DRAFT

UNIVERSITY OF TORONTO
FINANCIAL REPORT
APRIL 30, 2003

INDEX

University of Toronto
Financial Highlights
April 30, 2003

The mission of the University of Toronto is to be one of the best public universities in the world, with undergraduate, graduate and professional programs of excellent quality. Key opportunities and challenges for the year ended April 30, 2003 and continuing forward are student enrolment growth, program quality enhancement and research growth and their associated capital requirements in an environment where revenue growth is lagging expense growth and where the investment markets are performing poorly.

Expenses for the year of $1.41 billion exceeded revenues of $1.25 billion, resulting in a net loss of $164.4 million. This net loss comprised a $55.6 million investment loss on expendable funds and on internally restricted endowments and $108.8 million reflecting a revenue gap.

Over the past five years, expenses have grown at a compound growth rate of 9.9% while revenues have grown only at 4.7%. The following chart shows the key revenue and expense components.

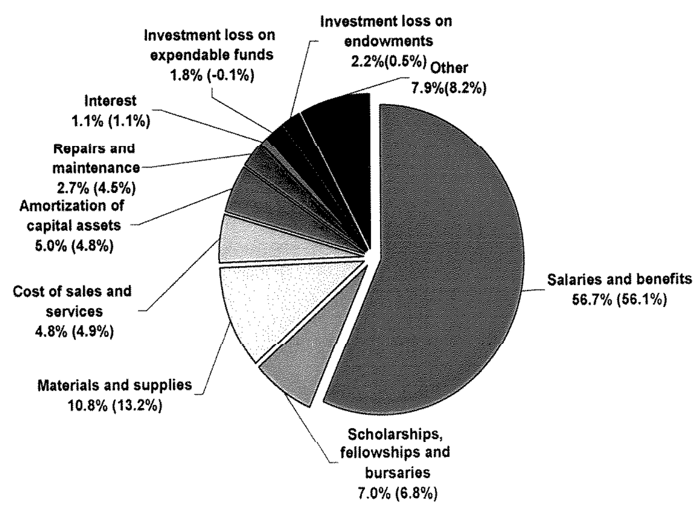
Financial Trends

	1998	1999	2000	2001	2002	2003
	%	%	%	%	%	%
Gov't grants for operations	35	36	33	36	34	33
Student fees	21	26	26	29	29	31
Donations	5	7	5	4	3	3
Grants for research and other purposes	13	13	12	16	21	20
Other	26	18	24	15	13	13
Total revenues	100	100	100	100	100	100
Salaries and benefits	61	58	57	58	56	57
Student aid	3	4	6	6	7	7
Other	36	38	37	36	37	36
Total expenses	100	100	100	100	100	100
	(millions of dollars)					
Total revenues	991.6	930.5	1,066.6	1,047.7	1,155.5	1,248.3
Total expenses	881.8	923.0	998.6	1,107.5	1,271.8	1,412.7

To deal with the revenue gap, the University is pursuing a strategy of increasing revenues and containing expenses. The strategy for increasing revenues has already resulted in significant successes in obtaining full average funding for enrolment growth and quality enhancement funds from the provincial government and funding for the indirect costs of federally funded research from the federal government, the latter two of which are effective with the 2003-04 year. Enrolment growth has already begun and will accelerate over about the next four years.

The strategy for containing expenses includes base budget reductions which are being implemented for the 2003-2004 year. The next long-range academic and budget plan for 2004-05 through 2009-2010 will continue to address the financial resource issue.

Expenses by Category
for the year ended April 30, 2003
(with 2001-02 percentages in brackets)



The total investment loss for the year was $167.4 million, comprising the $55.6 million recorded as an expense, and $111.8 million investment loss on externally restricted endowments, which was recorded as a direct reduction in capital. Effective April 2003, the University has revised its investment policy to reduce the investment return expectation thus reducing investment risk.

The net loss of $164.4 million, the investment loss of $111.8 million on externally restricted endowments and the receipt of $39.9 million of endowed donations and grants together resulted in a decline in the capital of the University to $1.26 billion from $1.50 billion, a reduction of $236.3 million.

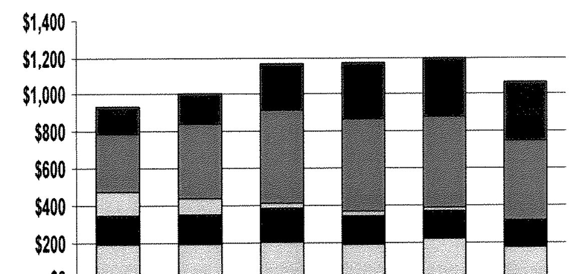
The capital of $1.26 billion consists of the $1.06 billion endowment (84%) and $189.6 million of equity in capital assets (15%). The remaining capital consists of $79.5 million of committed capital and negative $67.2 million of unrestricted capital. The sum of these latter two categories is $12.3 million, a reduction of $93.5 million from last year, which reduces the University's financial flexibility.

Endowments

The endowment declined to $1.06 billion at April 30, 2003 from $1.20 billion at April 30, 2002, a reduction of $137.4 million comprising a $142.5 million investment loss, the allocation of $43.0 million for spending from previously reinvested earnings, $39.9 million of externally endowed contributions to endowments and transfers to endowments of $8.2 million. The investment return on endowments, net of fees, was -11.7% for 2003 (-1.1% for 2002).

The University has reviewed its investment policy for university funds and concluded that the 5% return expectation for the endowment required it to assume too high a level of risk. The University has recently adopted a revised policy whereby the investment return expectation has been reduced from 5% to 4% and where the risk tolerance has been specified as 10% and is currently reviewing and revising the asset mix to realign it with the revised policy requirements. The allocation for program expenditures has correspondingly been reduced to 4.2% of current market values from 5% of a four year moving average of market values (which would have resulted in a payout in excess of 6% of current market values). This resulted in a payout of $6.60 per unit of the endowment for 2003, down from $9.36 per unit last year. In future, the payout per unit is expected to change at the rate of inflation rather than with fluctuations in market value. The endowment is governed by the policy for the preservation of capital of endowment funds, the purpose of which is to ensure that the rate of growth in the capital value of the endowment matches or exceeds the rate of inflation over time. As a result, further diminution of the endowment is not possible and it cannot be considered a sustainable source of funds to close the gap between revenues and expenses.

