REPORT

of the Treasurer

The financial results of the Art Institute of Chicago for the year ended June 30, 2003, and its financial position as of that date are presented in the following financial statements. Deloitte and Touche LLP, independent certified public accountants, have audited the financial statements and their report is on page 30.

The combined museum and School operating results for fiscal year 2003 show a deficit of $2.7 million. (This excludes a one-time impairment loss on one of the Art Institute's buildings that is for sale and discussed later in this report.) Fiscal years 2003 and 2004 were expected by the Trustees and management of the Institute to be deficit transition years. The Institute's goal is to achieve a break-even position in the operating activities of the museum by 2005 and those of the School by 2007. For the first time, the footnotes to this annual report show the unrestricted operating results separately for the museum and School and then on a combined basis for the Art Institute as a whole.

Museum attendance and memberships are significantly influenced by ticketed exhibition activity. There were no major revenue-producing exhibitions in fiscal year 2003. As a result, museum attendance and membership declined to approximately 1.3 million visitors and 108,000 members. These numbers were significantly greater last year due to the popularity of the exhibition "Van Gogh and Gauguin: The Studio of the South." Despite the decrease in attendance and membership, the museum achieved an operating surplus of $1.0 million by containing expenses. The presence of three ticketed exhibitions over the next twelve months should have a positive impact on attendance, membership, and other aspects of the museum's financial operating activities in fiscal year 2004.

The School posted an operating deficit of $3.7 million. The School's full-time-equivalent enrollment reached an all-time high of 2,265 students. This, combined with tuition-rate increases in the undergraduate and graduate programs of 5.6% and 6.3%, respectively, resulted in net tuition (i.e., tuition net of financial aid) of $23.6 million—an increase of $800,000 from a year ago. A long-range plan to balance the School's operating activities relies on broadening its degree offerings in the design and technology areas while reducing costs, including more efficiently utilizing existing facilities and selling those that are not cost-effective.

In fiscal year 2003, the Institute's investments rebounded to $599 million following two successive years of declines. Annualized returns for the pooled endowment beat fund indexes on a one-, three-, and five-year basis, posting returns of 8.7% in fiscal year 2003, -3.3% for the three-year period ending June 30, 2003, and 5.7% over the past five years. The S&P 500 Index reported returns of 0.3%, -11.2%, and -1.6% for the same one-, three-, and five-year periods. The Wilshire 5000 Index showed returns of 1.3%, -10.6%, and -1.3% for these same periods. The Institute has made tremendous progress over the past year in diversifying its portfolio. In the coming year we will complete our work implementing the revised investment allocation and asset diversification policy developed in conjunction with our investment advisor, Cambridge Associates LLP.

As part of the long-range plan to restore the School's operating activities to break-even, the Institute decided to sell its building at 36 S. State. In its place, the School is implementing policies that will more effectively use its existing space to expand its design and technology curriculum. The sale of this building results in a $21.6 million impairment loss because the investment in the building is greater than the assumed sale price. This one-time loss is largely responsible for the $16.6 million decline in the Art Institute's net assets, which now stand at $576.0 million.

On balance, the financial state of the institution is very positive. Significant challenges remain, but we are on the right course toward returning the Institute's operating activities to break-even, while making targeted investments that ensure that the Art Institute remains one of the world's preeminent cultural and educational centers.

DAVID J. VITALE, *Treasurer*

STATEMENT OF FINANCIAL POSITION *(in thousands)*

June 30, 2003

Assets:	
Cash and cash equivalents	$ 2,961
Accounts and investment income receivable	7,733
Contributions receivable	25,048
Inventories	4,399
Prepaid expenses and deferred assets	3,708
Assets held for debt service	1,622
Property and equipment	242,547
Long-term investments	599,431
Total assets	$ 887,449
Liabilities and net assets:	
Liabilities:	
Accrued interest payable	$ 1,993
Accounts payable and other liabilities	16,582
Minimum pension liability	18,294
Refundable advances	2,438
Deferred revenues	3,852
Notes payable	268,585
Total liabilities	311,744
Net assets:	
Unrestricted	115,822
Temporarily restricted	234,913
Permanently restricted	224,970
Total net assets	575,705
Total liabilities and net assets	$ 887,449

See Notes to Financial Statements.

