Baylor University

Financial Statements
Years Ended May 31, 2011 and 2010,
and Independent Auditors' Report

BAYLOR UNIVERSITY

FINANCIAL STATEMENTS

Years Ended May 31, 2011 and 2010

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INDEPENDENT AUDITORS' REPORT

Board of Regents
Baylor University

We have audited the accompanying balance sheets of Baylor University (the "University") as of May 31, 2011 and 2010, and the related statements of activities and cash flows for the years 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 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, the financial statements referred to above present fairly, in all material respects, the financial position of the University as of May 31, 2011 and 2010, 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.

Deloitte & Touche LLP

September 27, 2011

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BAYLOR UNIVERSITY
Balance Sheets

May 31, 2011 and 2010
(in thousands of dollars)

	2011	2010
ASSETS		
Cash & cash equivalents	$ 40,846	$ 38,736
Short-term investments	42,089	35,646
Student accounts receivable, net	14,724	14,546
Contributions, grants & other receivables	37,816	23,964
Prepaid expenses & other	6,953	6,025
Student loans receivable, net	11,025	12,744
Long-term investments, at fair value	1,079,330	933,745
Property, plant & equipment, net	634,333	622,548
Total assets	**$ 1,867,116**	**$ 1,687,954**
LIABILITIES & NET ASSETS		
Liabilities		
Accounts payable	$ 21,020	$ 16,302
Personnel related liabilities	16,778	19,565
Deposits & deferred revenue	55,614	36,845
Notes & bonds payable	328,350	317,376
Interest rate swap liability	1,068	--
Accrued postretirement benefits	52,161	45,710
Other liabilities	16,936	15,990
Total liabilities	**491,927**	**451,788**
Net Assets		
Unrestricted	469,283	437,852
Temporarily restricted	302,447	228,879
Permanently restricted	603,459	569,435
Total net assets	**1,375,189**	**1,236,166**
Total liabilities & net assets	**$ 1,867,116**	**$ 1,687,954**

See accompanying notes to financial statements.

BAYLOR UNIVERSITY
Statements of Activities

For the Years Ended May 31, 2011 and 2010
(in thousands of dollars)

	Year Ended May 31, 2011			
	Unrestricted	**Temporarily Restricted**	**Permanently Restricted**	**Total**
REVENUES				
Tuition & fees	$ 432,090	$ --	$ --	**$ 432,090**
Less scholarships	(170,503)	--	--	**(170,503)**
Net tuition & fees	261,587	--	--	**261,587**
Gifts	14,615	6,909	19,336	**40,860**
Investment income	3,059	29	79	**3,167**
Endowment returns distributed	43,780	6,520	2,131	**52,431**
Grants & contracts	27,443	618	--	**28,061**
Other sources - educational & general	19,705	2	--	**19,707**
Other sources - intercollegiate athletics	23,591	--	--	**23,591**
Sales & services of auxiliary enterprises	45,445	--	--	**45,445**
Total revenues	439,225	14,078	21,546	**474,849**
Net assets released from restrictions	11,895	(12,265)	370	**--**
Total net revenues	451,120	1,813	21,916	**474,849**
EXPENSES				
Program expenses				
Instruction	204,940			**204,940**
Academic support, research & public service	58,783			**58,783**
Student services & activities	87,566			**87,566**
Auxiliary enterprises	37,212			**37,212**
Support expenses				
Institutional support	57,998			**57,998**
Total expenses	446,499	--	--	**446,499**
Increase (decrease) in net assets before other changes	4,621	1,813	21,916	**28,350**
OTHER CHANGES				
Gains (losses) on investments, net of distributions	30,362	69,704	9,496	**109,562**
Gain (loss) on interest rate swap	(1,068)	--	--	**(1,068)**
Losses on disposal of property & equipment	(470)	--	--	**(470)**
Change in postretirement benefits obligation other than net periodic benefit cost	(2,079)	--	--	**(2,079)**
Change in value of split interest agreements	65	2,051	2,612	**4,728**
Total other changes	26,810	71,755	12,108	**110,673**
Increase (decrease) in net assets	31,431	73,568	34,024	**139,023**
Net assets at beginning of year	437,852	228,879	569,435	**1,236,166**
Net assets at end of year	$ 469,283	$ 302,447	$ 603,459	**$ 1,375,189**

See accompanying notes to financial statements.

Year Ended May 31, 2010			
Unrestricted	Temporarily Restricted	Permanently Restricted	**Total**
$ 399,351	$ --	$ --	**$ 399,351**
(150,014)	--	--	**(150,014)**
249,337	--	--	**249,337**
17,947	4,512	14,552	**37,011**
3,042	36	101	**3,179**
42,319	6,293	1,969	**50,581**
25,390	241	--	**25,631**
18,268	81	--	**18,349**
22,323	--	--	**22,323**
41,675	--	--	**41,675**
420,301	11,163	16,622	**448,086**
15,087	(13,756)	(1,331)	**--**
435,388	(2,593)	15,291	**448,086**
194,018			**194,018**
57,406			**57,406**
79,501			**79,501**
37,079			**37,079**
53,833			**53,833**
421,837	--	--	**421,837**
13,551	(2,593)	15,291	**26,249**
(13,180)	(22,084)	1,469	**(33,795)**
9,938	--	--	**9,938**
(1,204)	--	--	**(1,204)**
(9,359)	--	--	**(9,359)**
6	1,175	1,461	**2,642**
(13,799)	(20,909)	2,930	**(31,778)**
(248)	(23,502)	18,221	**(5,529)**
438,100	252,381	551,214	**1,241,695**
$ 437,852	$ 228,879	$ 569,435	**$ 1,236,166**

BAYLOR UNIVERSITY
Statements of Cash Flows

For the Years Ended May 31, 2011 and 2010
(in thousands of dollars)