Endowments at Market Value
for the year ended April 30
(millions of dollars)



	1998	1999	2000	2001	2002	2003
Chairs and professorships	145.8	164.1	260.4	311.4	324.5	314.4
Student aid	310.0	397.2	498.0	495.6	486.4	427.3
Matching funds	127.9	89.0	27.5	25.4	19.2	0
Academic programs	153.8	156.0	180.1	151.5	148.0	143.8
Research	193.2	194.9	205.3	192.3	221.6	176.8

Enrolment growth

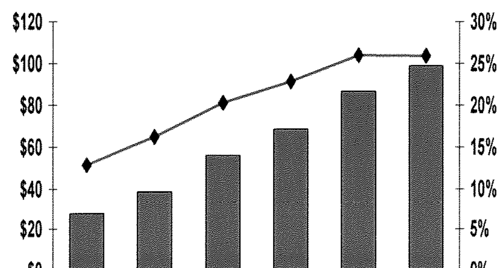
The University is currently expanding enrolment to accommodate additional student demand due to the elimination of Grade 13 in Ontario, demographic growth and increased participation rates.

The Provincial government has recognized that each additional student results in additional costs for universities and has agreed to provide full average funding for each additional student beyond the numbers enrolled in 2000-01. Government grants for general operations increased to $422.7 million for 2003 from $396.2 million for 2002, an increase of 6.7% due primarily to student enrolment growth.

Student fees for students in regulated programs rose in 2002-03 at a rate of 1.9% while fees for other programs increased at varying rates. Student fees revenue increased to $380.9 million for 2003 from $333.7 million for 2002 reflecting primarily student enrolment growth and an overall modest increase in tuition fees.

Student aid (scholarships, fellowships and bursaries) increased to $98.8 million for 2003 from $86.7 million for 2002. Over the 6 years from 1998 to 2003, student fees revenue increased by 79.8% while student aid expense has increased by 261.9%. Student aid comprises 40.2% of the University's endowment.

Student Aid: Scholarships, Fellowships and Bursaries as a Percentage of Student Fees Revenue
(millions of dollars)

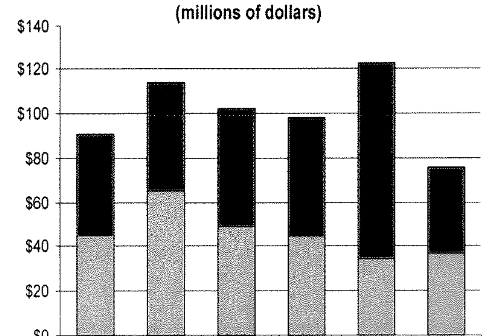


	1998	1999	2000	2001	2002	2003
Scholarships, Fellowships and Bursaries	27.3	38.6	55.9	68.6	86.7	98.8
As a % of fees revenues	12.9%	16.2%	20.3%	22.9%	26.0%	25.9%

Donations

Donations received were $75.9 million for 2003 as compared to $122.4 million for 2002. The decrease from last year is a result of receiving a one-time only $50.0 million gift from the R. Samuel McLaughlin Foundation in 2002. The $75.9 million of donations received this year were reported as follows: $36.6 million as revenue and $39.3 million as an addition to endowment capital. For the six year period from 1998 to 2003, the University received $603.1 million in donations, of which $274.8 million was reported as revenue and $328.3 million was added to endowment capital. These amounts do not include donations to the federated universities – Victoria, St. Michael's and Trinity. Together with its federated universities, the University has a campaign target of $1.0 billion which is expected to be achieved ahead of schedule.

Donations Received
for the year ended April 30
(millions of dollars)

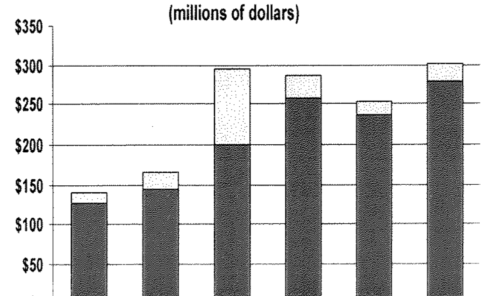


	1998	1999	2000	2001	2002	2003
Added to endowments	45.9	48.5	52.7	53.8	88.1	39.3
Reported as revenue	44.8	65.3	49.5	44.3	34.3	36.6

Government and other Grants for Restricted Purposes

Government and other grants for restricted purposes totalled $302.3 million for 2003, compared to $252.6 million for 2002, and were reported as follows: $222.1 million as revenue from grants for restricted purposes, $26.6 million as contract research revenue and $53.6 million as deferred contributions and deferred capital contributions. Grant funding has increased by 112.7% since 1998. The $302.3 million comprised $280.2 million for research and $22.1 million mostly for capital infrastructure. This increase in research is mainly due to the increase in research funding from the federal and provincial governments.

Government and Other Grants and Contracts
Received for Restricted Purposes
for the year ended April 30
(millions of dollars)



	1998	1999	2000	2001	2002	2003
Capital infrastructure	15.8	21.3	95.8	30.7	16.2	22.1
Research	126.3	145.6	200.3	257.0	236.4	280.2

Compensation

Salaries and benefits increased to $800.8 million for 2003 from $714.7 million, an increase of 12.0% which reflected increased number of employees to support enrolment growth as well as salary and benefit increases agreed with employee groups. The increase comprised $28.7 million in benefits expense (including $20.9 million in pension expense) and $57.4 million in salaries expense.

The University provides benefits such as pension, long-term disability coverage and medical benefits to pensioners, which create liabilities for future payments. The University's liability for such future benefits includes an accrued pension liability of $30.1 million and an employee future benefits obligation other than pension of $88.2 million.

