



VILLANOVA
UNIVERSITY
and Subsidiaries

**FINANCIAL
STATEMENTS**
MAY 31, 2009

VILLANOVA UNIVERSITY

FINANCIAL STATEMENTS May 31, 2009

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Report of Independent Auditors

To the Board of Trustees
Villanova University:

In our opinion, the accompanying consolidated balance sheets and the related consolidated statement of activities, changes in net assets, and cash flows present fairly, in all material respects, the financial position of Villanova University and its subsidiaries ("the University") at May 31, 2009 and 2008, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 1, the University adopted FASB Statement No. 157, *Fair Value Measurements*, in the year ended May 31, 2009.

PricewaterhouseCoopers LLP

August 18, 2009

VILLANOVA UNIVERSITY AND SUBSIDIARIES**Consolidated Statements of Financial Position at May 31, 2009 and 2008**

(in thousands)

| | <u>2009</u> | <u>2008</u> |
|--|-------------------|-------------------|
| ASSETS | | |
| Cash and cash equivalents | \$ 119,452 | \$ 137,137 |
| Short-term investments | 6,288 | 966 |
| Accounts receivable, less allowances of \$1,571 in 2009 and \$1,476 in 2008 | 9,336 | 8,687 |
| Inventories | 2,022 | 2,009 |
| Other assets | 7,891 | 7,692 |
| Assets whose use is limited | 118 | 7,090 |
| Pledges receivable, net | 28,683 | 37,759 |
| Student loans receivable, net | 11,581 | 11,214 |
| Investments | 269,604 | 358,894 |
| Land, buildings and equipment, net | <u>334,849</u> | <u>295,887</u> |
| Total assets | <u>\$ 789,824</u> | <u>\$ 867,335</u> |
| LIABILITIES | | |
| Accounts payable | \$ 9,742 | \$ 12,502 |
| Accrued expenses | 31,188 | 28,754 |
| Deposits | 4,328 | 4,806 |
| Deferred revenues | 9,908 | 9,618 |
| Accrued postretirement benefits | 8,982 | 9,237 |
| Refundable government loan funds | 6,283 | 6,152 |
| Long-term debt | 216,611 | 224,437 |
| Accrued pension cost | <u>11,220</u> | <u>1,777</u> |
| Total liabilities | <u>298,262</u> | <u>297,283</u> |
| NET ASSETS | | |
| Unrestricted | 275,841 | 307,420 |
| Temporarily restricted | 79,103 | 130,528 |
| Permanently restricted | <u>136,618</u> | <u>132,104</u> |
| Total net assets | <u>491,562</u> | <u>570,052</u> |
| Total liabilities and net assets | <u>\$ 789,824</u> | <u>\$ 867,335</u> |

The accompanying notes are an integral part of the consolidated financial statements.

VILLANOVA UNIVERSITY AND SUBSIDIARIES

Consolidated Statement of Activities for the Year Ended May 31, 2009

(in thousands)

| | <u>Unrestricted</u> | <u>Temporarily Restricted</u> | <u>Permanently Restricted</u> | <u>Total</u> | <u>2008 Total</u> |
|--|---------------------|-----------------------------------|-----------------------------------|--------------------|-----------------------|
| OPERATING REVENUES | | | | | |
| Student related revenue: | | | | | |
| Student tuition and fees, net of \$67,179 in student financial aid | \$238,553 | | | \$238,553 | \$224,642 |
| Sales and services of auxiliary enterprises, net of \$2,086 in student financial aid | 63,527 | | | 63,527 | 62,829 |
| | <u>302,080</u> | | | <u>302,080</u> | <u>287,471</u> |
| Private gifts and grants | 11,415 | \$ 4,150 | | 15,565 | 21,972 |
| Government grants | 7,630 | | | 7,630 | 8,303 |
| Endowment resources | 8,356 | 6,150 | | 14,506 | 12,219 |
| Investment income | 1,697 | 96 | | 1,793 | 6,076 |
| Other sources | 14,347 | 547 | | 14,894 | 14,238 |
| Net assets released from restrictions | 8,612 | (8,612) | \$ - | - | - |
| Total operating revenues | <u>354,137</u> | <u>2,331</u> | <u>-</u> | <u>356,468</u> | <u>350,279</u> |
| OPERATING EXPENSES | | | | | |
| Salaries and fringe benefits | 191,023 | | | 191,023 | 182,556 |
| Supplies and services | 43,407 | | | 43,407 | 44,657 |
| Depreciation | 14,801 | | | 14,801 | 13,068 |
| Cost of goods sold | 13,243 | | | 13,243 | 12,226 |
| Interest on indebtedness | 8,690 | | | 8,690 | 8,908 |
| Travel and special events | 10,486 | | | 10,486 | 10,914 |
| Utilities | 9,112 | | | 9,112 | 9,413 |
| Other | 29,001 | | | 29,001 | 30,048 |
| Total operating expenses | <u>319,763</u> | <u>-</u> | <u>-</u> | <u>319,763</u> | <u>311,790</u> |
| Change in net assets from operating activities | <u>34,374</u> | <u>2,331</u> | <u>-</u> | <u>36,705</u> | <u>38,489</u> |
| NON-OPERATING | | | | | |
| Investment Income | | | | | |
| Interest and dividends | 160 | 594 | 438 | 1,192 | 3,413 |
| Realized (losses)/gains | (12,422) | (12,301) | 11 | (24,712) | 24,849 |
| Other | | | | | |
| Rental property revenue | 2,091 | - | - | 2,091 | 2,047 |
| Rental property expenses | (1,581) | - | - | (1,581) | (1,577) |
| Change in fair value of investments | (37,059) | (35,899) | (240) | (73,198) | (14,809) |
| Adjustment to asset retirement obligations | 243 | - | - | 243 | (335) |
| Endowment resources | (8,356) | (6,150) | - | (14,506) | (12,219) |
| | <u>(56,924)</u> | <u>(53,756)</u> | <u>209</u> | <u>(110,471)</u> | <u>1,369</u> |
| Endowment and other gifts | | | 4,305 | 4,305 | 12,173 |
| Change in net assets from non-operating activities | <u>(56,924)</u> | <u>(53,756)</u> | <u>4,514</u> | <u>(106,166)</u> | <u>13,542</u> |
| Change in net assets before other adjustments | <u>\$ (22,550)</u> | <u>\$ (51,425)</u> | <u>\$ 4,514</u> | <u>\$ (69,461)</u> | <u>\$ 52,031</u> |

The accompanying notes are an integral part of the consolidated financial statements.

