McGill

2005 – 2006
Financial Report to the Board of Governors

McGill University,
Montreal, Quebec, Canada H3A 2T5.
www.mcgill.ca

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“The mission of McGill University is the advancement of learning through teaching, scholarship, and service to society by offering to outstanding undergraduate and graduate students the best education available, by carrying out scholarly activities judged to be excellent when measured against the highest international standards, and by providing service to society in those ways for which we are well suited by virtues of our academic strengths.”

McGill University

FINANCIAL REPORT TO THE BOARD OF GOVERNORS

Year Ended May 31, 2006

Part I: Financial and Operational Highlights

Part II: Audited Financial Statements – May 31, 2006

PART I

PART I: FINANCIAL AND OPERATIONAL HIGHLIGHTS

Overview

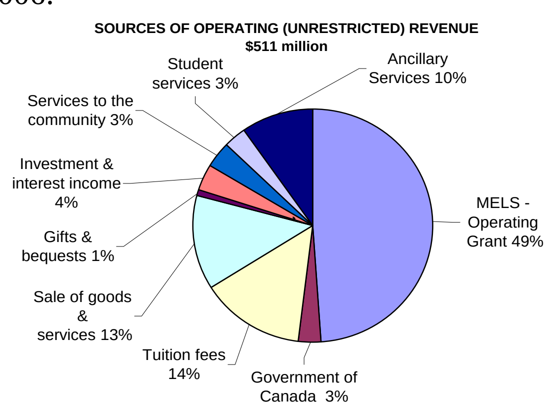
This financial report provides a summary of the financial activities of McGill University for the year June 1, 2005 to May 31, 2006, and presents the financial position of the University as at May 31, 2006. A presentation of the four funds; Operating, Restricted, Plant, and Endowment are provided, and highlights of changes affecting the accumulated deficit in the Operating Fund are presented. Specifically, changes from the 2005-2006 original Budget (document GD04-54) are presented, the various balance sheets are reviewed, and an estimate of the University's ongoing deferred maintenance requirements is provided. The audited financial statements of the University are included in *Part II.*

Sources of Revenue and Expenses

The University's income is derived from many sources including:

- Operating (Unrestricted) Fund – This fund derived 74% of its income from the Ministry of Education (MELS) operating grant, tuition, and student fees. During the year, income from all unrestricted sources was $511.2 million as compared to $492 million in the prior year - an increase of $19.2 million.

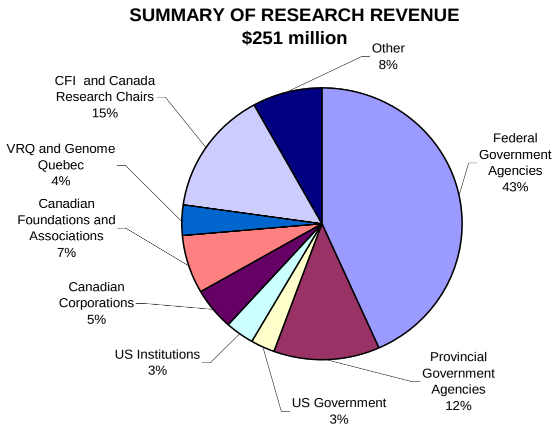
  The following pie chart highlights the various sources of operating (unrestricted) fund revenue for the year ended May 31, 2006:

  Total operating (unrestricted) expenditures required to fulfill the University's teaching mission increased by $25.5 million, including expenses related to other activities provided by the University, such as student services, services to the community, and ancillary services, which together increased by a net of $3.7 million. Overall, total operating (unrestricted) expenses increased to $523.1 million, as compared to $497.6 million in the prior year.

- Restricted Fund – Revenue is generated primarily from research grants (71%), restricted donations, and endowment income, which are targeted towards research, libraries, bursaries, scholarships, student loans, and other specific projects (20%). Other sources account for the remaining 9%. Total restricted income for the year was $356.1 million, as compared to $347.8 million in the prior year. The increase of $8.3 million resulted from a reduction in revenue from research grants and contracts totaling $26.2 million, offset by an increase in income generated by the McGill Investment Pool (MIP) of $27 million, and an increase in donations and other revenues of $7.5 million. The investment performance of the MIP is highlighted in a separate detailed report, the *2005-2006 Report on Endowment Performance*, which will be presented to the Board of Governors later this fall.

  Total revenue from research grants and contracts of $251.3 million is derived from various sources from year-to-year. Outlined in the next graph is a summary of the current year's sources of research revenue:



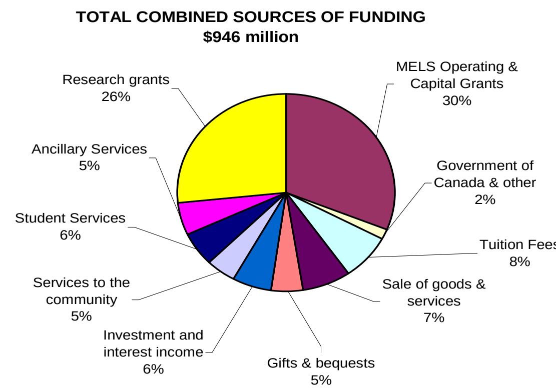
The Restricted Fund also includes expenses that are directly related to supporting the University's mission, of which research is the largest component (79%). These expenditures are classified as "restricted" due to the nature of the restriction imposed on the spending of these funds by the individual grantors. Overall, restricted expenses increased to $329.2 million from a level of $325.9 million in the prior year. The majority of the $3.3 million (net) increment is related to awards and similar aid funded to students ($2.3 million), reduction in expenditures supporting faculties and operations ($1.8 million), increased research activities ($0.9 million), and other sources ($1.9 million).

- Plant Fund – This fund derives its revenue from various sources including 73% from government grants, of which 53% is used to absorb the cost of long-term borrowing, 18% from gifts and bequests received for specific capital projects, and 9% from net interest income. Overall, revenue decreased to $52.4 million from $61.9 million in the prior year. Of the $9.5 million (net) decrease, $8.3 million is attributable to a decrease in MELS and other government grants, a decrease of $2.9 million in gifts, all offset by an increase in short-term interest income of $1.6 million and other sources ($0.1 million).

- Endowment Fund – This fund's only source of revenue is from gifts and bequests for designated purposes. Total revenue in this fund was $26.3 million, as compared to $13 million in the prior year. All of this revenue resulted in the creation of individual endowments, of which the generated income is to be spent according to Memorandum of Agreements entered into with donors.

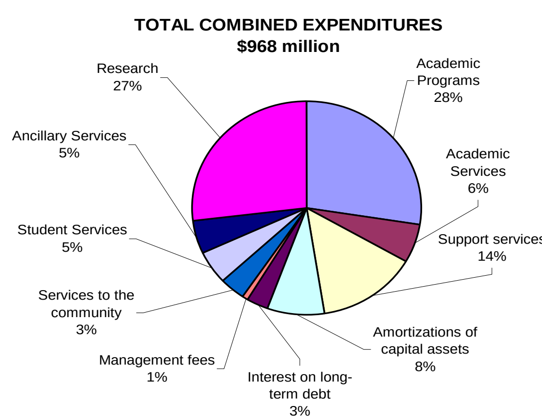
Total Combined Sources of Funding

The following pie chart presents a complete picture of the $946 million total combined sources of funding required to support the University's mission.



Total Combined Expenditures

Total combined expenses incurred to support the University's activities total $967.6 million. The following pie chart illustrates the breakdown of these expenses.