The pension plan's assets were $1.8 billion and the obligation was $2.2 billion resulting in a deficit of $398.3 million at April 30, 2003. The deficit resulted from investment losses, negotiated pension improvements and employee and employer contribution holidays. The employer contribution holiday was redirected as contributions to the supplemental retirement arrangement, to academic needs and for renovations, equipment and construction for research and teaching. The University will make employer contributions of about $18.8 million to the registered pension plan during 2004. The pension plan funding strategy is reviewed periodically and the long-range academic and budget plan for 2004-05 through 2009-2010 will update that funding strategy for the long-term.

Capital Plan

The University has undertaken an ambitious capital construction plan to significantly expand space capacity to accommodate enrolment growth and to enhance and update research infrastructure. This program began in 1999 and is expected to be largely completed by 2007. It includes a significant expansion of the University of Toronto at Mississauga and Scarborough and considerable expansion and renovation on the St. George campus. The estimated cost of the projects currently approved and initiated since 1999 is $739.2 million (not including projects arising from the most recent SuperBuild announcement). An additional $157.1 million is needed for other requirements, bringing the total cost to $896.3 million. Of this sum, $271.7 million has been assembled from donations, research infrastructure grants, ATOP and SuperBuild funds. The balance of $624.6 million is being financed, of which $216.7 million has been borrowed externally, and a further $78.0 million has been financed internally. The additional borrowing to be undertaken is estimated at $329.9 million.

Deferred maintenance and capital renewal:

The University's deferred maintenance and capital renewal requirements are currently estimated at $314.8 million including asbestos containment and removal. The Vice-President, Business Affairs is currently integrating the University's capital programs by pooling the various funds available and prioritizing maintenance and renewal requests. In an effort to provide additional data to assist in the prioritizing of projects, the University is participating, with all other Ontario universities, in a five-year study that is analyzing, in some detail and on a uniform basis, the deferred maintenance obligations of every university in the province.

Felix Chee
Vice-President, Business Affairs

STATEMENT OF ADMINISTRATIVE RESPONSIBILITY

The administration of the University is responsible for the preparation of the financial statements, the notes thereto and all other financial information contained in this annual report.

The administration has prepared the financial statements in accordance with Canadian generally accepted accounting principles developed by the Canadian Institute of Chartered Accountants. The administration believes the financial statements present fairly the University's financial position as at April 30, 2003 and the results of its operations and its cash flows for the year then ended. In order to achieve the objective of fair presentation in all material respects, the use of reasonable estimates and judgments were employed. Additionally, management has ensured that financial information presented elsewhere in this annual report has been prepared in a manner consistent with that in the financial statements.

In fulfilling its responsibilities and recognizing the limits inherent in all systems, the administration has developed and maintains a system of internal control designed to provide reasonable assurance that University assets are safeguarded from loss and that the accounting records are a reliable basis for the preparation of financial statements.

Hewitt Associates LLC has been retained by the University in order to provide an estimate of the University's current year position for pension and other employee future benefits. Management has provided the valuation actuary with the information necessary for the completion of the University's report and retains ultimate responsibility for the determination and estimation of the pension and other employee future benefits liabilities reported.

Governing Council carries out its responsibility for review of the financial statements and this annual report principally through the Business Board and its Audit Committee. The majority of the members of the Audit Committee are not officers or employees of the University. The Audit Committee meets regularly with the administration, as well as the internal auditors and the external auditors, to discuss the results of audit examinations and financial reporting matters, and to satisfy itself that each party is properly discharging its responsibilities. The auditors have full access to the Audit Committee with and without the presence of the administration.

The financial statements for the year ended April 30, 2003 have been reported on by Ernst & Young LLP, Chartered Accountants, the auditors appointed by Governing Council. The auditors' report outlines the scope of their audit and their opinion on the presentation of the information included in the financial statements.

Felix Chee
Vice-President, Business Affairs

Robert J. Birgeneau
President

AUDITORS' REPORT

To the Members of Governing Council of University of Toronto:

We have audited the financial statements of **University of Toronto** as at and for the year ended April 30, 2003 comprising the following:

Balance sheet
Statement of operations
Statement of changes in capital
Statement of cash flows

These financial statements are the responsibility of the administration of the University. 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 the administration, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the University as at April 30, 2003 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Toronto, Canada,
May 30, 2003.

Chartered Accountants

UNIVERSITY OF TORONTO

BALANCE SHEET
April 30, 2003
(with comparative figures as at April 30, 2002)
(millions of dollars)

	2003 $	2002 $
ASSETS		
Current		
Cash and short-term investments (note 4)	**309.2**	216.3
Accounts receivable	**72.1**	69.6
Inventories and prepaid expenses (note 18 (b))	**18.8**	12.4
	400.1	298.3
Deferred pension charge (note 3)		5.7
Investments (note 4)	**1,339.1**	1,654.8
Capital assets, net (note 5)	**706.0**	618.8
	2,445.2	2,577.6
LIABILITIES		
Current		
Accounts payable and accrued liabilities (note 7)	**130.7**	132.5
Deferred contributions (notes 9 and 13)	**267.0**	266.7
	397.7	399.2
Accrued pension liability (note 3)	**30.1**	
Employee future benefit obligation other than pension (note 3)	**88.2**	64.3
Other long-term debt (note 7)	**56.7**	58.6
Series A senior unsecured debenture (note 8)	**160.0**	160.0
Deferred capital contributions (note 10)	**448.3**	395.0
	1,181.0	1,077.1
CAPITAL (statement 3)		
Unrestricted capital (deficit)	**(67.2)**	(32.0)
Committed capital (note 11)	**79.5**	137.8
Equity in capital assets (note 6)	**189.6**	195.0
Endowments (notes 12 and 13)	**1,062.3**	1,199.7
	1,264.2	1,500.5
	2,445.2	2,577.6

On behalf of Governing Council:

Thomas H. Simpson
Chairman

Robert J. Birgeneau
President

(See notes to financial statements)

UNIVERSITY OF TORONTO

STATEMENT OF OPERATIONS
FOR THE FISCAL YEAR ENDED APRIL 30, 2003

(with comparative figures for the fiscal year ended April 30, 2002)
(millions of dollars)

