



VILLANOVA
UNIVERSITY
and Subsidiaries

**FINANCIAL
STATEMENTS**
MAY 31, 2008

VILLANOVA UNIVERSITY

FINANCIAL STATEMENTS May 31, 2008

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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, 2008 and 2007 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.

PricewaterhouseCoopers LLP

July 25, 2008

VILLANOVA UNIVERSITY AND SUBSIDIARIES

Consolidated Statements of Financial Position at May 31, 2008 and 2007

(in thousands)

	<u>2008</u>	<u>2007</u>
ASSETS		
Cash and cash equivalents	\$ 137,137	\$ 123,141
Short-term investments	966	957
Accounts receivable, less allowances of \$1,476 in 2008 and \$1,420 in 2007	8,687	7,844
Inventories	2,009	1,780
Other assets	7,692	10,125
Assets whose use is limited	7,090	38,277
Pledges receivable, net	37,759	35,458
Student loans receivable, net	11,214	10,055
Investments	358,894	339,397
Land, buildings and equipment, net	<u>295,887</u>	<u>261,152</u>
Total assets	<u>\$ 867,335</u>	<u>\$ 828,186</u>
LIABILITIES		
Accounts payable	\$ 12,502	\$ 16,220
Accrued expenses	28,754	28,530
Deposits	4,806	4,431
Deferred revenues	9,618	8,858
Accrued postretirement benefits	9,237	8,992
Refundable government loan funds	6,152	6,040
Long-term debt	224,437	231,977
Accrued pension cost	<u>1,777</u>	<u>2,587</u>
Total liabilities	<u>297,283</u>	<u>307,635</u>
NET ASSETS		
Unrestricted	307,420	281,418
Temporarily restricted	130,528	119,474
Permanently restricted	<u>132,104</u>	<u>119,659</u>
Total net assets	<u>570,052</u>	<u>520,551</u>
Total liabilities and net assets	<u>\$ 867,335</u>	<u>\$ 828,186</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 Statement of Activities for the Year Ended May 31, 2007

(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 \$56,594 in student financial aid	\$209,997			\$209,997
Sales and services of auxiliary enterprises, net of \$2,010 in student financial aid	61,568			61,568
	<u>271,565</u>			<u>271,565</u>
Private gifts and grants	9,969	\$ 11,096		21,065
Government grants	12,666			12,666
Endowment resources	5,757	4,889		10,646
Investment income	9,235	343		9,578
Other sources	13,391	68		13,459
Net assets released from restrictions	6,207	(8,463)	\$ 2,256	-
Total operating revenues	<u>328,790</u>	<u>7,933</u>	<u>2,256</u>	<u>338,979</u>
OPERATING EXPENSES				
Salaries and fringe benefits	172,099			172,099
Supplies and services	41,349			41,349
Depreciation	12,516			12,516
Cost of goods sold	12,884			12,884
Interest on indebtedness	9,481			9,481
Travel and special events	9,886			9,886
Utilities	8,220			8,220
Other	31,969			31,969
Total operating expenses	<u>298,404</u>	<u>-</u>	<u>-</u>	<u>298,404</u>
Change in net assets from operating activities	<u>30,386</u>	<u>7,933</u>	<u>2,256</u>	<u>40,575</u>
NON-OPERATING				
Investment Income				
Interest and dividends	1,152	1,842	410	3,404
Realized gains	4,908	4,820	40	9,768
Other				
Rental property revenue	2,017			2,017
Rental property expenses	(1,615)			(1,615)
Change in market value of investments	19,819	19,204	81	39,104
Endowment resources	(5,757)	(4,889)		(10,646)
	<u>20,524</u>	<u>20,977</u>	<u>531</u>	<u>42,032</u>
Endowment and other gifts	35	35	5,765	5,835
Change in net assets from non-operating activities	<u>20,559</u>	<u>21,012</u>	<u>6,296</u>	<u>47,867</u>
Change in net assets before other adjustments	<u>\$ 50,945</u>	<u>\$ 28,945</u>	<u>\$ 8,552</u>	<u>\$ 88,442</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, 2008 and 2007

