

Financial statements of

**THE ROYAL INSTITUTION FOR THE
ADVANCEMENT OF LEARNING /
McGILL UNIVERSITY**

(see Note 1)

May 31, 2008

**THE ROYAL INSTITUTION FOR THE
ADVANCEMENT OF LEARNING /
McGILL UNIVERSITY**
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Auditors' report

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

We have audited the balance sheet of the Royal Institution for the Advancement of Learning / McGill University (the "University") as at May 31, 2008 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 the accounting for accrued vacation pay, employee future benefits, capital assets, long-term grants receivable, bond discounts, and the presentation of the bond sinking fund in the long-term debt. Note 2 describes how the Cahier's recommendations, as applied by the University, 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 Royal Institution for the Advancement of Learning / McGill University as at May 31, 2008, and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

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

Chartered Accountants

August 8, 2008

**THE ROYAL INSTITUTION FOR THE
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**Balance sheet
as at May 31, 2008
(in thousands of dollars)**

	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund	Total	
					2008	2007
	\$	\$	\$	\$	\$	(Restated Note 15)
Assets						
Current assets						
Short-term investments	25,020	5,106	4,056	37,022	71,204	120,549
Receivables						
Operating	18,950	119	4,013	305	23,387	22,625
Student loans	-	3,643	-	-	3,643	3,500
Investment income	-	5	-	2,632	2,637	3,042
Government grants	50,727	-	544	-	51,271	67,266
Grants and contracts related to research	-	165,789	-	-	165,789	148,907
Pledges	325	26,866	-	-	27,191	18,815
Prepaid expenses and other assets	7,375	267	-	-	7,642	4,912
Inventory	2,230	-	-	-	2,230	1,958
Due from (to) other funds	(41,787)	129,612	(94,972)	7,147	-	-
	62,840	331,407	(86,359)	47,106	354,994	391,574
Marketable securities, at market value	-	1,321	29,999	854,188	885,508	906,440
Grants and contracts related to research receivable - long-term	-	97,400	-	-	97,400	107,892
Pledges receivable - long-term	453	65,675	-	-	66,128	35,928
Grant receivable	-	70	3,548	-	3,618	4,279
Capital assets (Note 3)	-	-	1,100,761	-	1,100,761	1,047,155
Other assets	-	-	6,349	-	6,349	6,854
Staff mortgages	-	-	-	1,153	1,153	1,422
Total assets	63,293	495,873	1,054,298	902,447	2,515,911	2,501,544
Liabilities						
Current liabilities						
Bank indebtedness (Note 7)	79,911	-	-	-	79,911	122,458
Accounts payable and accrued liabilities	25,653	10,369	18,035	644	54,701	57,430
Unearned revenue	16,553	-	-	-	16,553	16,649
Provisions for specific purposes	1,270	-	-	-	1,270	1,043
Current portion of long-term debt (Note 8)	-	67	64,020	-	64,087	56,706
	123,387	10,436	82,055	644	216,522	254,286
Long-term debt (Note 8)	-	-	524,014	-	524,014	519,989
	123,387	10,436	606,069	644	740,536	774,275
Commitments and contingent liabilities (Notes 12 and 13)						
Fund balances						
Invested in capital assets	-	-	449,246	-	449,246	404,601
Externally restricted (Note 4)	-	485,437	7,569	871,494	1,364,500	1,343,262
Internally restricted (Note 5)	47,934	-	(8,586)	30,309	69,657	71,918
Unrestricted	(108,028)	-	-	-	(108,028)	(92,512)
	(60,094)	485,437	448,229	901,803	1,775,375	1,727,269
Total liabilities and fund balances	63,293	495,873	1,054,298	902,447	2,515,911	2,501,544

Approved by the Board of Governors

..... Governor

..... Governor

**THE ROYAL INSTITUTION FOR THE
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**Statement of revenue and expenses and changes in fund balances
year ended May 31, 2008
(in thousands of dollars)**