STATEMENT OF ACTIVITIES *(in thousands)*

for the year ended June 30, 2003

	Unrestricted Funds	Temporarily Restricted Funds	Permanently Restricted Funds	Total
Operating revenue, gains, and other support:				
Contributions	$ 12,809	$ 34,198	$ 4,562	$ 51,569
Tuition and student program fees	55,964			55,964
Chicago Park District tax	7,295			7,295
Museum admissions	4,590			4,590
Annual membership dues	5,183			5,183
Special exhibitions, catalogues, and other revenues	993			993
Other program revenues	4,448			4,448
Investment return designated for current use	19,762	10,367	156	30,285
Auxiliary activities	21,310			21,310
Other	4,028			4,028
Net assets released from restrictions	35,198	(35,198)		
Total operating revenues, gains, and other support	171,580	9,367	4,718	185,665
Expenses and losses:				
Programs services:				
Curatorial, libraries, and collections	25,010			25,010
Special exhibitions	3,839			3,839
Museum education	2,953			2,953
Other programs	3,387			3,387
Instructional and academic	45,206			45,206
Student aid	32,340			32,340
Auxiliary activities	17,852			17,852
Managerial and general:				
General administration	14,058			14,058
Depreciation	14,299			14,299
Interest and debt issuance cost	6,532			6,532
Other	1,675			1,675
Member development	2,036			2,036
Fund-raising	5,070			5,070
Total operating expenses before building impairment loss	174,257			174,257
Net change in assets before building impairment loss	(2,677)	9,367	4,718	11,408
Building impairment loss	(21,567)			(21,567)
Change in net assets from operations	(24,244)	9,367	4,718	(10,159)
Nonoperating revenue, support, gains, and losses:				
Proceeds from the sale of art objects	7	110		117
Contribution for the purchase of art objects		932	103	1,035
Net assets released to fund acquisition of art objects	8,576	(8,576)		
Investment return designated for art purchases	361	4,873	31	5,265
Acquisition of art objects	(8,859)			(8,859)
Adjustment to reflect minimum pension liability	(7,201)			(7,201)
Investment return in excess of amounts designated for current operations	3,083	105	11	3,199
Other transfers	(2,998)	3,102	(104)	
Change in net assets	(31,275)	9,913	4,759	(16,603)
Net assets, Beginning of Year	147,097	225,000	220,211	592,308
Net assets, End of Year	$ 115,822	$ 234,913	$ 224,970	$ 575,705

See Notes to Financial Statements.

STATEMENT OF CASH FLOWS *(in thousands)*

for the year ended June 30, 2003

Cash flows from operating activities:	
Change in net assets	$(16,603)
Adjustments to reconcile change in net assets to net cash provided by operating activities:	
Depreciation and amortization	14,326
Retirement of property	801
Impairment loss on property	21,567
Adjustments to reflect minimum pension liability	7,201
Contributions restricted for permanently restricted endowment	(4,562)
Net unrealized and realized gains/losses on long-term investments	(23,482)
Acquisitions and sales of art, net	8,742
Change in assets and liabilities:	
Accounts and investment income receivable	2,856
Prepaid expenses, deferred assets, and inventories	1,723
Unrestricted and temporarily restricted contributions receivable	(301)
Accrued interest payable	229
Accounts payable and other liabilities	(5,313)
Refundable advances	86
Deferred revenues	(2,740)
Net cash provided by operating activities	4,530
Cash flows from investing activities:	
Purchases of property and equipment	(9,534)
Proceeds from sales of art	117
Acquisitions of art	(8,859)
Proceeds from sales of investments	722,106
Purchase of investments	(709,124)
Net cash used in investing activities	(5,294)
Cash flows from financing activities:	
Proceeds from contributions restricted for permanently restricted endowment	3,571
Increase in assets restricted for debt service	(12)
Payments on notes payable	(24,982)
Proceeds from notes payable	13,568
Net cash used in financing activities	(7,855)
Net decrease in cash and cash equivalents	(8,619)
Cash and cash equivalents at beginning of year	11,580
Cash and cash equivalents at end of year	$ 2,961
Supplemental data:	
Interest paid (net of capitalized interest of $150)	$ 5,936
Supplemental disclosure of noncash items:	
Property additions included in accounts payable	$ 2,048

See Notes to Financial Statements.

NOTES

to Financial Statements for the Year Ended June 30, 2003

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Art Institute of Chicago (the "Institute") is a not-for-profit corporation exempt from income tax under Section 501(c)(3) of the Internal Revenue Code. The Institute exists to provide appreciation and education in visual fine arts and design. The Institute fulfills this purpose through:

- Its museum programs ("Museum") by collecting, conserving, researching, publishing, exhibiting, and interpreting an internationally significant permanent collection of objects of art and by presenting temporary exhibitions of international importance, including loaned objects from other collections.

- Its academic programs ("School") by offering comprehensive undergraduate and graduate curricula that provide for the preparation of visual artists, teachers of art, designers, and others in areas that include written, spoken, and media formats.

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with the principles of not-for-profit accounting. A summary of the Institute's significant accounting policies is set forth below:

Management 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 judgments that affect the reported amounts of assets and liabilities and disclosures of contingencies at the date of the financial statements and the reported amounts of revenues and expenses recognized during the reporting period. Actual results could differ from those estimates.

Net Assets. Resources are classified for accounting and reporting purposes into three categories of net assets—unrestricted, temporarily restricted, or permanently restricted—according to externally (donor) imposed restrictions.

Unrestricted net assets include all resources that are not subject to donor-imposed restrictions of a more specific nature than those which only obligate the Institute to utilize funds in furtherance of its mission. Revenues received and expenses incurred in conducting the programs and services of the Institute are presented in the financial statements as unrestricted operating funds that increase or decrease unrestricted net assets. By action of the Board of Trustees of the Institute (the "Board"), certain unrestricted net assets have been earmarked for long-term investment or other special purposes.

Temporarily restricted net assets carry specific, donor-imposed restrictions on the expenditure or other use of contributed funds. Temporary restrictions may expire either because of the passage of time or because the Institute has fulfilled the restrictions. Donor-restricted gifts that are not permanently restricted are reported as temporarily restricted contributions regardless of when the net assets are expended. Transfers of temporarily restricted net assets associated with current expenditures for which the restrictions have been satisfied, as well as donor changes in the nature of restrictions on net assets, are reported as net assets released from restrictions. By action of the Board, certain temporarily restricted assets have been designated for long-term investment.

