



The University of Alabama  
Financial Report  
2005-2006

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### Report of Independent Auditors

To the Board of Trustees of The University of Alabama:

In our opinion, the financial statements listed in the accompanying table of contents, which collectively comprise the financial statements of The University of Alabama (the "University"), a campus of The University of Alabama System, which is a component unit of the State of Alabama, present fairly, in all material respects, the respective financial position of the University and its aggregate discretely presented component units at September 30, 2006 and 2005, and the respective changes in financial position and cash flows, as applicable, for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the University's management. Our responsibility is to express opinions on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions.

As discussed in Note 1, the financial statements of the University are intended to present the net assets, changes in net assets and the cash flows of only that portion of the business-type activities of the financial reporting entity of The University of Alabama System that is attributable to the transactions of the University. They do not purport to, and do not, present fairly the net assets of The University of Alabama System as of September 30, 2006 and 2005 and its changes in net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 3 through 12 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted primarily 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.

*PricewaterhouseCoopers LLP*

February 28, 2007



*The President's Mansion*

## The University of Alabama Management's Discussion and Analysis (Unaudited)

This section of The University of Alabama's (the "University") annual financial report presents a discussion and analysis of the financial performance of the University during the fiscal years ended September 30, 2006 and 2005. This discussion has been prepared by management along with the financial statements and related note disclosures and should be read in conjunction with the financial statements and notes. The financial statements, notes and this discussion are the responsibility of management.

### The University of Alabama

The University, the State of Alabama's (the "State") oldest institution of higher education, is the senior comprehensive doctoral-level institution in Alabama and began instructing students in 1831. Established by constitutional provision, with subsequent statutory mandates and authorizations, the University advances the intellectual and social condition of all the people of the State through quality programs of research, instruction and service. The University bases its activities on a broad range of research programs, many of which are recognized for their contributions to the economic, technological and cultural growth of the State and region. The University is a fully accredited institution of higher learning offering a wide

variety of undergraduate, graduate and professional programs. The University is located in Tuscaloosa, Alabama.

The University is accredited by and is a member of the Southern Association of Colleges and Schools. All degree programs in professional schools and colleges subject to recognized accrediting agencies are fully accredited by the appropriate national organization. The University is a member of the National Association of State Universities and Land-Grant Colleges.

The University is governed by The Board of Trustees of The University of Alabama (the "Board"), a body corporate under Alabama Law. The Board also governs The University of Alabama at Birmingham and The University of Alabama in Huntsville, which along with the University make up The University of Alabama System (the "System"). The Board determines policy, and approves operating budgets, educational programs, facilities and capital financings for each campus, and sets the separate tuition and fee schedules applicable at each campus. Oversight responsibilities of the Alabama Commission on Higher Education ("ACHE") and annual requests for appropriations from the Alabama legislature are coordinated for each campus by the Chancellor of the System with the approval of the Board.

## Overview of Financial Statements

The University's financial statements present the financial condition, the results of operations and cash flows of the University and its discretely presented component units through five primary financial statements and notes to the financial statements. Three of the primary statements, the statement of net assets, the statement of revenues, expenses and changes in net assets and the statement of cash flows, present the financial position, changes in financial position and cash flows of the University. The financial statements of certain affiliated foundations are presented discretely from the University. The notes to the financial statements provide additional information that is essential to a full understanding of the financial statements. A summary of new accounting standards and their anticipated effects conclude the financial statements. Brief summations of Governmental Accounting Standards Board (GASB) Statements 42, 45, 46, 47, 48 and 49 are outlined.

## Statement of Net Assets

The statement of net assets presents the financial position of the University at the end of the fiscal year. This statement reflects the various assets, liabilities and net assets of the University as of the fiscal years ended September 30, 2006 and 2005.

From the data presented, readers of the statement of net assets have the information to determine the

assets available to continue the operations of the University. They may also determine how much the University owes vendors, investors and lending institutions. Finally, the statement of net assets outlines the net assets (assets minus liabilities) available to the University.

Net assets are divided into three major categories. The first category, invested in capital assets, net of debt, provides the University's equity in property, plant and equipment owned by the University. The second category is restricted net assets, which is divided into two categories, non-expendable and expendable. The corpus of non-expendable restricted resources, as it pertains to endowments, is only available for investment purposes. Donors have primarily restricted income derived from these investments to fund scholarships and fellowships. Expendable restricted net assets are available for expenditure by the University but must be spent for purposes as determined by donors and/or external entities that have placed time or purpose restrictions on the use of the assets. The last category, unrestricted net assets, discloses the net assets available to the University for any lawful purpose of the University.

At September 30, 2006, the University's assets exceeded \$1.7 billion, liabilities were \$552 million and net assets exceeded \$1.1 billion, an overall increase in net assets of \$102.4 million from 2005. A summary of the University's assets, liabilities and net assets follows:

## Condensed Statements of Net Assets

	2006	2005	2004
Current assets			
Cash and cash equivalents	\$ 35,800,558	\$ 24,532,728	\$ 38,265,963
Short-term investments	74,626,817	91,240,725	60,289,433
Accounts receivable, net	54,597,972	40,288,600	33,983,238
Other	36,411,856	29,000,057	30,834,479
Noncurrent assets			
Endowment, life income and other investments	708,691,882	675,067,084	689,803,026
Capital assets, net	732,525,105	603,685,661	502,042,568
Other	67,970,413	60,695,707	50,351,017
Total assets	<u>1,710,624,603</u>	<u>1,524,510,562</u>	<u>1,405,569,724</u>
Current liabilities	163,942,468	138,568,818	136,128,004
Noncurrent liabilities	388,316,092	329,938,332	331,159,010
Total liabilities	<u>552,258,560</u>	<u>468,507,150</u>	<u>467,287,014</u>
Net assets			
Invested in capital assets, net of related debt	408,136,653	382,682,636	350,877,390
Restricted	504,988,230	460,482,380	415,850,284
Unrestricted	245,241,160	212,838,396	171,555,036
Total net assets	<u>\$ 1,158,366,043</u>	<u>\$ 1,056,003,412</u>	<u>\$ 938,282,710</u>



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## The University's Assets

The University's cash and cash equivalents totaled \$35.8 million and \$24.5 million at the end of 2006 and 2005, respectively. At the end of 2004, total cash and cash equivalents totaled \$38.3 million. Cash in demand deposits is minimized by investing excess cash balances in investment accounts on a daily basis. The University primarily utilizes the Short-Term Fund, a System-sponsored money market type investment pool, for short term investing.

Accounts receivable largely consists of billed and unbilled Contracts and Grants and Student Receivables. Accounts receivable increased \$14.3 million from approximately \$40.3 million at September 30, 2005 to approximately \$54.6 million at September 30, 2006. Of this increase, \$8.8 million is attributable to student accounts and the student population growth incurred in 2006, while the majority of the remaining increase stems from receivables for sponsored programs.

Investments totaled \$783.3 million at the end of 2006, \$74.6 million classified as current assets and \$708.7 million classified as noncurrent. At the end of 2005, investments totaled \$766.3 million and were classified as \$91.2 million in current assets and \$675.1 in noncurrent assets. In 2004, total investments reached \$750.1 million of which \$60.3 million was classified as current assets and \$689.8 million was noncurrent assets. Total investments increased \$17.0 million (2.2%), from 2005 to 2006, primarily as a result of new investments and investment results from the System Pooled Endowment Fund offset by spending of short-term investment balances. Investments classified as current are primarily used for operating purposes while noncurrent investments primarily relate to endowment, annuity & life income agreements and capital purposes. The University's investment portfolio is primarily invested in three separate investment pools sponsored by the System. The University's investment approach maximizes current investment returns consistent with annual liquidity needs while protecting principal. The University adopts the broad objective of investing assets as to preserve their real value, enhance the purchasing power of income, and keep pace with inflation and evolving University needs.

The Eminent Scholars Program, established by the State of Alabama Act No. 85-759 and administered by the Alabama Commission on Higher Education, provides that donor gifts of \$600,000 held in a foundation affiliated with the University are eligible for \$400,000 in State matching funds. In prior years, the University received funds from donors intended to be matched in accordance with this program and transferred the corpus of these funds to The Capstone Foundation. In fiscal year 2006, the receivable from The Capstone Foundation for the Eminent Scholars

Program increased \$2.7 million from \$7.8 million in 2005 to \$10.5 million in 2006, which, combined with an increase in noncurrent pledges, represents the majority of the \$3.4 increase in other noncurrent assets. This increase stems from the recording of unrealized gains which are included, along with the corpus, in the payable to the University. During fiscal year 2005, the University received an in-kind gift for the WVUA Channel 23 television license. The University recorded an intangible asset of \$5.7 million, the estimated fair value of the license, which is included in other noncurrent assets. The total increase in other noncurrent assets in 2005 was \$6.2 million, up from \$11.7 million in 2004.

Pledges increased \$6.9 million in 2006 to \$40.9 million from \$34.0 million in 2005 and \$23.5 million in 2004. On April 8, 2006, the University announced the "Our Students. Our Future." \$500 million Capital Campaign that focuses on student scholarships, faculty support, campus facilities and priority needs.

Capital assets include land and improvements, infrastructure, buildings and improvements, equipment, construction in progress, library materials and collections. Capital assets increased \$128.8 million (21.3%) in 2006, net of annual depreciation, from \$603.7 million in 2005 to \$732.5 million in 2006. As has been the case in recent years, the required spending for capital assets continues at a brisk pace in order to provide the facilities necessary to accommodate current and future enrollment growth. Major capital expenditures during the year include Athletic renovations/construction (\$50.3 million), construction of Lakeside Residence Halls (\$23.3 million), Law School addition (\$9.5 million), renovation and improvements to Graves Hall and Fifth Avenue (\$6.8 million collectively), and construction of the Central Warehouse (\$4.2 million). For fiscal year 2005, major capital expenditures included construction of Riverside and Lakeside Residence Halls (\$31.4 million), Administrative IT System upgrades (\$5.9 million), Athletic renovations/construction (\$36.6 million), and a parking deck addition (\$7.9 million). For fiscal year 2004, major capital expenditures included Athletic facility renovations (\$21.7 million), School of Medicine construction (\$8.0 million), renovation of University Recreation Center (\$7.0 million), and construction of Shelby Integrated Science Building (\$6.3 million).

## The University's Liabilities

Current liabilities consist primarily of accounts payable, accrued liabilities and deferred revenue. Current liabilities totaled \$163.9 million in 2006 compared to \$138.6 million in 2005, an increase of \$25.3 million (18.3%). Fiscal year 2005 saw an increase of \$2.4 million (1.8%) from \$136.1 million in 2004. This increase relates to the growth in accrued salaries, wages, and benefits liabilities including an increase in

## MANAGEMENT DISCUSSION AND ANALYSIS

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accrued vacation and sick leave reserves, and higher withholding amounts correlating to the increase in compensation and benefits for fiscal year 2006. Also contributing to the increase of current liabilities was the \$4.0 million increase in supplies and other services payables and a \$2.0 million increase in construction payables. Deposits, also classified as current liabilities, increased \$2.3 million, most significantly in the Dining Dollars program.

During 2006, noncurrent liabilities increased \$58.4 million (17.7%) from \$329.9 million in 2005 to \$388.3 million in 2006 due to the issuance of the 2006A and 2006B General Revenue Bonds in July 2006 which totaled \$64.3 million. These issues will be used to fund construction of Bryant and Lakeside Residential Communities, Bryant Denny Promenade, and construction and/or renovations of certain fraternity and sorority houses. The interest rate on this debt ranges from 4.125 % to 5.9%. During 2005, noncurrent liabilities decreased \$1.2 million from \$331.1 million in 2004 primarily due to a reduction in the net outstanding long-term debt.

### The University's Net Assets

Net assets represent the residual interest in the University's assets after all liabilities are deducted. The University's net assets increased \$102.4 million, 9.7%, during the year to \$1.16 billion. This follows a 12.6% increase, or \$117.7 million, in 2005.

Net assets invested in capital assets, net of accumulated depreciation and the related outstanding debt used to finance the acquisition, construction or improvement of these capital assets, increased \$25.5 million and \$31.8 million in 2006 and 2005, respectively. Major projects undertaken in fiscal year 2006 included renovations to athletic facilities and Graves Hall, new construction of Lakeside Residence Hall and the Central Warehouse, and the Law School addition. Restricted nonexpendable net assets increased \$12.6 million from \$215.5 in 2005 to \$228.1 million in 2006 primarily due to an increase in restricted endowment funds. Restricted nonexpendable net assets experienced a \$13.5 million (6.7%) increase in 2005 from \$201.9 million in 2004, pri-

marily due to \$8.4 million in permanent additions to endowments and \$4.3 million in restricted non-expendable net assets from the Alabama Shakespeare Festival, a blended component unit of the University. Restricted expendable net assets of \$276.9 million increased \$31.9 million over 2005 net assets of \$245.0 million. Unrestricted net assets increased \$32.4 million in 2006. Unrestricted net assets increased \$41.3 million in 2005 to \$212.8 million from \$171.5 million at September 30, 2004. Increases in quasi unrestricted (\$19.7 million), auxiliaries (\$6.6 million) and education and general self supporting operations (\$5.2 million) contributed this growth in unrestricted net assets.

### Statement of Revenues, Expenses and Changes in Net Assets

Changes in total net assets as presented on the statement of net assets are based on the activity presented in the statement of revenues, expenses and changes in net assets. The purpose of the statement is to present the revenues received by the University, both operating and nonoperating, and the expenses paid by the University, both operating and nonoperating, and any other revenues, expenses, gains and losses received or expended by the University.

Generally speaking, operating revenues are received for providing goods and services to the various customers and constituencies of the University. Operating expenses are those expenses paid to acquire or produce the goods and services provided in return for the operating revenues and to carry out the mission of the University. Nonoperating revenues are revenues received for which goods and services are not provided. For example, state appropriations are nonoperating because they are provided by the Legislature to the University without the Legislature directly receiving commensurate goods and services in return for those revenues. As noted below, without the nonoperating revenues, in particular the state appropriations and private gifts, the University would not be able to cover its costs of operations. These sources are critical to the University's financial stability and directly impact the quality of its programs.