	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund	Total	
					2008	2007
	\$	\$	\$	\$	\$	\$
Revenue						
Government sources						
Canada	19,158	194,687	-	-	213,845	179,004
Quebec	277,928	52,628	40,912	-	371,468	350,359
United States	-	5,692	-	-	5,692	6,668
Grants - other sources	-	25,917	-	-	25,917	20,936
Contracts	-	13,517	-	-	13,517	13,056
Tuition and fees	159,816	518	-	-	160,334	150,651
Sale of goods and services	83,031	6,587	263	-	89,881	97,963
Gifts and bequests	4,040	62,202	6,737	32,734	105,713	85,815
Short-term interest	6,688	839	6,525	-	14,052	14,969
Investment income (Note 10)	11,741	61,901	-	-	73,642	61,315
Total revenue	562,402	424,488	54,437	32,734	1,074,061	980,736
Expenses						
Salaries						
Academic	182,732	58,737	-	-	241,469	229,567
Administrative and support	157,701	22,532	-	-	180,233	172,861
Student	11,213	49,008	-	-	60,221	61,347
Student aid	7,210	24,292	-	-	31,502	24,500
Benefits	64,413	17,311	-	-	81,724	79,089
Total salaries	423,269	171,880	-	-	595,149	567,364
Non-salary						
Material, supplies and publications	22,436	25,871	-	-	48,307	46,435
Transfers to partner institutions	1,047	28,232	-	-	29,279	25,696
Contract services	8,326	8,575	-	-	16,901	16,691
Professional fees	13,116	5,622	-	7,249	25,987	23,467
Travel	7,996	12,798	-	-	20,794	20,430
Cost of goods sold and services rendered	21,489	-	-	-	21,489	24,525
Building occupancy costs	17,377	3,541	-	-	20,918	18,760
Tuition	789	711	-	-	1,500	1,926
Energy	16,470	1,095	-	-	17,565	18,210
Other non-salary expenses	12,452	26,974	-	-	39,426	33,815
Capital purchases	20,169	75,281	1,517	-	96,967	66,841
Amortization	-	-	73,501	-	73,501	73,601
Interest and bank charges	10,437	42	31,842	-	42,321	42,247
Total non-salary	152,104	188,742	106,860	7,249	454,955	412,644
Total expenses	575,373	360,622	106,860	7,249	1,050,104	980,008
Excess (deficiency) of revenue over expenses before the undernoted item	(12,971)	63,866	(52,423)	25,485	23,957	728
Unrealized gains (losses) on marketable securities (Note 10)	(6,468)	(59,369)	(108)	-	(65,945)	63,752
Excess (deficiency) of revenue over expenses	(19,439)	4,497	(52,531)	25,485	(41,988)	64,480
Fund balances (deficit), beginning of year	(43,841)	450,053	407,624	913,433	1,727,269	1,600,173
Interfund transfers (Note 6)	3,186	30,887	3,042	(37,115)	-	-
Capital expenditures financed by other funds	-	-	90,094	-	90,094	62,616
Fund balances (deficit), end of year	(60,094)	485,437	448,229	901,803	1,775,375	1,727,269

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**Statement of revenue and expenses and changes in fund balances (continued)
year ended May 31, 2007
(in thousands of dollars)**

	2007				
	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund	All Funds
	\$	\$	\$	\$	\$
	(Restated Note 15)				(Restated Note 15)
Revenue					
Government sources					
Canada	18,271	160,733	-	-	179,004
Quebec	277,163	31,676	41,520	-	350,359
United States	-	6,668	-	-	6,668
Grants - other sources	-	20,936	-	-	20,936
Contracts	-	13,056	-	-	13,056
Tuition and fees	149,832	819	-	-	150,651
Sale of goods and services	82,667	15,065	231	-	97,963
Gifts and bequests	5,422	39,028	4,692	36,673	85,815
Short-term interest	7,980	914	6,075	-	14,969
Investment income (Note 10)	10,943	50,372	-	-	61,315
Total revenue	552,278	339,267	52,518	36,673	980,736
Expenses					
Salaries					
Academic	173,570	55,997	-	-	229,567
Administrative and support	148,307	24,554	-	-	172,861
Student	9,957	51,390	-	-	61,347
Student aid	4,248	20,252	-	-	24,500
Benefits	62,070	17,019	-	-	79,089
Total salaries	398,152	169,212	-	-	567,364
Non-salary					
Material, supplies and publications	22,205	24,230	-	-	46,435
Transfers to partner institutions	935	24,761	-	-	25,696
Contract services	6,624	10,067	-	-	16,691
Professional fees	12,346	4,240	-	6,881	23,467
Travel	8,115	12,315	-	-	20,430
Cost of goods sold and services rendered	24,525	-	-	-	24,525
Building occupancy costs	15,421	3,339	-	-	18,760
Tuition	909	1,017	-	-	1,926
Energy	17,477	733	-	-	18,210
Other non-salary expenses	8,730	25,085	-	-	33,815
Capital purchases	25,055	39,409	2,377	-	66,841
Amortization	-	-	73,601	-	73,601
Interest and bank charges	12,218	313	29,716	-	42,247
Total non-salary	154,560	145,509	105,694	6,881	412,644
Total expenses	552,712	314,721	105,694	6,881	980,008
Excess (deficiency) of revenue over expenses before the undernoted item	(434)	24,546	(53,176)	29,792	728
Unrealized gain on marketable securities (Note 10)	7,426	53,268	3,058	-	63,752
Excess (deficiency) of revenue over expenses	6,992	77,814	(50,118)	29,792	64,480
Fund balances (deficit), beginning of year	(35,232)	438,506	395,069	801,830	1,600,173
Interfund transfers (Note 6)	(15,601)	(66,267)	57	81,811	-
Capital expenditures financed by other funds	-	-	62,616	-	62,616
Fund balances (deficit), end of year	(43,841)	450,053	407,624	913,433	1,727,269

