

***DRAKE UNIVERSITY***

***Financial Statements as of and for the  
Years Ended May 31, 2007 and  
2006 and Independent Auditors'  
Report***

# DRAKE UNIVERSITY

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## INDEPENDENT AUDITORS' REPORT

The Board of Trustees  
Drake University  
Des Moines, Iowa

We have audited the accompanying statements of financial position of Drake University (the "University") as of May 31, 2007 and 2006, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the management of the University. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we express no such opinion. An audit also 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, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of Drake University, as of May 31, 2007 and 2006, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the financial statements, the University adopted Statement of Financial Accounting Standards No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans – an amendment of FASB Statements No. 87, 88, 106, and 132(R)*, during the year ended May 31, 2007.

*Deloitte & Touche LLP*

October 12, 2007

# DRAKE UNIVERSITY

## STATEMENTS OF FINANCIAL POSITION MAY 31, 2007 AND 2006

<b>ASSETS</b>	<b>2007</b>	<b>2006</b>
Cash and cash equivalents	\$ 7,270,894	\$ 11,351,855
Student accounts receivable and notes receivable, net of allowance of \$175,000 in 2007 and \$125,000 in 2006	3,586,313	3,537,954
U.S. government receivables	689,475	650,997
Prepaid expenses and inventories	539,028	584,119
Contributions receivable, net	3,969,175	4,529,569
Other assets	2,303,149	2,728,013
U.S. government loans receivable, net of allowance of \$126,000 in 2007 and 2006	13,752,218	13,825,958
Investments:		
Money market accounts, commercial paper, certificates of deposit, and common collective trust funds	15,203,160	17,200,846
Bonds	29,633,931	33,491,920
Common stocks and mutual funds	152,722,187	127,866,918
Cash surrender value of life insurance policies	4,477,190	4,374,783
Real estate	7,963,388	6,380,694
Total investments	<u>209,999,856</u>	<u>189,315,161</u>
Unexpended bond funds	<u>20,772,602</u>	<u>-</u>
Land, buildings, and equipment:		
Land	17,415,747	17,105,628
Buildings	135,710,703	126,970,053
Equipment	45,789,371	42,699,975
Construction in progress	4,770,870	1,672,965
	<u>203,686,691</u>	<u>188,448,621</u>
Less accumulated depreciation	<u>(66,061,817)</u>	<u>(61,328,128)</u>
Land, buildings, and equipment, net	<u>137,624,874</u>	<u>127,120,493</u>
Funds held in trust by others	<u>10,468,200</u>	<u>9,081,822</u>
<b>TOTAL ASSETS</b>	<u><u>\$ 410,975,784</u></u>	<u><u>\$ 362,725,941</u></u>

(continued)

# DRAKE UNIVERSITY

## STATEMENTS OF FINANCIAL POSITION MAY 31, 2007 AND 2006

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<b>LIABILITIES AND NET ASSETS</b>	<b>2007</b>	<b>2006</b>
Liabilities:		
Accounts payable and accrued expenses	\$ 10,595,878	\$ 9,118,125
Student deposits and deferred income	6,673,736	6,153,059
Notes payable	-	5,803,571
Other liabilities	2,702,199	1,290,809
Annuities payable	30,547,725	37,946,752
Bonds payable	70,490,000	49,510,000
Accrued post-retirement benefit obligation	14,263,321	11,880,106
U. S. government grants refundable	<u>11,758,565</u>	<u>11,814,909</u>
 Total liabilities	 <u>147,031,424</u>	 <u>133,517,331</u>
Net assets:		
Unrestricted	154,212,721	129,002,489
Temporarily restricted	28,717,272	26,351,454
Permanently restricted	<u>81,014,367</u>	<u>73,854,667</u>
 Total net assets	 <u>263,944,360</u>	 <u>229,208,610</u>
 TOTAL LIABILITIES AND NET ASSETS	 <u>\$ 410,975,784</u>	 <u>\$ 362,725,941</u>

(concluded)

See notes to financial statements.

