UAH

The University of Alabama in Huntsville

FINANCIAL REPORT
2006

FINANCIAL REPORT
2005 – 2006

UAH President Frank Franz presides over the ribbon-cutting ceremony for the opening of Fraternity/Sorority Row on the east side of the university's campus. New homes opened this fall to five Greek societies at UAH. Attending the ceremony are, from left: Jack Killian, president of the Interfraternity Council; UAH benefactors Linda and Mark Smith; Mallory Crafton, Panhellenic Council President; Vice President for Student Affairs Delois Smith; and Ben and Thomas Howard, representing benefactor Susie Hudson.

Table of Contents

The University of Alabama in Huntsville

A Space Grant College
An Affirmative Action/Equal Opportunity Institution

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers LLP
10 Tenth Street, Northwest
Suite 1400
Atlanta, GA 30309-3851
Telephone (678) 419 1000
Facsimile (678) 419 1239
www.pwc.com

Report of Independent Auditors

To the Board of Trustees of The University of Alabama:

In our opinion, the financial statements listed in the accompanying table of contents, which collectively comprise the financial statements of The University of Alabama in Huntsville (the "University"), a campus of The University of Alabama System, which is a component unit of the State of Alabama, present fairly, in all material respects, the respective financial position of the University and its discretely presented component unit at September 30, 2006 and 2005, and the respective changes in financial position and cash flows, as applicable, for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the University's management. Our responsibility is to express opinions on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions.

As discussed in Note 1, the financial statements of the University are intended to present the net assets, changes in net assets and the cash flows of only that portion of the business-type activities of the financial reporting entity of The University of Alabama System that is attributable to the transactions of the University. They do not purport to, and do not, present fairly the net assets of The University of Alabama System as of September 30, 2006 and 2005 and its changes in net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 3 through 12 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted primarily of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

PricewaterhouseCoopers LLP

March 14, 2007

The University of Alabama in Huntsville

Management's Discussion and Analysis (Unaudited)

This section of The University of Alabama in Huntsville (the University) annual financial report presents a discussion and analysis of the financial performance of the University during the fiscal years ended September 30, 2006 and 2005. This discussion has been prepared by University management and should be read in conjunction with the financial statements and the related footnotes. The financial statements, footnotes and this discussion are the responsibility of University management.

Introduction

The University is a public research university that offers 62 degree-granting programs that meet the highest standards of excellence, including 35 bachelor's degree programs, 17 master's degree programs, and 10 Ph.D. programs through its five colleges: Administrative Science, Liberal Arts, Engineering, Nursing, and Science. The University is an autonomous campus within The University of Alabama System (the System).

The University received $94.3 million for externally funded projects during fiscal year 2006. Sponsors of research include federal and state agencies, academic institutions, industry and private foundations. Research is conducted within the individual colleges and through the University's 19 independent research centers, laboratories and institutes. Major interdisciplinary research thrusts include: optics; propulsion; space physics and astrophysics; earth system science; information technology; microgravity and materials; modeling and simulation; biotechnology; nanotechnology; and systems engineering.

Located at the southern edge of the Appalachian Mountains, Huntsville is a national center of aerospace and high technology research and development. It is home to the National Aeronautical and Space Administration's Marshall Space Flight Center, the U.S. Army Aviation and Missile Command, and the U.S. Army Space and Strategic Defense Command. The University is strategically located in Cummings Research Park, the second largest university research park in the United States and home to numerous high technology and research companies.

Financial and Enrollment Highlights

- Total net assets increased $53.3 million. The increase is primarily due to capital gifts and grants of $31.7 million, and a legal settlement of $20.4 million.

- The total of full time equivalent students increased 0.5% compared to last year. UAH also had a 0.1% increase in the total number of students attending in the fall semester.

Equivalent Full-time Student Enrollment (FTE)

	2002	2003	2004	2005	2006
Undergraduate	3894	4142	4283	4409	4456
Graduate	805	855	798	729	709
Total	**4699**	**4997**	**5081**	**5138**	**5165**

FTE calculated using ACHE formula; Undergraduate credit hour production (chp)/15; graduate I chp/12; graduate II chp/9.

Historical Fall Headcount by Earned Hours

	2002	2003	2004	2005*	2006*
Graduates	1447	1570	1513	1394	1372
Seniors	1335	1327	1398	1727	1709
Juniors	1034	1106	1114	1264	1186
Sophomores	945	972	1063	1125	1052
Freshmen	1310	1484	1472	1545	1701
Others	974	592	476	29	71
Total	**7045**	**7051**	**7036**	**7084**	**7091**

* Due to Banner conversion, class level is calculated differently. Students formerly classified as "Others" are now included in class level based on hours earned. "Others" in Fall 2005 and 2006 are second bachelor's students only.

Degrees Conferred

	2002	2003	2004	2005	2006
Bachelor's	735	807	810	798	816
Master's	269	258	379	374	343
Doctorate	34	21	31	39	31
Certificate	11	17	16	31	39
Total	**1049**	**1103**	**1236**	**1242**	**1229**

- Approximately $43.3 million in appropriations for operations were received from the State of Alabama for fiscal year 2006. In comparison to the prior year, appropriations increased 12.4% or $4.8 million.

Statement of Net Assets

The statement of net assets presents the assets, liabilities, and net assets of the University as of the end of the fiscal year. The purpose of the statement of net assets is to present a fiscal snapshot of the University to the readers of the financial statements. The statement of net assets presents end-of-year data concerning assets (current and noncurrent), liabilities (current and noncurrent), and net assets (assets minus liabilities).
The statement of net assets provides a summary of assets available to continue the operations of the University. The statement also shows how much the University owes vendors, investors and lending institutions. Finally, the statement of net assets provides a picture of the net assets and the availability for expenditure by the University.

Net assets are divided into three major categories. The first category, **invested in capital assets, net of related debt**, provides the University's equity in property, plant and equipment owned by the University. The second asset category is **restricted net assets**, which is divided into two categories, nonexpendable and expendable. The corpus of nonexpendable restricted resources, as it pertains to endowments, is only available for investment purposes. Donors have primarily restricted income derived from these investments to fund scholarships and fellowships. Expendable restricted net assets are available for expenditure by the University but must be spent for purposes as determined by donors or external entities that have placed a purpose restriction on the use of the assets. The final category is **unrestricted net assets**, which are available to the University for any lawful purpose of the University. Many of the University's unrestricted net assets have been designated or reserved for specific purposes such as: repairs and replacement of equipment, capital projects, future debt service, quasi-endowments, insurance reserves, research centers and instructional departments.

A summarized comparison of the University's assets, liabilities, and net assets follows:

Summary of Statements of Net Assets

	2006	2005	2004
Current assets	$ 71,849,951	$ 55,145,932	$ 45,507,127
Noncurrent assets:			
Endowment, life income and other investments	50,313,001	41,988,273	49,568,127
Capital assets, net	161,158,416	133,214,803	119,403,232
Legal settlement receivable	6,718,392	-	-
Other	2,420,293	2,373,284	2,498,541
Total assets	292,460,053	232,722,292	216,977,027
Current liabilities	39,851,725	31,934,264	24,950,674
Noncurrent liabilities	56,671,000	58,176,000	60,046,000
Total liabilities	96,522,725	90,110,264	84,996,674
Net assets			
Invested in capital assets, net of related debt	105,519,987	75,910,726	71,680,503
Restricted	7,625,669	7,737,275	7,412,483
Unrestricted	82,791,672	58,964,027	52,887,367
Total net assets	**$ 195,937,328**	**$ 142,612,028**	**$131,980,353**

For the year ending September 30, 2006, the University's current assets increased $16.7 million primarily due to receivables related to grants and contracts. Endowment, life income and other investments increased $8.3 million. The majority of this increase is the result of an endowment established by the University with the proceeds of a legal settlement. Capital assets, net of depreciation, increased $27.9 million primarily due to the construction of the Applied Sciences Building. The legal settlement receivable of $6.7 million is the net present value of an amount to be received in future years. Current liabilities increased $7.9 million. The majority of this increase stems from construction on the Applied Sciences Building. Noncurrent liabilities decreased $1.5 million, the result of bond principal payments.

For the year ending September 30, 2005, the University's current assets increased $9.6 million primarily due to an increase in investments and receivables. Endowment, life income and other investments decreased $7.6 million. The majority of this decrease was the result of unspent bond proceeds from the prior fiscal year. Capital assets, net of depreciation, increased $13.8 million primarily due to the construction of North Campus Residence Hall and the Applied Sciences Building. Current liabilities increased $7.0 million. This increase, in part, was the result of a payroll accrual. Also contributing to the increase were construction payables for the Applied Sciences Building totaling $1.4 million, and an increase of $1.0 million in deferred revenues. Deposits held for others, also classified as current liabilities, increased $2.5 million. Noncurrent liabilities decreased $1.9 million, the result of bond principal payments.

For the year ending September 30, 2006, the University's total net assets increased 37.4%. The University's investments in capital assets, net of related debt, increased approximately $29.6 million primarily due to capital gifts and grants. Restricted net assets decreased $111,606. Unrestricted net assets increased approximately $23.8 million primarily due to a legal settlement of $20.4 million. Although unrestricted net assets are not subject to externally imposed stipulations, substantially all of the University's unrestricted net assets have been designated for capital projects, as well as various academic and research programs and initiatives.

For the year ending September 30, 2005, the University's total net assets increased 8.1%. The University's investments in capital assets, net of related debt, increased approximately $4.2 million primarily due to capital gifts and grants. The increase in restricted net assets of $324,792 reflected the increase in market value of investments held for endowment purposes. Unrestricted net assets increased approximately $6.1 million primarily due to budget savings in departmental and general university accounts, and various revenue sources exceeding budget projections. Although unrestricted net assets are not subject to externally imposed stipulations, substantially all of the University's unrestricted net assets were designated for capital projects, as well as, various academic and research programs and initiatives.

Capital Assets

At September 30, 2006 and 2005, the University had approximately $295.8 million and $258.8 million invested in capital assets and accumulated depreciation of $134.7 million and $125.6 million, respectively. Depreciation charges for fiscal year 2006 and 2005 were $9.7 million and $9.1 million, respectively.

The following table summarizes the University's capital assets, net of accumulated depreciation, as of September 30:

Capital Assets, Net

	2006	2005	2004
Land	$ 3,076,864	$ 2,993,418	$ 2,981,802
Land improvements and infrastructure, net	1,253,828	696,515	900,511
Buildings and building improvements, net	137,419,186	109,347,973	97,934,211
Equipment, net	12,399,487	13,598,854	12,345,221
Library books, net	4,793,908	4,501,334	4,372,722
Computer software	2,215,143	2,076,709	868,765
Total capital assets, net	**$ 161,158,416**	**$ 133,214,803**	**$ 119,403,232**

Major capital expenditures during the year ended September 30, 2006, included the construction of the Applied Sciences Building and the completion of the Fraternity & Sorority houses. Funding for these projects was provided by a combination of federal sources, private gifts and University resources.