VILLANOVA UNIVERSITY AND SUBSIDIARIES

Consolidated Statement of Activities for the Year Ended May 31, 2008

(in thousands)

| | <u>Unrestricted</u> | <u>Temporarily Restricted</u> | <u>Permanently Restricted</u> | <u>Total</u> |
|--|---------------------|-----------------------------------|-----------------------------------|------------------|
| OPERATING REVENUES | | | | |
| Student related revenue: | | | | |
| Student tuition and fees, net of \$61,339 in student financial aid | \$ 224,642 | | | \$ 224,642 |
| Sales and services of auxiliary enterprises, net of \$2,037 in student financial aid | 62,829 | | | 62,829 |
| | <u>287,471</u> | | | <u>287,471</u> |
| Private gifts and grants | 11,183 | \$ 10,789 | | 21,972 |
| Government grants | 8,303 | | | 8,303 |
| Endowment resources | 6,839 | 5,380 | | 12,219 |
| Investment income | 5,646 | 430 | | 6,076 |
| Other sources | 13,543 | 695 | | 14,238 |
| Net assets released from restrictions | 7,688 | (7,688) | \$ - | - |
| Total operating revenues | <u>340,673</u> | <u>9,606</u> | <u>-</u> | <u>350,279</u> |
| OPERATING EXPENSES | | | | |
| Salaries and fringe benefits | 182,556 | | | 182,556 |
| Supplies and services | 44,657 | | | 44,657 |
| Depreciation | 13,068 | | | 13,068 |
| Cost of goods sold | 12,226 | | | 12,226 |
| Interest on indebtedness | 8,908 | | | 8,908 |
| Travel and special events | 10,914 | | | 10,914 |
| Utilities | 9,413 | | | 9,413 |
| Other | 30,048 | | | 30,048 |
| Total operating expenses | <u>311,790</u> | <u>-</u> | <u>-</u> | <u>311,790</u> |
| Change in net assets from operating activities | <u>28,883</u> | <u>9,606</u> | <u>-</u> | <u>38,489</u> |
| NON-OPERATING | | | | |
| Investment Income | | | | |
| Interest and dividends | 1,062 | 1,931 | 420 | 3,413 |
| Realized gains | 12,541 | 12,234 | 74 | 24,849 |
| Other | | | | |
| Rental property revenue | 2,047 | | | 2,047 |
| Rental property expenses | (1,577) | | | (1,577) |
| Change in market value of investments | (7,367) | (7,336) | (106) | (14,809) |
| Adjustment to asset retirement obligations | (335) | | | (335) |
| Endowment resources | (6,839) | (5,380) | | (12,219) |
| | <u>(467)</u> | <u>1,448</u> | <u>388</u> | <u>1,369</u> |
| Endowment and other gifts | 116 | | 12,057 | 12,173 |
| Change in net assets from non-operating activities | <u>(351)</u> | <u>1,448</u> | <u>12,445</u> | <u>13,542</u> |
| Change in net assets before other adjustments | <u>\$ 28,532</u> | <u>\$ 11,054</u> | <u>\$ 12,445</u> | <u>\$ 52,031</u> |

The accompanying notes are an integral part of the consolidated financial statements.

VILLANOVA UNIVERSITY AND SUBSIDIARIES

Consolidated Statements of Changes in Net Assets
For the Years Ended May 31, 2009 and 2008
(in thousands)

| | <u>2009</u> | <u>2008</u> |
|---|-------------------------|-------------------------|
| Unrestricted Net Assets: | | |
| Change in net assets before other adjustments | \$ (22,550) | \$ 28,532 |
| Adjustment for pension plan liability | <u>(9,029)</u> | <u>(2,530)</u> |
| Increase in unrestricted net assets | <u>(31,579)</u> | <u>26,002</u> |
| Temporarily Restricted Net Assets: | | |
| Change in net assets | <u>(51,425)</u> | <u>11,054</u> |
| Increase in temporarily restricted net assets | <u>(51,425)</u> | <u>11,054</u> |
| Permanently Restricted Net Assets: | | |
| Change in net assets | <u>4,514</u> | <u>12,445</u> |
| Increase in permanently restricted net assets | <u>4,514</u> | <u>12,445</u> |
| Increase in net assets | (78,490) | 49,501 |
| Net assets: | | |
| Beginning of Year | <u>570,052</u> | <u>520,551</u> |
| End of Year | <u>\$491,562</u> | <u>\$570,052</u> |

The accompanying notes are an integral part of the consolidated financial statements.

VILLANOVA UNIVERSITY AND SUBSIDIARIES

Consolidated Statements of Cash Flows

For the years ended May 31, 2009 and 2008

(in thousands)

| | <u>2009</u> | <u>2008</u> |
|---|------------------|------------------|
| CASH FLOW FROM OPERATING ACTIVITIES | | |
| (Decrease)/Increase in net assets | \$ (78,490) | \$ 49,501 |
| Adjustments to reconcile change in net assets to net cash provided by operating activities: | | |
| Depreciation | 14,801 | 13,068 |
| Contributions restricted for long-term investment | (9,954) | (8,539) |
| Realized losses/(gains) on sales of investments | 24,712 | (24,849) |
| Change in market value of investments | 73,198 | 14,809 |
| Pension and other postretirement benefit plan adjustments | 9,029 | 2,530 |
| Receipt of contributed securities | (453) | (5,937) |
| Amortization of debt (premium)/discount | (313) | (313) |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (744) | (899) |
| Pledges receivable | 9,154 | (3,295) |
| Provision for doubtful accounts | 80 | 1,053 |
| Accounts payable and accrued expenses | 3,050 | 2,460 |
| Other changes | (241) | 244 |
| Net cash provided by operating activities | <u>43,829</u> | <u>39,833</u> |
| CASH FLOW FROM INVESTING ACTIVITIES | | |
| Proceeds from sales of investments | 281,171 | 155,787 |
| Purchases of investments | (289,338) | (159,307) |
| Student loans receivable | (430) | (1,162) |
| Purchase of land, buildings and equipment | (57,139) | (53,757) |
| Short-term investments, net | (5,322) | (9) |
| Decrease in assets whose use is limited | 6,972 | 31,187 |
| Net cash used by investing activities | <u>(64,086)</u> | <u>(27,261)</u> |
| CASH FLOW FROM FINANCING ACTIVITIES | | |
| Contributions restricted for long-term investment | 9,954 | 8,539 |
| Repayment of debt | (7,513) | (7,227) |
| Government loan funds | 131 | 112 |
| Net cash used in financing activities | <u>2,572</u> | <u>1,424</u> |
| Net (decrease)/increase in cash and cash equivalents | (17,685) | 13,996 |
| Cash and cash equivalents at beginning of year | <u>137,137</u> | <u>123,141</u> |
| Cash and cash equivalents at end of year | <u>\$119,452</u> | <u>\$137,137</u> |
| SUPPLEMENTAL DISCLOSURES | | |
| Purchases of property, plant, and equipment in accounts payable | \$ 1,097 | \$ 4,473 |
| Cash paid for interest | 10,054 | 10,674 |
| Tax payments | 868 | 325 |
| Contributed securities | 453 | 5,937 |

The accompanying notes are an integral part of the consolidated financial statements.

