Woods Hole Oceanographic Institution

Financial Statements
December 31, 2003

PRICEWATERHOUSECOOPERS

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Report of Independent Auditors

To the Board of Trustees of
Woods Hole Oceanographic Institution

In our opinion, the accompanying statement of financial position and the related statements of activities and cash flows present fairly, in all material respects, the financial position of Woods Hole Oceanographic Institution (the "Institution") at December 31, 2003 and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Institution's management; our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the Institution's 2002 financial statements, and in our report dated March 14, 2003, we expressed an unqualified opinion on those financial statements. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America, which 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 audit provides a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

March 19, 2004

Woods Hole Oceanographic Institution
Statement of Financial Position
December 31, 2003 (with comparative information as of December 31, 2002)

	2003	2002
Assets		
Cash, unrestricted	$ 18,097,572	$ 13,973,766
Cash, restricted	1,507,755	2,042,155
Reimbursable costs and fees		
Billed	1,728,635	3,923,078
Unbilled	4,670,629	4,811,138
Receivable for investments sold (Note 3)	22,044,791	-
Interest and dividends receivable	497,941	532,226
Other receivables (Note 12)	8,034,611	14,924,983
Pledges receivable, net	4,846,696	4,463,055
Inventory	1,084,124	1,490,021
Deferred charges and prepaid expenses	775,518	999,204
Deferred fixed rate variance	3,197,693	426,870
Investments, pooled	242,720,582	231,262,026
Investments, nonpooled	5,326,668	6,318,027
Prepaid postretirement benefit cost	788,826	788,826
Supplemental retirement	6,257,039	5,494,326
Intangible pension asset	5,644,240	11,498,524
Other assets	11,983,651	4,177,187
Subtotal	339,206,971	307,125,412
Property, plant and equipment		
Land, buildings and improvements	65,789,103	62,363,781
Vessels and dock facilities	4,365,175	3,474,118
Laboratory and other equipment	15,880,819	14,485,199
Construction in process	7,523,530	3,788,855
	93,558,627	84,111,953
Accumulated depreciation	(49,070,058)	(45,009,763)
Net property, plant and equipment	44,488,569	39,102,190
Remainder trusts	10,532,306	9,395,272
Total assets	$ 394,227,846	$ 355,622,874
Liabilities		
Accounts payable and other liabilities (Note 12)	$ 17,114,484	$ 24,682,000
Accrued payroll and related liabilities	6,227,950	6,695,441
Payable for investments purchased	-	10,193
Accrued supplemental retirement benefits	6,257,039	5,494,326
Accrued pension liability	6,946,274	12,612,637
Deferred revenue and refundable advances	5,316,136	7,319,338
Loan payable	10,724,206	8,045,162
Total liabilities	52,586,089	64,859,097

Net Assets

	Unrestricted	Temporarily restricted	Permanently restricted		
Undesignated	$ 10,961,721	$ -	$ -	10,961,721	(2,502,046)
Pension	(645,885)	-	-	(645,885)	(801,849)
Designated	2,749,713	8,228,213	-	10,977,926	9,540,569
Pledges and other	-	5,504,283	10,773,064	16,277,347	15,893,707
Plant and facilities	30,068,830	1,351,467	-	31,420,297	30,468,808
Education	-	3,361,005	-	3,361,005	3,524,553
Endowment and similar funds	62,278,784	153,081,679	53,928,883	269,289,346	234,640,035
Total net assets	$ 105,413,163	$ 171,526,647	$ 64,701,947	341,641,757	290,763,777
Total liabilities and net assets				$ 394,227,846	$ 355,622,874

The accompanying notes are an integral part of these financial statements.

Woods Hole Oceanographic Institution
Statement of Activities
Year Ended December 31, 2003
(with summarized financial information for the year ended December 31, 2002)