# DRAKE UNIVERSITY

## STATEMENT OF ACTIVITIES FOR THE YEAR ENDED MAY 31, 2007

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>OPERATING REVENUES:</b>				
Revenue, gains and other support:				
Student tuition and fees	\$ 102,723,441	\$ -	\$ -	\$ 102,723,441
Less scholarships and fellowships	(37,628,066)	-	-	(37,628,066)
Net student tuition and fees	65,095,375	-	-	65,095,375
Government grants and contracts	9,883,447	-	-	9,883,447
Private grants and contracts	49,403	1,097,759	-	1,147,162
Private gifts	2,947,771	2,792,545	-	5,740,316
Endowment income used in operations	5,900,000	-	-	5,900,000
Sales and services of auxiliary enterprises	17,661,551	-	-	17,661,551
Other income, net	2,135,403	-	-	2,135,403
Net assets released from restriction	3,248,281	(3,248,281)	-	-
Total operating revenues	106,921,231	642,023	-	107,563,254
<b>OPERATING EXPENSES:</b>				
Instruction	31,201,036	-	-	31,201,036
Public service	10,078,144	-	-	10,078,144
Academic support	15,669,493	-	-	15,669,493
Student services	8,859,105	-	-	8,859,105
Institutional support	14,246,995	-	-	14,246,995
Auxiliary enterprises	24,779,845	-	-	24,779,845
Total operating expenses	104,834,618	-	-	104,834,618
Change in net assets from operations	2,086,613	642,023	-	2,728,636
<b>NONOPERATING ACTIVITIES:</b>				
Contributions for nonoperating purposes	553,423	1,870,945	7,454,510	9,878,878
Net unrealized gains from investments	16,780,419	4,437,953	-	21,218,372
Reinvested net gains and income from investments	787,505	4,630,846	5,180	5,423,531
Change in value of split interest agreements	-	(3,097,394)	(304,271)	(3,401,665)
Loss on disposal of property and equipment	(583,754)	-	-	(583,754)
Change in fair value of interest rate swap agreements	(532,529)	-	-	(532,529)
Other nonoperating activities	-	-	4,281	4,281
Net assets released from restriction	6,118,555	(6,118,555)	-	-
Change in net assets from nonoperating activities	23,123,619	1,723,795	7,159,700	32,007,114
CHANGE IN NET ASSETS	25,210,232	2,365,818	7,159,700	34,735,750
NET ASSETS AT BEGINNING OF YEAR	129,002,489	26,351,454	73,854,667	229,208,610
NET ASSETS AT END OF YEAR	\$ 154,212,721	\$ 28,717,272	\$ 81,014,367	\$ 263,944,360

See notes to financial statements.

# DRAKE UNIVERSITY

## STATEMENT OF ACTIVITIES FOR THE YEAR ENDED MAY 31, 2006

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>OPERATING REVENUES:</b>				
Revenue, gains and other support:				
Student tuition and fees	\$ 93,890,134	\$ -	\$ -	\$ 93,890,134
Less scholarships and fellowships	(34,650,292)	-	-	(34,650,292)
Net student tuition and fees	59,239,842	-	-	59,239,842
Government grants and contracts	9,580,568	-	-	9,580,568
Private grants and contracts	210,566	880,753	-	1,091,319
Private gifts	2,865,901	1,532,695	-	4,398,596
Endowment income used in operations	5,700,000	-	-	5,700,000
Sales and services of auxiliary enterprises	15,984,029	-	-	15,984,029
Other income, net	2,621,569	-	-	2,621,569
Net assets released from restriction	2,459,486	(2,459,486)	-	-
Total operating revenues	98,661,961	(46,038)	-	98,615,923
<b>OPERATING EXPENSES:</b>				
Instruction	28,525,692	-	-	28,525,692
Public service	9,881,526	-	-	9,881,526
Academic support	15,344,137	-	-	15,344,137
Student services	8,376,542	-	-	8,376,542
Institutional support	12,680,224	-	-	12,680,224
Auxiliary enterprises	22,427,222	-	-	22,427,222
Total operating expenses	97,235,343	-	-	97,235,343
Change in net assets from operations	1,426,618	(46,038)	-	1,380,580
<b>NONOPERATING ACTIVITIES:</b>				
Contributions for nonoperating purposes	342,847	2,905,659	4,182,234	7,430,740
Net unrealized gains from investments	6,190,611	1,722,906	-	7,913,517
Reinvested net gains and income from investments	2,228,453	3,748,357	5,114	5,981,924
Change in value of split interest agreements	-	(3,732,456)	(279,506)	(4,011,962)
Loss on disposal of property and equipment	(239,269)	-	-	(239,269)
Change in fair value of interest rate swap agreements	2,537,679	-	-	2,537,679
Other nonoperating activities	-	-	5,230	5,230
Net assets released from restriction	9,712,023	(9,712,023)	-	-
Change in net assets from nonoperating activities	20,772,344	(5,067,557)	3,913,072	19,617,859
CHANGE IN NET ASSETS	22,198,962	(5,113,595)	3,913,072	20,998,439
NET ASSETS AT BEGINNING OF YEAR	106,803,527	31,465,049	69,941,595	208,210,171
NET ASSETS AT END OF YEAR	\$ 129,002,489	\$ 26,351,454	\$ 73,854,667	\$ 229,208,610

See notes to financial statements.