	Year Ended May 31, 2011	Year Ended May 31, 2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Increase (Decrease) in Net Assets	**$ 139,023**	**$ (5,529)**
Adjustments to reconcile increase (decrease) in net assets to net cash provided by operating activities:		
Depreciation	30,950	29,643
Realized & unrealized (gains) losses on investments	(109,562)	33,795
Realized & unrealized (gain) loss on interest rate swap	1,068	(9,938)
Losses on disposal of property & equipment	470	1,204
Fixed assets gifts-in-kind	(177)	(131)
Contributions restricted for plant & permanent investment	(20,531)	(19,176)
Provision for bad debts	673	83
Decrease (increase) in:		
Short-term investments	(6,443)	(10,532)
Student accounts receivable	(152)	(229)
Contributions, grants & other receivables	(13,852)	110
Prepaid expenses & other	(928)	(287)
Increase (decrease) in:		
Accounts payable	4,718	(3,667)
Personnel related liabilities	(2,787)	1,409
Deposits & deferred revenue	18,769	687
Accrued postretirement benefits	6,451	12,617
Other liabilities	850	(821)
Net cash provided by operating activities	**48,540**	**29,238**
CASH FLOWS FROM INVESTING ACTIVITIES		
Student loans made	(701)	(212)
Proceeds from collections of student loans	1,721	1,260
Proceeds from sales of long-term investments	15,945	15,333
Purchases of long-term investments	(51,968)	(46,892)
Purchases of property, plant & equipment	(43,028)	(26,029)
Net cash used in investing activities	**(78,031)**	**(56,540)**
CASH FLOWS FROM FINANCING ACTIVITIES		
Contributions restricted for plant & permanent investment:		
Plant	1,195	4,624
Endowment	18,778	14,390
Annuity & living trusts	558	162
Proceeds from long-term debt	125,062	--
Repayment of long-term debt	(114,088)	(5,024)
Payment of interest rate swap liability	--	(17,623)
Increase in federal student loan funds refundable	96	94
Net cash provided by (used in) financing activities	**31,601**	**(3,377)**
Net increase (decrease) in cash & cash equivalents	**2,110**	**(30,679)**
Cash & cash equivalents at beginning of year	**38,736**	**69,415**
Cash & cash equivalents at end of year	**$ 40,846**	**$ 38,736**

See accompanying notes to financial statements.

OVERVIEW OF BAYLOR UNIVERSITY

The mission of Baylor University (the "University") is to educate men and women for worldwide leadership and service by integrating academic excellence and Christian commitment within a caring community.

Chartered in 1845 by the Republic of Texas and affiliated with the Baptist General Convention of Texas, the University is the oldest continuously operating institution of higher learning in the state of Texas. Established to be a servant of the church and of society, the University seeks to fulfill its calling through excellence in teaching and research, in scholarship and publication, and in service to the community, both local and global. The approximately 1,000-acre campus is located on the banks of the Brazos River in Waco, Texas, a metropolitan area of 229,000 people.

While remaining true to its Christian heritage, the University has grown to approximately 14,900 students, and its nationally recognized academic units offer 151 undergraduate, 76 master's, a Juris Doctor and 32 doctoral degree programs.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting & Reporting

The financial statements of Baylor University include the accounts of the University, Brazos Valley Public Broadcasting Foundation (KWBU), Waco Research Park, LLC, and Central Texas Technology & Research Park, legally separate entities, over which the University has control as a sole member or for which the board of directors are chosen by the University's Board of Regents. The University's financial statements do not include the accounts of the Baylor Foundation, Baylor Bear Foundation, Baylor "B" Association or Baylor Alumni Association. These entities are excluded due to the nature of their relationship to the University or due to their aggregate assets, revenues, expenses and net assets not being significant in relation to the University.

The financial statements of the University are prepared in conformity with accounting principles generally accepted in the United States of America. 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 or legal restrictions. Unrestricted net assets may be designated for specific purposes by the University's Board of Regents.

Temporarily restricted -- net assets subject to donor-imposed or legal restrictions that must 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 earnings on the related investments for general or specific purposes.

Revenues are reported as increases in unrestricted net assets unless the use of the related assets is limited by donor-imposed restrictions that are not anticipated to be met in the year of receipt. Expenses are reported as decreases in unrestricted net assets. Income and net gains and losses on investments in donor restricted endowments are reported as increases or decreases in temporarily restricted net assets until appropriated for expenditure by the University. All other 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 restrictions among applicable net asset classes. Changes or clarifications in donor stipulations may cause certain net assets to be reclassified between permanently restricted, temporarily restricted or unrestricted net assets. These reclassifications are reported as net assets released from restrictions among applicable net assets classes.

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.

Cash & Cash Equivalents

Cash on deposit and all highly liquid financial instruments with original maturities of three months or less are classified as cash and cash equivalents, except those amounts assigned to investment managers, which are classified as investments.

Short-Term Investments

Short-term investments consist of operational funds invested in bank time deposits, short-term U.S. government securities, those having maturities longer than three months but less than one year, and highly liquid money market funds.

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 long-term investments (see Note 4), 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 5). Annuities payable are recorded at the present value of future payments, based on the Internal Revenue Service ("IRS") discount rate at the time of the original gift.

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 included in other liabilities in the accompanying balance sheets.

Property, Plant & Equipment

Property, plant and equipment valued at $5,000 or more are recorded at cost at the date of acquisition or, if acquired by gift, at estimated fair value at the 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. Land and art/collections are considered non-depreciable given the nature of the assets. Equipment is removed from the records at the time of disposal.

The University recognizes asset retirement obligations (AROs) that are conditional on a future event, such as the legal obligation to safely dispose of asbestos when a building is remodeled or demolished. The University measures conditional AROs at estimated fair value using site specific surveys and a probability-weighted, discounted cash flow model with multiple scenarios, if applicable.

The University reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. An impairment charge is recognized when the fair value of the asset is less than the carrying value.

Deposits & Deferred Revenue

Deposits and deferred revenue consist of amounts billed or received for educational, research, intercollegiate athletics or auxiliary goods and services that have not yet been earned.

Tuition & Fees

Tuition and fees revenues are recognized in the fiscal year during which the related semester concludes. Scholarships provided by the University for tuition and fees are reflected as a reduction of tuition and fees revenues. Scholarships are awarded to students by the University from unrestricted revenues, restricted endowment earnings, restricted gifts or government grants. Scholarships do not include payments to students for services rendered to the University.