Permanently restricted net assets are those that are subject to donor-imposed restrictions that will never lapse, thus requiring the assets to be maintained permanently as endowment funds. Net realized and unrealized appreciation on endowment funds is classified in the financial statements as part of either unrestricted, temporarily restricted, or permanently restricted net assets based on donors' restrictions and interpretations of Illinois law.

Art Objects and Library Collections. The value of the art objects in the permanent collection, as well as the holdings of the libraries, is excluded from the Statement of Financial Position. An addition of a work of art to the permanent collection is made either by a donation from a benefactor or through a purchase from Institute acquisition funds. Institute acquisition funds may be classified as permanently restricted, for which only the income earned on principal balances may be used for acquisitions; temporarily restricted, for which both the principal and earned income may be used for acquisitions; or unrestricted, representing donated funds designated by the Board to be used for acquisitions.

The withdrawal of works of art from the collection of the Institute is performed in accordance with a formal policy adopted in 1975. The objects are generally offered for sale at a public auction, and the proceeds from such sales are classified either as temporarily restricted or as trustee-designated for the purchase of works of art. All works of art and library collections are held for public exhibition, education, or research; are protected, kept unencumbered, cared for, and preserved; and are subject to strict organizational policies governing their use. The value of the Institute's permanent collection is not subject to reasonable estimation.

Cash and Cash Equivalents. Cash equivalents not earmarked as long-term investments are stated at cost which approximates market and consist of short-term United States Treasury obligations, high-grade commercial paper, certificates of deposit, or money market funds acquired within 90 days of maturity.

Accounts and Investment Income Receivable and Accounts Payable and Other Liabilities. The carrying amount approximates fair value because of the short-term maturity of those instruments.

Contributions Receivable. The receipt of unconditional promises to give with payments due in future periods is reported as temporarily or permanently restricted support unless explicit donor stipulations or circumstances surrounding the receipt of the promise make clear that the donor intended it to be used to support activities of the current period. Unconditional promises to give are reported at the present value of estimated future cash flows, net of the allowance for uncollectible pledges, using a discount rate that approximates the rate of government securities. Amortization of the discount is recorded as additional contribution revenue.

Inventories. Inventories are stated generally at the lower of average cost or market based upon the moving average cost method.

Prepaid Expenses. Prepaid expenses primarily include expenditures made in connection with the development of future exhibitions. These expenditures typically relate to research, organizational travel, insurance and transport costs of the works to be included in the exhibitions, and the development of exhibition catalogues.

Property and Equipment. Legal title to the Institute's Grant Park facility, a significant component of which has been designated a historical monument, and to the land on which it is situated is vested in the Chicago Park District. The sole and permanent right to the use and occupancy of the land and buildings, including any future improvements, was vested at no cost to the Institute in 1893 as long as the Institute uses the property for the purposes for which it is incorporated. Additions and improvements made to the Grant Park facility since 1984 are capitalized at cost, net of related depreciation.

The Institute owns ten buildings in close proximity to the Grant Park facility that provide instructional, public programming, administrative, storage, and student housing space. Portions of some of these facilities are leased to others. The land, buildings, building improvements, and related equipment, furniture, and fixtures are stated at cost, net of depreciation.

One downtown Chicago office building, purchased in 2000, was undergoing renovation with the intention to provide space for the School. During 2003, the Institute decided to sell the property in its current condition. Based on the current real estate market conditions, and in accordance with Statement of Financial Accounting Standard ("SFAS") No. 144, management has recognized a loss of $21,567,000 to reduce the carrying value of this property to the estimated sales price.

Depreciable assets are being depreciated using the straight-line method over the estimated useful life of the assets. Buildings constructed on Grant Park property have a useful life of 50 years, whereas the purchase and the initial major improvements of all other buildings have a useful life of 40 years. Subsequent building improvements have a useful life of 31.5 years. Equipment, furniture, and fixtures have useful lives ranging from 3 years to 20 years.

The Institute revised its estimate of depreciable useful life on computer equipment. The net effect of this revision was an increase of depreciation expense by $866,000 in 2003.

Long-term Investments. Investments in equity and debt securities are carried at fair value based upon quoted market prices. Certain investments, for which quoted market prices are not available, are carried at cost and approximate $718,000. Purchases and sales of investments are recorded on trade dates, and realized and unrealized gains and losses are determined on the basis of average cost of securities. Realized and unrealized appreciation or depreciation in the carrying value of investments is classified as part of either unrestricted, temporarily restricted, or permanently restricted net assets in accordance with applicable donor requirements. Included in long-term investments are funds held in trust by others, the income from which is paid in whole or in part to the Institute, and split-interest gifts, the principal of which will be turned over to the Institute at some future date.

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

Special Exhibitions. Museum admissions, gifts and grants, auxiliary activities, and restricted endowment income include revenues specific to special exhibitions.

Auxiliary Activities. Auxiliary activities include revenues and certain direct expenditures related to the operation of museum shops and restaurants and two residence halls for the School.

