

Management's Discussion and Analysis (Unaudited)

INTRODUCTION

This discussion and analysis provides an overview of the financial position and results of activities of the University of Virginia for the year ended June 30, 2005. Comparative information for the year ended June 30, 2004, has been provided where applicable. This overview has been prepared by management and should be read in conjunction with the financial statements and the notes that follow this section.

The University of Virginia is an agency of the Commonwealth of Virginia and is governed by the University's Board of Visitors. The Commonwealth prepares a separate financial report that incorporates all agencies, boards, commissions, and authorities over which the Commonwealth exercises or has the ability to exercise oversight authority. The University, consisting of three major divisions, is a component unit of the Commonwealth of Virginia and is included in these basic financial statements of the Commonwealth. The University of Virginia's three divisions are its Academic Division, Medical Center, and the College at Wise.

Academic Division

A public institution of higher learning with 20,399 students and 2,053 instructional and research faculty members in ten separate schools, the University offers a wide diversity of degree programs, including doctorates in fifty-four disciplines. The University is recognized internationally for the quality of its faculty and for its commitment to the primary academic missions of instruction, research, and public service. The University consistently ranks among the nation's top colleges and universities, both for its general academic programs and for its strengths in specific disciplines. Its emphasis on the student experience is extraordinary among major public institutions, and its dedication to new advances in research permeates all of its schools and colleges.

University of Virginia Medical Center

The University of Virginia Medical Center is an integrated network of primary and specialty care services ranging from wellness programs and routine checkups to the most technologically advanced care. The hub of the Medical Center is a hospital with more than 500 beds in operation and a state-designated Level 1 trauma center. In addition, primary and specialty care is provided at convenient clinic locations throughout Central Virginia communities.

University of Virginia's College at Wise

Located in Southwestern Virginia, the College at Wise is a public liberal arts college with 1,820 students and 120 instructional faculty. It offers twenty-five majors, including pre-professional programs in dentistry, forestry, law, medicine, physical therapy, and veterinary medicine. Degrees include the bachelor of arts, the bachelor of science, and the bachelor of science in nursing.

FINANCIAL HIGHLIGHTS

For the fiscal year ended June 30, 2005:

- The Board of Visitors has committed to increasing faculty compensation, with a goal to rank in the top 20 among the Association of American Universities (AAU) institutions. As a result of compensation increases, the University has already raised its AAU faculty compensation ranking from thirtieth in 2002-03 to twenty-third in 2004-05.
- The Board of Visitors has also committed \$60 million to strengthen the University's status as a top-ranked research institution. In fiscal year 2005, the University secured the first of ten planned new National Academy-level research teams, attracting a renowned innovator in electrical engineering and nanotechnology for the Charles L. Brown Department of Electrical and Computer Engineering.
- The Board of Visitors approved an additional debt issuance of \$193 million. The funds will be used to finance existing capital projects under construction and to refund previous debt issuances. The issuance was priced in June 2005, with final issuance taking place in July 2005.
- The Board of Visitors approved an increase in the authorized limit of the commercial paper program from \$100 million to \$175 million.
- The Board of Visitors authorized the establishment of the University of Virginia Investment Management Company (UVIMCO) as a private foundation. At June 30, 2005, the University's endowment investments were exchanged for shares of equal value in a long-term pool managed by UVIMCO.
- The President and the Board of Visitors approved an expansion of the University's AccessUVA program to accommodate Virginia Community College System transfer students on an accelerated schedule. This program enhancement required an additional commitment of University funds, bringing the University's total institutional investment to \$13.3 million for fiscal year 2006 and more than \$20 million per year when fully implemented in fiscal year 2009.

Comparing fiscal year 2005 to 2004, the University's financial situation continued to strengthen.

Summary of the Increase in Net Assets (in thousands)			INCREASE	
	2005	2004	Amount	Percent
Total revenues before investment income	\$ 1,807,562	\$ 1,645,146	\$ 162,416	9.9%
Total expenses	(1,790,425)	(1,642,364)	(148,061)	9.0%
Increase in net assets before investment income	17,137	2,782	14,355	516.0%
Investment income	329,973	255,384	74,589	29.2%
Total increase in net assets	\$ 347,110	\$ 258,166	\$ 88,944	34.5%

- Revenues before investment income rose 9.9 percent against a rise in expenditures of 9.0 percent, leading to an overall increase before investment income of \$14.4 million.
- Annual investment income grew to \$330 million.
- Accordingly, net assets increased \$347 million, which was \$89 million, or 34.5 percent, more than last year's increase in net assets.
- The total return on net assets was 9.4 percent.