	Unrestricted					
	Operating	Sponsored research	Temporarily restricted	Permanently restricted	2003	2002
Operating						
Revenues						
Fees	$ 483,754				$ 483,754	$ 607,986
Sponsored research						
Government		$ 63,389,385			63,389,385	59,124,026
Nongovernment		16,054,625	$ 4,657,347		20,711,972	21,384,225
Ships and subs operations		17,558,382			17,558,382	17,774,506
Sponsored research assets released to operations	100,749,264	(97,002,392)	(3,746,872)		-	-
Education						
Tuition	2,977,535				2,977,535	2,963,417
Endowment income	3,683,100		1,988,455		5,671,555	5,354,459
Gifts			170,620		170,620	239,556
Education funds released from restriction	2,374,247		(2,374,247)		-	-
Investment return designated for current operations	3,453,967				3,453,967	3,682,563
Contributions and gifts	15,070,373		1,462,380	$ 2,334,192	18,866,945	10,618,986
Contributions in kind	309,153				309,153	237,791
Rental income	718,440				718,440	683,358
Communication and publications	262,004				262,004	283,189
Other	195,644				195,644	210,809
Total revenues	130,277,481	-	2,157,683	2,334,192	134,769,356	123,164,871
Expenses						
Sponsored research						
National Science Foundation	34,097,378				34,097,378	32,456,976
United States Navy	18,379,000				18,379,000	16,903,854
Subcontracts	9,324,911				9,324,911	6,921,702
National Oceanic & Atmospheric Administration	7,412,224				7,412,224	5,513,645
Department of Energy	878,280				878,280	671,558
United States Geological Survey	822,196				822,196	1,150,464
National Aeronautics & Space Administration	753,186				753,186	598,067
Ships Operations	13,001,577				13,001,577	13,920,251
Submersible and ROV operations	4,556,805				4,556,805	3,854,255
Privately funded grants	3,742,846				3,742,846	3,898,586
Other	7,780,861				7,780,861	11,578,173
Education						
Faculty expense	2,968,490				2,968,490	2,633,267
Student expense	3,840,130				3,840,130	3,591,195
Postdoctoral programs	472,037				472,037	502,313
Other	647,797				647,797	653,290
Rental expenses	535,178				535,178	527,772
Communication, publications and development	2,284,343				2,284,343	1,706,855
Fundraising expenses	2,201,452				2,201,452	1,980,070
Unsponsored programs	3,821,259				3,821,259	4,119,677
Other expenses (Note 12)	980,073				980,073	2,747,399
Total expenses	118,500,023	-	-	-	118,500,023	115,929,369
Change in net assets from operating activities	11,777,458	-	2,157,683	2,334,192	16,269,333	7,235,502
Nonoperating income						
Investment return in excess of (less than) amounts designated for sponsored research, education and current operations	9,012,280		22,170,140		31,182,420	(44,302,970)
Change in split interest agreements	27,968		27,818	1,093,605	1,149,391	(1,252,598)
Net periodic pension cost	(5,819,299)				(5,819,299)	(1,233,787)
Contributions and gifts	-		2,163,286		2,163,286	-
Net assets released from restriction	1,466,753		(1,466,753)		-	-
Nonoperating expenses						
Other nonoperating revenues (expenses)	(81,972)		40,658	(1,100)	(42,414)	(668,567)
Change in net assets from nonoperating activities	4,605,730	-	22,935,149	1,092,505	28,633,384	(47,457,922)
Change in net assets from operating and nonoperating activities	16,383,188	-	25,092,832	3,426,697	44,902,717	(40,222,420)
Change in additional pension minimum liability (Note 8)	5,975,263	-	-	-	5,975,263	(5,975,263)
Total change in net assets	22,358,451	-	25,092,832	3,426,697	50,877,980	(46,197,683)
Net assets at beginning of year	83,054,712	-	146,433,815	61,275,250	290,763,777	336,961,460
Net assets at end of year	$ 105,413,163	$ -	$ 171,526,647	$ 64,701,947	$ 341,641,757	$ 290,763,777

The accompanying notes are an integral part of these financial statements.

Woods Hole Oceanographic Institution
Statement of Cash Flows
Year Ended December 31, 2003
(with comparative information for the year ended December 31, 2002)

