Financial statements of

THE ROYAL INSTITUTION FOR THE ADVANCEMENT OF LEARNING / McGILL UNIVERSITY

(see Note 1)

May 31, 2009

THE ROYAL INSTITUTION FOR THE ADVANCEMENT OF LEARNING / McGILL UNIVERSITY

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Deloitte.

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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, 2009 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, 2009, 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.[1]

August 28, 2009

[1] Chartered accountant auditor permit no 22220

THE ROYAL INSTITUTION FOR THE ADVANCEMENT OF LEARNING / McGILL UNIVERSITY

Balance sheet

as at May 31, 2009
(in thousands of dollars)

	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund	Total 2009	Total 2008
	$	$	$	$	$	$
Assets						
Current assets						
Short-term investments	**49,688**	**-**	**-**	**64,302**	**113,990**	71,204
Receivables						
Operating	**19,510**	**69**	**3,813**	**343**	**23,735**	23,387
Student loans	**-**	**3,374**	**-**	**-**	**3,374**	3,643
Investment income	**-**	**8**	**-**	**2,773**	**2,781**	2,637
Government grants	**43,079**	**-**	**739**	**-**	**43,818**	51,271
Grants and contracts related to research	**-**	**152,279**	**-**	**-**	**152,279**	165,789
Pledges	**407**	**27,618**	**-**	**-**	**28,025**	27,191
Prepaid expenses and other assets	**5,750**	**158**	**-**	**-**	**5,908**	7,642
Inventory	**2,171**	**-**	**-**	**-**	**2,171**	2,230
Due from (to) other funds	**16,973**	**119,782**	**(137,649)**	**894**	**-**	-
	137,578	**303,288**	**(133,097)**	**68,312**	**376,081**	354,994
Marketable securities, at market value	**-**	**2,565**	**35,889**	**694,372**	**732,826**	885,508
Grants and contracts related to research receivable - long-term	**-**	**101,273**	**-**	**-**	**101,273**	97,400
Pledges receivable - long-term	**277**	**79,536**	**-**	**-**	**79,813**	66,128
Grants receivable	**6,627**	**-**	**3,236**	**-**	**9,863**	3,618
Capital assets (Note 3)	**-**	**-**	**1,186,633**	**-**	**1,186,633**	1,100,761
Other assets	**-**	**-**	**5,968**	**-**	**5,968**	6,349
Staff mortgages	**-**	**-**	**-**	**1,029**	**1,029**	1,153
Total assets	**144,482**	**486,662**	**1,098,629**	**763,713**	**2,493,486**	2,515,911
Liabilities						
Current liabilities						
Bank indebtedness (Note 7)	**165,682**	**-**	**-**	**-**	**165,682**	79,911
Accounts payable and accrued liabilities	**30,448**	**9,235**	**26,802**	**349**	**66,834**	54,701
Unearned revenue	**18,346**	**65**	**-**	**-**	**18,411**	16,553
Provisions for specific purposes	**1,535**	**-**	**-**	**-**	**1,535**	1,270
Current portion of long-term debt (Note 8)	**-**	**-**	**53,377**	**-**	**53,377**	64,087
	216,011	**9,300**	**80,179**	**349**	**305,839**	216,522
Long-term debt (Note 8)	**-**	**-**	**547,606**	**-**	**547,606**	524,014
	216,011	**9,300**	**627,785**	**349**	**853,445**	740,536

Commitments and contingent liabilities (Notes 12 and 13)

	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund	Total 2009	Total 2008
Fund balances						
Invested in capital assets	**-**	**-**	**475,135**	**-**	**475,135**	449,246
Externally restricted (Note 4)	**-**	**477,362**	**7,452**	**732,911**	**1,217,725**	1,364,500
Internally restricted (Note 5)	**39,712**	**-**	**(11,743)**	**30,453**	**58,422**	69,657
Unrestricted	**(111,241)**	**-**	**-**	**-**	**(111,241)**	(108,028)
	(71,529)	**477,362**	**470,844**	**763,364**	**1,640,041**	1,775,375
Total liabilities and fund balances	**144,482**	**486,662**	**1,098,629**	**763,713**	**2,493,486**	2,515,911