Membership Development Activities. Membership development activities include identifying and offering memberships to prospective members, member relations, and member communications. The imputed value of membership benefits provided to upper level and Sustaining Fellow members approximate $935,000 and are included in contributions.

Purchases and Sales of Art. All revenues and expenses associated with the purchases and sales of art objects, including restricted giving and the release and use of restricted and unrestricted funds for such purposes, are considered nonoperating revenues and expenses.

Endowment Funds. The Institute established the Endowment Funds for the purpose of investing assets in a manner that preserves the real value of the endowment principal and, in addition, provides spendable funds that can be used to fulfill the purposes for which the endowments were established. All Permanently Restricted Net Assets, as well as a significant portion of the Institute's Unrestricted Net Assets and Temporarily Restricted Net Assets, are classified as Endowment Funds. Additions to the Endowment Funds primarily originate from Permanently Restricted Gifts or actions taken by the Board to designate funds as endowment, as well as unrestricted bequests and unspent returns on Endowment Funds investments that are added to the Endowment Funds net assets either at the direction of the donor or as a matter of policy.

In-Kind Support. The Institute records various types of in-kind support, including contributed facilities, services, and other property. Contributions of tangible assets and services are recognized at fair value when received. The amounts reflected in the accompanying financial statements as in-kind support are offset by like amounts included in expenses or assets.

Additionally, the Institute receives a significant amount of volunteer time that does not meet the criteria for recognition as a contribution. Accordingly, the value of this contributed time has not been determined and is not reflected in the accompanying financial statements.

New Accounting Pronouncements. On August 16, 2001, the Financial Accounting Statements Board ("FASB") issued SFAS No. 143, "Accounting for Asset Retirement Obligations," which is effective for all fiscal years beginning after June 15, 2002. SFAS No. 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. The Institute adopted SFAS No. 143 effective July 1, 2002, and there was no impact on the financial statements. On October 3, 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," which is effective for all fiscal years beginning after December 15, 2001. SFAS No. 144 addresses accounting and reporting for the impairment or disposal of long-lived assets, including discontinued operations, and establishes a single accounting model for long-lived assets to be disposed of by sale. On June 1, 2002, FASB issued SFAS No. 146 "Accounting for Costs Associated with Exit or Disposal Activities" which is effective for all fiscal years beginning after December 31, 2002. SFAS No. 146 addresses accounting and reporting obligations associated with liabilities arising from exit or disposal activities. These pronouncements have been adopted and their impact is disclosed.

2. LONG-TERM INVESTMENTS

Long-term investments at June 30, 2003, consist of the following net of management fees (in thousands):

Cash and cash equivalents	$ 111,770	18.7%
Fixed income securities	116,458	19.4
Equity securities	270,632	45.1
Alternative investments	48,688	8.1
Other investments	4,686	0.8
Total assets held for investment	552,234	92.1%
Assets held in trust by others	47,197	7.9
Total long-term investments	$ 599,431	100.0%

The changes in fair value of assets held for long-term investment and assets held in trust by others for the year ended June 30, 2003, were as follows (in thousands):

	Assets Held for Investment	*Assets Held in Trust by Others*	*Total*
Net gain (loss) in market value:			
Realized	$ 16,863	$ —	$ 16,863
Unrealized	8,715	(2,096)	6,619
Dividend and interest income	7,896	3,012	10,908
Gifts and other additions	25,381	225	25,606
Allocation of spendable funds	(41,922)	(7,574)	(49,496)
Change in fair value	16,933	(6,433)	10,500
Fair value, beginning of year	535,301	53,630	588,931
Fair value, end of year	$ 552,234	$ 47,197	$ 599,431

Because long-term investments include funds derived originally from permanently restricted gifts, the management of these funds is subject to Illinois state law. The Institute has interpreted state law as requiring the preservation of the original dollar value of these permanently restricted gifts. After maintaining this value, the Institute interprets the law as allowing it to use any of the investment returns as is prudent considering the Institute's long- and short-term needs, expected total return on its investments, price level trends, and general economic conditions.

In accordance with this interpretation, the Institute adopted a long-term investment objective of sustaining the buying power of the investment principal through limiting the spendable portion of the annual total returns. This spendable amount for the year ended June 30, 2003, which is classified in the revenues section of the Statement of Activities, was equal to 5.25% of the average market value of assets over the six semi-annual periods ending June 30, 2002, factoring in additions to principal on a weighted-average basis through June 30, 2003. Prior year accumulated capital gains are utilized to the extent necessary to meet the annual spendable objective.

Certain investment-related expenses incurred to achieve the investment objectives are treated as decreases to the total investment returns. During the year ended June 30, 2003, these expenses included (in thousands):

Custodial and advisory fees	$ 838
Unrelated business income taxes	20
Total	$ 858

Prior to December 31, 2003, two separate pooled investment funds were maintained. These funds were combined on January 1, 2003, and are included in the fair market value of the assets above. The June 30, 2003, market values (in thousands) and the rates of investment return on these pooled investments for the year ended June 30, 2003, are summarized as follows:

	Fair Market Value	*Rate of Return*
Pooled Endowment Funds investments	$ 512,516	8.7%

The annualized rate of return is computed using monthly returns of individual investment managers. Individual manager returns are calculated using a weighted average capital base, which is determined by the beginning fair market value plus the weighted average of net monthly additions.