Contributions

Contributions are recorded as revenues in the appropriate net asset class based on donor-imposed restrictions. Expiration of temporary restrictions on donor contributions are reported as net assets released from restrictions.

Contributions received with donor-imposed restrictions that are anticipated to be 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.

Contributions receivable are recorded at the present value of estimated future cash flows using an appropriate discount rate at the time the contribution was recorded.

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, interest expense and operation and maintenance of plant have been allocated directly or based on square footage among the functional categories.

Fundraising expenses of approximately $13,291,000 and $13,380,000 incurred by the University in 2011 and 2010, respectively, are included primarily in the institutional support category in the statements of activities.

Use of Estimates & Assumptions

The preparation of financial statements requires management to make estimates and assumptions that affect reported amounts of assets, liabilities, revenues and expenses during the reporting period, as well as the disclosure of contingent assets and liabilities. Significant items subject to such estimates and assumptions include valuations of certain investments which do not have readily determinable fair values, allowances for uncollectible accounts and contingency reserves, calculations of asset retirement obligations, interest rate swap liability and actuarially determined liabilities related to postretirement benefit plans. Actual results ultimately could differ from management’s estimates and assumptions.

Other

To conform to the May 31, 2011 statements presentation, $1,484,000 of private contract revenues, previously included in other sources – educational & general in the year ended May 31, 2010 statement of activities, has been moved to grants & contracts revenues. Also, $4,624,000 of contributions restricted for plant assets received during the year ended May 31, 2010 have been separated from contributions provided by operating activities and are reported as cash flows from financing activities on the accompanying statements of cash flows.

2. FAIR VALUE MEASUREMENTS

The estimated fair values of financial instruments that differ from the carrying amounts have been determined by the University using available market information. The estimates are not necessarily indicative of the amounts the University could realize in a current market exchange.

The carrying amounts of cash and cash equivalents, short-term investments, student accounts receivable, accounts payable, personnel related liabilities and deposits and deferred revenue approximate fair value because of their short maturity.

The carrying value of loans receivable from students under government loan programs is a reasonable estimate of fair value since the loans receivable cannot be sold and can only be assigned to the U.S. government or its designees. The fair value of loans receivable from students under University loan programs approximates carrying value.

The University records long-term investments and interest rate swaps at fair value. The estimated fair value of investments is based on quoted market prices except for certain investments for which quoted market prices are not available. Generally accepted accounting principles provide guidance for estimating the fair value of investments in investment companies that calculate net asset value. Accordingly, investments for which observable market prices in active markets do not exist are reported at fair value, as determined by the University, using net asset value as a practical expedient of fair value and other available information. The amount determined to be fair value may incorporate the University’s own assumptions (including appropriate risk adjustments for nonperformance and lack of marketability).

The estimated fair value of most alternative assets managed and held in limited partnership or other private investment fund structures is based on the most recent valuations provided by the external investment fund managers, adjusted for receipts and disbursements through May 31. The University reviewed and evaluated the values provided by the managers and agreed with the valuation methods and assumptions used to determine those values except in a few immaterial instances. In those limited instances, the University applied additional valuation procedures furnished by qualified third parties or incorporated additional related financial data provided by fund managers to arrive at a fair value different than manager provided values. When the University determines a different value, the investment is carried at the more conservative of the two values. Therefore, the University believes the carrying amount of these financial instruments is a reasonable estimate of the fair value. Because alternative assets are not readily marketable, their estimated value is subject to uncertainty and, therefore, may differ from the value that would have been used had a ready market for such investments existed. 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 interests is estimated based on the expected net revenues generated by those assets. With certain holdings, geological reserve analysis can provide additional information for estimating fair value. For the fiscal years ended May 31, 2011 and 2010, the University commissioned an engineering report and geological study of its largest mineral interest holding to obtain a more informed estimate of fair value and incorporated the results of the study into its estimate of expected net revenues and fair value for this holding.

Fair value is reflected in a hierarchy which prioritizes and ranks the level of market price observability. Market price observability is impacted by a number of factors, including the type of investment, the characteristics specific to the investment, and the state of the marketplace (including the existence and transparency of transactions between market participants). Investments with readily-available actively quoted prices or for which fair value can be measured from actively-quoted prices in an orderly market will generally have a higher degree of market price observability and a lesser degree of judgment used in measuring fair value.

Investments measured and reported at fair value are classified and disclosed in one of the following categories based on inputs:

Level 1 – Quoted prices (unadjusted) are available in active markets for identical investments that the University has the ability to access as of the reporting date. The type of investments generally included in Level 1 are listed securities traded on public exchanges and open-end mutual funds and other publicly traded listed securities held indirectly through separately managed accounts.

Level 2 – Pricing inputs are observable for the investments, either directly or indirectly, as of the reporting date, but are not the same as those used in Level 1. Fair value is determined through the use of models or other valuation methodologies. The types of investments generally included in this category are hedge funds primarily holding publicly-traded securities with significant fund level liquidity within ninety days.

Level 3 – Pricing inputs are unobservable for the investments and include situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require significant judgment or estimation by the fund manager. These types of investments generally include hedge funds with significant liquidity restrictions, private equities and real assets held in partnership format.

Whereas Level 1 investments are able to be liquidated as of the reporting date at published market values, Level 2 and 3 investments may contain restrictions on the ability to liquidate assets as of the reporting date. Investments that can be liquidated within ninety days of the reporting date at net asset value or its equivalent are classified as Level 2 investments. Investments classified as Level 3 have significant liquidity restrictions which would prevent redemption within ninety days of the reporting date, if at all.

Generally accepted accounting principles permit entities to choose to measure financial instruments and other items at fair value that are not currently required to be measured at fair value. The University has elected not to value any other financial assets or liabilities at fair value as provided for in accounting guidelines.

