BAYLOR UNIVERSITY 2002-2003 ANNUAL REPORT

BAYLOR
UNIVERSITY

IN 1995, BAYLOR'S SCULPTURE COMMITTEE
ENVISIONED A SCULPTURE THAT WOULD RESIDE IN FRONT OF
THE YET-TO-BE-BUILT MCLANE STUDENT LIFE CENTER

FROM THINKING TO FORWARD THINKING

Fiscal year 2002-2003 represented a transitional period for Baylor University. Across campus, progress toward fulfillment of Baylor 2012 — the University's Vision to move to the top tier among American institutions while reaffirming and deepening its distinctly Christian mission — became visible in big ways and small. Concurrently, the economy, financial markets, international political uncertainty and campus matters challenged the University in unprecedented ways.

The Vision framework enabled University leadership to address these challenges while significantly moving toward accomplishment of all that the Vision promises. The ability of the University to remain on course while overcoming adversity is a testament to its character as a community of faithful people. It also confirms that stakeholders across the University have embraced the Vision and made the move *beyond thinking to forward thinking* — a critical element of the success of Baylor 2012.

Fulfilling the Vision means creating excellence at all levels of the University and across its breadth. This is what fiscal year 2002-2003 was all about — looking to the future while embracing and building upon the University's finest traditions; extending excellence deeper into key areas; and ensuring alignment of these activities with Vision imperatives. The following sections highlight these activities.

NEARLY A DECADE IN THE MAKING, A BRONZE SCULPTURE OF THE BAYLOR BEAR IS NEARING COMPLETION. CREATED BY BAYLOR SCULPTOR-IN-RESIDENCE, PROFESSOR DOUGLAS CROW, THE NINE-FOOT WORK OF ART WILL BE UNVEILED IN FRONT OF THE McLANE STUDENT LIFE CENTER NEXT SPRING DURING DIADELOSO 2004. FROM THE INITIAL CONCEPT TO THE MANY CONTRIBUTIONS OF TIME, EFFORT AND FUNDS NECESSARY TO BRING THE SCULPTURE TO COMPLETION, THE PROJECT IS A STUDY IN FORWARD THINKING — LOOKING TO THE FUTURE WHILE EMBRACING AND BUILDING UPON THE PAST.

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ROBERT B. SLOAN JR.
PRESIDENT, BAYLOR UNIVERSITY

While the Annual Report reflects the activities of the University for the 2002-2003 academic and fiscal year, it also provides an opportunity for reflection and assessment related to our ten-year Vision, which we call Baylor 2012.

There is visible proof throughout the campus that the imperatives of 2012 are moving ahead with positive results. A drive down University Parks Drive is an exciting ride, especially for those who have not been on the campus on a regular basis. The new sights include:

- an architecturally pleasing office/parking facility, which houses the first Chili's Too on a college campus as well as a Starbucks coffee shop;
- the magnificent Harry and Anna Jeanes Discovery Center, the centerpiece of the Sue and Frank Mayborn Museum Complex, and home to our Department of Museum Studies;
- the 500,000-square-foot Baylor Sciences Building, which will dramatically improve our science classrooms and research possibilities;
- the North Village Residential Community, the first living space built on campus in almost 40 years and the location for the Engineering and Computer Science Living-Learning Center; and
- lighted intramural fields with restrooms and equipment storage.

On the other side of campus, the completed Stacy Riddle Forum, which houses nine large suites for our Panhellenic groups, can be viewed from the Eighth Street entrance of the campus. All of these buildings enhance our campus and provide significant academic and wellness opportunities for our students.

As you will see as you read this report, our ten-year Vision, Baylor 2012, takes us "beyond thinking to forward thinking." Our founders of nearly 160 years ago envisioned a university that would be "fully susceptible of enlargement and development to meet the needs of all ages to come." We, therefore, honor the legacy and heritage bestowed upon us by those who have gone before us, knowing that those who have laid Baylor's foundations would approve of our earnest and strategic efforts to meet the needs of our students in this century.

2002-2003 FISCAL YEAR HIGHLIGHTS

During fiscal year 2002-2003, Baylor University continued to move toward accomplishing the imperatives of Baylor 2012, our ten-year Vision. While dealing with the financial difficulties that are affecting all of higher education, the University's new financial model generated significant new revenues allowing progress on the student-centered Vision for the University. The year was marked by challenges in the world financial markets which constrain the growth of our endowment and gifts to the endowment. In the face of this, the University has been able to provide financial aid to our student body at unprecedented levels, attract and retain world-class faculty, and continue our comprehensive construction plan.

In fiscal year 2002-2003, the total assets of the University decreased slightly from $1.238 billion to $1.231 billion. Baylor's net assets decreased $48 million during fiscal year 2002-2003. Approximately $44 million of gifts and private grants and $9 million of realized gains on investments helped offset $82 million of unrealized losses, which were primarily attributable to the continued downturn in the equity markets. These financial market declines also resulted in a decrease in total endowment from $584 million at May 31, 2002, to $557 million at May 31, 2003.

Fiscal year 2002-2003 was the first year of transition to a flat-rate tuition plan that will fund elements of Baylor 2012 and align the institution's pricing system with its peer universities. The fall class of 2,620 freshmen and 437 transfers, participating in this new tuition structure, helped to generate total tuition and fees for the year of $205 million, an increase of $25 million over the prior year. Total revenues, net of scholarships, were $309 million for 2002-2003, up $30 million from $279 million in 2001-2002.

The University's balance sheet remained strong with total investments of $745 million at fiscal year end. Baylor's net investment in property, plant and equipment totaled $424 million at the end of the fiscal year as compared to $332 million as of May 31, 2002. At May 31, 2003, the University had $261 million of long-term debt and total liabilities of $380 million.

During 2002-2003, construction was completed on the $7 million Stacy Riddle Forum Panhellenic Building. As part of Baylor 2012, the University also continued construction on the $103 million Baylor Sciences Building, $23 million Harry and Anna Jeanes Discovery Center in the new Mayborn Museum Complex, $15 million Dutton Avenue Office and Parking Facility and began constructing the $33 million North Village residential complex. We anticipate completing each of these projects by summer 2004, making them available to our students for the fall semester of 2004.

As we progress toward making Baylor University stronger, we continue to take a proactive approach while maintaining conservative financial principles that will allow for the accomplishment of Baylor 2012 and prepare the University to accomplish the vision and dreams of those who come after us. It takes the contributions of our students, alumni, faculty, staff and donors to continue moving Baylor University forward. My deepest appreciation to all those who continue to do their part to make Baylor great.

DAVID R. BROOKS
VICE PRESIDENT FOR FINANCE AND ADMINISTRATION

FACULTY RECRUITMENT

During the fiscal year, the University continued to fulfill its intent to "develop a world-class faculty." Building upon the extraordinary recruiting successes of the 2001-2002 year, Baylor attracted approximately 50 new faculty members from around the world representing tremendous diversity in disciplines and experience. Approximately half of these individuals are Vision recruits — incremental additions to the faculty in areas targeted for development and growth as part of Baylor 2012. This brings to well over 150 the number of new faculty and staff members hired during the first two years of the Vision implementation.