Major capital expenditures during the years ended September 30, 2005 and 2004, respectively, included the construction of North Campus Residence Hall Phase 2 and the Applied Sciences Building. Funding for these projects was provided by a combination of federal sources, private gifts and University resources.

Additional information about the University's capital assets is presented in Note 5 to the financial statements.

Long-Term Debt

The following table summarizes outstanding long-term debt by type, as of September 30:

Long-Term Debt

	2006	2005	2004
Bonds	$ 58,666,000	$ 60,046,000	$ 61,876,000
Total debt outstanding	**$ 58,666,000**	**$ 60,046,000**	**$ 61,876,000**

Principal and interest on these revenue bonds are collateralized by a pledge of revenues produced by student housing and student tuition and fees.

Statement of Revenues, Expenses, and Changes in Net Assets

Changes in total net assets as presented on the statement of net assets are based on the activity presented in the statement of revenues, expenses, and changes in net assets, which presents the University's results of operations. The purpose of the statement is to present the revenues received by the University, both operating and nonoperating, and expenses paid by the University, operating and nonoperating, and any other revenues, expenses, gains and losses received or expended by the University. Annual state appropriations are considered nonoperating revenues according to generally accepted accounting principles, while the funds are used to support the operations of the University.

A summarized comparison of the University's revenues, expenses and changes in net assets is as follows:

Summary of Statements of Revenues, Expenses, and Changes in Net Assets

	2006	2005	2004
Operating revenues:			
Tuition and fees	$ 35,788,029	$ 34,497,632	$ 31,997,670
Less: scholarship allowances	(8,161,802)	(7,683,494)	(7,283,473)
Tuition and fees, net	27,626,227	26,814,138	24,714,197
Federal, state and private grants and contracts	59,453,587	55,334,316	50,552,812
Sales and services of educational departments	1,490,755	2,754,994	2,606,536
Auxiliary, net of $284,504 in 2006 and $272,182 in 2005 of scholarship allowances	4,965,498	5,195,915	4,593,743
Total operating revenue	93,536,067	90,099,363	82,467,288
Operating expenses	140,825,812	127,823,831	117,287,825
Operating loss	(47,289,745)	(37,724,468)	(34,820,537)
Nonoperating revenues (expenses):			
State appropriations	43,292,282	38,516,070	37,430,572
Private gifts	3,115,836	2,684,513	2,391,172
Net investment income	4,933,857	4,369,339	4,647,883
Loss on disposal of capital assets	(149,670)	(57,169)	(49,820)
Interest expense	(2,695,679)	(2,707,938)	(2,289,260)
Capital gifts and grants	31,698,914	5,551,328	618,383
Legal settlement	20,419,505	-	-
Net nonoperating revenues	100,615,045	48,356,143	42,748,930
Increase in net assets	53,325,300	10,631,675	7,928,393
Net assets, beginning of year	142,612,028	131,980,353	124,051,960
Net assets, end of year	**$ 195,937,328**	**$ 142,612,028**	**$ 131,980,353**

The following is a summary of revenues by source (both operating and nonoperating), which are used to fund the University's operating activities. Significant recurring sources of the University's revenues, such as state appropriations, are considered nonoperating, as defined by GASB Statement No. 35

Revenue Sources

	2006		2005		2004	
State appropriations	$43,292,282	22.0%	$38,516,070	27.3%	$37,430,572	29.3%
Net investment income	4,933,857	2.5%	4,369,339	3.1%	4,647,883	3.6%
Grants and contracts	59,453,587	30.2%	55,334,316	39.2%	50,552,812	39.6%
Gifts	3,115,836	1.6%	2,684,513	1.9%	2,391,172	1.9%
Auxiliary	4,965,498	2.6%	5,195,915	3.7%	4,593,743	3.6%
Net tuition and fees	27,626,227	14.0%	26,814,138	19.0%	24,714,197	19.4%
Sales and services	1,490,755	0.7%	2,754,994	1.9%	2,606,536	2.1%
Capital gifts and grants	31,698,914	16.1%	5,551,328	3.9%	618,383	0.5%
Legal settlement	20,419,505	10.3%	-	0%	-	0%
Total revenues	**$196,996,461**		**$141,220,613**		**$127,555,298**	

Grants and contracts increased $4.1 million and $4.8 million in fiscal year ended September 30, 2006 and 2005, respectively, primarily due to an increase in Federal grants and contracts related to research projects. Capital gifts and grants increased $26.1 million and $4.9 million in fiscal year ended September 30, 2006 and 2005, respectively, primarily the result of a large construction grant for the Applied Sciences Building. The University reached an amicable settlement in a legal dispute regarding a research patent, resulting in revenue of $20.4 million for the fiscal year ending September 30, 2006.

The University receives grant and contract revenue from federal, state and local governments and private agencies. These funds are used to further the mission of the University: research, education, and public service. These funds were received in exchange for services performed and are recorded as operating revenues. The chart reflects the funding sources for federal operating grant and contract revenue:

Detail of Federal Grants & Contracts Revenue

	2006	2005	2004
National Aeronautics and Space Administration	$ 21,325,256	$ 21,571,580	$ 21,729,063
Department of Defense	18,947,642	16,574,411	12,847,264
National Science Foundation	3,380,912	3,744,050	3,076,057
Department of Education	4,270,366	4,020,390	4,006,614
Other	2,877,233	4,167,810	4,368,795
Total	**$ 50,801,409**	**$ 50,078,241**	**$ 46,027,793**

Department of Defense revenues increased approximately $2.4 million and $3.7 million in fiscal year ended September 30, 2006 and 2005, respectively, primarily due to an increase in Army contracts.

The following is a comparison of the University's operating expenses:

Operating expenses (by functional classification)

	2006	2005	2004
Instruction	$ 39,527,055	$ 36,873,855	$ 32,868,400
Research	48,592,689	42,234,860	39,485,541
Public service	3,869,161	4,713,340	3,804,260
Academic support	5,691,060	5,022,485	4,383,913
Student services	9,362,320	8,047,676	6,986,483
Institutional support	11,815,202	9,855,414	9,376,108
Operations and maintenance of plant	9,116,318	7,809,192	7,636,922
Scholarships and fellowships	641,399	569,210	583,429
Auxiliary enterprises	2,557,820	3,634,744	3,072,659
Depreciation	9,652,788	9,063,055	9,090,110
Total operating expenses	**$ 140,825,812**	**$ 127,823,831**	**$ 117,287,825**

Operating expenses (by natural classification)

	2006	2005	2004
Compensation and benefits	$ 97,469,425	$ 88,694,854	$ 78,894,920
Supplies and services	33,062,200	29,496,712	28,719,366
Depreciation	9,652,788	9,063,055	9,090,110
Scholarships and fellowships	641,399	569,210	583,429
Total operating expenses	**$ 140,825,812**	**$ 127,823,831**	**$ 117,287,825**

Instruction expense increased $2.7 million and $4.0 million in fiscal year ended September 30, 2006 and 2005, respectively, primarily due to an increase in compensation and benefits.

Research expense increased $6.4 million and $2.7 million in fiscal year ended September 30, 2006 and 2005, respectively, primarily due to an increase in contracts and grants.

Compensation and benefits increased $8.8 million and $9.8 million in fiscal year ended September 30, 2006 and 2005, respectively, primarily due to annual merit based salary increases and increases in health insurance and other benefit costs.

Statement of Cash Flows

The statement of cash flows presents the significant sources and uses of cash. The University's cash, primarily held in demand deposit accounts, is minimized by sweeping available cash balances into investment accounts.

Condensed Statements of Cash Flows

	2006	2005
Cash received from operations	$ 80,166,963	$ 88,186,065
Cash payments for operations	(128,671,485)	(116,862,550)
Net cash used in operating activities	(48,504,522)	(28,676,485)
Net cash provided by noncapital financing activites	60,359,138	43,665,449
Net cash used in capital and related financing activities	(13,761,713)	(21,751,883)
Net cash provided by (used in) investing activities	4,389,761	(6,569,939)
Net increase (decrease) in cash and cash equivalents from other than operating activities	50,987,186	15,343,627
Cash, beginning of year	1,508,066	14,840,924
Cash, end of year	$ 3,990,730	$ 1,508,066

The University used $48.5 million of cash for operating activities in 2006, offset by approximately $60.4 million of cash provided by noncapital financing activities. Similarly, in 2005, $28.7 million of cash used for operating activities was offset by $43.7 million in cash provided by noncapital financing activities. Noncapital financing activities, as defined by the GASB, include state educational appropriations and gifts received for other than capital purposes that are used to support operating expenses.

Cash of $13.8 million and $21.8 million in 2006 and 2005, respectively, was used for capital and related financing activities, primarily for purchases of capital assets and principal and interest payments, partially offset by sources that included bond proceeds, gifts, grants and contracts for capital purposes.

Cash provided by (used in) investing activities totaled $4.4 million in 2006 and $6.6 million in 2005. The differences are primarily a result of additional purchases of investments in 2006 resulting in less cash from investing.

Economic Factors That Will Affect the Future

The University's state appropriations have not kept pace with the amounts recommended by the Alabama Commission on Higher Education (ACHE). For fiscal year 2006, the University was funded at approximately 65.6% of the ACHE funding recommendation.

The University continues to attract federal grant and contract revenue. Over 75% of the University's federal operating revenue comes from two agencies: the National Aeronautical and Space Administration and the Department of Defense. The outcome of the federal budget process has important ramifications for the University's research budget.

The University's achievement in recent years in obtaining private and federal support is a testament to the high regard in which the University is held. The level of support underscores the continued confidence among donors and grantors in the quality of the University's programs and the importance of its mission.

The University must have a balanced array of many categories of facilities to meet its education, research and public service goals and continues to assess its long-term capital requirements. Support for the University's recent capital expenditures has been provided primarily from federal funds, bond issues repaid through student rental and facility fees, and gifts.