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Statement of cash flows
year ended May 31, 2008
(in thousands of dollars)

	2008	2007
	\$	\$ (Restated Note 15)
Operating activities		
(Deficiency) excess of revenue over expenses*	(67,473)	34,688
Adjustments for:		
Amortization	73,501	73,601
Gain on sale of marketable securities	(31,099)	(33,792)
Unrealized losses (gains) on marketable securities	65,945	(63,752)
Net change in non-cash working capital items	9,895	(20,704)
(Increase) decrease in grants and contracts related to research receivable	(5,729)	50,157
Increase in pledges receivable	(38,576)	(19,170)
	6,464	21,028
Investing activities		
Acquisition of capital assets and other assets	(126,602)	(144,221)
Acquisition of marketable securities, net	(13,914)	(22,170)
Proceeds from staff mortgages	269	434
Additions to staff mortgages	-	(346)
	(140,247)	(166,303)
Financing activities		
Net change in Endowment Fund balance	25,485	29,792
Decrease (increase) in contribution to sinking fund	8,676	(833)
Issuance of long-term debt	75,000	110,000
Repayment of long-term debt	(72,270)	(50,934)
Capital expenditures financed by other funds	90,094	62,616
	126,985	150,641
Net (decrease) increase in cash position	(6,798)	5,366
Cash position, beginning of year	(1,909)	(7,275)
Cash position, end of year	(8,707)	(1,909)
Cash position comprises:		
Short-term investments		
- Operating Fund	25,020	47,457
- Restricted Fund**	5,106	3,399
- Plant Fund	4,056	40,613
- Endowment Fund**	37,022	29,080
Bank indebtedness	(79,911)	(122,458)
	(8,707)	(1,909)

* Endowment Fund results are included in financing activities.

** These assets are subject to external restriction.

THE ROYAL INSTITUTION FOR THE ADVANCEMENT OF LEARNING / McGILL UNIVERSITY

Notes to the financial statements

year ended May 31, 2008

(tabular amounts in thousands of dollars)

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”). McGill’s operations include all of the activities of its teaching and research units, such as the Montreal Neurological Institute, Macdonald Campus in Ste-Anne de Bellevue and the Morgan Arboretum.

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*.

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 \$90.1 million (\$62.6 million in 2007), 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 \$32.3 million (\$28.6 million in 2007), resulting in a decrease of \$3.7 million in the excess of revenue over expenses for the year (\$1.1 million in 2007).
- 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 \$33.5 million (\$42.2 million in 2007) be presented as a reduction of long-term debt.
- 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.

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Notes to the financial statements

year ended May 31, 2008

(tabular amounts in thousands of dollars)

2. Significant accounting policies (continued)

- MELS requires that long-term government grants receivable not be discounted to a present value, as the assumption is that the “market” rate of interest for such receivables is 0%. Were these receivables discounted using the bank rate in effect at May 31, 2008, they would have been discounted by \$6.1 million (\$6.4 million in 2007), resulting in an increase of \$321,000 in the excess of revenues over expenses in the restricted fund (excess of \$1.6 million in 2007).
- MELS requires bond discounts to be amortized on a straight-line basis and presented as other assets as opposed to reduction of debt. The difference between the straight-line and effective interest rate method is not significant.