In this recruitment process, the University has attracted incredible faculty. The roster of incoming Distinguished Professors is impressive in number and depth, including Earl Grinols, Distinguished Professor of Economics; Bennie Ward, Distinguished Professor of Physics and the new chair of the Department of Physics; Martin Medhurst, Distinguished Professor of Rhetoric and Communications; and Robert Marks, Distinguished Professor of Electrical Engineering.

WHAT MAKES AN ARTIST GREAT IS THE WAY IN WHICH HE USES COMMON TOOLS AND MATERIALS TO BRING HIS VISION TO LIFE AND TO GIVE IT A DISTINCTIVE PERSONA.

Prominent among the new faculty members, as well, are individuals who have been honored by other universities for their excellence in teaching, including:

JULIA DYSON, associate professor, Ph.D, Harvard University. Coming to Baylor from the University of Texas at Arlington, Dr. Dyson was the winner of Harvard University's Certificate of Distinction in Teaching from the Derek Bok Center.

CLARENCE DOUGLAS WEAVER, assistant professor, Ph.D, Southern Baptist Theological Seminary. Coming to Baylor from Brewton–Parker College in Mt. Vernon, Ga., Dr. Weaver was the chair of the Division of Religion and Philosophy and the Barney Averitt Professor of Christianity, as well as winner of two teaching awards — the Jordan Teacher Excellence Award and the Brewton-Parker Teacher of the Year Award.

DENNIS JOHNSTON, professor, Ph.D, Texas Tech University. Coming to Baylor from the Department of Biomathematics at the University of Texas M.D. Anderson Cancer Center, Dr. Johnston was a winner of the Dean's Teaching Excellence Award from the University of Texas Health Science Center at Houston.

ROBIN WALLACE, associate professor, Ph.D., Yale University. Coming to Baylor from Converse College, he was the winner of Yale University's Prize Teaching Fellowship, awarded in recognition of his potential to teach undergraduates — the first person in the history of Yale's music department to win this award.

SARAH-JANE MURRAY, assistant professor, Ph.D, Princeton University. She was the 2002-2003 winner of Princeton University's Porter Ogden Jacobus Honorific Fellowship, a university-wide honor awarded to the doctoral student at Princeton who, in the judgment of the faculty, demonstrates the highest level of academic achievement and promise.

These outstanding teachers represent the future generation of Baylor educators, reaffirming the University's teaching mission and building upon its strong tradition of scholarly excellence, both in research and teaching.

FACILITIES

Among the most visible signs of progress toward fulfillment of Baylor 2012 are the structures reshaping the campus skyline. Reflecting the influence of the Vision imperatives, these structures are consistent in design with the University's existing buildings and deliberately located to facilitate interaction between — and to develop a stronger sense of community among — students and faculty. Notable among these new structures are the following:

THE WORLD-CLASS BAYLOR SCIENCES BUILDING An imposing presence, the largest and most ambitious construction project in the University's history is shifting the epicenter of campus. The 500,000-square-foot facility, which will be the educational centerpiece for so many students following its opening in fall 2004 — not just science majors, but all Baylor students — almost adjoins the McLane Student Life Center. It is a vivid symbol of excellence to come as a result of forward thinking.

THE NORTH VILLAGE Groundbreaking took place on May 16, 2003, for the University's first new residential project in nearly 40 years. Initiating the construction phase for the imperative of "creating a truly residential campus," this complex will be both functionally and aesthetically pleasing. It has been designed with purpose, incorporating "community" into the physical structure. When completed, it will help Baylor recapture an aspect of greatness that characterized the University in past generations.

THE DUTTON OFFICE AND PARKING FACILITY This new campus landmark easily could be mistaken for an academic building. Instead, this new facility at the corner of Dutton Avenue and University Parks Drive plays an important role in bringing to reality the imperatives of "creating a truly residential campus" and "enhancing involvement of the entire Baylor family." In addition to office space for several academic, administrative and support departments, there also is a Chili's Too @ BU and a Starbucks coffee shop. Furthermore, the building's 1,200 parking spaces will significantly expand the University's parking capacity and improve access to the North Village and other facilities on the north end of campus.

STACY RIDDLE FORUM The new $7 million Panhellenic building opened in January 2003, becoming home to nine sororities, providing additional common areas for the student body, and freeing vital space across campus for other activities.

MORRISON CONSTITUTION HALL Faculty move-in began in fall 2002 at this former home of the Baylor Law School. It now contains offices and classrooms for the philosophy, classics and modern languages departments; several areas of the Baylor Success Center; the Center for Christian Ethics; the Institute for Faith and Learning; the Graduate School; and the Honors College.

TANGIBLE SIGNS OF PROGRESS ARE INTERIM REWARDS IN THE PAINSTAKING PROCESS OF SCULPTING.

ACADEMICS AND STUDENT LIFE

Baylor's Honors College was created by the Board of Regents in summer 2002 and Thomas Hibbs was named both dean and Distinguished Professor in spring 2003. The Honors College joins under one roof the University's existing Honors, University Scholars, and Baylor Interdisciplinary Core (BIC) programs, along with the proposed Great Texts program.

Pursuant to the Vision, Great Texts will become a part of every Baylor undergraduate's experience by 2012, when all Baylor students will be required to take two Great Texts courses. A Great Texts major is under development, as well, with additional courses and instructors being added during the fiscal year.

The improvement of student life and expansion of students' world view are other important precepts of the University and, consequently, of Baylor 2012. Baylor's University Ministries office made great strides in this direction during the fiscal year, including establishing the Department for Student Missions with Steve Graves as the new director of student missions.

Under Graves' leadership, Student Missions launched a concept called vocation-specific missions, which bonds students' academic, professional and spiritual development. For example, in summer 2002, the University conducted a mission to Honduras involving students from the Department of Communication Sciences and Disorders. For a country that has no education for the deaf, this team created a computer-based sign language learning program, took along several computers for the missionary, and introduced sign language in the Honduran language to groups of targeted Honduran children and their families. They filmed the process to create a documentary that is being used to garner support for the mission both in Honduras and the United States.

This work expands upon the rich tradition of missionary work by the Baptist Student Ministry and other University mission organizations, which have carried out medical and social work missions to countries around the world. As a pioneering effort, the *vocation-specific* mission program directly supports the Vision imperative to "guide all Baylor students, through academic and student life programming, to understand life as a stewardship and work as a vocation."

University Ministries, under the direction of Dr. Todd Lake, also expanded its resident chaplain program during the fiscal year. Funded by the University and built upon the success of the program's five existing grant-funded positions, the office added four additional chaplains.

Resident chaplains are George W. Truett Theological Seminary students who are provided with living quarters in nine of the University's 10 residence halls. They extend pastoral care and counseling for students there, help students locate congregations of their chosen denomination within the Waco community and lead mission trips. This program contributes to the fulfillment of the Vision imperative relating to stewardship and helps the University attract and support a top-tier student body by promoting an environment in which learning can flourish.