VILLANOVA UNIVERSITY AND SUBSIDIARIES
NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED MAY 31, 2009

NOTE 1 - SUMMARY OF NATURE OF OPERATIONS, SIGNIFICANT ACCOUNTING POLICIES AND REPORTING PRACTICES:

Nature of Operations

Villanova University and Subsidiaries (the “University”) is an independent, coeducational institution offering undergraduate and graduate instruction, located in Radnor Township, Delaware County, Pennsylvania. The campus presently covers approximately 260 acres and comprises 72 buildings. The University also has a Conference Center approximately one-half mile from the campus which encompasses 32 acres. The University has approximately 10,200 students, of whom approximately 6,400 are full-time undergraduates. Refer to Note 15 for a description of the University’s subsidiaries.

Significant Accounting Policies and Reporting Practices

Principles of Consolidation

The consolidated financial statements include the accounts of the University and its subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

Financial Statement Presentation

The accompanying consolidated financial statements have been prepared on the accrual basis of accounting.

Resources are reported for accounting purposes into separate classes of net assets based on the existence or absence of donor-imposed restrictions. In the accompanying consolidated financial statements, net assets that have similar characteristics have been combined into similar categories. Change in net assets from operating activities, in the consolidated statement of activities, reflects all transactions increasing or decreasing unrestricted net assets.

- **Unrestricted Net Assets** - Unrestricted net assets generally result from revenues derived from providing services, receiving unrestricted contributions, receiving dividends and interest from investing in income-producing assets, and unrestricted gains and losses, less expenses incurred in providing services, raising contributions, and performing administrative functions. Unrestricted net assets may be designated for specific purposes by action of the Board of Trustees.
- **Temporarily Restricted Net Assets** – Temporarily restricted net assets generally result from contributions and other inflows of assets whose use by the University is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the University pursuant to those stipulations or by law. Gifts of cash and other non-capital assets are reported as temporarily restricted operating revenue if the gifts are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose for restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statement of activities as net assets released from restrictions.
- **Permanently Restricted Net Assets** – Permanently restricted net assets generally represent the corpus of contributions and other inflows of assets whose use by the University is limited by donor-imposed stipulations that neither expire by the passage of time nor can be fulfilled or otherwise removed by the University.

Fair Value

Effective June 1, 2008, the University adopted the provisions of Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards (FASB) No. 157, “Fair Value Measurements” (SFAS 157), which defines the term “fair value,” establishes a framework for measuring it within generally accepted accounting principles, and expands disclosure about fair value measurements.

NOTE 1 - SUMMARY OF NATURE OF OPERATIONS, SIGNIFICANT ACCOUNTING POLICIES AND REPORTING PRACTICES: (Continued)

SFAS 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering assumptions, SFAS 157 establishes a three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. SFAS 157 expands disclosures about instruments measured at fair value. SFAS 157 also applies to other accounting pronouncements that require or permit fair value measurements and, accordingly, SFAS 157 does not require any new fair value measurements. Adopting SFAS 157 did not have a material impact on the University's financial position and results of operations.

As noted above, SFAS 157 establishes a three-level valuation hierarchy for disclosure of fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

- *Level 1* – Observable inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets;
- *Level 2* – Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the same term of the financial instrument; and
- *Level 3* – Unobservable inputs to the valuation methodology in which there is little or no market data and which are significant to the fair value measurement.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

Cash and Cash Equivalents

Cash and cash equivalents represent demand deposits and other investments with an original maturity date not exceeding 90 days, while short-term investments reflect liquid investments with a maturity date in excess of 90 days, but less than one year.

Investments

The University records investments at fair value in accordance with SFAS 157. Gains or losses on investments are recognized as increases or decreases in unrestricted net assets unless their use is temporarily or permanently restricted by explicit donor stipulations or by law.

Investment Income

Investment income related to long-term investments is recorded as non-operating income, and the portion of investment income that is utilized in operating revenues under the University's endowment spending formula (see description in Note 3) is shown as a reduction in non-operating income ("Endowment resources"). Investment income related to the endowment is classified as unrestricted or temporarily restricted, depending on donor specifications and applicable law.

Student Loans Receivable

Student loans receivable are stated net of allowances for doubtful accounts. Student loans receivable are principally amounts due from students under U.S. Government-sponsored loan programs, which are subject to significant restrictions.

Land, Building, and Equipment

Land, buildings and equipment are carried at cost or fair value on the date of gift. Depreciation is computed on a straight-line basis over the estimated useful lives of land improvements (10-25 years), buildings (10-55 years) and equipment (4-10 years). All gifts of land, buildings and equipment are recorded as unrestricted non-operating activity unless explicit donor stipulations specify how the donated assets must be used.

Capitalized Software Costs

Capitalized software costs included in property, plant and equipment relate to purchased software, which is capitalized and depreciated on a straight-line basis over a five-year period.

NOTE 1 - SUMMARY OF NATURE OF OPERATIONS, SIGNIFICANT ACCOUNTING POLICIES AND REPORTING PRACTICES: (Continued)

Early Retirement Benefits

The University offers an early retirement program to full-time faculty members who meet certain eligibility criteria. The University accrues the present value of all future benefit payments in accrued expenses for individuals who accept the University's early retirement offer at the time of acceptance.

Deferred Revenue

All revenues received and expenditures incurred prior to the end of the fiscal year which relate to the following fiscal year are recorded as deferred revenues or other assets, respectively.

Noncash Gifts

Noncash gifts are recorded at fair value on the date of donation.

Use of Estimates

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

Statement of Activities

Operating revenues reflect all transactions increasing unrestricted and temporarily restricted net assets except those of a capital or long-term nature, such as gifts for long-term investments and endowments. Operating revenues include realized gains appropriated in accordance with the University's endowment spending policy (see description in Note 3).