USING THE FINANCIAL STATEMENTS

The University's financial report includes three financial statements and related notes:

1. The Statement of Net Assets
2. The Statement of Revenues, Expenses, and Changes in Net Assets
3. The Statement of Cash Flows

These financial statements are prepared in accordance with Governmental Accounting Standards Board (GASB) principles, which establish standards for external financial reporting for public colleges and universities. These principles require that financial statements be presented on a consolidated basis to focus on the University as a whole, with resources classified for accounting and reporting purposes into four net asset categories. Please note that although the University's foundations identified under guidance from GASB Statement No. 39 are reported in the component unit financial statements, this Management's Discussion and Analysis excludes them except where specifically noted.

STATEMENT OF NET ASSETS

The Statement of Net Assets presents the financial position of the University at the end of the fiscal year and includes all assets and liabilities of the University. The difference between total assets and total liabilities—net assets—is one indicator of the current financial condition of the University, while the change in net assets is an indicator of whether the overall financial condition has improved or worsened during the year. Assets and liabilities are generally measured using current values. One notable exception is capital assets, which are stated at historical cost less an allowance for depreciation. A summary of the University's assets, liabilities, and net assets at June 30, 2005, and June 30, 2004 (restated), follows.

Summary of the Statement of Net Assets (in thousands)			INCREASE (DECREASE)	
	2005	2004	Amount	Percent
Current Assets	\$ 980,904	\$ 827,401	\$ 153,503	18.6%
Noncurrent assets:				
Endowment and other long-term investments	2,387,332	2,511,497	(124,165)	(4.9%)
Capital assets, net	1,500,627	1,378,798	121,829	8.8%
Other	99,360	95,373	3,987	4.2%
Total assets	4,968,223	4,813,069	155,154	3.2%
Current liabilities	395,574	444,654	(49,080)	(11.0%)
Noncurrent liabilities	519,861	662,737	(142,876)	(21.6%)
Total liabilities	915,435	1,107,391	(191,956)	(17.3%)
Net assets	\$ 4,052,788	\$ 3,705,678	\$ 347,110	9.4%

This snapshot of the University's financial position shows that the institution rests on a strong financial foundation. This reflects the prudent use of financial resources, including careful cost controls, effective management of the endowment, conservative utilization of debt, and adherence to a long-range capital plan for the maintenance and replacement of the physical plant.

CURRENT ASSETS AND LIABILITIES

Current assets, which totaled \$981 million as compared to the previous year's \$827 million, an increase of \$154 million, or 18.6 percent, consist primarily of cash and cash equivalents, operating investments, and accounts receivable. Cash and cash equivalents more than doubled over the prior year, primarily due to the accounting treatment necessary to reflect the change in the University's relationship with UVIMCO when it became a private foundation. The investment of the University's current operating funds is now managed by UVIMCO in an aggregate cash pool. The result on our statements was growth in cash equivalents from two primary sources, a reclassification of short-term investments to cash equivalents of \$95 million and a reclassification from long-term investments to cash equivalents of \$127 million.

Current liabilities, which consist primarily of accounts payable, obligations under securities lending, and the current portion of long-term liabilities, fell by \$49 million, or 11 percent. Obligations under securities lending decreased this year by \$70.2 million, or 60 percent. Another fluctuation in current liabilities was a drop in the current portion of long-term debt. It decreased \$18 million, or 52 percent. Last year, commercial paper made up a significant portion of this current liability. This year, the decrease can be attributed to the fact that the University's commercial paper was refinanced with long-term bonds, with the refinancing taking place after the end of the fiscal year; in accordance with Financial Accounting Standards Board Statement No. 6, the commercial paper was reclassified to a long-term liability.

From a liquidity perspective, current assets cover current liabilities 2.5 times, an indicator of good liquidity and the ability to weather short-term demands on working capital. This year's coverage is better than last year's rate of 1.9. Current assets also cover more than seven months of total operating expenses, excluding depreciation.

ENDOWMENT AND OTHER INVESTMENTS

Performance. At June 30, 2005, the major portion of the University's endowment was maintained in a long-term investment pool managed by UVIMCO. The annual return for the long-term investment pool this year was 14.3 percent, an improvement over last year's return of 12.7 percent. Included in the calculation of this performance figure are realized and unrealized gains and losses, along with cash income. With this return, total investment income for all funds rose \$74.6 million, or 29.2 percent.

Distribution. The University distributes endowment earnings in a way that balances the annual support needed for operational purposes against the requirement to preserve the future purchasing power of the endowment. The endowment spending-rate policy is approved by the Board of Visitors and is based on total return, not just cash earnings. The total distribution for the endowment was \$90 million, consisting of \$18 million in current year's cash income and \$72 million in previously earned gains and asset appreciation.