During 2005-2006, a total of $68.2 million in gift revenue was generated for teaching and research activities, which contributed positively to the following funds:

Gifts and bequests	2006	2005
	$Million	
Operating	4.3	4.8
Restricted	11.8	13.0
Plant	9.3	12.1
Endowment	26.3	13.0
Total gifts and bequests received:	**51.7**	**42.9**
Increase (decrease) in pledges	16.5	(2.2)
Total Gifts and bequests:	68.2	40.7

Included in the above totals are donations totaling $0.5 million and $23.1 million (including pledges), respectively, which have been included in other operating and restricted revenue line items. The restricted amount includes $4.2 million for community services; $2.5 million for Student Services; and $16.4 million for Research. *The Annual Report on Private Giving* provides comprehensive details of the total gifts and captures other amounts that are not classified as donation income for financial statement purposes. These include: donations from charitable foundations ($12 million; classified as research income), gifts in kind ($0.6 million; not reported), contributions from student associations ($1 million; classified as student fees - Student Services).

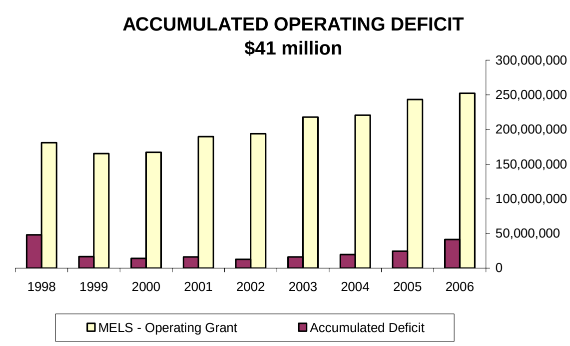
Overall, Plant Fund gifts are received for the purposes of acquiring specific assets and may also include contributions to finance specific buildings and other assets. All donations received in the Endowment Fund were endowed, based on the specific wishes of the donors.

In addition to donations, investment in the McGill Investment Pool (MIP) generated total realized earnings of $60.2 million (2004-2005: $26.3 million). The year-over-year change of $33.9 million was a result of additional investment income ($2.5 million) and increased gains on the sale of investments ($31.4 million). The market value of the investments (including cash, short-term investments, and accrued income) increased to $800.3 million at May 31, 2006, as compared to $763.2 million one year earlier. Consistent with University policy, $40.8 million (2004-2005: $40.8 million) of the total was distributed to the respective unit holders. Unlike the previous two years, amounts earned in excess of the amount distributed were returned to the Endowment Fund via an inter-fund transfer ($18.4 million). In the past two years, amounts distributed for spending exceeded earnings. Accordingly, the shortfall was funded by the accumulated investment income in the Endowment Fund, via an inter-fund transfer (2004-2005: $15 million) from accumulated endowment earnings to the Operating Fund.

Accumulated Deficit – Operating Fund

In the current year, the accumulated deficit has increased from its May 31, 2005 level of $24.4 million to $41.4 million (as compared to a budgeted accumulated deficit of $33.9 million) as at May 31, 2006. From its maximum level of $79.5 million fourteen years ago, the accumulated deficit of the University decreased to $48 million as at May 31, 1998, and to $16.5 million as at May 31, 1999, the latter resulting mainly from a one-time MELS contribution of $24.6 million towards reducing the accumulated deficit.

The following graph outlines the evolution of the Operating Fund accumulated deficit and that of the MELS operating grants.



In the 2005-2006 approved budget, a deficit of $9.5 million was budgeted. In March 2006, our forecast of the year-end position highlighted an increase of $4.7 million to the operating deficit, which was primarily attributable to:

	$ Million
Adjusted government grants	1.1
Decreased tuition	(1.8)
Decreased sale of goods and services	(1.8)
Decreased donations and investment income	(0.6)
Increased Faculty expenditures, net	(0.3)
Increased library costs	(1.3)
Increased student services revenues, net	0.7
Other expenses, net	(0.7)
Net increase to budgeted deficit:	(4.7)

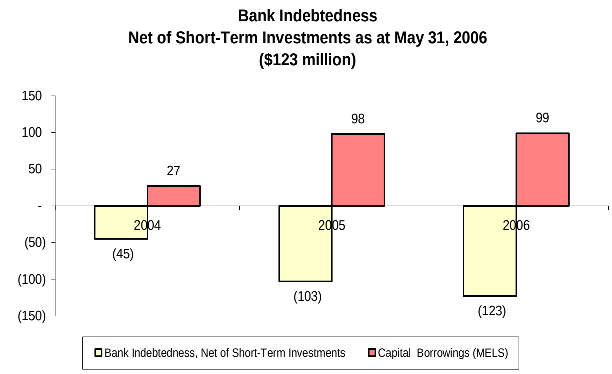
Further to the revised accumulated deficit estimate, an additional $2.8 million increase to the accumulated deficit was realized as a result of the following specific items below (reflecting an increase of $7.5 million from the original budgeted accumulated deficit):

	$ Million
Adjustment to grants	(0.8)
Increased Faculty costs, net	(4.7)
Reduced library costs	0.7
Delayed IT projects	3.8
Decreased administrative costs	1.8
Exchange loss	(2.7)
Other expenses, net	(0.9)
Net increase to forecasted deficit:	(2.8)

Balance Sheet

The University's four Funds capture the total assets, liabilities, and fund balances.

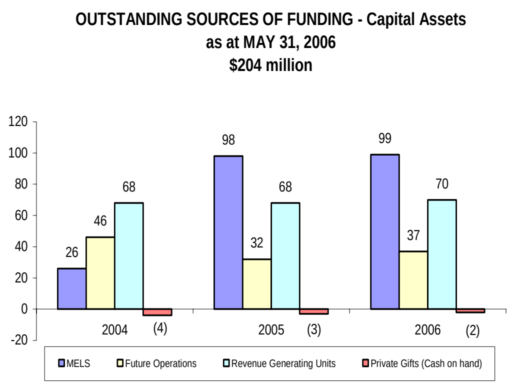
- Operating (Unrestricted) Fund – This fund captures all of the working capital associated with the operations of the University, including its overall cash position with outside lenders, which have extended McGill a $250 million line of credit. As at May 31, 2006, the University had bank indebtedness of $176.5 million, as compared to $155.6 million one year earlier. The bank indebtedness, net of short term investments, was $122.6 million. This increased from the prior year's net of $103 million due to increased capital expenditures, of which outstanding financing from MELS totals $99.1 million (as compared to $98 million in the prior year), and $7.5 million increase in capital expenditures which will be recovered from future operations. The remainder of the increase is mainly due to an increased accumulated deficit and other changes in working capital items. The following chart outlines the progression of the cash position over the last three years, as compared to the level of capital borrowing on behalf of MELS.



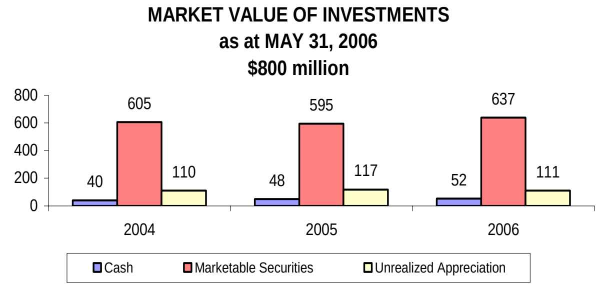
- Restricted Fund – The majority of the Restricted Fund assets are used to support restricted activities, as specified by the individual donors or granting agencies. Total Restricted Fund assets increased to $453.9 million, as compared to $444.7 million one year earlier. Of the total assets, $344.7 million is due from either granting agencies or donor pledges, $18.2 million in marketable securities, $3.7 million in student loans receivable, $85.6 million in net cash received in advance of spending, and $1.7 million in other assets.