A summary of the University's revenues, expenses and changes in net assets follows:

### Condensed Statements of Revenues, Expenses and Changes in Net Assets

	2006	2005	2004
Operating revenues			
Tuition and fees	\$ 168,337,662	\$ 135,238,566	\$ 114,751,427
Less: scholarship allowances	(32,917,319)	(26,937,891)	(24,630,219)
Tuition and fees, net	135,420,343	108,300,675	90,121,208
Sponsored programs	65,092,207	65,589,747	65,492,376
Auxiliary, net	104,203,777	90,801,084	71,727,171
Sales and services of educational activities	9,973,238	8,792,936	9,396,243
Other	11,463,330	13,607,777	12,209,213
Total operating revenues	326,152,895	287,092,219	248,946,211
Operating expenses	486,263,506	435,277,439	399,466,345
Operating loss	(160,110,611)	(148,185,220)	(150,520,134)
Nonoperating revenues (expenses)			
State appropriations	145,930,652	126,910,824	123,076,215
Gifts	41,007,849	56,072,769	25,877,659
Grants	1,315,148	1,813,205	1,576,469
Investment income, net	56,484,511	72,376,705	67,248,521
Interest expense	(8,885,356)	(14,496,816)	(4,645,089)
Other nonoperating expenses, net	(1,407,278)	(20,588)	(211,793)
Net nonoperating revenues	234,445,526	242,656,099	212,921,982
Income before other changes in net assets	74,334,915	94,470,879	62,401,848
Other changes in net assets			
Capital gifts and grants	16,113,911	7,709,438	11,544,774
Additions to permanent endowments	11,913,805	15,540,385	9,686,477
Increase in net assets	102,362,631	117,720,702	83,633,099
Net assets, beginning of year	1,056,003,412	938,282,710	854,649,611
Net assets, end of year	\$ 1,158,366,043	\$ 1,056,003,412	\$ 938,282,710

The statement of revenues, expenses and changes in net assets (the "SRECNA") reflects increases in net assets of \$102.4 million, \$117.7 million, and \$83.6 million for the fiscal years ended September 30, 2006, 2005, and 2004, respectively. As noted in the SRECNA, the University experienced operating losses in fiscal year 2006, 2005, and 2004 of \$160.1 million, \$148.2 million, and \$150.5 million respectively. These operating losses highlight the University's dependency on nonoperating revenues, state appropriations and private gifts, to meet its cost of operations and provide funds for the acquisition of capital equipment.

In fiscal year 2006, the University received \$145.9 million in State appropriations to be used for operations and \$41.0 million in private gifts. These revenues, along with an additional \$56.5 million of net investment income assisted in offsetting the University's operating loss of \$160.1 million. The University received \$126.9 million in State appropriations, \$56.1 million in gifts and had \$72.4 million in net investment income in 2005 which assisted in offsetting the \$148.2 million operating loss experienced in 2005. In fiscal year 2004, the University received \$123.1 million in State appropriations, \$25.9 million in gifts and had \$67.2 million in net investment income which contributed to the offset of the \$150.5 million operating loss.



## MANAGEMENT DISCUSSION AND ANALYSIS

Tuition and fees revenue, net of scholarship allowances, increased \$27.1 million to \$135.4 million in 2006 from \$108.3 million in 2005 due to enrollment growth of approximately 900 students in the Fall semester and over 1,000 students in the Spring semester. Tuition rate increases in 2006 of 5% in-state and 6.7% out-of-state also contributed to this increase. The University's current initiative to increase enrollment to 28,000 by 2010 will result in tuition increases in correlation to the population growth. In 2005, tuition and fees, net of scholarship allowances increased \$18.2 million from \$90.1 million in 2004. Tuition rates are reviewed annually by the University and presented to the Board of Trustees for approval.

Auxiliary revenue increased \$13.4 million to \$104.2 million in 2006 from \$90.8 million in 2005, which followed a \$19.1 million increase in 2004. The University's auxiliaries are comprised of athletics, food services, housing, supply store, telecommunications, and other miscellaneous auxiliary enterprises. In 2006, The Bryant-Denny Stadium expansion was completed. This addition created 8300 seats and generated an additional \$7 million in revenue for the Intercollegiate Athletics Department. In addition, other auxiliary enterprises that experienced increased revenue in correlation to the growth of the student population include Housing and The Supply Store.

Gift revenues decreased \$15.1 million to \$41 million from \$56.1 million in 2005. During fiscal year 2005, gifts increased \$29.7 million from \$25.9 million in 2004. The increase in 2005 was primarily due to a \$12.5 million increase of gifts to the Crimson Tide Foundation and a \$10.1 million increase in the recognition of Athletic gifts.

Investment income decreased \$15.9 million from \$72.4 million in 2005 to \$56.5 million in 2006. Investment income in 2006 is largely comprised of \$33 million of earnings and realized gains from endowments invested in the System-sponsored investment pool, earnings on funds other than endowments invested in other System-sponsored investment pools of \$10.1 million and \$8.5 million in unrealized gains. Earnings on unspent bond proceeds totaled \$3 million in 2006. Unrealized and realized gains declined \$17.5 million from \$38.7 million in 2005 to \$23.9 million in 2006.

Interest expense incurred by the University in 2006 totaled \$15.4 million, netted to \$8.9 million by interest capitalized for various construction projects. Interest expense decreased \$5.6 million between 2006 and 2005 due to an increase in capitalized interest.

### Operating Expenses (by natural classification)

	2006	2005	2004
Salaries, wages and benefits	\$ 304,103,690	\$ 274,166,002	\$ 252,577,048
Scholarships and fellowships	10,817,099	10,087,071	13,069,809
Supplies and other services	110,818,018	105,052,148	93,255,742
Utilities	22,054,338	16,030,990	14,877,715
Depreciation	38,470,361	29,941,228	25,686,031
Total operating expenses	<u>\$ 486,263,506</u>	<u>\$ 435,277,439</u>	<u>\$ 399,466,345</u>

Salaries, wages and benefits increased \$29.9 million to \$304.1 million in 2006 from \$274.2 million in 2005 which followed a \$21.6 million increase in 2004. The University's most important resource is its outstanding faculty and staff. In fiscal year 2006, 62.5% of the University's total operating expenses were for employee compensation. As of September 2006, the University employed approximately 4,000 full-time, permanent employees. Even though the major portion of the operating expenses are focused on employee compensation, the University must continue to focus on being more competitive with peer institutions and non-academic employers. The reality of the national landscape requires attractive

compensation and benefit packages in order to recruit and retain this important resource that so directly impacts the University's ability to accomplish its mission. A merit compensation pool of 5% was provided for faculty and staff with additional funds provided for merit based equity increases. In addition, funding was used to adjust the Maintenance Pay Plan and the Custodial and Grounds Career Ladders as well as the main staff pay structure for non-facilities related positions. Also, funding was provided for faculty promotions and new faculty, to bring staff salaries to new minimums, and to provide an increase of 5% for graduate assistants.



Utilities increased approximately \$6.0 million in 2006 while supplies and other services increased \$5.8 million. This increase is attributable to rising utility costs and additional buildings opened on campus. Depreciation expense increased primarily due to new projects being completed and placed into service.

In addition to their natural classification, operating expenses can also be reported by their functional classification. This method reflects, by function of the University, amounts expended in areas such as Instruction, Research and Operations and Maintenance and is used most commonly for comparative reporting purposes.

### 2006 Operating Expenses (by functional classification)

	Salaries, wages and benefits	Scholarships and fellowships	Supplies and other services	Depreciation	Total
Instruction	\$ 122,156,420	\$ 1,114,738	\$ 20,233,924	\$ -	\$ 143,505,082
Research	13,595,882	336,036	12,146,981	-	26,078,899
Public service	24,354,248	175,099	13,529,197	-	38,058,544
Academic support	33,031,082	690,383	11,550,195	-	45,271,660
Student services	8,860,758	108,298	4,618,621	-	13,587,677
Institutional support	31,842,872	12,192	9,897,677	-	41,752,741
Operations and maintenance	24,287,441	37,075	14,550,823	-	38,875,339
Scholarships and fellowships	10,781,738	5,524,958	603,267	-	16,909,963
Auxiliary enterprises	35,193,249	2,818,320	45,741,671	-	83,753,240
Depreciation	-	-	-	38,470,361	38,470,361
	<u>\$ 304,103,690</u>	<u>\$ 10,817,099</u>	<u>\$ 132,872,356</u>	<u>\$ 38,470,361</u>	<u>\$ 486,263,506</u>

### 2005 Operating Expenses (by functional classification)

	Salaries, wages and benefits	Scholarships and fellowships	Supplies and other services	Depreciation	Total
Instruction	\$ 111,089,828	\$ 486,395	\$ 20,448,730	\$ -	\$ 132,024,953
Research	13,745,344	407,319	10,316,065	-	24,468,728
Public service	25,604,990	118,659	11,474,176	-	37,197,825
Academic support	26,178,518	37,936	10,744,299	-	36,960,753
Student services	7,752,691	31,482	3,807,391	-	11,591,564
Institutional support	28,355,218	1,917	4,498,653	-	32,855,788
Operations and maintenance	19,160,387	2,134	14,539,083	-	33,701,604
Scholarships and fellowships	7,488,165	7,906,317	93,847	-	15,488,329
Auxiliary enterprises	34,790,861	1,094,912	45,160,894	-	81,046,667
Depreciation	-	-	-	29,941,228	29,941,228
	<u>\$ 274,166,002</u>	<u>\$ 10,087,071</u>	<u>\$ 121,083,138</u>	<u>\$ 29,941,228</u>	<u>\$ 435,277,439</u>

## Capital Assets and Debt Administration

At September 30, 2006, the University had \$1.1 billion invested in capital assets, net of accumulated depreciation of \$351.1 million. Depreciation charges totaled \$38.5 million for the current fiscal

year. Buildings and fixed equipment alone increased \$140.2 million creating an increase in accumulated depreciation of \$13.5 million.

## MANAGEMENT DISCUSSION AND ANALYSIS

The following schedule summarizes the University's capital assets, net of accumulated depreciation:

### Capital Assets, Net of Accumulated Depreciation

	2006	2005	2004
Land	\$ 9,216,339	\$ 9,216,339	\$ 9,089,098
Land improvements	3,181,139	3,591,291	4,999,684
Infrastructure	6,908,300	8,289,147	11,452,896
Buildings and fixed equipment	653,802,941	513,575,992	416,147,438
Equipment	41,951,101	46,118,168	37,849,956
Library materials	17,465,285	22,894,724	22,503,496
	<u>\$ 732,525,105</u>	<u>\$ 603,685,661</u>	<u>\$ 502,042,568</u>

The University continues to invest in various capital projects on campus to maintain competitiveness in academic arenas and attract and retain students. Capital asset expenditures for fiscal year 2006 included (in millions):

• Athletic facility renovations	\$50.3
• Lakeside Residence Hall	\$23.3
• Law School addition	\$9.5
• Graves Hall renovation	\$4.6
• Central Warehouse	\$4.2
• Fifth Avenue improvements	\$2.2

Capital asset expenditures for fiscal year 2005 (in millions):

• Athletic facility renovations	\$36.6
• Riverside Residence Hall	\$28.4
• ten Hoor parking deck addition	\$7.9
• Administrative IT system upgrade	\$5.9
• Tutwiler Hall renovation and roof	\$4.4
• Child Development Center	\$3.9
• East & West Substation	\$3.3
• Student Health addition	\$3.4
• Law School addition	\$3.2
• Lakeside Residence Hall	\$3.0

The University plans to fund ongoing construction projects with debt proceeds, private gifts and various Federal and State grants.

In July 2006, the University issued two separate bond series: Series 2006A for \$40,575,000 and Series 2006B for \$23,750,000. Standard & Poor's Credit Markets Service, Moody's Investors Service and Fitch Ratings have assigned the respective ratings of "AAA" and "AA" for the 2006A and 2006B series, respectively. The series 2006A and 2006B, fixed rate issues, were issued for the purposes of financing the costs of constructing and equipping various capital improvements on the University campus, including Lakeside Residence and Dining Hall, Bryant Residence Hall, various fraternity and sorority houses and Bryant Denny Promenade.

At September 30, 2006, the University had \$383.0 million in debt outstanding. Debt obligations bear interest at fixed and variable rates ranging from 3.0% to 7.75% and mature at various dates through fiscal year 2036.

The University's outstanding debt obligations are summarized below:

### Schedule of Long Term Debt

	2006	2005	2004
Bonds payable	\$ 373,800,000	\$ 314,745,000	\$ 319,780,000
Notes payable	8,974,240	9,552,040	4,848,784
Capital leases payable	217,013	323,862	442,083
	<u>\$ 382,991,253</u>	<u>\$ 324,620,902</u>	<u>\$ 325,070,867</u>



## Statement of Cash Flows

The statement of cash flows presents the significant sources and uses of cash. The University's cash, primarily held in demand deposit accounts, is minimized by sweeping available cash balances into investment accounts on a daily basis.

### Condensed Statement of Cash Flows

	2006	2005
Cash received from operations	\$ 313,285,139	\$ 272,764,955
Cash payments for operations	(434,097,125)	(387,827,791)
Net cash used in operating activities	(120,811,986)	(115,062,836)
Net cash provided by noncapital financing activities	190,971,195	170,256,166
Net cash used in capital and related financing activities	(102,494,782)	(126,672,953)
Net cash provided by investing activities	42,580,624	56,130,407
Net increase (decrease) in cash and cash equivalents	10,245,051	(15,349,216)
Cash, beginning of year	30,921,653	46,270,869
Cash, end of year	41,166,704	30,921,653

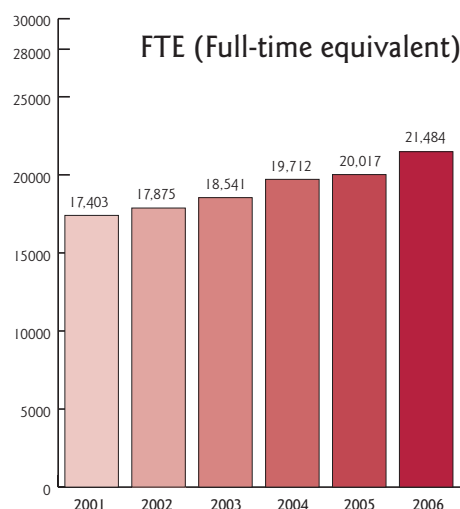
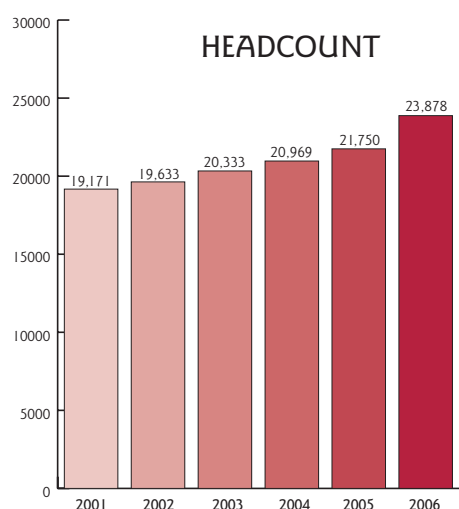
The University used \$120.8 million of cash for operating activities in 2006, offset by approximately \$191.0 million of cash provided by noncapital financing activities. Similarly, in 2005, \$115.1 million of cash used for operating activities was offset by \$170.3 million in cash provided by noncapital financing activities. Noncapital financing activities, as defined by the GASB, include state educational appropriations and gifts received for other than capital purposes that are used to support operating expenses.

Cash of \$102.5 million and \$126.7 million in 2006 and 2005, respectively, was used for capital and related financing activities, primarily for purchases of capital assets and principal and interest payments, partially offset by sources that included bond proceeds, gifts, grants and contracts for capital purposes.

Cash provided by investing activities totaled \$42.6 million in 2006 and \$56.1 million in 2005. The differences are primarily a result of additional purchases of investments in 2006 resulting in less cash from investing.

### Enrollment

Headcount enrollment at the University reached 23,878 in 2006, a significant increase of 2,128, while Full-time equivalent (“FTE”) enrollment exceeded 21,000. This increase advances the University closer to its goal of reaching enrollment of 28,000 by the fall of 2010.