Endowment investments. The total for endowment investments on the Statement of Net Assets is \$2.2 billion. At June 30, 2005, the University exchanged its endowment assets for shares in a long-term investment pool managed by UVIMCO, which made the transition to a private, 501(c)(3) organization. Last year's endowment investment balance included \$227 million of endowment assets the University held on behalf of its related foundations. These foundation assets are no longer an endowment asset of the University, nor a corresponding liability.

From a net assets perspective, earnings from the endowment, while expendable, are mostly restricted as to use by the donors. It is important to note that of the University's endowment funds, only \$624 million, or 28 percent, can be classified as unrestricted net assets. From this unrestricted endowment, a significant portion of the income is internally designated by the University for scholarships, fellowships, professorships, and research efforts.

Including endowment investments held by the related foundations, the combined University system endowment was approximately \$3.1 billion as of June 30, 2005.

CAPITAL AND DEBT ACTIVITIES

One of the critical factors in sustaining the quality of the University's academic and research programs and residential life is the development and renewal of its capital assets. The University continues to implement its long-range plan to modernize its older teaching and research facilities, balanced with new construction.

Capital additions, net of retirements, were \$193.4 million in 2005 and \$113.4 million in 2004. Capital additions comprise replacement, renovation, and new construction of academic, research, and health care facilities, as well as significant investments in equipment, including information technology.

Projects in progress at June 30, 2005, included Cocks Hall, Fayerweather Hall, Wilsdorf Hall, the Rouss Hall Complex for the McIntire School of Commerce, the College at Wise Residence Hall, expansion of the University Hospital, and construction of the John Paul Jones Arena. Other projects at the design stage include Ruffin Hall (the new studio art building), the South Lawn Project for Arts and Sciences, and additions to Campbell Hall.

Financial stewardship requires the effective management of resources, including the use of debt to finance capital projects. As evidence of the University's effective stewardship, Moody's Investors Service has assigned the University its highest credit rating (Aaa) for bonds backed by a broad revenue pledge. Standard and Poor's and Fitch Ratings also have assigned their AAA ratings to the University. The University of Virginia is one of only two public institutions with the highest bond ratings from all three agencies. Besides being an official acknowledgement of the University's financial strength, these ratings enable the University to obtain future debt financing at optimum pricing. In addition to issuing its own bonds, the University is using its commercial paper program for short-term bridge financing. The Board of Visitors increased the University's commercial paper authorization from \$100 million to \$175 million.

Debt additions totaled approximately \$109 million. These additions came from two sources. The Commonwealth of Virginia advance refunded \$43.3 million of bonds on behalf of the University to obtain present value savings of \$2.4 million. The University drew another \$65.3 million in commercial paper for bridge financing. Because the University intended to refinance its outstanding commercial paper at June 30 with long-term bonds, and because it executed this intent with a bond issuance in July, the commercial paper balance is reported as a long-term obligation this year in conjunction with Financial Accounting Standards Board Statement No. 6. The University's debt portfolio contains a strategic mix of both variable- and fixed-rate obligations. The seven foundations now required by GASB Statement No. 39 to be reported as component units held \$161.5 million of long-term debt outstanding at June 30, 2005.

NET ASSETS

Net assets represent the residual interest in the University's assets after liabilities are deducted. The University's net assets at June 30, 2005, and June 30, 2004 (restated), are summarized below.

Net Assets (in thousands)			INCREASE	
	2005	2004	Amount	Percent
Invested in capital assets, net of related debt	\$ 1,012,969	\$ 955,092	\$ 57,877	6.1%
Restricted:				
Nonexpendable	333,544	322,218	11,326	3.5%
Expendable	1,567,246	1,384,623	182,623	13.2%
Unrestricted	1,139,029	1,043,745	95,284	9.1%
Total net assets	\$ 4,052,788	\$ 3,705,678	\$ 347,110	9.4%

Net assets invested in capital assets, net of related debt, represent the University's capital assets net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction, or improvement of those assets. Net capital assets increased \$58 million, or 6.1 percent, in the current fiscal year, compared with 4 percent growth in the previous year. This continued the University's plan for steady but predictable growth in capital assets.

Restricted nonexpendable net assets comprise the University's permanent endowment funds.

Restricted expendable net assets are subject to externally imposed restrictions governing their use. This category of net assets includes permanent endowment fund earnings that can be spent, but only in accordance with restrictions imposed by external parties. This asset category grew 13.2 percent, or \$183 million, primarily due to the investment performance of the University's endowment.

Unrestricted net assets are not subject to externally imposed stipulations. The majority of the University's unrestricted net assets have been designated for various instruction and research programs and initiatives, as well as capital projects.