- Plant Fund – Total assets in this fund were $1.07 billion as at May 31, 2006 compared to $1.03 billion one year earlier. Of the total, capital assets accounted for $983.4 million as compared to $945.5 million in 2004-2005. In addition, $80.5 million was held in cash and short-term deposits, and marketable securities, as a direct result of the bond proceeds generated in 2002-2003. Other assets amounted to $6.3 million. The majority of financing relating to the total Plant Fund assets (48%) is by way of long-term debt ($518.2 million) issued primarily through bonds. The remaining financing is by way of suppliers (2%), from capital fund balances (37%), and (13%) from inter-fund borrowings. During the year, net long-term debt stayed constant, as bonds maturing during the year were replaced by new issues.

The total outstanding source of funding at May 31, 2006 was $204 million, of which $99 million is expected to be received from MELS relating to annual and specific capital grants. In addition, $69.4 million will be recovered from revenue generating Units, such as residences, and other sources, while $29.6 million remains as borrowings for deferred maintenance and campus renewal, and $7.6 million of additional borrowings will be repaid from future internal sources. A total of $10.8 million is outstanding financing from future donations, while $13.1 million has already been received in advance from private gifts (resulting in a reduction in overall borrowings). The following bar chart outlines the three years of outstanding sources of funding which, when received, will reduce the short-term borrowings.



- Endowment Fund – These assets stand at $802.2 million as at May 31, 2006, as compared to $765.6 million one year earlier. Of this total, $800.3 million related to cash, short-term investments, marketable securities, and accrued income (2004-2005: $763.2 million).



Deferred Maintenance – Campus Renewal

The University estimates that its outstanding deferred maintenance requirements are at least $175 million. This deferred maintenance "deficit" has been on the decline in the last few years due to a persistent approach of repairing and renovating required properties. To date, internal loans of $50 million have been approved with the goal of partially addressing the University's outstanding deferred maintenance situation. A total of $37.6 million has been spent to date, with another $12.4 million committed to specific projects. These actions initiated a positive momentum in the decline of deferred maintenance requirements.

An additional $10 million loan was approved for the fiscal 2007 year, which will continue to address the deferred maintenance issue. Each $10 million loan will require an annual repayment of $1 million (including capital and interest) for a 15-year duration, unless earlier financing is obtained.

Multi-year Planning

Strategic planning and multi-year resource allocation have become very familiar terms to the McGill community. These undertakings were best described by the Principal in her introduction to the 2004-2005 Budget (document GD 03-65).

The University is currently engaged in a new comprehensive, academically-driven planning process that will impact virtually every aspect of McGill's operations including finances, administrative services, physical resources, and University goals and activities with respect to philanthropy and government relations. It is a demanding but crucial process as we aim to build on our exceptional teaching and research strengths for the future. The competition for talent and resources has never been as fierce – and this competition is worldwide, not only local. If we are to sustain and build on our academic strengths, impact, and reputation, consistent with our mission, we must be selective and strategic in our activities, investments, and resource generation and expenditures. The purpose of this process is to identify the academic priorities and objectives of each Faculty, and the University as a whole, implement plans to achieve them, and measure our progress with discipline.

The implementation of the five-year Academic Plan necessitates upfront investment and will consequently place McGill in an operating deficit position in the initial years of the Plan, with the aim of re-establishing a balanced budget in the Plan's latter years. This approach is increasingly being adapted by North American research-intensive universities. Indeed, many have used this planning approach for some time as a means of improving academic quality and distinctiveness.

The purpose of the new investment is to enable McGill University to achieve its academic goals, provide increased leveraging of resources, advance student and administrative support, and provide accountable enhanced investment in new and current programs, technologies, administrative infrastructure, and other priority initiatives. It will support the University to sustain and advance our leadership position amongst Canadian and North American public university peers.

The 2005-2006 year represents the second *tranche* of the University's multi-year Resource Planning Model that supports the Academic Plan. The Model assumes that we will fund our plans through reallocations and newly-generated revenue versus internal base budget reductions during the five-year planning horizon. Mechanisms have been built into the Model that would allow for the flexibility to introduce across-the-board and/or selective reductions in expense budgets should they prove to be necessary.

Financial Position – Debt Rating View

In 2005-2006, Moody's Investors Services and Standard & Poor's Rating Service reaffirmed the University's long-term debt ratings affecting $150 million of unsecured debentures.

Moody's confirmed an Aa1 rating (up from Aa2), and changed from a stable to positive outlook citing the University's:

- Strong student demand underpinning the University's market position.
- Leading research role that enhances competitive positioning and contributes to revenue diversity.
- Prudent financial management which offsets concerns regarding cost pressures.
- Substantial financial resources.
- Debt burden which is below peers.

Standard & Poor's confirmed an AA- rating and continued a stable outlook citing that McGill University has:

- A low debt burden and strong unrestricted resources.
- Solid demand metrics.
- Continued government support.
- Strong tradition of research.

Morty Yalovsky
Vice-Principal (Administration and Finance)

September 2006

PART II

Financial statements of

McGILL UNIVERSITY
(see Note 1)

May 31, 2006

MCGILL UNIVERSITY
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Samson Bélair / Deloitte & Touche s.e.n.c.r.l.
1 Place Ville Marie
Suite 3000
Montreal QC H3B 4T9
Canada

Tel: 514-393-7343
Fax: 514-390-4104
www.deloitte.ca

Auditors' report

To the Board of Governors of McGill University and Trustees of The Royal Institution for the Advancement of Learning:

We have audited the balance sheet of McGill University as at May 31, 2006 and the statements of revenue and expenses and changes in fund balances and cash flows for the year then ended. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

The University has prepared its financial statements in accordance with the recommendations in the *Cahier des définitions, des termes et des directives de présentation du rapport financier annuel pour les universités du Québec* (the "Cahier"), as they are applied in the annual financial report submitted to the ministère de l'Éducation, du Loisir et du Sport du Québec. These recommendations are consistent with Canadian generally accepted accounting principles with the principal exceptions relating to accrued vacation pay, employee future benefits and capital assets. Note 2 describes how the Cahier's recommendations differ from Canadian generally accepted accounting principles.

In our opinion, except for the effects of the accounting methods described in the preceding paragraph, these financial statements present fairly, in all material respects, the financial position of the University as at May 31, 2006 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Chartered Accountants

September _, 2006

McGILL UNIVERSITY
Balance sheet
as at May 31, 2006
(in thousands of dollars)