3. CONTRIBUTIONS RECEIVABLE

Contributions receivable at June 30, 2003, consists of (in thousands):

Collectible during the year ended June 30:	
2004	$ 13,005
2005	9,212
2006	2,862
2007	1,228
2008	1,171
Gross Contributions Receivable	27,478
Present Value Discount at annualized rate of 2.4%	(1,119)
Allowance for uncollectible contributions	(1,311)
Net contributions receivable	$ 25,048

4. PROPERTY AND EQUIPMENT

Property and equipment at June 30, 2003, consist of (in thousands):

Land	$ 19,975
Buildings and improvements	248,167
Equipment, furniture, and fixtures	27,638
Total property and equipment	295,780
Accumulated depreciation	(71,243)
Net depreciable property and equipment	224,537
Construction/systems in progress	18,010
Net property and equipment	$ 242,547

5. NOTES PAYABLE

Notes payable at June 30, 2003, consist of (in thousands):

	Principal Amount	*% of Total Bonds*	*% of Total O/S Debt*	*Date of Maturity*	*Principal Payable*	*Interest Payment Dates*	*Interest Reset Period*	*Interest Rates*
Bonds:								
Variable / Short-term:								
Adjustable Interest Rates,								
Demand Revenue—								
Tax-exempt:								
Series 2000A	$ 86,800			3/1/34	At maturity	Monthly	Weekly	1.05%
Series 1996	31,700			3/1/27	At maturity	Monthly	Weekly	1.05%
Series 1995	22,000			3/1/27	At maturity	Monthly	Weekly	1.05%
Series 1992	18,000			3/1/27	At maturity	Monthly	Weekly	1.05%
Total Variable / Short-Term	158,500	*70.1%*	*58.9%*					
Medium / Long-Term:								
Adjustable Interest Rates,								
Demand Revenue—								
Taxable:								
Series 2000B	7,100			3/1/34	At maturity	Monthly	Weekly	1.25%
Medium Term Revenue:								
Tax-exempt:								
Series 1998A	32,130			3/1/30	At maturity	March 1, September 1	1–6 years	3.50% to 4.85%
Taxable:								
Series 1998B	8,835			3/1/30	At maturity	March 1, September 1	1–3 years	3.85% to 4.85%
Fixed Interest Rates:								
Revenue Refunding:								
Series 1993	19,700			3/1/27	Varying dates and amounts	March 1, September 1	N/A	5.50% to 5.80%
Total Medium / Long-Term	67,765	*29.9%*	*25.2%*					
Total Bonds	226,265	*100.0%*	*84.1%*					
Lines of Credit:								
$35 million Northern Trust	33,133			5/1/04	At maturity	Quarterly	Varying dates	1.39%
$25 million Bank One	9,500			5/30/04	On demand	Varying dates	Varying dates	1.71%
Total Lines of Credit	42,633		*15.8%*					
Auxiliary activity note:	339		*0.1%*	5/1/13	On demand	Monthly	N/A	1.09%
Total Outstanding Debt	269,237		*100.0%*					
Unamortized discount and issuance expenses	(652)							
Total	$ 268,585							

The market value of notes payable approximates carrying value. All bonds are issued through the Illinois Educational Facilities Authority. Adjustable interest rate bonds are remarketed with new interest rates and interest reset periods after the expiration of the applicable interest reset period. Taxable bond issues may be converted to tax-exempt upon the occurrence of certain events.

The Institute entered into an interest swap agreement on December 6, 2000, with Bank One. The swap agreement, which expires on January 1, 2006, effectively fixes the interest rate on the 2000B issue at 6.58% and is recorded as a liability with an estimated fair value at June 30, 2003 of $(828,000).

The Institute has agreed to maintain certain financial ratios related to debt service, including ratios of indebtedness to net assets and assets available for debt service to debt service requirements. Minimum mandatory redemption payments on the Illinois Education Facilities Authority Bond Issues, which approximate minimum sinking fund requirements, are $375,000 per year for each of the next four years, and an additional total of $224,765,000 through the ultimate maturity dates of the bonds.

On July 1, 2003, $80,800,000 of tax-exempt Series 2000A Bonds were converted from a weekly rate mode to adjustable rate periods of five to twelve years at interest rates ranging from 3.10% to 4.45% with a maturity date of March 1, 2034.

On July 9, 2003, the Series 1993 Bond Issue was refinanced through the issuance of $18,105,000 Series 2003 Revenue Refunding Bonds payable in varying amounts through March 1, 2023, with fixed interest payment dates of March 1 and September 1. The bonds bear interest rates ranging from 2.50% to 5.38%.

6. PENSION AND OTHER POSTRETIREMENT BENEFITS

The Institute has a trusteed, non-contributory defined benefit pension plan (the "Plan") covering substantially all full-time employees. Members of the faculty of the School participate in the contributory pension plan of the Teachers' Insurance and Annuity Association ("TIAA") in lieu of participation in the Institute's pension plan. A non-qualified, supplemental retirement plan is provided for certain employees. The Institute also provides medical, dental, and life insurance benefits ("Other Benefits") on a contributory basis to early retirees until they attain the age of 65.