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

The Statement of Revenues, Expenses, and Changes in Net Assets presents the University's results of activities for the year. Presented below is a summarized statement of the University's revenues, expenses, and changes in net assets for the years ended June 30, 2005, and June 30, 2004 (restated).

Summary of the Statement of Revenues, Expenses, and Changes in Net Assets (in thousands)			INCREASE	
	2005	2004	Amount	Percent
Operating revenues	\$ 1,515,205	\$ 1,381,762	\$ 133,443	9.7%
Operating expenses	1,761,085	1,617,606	143,479	8.9%
Operating loss	(245,880)	(235,844)	(10,036)	4.3%
Nonoperating revenues (expenses)				
State appropriations	143,605	125,531	18,074	14.4%
Gifts	96,547	84,836	11,711	13.8%
Investment income	329,973	255,384	74,589	29.2%
Other net nonoperating expenses	(29,340)	(10,113)	(19,227)	190.1%
Net nonoperating revenues	540,785	455,638	85,147	18.7%
Income before other revenues, expenses, gains, or losses	294,905	219,794	75,111	34.2%
Capital appropriations, gifts, and grants	40,753	40,296	457	1.1%
Additions to permanent endowments	11,452	10,215	1,237	12.1%
Special item: write-down of equipment	-	(12,139)	12,139	(100.0%)
Total other revenues	52,205	38,372	13,833	36.0%
Increase in net assets	347,110	258,166	88,944	34.5%
Net assets—beginning of year	3,705,678	3,447,512	258,166	7.5%
Net assets—end of year	\$ 4,052,788	\$ 3,705,678	\$ 347,110	9.4%

Under GASB principles, revenues and expenses are categorized as either operating or nonoperating. Significant recurring sources of the University's revenues, including state appropriations, gifts, and investment income, are considered nonoperating, as defined by GASB Statement No. 34. Consequently, the operating loss of \$246 million does not account for these normal revenue sources. Adding the net nonoperating revenues of \$541 million for the fiscal year more than offsets the operating loss, and results in an adjusted income figure of \$295 million. This provides a more accurate picture of the University's total scope and results of operations.

REVENUES

One of the University's greatest strengths is its well-balanced stream of revenues, which allows it to weather difficult economic times.

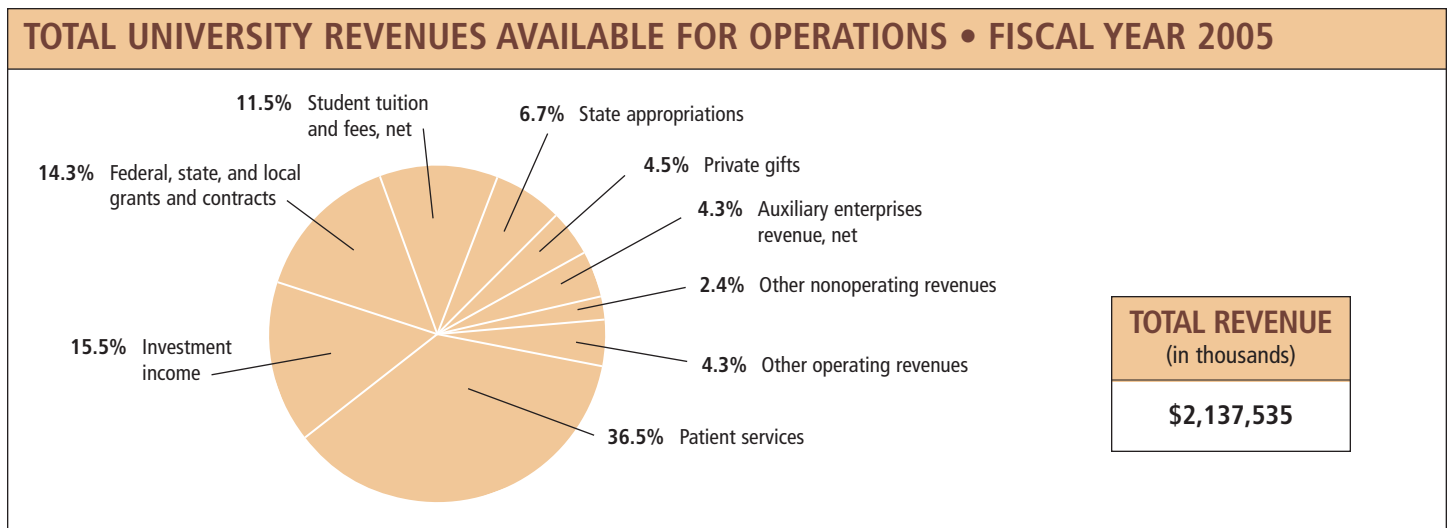
SUMMARY OF REVENUES, TOTAL UNIVERSITY

A summary of the University's revenues, for the years ended June 30, 2005, and June 30, 2004 (restated).