Had the above items been accounted for in accordance with Canadian GAAP as at May 31, 2008, the total excess (deficiency) of revenue over expenses would have increased by \$86.7 million to an excess of revenue of \$44.9 million (\$63.1 million and \$127.5 million, respectively in 2007). 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 providers 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 the donors. The net investment income is comprised of both the 5% investment income distribution, as well as any undistributed investment income attributable to the various 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, fair values of private equity investments, estimated useful lives of capital assets and provisions for contingencies.

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**Notes to the financial statements
year ended May 31, 2008
(tabular amounts in thousands of dollars)**

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. Contributions are recognized 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 five years.

Investment income earned on Restricted 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 revenue and expenses.

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

Government of Québec operating grants are recorded in the financial year for which they are granted.

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.

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**Notes to the financial statements
year ended May 31, 2008
(tabular amounts in thousands of dollars)**

2. Significant accounting policies (continued)

Other significant accounting policies (continued)

Financial instruments

Financial instruments are initially recorded at fair value (except for GAAP differences previously described) and their subsequent measurement is dependent on their classification. McGill classifies all financial instruments per the guideline of CICA Section 3855 *Recognition and Measurement*, as either held-for-trading, available for sale, held-to-maturity, loans and receivables or other financial liabilities. Financial instruments classified as held-for-trading are measured at fair value with unrealized gains and losses recognized in operating results. Financial instruments classified as available for sale are measured at fair value, with unrealized gains and losses recognized in changes in fund balances. Financial instruments classified as held-to-maturity, loans and receivables or other financial liabilities are measured at amortized cost.

Marketable securities, short-term investments and bank indebtedness

Marketable securities, short-term investments and bank indebtedness are classified as held for trading and are recorded at fair value. Fair value for publicly traded securities is based on quoted market values using bid prices. The fair value of infrequently traded securities, including private equity investments, is determined based on quoted market yields, or on prices of recent transactions in the applicable securities, as appropriate. Changes in fair value in the period are recorded in the statement of revenue and expenses under the caption "Unrealized gains (losses) on marketable securities".

Realized gains and losses representing sale price less original cost are presented as part of net investment income.

Investment-related transactions are recognized at the date of the transaction.

Receivables

Accounts receivable, student loans, accrued investment income, pledges receivable and staff mortgages are classified as loans and receivables and are measured at amortized cost.

Grants receivable

Grants receivable are recorded at their notional value and are classified as loans and receivables and are mostly receivable within three years.

Accounts payable and accrued liabilities and long-term debt

Accounts payable and accrued liabilities and long-term debt are classified as other financial liabilities, which are measured at amortized cost.

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Notes to the financial statements
year ended May 31, 2008
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2. Significant accounting policies (continued)

Other significant accounting policies (continued)

Derivative financial instruments

Derivative financial instruments are used as a substitute for more traditional investments. McGill holds derivative financial instruments related to the marketable securities purchased to eventually redeem the \$150 million of McGill Senior Debentures (see Note 14 for details). Derivative financial instruments are recorded at their fair values and changes in the fair value are recorded as other investment income.

Student loans

Student loans are due within one year after graduation and do not bear interest up until that time. After their due date, interest is charged based on the prevailing rates when the loan agreements were signed. 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 do not normally include interest capitalized during construction. 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 by 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.

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
Library materials	Straight-line	40 years
Intangible assets*	Straight-line	5 years

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

Other assets

Other assets comprise bond discounts and are amortized on a straight-line basis over the term of the bond.

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**Notes to the financial statements
year ended May 31, 2008
(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.

Accounting policy changes

Accounting changes

Effective June 1, 2007, the University adopted CICA Handbook Section 1506, *Accounting Changes*, which establishes criteria for changing accounting policies. The section requires changes in accounting policy and corrections of prior period errors to be accounted for and applied retroactively as well as additional enhanced disclosure information about such changes. In addition, voluntary changes in accounting policy can be made only when the change results in a more relevant and reliable presentation of the financial statements.

This standard did not affect the University's financial position or results of operations.

Future accounting policy changes

Financial instruments

On December 1, 2006, the CICA issued two new accounting standards, Section 3862, *Financial Instruments - Disclosures*, and Section 3863, *Financial Instruments - Presentation*. These new standards will be effective for fiscal years beginning on or after October 1, 2007. Sections 3862 and 3863 will replace Section 3861 - *Financial Instruments - Disclosure and Presentation*, revising and enhancing its disclosure requirements. Section 3862 places increased emphasis on the disclosure of information, namely on: a) the significance of financial instruments for the entity's financial position and performance and b) the nature and extent of risks arising and how the entity manages those risks. Section 3863 on the presentation of financial instruments is unchanged from the presentation requirements included in Section 3861.