The following table sets forth the funded status of the Plan and Other Benefits and the amounts set forth in the statement of financial position at June 30, 2003 (in thousands):

	Plan Benefits	*Other Benefits*
Projected benefit obligation	$ 64,325	$ 667
Fair value of Plan's assets	37,111	—
Funded status	$(27,214)	$(667)
Additional liability	$ 23,340	$ —
Prepaid (accrued) benefit cost	5,046	(682)
Minimum liability	$ 18,294	N/A
Minimum pension liability adjustment to be recognized in the statement of activities	$(7,201)	N/A
Curtailment gain	N/A	$ 3,403
Benefit cost	$ 4,435	$ 321
Employer contributions	$ —	$ —
Plan participants' contributions	$ —	$ —
Benefits paid	$ 2,095	$ 54
Weighted average assumptions as of June 30, 2003:		
Discount rate	6.25%	6.25%
Rate of increase in future compensation levels	4.20%	N/A
Expected long-term rate of return on assets	9.50%	N/A

Under SFAS No. 87, *Employers Accounting for Pensions*, a minimum pension liability has been recorded as of June 30, 2003, as the fair value of Plan assets of $37,111,000 is less than the accumulated benefit obligation of $55,405,000. As a result, the statement of financial position includes a minimum pension liability of $18,294,000 and the statement of activities includes an adjustment to reflect the minimum pension liability of $7,201,000.

The initial assumed health care cost trend rate was 6.0% in fiscal 2003.

Net cost and employer contribution to the TIAA plan and the supplemental retirement plan totaled $652,000 and $160,000, respectively, for the year ended June 30, 2003.

The Institute made significant modifications to its retiree medical plan in 2003. These modifications effectively increased the service requirement thereby substantially reducing the number of previously eligible participants. The individual contribution levels for all current and future plan participants also increased. As a result, the post retiree plan experienced a curtailment gain of $3,403,000 in fiscal 2003.

7. NATURAL CLASSIFICATION OF EXPENSES

Expenses by natural classification for operating activities for the year ended June 30, 2003, are as follows (in thousands):

	Museum	*School*	*Total Unrestricted*	*% of Total*
Salaries and wages	$ 25,941	$ 31,921	$ 57,862	29.5%
Fringe benefits	6,816	8,052	14,868	7.6%
Contracted services	7,756	4,802	12,558	6.4%
Equipment and maintenance	1,773	2,817	4,590	2.3%
Travel and entertainment	1,441	758	2,199	1.1%
Telephone, copy, fax, postage	1,234	932	2,166	1.1%
Supplies, books, and subscriptions	1,792	801	2,593	1.3%
Publications and printing	2,306	904	3,210	1.6%
Publicity and promotions	1,051	850	1,901	1.0%
Financial aid		32,340	32,340	16.5%
Cost of sales	7,575	73	7,648	3.9%
Utilities	2,047	1,653	3,700	1.9%
Bad debt	12	(161)	(149)	–0.1%
Interest	2,256	4,276	6,532	3.3%
Depreciation	6,499	7,800	14,299	7.3%
Impairment loss		21,567	21,567	11.0%
Other	4,798	3,142	7,940	4.1%
Total	$ 73,297	$ 122,527	$ 195,824	100.0%

8. OPERATING LEASES

The Institute leases academic, office, storage, and retail space. Minimum rental payments required under operating leases that have initial or remaining noncancellable lease terms in excess of one year as of June 30, 2003, total $629,000, $465,000, $248,000, $55,000,and $33,000 for the years ended June 30, 2004, 2005, 2006, 2007, and 2008, respectively.

Total lease expense was $707,000 during the year ended June 30, 2003.

9. RESTRICTIONS ON NET ASSETS

The nature of restrictions on restricted revenues and on net assets released from donor restrictions during the year ended June 30, 2003, are summarized as follows (in thousands):

	Temporarily Restricted Revenues/ Gains/(Losses)— Restrictions on Use of Net Assets	*Permanently Restricted Revenues/ Gains/(Losses)— Restrictions on Use of Future Revenues Generated by Net Assets*	*Restrictions on Net Assets Released from Donor Restrictions*
Purchase of art objects	$ 11,286	$ 143	$ 6,918
Purchase of books	255	53	232
Student aid	19,435	1,358	20,065
Museum exhibitions	3,009	8	3,567
Museum publications	288		140
Gallery maintenance, professorships, and curatorships	9,979	2,091	7,630
Education, instruction, and other	10,766	1,654	5,222
Time-restricted net assets/assets held in trust by others	(4,433)	99	
General purposes		(543)	
Total	$ 50,585	$ 4,863	$ 43,774

Net assets categorized by donor restrictions as of June 30, 2003 are summarized as follows (in thousands):

	Temporarily Restricted	*Permanently Restricted*
Purchase of art objects	$ 71,375	$ 31,386
Purchase of books	192	1,613
Student aid	13,006	14,663
Museum exhibitions	2,143	10,354
Museum publications	2,165	1,510
Gallery maintenance, professorships, and curatorships	1,715	46,278
Education, instruction, and other	59,075	
Time-restricted net assets/assets held in trust by others	11,826	37,512
General purposes		57,313
Other	73,416	24,341
Total	$ 234,913	$ 224,970