(in thousands)

	<u>2008</u>	<u>2007</u>
Unrestricted Net Assets:		
Change in net assets before other adjustments	\$ 28,532	\$ 50,945
Adjustment for pension plan liability	<u>(2,530)</u>	<u>1,917</u>
Increase in unrestricted net assets before cumulative effect of change in accounting principle	26,002	52,862
Cumulative effect of change in accounting principle	<u>-</u>	<u>(1,862)</u>
Increase in unrestricted net assets	<u>26,002</u>	<u>51,000</u>
Temporarily Restricted Net Assets:		
Change in net assets	<u>11,054</u>	<u>28,945</u>
Increase in temporarily restricted net assets	<u>11,054</u>	<u>28,945</u>
Permanently Restricted Net Assets:		
Change in net assets	<u>12,445</u>	<u>8,552</u>
Increase in permanently restricted net assets	<u>12,445</u>	<u>8,552</u>
Increase in net assets	49,501	88,497
Net assets:		
Beginning of Year	<u>520,551</u>	<u>432,054</u>
End of Year	<u>\$570,052</u>	<u>\$520,551</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, 2008 and 2007 (in thousands)

	<u>2008</u>	<u>2007</u>
CASH FLOW FROM OPERATING ACTIVITIES		
Increase in net assets	\$ 49,501	\$ 88,497
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation	13,068	12,516
Contributions restricted for long-term investment	(6,957)	(6,369)
Realized gains on sales of investments	(24,849)	(9,768)
Change in market value of investments	14,809	(39,104)
Pension and other postretirement benefit plan adjustments	(565)	(538)
Receipt of contributed securities	(5,937)	(3,089)
Changes in operating assets and liabilities:		
Accounts receivable	(899)	(1,366)
Pledges receivable	(3,295)	(1,284)
Provision for doubtful accounts	1,053	1,228
Accounts payable and accrued expenses	2,460	2,655
Other changes	3,339	1,620
Net cash provided by operating activities	<u>41,728</u>	<u>44,998</u>
CASH FLOW FROM INVESTING ACTIVITIES		
Proceeds from sales of investments	155,787	117,243
Purchases of investments	(159,307)	(123,179)
Student loans receivable	(1,162)	(299)
Purchase of land, buildings and equipment	(53,757)	(28,441)
Short-term investments, net	(9)	428
(Increase)/decrease in assets whose use is limited	31,187	13,518
Net cash used by investing activities	<u>(27,261)</u>	<u>(20,730)</u>
CASH FLOW FROM FINANCING ACTIVITIES		
Contributions restricted for long-term investment	6,957	6,369
Repayment of debt	(7,540)	(6,586)
Government loan funds	112	(7)
Net cash provided by financing activities	<u>(471)</u>	<u>(224)</u>
Net increase in cash and cash equivalents	13,996	24,044
Cash and cash equivalents at beginning of year	<u>123,141</u>	<u>99,097</u>
Cash and cash equivalents at end of year	<u>\$ 137,137</u>	<u>\$ 123,141</u>
SUPPLEMENTAL DISCLOSURES		
Purchases of property, plant, and equipment in accounts payable	\$ 4,473	\$ 10,427
Cash paid for interest	10,674	11,023
Tax payments	325	309
Contributed securities	5,937	3,089

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, 2008

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 255 acres and comprises 70 buildings. The University also has a Conference Center approximately one-half mile from the campus which encompasses 32 acres. The University has approximately 10,300 students, of whom approximately 6,500 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.
- **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.

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.