	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund	Total 2006	Total 2005
	$	$	$	$	$	$
Assets						
Current assets						
Short term investments	**53,843**	**2,154**	**55,375**	**51,678**	**163,050**	155,409
Receivables						
Operating	**19,142**	**157**	**529**	**342**	**20,170**	21,188
Student loans	-	**3,741**	-	-	**3,741**	3,579
Investment income	-	-	-	**3,076**	**3,076**	3,638
Government grants	**42,732**	-	**1,037**	-	**43,769**	44,084
Grants and contracts related to research	-	**171,429**	-	-	**171,429**	182,411
Pledges	**7**	**10,299**	-	-	**10,306**	6,994
Prepaid expenses	**4,912**	**878**	-	-	**5,790**	6,672
Inventory	**1,452**	-	-	-	**1,452**	2,012
Due from (to) other funds	**56,492**	**85,915**	**(142,374)**	**(33)**	-	-
	178,580	**274,573**	**(85,433)**	**55,063**	**422,783**	425,987
Marketable securities, at market value	-	**16,001**	**25,140**	**745,584**	**786,725**	751,693
Grants and contracts related to research receivable - long-term	-	**134,774**	-	-	**134,774**	120,617
Pledges receivable - long-term	**7**	**28,229**	-	-	**28,236**	15,101
Grant receivable (Note 8(c))	-	**301**	**4,731**	-	**5,032**	4,052
Capital assets (Note 3)	-	-	**983,389**	-	**983,389**	945,512
Staff mortgages	-	-	-	**1,511**	**1,511**	2,177
Total assets	**178,587**	**453,878**	**927,827**	**802,158**	**2,362,450**	2,265,139
Liabilities						
Current liabilities						
Bank indebtedness (Note 7)	**176,468**	-	-	-	**176,468**	155,588
Accounts payable and accrued liabilities	**27,507**	**12,012**	**13,524**	**328**	**53,371**	53,627
Unearned revenue	**14,944**	**90**	**1,073**	-	**16,107**	16,144
Provisions for specific purposes	**1,043**	-	-	-	**1,043**	2,867
Current portion of long-term debt (Note 8)	-	-	**40,717**	-	**40,717**	44,148
	219,962	**12,102**	**55,314**	**328**	**287,706**	272,374
Long-term debt (Note 8)	-	**301**	**477,444**	-	**477,745**	436,380
	219,962	**12,403**	**532,758**	**328**	**765,451**	708,754
Commitments and contingent liabilities (Notes 12 and 13)						
Fund balances						
Invested in capital assets	-	-	**387,824**	-	**387,824**	367,820
Externally restricted (Note 4)	-	**441,475**	**13,053**	**775,330**	**1,229,858**	1,186,044
Internally restricted (Note 5)	**38,389**	-	**(5,808)**	**26,500**	**59,081**	61,296
Unrestricted	**(79,764)**	-	-	-	**(79,764)**	(58,775)
	(41,375)	**441,475**	**395,069**	**801,830**	**1,596,999**	1,556,385
Total liabilities and fund balances	**178,587**	**453,878**	**927,827**	**802,158**	**2,362,450**	2,265,139

Approved by the Board of Governors

.... Governor

.... Governor

McGILL UNIVERSITY
Statement of revenue and expenses and changes in fund balances
year ended May 31, 2006
(in thousands of dollars)

	2006					2005				
	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund	Total	Total	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund
	$	$	$	$	$	$	$	$	$	$
Revenue										
Government of Québec										
Grant	250,344	6,272	17,719	-	274,335	264,193	241,280	7,711	15,202	-
Interest on MELS bonds	-	-	20,276	-	20,276	23,695	-	-	23,695	-
Government of Canada	15,394	-	-	-	15,394	16,997	13,585	-	3,412	-
Other government grants	-	-	-	-	-	4,013	-	-	4,013	-
Tuition fees	72,029	-	-	-	72,029	70,121	70,121	-	-	-
Sale of goods and services	67,418	-	156	-	67,574	67,874	67,797	-	77	-
Gifts and bequests	3,807	5,244	9,275	26,321	44,647	32,734	4,141	3,487	12,141	12,965
Net short-term interest income	6,916	-	4,456	-	11,372	10,789	7,443	-	3,346	-
Net investment income (Note 10)	11,543	19,462	490	-	31,495	16,429	7,157	9,269	3	-
	427,451	30,978	52,372	26,321	537,122	506,845	411,524	20,467	61,889	12,965
Services to the community (Note 10)	18,276	25,295	-	-	43,571	36,973	19,926	17,047	-	-
Student services										
Fees and sales of goods and services	13,048	-	-	-	13,048	12,158	12,158	-	-	-
Student aid										
Net investment income (Note 10)	-	19,323	-	-	19,323	8,353	-	8,353	-	-
Donations and grants	329	17,926	-	-	18,255	19,260	240	19,020	-	-
Government of Québec grant	2,033	-	-	-	2,033	1,950	1,950	-	-	-
	15,410	37,249	-	-	52,659	41,721	14,348	27,373	-	-
Ancillary services	50,042	182	-	-	50,224	46,410	46,210	200	-	-
Research										
Net investment income (Note 10)	-	11,124	-	-	11,124	5,307	-	5,307	-	-
Government grants										
Federal	-	109,043	-	-	109,043	106,943	-	106,943	-	-
Provincial	-	30,322	-	-	30,322	48,229	-	48,229	-	-
United States	-	6,921	-	-	6,921	7,099	-	7,099	-	-
Grants from other sources	-	104,999	-	-	104,999	115,177	-	115,177	-	-
	-	262,409	-	-	262,409	282,755	-	282,755	-	-
Total revenue	511,179	356,113	52,372	26,321	945,985	914,704	492,008	347,842	61,889	12,965

McGILL UNIVERSITY
Statement of revenue and expenses and changes in fund balances (continued)
year ended May 31, 2006
(in thousands of dollars)

	2006					2005				
	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund	Total	Total	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund
	$	$	$	$	$	$	$	$	$	$
Total revenue (from previous page)	511,179	356,113	52,372	26,321	945,985	914,704	492,008	347,842	61,889	12,965
Expenses										
Faculties	256,613	9,817	-	-	266,430	250,797	241,692	9,105	-	-
Academic services	53,295	3,534	-	-	56,829	60,382	53,869	6,513	-	-
Support services	131,016	6,287	-	-	137,303	129,414	123,586	5,828	-	-
Amortization and write-downs of capital assets	-	-	73,416	-	73,416	69,854	-	-	69,854	-
Capital assets	-	-	2,632	-	2,632	3,670	-	-	3,670	-
Interest on long-term debt	-	-	29,741	-	29,741	32,920	-	-	32,920	-
Management fees	-	-	-	6,884	6,884	6,892	-	-	-	6,892
Withdrawal	-	-	-	2,557	2,557	-	-	-	-	
	440,924	19,638	105,789	9,441	575,792	553,929	419,147	21,446	106,444	6,892
Services to the community	17,500	16,560	-	-	34,060	33,617	18,935	14,682	-	-
Student services	18,314	31,458	-	-	49,772	45,603	16,455	29,148	-	-
Ancillary services	46,395	192	-	-	46,587	43,287	43,088	199	-	-
Research	-	261,350	-	-	261,350	260,443	-	260,443	-	-
Total expenses	523,133	329,198	105,789	9,441	967,561	936,879	497,625	325,918	106,444	6,892
(Deficiency) excess of revenue over expenses, before the undernoted item	(11,954)	26,915	(53,417)	16,880	(21,576)	(22,175)	(5,617)	21,924	(44,555)	6,073
Unrealized gains (losses) on marketable securities (Note 10)	(778)	(4,974)	1,180	-	(4,572)	8,723	929	1,321	6,474	-
(Deficiency) excess of revenue over expenses	(12,732)	21,941	(52,237)	16,880	(26,148)	(13,451)	(4,688)	23,245	(38,081)	6,073
Fund balance (deficit), beginning of year	(24,384)	435,459	381,123	764,187	1,556,385	1,550,307	(19,636)	415,606	396,618	757,719
Interfund transfers (Note 6)	(4,259)	(15,925)	(579)	20,763	-	-	(60)	(3,392)	3,057	395
Capital expenditures financed by other funds	-	-	66,762	-	66,762	19,529	-	-	19,529	-
Fund balance (deficit), end of year	**(41,375)**	**441,475**	**395,069**	**801,830**	**1,596,999**	1,556,385	(24,384)	435,459	381,123	764,187

McGILL UNIVERSITY
Statement of cash flows
year ended May 31, 2006
(in thousands of dollars)