10. UNRESTRICTED STATEMENT OF ACTIVITIES BY PROGRAM

Unrestricted activity for museum and School programs, for the year ended June 30, 2003, are as follows (in thousands):

	Museum	*School*	*Total*
Operating revenue, gains, and other support:			
Contributions	$ 9,731	$ 3,078	$ 12,809
Tuition and student program fees		55,964	55,964
Chicago Park District tax	7,295		7,295
Museum admissions	4,590		4,590
Annual membership dues	5,183		5,183
Special exhibitions, catalogues and other revenues	993		993
Other program revenues	3,135	1,313	4,448
Investment return designated for current use	13,745	6,017	19,762
Auxiliary activities	15,458	5,852	21,310
Other	1,436	2,592	4,028
Net assets released from restrictions	12,731	22,467	35,198
Total operating revenues, gains, and other support	74,297	97,283	171,580
Expenses and losses:			
Programs services:			
Curatorial, libraries, and collections	25,010		25,010
Special exhibitions	3,839		3,839
Museum education	2,953		2,953
Other programs	2,069	1,318	3,387
Instructional and academic		45,206	45,206
Student aid		32,340	32,340
Auxiliary activities	15,499	2,353	17,852
Managerial and general:			
General administration	8,656	5,402	14,058
Depreciation	6,486	7,813	14,299
Interest and debt issuance cost	2,238	4,294	6,532
Other	750	925	1,675
Member development	2,036		2,036
Fund-raising	3,761	1,309	5,070
Total operating expenses before building impairment loss	73,297	100,960	174,257
Net change in asset before building impairment loss	1,000	(3,677)	(2,677)
Building impairment loss		(21,567)	(21,567)
Change in net assets from operations	$ 1,000	$(25,244)	$(24,244)

11. RELATED PARTY TRANSACTIONS

All Trustees, members of Standing and Advisory Trustee committees, officers of the Woman's Board and Auxiliary Boards, officers, and assistant officers of the Institute, as well as the spouses of these individuals (collectively, the "Related Parties"), are required to conduct their personal affairs in such a manner as to avoid any possible conflict of interest with their duties and responsibilities as Related Parties of the Institute. Any duality of interest on the part of any Related Party shall be disclosed when the interest becomes a matter of Trustee Committee or Board of Trustee action. Any Related Party having a duality of interest shall not vote or use his or her personal influence on the related matter. In the event that a vote on the matter is taken, the Related Party having a duality of interest shall not be counted in determining a quorum for the meeting and shall abstain from voting. Any conflicts with or violation of these policies must be formally identified and reported.

The Institute required Trustees, members of Standing and Advisory Trustee committees, officers of the Woman's Board and Auxiliary Boards, officers, and assistant officers of the Institute to formally identify all personal financial interests, as well as their compliance with this policy. Based on the responses received as well as the minutes of all Trustee and Trustee committee meetings, the policy was followed during the year ended June 30, 2003, without exception. Additionally, amounts paid during the year ended June 30, 2003, to any of the organizations reported on by the Related Parties were commensurate to or less than amounts normally charged for comparable goods or for services requiring comparable skill and experience in their respective fields.

INDEPENDENT AUDITORS' REPORT

To the Board of Trustees of The Art Institute of Chicago:

We have audited the statement of financial position of The Art Institute of Chicago (the "Institute") as of June 30, 2003, and the related statements of activities and of cash flows for the year then ended. These financial statements are the responsibility of the Institute's management. Our responsibility is to express an opinion on these financial statements based on our audit.