Approved by the Board of Governors

.... Governor

.... Governor

THE ROYAL INSTITUTION FOR THE ADVANCEMENT OF LEARNING / McGILL UNIVERSITY

Statement of revenue and expenses and changes in fund balances

year ended May 31, 2009
(in thousands of dollars)

	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund	Total 2009	Total 2008
	$	$	$	$	$	$
Revenue						
Government sources						
Canada	**17,076**	**175,720**	**-**	**-**	**192,796**	213,846
Quebec	**299,837**	**46,045**	**43,220**	**-**	**389,102**	372,768
United States	**-**	**7,190**	**-**	**-**	**7,190**	5,692
Grants - other sources	**-**	**24,167**	**-**	**-**	**24,167**	24,617
Contracts	-	**21,721**	**-**	**-**	**21,721**	13,517
Tuition and fees	**169,797**	**18**	**-**	**-**	**169,815**	158,805
Sale of goods and services	**92,861**	**7,065**	**571**	**-**	**100,497**	91,410
Gifts and bequests	**4,935**	**27,223**	**5,717**	**46,469**	**84,344**	105,713
Short-term interest	**3,944**	**581**	**4,232**	**-**	**8,757**	14,051
Investment (loss) income (Note 10)	**893**	**(42,667)**	**-**	**-**	**(41,774)**	73,642
Total revenue	**589,343**	**267,063**	**53,740**	**46,469**	**956,615**	1,074,061
Expenses						
Salaries						
Academic	**190,230**	**61,263**	**-**	**-**	**251,493**	241,469
Administrative and support	**164,122**	**22,345**	**-**	**-**	**186,467**	180,233
Student	**11,577**	**51,509**	**-**	**-**	**63,086**	60,221
Student aid	**13,011**	**28,878**	**-**	**-**	**41,889**	31,502
Benefits	**67,397**	**17,430**	**-**	**-**	**84,827**	81,724
Total salaries	**446,337**	**181,425**	**-**	**-**	**627,762**	595,149
Non-salary						
Material, supplies and publications	**24,649**	**26,826**	**-**	**-**	**51,475**	48,307
Transfers to partner institutions	**1,242**	**28,712**	**-**	**-**	**29,954**	29,279
Contract services	**8,779**	**12,827**	**-**	**-**	**21,606**	22,204
Professional fees	**11,568**	**6,280**	**-**	**7,639**	**25,487**	25,987
Travel	**8,412**	**15,530**	**-**	**-**	**23,942**	20,794
Cost of goods sold and services rendered	**16,339**	**-**	**-**	**-**	**16,339**	16,903
Building occupancy costs	**22,635**	**5,902**	**-**	**-**	**28,537**	22,521
Tuition	**1,077**	**838**	**-**	**-**	**1,915**	1,500
Energy	**21,967**	**838**	**-**	**-**	**22,805**	17,565
Other non-salary expenses	**17,076**	**20,124**	**-**	**-**	**37,200**	37,106
Capital purchases	**18,804**	**55,663**	**1,359**	**-**	**75,826**	96,967
Amortization	**-**	**-**	**76,658**	**-**	**76,658**	73,501
Interest and bank charges	**9,381**	**12**	**30,689**	**-**	**40,082**	42,321
Total non-salary	**161,929**	**173,552**	**108,706**	**7,639**	**451,826**	454,955
Total expenses	**608,266**	**354,977**	**108,706**	**7,639**	**1,079,588**	1,050,104
Excess (deficiency) of revenue over expenses before the undernoted item	**(18,923)**	**(87,914)**	**(54,966)**	**38,830**	**(122,973)**	23,957
Unrealized gains (losses) on marketable securities (Note 10)	**(7,932)**	**(78,738)**	**1,889**	**-**	**(84,781)**	(65,945)
Excess (deficiency) of revenue over expenses	**(26,855)**	**(166,652)**	**(53,077)**	**38,830**	**(207,754)**	(41,988)
Fund balances (deficit), beginning of year	**(60,094)**	**485,437**	**448,229**	**901,803**	**1,775,375**	1,727,269
Interfund transfers (Note 6)	**15,420**	**158,577**	**3,272**	**(177,269)**	**-**	-
Capital expenditures financed by other funds	**-**	**-**	**72,420**	**-**	**72,420**	90,094
Fund balances (deficit), end of year	**(71,529)**	**477,362**	**470,844**	**763,364**	**1,640,041**	1,775,375

