaults.

Securities on loan at June 30, 2001, totaled \$285,526,000 and are listed by investment type in Table 1. The securities lending program resulted in net revenues of \$846,000 for the year ended June 30, 2001.

NOTE 7

Metropolitan Tract

The Metropolitan Tract, ten acres in downtown Seattle, is developed and managed by UNICO Properties, Inc. (UNICO) and a joint venture partnership of Four Seasons Hotels, Ltd. and The Urban Investment and Development Company in accordance with leases with the University. The UNICO lease provides that the University reimburse UNICO from Tract rental income for its advances for approved additions and modernization.

The balance at June 30, 2001, represents 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 \$69,394,000.

NOTE 8

Leases

Capital Leases

The University has certain lease agreements in effect that are considered capital leases. As of June 30, 2001, the University had recorded buildings in the amount of \$33,643,000 and equipment in the amount of \$14,476,000, related to capitalized leases.

Future minimum lease payments under capital leases, together with the present value of the net minimum lease payments, as of June 30, 2001, are as follows:

Year	Dollars in thousands
2002	\$ 8,298
2003	7,936
2004	7,246
2005	6,723
2006	6,486
THEREAFTER	40,034
TOTAL MINIMUM LEASE PAYMENTS	76,723
LESS AMOUNT REPRESENTING INTEREST	(20,797)
OBLIGATIONS UNDER CAPITAL LEASES	\$55,926

Operating Leases

The University has certain lease agreements in effect that are considered operating leases, primarily for leased building space. During the year ended June 30, 2001, the University recorded expenses of \$15,989,000 for these leases.

Future lease payments under these leases as of June 30, 2001, are as follows:

Year	Dollars in thousands
2002	\$ 15,644
2003	13,008
2004	10,568
2005	8,343
2006	6,663
THEREAFTER	36,102
	\$ 90,328

NOTE 9

Bonds and Notes Payable

Bonds and notes payable at June 30, 2001, consist of State of Washington General Obligation and Refunding Bonds, University Revenue and Facilities Bonds, and other notes as shown in Table 2 on page 43.

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 portion of special student fees to retire the related revenue and facilities bonds.

Obligations outstanding at June 30, 2001, mature in the following fiscal years:

Year	Dollars in thousands
2002	\$ 16,681
2003	14,637
2004	14,716
2005	15,362
2006	15,240
THEREAFTER	313,132
	\$ 389,768

The following State of Washington General Obligation Bond issues were partially refunded during the year ended June 30, 2001:

On June 1, 2001, \$22,980,000 of University of Washington Medical Center Bonds, Series R92A (R86D-AQB) with an average interest rate of 6.469 % were partially refunded, through the issuance of a State of Washington General Obligation Bond issue of \$22,300,000 of University of Washington Medical Center Bonds, Series R2001A (R92A(R86D-AQB)) with an average interest rate of 5.697 %.

On June 1, 2001, \$5,037,000 of Education Bonds, Series R92A (R86D-AQA) with an average interest rate of 6.415 % were partially refunded, through the issuance of a State of Washington General Obligation Bond issue of \$4,889,000 of Education Bonds, Series R2001A (R92A(R86D-AQA)) with an average interest rate of 5.696 %.

The net proceeds of these refunding issues were used to purchase U.S. Government securities, which were deposited in irrevocable trusts with escrow agents to provide for all future debt service payments on the refunded bonds. As a result, the

bonds are defeased and the liability for those bonds and the assets of the trusts have been removed from the Investment in Plant fund.

The refunding of the bonds decreased the University's total debt service payments over the next 9 years by \$2,855,000. The defeasance resulted in an accounting gain of \$828,000 and an economic gain (difference between the present values of the debt service payments on the old and new debt) of \$2,396,000.

In prior years certain Housing and Dining System Revenue Bonds and Intercollegiate Athletics Revenue Bonds were defeased by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability of the defeased bonds are not included in these financial statements. At June 30, 2001, \$43,051,000 of these defeased bonds were outstanding.

NOTE 10

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 payment, 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 Plan 2 provides retirement and disability benefits, and a cost-of-living allowance, to eligible non-academic plan members hired on or after October 1, 1977. 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.

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, 2001, was 2.43%. The contribution rate for the University at June 30, 2001, for both PERS Plans 1 and 2 was 4.67%.