# DRAKE UNIVERSITY

## STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED MAY 31, 2007 AND 2006

	2007	2006
CASH FLOWS FROM OPERATING ACTIVITIES:		
Change in net assets	\$ 34,735,750	\$ 20,998,439
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	6,641,136	5,116,541
Net unrealized gains from investments	(21,218,372)	(7,913,517)
Change in fair value of interest rate swap agreements	532,529	(2,537,679)
Net realized gains from investments	(6,440,913)	(7,957,017)
Loss on disposal of property and equipment	583,754	239,269
Change in value of split interest agreements	3,401,665	4,011,962
Contributions restricted for long-term investment	(7,454,510)	(4,182,234)
Income restricted for long-term investment	(5,180)	(5,114)
Noncash contributions of investments	(5,262,041)	(1,572,181)
Change in:		
Student accounts, notes and U.S. government receivables	(86,837)	(289,820)
Prepaid expenses and inventories	45,091	251,712
Contributions receivable	560,394	2,804,518
Other assets	(43,500)	(1,003,006)
Accounts payable and accrued expenses	1,326,027	3,070,597
Student deposits and deferred income	520,677	863,128
Other liabilities	1,228,785	(22,260)
Accrued post-retirement benefit obligation	2,383,215	2,040,452
Net cash provided by operating activities	<u>11,447,670</u>	<u>13,913,790</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investments	(112,505,122)	(250,355,381)
Proceeds from sales and maturities of investments	104,165,467	255,696,004
Purchases of property and equipment	(17,477,155)	(16,628,196)
Proceeds from sales of property and equipment	18,050	22,650
Issuance of U. S. government loans receivable	(3,005,846)	(3,325,781)
Payments from U. S. government loans receivable	3,079,586	3,478,941
Net real estate and contracts receivable activity	<u>(1,582,694)</u>	<u>33,169</u>
Net cash used in investing activities	<u>(27,307,714)</u>	<u>(11,078,594)</u>

(continued)

# DRAKE UNIVERSITY

## STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED MAY 31, 2007 AND 2006

	2007	2006
CASH FLOWS FROM FINANCING ACTIVITIES:		
Issuance of notes payable	-	6,500,000
Payments on notes payable	(5,803,571)	(696,429)
Issuance of bonds payable	22,020,000	42,118,100
Bond issuance fees on refunding	-	995,000
Refunding of bonds payable	-	(42,118,100)
Payments on bonds payable	(1,040,000)	(2,025,000)
Payments to annuitants	(10,800,692)	(9,826,564)
Contributions restricted for long-term investment	7,454,510	4,182,234
Income restricted for long-term investment	5,180	5,114
Increase in U. S. government grants refundable, net	(56,344)	27,436
Net cash provided by (used in) financing activities	<u>11,779,083</u>	<u>(838,209)</u>
NET CHANGE IN CASH AND CASH EQUIVALENTS	(4,080,961)	1,996,987
CASH AND CASH EQUIVALENTS:		
BEGINNING OF YEAR	<u>11,351,855</u>	<u>9,354,868</u>
END OF YEAR	<u>\$ 7,270,894</u>	<u>\$ 11,351,855</u>
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid for interest	<u>\$ 2,179,920</u>	<u>\$ 2,892,385</u>
		(concluded)

See notes to financial statements.

# DRAKE UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED MAY 31, 2007 AND 2006

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### 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Organization and Nature of Operations** - Drake University (the "University") is an independent, private, coeducational university in Des Moines, Iowa, serving primarily students from the Midwest. The University is accredited as a member of the North Central Association of Colleges and Universities.

**Basis of Presentation** - The accompanying financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America. Net assets, revenue, expenses, and gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the University and changes therein are classified and reported as follows:

*Unrestricted* – net assets that are not subject to donor-imposed restrictions.

*Temporarily Restricted* – net assets subject to donor-imposed restrictions that may or will be met either by actions of the University and/or the passage of time.

*Permanently Restricted* – net assets subject to donor-imposed restrictions that they be maintained permanently by the University. Generally, the donors of these assets permit the University to use all or part of the income earned on related investments for general or specific purposes.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law.