	2003 $	2002 $
REVENUES		
Government grants for general operations	**422.7**	396.2
Student fees	**380.9**	333.7
Government and other grants for restricted purposes (note 16)	**222.1**	211.2
Sales, services and sundry income	**159.4**	149.6
Donations (note 15)	**36.6**	34.3
Contract research	**26.6**	30.5
	1,248.3	1,155.5
EXPENSES		
Salaries and benefits (note 3)	**800.8**	714.7
Investment loss (note 4)	**55.6**	3.4
Materials and supplies	**153.4**	166.1
Scholarships, fellowships and bursaries	**98.8**	86.7
Amortization of capital assets	**71.1**	61.4
Cost of sales and services	**67.4**	63.0
Utilities	**39.1**	35.1
Repairs and maintenance	**38.8**	57.3
Travel and conferences	**28.8**	26.6
Interest	**15.4**	13.4
External contracted services	**14.8**	16.7
Telecommunications	**9.6**	9.4
Other	**19.1**	18.0
	1,412.7	1,271.8
NET LOSS	**(164.4)**	(116.3)

(See notes to financial statements)

UNIVERSITY OF TORONTO

STATEMENT OF CHANGES IN CAPITAL
FOR THE YEAR ENDED APRIL 30, 2003

(with comparative figures for the year ended April 30, 2002)
(millions of dollars)

	Unrestricted Capital (deficit) $	Committed capital (note 11) $	Equity in capital assets (note 6) $	Endowments (note 12) $	2003 Total $	2002 Total $
Capital, beginning of year	(32.0)	137.8	195.0	1,199.7	1,500.5	1,535.9
Net loss	(164.4)				(164.4)	(116.3)
Net change in committed capital (note 11)	58.3	(58.3)				
Net change in equity in capital assets (note 6)	5.4		(5.4)			
Transfer from internally and externally restricted endowments (note 12)						
- available for spending	43.0			(43.0)		
- investment loss	30.7			(30.7)		
Transfer to endowments						
- Donations	(5.3)			5.3		
- Matching funds	(2.9)			2.9		
Investment loss on externally restricted endowments				(111.8)	(111.8)	(8.8)
Externally endowed contributions						
- Donations				39.3	39.3	88.1
- Ontario grants				0.6	0.6	1.6
Capital, end of year	(67.2)	79.5	189.6	1,062.3	1,264.2	1,500.5

(See notes to financial statements)

UNIVERSITY OF TORONTO

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED APRIL 30, 2003
(with comparative figures for the year ended April 30, 2002)
(millions of dollars)

	2003 $	2002 $
OPERATING ACTIVITIES		
Net loss	**(164.4)**	(116.3)
Add (deduct) non-cash items:		
Amortization of capital assets (note 5)	**71.1**	61.4
Amortization of deferred capital contributions (note 10)	**(31.3)**	(25.6)
Net capital loss from investments	**118.6**	59.4
Change in other non-cash items (note 14)	**(10.4)**	17.3
	(16.4)	(3.8)
INVESTING AND FINANCING ACTIVITIES		
Accrued pension liability	**35.8**	16.6
Employee future benefit obligation other than pension	**23.9**	23.0
Net sale (purchase) of investments	**85.3**	(110.2)
Purchase of capital assets (note 5)	**(158.3)**	(210.9)
Contributions for capital asset purchases (note 10)	**84.6**	48.6
Other long-term debt principal repayments	**(1.9)**	(7.1)
Long-term debt obtained		7.4
Series A senior unsecured debenture issue (note 8)		160.0
Endowment contributions		
- donations	**39.3**	88.1
- Ontario grants	**0.6**	1.6
	109.3	17.1
Increase in cash and short-term investments during the year	**92.9**	13.3
Cash and short-term investments, beginning of year	**216.3**	203.0
Cash and short-term investments, end of year	**309.2**	216.3

(See notes to financial statements)

1. Description

The Governing Council of the University of Toronto which operates under the name, University of Toronto (the "University"), is a corporation under the University of Toronto Act, a statute of the Legislative Assembly of Ontario. The University is an institution dedicated to providing post-secondary education and to conducting research. The University's mission is to be one of the top public research universities in the world with undergraduate, graduate and professional programs of excellent quality.

These financial statements include the assets, liabilities, capital, revenues, expenses and other transactions of all of the operations and organizations under the jurisdiction of Governing Council. These financial statements do not include the assets, liabilities and operations of Victoria University, Trinity College, the University of St. Michael's College, Sunnybrook & Women's College Health Sciences Centre ("Sunnybrook & Women's") and the affiliated colleges under the memorandum of agreement with the Toronto School of Theology, each of which is a separate non-controlled corporate body with separate financial statements.

The University has an economic beneficial interest in a Crown-controlled foundation, University of Toronto Foundation ("Foundation"), which is not consolidated in these financial statements. The principal objectives of the Foundation are to solicit, receive and distribute money and other property to support education and research at the University and its federated and affiliated organizations.

The University holds title to the land and original buildings of the Sunnybrook Campus of Sunnybrook & Women's. The land and original buildings were acquired for the sum of one dollar and are used for hospital purposes and for related medical research and teaching purposes. The property is leased to the Board of Directors of Sunnybrook & Women's, a separate corporation, under a ground lease, which is perpetually renewable every twenty-one years at the option of the Board of Directors of Sunnybrook & Women's.

The University is a registered charitable organization and, as such, is exempt from income taxes under the Income Tax Act (Canada).

2. Summary of significant accounting policies and reporting practices

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles applied within the framework of the significant accounting policies summarized below:

a) Investments -

Investments are carried at fair values. Fair value amounts represent estimates of the consideration that would be agreed upon between knowledgeable, willing parties who are under no compulsion to act. It is best evidenced by a quoted market price, if one exists. The calculation of estimated fair value is based upon market conditions at a specific point in time and may not be reflective of future fair values. Changes in fair values from one year to the next are reflected in the statement of operations.