THE ROYAL INSTITUTION FOR THE ADVANCEMENT OF LEARNING / McGILL UNIVERSITY

Statement of revenue and expenses and changes in fund balances (continued)

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

	2008				
	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund	Total
	$	$	$	$	$
Revenue					
Government sources					
Canada	19,158	194,688	-	-	213,846
Quebec	277,928	53,928	40,912	-	372,768
United States	-	5,692	-	-	5,692
Grants - other sources	-	24,617	-	-	24,617
Contracts	-	13,517	-	-	13,517
Tuition and fees	158,287	518	-	-	158,805
Sale of goods and services	84,560	6,587	263	-	91,410
Gifts and bequests	4,040	62,202	6,737	32,734	105,713
Short-term interest	6,688	838	6,525	-	14,051
Investment income (Note 10)	11,741	61,901	-	-	73,642
Total revenue	562,402	424,488	54,437	32,734	1,074,061
Expenses					
Salaries					
Academic	182,732	58,737	-	-	241,469
Administrative and support	157,701	22,532	-	-	180,233
Student	11,213	49,008	-	-	60,221
Student aid	7,210	24,292	-	-	31,502
Benefits	64,413	17,311	-	-	81,724
Total salaries	423,269	171,880	-	-	595,149
Non-salary					
Material, supplies and publications	22,436	25,871	-	-	48,307
Transfers to partner institutions	1,047	28,232	-	-	29,279
Contract services	8,326	13,878	-	-	22,204
Professional fees	13,116	5,622	-	7,249	25,987
Travel	7,996	12,798	-	-	20,794
Cost of goods sold and services rendered	16,903	-	-	-	16,903
Building occupancy costs	18,980	3,541	-	-	22,521
Tuition	789	711	-	-	1,500
Energy	16,470	1,095	-	-	17,565
Other non-salary expenses	15,435	21,671	-	-	37,106
Capital purchases	20,169	75,281	1,517	-	96,967
Amortization	-	-	73,501	-	73,501
Interest and bank charges	10,437	42	31,842	-	42,321
Total non-salary	152,104	188,742	106,860	7,249	454,955
Total expenses	575,373	360,622	106,860	7,249	1,050,104
Excess (deficiency) of revenue over expenses before the undernoted item	(12,971)	63,866	(52,423)	25,485	23,957
Unrealized gains (losses) on marketable securities (Note 10)	(6,468)	(59,369)	(108)	-	(65,945)
Excess (deficiency) of revenue over expenses	(19,439)	4,497	(52,531)	25,485	(41,988)
Fund balances (deficit), beginning of year	(43,841)	450,053	407,624	913,433	1,727,269
Interfund transfers (Note 6)	3,186	30,887	3,042	(37,115)	-
Capital expenditures financed by other funds	-	-	90,094	-	90,094
Fund balances (deficit), end of year	(60,094)	485,437	448,229	901,803	1,775,375

THE ROYAL INSTITUTION FOR THE ADVANCEMENT OF LEARNING / McGILL UNIVERSITY

Statement of cash flows

year ended May 31, 2009
(in thousands of dollars)

		2009	2008
		$	$
Operating activities			
Deficiency of revenue over expenses*		**(246,584)**	(67,473)
Adjustments for:			
Amortization		**76,658**	73,501
Loss (gain) on sale of marketable securities		**25,896**	(31,099)
Unrealized losses on marketable securities		**84,781**	65,945
Net change in non-cash working capital items		**15,826**	(6,100)
Decrease in government grant receivable		**826**	15,995
(Increase) decrease in grants and contracts related to research receivable		**10,019**	(5,729)
Increase in pledges receivable		**(14,519)**	(38,576)
		(47,097)	6,464
Investing activities			
Acquisition of capital assets and other assets		**(162,149)**	(126,602)
Change in marketable securities, net		**42,005**	(13,914)
Proceeds from staff mortgages		**124**	269
		(120,020)	(140,247)
Financing activities			
Net change in Endowment Fund balance		**38,830**	25,485
Decrease in contribution to sinking fund		**5,177**	8,676
Issuance of long-term debt		**82,509**	75,000
Repayment of long-term debt		**(74,804)**	(72,270)
Capital expenditures financed by other funds		**72,420**	90,094
		124,132	126,985
Net decrease in cash position		**(42,985)**	(6,798)
Cash position, beginning of year		**(8,707)**	(1,909)
Cash position, end of year		**(51,692)**	(8,707)
Cash position comprises:			
Short-term investments	- Operating Fund	**49,688**	25,020
	- Restricted Fund**	**-**	5,106
	- Plant Fund	**-**	4,056
	- Endowment Fund**	**64,302**	37,022
Bank indebtedness	- Operating Fund	**(165,682)**	(79,911)
		(51,692)	(8,707)