3. ENDOWMENT

The University's endowment pool consists of donor-restricted endowment funds and board designated endowment funds and is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA). The Board of Regents (the "Board") of the University has an established policy consistent with UPMIFA as adopted by the state of Texas. The University seeks to preserve the fair value of the original gift as of the gift date of the donor restricted endowment funds absent explicit donor stipulations to the contrary. Accordingly, the University classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor agreement at the time the accumulation is added to the fund. The remaining portion of the donor restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the University in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the University considers the following factors in making a determination to appropriate or accumulate donor restricted endowment funds:

(1) The duration and preservation of the fund
(2) The purposes of the University and the donor restricted endowment fund
(3) General economic conditions
(4) The possible effect of inflation and deflation
(5) The expected total return from income and the appreciation of investments
(6) Other resources of the University
(7) The investment policies of the University

Board designated endowment net assets include gifts and other revenues that have been designated by 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.

Changes in endowment net assets for the year ended May 31, 2011 are as follows *(in thousands of dollars)*:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, May 31, 2010	$ 121,306	$ 203,863	$ 546,797	$ 871,966
Endowment earnings	43,813	6,520	4,196	54,529
Gains (losses) on investments	25,174	69,673	9,363	104,210
Contributions	--	--	18,761	18,761
Terminated annuities & other	--	--	2,241	2,241
Transfers to board designated	3,942	711	--	4,653
Distributed earnings	(43,780)	(6,520)	(2,131)	(52,431)
Endowment net assets, May 31, 2011	$ 150,455	$ 274,247	$ 579,227	$ 1,003,929

Changes in endowment net assets for the year ended May 31, 2010 are as follows *(in thousands of dollars)*:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, May 31, 2009	$ 126,639	$ 224,083	$ 529,534	$ 880,256
Endowment earnings	42,348	6,293	3,873	52,514
Gains (losses) on investments	(10,947)	(22,029)	1,525	(31,451)
Contributions	--	--	14,151	14,151
Terminated annuities & other	--	--	(317)	(317)
Transfers to board designated	5,585	1,809	--	7,394
Distributed earnings	(42,319)	(6,293)	(1,969)	(50,581)
Endowment net assets, May 31, 2010	$ 121,306	$ 203,863	$ 546,797	$ 871,966

Funds totaling $4,237,000 and $13,993,000, which market values are less than original values, are reported in unrestricted net assets in the accompanying balance sheets as of May 31, 2011 and 2010, respectively.

Return Objectives & Risk Parameters

The University has adopted investment and spending policies for endowment assets that attempt to meet three objectives: (1) provide a predictable, stable stream of earnings to participating accounts; (2) ensure that the purchasing power of this revenue stream does not decline over time; and (3) ensure that the purchasing power of the endowment assets do not decline over time. To meet its long-term rate-of-return objectives, the University relies on a total return strategy utilizing both income and growth to maximize the risk adjusted return through diversification of the assets. Under this policy, actual earnings, as well as a prudent portion of realized and unrealized gains may be distributed for operational needs or in accordance with donor restrictions. Accordingly, the endowment assets are invested in a diversified manner that is intended to produce results that exceed its long-term performance benchmarks. The University expects its endowment funds, over time, to provide an average rate of return at least equal to the spending policy requirements plus the rate of inflation. Actual returns in any given year may vary from this amount.

Spending Policy & How the Investment Objectives Relate to Spending Policy

The Baylor University Fund ("BUF") is a unitized fund consisting of publicly traded equity and fixed income securities, alternative assets and mineral rights; and serves as the primary investment vehicle for the University's endowment and other long-term investments. As permitted under Texas law, the Board has adopted a spending policy for the BUF that authorizes a dividend to be paid for endowments participating in the BUF to be used for the purposes intended by donors. For the years ended May 31, 2011 and 2010, this dollar dividend per BUF unit was based on 5% of the previous 48-months' rolling average net asset market value per unit of the BUF. The permitted change in this dividend amount from the previous year shall be no less than 0% and no more than 6%, and in no case shall the annual fiscal year distribution (dollar dividend amount per BUF unit) exceed 7% of the previous 48-months' rolling average net asset market value per BUF unit. The dividend rate increased slightly for the years ended May 31, 2011 and 2010. Endowment earnings distributed include endowment distributions in accordance with the University's BUF spending policy, as well as, distributions of income from other endowment assets.

In establishing this spending policy, the University considered the long-term expected return on its endowment assets. Accordingly, the University expects the current spending policy to preserve the real purchasing power of the endowment assets, while helping to maintain intergenerational value of the assets, as well as to provide additional real growth through new gifts and investment return.

4. LONG-TERM INVESTMENTS

The University diversifies its investments among various financial instruments and asset categories and uses multiple investment strategies. As with most large endowments, these financial assets are managed primarily through external investment management firms selected and monitored by the University's Office of Investments and the Baylor Executive Investment Committee in accordance with the University's Endowment Investment Policy. The investment management firms are predominately organized in limited partnership, registered investment company (mutual fund), and trust format.

Fixed income securities are assets invested (directly or indirectly) in domestic and international government or corporate bonds for which active trading markets exist, including open and closed-end mutual funds holding such securities.

Public equities are assets invested (directly or indirectly) in publicly traded equity shares which are listed on national and international exchanges as well as publicly traded open and closed-end mutual funds holding such securities.

Alternative assets consist of private equities, real assets, and hedge funds investments and are all held primarily in partnership format. Capital is allocated to domestic and international markets in the various alternative investment funds. Most of the underlying assets in the private equity and real asset partnerships and trusts are not immediately liquid. Private equity fund strategies include buyouts, venture capital, distressed/special situations, emerging markets and secondary markets. Real asset funds are predominately private limited partnerships investing in numerous types of properties and strategies such as commercial real estate, energy, power and infrastructure, as well as timber and other natural resources and commodities including industrial and precious metals. Private equity and real asset funds are held as long-term investments and are structured as closed-end, commitment-based investment funds where the investor commits a specified amount of capital upon inception of the fund which is then drawn down over a specified period of the fund's life. These funds generally cannot be redeemed prior to the specified termination date and will only receive distributions upon a disposition of the underlying assets of the portfolio. As a limited partner, the University will not generally have any influence over the timing of such distributions. At May 31, 2011, the remaining life of private equity and real asset funds ranged from one to ten years. Hedge fund investments are generally open-end funds structured in limited partnership format. These funds employ various investment strategies such as long/short equity, fundamental value, multi-strategy (including a small allocation to fund-of-funds), distressed asset and debt, and short credit. The amount of liquidity available to investors is directly related to the liquidity and risk associated with the underlying portfolio. Hedge funds typically offer subscription and redemption options to investors over time periods shorter than private equity/real asset funds; however, the frequency of subscriptions or redemptions is dictated by each fund's governing documents. Liquidity of individual hedge funds also varies due to illiquid "side-pocket" investments, as well as contractual restrictions on redemption such as gating and holdback provisions. Redemption terms of hedge funds range from monthly upon thirty day notice to rolling three years upon forty-five day notice. Of eighteen hedge funds totaling $178,336,000, six funds totaling $20,948,000 have been suspended or gated, and as of May 31, 2011, three of these six were in liquidation mode.