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

Investments

The University records investments at fair value to more appropriately reflect investment activities. Marketable securities are stated at quoted market prices, and real estate is stated at most recent fair values established by outside parties. For non-marketable investments, estimates of fair value are provided by external investment managers, and are reviewed by management. 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 under the University's endowment spending formula (see description below) 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 whether it is related to the quasi-endowment or endowment, respectively.

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 market 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.

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 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 are recorded at market value on the date of donation. 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.

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

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. Under this 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.

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 conform to the current year's presentation.

NOTE 2 - DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS:

At May 31, 2008 and 2007, 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, 2008 and 2007 are as follows:

<u>2008</u>		<u>2007</u>	
Carrying Amount	Fair Value	Carrying Amount	Fair Value
\$207,730,000	\$212,586,000	\$214,430,000	\$220,778,000

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 3 - NET ASSETS:

	(in thousands)	
	<u>2008</u>	<u>2007</u>
Temporarily restricted net assets consist of the following:		
Unexpended income for instruction and scholarships	\$17,193	\$12,314
Unexpended income for capital expenditures	17,811	19,271
Property, plant, and equipment acquired through donations	17,062	11,138
Annuity and life income funds	1,361	1,342
Endowment – accumulated change in market value of investments and realized gains	<u>77,101</u>	<u>75,409</u>
	<u>\$130,528</u>	<u>\$119,474</u>

Permanently restricted net assets consist of the following:

Student loans	\$1,936	\$1,937
Endowment principal, primarily for scholarships and instruction	<u>130,168</u>	<u>117,722</u>
	<u>\$132,104</u>	<u>\$119,659</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.

NOTE 5 - INVESTMENTS:

Investments are stated at fair value. The fair value of all debt and equity securities with a readily determinable fair value is based on quotations obtained from national securities exchanges. Alternative investments, which are not readily marketable, are carried at estimated fair values as provided by the investment managers. The estimated fair value of certain alternative investments such as private equity interests, is based on valuations provided by the external investment managers as of December 31, adjusted for cash receipts and cash disbursements through May 31. The University reviews and evaluates the values provided by the investment managers, and believes that the valuation methods and assumptions used in determining the fair value of the alternative investments are reasonable. Because alternative investments are not readily marketable, their estimated value is subject to uncertainty, and therefore may differ from the value that would have been used had a ready market for such investments existed. Such difference could be material.

NOTE 5 - INVESTMENTS: (Continued)

Investments at May 31, 2008 and 2007 consisted of the following:

	(in thousands)			
	<u>2008</u>		<u>2007</u>	
	<u>FAIR</u> <u>VALUE</u>	<u>COST</u>	<u>FAIR</u> <u>VALUE</u>	<u>COST</u>
Domestic equities	\$96,933	\$85,930	\$103,212	\$81,033
Domestic corporate and other bonds	38,079	37,372	37,455	37,087
Foreign equities	81,068	59,273	84,400	51,495
Foreign bonds	19	19	355	352
Hedge funds	67,405	54,947	56,250	46,602
Inflation hedging	48,066	30,974	31,073	18,283
Cash and cash equivalents	7,076	7,075	11,579	11,579
Other	20,248	17,862	15,073	12,710
	<u>\$358,894</u>	<u>\$293,452</u>	<u>\$339,397</u>	<u>\$259,141</u>

NOTE 6 - LAND, BUILDINGS, AND EQUIPMENT:

Land, buildings, and equipment at May 31, 2008 and 2007 consisted of the following:

	(in thousands)	
	<u>2008</u>	<u>2007</u>
Land and improvements	\$26,855	\$26,830
Buildings and improvements	358,247	324,614
Equipment	48,242	43,970
Construction in progress	40,541	32,776
Capitalized interest	1,162	613
Unamortized environmental remediation costs	1,849	1,728
Aldwyn Lane Rental Properties – Land and Buildings	<u>18,385</u>	<u>18,385</u>
	495,281	448,916
Less accumulated depreciation	<u>(199,394)</u>	<u>(187,764)</u>
	<u>\$295,887</u>	<u>\$261,152</u>

Depreciation expense totaled \$13,068,000 and \$12,516,000 for the years ended May 31, 2008 and 2007, respectively.