	2003	2002
Cash flows from operating activities		
Total change in net assets	$ 50,877,980	$ (46,197,683)
Adjustments to reconcile increase (decrease) in net assets to net cash used in operating activities		
Depreciation	4,585,752	4,334,922
Change in split interest agreements	(1,149,391)	1,252,598
Allowance for uncollectible pledges	4,708	-
Discount on pledges	(56,202)	64,446
Net realized and unrealized (gain) loss on investments	(41,731,926)	36,276,953
Intangible pension asset	5,854,284	(11,498,524)
Additional minimum pension liability	(5,975,263)	5,975,263
Contributions to be used for long-term investment	(4,926,199)	(3,094,823)
Gift of property	(7,620,000)	-
(Increase) decrease in assets		
Restricted cash	534,400	85,164
Interest and dividends receivable	34,285	215,512
Reimbursable costs and fees		
Billed	2,194,443	(1,653,014)
Unbilled	140,509	(1,018,751)
Other receivables	6,890,372	(14,435,961)
Pledges receivable	(332,147)	(2,690,068)
Inventory	405,897	(151,821)
Deferred charges and prepaid expenses	223,686	(366,405)
Deferred fixed rate variance	(2,770,823)	(426,870)
Other assets	(186,464)	78,272
Prepaid pension cost	-	6,407,201
Supplemental retirement	(762,713)	970,260
Increase (decrease) in liabilities		
Accrued pension liability	308,900	6,637,374
Accounts payable and other liabilities	(7,555,154)	14,754,067
Accrued payroll and related liabilities	(467,491)	859,707
Deferred revenue and refundable advances	(2,003,202)	(164,516)
Accrued supplemental retirement benefits	762,713	(970,260)
Deferred fixed rate variance	-	(2,196,646)
Net cash used in operating activities	(2,719,046)	(6,953,603)
Cash flows from investing activities		
Capital expenditures		
Additions to property and equipment	(9,972,134)	(8,743,124)
Short-term investments		
Purchase of investments	1,000,000	10,811,667
Endowment		
Receivable for investments sold	(22,044,791)	-
Payable for investments purchased	(10,193)	(271,719)
Proceeds from the sale of investments	51,764,068	252,731,559
Purchase of investments	(21,499,341)	(264,952,755)
Net cash used in investing activities	(762,391)	(10,424,372)
Cash flows from financing activities		
Borrowings under debt agreement	2,679,044	2,977,210
Contributions to be used for long-term investment	4,926,199	3,094,823
Net cash provided by financing activities	7,605,243	6,072,033
Net increase (decrease) in cash and cash equivalents	4,123,806	(11,305,942)
Cash and cash equivalents, beginning of year	13,973,766	25,279,708
Cash and cash equivalents, end of year	$ 18,097,572	$ 13,973,766
Supplemental disclosures		
Cash paid for interest	$ 117,284	$ 109,293
Noncash activity - gift of property	7,620,000	-

The accompanying notes are an integral part of these financial statements.

1. Background

Woods Hole Oceanographic Institution (the "Institution") is a private, independent not-for-profit research and educational institution located in Woods Hole, Massachusetts. Founded in 1930, the Institution is dedicated to working and learning at the frontier of ocean science and attaining maximum return on intellectual and material investments in oceanographic research.

The Institution is a qualified tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code as it is organized and operated for education and scientific purposes.

2. Summary of Significant Accounting Policies

Basis of Presentation
The accompanying financial statements have been prepared on the accrual basis and in accordance with the reporting principles of not-for-profit accounting.

The financial statements include certain prior-year summarized comparative information, but do not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Institution's audited financial statements for the year ended December 31, 2002, from which the summarized information was derived.

Net assets, revenues, and realized and unrealized gains and losses are classified based on the existence or absence of donor-imposed restrictions and legal restrictions imposed under Massachusetts State law. Accordingly, net assets and changes therein are classified as follows:

Permanently Restricted Net Assets
Permanently restricted net assets are subject to donor-imposed stipulations that they be maintained permanently by the Institution. Generally the donors of these assets permit the Institution to use all or part of the income earned and capital appreciation, if any, on related investments for general or specific purposes.

Temporarily Restricted Net Assets
Temporarily restricted net assets are subject to donor-imposed stipulations that may or will be met by actions of the Institution and/or the passage of time. Unspent gains on permanent endowment are classified as temporarily restricted until the Institution appropriates and spends such sums in accordance with the terms of the underlying endowment funds at which time they will be released to unrestricted revenues.

Unrestricted Net Assets
Unrestricted net assets are not subject to donor-imposed stipulations. Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulations or law. Expirations of temporary restrictions on net assets, that is, the donor-imposed stipulated purpose has been accomplished and/or the stipulated time period has elapsed, are reported as reclassifications between the

applicable classes of net assets. Amounts received for sponsored research (under exchange transactions) are reflected in unrestricted sponsored research and released to operations when spent for the appropriate purpose, or as deferred revenue if expenditures have yet to be incurred.

Contributions
Contributions, including unconditional promises to give, are recognized as revenues in the period received. Contributions subject to donor-imposed stipulations that are met in the same reporting period are reported as unrestricted support. Promises to give that are scheduled to be received after the balance sheet date are shown as increases in temporarily restricted net assets and are reclassified to unrestricted net assets when the purpose or items' restrictions are met. Promises to give, subject to donor-imposed stipulations that the corpus be maintained permanently, are recognized as increases in permanently restricted net assets. Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met. Contributions other than cash are generally recorded at market value on the date of the gift (or an estimate of fair value), although certain noncash gifts, for which a readily determinable market value cannot be established, are recorded at a nominal value until such time as the value becomes known. Contributions to be received after one year are discounted at the appropriate rate commensurate with risk. Amortization of such discount is recorded as additional contribution revenue in accordance with restrictions imposed by the donor on the original contribution, as applicable. Amounts receivable for contributions are reflected net of an applicable reserve for collectibility.