FINANCIAL STATEMENTS

THE UNIVERSITY OF ALABAMA IN HUNTSVILLE
STATEMENTS OF NET ASSETS
September 30, 2006 and 2005

	2006	2005
Assets		
Current Assets:		
Cash and cash equivalents	$ 3,470,975	$ 589,965
Operating investments	25,316,957	33,575,108
Accounts receivable, net	39,355,767	17,254,947
Other current assets	3,706,252	3,725,912
Total current assets	71,849,951	55,145,932
Noncurrent Assets:		
Restricted cash and cash equivalents	519,755	918,101
Endowment investments	16,256,349	4,133,252
Investments for capital activities	33,536,897	36,936,920
Capital assets, net	161,158,416	133,214,803
Legal settlement receivable	6,718,392	-
Other noncurrent assets	2,420,293	2,373,284
Total noncurrent assets	220,610,102	177,576,360
Total Assets	**$ 292,460,053**	**$ 232,722,292**
Liabilities and Net Assets		
Current Liabilities:		
Accounts payable and accrued liabilities	$ 21,131,802	$ 13,971,733
Deferred revenues	13,466,390	13,090,307
Current portion of long-term debt	1,995,000	1,870,000
Deposits held for others	3,258,533	3,002,224
Total current liabilities	39,851,725	31,934,264
Noncurrent Liabilities:		
Long-term debt	56,671,000	58,176,000
Total noncurrent liabilities	56,671,000	58,176,000
Total Liabilities	96,522,725	90,110,264
Net Assets:		
Invested in capital assets, net of related debt	105,519,987	75,910,726
Restricted:		
Nonexpendable	1,864,511	1,797,288
Expendable	5,761,158	5,939,987
Unrestricted	82,791,672	58,964,027
Total Net Assets	195,937,328	142,612,028
Total Liabilities and Net Assets	**$ 292,460,053**	**$ 232,722,292**

See accompanying notes to financial statements

UNIVERSITY OF ALABAMA HUNTSVILLE FOUNDATION
DISCRETELY PRESENTED COMPONENT UNIT
STATEMENTS OF FINANCIAL POSITION
September 30, 2006 and 2005

	2006	2005
Assets		
Cash and cash equivalents	$ 1,903,647	$ 1,780,744
Investments	31,198,896	27,709,935
Investment real estate	3,515,208	4,231,817
Accrued interest	181,526	182,167
Mortgages receivable	103,138	116,885
Pledges receivable, net	1,380,840	2,508,551
Collections	219,690	219,690
Land and buildings, net	1,811,887	1,846,378
Total Assets	**$ 40,314,832**	**$ 38,596,167**
Liabilities		
Accounts payable	$ 310,881	$ 282,536
Annuity liability	433,629	446,385
Total Liabilities	744,510	728,921
Net Assets		
Unrestricted net assets	14,381,469	11,835,243
Temporarily restricted net assets	11,811,493	13,307,028
Permanently restricted net assets	13,377,360	12,724,975
Total Net Assets	39,570,322	37,867,246
Total Liabilities and Net Assets	**$ 40,314,832**	**$ 38,596,167**

See accompanying notes to financial statements

THE UNIVERSITY OF ALABAMA IN HUNTSVILLE
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
Years Ended September 30, 2006 and 2005

	2006	2005
Operating Revenues		
Tuition and fees	$ 35,788,029	$ 34,497,632
Less: scholarship allowances	(8,161,802)	(7,683,494)
Tuition and fees, net	27,626,227	26,814,138
Grants and contracts		
Federal	50,801,409	50,078,241
State	3,668,782	967,399
Private	4,983,396	4,288,676
Sales and services of educational departments	1,490,755	2,754,994
Auxiliary, net of $284,504 in 2006 and $272,182 in 2005 of scholarship allowances	4,965,498	5,195,915
Total Operating Revenues	**93,536,067**	**90,099,363**
Operating Expenses		
Compensation and benefits	97,469,425	88,694,854
Supplies and services	33,062,200	29,496,712
Depreciation	9,652,788	9,063,055
Scholarships and fellowships	641,399	569,210
Total Operating Expenses	**140,825,812**	**127,823,831**
Operating loss	(47,289,745)	(37,724,468)
Nonoperating Revenues (Expenses)		
State appropriations	43,292,282	38,516,070
Private gifts	3,115,836	2,684,513
Net investment income	4,933,857	4,369,339
Loss on disposal of capital assets	(149,670)	(57,169)
Interest expense	(2,695,679)	(2,707,938)
Legal settlement	20,419,505	-
Net Nonoperating Revenues	68,916,131	42,804,815
Capital gifts	3,077,197	2,091,559
Capital grants	28,621,717	3,459,769
	100,615,045	**48,356,143**
Increase in net assets	53,325,300	10,631,675
Net Assets, Beginning of Year	142,612,028	131,980,353
Net Assets, End of Year	**$ 195,937,328**	**$ 142,612,028**

See accompanying notes to financial statements

UNIVERSITY OF ALABAMA HUNTSVILLE FOUNDATION
DISCRETELY PRESENTED COMPONENT UNIT
STATEMENTS OF ACTIVITIES
Years Ended September 30, 2006 and 2005

	2006	2005
Changes in net assets		
Revenue, gains, and other support:		
Contributions	$ 1,873,339	$ 3,874,069
In-kind gifts	-	159,300
Rent income	26,799	26,790
Investment income	1,163,126	1,076,799
Unrealized gain/(loss) on investments	171,034	1,453,288
Realized gain/(loss) on sale of investments	3,583,744	872,174
Other income	89,786	27,585
Change in value of split-interest agreement	13,582	(77,767)
Total Revenues	**6,921,410**	**7,412,238**
Expenses:		
Contributions to or in support of UAH	4,087,226	1,322,612
Scholarships to UAH	729,142	697,461
Professional services	155,977	145,429
Depreciation	34,491	34,492
Other expenses	211,498	139,801
Total Expenses	**5,218,334**	**2,339,795**
Change in net assets	1,703,076	5,072,443
Net Assets, Beginning of year	37,867,246	32,794,803
Net Assets, End of Year	**$ 39,570,322**	**$ 37,867,246**

See accompanying notes to financial statements

THE UNIVERSITY OF ALABAMA IN HUNTSVILLE
STATEMENTS OF CASH FLOWS
Years Ended September 30, 2006 and 2005

	2006	2005
Cash Flows from Operating Activities		
Student tuition and fees	$ 28,339,735	$ 26,381,709
Federal grants and contracts	38,921,307	49,125,779
State grants and contracts	2,784,306	949,000
Private grants and contracts	3,781,991	4,207,108
Sales and services of educational and other departmental activities	1,435,771	2,750,124
Auxiliary enterprises	4,903,853	4,772,345
Payments to suppliers	(32,026,137)	(28,456,264)
Payments to employees and related fringes	(96,129,672)	(87,549,804)
Payments for scholarships and fellowships	(515,676)	(856,482)
Net Cash Used in Operating Activities	**(48,504,522)**	**(28,676,485)**
Cash Flows from Capital and Related Financing Activities		
Proceeds from issuance of bonds	8,580,000	-
Principal refinanced	(7,910,000)	-
Bond issuance cost	(670,000)	-
Capital gifts, grants and contracts	23,481,703	4,172,595
Purchase of capital assets	(32,486,878)	(21,542,584)
Principal payments on capital debt	(2,050,000)	(1,830,000)
Interest payments on capital debt	(2,706,538)	(2,551,894)
Net Cash (Used In) Provided by Capital and Related Financing Activities	**(13,761,713)**	**(21,751,883)**
Cash Flows from Investing Activities		
Interest and dividends on investments, net	4,854,684	4,369,339
Proceeds from sales and maturities of investments	43,500,000	46,190,000
Purchase of investments	(43,964,923)	(57,129,278)
Net Cash Used in Investing Activities	**4,389,761**	**(6,569,939)**
Cash Flows from Noncapital Financing Activities		
State educational appropriations	43,292,282	38,516,070
Private gifts	3,115,836	2,684,513
Student direct lending receipts	18,504,394	16,368,381
Student direct lending disbursements	(17,559,683)	(16,441,514)
Amounts received from affiliates	481,212	2,748,429
Amounts paid to affiliates	(224,903)	-
Legal settlement	12,750,000	(210,430)
Net Cash Provided by Noncapital Financing Activities	**60,359,138**	**43,665,449**
Net decrease in cash and cash equivalents	2,482,664	(13,332,858)
Cash and Cash Equivalents, Beginning of Year	1,508,066	14,840,924
Cash and Cash Equivalents, End of Year	**$ 3,990,730**	**$ 1,508,066**

See accompanying notes to financial statements

THE UNIVERSITY OF ALABAMA IN HUNTSVILLE
STATEMENTS OF CASH FLOWS -- Continued
Years Ended September 30, 2006 and 2005

	2006	2005
Reconciliation of Operating Loss to Net Cash Used in Operating Activities		
Operating loss	$ (47,289,745)	$ (37,724,468)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation expense	9,652,788	9,063,055
Changes in allowance for doubtful accounts	(173,570)	48,608
Changes in assets and liabilities:		
Accounts receivable	(13,624,464)	(2,966,962)
Other current assets	19,660	(82,309)
Accounts payable and accrued liabilities	2,520,696	1,975,378
Deferred revenues	376,083	1,005,057
Deposits held for others	14,030	5,156
Net Cash Used in Operating Activities	$ (48,504,522)	$ (28,676,485)
Supplemental Noncash Activities Information		
Loss on disposal of capital assets	$ 149,670	$ 57,169
Gift of capital assets	609,909	-
Capital assets acquired with a liability	7,629,565	2,392,090

See accompanying notes to financial statements

THE UNIVERSITY OF ALABAMA IN HUNTSVILLE
Notes to Financial Statements
Year Ended September 30, 2006

Note 1 – Organization and Summary of Significant Accounting Policies

Financial Reporting Entity - The University of Alabama in Huntsville (the University) is one of three campuses of The University of Alabama System (the System), which is a discretely presented component unit of the State of Alabama. The financial statements of the University are intended to present the financial position, changes in financial position, and the cash flows of only that portion of the business type activities of the financial reporting entity of the System that is attributable to the transactions of the University. The financial statements include individual schools, colleges and departments, and certain affiliated operations determined to be a part of the University's financial reporting entity. The System is recognized as an organization exempt from Federal Income tax under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(3) of the Internal Revenue Code.

Scope of Statements - As of October 1, 2003, the University implemented Governmental Accounting Standards Board (GASB) Statement Number 39, *Determining Whether Certain Organizations are Component Units*. This Statement amends GASB Statement No. 14, *The Financial Reporting Entity*, to provide additional guidance to determine whether certain organizations for which the University is not financially accountable should be reported as component units based on the nature and significance of their relationship with the University.

As defined by generally accepted accounting principles established by the GASB, the financial reporting entity consists of the University, as well as its component unit, the University of Alabama Huntsville Foundation (UAHF).