NOTE 7 - ACCRUED EXPENSES:

Accrued expenses at May 31, 2008 and 2007 consisted of the following:

	(in thousands)	
	<u>2008</u>	<u>2007</u>
Faculty and Staff Salaries	\$11,700	\$11,194
Voluntary Severance Plan Payments	1,239	1,173
Interest on Long-Term Debt	1,821	1,886
Vacation Accrual	2,068	1,919
Asset Retirement Obligations	2,646	2,013
Payroll Tax Withholdings	1,943	1,574
Annuities Payable	1,084	1,123
Other	6,253	7,648
	<u>\$28,754</u>	<u>\$28,530</u>

NOTE 8 - LONG-TERM DEBT:

Long-term debt payable at May 31, 2008 and 2007 consisted of the following:

<u>DESCRIPTION</u>	<u>MATURITY DATE</u>	<u>INTEREST RATE</u>	<u>(in thousands)</u>	
			<u>PRINCIPAL BALANCE</u>	<u>2008</u>
Delaware County Authority (a):				
2006 Bonds	08/01/08 to 08/01/24	3.50% to 5.00%	\$ 51,642*	\$ 52,508*
2005 Bonds	08/01/08 to 08/01/24	3.00% to 5.00%	26,405*	27,435*
2003 Bonds	08/01/08 to 08/01/22	4.00% to 5.25%	36,435*	37,494*
2002 Bonds	08/01/17	variable	9,065	10,435
2001 Bonds	08/01/30 to 08/01/32	variable	12,525	12,525
1998 B Bonds	12/01/08 to 12/01/15	4.15% to 4.75%	9,221*	10,171*
1998 A Bonds	12/01/08 to 12/01/28	4.70% to 5.50%	66,902*	68,639*
U.S. Dept. of HUD (b):				
1969 Dormitory Bonds	04/01/19	3.00%	725	780
Mortgage Note – Aldwyn Lane Rental Properties (c)	01/10/22	7.35%	<u>11,517</u>	<u>11,990</u>
			<u>\$224,437</u>	<u>\$231,977</u>

NOTE 8 - LONG-TERM DEBT: (Continued)

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

	(in thousands)	
	<u>2008</u>	<u>2007</u>
2006 Bonds	\$(2,362)	\$(2,508)
2005 Bonds	(890)	(945)
2003 Bonds	(2,600)	(2,784)
1998B Bonds	29	34
1998A Bonds	<u>1,358</u>	<u>1,426</u>
	<u>\$(4,465)</u>	<u>\$(4,777)</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 \$16,757,000 through 2013, and \$12,514,000 from 2014 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 \$85,000.
- (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:

2009	\$7,513,000
2010	7,842,000
2011	8,199,000
2012	8,588,000
2013	9,027,000
Thereafter	178,803,000

Interest paid on long-term debt amounted to \$10,674,000 and \$11,023,000 for the years ended May 31, 2008 and 2007, respectively. Interest expense allocated to the operating expense categories in the consolidated statement of activities amounted to \$8,908,000 and \$9,481,000 for the years ended May 31, 2008 and 2007, 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, 2008 and 2007.

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 \$8,809,000 and \$8,080,000 for the years ended May 31, 2008 and 2007, respectively.

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

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.

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.

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*, an amendment of FASB Statements No. 87, 88, 106, and 132(R) ("SFAS 158"), which requires an employer to recognize the over-funded or under-funded status of a defined benefit postretirement plan (other than a multiemployer plan) as an asset or liability in its statement of financial position, and to recognize changes in that funded status in the year in which the changes occur. This Statement also requires an employer to measure the funded status of a plan as of the date of its year-end statement of financial position, with limited exceptions. The provisions of SFAS 158 were adopted at the end of the University's fiscal year ended May 31, 2007. The adoption of SFAS 158 reduced unrestricted net assets by approximately \$1.9 million.