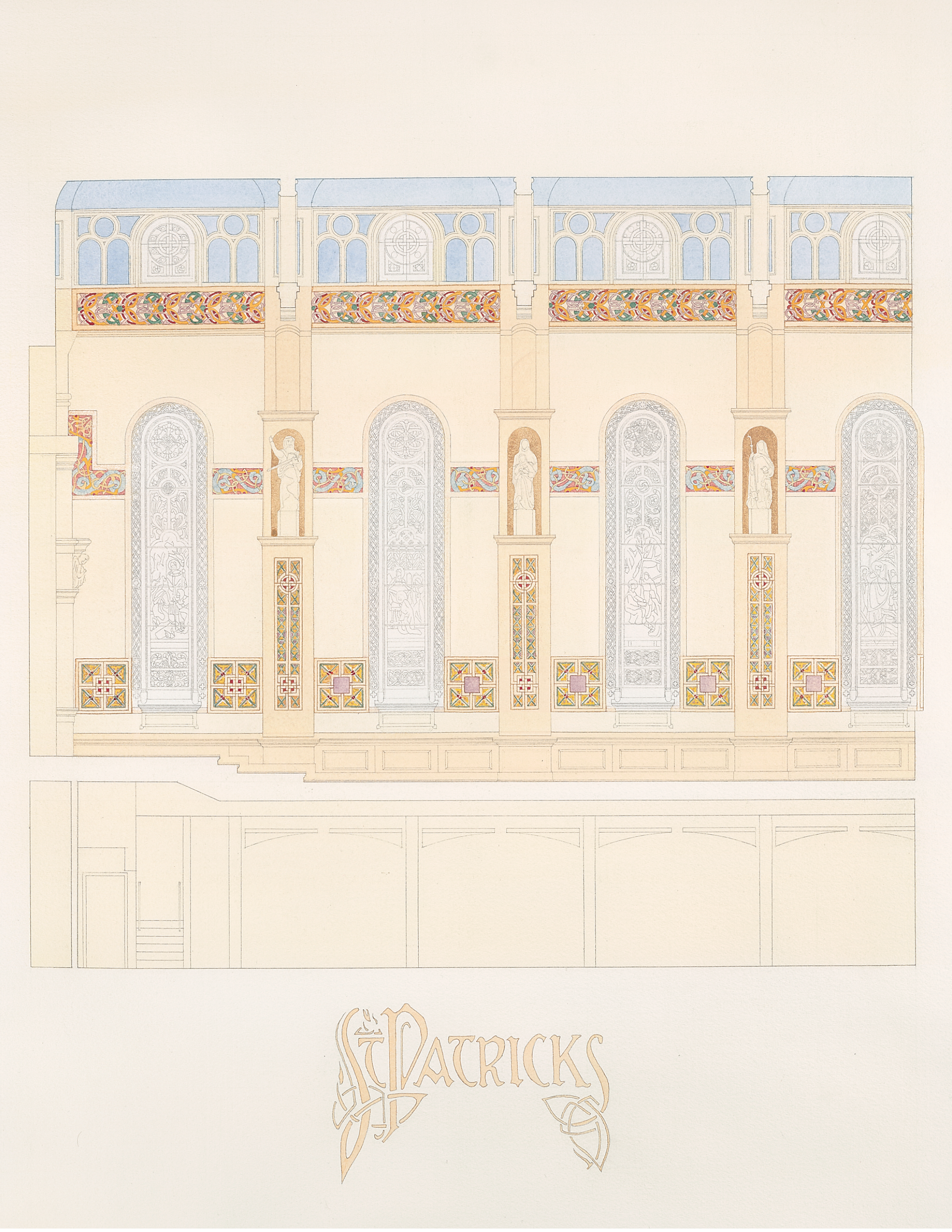
We conducted our audit in accordance with auditing standards generally accepted in the United States of America and Government Auditing Standards as issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about 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. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Institute as of June 30, 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.

In accordance with Government Auditing Standards, we also have issued a report, dated September 26, 2003, on our consideration of the Institute's internal control over financial reporting. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Deloitte & Touche LLP

Chicago, Illinois
September 26, 2003



Booth/Hansen Associates, designer: Laurence O. Booth, *Old Saint Patrick's Church: Interior elevation of the nave with stencil detailing*, c. 1995, graphite, watercolor, and gold inlay on watercolor paper, 72.1 x 55.6 cm. Gift of Laurence O. Booth (2003.55).

SUPPLEMENTAL FINANCIAL INFORMATION

for the years ended June 30,	2003	2002	2001	2000	1999
Museum attendance	1,339,162	1,842,125	1,346,004	1,240,431	1,480,221
Museum admissions revenue (in thousands):					
General	$ 4,590	$ 4,189	$ 3,735	$ 3,631	$ 3,465
Special exhibitions		5,391	865		1,110
Total	$ 4,590	$ 9,580	$ 4,600	$ 3,631	$ 4,575
Membership:					
Number	108,059	141,206	133,279	118,877	136,879
Revenues (in thousands):	$ 5,183	$ 7,696	$ 6,413	$ 5,515	$ 6,237
School enrollment					
Applications, admissions for fall semester new enrollment, degree programs:					
Qualified applicants	3,398	3,274	3,197	3,085	3,078
Applicants admitted	1,945	1,962	1,801	1,819	1,913
Applicants enrolled	834	850	770	757	797
Total enrollment, average for fall/spring semesters:					
Degree programs	2,527	2,458	2,352	2,303	2,259
Non-degree programs	946	940	948	937	858
Total	3,473	3,398	3,300	3,240	3,117
Full-time-equivalent enrollment (15-hour base):					
Degree programs	2,194	2,142	2,056	2,022	1,978
Non-degree programs	71	83	88	85	76
Total	2,265	2,225	2,144	2,107	2,054
School tuition, housing, and program fees (in thousands):	$ 61,743	$ 56,424	$ 50,991	$ 45,698	$ 42,252
Gifts, grants, and bequests (in thousands):					
Unrestricted	$ 12,809	$ 11,916	$ 10,458	$ 16,341	$ 24,679
Temporarily restricted	34,198	35,168	35,774	43,116	26,770
Permanently restricted	4,562	14,087	11,716	19,319	8,270
Total	$ 51,569	$ 61,171	$ 57,948	$ 78,776	$ 59,719
Pooled Endowment investment results:					
Total annualized returns					
1 Year	8.7%	–15.4%	–3.3%	17.4%	11.7%
3 Year	–3.3%				
5 Year	5.7%				
Funds balances (in thousands):					
Unrestricted	$ 115,822	$ 147,097	$ 280,501	$ 315,676	$ 275,515
Temporarily Restricted	234,913	225,000	199,564	211,787	165,627
Permanently restricted	224,970	220,211	213,289	199,069	179,899
Total	$ 575,705	$ 592,308	$ 693,354	$ 726,532	$ 621,041