### Economic Factors That Will Affect the Future

A crucial element to the University’s future will continue to be our relationship with the State of Alabama as we work to maintain competitive tuition while providing an outstanding college education for our students. For 2005-2006, the University ranked 13<sup>th</sup> among public universities and 31<sup>st</sup> overall in enrollment of National Merit Scholars. We continuously strive to attract the best students while increasing the intrinsic and marketable value of education offered at The University of Alabama.

There is a direct relationship between the growth of State support and the University’s ability to control tuition growth as declines in State appropriations adversely affect tuition levels. Major financial strengths of the University include a diverse source of revenues, including State appropriations, tuition and fees (net of scholarship allowances), auxiliary units’ revenue, private support and federally sponsored grants and contracts.

The University must have campus facilities that are competitive in order to facilitate its mission of education, research and public service and to meet student enrollment goals. The University continues to execute its long-term plan to modernize and expand its teaching, research and student facilities with a balance of new construction and technology.

The continuous improvement of the University’s aesthetic appeal offers visitors, current and prospective students, employees and the surrounding communities an attractive and appealing atmosphere in which to live, work and enjoy.

The University’s private support is fundamental in meeting budgetary needs. Gifts received are testaments to the high regard in which its alumni, corporations, foundations and other supporters hold the University. The level of private support underscores the continued confidence among donors in the quality of the University’s programs and the importance of its mission. At the same time, economic pressures affecting donors may also affect the future level of support the University receives from corporate and individual giving.

### Requests for Information

These financial statements are designed to provide a general overview of the University of Alabama and its component units’ financial activities and to demonstrate the University’s accountability. Questions concerning any of the information provided in this report or requests for additional information, including the separate financial reports of the discretely presented and blended component units of the University, should be addressed to the Office of Finance, The University of Alabama, Box 870136, Tuscaloosa, Alabama, 35487.



**The University of Alabama**  
**Statements of Net Assets**  
**September 30, 2006 and 2005**

Assets	2006	2005
Current assets		
Cash and cash equivalents	\$ 35,800,558	\$ 24,532,728
Short-term investments	74,626,817	91,240,725
Accounts receivable, net	54,597,972	40,288,600
Current portion of loans receivable	2,948,350	2,888,761
Current portion of pledges receivable	9,125,194	7,054,751
Inventories	5,291,695	5,305,093
Prepaid and deferred expenses	16,918,843	12,111,499
Other current assets	2,127,774	1,639,953
Total current assets	201,437,203	185,062,110
Noncurrent assets		
Restricted cash and cash equivalents	5,366,146	6,388,925
Endowment and life income investments	451,578,206	419,542,146
Investments for capital activities	145,370,001	150,347,334
Other long-term investments	111,743,675	105,177,604
Student loans receivable, net	9,560,625	9,480,918
Pledges receivable, net	31,783,759	26,914,664
Capital assets, net	732,525,105	603,685,661
Other noncurrent assets	21,259,883	17,911,200
Total noncurrent assets	1,509,187,400	1,339,448,452
Total assets	<u>\$ 1,710,624,603</u>	<u>\$ 1,524,510,562</u>
Liabilities and net assets		
Current liabilities		
Accounts payable and accrued liabilities	\$ 81,204,445	\$ 60,667,792
Deferred revenue	68,754,995	67,510,270
Deposits	6,341,025	4,086,885
Current portion of long-term debt	7,642,003	6,303,871
Total current liabilities	163,942,468	138,568,818
Noncurrent liabilities		
Federal refundable loans	9,653,244	9,841,527
Other liabilities	4,577,756	3,971,335
Long-term debt, net	374,085,092	316,125,470
Total noncurrent liabilities	388,316,092	329,938,332
Total liabilities	552,258,560	468,507,150
Net Assets		
Invested in capital assets, net of related debt	408,136,653	382,682,636
Restricted		
Nonexpendable	228,047,012	215,449,644
Expendable	276,941,218	245,032,736
Unrestricted	245,241,160	212,838,396
Total net assets	1,158,366,043	1,056,003,412
Total liabilities and net assets	<u>\$ 1,710,624,603</u>	<u>\$ 1,524,510,562</u>

*See accompanying notes to financial statements.*

## The University of Alabama Discretely Presented Component Units Statements of Financial Position 2006 and 2005

	2006	2005
<b>Assets</b>		
Cash and cash equivalents	\$ 1,291,470	\$ 1,246,451
Investments	69,744,252	66,278,003
Contributions receivable, net	1,902,485	2,871,866
Other receivables	1,182,446	1,600,425
Other assets	452,449	584,339
Property, plant and equipment, net	191,548	196,038
Total assets	<u>\$ 74,764,650</u>	<u>\$ 72,777,122</u>
<b>Liabilities and net assets</b>		
Accounts payable and accrued liabilities	\$ 479,571	237,551
Deferred revenue	551,265	499,428
Annuities payable	2,755,547	2,897,538
Other liabilities	11,143,063	7,938,990
Total liabilities	<u>14,929,446</u>	<u>11,573,507</u>
<b>Net Assets</b>		
Unrestricted	12,447,636	11,923,152
Temporarily restricted	24,284,080	27,807,538
Permanently restricted	23,103,488	21,472,925
Total net assets	<u>59,835,204</u>	<u>61,203,615</u>
Total liabilities and net assets	<u>\$ 74,764,650</u>	<u>\$ 72,777,122</u>

*See accompanying notes to financial statements.*



**The University of Alabama**  
**Statements of Revenues, Expenses**  
**and Changes in Net Assets**  
**For the Years Ended September 30, 2006 and 2005**

	2006	2005
Operating revenues		
Tuition and fees	\$ 168,337,662	\$ 135,238,566
Less: scholarship allowances	(32,917,319)	(26,937,891)
Tuition and fees, net	135,420,343	108,300,675
Federal grants and contracts	50,474,698	53,190,925
State grants and contracts	12,970,100	9,059,681
Local grants and contracts	376,152	115,166
Private grants and contracts	1,271,257	3,223,975
Sales and services of educational activities	9,973,238	8,792,936
Auxiliary sales & services	104,203,777	90,801,084
Other operating revenues	11,463,330	13,607,777
Total operating revenues	326,152,895	287,092,219
Operating expenses		
Salaries, wages and benefits	304,103,690	274,166,002
Scholarships and fellowships	10,817,099	10,087,071
Supplies and other services	110,818,018	105,052,148
Utilities	22,054,338	16,030,990
Depreciation	38,470,361	29,941,228
Total operating expenses	486,263,506	435,277,439
Operating loss	(160,110,611)	(148,185,220)
Nonoperating revenues (expenses)		
State appropriations	145,930,652	126,910,824
Gifts	41,007,849	56,072,769
Grants	1,315,148	1,813,205
Investment income, net	56,484,511	72,376,705
Interest expense	(8,885,356)	(14,496,816)
Other nonoperating expenses, net	(1,407,278)	(20,588)
Net nonoperating revenues	234,445,526	242,656,099
Income before other changes in net assets	74,334,915	94,470,879
Other changes in net assets		
Capital gifts and grants	16,113,911	7,709,438
Additions to permanent endowments	11,913,805	15,540,385
Increase in net assets	102,362,631	117,720,702
Net assets, beginning of year	1,056,003,412	938,282,710
Net assets, end of year	\$ 1,158,366,043	\$ 1,056,003,412

*See accompanying notes to financial statements.*

**The University of Alabama  
Discretely Presented Component Units  
Statements of Activities and Changes in Net Assets  
For the Years Ended 2006 and 2005**

	2006	2005
Revenues, gains and other support		
Gifts	\$ 8,170,085	\$ 9,463,148
Investment income	2,425,338	2,247,076
Unrealized and realized gains on investments, net	1,706,406	3,414,387
Royalties	1,141,593	1,129,106
Other	744,864	842,902
Total revenues, gains and other support	<u>14,188,286</u>	<u>17,096,619</u>
Expenses and losses		
Program services	11,013,317	6,196,283
Fundraising	453,399	448,226
General and administrative	1,416,974	1,578,583
Change in value of split-interest agreements	92,424	184,206
Total expenses and losses	<u>12,976,114</u>	<u>8,407,298</u>
Change in net assets	1,212,172	8,689,321
Net assets, beginning of year	61,203,615	52,514,294
Cumulative effect of adjustment (Note 1)	<u>(2,580,583)</u>	<u>-</u>
Net assets, end of year	<u>\$ 59,835,204</u>	<u>\$ 61,203,615</u>

*See accompanying notes to financial statements.*





**The University of Alabama**  
**Statements of Cash Flows**  
**For the Years Ended September 30, 2006 and 2005**

	2006	2005
Cash flows from operating activities		
Student tuition and fees	\$ 136,895,962	\$ 112,247,380
Grants and contracts	59,052,900	64,427,491
Receipts from sales and services of:		
Educational activities	11,063,894	8,273,773
Auxiliary enterprises, net	96,192,561	73,524,047
Payments to suppliers	(119,992,705)	(114,588,855)
Payments to employees	(297,852,859)	(264,519,363)
Payments for scholarships and fellowships	(16,112,265)	(8,719,573)
Student loan (disbursements) collections	(139,296)	384,165
Other receipts, net	10,079,822	13,908,099
Net cash used in operating activities	<u>(120,811,986)</u>	<u>(115,062,836)</u>
Cash flows from noncapital financing activities		
State appropriations	145,930,652	126,910,824
Private gifts	43,049,793	48,521,177
Grants	1,315,148	1,813,205
Student direct lending receipts	88,461,597	66,893,373
Student direct lending disbursements	(88,248,311)	(72,984,043)
Deposits from (to) affiliates, net	1,852,570	(844,515)
Other disbursements, net	(1,390,254)	(53,855)
Net cash provided by noncapital financing activities	<u>190,971,195</u>	<u>170,256,166</u>
Cash flows from capital and related financing activities		
Proceeds from issuance of bonds and notes	64,935,612	5,000,000
Capital gifts, grants and contracts	7,471,068	20,267,426
Purchases of capital assets	(153,689,386)	(131,694,953)
Principal payments on capital debt	(5,954,649)	(5,449,965)
Interest payments on capital debt	(15,257,427)	(14,795,461)
Net cash used in capital and related financing activities	<u>(102,494,782)</u>	<u>(126,672,953)</u>
Cash flows from investing activities		
Interest and dividends on investments, net	35,643,742	30,256,334
Proceeds from sales and maturities of investments	89,225,384	99,660,641
Purchase of investments	(82,288,502)	(73,786,568)
Net cash provided by investing activities	<u>42,580,624</u>	<u>56,130,407</u>
Net increase (decrease) in cash and cash equivalents	10,245,051	(15,349,216)
Cash and cash equivalents, beginning of year	30,921,653	46,270,869
Cash and cash equivalents, end of year	<u>\$ 41,166,704</u>	<u>\$ 30,921,653</u>
Reconciliation of cash and cash equivalents to the statement of net assets		
Cash and cash equivalents in current assets	\$ 35,800,558	\$24,532,728
Restricted cash and cash equivalents	5,366,146	6,388,925
Total cash and cash equivalents	<u>\$ 41,166,704</u>	<u>\$30,921,653</u>

*See accompanying notes to financial statements.*

## FINANCIAL STATEMENTS

	2006	2005
Reconciliation of operating loss to net cash used in operating activities		
Operating loss	\$ (160,110,611)	\$ (148,185,220)
Adjustments to reconcile operating loss to net cash used in operating activities		
Depreciation expense	38,470,361	29,941,228
Bad debt expense	392,957	289,802
Changes in assets and liabilities		
Accounts and other receivables	(14,585,514)	28,051
Inventories and other assets	(4,814,644)	6,582,026
Accounts payable and accrued liabilities	18,524,061	10,407,969
Deferred revenue	1,311,404	(14,126,692)
Net cash used in operating activities	<u>\$ (120,811,986)</u>	<u>\$ (115,062,836)</u>
Supplemental noncash activities information		
Gift of capital assets	\$ 4,997,250	\$ 417,177
Gift of investments	1,387,683	95,044
Capital assets acquired with a liability at year end	19,759,998	17,746,250
Gain (loss) on the disposal of capital assets	105,441	(555,175)
Gift of television license	-	5,709,300

*See accompanying notes to financial statements.*







## THE UNIVERSITY OF ALABAMA NOTES TO FINANCIAL STATEMENTS Years Ended September 30, 2006 and 2005

### Note 1 – Summary of Significant Accounting Policies

The University of Alabama (the “University”), Tuscaloosa, Alabama is one of three campuses of The University of Alabama System (the “System”) which is a component unit of the State of Alabama. These financial statements include individual schools, colleges and departments and certain affiliated operations determined to be a part of the University’s financial reporting entity. The financial statements of the University are intended to present the financial position, changes in financial position and the cash flows of only that portion of the business-type activities of the System that are attributable to the transactions of the University. The System is recognized as an organization exempt from Federal Income tax under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(3) of the Internal Revenue Code.

The University, as a public institution, prepares its financial statements in accordance with accounting principles generally accepted in the United States of America, as prescribed by the Governmental Accounting Standards Board (“GASB”), including all applicable effective statements of the GASB and all statements of the Financial Accounting Standards Board (“FASB”) through November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. The University has elected not to apply FASB pronouncements issued after November 30, 1989.

GASB Statement No. 35, *Basic Financial Statements and Management’s Discussion and Analysis for Public Colleges and Universities*, establishes standards for external financial reporting for public college and universities and requires that resources be classified for accounting and reporting purposes into the following three net asset categories:

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

- **Restricted:**

**Nonexpendable** – Net assets subject to externally imposed stipulations that they be maintained permanently by the University. Such assets include the corpus of the University's permanent endowment funds.

**Expendable** – Net assets whose use by the University is subject to externally imposed stipulations that can be fulfilled by actions of the University pursuant to those stipulations or that expire by the passage of time.

- **Unrestricted:** Net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or may otherwise be limited by contractual agreements with outside parties. Substantially all unrestricted net assets are internally designated for academic, research and capital programs.

For financial reporting purposes, the University is considered a special-purpose government engaged only in business-type activities as defined by GASB Statement No. 35. Business-type activities are those that are financed in whole or in part by fees charged to external parties for goods or services. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred.

The University's policy for defining operating activities as reported on the statements of revenues, expenses and changes in net assets are those that generally result from exchange transactions such as payments received for providing services and payments made for services or goods received. Certain significant revenue streams relied upon for operations are recorded as nonoperating revenues, including state appropriations, private gifts and investment income.

Auxiliary enterprise revenues primarily represent revenues generated by university housing, intercollegiate athletics, supply store and student related activities. Revenues received for capital activities are considered neither operating nor nonoperating activities

and are presented after nonoperating activities on the accompanying statements of revenues, expenses and changes in net assets.

All internal sales between University departments from sales and service units (fleet services, postal services, telecommunications, etc.) have been eliminated in the accompanying financial statements.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates. The estimates susceptible to significant changes include those used in determining the allowance for uncollectible accounts, useful lives of capital assets, reserves for self insurance and reserves for general and professional liability claims. Although some variability is inherent in these estimates, management believes that the amounts provided are adequate.