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	<u>2008</u>	<u>2007</u>
Benefit obligation at the beginning of the year	\$44,440	\$42,592
Interest cost on projected benefit obligations	2,573	2,596
Service costs – during the year	435	411
Actuarial (gain)/loss	(697)	988
Benefits and administrative expenses paid	<u>(2,187)</u>	<u>(2,147)</u>
Benefit obligation at the end of the year	<u>\$44,564</u>	<u>\$44,440</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	<u>2008</u>	<u>2007</u>
Fair value of plan assets at beginning of year	\$41,853	\$37,736
Actual return on plan assets	21	5,164
Employer contributions	3,100	1,100
Benefits and administrative expenses paid	<u>(2,187)</u>	<u>(2,147)</u>
Fair value of plan assets at end of year	<u>\$42,787</u>	<u>\$41,853</u>

Funded Status

Actuarial present value of benefit obligations:		
Projected benefit obligation	\$(44,564)	\$(44,440)
Plan assets at fair value*	<u>42,787</u>	<u>41,853</u>
Funded Status	<u>\$(1,777)</u>	<u>\$(2,587)</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:

	<u>2008</u>	<u>2007</u>
Weighted average discount rate	6.25%	6.00%
Rate of increase in compensation levels	4.00%	4.00%
Expected long-term rate of return on assets	8.50%	8.50%

	(in thousands)	
Components of Net Periodic Benefit Cost	<u>2008</u>	<u>2007</u>
Service cost – benefits earned during the period	\$436	\$411
Interest cost on projected benefit obligation	2,573	2,595
Expected return on plan assets	(3,658)	(3,160)
Amortization of unrecognized net loss	320	581
Amortization of prior service cost	89	89
Total net periodic benefit cost	<u>\$(240)</u>	<u>\$516</u>

Plan assets are allocated at May 31, 2008 and May 31, 2007 as follows:

	<u>2008</u>	<u>2007</u>
Plan Assets		
Equity Securities	61%	61%
Debt Securities	39%	38%
Other	0%	1%
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, 2009	\$2,712
May 31, 2010	2,833
May 31, 2011	2,886
May 31, 2012	2,989
May 31, 2013	3,106
May 31, 2014 through May 31, 2018	16,548

The components of medical postretirement benefits as of May 31, 2008 and 2007 are as follows:

	(in thousands)	
	<u>2008</u>	<u>2007</u>
Projected benefit obligation	\$9,091	\$8,711
Fair value of plan assets	-	-
Unfunded status	<u>\$(9,091)</u>	<u>\$(8,711)</u>
Accrued post-retirement benefits	<u>\$(9,237)</u>	<u>\$(8,992)</u>
Weighted-average assumptions:		
Discount rate	6.25%	6.00%

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 \$696,000 and \$643,000 for the years ended May 31, 2008 and 2007, respectively. Benefits paid totaled \$451,000 and \$458,000 for the years ended May 31, 2008 and 2007, 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 \$1,239,000 and \$1,174,000 as of May 31, 2008 and 2007, respectively.

NOTE 10 - OPERATING EXPENSE:

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

	(in thousands)	
	<u>2008</u>	<u>2007</u>
Instruction	\$125,967	\$120,121
Research	6,685	9,770
Academic support	39,520	36,860
Student services	40,059	35,621
Institutional support	36,553	33,569
Auxiliary enterprises	<u>63,006</u>	<u>62,463</u>
Total operating expense	<u>\$311,790</u>	<u>\$298,404</u>

Included in the above operating expenses are expenditures related to fund-raising activities for the year ended May 31, 2008 and 2007 of approximately \$7,206,000 and \$7,177,000, respectively.

