Financial statements of

McGILL UNIVERSITY
(see Note 1)

May 31, 2004

MCGILL UNIVERSITY
Table of contents

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, 2004 and the statements of revenue and expenses and changes in fund balances and of 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 Québec. These recommendations are consistent with Canadian generally accepted accounting principles with the principal exceptions relating to accrued vacation pay, employee future benefits, fixed assets, and marketable securities. 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, 2004 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Samson Bélair / Deloitte & Touche s.e.n.c.r.l.

Chartered Accountants

September 3, 2004

McGILL UNIVERSITY
Balance sheet
as at May 31, 2004
(in thousands of dollars)

	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund	Total 2004	Total 2003
	$	$	$	$	$	$ (Restated) (Note 3)
Assets						
Current assets						
Cash and short-term investments	-	-	60,300	40,385	100,685	128,561
Receivables and accruals						
Operating	22,633	1,017	1,626	369	25,645	28,812
Student loans	-	3,349	-	-	3,349	3,107
Investment income	-	-	-	3,417	3,417	4,236
Government grants	40,154	213	-	-	40,367	52,562
Grants and contracts related to research	-	167,084	-	-	167,084	136,083
Pledges	5	8,827	-	-	8,832	11,948
Prepaid expenses	4,080	1,599	-	-	5,679	3,959
Inventory	2,157	-	-	-	2,157	173
Due from (to) other funds	13,170	61,651	(71,263)	(3,558)	-	-
	82,199	243,740	(9,337)	40,613	357,215	369,441
Marketable securities, at market	-	21,284	17,489	715,105	753,878	651,289
Grants and contracts related to research receivable - long-term	-	145,087	-	-	145,087	38,452
Pledges receivable - long-term	42	15,438	-	-	15,480	15,926
Grant receivable (Note 9(c))	-	459	3,939	-	4,398	-
Capital assets (Note 4)	-	-	881,392	-	881,392	801,581
Staff mortgages	-	-	-	2,308	2,308	3,497
Total assets	82,241	426,008	893,483	758,026	2,159,758	1,880,186
Liabilities						
Current liabilities						
Bank indebtedness (Note 8)	45,249	-	-	-	45,249	23,159
Payables						
Operating	31,072	9,932	16,721	307	58,032	60,012
Special early retirement	1,169	-	-	-	1,169	1,422
Current portion of long-term debt (Note 9)	-	-	98,125	-	98,125	4,000
Unearned revenue	19,571	11	-	-	19,582	15,770
Provisions for specific purposes	4,816	-	-	-	4,816	8,300
	101,877	9,943	114,846	307	226,973	112,663
Long-term debt (Note 9)	-	459	382,019	-	382,478	438,745
	101,877	10,402	496,865	307	609,451	551,408
Commitments and contingent liabilities (Notes 13 and 14)						
Fund balances						
Invested in capital assets	-	-	386,608	-	386,608	335,521
Externally restricted (Note 5)	-	415,606	9,420	732,003	1,157,029	979,305
Internally restricted (Note 6)	24,012	-	590	25,716	50,318	59,081
Unrestricted	(43,648)	-	-	-	(43,648)	(45,129)
	(19,636)	415,606	396,618	757,719	1,550,307	1,328,778
Total liabilities and fund balances	82,241	426,008	893,483	758,026	2,159,758	1,880,186

Approved by the Board of Governors

.... Governor

.... Governor

McGILL UNIVERSITY
Statement of revenue and expenses and changes in fund balances
year ended May 31, 2004
(in thousands of dollars)