Summary of Revenues (in thousands)	2005			2004			TOTAL INSTITUTION INCREASE (DECREASE)	
	ACADEMIC DIVISION AND WISE	MEDICAL CENTER	TOTAL INSTITUTION	ACADEMIC DIVISION AND WISE	MEDICAL CENTER	TOTAL INSTITUTION	Amount	Percent
Operating revenues:								
Student tuition and fees, net	\$ 246,062	\$ -	\$ 246,062	\$ 232,587	\$ -	\$ 232,587	\$ 13,475	5.8%
Federal, state, and local governmental grants and contracts	305,342	-	305,342	284,923	-	284,923	20,419	7.2%
Nongovernmental grants and contracts	44,737	-	44,737	42,316	-	42,316	2,421	5.7%
Sales and services of educational departments	16,473	-	16,473	17,563	-	17,563	(1,090)	(6.2%)
Auxiliary enterprises revenue, net	92,202	-	92,202	90,961	-	90,961	1,241	1.4%
Other operating revenues	-	30,192	30,192	-	26,834	26,834	3,358	12.5%
Patient services	-	780,197	780,197	-	686,578	686,578	93,619	13.6%
Total operating revenues	\$ 704,816	\$ 810,389	\$1,515,205	\$ 668,350	\$ 713,412	\$1,381,762	\$ 133,443	9.7%
Nonoperating revenues:								
State appropriations	\$ 143,605	\$ -	\$ 143,605	\$ 125,531	\$ -	\$ 125,531	\$ 18,074	14.4%
Private gifts	93,761	2,786	96,547	84,300	536	84,836	11,711	13.8%
Investment income	305,600	24,373	329,973	239,212	16,172	255,384	74,589	29.2%
Other nonoperating revenues	52,205	-	52,205	55,309	-	55,309	(3,104)	(5.6%)
Total nonoperating revenues	\$ 595,171	\$ 27,159	\$ 622,330	\$ 504,352	\$ 16,708	\$ 521,060	\$ 101,270	19.4%
Total Revenues Available for Operations	\$1,299,987	\$ 837,548	\$2,137,535	\$1,172,702	\$ 730,120	\$1,902,822	\$ 234,713	12.3%

Below is a graph of revenues by source (both operating and nonoperating), which are used to fund the University's operating activities for the fiscal year ended June 30, 2005. As noted earlier, GASB Statement No. 34 requires state appropriations, gifts, and other significant revenues to be treated as nonoperating revenues. Because these revenues support operating expenses, they are included in the charts.

Patient services revenues accounted for 51.5 percent of the University's operating revenues and 36.5 percent of the operating and nonoperating revenues combined. State appropriations and student tuition and fees, which represent 6.7 percent and 11.5 percent, respectively, of the University's total revenues are used to fund current operations.