Fair values of investments are determined as follows:

1. Publicly traded bonds and equities are determined based on quoted market values.
2. Investments in pooled funds are valued at their unit values.
3. Unlisted or infrequently traded securities are based on quoted market yields or comparable security prices, as appropriate.
4. Real estate is generally valued through an appraisal process, which utilizes discounted future cash flows. In estimating future cash flows certain assumptions are made with respect to future economic conditions and rates of return. The appraisal process is carried out periodically by accredited appraisers. A year-end estimate is then arrived at by considering the appraisals performed.

b) Derivative financial instruments -

Derivative financial instruments are used to manage particular market and currency exposures for hedging and risk management purposes with respect to the University's investments and as a substitute for more traditional investments. Derivative financial instruments and synthetic products that may be employed include debt, equity and currency futures, options, swaps and forward contracts. These contracts are supported by liquid assets with a market value approximately equal to the market value of the instruments underlying the derivative contract.

The fair value of derivative financial instruments reflects the daily quoted market amount of those instruments, thereby taking into account the current unrealized gains or losses on open contracts. Investment dealer quotes or quotes from a bank are available for substantially all of the University's derivative financial instruments. Gains and losses on these instruments are recognized as investment income in the year in which the changes in fair value occur.

c) Inventory valuation -

Supplies and other inventories are carried at the lower of average cost or net realizable value.

d) Employee benefit plans -

The University has a defined benefit pension plan for its employees and provides other retirement benefits such as extended health, semi-private and dental care. The cost of pensions and other retirement benefits earned by employees is determined using the projected benefit actuarial method based on services rendered and management's best estimates regarding assumptions about a number of future conditions including investment returns, salary changes, withdrawals, mortality rates and expected health care costs. Changes in management's best estimates resulting from changes in future conditions could require a change in the recognized amounts.

The net actuarial gain or loss is amortized on a straight-line basis over the average remaining service life of the active employees. Assets of the pension fund and other benefit plans are valued using year-end market values. Liabilities are discounted using current interest rates on long-term bonds.

e) **Capital assets** -

Purchased capital assets are recorded at cost. Contributed capital assets are recorded at market value at the date of contribution. Amortization is provided on a straight-line basis using the following annual rates:

Buildings	2.5%
Co-generation facility	5%
Equipment and furnishings	10% - 15%
Library books	20%
Computers	20%

Contributed rare books and other collections are expensed in the year received.

f) **Revenue recognition** -

The University follows the deferral method of accounting for contributions, which include donations and government grants. Contributions externally restricted for purposes other than endowment are recognized as revenue in the year in which the related expenses are recognized. Externally restricted contributions for depreciable capital assets are deferred and amortized over the life of the related capital assets. Deferred contributions and amortization of capital contributions recognized as revenue in the current year are presented as donations revenue and investment income to the extent that restricted amounts have been received in the current year, with the difference recorded as government and other grants for restricted purposes. Endowment contributions and contributions of non-depreciable capital assets are recognized as direct increases in capital in the year in which they are received. The University actively fundraises and unrestricted donations are recorded when received since pledges are not legally enforceable claims. Student fees are recognized as revenue when courses and seminars are held. Sales and services revenues are recognized at point of sale or when the service has been provided.

g) **Foreign currency translation** -

Monetary assets and liabilities denominated in foreign currencies are translated at the exchange rate in effect at year end. Operating revenues and expenses are translated at exchange rates prevailing on the transaction dates. Gains or losses arising from these translations are included in earnings.

h) **Accounting estimates** -

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. These amounts are based on management's best knowledge of current events and actions that the University may undertake in the future. Actual results could differ from those estimates.

i) Contributed services and materials -

Volunteers contribute an indeterminable number of hours per year. Because of the difficulty of determining their market value, contributed services and materials are not recognized in the financial statements.

3. Employee benefit plans

The University has a number of defined benefit plans including pension plans and other benefit plans which includes other retirement and post-employment benefits to most of its employees. The calculation of expense in connection with these plans is based on the current service cost of employee benefits, amortization of transitional amounts and the amortization of actuarial gains and losses on assets and liabilities.

The employee benefits expense for the year includes pension expense of $39.7 million (2002 – $18.8 million) and other retirement benefits expense of $30.0 million (2002 - $28.2 million).

Information about the University's defined benefit plans as at April 30 is as follows:

	(millions of dollars)			
	2003		2002	
	Pension benefit plans	**Other benefit plans**	Pension benefit plans	Other benefit plans
Accrued benefit obligation	**2,203.1**	**184.7**	2,039.4	172.7
Fair value of plan assets	**1,804.8**	**26.6**	2,123.1	27.7
Plan surplus (deficit)	**(398.3)**	**(158.1)**	83.7	(145.0)
Accrued pension liability (deferred pension charge)	**30.1**		(5.7)	
Employee future benefit obligation other than pension		**88.2**		64.3

Of the $398.3 million deficit (2002 – surplus of $83.7 million) of the pension benefit plans, only $30.1 million is recorded in the University's financial statements as a pension liability (2002 – deferred pension charge of $5.7 million).

Included in the accrued benefit obligation of pension benefit plans is the unfunded supplementary retirement arrangement obligation of $98.7 million (2002 - $118.9 million) of which the University has set aside $89.1 million (2002 - $92.0 million) as committed capital to April 30, 2003 (note 11).

The significant actuarial assumptions adopted in measuring the University's accrued benefit obligation are as follows:

	2003		2002	
	Pension benefit plans	**Other benefit plans**	Pension benefit plans	Other benefit plans
Discount rate	**7.0%**	**7.0%**	7.0%	7.0%
Expected long-term rate of return on plan assets	**7.0%**	N/A	7.0%	N/A
Rate of compensation increase	**4.5%**	**4.5%**	4.5%	4.5%

For measurement purposes, a 6.6% (2002 - 7.0%) annual rate of increase in the per capita cost of covered health care benefits was assumed for 2003. The rate of increase was assumed to decrease gradually to 5% for 2007 and remain at that level thereafter.