Real estate & other investments represent direct real estate and asset holdings of the University and are not held in the fund, limited partnership, and trust structures described above.

Mineral rights are held and managed for the benefit of the University under various contractual and revocable trust arrangements and are not held in the fund and limited partnership structures described above. The University retains ultimate ownership and control of these assets.

Income interests/perpetual trusts are held and managed by outside trustees under various annuity and trust arrangements for the benefit of Baylor. The University receives income distributions over time in accordance with the governing annuity, trust and gift instruments. The underlying investments of the income interests/perpetual trusts are primarily comprised of publicly traded equity and fixed income investments held in common trust funds and other funds managed or selected by the outside trustees.

The following table presents information about the University's long-term investments that are measured at fair value as of May 31, 2011 and indicates the fair value hierarchy of the valuation techniques utilized to determine such fair value *(in thousands of dollars)*:

	Level 1	Level 2	Level 3	Total
Fixed income securities	$ 67,558	$ --	$ --	$ 67,558
Public equities	236,919	--	441	237,360
Alternative assets	--	114,029	452,239	566,268
Real estate & other	--	--	3,377	3,377
Mineral rights	--	--	37,647	37,647
Income interests/perpetual trusts	--	--	167,120	167,120
Total	$ 304,477	$ 114,029	$ 660,824	$ 1,079,330

Alternative assets reflected as Level 2 have been valued using net asset value as a practical expedient of fair value.

The following table presents additional information about assets that have been measured at fair value as of May 31, 2011 on a recurring basis using significant unobservable inputs (Level 3) *(in thousands of dollars)*:

	May 31, 2010 Balance	Transfers In (Out) of Level 3	Additions & (Distributions) Net	Realized & Unrealized Gains (Losses)	May 31, 2011 Balance
Fixed income securities	$ --	$ --	$ --	$ --	$ --
Public equities	456	--	--	(15)	441
Alternative assets	408,524	--	(15,121)	58,836	452,239
Real estate & other	4,349	--	(980)	8	3,377
Mineral rights	37,685	--	13	(51)	37,647
Income interests/ perpetual trusts	143,016	--	4,795	19,309	167,120
Total	$ 594,030	$ --	$ (11,293)	$ 78,087	$ 660,824

There were no significant transfers in or out of Levels 1 and 2 for the year ended May 31, 2011.

The following table presents information about the University's long-term investments that are measured at fair value as of May 31, 2010 and indicates the fair value hierarchy of the valuation techniques utilized to determine such fair value *(in thousands of dollars)*:

	Level 1	Level 2	Level 3	Total
Fixed income securities	$ 28,810	$ --	$ --	$ 28,810
Public equities	199,936	--	456	200,392
Alternative assets	--	110,969	408,524	519,493
Real estate & other	--	--	4,349	4,349
Mineral rights	--	--	37,685	37,685
Income interests/perpetual trusts	--	--	143,016	143,016
Total	$ 228,746	$ 110,969	$ 594,030	$ 933,745

The following table presents additional information about assets that have been measured at fair value as of May 31, 2010 on a recurring basis using significant unobservable inputs (Level 3) *(in thousands of dollars)*:

	May 31, 2009 Balance	Transfers In (Out) of Level 3	Additions & (Distributions) Net	Realized & Unrealized Gains (Losses)	May 31, 2010 Balance
Fixed income securities	$ 59	$ --	$ (59)	$ --	$ --
Public equities	51,830	(51,422)	--	48	456
Alternative assets	479,803	(96,862)	(3,208)	28,791	408,524
Real estate & other	4,196	--	395	(242)	4,349
Mineral rights	117,970	--	--	(80,285)	37,685
Income interests/ perpetual trusts	138,053	--	(859)	5,822	143,016
Total	$ 791,911	$ (148,284)	$ (3,731)	$ (45,866)	$ 594,030

For the fiscal year ended May 31, 2010, transfers of $51,422,000 were made into Level 1 and $96,862,000 were made into Level 2 based upon additional information related to investment asset fund structures, characteristics, holdings and liquidity provisions. These transfers were valued using June 1, 2009 balances.

Whereas the preceding tables reflect investments based on fair value hierarchy, the following table reflects investments using traditional classification descriptions. The underlying assets of income interests/perpetual trusts are reflected within the investment classifications. Estimated fair value of investments as of May 31, 2011 and 2010, are as follows:

	(in thousands of dollars)	
	2011	2010
Investments:		
Fixed income securities	$ 104,921	$ 64,649
Public equities	333,343	280,952
Alternative assets	593,890	541,742
Mineral rights	47,176	46,402
Total investments	$ 1,079,330	$ 933,745

Total investments include assets under split-interest agreements of $23,782,000 and $20,192,000 as of May 31, 2011 and 2010, respectively.

The cost of long-term investments was $826,703,000 and $792,891,000 as of May 31, 2011 and 2010, respectively.

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

At May 31, 2011 and 2010, alternative assets were invested with fifty-seven different managers. The total fair values by strategy type are as follows:

	(in thousands of dollars)	
	2011	2010
Alternative assets:		
Private equities	$ 192,999	$ 168,052
Hedge funds	178,336	181,082
Real assets	222,555	192,608
Total alternative assets	$ 593,890	$ 541,742

As part of the University's alternative assets program, the University is obligated under certain limited partnership agreements to advance funding up to specified levels upon the request of the general partner. The University had unfunded commitments consisting of the following at May 31, 2011 and 2010, respectively, which are expected to be called over the next three years.