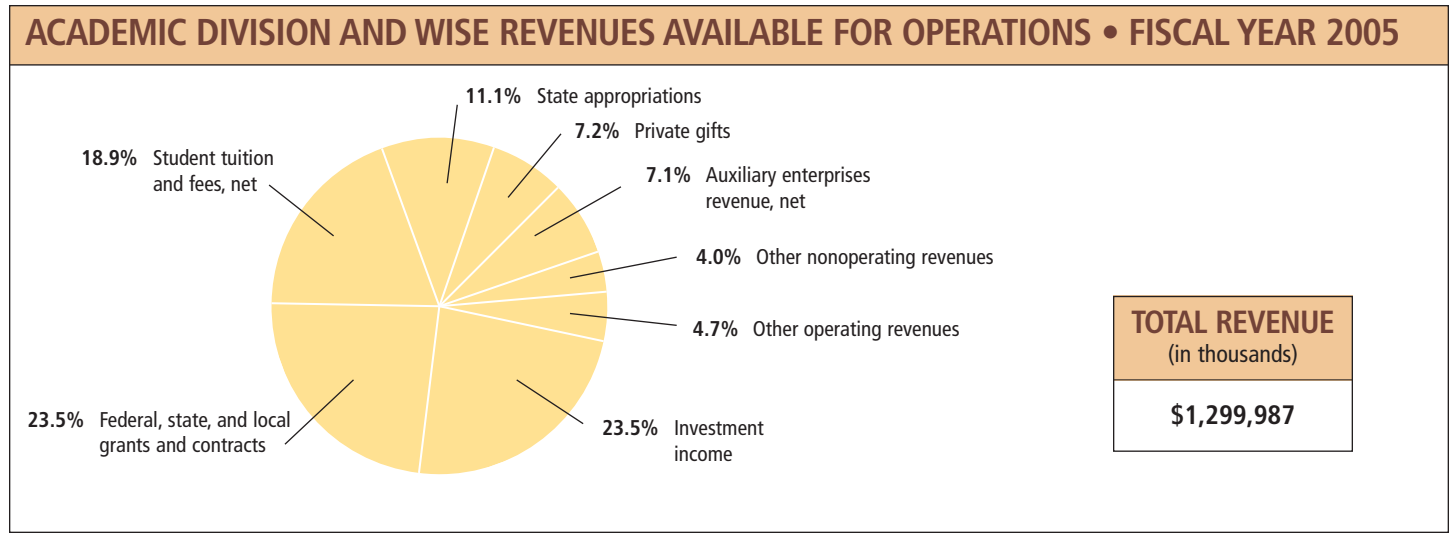


State appropriations increased for the first time in recent history by \$18 million, or 14.4 percent. Two components of this increase were \$4 million for operations and a one-time commitment of \$2 million to support special research initiatives. Net tuition and fees increased by 5.8 percent. The Board of Visitors approved a tuition and fee increase last year to fund academic initiatives.

Excluding the Medical Center data more clearly demonstrates that the academic revenue streams are well balanced. Major sources for 2005 included investment income, 23.5 percent; federal, state, and local grants and contracts, 23.5 percent; net tuition and fees, 18.9 percent; and state appropriations, 11.1 percent. The greatest change is in investment income, rising from 21 percent in fiscal year 2004.

The University continues to emphasize revenue diversification, along with cost containment, as ongoing priorities. This is necessary as the University continues to face significant financial pressure with increased compensation and benefit costs, as well as escalating technology and energy prices. Private support has been, and will continue to be, essential to maintaining the University's academic excellence. Private support comes in the form of gifts and additions to permanent endowment.

Revenues for all sponsored programs increased \$20.4 million, or 7.2 percent, to a total of \$305.3 million in 2005. The increase is less than last year's 14.7 percent rise, but this was expected. While the National Institutes of Health (NIH) continues to provide substantial funding for sponsored programs, that funding increased at a lesser rate than in recent years.



EXPENSES

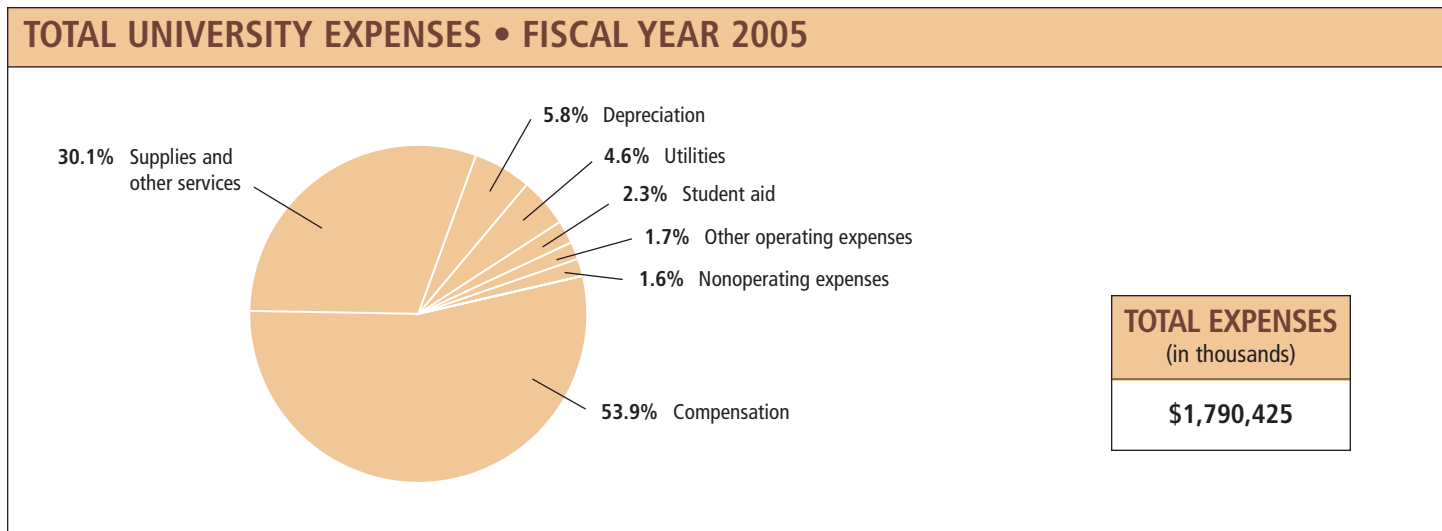
The University continues to be a good steward in the judicious expenditure of funds.