The Institution reports contributions in the form of land, buildings, or equipment as unrestricted operating support at fair market value when received.

Dividends, interest and net gains on investments of endowment and similar funds are reported as follows:

- as increases in permanently restricted net assets if the terms of the gift require that they be added to the principal of a permanent endowment fund;

- as increases in temporarily restricted net assets if the terms of the gift or relevant state law impose restrictions on the current use of the income or net realized and unrealized gains; and

- as increases in unrestricted net assets in all other cases.

Operations
The statement of activities report the Institution's operating and nonoperating activities. Operating revenues and expenses consist of those activities attributable to the Institution's current annual research or educational programs, including a component of endowment income appropriated for operations (Note 3). Unrestricted endowment investment income and gains over the amount appropriated under the Institution's spending plan are reported as nonoperating revenue as investment return in excess of (less than) amounts designated for sponsored research, education and current operations. Nonoperating revenue also includes the change in value of split interest agreements, contributions restricted for property, plant and equipment purposes and the net periodic pension cost (income) on the noncontributory defined benefit pension plan.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash, money market accounts, certificates of deposit and overnight repurchase agreements with initial maturities of three months or less when purchased which are stated at cost, which approximates market value. At times the Institution maintains amounts at a single financial institution in excess of federally insured limits.

Included in restricted cash at December 31, 2003 and 2002 is $1,268,574 and $1,803,162, respectively, representing advances received from the United States Navy and other U.S. Government and state agencies. Such amounts are restricted as to use for research programs. Interest earned on unspent funds is remitted to the federal government.

Also included in restricted cash at December 31, 2003 and 2002 is $239,181 and $238,993, respectively, representing cash restricted by the Massachusetts Department of Public Health. Interest earned on unspent funds is reinvested within the restricted cash account.

In addition, cash and cash equivalents include uninvested amounts from each classification of net assets (e.g., endowment).

Investments

Investment securities are carried at market value determined as follows: securities traded on a national securities exchange are valued at the last reported sales price on the last business day of the year; securities traded in the over-the-counter market and listed securities for which no sales prices were reported on that day are valued at closing bid prices. Investments in closely held, unregistered and nonnegotiable securities, for which market quotations are not readily available, are valued by management at an estimated fair value as approved by the investment committee of the Board of Trustees.

Purchases and sales of investment securities are recorded on a trade date basis. Realized gains and losses are computed on a specific identification method. Investment income, net of investment expenses, is distributed on the unit method.

Investment Income Unitization

The Institution's investments are pooled in an endowment fund and the investments and allocation of income are tracked on a unitized basis. The Institution distributes to operations for each individual fund an amount of investment income earned by each of the fund's proportionate share of investments based on a total return policy.

The Board of Trustees has appropriated all of the income and a specified percentage of the net appreciation (depreciation) to operations as prudent considering the Institution's long and short-term needs, present and anticipated financial requirements, expected total return on its investments, price level trends, and general economic conditions. Under the Institution's current endowment spending policy, which is within the guidelines specified under state law, between 4 percent and 5.5 percent of the average of the market value of qualifying endowment investments at September 30 of each of the previous three years is appropriated. This amounted to $13,509,442 and $12,577,096 for the years ending December 31, 2003 and 2002, respectively, and is classified in operating revenues (research, education, and operations). The Institution has interpreted relevant state law as generally permitting the spending of gains on endowment funds over a stipulated period of time.

Inventories
Inventories are stated at the lower of cost or market. Cost is determined using the first-in, first-out method.

Contracts and Grants
Revenues earned on contracts and grants for research are recognized as related costs are incurred.

The Institution received approximately 90% and 86% of its operating revenues from government agencies including 50% and 49% of its operating revenues from the National Science Foundation and 21% and 20% from the United States Navy in fiscal years 2003 and 2002, respectively. Although applications for research funding to federal agencies historically have been funded, authorizations are subject to annual Congressional appropriations and payment.

Property, Plant and Equipment
Property, plant and equipment are stated at cost. Depreciation is provided on a straight-line basis at annual rates of 12 to 39 years on buildings and improvements, 10 to 15 years on vessels and dock facilities and 5 to 10 years on laboratory and other equipment. Depreciation expense on property, plant, and equipment purchased by the Institution in the amounts of $4,485,774 and $4,234,946 in 2003 and 2002, respectively, has been charged to operating activities. Construction commitments totaled $3,166,754 at December 31, 2003.

Depreciation on certain government-funded facilities (the Laboratory for Marine Science and the dock facility) amounting to $99,978 in 2003 and $99,976 in 2002 has been charged to nonoperating expenses as these assets were gifted by the Government.