NOTE 11 - ALLOCATION OF EXPENSES:

The University allocated operation and maintenance of plant, interest on indebtedness and depreciation expenses to functional expense categories in the consolidated statement of activities for the fiscal years ended May 31, 2008 and 2007. Those expenses were allocated to the individual functional categories as follows:

	(in thousands)		
	<u>2008</u>		
	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>

	(in thousands)		
	<u>2007</u>		
	Operation and Maintenance	Interest on Indebtedness	Depreciation
Instruction	\$7,305	\$4,758	\$4,444
Research	-	181	91
Academic support	1,315	231	715
Student services	3,436	124	1,147
Institutional support	1,434	105	669
Auxiliary enterprises	11,904	3,823	4,507
Operation and maintenance of plant	-	259	943
	<u>\$25,394</u>	<u>\$9,481</u>	<u>\$12,516</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 \$145,000 as of May 31, 2008, 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 (FIN 48), which 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 2008 fiscal year, the University invested \$7,464,000 in fifteen long-term partnerships which were formed prior to the 2008 fiscal year, bringing its cumulative contributions to the partnerships to \$24,784,000. Under the terms of the partnership agreements, the University and other investors are committed to fund additional investments. As of May 31, 2008, the University's remaining commitments to these fifteen partnerships total approximately \$23,736,000.

The University also committed a total of \$12,000,000 to three additional long-term partnerships which were formed during the 2008 fiscal year. As of May 31, 2008, the University had invested \$169,000 in these partnerships; as a result, the University's remaining commitments to the three partnerships total \$11,831,000.

As of May 31, 2008, the University's remaining commitments to all eighteen partnerships total \$35,567,000.

Outstanding commitments for construction contracts totaled approximately \$62,600,000 as of May 31, 2008.

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, 2008 and 2007 and the time periods in which they are expected to be realized are as follows:

	(in thousands)	
	<u>2008</u>	<u>2007</u>
In one year or less	\$19,331	\$16,940
Between one year and five years	27,360	27,135
In more than five years	946	683
Less: discount	(3,639)	(4,055)
allowance for doubtful accounts	<u>(6,239)</u>	<u>(5,245)</u>
	<u>\$37,759</u>	<u>\$35,458</u>

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 preceding financial statements, and the net income from the rental of the property is shown as non-operating income on the consolidated statement of activities.

NOTE 16 - RECENT AUTHORITATIVE PRONOUNCEMENTS:

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (FASB) No. 157, "Fair Value Measurements" (SFAS 157). SFAS 157 defines the term "fair value", establishes a framework for measuring it within generally accepted accounting principles and expands disclosures about its measurements. In February 2008, the FASB issued FASB Staff Position No. FAS 157-1 ("FSP FAS 157-7") and FASB Staff Position No. FAS 157-2, ("FSP FAS 157-2"), affecting implementation of SFAS 157. FSP FAS 157-1 excludes FASB Statement No. 13, Accounting for Leases ("SFAS 13"), and other accounting pronouncements that address fair value measurements under SFAS 13, from the scope of SFAS 157. FSP FAS 157-2 delays the effective date of SFAS 157 for nonfinancial assets and nonfinancial liabilities, except for items that are recognized or disclosed at fair value on a recurring basis, to fiscal years beginning after November 15, 2008. For all other items, SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, at which time the University will be required to categorize and disclose certain assets and liabilities, including investments, at fair value, according to three levels of inputs that may be used to measure fair value:

- Level 1: Quoted prices in active markets for identical assets or liabilities.
- Level 2: Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

NOTE 16 – RECENT AUTHORITATIVE PRONOUNCEMENTS: (Continued)

SFAS 157 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. University management is evaluating the impact this will have on the consolidated financial statements beginning in fiscal year 2009.

In February 2007, the FASB issued SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities” (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS 159 is effective for fiscal years beginning after November 15, 2007. University management is evaluating what items, if any, will be measured at fair value in accordance with SFAS 159.



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