Contributions, including unconditional promises to give, are recognized as revenue in the period received. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value. Contributions received with donor-imposed restrictions that are met within the same year as received are reported as revenues of the temporarily restricted net asset class. Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassifications between the applicable classes of net assets.

Contributions to be received after one year are discounted at a risk-free rate. Amortization of discounts is recorded as additional contribution revenue in accordance with donor-imposed restrictions, if any, on the contributions. An allowance for uncollectible contributions receivable is provided based upon management's judgment, including such factors as prior collection history, type of contribution, and nature of fund-raising activity.

Contributions of land, buildings, and equipment without donor stipulations concerning the use of such long-lived assets are reported as revenue of the unrestricted net asset class. Contributions of cash or other assets to be used to acquire land, buildings, and equipment with such donor stipulations are reported as revenue of the temporarily restricted net asset class; the restrictions are considered to be released at the time of acquisition of such long-lived assets.

Net unrealized and realized gains on investments and income from investments are reported as follows:

- As increases in permanently restricted net assets if the terms of the gift require that it be added to the principal of a permanent endowment fund.
- As increases in temporarily restricted net assets if the terms of the gift impose restrictions on the use of the income.
- As increases in unrestricted net assets in all other cases.

***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 judgments that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

***Cash and Cash Equivalents*** - Cash and cash equivalents include interest-bearing money market accounts, repurchase agreements, and short-term investments with a maturity of three months or less at the date of purchase that are available for current operating purposes.

***Income Taxes*** - The University has received a tax determination letter from the IRS indicating it is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code (the "Code") as a charitable educational institution. As such, the University is taxed only on any net unrelated business income under Section 511 of the Code.

***Inventories*** - Inventories of the University, primarily composed of printing supplies and physical plant items, are stated at the lower of cost (first-in, first-out) or market.

***Investments*** - Investments in commercial paper, bonds, common stocks, and mutual funds are recorded at fair value, with gains and losses included in the statements of activities. Common collective trust funds are stated at fair value as determined by the issuer of the common/collective trust funds based on the fair market value of the underlying investments. Direct investments in real estate are stated at historical cost. Expenditures for building improvements which substantially extend the useful life of an asset are capitalized. At May 31, 2007, the University had an investment balance in one stock index fund of approximately \$45,578,000 which accounted for 22% of its total investments. At May 31, 2006, the University had an investment balance in one stock index fund of approximately \$37,042,000 which accounted for 20% of its total investments. No other individual investment accounted for more than 10% of total investments at May 31, 2007 and 2006.

***Split Interest Agreements*** - The University has a number of split interest agreements with individuals that generally require annuity payments to these individuals in exchange for property, securities, or cash. The assets in the split interest agreements are stated at fair value in the University's financial statements. These assets total approximately \$53,683,000 and \$55,112,000 at May 31, 2007 and 2006, respectively, and are included in "Investments" in the statements of financial position. The University's liability to the annuitants is recorded based on the present value of the expected payments using discount rates between 5.5% and 11.0% as of May 31, 2007 and 2006. Annuities payable total approximately \$30,548,000 and \$37,947,000 at May 31, 2007 and 2006, respectively.

***Insurance Policies*** - Insurance policies donated to the University are recorded at the cash surrender value of the policy and adjusted annually for increases in such values. Certain insurance policies require premium payments over several years.

***Land, Buildings, and Equipment*** - Land, buildings, and equipment are stated at cost or, if received by gift, at the market or appraised value at the date of gift. Depreciation is provided on the straight-line basis over estimated useful lives ranging from 5 to 50 years.

Expenditures for new equipment and buildings and improvements which substantially extend the useful life of an asset are capitalized. Ordinary repairs and maintenance are expensed as incurred. The University capitalizes interest on major projects during construction and amortizes the amounts over the related assets' estimated useful lives. Costs incurred for building materials and equipment comprises construction in progress.

***Funds Held in Trust by Others*** - Funds held in trust by others are recorded at fair value. These investments, which are not in the possession or under the control of the University, are administered by outside fiscal agents, with the University deriving income from the investments as stipulated by the various gift instruments.

***U.S. Government Grants Refundable*** - Funds provided by the U.S. government under the Federal Perkins Loan and Health Professions Student Loan Programs are loaned to qualified students and may be reloaned after collections. These funds are ultimately refundable to the U.S. government and are included as a liability in the statements of financial position.