Included in construction in process is $4,829,373 and $1,735,010 at December 31, 2003 and 2002, respectively, relating to campus development.

Use of Estimates
The preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

Reclassification of Amounts
Certain prior year amounts have been reclassified to conform to the December 31, 2003 presentation.

3. Investments

The cost and market value of pooled investments held at December 31 are as follows:

	2003		2002	
	Cost	**Market**	**Cost**	**Market**
Corporate bonds	$ 52,788,223	$ 53,788,201	$ 52,633,479	$ 53,238,160
International bonds	6,993,216	7,124,933	13,286,797	12,726,162
Equity securities and mutual funds	88,645,967	110,400,060	93,437,150	89,751,465
International equities	43,002,089	50,950,411	43,002,089	36,751,352
Hedge fund limited partnerships	2,741,760	3,116,672	23,920,000	23,523,925
Venture Capital and private equity	24,147,061	17,261,882	21,928,173	15,171,834
Other	78,423	78,423	99,128	99,128
Total investments	$ 218,396,739	$ 242,720,582	$ 248,306,816	$ 231,262,026

Amounts held in venture capital and investment partnerships and other investments are invested in securities or other assets for which there is not necessarily a publicly traded market value or which are restricted as to disposition. The return on such investments was ($128,840) and ($5,372,617) for the years ended December 31, 2003 and 2002, respectively, including dividends, distributions and changes in the estimated value of such investments.

During the year, the Institution terminated certain investment managers. Several of these managers were terminated on December 31, 2003 resulting in a receivable for investments sold of $22,044,791.

The following schedule summarizes the investment return on pooled and nonpooled investments and its classification in the statement of activities:

	Unrestricted	**Temporarily restricted**	**2003 Total**	**2002 Total**
Dividend and interest income	$ 2,566,279	$ 1,988,455	$ 4,554,734	$ 6,355,984
Investment management costs	(1,282,538)	-	(1,282,538)	(1,209,557)
Net realized gains	79,514	275,155	354,669	254,408
Change in unrealized appreciation	14,786,092	26,591,165	41,377,257	(36,531,361)
Total return on investments	16,149,347	28,854,775	45,004,122	(31,130,526)
Investment return designated for				
Sponsored research		(4,696,180)	(4,696,180)	(4,135,422)
Education	(3,683,100)	(1,988,455)	(5,671,555)	(5,354,459)
Current operations	(3,453,967)	-	(3,453,967)	(3,682,563)
Total distributions to operations	(7,137,067)	(6,684,635)	(13,821,702)	(13,172,444)
Investment return in excess of (less than) amounts designated for sponsored research, education and current operations	$ 9,012,280	$ 22,170,140	$ 31,182,420	$ (44,302,970)

Investment return distributed to operations includes $312,260 and $595,348 earned on non-endowment investments for the years ended December 31, 2003 and 2002, respectively.

As a result of market declines, the fair value of certain donor restricted endowments is less than the historical cost value of such funds by $1,014,212 at December 31, 2003, and $2,537,533 at December 31, 2002. These unrealized losses have been recorded as reductions in unrestricted net assets. Future market gains will be used to restore this deficiency in unrestricted net assets before any net appreciation above the historical cost value of such fund increases temporarily restricted net assets.

Investment securities are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investments, it is at least reasonably possible that changes in the value of investment securities will occur in the near term and that such changes could materially affect the market values and the amounts reported in the statement of financial position.

Endowment income is allocated to each individual fund based on a per unit valuation. The value of an investment unit at December 31, is as follows:

	2003	2002
Unit value, beginning of year	$ 3.4719	$ 4.0787
Unit value, end of year	3.9177	3.4719
Net change for the year	.4458	(.6068)
Investment income per unit for the year	.0419	.0647
Total return per unit	$ .4877	$ (.5421)

4. Pledges Receivable

Pledges receivable consist of the following at December 31:

	2003	2002
Unconditional promises expected to be collected in:		
Less than one year	$ 1,688,779	$ 2,101,126
One year to five years	3,428,933	2,684,439
Reserve for uncollectible pledges receivable	(204,708)	(200,000)
Unamortized discount	(66,308)	(122,510)
	$ 4,846,696	$ 4,463,055

5. Contribution Receivable from Remainder Trusts

The Institution recorded $10,532,306 and $9,395,272 at December 31, 2003 and 2002, respectively, relating to various charitable remainder trusts in its statement of financial position. The receivable and related revenue is measured at the present value of estimated future cash flows to be received and recorded in the appropriate net asset category based on donor stipulation. During the term of these agreements, changes in the value are recognized based on amortization of discounts and changes in actuarial assumptions.