**Scope of Statements** – GASB Statement No. 14, The Financial Reporting Entity, as amended, requires governmental entities to include in their financial statements as a component unit, organizations that are legally separate entities for which the governmental entity, as a primary organization, is financially accountable.

The Alabama Shakespeare Festival, Inc. (the "Festival") has been presented as a blended component unit within the University's financial statements. The Festival's financial statements include the financial data of its discretely presented component unit, The Alabama Shakespeare Endowment Trust (the "Endowment Trust"). The Endowment Trust, a legally separate entity, was established to support the Festival's activities. The Festival is a regional theater dedicated to providing both classical and artistic endeavors and to promote and contribute to the educational resources available in these areas. The University has sole voting power and acts through its chosen designees, the Festival's current Board of Directors.





Summary financial information of the Festival for the years ended September 30, 2006 and 2005 is included in the University's financial statements as follows:

	2006	2005
<b>Assets</b>		
Cash	\$ 785,363	\$ 227,812
Other current assets	1,360,139	949,381
Endowment investments	14,374,052	16,887,966
Other long-term investments	10,581	-
Other noncurrent assets	2,133,992	2,645,229
<b>Total assets</b>	<b>\$ 18,664,127</b>	<b>\$ 20,710,388</b>
<b>Liabilities and Net Assets</b>		
Current liabilities	\$ 2,096,230	\$ 1,619,115
Noncurrent liabilities	884,511	253,223
Net assets	15,683,386	18,838,050
<b>Total liabilities and net assets</b>	<b>\$ 18,664,127</b>	<b>\$ 20,710,388</b>
<b>Major components of revenues, expenses and changes in net assets</b>		
Operating revenues	\$ 3,536,052	\$ 3,142,655
Operating expenses	(9,758,521)	(9,133,160)
Net nonoperating revenues	3,067,805	10,752,708
<b>Change in net assets</b>	<b>\$ (3,154,664)</b>	<b>\$ 4,762,203</b>

The Crimson Tide Foundation ("CTF"), chartered on October 1, 2004 with a fiscal year end of June 30, has also been presented as a blended component unit within the University's financial statements. CTF is a nonprofit corporation organized exclusively to promote and encourage a continuing interest in and loyalty to the intercollegiate athletics program at the University; to promote, encourage and support the construction, improvement and renovation of athletic facilities; to encourage alumni and friends of the University to generously support the University and its Athletics Department by gifts, devises

and bequests; to support, promote and encourage the education of University students; to provide and contribute to scholarship funding to the University for the University's student-athletes, both men and women, in all of the University's intercollegiate sports; and to conduct any and all appropriate activities, in accordance with National Collegiate Athletic Association and Southeastern Conference policies on institutional control, in order to accomplish the above objects and purposes. The foundation is governed by a Board of Directors that is appointed by the University's Board.

## NOTES TO FINANCIAL STATEMENTS

Summary financial information of CTF for the years ended June 30, 2006 and June 30, 2005 is included in the University's financial statements as follows:

	2006	2005
<b>Assets</b>		
Cash	\$ 2,626,549	\$ 1,597
Investments	6,166,150	3,499,791
Current contributions receivable, net	6,434,553	6,113,204
Other current assets	107,579	68,630
Restricted cash	255,000	583,397
Endowment investments	35,107	-
Noncurrent contributions receivable, net	22,619,362	23,118,279
Equipment, net	5,039,670	5,475,042
<b>Total assets</b>	<b>\$ 43,283,970</b>	<b>\$ 38,859,940</b>
<b>Liabilities and Net Assets</b>		
Current liabilities	\$ 420,806	\$ 373,645
Noncurrent liabilities	4,198,579	4,596,257
Net assets	38,664,585	33,890,038
<b>Total liabilities and net assets</b>	<b>\$ 43,283,970</b>	<b>\$ 38,859,940</b>
<b>Major components of revenues, expenses and changes in net assets</b>		
Operating revenues	\$ 147,231	\$ 132,802
Operating expenses	(6,441,641)	(237,478)
Net nonoperating revenues	11,068,957	33,994,714
<b>Change in net assets</b>	<b>\$ 4,774,547</b>	<b>\$ 33,890,038</b>

As of October 1, 2003, the University implemented GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units*, an amendment to GASB Statement No. 14. The primary objective of Statement No. 14 is to determine whether all entities associated with a primary government are potential component units and should be evaluated for inclusion in the financial reporting entity. Statement No. 39 amends Statement No. 14 and provides additional guidance to determine whether certain organizations for which the primary government is not financially accountable should be reported as component units based on the nature and significance of their relationship with the primary government. Generally, it requires reporting as a component unit, an organization that raises and holds economic resources for the direct benefit of a governmental unit.

The University has three foundations which have been organized exclusively for charitable, scientific and educational purposes for the benefit of the University. The three foundations are The National Alumni Association of The University of Alabama, The Capstone Foundation and The University of Alabama Law School Foundation (the "Foundations"). Because of the relationship between the University and the Foundations, the Foundations are considered

component units of the University and are discretely presented in the accompanying financial statements. The Foundations are reported in separate financial statements because of the difference in the reporting model for the Foundations.

The Foundations are not-for-profit organizations that report financial results under principles prescribed by the FASB. Most significant to the Foundations operations and reporting model are FASB Statement No. 116, *Accounting for Contributions Received and Contributions Made*, FASB Statement No. 117, *Financial Reporting for Not-for-Profit Organizations*, FASB Statement No. 124, *Accounting for Certain Investments Held by Not-for-Profit Organizations*, and FASB Statement No. 136, *Transfers of Assets to a Not-for-Profit Organization or Charitable Trust that Raises or Holds Contributions for Others*. As such, certain revenue recognition criteria and presentation features are different from GASB revenue recognition criteria and presentation features. No modifications have been made to the Foundations' financial information in the University's financial reporting entity for these differences. However, the Foundations' accompanying statements of activities and changes in net assets do not present the revenues, expenses, gains and losses by net asset classifications.

Summary information for the Foundations, the University's discretely presented component units, is as follows:

Statements of Financial Position				
	National Alumni Association June 30, 2006	Law School Foundation June 30, 2006	Capstone Foundation September 30, 2006	Total 2006
<b>Assets</b>				
Cash and cash equivalents	\$ 375,796	\$ 766,300	\$ 149,374	\$ 1,291,470
Investments	23,130,503	24,197,596	22,416,153	69,744,252
Contributions receivable, net	2,960	1,243,396	656,129	1,902,485
Other receivables	174,219	21,950	986,277	1,182,446
Other assets	154,139	211,499	86,811	452,449
Property, plant and equipment	-	-	191,548	191,548
<b>Total assets</b>	<b>\$ 23,837,617</b>	<b>\$ 26,440,741</b>	<b>\$ 24,486,292</b>	<b>\$ 74,764,650</b>
<b>Liabilities and Net Assets</b>				
Accounts payable and accrued liabilities	74,306	130,745	274,520	479,571
Deferred revenue	-	-	551,265	551,265
Annuities payable	-	-	2,755,547	2,755,547
Other liabilities	-	-	11,143,063	11,143,063
<b>Total liabilities</b>	<b>74,306</b>	<b>130,745</b>	<b>14,724,395</b>	<b>14,929,446</b>
<b>Net Assets</b>				
Unrestricted	8,777,530	3,020,117	649,989	12,447,636
Temporarily restricted	4,534,898	10,655,135	9,094,047	24,284,080
Permanently restricted	10,450,883	12,634,744	17,861	23,103,488
<b>Total net assets</b>	<b>23,763,311</b>	<b>26,309,996</b>	<b>9,761,897</b>	<b>59,835,204</b>
<b>Total liabilities and net assets</b>	<b>\$ 23,837,617</b>	<b>\$26,440,741</b>	<b>\$24,486,292</b>	<b>\$74,764,650</b>
	National Alumni Association June 30, 2005	Law School Foundation June 30, 2005	Capstone Foundation September 30, 2005	Total 2005
<b>Assets</b>				
Cash and cash equivalents	\$ 142,869	\$ 777,802	\$ 325,780	\$ 1,246,451
Investments	20,803,064	24,476,651	20,998,288	66,278,003
Contributions receivable, net	2,224	1,914,388	955,254	2,871,866
Other receivables	545,976	22,283	1,032,166	1,600,425
Other assets	206,445	279,252	98,642	584,339
Property, plant and equipment	-	-	196,038	196,038
<b>Total assets</b>	<b>\$ 21,700,578</b>	<b>\$ 27,470,376</b>	<b>\$ 23,606,168</b>	<b>\$ 72,777,122</b>
<b>Liabilities and Net Assets</b>				
Accounts payable and accrued liabilities	53,942	98,207	85,402	237,551
Deferred revenue	-	-	499,428	499,428
Annuities payable	-	-	2,897,538	2,897,538
Other liabilities	-	-	7,938,990	7,938,990
<b>Total liabilities</b>	<b>53,942</b>	<b>98,207</b>	<b>11,421,358</b>	<b>11,573,507</b>
<b>Net Assets</b>				
Unrestricted	7,993,907	3,051,733	877,512	11,923,152
Temporarily restricted	3,819,136	12,698,965	11,289,437	27,807,538
Permanently restricted	9,833,593	11,621,471	17,861	21,472,925
<b>Total net assets</b>	<b>21,646,636</b>	<b>27,372,169</b>	<b>12,184,810</b>	<b>61,203,615</b>
<b>Total liabilities and net assets</b>	<b>\$ 21,700,578</b>	<b>\$ 27,470,376</b>	<b>\$ 23,606,168</b>	<b>\$ 72,777,122</b>

## NOTES TO FINANCIAL STATEMENTS

### Statements of Activities and Changes in Net Assets

	National Alumni Association June 30, 2006	Law School Foundation June 30, 2006	Capstone Foundation September 30, 2006	Total 2006
<b>Revenues, gains and other support</b>				
Gifts	\$ 2,473,201	\$ 2,332,712	\$ 3,364,172	\$ 8,170,085
Investment income	906,597	1,119,082	399,659	2,425,338
Unrealized and realized gains on investments, net	722,132	488,719	495,555	1,706,406
Royalties	1,141,593	-	-	1,141,593
Other	58,400	195,150	491,314	744,864
<b>Total revenues, gains and other support</b>	<b>5,301,923</b>	<b>4,135,663</b>	<b>4,750,700</b>	<b>14,188,286</b>
<b>Expenses and losses</b>				
Program services	1,924,949	4,826,432	4,261,936	11,013,317
Fundraising	437,041	16,358	-	453,399
General and administrative	823,258	355,046	238,670	1,416,974
Change in value of split-interest agreements	-	-	92,424	92,424
<b>Total expenses and losses</b>	<b>3,185,248</b>	<b>5,197,836</b>	<b>4,593,030</b>	<b>12,976,114</b>
<b>Change in net assets</b>	<b>2,116,675</b>	<b>(1,062,173)</b>	<b>157,670</b>	<b>1,212,172</b>
Net assets, beginning of year	21,646,636	27,372,169	12,184,810	61,203,615
Cumulative effect of adjustment (Note 1)	-	-	(2,580,583)	(2,580,583)
<b>Net assets, end of year</b>	<b>\$ 23,763,311</b>	<b>\$ 26,309,996</b>	<b>\$ 9,761,897</b>	<b>\$ 59,835,204</b>
	National Alumni Association June 30, 2005	Law School Foundation June 30, 2005	Capstone Foundation September 30, 2005	Total 2005
<b>Revenues, gains and other support</b>				
Gifts	\$ 3,803,320	\$ 2,312,561	\$ 3,347,267	\$ 9,463,148
Investment income	839,118	1,030,898	377,060	2,247,076
Unrealized and realized gains on investments, net	875,087	968,247	1,571,053	3,414,387
Royalties	1,129,106	-	-	1,129,106
Other	136,182	67,667	639,053	842,902
<b>Total revenues, gains and other support</b>	<b>6,782,813</b>	<b>4,379,373</b>	<b>5,934,433</b>	<b>17,096,619</b>
<b>Expenses and losses</b>				
Program services	2,095,507	971,879	3,128,897	6,196,283
Fundraising	428,520	19,706	-	448,226
General and administrative	893,876	447,183	237,524	1,578,583
Change in value of split-interest agreements	-	-	184,206	184,206
<b>Total expenses and losses</b>	<b>3,417,903</b>	<b>1,438,768</b>	<b>3,550,627</b>	<b>8,407,298</b>
<b>Change in net assets</b>	<b>3,364,910</b>	<b>2,940,605</b>	<b>2,383,806</b>	<b>8,689,321</b>
Net assets, beginning of year	18,281,726	24,431,564	9,801,004	52,514,294
<b>Net assets, end of year</b>	<b>\$ 21,646,636</b>	<b>\$ 27,372,169</b>	<b>\$ 12,184,810</b>	<b>\$ 61,203,615</b>



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**Basis of Accounting-Discretely Presented Component Units** – The financial statements of the Foundations have been prepared on the accrual basis.

Net assets and revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Foundations and changes therein are classified and reported as follows:

**Unrestricted** – Net assets that are not subject to donor-imposed restrictions. Items that affect this net asset category included unrestricted gifts and earnings on these unrestricted gifts.

**Temporarily Restricted** – Net assets subject to donor-imposed restrictions that may or will be met either by actions of the Foundations or the passage of time. Items that affect this net asset category include restricted gifts and earnings on endowment funds expendable for purposes stipulated by the donor. These amounts are reclassified to unrestricted net assets when such purpose or time restrictions are met.

**Permanently Restricted** – Net assets subject to donor-imposed restrictions to be maintained permanently by the University. Items that affect this net asset category include gifts wherein donors stipulate that the corpus be held in perpetuity (primarily gifts for endowment) and only the income be made available for expenditure.

Unrealized and realized gains and losses and dividends and interest from investing in income-producing assets may be included in any of these net asset classifications depending on donor restrictions or the absence thereof.

**New Accounting Pronouncement - Adopted by The Capstone Foundation**

In September 2006, the Securities and Exchange Commission ("SEC") staff issued Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements." The Capstone Foundation ("Capstone") adopted SAB 108 during the year ended September 30, 2006. SAB 108 permits Capstone to initially apply the provisions of SAB 108 by recording the cumulative effect of any prior immaterial misstatements to the carrying values of assets and liabilities as of October 1, 2005, with an offsetting adjustment recorded to the opening balance of net assets.

Under the provisions of SAB 108, Capstone adjusted its payable to the University as of October 1, 2005, in order to reflect approximately \$2.28 million of net unrealized gains and losses related to the Eminent Scholar Program corpus (Note 16) for which Capstone is agent for the University. These net unrealized gains and losses were previously recognized by Capstone in its Statement of Activities instead of adjusting its payable to the University for this activity. The previous accounting treatment had been used since the adoption, in fiscal year 1997, of FASB Statement No. 124, *Accounting for Certain Investments Held by Not-for-Profit Organizations*, which required most of Capstone's investments to be measured at fair value, thus creating unrealized gains and losses on these investments held by Capstone.

Under the provisions of SAB 108, Capstone also reduced contributions receivable by \$300,000 as of October 1, 2005, in order to remove a receivable recorded in 2005 which was a receivable of the University, not Capstone.