***Operating and Nonoperating Activities*** - The statements of activities reports the change in net assets from operating and nonoperating activities. Operating revenues consist of substantially all the activity of the University except for certain items specifically considered to be of a nonoperating nature. Contributions included in nonoperating activities consist of bequests and other unrestricted gifts not solicited as part of the annual fundraising campaigns, gifts restricted for the acquisition of capital assets, and gifts restricted to endowment funds. Nonoperating activities also include realized and unrealized gains/losses on investments, endowment income not used in operations, change in net present value of split interest agreements, change in fair value of interest rate swap agreements, and significant items of an unusual or nonrecurring nature.

***Fair Value of Financial Instruments*** - Financial instruments are generally described as cash, contractual obligations or rights to pay or receive cash. The carrying amount approximates fair value for certain financial instruments because of the short-term maturity of these instruments, which include cash and cash equivalents, accounts receivable, U.S. government receivables, accounts payable, and student deposits.

Fair value estimates are made at a specific point in time based on relevant market information. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and, therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Investments are recorded at fair value primarily as determined by values provided by external investment managers or quoted market prices.

Common collective trust funds are stated at fair value as determined by the issuer of the common/collective trust funds based on the fair market value of the underlying investments. Common collective trust funds with underlying investments in investment contracts are valued at fair market value of the underlying investments and then adjusted by the issuer to contract value.

U.S. government loans receivable and U.S. government grants refundable are not saleable and can only be assigned to the U.S. Government or its designees. The carrying value approximates fair value.

The carrying value of notes receivable approximates fair value because the notes bear interest at rates which approximate current rates the University could obtain on notes with similar maturities and credit qualities.

The estimated fair value of bonds payable was calculated by discounting future cash flows through estimated maturity using the borrowing rate currently available to the University for debt of similar original maturity. The carrying value of the University's notes and bonds payable was approximately \$70,490,000 and \$55,314,000 at May 31, 2007 and 2006, respectively; the fair value was approximately \$71,212,000 and \$55,865,000 at May 31, 2007 and 2006, respectively.

***Derivative Financial Instruments*** - From time to time, the University enters into interest rate swap agreements to modify the interest rate characteristics of its outstanding debt from floating to fixed. In accordance with Statement of Financial Accounting Standards ("SFAS") No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended, the University accounts for derivative instruments, including derivative instruments embedded in other contracts. SFAS No. 133 requires that derivative instruments be measured at fair value and reported as assets or liabilities in the statements of financial position. Changes in the fair value of derivatives during the year are reported in the statements of activities. The University's interest rate swap agreements are considered derivative financial instruments and have been reported as other liabilities in the statements of financial position at fair value. The net change in the fair value of the agreements during the year is reported as an unrealized gain/loss in the nonoperating activities section of the statements of activities. The net cash received or paid under the terms of the interest rate swap agreements over their term are reported as a component of interest expense.

***Fund-Raising Expenses*** - Fund-raising expenses for the University consist of development expenses, capital campaign costs, and alumni relations. Total fund-raising expenses for the years ended May 31, 2007 and 2006, were approximately \$3,088,000 and \$2,703,000, respectively.

***Adoption of New Accounting Pronouncement*** - During the year ended May 31, 2007, the University adopted Statement of Financial Accounting Standards 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 No. 158"). SFAS No. 158 requires an employer to recognize in its statement of financial position the over-funded or under-funded status of a defined benefit postretirement plan measured as the difference between the fair value of plan assets and the benefit obligation. For a pension plan, the benefit obligation is the projected benefit obligation; for any other postretirement plan, such as a retiree health care plan, the benefit obligation is the accumulated postretirement benefit obligation. SFAS No. 158 does not impact the calculation of net periodic benefit cost. In addition, SFAS No. 158 requires that the measurement date of the plan obligation coincide with an employer's fiscal year-end. Note that the funded status recognition provision of SFAS No. 158 was early-adopted by the University during the year ended May 31, 2007. See the impact of the adoption of SFAS No. 158 in Note 8. The measurement date provision of SFAS No. 158 is not effective for the University until its fiscal year ended May 31, 2009 and is expected to be adopted by the University during its fiscal year ended May 31, 2009.