SUMMARY OF EXPENSES, TOTAL UNIVERSITY

A summary of the University's expenses for the years ended June 30, 2005, and June 30, 2004 (restated).

Summary of Expenses (in thousands)	2005			2004			TOTAL INSTITUTION INCREASE	
	ACADEMIC DIVISION AND WISE	MEDICAL CENTER	TOTAL INSTITUTION	ACADEMIC DIVISION AND WISE	MEDICAL CENTER	TOTAL INSTITUTION	Amount	Percent
Operating expenses:								
Compensation	\$ 629,893	\$ 334,828	\$ 964,721	\$ 587,994	\$ 305,817	\$ 893,811	\$ 70,910	7.9%
Supplies and other services	194,584	344,438	539,022	177,619	304,916	482,535	56,487	11.7%
Student aid	40,944	-	40,944	38,940	-	38,940	2,004	5.1%
Utilities	69,306	13,016	82,322	62,647	12,203	74,850	7,472	10.0%
Depreciation	62,446	42,008	104,454	65,361	37,656	103,017	1,437	1.4%
Other operating expense	2,233	27,389	29,622	3,077	21,376	24,453	5,169	21.1%
Total operating expenses	999,406	761,679	1,761,085	935,638	681,968	1,617,606	143,479	8.9%
Nonoperating expenses:								
Interest expense	9,844	4,816	14,660	8,298	4,321	12,619	2,041	16.2%
Other nonoperating expense	12,763	1,917	14,680	12,139	2,292	14,431	249	1.7%
Total nonoperating expenses	22,607	6,733	29,340	20,437	6,613	27,050	2,290	8.5%
Total University expenses	\$1,022,013	\$ 768,412	\$1,790,425	\$ 956,075	\$ 688,581	\$1,644,656	\$ 145,769	8.9%

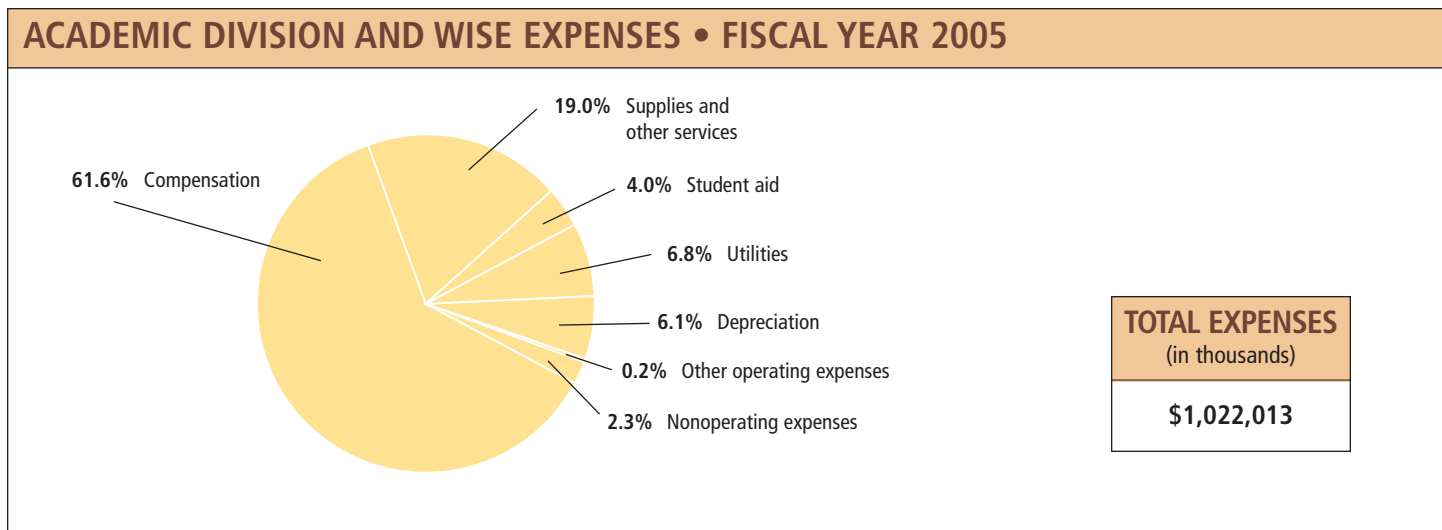
Following is a graphic illustration of expenses (both operating and nonoperating) for the fiscal year ended June 30, 2005.