	(in thousands of dollars)	
	2011	2010
Alternative assets:		
Private equities	$ 41,759	$ 61,568
Real assets	27,939	49,465
Total unfunded commitments	$ 69,698	$ 111,033

Long-term investment returns for the years ended May 31, 2011 and 2010, consist of the following:

	(in thousands of dollars)	
	2011	2010
Endowment earnings distributed	$ 52,431	$ 50,581
Net appreciation (depreciation), realized and unrealized	109,562	(33,795)
Total long-term investment returns (losses)	$ 161,993	$ 16,786

The total long-term investment returns are net of investment expenses of $3,445,000 and $3,418,000 for the years ended May 31, 2011 and 2010, respectively.

5. 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 unconditional promise to give is recorded as a contribution receivable and as gifts revenue at the present value of the estimated future cash flows. Unconditional promises to give related to split interest agreements are discounted based on life expectancies of the annuity recipients.

As of May 31, 2011 and 2010, unconditional promises to give consist of the following:

	(in thousands of dollars)	
	2011	2010
Restricted current funds	$ 93	$ 214
Endowment funds	2,000	--
Plant projects:		
Due in 1 year	1,000	800
Due in 1 to 5 years	--	1,000
Split interest agreements	21,988	20,510
Less: Present value adjustment	(8,762)	(8,721)
Total contributions receivable	$ 16,319	$ 13,803

An intent to give is not recorded as gifts revenue until collected or converted to an unconditional promise to give. Intents to give total $22,681,000 and $14,484,000 as of May 31, 2011 and 2010, respectively. Payments on these intents to give are due in varying periods. Additionally, the University is the beneficiary under various wills and trust agreements of which the realizable amounts 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.

6. PROPERTY, PLANT & EQUIPMENT

At May 31, 2011 and 2010, property, plant and equipment assets consist of the following:

	(in thousands of dollars)	
	2011	2010
Land	$ 65,259	$ 60,145
Land/leasehold improvements	69,201	66,919
Buildings	691,144	670,990
Equipment	71,322	66,627
Arts/collections	10,527	10,315
Other	38,628	37,013
	946,081	912,009
Less accumulated depreciation	(331,105)	(303,796)
	614,976	608,213
Construction-in-progress	19,357	14,335
Property, plant & equipment, net	$ 634,333	$ 622,548

Depreciation expense was $30,950,000 and $29,643,000 as of May 31, 2011 and 2010, respectively. The “Equipment” category includes computers, software and other types of equipment above the $5,000 threshold. The “Other” category includes vehicles, library materials and miscellaneous other assets. Real and personal property were insured for $1.3 billion at May 31, 2011 and 2010. The liability for conditional asset retirement obligations was $3,935,000 and $3,664,000 as of May 31, 2011 and 2010, respectively, and is included in other liabilities in the accompanying balance sheets.

7. NOTES & BONDS PAYABLE

Notes and bonds payable consist of both non-interest bearing unsecured notes and interest bearing unsecured and secured notes, commercial paper with varying maturities, and bonds with varying terms and maturity dates to March 1, 2036. Interest payments on a cash basis totaled $7,764,000 and $14,011,000, and interest expense was $8,591,000 and $11,480,000 for the years ended May 31, 2011 and 2010, respectively.

As of May 31, 2011 and 2010, unamortized bond and commercial paper issuance costs of $2,070,000 and $1,257,000, respectively, were included in prepaid expenses and other in the University’s balance sheets. Amortization expense for issuance costs was $77,000 and $73,000 for the years ended May 31, 2011 and 2010, respectively.

Notes and bonds payable at May 31, 2011 and 2010, consist of the following:

	(in thousands of dollars)	
	2011	2010
Non-interest bearing unsecured note payable to a foundation, due in annual installments beginning June 30, 2004 to June 30, 2013	$ 1,500	$ 2,000
Non-interest bearing unsecured note payable to a foundation, due in quarterly installments	118	209
Secured note payable to a private entity (secured by land), bearing interest at 7.5%, due in annual installments to January 2, 2012	695	1,342
Taxable Commercial Paper Notes, Series A, with varying maturities and discount rates rolled at each maturity	30,000	50,000
Series 2008A Waco Education Finance Corporation Tax-Exempt Variable Rate Demand Bonds, swapped to a fixed rate of 2.476% (see Note 9), interest payable monthly, principal payable annually to February 1, 2032	73,875	75,860
Series 2008B Waco Education Finance Corporation Tax-Exempt Variable Rate Demand Bonds redeemed on April 25, 2011	--	75,865

	(in thousands of dollars) 2011	2010
Series 2008C Waco Education Finance Corporation Tax-Exempt Fixed Rate Bonds, interest ranging from 5.0% to 5.25% payable semiannually, principal payable annually beginning March 1, 2019 to March 1, 2036	112,100	112,100
Series 2011 Clifton Higher Education Finance Corporation Tax-Exempt Fixed Rate Bonds, interest ranging from 3.0% to 5.25% payable semiannually, principal payable annually beginning March 1, 2012 to March 1, 2032	102,980	--
Total notes & bonds payable prior to unamortized bond premium	321,268	317,376
Unamortized bond premium	7,082	--
Total notes & bonds payable	$ 328,350	$ 317,376

The fair values of notes and bonds payable were approximately $334,637,000 and $323,135,000 as of May 31, 2011 and 2010, respectively.

The Series 2008A Tax-Exempt Variable Rate Demand Bonds are subject to purchase upon tender with proper notice and delivery to the remarketing agent. The University has a Standby Bond Purchase Agreement (SBPA) with a bank to purchase the bonds in the event the remarketing agent is unable to remarket the bonds. The SBPA, which is for a term of two years, is renewable in April 2013 and includes a term out period of twelve equal quarterly installments commencing on the first business day of the fourth full month after purchase of the bonds.