	2004					2003 (Restated) (Note 3)				
	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund	Total	Total	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund
	$	$	$	$	$	$	$	$	$	$
Revenue										
Government of Québec										
Grant	218,922	7,989	13,851	-	240,762	239,351	216,022	8,373	14,956	-
Interest on MEQ bonds	-	-	22,527	-	22,527	23,354	-	-	23,354	-
Government of Canada	13,414	-	-	-	13,414	-	-	-	-	-
Tuition fees	67,795	-	-	-	67,795	64,374	64,374	-	-	-
Sale of goods and services	58,869	-	-	-	58,869	51,753	51,753	-	-	-
Gifts and bequests	3,220	2,093	8,198	16,874	30,385	48,935	4,306	9,812	15,134	19,683
Net short-term interest income	4,708	-	4,735	-	9,443	10,650	6,648	-	4,002	-
Net investment income (Note 11)	6,227	8,931	-	-	15,158	4,234	2,460	1,774	-	-
	373,155	19,013	49,311	16,874	458,353	442,651	345,563	19,959	57,446	19,683
Services to the community (Note 11)	19,121	20,095	-	-	39,216	24,099	21,018	3,081	-	-
Student services										
Fees and sales of goods and services	11,541	-	-	-	11,541	10,632	10,632	-	-	-
Student aid										
Net investment income (Note 11)	-	13,224	-	-	13,224	1,864	-	1,864	-	-
Donations and grants	424	15,978	-	-	16,402	13,875	430	13,445	-	-
Government of Québec grant	1,812	-	-	-	1,812	1,813	1,813	-	-	-
	13,777	29,202	-	-	42,979	28,184	12,875	15,309	-	-
Ancillary services	42,996	222	-	-	43,218	27,853	27,631	222	-	-
Research										
Net investment income (Note 11)	-	6,213	-	-	6,213	1,027	-	1,027	-	-
Government grants										
Federal	-	114,611	-	-	114,611	90,435	-	90,435	-	-
Provincial	-	59,986	-	-	59,986	31,869	-	31,869	-	-
United States	-	8,460	-	-	8,460	9,555	-	9,555	-	-
Grants and contracts from other sources	-	155,782	-	-	155,782	103,683	-	103,683	-	-
	-	345,052	-	-	345,052	236,569	-	236,569	-	-
Total revenue	449,049	413,584	49,311	16,874	928,818	759,356	407,087	275,140	57,446	19,683

McGILL UNIVERSITY
Statement of revenue and expenses and changes in fund balances (continued)
year ended May 31, 2004
(in thousands of dollars)

	2004					2003 (Restated) (Note 3)				
	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund	Total	Total	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund
	$	$	$	$	$	$	$	$	$	$
Total revenue (from previous page)	449,049	413,584	49,311	16,874	928,818	759,356	407,087	275,140	57,446	19,683
Expenses										
Faculties	218,563	15,922	-	-	234,485	217,392	202,026	15,366	-	-
Academic services	57,386	5,515	-	-	62,901	56,293	49,337	6,956	-	-
Support services	102,273	971	-	-	103,244	101,536	100,626	910	-	-
Amortization, write-downs, and disposals of capital assets	-	-	64,556	-	64,556	55,355	-	-	55,355	-
Capital assets	-	-	2,189	-	2,189	1,508	-	-	1,508	-
Loss on disposal of assets	-	-	162	-	162	-	-	-	-	-
Interest on long-term debt	-	-	31,831	-	31,831	29,663	-	-	29,663	-
Management fees	-	-	-	7,039	7,039	6,567	-	-	-	6,567
	378,222	22,408	98,738	7,039	506,407	468,314	351,989	23,232	86,526	6,567
Services to the community	19,696	14,907	-	-	34,603	35,099	21,685	13,414	-	-
Student services	15,961	26,770	-	-	42,731	39,043	15,040	24,003	-	-
Ancillary services	40,177	222	-	-	40,399	27,120	26,909	211	-	-
Research		251,836	-	-	251,836	213,521	-	213,521	-	-
Total expenses	454,056	316,143	98,738	7,039	875,976	783,097	415,623	274,381	86,526	6,567
Excess (deficiency) of revenue over expenses, before the undernoted item	(5,007)	97,441	(49,427)	9,835	52,842	(23,741)	(8,536)	759	(29,080)	13,116
Unrealized gains (losses) on marketable securities (Note 11)	7,897	64,346	-	-	72,243	(65,852)	(7,684)	(54,966)	(3,202)	-
Excess (deficiency) of revenue over expenses	2,890	161,787	(49,427)	9,835	125,085	(89,593)	(16,220)	(54,207)	(32,282)	13,116
Fund balance (deficit), beginning of year (as restated, see Note 3)	(16,301)	312,849	352,579	679,651	1,328,778	1,331,957	(12,447)	291,203	293,609	759,592
Interfund transfers (Note 7)	(6,225)	(59,030)	(2,978)	68,233	-	-	12,366	75,853	4,838	(93,057)
Capital expenditures financed by other funds	-	-	96,444	-	96,444	86,414	-	-	86,414	-
Fund balance (deficit), end of year	(19,636)	415,606	396,618	757,719	1,550,307	1,328,778	(16,301)	312,849	352,579	679,651