**Investments - Discretely Presented Component Units**

In accordance with FASB Statement No. 124, the Foundations' investments in debt securities, equity securities and mutual funds with readily determinable market values are reported at their fair market values based on published market prices. The Foundations invest certain amounts in a System-sponsored investment pool, the Endowment Fund (Note 3). The value of the investment in the pool is determined by the System and based on the Foundations' proportionate shares of the net asset value of the pool. The pool invests in various investment securities, including both marketable and non-readily marketable securities. The pool values investments that do not have readily determinable market values at cost.

Investments received by gift are stated at fair value at date of receipt. Changes in market values are reported as unrealized gains or losses on the statement of activities and changes in net assets. All interest income and realized and unrealized gains and losses are reported in the statement of activities and changes in net assets.

**Contributions Receivable - Discretely Presented Component Units**

In accordance with SFAS No. 116, *Accounting for Contributions Received and Contributions Made*, contributions received, including unconditional promises to give, are recognized as revenues at their fair values in the period received. For financial

## NOTES TO FINANCIAL STATEMENTS

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reporting purposes, the Foundations distinguish between contributions of unrestricted assets, temporarily restricted assets and permanently restricted assets. Contributions for which donors have imposed restrictions which limit the use of the donated assets are reported as restricted support if the restrictions are not met in the same reporting period. When such donor-imposed restrictions are met in subsequent reporting periods, temporarily restricted net assets are reclassified to unrestricted net assets and reported as net assets released from restrictions when the purpose or time restrictions are met. Contributions of assets which donors have stipulated must be maintained permanently, with only the income earned thereon available for current use, are classified as permanently restricted assets. Contributions for which donors have not stipulated restrictions are reported as unrestricted support.

Unconditional promises to give with payments due in future periods are reported as restricted support. Gifts of land, buildings and equipment are reported as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulation, the Foundations report expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

Other significant accounting policies of the University are as follows:

**Cash and Cash Equivalents:** For purposes of the statement of cash flows, the University considers all highly liquid investments with an original maturity of three months or less to be cash equivalents, including restricted cash and cash equivalents. Cash equivalents representing assets of the University's endowment, life income and other long-term investments are included in the noncurrent investments category.

**Investments:** The University's investments are primarily reported at fair value. The University's investment portfolio is primarily invested in three separate investment pools sponsored by the System. Fair value for the investment pools is provided by the System, based on the fair value of the underlying investment securities held by each investment pool. Fair value of the underlying securities held in each investment pool is based on quoted market prices or dealer quotes, where available, or determined using net asset values provided by underlying investment partnerships or companies, which primarily invest in

readily marketable securities. Certain real estate and non-readily marketable securities held in the System sponsored endowment investment pool are carried at cost. Fair value for equity securities, debt securities, mutual funds and U.S. government and agency obligations held by the University is determined from quoted market prices or market prices of similar instruments. Investments received by gift are reported at fair value at date of receipt. Net investment income, including realized and unrealized gains and losses, are reported as nonoperating revenues (expenses) in the statements of revenues, expenses and changes in net assets.

Investments are reported in four categories in the statement of net assets. Investments recorded as endowment and life income are those invested funds that cannot be used to fund current operations and thus are included in noncurrent assets. Investments held for future capital projects are included in noncurrent assets, except for amounts included in current assets to offset current construction-related payables. Other long-term investments are those invested funds with maturities greater than one year or are considered by management to be of a long duration that are not an investment of the endowment and life income fund or the plant fund. All other investments are included as short-term investments.

**Loans Receivable:** Loans receivable represent all amounts owed on promissory notes from debtors including campus-based and Federal student loans.

**Inventories:** Inventories are carried at the lower of cost or market and consist primarily of the University Supply Store inventory.

**Accounts Receivable:** Accounts receivable consist primarily of tuition and fees charged to students and amounts due from federal, state and local governments, or private sources, in connection with reimbursement of allowable expenditures made pursuant to the University's contracts and grants. Accounts receivable are recorded net of estimated uncollectible amounts.

**Capital Assets:** Capital assets are recorded at cost at the date of acquisition, or fair value at date of donation in the case of gifts, less accumulated depreciation. Renovations to buildings, infrastructure and land improvements that significantly increase the value or extend the useful life of the structure are capitalized. Routine repairs and maintenance are charged to operating expense in the year in which the expense is incurred.

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The University capitalizes certain software and development costs associated with obtaining and developing internal-use computer software. Training costs and data conversion costs are expensed as incurred.

Capital assets acquired through federal grants and contracts where the federal government retains a reversionary interest are capitalized and depreciated. Interest costs, net of any related investment earnings, as applicable, for certain qualifying assets acquired with the proceeds of tax-exempt borrowings are capitalized as a component of the cost of acquiring those assets.

Depreciation of buildings and building improvements and infrastructure (20-50 years), land improvements (5-25 years), library collection (10 years) and inventoried equipment (5-20 years) is computed on a straight-line basis.

**Pledges:** The University receives pledges and bequests of financial support. Revenue is recognized when a pledge representing an unconditional promise to give is received and all eligibility requirements, including time requirements, have been met. In the absence of such a promise, revenue is recognized when the gift is received. Pledges are recorded at their gross, undiscounted amount. Endowment pledges do not meet eligibility requirements and are not recorded as assets until the related gift is received. Due to uncertainties with regard to their realization and valuation, bequest intentions and other conditional promises are not recognized as assets until the specified conditions are met. The University's trust policies do not differ in nature from endowment policies.

**Charitable Remainder Trusts:** The University is the beneficiary of various charitable remainder trust funds administered by unaffiliated organizations. Under the terms of the agreements, the University has the irrevocable right to receive the remaining assets of the trusts upon the death of a specified beneficiary or beneficiaries in exchange for a stipulated amount to be paid periodically to the donor or their designee until the death of the beneficiary. Following the death of the beneficiary, the remainder is transferred to the University as either unrestricted or restricted funds depending on donor-imposed purpose restrictions.

The assets received at the inception of a charitable remainder trust agreement are recorded at fair value at the date of gift. The fair value of the remainder interest to be received from trusts is approximately \$5.8 million and \$5.7 million at September 30, 2006 and 2005, respectively. Any change in value related to these trusts is recorded as investment income in the statements of revenues, expenses and changes in net assets.

The liability associated with these agreements is recorded at the present value based on IRS mortality tables and prevailing interest rates. The liability is reduced for distributions made to the beneficiaries and is adjusted annually for revaluations of expected future payments to the beneficiaries based on changes in life expectancy. The present value of the liability associated with these agreements is approximately \$3.1 million and \$2.9 million at September 30, 2006 and 2005, respectively.

**Beneficial Interest in Perpetual Trusts:** Perpetual trusts are trusts under which the University will receive income distributions in perpetuity, but will never receive the corpus of the trust assets (principal). Perpetual trusts are initially recorded as permanently restricted contribution revenue at the current fair value of the University's interest in the trust assets at the date of gift. Subsequent changes to the trust's fair value are recorded as investment income in the statements of revenues, expenses and changes in net assets. Income received from perpetual trusts is recognized as unrestricted or restricted expendable investment income depending on donor restrictions.

**Endowment Spending:** For donor-restricted endowments, the Uniform Management of Institutional Funds Act, as adopted in Alabama, permits The Board of Trustees of the University of Alabama (the "Board") to appropriate an amount of realized and unrealized endowment appreciation as the Board determines to be prudent. The University's policy is to retain the endowment realized and unrealized appreciation with the endowment after the spending rate distributions. The Board approved a spending rate for the fiscal year ending September 30, 2006 and 2005 of 5.0% of a moving three-year average of the market (unit) value.

## NOTES TO FINANCIAL STATEMENTS

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**Deferred Revenues:** Deferred revenues consist primarily of tuition and fees related predominantly to future fiscal years.

**Federal Refundable Loans:** Certain loans to students are administered by the University with funding primarily supported by the federal government. The University's statement of net assets includes both the notes receivable and the related federal refundable loan liability representing federal capital contributions and related activity owed upon termination of the program.

**Compensated Absences:** The University accrues annual leave for employees at rates based upon length of service and job classification and compensatory time based upon job classification and hours worked. These amounts are included in accounts payable and accrued liabilities.

**Scholarship Allowances and Student Aid:** Student tuition and fees are presented net of scholarships and fellowships applied to student accounts, while stipends and other payments made directly to students are presented as scholarship and fellowship expenses.

**Grant and Contract Revenue:** The University receives grant and contract revenue from governmental and private sources. The University recognizes revenue associated with the sponsored programs in accordance with GASB Statement No. 33, based on the terms of the individual grant or contract.

### Note 2 – Cash and Cash Equivalents

The Board approves, by resolution, all banks or other financial institutions utilized as depositories for University funds. Prior to approval, each proposed depository must provide evidence of its designation by the Alabama State Treasurer as a qualified public depository under the Security of Alabama Funds Enhancement Act ("SAFE"). From time to time, the Board may request that the depository provide evidence of its continuing designation as a qualified public depository. The enactment of the SAFE program changed the way all Alabama public deposits are collateralized. In the past, the bank pledged collateral directly to each individual public entity. Under the mandatory SAFE program,

each qualified public depository ("QPD") is required to hold collateral for all its public depositories on a pooled basis in a custody account established for the State Treasurer as SAFE administrator. In the unlikely event a public entity should suffer a deposit loss due to QPD insolvency or default, a claim form would be filed with the State Treasurer who would use the SAFE pool collateral or other means to reimburse the loss.

During fiscal year 2005, the Board established a short-term investment pool for the System campuses to invest operating cash reserves. As of September 30, 2006 and 2005, the University had approximately \$34,098,000 and \$28,511,000, respectively, in this System-sponsored investment pool, which is presented in cash and cash equivalents and restricted cash and cash equivalents on the statements of net assets. See Note 3 for further disclosure regarding this short-term investment pool.

### Note 3 – Investments

The Board has the responsibility for the establishment of the investment policy and the oversight of the investments for the various System and related entities. In order to facilitate system-wide investment economies and objectives, the Board has established four distinct investment pools based primarily on the projected investment time-horizons for cash reserves. These investment pools are the Endowment Fund, Prime Fund, Intermediate Fund and the Short-Term Fund (collectively, the "System Pools"). Pursuant to Board investment policies, each System or related entity may include all or a portion of their investments within the System-sponsored investment pools. These investment funds are considered 'internal' investment pools under GASB Statement No. 31, *"Accounting and Financial Reporting for Certain Investments and for External Investment Pools"*, with the assets pooled on a market value basis. Separately managed funds that are resident on each campus are to be invested consistent with the asset mix of the corresponding System investment pool. The following disclosures relate to both the System Pools, which include the investments of other System entities and other affiliated entities, and the University-specific investment portfolio.



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### **Endowment Fund**

The purpose of the Endowment Fund is to pool endowment and similar funds to support the System campuses, hospital and related entities in carrying out their respective missions over an indefinite time frame. Accordingly, the primary investment objectives of the Endowment Fund are to preserve the purchasing power of the principal and provide a stable source of perpetual financial support. To satisfy the long-term rate of return objective, the Endowment Fund relies on a total return strategy in which investment returns are achieved through both capital appreciation and natural income. Asset allocations are established to meet targeted returns while providing adequate diversification in order to minimize investment volatility.

### **Prime Fund**

The Prime Fund is a longer-term pool used as a source of funds to meet projected cash reserve needs over a period of seven to ten years. This fund has an investment objective of growth through income and is invested in a diversified asset mix of liquid and semi-liquid securities. Long-term lockup funds with illiquid assets are inappropriate investments for this fund.

### **Intermediate Fund**

The Intermediate Fund serves as a source of funds to meet projected cash reserve needs over a two to

six year period. This fund is also used to balance the other funds when looking at the System's entire asset allocation of cash reserves relative to its investment objectives. The Intermediate Fund has an investment objective of income with preservation of capital and is invested in intermediate term fixed income securities. At least one of the investment managers must be a large mutual fund providing daily liquidity.

### **Short-Term Fund**

The Short-Term Fund contains the short-term cash reserves of the various System entities. Because of the different income and disbursement requirements of each campus, consolidation of these funds reduces daily cash fluctuations and minimizes the amount of short-term cash reserves needed. Assets held in the Short-Term Fund are invested with the primary objectives of stability of principal and liquidity. Such investments are restricted to high quality, liquid, money market funds and other fixed income obligations with a maturity of one year or less.

Although the investment philosophy of the Board is to minimize the direct ownership of investment vehicles, preferring ownership in appropriate investment fund groups, there are certain direct investments that are held in the name of the Board. All other investments in the System Pools are classified as commingled funds.



## NOTES TO FINANCIAL STATEMENTS

The composition in investments, by investment type, for the System Pools, at September 30, 2006 and 2005 is as follows:

	Endowment Fund		Prime Fund		Intermediate Fund		Short Term Fund	
	2006	2005	2006	2005	2006	2005	2006	2005
Cash and Receivables								
Cash	\$ -	\$ 1,011,107	\$ -	\$ 17,507	\$ 12,503	\$ -	\$ -	-
Accrued Income Receivables	981,140	975,095	1,118,196	559,496	2,267,460	1,877,554	-	-
<b>Total Cash and Receivables</b>	<b>981,140</b>	<b>1,986,202</b>	<b>1,118,196</b>	<b>577,003</b>	<b>2,279,963</b>	<b>1,877,554</b>	<b>-</b>	<b>-</b>
Cash and Equivalents								
Commerical Paper	-	-	-	-	13,748,821	9,855,000	-	-
Money Market Funds	7,574,688	9,105,229	6,428,567	8,381,106	8,434,541	18,673,245	-	-
<b>Total Cash and Equivalents</b>	<b>7,574,688</b>	<b>9,105,229</b>	<b>6,428,567</b>	<b>8,381,106</b>	<b>22,183,362</b>	<b>28,528,245</b>	<b>-</b>	<b>-</b>
Equities								
Common Stock	123,226,310	130,665,163	158,268,913	108,768,522	-	-	-	-
<b>Total Equities</b>	<b>123,226,310</b>	<b>130,665,163</b>	<b>158,268,913</b>	<b>108,768,522</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
Fixed Income Securities								
U.S. Government Obligations	16,359,318	13,447,557	18,806,639	19,114,820	65,619,783	31,940,657	-	-
Mortgage Backed Securities	3,069,336	11,742,454	9,057,376	16,241,626	39,269,785	31,995,079	-	-
Collateralized Mortgage Obligations	8,254,290	-	8,165,028	-	61,062,777	162,260,168	-	-
Corporate Bonds	9,740,519	10,375,216	11,933,901	14,385,448	158,852,908	81,317,880	-	-
Foreign Bonds	-	-	-	-	1,426,864	4,620,889	-	-
<b>Total Fixed Income Securities</b>	<b>37,423,463</b>	<b>35,565,227</b>	<b>47,962,944</b>	<b>49,741,894</b>	<b>326,232,117</b>	<b>312,134,673</b>	<b>-</b>	<b>-</b>
Commingled Funds								
U.S. Equity Funds	278,168,873	253,692,939	140,886,041	167,310,710	-	-	-	-
Non U.S. Equity Funds	149,893,182	122,522,440	49,545,096	103,392,044	-	-	-	-
U.S. Bond Funds	121,167,857	75,149,275	187,554,297	120,190,770	8,748,701	48,931,227	85,805,856	136,905,991
Hedge Funds	73,778,807	71,679,148	64,690,006	51,030,321	-	-	-	-
Private Equity Funds	20,670,307	18,860,126	-	-	-	-	-	-
Timberland Funds	10,000,141	11,826,958	-	-	-	-	-	-
Real Estate Funds	5,899,508	12,263,142	-	-	-	-	-	-
<b>Total Commingled Funds</b>	<b>659,578,675</b>	<b>565,994,028</b>	<b>442,675,440</b>	<b>441,923,845</b>	<b>8,748,701</b>	<b>48,931,227</b>	<b>85,805,856</b>	<b>36,905,991</b>
<b>Total Fund Investments</b>	<b>827,803,136</b>	<b>741,329,647</b>	<b>655,335,864</b>	<b>608,815,367</b>	<b>357,164,180</b>	<b>389,594,145</b>	<b>85,805,856</b>	<b>136,905,991</b>
<b>Total Fund Assets</b>	<b>828,784,276</b>	<b>743,315,849</b>	<b>656,454,060</b>	<b>609,392,370</b>	<b>359,444,143</b>	<b>391,471,699</b>	<b>85,805,856</b>	<b>136,905,991</b>
<b>Total Fund Liabilities</b>	<b>(215,789)</b>	<b>(223,485)</b>	<b>(204,829)</b>	<b>(238,494)</b>	<b>(370,639)</b>	<b>(209,221)</b>	<b>-</b>	<b>-</b>
Affiliated Entity Investments								
in Funds	(87,266,923)	(80,114,158)	-	-	-	-	-	-
<b>Total Net Asset Value</b>	<b>\$ 741,301,564</b>	<b>\$ 662,978,206</b>	<b>\$ 656,249,231</b>	<b>\$ 609,153,876</b>	<b>\$ 359,073,504</b>	<b>\$ 391,262,478</b>	<b>\$ 85,805,856</b>	<b>\$ 136,905,991</b>