		2006	2005
		$	$
Operating activities			
Deficiency of revenue over expenses*		**(43,028)**	(19,524)
Non-cash items			
Amortization and write-downs of capital assets		**73,416**	69,854
Gain on sale of marketable securities		**(30,501)**	(12,520)
Unrealized (gains) losses on marketable securities		**4,572**	(8,723)
Net change in non-cash working capital items		**1,059**	(11,521)
Decrease (increase) in grants and contracts related to research receivable		**(3,175)**	9,144
Decrease (increase) in pledges receivable		**(16,447)**	2,217
Decrease (increase) in grant receivable		**(980)**	346
		(15,085)	29,273
Investing activities			
Acquisition of capital assets		**(111,293)**	(133,974)
Disposal (acquisition) of marketable securities, net		**(9,103)**	23,428
Proceeds from staff mortgages, net		**666**	131
		(119,730)	(110,415)
Financing activities			
Net change in Endowment Fund balance		**16,880**	6,073
Net reduction of (contribution to) sinking fund		**(1,121)**	8,066
Issuance of long-term debt		**87,000**	90,000
Repayment of long-term debt		**(47,945)**	(98,141)
Capital expenditures financed by other funds		**66,762**	19,529
		121,576	25,527
Net decrease in cash position		**(13,239)**	(55,615)
Cash position, beginning of year		**(179)**	55,436
Cash position, end of year		**(13,418)**	(179)
Cash position comprises:			
Short-term investments	- Operating Fund	**53,843**	52,557
	- Restricted Fund**	**2,154**	1,496
	- Plant Fund	**55,375**	53,801
	- Endowment Fund**	**51,678**	47,555
Bank indebtedness	- Operating Fund	**(176,468)**	(155,588)
		(13,418)	(179)

* Endowment Fund results are included in financing activities.
** These assets are subject to external restriction.

1. Status and nature of activities

The Corporation with the legal name "Governors, Principal and Fellows of McGill College" ("McGill College") was incorporated in 1821 under Royal Charter and is a university with the power of conferring degrees. The Royal Institution for the Advancement of Learning (the "Royal Institution") was incorporated in 1802 and holds all property acquired by or transferred or bequeathed to McGill College and assumes all debt incurred by McGill College. Together these two corporations constitute the entity known as McGill University ("McGill" or the "University"). These are the financial statements of McGill.

McGill is a not-for-profit organization dedicated to providing post-secondary education and to conducting research and is exempt from tax under provisions of the *Income Tax Act (Canada).*

2. Significant accounting policies

McGill follows the accounting policies and practices required by the *Cahier des définitions, des termes et des directives de présentation du rapport financier annuel pour les universités du Québec* (the "Cahier"), as they are applied in the annual financial report submitted to the Ministère de l'Éducation, du Loisir et du Sport du Québec ("MELS"). These accounting policies, as applied to McGill, are in conformity with Canadian generally accepted accounting principles ("GAAP") except for the following:

- In the course of operations, capital assets are purchased by the Operating and Restricted Funds. MELS requires that these assets be recorded as expenses of the respective fund, and capitalized and amortized in the Plant Fund. During the year, the capital assets acquired in the operating and restricted funds totaled $66,762,000 ($19,529,000 in 2005), as presented in the separate line item "capital expenditures financed by other funds".

- As required by MELS, McGill accounts for vacation pay on a cash basis rather than on an accrual basis. Under the accrual method, the estimated vacation pay accrual would have been $27,498,000 ($26,576,000 in 2005), resulting in a decrease of $922,000 in the excess of revenue over expenses for the year ($1,689,000 in 2005).

- The Government of Québec contributes annually to a bond sinking fund on behalf of McGill. This fund is intended for repayment of bonds at maturity and consequently MELS requires that the amount of $41,384,000 ($40,263,000 in 2005) be presented as a reduction of long-term debt.

2. Significant accounting policies (continued)

– Employee future benefits and pension costs are expensed when paid, rather than accrued during the employee's service. The impractical nature of determining the calculation for disclosure purposes is such that the amount was not determined as of the date of this report.

Had the above items been accounted for as at May 31, 2006, the total excess (deficiency) of operating fund revenue over expenses would have increased by $65,840,000 to an excess of $39,692,000 ($15,415,000 and $1,964,000, respectively in 2005). This amount does not include the effect of accounting for employee future benefits which has not been quantified.

Other significant accounting policies

Fund accounting

McGill follows the restricted fund method of accounting for contributions. This method involves the recording of assets, liabilities, revenue and expenses of distinct activities in separate funds.

The Operating Fund records all teaching, administrative and support activities, together with all unrestricted resources provided to McGill.

The Restricted Fund records resources which are subject to restrictions set by the external provider of the funds.

The Plant Fund records the assets, liabilities, revenue and expenses related to capital property owned and managed by McGill.

The Endowment Fund records gifts received for endowment purposes. Investment income on resources of the Endowment Fund is reported in the Operating, Restricted or Plant Fund depending on the nature of the restriction, if any, imposed by contributors of endowment funds.

Use of estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the amounts of revenue and expenses reported in the financial statements. Actual results may ultimately differ from these estimates. In particular, significant estimates are made regarding valuation of receivables, for values of marketable securities, estimated useful lives of capital assets, and provisions for contingencies.

2. Significant accounting policies (continued)

Other significant accounting policies (continued)

Revenue recognition

Unrestricted contributions are recognized as revenue of the Operating Fund. Restricted contributions are recognized as revenue of the appropriate restricted fund in the year received, or receivable if the amount to be received can be reasonably estimated and collection is reasonably assured. The majority of the pledges receivable are scheduled for receipt within the next five years.

Restricted investment income earned on Endowment Fund assets is recognized as revenue of the appropriate restricted fund. Unrestricted investment income earned on Endowment Fund assets is recognized as revenue of the Operating Fund. Income earned on unexpended Plant Fund balances is recognized as revenue of the Plant Fund.

Interest and dividend revenue is recorded on an accrual basis. Realized gains or losses on sales of investments are recorded when securities are sold based on the cost. Unrealized gains and losses related to the change in market value are disclosed as a distinct line on the statement of revenues and expenses.

Tuition fees are recognized as revenue in the academic year during which the course sessions are held.

Government of Québec operating grants are recorded in the financial year for which they are granted. The Government of Québec grants are based on second prior year student enrolment information. The future grant amount otherwise receivable to reflect actual enrolment figures in the most recent two years have not been recorded as their collection is not considered reasonably assured.

Consolidation

The net results of not-for-profit organizations affiliated with McGill are not reported in these financial statements, as those organizations are not under the control of McGill.

Contributed services

These financial statements do not report the value of contributed volunteer hours and small gifts-in-kind, as the fair value thereof is not practicably determinable. Similarly, gifts-in-kind are not recorded unless a formal valuation to support the amount for tax receipt purposes has been made.

Short-term investments

For the purposes of the statement of cash flows, short-term investments are defined as highly liquid investments with short-term maturities.

2. Significant accounting policies (continued)

Other significant accounting policies (continued)

Marketable securities

Marketable securities are classified as held for trading and are recorded at market value. Changes in market value in the period are recorded in the statement of revenue and expenses.

Realized gains and losses representing sale price less original cost are presented as part of net investment income, and unrealized gains and losses are presented as a distinct line on the statement of revenue and expenses.

Student loans

Student loans are due within one year after graduation and do not bear interest. A provision is recorded for estimated uncollectible amounts.

Inventory

Inventory, including books and supplies, is valued at the lower of cost and net realizable value.

Capital assets

Capital assets are recorded at cost. Constructed assets normally include interest capitalized during construction, based on the current cost of borrowing. Contributed capital assets are recorded at appraised fair value at the date of contribution when fair value can be reasonably estimated; otherwise they are recorded at a nominal amount.