McGILL UNIVERSITY
Statement of cash flows
year ended May 31, 2004
(in thousands of dollars)

	2004	2003
	$	$ (Restated) (Note 3)
Operating activities		
Excess (deficiency) of revenue over expenses *	**115,250**	(102,709)
Non-cash items		
Amortization, write-downs, and disposals of capital assets	**64,556**	55,355
(Gain) loss on sale of marketable securities	**(14,667)**	9,427
Unrealized (gains) losses on marketable securities	**(72,243)**	65,852
Net change in non-cash working capital items	**10,330**	(23,004)
Increase in grants and contracts receivable related to research	**(137,636)**	(42,494)
Decrease in pledges receivable	**3,562**	3,527
Increase in grant receivable	**(4,398)**	-
	(35,246)	(34,046)
Investing activities		
Acquisition of capital assets	**(144,367)**	(184,161)
Acquisition of marketable securities, net	**(15,678)**	11,845
Proceeds from staff mortgages, net	**1,189**	1,646
	(158,856)	(170,670)
Financing activities		
Net change in Endowment Fund balance	**9,835**	13,116
Net reduction of (contribution to) sinking fund	**(13,851)**	1,541
Issuance of long-term debt	**55,773**	194,309
Repayment of long-term debt	**(4,065)**	(75,226)
Capital expenditures financed by other funds	**96,444**	86,414
	144,136	220,154
Net (decrease) increase in cash and short-term investments	**(49,966)**	15,438
Cash position, beginning of year	**105,402**	89,964
Cash position, end of year	**55,436**	105,402
Cash position comprises:		
Cash and short-term investments - Plant Fund	**60,300**	79,555
- Endowment Fund**	**40,385**	49,006
Bank indebtedness - Operating Fund	**(45,249)**	(23,159)
	55,436	105,402

* 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 Québec ("MEQ"). 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. The MEQ 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 totalled $96,444,000 ($86,414,000 in 2003).

- As required by the MEQ, 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 $24,887,000 ($23,805,000 in 2003), resulting in a reduction of $1,082,000 in the excess of revenue over expenses for the year ($2,214,000 in 2003).

- The MEQ allows universities to present marketable securities at either cost or market value. These financial statements present marketable securities at market value. Unrealized gains and losses related to changes in market value are disclosed in the statement of revenue and expenses.

  Under GAAP, the marketable securities would have to be recorded at cost, less the effect of any other than temporary declines in value of individual securities. Had the University recorded its marketable securities at cost, the assets reported would have been lower by $72,243,000 ($41,373,000 in 2003). Similarly, under GAAP, the unrealized gain would not have been recorded and the excess of revenue over expenses would have been lower by this amount. The amount of these differences from GAAP does not reflect the potential additional impact that might have been recorded had the University performed a review for other than temporary declines in securities values.

2. Significant accounting policies (continued)

- 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 the MEQ requires that the amount be presented as a reduction of long-term debt.

- Bond discounts are recorded as capital assets in accordance with MEQ requirements rather than as a deferred charge.

- 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, 2004, the total excess (deficiency) of revenue over expenses would have increased by $23,119,000 to $148,204,000 ($42,827,000 and $46,766,000 loss, respectively in 2003). 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.

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.

Investment income earned on restricted Endowment Fund assets is recognized as revenue of the appropriate restricted fund. Such income earned on unrestricted Endowment Fund assets is recognized as revenue of the Operating Fund. That 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.

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 enrollment information. The grant amount is adjusted to reflect actual figures in future years based on then current calculation methods. Due to the uncertainty of the treatment of deregulated students by the Government of Québec and the calculation method to be used, the amount of the future grant cannot be reasonably estimated and as such has not been recorded by the University.

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

Consolidation

The net results of not-for-profit organizations affiliated with McGill are not reported in these financial statements.

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.

2. Significant accounting policies (continued)

Cash and short-term investments

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

Marketable securities

Marketable securities are recorded at market value.

Student loans

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

Inventory

Inventory, including books and supplies, is valued at 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. The amortization rate and method is prescribed by the MEQ 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
Library books	Straight-line	40 years
Bond discounts	Straight-line	Term of bond

(tabular amounts in thousands of dollars)

2. 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 interfund 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. Restatement of comparative results

Effective June 1, 2003, the University adopted a new accounting policy, in accordance with MEQ guidelines, to record marketable securities at market values whereas they were previously recorded at cost. This adjustment was applied retroactively and resulted in an adjustment to the 2003 financial statements thereby increasing marketable securities and total assets by $41,373,000, and ending fund balances by $1,238,000 in the restricted fund and $40,135,000 in the endowment fund. The excess of revenue over expenses decreased by the amount of the unrealized losses on marketable securities of $65,852,000 and the opening fund balance was increased by $3,056,000 in the restricted fund and $104,169,000 in the endowment fund.