The composition in investments, by investment type and excluding Short-Term Fund amounts, for the University's separately held investments, at September 30, 2006 and 2005 is as follows:

	2006	2005
Cash and Equivalents		
Certificates of Deposit	\$ 284,354	\$ 291,506
Money Market Funds	84,275	94,497
<u>Total Cash and Equivalents</u>	<u>368,629</u>	<u>386,003</u>
Equities		
Common Stock	8,950,223	8,871,458
Preferred Stock	263,465	271,295
<u>Total Equities</u>	<u>9,213,688</u>	<u>9,142,753</u>
Fixed Income Securities		
U.S. Government Obligations	416,581	3,067,155
Corporate Bonds	381,133	612,473
Foreign Bonds	65,234	-
<u>Total Fixed Income Securities</u>	<u>862,948</u>	<u>3,679,628</u>
Commingled Funds		
U.S. Equity Funds	11,514,264	8,538,998
U.S. Bond Funds	106,708,665	105,087,388
Private Equity Funds	114,497	114,497
<u>Total Commingled Funds</u>	<u>118,337,426</u>	<u>113,740,883</u>
<u>Total Real Estate</u>	<u>2,354,907</u>	<u>2,356,907</u>
System Pooled Investments		
Endowment Fund	428,815,940	395,457,391
Prime Fund	156,046,082	148,509,020
Intermediate Fund	67,319,079	93,035,224
<u>Total System Pooled Investments</u>	<u>652,181,101</u>	<u>637,001,635</u>
<u>Total University Investments</u>	<u>\$ 783,318,699</u>	<u>\$ 766,307,809</u>



### Investment Risk Factors

There are many factors that can affect the value of investments. Some, such as custodial credit risk, concentration of credit risk and foreign currency risk, may affect both equity and fixed income securities. Equity securities respond to such factors as economic conditions, individual company earnings performance and market liquidity, while fixed income securities are particularly sensitive to credit risks and changes in interest rates.

### Credit Risk

Fixed income securities are subject to credit risk, which is the chance that a bond issuer will fail to pay interest or principal in a timely manner, or that negative perceptions of the issuer's ability to make these payments will cause security prices to decline. These circumstances may arise due to a variety of factors such as financial weakness, bankruptcy, litigation, and/or adverse political developments. Certain fixed income securities, primarily obligations of the U.S. government or those explicitly guaranteed by the U.S. government, are not considered to have credit risk.

A bond's credit quality is an assessment of the issuer's ability to pay interest on the bond, and ultimately, to pay the principal. Credit quality is evaluated by one of the independent bond-rating agencies, for example Moody's Investors Service (Moody's) or Standards and Poor's (S&P). The lower the rating, the greater the chance—in the rating agency's opinion—that the bond issuer will default, or fail to meet its payment obligations. Generally, the lower a bond's credit rating, the higher its yield should be to compensate for the additional risk.

Board policy recognizes that a limited amount of credit risk, properly managed and monitored, is prudent and provides incremental risk adjusted return over its benchmark. Credit risk in each investment pool is managed primarily by diversifying across issuers and limiting the amount of portfolio assets that can be invested in non-investment grade securities. Fixed income holdings in a single entity (excluding obligations of the U.S. government and its agencies) may not exceed 6% of a manager's portfolio measured at market value. At least 95%

of these fixed income investments must be in investment grade securities (securities with ratings of BBB- or Baa3) or higher. However, multi-strategy fixed income managers may have up to 20% of their investments in non-investment grade securities. Securities of foreign entities either denominated in U.S. dollars or other currencies shall be limited to 20% of a manager's portfolio.

The investment policy recognizes that credit risk is appropriate in balanced investment pools such as the Endowment and Prime Funds, which are tracked against the Lehman Aggregate Index benchmark for the fixed income portion of these pools. For the Endowment Fund, 15% of the fund is committed to fixed income investments, of which, 5% are actively managed. For the Prime Fund, 30% of the fund is invested in fixed income securities, of which, 20% are actively managed. Fixed income investments within the Endowment and Prime Funds include corporate, mortgage backed, asset backed and U.S. treasury and/or agency bonds with a minimum BBB- rating and an average duration of four years. In addition, approximately \$28,768,450 and \$26,004,700 at September 30, 2006 and 2005 is invested in unrated securities. Commingled funds were \$322,725,409 and \$212,826,380 at September 2006 and 2005, respectively.

The Intermediate Fund is benchmarked against the Lehman 1-3 Government Index with funds invested with three separate fund managers. Fixed income investments include corporate, mortgage backed, asset backed, collateralized mortgage and U.S. treasury and/or agency bonds with an average duration of 1.73 years and a minimum rating of BB or higher. For September 30, 2006 and 2005, \$62,077,035 and \$73,303,812, respectively, were invested in unrated fixed securities.

The Short-Term Fund is committed to immediate liquidity to meet the operating needs of the campuses and hospital. These funds are invested in a bank sponsored common/collective trust fund, which in turn invests in money market, corporate, mortgage backed, asset backed and U.S. treasury and/or agency securities. These funds are all commingled with funds of other investors.



The credit risk for fixed and variable income securities, for the System Pools, at September 30, 2006 and 2005 are as follows:

	Endowment Fund		Prime Fund		Intermediate Fund		Short Term Fund	
	2006	2005	2006	2005	2006	2005	2006	2005
Fixed or Variable Income Securities								
U.S. Government Guaranteed	\$ 16,359,318	\$ 13,447,557	\$ 18,806,639	\$ 19,114,820	\$ 65,619,783	\$ 31,940,657	\$ -	\$ -
Other U.S. Denominated								
AAA	499,000	1,493,845	499,000	1,999,455	119,590,000	119,010,472	-	-
AA	1,191,000	2,010,900	1,752,000	3,791,378	28,772,000	39,696,871	-	-
A	6,139,000	6,203,748	6,514,000	6,984,790	44,855,000	28,954,121	-	-
BBB	1,688,000	1,656,413	3,170,000	2,599,515	10,603,000	15,384,932	-	-
BB	-	-	-	-	-	3,843,808	-	-
B	-	-	-	-	3,464,000	-	-	-
Unrated	11,547,145	10,752,764	17,221,305	15,251,936	53,328,334	73,303,812	-	-
Commingled Funds								
U.S. Bond Funds Unrated	121,167,857	75,149,275	187,554,297	120,190,770	8,748,701	48,931,227	85,805,856	136,905,991
Money Market Funds Unrated	7,574,688	9,105,229	6,428,567	8,381,106	8,434,541	18,673,245	-	-
Commercial Paper Unrated	-	-	-	-	13,748,821	9,855,000	-	-
Total	\$ 166,166,008	\$ 119,819,731	\$ 241,945,808	\$ 178,313,770	\$ 357,164,180	\$ 389,594,145	\$ 85,805,856	\$ 136,905,991

In accordance with the Board policy disclosed above, credit risk for the University's fixed and variable income securities held outside of the System Pools is managed by diversifying across issuers and limiting the amount of portfolio assets that are invested in non-investment grade securities.

The credit risk for fixed and variable income securities, for the University's separately held investments, at September 30, 2006 and 2005 are as follows:

	2006	2005
Fixed or Variable Income Securities		
U.S. Government Guaranteed	\$ 416,581	\$ 3,067,155
Other U.S. Dollar and Commingled Bonds		
AAA	2,284,833	5,614,710
AA	7,760,158	5,313,698
A	388,139	344,747
BBB	-	-
BB	80,330	157,202
B	-	103,293
Unrated	96,725,847	94,260,708
	\$ 107,655,888	\$ 108,861,513

## NOTES TO FINANCIAL STATEMENTS

### Custodial Credit Risk

Custodial credit risk is the risk that in the event of the corporate failure of the custodian, the investment securities may not be returned.

Investment securities in the System Pools and the University's separately held portfolio are registered in the Board's name by the custodial bank as an agent for the System. Other types of investments (e.g. open-ended mutual funds, common/collect trusts) represent ownership interests that do not exist in physical or book-entry form. As a result, custodial credit risk is remote.

### Concentration of Credit Risk

Concentration of credit risk is the risk associated with a lack of diversification, such as having substantial investments in a few individual issuers, thereby exposing the organization to greater risks resulting from adverse economic, political, regulatory, geographic, or credit developments.

As previously mentioned, credit risk in each investment pool and the University's separately held investment portfolio is managed primarily by diversifying across issuers and limiting the amount of portfolio assets that can be invested in non-investment grade

securities. As of September 30, 2006 and 2005, there was no investment in a single issuer that represents 5% or more of total investments in the System Pools or the University's separately held investment portfolio.

### Interest Rate Risk

Interest rate risk is the risk that the value of fixed income securities will decline because of changing interest rates. The prices of fixed income securities with a longer time to maturity, measured by effective duration, tend to be more sensitive to changes in interest rates and, therefore, more volatile than those with shorter durations. Effective duration is the approximate change in price of a security resulting from a 100 basis point (1 percentage point) change in the level of interest rates. It is not a measure of time. The Board does not have a specific policy relative to interest rate risk. As such, there are no restrictions on weighted average maturity for each investment pool as they are managed relative to the investment objectives and liquidity demands of the investors.

The effective durations for fixed or variable income securities, for the System Pools, at September 30, 2006 and 2005 are as follows:

	Endowment Fund		Prime Fund		Intermediate Fund		Short Term Fund	
	2006	2005	2006	2005	2006	2005	2006	2005
U.S. Government Obligations	5.7	6.9	5.8	6.3	1.7	1.5	-	-
Mortgage Backed Securities	3.4	11.6	3.5	11.0	2.3	12.2	-	-
Corporate Bonds	4.7	3.6	5.0	2.8	2.5	7.3	-	-
Commingled Bond Funds	5.2	4.5	4.9	4.5	1.9	1.8	-	-

(The information presented above does not take into account the relative weighting of the portfolio components to the total portfolio.)

While the Board does not have a specific policy relative to interest rate risk, the University has historically invested funds outside of the investments pools in fixed income and variable income securities with short maturity terms.



The effective durations for fixed or variable income securities, for the University's separately held investments, at September 30, 2006 and 2005 are as follows:

	2006	2005
U.S. Government Obligations	4.5	1.1
Commingled Bond Funds	0.6	0.6
Corporate Bonds	4.9	2.9

Investments may also include mortgage pass through securities and collateralized mortgage obligations that may be considered to be highly sensitive to changes in interest rates due to the existence of prepayment or conversion features. At September 30, 2006 and 2005 the fair market value of these investments, for the System Pools, are as follows:

	Endowment Fund		Prime Fund		Intermediate Fund		Short Term Fund	
	2006	2005	2006	2005	2006	2005	2006	2005
Mortgage Backed Securities	\$ 3,069,336	\$ 11,742,454	\$ 9,057,376	\$ 16,241,626	\$ 39,269,785	\$ 31,995,079	\$ -	\$ -
Collateralized Mortgage Obligations	8,254,290	-	8,165,028	-	61,062,777	162,260,168	-	-
Total	\$ 11,323,626	\$ 11,742,454	\$ 17,222,404	\$ 16,241,626	\$ 100,332,562	\$ 194,255,247	\$ -	\$ -

## NOTES TO FINANCIAL STATEMENTS

**Mortgage Backed Securities.** These securities are issued by the Federal National Mortgage Association (Fannie Mae), Government National Mortgage Association (Ginnie Mae) and Federal Home Loan Mortgage Association (Freddie Mac) and include short embedded prepayment options. Unanticipated prepayments by the obligees of the underlying asset reduce the total expected rate of return.

**Collateralized Mortgage Obligations.** Collateralized mortgage obligations (CMOs) generate a return based upon either the payment of interest or principal on

mortgages in an underlying pool. The relationship between interest rates and prepayments makes the fair value highly sensitive to changes in interest rates. In falling interest rate environments, the underlying mortgages are subject to a higher propensity of prepayments. In a rising interest rate environment, the opposite is true.

At September 30, 2006 and 2005, the effective durations for these securities held in the System Pools are as follows:

	Endowment Fund		Prime Fund		Intermediate Fund		Short Term Fund	
	2006	2005	2006	2005	2006	2005	2006	2005
Mortgage Backed Securities	3.4	11.6	3.5	11.0	2.3	12.2	-	-
Collateralized Mortgage Obligations	-	-	-	-	1.6	9.7	-	-

At September 30, 2006 and 2005, the University did not hold any investments in these security types outside of the System Pools.

### Foreign Currency Risk

The strategic asset allocation policy for the Endowment Fund and the Prime Fund includes an allocation to non-United States equity securities. Under Board policy foreign equity holdings in a single industry should not exceed 25% of the investment manager's portfolio measured at market value, with 50% of the portfolio's holdings representing EAFE Index firms. Each investment manager must hold a minimum of 30 individual stocks with equity holdings in a single company remaining below 8% of the investment manager's portfolio, measured at market value. Hedging of foreign currency risks is allowed at the investment manager's discretion. In addition, investments in foreign bonds are allowed under Board policy. Foreign bonds denominated in U.S. dollars are limited to 20% of the investment manager's portfolio, and bonds denominated in currencies other than U.S. dollars are limited to 20% of the investment manager's portfolio, measured at market value. As of September 30, 2006 and 2005, all foreign investments in the System Pools are in international commingled funds, which in turn in-

vest in equity securities and bonds of foreign issuers. At September 30, 2006 and 2005, the University did not hold any foreign securities in its separately held investment portfolio.