Capital assets also include equipment purchased from operating funds, where the cost is to be charged against revenue in accordance with amortization schedules or other arrangements which provide for full recovery of costs over the estimated useful lives of such assets. Interest is charged on the amount outstanding based on the external cost of borrowing at the time of purchase. In exceptional cases of particular need, the internal recovery of interest costs may be waived or reduced.

Amortization of capital assets is recorded as an expense in the Plant Fund. Amortization of assets under development commences when development is completed. The amortization rate and method is prescribed by the MELS based on the estimated useful lives of various asset categories as follows:

Land improvements	Straight-line	20 years
Buildings	Declining balance	2% per year
Leasehold improvements	Straight-line	Term of lease
Equipment	Straight-line	5 to 8 years
Intangible assets*	Straight-line	5 years
Library materials	Straight-line	40 years
Bond discounts	Straight-line	Term of bond

* Intangible assets include software licences and user licenses for electronic information resources.

(tabular amounts in thousands of dollars)

2. Significant accounting policies (continued)

Other significant accounting policies (continued)

Capitalization of investment income

As outlined above (revenue recognition), all investment income is attributed to a specific fund in its totality.

A portion of investment income earned on endowment fund assets is reinvested, through inter-fund transfers, to maintain the purchasing power of the original capital. Although this policy is an internal restriction, the amounts so capitalized are added to the externally restricted balances for reporting purposes.

3. Capital assets

	2006			2005		
	Cost	Accumulated amortization	Net book value	Cost	Accumulated amortization	Net book value
	$	**$**	**$**	$	$	$
Land	**8,110**	**-**	**8,110**	8,110	-	8,110
Land improvements	**3,272**	**1,219**	**2,053**	3,221	1,055	2,166
Buildings	**835,119**	**217,319**	**617,800**	762,204	204,711	557,493
Leasehold improvements	**763**	**291**	**472**	304	152	152
Equipment	**332,992**	**169,105**	**163,887**	305,533	144,239	161,294
Library materials	**191,268**	**37,544**	**153,724**	177,960	32,763	145,197
Intangible assets	**26,542**	**19,305**	**7,237**	34,365	24,942	9,423
Bond discounts	**11,409**	**3,839**	**7,570**	12,771	4,936	7,835
	1,409,475	**448,622**	**960,853**	1,304,468	412,798	891,670
Assets under development	**22,536**	-	**22,536**	53,842	-	53,842
	1,432,011	**448,622**	**983,389**	1,358,310	412,798	945,512

(tabular amounts in thousands of dollars)

4. Externally restricted fund balances

	2006				2005
	Restricted Fund	Plant Fund	Endowment Fund	Total	Total
	$	$	$	$	$
Research	**373,618**	**-**	**86,449**	**460,067**	451,118
Faculties	**8,389**	**-**	**216,076**	**224,465**	213,893
Academic services	**3,534**	**-**	**21,116**	**24,650**	23,948
Support services	**6,818**	**13,053**	**14,855**	**34,726**	34,332
Community services	**28,735**	**-**	**11,945**	**40,680**	34,970
Student services	**20,381**	**-**	**181,083**	**201,464**	187,350
Accumulated income (i)	**-**	**-**	**243,806**	**243,806**	240,433
	441,475	**13,053**	**775,330**	**1,229,858**	1,186,044

(i) This income is presented as externally restricted, however, as stated in Note 2 ("Capitalization of investment income") the accumulated reinvested income is subject to internal restrictions imposed by the Board of Governors.

5. Internally restricted fund balances

	2006				2005
	Operating Fund	Plant Fund	Endowment Fund	Total	Total
	$	$	$	$	$
Faculties	**9,806**	**-**	**2,297**	**12,103**	12,401
Academic services	**520**	**-**	**2,269**	**2,789**	5,199
Support services	**15,108**	**(5,808)**	**20,881**	**30,181**	30,341
Community services	**9,496**	**-**	**990**	**10,486**	9,415
Student services	**3,224**	**-**	**63**	**3,287**	3,940
Ancillary services	**235**	**-**	**-**	**235**	-
	38,389	**(5,808)**	**26,500**	**59,081**	61,296

(tabular amounts in thousands of dollars)

6. Interfund transfers

	2006			
	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund
	$	**$**	**$**	**$**
Underdistributed income (a)	**(2,419)**	**(16,021)**	**-**	**18,440**
Unrealized gains on endowment investments	778	5,154	-	(5,932)
Net capitalization of income (b)	**101**	**(8,106)**	**1,006**	**6,999**
Other transfers (c)	**(2,719)**	**3,048**	**(1,585)**	**1,256**
	(4,259)	**(15,925)**	**(579)**	**20,763**

	2005			
	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund
	$	**$**	**$**	**$**
Overdistributed income (a)	2,047	12,903	2	(14,952)
Unrealized gains on endowment investments	(929)	(5,856)	(2)	6,787
Net capitalization of income (b)	132	(9,172)	322	8,718
Other transfers (c)	(1,310)	(1,267)	2,735	(158)
	(60)	(3,392)	3,057	395

(a) Realized investment income does not normally equal the amount determined by the University’s annual income distribution policy. Accordingly, the difference between the two is represented as either under or over distributed income, and flows to and from the Endowment Fund to the other funds.

(b) Represents the re-investment of unspent annual income distribution.

(c) Other transfers include transfers of internally restricted funds and authorized transfers of externally restricted funds.

7. Bank indebtedness

The University’s Board of Governors has approved a maximum borrowing on short-term credit facilities of $250 million, arranged through unsecured lines of credit up to a maximum of $195 million, normally drawn through bankers’ acceptances for periods ranging up to one year. The balance is available through other individually negotiated credit facilities. The lines of credit bear interest at the prime rate, which averaged 4.9% for the year.

The University manages its cash centrally in the Operating Fund. As a result, receipts and disbursements of other funds are recorded as amounts due to or from the Operating Fund. The amounts are non-interest bearing and have no fixed terms of repayment, however they are primarily working capital in nature and, accordingly, are classified as short-term.

(tabular amounts in thousands of dollars)

8. Long-term debt

	2006	2005
	$	$
a) Government of Québec debt, net		
1) MELS Bonds (i)		
3.75% Series "9C" due September 12, 2005	**-**	5,685
8.85% Series "1B" due September 15, 2005	**-**	3,892
11% Series "KK" due December 20, 2005	**-**	6,120
4.20% Series "6C" due February 14, 2006	**-**	3,360
5.75% Series "6B" due February 15, 2006	**-**	2,000
4.10% Series "7C" due February 15, 2006	**-**	3,603
3.55% Series "10C" due February 27, 2006	**-**	5,885
4.40% Series "8C" due February 28, 2006	**-**	4,795
8.0% Series "2B" due April 12, 2006	**-**	4,245
8.15% Series "2B" due April 12, 2006	**-**	4,356
5.35% Series "4C" due June 14, 2006	**10,593**	10,593
5.55% Series "5C" due July 27, 2006	**11,523**	11,523
7.90% Series "3B" due August 2, 2006	**3,122**	3,122
8.00% Series "3B" due August 2, 2006	**6,843**	6,843
10.25% Series "LL" due November 12, 2006	**1,000**	1,000
4.75% Series "8C" due February 28, 2007	**8,700**	8,700
11.50% Series "1" due January 29, 2008	**4,525**	4,525
5.00% Series "6C" due February 14, 2008	**12,782**	12,782
4.95% Series "7C" due February 15, 2008	**6,039**	6,039
5.05% Series "8C" due February 28, 2008	**15,900**	15,900
5.10% Series "8C" due February 28, 2008	**11,333**	11,333
5.80% Series "6B" due March 13, 2008	**6,218**	6,218
3.15% Series "11C" due May 27, 2008	**6,726**	6,726
3.55% Series "12C" due November 24, 2008	**9,395**	-
4.70% Series "9C" due September 12, 2008	**6,910**	6,910
13.25% Series "II" due January 12, 2009	**3,000**	3,000
3.75% Series "13C" due February 24, 2009	**6,510**	-
4.55% Series "10C" due February 27, 2009	**7,973**	7,973
10.75% Series "3" due May 30, 2009	**7,000**	7,000
5.50% Series "1C" due June 4, 2009	**2,100**	2,100
6.65% Series "2C" due November 26, 2009	**6,575**	6,575
4.00% Series "14C" due March 8, 2010	**10,000**	-
6.20% Series "4C" due June 14, 2011	**13,981**	13,981
4.005 Series "12C" due November 24, 2011	**5,605**	-