4. Capital assets

	2004			2003		
	Cost	Accumulated amortization	Net book value	Cost	Accumulated amortization	Net book value
	$	$	$	$	$	$
Land	**8,110**	**-**	**8,110**	8,110	-	8,110
Land improvements	**3,221**	**894**	**2,327**	2,468	733	1,735
Buildings	**732,617**	**193,333**	**539,284**	664,321	182,473	481,848
Leasehold improvements	**-**	**-**	**-**	1,397	1,397	-
Equipment	**303,892**	**139,487**	**164,405**	252,606	112,688	139,918
Library materials	**163,940**	**28,314**	**135,626**	151,111	24,215	126,896
Bond discounts	**13,248**	**4,858**	**8,390**	13,742	4,434	9,308
	1,225,028	**366,886**	**858,142**	1,093,755	325,940	767,815
Assets under development	**23,250**	**-**	**23,250**	33,766	-	33,766
	1,248,278	**366,886**	**881,392**	1,127,521	325,940	801,581

(tabular amounts in thousands of dollars)

5. Externally restricted fund balances

	2004				2003
	Restricted Fund	Plant Fund	Endowment Fund	Total	Total
	$	**$**	**$**	**$**	$ (Restated)
Research	**367,214**	**-**	**76,595**	**443,809**	342,558
Faculties	**7,415**	**-**	**193,514**	**200,929**	188,571
Academic services	**3,882**	**-**	**22,232**	**26,114**	26,350
Support services	**1,387**	**9,420**	**16,510**	**27,317**	33,082
Community services	**15,222**	**-**	**11,768**	**26,990**	23,040
Student services	**20,486**	**-**	**153,758**	**174,244**	162,267
Accumulated income (i)	**-**	**-**	**257,626**	**257,626**	203,437
	415,606	**9,420**	**732,003**	**1,157,029**	979,305

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

6. Internally restricted fund balances

	2004				2003
	Operating Fund	Plant Fund	Endowment Fund	Total	Total
	$	**$**	**$**	**$**	$
Faculties	**8,085**	**-**	**22,427**	**30,512**	29,841
Academic services	**3,062**	**-**	**2,267**	**5,329**	6,817
Support services	**1,572**	**590**	**4**	**2,166**	12,526
Community services	**7,264**	**-**	**958**	**8,222**	6,702
Student services	**3,905**	**-**	**60**	**3,965**	2,575
Ancillary services	**124**	**-**	**-**	**124**	620
	24,012	**590**	**25,716**	**50,318**	59,081

(tabular amounts in thousands of dollars)

7. Interfund transfers

	2004			
	Operating Fund	Restricted Fund	Plant Fund	Endowment fund
	$	**$**	**$**	**$**
Overdistributed income (a)	**1,076**	**8,489**	**-**	**(9,565)**
Net capitalization of income (b)	**(1,882)**	**(5,743)**	**-**	**7,625**
Unrealized gains on endowment investments	**(7,897)**	**(62,302)**	**-**	**70,199**
Other transfers (c)	**2,478**	**526**	**(2,978)**	**(26)**
	(6,225)	**(59,030)**	**(2,978)**	**68,233**

	2003			
	Operating Fund	Restricted Fund	Plant Fund	Endowment fund
	$	**$**	**$**	**$**
Overdistributed income (a)	4,231	29,375	1,693	(35,299)
Net capitalization of income (b)	(2,018)	(4,257)	-	6,275
Unrealized losses on endowment investments	7,684	53,147	3,202	(64,033)
Other transfers (c)	2,469	(2,412)	(57)	-
	12,366	75,853	4,838	(93,057)

(a) Represents the de-investment of accumulated net investment income.

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

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

8. Bank indebtedness

The University has unsecured lines of credit available varying from $105 million to $145 million. As at May 31, 2004, $67 million was drawn on these facilities. The lines of credit bear interest at prime and the average prime rate for the year was 4.37%. The University is able to lower its borrowing costs by “locking in” using bankers’ acceptances for periods ranging up to one year. The amount of indebtedness reported on the balance sheet is net of accounts with cash on hand.