Operation and maintenance of plant, depreciation and interest expenses have been allocated to the other operating expense categories in Note 10. In addition, student tuition and fees as well as sales and services of auxiliary enterprises are shown net of student financial aid.

Reclassification

Certain amounts from prior years have been reclassified to confirm to the current year's presentation.

NOTE 2 - DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS:

At May 31, 2009 and 2008, the fair value of cash and cash equivalents, short-term investments, and deposits with bond trustees approximate their respective carrying amounts. The fair value of short-term investments, investments and deposits with bond trustees are based on the quoted market price of the underlying securities; the fair value of long-term debt is estimated based primarily on quoted market prices of similar bonds and currently offered mortgage interest rates.

The aggregate carrying amount and fair value of the University's outstanding bonds at May 31, 2009 and 2008 are as follows:

| <u>2009</u> | | <u>2008</u> | |
|-----------------|---------------|-----------------|---------------|
| Carrying Amount | Fair Value | Carrying Amount | Fair Value |
| \$200,780,000 | \$205,759,000 | \$207,730,000 | \$212,586,000 |

Determination of the fair value of student loans receivable, which are primarily federally sponsored student loans with U.S. government mandated interest rates and repayment terms and subject to significant restrictions as to their transfer or disposition, could not be made without incurring excessive costs.

NOTE 2 - DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS: (Continued)

The following table presents the financial instruments carried at fair value on a recurring basis as of May 31, 2009, and indicates the fair value hierarchy of the valuation techniques that were utilized to determine such fair value.

| | Fair Value Measurements at Reporting Date Using (in thousands) | | | |
|--|---|------------------|------------------|-------------------|
| | Fair Value | Level 1 | Level 2 | Level 3 |
| Cash and cash equivalents | \$ 14,846 | \$ 14,846 | - | - |
| Domestic equities | 47,116 | 29,760 | - | \$ 17,356 |
| Domestic corporate and other bonds | 41,338 | 10,854 | \$ 30,484 | - |
| Foreign equities | 39,533 | 13,419 | 26,114 | - |
| Hedge funds | 58,691 | - | - | 58,691 |
| Inflation hedging | 29,302 | 12,271 | 15,554 | 1,477 |
| Private equities | 8,812 | - | - | 8,812 |
| Venture capital | 7,373 | - | - | 7,373 |
| Real estate | 1,247 | - | - | 1,247 |
| Senior loan fund | 16,404 | - | - | 16,404 |
| Other investments | 4,942 | 4,942 | - | - |
| Total investments at fair value | \$ 269,604 | \$ 86,092 | \$ 72,152 | \$ 111,360 |

Following is a description of the University's valuation methodologies for assets measured at fair value. Fair value for Level 1 is based upon quoted market prices. Fair value for Level 2 is based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets. Inputs are obtained from various sources including market participants, dealers, and brokers. Level 3, which primarily consists of alternative investments (principally interests in hedge funds, private equity, venture capital, inflation hedging, real estate, and natural resources partnerships), represents the University's ownership interest in the net asset value (NAV) of the respective partnership. Investments consist of marketable securities as well as securities that do not have readily determinable fair values. The fair values of the securities that do not have readily determinable fair values are determined by the investment fund manager and are based on historical costs, appraisals, or other estimates that require varying degrees of judgment. If no public market exists for the investment securities, the fair value is determined by the general partner taking into consideration, among other things, the cost of the securities, prices of recent significant placements of securities of the same issuer, and subsequent developments concerning the companies to which the securities relate.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the University believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

NOTE 2 - DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS: (Continued)

The following table is a rollforward of the statement of financial position amounts for financial instruments classified by the University within Level 3 of the valuation hierarchy defined above:

| | Level 3 Fair Value Measurements (in thousands) | | | | | Total |
|--------------------------------------|--|------------------|-------------------|------------------|------------------|------------------|
| | Domestic Equities | Hedge Funds | Inflation Hedging | Private Equities | Senior Loan Fund | |
| Fair Value, June 1, 2008 | - | \$ 67,405 | \$ 14,638 | \$ 16,524 | - | \$ 98,567 |
| Unrealized Gains/(Losses) | \$ (4,344) | (7,769) | (7,102) | (3,686) | \$ 1,404 | (21,497) |
| Net Purchases, sales and settlements | 21,700 | (945) | (4,812) | 3,347 | 15,000 | 34,290 |
| Fair Value, May 31, 2009 | <u>\$ 17,356</u> | <u>\$ 58,691</u> | <u>\$ 2,724</u> | <u>\$ 16,185</u> | <u>\$ 16,404</u> | <u>\$111,360</u> |

The amount of unrealized gains/(losses) related to financial instruments held at May 31, 2009, included in the statement of activities is as follows (in thousands):

| | |
|-------------------|--------------------|
| Domestic Equities | \$ (4,344) |
| Hedge Funds | (7,769) |
| Inflation Hedging | (30) |
| Private Equities | (3,686) |
| Senior Loan Fund | 1,404 |
| Total | <u>\$ (14,425)</u> |

NOTE 3 - NET ASSETS:

| | (in thousands) | |
|--|-------------------|-------------------|
| | 2009 | 2008 |
| Temporarily restricted net assets consist of the following: | | |
| Unexpended income for instruction and scholarships | \$ 15,603 | \$ 17,193 |
| Unexpended income for capital expenditures | 1,190 | 17,811 |
| Property, plant, and equipment acquired through donations | 35,318 | 17,062 |
| Annuity and life income funds | 1,979 | 1,361 |
| Endowment – accumulated change in market value of investments and realized gains | 25,013 | 77,101 |
| | <u>\$ 79,103</u> | <u>\$ 130,528</u> |
| Permanently restricted net assets consist of the following: | | |
| Student loans | \$ 1,862 | \$ 1,936 |
| Endowment principal, primarily for scholarships and instruction | 134,756 | 130,168 |
| | <u>\$ 136,618</u> | <u>\$ 132,104</u> |

NOTE 3 - NET ASSETS: (Continued)

In August 2008, the FASB issued FASB Staff Position No. 117-1, "Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds (FSP FAS 117-1), which, among other things, provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Act of 2006 (UPMIFA) and additional disclosures about an organization's endowment funds. The University is not subject to UPMIFA's guidance on the net asset classification of donor-restricted endowment funds as the State of Pennsylvania has not adopted UPMIFA. However, under FSP FAS 117-1, a not-for-profit organization, whether or not it is subject to an enacted version of UPMIFA, shall disclose information to enable users of financial statements to understand the net asset classification, net asset composition, changes in net asset composition, spending policy, and related investment policy of its endowment funds. The following disclosures are made as required by FSP FAS 117-1.