(tabular amounts in thousands of dollars)

8. Long-term debt (continued)

	2006	2005
	$	$
a) Government of Québec debt, net (continued)		
1) MELS Bonds (i) (continued)		
5.75% Series "6C" due February 14, 2012	**3,858**	3,858
5.70% Series "7C" due February 15, 2012	**5,358**	5,358
4.10% Series "13C" due February 24, 2012	**8,837**	-
5.75% Series "8C" due February 28, 2012	**5,400**	5,400
5.80% Series "8C" due February 28, 2012	**3,872**	3,872
4.05% Series "11C" due May 27, 2012	**8,571**	8,571
5.40% Series "9C" due September 12, 2012	**7,405**	7,405
5.30% Series "10C" due February 27, 2013	**10,451**	10,451
4.50% Series "11C" due May 27, 2015	**4,703**	4,703
4.40% Series "13C" due February 24, 2016	**4,653**	-
4.50% Series "14C" due March 8, 2016	**7,000**	-
	254,461	246,402
2) Financement Québec Notes (ii)		
4.516% due December 1, 2008	**22,989**	24,340
3.849% due December 1, 2009	**24,297**	25,309
4.059% due December 1, 2010	**30,000**	-
4.167% due December 1, 2010	**5,000**	-
4.288% due December 1, 2011	**25,000**	25,000
4.9515% due November 1, 2012	**42,376**	45,000
4.267% due December 1, 2015 (iii)	**1,503**	-
	151,163	119,649
	405,624	366,051
Accumulated contributions to sinking fund (iv)	**(41,384)**	(40,263)
Total Government of Québec debt, net	**364,240**	325,788
b) McGill University Senior Debentures (v), 6.15% Series "A", due September 22, 2042	**150,000**	150,000
c) Royal Bank loans (vi),		
5.81%, due February 2014	**3,594**	3,939
5.17%, due June 2008	**301**	459
d) Other	**325**	342
Total long-term debt	**518,459**	480,528
Current portion of long-term debt	**(40,717)**	(44,148)
Long-term debt	**477,745**	436,380

(tabular amounts in thousands of dollars)

8. Long-term debt (continued)

(i) Debt issued by the Government of Québec is secured by an assignment of subsidies covering principal and interest granted to McGill by the Government of Québec under Orders-in-Council. Future subsidies which secure repayment of outstanding bonds and related interest as well as approved Orders-in-Council not yet utilized by McGill are not recorded.

The University has also made capital expenditures of $99 million ($98 million in 2005), currently financed through bank indebtedness, which will be financed by bonds to be issued at future dates as determined by the Government of Québec.

(ii) As with MELS bonds, Financement Québec notes are secured by the Government of Québec, however as opposed to sinking fund contributions, regular interest and capital repayments are made by the Government on McGill's behalf. Interest on the notes is paid semi-annually and capital repayments are due on each note's anniversary date. Capital repayments due annually and lump sum payments due at maturity are as follows:

	Annual payment	Lump sum payment
	$	$
4.516% due December 1, 2008	1,351	20,288
3.849% due December 1, 2009	1,012	21,260
4.059% due December 1, 2010	1,389	24,445
4.167% due December 1, 2010	200	4,200
4.288% due December 1, 2011	1,162	19,188
4.9515% due November 1, 2012	2,624	26,635

(iii) The Financement Québec note are secured by a grant receivable from the Ministère du Développement économique de l'innovation et de l'Exportation (MDEIE) of $1.5 million. Semi-annual payments of capital and interest are paid by MDEIE, on the University's behalf, to Financement Québec.

(iv) In 1994, the Government of Québec established a sinking fund to set aside amounts in order to repay outstanding bonds issued by certain universities. During the year, MELS contributed $11,151,000 to this fund ($13,851,000 in 2005) and applied $10,030,000 towards repaid bonds ($21,917,000 in 2005).

(v) In September 2002, McGill University issued $150 million of unsecured debentures. Unlike MELS bonds, McGill will be required to repay these obligations from resources generated by the University (see Note 14). Semi-annual interest payments are paid by the University.

(vi) The Royal Bank loans are secured by grants receivable from the Ministère des Affaires municipals et des Régions ("MAMR") and the Ministère de la Culture et des Communications ("MCC"), of $3.6 million and $0.3 million, respectively. Semi-annual payments of capital and interest are paid by the University and reimbursed by both MAMR and MCC.

(tabular amounts in thousands of dollars)

8. Long-term debt (continued)

Repayments of the principal due in each of the next five years (net of the accumulated contributions to the sinking fund allocated by year) are as follows:

	$
2007	**40,717**
2008	**58,713**
2009	**54,396**
2010	**43,675**
2011	**33,035**

9. Employee future benefits

Pension plans

The majority of McGill University's employees are members of a defined contribution pension plan (the "Plan"). Employee contributions are accumulated together with employer contributions and invested in the Plan's Accumulation Fund. At retirement age, the accumulated amount is available for the purchase of a retirement annuity to be underwritten by a provider of the retiree's choice, including, if elected, an annuity provided by McGill. For the University's pensions subject to defined benefits, the actuarial obligations on a going concern basis of $1,082,781,000 at July 31, 2004 under this plan are virtually fully funded by plan assets having a market value of $1,082,206,000 at July 31, 2004, with any shortfall based on the actuarial valuation to be paid by the University.

An actuarial valuation, carried out July 31, 2004 by Eckler Partners Ltd. using the solvency method, confirmed a funding deficit of approximately $7.8 million. The regulatory body requires an annual contribution of $2.75 million (capital and interest) until December 31, 2005 and $1.75 million thereafter until October 31, 2008 in order to fully absorb the deficiency. The total current year contribution of $21.9 million has been recorded as the pension expense for this fiscal year ($20.3 million in 2005).

The next such valuation is required no later than December 31, 2006.

Other plans and arrangements

The University has a commitment to a specific group of employees who accepted early retirement settlements in 1996. These settlements entitled the employees to receive annual retirement allowance payments over their lifetime. The present value of these commitments as at May 31, 2006 is estimated at $3 million.

(tabular amounts in thousands of dollars)

10. Net investment income from endowments

Realized net investment income is included in the statement of revenue and expenses in the following revenue line items: net investment income, services to the community, student services net investment income, and research net investment income.

During the year, realized net investment income earned on resources held for endowment amounted to $59,263,000 and were reported in the following funds:

	2006	2005
	$	$
Operating Fund	**4,659**	268
Restricted Fund	**54,604**	27,247
Plant Fund	**-**	5
	59,263	27,520

In addition, the total unrealized loss on marketable securities related to resources held for endowment amounted to $5,752,000 ($2,249,000 of unrealized gains in 2005). This was offset by an unrealized gain of $1,180,000 ($6,474,000 in 2005) relating to investments purchased using the proceeds of the Debenture issue (see Note 14). Consequently, the total net unrealized loss as at May 31, 2006 was $4,572,000 ($8,723,000 unrealized gains in 2005).