* 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"). 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 $72.4 million ($90.1 million in 2008), 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 $33.3 million ($32.3 million in 2008), resulting in a decrease of $1.0 million in the excess of revenue over expenses for the year ($3.7 million in 2008).

- 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 $28.3 million ($33.5 million in 2008) 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.

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, 2009, they would have been discounted by $3.9 million ($6.1 million in 2008), resulting in an increase of $2.2 million in the excess of revenue over expenses in the restricted fund (excess of $321,000 in 2008).

- 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, 2009, the total deficiency of revenue over expenses would have decreased by $73.6 million to a deficiency of revenue over expenses of $134.1 million ($86.7 million decrease in expenses and $44.7 million excess of revenue over expenses in 2008). 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, and financial instruments, 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. 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.

2. Significant accounting policies (continued)

Other significant accounting policies (continued)

Financial instruments

The University has elected to use the exemption provided by the Canadian Institute of Chartered Accountants ("CICA") permitting not-for-profit organizations not to apply the following Sections of the CICA Handbook: 3862 and 3863, which would otherwise have applied to the financial statements of the University for the year ended May 31, 2009. The University applies the requirements of Section 3861 of the CICA Handbook.

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 using the effective interest method.

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, including consideration of the credit risk of the issuer. 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. Transactions costs are expensed as incurred.

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.

2. Significant accounting policies (continued)

Other significant accounting policies (continued)

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.

Derivative financial instruments

Derivative financial instruments are used as a substitute for more traditional investments. Derivative financial instruments are recorded at their fair values and changes in the fair value are recorded in the statement of revenue and expenses.

Foreign exchange

Monetary assets and liabilities and other assets accounted for at fair value denominated in foreign currencies are translated into Canadian dollars using foreign exchange rates at the balance sheet date. Revenue and expense items are translated into Canadian dollars at the rates of exchange prevailing at the date of the transaction. The gain or loss resulting from translation is included in the statement of revenue and expenses.

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 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.

2. Significant accounting policies (continued)

Other significant accounting policies (continued)

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.

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

Capital disclosures

The University adopted the recommendations of CICA Handbook Section 1535, *Capital Disclosures.* This Section requires the disclosure of information about externally imposed capital requirements. The required disclosures are included in Note 4. The adoption of this Section had no impact on the financial statements.

2. Significant accounting policies (continued)

Accounting policy changes

MELS accounting requirements

Commencing on June 1, 2009, Quebec universities must conform to Canadian generally accepted accounting principles (Canadian GAAP) in all respects.

The universities will adopt the deferral method of accounting, which will result in the transfer of a portion of the fund balances to deferred contributions.

In addition, Quebec universities must adhere to the new accounting policies for capital assets as required by MELS. These new accounting policies will result in modifications in the categories of capital assets as well as the amortization rates and estimated useful lives.

The University is currently evaluating the impact of the adoption of Canadian GAAP on its financial statements.

Accounting standards

In November 2008, the CICA issued amendments to Section 1540, *Cash Flow Statements,* Section 4400, *Financial Statement Presentation by Not-for-profit Organizations* and Section 4460, *Disclosure of Related Party Transactions by Not-for-profit Organizations.* The new standards will be applicable to financial statements relating to fiscal years beginning on or after January 1, 2009. Accordingly, the University will adopt the new standards as of June 1, 2009.