6. Deferred Fixed Rate Variance

The Institution receives funding or reimbursement from federal government agencies for sponsored research under government grants and contracts. Revenue is recognized as related costs are incurred. The Institution has negotiated fixed rates with the federal government for the recovery of certain fringe benefits and indirect costs on these grants and contracts. Such recoveries are subject to carryforward provisions that provide for adjustments to be included in the negotiation of future fixed rates. The deferred fixed rate variance accounts represent the cumulative amount owed to or due from the federal government. The Institution's rates are negotiated with the Office of Naval Research (ONR), the Institution's cognizant agency.

The composition of the deferred fixed rate variance is as follows:

Deferred Fixed Rate Variance (liability), December 31, 2001	$ (2,196,646)
2002 indirect costs	44,079,157
2001 adjustment	(8,664)
Amounts recovered	(41,446,977)
2002 change in receivable	2,623,516
Deferred Fixed Rate Variance asset, December 31, 2002	426,870
2003 indirect costs	50,441,014
2002 adjustment	(7,931)
Amounts recovered	(47,662,260)
2003 change in receivable	2,770,823
Deferred Fixed Rate Variance asset, December 31, 2003	$ 3,197,693

As of December 31, 2003, the Institution has expended a cumulative amount in excess of recovered amounts of $3,197,693 which will be reflected as an addition to future year recoveries. This amount has been reported as an asset of the Institution.

7. Loan Payable

On May 27, 1999, the Institution entered into a $3,000,000 loan agreement with the Massachusetts Health and Educational Facilities Authority (the "Authority") to finance various capital projects. On January 31, 2000, the agreement was amended to increase the maximum loan commitment to $6,000,000. As of December 31, 2003, $5,485,951 had been drawn down on the loan and was outstanding at year-end. The Institution is required to pay interest on the drawdowns at a variable rate established by the Authority, which was 1% at December 31, 2003. The final drawdown has not yet occurred. Once a final drawdown has occurred, a schedule of principal payments will be established by the Authority. The final payment is due on July 1, 2010.

On March 1, 2001, the Institution entered into an $11,000,000 loan agreement with the Authority to finance additional capital projects. As of December 31, 2003, $5,238,255 had been drawn down on the loan and was outstanding at year-end. Drawdowns are expected to occur during an eighteen-month period. During this period, no principal payments are due on the loan, but the Institution is required to pay interest on the drawdowns at a variable rate established by the Authority, which was 1% at December 31, 2003. Once the final drawdown has occurred or the eighteen-month period has lapsed, a schedule of principal payments will be established by the Authority until the final payment due on July 1, 2010. As of December 31, 2003, a schedule of principal payments has not been received from the Authority.

The loan agreements have covenants, the most restrictive of which requires the Institution to maintain unrestricted net assets at a market value equal to at least 1.0x outstanding indebtedness.

The Institution's variable rate debt approximates fair value. Fair value is based on estimates using current interest rates available for debt with equivalent maturities.

On October 16, 2003, the Board of Trustees voted to approve various capital projects to be financed through a tax-exempt obligation with total outstanding debt not to exceed $50,000,000.

8. Retirement Plans

The Institution maintains a noncontributory defined benefit pension plan covering substantially all employees of the Institution, as well as a supplemental benefit plan which covers certain employees. Pension benefits are earned based on years of service and compensation received. The Institution's policy is to fund at least the minimum required by the Employee Retirement Income Security Act of 1974.

The Institution also maintains a restoration plan which covers certain employees. Included in the statement of financial position is a payable of $770,184 and $530,044 and an intangible pension asset of $114,035 and $217,780 related to this plan at December 31, 2003 and 2002, respectively.