## 2. CONTRIBUTIONS RECEIVABLE, NET

Net contributions receivable at May 31, 2007 and 2006, are summarized as follows:

	2007	2006
Unconditional promises expected to be collected in:		
Less than one year	\$ 1,855,928	\$ 1,927,235
One year to five years	2,552,422	3,076,981
Over five years	<u>683,750</u>	<u>800,000</u>
	5,092,100	5,804,216
Less:		
Unamortized discount on contributions receivable (3.4%-6.3%)	(555,900)	(627,567)
Allowance for uncollectible contributions	<u>(567,025)</u>	<u>(647,080)</u>
Contributions receivable, net	<u>\$ 3,969,175</u>	<u>\$ 4,529,569</u>

## 3. INVESTMENT INCOME

For the years ended May 31, 2007 and 2006, investment income consisted of the following:

	2007	2006
Interest, rents, and dividends	\$ 5,570,078	\$ 4,384,940
Net realized gains from investments	6,440,913	7,957,017
Investment expenses	<u>(687,460)</u>	<u>(660,033)</u>
Investment income, net	11,323,531	11,681,924
Net unrealized gains from investments	<u>21,218,372</u>	<u>7,913,517</u>
Total investment income	<u>\$ 32,541,903</u>	<u>\$ 19,595,441</u>

For the years ended May 31, 2007 and 2006, as reflected in the statements of activities, investment income was as follows:

	2007	2006
Operating revenues:		
Endowment income used in operations	\$ 5,900,000	\$ 5,700,000
Nonoperating activities:		
Net unrealized gains from investments	21,218,372	7,913,517
Reinvested net gains and income from investments	<u>5,423,531</u>	<u>5,981,924</u>
Total investment income	<u>\$ 32,541,903</u>	<u>\$ 19,595,441</u>

#### 4. BONDS PAYABLE

Bonds payable at May 31, 2007 and 2006 are as follows:

	2007	2006
Private College Refunding Revenue Bonds – Series 1996 5.50-5.75% bonds maturing serially on December 1 through 2008, as well as 6.5%, term bonds maturing December 1, 2011 (a) (b)	\$ 5,695,000	\$ 6,710,000
Adjustable Rate Revenue Refunding Bonds – Series 2005 Auction rate securities maturing April 1, 2031. The bond interest rate as of May 31, 2007 was 3.89% (b)	42,775,000	42,800,000
Private University Revenue Bonds – Series 2007 maturing serially on April 1, 2022. The bond interest rates are from 4.0% to 5.0% (b)	<u>22,020,000</u>	<u>-</u>
	70,490,000	49,510,000
Less current portion	<u>(2,475,000)</u>	<u>(1,365,000)</u>
Bonds payable, long-term	<u>\$ 68,015,000</u>	<u>\$ 48,145,000</u>

- (a) The University exercised the option to redeem the callable portion of the bonds on December 1, 2005, at a redemption price of 102% of par. Interest on the remaining bonds is due each June 1 and December 1. The bonds are secured by a mortgage and security agreement on the land, buildings, and equipment of Opperman Law Library, Tennis Center, and the Kinne Center. Interest and principal on the bonds are guaranteed by MBIA Insurance Corporation.

The University is required to maintain a sinking fund. The balance in the sinking fund account at May 31, 2007 and 2006 was \$700,750 and \$711,163, respectively. The bonds have two financial covenants, which were met at May 31, 2007.

In addition, the University purchased a surety bond for \$100,000 to cover the debt service reserve requirement in the loan agreement.

- (b) The net proceeds of the 2005 bonds were used to redeem the callable portion of the 1996 series as well as the entire 2001 and 2003 series bonds. The bonds have a variable interest rate with payments due every 35 days. The bonds are secured by a mortgage and security agreement on the land, buildings, and equipment of the Knapp Center, which expires December 1, 2011. Interest and principal on the bonds are guaranteed by CIFG Assurance North America Inc.

In order to minimize the impact of interest rate changes, the University entered into an interest rate swap agreement on a notional amount of \$12,000,000. Under the terms of the interest rate swap, the University receives variable interest rate payments and makes fixed interest rate payments, thereby creating the equivalent of fixed-rate debt. The swap transaction resulted in a liability of approximately \$1,327,000 and \$1,144,000 at May 31, 2007 and 2006, respectively, and is included within other liabilities in the statements of financial position. The term of the swap transaction is aligned with the underlying bonds and expires July 1, 2031.

The University entered into an interest rate swap agreement on a notional amount of \$11,500,000. Under the terms of the interest rate swap, the University receives variable interest rate payments and makes fixed interest rate payments, thereby creating the equivalent of fixed-rate debt. The swap transaction resulted in an asset of approximately \$415,000 and \$567,000 at May 31, 2007 and 2006, respectively, and is included within other assets in the statements of financial position. The term of the swap transaction is aligned with the underlying bonds and expires June 1, 2024.