UAHF is a legally separate, tax-exempt component unit of the University. UAHF is organized exclusively for charitable, scientific, and educational purposes in order to benefit the University. UAHF is governed by a 34-member board of trustees. Although the University does not control the timing or amount of receipts from UAHF, the majority of resources, or income thereon that UAHF holds and invests are restricted to the activities of the University by the donors. Because these restricted resources held by UAHF can only be used by, or for the benefit of, the University, UAHF is considered a component unit of the University. UAHF is reported in separate financial statements because of the difference in its reporting model, as further described below.

UAHF is a not-for-profit organization that reports its financial results under the Financial Accounting Standard Board (FASB) Statements. Most significant to UAHF's operations and reporting model are FASB Statement No.116, *Accounting for Contributions Received and Contributions Made*, and FASB Statement No. 117, *Financial Reporting for Not-for-Profit Organizations,* FASB Statement No. 124, *Accounting for Certain Investments Held by Not-for-Profit Organizations*, and FASB Statement No. 136, *Transfers of Assets to a Not-for-Profit Organization or Charitable Trust That Raises or Holds Contributions for Others*.

As such, certain revenue recognition criteria and presentation features are different from GASB revenue recognition criteria presentation features. No modifications have been made to UAHF's financial information in the University's financial reporting entity for these differences, however significant note disclosures (see note 16) to UAHF's financial statements have been incorporated into the University's notes to the financial statements. During the years ended September 30, 2006 and 2005, UAHF distributed $4,816,368 and $2,020,073 respectively, to or for the University for both restricted and unrestricted purposes. Complete financial statements for UAHF can be obtained by calling 256-824-6503.

The University is also affiliated with the Eminent Scholars Foundation, Alabama Engineering Foundation, UAH Alumni Association and UAH Athletic Association. These entities' resources are not significant to the University; therefore, they do not constitute component units under the provisions of GASB Statement No. 39.

Basis of Accounting: For financial reporting purposes, the University is considered a special-purpose government engaged only in business-type activities as defined by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities,* an amendment of Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. Business-type activities are those that are financed in whole or in part by fees charged to external parties for goods or services. Accordingly, the financial statements of the University have been prepared in accordance with accounting principles generally accepted in the United States of America, including all applicable effective statements of the GASB and all statements of the Financial Accounting Standards Board through November 30, 1989, using the economic measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred.

Net Assets: Net assets are classified into the following four categories according to external donor restrictions or availability of assets for satisfaction of University obligations:

- **Invested in capital assets, net of related debt**: Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction, or improvement of those assets.

- **Restricted**:

  Nonexpendable – Net assets subject to externally imposed stipulations that they be maintained permanently by the University. Such assets include the corpus of the University's permanent endowment funds.

  Expendable – Net assets whose use by the University is subject to externally imposed stipulations that can be fulfilled by actions of the University pursuant to those stipulations or that expire by the passage of time.

- **Unrestricted:** Net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or may otherwise be limited by contractual agreements with outside parties. Substantially all unrestricted net assets are designated for academic, research, and capital programs.

Cash and Cash Equivalents: For purposes of the statement of cash flows, the University considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. Cash equivalents representing assets of the University's endowment, life income, and other long-term investments are included in the noncurrent investments category.

Investments: The University's investments are primarily reported at fair value. The University's investment portfolio is primarily invested in three separate investment pools sponsored by the System. Fair value for the investment pools is provided by the System, based on the fair value of the underlying investment securities held by each investment pool. Fair value of the underlying securities held in each investment pool is based on quoted market prices or dealer quotes, where available, or determined using net asset values provided by underlying investment partnerships or companies, which primarily invest in readily marketable securities. Certain real estate and non-readily marketable securities held in the System sponsored endowment investment pool are carried at cost. Fair value for investments held by the University is determined from quoted market prices or market prices of similar instruments. Net investment income, including realized and unrealized gains and losses, is reported as nonoperating revenues (expenses) in the statements of revenues, expenses and changes in net assets.

Accounts Receivable: Accounts receivable consist primarily of tuition and fees charged to students, amounts due from the federal government, state and local governments, or private sources, in connection with reimbursement of allowable expenditures made pursuant to the University's contracts and grants, and amounts due related to a legal settlement. Accounts receivable are recorded net of estimated uncollectible amounts; the legal settlement receivable is recorded at net present value as the term is greater than one year.

Capital Assets: Capital assets are recorded at cost at the date of acquisition, or fair value at date of donation in the case of gifts, less accumulated depreciation. For equipment, the University's capitalization policy includes all items with a unit cost of $5,000 or more and an estimated useful life of greater than one year. Renovations to buildings, infrastructure and land improvements that significantly increase the value or extend the useful life of the structure are capitalized. Routine repairs and maintenance are charged to operating expense in the year in which the expense was incurred. The University capitalizes certain software and development costs associated with obtaining and developing internal-use computer software. Implementation costs include consulting expenses and allocation of internal salaries and fringes for the core implementation team. Training costs are expensed as incurred.

Capital assets acquired through federal grants and contracts where the federal government retains a reversionary interest are capitalized and depreciated. Interest costs, net of any related investment earnings, for certain assets acquired with the proceeds of tax-exempt borrowings are capitalized as a component of the cost of acquiring those assets.

Depreciation of buildings and building improvements (5-50 years), land improvements and infrastructure (10 years), library collection (10 years), computer software (10 years) and inventoried equipment (5-8 years) is computed on a straight-line basis. The University computes depreciation for certain buildings and building improvements using a componentized method

Deferred Revenues: Deferred revenues consist primarily of amounts received for fall student tuition and fees that are not earned until the next fiscal year. Deferred revenues also include amounts received from grant and contract sponsors that have not yet been earned.

Revenues: The University's policy for defining operating activities as reported on the statement of revenues, expenses, and changes in net assets are those that generally result from exchange transactions such as payments received for providing services and payments made for services or goods received. Nearly all of the University's operating revenues are from exchange transactions. Certain significant revenue streams relied upon to support operations are recorded as nonoperating revenues, as defined by GASB Statement No. 35, including state appropriations, gifts and investment income.

Auxiliary enterprise revenues are primarily generated by University Housing.

Revenues received for capital activities are considered neither operating nor nonoperating activities, and are presented after nonoperating activities on the accompanying statement of revenues, expenses, and changes in net assets.

Contract and grant revenue: The University receives contract and grant revenue from governmental and private sources. The University recognizes revenue associated with the sponsored programs in accordance with GASB Statement No. 33, based on the terms of the individual contract or grant.

Scholarship Allowances and Student Aid: Scholarship allowances applied to student accounts are recorded as an offset to student tuition and fees and auxiliary revenue. Payments of financial aid made directly to students continue to be classified as scholarship and fellowship expenses.

Internal Sales Activities: All internal sales activities to the University departments from sales and service units (motor pool, postal services, telecommunications, etc.) have been eliminated in the accompanying financial statements.

Compensated Absences: The University accrues annual leave for employees at rates based upon length of service and job classification and compensatory time based upon job classification and years worked.

Endowment Spending: For donor restricted endowments, the Uniform Management of Institutional Funds Act, as adopted in Alabama, permits The Board of Trustees of the University of Alabama (the Board) to appropriate an amount of realized and unrealized endowment appreciation as the Board determines to be prudent. The University's policy is to retain the endowment realized and unrealized appreciation within the endowment after the spending rate distributions. The Board approved a spending rate for the fiscal years ended September 30, 2006 and 2005 of 5.0% of a moving three-year average of the market (unit) value

Use of Estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Note 2 - Cash

The Board approves, by resolution, all banks or other financial institutions utilized as depositories for University funds. Prior to approval, each proposed depository must provide evidence of its designation by the Alabama State Treasurer as a qualified public depository under the Security of Alabama Funds Enhancement Act (SAFE). From time to time, the Board may request that the depository provide evidence of its continuing designation as a qualified public depository. The enactment of the SAFE program changed the way all Alabama public deposits are collateralized. In the past, the bank pledged collateral directly to each individual public entity. Under the mandatory SAFE program, each qualified public depository (QPD) is required to hold collateral for all its public depositories on a pooled basis in a custody account established for the State Treasurer as SAFE administrator. In the unlikely event a public entity should suffer a deposit loss due to QPD insolvency or default, a claim form would be filed with the State Treasurer who would use the SAFE pool collateral or other means to reimburse the loss.

As of September 30, 2006 and 2005, the University had cash and cash equivalents totaling $3,990,730 and $1,508,066, respectively. Included in the amounts are deposits with trustees held for reserves, which totaled $519,755 in 2006 and $399,342 in 2005.

Note 3 – Investments

The University invests its endowment funds in accordance with applicable limitations set forth in gift instruments, Board guidelines, or applicable laws. Also certain bond indentures require the University to invest the amounts held in specific construction funds, redemption funds, and bond funds in federal securities, eligible certificates, or eligible investments.

At September 30, 2006 and 2005, the University's investments included custodial credit risk category I investments (investments that are insured or registered, or securities held by the University or its agent in the University's name) and other investments not categorized by risk category as follows:

	2006	2005
Category I:		
Time deposits	$ 127,382	$ 125,375
Not categorized:		
Mutual funds	51,658	50,192
Short Term Fund	87,816	3,091,616
Intermediate Fund	21,203,258	33,027,882
Prime Fund	34,556,939	31,502,867
Endowment Fund	16,256,349	4,133,252
Agency Funds	2,826,801	2,714,096
Total Investments	$ 75,110,203	$ 74,645,280

The Board of Trustees of the University of Alabama (the "Board") has the responsibility for the establishment of the investment policy and the oversight of the investments for the various System and related entities. In order to facilitate system-wide investment economies and objectives, the Board has established four distinct investment pools based primarily on the projected investment time-horizons for cash reserves. These investment pools are the Endowment Fund, Prime Fund, Intermediate Fund and the Short-Term Fund. Pursuant to Board investment policies, each System or related entity may include all or a portion of their investments within the System-sponsored investment pools. These investment funds are considered 'internal' investment pools under GASB Statement No. 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools," with the assets pooled on a market value basis. Separately managed funds that are resident on each campus are to be invested consistent with the asset mix of the corresponding System investment pool. The University has no separately managed funds at September 30, 2006 and 2005.

Endowment Fund: The purpose of the Endowment Fund is to pool endowment and similar funds to support the System campuses, hospital and related entities in carrying out their respective missions over an indefinite time frame. Accordingly, the primary investment objectives of the Endowment Fund are to preserve the purchasing power of the principle and provide a stable source of perpetual financial support. To satisfy the long-term rate of return objective, the Endowment Fund relies on a total return strategy in which investment returns are achieved through both capital appreciation and natural income. Asset allocations are established to meet targeted returns while providing adequate diversification in order to minimize investment volatility. Of the $16,256,349 invested by the University in 2006, $4,011,962 is donor restricted. Of the $4,133,252 invested by the University in 2005, $3,711,127 is donor restricted.