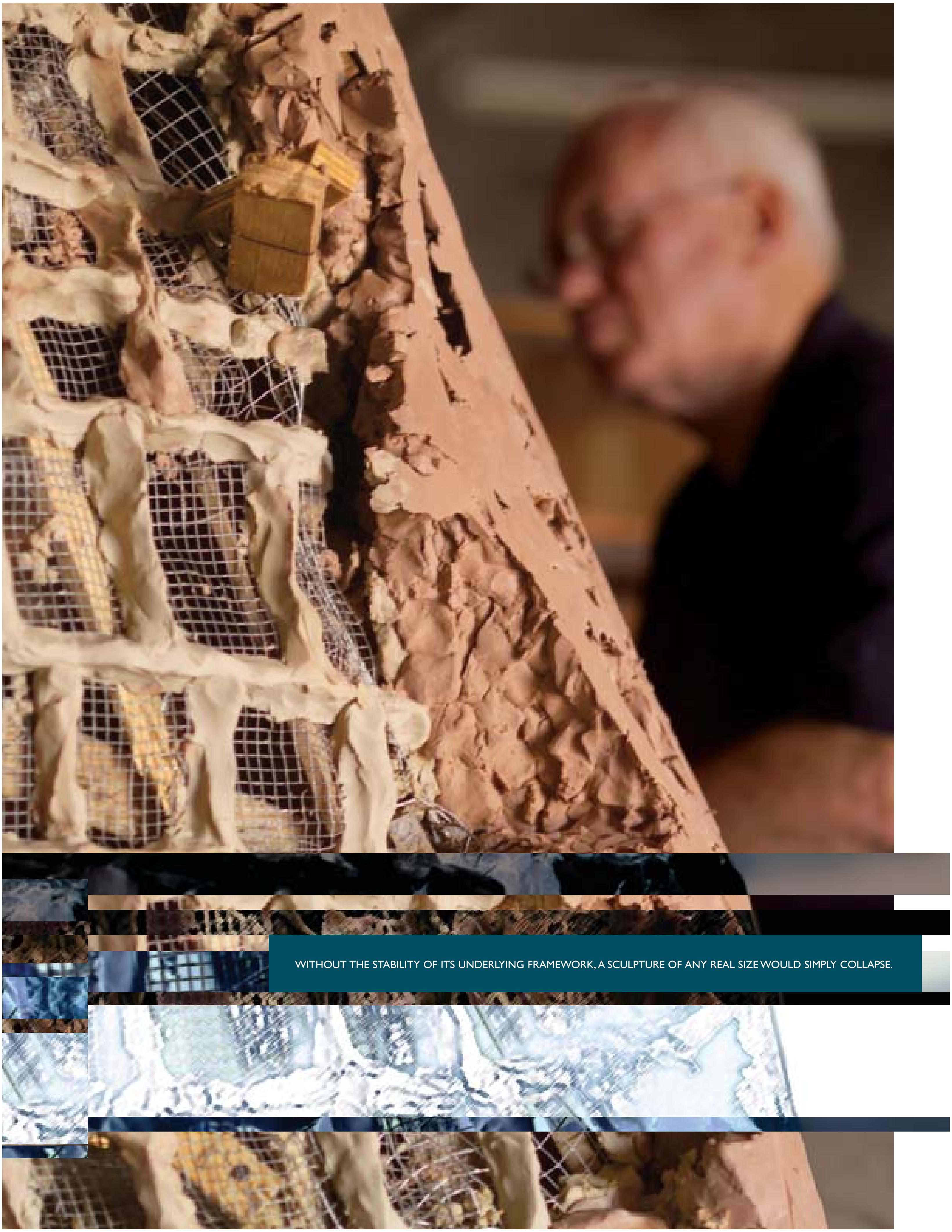
Spiritual development and support are not limited to the student population. During the fiscal year, the University Ministries established two venues for faculty and staff worship. First is a five-day, four-night retreat at Laity Lodge in the Texas Hill Country featuring daily sessions for discussion about vocation and calling as it relates to participants' fields, framed by morning and evening worship gatherings. Also, by popular demand a 30-minute, Thursday-afternoon "Evensong" program was established in January 2003 in conjunction with the School of Music under the guidance of professor of church music Randall Bradley.

Additionally, final groundwork was prepared for a Sports Chaplain Program, officially launched after the end of the fiscal year in July 2003. This program — the planning for which had been in the works for three years — is recruiting chaplains from the Waco area to work on a volunteer basis with the University's sports teams on campus.

Each of the new programs strengthen and connect with well-established programs to play important roles in forming the fabric of life at Baylor and in meeting the Vision imperatives. For students, faculty and staff alike, participation in these activities helps define "the Baylor experience" and encourages them in a forward-thinking manner to excel in all areas of their lives.

TEXTURE AND DETAIL ARE TWO DEFINING QUALITIES OF ANY SCULPTURE,

REVEALING
THE
DEPTH
AND
CHARACTER
OF
THE
ARTIST.


WITHOUT THE STABILITY OF ITS UNDERLYING FRAMEWORK, A SCULPTURE OF ANY REAL SIZE WOULD SIMPLY COLLAPSE.

Affected for most of the fiscal year by the continued sluggish economy, the University weathered the storm by aggressively exercising the forward-thinking flexibility that is built into the Vision framework and by taking extraordinary measures to live within its means.

BOND DEBT

In the year since the Board of Regents approved more than $200 million in bonds to fund strategic building projects, the decision has proven to be a prudent move for the University. Representing insightful stewardship for the University to proceed with building these facilities, the decision to tap the debt market is sound from two perspectives in light of the current economic environment:

- With equity markets still being depressed for most of the fiscal year, University investments continued to languish. At the same time, the current fundraising environment for major building projects was at arguably an all-time low.
- Offsetting the challenges presented by this environment were 50-year-low interest rates. Consequently, the University was able to take full advantage of the current weighted average interest rates on its bonds of 3.8 percent.

By pressing forward with these construction projects while these two factors are in confluence, rather than spending the next five to seven years raising the money, Baylor will have the state-of-the-art facilities necessary to be more competitive in coming years in terms of attracting top faculty and students. Moreover, this bonded indebtedness is within the parameters of other universities of Baylor's type nationally, and the University is mitigating risks by employing the most respected investment-banking firm for higher education to guide the initiative.

NEW TUITION STRUCTURE

Fiscal year 2002-2003 was the first year of transition to a flat-rate tuition plan that will fund elements of the Vision. As the year unfolded, the median family incomes for incoming freshmen fell and the number of incoming minority students increased.

This trend demonstrates that Baylor is accessible to students of varied socio-economic backgrounds, largely due to allocating approximately one-third of the additional revenue generated by the tuition increase into scholarships. In fact, 82 percent of incoming freshman received some form of financial assistance.

Further supporting the supposition, higher education industry surveys indicate that the University remains a strong value relative to its competitive peers. Baylor's tuition rate is only at 82 percent of most private Tier 2 institutions and 65 percent of most private Tier 1 institutions.

As a result of these factors, Baylor continued to see its revenue increase during a year in which many other universities across the country — particularly public institutions — faced layoffs, budget shortfalls and cutbacks. The tuition increase, consequently, is timely and forward thinking because it virtually guarantees that for four years Baylor will enjoy a positive increase in revenue due to the manner in which the program is being grandfathered. At the same time, value is being increased in terms of new faculty, facilities, academic programs and student life programs.

FRESHMAN ENROLLMENT

The fall 2002 semester saw Baylor fall short of its freshman enrollment projections. This was attributable to many factors, including the economy, the national and state unemployment rates, and international political uncertainty. Although the University's revenue actually increased for the year, it still did not meet expectations. As a result, University leadership enacted cost reduction measures that helped Baylor remain within budget.