The University entered into an interest rate swap agreement on a notional amount of \$16,365,000 at 3.48%. Under the terms of the interest rate swap, the University receives variable interest rate payments and makes fixed interest rate payments, thereby creating the equivalent of fixed-rate debt. The swap transaction resulted in an asset of approximately \$187,000 and \$385,000 at May 31, 2007 and 2006, respectively, and is included within other assets in the statement of financial position. The term of the swap transaction is aligned with the underlying bonds and expires December 1, 2021.

Series 2007 bonds were loaned pursuant to the Series 2005 bond agreement as amended April 1, 2007, to finance the costs of renovation of four student residence halls and the renovation and expansion of other facilities on the University’s campus.

The bonds have two financial covenants, which were met at May 31, 2007.

Reserve fund accounts totaling approximately \$1,082,000 and \$738,000 at May 31, 2007 and 2006, respectively, are included in “Investments” in the statements of financial position.

Maturities on bonds payable of the University subsequent to May 31, 2007 are as follows:

2008	\$ 2,475,000
2009	2,585,000
2010	2,660,000
2011	2,800,000
2012	5,940,000
Thereafter	<u>54,030,000</u>
	<u>\$ 70,490,000</u>

The University incurred interest expense of approximately \$2,309,000 and \$2,462,000 (including approximately \$125,000 and \$255,000 of interest expense on the notes payable disclosed in Note 5) for the years ended May 31, 2007 and 2006, respectively.

## 5. NOTES PAYABLE

On June 1, 2005, Windsor Heights, Iowa issued \$6,500,000 of Private College Revenue Bonds – Series 2005. Proceeds of the bonds were then loaned to the University to be used to renovate and expand the Drake stadium facilities. The bonds accrue interest at variable rates. Gifts and grants received by the University as a result of a capital campaign for the stadium project were used to pay off the loan during the year ended May 31, 2007. Notes payable at May 31, 2007 and 2006 were \$0 and \$5,803,571.

## 6. ENDOWMENT

The University's endowment consists of donor gifts (permanently restricted) plus other Board designated funds (unrestricted) which are deemed to be held and invested in perpetuity. The Board of Trustees approves a spending policy annually for the endowment, which is approximately 5.0% of the average market value of the endowment.

The endowment investment activity consisted of the following for the years ended May 31, 2007 and 2006:

	<b>2007</b>	<b>2006</b>
Beginning balance	<u>\$ 128,768,203</u>	<u>\$ 116,968,473</u>
Total gifts	7,978,402	3,453,538
Total other deletions	1,582,027	402,305
Return on investment:		
Interest and dividends	3,155,491	2,630,990
Management and custodial fees	(332,479)	(342,146)
Net realized gains from investments	2,913,752	5,481,312
Net unrealized gains from investments	<u>15,170,852</u>	<u>5,873,731</u>
Total	20,907,616	13,643,887
Endowment income used in operations	<u>(5,900,000)</u>	<u>(5,700,000)</u>
Endowment return net of amounts used in operations	<u>15,007,616</u>	<u>7,943,887</u>
Ending balance	<u>\$ 153,336,248</u>	<u>\$ 128,768,203</u>

## 7. TEMPORARILY AND PERMANENTLY RESTRICTED NET ASSETS

Temporarily restricted net assets consisted of the following at May 31, 2007 and 2006:

	<b>2007</b>	<b>2006</b>
Unexpended contributions for restricted purposes	\$ 2,182,466	\$ 2,116,030
Contributions for capital asset acquisition	708,517	4,219,159
Annuity and life income	22,243,022	16,276,366
Contributions receivable	<u>3,583,267</u>	<u>3,739,899</u>
Total temporarily restricted net assets	<u>\$ 28,717,272</u>	<u>\$ 26,351,454</u>

Permanently restricted net assets consisted of the following at May 31, 2007 and 2006:

	<b>2007</b>	<b>2006</b>
Student loans	\$ 492,426	\$ 467,880
Endowment	69,269,774	62,785,902
Annuity and life income	398,059	729,393
Funds held in trust by others	10,468,200	9,081,822
Contributions receivable	<u>385,908</u>	<u>789,670</u>
Total permanently restricted net assets	<u>\$ 81,014,367</u>	<u>\$ 73,854,667</u>

## 8. RETIREMENT BENEFITS

The University is a participant in the Teachers Insurance and Annuity Association – College Retirement Equity Fund (“TIAA-CREF”), which is a defined contribution plan. TIAA-CREF does not segregate the assets, liabilities, or costs by participating employer, since the accounts are maintained on an employee-basis only. Total pension expense for the years ended May 31, 2007 and 2006, was approximately \$3,073,000 and \$2,600,000, respectively. Accrued pension costs are funded on a current basis.