Prime Fund: The Prime Fund is a longer-term fund used as a source of funds to meet projected cash reserve needs over a period of seven to ten years. This fund has an investment objective of growth through income and is invested in a diversified asset mix of liquid and semi-liquid securities. Long-term lockup funds with illiquid assets are inappropriate investments for this fund.

Intermediate Fund: The Intermediate Fund serves as a source of funds to meet projected cash reserve needs over a two to six year period. This fund is also used to balance the other funds when looking at the System's entire asset allocation of cash reserves relative to its investment objectives. The Intermediate Fund has an investment objective of income with preservation of capital and is invested in intermediate term fixed income securities. At least one of the investment managers must be a large mutual fund providing daily liquidity.

Short-Term Fund: The Short-Term Fund contains the short-term cash reserves of the various System entities. Because of the different income and disbursement requirements of each campus, consolidation of these funds reduces daily cash fluctuations and minimizes the amount of short-term cash reserves needed. Assets held in the Short-Term Fund are invested with the primary objective of stability of principal and liquidity. Such investments are restricted to high quality, liquid, money market funds and other fixed income obligations with a maturity of one year or less.

Although the investment philosophy of the Board is to minimize the direct ownership of investment vehicles, preferring ownership in appropriate investment fund groups, there are certain direct investments that are held in the name of the Board. All other in the System Pools are classified as commingled funds.

The composition of the System's investments, by investment type, at September 30, 2006 and 2005 is as follows:

	Endowment Fund		Prime Fund		Intermediate Fund		Short Term Fund	
	2006	2005	2006	2005	2006	2005	2006	2005
Cash and Receivables:								
Cash	$ -	$ 1,011,107	$ (952)	$ 17,507	$ 12,503	$ -	$ -	$ -
Accrued Income Receivables	981,140	975,095	914,319	559,496	2,267,460	1,877,554	-	-
Total Cash & Receivables	981,140	1,986,202	913,367	577,003	2,279,963	1,877,554	-	-
Cash and Equivalents:								
Commercial Paper	-	-	-	-	13,748,821	9,855,000	-	-
Treasury Bills	-	-	-	-	-	-	-	-
Money Market Funds	7,574,688	9,105,229	6,633,396	8,381,106	8,434,541	18,673,245	-	-
Total Cash & Equivalents	7,574,688	9,105,229	6,633,396	8,381,106	22,183,362	28,528,245	-	-
Equities:								
Common Stock	123,226,310	130,665,163	158,268,913	108,768,522	-	-	-	-
Total Equities	123,226,310	130,665,163	158,268,913	108,768,522	-	-	-	-
Fixed Income Securities:								
U.S. Government Obligations	16,359,318	13,447,557	18,806,639	19,114,820	65,619,783	31,940,657	-	-
Mortgage Backed Securities	3,069,336	11,742,454	9,057,376	16,241,626	39,269,785	31,995,079	-	-
Collateralized Mortgages	8,254,290	-	8,165,028	-	61,062,777	162,260,168	-	-
Corporate Bonds	9,740,519	10,375,216	11,933,901	14,385,448	158,852,908	81,317,880	-	-
Foreign Bonds	-	-	-	-	1,426,864	4,620,889	-	-
Total Fixed Income Securities	37,423,463	35,565,227	47,962,944	49,741,894	326,232,117	312,134,673	-	-
Commingled Funds:								
U.S. Equity Funds	278,168,873	253,692,939	140,886,041	167,310,710	-	-	-	-
Non-U.S. Equity Funds	149,893,182	122,522,440	49,545,096	103,392,044	-	-	-	-
U.S. Bond Funds	121,167,857	75,149,275	187,554,297	120,190,770	8,748,701	48,931,227	85,805,856	136,905,991
Hedge Funds	73,778,807	71,679,148	64,690,006	51,030,321	-	-	-	-
Private Equity Funds	20,670,307	18,860,126	-	-	-	-	-	-
Timberland Funds	10,000,141	11,826,958	-	-	-	-	-	-
Real Estate Funds	5,899,508	12,263,142	-	-	-	-	-	-
Total Commingled Funds	659,578,675	565,994,028	442,675,440	441,923,845	8,748,701	48,931,227	85,805,856	136,905,991
Total Fund Investments	827,803,136	741,329,647	655,540,693	608,815,367	357,164,180	389,594,145	85,805,856	136,905,991
Total Fund Assets	828,784,276	743,315,849	656,454,060	609,392,370	359,444,143	391,471,699	85,805,856	136,905,991
Total Fund Liabilities	(215,789)	(223,485)	(204,829)	(238,494)	(370,639)	(209,221)	-	-
Affiliated Entity Investments in Funds	(87,266,923)	(80,114,158)	-	-	-	-	-	-
Total Net Asset Value	$ 741,301,564	$ 662,978,206	$ 656,249,231	$ 609,153,876	$ 359,073,504	$ 391,262,478	$ 85,805,856	$ 136,905,991

Investment Risk Factors: There are many factors that can affect the value of investments. Some, such as custodial credit risk, concentration of credit risk and foreign currency risk, may affect both equity and fixed income securities. Equity securities respond to such factors as economic conditions, individual company earnings performance and market liquidity, while fixed income securities are particularly sensitive to credit risks and changes in interest rates.

Credit Risk: Fixed income securities are subject to credit risk, which is the chance that a bond issuer will fail to pay interest or principal in a timely manner, or that negative perceptions of the issuer's ability to make these payments will cause security prices to decline. These circumstances may arise due to a variety of factors such as financial weakness, bankruptcy, litigation, and/or adverse political developments. Certain fixed income securities, primarily obligations of the U.S. government or those explicitly guaranteed by the U.S. government, are not considered to have credit risk.

A bond's credit quality is an assessment of the issuer's ability to pay interest on the bond, and ultimately, to pay the principal. Credit quality is evaluated by one of the independent bond-rating agencies, for example Moody's Investors Service (Moody's) or Standards and Poor's (S&P). The lower the rating, the greater the chance—in the rating agency's opinion—that the bond issuer will default, or fail to meet its payment obligations. Generally, the lower a bond's credit rating, the higher its yield should be to compensate for the additional risk.

Board policy recognizes that a limited amount of credit risk, properly managed and monitored, is prudent and provides incremental risk adjusted return over its benchmark. Credit risk in each investment pool is managed primarily by diversifying across issuers and limiting the amount of portfolio assets that can be invested in non-investment grade securities. Fixed income holdings in a single entity (excluding obligations of the U.S. government and its agencies) may not exceed 6% of a manager's portfolio measured at market value. At least 95% of these fixed income investments must be in investment grade securities (securities with ratings of BBB- or Baa3) or higher. However, multi-strategy fixed income managers may have up to 20% of their investments in non-investment grade securities. Securities of foreign entities either dominated in U.S. dollars or other currencies shall be limited to 20% of a manager's portfolio.

The System's investment policy recognizes that credit risk is appropriate in balanced investment pools such as the Endowment and Prime Funds, which are tracked against the Lehman Aggregate Index benchmark for the fixed income portion of these pools. For the Endowment Fund, 15% of the fund is committed to fixed income investments, of which, 5% are actively managed. For the Prime Fund, 30% of the fund is invested in fixed income securities, of which, 20% are actively managed. Fixed income investments within the Endowment and Prime Funds include corporate, mortgage backed, asset backed and U.S. treasury and/or agency bonds with a minimum BBB- rating and an average duration of four years. In addition, approximately $29,000,000 and $26,000,000 at September 30, 2006 and 2005 is invested in unrated fixed income securities. Commingled funds were $323,000,000 and $213,000,000 at September 30, 2006 and 2005, respectively.

The Intermediate Fund is benchmarked against the Lehman 1-3 Government Index with funds invested with three separate fund managers. Fixed income investments include corporate, mortgage backed, asset backed, collateralized mortgage and U.S. treasury and/or agency bonds with an average duration of 1.73 years and a minimum rating of BB or higher. For September 30, 2006 and 2005, $53,000,000 and $73,000,000, respectively, were invested in unrated fixed securities.

The Short-Term Fund is committed to immediate liquidity to meet the operating needs of the campuses and hospital. These funds are invested in a bank sponsored common/collective trust fund, which in turn invests in money market, corporate, mortgage backed, asset backed and U.S. treasury and/or agency securities. These funds are all commingled with other investors.

The credit risk for fixed and variable income securities, for the System Pools, at September 30, 2006 and 2005 are as follows:

	Endowment Fund		Prime Fund		Intermediate Fund		Short Term Fund	
	2006	2005	2006	2005	2006	2005	2006	2005
Fixed or Variable Income Securities								
U.S. Government Guaranteed	$ 16,359,318	$ 13,447,557	$ 18,806,639	$ 19,114,820	$ 65,619,783	$ 31,940,657	$ -	$ -
Other U.S. Denominated								
AAA	499,000	1,493,845	499,000	1,999,455	119,590,000	119,010,472	-	-
AA	1,191,000	2,010,900	1,752,000	3,791,378	28,772,000	39,696,871	-	-
A	6,139,000	6,203,748	6,514,000	6,984,790	44,855,000	28,954,121	-	-
BBB	1,688,000	1,656,413	3,170,000	2,599,515	10,603,000	15,384,932	-	-
BB	-	-	-	-	-	3,843,808	-	-
B	-	-	-	-	3,464,000	-	-	-
Unrated	11,547,145	10,752,764	17,221,305	15,251,936	53,328,334	73,303,812	-	-
Commingled Funds								
U.S. Bond Funds Unrated	121,167,857	75,149,275	187,554,297	120,190,770	8,748,701	48,931,227	85,805,856	136,905,991
Money Market Funds Unrated	7,574,688	9,105,229	6,428,567	8,381,106	8,434,541	18,673,245	-	-
Commercial Paper Unrated	-	-	-	-	13,748,821	9,855,000	-	-
TOTAL	$ 166,166,008	$ 119,819,731	$ 241,945,808	$ 178,313,770	$ 357,164,180	$ 389,594,145	$ 85,805,856	$ 136,905,991

Custodial Credit Risk: Custodial credit risk is the risk that in the event of the failure of the custodian, the System's investment securities may not be returned. Investment securities in the System sponsored investment pools are registered in the Board's name by the custodial bank as an agent for the System. Other types of investments (i.e. open-ended mutual funds, common/collective trusts) represent ownership interests that do not exist in physical or book-entry form. As a result, custodial credit risk is remote.

Concentration of Credit Risk: Concentration of credit risk is the risk associated with a lack of diversification, such as having substantial investments in a few individual issuers, thereby exposing the organization to greater risks resulting from adverse economic, political, regulatory, geographic, or credit developments.