	Qualified Plan Pension Benefits 2003	Qualified Plan Pension Benefits 2002
Change in benefit obligation		
Benefit obligation at beginning of year	$ 169,123,168	$ 142,163,706
Service cost	6,118,111	5,024,294
Interest cost	11,068,835	10,340,134
Plan amendments	-	2,628,426
Actuarial loss	4,019,659	16,311,089
Benefits paid	(13,415,396)	(7,344,481)
Benefit obligation at end of year	$ 176,914,377	$ 169,123,168
Change in plan assets		
Fair value of plan assets at beginning of year	$ 133,980,735	$ 160,254,856
Employer contributions	-	-
Actual return on plan assets	23,186,048	(18,929,640)
Benefits paid	(13,415,396)	(7,344,481)
Fair value of plan assets at end of year	$ 143,751,387	$ 133,980,735
Funded status	$ (33,162,990)	$ (35,142,433)
Unrecognized net actuarial loss	22,579,627	29,035,103
Unrecognized prior service costs	9,937,478	11,280,744
Net amount recognized	$ (645,885)	$ 5,173,414
Amounts recognized in the statement of financial position consist of		
Accrued benefit liability	$ (6,176,090)	$ (12,082,593)
Accumulated other minimum liability	-	5,975,263
Intangible asset	5,530,205	11,280,744
Net amount recognized	$ (645,885)	$ 5,173,414
Cumulative (addition) reduction in net assets attributable to change in additional minimum liability recognition	$ (5,975,263)	$ 5,975,263
Weighted average assumptions		
Discount rate as of December 31	6.25%	6.75%
Expected return on plan assets for the year	8.50%	10.00%
Rate of compensation increase as of December 31	3.50%	3.50%
Components of net periodic benefit cost		
Service cost	$ 6,118,111	$ 5,024,294
Interest cost	11,068,835	10,340,134
Expected return on plan assets	(12,710,913)	(15,286,868)
Amortization of prior service cost	1,343,266	1,156,227
Net periodic benefit cost	$ 5,819,299	$ 1,233,787

The Institution has reflected the net periodic benefit cost in nonoperating income. In 2002, the Institution was required to record an additional charge of $5,975,263 to reflect a minimum balance sheet liability equal to the Plan's unfunded accumulated benefit obligation. This minimum was triggered due to investment losses on plan assets during the 2002 fiscal year. In 2003, the additional minimum liability was reversed as the minimum balance sheet liability was no longer necessary.

	Supplemental Plan Pension Benefits	
	2003	**2002**
Change in benefit obligation		
Benefit obligation at beginning of year	$ 3,282,549	$ 3,243,021
Service cost	78,650	79,154
Interest cost	209,638	216,030
Plan amendments	-	2,261
Actuarial (gain)/loss	53,532	(2,046)
Benefits paid	(193,392)	(255,871)
Benefit obligation at end of year	$ 3,430,977	$ 3,282,549
Change in plan assets		
Fair value of plan assets at beginning of year	$ -	$ -
Employer contribution	193,392	255,871
Benefits paid	(193,392)	(255,871)
Fair value of plan assets at end of year	$ -	$ -
Funded status	$ (3,430,977)	$ (3,282,549)
Unrecognized actuarial (gain)	(115,013)	(259,057)
Unrecognized prior service costs	1,631	1,946
Net amount recognized	$ (3,544,359)	$ (3,539,660)
Amounts recognized in the statement of financial position consist of		
Supplemental retirement/accrued supplemental retirement benefits	$ (3,544,359)	$ (3,539,660)
Weighted average assumptions		
Discount rate as of December 31	6.25%	6.75%
Expected return on plan assets for the year	8.50%	10.00%
Rate of compensation increase as of December 31	3.50%	3.50%
Components of net periodic benefit cost		
Service cost	$ 78,650	$ 79,154
Interest cost	209,638	216,030
Expected return on plan assets	(215,441)	(263,588)
Amortization of prior year service costs	315	315
Actuarial loss/(gain)	-	(26,091)
Net periodic benefit cost	$ 73,162	$ 5,820

The accrued supplemental retirement is matched by a "Rabbi" Trust with $6,257,039 and $5,494,326, respectively, as of December 31, 2003 and 2002. An additional accrual of $2,712,680 and $1,954,666 has been established for the excess of the "Rabbi" Trust assets over the accrued supplemental retirement benefits at December 31, 2003 and 2002, respectively.

9. Other Postretirement Benefits

In addition to providing retirement plan benefits, the Institution provides certain health care benefits for retired employees and their spouses. Substantially all of the Institution's employees may become eligible for the benefits if they reach normal retirement age (as defined) or elect early retirement after having met certain time in service criteria.

	Other Postretirement Benefits	
	2003	**2002**
Change in benefit obligation		
Benefit obligation at beginning of year	$ 30,459,830	$ 24,305,656
Service cost	669,237	529,739
Interest cost	1,746,394	1,936,615
Actuarial loss	1,407,135	4,803,608
Benefits paid	(1,318,863)	(1,256,870)
Plan participants' contributions	190,142	141,082
Benefit obligation at end of year	$ 33,153,875	$ 30,459,830
Change in plan assets		
Fair value of plan assets at beginning of year	$ 12,619,281	$ 14,532,884
Actual return on plan assets	2,753,110	(2,331,389)
Employer contribution	2,063,679	1,621,939
Benefits paid	(1,318,863)	(1,256,870)
Plan participants' contributions	190,142	141,082
Administrative expenses	(93,679)	(88,365)
Fair value of plan assets at end of year	$ 16,213,670	$ 12,619,281
Funded status	$ (16,940,205)	$ (17,840,549)
Unrecognized actuarial loss	12,153,392	12,726,764
Unrecognized portion of net obligation/(asset) at transition	7,681,947	8,535,496
Unrecognized prior service cost/(credit)	(2,106,308)	(2,632,885)
Net amount recognized	$ 788,826	$ 788,826
Amounts recognized in the statement of financial position consist of		
Prepaid benefit cost	$ 788,826	$ 788,826
Weighted average assumptions		
Discount rate as of December 31	6.25%	6.75%
Expected return on plan assets for the year	8.50%	10.00%