Section 1540 has been amended to included not-for-profit organizations within its scope.

Section 4400 has been amended in order to eliminate the requirement to treat net assets invested in capital assets as a separate component of fund balance and, instead, permit a not-for-profit organization to present such an amount as a category of internally restricted fund balance when it chooses to do so. It also clarifies that revenues and expenses must be recognized and presented on a gross basis when a not-for-profit organization is acting as a principal in transactions.

Section 4460 has been amended to make the language in Section 4460 consistent with related party transactions, Section 3480.

The University is currently evaluating the impact of the adoption of these new standards on its financial statements.

(tabular amounts in thousands of dollars)

3. Capital assets

	2009			2008		
	Cost	Accumulated amortization	Net book value	Cost	Accumulated amortization	Net book value
	$	$	$	$	$	$
Land	**8,110**	**-**	**8,110**	8,110	-	8,110
Land improvements	**4,163**	**1,792**	**2,371**	3,774	1,584	2,190
Buildings	**1,037,670**	**261,178**	**776,492**	979,044	245,336	733,708
Leasehold improvements	**627**	**390**	**237**	812	578	234
Equipment	**375,849**	**207,010**	**168,839**	352,057	192,811	159,246
Library materials	**234,235**	**54,012**	**180,223**	219,082	48,156	170,926
Intangible assets	**11,251**	**7,120**	**4,131**	23,306	19,110	4,196
	1,671,905	**531,502**	**1,140,403**	1,586,185	507,575	1,078,610
Assets under development	**46,230**	**-**	**46,230**	22,151	-	22,151
	1,718,135	**531,502**	**1,186,633**	1,608,336	507,575	1,100,761

4. Externally restricted fund balances

	2009			
	Restricted Fund	Plant Fund	Endowment Fund	Total
	$	$	$	$
Research	**343,017**	**-**	**103,071**	**446,088**
Faculties	**18,687**	**-**	**271,746**	**290,433**
Academic services	**7,476**	**-**	**22,289**	**29,765**
Support services	**3,691**	**7,452**	**17,712**	**28,855**
Community services	**63,558**	**-**	**8,306**	**71,864**
Student services	**40,933**	**-**	**239,687**	**280,620**
Accumulated income (i)	**-**	**-**	**70,100**	**70,100**
	477,362	**7,452**	**732,911**	**1,217,725**

(tabular amounts in thousands of dollars)

4. Externally restricted fund balances (continued)

	2008			
	Restricted Fund	Plant Fund	Endowment Fund	Total
	$	$	$	$
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

(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

	2009			
	Operating Fund	Plant Fund	Endowment Fund	Total
	$	**$**	**$**	**$**
Faculties	**29,131**	**-**	**22,551**	**51,682**
Academic services	**5,755**	**-**	**2,306**	**8,061**
Support services	**(548)**	**(11,743)**	**3,693**	**(8,598)**
Student services	**5,374**	**-**	**1,903**	**7,277**
	39,712	**(11,743)**	**30,453**	**58,422**

(tabular amounts in thousands of dollars)

5. Internally restricted fund balances (continued)

	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

6. Interfund transfers

	2009			
	Operating Fund	Restricted Fund	Plant Fund	Endowment Fund
	$	**$**	**$**	**$**
Overdistributed income transferred (a)	**8,997**	**87,923**	**-**	**(96,920)**
Unrealized losses on endowment investments transferred	**7,932**	**78,520**	**-**	**(86,452)**
Net capitalization of income (b)	**553**	**(8,606)**	**-**	**8,053**
Other transfers (c)	**(2,062)**	**740**	**3,272**	**(1,950)**
	15,420	**158,577**	**3,272**	**(177,269)**

(tabular amounts in thousands of dollars)

6. Interfund transfers (continued)

	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)

(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 of $250 million under short-term credit facilities, of which $159 million has been used at May 31, 2009. Unsecured and uncommitted lines of credit, totalling $345 million, are available to McGill and are normally drawn through bankers' acceptances for periods of up to one year. The lines of credit bear interest at the prime rate, which averaged 2.85% for the year. Bankers' acceptances outstanding at year end bear interest at rates ranging from 0.36% to 3.68%.

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.