As previously mentioned, credit risk in each investment pool is managed primarily by diversifying across issuers and limiting the amount of portfolio assets that can be invested in non-investment grade securities. As of September 30, 2006 and 2005, there was no investment in a single issuer that represents 5% or more of total investments.

Interest Rate Risk: Interest rate risk is the risk that the value of fixed income securities will decline because of changing interest rates. The prices of fixed income securities with a longer time to maturity, measured by effective duration, tend to be more sensitive to changes in interest rates and, therefore, more volatile than those with shorter durations. Effective duration is the approximate change in price of a security resulting from a 100 basis point (1 percentage point) change in the level of interest rates. It is not a measure of time. The Board does not have a specific policy relative to interest rate risk. As such, there are no restrictions on weighted average maturity for each portfolio as they are managed relative to the investment objectives and liquidity demands of the investors.

The effective durations for fixed or variable income securities, for the System Pools, at September 30, 2006 and 2005 are as follows:

	Endowment Fund		Prime Fund		Intermediate Fund		Short Term Fund	
	2006	**2005**	**2006**	**2005**	**2006**	**2005**	**2006**	**2005**
U.S. Government Obligations	5.7	6.9	5.8	6.3	1.7	1.5	-	-
Collateralized Mortgages	-	-	-	-	1.6	9.7	-	-
Corporate Bonds	4.7	3.6	5.0	2.8	2.5	7.3	-	-
Commingled Bond Funds	5.2	4.5	4.9	4.5	1.9	1.8	-	-

The information presented does not take into account the relative weighting of the portfolio components to the total portfolio.

Investments may also include mortgage pass through securities and collateralized mortgage obligations that may be considered to be highly sensitive to changes in interest rates due to the existence of prepayment or conversion features. At September 30, 2006 and 2005 the fair market value of these investments for the System Pools, are as follows:

	Endowment Fund		Prime Fund		Intermediate Fund		Short Term Fund	
	2006	**2005**	**2006**	**2005**	**2006**	**2005**	**2006**	**2005**
Mortgage Backed Securities	$ 3,069,336	$ 11,742,454	$ 9,057,376	$ 16,241,626	$ 39,269,785	$ 31,995,079	$ -	$ -
Collateralized Mortgage Obilgations	8,254,290	-	8,165,028	-	61,062,777	162,260,168	-	-
Total Fixed	$11,323,626	$ 11,742,454	$17,222,404	$ 16,241,626	$ 100,332,562	$194,255,247	$ -	$ -

Mortgage Backed Securities: These securities are issued by the Federal National Mortgage Association (Fannie Mae), Government National Mortgage Association (Ginnie Mae) and Federal Home Loan Mortgage Association (Freddie Mac) and include short embedded prepayment options. Unanticipated prepayments by the obligees of the underlying asset reduce the total expected rate of return.

Collateralized Mortgage Obligations: Collateralized mortgage obligations (CMOs) generate a return based upon either the payment of interest or principal on mortgages in an underlying pool. The relationship between interest rates and prepayments makes the fair value highly sensitive to changes in interest rates. In falling interest rate environments, the underlying mortgages are subject to a higher propensity of prepayments. In a rising interest rate environment, the opposite is true.

At September 30, 2006 and 2005, the effective durations for these securities are as follows:

	Endowment Fund		Prime Fund		Intermediate Fund		Short Term Fund	
	2006	**2005**	**2006**	**2005**	**2006**	**2005**	**2006**	**2005**
Mortgage Backed Securities	3.4	11.6	3.5	11.0	2.3	12.2	-	-
Collateralized Mortgage Obligations	-	-	-	-	1.6	9.7	-	-

Foreign Currency Risk: The strategic asset allocation policy for the Endowment Fund and the Prime Fund includes an allocation to non-United States equity securities. Under Board policy foreign equity holdings in a single industry should not exceed 25% of the investment manager's portfolio measured at market value, with 50% of the portfolio's holdings representing EAFE Index firms. Each investment manager must hold a minimum of 30 individual stocks with equity holdings in a single company remaining below 8% of the investment manager's portfolio, measured at market value. Hedging of foreign currency risks is allowed at the investment manager's discretion. In addition, investments in foreign bonds are allowed under Board policy. Foreign bonds denominated in U.S. dollars are limited to 20% of the investment manager's portfolio, and bonds denominated in currencies other than U.S. dollars are limited to 20% of the investment manager's portfolio, measured at market value. As of September 30, 2006 and 2005, all foreign investments are in international commingled funds, which in turn invest in equity securities and bonds of foreign issuers.

Securities Lending: Board policies permit security lending as a mechanism to augment income. Loans of the securities shall be collateralized by cash, letters of credit or securities issued or guaranteed by the U.S. Government or its agencies. The collateral must equal at least 102% of the current market value of the loaned securities. Securities lending contracts must state acceptable collateral for securities loaned, duties of the borrower, delivery of loaned securities and acceptable investment of the collateral.

The System participates in a securities lending program managed by one of the System's custodial banks. The program is designed to allow the System to lend certain securities from the investment pools and receive a pledge of collateral sufficient to cover the market value of the securities lent. The collateral securities cannot be pledged or sold by the System unless the borrower defaults. At September 30, 2006 and 2005, there were no securities on loan from the investment pools and no collateral held by the System.

Note 4 – Accounts Receivable

The composition of accounts receivable at September 30, 2006 and 2005 is summarized as follows:

	2006	2005
Tuition and fees (net of allowance for doubtful accounts of $202,372 in 2006 and $375,942 in 2005)	$ 2,768,084	$ 3,420,378
Auxiliary enterprises and other operating activities	536,944	527,614
Federal, state, and private grants and contracts (net of allowance for doubtful accounts of $157,035 in 2006 and 2005)	34,933,057	13,248,217
Legal settlement, net present value	951,113	-
Other	166,569	58,738
Net accounts receivable	$ 39,355,767	$ 17,254,947

Note 5 – Capital Assets

Capital assets activity for the years ended September 30, 2006 and 2005 is summarized as follows:

	October 1, 2005	Additions	Retirements	September 30, 2006
Land	$ 2,993,418	$ 83,446	$ -	$ 3,076,864
Land improvements and infrastructure	4,800,682	845,900	-	5,646,582
Buildings and building improvements	172,662,637	7,670,714	-	180,333,351
Construction in progress	-	25,518,343	-	25,518,343
Equipment	54,005,086	1,952,323	(763,568)	55,193,841
Library books	22,293,688	1,290,784	-	23,584,472
Computer software	2,076,709	384,561	-	2,461,270
Total cost of capital assets	258,832,220	37,746,071	(763,568)	295,814,723
Less accumulated depreciation	125,617,417	9,652,788	613,898	134,656,307
Capital assets - net	$ 133,214,803	$ 28,093,283	$ (149,670)	$ 161,158,416

	October 1, 2004	Additions	Retirements	September 30, 2005
Land	$ 2,981,802	$ 11,616	$ -	$ 2,993,418
Land improvements and infrastructure	4,811,557	-	(10,875)	4,800,682
Buildings and building improvements	156,706,282	16,242,196	(285,841)	172,662,637
Equipment	50,903,059	4,373,481	(1,271,454)	54,005,086
Library books	21,197,130	1,096,558	-	22,293,688
Computer software	868,765	1,207,944	-	2,076,709
Total cost of capital assets	237,468,595	22,931,795	(1,568,170)	258,832,220
Less accumulated depreciation	118,065,363	9,063,055	1,511,001	125,617,417
Capital assets - net	$ 119,403,232	$ 13,868,740	$ (57,169)	$ 133,214,803

Note 6 – Long-term Debt

Long-term debt activity for the years ended September 30, 2006 and 2005 is summarized as follows:

Type/Supported by	October 1, 2005	New Debt, net	Principal Repayment/ Defeasance	September 30, 2006
Bonds:				
Student housing revenue	$ 31,386,000	$ -	$ 1,075,000	$ 30,311,000
General fee revenue	28,660,000	8,580,000	8,885,000	28,355,000
Total debts	60,046,000	$ 8,580,000	$ 9,960,000	58,666,000
Less current portion	1,870,000			1,995,000
Total long-term debt	$ 58,176,000			$ 56,671,000

Type/Supported by	October 1, 2004	New Debt, net	Principal Repayment/ Defeasance	September 30, 2005
Bonds:				
Student housing revenue	$ 32,441,000	$ -	$ 1,055,000	$ 31,386,000
General fee revenue	29,435,000	-	775,000	28,660,000
Total debts	61,876,000	$ -	$ 1,830,000	60,046,000
Less current portion	1,830,000			1,870,000
Total long-term debt	$ 60,046,000			$ 58,176,000

Maturities and interest on long-term debt, including obligations under capital leases, for the next five years and in subsequent five-year periods are as follows:

	Principal	Interest	Total
2007	$ 1,995,000	$ 2,446,980	$ 4,441,980
2008	2,060,000	2,387,621	4,447,621
2009	2,125,000	2,323,472	4,448,472
2010	2,195,000	2,253,870	4,448,870
2011	2,275,000	2,179,919	4,454,919
2012 - 2016	12,855,000	9,590,713	22,445,713
2017 - 2021	11,336,000	7,093,888	18,429,888
2022 - 2026	13,250,000	4,325,122	17,575,122
2027 - 2031	7,725,000	1,518,798	9,243,798
2032 - 2034	2,850,000	227,675	3,077,675
	$ 58,666,000	$ 34,348,058	$ 93,014,058

The following is a detailed schedule of long-term debt:

Description and Purpose	Date Issued	Final Maturity	Interest Rate - %	Original Indebtedness	Outstanding Indebtedness September 30, 2006	Outstanding Indebtedness September 30, 2005
Bonds Payable:						
Dormitory Revenue Bonds of 1980	5/1/1980	5/1/2020	3.00	$ 2,180,000	$ 1,095,000	$ 1,155,000
Dormitory Revenue Bonds of 1981	7/23/1982	5/1/2021	3.00	2,602,000	1,346,000	1,416,000
Revenue Bonds-Series 1999-A	12/1/1999	12/1/2024	5.10 - 6.00	8,900,000	-	7,910,000
Student Housing Revenue Bonds-Series 2001	12/27/2001	12/1/2031	3.00 - 5.30	9,370,000	8,785,000	8,945,000
Revenue Bonds-Series 2002-A	12/19/2002	9/30/2027	1.40 - 4.75	3,965,000	3,675,000	3,775,000
Revenue Bonds-Series 2003-A	2/3/2003	9/30/2027	1.45 - 4.70	17,890,000	16,505,000	16,975,000
Student Housing Revenue Bonds-Series 2004-A	9/30/2004	9/1/2034	3.00 - 4.63	13,130,000	12,640,000	12,885,000
Student Housing Revenue Bonds-Series 2004-B	9/30/2004	9/1/2016	3.00 - 3.63	7,515,000	6,445,000	6,985,000
Revenue Bonds-Series 2005-A	10/1/2005	6/1/2025	3.0 - 4.38	8,580,000	8,175,000	-
Total Bonds Payable				74,132,000	58,666,000	60,046,000
Total Debt				$ 74,132,000	$ 58,666,000	$ 60,046,000

The University has various bond covenants in which the University is in compliance at September 30, 2006. In October 2005, the University refinanced the Revenue Bonds Series 1999-A, which resulted in a reduction of future principal and interest payments of $867,032. This savings averages $43,352 a year for the next 20 years.