The University manages its cash centrally in the operating fund. Correspondingly, 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)

9. Long-term debt

	2004	2003
	$	$
a) Government of Québec debt, net		
1) MEQ Bonds (i)		
13.25% Series “II” due January 12, 2004	**-**	4,000
5.00% Series “1C” due June 4, 2004	**8,781**	8,781
5.00% Series “1C” due June 4, 2004	**7,900**	7,900
4.90% Series “4C” due June 14, 2004	**3,964**	3,964
5.00% Series “4C” due June 14, 2004	**6,462**	6,462
9.10% Series “1A” due June 30, 2004	**15,325**	15,325
5.15% Series “5C” due July 27, 2004	**8,477**	8,477
6.30% Series “2C” due November 26, 2004	**17,709**	17,709
12.25% Series “JJ” due March 6, 2005	**11,700**	11,700
10% Series “2A” due March 8, 2005	**5,753**	5,753
6.15% Series “3C” due March 28, 2005	**10,377**	10,377
8.85% Series “1B” due September 15, 2005	**3,892**	3,892
3.75% Series “9C” due December 9, 2005	**5,685**	5,685
11% Series “KK” due December 20, 2005	**6,120**	6,120
4.20% Series “6C” due February 14, 2006	**3,360**	3,360
5.75% Series “6B” due February 15, 2006	**2,000**	2,000
4.10% Series “7C” due February 15, 2006	**3,603**	3,603
3.55% Series “10C” due February 27, 2006	**5,885**	5,885
4.40% Series “8C” due February 28, 2006	**4,795**	4,795
8.0% Series “2B” due April 12, 2006	**4,245**	4,245
8.15% Series “2B” due April 12, 2006	**4,356**	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
4.55% Series “10C” due February 27, 2007	**7,973**	7,973
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

(tabular amounts in thousands of dollars)

9. Long-term debt (continued)

	2004	2003
	$	$
1) MEQ Bonds (i) (continued)		
5.10% Series "8C" due February 28, 2008	**11,333**	11,333
5.80% Series "6B" due March 13, 2008	**6,218**	6,218
4.70% Series "9C" due December 9, 2008	**6,910**	6,910
13.25% Series "II" due January 12, 2009	**3,000**	3,000
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
6.20% Series "4C" due June 14, 2011	**13,981**	13,981
5.75% Series "6C" due February 14, 2012	**3,858**	3,858
5.70% Series "7C" due February 14, 2012	**5,358**	5,358
5.75% Series "8C" due February 28, 2012	**5,400**	5,400
5.80% Series "8C" due February 28, 2012	**3,872**	3,872
5.40% Series "9C" due December 9, 2012	**7,405**	7,405
5.30% Series "10C" due February 27, 2013	**10,451**	10,451
	322,850	326,850
2) Financement Québec Notes (ii)		
4.516% due December 1, 2008	**25,691**	-
3.849% due December 1, 2009	**25,309**	-
	51,000	-
Accumulated contributions to sinking fund (iii)	**(48,329)**	(34,478)
Total Government of Québec debt, net	**325,521**	292,372
b) McGill University Senior Debentures (iv),		
6.15% Series "A", due September 22, 2042	**150,000**	150,000
c) Royal Bank loan (v),		
5.81%, due February 2014	**4,266**	-
5.17%, due June 2008	**459**	-
d) Other	**357**	373
Total long-term debt	**480,603**	442,745
Current portion of long-term debt	**(98,125)**	(4,000)
Long-term debt	**382,478**	438,745

(tabular amounts in thousands of dollars)

9. 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 amount of future subsidies totals $401 million ($372 million in 2003).

Capital expenditures of $27 million will be financed by bonds to be issued at future dates as determined by the Government of Québec.

(ii) During the year, the Government of Québec issued new debt through Financement Québec. The treatment of these notes is the same as the MEQ bonds, in that they are secured by the Government of Québec and a sinking fund has been established. The Financement Québec notes were issued in June 2003 and March 2004, respectively, and require semiannual interest payments on June 1 and December 1. Repayment of principal of $1,350,760 and $1,012,360, respectively, are due annually on December 1, with lump-sum payments of $20,287,960 and $21,259,560, respectively, due at maturity.

(iii) 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, the MEQ contributed $13,851,000 to this fund ($14,956,000 in 2003) and applied nil towards repaid bonds ($16,497,000 in 2003).