FUNDRAISING AND THE ENDOWMENT

The Campaign for Greatness — Baylor's current major fundraising initiative — flourished in spite of the economy and a fundraising environment that could only be characterized as challenging. By the end of the May 31, 2003 fiscal year, total pledges and gifts generated by the campaign since its inception in January 1999 stood at $453 million, nearly $51 million of which was raised during the fiscal year. These figures indicate that the program is on schedule to surpass its target of $500 million at the end of December 2005.

Weak equity market performance for most of the fiscal year resulted in a decline in market value of Baylor's total endowment, from $584 million to $557 million, during the fiscal year. However, market indicators were improving rapidly with the onset of summer, and this negative trend showed strong signs of reversal as the fiscal year concluded.

STRATEGIC PLANNING — AT THE HEART OF FORWARD THINKING

With the appointment of a new strategic planning director at the end of fiscal year 2001-2002, the University began creating a new strategic planning framework. This new framework, crafted by Van Gray, will help University leadership implement Baylor 2012 in terms of approving strategic initiatives and integrating them with the University's budget process.

Achieving the Vision requires that the University meet internal and external metrics. Internal metrics are embodied within the 12 Vision imperatives. Primary external metrics are the 16 variables measured by *U.S. News & World Report*.

No single initiative can address all of these metrics. So during the 2002-2003 fiscal year, the University's Strategic Planning Office, under Dr. Gray's direction, designed, created and began implementing a database portfolio management approach to managing the Vision. This approach enables the University to develop a portfolio of funded projects that will specifically address all of the internal and external imperatives.

In its first year utilizing this approach, the Strategic Planning Office received 107 strategic planning initiative proposals from the University's Executive Council and the departments that report to council members. Each proposal is required to provide visibility into the proposal's effects on the Vision imperatives. Faculty hiring decisions, for example, are now predicated on factors such as personnel costs — for the current year and each subsequent year for 10 years — as well as the availability of funds, physical space, support personnel and resources, and library and technology resources, among many other variables.

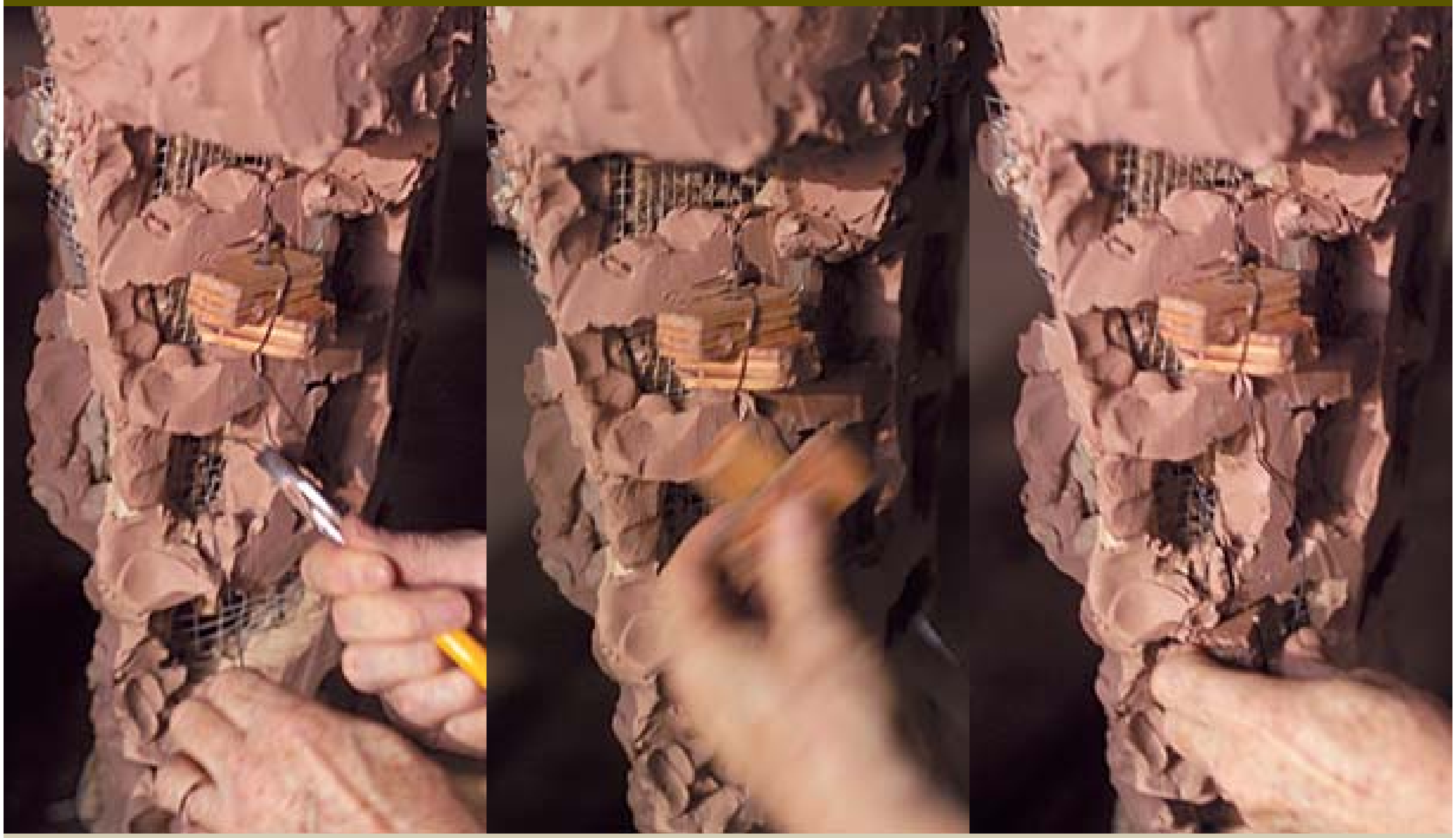
The approach, supported by commercially available portfolio database software, allows the planning team to route the proposal electronically through an appropriate set of University service providers who review it and help the proposal's owner to answer those detailed questions. The effect of this is to substantially elevate the University's strategic decision-making capabilities.

Of the 107 proposals submitted during the fiscal year, nearly half had been reviewed and prioritized by University leadership by May 31, representing more than $30 million in projected investments. First-year expenditures for these initiatives, if approved, represent slightly less than $5 million, or nearly 1.5 percent of the University's annual operating budget. This figure is anticipated to grow to nearly 10 percent annually by the end of the 10-year Vision period.

During the fiscal year, the foundation was laid so that as future decisions are made regarding these proposals and action plans for the initiatives are developed, the planning team will be able to track and monitor those plans over time and begin to improve visibility into their return on the University's investment. As such, the new processes represent a scorecard approach to strategic planning and decision making. These hold significant promise in terms of aligning the University's current and future initiatives with the imperatives of the Vision and ensuring that the Vision is achieved in the most forward-thinking manner possible.

FROM CONCEPT TO COMPLETION,
THE SCULPTURE IS A LABOR OF LOVE THAT REQUIRES IN EQUAL PARTS:
FORESIGHT, ENTHUSIASM, ENERGY, PATIENCE AND FAITH.


t Life Center



FINANCIAL STATEMENTS

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INDEPENDENT AUDITORS' REPORT

BOARD OF REGENTS
BAYLOR UNIVERSITY

We have audited the accompanying balance sheet of Baylor University (the "University") as of May 31, 2003 and the related statements of activities and cash flows for the year then ended. 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 audit. The financial statements of the University for the year ended May 31, 2002 were audited by other auditors whose report, dated July 26, 2002, expressed an unqualified opinion on those statements.