Note 7 – Self-Insurance

The University participates with other campuses in the System in a self-insurance program for general liability risks. The Board established a separate revocable trust fund for payment of these self-insurance claims under its risk retention program. Annual contributions are made to the trust fund, at an actuarially determined rate, to provide funding for the retained risk. The accompanying statements of net assets include a reserve of $180,957 and $180,925 for general liability at September 30, 2006 and 2005, respectively.

The University also maintains a self-insurance health plan. The University pays Blue Cross/Blue Shield of Alabama a monthly administrative charge in the amount of 6.5% of the claim costs actually paid in the previous month. The accompanying statements of net assets include a self-insurance reserve of $903,031 and $383,467 for health insurance at September 30, 2006 and 2005, respectively. Annual contributions are made to the health plan, utilizing an actuarially determined rate, to provide funding for the reserve.

The changes in the total reported self-insurance liabilities are summarized as follows:

		2006		2005
Balance, beginning of year	$	564,392	$	541,976
Claims paid		(4,913,567)		(5,346,635)
Contributions		5,433,163		5,369,051
Balance, end of year	$	1,083,988	$	564,392

Note 8 – Retirement Plans

Most employees of the University participate in the Teachers' Retirement System of Alabama (TRS), a cost sharing, multiple-employer public retirement system. In addition, certain employees meeting eligibility requirements participate in optional programs with the Teachers Insurance and Annuity Association – College Retirement Equities Fund (TIAA - CREF). TRS is a defined benefit plan while the TIAA - CREF programs are defined contribution plans.

Participants in TRS who retire at age 60 with 10 years of credited service, or after completing 25 years of credited service, regardless of age, are entitled to an annual benefit, payable monthly for life. Service retirement benefits are calculated by three methods with the participants receiving payments under the method which yields the highest monthly benefit. These methods include (1) minimum guaranteed, (2) money purchase, or (3) formula. Under the formula method, participants are allowed 2.0125% of their final average salary (average of three highest years of annual compensation during the last ten years of service) for each year of service. A participant terminating before reaching retirement age, but after completing 10 years of credited service, is eligible for a vested allowance at age 60 provided accumulated employee contributions are not withdrawn. TRS also provides death and disability benefits.

Covered employees are required by law to contribute to TRS. All regular employees of the University are members of TRS with the exception of temporary employees.
The following is a comparative of contribution requirements:

	2006	2005	2004
University contributions	$5,446,436	$4,231,538	$3,561,461
Employee contributions	3,337,432	3,013,214	2,714,528
Total contributions	$8,783,868	$7,244,752	$6,275,989
University contribution rate	8.17%	7.03%	6.56%
Employee contribution rate	5.00%	5.00%	5.00%

The actuarial accrued liability (AAL), which is the actuarial present value of credited projected benefits, is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of employee service to date. The actuarial value of assets, which is the actuarial present value of assets, is a standardized disclosure measure of the present value of accumulated assets, adjusted for projected investment performance and contributions. TRS does not make separate measurements of assets and the AAL for individual employers. The AAL at September 30, 2005 (the most recent valuation date) and September 30, 2004 for TRS as a whole, determined through actuarial valuations performed as of that date, were approximately as follows:

	2005	2004
Actuarial accrued liability (AAL)	$23,027,338,000	$20,886,190,000
Actuarial valuations of assets	19,248,207,000	18,704,009,000
Overfunded (underfunded) AAL	(3,779,131,000)	(2,182,181,000)

Complete financial presentation and disclosure of the financial position and activities of the TRS is presented in the September 30, 2005 annual financial report of the TRS. That report is publicly available and may be obtained by contacting the TRS Communication Department at 1-800-214-2158, ext. 695.

As previously noted, some employees participate in the optional TIAA-CREF programs, which are defined contribution plans. In defined contribution plans, benefits depend solely on amounts contributed plus investment earnings. All full time regular monthly exempt employees are eligible to participate from the date of employment. The University contributes a matching amount up to 5% of total salaries for participating employees. The University's contribution is funded as it accrues and, along with that of employees, is immediately and fully vested.

The contribution for fiscal years 2006 and 2005, excluding amounts from employees who are not eligible for matching, is summarized as follows:

	2006	2005
University contributions	$2,177,869	$1,834,989
Employee contributions	3,549,334	2,997,034
Total contributions	$5,727,203	$4,832,023

The University's total salaries and wages for fiscal years 2006 and 2005 are summarized in the table below:

	2006	2005
Total Salaries and Wages	$76,614,033	$70,574,172
Salaries and Wages of employees participating in:		
TRS	$72,107,266	$60,192,575
TIAA - CREF	$41,490,439	$39,071,471

Note 9 – Post-Employment Benefits

Certain retired employees may elect to continue to participate in the University's group health plan until eligible for Medicare by paying the full cost of the plan premium. Retired employees age sixty-five or older who are eligible for Medicare must enroll in Medicare Coordinated Plan under which Medicare is the primary insurer and the University's health care plan becomes the secondary insurer. Despite the availability of the University's plan, most retirees elect to participate in the Public Education Employees Health Insurance Plan (PEEHIP) with TRS, in which case the retirees pay a portion of the PEEHIP premium, with the University paying an allocation toward the cost of retiree coverage. The University paid $1,174,476 and $971,908 for 256 and 245 retirees for the year ended September 30, 2006 and 2005, respectively.

Certain retirees may also elect to continue their basic term life insurance coverage and accidental death and dismemberment insurance up to certain maximum amounts. The retirees pay the full amount of the premiums in such cases.

Retirees are eligible for tuition assistance benefits for themselves as well as for their spouse and unmarried dependent children.

Note 10 – Compensated Absences

Certain University employees accrue vacation and sick leave at varying rates depending upon their years of continuous service and payroll classification, subject to maximum limitations. Upon termination of employment, employees are paid all unused accrued vacation at their regular rate of pay up to a designated maximum number of days. The statement of net assets includes accruals of $2,897,495 and $2,655,605 as of September 30, 2006 and 2005, respectively, for accrued vacation pay and salary-related payments associated with vacation pay. There is no such accrual recognized for sick leave benefits because no terminal cash benefit is available to employees for accumulated sick leave.

Note 11 – Federal Direct Lending Program

The Federal Direct Student Loan Program (FDSLP) was established under the Higher Education Act of 1965, as amended in the Student Loan Reform Act of 1993. The FDSLP enables an eligible student or parent to obtain a loan to pay for the student's cost of attendance directly through the University rather than through private lenders. The University began participation in the FDSLP on July 1, 1995. As a university qualified to originate loans, the University is responsible for handling the complete loan process, including funds management as well as promissory note functions. The University is not responsible for collection of these loans. For fiscal years ended September 30, 2006 and 2005, the University disbursed approximately $17,559,700 and $16,441,500 respectively, under the FDSLP.

Note 12 – Contracts and Grants

At September 30, 2006, the University has been awarded approximately $67.5 million in contracts and grants which have not been expended. These awards, which represent commitments of sponsors to provide funds for specific research, training, and service projects, have not been reflected in the financial statements.

Note 13 – Contingencies and Commitments

The University has sovereign immunity and is therefore, in the opinion of System Counsel, immune to ordinary tort actions. The University has consistently been dismissed from lawsuits on the basis of the sovereign immunity doctrine. That doctrine also protects the University from vicarious liability arising from the negligence of its employees. As a matter of policy, the University has chosen to indemnify its employees through a self-insured trust fund against liability arising from the performance of their official duties. There are some exceptions to the sovereign immunity doctrine, most notably federal court cases arising under the federal constitution or federal statutes. The University is engaged in various legal actions in the ordinary course of business. Management does not believe the ultimate outcome of those actions will have a material adverse effect on the financial statements.

The University has contracted for a portion of the construction of the Applied Sciences Building. At September 30, 2006, the estimated remaining cost to complete the construction of this facility was $27 million, which is expected to be paid from federal and state sources.

Note 14 – Operating Expenses by Function

Operating expenses by functional classification for the years ended September 30, 2006 and 2005 are summarized as follows:

	Year Ended September 30, 2006					
	Salaries and Wages	Fringe Benefits	Supplies and Services	Depreciation	Scholarships and Fellowships	Total
Instruction	$ 27,432,336	$ 7,851,756	$ 4,242,963	$ -	$ -	$ 39,527,055
Research	29,612,344	7,575,511	11,404,834	-	-	48,592,689
Public service	1,416,186	329,411	2,123,564	-	-	3,869,161
Academic support	3,418,685	935,490	1,336,885	-	-	5,691,060
Student services	4,017,128	1,104,794	4,240,398	-	-	9,362,320
Institutional support	7,193,510	1,944,954	2,676,738	-	-	11,815,202
Operations and maintenance of plant	2,890,969	982,638	5,242,711	-	-	9,116,318
Scholarships and fellowships	-	-	-	-	641,399	641,399
Auxiliary enterprises	632,875	130,838	1,794,107	-	-	2,557,820
Depreciation	-	-	-	9,652,788	-	9,652,788
Total Operating Expenses	$ 76,614,033	$ 20,855,392	$ 33,062,200	$ 9,652,788	$ 641,399	$ 140,825,812

	Year Ended September 30, 2005					
	Salaries and Wages	Fringe Benefits	Supplies and Services	Depreciation	Scholarships and Fellowships	Total
Instruction	$ 25,834,281	$ 6,723,790	$ 4,315,784	$ -	$ -	$ 36,873,855
Research	27,557,545	6,447,876	8,229,439	-	-	42,234,860
Public service	984,113	212,350	3,516,877	-	-	4,713,340
Academic support	3,143,144	803,533	1,075,808	-	-	5,022,485
Student services	3,062,384	793,107	4,192,185	-	-	8,047,676
Institutional support	6,837,304	2,201,734	816,376	-	-	9,855,414
Operations and maintenance of plant	2,632,434	834,598	4,342,160	-	-	7,809,192
Scholarships and fellowships	-	-	-	-	569,210	569,210
Auxiliary enterprises	522,967	103,694	3,008,083	-	-	3,634,744
Depreciation	-	-		9,063,055	-	9,063,055
Total Operating Expenses	$ 70,574,172	$ 18,120,682	$ 29,496,712	$ 9,063,055	$ 569,210	$ 127,823,831

Note 15 – Recently Issued Accounting Standards

The GASB issued Statement No. 45, *Accounting and Reporting by Employers for Postretirement Benefits Other Than Pensions* (GASB 45), in June 2004. This Statement requires governmental entities to recognize and match other postretirement benefit costs, for example health and life insurance expense, with related services received and also to provide information regarding the actuarial accrued liability and funding level of the benefits associated with past services. GASB 45 will be effective for financial statement periods beginning after December 15, 2006. The University is currently evaluating the impact, if any, that GASB 45 will have on the September 30, 2008 financial statements. Most retirees elect to participate in the state-sponsored PEEHIP (Note 9) which is a multi-employer plan. GASB 45 is not expected to affect the University's accounting for PEEHIP.