The University's endowment consists of approximately 450 individual funds established for a variety of purposes. The endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. Net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

The University has interpreted relevant Pennsylvania law as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the University classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the University in a manner consistent with the standard of prudence prescribed by Pennsylvania law.

The University has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the University must hold in perpetuity or for a donor-specific period(s) as well as board-designated funds. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce a real return, net of inflation and investment management costs, of at least 5% over the long term. Actual returns in any given year may vary from this amount.

To satisfy its long-term rate-of-return objectives, the University relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The University targets a diversified asset allocation that places a greater emphasis on equity-based and alternative investments to achieve its long-term objective within prudent risk constraints.

Under the University's spending policy, the University utilizes endowment and quasi-endowment resources to support operations at a level of 5% of the 12 calendar quarter moving average of the fair value of endowment and quasi-endowment investment assets calculated as of December 31st of the year immediately preceding the beginning of the University's fiscal year. Any difference between actual investment income and the amounts distributed is retained to support operations of future years. These retained balances are used in any year that the actual total investment return is below the spending rate. The remaining realized and unrealized gains/losses are reported as non-operating revenues. In establishing this policy, the University considered the long-term expected return on its endowment. Accordingly, over the long term, the University expects the current spending policy to allow its endowment to grow at an average of the long-term rate of inflation. This is consistent with the University's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specific term as well as to provide additional real growth through new gifts and investment return.

NOTE 3 - NET ASSETS: (Continued)

At May 31, 2009, the endowment net asset composition by type of fund consisted of the following:

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|------------------------|-------------------|---------------------------|---------------------------|-------------------|
| Donor-restricted funds | \$ - | \$ 25,013 | \$ 118,017 | \$ 143,030 |
| Board-designated funds | 122,685 | - | - | 122,685 |
| Total Funds | <u>\$ 122,685</u> | <u>\$ 25,013</u> | <u>\$ 118,017</u> | <u>\$ 265,715</u> |

Changes in endowment net assets for the fiscal year ended May 31, 2009 consisted of the following:

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|---|-------------------|---------------------------|---------------------------|-------------------|
| Endowment net assets, beginning of year | \$ 170,955 | \$ 77,101 | \$ 107,199 | \$ 355,255 |
| Investment return: | | | | |
| Investment Income | 1,004 | 2,883 | - | 3,887 |
| Management and Admin Fees | (1,397) | (1,375) | - | (2,772) |
| Net depreciation (realized and unrealized) | (48,821) | (47,446) | - | (96,267) |
| Total investment return | (49,214) | (45,938) | - | (95,152) |
| Contributions | - | - | 10,818 | 10,818 |
| Planned Savings | 8,800 | - | - | 8,800 |
| Distribution for Spending | (8,356) | (6,150) | - | (14,506) |
| Other changes: | | | | |
| Aldwyn Lane Distribution | 500 | - | - | 500 |
| Endowment net assets, end of year | <u>\$ 122,685</u> | <u>\$ 25,013</u> | <u>\$ 118,017</u> | <u>\$ 265,715</u> |

At May 31, 2008, the endowment net asset composition by type of fund consisted of the following:

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|------------------------|-------------------|---------------------------|---------------------------|-------------------|
| Donor-restricted funds | \$ - | \$ 77,101 | \$ 107,199 | \$ 184,300 |
| Board-designated funds | 170,955 | - | - | 170,955 |
| Total Funds | <u>\$ 170,955</u> | <u>\$ 77,101</u> | <u>\$ 107,199</u> | <u>\$ 355,255</u> |

NOTE 3 - NET ASSETS: (Continued)

Changes in endowment net assets for the fiscal year ended May 31, 2008 consisted of the following:

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|---|-------------------|---------------------------|---------------------------|-------------------|
| Endowment net assets, beginning of year | \$ 162,546 | \$ 75,409 | \$ 97,778 | \$ 335,733 |
| Investment return: | | | | |
| Investment Income | 2,597 | 3,096 | - | 5,693 |
| Management and Admin Fees | (1,279) | (997) | - | (2,276) |
| Net appreciation (realized and unrealized) | 5,180 | 4,973 | - | 10,153 |
| Total investment return | 6,498 | 7,072 | - | 13,570 |
| Contributions | - | - | 9,421 | 9,421 |
| Planned Savings | 8,300 | - | - | 8,300 |
| Distribution for Spending | (6,839) | (5,380) | - | (12,219) |
| Other changes: | | | | |
| Aldwyn Lane Distribution | 450 | - | - | 450 |
| Endowment net assets, end of year | <u>\$ 170,955</u> | <u>\$ 77,101</u> | <u>\$ 107,199</u> | <u>\$ 355,255</u> |

NOTE 4 - ASSETS WHOSE USE IS LIMITED:

Assets whose use is limited were comprised primarily of unspent proceeds from the issuance of long-term debt related to construction projects, as well as amounts required to be held by bond trustees for debt service payments. As of May 31, 2009, proceeds from the issuance of long-term debt related to construction projects were fully expended.

NOTE 5 - INVESTMENTS:

Investments at May 31, 2009 and 2008 consisted of the following:

| | (in thousands) | | | |
|------------------------------------|-------------------|-------------------|-------------------|-------------------|
| | 2009 | | 2008 | |
| | FAIR VALUE | COST | FAIR VALUE | COST |
| Domestic equities | \$ 47,116 | \$ 55,322 | \$ 96,933 | \$ 85,930 |
| Domestic corporate and other bonds | 41,338 | 40,697 | 38,079 | 37,372 |
| Foreign equities | 39,533 | 47,690 | 81,068 | 59,273 |
| Foreign bonds | - | - | 19 | 19 |
| Hedge funds | 58,691 | 54,001 | 67,405 | 54,947 |
| Inflation hedging | 29,302 | 24,423 | 48,066 | 30,974 |
| Cash and cash equivalents | 14,846 | 14,846 | 7,076 | 7,075 |
| Other | 38,778 | 39,722 | 20,248 | 17,862 |
| | <u>\$ 269,604</u> | <u>\$ 276,701</u> | <u>\$ 358,894</u> | <u>\$ 293,452</u> |

NOTE 5 - INVESTMENTS: (Continued)

The University uses various external investment managers to diversify the investments in alternative assets. The largest allocation to any alternative investment strategy manager as of May 31, 2009 and 2008 was 7.2% and 9.4%, respectively. At May 31, 2009, based on partnership agreements, the University was committed to invest an additional \$36.5 million in alternative investments, which is expected to occur over the next five to ten years. Alternative investments have liquidity restrictions. Amounts can be divested only at specified times based on terms in the partnership agreements. The financial statements of the limited partnerships are audited annually, generally as of December 31.