We conducted our audit 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. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2003 financial statements present fairly, in all material respects, the financial position of the University as of May 31, 2003 and the changes in net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

JULY 25, 2003

MAY 31, 2003 AND 2002
(in thousands of dollars)

	MAY 31, 2003			
	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
ASSETS				
Cash & cash equivalents	$ 7,057	$ 3	$ —	**$ 7,060**
Student accounts receivable, net	4,200	—	—	**4,200**
Contributions, grants & other receivables	17,338	7,556	5,960	**30,854**
Prepaid expenses & other	7,734	7	4	**7,745**
Student loans receivables, net	9,952	—	1,641	**11,593**
Investments, at fair value	282,118	43,514	419,404	**745,036**
Property, plant & equipment, net of accumulated depreciation of $214,851 and $212,772	424,063	—	—	**424,063**
TOTAL ASSETS	**$ 752,462**	**$ 51,080**	**$ 427,009**	**$ 1,230,551**
LIABILITIES & NET ASSETS				
LIABILITIES				
Accounts payable	$ 21,404	$ 667	$ 99	**$ 22,170**
Salaries & payroll taxes payable	19,582	—	—	**19,582**
Deposits & deferred income	20,586	121	—	**20,707**
Annuities payable	—	1,686	5,561	**7,247**
Notes & bonds payable	261,209	—	—	**261,209**
Liability for interest rate swap	41,711	—	—	**41,711**
Federal student loan funds refundable	7,190	—	—	**7,190**
TOTAL LIABILITIES	371,682	2,474	5,660	**379,816**
NET ASSETS				
Unrestricted	2,608	—	—	**2,608**
Designated for operations	15,632	—	—	**15,632**
Restricted	—	8,043	5,643	**13,686**
Annuity & living trusts	—	7,228	16,428	**23,656**
Endowment	46,078	19,833	399,278	**465,189**
Board designated endowment	87,694	4,459	—	**92,153**
Net invested in plant	228,768	9,043	—	**237,811**
TOTAL NET ASSETS	380,780	48,606	421,349	**850,735**
TOTAL LIABILITIES & NET ASSETS	**$ 752,462**	**$ 51,080**	**$ 427,009**	**$ 1,230,551**

See accompanying notes to financial statements.

MAY 31, 2002			
UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
$ 12,881	$ —	$ —	**$ 12,881**
1,510	—	—	**1,510**
11,984	10,556	5,547	**28,087**
8,313	128	4	**8,445**
9,856	—	1,277	**11,133**
398,631	53,872	392,071	**844,574**
331,769	—	—	**331,769**
$ 774,944	**$ 64,556**	**$ 398,899**	**$1,238,399**
$ 9,549	$ 711	$ 98	**$ 10,358**
16,320	—	—	**16,320**
19,910	9	—	**19,919**
—	2,120	3,000	**5,120**
264,979	—	—	**264,979**
15,420	—	—	**15,420**
7,098	—	—	**7,098**
333,276	2,840	3,098	**339,214**
1,141	—	—	**1,141**
16,526	—	—	**16,526**
—	9,070	5,568	**14,638**
—	7,594	15,579	**23,173**
77,675	27,399	374,654	**479,728**
100,185	4,420	—	**104,605**
246,141	13,233	—	**259,374**
441,668	61,716	395,801	**899,185**
$ 774,944	**$ 64,556**	**$ 398,899**	**$1,238,399**

FOR THE YEARS ENDED MAY 31, 2003 AND 2002
(in thousands of dollars)

	MAY 31, 2003			
	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
REVENUES				
Tuition & fees	$ 205,258	$ —	$ —	**$ 205,258**
Less scholarships	(50,208)	—	—	**(50,208)**
Net tuition & fees	155,050	—	—	**155,050**
Gifts, private grants & Baptist General Convention of Texas appropriation	14,699	8,150	20,999	**43,848**
Endowment & investment income	30,079	4,326	192	**34,597**
Realized gains (losses) on investments	127	366	8,967	**9,460**
Other sources	17,991	8,119	—	**26,110**
Auxiliary enterprises	39,554	—	—	**39,554**
TOTAL REVENUES	257,500	20,961	30,158	**308,619**
Net assets released from temporary restrictions	24,317	(25,602)	1,285	—
TOTAL NET REVENUES	281,817	(4,641)	31,443	**308,619**
EXPENSES				
Program expenses				
Instruction	124,092			**124,092**
Academic support, research & public service	36,720			**36,720**
Student services	19,831			**19,831**
Auxiliary enterprises	50,877			**50,877**
Support expenses				
Institutional support	42,004			**42,004**
TOTAL EXPENSES	273,524			**273,524**
INCREASE (DECREASE) IN NET ASSETS BEFORE OTHER CHANGES	8,293	(4,641)	31,443	**35,095**
OTHER CHANGES				
Unrealized losses on investments	(42,386)	(8,229)	(4,983)	**(55,598)**
Unrealized loss on interest rate swap	(26,291)	—	—	**(26,291)**
Loss on debt prepayment & disposal of fixed assets	(504)	—	—	**(504)**
Change in value of split interest agreements:				
Present value adjustments	—	(240)	(912)	**(1,152)**
Terminated annuities	—	—	—	—
TOTAL OTHER CHANGES	(69,181)	(8,469)	(5,895)	**(83,545)**
INCREASE (DECREASE) IN NET ASSETS	(60,888)	(13,110)	25,548	**(48,450)**
NET ASSETS AT BEGINNING OF YEAR	441,668	61,716	395,801	**899,185**
NET ASSETS AT END OF YEAR	$ 380,780	$ 48,606	$ 421,349	**$ 850,735**

See accompanying notes to financial statements.

MAY 31, 2002

UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
$ 180,558	$ —	$ —	**$ 180,558**
(37,947)	—	—	**(37,947)**
142,611	—	—	**142,611**
13,363	15,159	10,871	**39,393**
23,986	4,655	375	**29,016**
1,197	(18)	2,300	**3,479**
18,493	6,262	—	**24,755**
40,012	—	—	**40,012**
239,662	26,058	13,546	**279,266**
44,260	(50,963)	6,703	**—**
283,922	(24,905)	20,249	**279,266**
109,845			**109,845**
33,873			**33,873**
16,190			**16,190**
49,277			**49,277**
36,661			**36,661**
245,846			**245,846**
38,076	(24,905)	20,249	**33,420**
(47,405)	(8,446)	(6,822)	**(62,673)**
(15,420)	—	—	**(15,420)**
(2,169)	—	—	**(2,169)**
—	(489)	1,026	**537**
1,154	(33)	(1,121)	**—**
(63,840)	(8,968)	(6,917)	**(79,725)**
(25,764)	(33,873)	13,332	**(46,305)**
467,432	95,589	382,469	**945,490**
$ **441,668**	$ **61,716**	$ **395,801**	$ **899,185**

FOR THE YEARS ENDED MAY 31, 2003 AND 2002
(in thousands of dollars)