The table below outlines the funding provided by the University and its employees and the benefits paid under the University's defined benefit plans:

	(millions of dollars)			
	2003		2002	
	Pension benefit plans	**Other benefit plans**	Pension benefit plans	Other benefit plans
Funding by Employer	**3.9**	**9.6**	2.3	8.4
Funding by Employees	**22.1**	**2.6**	9.5	2.4
Benefits paid	**98.1**	**11.3**	91.1	10.6

4. **Investments**

The market values of investments are as follows:

	(millions of dollars)	
	2003	2002
Cash, short-term notes and treasury bills	**325.1**	191.6
Government and corporate bonds	**302.1**	441.4
Canadian equities	**102.6**	117.6
United States equities	**258.8**	337.7
Other international equities	**225.0**	387.8
Hedge funds	**372.9**	345.1
Real estate	**40.2**	41.9
Derivative related net receivable	**21.6**	8.0
	1,648.3	1,871.1
Less amounts reported as cash and short-term investments	**309.2**	216.3
	1,339.1	1,654.8

At April 30, 2003 $892.9 million (2002 - $1,204.0 million) of the University's investments were held in pooled funds and have been classified in the appropriate investment category.

The University's investments are managed using two pools. The long-term capital appreciation pool ("LTCAP") mainly includes endowment funds and all other funds are managed in the expendable funds investment pool ("EFIP"). The asset mix for each pool is as follows:

	(millions of dollars)			
	2003		2002	
	EFIP	**LTCAP**	EFIP	LTCAP
Cash, short-term notes and treasury bills	**299.2**	**25.9**	182.5	9.1
Government and corporate bonds	**97.3**	**204.8**	104.1	337.3
Canadian equities		**102.6**	7.0	110.6
United States equities		**258.8**	17.9	319.8
Other international equities		**225.0**	20.5	367.3
Hedge funds	**115.3**	**257.6**	167.8	177.3
Real estate		**40.2**		41.9
Derivative related net receivable	**2.7**	**18.9**	0.5	7.5
	514.5	**1,133.8**	500.3	1,370.8

Risk management relates to the understanding and active management of the risks associated with all areas of the University's financial instruments. Investments are primarily exposed to foreign currency, interest rate volatility, market and credit risk. The University, through its University of Toronto Asset Management Corporation, has formal policies and procedures in place governing asset mix among equity, fixed income and real estate instruments, requiring diversification within categories, and setting limits on the size of exposure to individual investments and counterparties. In addition, derivative instruments are used in the management of these risks (see below).

Derivative financial instruments

Description

The University has entered into equity index futures contracts which oblige it to pay the difference between a predetermined amount and the market value of certain equities when the market value is less than the predetermined amount, or receive the difference when the market value is more than the predetermined amount.

The University enters into foreign currency forward contracts to minimize exchange rate fluctuations and the resulting uncertainty on future financial results. All outstanding contracts have a remaining term to maturity of less than one year. The University has significant contracts outstanding held in U.S. dollars, the Euro, Japanese yen and the British Pound.

The University has entered into interest rate swap agreements in order to manage the interest rate exposure associated with certain long-term debt obligations. The contracts have the effect of converting the floating rate of interest on certain debt to a fixed rate.

Risks

The notional amounts of the derivative financial instruments do not represent amounts exchanged between parties and are not a measure of the University's exposure resulting from the use of financial instrument contracts. The amounts exchanged are based on the applicable rates applied to the notional amounts.

The University is exposed to credit-related losses in the event of non-performance by counterparties to these financial instruments, but it does not expect any counterparties to fail to meet their obligations given their high credit ratings. The University limits its derivative financial instruments' credit risk by dealing with counterparties that are at least rated A.

Terms and conditions

The notional and fair value amounts of the financial instruments are as follows:

	(millions of dollars)			
	2003		2002	
	Notional value	**Fair value**	Notional value	Fair value
Foreign currency forward contracts:				
- U.S. dollars	**599.8**	**15.6**	525.2	7.0
- Global	**137.9**	**2.0**	178.5	(1.6)
		17.6		5.4
Equity index futures contracts				
- U.S. dollars	**42.8**	**4.0**	90.8	2.6
Interest rate swap contracts	**38.4**	**(4.4)**	39.3	(2.2)

The interest rate swap contracts result in the University paying a fixed long-term interest rate of 6.72% (2002 – 6.72%) on certain debt obligations instead of paying a weighted average short-term floating interest rate of 2.96% (2002 – 3.39%).

The University's investment loss of $55.6 million (2002 - $3.4 million) is made up of a loss on internally restricted endowments of $30.7 million (2002 - $4.8 million) and a loss of $24.9 million (2002 – income of $1.4 million) on other investments.

5. Capital assets

	(millions of dollars)			
	2003		2002	
	Total Cost	**Accumulated Amortization**	Total Cost	Accumulated Amortization
Land	**30.8**		30.8	
Buildings	**986.8**	**515.9**	910.5	501.3
Equipment and furnishings	**731.0**	**566.7**	669.4	529.6
Library books	**291.9**	**251.9**	271.5	232.5
	2,040.5	**1,334.5**	1,882.2	1,263.4
Less accumulated amortization	**1,334.5**		1,263.4	
Net book value	**706.0**		618.8	

The University's insurer develops replacement values of buildings and contents for insurance purposes using an independent appraisal service. Fine art and rare book collections are valued by the appropriate University officers. The insured replacement value of buildings is $2.5 billion (2002 - $2.2 billion); contents is $3.4 billion (2002 - $3.2 billion), which includes library books of $2.4 billion (2002 - $2.2 billion).

The change in net book value of capital assets is due to the following:

	(millions of dollars)			
		2003		2002
Balance, beginning of year		**618.8**		469.3
Purchase of capital assets funded by capital contributions	**89.0**		93.5	
Purchase of capital assets financed by Series A debenture (note 8)	**38.6**		54.5	
Purchase of capital assets internally funded	**30.7**	**158.3**	62.9	210.9
Less: Amortization of capital assets		**(71.1)**		(61.4)
Balance, end of year		**706.0**		618.8

6. Equity in capital assets

Equity in capital assets represents the following:

	(millions of dollars)	
	2003	2002
Capital assets, net	**706.0**	618.8
Less net book value of assets financed by:		
Long-term debt and debenture (notes 7 and 8)	**(149.4)**	(114.5)
Deferred capital contributions (note 10)	**(367.0)**	(309.3)
Balance, end of year	**189.6**	195.0

The net (decrease) increase in equity in capital assets is as follows:

	(millions of dollars)	
	2003	2002
Long-term debt principal repayments	**1.9**	7.1
Purchase of capital assets internally financed	**30.7**	62.9
Increase in equity in capital assets	**32.6**	70.0
Long-term debt obtained during the year		7.4
Amortization expense	**71.1**	61.4
Less: Amount of amortization expense related to capital assets purchased with:		
a) series A debenture	**(1.8)**	(0.5)
b) restricted contributions	**(31.3)**	(25.6)
Decrease in equity in capital assets	**38.0**	42.7
Net (decrease) increase	**(5.4)**	27.3

7. Other long-term debt

Other long-term debt consists of mortgages of $18.6 million (2002 – $19.0 million) maturing from 2010 to 2029 and term loans of $40.0 million (2002 – $41.5 million) maturing from 2003 to 2024 of which the current portion of $1.9 million (2002 - $1.9 million) is included in accounts payable and accrued liabilities. The weighted average effective interest rate of the mortgages and term loans, after giving effect to the interest rate swaps, was 7.43% (2002 – 7.43%) and 6.70% (2002 – 6.78%) respectively. The fair value of long-term debt at April 30, 2003 was $54.2 million (2002 - $62.7 million) compared to a carrying amount of $58.6 million (2002 -$60.5 million). Anticipated requirements to meet the principal portion of the long-term debt repayments over the next five years are as follows:

2004 - $1.9 million, 2005 - $1.7 million, 2006 - $1.8 million, 2007 - $1.9 million, 2008 - $2.1 million.

8. Series A senior unsecured debenture

On July 18, 2001, the University issued Series A senior unsecured debenture in the aggregate principal amount of $160.0 million at a price of $999.62 for proceeds of $159.9 million. The debenture bears interest at 6.78%, which is payable semi-annually on January 18 and July 18 with the principal amount to be repaid on July 18, 2031. The proceeds of the issue are being used to finance capital projects including the construction of student residences and parking facilities and real estate acquisitions. To date, the University has spent $93.1 million (2002 - $54.5 million) of the proceeds on capital assets with the remainder to be spent in future years. The fair value of the debenture at April 30, 2003 was $180.6 million (2002 - $169.3 million) compared to a carrying amount of $160 million (2002 - $160.0 million).

9. Deferred contributions

Deferred contributions represent externally restricted grants and donations for future expenditures. Changes in the deferred contributions balance are as follows:

	(millions of dollars)	
	2003	2002
Balance, beginning of year	**266.7**	278.9
Grants, donations and investment income	**303.5**	265.4
Recognized as revenue during the year	**(303.2)**	(277.6)
Balance, end of year	**267.0**	266.7

The deferred contributions will be spent as follows:

	(millions of dollars)	
	2003	2002
Research	**159.2**	163.3
Student aid	**37.9**	41.6
Other restricted purposes	**69.9**	61.8
	267.0	266.7

10. Deferred capital contributions

Deferred capital contributions represent the unamortized amount of donations and grants received for the purchase of capital assets. The amortization of capital contributions is recorded as revenue in the statement of operations. The changes in the deferred capital contributions balance for the year are as follows:

	(millions of dollars)	
	2003	2002
Balance, beginning of year	**395.0**	372.0
Less amortization of deferred capital contributions	**(31.3)**	(25.6)
Add contributions received for capital asset purchases	**84.6**	48.6
Balance, end of year	**448.3**	395.0

This balance represents:

Amount used for the purchase of capital assets	**367.0**	309.3
Amount to be spent on capital assets	**81.3**	85.7
	448.3	395.0

11. Committed Capital

	(millions of dollars)	
	2003	2002
Supplemental retirement arrangement	**89.1**	92.0
Departmental trust funds	**68.0**	70.3
Unexpended operating funds		
Net divisional carryforwards	**54.4**	46.1
Employee future benefits	**(98.0)**	(37.1)
Investment income reserve	**(47.6)**	(22.6)
Research overhead	**6.3**	7.5
Infrastructure		
Alterations and renovations	**16.8**	12.8
Unfunded projects	**(10.8)**	(31.5)
Other funds	**1.3**	0.3
	79.5	137.8

Committed capital is internally restricted funds set aside reflecting the application of Governing Council policy as follows:

a) **Supplementary retirement arrangement -**
These funds, which will be accumulating over a number of years, have been set aside to meet future obligations of the supplemental retirement arrangement.

b) **Departmental trust funds -**
These are departmental trust funds available for spending by divisions with no external restrictions.

c) **Unexpended operating funds -**
Divisions are permitted to carry forward unspent budgets at the end of each year for expenditure in the following year. Funds for unfilled purchase orders have been committed for goods or services to be received in the following year. These amounts have been reduced by the vacation pay accrual representing the unfunded cost of vacation credits earned but not taken by administrative employee groups at year end and by the voluntary early retirement liability for faculty and librarians representing the unfunded liability of voluntary early retirement incentive costs paid to or committed to specific faculty members. This category also includes the unfunded portion of employee future benefits obligations and a portion of investment losses incurred on the unexpended asset balance to be reduced over the next 4 years.

d) **Research overhead** -
Research overhead recoveries from customers in calendar year 2002 are appropriated and available for spending in the following year.

e) **Infrastructure -**
These represent unspent funds in respect of approved alterations and renovations projects in progress at the end of the fiscal year less amounts spent without funding on hand.

f) **Other funds -**
These funds are to support various initiatives to enhance the quality, structure and organization of programs and activities as well as the restructuring needed to adapt to the long-range budget plan and to improve the productivity of physical assets.

12. Endowments

Endowments consist of externally restricted donations received by the University and internal resources transferred by Governing Council, in the exercise of its discretion. With respect to the latter cases, Governing Council may have the right to subsequently decide to remove the designation. The endowment principal is required to be maintained intact subject to the University's preservation of capital policy. The investment income generated from endowments must be used in accordance with the various purposes established by donors or Governing Council. The University ensures, as part of its fiduciary responsibilities, that all funds received with a restricted purpose are expended for the purpose for which they were provided.