Investment gain (loss) consisted of and is reported in the consolidated statements of activities as follows for the year ended May 31:

| | (in thousands) | |
|---|--------------------|------------------|
| | 2009 | 2008 |
| Interest and dividends | \$ 1,192 | \$ 3,413 |
| Net realized (losses) gains | (24,712) | 24,849 |
| Net change in unrealized gains and losses | (73,198) | (14,809) |
| | <u>\$ (96,718)</u> | <u>\$ 13,453</u> |

NOTE 6 - LAND, BUILDINGS, AND EQUIPMENT:

Land, buildings, and equipment at May 31, 2009 and 2008 consisted of the following:

| | (in thousands) | |
|--|-------------------|-------------------|
| | 2009 | 2008 |
| Land and improvements | \$ 27,022 | \$ 26,855 |
| Buildings and improvements | 397,053 | 358,247 |
| Equipment | 50,099 | 48,242 |
| Construction in progress | 53,970 | 40,541 |
| Capitalized interest | 519 | 1,162 |
| Unamortized asset retirement costs | 1,429 | 1,849 |
| Aldwyn Lane Rental Properties – Land and Buildings | 18,385 | 18,385 |
| | <u>548,477</u> | <u>495,281</u> |
| Less accumulated depreciation | <u>(213,628)</u> | <u>(199,394)</u> |
| | <u>\$ 334,849</u> | <u>\$ 295,887</u> |

Depreciation expense totaled \$14,801,000 and \$13,068,000 for the years ended May 31, 2009 and 2008, respectively.

NOTE 7 - ACCRUED EXPENSES:

Accrued expenses at May 31, 2009 and 2008 consisted of the following:

| | (in thousands) | |
|--------------------------------|------------------|------------------|
| | 2009 | 2008 |
| Faculty and Staff Salaries | \$ 12,418 | \$ 11,700 |
| Early Retirement Plan Payments | 889 | 1,239 |
| Interest on Long-Term Debt | 1,747 | 1,821 |
| Vacation Accrual | 2,195 | 2,068 |
| Asset Retirement Obligations | 2,108 | 2,646 |
| Payroll Tax Withholdings | 1,918 | 1,943 |
| Annuities Payable | 1,777 | 1,084 |
| Workers Compensation Claims | 1,316 | 1,265 |
| Other | 6,820 | 4,988 |
| | <u>\$ 31,188</u> | <u>\$ 28,754</u> |

NOTE 8 - LONG-TERM DEBT:

Long-term debt payable at May 31, 2009 and 2008 consisted of the following:

| DESCRIPTION | MATURITY DATE | INTEREST RATE | (in thousands) PRINCIPAL BALANCE | |
|--|------------------------------|----------------------|-------------------------------------|-------------|
| | | | 2009 | 2008 |
| Delaware County Authority (a): | | | | |
| 2006 Bonds | 8/1/2009 to 8/1/2024 | 3.50% to 5.00% | \$ 50,751 * | \$ 51,642 * |
| 2005 Bonds | 8/1/2009 to 8/1/2024 | 3.00% to 5.00% | 25,345 * | 26,405 * |
| 2003 Bonds | 8/1/2009 to 8/1/2022 | 4.00% to 5.25% | 34,687 * | 36,435 * |
| 2002 Bonds | 8/1/2017 | variable | 8,310 | 9,065 |
| 2001 Bonds | 8/1/2030 to 8/1/2032 | variable | 12,525 | 12,525 |
| 1998 B Bonds | 12/1/2009 to 12/1/2015 | 4.15% to 4.75% | 8,235 * | 9,221 * |
| 1998 A Bonds | 12/1/2009 to 12/1/2028 | 4.70% to 5.50% | 65,080 * | 66,902 * |
| U.S. Dept. of HUD (b): | | | | |
| 1969 Dormitory Bonds | 4/1/2019 | 3.00% | 670 | 725 |
| Mortgage Note – Aldwyn Lane Rental Properties (c) | 1/10/2022 | 7.35% | 11,008 | 11,517 |
| | | | \$ 216,611 | \$ 224,437 |

NOTE 8 - LONG-TERM DEBT: (Continued)

*Net of original issue discount/(premium) as follows:

| | (in thousands) | |
|-------------|-------------------|-------------------|
| | 2009 | 2008 |
| 2006 Bonds | \$ (2,216) | \$ (2,362) |
| 2005 Bonds | (835) | (890) |
| 2003 Bonds | (2,417) | (2,600) |
| 1998B Bonds | 25 | 29 |
| 1998A Bonds | 1,290 | 1,358 |
| | <u>\$ (4,153)</u> | <u>\$ (4,465)</u> |

- (a) The University has pledged and granted to the Delaware County Authority a lien on and security interest in the University's unrestricted revenues and certain property and equipment to collateralize the annual principal maturities and interest payments which average approximately \$16,926,000 through 2014, and \$12,359,000 from 2015 to 2032. The University is required to maintain unrestricted net revenues equal to 100% of the annual debt service requirement.
- (b) To collateralize the annual principal and interest payments, the University has granted a mortgage lien on the Stanford dormitory and related parcels of land. Annual principal and interest payments are approximately \$80,000.
- (c) The mortgage note on the Aldwyn Lane rental properties is collateralized by the related buildings and parcels of land. The mortgage note is non-recourse to the University. Equal monthly payments are to be made over the twenty-year term of the loan.

Aggregate maturities of long-term debt including call provisions at 100% for each of the next five fiscal years are as follows (in thousands):

| | |
|------------|---------|
| 2010 | \$7,842 |
| 2011 | 8,199 |
| 2012 | 8,588 |
| 2013 | 9,027 |
| 2014 | 9,483 |
| Thereafter | 169,319 |

Interest paid on long-term debt amounted to \$10,054,000 and \$10,674,000 for the years ended May 31, 2009 and 2008, respectively. Interest expense allocated to the operating expense categories in the consolidated statement of activities amounted to \$8,690,000 and \$8,908,000 for the years ended May 31, 2009 and 2008, respectively.

The University is required, among other things, to generate net revenue at least equal to 100% of annual debt service requirements. The University was in compliance with such requirements at May 31, 2009 and 2008.