The University is in the process of evaluating the impact of the disclosure and presentation requirements of the new standards.

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Notes to the financial statements

year ended May 31, 2008

(tabular amounts in thousands of dollars)

3. Capital assets

	2008			2007		
	Cost	Accumulated amortization	Net book value	Cost	Accumulated amortization	Net book value
	\$	\$	\$	\$	\$	\$
Land	8,110	-	8,110	8,110	-	8,110
Land improvements	3,774	1,584	2,190	3,529	1,395	2,134
Buildings	979,044	245,336	733,708	874,958	230,362	644,596
Leasehold improvements	812	578	234	763	431	332
Equipment	352,057	192,811	159,246	344,739	184,657	160,082
Library materials	219,082	48,156	170,926	205,390	42,679	162,711
Intangible assets	23,306	19,110	4,196	21,803	16,785	5,018
	1,586,185	507,575	1,078,610	1,459,292	476,309	982,983
Assets under development	22,151	-	22,151	64,172	-	64,172
	1,608,336	507,575	1,100,761	1,523,464	476,309	1,047,155

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4. Externally restricted fund balances

	2008			
	Restricted	Plant	Endowment	Total
	Fund	Fund	Fund	Fund
	\$	\$	\$	\$
Research	358,504	-	99,610	458,114
Faculties	18,016	-	252,741	270,757
Academic services	7,920	-	21,798	29,718
Support services	4,238	7,569	13,967	25,774
Community services	65,029	-	7,625	72,654
Student services	31,730	-	215,035	246,765
Accumulated income (i)	-	-	260,718	260,718
	485,437	7,569	871,494	1,364,500

	2007			
	Restricted	Plant	Endowment	Total
	Fund	Fund	Fund	Fund
	\$	\$	\$	\$
Research	370,781	-	96,473	467,254
Faculties	9,535	-	238,002	247,537
Academic services	3,708	-	21,321	25,029
Support services	7,419	8,506	14,817	30,742
Community services	38,109	-	10,767	48,876
Student services	20,501	-	195,347	215,848
Accumulated income (i)	-	-	307,976	307,976
	450,053	8,506	884,703	1,343,262

- (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.

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5. Internally restricted fund balances

	2008			
	Operating Fund	Plant Fund	Endowment Fund	Total
	\$	\$	\$	\$
Faculties	28,642	-	23,300	51,942
Academic services	10,981	-	2,306	13,287
Support services	3,835	(8,586)	4,635	(116)
Student services	4,476	-	68	4,544
	47,934	(8,586)	30,309	69,657

	2007			
	Operating Fund	Plant Fund	Endowment Fund	Total
	\$	\$	\$	\$
Faculties	26,445	-	23,288	49,733
Academic services	11,784	-	2,306	14,090
Support services	4,368	(5,483)	3,070	1,955
Student services	6,074	-	66	6,140
	48,671	(5,483)	28,730	71,918

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6. Interfund transfers

	2008			
	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund
	\$	\$	\$	\$
Underdistributed income transferred (a)	(2,230)	(20,146)	-	22,376
Unrealized (gains) losses on endowment investments transferred	6,468	59,168	-	(65,636)
Net capitalization of income (b)	(244)	(8,563)	-	8,807
Other transfers (c)	(808)	428	3,042	(2,662)
	3,186	30,887	3,042	(37,115)

	2007			
	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund
	\$	\$	\$	\$
Underdistributed income transferred (a)	(1,750)	(12,060)	-	13,810
Unrealized gains on endowment investments transferred	(7,426)	(52,112)	-	59,538
Net capitalization of income (b)	(201)	(8,148)	-	8,349
Other transfers (c)	(6,224)	6,053	57	114
	(15,601)	(66,267)	57	81,811

- (a) Realized investment income does not normally equal the amount determined by McGill's annual income distribution policy of 5%. Accordingly, the difference between the two is represented as either under or overdistributed income.
- (b) Represents the re-investment (i.e. capitalization) of unspent annual income distribution.
- (c) Other transfers include transfers of internally restricted funds and authorized transfers of externally restricted funds.