As a percentage of total expenses, compensation (salaries and benefits) remained almost constant. However, in dollars, compensation increased by \$70.9 million. The Board of Visitors continues to address faculty and staff compensation levels, as they had fallen well below those of the University's national peers.

Student aid expense increased to \$40.9 million, a change of more than \$2 million, as the University continued to support its commitment to AccessUVA. Depreciation increased slightly by \$1.4 million, or 1.4 percent. Interest expense increased by 16.2 percent, or \$2 million.

In addition to their natural (object) classification, it is also informative to review operating expenses by function. A complete matrix of expenses, natural versus functional, is contained in the notes to the financial statements. Expenses for patient services, instruction, and research account for 42.5 percent, 13.5 percent, and 17.7 percent, respectively, of total operating expenses. When combined, these major functions account for 73.7 percent of the total, which is consistent with the mission-critical nature of instruction, research, and patient services for the University.



SUMMARY OF STATEMENT OF CASH FLOWS

The Statement of Cash Flows provides additional information about the University's financial results by reporting the major sources and uses of cash. GASB principles define four major categories of cash flows: cash flows from operating activities, cash flows from noncapital financing activities, cash flows from capital and related financing activities, and cash flows from investing activities.

Summary of the Statement of Cash Flows (in thousands)	INCREASE (DECREASE)			
	2005	2004	Amount	Percent
Cash flows from operating activities	\$ (98,145)	\$ (115,681)	\$ 17,536	15.2%
Cash flows from noncapital financing activities	218,272	206,661	11,611	5.6%
Cash flows from capital and related financing activities	(369,393)	(164,959)	(204,434)	(123.9%)
Cash flows from investing activities	533,265	67,108	466,157	694.6%
Net increase (decrease) in cash and cash equivalents	\$ 283,999	\$ (6,871)	\$ 290,870	4,233.3%

This statement provides a slightly different financial perspective from the Statement of Revenues, Expenses, and Changes in Net Assets. On the latter statement, state appropriations, gifts, and investment income are considered nonoperating revenues. However, on the Statement of Cash Flows, state appropriations and gifts are reflected under noncapital financing activities, while investment income resides under investing activities. These cash inflows are critical to funding the operations of the University.

Noncapital financing activities produced a modest cash flow increase of 5.6 percent, or \$11.6 million, over last year as state appropriations and gifts to the academic division of the University increased slightly. Gift income to the overall University system is likely to increase as the capital campaign continues. Gift revenue for the significant affiliated foundations is reflected in the component unit financial statements.

Cash flow from investing activities is a critical source to the institution. With the endowment's continued strong performance, the University is able to fund new initiatives that make a difference to the institution.

FUTURE ECONOMIC OUTLOOK

Executive management believes that the University remains well positioned financially to continue providing excellent programs and service to its constituents. The University's financial position, as evidenced by the highest credit rating obtainable, provides a high degree of accessibility to capital funds on the most competitive terms. The issuance of long-term bonds and the use of its expanded short-term commercial paper program, along with the ongoing efforts toward revenue diversification, will enable the University to obtain the necessary resources to support and maintain its level of excellence.

A major factor in the University's future will be its relationship with the Commonwealth of Virginia. With the passage of last year's higher education restructuring legislation, the promise for a new, more effective relationship with the Commonwealth is closer to reality.

In addition to the six-year financial plan required by restructuring, the Board of Visitors has requested a separate ten-year, all-sources-of-funds financial plan. Such long-range projections are critical to planning for future University initiatives while ensuring that the University does not overcommit itself financially. One example of such an initiative is the board's resolution to restore faculty compensation to nationally competitive levels by fiscal year 2007. Specifically, the University's goal is to achieve a ranking between fifteenth and nineteenth in compensation among members of the Association of American Universities. Achieving this ranking would place the University in approximately the same position it held in 1989-90 before the era of reduced state support.

The board and the provost of the University have outlined an aggressive strategy to raise the stature of the University's research programs in selected areas of science, engineering, and medicine. Specifically, the board funded \$60 million of a five-year, \$126 million program to recruit world-class investigators, to fund salaries for their research teams, and to build new research space.

In other areas, the board has made a commitment to fund expected deferred maintenance over the next ten years. The cost of the University's health benefits has increased and is expected to increase as the cost of medical care and prescription drugs are forecast to rise.

To meet these demands, the board authorized UVIMCO's change to a private, affiliated organization, which will provide more flexibility in its operations and investment strategies. Additionally, the University has entered the nucleus phase of what is expected to be a \$3 billion capital campaign.

The development of a new relationship with the Commonwealth, combined with the Board of Visitors' emphasis on long-term planning, will ensure that the University continues to meet its public mission and continues to increase its financial strength in the years to come.