During the fiscal year ended May 31, 2011, the University issued $102,980,000 of tax-exempt bonds in order to refinance the Series 2008B bonds and $35,000,000 of the taxable commercial paper notes. The Series 2011 bonds were issued at a premium of $7,222,000. The premium is being amortized using the effective interest method over the life of the bonds as a net to the bond interest payments.

Excluding the maturity of commercial paper, scheduled principal payments on long-term notes and bonds for the periods subsequent to May 31, 2011, are as follows *(in thousands of dollars)*:

2012	$ 6,180
2013	5,633
2014	5,800
2015	5,540
2016	5,820
2017 and thereafter	262,295
Total	$ 291,268

In December 2008, the University issued taxable commercial paper notes with varying maturities and discount rates in an aggregate total of $50,000,000. The notes bear a fixed discount rate, established on the borrowing date, over their individual terms, not to exceed $15,000,000 maturing on any one day with maturities not to exceed two hundred seventy days. The University refunded $35,000,000 of commercial paper during April 2011 and subsequently reissued $15,000,000 on April 29, 2011. At May 31, 2011, the University had an outstanding balance of $30,000,000 in commercial paper notes with various maturities to October 26, 2011 and an average discount rate of 0.30%. The University anticipates that the commercial paper will continue to be rolled at maturity until such time that it is refunded by long-term debt.

The estimated fair value of the commercial paper notes approximates the face value.

8. NET ASSETS

The University's unrestricted, temporarily restricted and permanently restricted net assets for the year ended May 31, 2011 are categorized by purpose as follows *(in thousands of dollars)*:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Unrestricted-designated for operations	$ 35,076	$ --	$ --	$ 35,076
Unrestricted-designated for plant	30,964	--	--	30,964
Restricted	--	9,879	6,266	16,145
Endowment	(4,237)	259,779	579,227	834,769
Endowment-Board designated	154,692	14,468	--	169,160
Annuity & living trusts	--	16,424	17,966	34,390
Invested in plant	252,788	1,897	--	254,685
Total net assets	$ 469,283	$ 302,447	$ 603,459	$ 1,375,189

The University's unrestricted, temporarily restricted and permanently restricted net assets for the year ended May 31, 2010 are categorized by purpose as follows *(in thousands of dollars)*:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Unrestricted-designated for operations	$ 24,917	$ --	$ --	$ 24,917
Unrestricted-designated for plant	30,416	--	--	30,416
Restricted	--	10,255	6,622	16,877
Endowment	(13,993)	191,413	546,797	724,217
Endowment-Board designated	135,299	12,450	--	147,749
Annuity & living trusts	--	11,205	16,016	27,221
Invested in plant	261,213	3,556	--	264,769
Total net assets	$ 437,852	$ 228,879	$ 569,435	$1,236,166

9. DERIVATIVE FINANCIAL INSTRUMENTS

Until February 19, 2010, the University had a long-term interest rate swap agreement with a financial institution counterparty to manage the interest cost and risk associated with its Series 2008A and 2008B bonds. The purpose of this agreement was to swap the University's Series 2008A/B variable rate demand bonds having a balance of $151,725,000 as of May 31, 2010, for a fixed rate of 4.91% through February 1, 2032. The value of the interest rate swap represented the estimated cost to terminate at the reporting date, taking into account current and projected interest rates. This interest rate swap was terminated effective February 19, 2010, resulting in a realized loss of $17,623,000 and an unrealized gain of $27,561,000, resulting in a net gain of $9,938,000 for the year ended May 31, 2010.

On June 11, 2010, the University entered into a new swap arrangement with a financial institution counterparty in order to swap the University's Series 2008A variable rate demand bonds having a balance of $75,860,000 as of May 31, 2010 for a fixed rate of 2.476% through February 1, 2032, in exchange for monthly payments equal to 68% of three-month London Interbank Offered Rate (LIBOR). At May 31, 2011, the fair value of the University's interest rate swap liability was $1,068,000, which was measured using Level 2 valuation techniques.

10. EXPENSES BY NATURAL CLASSIFICATION

While the statements of activities present expenses by function, the University's expenses by natural classification are as follows:

	(in thousands of dollars)	
	2011	2010
Salaries & wages	$ 179,771	$ 169,756
Personnel benefits	60,029	55,765
Student wages & fellowships	19,491	17,999
Operating expenses	147,667	136,990
Depreciation	30,950	29,847
Interest on indebtedness	8,591	11,480
Total expenses	$ 446,499	$ 421,837

11. RETIREMENT PLAN

The University provides a defined contribution retirement income plan and a voluntary tax deferred annuity program for faculty and staff that are administered by outside sources. The defined contribution plan is not a matching plan. 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, 2011 and 2010 were $17,186,000 and $16,079,000, respectively.

12. POSTRETIREMENT BENEFITS

The University provides medical and life insurance benefits for eligible retired faculty and staff. Employees are eligible for such benefits if they retire after attaining specified age and service requirements while employed by the University. Group medical benefits have no lifetime maximum, and the maximum benefit for life insurance is $20,000.

Through May 31, 2002, full-time faculty and staff became eligible for these benefits upon reaching age fifty-five and having twenty years of full-time service at retirement. Effective June 1, 2002, employees with twenty years of continuous, full-time service at the University as of May 31, 2007, continue under the postretirement medical and life insurance programs in effect before June 1, 2002. Employees not meeting the above eligibility requirements may still participate in the postretirement medical program upon reaching age fifty-five and having ten years of full-time service at retirement. These employees will not receive 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 fifty-five and having ten years of full-time service at retirement. Effective June 1, 2002, upon death of a retiree, the surviving spouse (current spouse upon retirement) has the same option of continuation in the postretirement medical program. These surviving spouses will not receive postretirement life insurance benefits and will not be reimbursed for Medicare Part B premiums.

Medical cost inflation rates are assumed to be 8.0% for the first year decreasing by .5% per year to an ultimate of 5%. The inflation rates for retiree contributions are assumed to be the same as the medical cost inflation rates. The expected effect of provisions of the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 related to postretirement benefits is included in the accumulated postretirement benefit obligation.