	YEAR ENDED MAY 31, 2003	YEAR ENDED MAY 31, 2002
CASH FLOWS FROM OPERATING ACTIVITIES		
DECREASE IN NET ASSETS	$ (48,450)	$ (46,305)
Adjustments to reconcile decrease in net assets to net cash provided by operating activities:		
Depreciation	23,669	21,245
Fixed assets gifts-in-kind	(44)	(52)
Net realized & unrealized losses on investments	46,138	59,194
Contributions restricted for permanent investments	(20,999)	(10,871)
Unrealized loss on interest swap	26,291	15,420
Decrease (increase) in:		
Student accounts receivable	(2,690)	1,690
Contributions, grants & other receivables	(2,767)	3,469
Prepaid expenses & other	700	(5,059)
Increase (decrease) in:		
Accounts payable	11,812	(2,016)
Salary & payroll taxes payable	3,262	1,606
Deposits & deferred income	788	(709)
Annuities payable	2,127	(1,981)
Net cash provided by operating activities	**39,837**	**35,631**
CASH FLOWS FROM INVESTING ACTIVITIES		
Loans to students, net change	(460)	(751)
Proceeds from sales of investments	472,929	280,154
Purchases of investments	(419,529)	(472,777)
Purchases of property, plant & equipment	(115,919)	(64,288)
NET CASH USED IN INVESTING ACTIVITIES	**(62,979)**	**(257,662)**
CASH FLOWS FROM FINANCING ACTIVITIES		
Contributions restricted for permanent investments:		
Endowment	18,537	9,804
Annuity & living trust	2,462	1,067
Proceeds from long-term debt	542	263,263
Repayment of long-term debt	(4,312)	(47,343)
Increase in federal student loan funds refundable	92	90
NET CASH PROVIDED BY FINANCING ACTIVITIES	**17,321**	**226,881**
NET INCREASE (DECREASE) IN CASH & CASH EQUIVALENTS	**(5,821)**	**4,850**
CASH & CASH EQUIVALENTS AT BEGINNING OF YEAR	**12,881**	**8,031**
CASH & CASH EQUIVALENTS AT END OF YEAR	**$ 7,060**	**$ 12,881**

See accompanying notes to financial statements.

MAY 31, 2003 AND 2002

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF ACCOUNTING & REPORTING

The financial statements of Baylor University (the "University") include the accounts of the University and Brazos Valley Public Broadcasting Foundation (KWBU), a legally separate entity, the board of directors of which is chosen by the University's Board of Regents. The University's financial statements do not include the accounts of the Baylor Foundation, Baylor Stadium Corporation, Baylor Bear Foundation, Baylor-Waco Foundation or Baylor Alumni Association. These entities are excluded due to the nature of their relationship to the University or due to the fact that their aggregate assets, revenues, expenses, and net assets are not significant in relation to the University.

The financial statements of the University are prepared on the accrual basis. The University's net assets and revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified as follows:

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

Temporarily restricted — net assets subject to donor-imposed or legal 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 the assets be maintained permanently. Generally, the donors of these assets permit the University to use all or part of the income earned on the 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 are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions on net assets are reported as net assets released from temporary restrictions among applicable net asset classes.

Income and realized net gains and losses on investments are reported as follows:

- As changes in permanently restricted net assets if so restricted by the donor;
- As changes in temporarily restricted net assets if the terms of the gift impose restrictions on the use of the income or gains and losses;
- As changes in unrestricted net assets in all other cases.

FUND ACCOUNTING

To ensure observance of limitations and restrictions placed on the use of resources available to the University, the internal accounts are maintained in accordance with the principles of fund accounting. This is the procedure by which resources for various purposes are classified into funds that are in accordance with specified activities or objectives. These financial statements, however, are prepared to focus on the entity as a whole and to present transactions according to the existence or absence of donor-imposed restrictions.

FUNCTIONAL ALLOCATION OF EXPENSES

The expenses of providing various programs and support services have been categorized on a functional basis in the statements of activities. Accordingly, expenses such as depreciation and operation and maintenance of plant have been allocated directly or based on square footage among the functional categories.

Fundraising expenses of approximately $6,559,000 and $6,159,000 incurred by the University in 2003 and 2002, respectively, are included in the institutional support category in the statements of activities.

CONTRIBUTIONS

Contributions received with donor-imposed restrictions that are met in the same year as received are reported as revenues of the unrestricted net asset class.

Donor contributions to fund construction projects are classified as temporarily restricted net assets until the facility is placed in service. At that time, the temporarily restricted net assets are released from restriction and replenish unrestricted net asset balances designated for plant projects. The University follows the policy of recording contributions of long-lived assets directly as invested in plant assets instead of recognizing the gift over the useful life of the asset.

CASH EQUIVALENTS

Cash on deposit for operations and all highly liquid financial instruments with maturities of 90 days or less are classified as cash equivalents, except those amounts assigned to investment managers, which are classified as investments. The fair value of cash equivalents is estimated to be the same as book value due to the short maturity of these instruments.

ENDOWMENT

Endowment net assets classified as unrestricted include realized gains and losses and net unrealized appreciation (depreciation) on endowment assets the earnings of which are unrestricted by the donor. Endowment net assets classified as temporarily restricted include realized gains and losses and net unrealized appreciation (depreciation) on endowment assets that are restricted by the donor for a specific purpose. Permanently restricted endowment net assets are those assets that must be invested in perpetuity to provide a permanent source of income.

Board designated endowment net assets include gifts and funds that have been designated by the Board of Regents (the "Board") to function as endowment. These funds may be expended at the discretion of the Board. Also included are certain temporarily restricted net assets that have not been expended for their restricted purpose but are being invested and the earnings expended for the restricted purpose.

The Baylor University Fund (BUF) is a unitized fund consisting of equities, fixed income and alternative assets and serves as the primary investment vehicle for the University's endowment and other long-term investments. The University has adopted a spending policy for the BUF whereby the Board authorizes a dividend be paid for endowments participating in the BUF for the purposes intended by the donors. This dividend was based on 5 percent and 5.25 percent of the previous 48 months average market value per unit of the BUF for the years ended May 31, 2003 and 2002, respectively. If the current income of the BUF is not sufficient to cover the dividend amount, the amount needed is taken from the accumulated capital gains within the BUF.

SPLIT INTEREST AGREEMENTS

Split interest agreements consist primarily of gift annuities, charitable remainder unitrusts and annuity trusts, life income funds and perpetual trusts. Assets held under these agreements are included in investments (see Note 2), except for agreements administered by the Baptist Foundation of Texas (BFT) and others as temporary trustees. The net present values of these agreements administered by the BFT and others as temporary trustees are reflected as unconditional promises to give (see Note 10). Annuities payable are recorded at the present value of future payments discounted at 3.80 percent and 6.0 percent for the years ended May 31, 2003 and 2002, respectively.

STUDENT LOANS

The assets and liabilities of student loans financed primarily by the federal government and administered by the University, primarily the Federal Perkins Loan Program, are included with those of the University. The total of the federal government portion of these net assets is shown as Federal student loan funds refundable in the accompanying balance sheets.

PROPERTY, PLANT & EQUIPMENT

Property, plant and equipment valued at $2,000 or more are recorded at cost at date of acquisition or, if acquired by gift, at estimated fair value at date of gift. Additions to plant assets are capitalized while maintenance and minor renovations are charged to operations. Plant assets are reflected net of accumulated depreciation calculated on a straight-line basis over the estimated useful lives ranging from three to fifty years.