For measurement purposes, annual rates of increase of 9% and 10% in the per capita cost of covered healthcare benefits was assumed for 2003 and 2002 for both pre-65 and post-65 benefits.

These were assumed to decrease gradually to 5.0% in 2010 and remain at that level thereafter.

	2003	**2002**
Components of net periodic benefit cost		
Service cost	$ 669,237	$ 529,739
Interest cost	1,746,394	1,936,615
Expected return on plan assets	(1,112,924)	(1,487,375)
Recognized actuarial (gain) loss		
Amortization of transition obligation	853,549	853,549
Amortization of prior service cost	(526,577)	(526,577)
Recognized actuarial loss	434,000	315,988
Net periodic benefit cost	$ 2,063,679	$ 1,621,939

The Institution has reflected the net periodic benefit cost in operating expenses, as the amount is reimbursed through federal awards.

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plan. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

	December 31, 2003	
	1-Percentage Point Increase	**1-Percentage Point Decrease**
Effect on total of service cost and interest cost	$ 578,023	$ (446,376)
Effect on the postretirement benefit obligation	$ 5,633,557	$ (4,483,697)

10. Commitments and Contingencies

The Defense Contract Audit Agency (DCAA) is responsible for auditing both direct and indirect charges to grants and contracts on behalf of the ONR. The Institution and the ONR have settled the years through 2002. The current indirect cost recovery rates, which are fixed, include the impact of prior year settlements. The DCAA issued an audit report on the completed audit of direct and indirect costs for the year ended December 31, 2002 on September 11, 2003. The audit resulted in no questioned direct or indirect costs.

The Institution through its endowment fund is committed to invest $53,760,426 in certain venture capital and investment partnerships, of which $29,492,608 has been contributed as of December 31, 2003.

The Institution is a defendant in legal proceedings incidental to the nature of its operations. The Institution believes that the outcome of these proceedings will not materially affect its financial position.

11. Related Party Transactions

In fiscal year 2003, the Institution passed through Federal Awards of approximately $1,227,000 to subgrantee organizations in which an individual at the subgrantee organization is also a member of the Institution's Board of Trustees or Corporation. Additionally, a member of the Board of Trustees is affiliated with a law firm which provides legal services to the Institution. The Institution has purchased insurance services from insurance companies in which officers of the companies are also members of the Board of Trustees. The Institution also has other transactions with organizations where a member of the Board of Trustees or Corporation is affiliated with the organization. Total expenditures for legal, insurance and other transactions were approximately $861,000 for the year ended December 31, 2003.

12. Clark Laboratory Fire

In October 2002, the Institution experienced a fire in the Clark Laboratory Building which resulted in contamination and damage to several laboratories, clean rooms and equipment. Since then, the Institution has coordinated with its insurance carrier and other interested parties to identify and quantify the damage caused by the fire. At December 31, 2002, the Institution had recorded a receivable due from the insurance company of approximately $13,259,000 to reflect the estimated insurance proceeds to cover the cost of renting temporary clean laboratories, repairing the laboratories, and cleaning and repairing or replacing damaged or destroyed equipment. Additionally, the Institution established an accrual of approximately $14,669,000 to estimate the costs to be paid going forward associated with the fire. Included in the accrual but not covered by insurance was approximately $1,500,000 relating to displaced employees' salaries, fringe benefits and general and administrative costs as well as $100,000 associated with renting temporary clean laboratories. The total amount not covered by insurance of $1,600,000 had been reflected as a loss on the fire and included in other expenses in the statement of activities.

In 2003, the Institution has continued to coordinate its fire loss recovery efforts with its insurance carrier and other interested parties. At December 31, 2003, a receivable due from the insurance company of $7,435,000 and an accrual of $8,877,000 are included in the statement of financial position. During 2003, $4,000,000 has been received in cash from the insurance company and approximately $4,150,000 has been paid to various outside parties for fire-related damages. The estimated amounts relating to the fire continue to be subject to revision as more information becomes available. Any resulting gain or loss related to accounting for the fire will be recognized when such amounts can be determined with certainty.