(iv) In September 2002, McGill University issued $150 million of unsecured debentures. Unlike MEQ bonds, McGill will be required to repay these obligations from resources generated by the University (see Note 15). Semi-annual payments of capital and interest are paid by the University.

(v) The Royal Bank loans are secured by grants receivable from the Ministère des Affaires Municipales, Sports et Loisirs (“MAMSL”) and the Ministère de la Culture et des Communications (MCC), of $4.3 million and $0.5 million, respectively. Semi-annual payments of capital and interest are paid by the University and re-imbursed by both MAMSL and MCC.

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

	$
2006	**46,651**
2007	**52,483**
2008	**59,547**
2009	**38,619**
2010	**30,367**

(tabular amounts in thousands of dollars)

10. Pension plan

Substantially all 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. The University actuarial obligations of $1,016,305,000 under this plan are virtually fully funded by plan assets having a market value of $1,011,023,000 at May 31, 2004, with any shortfall based on the actuarial valuation to be paid by the University.

An actuarial valuation, carried out October 31, 2003 by Eckler Partners Ltd. using the solvency method, confirmed a funding deficit of approximately $10.7 million. The regulatory body requires an annual contribution of $3.3 million (capital and interest) until December 31, 2005 and $1.7 million thereafter until October 31, 2008 in order to fully absorb the deficiency. The total current year contribution of $23 million has been recorded as the pension expense for this fiscal year.

The next such valuation is required by no later than December 31, 2005.

11. Net investment income from endowments

The realized net investment income earned on resources held for endowment is reported in the following funds:

	2004	2003
	$	$
Operating Fund	**3,650**	624
Restricted Fund	**28,795**	4,330
Plant Fund	**-**	250
	32,445	5,204

These amounts are included in the statement of revenue and expenses in the following revenue line items: net investment income, services to the community, and student services net investment income.

The unrealized gains on marketable securities is included in the statement of revenue and expenses as a separate line item. The total unrealized gains on marketable securities of $72,243,000 include $70,199,000 related to resources held for endowment ($65,852,000 and $64,033,000 unrealized losses in 2003, respectively).

12. 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 adverse consequences 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.

Fair values

At May 31, 2004, the carrying values of cash and short-term investments, receivables and accruals, grants and contracts related to research receivable, staff mortgages, bank indebtedness and payables 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.

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 $547,958,000 at May 31, 2004 ($509,913,000 in 2003).

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 15 for details.

(tabular amounts in thousands of dollars)

13. Commitments

Year ending May 31	Minimum lease payments (a)	Special early retirement program (b)
	$	$
2005	**1,202**	**241**
2006	**673**	**241**
2007	**581**	**241**
2008	**407**	**241**
2009	**33**	**205**
Thereafter	**33**	**-**
	2,929	**1,169**

(a) The amounts represent future minimum lease payments under existing operating leases in excess of one year.

(b) This program was offered in the spring of 1996. Amounts remaining to be paid are in respect of annuities to be paid over the lives of certain retirees.

Construction in progress

The University has undertaken the construction of several new buildings, and as a result has commitments totalling $40.5 million. These commitments are expected to be met in the normal course of operations.

14. 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 3, 2004, 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, 2004, 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)

15. 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 9). Details of these items are as follows:

	2004	2003
	$	$
Assets		
Cash and short-term investments (i)	**60,300**	79,555
Marketable securities, at market (ii)	**17,485**	5,056
Due from other funds	**34**	132
Capital assets		
Land	**1,730**	1,730
Buildings	**67,526**	63,707
Equipment	**653**	130
Bond discounts (iii)	**6,391**	6,429
Total assets	**154,119**	156,739
Liabilities		
Interest payable	**1,611**	1,538
Long-term debt	**150,000**	150,000
Total liabilities	**151,611**	151,538
Fund balance		
Invested in capital assets	**10,374**	8,339
Internally restricted (iv)	**(7,866)**	(3,138)
Total fund balance	**2,508**	5,201
Total liabilities and fund balance	**154,119**	156,739

(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 $17.5 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.

15. Supplementary information (continued)

(iii) Includes bond issue costs of $6,667,000, which will be amortized on a straight-line basis over the 40 year lives of the bonds. The annual amortization is approximately $166,000.

(iv) 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.

16. Comparative amounts

Certain comparative amounts for the year ended May 31, 2003 have been reclassified in order to conform to the presentation adopted in the current year.