7. Bank indebtedness

McGill's Board of Governors has approved maximum borrowings under short-term credit facilities of \$250 million. A maximum of \$345 million is available through unsecured lines of credit, normally drawn through bankers' acceptances for periods of up to one year. The lines of credit bear interest at the prime rate, which averaged 4.37% for the year. Bankers' acceptances outstanding at year end bear interest at rates ranging from 3.18% to 3.29%.

McGill 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.

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8. Long-term debt

	2008	2007
	\$	\$
a)		
1) Bonds (i)		
11.50% Series "1" due January 29, 2008	-	4,525
5.00% Series "6C" due February 14, 2008	-	12,782
4.95% Series "7C" due February 15, 2008	-	6,039
5.05% Series "8C" due February 28, 2008	-	15,900
5.10% Series "8C" due February 28, 2008	-	11,333
5.80% Series "6B" due March 13, 2008	-	6,218
3.15% Series "11C" due May 27, 2008	-	6,726
	-	63,523
3.55% Series "12C" due November 24, 2008	9,395	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	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
	40,788	40,788
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	10,000
	18,675	18,675
6.20% Series "4C" due June 14, 2011	13,981	13,981
4.00% Series "12C" due November 24, 2011	5,605	5,605
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	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
	55,482	55,482
5.40% Series "9C" due September 12, 2012	7,405	7,405
5.30% Series "10C" due February 27, 2013	10,451	10,451
	17,856	17,856
4.50% Series "11C" due May 27, 2015	4,703	4,703
	4,653	4,653
4.40% Series "13C" due February 24, 2016	7,000	7,000
4.50% Series "14C" due March 8, 2016	11,653	11,653
	149,157	212,680
Total Bonds:	149,157	212,680

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8. Long-term debt (continued)

	<u>2008</u>	<u>2007</u>
	\$	\$
a)		
2) Notes (ii)		
4.516% due December 1, 2008	20,288	21,639
3.849% due December 1, 2009	22,272	23,284
4.059% due December 1, 2010	27,222	28,611
4.167% due December 1, 2010	4,600	4,800
4.288% due December 1, 2011	22,676	23,838
4.814% due April 25, 2012	18,400	19,200
4.9515% due November 1, 2012	37,129	39,753
4.355% due September 16, 2013	90,000	90,000
4.607% due September 16, 2013	35,000	-
3.839% due December 1, 2014	40,000	-
4.267% due December 1, 2015 (iii)	1,251	1,379
	Total Notes:	252,504
	467,995	465,184
	Accumulated contributions to sinking fund (iv)	(42,217)
	434,454	422,967
	Total Government of Québec debt, net	
b) McGill Senior Debentures (v),		
6.15% Series "A", due September 22, 2042	150,000	150,000
c) Royal Bank loans (vi),		
5.81%, due March 19, 2014	2,841	3,228
5.17%, due June 2008	67	187
d) Other	739	313
Total long-term debt	588,101	576,695
Current portion of long-term debt (vii)	(64,087)	(56,706)
Long-term debt	524,014	519,989

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8. Long-term debt (continued)

- (i) These bonds are 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.

McGill has also made capital expenditures of \$63 million (\$54 million in 2007), 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) These 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	18,937
3.849% due December 1, 2009	1,012	21,260
4.059% due December 1, 2010	1,389	24,444
4.167% due December 1, 2010	200	4,200
4.288% due December 1, 2011	1,162	19,190
4.9515% due November 1, 2012	2,624	26,633
4.814% due April 25, 2012	800	16,000
4.355% due September 16, 2013	4,337	68,315
4.607% due September 16, 2013	1,400	28,000
3.839% due December 1, 2014	2,440	27,800

- (iii) These notes are secured by a grant receivable from the Ministère du Développement économique de l'innovation et de l'Exportation (MDEIE) of \$1.2 million. Semi-annual payments of capital and interest are paid by MDEIE, on the McGill'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 \$10 million to this fund (\$11.8 million in 2007) and applied \$18.7 million towards repaid bonds (\$11 million in 2007).
- (v) In September 2002, McGill issued \$150 million of unsecured debentures. Unlike MELS bonds, McGill will be required to repay these obligations from resources generated by McGill (see Note 14). Semi-annual interest payments are paid by McGill.
- (vi) The Royal Bank loans are secured by grants receivable from the Ministère des Affaires municipales et des Régions ("MAMR") and the Ministère de la Culture et des Communications ("MCC"), of \$2.8 million and \$0.1 million, respectively. Semi-annual payments of capital and interest are paid by McGill and reimbursed by both MAMR and MCC.