The GASB issued Statement No. 47, *Accounting for Termination Benefits* (GASB 47), in June 2005. GASB 47 establishes recognition, measurement, and disclosure requirements for both voluntary termination benefits (for example, early-retirement incentives) and involuntary termination benefits (for example, severance benefits). The requirements of GASB 47 are effective in two parts. For termination benefits provided through an existing defined benefit OPEB plan, the provisions of this statement should be implemented simultaneously with the requirements of GASB 45. For all other termination benefits, this statement is effective for financial statements for periods beginning after June 15, 2005. The University has adopted this statement effective October 1, 2005. There was not a material impact on the University's financial statements from the adoption of this statement.

The GASB issued Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues* (GASB 48), in September 2006. This Statement establishes criteria to ascertain whether certain transactions should be regarded as a sale or a collateralized borrowing. GASB 48 is effective for financial statement periods beginning after December 15, 2006. The University is currently evaluating the impact, if any, that GASB 48 will have on its financial statements.

The GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations* (GASB 49), in December 2006. This Statement will require that governments provide more detailed information regarding the effect of environmental cleanups and will be effective for financial periods beginning after December 15, 2007. The University is currently evaluating the impact, if any, that GASB 49 will have on its financial statements.

Note 16 – Component Unit

Basis of Accounting – University of Alabama Huntsville Foundation

The financial statements of UAHF have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

Net assets and revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of UAHF and changes therein are classified and reported as follows:

- **Unrestricted-** Net assets that are not subject to donor-imposed restrictions. Items that affect this net asset category include unrestricted gifts and earnings on these unrestricted gifts.

- **Temporarily Restricted-** Net assets subject to donor-imposed restrictions that may or will be met either by actions of UAHF or the passage of time. Items that affect this net asset category include restricted gifts and earnings on endowment funds expendable for purposes stipulated by the donor. These amounts are reclassified to unrestricted net assets when such purpose or time restrictions are met.

- **Permanently Restricted-** Net assets subject to donor-imposed restrictions to be maintained permanently by UAHF. Items that affect this net asset category include gifts wherein donors stipulate that the corpus be held in perpetuity (primarily gifts for endowment) and only the income be made available for expenditure.

Unrealized and realized gains and losses and dividends and interest from investing in income-producing assets may be included in any of these net asset classifications depending on donor restrictions.

In accordance with SFAS No. 124, *Accounting for Certain Investments Held by Not-for-Profit Organizations*, investments in debt securities and investments in equity securities with readily determinable fair values are reported at their fair values based on published market prices. Other investments, including real estate, are stated at cost or fair value at date of donation in the case of gifts. Changes in fair values are reported as unrealized gains or losses in the statement of activities and changes in net assets. All interest income and realized gains and losses are reported in the statement of activities and changes in net assets.

Investment real estate is stated at cost at the date of acquisition or appraised value at the date of donation in the case of gifts.

Investments – The cost and fair value of investments at September 30, 2006 and 2005 are presented below:

	2006		2005	
	Fair Value	**Cost**	**Fair Value**	**Cost**
Certificates of deposit	$88,245	$88,245	$86,130	$86,130
Pooled Endowment Fund	21,029,829	19,512,214	19,475,945	18,011,897
Marketable debt securities	3,139,163	3,140,561	3,472,895	3,490,833
Marketable equity securities	6,339,578	6,058,621	4,436,803	4,227,494
Mutual funds	602,081	588,310	238,162	253,669
Total	$31,198,896	$29,387,951	$27,709,935	$26,070,023

Certain endowment and similar funds are invested and administered in a common investment pool (Pooled Endowment Fund) established by the Board of Trustees of the University of Alabama. At September 30, 2006 and 2005, respectively, the combined investment pool had total investments of approximately $827,800,000 and $741,330,000 at fair value. Assets of the investment pool are pooled on a fair value basis and consist of cash, U.S. Treasury and agency obligations, corporate debt securities, corporate equity securities, mutual funds, and real estate funds.

Restricted Net Assets – Restricted net assets are classified as either temporarily restricted net assets and available for the following purposes, or permanently restricted net assets, which are restricted to investment in perpetuity, the income from which is expendable for the following purposes at September 30, 2006 and 2005:

	Temporarily Restricted		Permanently Restricted	
	2006	2005	2006	2005
Student support	$ 5,747,289	$ 5,195,474	$ 7,723,009	$ 7,122,227
Faculty support	3,221,236	2,868,675	3,863,455	3,863,455
Academic support	2,450,181	2,587,193	1,740,468	1,678,865
Facilities renovation	297,191	2,567,720	-	-
Other	95,596	87,966	50,428	60,428
Total	$ 11,811,493	$ 13,307,028	$ 13,377,360	$ 12,724,975

Note 17 – Segment Information

The University constructed Southeast Housing and issued bonds in 1980 and 1982. The bonds were payable from revenues received by the University for the use and occupancy of the facility.

Condensed financial information of the University's segment is as follows:

Condensed Balance Sheets

	Dorm Revenue Bonds 1980 2006	Dorm Revenue Bonds 1980 2005	Dorm Revenue Bonds 1981 2006	Dorm Revenue Bonds 1981 2005
Assets				
Current assets	$ 355,180	$ 338,456	$ 561,095	$ 601,387
Capital assets, net of accumulated depreciation	1,468,683	1,577,263	1,887,842	1,198,224
Total assets	$ 1,823,863	$ 1,915,719	$ 2,448,937	$ 1,799,611
Liabilities				
Current liabilities	$ 80,259	$ 76,009	$ 93,100	$ 301,486
Noncurrent liabilities	1,030,000	1,095,000	1,408,931	1,346,000
Total liabilities	$ 1,110,259	$ 1,171,009	$ 1,502,031	$ 1,647,486
Net assets				
Invested in capital assets, net of related debt	373,683	422,263	541,841	(217,776)
Restricted				
Expendable	72,000	72,000	280,000	280,000
Unrestricted	267,921	250,447	125,065	89,901
Total net assets	713,604	744,710	946,906	152,125
Total liabilities and net assets	$ 1,823,863	$ 1,915,719	$ 2,448,937	$ 1,799,611

Condensed Statements of Revenues, Expenses and Changes in Net Assets

	Dorm Revenue Bonds 1980 2006	Dorm Revenue Bonds 1980 2005	Dorm Revenue Bonds 1981 2006	Dorm Revenue Bonds 1981 2005
Operating revenues	$ 394,909	$ 466,008	$ 615,539	$ 493,986
Operating expenses	(289,389)	(393,064)	(472,971)	(474,602)
Depreciation expense	(108,580)	(108,580)	(130,129)	(75,479)
Operating income	(3,060)	(35,636)	12,439	(56,095)
Nonoperating revenues (expenses)	(28,046)	(34,270)	(37,405)	(41,029)
Transfers from general fund	-	465,962	819,747	-
Changes in net assets	(31,106)	396,056	794,781	(97,124)
Net assets, beginning of year	744,710	348,654	152,125	249,249
Net assets, end of year	$ 713,604	$ 744,710	$ 946,906	$ 152,125

Condensed Statements of Cash Flows

	Dorm Revenue Bonds 1980 2006	Dorm Revenue Bonds 1980 2005	Dorm Revenue Bonds 1981 2006	Dorm Revenue Bonds 1981 2005
Cash flows from				
Operating activities	$ 97,063	$ 534,873	$ 61,590	$ 89,411
Capital and related financing activities	(95,753)	(563,515)	(113,336)	(115,430)
Investing activities	7,707	3,283	5,930	4,401
Net decrease in cash	9,017	(25,359)	(45,816)	(21,618)
Cash, beginning of year	182,608	207,967	462,770	484,388
Cash, end of year	$ 191,625	$ 182,608	$ 416,954	$ 462,770

Note 18- Legal Settlement

In July 2006, Nektar Therapeutics (Nektar) and the University announced the settlement of the University's litigation against Nektar and Dr. Milton Harris, in exchange for a total cash payment of $25,000,000. Under the terms of the agreement, Nektar and Dr. Harris have jointly made an upfront payment totaling $15,000,000 to the University. In addition, Nektar will pay the University the sum of $1,000,000 per year for ten years. In exchange, the University has agreed to dismiss all claims related to Nektar's patent portfolio and Nektar has agreed to dismiss all counterclaims. This settlement is reflected in the University's financial statements of September 30, 2006.

THE BOARD OF TRUSTEES OF THE UNIVERSITY OF ALABAMA

ADMINISTRATION

Frank A. Franz
President

Lawrence R. Greenwood
Vice President for Research

J. Derald Morgan
Vice President for University Advancement

Ray M. Pinner
Vice President for Finance & Administration

Lewis J. Radonovich
Provost, Vice President for Academic Affairs

Delois H. Smith
Vice President for Student Affairs

Jorge I. Aunon
Dean, College of Engineering

C. David Billings
Dean, College of Administrative Science

John D. Fix
Dean, College of Science

Sue W. Kirkpatrick
Dean, College of Liberal Arts

Wilson Luquire
Dean, M. Louis Salmon Library

Debra M. Moriarity
Dean, Graduate Studies

C. Fay Raines
Dean, College of Nursing

FINANCIAL STAFF

Mark Richard
Associate Vice President for Financial Affairs

Robert C. Leonard
Controller

Debbie S. Allen
Senior Staff Assistant

Patricia D. Ewert
Manager, Accounts Payable

Winnet H. Leonard
Bursar

Melanie C. Newby
Director, Accounting & Financial Reporting

Charles A. Burns
Associate Director, Accounting & Financial Reporting

Mattie B. Draper
Senior Accounting Assistant

Betty M. Eley
Senior Accountant

Alicia B. Glenn
Accountant II

Laura E. Segraves
Accountant II

Tanya K. Smith
Foundation & Endowment Accountant

Photographs courtesy of University Relations