NOTE 9 - PENSION AND OTHER POSTRETIREMENT BENEFIT COSTS:

For full-time faculty members and for certain full-time non-academic employees not covered by the defined benefit plan, the University sponsors a defined contribution retirement plan under which the University makes annual contributions for the benefit of the participants to either the Teachers Insurance Annuity Association of America--College Retirement Equities Fund (TIAA-CREF) or The Vanguard Group, at the option of the participants, and the University has no further liability. The University's contributions to the defined contribution plan amounted to \$9,309,000 and \$8,809,000 for the years ended May 31, 2009 and 2008, respectively.

The University has a non-contributory defined benefit pension plan for certain full-time non-academic employees employed prior to May 31, 1996. Benefits under the plan are based on years of service and the highest average level of earnings for any three consecutive years during the last ten years of service. In October 1999, the University offered participants in the plan the opportunity to transfer to the defined contribution plan effective January 1, 2000. Effective January 1, 2000, the benefits for new retirees, those employees that did not transfer to the defined contribution plan in October 1999 and those employees retiring between June 1, 1998 and December 31, 1999 are based on the highest average level of earnings for any three consecutive years during the last ten years of service.

NOTE 9 - PENSION AND OTHER POSTRETIREMENT BENEFIT COSTS: (Continued)

The University provides postretirement medical benefits to all employees who meet certain eligibility requirements. The University accrues for expected medical postretirement benefits over the years that the employees render the necessary service.

The University recognizes the funded status pursuant to the provisions of FASB Statement No. 159, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans* (i.e., the difference between the fair value of plan assets and the benefit obligation) of its pension and other postretirement plans in the consolidated statement of financial position, with a corresponding adjustment to unrestricted net assets. These amounts are recognized as net periodic cost. Further, actuarial gains and losses that are not recognized as net periodic costs in the same periods are recognized as other changes in unrestricted net assets.

The following is a reconciliation of the beginning and ending balances of the pension benefits projected benefit obligation of the University (in thousands):

| Change in Benefit Obligation | 2009 | 2008 |
|---|------------------|------------------|
| Benefit obligation at the beginning of the year | \$ 44,564 | \$ 44,440 |
| Interest cost on projected benefit obligations | 2,720 | 2,573 |
| Service costs – during the year | 433 | 435 |
| Actuarial (gain)/loss | (1,878) | (697) |
| Benefits and administrative expenses paid | (2,294) | (2,187) |
| Benefit obligation at the end of the year | <u>\$ 43,545</u> | <u>\$ 44,564</u> |

The following table sets forth the funded status and amount recognized in the University's consolidated balance sheets for its defined benefit plan:

| Change in Plan Assets | 2009 | 2008 |
|--|------------------|------------------|
| Fair value of plan assets at beginning of year | \$ 42,787 | \$ 41,853 |
| Actual return on plan assets | (8,168) | 21 |
| Employer contributions | - | 3,100 |
| Benefits and administrative expenses paid | (2,294) | (2,187) |
| Fair value of plan assets at end of year | <u>\$ 32,325</u> | <u>\$ 42,787</u> |

Funded Status

Actuarial present value of benefit obligations:

| | | |
|------------------------------|--------------------|-------------------|
| Projected benefit obligation | \$ (43,545) | \$ (44,564) |
| Plan assets at fair value* | <u>32,325</u> | <u>42,787</u> |
| Funded Status | <u>\$ (11,220)</u> | <u>\$ (1,777)</u> |

*Consist principally of investments in debt and equity funds.

NOTE 9 - PENSION AND OTHER POSTRETIREMENT BENEFIT COSTS: (Continued)

The principal assumptions used in determining the actuarial present value of projected benefit obligations were as follows:

| | 2009 | 2008 |
|---|-------------|-------------|
| Weighted average discount rate | 6.76% | 6.25% |
| Rate of increase in compensation levels | 4.00% | 4.00% |
| Expected long-term rate of return on assets | 8.00% | 8.50% |

| | (in thousands) | |
|--|-----------------------|-----------------|
| Components of Net Periodic Benefit Cost | 2009 | 2008 |
| Service cost – benefits earned during the period | \$ 433 | \$ 436 |
| Interest cost on projected benefit obligation | 2,720 | 2,573 |
| Expected return on plan assets | (3,525) | (3,658) |
| Amortization of unrecognized net loss | 778 | 320 |
| Amortization of prior service cost | 9 | 89 |
| Total net periodic benefit cost | <u>\$ 415</u> | <u>\$ (240)</u> |

Plan assets are allocated at May 31, 2009 and May 31, 2008 as follows:

| Plan Assets | 2009 | 2008 |
|--------------------|-------------|-------------|
| Equity Securities | 60% | 61% |
| Debt Securities | 39% | 39% |
| Other | 1% | 0% |
| Total | <u>100%</u> | <u>100%</u> |

The expected benefit payments from the Plan in subsequent years are as follows:

| Year ending | (in thousands) |
|-----------------------------------|-----------------------|
| May 31, 2010 | \$ 2,829 |
| May 31, 2011 | 2,907 |
| May 31, 2012 | 3,005 |
| May 31, 2013 | 3,170 |
| May 31, 2014 | 3,253 |
| May 31, 2015 through May 31, 2019 | 17,272 |

The components of medical postretirement benefits as of May 31, 2009 and 2008 are as follows:

| | (in thousands) | |
|----------------------------------|-----------------------|-------------------|
| | 2009 | 2008 |
| Projected benefit obligation | \$ 8,982 | \$ 9,091 |
| Fair value of plan assets | - | - |
| Unfunded status | <u>\$ (8,982)</u> | <u>\$ (9,091)</u> |
| Accrued post-retirement benefits | <u>\$ (8,982)</u> | <u>\$ (9,237)</u> |
| Weighted-average assumptions: | | |
| Discount rate | 6.70% | 6.25% |

There is no healthcare cost trend rate associated with the liabilities, because the University provides a fixed subsidy for postretirement medical benefits. Benefit expense totaled \$763,000 and \$696,000 for the years ended May 31, 2009 and 2008, respectively. Benefits paid totaled \$455,000 and \$451,000 for the years ended May 31, 2009 and 2008, respectively.

The University allows faculty members that meet specific criteria for eligibility to elect to participate in an ongoing voluntary severance program. The accrued liability for future payments under this program amounted to \$889,000 and \$1,239,000 as of May 31, 2009 and 2008, respectively.