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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:

	\$
2009	64,087
2010	50,633
2011	42,124
2012	90,237
2013	48,720

9. Employee future benefits

Pension plans

The majority of McGill'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. Upon an employee's retirement, 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. If an employee elects an annuity provided by McGill, the accumulated amount of the employee's holdings in the Accumulation Fund is transferred to the Plan's Pensioner Fund where it is available to fund annuity payments made by the Plan. Under certain circumstances, employees in the accumulation fund are also eligible for an enhancement to their accumulated amount. For the McGill pensions subject to defined benefits, the actuarial obligations on a going concern basis of \$1.3 billion at December 31, 2006 under this plan are less than plan assets having a market value of \$1.3 billion at December 31, 2006. Any going concern shortfall based on the actuarial valuation will be paid by McGill.

An actuarial valuation, carried out December 31, 2006 by Eckler Ltd. using the solvency method, confirmed a solvency funding deficit of approximately \$11.1 million. However, effective December 31, 2006, the Government of Quebec's regulatory body eliminated the requirement for universities to fund solvency deficits. The amortization of the solvency deficit for the period of June 1, 2006 to December 31, 2006 totaled \$1.4 million. The total current year contribution of \$26.2 million has been recorded as the pension expense for this fiscal year (\$25.8 million in 2007).

Other plans and arrangements

McGill 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, 2008 is estimated at \$2.5 million (\$2.5 million in 2007).

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10. Net investment income from endowments

a) Investment income

Realized net investment income is included in the statement of revenue and expenses and changes in fund balance in the investment income revenue line. Total income of \$73.6 million (\$61.3 million in 2007) was generated in 2008.

Included in the above total is realized net investment income earned on resources held for endowment which amounted to \$66.4 million (\$54.5 million in 2007) and were reported in the following funds:

	2008	2007
	\$	\$
Operating Fund ⁽ⁱ⁾	4,492	4,090
Restricted Fund	61,901	50,372
	66,393	54,462

⁽¹⁾ The total investment income reported in the operating fund includes a \$7.2 million (\$6.9 million in 2007) contribution from the Endowment Fund.

b) Unrealized loss on marketable securities

In addition, the total unrealized loss on marketable securities related to resources held for endowment amounted to \$65.8 million (\$60.7 million of unrealized gain in 2007). This was augmented by an unrealized loss of \$0.1 million (\$3.1 million unrealized gain in 2007) relating to investments purchased in the Plant Fund using the proceeds of the Debenture issue (see Note 14). Consequently, the total net unrealized loss for the year was \$65.9 million (\$63.8 million unrealized gain in 2007).

11. Financial instruments

Financial risks

McGill 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 McGill's diversification of its investment portfolio.

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11. Financial instruments (continued)

Financial risks (continued)

The University has foreign currency risk arising from its foreign denominated cash accounts, and its holdings of foreign equities and bonds. As at May 31, 2008, McGill's foreign denominated cash and marketable securities had a market value of \$440 million.

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

McGill is exposed to credit risk from its debtors. A significant portion of McGill'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 McGill's large and diverse base of counter-parties and investments.

Fair values

At May 31, 2008, the carrying values of cash and short-term investments, receivables, bank indebtedness and accounts payable and accrued liabilities approximate their fair values.

Marketable securities are presented at fair value. Note 2 discloses the difference between the fair value and the carrying value of long-term grants receivable.

Staff mortgages are issued at rates and terms comparable to commercial home mortgages. Their 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 McGill for debt with similar terms and maturities, is \$654.4 million at May 31, 2008 (\$645.4 million in 2007).

McGill has forward contracts outstanding as at May 31, 2008 to sell US\$260 million with an average forward rate of 1.00765 maturing on July 24, 2008. As at May 31, 2008, the unrealized gain on these contracts approximated \$3.4 million. McGill has a natural gas forward contract with an unrealized gain of \$1.7 million.

The US Dollar denominated investment outstanding, as described in Note 14 (ii), will result (at maturity) in the forfeiture of the interest receivable, in exchange for a fixed amount of proceeds. As at May 31, 2008, the fair value of the swap is \$13.5 million (\$10.8 million in 2007).