DEPOSITS AND DEFERRED INCOME

Deposits and deferred income consists of amounts billed or received for educational, research and auxiliary goods and services that have not yet been earned.

USE OF ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the statements and accompanying notes. Actual results could differ from those estimates.

2. CASH & CASH EQUIVALENTS AND INVESTMENTS

The University's investments are recorded at fair value. Cost and estimated fair value of financial instruments as of May 31, 2003 and 2002, respectively, are as follows:

(in thousands of dollars)

	2003		2002	
	Cost	Estimated Fair Value	Cost	Estimated Fair Value
CASH & CASH EQUIVALENTS	$ 7,060	$ 7,060	$ 12,881	$ 12,881
Investments:				
Short-term	$ 27,173	$ 29,185	$ 51,470	$ 51,470
Collateralized investment contract	133,777	133,777	181,285	181,285
Debt securities	75,936	84,866	83,182	102,701
Equity securities	373,859	408,511	358,021	446,006
Alternative assets	50,641	54,982	37,969	38,112
Real estate	14,234	18,300	17,020	16,934
Mineral rights	11,901	15,145	1,986	7,859
Other	270	270	207	207
TOTAL INVESTMENTS	$ 687,791	$ 745,036	$ 731,140	$ 844,574
NOTES & BONDS PAYABLE	$ 261,209	$ 261,209	$ 264,979	$ 264,979

Net appreciation (depreciation) in the fair value of investments, which consists of the realized gains and losses and the unrealized appreciation (depreciation) on those investments, is shown in the statements of activities.

Short-term investments consist primarily of short-term U.S. Government securities and money market funds and are not subject to significant market or credit risks. The collateralized investment contract is with Trinity Plus Funding Company, LLC and pays interest at a rate tied to the Bond Market Association Municipal Swap Index. Alternative assets consist of distressed securities, venture capital, hedge funds and private equities.

The fair value of real estate is determined from the most recent information available to the University, i.e. appraisals and/or property tax statements. The fair value of mineral rights is estimated based on the income stream those assets generate.

Investments, at fair value, are managed by the following:

(in thousands of dollars)

	2003	2002
Baylor	$ 602,029	$ 676,951
Baptist Foundation of Texas (BFT)	111,155	126,998
Others	31,852	40,625
TOTAL	$ 745,036	$ 844,574

The BFT is an agency of the Baptist General Convention of Texas created to manage investment funds for Texas Baptist institutions. The investments managed by the BFT for the University represent approximately 9 percent and 10 percent of BFT's total assets as of May 31, 2003 and 2002, respectively.

Investments include interests in split interest agreements. The fair values representing interests in split interest agreements are $117,866,000 and $113,306,000 as of May 31, 2003 and 2002, respectively.

Investment return for the years ended May 31, 2003 and 2002 is comprised of the following:

(in thousands of dollars)

	2003	2002
Endowment/investment income	$ 34,597	$ 29,016
Realized gains	9,460	3,479
Unrealized losses	(55,598)	(62,673)
TOTAL INVESTMENT RETURN	$ (11,541)	$ (30,178)

The endowment/investment income reflected is net of investment expenses of $3,771,000 and $3,761,000 for the years ended May 31, 2003 and 2002, respectively.

3. PROPERTY, PLANT & EQUIPMENT

At May 31, 2003 and 2002, plant assets consist of:

(in thousands of dollars)

	2003	2002
Land	$ 27,913	$ 25,443
Buildings	347,196	325,883
Equipment	107,612	119,024
Other improvements	65,247	56,863
	547,968	527,213
Less accumulated depreciation	(214,851)	(212,772)
	333,117	314,441
Construction-in-progress	90,946	17,328
PROPERTY, PLANT & EQUIPMENT, NET	$ 424,063	$ 331,769

Real and personal property are insured at $600,000,000 at both May 31, 2003 and 2002.

4. NOTES & BONDS PAYABLE

Notes and bonds payable consisting of both non-interest bearing unsecured notes and interest bearing unsecured and secured notes and bonds with varying terms and maturity dates to February 1, 2032, were $261,209,000 and $264,979,000 at May 31, 2003 and 2002, respectively. Interest payments on a cash basis totaled $7,467,000 and $3,011,000 and interest expense was $10,133,000 and $2,368,000 for the years ended May 31, 2003 and 2002, respectively. Interest expense totaling $6,503,000 and $0 was capitalized to projects for the years ended May 31, 2003 and 2002, respectively. Earnings on bond proceeds, which offset interest capitalized, were $2,092,000 and $0 for the years ended May 31, 2003 and 2002, respectively.

The University issued $247,500,000 in tax exempt and taxable revenue bonds through the Waco Education Finance Corporation during the fiscal year ended May 31, 2002, of which $47,059,000 was used to refinance Series 1997, 1998, 1999, 2000 and 2002 bonds. As a result of refinancing these bonds, a prepayment penalty of $1,455,000 was paid and is included as a loss on debt prepayment in the University's May 31, 2002, statement of activities. The University capitalized and is amortizing on a straight-line basis bond issue costs related to the Series 2002A, 2002B and 2002C issues over the life of the bonds. As of May 31, 2003 and 2002, unamortized bond issue costs of $3,938,000 and $3,519,000, respectively, are included in prepaid expenses and other in the University's balance sheets. Amortization expense for issue costs was $151,000 and $0 for the years ended May 31, 2003 and 2002, respectively.

Notes and bonds payable at May 31, 2003 and 2002 consist of the following:

(in thousands of dollars)

	2003	2002
Non-interest bearing unsecured note payable to a foundation, due in annual installments beginning 6/30/2004	$ 4,958	$ 4,417
Non-interest bearing unsecured note payable to a foundation, due in quarterly installments as repayments from loans to students are received	2,650	2,650
Unsecured note payable to a foundation, bearing interest at 5 percent, due in annual installments to 5/15/2006, interest only 5/15/2003	3,000	3,000
Non-interest bearing unsecured notes payable to a corporation, due in monthly installments through 9/1/2008	1,334	1,583
Secured note payable to a private entity (secured by land), bearing interest at 7.5 percent, due in annual installments of $747,314 to 1/1/2012	4,767	5,130
Series 2002A Waco Education Finance Corporation Tax-exempt Variable Rate Demand Bonds (VRDB) swapped to fixed rate of 4.91 percent (see Note 5), interest payable semi-annually, principal payable annually to 2/1/2032	174,075	174,800
Series 2002B Waco Education Finance Corporation Tax-exempt Select Auction Variable Rate Securities (SAVRS) bearing interest at SAVRS rate for each 35-day auction rate period. The interest rate as of 5/31/2003 was 1.13 percent, principal payable annually to 2/1/2032	58,900	61,000
Series 2002C Waco Education Finance Corporation Taxable Select Auction Variable Rate Securities (SAVRS) bearing interest at SAVRS rate for each 35-day auction rate period. The interest rate as of 5/31/2003 was 1.30 percent. Principal payable annually to 2/1/2032	11,525	11,700
Other notes with varying terms	—	699
TOTAL NOTES & BONDS PAYABLE	$ 261,209	$ 264,979

Aggregate maturities of notes and bonds payable for the periods subsequent to May 31, 2003 are as follows:

(in thousands of dollars)

	2004	2005	2006	2007	2008	2009 AND THEREAFTER	TOTAL
Notes	$ 2,110	$ 2,619	$ 2,650	$ 1,634	$ 1,671	$ 6,025	$ 16,709
Bonds	5,000	6,200	6,475	6,750	4,850	215,225	244,500
TOTAL	$ 7,110	$ 8,819	$ 9,125	$ 8,384	$ 6,521	$ 221,250	$ 261,209

5. DERIVATIVES & FINANCIAL INSTRUMENTS

The University has limited involvement with derivative financial instruments and does not use them for trading purposes. The University has entered into a long-term interest rate swap agreement with a financial institution counterparty. The purpose of this agreement is to swap the University's Series 2002A variable rate demand bonds having a notional amount of $174,800,000 for a fixed rate of 4.91 percent through February 1, 2032. The University entered into the swap agreement to obtain fixed rate financing at the lowest available cost at the time of the transaction. The value of the swap instrument represents the estimated cost to terminate the swap agreement at the reporting date, taking into account current interest rates. The fair value of the interest rate swap included in the University's balance sheets as a liability at May 31, 2003 and 2002, was $41,711,000 and $15,420,000, respectively. To control counterparty credit risk, the University considered the credit rating, business risk and reputation of the counterparty before entering into the transaction and will monitor the credit standing of its counterparty during the life of the transaction.

The amounts charged to net assets representing the effect of changes in the swap's fair value for the years ended May 31, 2003 and 2002, were $26,291,000 and $15,420,000, respectively.

6. RETIREMENT PLAN

The University has a noncontributory retirement plan covering all full-time faculty and staff. The plan is a defined contribution plan and is administered by outside agencies. Retirement benefits equal the amount accumulated to each individual employee's credit at the date of retirement. The University's contributions to the plan for the years ended May 31, 2003 and 2002 were $8,463,000 and $7,690,000, respectively.

7. POSTRETIREMENT BENEFITS

The University provides medical and life insurance benefits for eligible retired faculty and staff. Currently, substantially all of the University's full-time faculty and staff become eligible for these benefits upon reaching age 55 and having 20 years of full-time service at retirement. The lifetime maximum on group medical benefits is $2,000,000, and the maximum benefit for life insurance is $20,000. The factors in the calculation of medical benefits include retiree premium contributions, deductibles and coinsurance provisions that are assumed to grow with the medical inflation rate.

Effective June 1, 2002, employees attaining the age of 55 with 20 years of continuous, full-time service at Baylor as of May 31, 2007, will continue under the postretirement medical and life insurance programs in effect before June 1, 2002. Those employees not meeting the above eligibility requirements may still participate in the postretirement medical program but will receive no postretirement life insurance benefits and will not be reimbursed for medicare Part B premiums. Under the new plan, all full-time faculty and staff become eligible for postretirement benefits upon reaching age 55 and having 10 years of full-time service at retirement.

The University follows provisions of Statement of Financial Accounting Standards (SFAS) No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions." This standard requires that the expected cost of postretirement benefits be charged to operations on an accrual basis during the years that the faculty and staff render service. SFAS No. 106 also requires that the accumulated obligation at the implementation date be recognized as a liability and that an offsetting amount be recognized as a reduction in fund balance or amortized as an expenditure over 20 years. The University chose to amortize the accumulated postretirement benefits over 20 years.

The benefit obligation, which represents the actuarial present value of benefits attributed to employee service rendered as of May 31, 2003 and 2002, for the unfunded plan, include the following components:

	(in thousands of dollars)	
	2003	**2002**
Benefit obligation at May 31	$ 23,895	$ 17,840
Fair value of plan assets at May 31	—	—
Funded status	$ (23,895)	$ (17,840)
Adjusted accrued benefit liability	$ (8,663)	$ (7,250)
Weighted-average assumptions as of May 31:		
Discount rate	6.00%	7.50%
Expected return on plan assets	N/A	N/A
Rate of compensation increase	4.00%	4.50%

The benefit obligation at May 31, 2003, is determined using an assumed medical cost trend rate of eleven percent. The medical cost trend rates are assumed to decrease gradually to 5 percent over eight years and remain at that level thereafter.

	(in thousands of dollars)	
	2003	**2002**
Net periodic benefit cost	$ 2,381	$ 1,812
Employer contribution	968	943
Plan participants' contribution	713	646
Benefits paid	1,681	1,589

Medical cost trend rate assumptions have a significant impact on the amounts reported. A one percentage point increase in the assumed medical cost trend rate for each future year increases the medical portion of the total June 1, 2003, Accumulated Postretirement Benefit Obligation (APBO) by $2,412,000.

8. OUTSTANDING LEGACIES

The University is the beneficiary under various wills and trust agreements, the realizable amounts of which are not presently determinable. The University's share of such bequests is recorded when the University has an irrevocable right to the bequest and the proceeds are measurable.

9. TAX STATUS

Baylor University is exempt from income tax under Section 501(c)(3) of the Internal Revenue Code. The University has been classified as an organization that is not a private foundation, and contributions to it qualify for deduction as charitable contributions. The University files unrelated business income tax and other information returns as required by government authorities.

10. UNCONDITIONAL PROMISES TO GIVE

As pledges are made to the University, the intent of the donor, the circumstances surrounding the pledge, and any action taken by the University in response to the pledge are considered in determining whether the pledge is an "intent to give" or an "unconditional promise to give." An "intent to give" is not recorded as revenue until collected. An "unconditional promise to give" is recorded as a contribution receivable and as revenue at the present value of the estimated future cash flows.

"Intents to give" total $49,531,000 and $52,860,000 as of May 31, 2003 and 2002, respectively. Payments on these "intents to give" are due in varying periods.

As of May 31, 2003 and 2002, unconditional promises to give consist of the following:

(in thousands of dollars)

	2003	2002
Building projects		
Due in 1 year	$ 1,670	$ 1,814
Due in 1-5 years	2,178	4,649
Due thereafter	—	102
Split interest agreements	15,313	15,758
Less present value adjustment	(7,888)	(8,556)
TOTAL CONTRIBUTIONS RECEIVABLE	$ 11,273	$ 13,767

The unconditional promises to give related to split interest agreements are discounted based on life expectancies of the annuity recipients.

11. COMMITMENTS AND CONTINGENCIES

CAPITAL EXPENDITURES

The University is contractually obligated for amounts aggregating a maximum of approximately $79,412,000 and $26,903,000 at May 31, 2003 and 2002, respectively. Such obligations relate primarily to capital projects.

INVESTMENTS

As part of the University's alternative investments program, the University is obligated under certain limited partnership agreements to advance additional funding up to specified levels upon the request of the general partner. The University had unfunded commitments of $40,672,000 and $39,556,000 at May 31, 2003 and 2002, respectively, which are expected to be called over the next five years.

CONTINGENCIES

The University is a party to various legal proceedings and complaints arising in the ordinary course of operations, some of which are covered by insurance. The administration is not aware of any claims or contingencies, which are not covered by insurance, that would be material to the financial position of the University.

The University participates in several state and federal grant programs and must comply with requirements of the grantor agencies. The administration is of the opinion that the University is in compliance with these grantor requirements.

AS OF MAY 31, 2003

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