(tabular amounts in thousands of dollars)

8. Long-term debt

	2009	2008
	$	$
a)		
1) Bonds (i)		
4.70% Series “9C” due September 12, 2008	**-**	6,910
3.55% Series “12C” due November 24, 2008	**-**	9,395
13.25% Series “II” due January 12, 2009	-	3,000
3.75% Series “13C” due February 24, 2009	-	6,510
4.55% Series “10C” due February 27, 2009	-	7,973
10.75% Series “3” due May 30, 2009	-	7,000
	-	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
4.40% Series “13C” due February 24, 2016	**4,653**	4,653
4.50% Series “14C” due March 8, 2016	**7,000**	7,000
	11,653	11,653
Total Bonds:	**108,369**	149,157

(tabular amounts in thousands of dollars)

8. Long-term debt (continued)

	2009	2008
	$	$
2) Notes (ii)		
4.516% due December 1, 2008	**-**	20,288
3.849% due December 1, 2009	**21,260**	22,272
4.059% due December 1, 2010	**25,833**	27,222
4.167% due December 1, 2010	**4,400**	4,600
3.794% due June 16, 2011 (iii)	**426**	-
4.288% due December 1, 2011	**21,514**	22,676
4.814% due April 25, 2012	**17,600**	18,400
4.9515% due November 1, 2012	**34,505**	37,129
4.355% due September 16, 2013	**85,663**	90,000
4.607% due September 16, 2013	**33,600**	35,000
3.240% due September 23, 2013	**40,000**	-
3.320% due June 1, 2014	**14,000**	-
3.690% due December 1, 2014	**28,000**	-
3.839% due December 1, 2014	**40,000**	40,000
4.267% due December 1, 2015 (iii)	**1,116**	1,251
Total Notes:	**367,917**	318,838
Total Government of Quebec debt:	**476,286**	467,995
Accumulated contributions to sinking fund (iv)	**(28,364)**	(33,541)
Total Government of Québec debt, net	**447,922**	434,454
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	**2,432**	2,841
5.17%, due June 2008	**-**	67
d) Other	**629**	739
Total long-term debt	**600,983**	588,101
Current portion of long-term debt	**(53,377)**	(64,087)
Long-term debt	**547,606**	524,014

(tabular amounts in thousands of dollars)

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. A sinking fund has been established by the Government to set aside funds (see Note iv below).

(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
	$	$
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
4.814% due April 25, 2012	800	16,000
4.952% due November 1, 2012	2,624	26,633
4.355% due September 16, 2013	4,337	68,315
4.607% due September 16, 2013	1,400	28,000
3.240% due September 23, 2013	1,906	32,375
3.320% due June 1, 2014	928	10,287
3.690% due December 1, 2014	1,758	19,208
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 $1.5 million. Semi-annual payments of capital and interest are paid by MDEIE, on 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 $7.2 million to this fund ($10 million in 2008) and applied $12.4 million towards repaid bonds ($18.7 million in 2008).

(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. Semi-annual interest payments are paid by McGill.

(vi) The Royal Bank loan is secured by grants receivable from the Ministère des Affaires Municipales et des Régions ("MAMR") of $2.4 million. Semi-annual payments of capital and interest are paid by McGill and reimbursed by MAMR.

(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:

	$
2010	**53,377**
2011	**46,888**
2012	**92,287**
2013	**52,365**
2014	**135,550**

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. The Plan's 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 $27.1 million has been recorded as the pension expense for this fiscal year ($26.2 million in 2008).

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, 2009 is estimated at $2.3 million ($2.5 million in 2008).

(tabular amounts in thousands of dollars)

10. Net investment (loss) income from endowments

a) Investment income (loss)

Realized net investment income is included in the statement of revenue and expenses and changes in fund balance in the "Investment income (loss)" revenue line. Total losses of $41.8 million were realized in 2009 (income of $73.6 million in 2008).