In addition to providing pension benefits, the University provides certain health care insurance benefits for retired employees. Substantially all of the University’s employees who were hired prior to September 15, 1994, may become eligible for those benefits if they reach normal retirement age while working for the University or have elected to take early retirement under voluntary early retirement agreements. Employees hired after September 15, 1994 may elect to participate in the health care plans at their own cost. The plan is contributory, with retiree contributions adjusted annually, and contains other cost-sharing features, such as deductibles and coinsurance. The University’s policy is to fund the cost of medical benefits in amounts determined at the discretion of management.

During the year ended May 31, 2007, the University implemented the recognition provision of SFAS No. 158. As a result, the University recognized an unrealized actuarial loss of \$1,797,546. This item is included in the institutional support line of the consolidated statements of activities and changes in net assets.

The measurement date for the postretirement plan is March 1. The following tables set forth the plan’s benefit obligation, accrued liability, components of net periodic benefit costs, and weighted average actuarial assumptions as of May 31, 2007 and 2006:

	2007	2006
<b>Change in Benefit Obligation:</b>		
Benefit obligation at beginning of year	\$ 14,069,972	\$ 12,251,618
Service cost	193,216	291,884
Interest cost	854,602	675,389
Actuarial (gain) loss	(61,777)	1,511,010
Benefits paid	<u>(792,692)</u>	<u>(659,929)</u>
Benefit obligation at end of year	<u>\$ 14,263,321</u>	<u>\$ 14,069,972</u>
	<b>2007</b>	<b>2006</b>
<b>Change in Plan Assets:</b>		
Fair value of plan assets at beginning of year	\$ -	\$ -
Employer contributions	792,692	659,929
Benefits paid	<u>(792,692)</u>	<u>(659,929)</u>
Fair value of plan assets at end of year	<u>\$ -</u>	<u>\$ -</u>

	2007	2006
<b>Reconciliation of the Accrued Liability:</b>		
Funded status	\$ 14,263,321	\$ 14,069,972
Unrecognized accumulated net gain (loss)	(2,686,201)	(3,169,479)
Unrecognized translation obligation	(107,418)	(125,321)
Unrecognized prior service cost	<u>996,073</u>	<u>1,104,934</u>
Accrued postretirement benefit obligation before effect of SFAS 158	12,465,775	11,880,106
Effect of SFAS 158	<u>1,797,546</u>	<u>-</u>
Accrued balance sheet liability at end of year	<u>\$ 14,263,321</u>	<u>\$ 11,880,106</u>

	2007	2006
<b>Components of Net Periodic Benefit Cost:</b>		
Service cost	\$ 193,216	\$ 291,884
Interest cost	854,602	675,389
Amortization of loss	421,501	185,031
Amortization of prior service cost	(108,861)	(108,861)
Amortization of transition obligation	<u>17,903</u>	<u>17,903</u>
Net periodic benefit cost	<u>\$ 1,378,361</u>	<u>\$ 1,061,346</u>

**Actuarial Assumptions:**

Discount rate	6.00 %	6.25 %
Healthcare cost present trend rate	9.00 %	10.00 %
Healthcare cost ultimate trend rate (year of stabilization)	5.00% (2011)	5.00% (2011)

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

	Increase	Decrease
Effect on total of service and interest cost components	\$ 130,745	\$ (113,597)
Effect on post-retirement benefit obligations	1,568,264	(1,320,875)

***Cash Contributions and Benefit Payments***

The University's postretirement benefits are unfunded, therefore cash contributions for postretirement benefits are equal to the benefit payments.

The following table details the expected cash contributions and benefit payments for 2008 through 2017:

2008	\$ 791,621
2009	859,032
2010	903,725
2011	930,079
2012	957,795
Years 2013-2017	5,037,833

All benefit payments for other postretirement benefits are voluntary, as the postretirement plans are not funded, and are not subject to any minimum regulatory funding requirements. Benefit payments for each year represent claims paid for medical expenses, and the University anticipates the 2008 postretirement benefit payments will be made from cash generated from operations.

***Asset Allocation***

The University's postretirement plan is fully unfunded as of May 31, 2007.

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