11. Financial Instruments

Financial risks

The University is subject to market risk which is the risk that the value of a financial instrument will fluctuate as a result of changes in market prices whether those changes are caused by factors specific to the individual security or its issuer or factors affecting all securities traded in the market. The concentration of risk is minimized because of the University's diversification of their investment portfolio.

The University has foreign currency risk arising from its foreign denominated cash accounts, and its holdings of foreign equities and bonds.

The University has interest rate risk from the impact of interest rate changes on the University's cash flows and financial position.

The University is exposed to credit risk from its debtors. A significant portion of the University's receivables are due from governments which are believed to be at low risk of default. For the remaining receivables, the concentration of risk is minimized because of the University's large and diverse base of counter-parties and investments.

(tabular amounts in thousands of dollars)

11. Financial Instruments (continued)

Fair values

At May 31, 2006, the carrying values of cash and short-term investments, receivables, grants and contracts related to research receivable, bank indebtedness and accounts payable and accrued liabilities approximate their fair values.

As disclosed in Note 2, marketable securities are presented at market value.

Pledges receivable are not considered to be financial assets due to the fact that they do not arise from contractually binding arrangements. In addition, due to the nature of the asset, it is not practicable to assess its fair value.

Staff mortgages are issued at rates and terms comparable to commercial home mortgages. Accordingly, carrying value approximates fair value.

The fair value of long-term debt, excluding reductions for the sinking fund and based on rates currently available to the University for debt with similar terms and maturities, is $543,350,000 at May 31, 2006 ($543,615,000 in 2005).

The University holds derivative financial instruments related to the marketable securities purchased to eventually redeem the $150 million of debentures. The instruments are recorded at their fair values. See Note 14 for details.

McGill has forward contracts outstanding as at May 31, 2006 to sell US$100 million with an average forward rate of 1.13 maturing on July 24, 2006. As at May 31, 2006, the fair value of these contracts approximated $3,550,000.

The marketable securities portfolio is comprised of the following types of investments:

	Endowment Fund	Restricted Fund
	%	%
Canadian Equity	21	20
US Equity	29	28
Non North American Equity	17	16
Canadian Fixed Income	32	35
US Fixed Income	1	1

(tabular amounts in thousands of dollars)

12. Commitments

Year ending May 31	Minimum lease payments
	$
2007	**1,905**
2008	**1,737**
2009	**1,367**
2010	**1,293**
2011	**1,011**
Thereafter	**3,804**
	$11,117

The amounts represent future minimum lease payments under existing operating leases.

Construction in progress

The University has undertaken the construction of several new buildings, and as a result has commitments totalling $75.5 million ($24.8 million in 2005). These commitments are expected to be met in the normal course of operations.

Private equity funding commitments

As part of its investment activities, McGill places some of its endowment investments through private equity funds. McGill is committed to invest an additional $50.8million in accordance with its arrangements with these funds.

13. Contingent liabilities

Litigation

In February 2002, an action was instituted against McGill in the amount of $12.85 million for bodily injuries. The plaintiff alleged the University was negligent because it did not properly maintain the ventilation system in a laboratory causing the plaintiff to develop leukemia. Two other proceedings alleging substantially the same causes of action were also instituted against the University in March and May 2002, totaling $2.5 million. As of September 1, 2005, McGill has not yet filed a defense to any of the actions as no plea has been filed in these proceedings. McGill's insurers have taken a position that the claims are excluded under a clause of the applicable insurance policies. McGill considers that this matter is unresolved at this time. The outcome of any proceedings, and impact thereof, cannot be reasonably determined at this time. Consequently, these financial statements do not include any effect of potential outcomes.

In the normal course of its activities, McGill is party to various legal proceedings, including claims related to labour laws and the Civil Code. Although it is not possible to determine the ultimate outcome of such proceedings initiated and ongoing at May 31, 2006, management is of the opinion that they will be resolved without material effect on McGill's financial position. Any amount McGill may be required to pay will be charged to operations in the year of settlement; if the amount can be estimated and is considered likely to occur, it is provided for in the provision for specific purposes.

(tabular amounts in thousands of dollars)

14. Supplementary information

Included in the assets, liabilities, and fund balance of the Plant Fund are items related to ancillary service activities financed by the proceeds of the September 2002 issuance of McGill debentures (Note 8). Details of these items are as follows:

	2006	2005
	$	$
Assets		
Cash and short-term investments (i)	**55,375**	53,801
Marketable securities, at market (ii)	**25,136**	23,956
Due from other funds (iii)	**-**	4,125
Capital assets		
Land	**1,730**	1,730
Buildings	**71,630**	66,061
Equipment	**871**	942
Bond discounts (iii)	**6,058**	6,225
Total assets	**160,800**	156,840
Liabilities		
Interest payable	**1,703**	1,540
Due to other funds (iv)	**5,459**	-
Long-term debt	**150,000**	150,000
Total liabilities	**157,162**	151,540
Fund balance		
Invested in capital assets	**15,220**	12,803
Internally restricted (v)	**(11,582)**	(7,503)
Total fund balance	**3,638**	5,300
Total liabilities and fund balance	**160,800**	156,840

(i) Represents cash, bankers' acceptances, and treasury bills held for the purpose of future investment in revenue generating properties.

(ii) In October 2003, the University entered into an agreement with RBC Dominion Securities ("RBCDS") whereby it invested in a US$13 million denominated bond maturing in 2029. Under this agreement, the bond principal and the semi-annual interest payments due to McGill were swapped with RBCDS in exchange for RBCDS paying McGill $85.7 million Canadian dollars in 2029. The $25.1 million presented includes the market value of the bond and the swap agreement.

The future value of this investment, including accumulated growth to the year 2042, is expected to be sufficient to effectively redeem the $150 million of outstanding long-term debt.

(tabular amounts in thousands of dollars)

14. Supplementary information (continued)

(iii) Original bond issue costs amounted to $6,667,000, and are being amortized on a straight-line basis over the 40 year term of the bonds. The annual amortization is approximately $166,000.

(iv) The amounts relate to inter-fund transactions conducted in the normal course of business. Cash settlement is expected in June 2006, which will effectively decrease overall unspent cash balance relating to the McGill debentures.

(v) The fund balance, currently in a deficit position, will increase over the years as a result of net surpluses generated from revenue generating activities. These activities have been financed by the McGill unsecured debenture. All future surpluses will be internally restricted in order to generate a sinking fund which is intended to be used to contribute towards the repayment of the debentures maturing in September 2042, and other potential purchases of revenue generating assets.

Included in the revenues and expenses of the Plant Fund are items related to ancillary service activities financed by the proceeds of the September 2002 issuance of McGill debentures (Note 8). Details of these items are as follows:

	2006	2005
	$	$
Revenue		
Net short term interest income	**3,914**	3,089
Total revenue	**3,914**	3,089
Expenses		
Amortization	**2,004**	1,736
Expensed capital assets	**4**	5
Interest on long-term debt	**9,225**	9,225
Total expenses	**11,233**	10,966
Deficiency of revenues over expenses	**(7,319)**	(7,877)
Capital costs recovered from other funds	**4,477**	4,774
Unrealized gains on marketable securities	**1,180**	6,471
Interfund transfers	**-**	(577)
Total increase (decrease) in fund balance	**(1,662)**	2,791

15. Comparative amounts

Certain comparative amounts for the year ended May 31, 2005 have been reclassified in order to conform to the presentation adopted in the current year.