The above total represents realized net investment income or losses on resources held for endowment and was reported in the following funds:

	2009		
	Operating	Restricted	Total
	$	**$**	**$**
Under Distributed Income (i)	**(8,997)**	**(87,923)**	**(96,920)**
Endowment Income distributed	**2,252**	**45,256**	**47,508**
Endowment Fund contribution (ii)	**7,639**	**-**	**7,639**
Total investment income (loss)	**894**	**(42,667)**	**(41,773)**

	2008		
	Operating	Restricted	Total
	$	**$**	**$**
Over Distributed Income (i)	2,230	20,146	22,376
Endowment Income distributed	2,262	41,755	44,017
Endowment Fund contribution (ii)	7,249	-	7,249
Total investment income (loss)	11,741	61,901	73,642

i) A corresponding interfund transfer from the Endowment Fund to the Operating and Restricted Funds is recorded to offset the investment income (loss) recorded in those funds as per the above (see Note 6).

ii) Represents the 90 basis points charged to the Endowment Fund to absorb investment management, custodial fees, costs of Investment Office, and the contribution to University overheads.

b) Unrealized loss on marketable securities

In addition, the total unrealized loss on marketable securities related to resources held for endowment amounted to $86.5 million ($65.6 million of unrealized loss in 2008).

10. Net investment (loss) income from endowments (continued)

A corresponding interfund transfer is recorded from the Endowment Fund to the various funds which have incurred the unrealized loss (see Note 6). This loss was reduced by an unrealized gain of $1.9 million ($0.1 million unrealized loss in 2008) relating to investments purchased in the Plant Fund using the proceeds of the McGill Senior Debenture issue. Consequently, the total net unrealized loss for the year was $84.8 million ($65.9 million unrealized loss in 2008).

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.

As part of its Endowment asset holdings, 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, 2009, McGill's foreign denominated cash and marketable securities had a fair value of $371 million.

The University has interest rate risk from the impact of interest rate changes on 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, 2009, the carrying values of 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 $663 million at May 31, 2009 ($654.4 million in 2008).

11. Financial instruments (continued)

Fair values (continued)

As approved by the Investment Committee of the Board, McGill has forward contracts outstanding as at May 31, 2009 to sell US$200 million of assets held for endowed purposes with an average forward rate of 1.214 maturing on July 24, 2009. At May 31, 2008, US$260 million of contracts existed with a forward rate of 1.008 maturing on July 24, 2008. As at May 31, 2009, the fair value of these contracts approximated $23.8 million ($3.4 million unrealized gain in 2008) and is included in marketable securities.

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 fair value of the bond and the swap agreement is $31.8 million and is included in marketable securities in the Plant Fund.

The US Dollar denominated investment outstanding will result (at maturity) in the forfeiture of the interest receivable, in exchange for a fixed amount of proceeds. As at May 31, 2009, the fair value of the swap is $14.4 ($13.5 million in 2008).

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.

As at May 31, 2009, McGill held securities classified as non-bank asset-backed commercial paper in the Plant Fund and the Restricted Fund. These securities were carried as marketable securities and had a market value of $4.0 million and $2.2 million, respectively, as estimated by management, based on the present value of future cash flows expected. 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.

(tabular amounts in thousands of dollars)

11. Financial instruments (continued)

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

	2009		2008	
	Endowment Fund	Restricted Fund	Endowment Fund	Restricted Fund
	%	**%**	%	%
Canadian Equity	**19**	**80**	22	62
US Equity	**7**	**20**	14	38
Non North American Equity	**19**	**-**	16	-
Canadian Fixed Income	**25**	**-**	27	-
US Fixed Income	**1**	**-**	-	-
Hedge Funds	**18**	**-**	13	-
Alternate strategies, including Private equity	**11**	**-**	8	-
	100	**100**	100	100

12. Commitments

Year ending May 31	Minimum lease payments
	$
2010	**2,096**
2011	**1,586**
2012	**1,010**
2013	**1,030**
2014	**1,051**
Thereafter	**2,911**
	9,684

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

12. Commitments (continued)

Construction in progress

McGill has undertaken the construction of several new buildings and, as a result, has commitments totalling $37.1 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 $44.7 million within the next four years in accordance with its arrangements with these funds.

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 of Quebec. Although it is not possible to determine the ultimate outcome of such proceedings initiated and ongoing at May 31, 2009, 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. Comparative figures

Certain comparative figures for the year ended May 31, 2008 have been reclassified in order to conform to the presentation adopted in the current year.