NOTE 10 - OPERATING EXPENSE:

Expenses were incurred for the following functions for the years ended May 31:

| | (in thousands) | |
|-------------------------|-----------------------|-------------------|
| | 2009 | 2008 |
| Instruction | \$ 131,470 | \$ 125,967 |
| Research | 6,293 | 6,685 |
| Academic support | 38,782 | 39,520 |
| Student services | 41,343 | 40,059 |
| Institutional support | 37,097 | 36,553 |
| Auxiliary enterprises | 64,778 | 63,006 |
| Total operating expense | <u>\$ 319,763</u> | <u>\$ 311,790</u> |

Included in the above operating expenses are expenditures related to fund-raising activities for the year ended May 31, 2009 and 2008 of approximately \$6,817,000 and \$7,206,000, respectively.

NOTE 11 - ALLOCATION OF EXPENSES:

The University allocated operation and maintenance of plant, interest on indebtedness and depreciation expenses to functional expense categories for the fiscal years ended May 31, 2009 and 2008. Those expenses were allocated to the individual functional categories as follows:

| | (in thousands) | | |
|------------------------------------|----------------------------------|---------------------------------|---------------------|
| | 2009 | | |
| | Operation and Maintenance | Interest on Indebtedness | Depreciation |
| Instruction | \$ 8,619 | \$ 4,625 | \$ 5,007 |
| Research | - | 175 | 102 |
| Academic support | 1,461 | 200 | 778 |
| Student services | 4,178 | 110 | 2,035 |
| Institutional support | 1,841 | 96 | 1,005 |
| Auxiliary enterprises | 13,118 | 3,270 | 4,577 |
| Operation and maintenance of plant | - | 214 | 1,297 |
| | <u>\$ 29,217</u> | <u>\$ 8,690</u> | <u>\$ 14,801</u> |

| | (in thousands) | | |
|------------------------------------|----------------------------------|---------------------------------|---------------------|
| | 2008 | | |
| | Operation and Maintenance | Interest on Indebtedness | Depreciation |
| Instruction | \$ 8,056 | \$ 4,615 | \$ 4,433 |
| Research | - | 192 | 92 |
| Academic support | 1,451 | 219 | 768 |
| Student services | 4,173 | 118 | 1,498 |
| Institutional support | 1,581 | 101 | 652 |
| Auxiliary enterprises | 12,793 | 3,423 | 4,396 |
| Operation and maintenance of plant | - | 240 | 1,229 |
| | <u>\$ 28,054</u> | <u>\$ 8,908</u> | <u>\$ 13,068</u> |

NOTE 12 - INCOME TAX:

The University is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. The University files IRS Form 990-T (Exempt Organization Business Income Tax Return) annually, and has recorded a liability of \$163,000 as of May 31, 2009, with regards to unrelated business income reported on IRS Form 990-T.

Effective July 1, 2007, the University adopted FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109* (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements and prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of tax position taken or expected to be taken in a tax return. FIN 48 requires the use of a two-step approach for recognizing and measuring tax benefits taken or expected to be taken in an unrelated business activity tax return and disclosures regarding uncertainties in tax positions. The first step is recognition: the University determines whether it is more likely than not that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position. In evaluating whether a tax position has met the more-likely-than-not recognition threshold, the University presumes that the position will be examined by the appropriate taxing authority that has full knowledge of all relevant information. The second step is measurement: A tax position that meets the more-likely-than-not threshold is measured to determine the amount of benefit to recognize in the financial statements. The tax position is measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement. Difference between tax positions taken in a tax return and amounts recognized in the financial statements will generally result in an increase in a liability for income taxes payable or a reduction of an income tax refund receivable. No adjustments to the financial statements were required as a result of the implementation of FIN 48.

NOTE 13 - COMMITMENTS AND CONTINGENCIES:

During the 2009 fiscal year, the University invested \$4,862,000 in eighteen long-term partnerships which were formed prior to the 2009 fiscal year, bringing its cumulative contributions to the partnerships to \$29,815,000. Under the terms of the partnership agreements, the University and other investors are committed to fund additional investments. As of May 31, 2009, the University's remaining commitments to these eighteen partnerships total approximately \$30,705,000.

The University also committed a total of \$6,000,000 to one additional long-term partnership which was formed during the 2009 fiscal year. As of May 31, 2009, the University had invested \$225,000 in this partnership. As a result, the University's remaining commitment to this partnership totals \$5,775,000.

As of May 31, 2009, the University's remaining commitments to all nineteen partnerships total \$36,480,000.

Outstanding commitments for construction contracts totaled approximately \$22,318,000 as of May 31, 2009.

The University has a \$5,000,000 unsecured line of credit. No portion of the line was utilized during the fiscal year.

NOTE 14 - UNCONDITIONAL PROMISES AND PLEDGES:

Contributions received, including unconditional promises, are recognized as revenue when the donor's commitment is received. Unconditional promises are recognized at the estimated present value of the future cash flows, net of allowances (fair value). Promises made that are designated for future periods or restricted by the donor for specific purposes are reported as temporarily restricted or permanently restricted support. However, if a restriction is fulfilled in the same time period in which the contribution is received, the University reports the support as unrestricted. Conditional promises are recorded when donor stipulations are substantially met.

NOTE 14 - UNCONDITIONAL PROMISES AND PLEDGES: (Continued)

Unconditional promises at May 31, 2009 and 2008 and the time periods in which they are expected to be realized are as follows:

| | (in thousands) | |
|---------------------------------|------------------|------------------|
| | 2009 | 2008 |
| In one year or less | \$ 18,507 | \$ 19,331 |
| Between one year and five years | 18,782 | 27,360 |
| In more than five years | 576 | 946 |
| Less: Discount | (3,021) | (3,639) |
| Allowance for doubtful accounts | (6,161) | (6,239) |
| | <u>\$ 28,683</u> | <u>\$ 37,759</u> |

Estimated cash flows from pledge receivables due after one year are discounted using a base rate of the Federal Reserve Treasury constant maturities 5-year rate of return, adjusted for a risk factor related to potential write-offs of uncollectible pledges.

NOTE 15 - SUBSIDIARIES:

The Aldwyn Lane LLC (LLC) and the Aldwyn Lane Limited Partnership (Partnership) were formed by the University for the purpose of acquiring property and office space adjacent to the campus. The LLC is 100% owned by the University, and it is the general partner in the Partnership, in which the University is the limited partner. The Partnership purchased property and office space adjacent to the campus in December 2001, and entered into an agreement to lease back the property to the previous owner for a period of twenty years. The Partnership also obtained a mortgage on the property at the time of purchase.

Rental income related to the property is collected by the Partnership, and the mortgage payments are made by the Partnership. The title to the property and the related mortgage are both held by the Partnership. The assets and liabilities of both the Partnership and the LLC are consolidated into the University financial statements, and the net income from the rental of the property is shown as non-operating income on the consolidated statement of activities.



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