### Securities Lending

Board policies permit security lending as a mechanism to augment income. Loans of the securities shall be collateralized by cash, letters of credit or securities issued or guaranteed by the U.S. Government or its agencies. The collateral must equal at least 102% of the current market value of the loaned securities. Securities lending contracts must state acceptable collateral for securities loaned, duties of the borrower, delivery of loaned securities and acceptable investment of the collateral.

The System Pools participate in a securities lending program managed by one of the System's custodial banks. The program is designed to allow the System to lend certain securities from the investment pools and receive a pledge of collateral sufficient to cover the market value of the securities lent. The collateral securities cannot be pledged or sold by the System unless the borrower defaults. At September 30, 2006 and 2005, there were no securities on loan from the investment pools and no collateral held by the System.



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## Note 4 – Accounts Receivable

The composition of accounts receivable at September 30, 2006 and 2005 is summarized as follows:

	2006	2005
Student accounts	\$ 23,561,162	\$ 14,760,239
Receivables from sponsoring agencies	25,636,182	18,384,827
Accrued interest receivable	4,983,680	5,225,038
Other	1,632,659	2,741,251
	<u>\$ 55,813,683</u>	<u>\$ 41,111,355</u>
Less provision for doubtful accounts	(1,215,711)	(822,755)
Accounts receivable, net	<u>\$ 54,597,972</u>	<u>\$ 40,288,600</u>

## Note 5 – Loans and Pledges Receivable

Loans receivable represent all amounts owed on promissory notes from debtors, including student loans made under the Federal Perkins Loan Program and other loan programs. Pledges receivable represent unconditional promises to give from third party donors and are presented at their gross, undiscounted amount.

The composition of loans and pledges receivable at September 30, 2006 and 2005, is summarized as follows:

	2006	2005
Loans receivable		
Federal loan program	\$ 15,251,530	\$ 13,568,641
University loan funds	954,162	1,142,288
Less allowance for doubtful loans	<u>(3,696,717)</u>	<u>(2,341,250)</u>
Total loans outstanding, net	12,508,975	12,369,679
Less current portion	<u>(2,948,350)</u>	<u>(2,888,761)</u>
Total loans outstanding, noncurrent	<u>\$ 9,560,625</u>	<u>\$ 9,480,918</u>
Pledges outstanding		
Operations	\$ 38,906,994	\$ 33,205,400
Capital	2,001,959	764,015
Total pledges, net	<u>40,908,953</u>	<u>33,969,415</u>
Less current portion	<u>(9,125,194)</u>	<u>(7,054,751)</u>
Total pledges, noncurrent	<u>\$ 31,783,759</u>	<u>\$ 26,914,664</u>

## NOTES TO FINANCIAL STATEMENTS

### Note 6 – Capital Assets

Capital assets activity for the years ended September 30, 2006 and 2005 is summarized as follows:

	Balance 10/01/05	Additions	Retirements/ Transfers	Balance 09/30/06
Land	\$ 9,216,339	\$ -	\$ -	\$ 9,216,339
Land improvements	13,616,354	-	-	13,616,354
Infrastructure	23,719,270	202,192	-	23,921,462
Buildings and improvements	599,479,845	79,242,582	37,983,083	716,705,510
Construction in progress	75,958,790	74,337,266	(37,983,083)	112,312,973
Equipment	154,905,469	10,693,707	(50,757,299)	114,841,877
Library materials and collections	89,618,377	3,292,240	-	92,910,617
Total cost of capital assets	966,514,444	167,767,987	(50,757,299)	1,083,525,132
Less accumulated depreciation	(362,828,783)	(32,681,032)	44,509,788	(351,000,027)
Capital assets, net	<u>\$ 603,685,661</u>	<u>\$ 135,086,955</u>	<u>\$ (6,247,511)</u>	<u>\$ 732,525,105</u>

	Balance 10/01/04	Additions	Retirements/ Transfers	Balance 09/30/05
Land	\$ 9,089,098	\$ 127,241	\$ -	\$ 9,216,339
Land improvements	13,607,930	8,424	-	13,616,354
Infrastructure	22,814,383	904,887	-	23,719,270
Buildings and improvements	461,445,317	59,381,690	78,652,838	599,479,845
Construction in progress	108,756,555	48,048,823	(80,846,588)	75,958,790
Equipment	142,504,807	18,750,292	(6,349,630)	154,905,469
Library materials and collections	83,416,359	6,202,018	-	89,618,377
Total cost of capital assets	841,634,449	133,423,375	(8,543,380)	966,514,444
Less accumulated depreciation	(339,591,881)	(29,941,228)	6,704,326	(362,828,783)
Capital assets, net	<u>\$ 502,042,568</u>	<u>\$ 103,482,147</u>	<u>\$ (1,839,054)</u>	<u>\$ 603,685,661</u>

The University increased its moveable equipment threshold from \$2,000 to \$5,000 beginning October 1, 2006 resulting in the write off of approximately \$19.1 million of fully depreciated equipment. These write-offs had no impact on the University's net assets.

### Note 7 – Construction Commitments and Financing

The University has contracted for the construction and renovation of several facilities. At September 30, 2006 and 2005, the estimated remaining cost to complete the construction and renovation of these facilities was approximately \$26.1 million and \$48.3 million, respectively, which is expected to be financed from private gifts, grants, bond proceeds and University funds.

## Note 8 – Long-term Debt

Long-term debt activity for the years ended September 30, 2006 and 2005 is summarized as follows:

Type/Supported by	Balance 10/01/05	New Debt	Principal Repayment	Reclass	Balance 09/30/06
Leases payable					
Departmental budgets	\$ 323,862	\$	\$ 106,849	\$	\$ 217,013
Notes payable					
Crimson Tide Foundation gifts	4,969,902		373,645		4,596,257
Student housing revenue	4,193,543		157,884		4,035,659
Rental income	388,595		46,271		342,324
Bonds					
Student housing revenue	52,295,101	47,141,998	71,472		99,365,627
Intercollegiate athletics	123,268,826	3,932,360	244,838		126,956,348
Auxiliaries	38,480,421	13,250,642	2,817,980	(15,917,458)	32,995,625
General fee	100,700,652		2,135,710	15,917,458	114,482,400
	<u>324,620,902</u>	<u>64,325,000</u>	<u>5,954,649</u>		<u>382,991,253</u>
Plus net unamortized bond premium/discount	402,587				1,240,536
Less deferred amount on refunding	(2,594,148)				(2,504,694)
Less current portion	(6,303,871)				(7,642,003)
	<u>\$ 316,125,470</u>				<u>\$ 374,085,092</u>

Type/Supported by	Balance 10/01/04	New Debt	Principal Repayment	Balance 09/30/05
Leases payable				
Departmental budgets	\$ 442,083	\$ -	\$ 118,221	\$ 323,862
Notes payable				
Crimson Tide Foundation gifts	-	5,000,000	30,098	4,969,902
Student housing revenue	4,408,900	-	215,357	4,193,543
Rental income	439,884	-	51,289	388,595
Bonds				
Student housing revenue	53,154,072	-	858,971	52,295,101
Intercollegiate athletics	125,334,183	-	2,065,357	123,268,826
Auxiliaries	39,179,279	-	698,858	38,480,421
General fee	102,112,466	-	1,411,814	100,700,652
	<u>325,070,867</u>	<u>5,000,000</u>	<u>5,449,965</u>	<u>324,620,902</u>
Plus net unamortized bond premium/discount	416,459			402,587
Less deferred amount on refunding	(2,683,601)			(2,594,148)
Less current portion	(5,415,786)			(6,303,871)
	<u>\$ 317,387,939</u>			<u>\$ 316,125,470</u>

## NOTES TO FINANCIAL STATEMENTS

Several operations within the University are self-supporting. However, in 2006, the University restructured tuition and fees resulting in the termination of specific fee allocations to various units, ending their self-supporting abilities. Due to this change, the correlating long-term debt of these areas was reclassified from auxiliaries to general fee support as reflected in the 2006 Long-term debt scheduled. Debt obliga-

tions bear interest at fixed and variable rates ranging from 3.0% to 7.75% and mature at various dates through fiscal year 2036.

Maturities and interest on notes, leases and bonds payable, using rates in effect at September 30, 2006, for the next five years and in subsequent five-year periods are as follows:

	Notes & Leases Principal	Bonds Principal	Total Principal	Notes & Leases Interest	Bond Interest	Total Interest	Total Estimated Debt Service
2007	\$ 715,950	\$ 6,940,000	\$ 7,655,950	\$ 487,442	\$ 17,685,106	\$ 18,172,548	\$ 25,828,498
2008	981,341	6,715,000	7,696,341	431,927	17,909,629	18,341,556	26,037,897
2009	643,717	7,030,000	7,673,717	385,799	17,591,478	17,977,276	25,650,994
2010	662,595	7,340,000	8,002,595	350,120	17,280,058	17,630,178	25,632,774
2011	700,416	7,675,000	8,375,416	312,299	16,944,585	17,256,884	25,632,300
2012-2016	3,401,088	44,130,000	47,531,088	932,668	78,974,128	79,906,796	127,437,884
2017-2021	944,588	56,260,000	57,204,588	412,390	66,851,427	67,263,817	124,468,405
2022-2026	607,158	72,100,000	72,707,158	242,525	51,004,452	51,246,977	123,954,135
2027-2031	534,400	91,505,000	92,039,400	60,378	31,610,153	31,670,531	123,709,931
2032-2036	-	74,105,000	74,105,000	-	8,064,545	8,064,545	82,169,545
	<u>\$ 9,191,253</u>	<u>\$ 373,800,000</u>	<u>\$ 382,991,253</u>	<u>\$ 3,615,548</u>	<u>\$ 323,915,560</u>	<u>\$ 327,531,109</u>	<u>\$ 710,522,362</u>

Pledged revenues for the years ended September 30, 2006 and 2005 as defined by outstanding bonds covenants are as follows:

	2006	2005
Tuition and fees	\$ 168,337,662	\$ 135,238,566
Sales and services of educational activities	9,973,238	6,989,477
Auxiliary sales and services	104,203,777	94,142,660
Investment income	21,596,034	52,870,013
Other operating revenue	10,491,118	12,656,683
	<u>\$ 314,601,829</u>	<u>\$ 301,897,399</u>

The University defeased certain indebtedness during 1986, 1997, 2003 and 2005 by depositing funds in escrow trust accounts sufficient to provide for the subsequent payment of principal and interest on the defeased indebtedness. Under the trust agreements, funds deposited in the trust accounts were invested in obligations of the U.S. Government. The University estimates that the amounts on deposit will be sufficient to satisfy the debt service requirements on the defeased indebtedness and that the defeasance will result in lower overall debt service payments to the University. Should the amounts on deposit

not be sufficient to retire the defeased indebtedness upon maturity, the University would be responsible to satisfy the shortfall. The University remains legally obligated for the repayment of the defeased indebtedness. Neither the assets of the trust accounts nor the defeased indebtedness are included in the accompanying statements of net assets. The principal outstanding on the 1986, 1997, 2003 and 2005 defeased indebtedness at September 30, 2006 and September 30, 2005 is approximately \$52.9 million and \$87.2 million, respectively.





The following is a detailed schedule of long-term debt at September 30, 2006:

Description and Purpose	Date Issued	Final Maturity	Interest Rate-%	Original Debt	Outstanding Debt
Bonds Payable:					
General Fee Revenue Bond Series 1997	7/1/04	6/1/11	4.375-4.75	\$ 7,155,000	\$ 5,325,000
General Fee Revenue Bond Series 2001	7/1/04	12/1/26	4.0-5.0	34,645,000	32,320,000
General Fee Revenue Bond Series 2004A	7/1/04	7/1/34	4.0-5.25	215,995,000	215,995,000
General Fee Revenue Bond Series 2004B	8/30/04	7/1/09	variable	13,885,000	8,680,000
General Fee Revenue Bond Series 2004C	8/30/04	7/1/34	variable	48,100,000	47,155,000
General Fee Revenue Bond Series 2006A	9/1/06	7/1/36	4.125-5.0	40,575,000	40,575,000
General Fee Revenue Bond Series 2006B	9/1/06	7/1/23	5.22-5.9	23,750,000	23,750,000
Total Bonds Payable				384,105,000	373,800,000
Notes Payable:					
U. S. Department of Education	7/20/89	4/15/19	3.0	3,188,000	1,809,236
Regional bank and individual owners	12/4/00	12/20/07	7.5-7.75	722,822	342,323
Commercial finance co., CTF airplane	5/10/05	5/10/15	6.25	5,000,000	4,596,257
U. S. Department of Education	3/23/00	7/1/29	5.5	2,483,000	2,226,424
Total Notes Payable				11,393,822	8,974,240
Lease Obligations Payable:					
Miscellaneous leases	3/1/99	6/1/08	0.0-4.0	1,962,000	217,013
Total Lease Obligations				1,962,000	217,013
				\$ 397,460,822	\$ 382,991,253

## NOTES TO FINANCIAL STATEMENTS

The variable interest rates for General Fee Revenue Bonds Series 2004B ranged from 4.07% to 5.46% during fiscal year 2006 and are based on the Wednesday Libor weekly calculation, as defined. The variable interest rates for General Fee Revenue Bonds Series 2004C are based on the Bond Market Association Municipal Swap Index ("BMA"). The variable rate is set equal to the BMA Municipal Index calculation weekly. The variable interest rate bonds incurred interest at varying rates from 2.62% to 4.00% during fiscal year 2006.

The University's general fee bonds are subject to certain covenants. These covenants, among other things, require the Board to adopt an annual budget; to establish and maintain reasonable fees, rates, and other charges to ensure pledged revenues are sufficient for debt service coverage; to maintain books and records pertaining to the pledged revenues; to furnish annual audits and other periodic reports; and to comply with certain restrictions as to additional indebtedness. The University is in compliance with all appropriate debt covenants as of September 30, 2006.

### Note 9 – Self-Insurance

The University participates with other campuses in the System in a self-insurance program for general liability. The Board established a separate revocable trust fund for payment of these self-insurance claims under its risk retention program. Annual contributions are made to the trust fund, at an actuarially determined rate, to provide funding for the retained risk. The accompanying statements include a reserve of approximately \$1,092,000 and \$927,000 for general liability at September 30, 2006 and 2005, respectively.

The University is self-insured for health insurance. The liability for unpaid claims includes an accrual for an estimate of claims incurred but not reported.

The changes in the total reported self-insurance liabilities for the years ended September 30, 2006 and 2005 are summarized as follows:

	2006	2005
Balance, beginning of year	\$ 2,278,508	\$ 3,478,559
Claims paid	(17,903,501)	(17,771,936)
Contributions	19,085,979	16,571,885
Balance, end of year	<u>\$ 3,460,986</u>	<u>\$ 2,278,508</u>



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## Note 10 – Retirement Plan

Most employees of the University participate in the Teachers' Retirement System of Alabama ("TRS"), a cost sharing, multiple-employer public retirement system. In addition, certain employees meeting eligibility requirements participate in an optional program with the Teachers Insurance and Annuity Association – College Retirement Equities Fund ("TIAA – CREF"). TRS is a defined benefit plan while the TIAA-CREF programs are defined contribution plans.