The University's contributions to PERS for the years ended June 30, 2001, 2000, and 1999 were \$23,799,000, \$21,864,000, and \$33,402,000, respectively, 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 28.B.10.400 et. seq. assigns the authority to establish and amend benefit provisions to the University of Washington Board of Regents.

The Plan has a supplemental payment component which guarantees a minimum retirement benefit based upon a one-time calculation at each employee's retirement

NOTES TO FINANCIAL STATEMENTS

TABLE 2

BONDS AND NOTES PAYABLE			
Bonds Payable	Interest Rate	Fiscal Year Maturity Date	Amount Outstanding
STATE GENERAL OBLIGATION AND REFUNDING BONDS (SERIES/ISSUED):			
R-1998B/1998	4.00%	2002	\$ 2,432
R-1992A/1991, R-2001A/2001	4.50-9.00%	2002-2010	30,206
A-1992/1992, B-1992/1992, R-98A/1998, R-99/1999	4.50-6.40%	2002-2017	43,220
R-1993A, B & B-1/1992	4.75-5.75%	2002-2011	4,992
B-1993/1993	4.88-5.50%	2002-2018	7,265
A-1994/1993	4.10-4.88%	2002-2019	30,345
C-1998/1998	4.50-6.00%	2002-2024	17,815
E-1997/1997	4.80-6.00%	2002-2022	930
R-1994A, C (M)/1993	4.50-7.00%	2002-2003	680
R-1995A	5.25-5.90%	2002-2012	22,770
B-1999/1999	4.25-5.00%	2002-2024	32,910
A-2000/2000	4.40-5.63%	2011-2025	50,550
C-2000/2000	5.00-5.25%	2002-2026	5,025
TOTAL STATE GENERAL OBLIGATION AND REFUNDING BONDS			249,140
REVENUE AND FACILITIES BONDS (SERIES/ISSUED):			
HOUSING & DINING/1991, '94, '96	4.00-7.00%	2002-2022	39,445
STUDENT FACILITIES CONSTRUCTION/1972, '94, 2000	4.60-6.00%	2002-2030	51,960
INTERCOLLEGIATE ATHLETICS/1993, 2001	4.35-5.30%	2002-2014	18,475
PARKING SYSTEM/1995	5.50-6.13%	2002-2015	4,590
ALUMNI ASSOCIATION/1994	5.40-6.40%	2002-2015	19,865
TOTAL REVENUE AND FACILITIES BONDS			134,335
TOTAL BONDS PAYABLE			383,475
NOTES PAYABLE:			
BANK OF AMERICA BANK NOTE	8.47%	2002-2009	3,360
OTHER LOANS	VARIOUS	VARIOUS	2,933
TOTAL NOTES PAYABLE			6,293
TOTAL BONDS AND NOTES PAYABLE			\$ 389,768

Dollars in thousands

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, 2001, were each \$39,816,000.

The supplemental payment component of the University of Washington Retirement Plan is financed on a pay-as-you-go basis. Annual payments are not significant.

NOTE 11

Commitments and Contingencies

Authorized expenditures for construction projects unexpended as of June 30, 2001, were \$508,831,000. These expenditures will be funded from local funds and state appropriations.

Substantial amounts are received and expended by the University under federal

and state grants and contracts. This funding relates to 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*. University management believes that any liabilities arising from subsequent audits will not have a material effect on the University's financial statements.

The Office of the United States Attorney for the Western District of Washington is

NOTES TO FINANCIAL STATEMENTS

investigating the University of Washington Physicians (UWP), an affiliated organization, under the laws and regulations relating to physician billing for services provided to beneficiaries of federally-funded health care programs. As part of this investigation, the government has asked for a broad range of information from UWP and related institutions, including the University of Washington Medical Center. At this time, the University and its counsel are unable to provide any meaningful assessment of the risk to the University associated with this investigation.

The University is a defendant in a class action suit on behalf of former and current women faculty at the University, alleging gender discrimination in pay, promotion, and other terms of employment. The

University has appealed the class certification. At this time the University and its counsel are not able to determine the likely outcome of this matter.

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 involving 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 relating to 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 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, 2000 and 2001, are noted below.

	2000	2001
RESERVE AT BEGINNING OF FISCAL YEAR	\$ 32,096	\$ 31,704
INCURRED CLAIMS AND CHANGES IN ESTIMATES	7,225	10,852
CLAIM PAYMENTS	(7,617)	(5,903)
RESERVE AT END OF FISCAL YEAR	\$ 31,704	\$ 36,653
<i>Dollars in thousands</i>		