Investment income on endowments, which is comprised of interest, dividend income and realized and unrealized gains and losses, is recorded in the statement of operations when this income is available for spending, at the discretion of the University or is available for spending as conditions have been met. University policy has been established with the objective of protecting the real value of the endowments by limiting the amount of income made available for spending and requiring the reinvestment of income not made available. In this fiscal year, the policy was changed to reduce the real rate of return objective from 5% to 4% enabling a less aggressive asset mix. As such, this year's income available for spending is calculated at 4.2% of the market value of endowment assets, representing $6.60 per unit of the long-term capital appreciation pool. In the future, the amount available for spending will be calculated at $6.60 per unit increased by inflation instead of using 5% of the market value of endowment assets smoothed over 4 years. In any particular year, should net investment income be insufficient to fund the amount to be made available for spending or the investment return is negative, the amount that is made available for spending is funded by the accumulated reinvested income. However, for individual endowment funds without sufficient accumulated reinvestment income, endowment capital is used in the current year. This amount is expected to be recovered by future net investment income.

During the year, the investment loss on externally restricted endowments was $111.8 million (2002 - $8.8 million) and $30.7 million (2002 - $4.8 million) million on internally restricted endowments. A transfer of $73.7 million (2002 - $62.1 million) was required to cover the investment loss on internally restricted endowments and the $43.0 million (2002 - $57.3 million) made available for spending for the following year. As a result, transfers were recorded of $33.9 million (2002 - $41.6 million) from externally restricted endowments and $39.8 million (2002 - $20.5 million) from internally restricted endowments to unrestricted capital (deficit). Capital restricted for endowments consist of:

	(millions of dollars)	
	2003	2002
Externally restricted endowments	**846.5**	917.4
Internally restricted endowments	**215.8**	282.3
	1,062.3	1,199.7

The University transferred $34.9 million (2002 - $8.7 million) from internally restricted to externally restricted endowments as a result of being committed under gifting arrangements to match certain donations received during the year for chairs and professorships and for the student aid program.

13. Ontario Student Opportunity Trust Fund

Externally restricted endowments include grants provided by the Government of Ontario from the Ontario Student Opportunity Trust Fund matching program to award student aid as a result of raising an equal amount of endowed donations. The University also matched certain of these endowed donations.

	(millions of dollars)	
	2003	2002
Endowment balance, beginning of year	**304.6**	327.2
Donations	**2.0**	
Transfer to other funds		(3.3)
Transfer to expendable funds	**(48.5)**	(19.3)
Endowment balance, end of year	**258.1**	304.6
Expendable funds available for awards, beginning of year	**22.9**	20.1
Transfer from endowment balance	**48.5**	19.3
Investment loss	**(37.1)**	(2.5)
Bursaries awarded	**(14.2)**	(14.0)
Expendable funds available for awards, end of year	**20.1**	22.9
Number of bursaries awarded	**4,862**	4,640

The expendable funds available for awards are included in deferred contributions (note 9) on the balance sheet.

14. Change in other non-cash items

The net change in other non-cash items is as follows:

	(millions of dollars)	
	2003	2002
Accounts receivable	**(2.5)**	(6.2)
Inventories and prepaid expenses	**(6.4)**	(0.9)
Deferred contributions	**0.3**	(12.2)
Accounts payable and accrued liabilities	**(1.8)**	36.6
	(10.4)	17.3

15. Donations

During the year, the University received donations of $75.9 million (2002 - $122.4 million). Of that amount, $39.3 million (2002 - $88.1 million) is recorded as a direct addition to endowments in accordance with the accounting policy and is not recorded as donations revenue.

16. Government and other grants for restricted purposes

During the year, the University received $253.6 million (2002 - $205.9 million) of government and other grants for research and $22.1 million (2002 - $16.2 million) for capital infrastructure of which $53.6 million (2002 - $10.9 million) was deferred for future spending and $222.1 million (2002 - $211.2 million) was recorded as revenue.

17. University of Toronto Foundation

At the year end, the Foundation, a Crown-controlled foundation, had a balance of donations on hand of $1.0 million (2002 - $0.8 million).

The University acts as investment manager for the Foundation. At year end, investments include an amount of $1.1 million (2002 - $0.8 million) held for the Foundation offset by an equal amount in accounts payable and accrued liabilities.

18. Other commitments

a) The estimated cost to complete construction and renovation projects in progress at April 30, 2003, which will be funded by government grants, donations and operations, is approximately $340.0 million (2002 - $383.6 million).

b) During the year, the University entered into an agreement to purchase the Colony Hotel located at 89 Chestnut Street, Toronto for a price of $67.4 million. The University made a deposit to the vendor of $5.0 million at April 30, 2003 with the balance paid on the closing date of June 2, 2003. The Colony Hotel will be transformed into an innovative student community living arrangement by September 1, 2003 at an estimated additional cost of $4.0 million.

c) The annual payments under various operating leases are approximately $6.2 million (2002 - $5.7 million).

19. Contingencies

a) The University has a program under which it guarantees bank loans to faculty and staff members to assist in the purchase or refinancing of their homes. The University holds mortgages as collateral security against such guarantees. At April 30, 2003, the amount of loans guaranteed was $5.6 million (2002 - $4.7 million). The University's estimated obligation under these guarantees is not material.

b) The nature of the University's activities is such that there is usually litigation pending or in prospect at any one time. With respect to claims at April 30, 2003, the University believes it has valid defenses and appropriate insurance coverage in place. In the event any claims are successful, such claims are not expected to have a material effect on the University's financial position.

c) The University is a member of a reciprocal exchange of insurance risks in association with fifty other Canadian universities. This self-insurance co-operative is named the Canadian Universities Reciprocal Insurance Exchange ("CURIE") and involves a contractual agreement to share the insurable property and liability risks of member universities.

The projected cost of claims is funded through members' premiums based on actuarial projections. As of December 31, 2002, CURIE had a surplus of $4.1 million (2001 - $7.2 million), of which the University's pro rata share is approximately 9.3% (2001 – 9.4%) on an ongoing basis.

20. Comparative financial statements

The comparative financial statements have been reclassified from statements previously presented to conform to the presentation of the 2003 financial statements.