Participants in TRS who retire at age 60 with 10 years of credited service, or after completing 25 years of credited service, regardless of age, are entitled to an annual benefit, payable monthly for life. Service retirement benefits are calculated by three methods with the participants receiving payments under the method which yields the highest monthly benefit. These methods include (1) minimum guaranteed, (2) money purchase or (3) formula. Under the formula method, participants are allowed 2.1025% of their final average salary (average of three highest years of annual compensation during the last ten years of service) for each year of service. A participant terminating before reaching retirement age, but after completing 10 years of credited service, is eligible for a vested allowance at age 60 provided accumulated employee contributions are not withdrawn. TRS also provides death and disability benefits.

Covered employees are required by law to contribute to TRS. The University, as the employer, contributes to TRS. The contribution requirement for fiscal year 2006 and 2005 was approximately \$26,287,000 and \$21,308,000, respectively, which consisted of \$16,307,000 from the University and \$9,980,000 from employees in 2006 and \$12,092,000 from the University and \$9,216,000 from employees in 2005. The University's contribution rate for fiscal year ended September 30, 2006 is 8.17% and the contribution rate for fiscal year ended September 30, 2005 was 6.56% of salaries and wages for covered employees. The contribution for employees is 5% of earnable compensation. All regular employees of the University are members of TRS with the exception of temporary employees.

The actuarial accrued liability ("AAL"), which is the actuarial present value of credited projected benefits, is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of

employee service to date. The actuarial value of assets, which is the actuarial present value of assets, is a standardized disclosure measure of the present value of accumulated assets, adjusted for projected investment performance and contributions. TRS does not make separate measurements of assets and the AAL for individual employers. The AAL and the actuarial valuation of assets at September 30, 2005 (the most recent valuation date) for TRS as a whole, determined through actuarial valuations performed as of that date, were \$23,027,338,000 and \$19,248,207,000, respectively, resulting in an under-funded AAL of \$3,779,131,000. Complete financial presentation and disclosure of the financial position and activities of the TRS is presented in the September 30, 2005 annual financial report of TRS. That report is publicly available and may be obtained by contacting TRS.

As previously noted, some employees participate in the optional TIAA-CREF programs, which are defined contribution plans. In defined contribution plans, benefits depend solely on amounts contributed plus investment earnings. All full time regular monthly exempt employees are eligible to participate from the date of employment. The University contributes a matching amount up to 5% of total salaries for participating employees. The University's contribution is funded as it accrues and, along with that of employees, is immediately and fully vested. The contribution for fiscal years 2006 and 2005, excluding amounts not eligible for matching, was approximately \$10,410,000 and \$9,358,000, which included approximately \$5,205,000 and \$4,679,000 each from the University and its employees.

The University's total salaries and wages for fiscal years 2006 and 2005 were approximately \$230,175,000 and \$207,961,000, respectively. The total salaries and wages during the fiscal years 2006 and 2005, respectively, for covered employees participating in TRS and TIAA – CREF were approximately \$199,599,000 and \$184,323,000 and \$121,153,000 and \$101,100,000.

## Note 11 – Post-Employment Benefits

Certain retired employees may elect to continue to participate in the University's group health plan until eligible for Medicare by paying the full cost of the plan premium. Retired employees age sixty-five or older who are eligible for Medicare must enroll in Medicare Coordinated Plan under which Medicare is the primary insurer and the University's health care plan becomes the secondary insurer. Despite



the availability of the University's plan, most retirees elect to participate in the Public Education Employees Health Insurance Plan ("PEEHIP") with TRS, in which case the retirees pay a portion of the PEEHIP premium with the University paying an allocation toward the cost of retiree coverage.

Certain retirees may also elect to continue their basic term life insurance coverage and accidental death and dismemberment insurance up to certain maximum amounts. The retirees pay the full amount of the premiums in such cases.

Retirees are eligible for tuition assistance benefits for themselves as well as for their spouse and unmarried dependent children.

### Note 12 – Compensated Absences

Certain University employees accrue vacation and sick leave at varying rates depending upon their years of continuous service and payroll classification, subject to maximum limitations. Upon termination of employment, employees are paid all unused accrued vacation at their regular rate of pay up to a designated maximum number of days. Depending on their payroll classification, some employees are also paid one-half of their unused accrued sick leave at their regular rate of pay. The statement of net assets include an accrual of approximately \$12,563,000 and \$9,970,000 as of September 30, 2006 and 2005, respectively, for accrued vacation, sick leave and payroll related benefits.

### Note 13 – Federal Direct Lending Program

The Federal Direct Student Loan Program ("FDSLP") was established under the Higher Education Act of 1965, as amended in the Student Loan Reform Act of 1993. The FDSLP enables an eligible student or parent to obtain a loan to pay for the student's cost of attendance directly through the university rather than through private lenders. The University began participation in the FDSLP on July 1, 1995. As a university qualified to originate loans, the University is

responsible for handling the complete loan process, including funds management as well as promissory note functions. The University is not responsible for collection of these loans. During the years ended September 30, 2006 and 2005, respectively, the University disbursed approximately \$88,300,000 and \$73,000,000, respectively, under the FDSLP.

### Note 14 – Contingencies and Commitments

The University has sovereign immunity and is therefore, in the opinion of University Counsel, immune to ordinary tort actions. The University has consistently been dismissed from lawsuits on the basis of the sovereign immunity doctrine. That doctrine also protects the University from vicarious liability arising from the negligence of its employees. As a matter of policy, the University has chosen to indemnify its employees through a self-insured trust fund against liability arising from the performance of their official duties. There are some exceptions to the sovereign immunity doctrine, most notably federal court cases arising under the federal Constitution or federal statutes. The University is engaged in various legal actions in the ordinary course of business. Management does not believe the ultimate outcome of those actions will have a material adverse effect on the financial statements.

Amounts received or receivable from grantor agencies are subject to audit and adjustments by such agencies, principally the United States Government. Any disallowed claims, including amounts already collected, may constitute a liability of the University. The amount, if any, of expenditures that may be disallowed by the grantor cannot be determined at this time, although the University expects any such amounts to be immaterial.

The University is a guarantor of a third party obligation totaling approximately \$2,320,000 and \$2,320,000 at September 30, 2006 and 2005, respectively. Commitments relating to construction activities are discussed at Note 7.



## Note 15 – Operating Expenses by Function

Operating expenses by functional classification for the years ended September 30, 2006 and 2005 are summarized as follows:

<b>2006 Operating Expenses</b>					
	Salaries, wages and benefits	Scholarships and fellowships	Supplies and other services	Depreciation	Total
Instruction	\$ 122,156,420	\$ 1,114,738	\$ 20,233,924	\$ -	\$ 143,505,082
Research	13,595,882	336,036	12,146,981	-	26,078,899
Public service	24,354,248	175,099	13,529,197	-	38,058,544
Academic support	33,031,082	690,383	11,550,195	-	45,271,660
Student services	8,860,758	108,298	4,618,621	-	13,587,677
Institutional support	31,842,872	12,192	9,897,677	-	41,752,741
Operations and maintenance	24,287,441	37,075	14,550,823	-	38,875,339
Scholarships and fellowships	10,781,738	5,524,958	603,267	-	16,909,963
Auxiliary enterprises	35,193,249	2,818,320	45,741,671	-	83,753,240
Depreciation	-	-	-	38,470,361	38,470,361
	<u>\$ 304,103,690</u>	<u>\$ 10,817,099</u>	<u>\$ 132,872,356</u>	<u>\$ 38,470,361</u>	<u>\$ 486,263,506</u>

<b>2005 Operating Expenses</b>					
	Salaries, wages and benefits	Scholarships and fellowships	Supplies and other services	Depreciation	Total
Instruction	\$ 111,089,828	\$ 486,395	\$ 20,448,730	\$ -	\$ 132,024,953
Research	13,745,344	407,319	10,316,065	-	24,468,728
Public service	25,604,990	118,659	11,474,176	-	37,197,825
Academic support	26,178,518	37,936	10,744,299	-	36,960,753
Student services	7,752,691	31,482	3,807,391	-	11,591,564
Institutional support	28,355,218	1,917	4,498,653	-	32,855,788
Operations and maintenance	19,160,387	2,134	14,539,083	-	33,701,604
Scholarships and fellowships	7,488,165	7,906,317	93,847	-	15,488,329
Auxiliary enterprises	34,790,861	1,094,912	45,160,894	-	81,046,667
Depreciation	-	-	-	29,941,228	29,941,228
	<u>\$ 274,166,002</u>	<u>\$ 10,087,071</u>	<u>\$ 121,083,138</u>	<u>\$ 29,941,228</u>	<u>\$ 435,277,439</u>

## NOTES TO FINANCIAL STATEMENTS

### Note 16 – Other Noncurrent Assets and Liabilities

The composition of other noncurrent assets at September 30, 2006 and 2005 is summarized as follows:

	2006	2005
Receivable from Capstone Foundation	\$ 10,498,083	\$ 7,800,000
Intangible assets, net of accumulated amortization	5,566,567	5,709,300
ASF noncurrent assets	2,133,992	1,619,837
Other	3,061,241	2,782,063
	<u>\$ 21,259,883</u>	<u>\$ 17,911,200</u>

The receivable from The Capstone Foundation relates to the Eminent Scholars Program established by the State of Alabama Act No. 85-759 and administered by the Alabama Commission on Higher Education. The program provides that donor gifts of \$600,000 held in a foundation affiliated with the University are eligible for \$400,000 in State matching funds. In prior years, the University received funds from donors intended to be matched in accordance with this program. Consistent with the provision of the program, the University transferred the corpus of these funds to The Capstone Foundation, as agent for the University, whereby the State would match these donations. The program has been inactive since 1997, and no matching funds have been provided to date. These funds held by the Capstone Foundation include both the corpus and any unrealized gains earned thereon and are shown as a receivable from the Capstone Foundation. Unrealized gains earned

each year on the corpus are added to the receivable and reported as investment income by the University. Realized gains and investment income earned each year on the corpus amount are distributed to the University and reported as investment income.

During fiscal year 2005, the University received an in-kind gift of approximately \$5.7 million related to a television license to be used by the University's on-campus television station. The University recorded the license as an intangible asset at the estimated fair value on the date of the gift. The University recognizes amortization expense related to the intangible asset on a straight-line basis using an estimated useful life of forty years.

The activity with respect to other noncurrent liabilities for the years ended September 30, 2006 and 2005, is as follows:

	2006	2005
Federal loan funds		
Federal refundable loans, beginning of year	\$ 9,841,527	\$ 9,896,882
Deposits received	257,133	340,223
Deposits disbursed	(445,416)	(395,578)
Federal refundable loans, end of year	<u>\$ 9,653,244</u>	<u>\$ 9,841,527</u>
Other liabilities		
Split-interest agreement obligations, beginning of year	\$ 3,151,594	\$ 3,215,876
Investment income	111,979	97,821
Payments on obligations	(359,262)	(359,018)
Actuarial change in obligations	139,374	196,915
Total split-interest agreement obligations	<u>3,043,685</u>	<u>3,151,594</u>
Less current portion	<u>(358,881)</u>	<u>(360,036)</u>
Split-interest agreement obligations, end of year	2,684,804	2,791,558
General liability trust fund liability	1,091,774	926,554
Other liabilities	801,178	253,223
Total other liabilities	<u>\$ 4,577,756</u>	<u>\$ 3,971,335</u>

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## Note 17 – Recently Issued Pronouncements

The GASB issued Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, in November 2003. GASB Statement No. 42 requires governments to evaluate and report any capital asset impairment loss in their financial statements on an annual basis offset by any related insurance recoveries. This statement is effective for fiscal year periods beginning after December 15, 2004. There was not a material impact on the University's financial statements from the adoption of this Statement.

The GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, in July 2004. This Statement requires governmental entities to recognize and match other postretirement benefit costs, for example health and life insurance expense, with related services received and also to provide information regarding the actuarial accrued liability and funding level of the benefits associated with past services. The requirements of this Statement are effective in three phases based on a government's total annual revenues in the first fiscal year ending after June 15, 1999 with phase I for periods beginning after December 15, 2006. The University is currently evaluating the impact that GASB Statement No. 45 will have on its financial statements, although it is expected that there will be an increase in the University's operating expenses and liabilities, as well as a decrease in unrestricted net assets, as a result of adopting this statement. However, most retirees elect to participate in the State-sponsored PEEHIP (Note 11) which is a multi-employer plan. GASB Statement No. 45 is not expected to effect the University's accounting for the PEEHIP.

The GASB issue Statement No. 46, *Net Assets Restricted by Enabling Legislation an amendment of GASB Statement No. 34*, in December 2004. GASB Statement No. 46 amends GASB Statement No. 34 to clarify the definition of a legally enforceable enabling legislation restriction and specifies the accounting and financial reporting requirements if new enabling legislation replaces existing enabling legislation or if legal enforceability is reevaluated. GASB Statement No. 46 will be effective for financial statement periods beginning after June 15, 2005. The University adopted this Statement effective October 1, 2005. There was not a material impact on the University's financial statements from the adoption of this statement.

The GASB issued Statement No. 47, *Accounting for Termination Benefits*, in July 2005. GASB Statement No. 47 establishes recognition, measurement, and disclosure requirements for both voluntary termination benefits (for example, early-retirement incentives) and involuntary termination benefits (for example, severance benefits). The requirements of GASB Statement No. 47 are effective in two parts. For termination benefits provided through an existing defined benefit OPEB plan, the provisions of this statement should be implemented simultaneously with the requirements of GASB Statement No. 45. For all other termination benefits, this statement is effective for financial statements for periods beginning after June 15, 2005. The University adopted this Statement effective October 1, 2005. In accordance with GASB Statement No. 47, during December 2006, the University recognized approximately \$3.0 million of expense for compensation to be paid to a former coaching staff member according to the terms of the staff member's employment agreement. This obligation will require sixty-two months of consecutive payments, estimated to be approximately \$47,800 each, subject to adjustment based on earned compensation from new employment.

The GASB issued Statement No. 48, *Sales and Pledges of Receivable and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, in September 2006. This Statement establishes criteria to ascertain whether certain transactions should be regarded as a sale or a collateralized borrowing. GASB Statement No. 48 is effective for financial statement periods beginning after December 15, 2006. The University is currently evaluating the impact, if any, that GASB Statement No. 48 will have on its financial statements.

The GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, in December 2006. This Statement will require that governments provide more detailed information regarding the effect of environmental cleanups and will be effective for the financial periods beginning after December 15, 2007. The University is currently evaluating the impact, if any, that GASB Statement No. 49 will have on its financial statements.

## Note 18 – Grants and Contracts

At September 30, 2006, the University had been awarded approximately \$56,201,000 in grants and contracts which had not been expended. These awards, which represent commitments of sponsors to provide funds for specific research, training, and service projects, have not been reflected in the financial statements as of and for the year ended September 30, 2006.

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