The following tables set forth the required disclosures for postretirement benefits, as well as the components of net periodic benefit costs and weighted-average assumptions as of the measurement date, May 31:

	(in thousands of dollars)	
	2011	2010
Change in benefit obligation:		
Measurement date	5/31/2011	5/31/2010
Accumulated postretirement benefit obligation (APBO) at beginning of year	$ 45,710	$ 33,093
Service cost	1,463	943
Interest cost	2,821	2,472
Plan participants' contributions	1,402	1,347
Actuarial loss	3,627	10,363
Retiree drug subsidy paid	162	197
Benefit payments	(3,024)	(2,705)
Accumulated postretirement benefit obligation (APBO) at end of year	$ 52,161	$ 45,710
Change in plan assets:		
Fair value of plan assets at beginning of year	$ --	$ --
Employer contributions	1,622	1,358
Plan participants' contributions	1,402	1,347
Benefit payments	(3,024)	(2,705)
Fair value of plan assets at end of year	$ --	$ --
Funded (unfunded) status of plan	$ (52,161)	$ (45,710)

Amounts recognized as changes in unrestricted net assets arising from postretirement benefits plan but not yet included in periodic benefit cost:

	(in thousands of dollars)	
	2011	2010
Transition obligation	$ 547	$ 821
Prior service cost	2,154	2,797
Net loss	18,047	15,051
Total	$ 20,748	$ 18,669

The University expects to amortize, from accumulated unrestricted net assets, $274,000 of transition obligation, $643,000 of prior service costs and $767,000 of net losses as components of net periodic benefit cost during the fiscal year ending May 31, 2012.

Weighted-average assumptions at measurement date:	5/31/2011	5/31/2010
Discount rate	5.80%	6.28%
Health care cost trend rate	8.00%	8.50%
Ultimate health care cost trend rate	5.00%	5.00%
Year ultimate trend rate reached	2017	2017

Plan contributions:

The University expects to contribute $1,601,000 to its postretirement benefit plan during the fiscal year ending May 31, 2012.

Projected cash flows:	Gross Benefit Payments Net of Employee Contributions (in thousands of dollars)	Gross Subsidy Receipts (in thousands of dollars)
2012 Fiscal year	$ 1,853	$ 253
2013 Fiscal year	2,014	283
2014 Fiscal year	2,153	316
2015 Fiscal year	2,321	358
2016 Fiscal year	2,457	407
2017-2021 Fiscal years	15,187	2,803

Components of net periodic postretirement benefit cost:	6/1/2010-5/31/2011 (in thousands of dollars)	6/1/2009-5/31/2010 (in thousands of dollars)
Measurement date	5/31/2010	5/31/2009
Service cost	$ 1,463	$ 943
Interest cost	2,821	2,472
Amortization of:		
Transition obligation	274	274
Prior service cost	643	643
Actuarial loss	631	87
Net periodic postretirement benefit cost	$ 5,832	$ 4,419
Other changes in plan assets & benefit obligation recognized:		
Net actuarial loss	$ 3,627	$ 10,363
Amortization of:		
Transition obligation	(274)	(274)
Prior service cost	(643)	(643)
Actuarial loss	(631)	(87)
Total loss recognized in net assets	$ 2,079	$ 9,359
Total loss recognized in net assets & net periodic benefit cost	$ 7,911	$ 13,778

Weighted-average assumptions for net periodic postretirement benefit cost:

Measurement date	5/31/2010	5/31/2009
Discount rate	6.28%	7.63%
Health care cost trend rate	8.50%	9.00%
Ultimate health care cost trend rate	5.00%	5.00%
Year ultimate trend rate reached	2017	2017
Average future working lifetime (years)	16.6	16.8

Other Information:	*(in thousands of dollars)* 6/1/2010-5/31/2011	6/1/2009-5/31/2010
1% increase in trend rates		
Effect on service + interest cost	$ 613	$ 419
Effect on APBO	5,814	5,057
1% decrease in trend rates		
Effect on service + interest cost	$ (476)	$ (332)
Effect on APBO	(4,622)	(4,059)

13. TAX STATUS & ACCOUNTING FOR UNCERTAINTY IN INCOME TAXES

The 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.

Tax positions taken related to the University's tax exempt status, unrelated business activities taxable income and deductibility of expenses and other miscellaneous tax positions have been reviewed, and management is of the opinion that material positions taken by the University would more likely than not be sustained by examination. Accordingly, the University has not recorded an income tax liability for uncertain tax benefits. As of May 31, 2011, the University's tax years 2006 to 2011 remain subject to examination.

14. RELATED PARTY TRANSACTIONS

Members of the University's Board of Regents and senior administration may, from time to time, be associated, either directly or indirectly, with entities doing business with the University. Accordingly, the University has Board of Regents, faculty and staff written conflict of interest policies that require any such association, including those of immediate family members, to be disclosed on an annual basis and updated as appropriate during the year. If such associations exist, measures are taken to mitigate any actual or perceived conflict. For the years ended May 31, 2011 and 2010, there were no related party transactions that were considered to be significant or that were not effectively mitigated.

15. COMMITMENTS & CONTINGENCIES

Capital Expenditures & Other Commitments

The University is contractually obligated for amounts aggregating a maximum of approximately $16,333,000 and $3,927,000 at May 31, 2011 and 2010, respectively. Such obligations relate to major capital projects.

The University also is contractually obligated under various agreements ensuring access to, or advantageous pricing of, goods and services used in the operations of the University.

Leases

The University incurred $1,349,000 and $996,000 in operating lease expenses for facilities and equipment in the fiscal years ended May 31, 2011 and 2010, respectively. As of May 31, 2011, the University has lease commitments for future periods as follows *(in thousands of dollars)*:

	2012	2013	2014	2015	2016	2017 and Thereafter	Total
Equipment	$ 516	$ 390	$ 347	$ 340	$ 340	$ --	$ 1,933
Other	974	604	440	422	416	813	3,669
Total	$ 1,490	$ 994	$ 787	$ 762	$ 756	$ 813	$ 5,602

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 federal and state 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.

16. SUBSEQUENT EVENTS

The University has evaluated subsequent events through September 27, 2011, the date when financial statements were issued. The University did not identify any subsequent events to be disclosed.