As at May 31, 2008, McGill held securities classified as non-bank asset-backed commercial paper in the Plant Fund and the Restricted Fund. These securities were carried as short-term investments and had a market value of \$4.0 million and \$2.2 million, respectively. As a result of changes to the market conditions for this type of security, the net realizable value of these securities may materially differ from their carrying value.

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11. Financial instruments (continued)

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

	2008		2007	
	Endowment	Restricted	Endowment	Restricted
	Fund	Fund	Fund	Fund
	%	%	%	%
Canadian Equity	22	13	24	10
US Equity	29	8	29	2
Non North American Equity	19	-	19	-
Canadian Fixed Income	29	79	27	88
US Fixed Income	1	-	1	-
	100	100	100	100

12. Commitments

Year ending	Minimum lease
May 31	payments
	\$
2009	1,805
2010	1,272
2011	973
2012	989
2013	1,005
Thereafter	3,801
	9,845

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

Construction in progress

McGill has undertaken the construction of several new buildings, and as a result has commitments totalling \$22.5 million. 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 \$50.1 million in accordance with its arrangements with these funds.

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13. Contingent liabilities

Litigation

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, 2008, 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 will be provided for in the provision for specific purposes.

In the normal course of McGill's building construction projects, various claims secured by construction hypothecs have been made by building contractors to secure payments. Such hypothecs are related to the buildings constructed or under construction.

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 Senior Debentures (Note 8). Details of these items are as follows:

	<u>2008</u>	<u>2007</u>
	\$	\$
Assets		
Cash and short-term investments (i)	4,056	40,613
Marketable securities, at market (ii)	29,995	28,195
Due from other funds (iii)	32,586	3,372
Capital assets		
Land	1,730	1,730
Buildings	77,352	73,998
Equipment	1,240	1,233
Bond discounts (iv)	5,725	5,891
Total assets	152,684	155,032

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14. Supplementary information (continued)

	<u>2008</u>	<u>2007</u>
	\$	\$
Liabilities		
Interest payable	1,666	1,837
Long-term debt	150,360	150,000
Total liabilities	152,026	151,837
Fund balance		
Invested in capital assets	16,790	15,472
Internally restricted (v)	(16,132)	(12,277)
Total fund balance	658	3,195
Total liabilities and fund balance	152,684	155,032

- (i) Represents cash, bankers' acceptances, and treasury bills held for the purpose of future investment in revenue-generating properties.
- (ii) In October 2003, McGill 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 \$30 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 Senior Debentures.
- (iii) The amounts relate to inter-fund transactions conducted in the normal course of business. Cash settlement is expected in June 2008, which will effectively decrease the overall unspent cash balance relating to the McGill Senior Debentures.
- (iv) Original bond issue costs amounted to \$6.7 million, and are being amortized on a straight-line basis over the 40-year term of the bonds. The annual amortization is approximately \$166,000.
- (v) The fund balance 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.

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14. Supplementary information (continued)

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

	<u>2008</u>	<u>2007</u>
	\$	\$
Revenue		
Net short-term interest income	5,656	4,947
Total revenue	5,656	4,947
Expenses		
Amortization	2,119	2,184
Interest on long-term debt	9,230	9,230
Total expenses	11,349	11,414
Deficiency of revenue over expenses	(5,693)	(6,467)
Capital costs recovered from other funds	2,845	2,422
Unrealized gains on marketable securities	1,801	3,059
Interfund transfers	420	543
Total decrease in fund balance	(627)	(443)

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15. Restatement of comparative year

Historically, the Government of Québec grants have been based on second prior year student enrolment information. The Cahier requires that universities calculate and accrue the estimated grant difference based on actual enrolment figures. McGill did not record this accrual in the past. The 2007 financial statements have been restated to reflect these accruals, which are approximately equal to current year Government of Québec operating grants which now include estimates of current student enrolment information. The effect of this change is to increase the opening operating fund balance in fiscal 2007 by \$6.1 million, operating revenues by \$8.0 million and the government grant receivable of the 2007 financial statements by \$14.1 million.

	<u>As previously reported</u> \$	<u>Adjustment</u> \$	<u>As restated</u> \$
Opening fund balance	(41,375)	6,143	(35,232)
Excess of revenue over expenses	(990)	7,982	6,992
Interfund transfers	(15,601)	-	(15,601)
Fund balance, end of year	(57,966)	14,125	(43,841)

16. Comparative figures

Certain comparative figures for the year ended May 31, 2007 have been reclassified in order to conform to the presentation adopted in the current year.