



CASE WESTERN RESERVE
UNIVERSITY EST. 1826



CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2008

Case Western Reserve University
Consolidated Financial Statements for the Year Ending June 30, 2008

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Report of Independent Auditors

To the Board of Trustees
Case Western Reserve University:

In our opinion, the accompanying balance sheets and the related statements of activities and cash flows present fairly, in all material respects, the financial position of Case Western Reserve University (the "University") as of June 30, 2008, and the changes in net assets and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the University's 2007 financial statements, and in our report dated October 19, 2007, we expressed an unqualified opinion on those financial statements. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

October 17, 2008

CASE WESTERN RESERVE UNIVERSITY
Consolidated Balance Sheet
June 30, 2008 and 2007
(in thousands)

| | <u>June 30, 2008</u> | <u>June 30, 2007</u> |
|---------------------------------------------|----------------------|----------------------|
| Assets | | |
| Cash and temporary investments | \$ 53,090 | \$ 100,417 |
| Accounts and loans receivable, net | 105,555 | 125,292 |
| Securities pledged under lending agreements | 36,346 | 84,083 |
| Pledges receivable, net | 44,326 | 52,928 |
| Prepaid expenses and other assets | 16,963 | 12,368 |
| Prepaid pension asset | 11,418 | - |
| Investments | 1,607,277 | 1,599,556 |
| Property, plant, equipment and books, net | 801,064 | 822,941 |
| Funds held in trust by others | 300,719 | 326,033 |
| Total assets | <u>\$ 2,976,758</u> | <u>\$ 3,123,618</u> |
| Liabilities | | |
| Accounts payable and accrued expenses | \$ 69,619 | \$ 78,378 |
| Deferred income and other liabilities | 38,604 | 27,842 |
| Payable under securities lending agreements | 37,655 | 86,892 |
| Annuities payable | 43,796 | 52,616 |
| Refundable advances | 6,057 | 12,394 |
| Accrued pension liability | - | 1,133 |
| Notes and bonds payable | 590,998 | 589,357 |
| Refundable federal student loans | 16,153 | 17,001 |
| Total liabilities | <u>802,882</u> | <u>865,613</u> |
| Net Assets | | |
| Unrestricted | 1,301,680 | 1,376,105 |
| Temporarily restricted | 23,509 | 27,297 |
| Permanently restricted | 848,687 | 854,603 |
| Total net assets | <u>2,173,876</u> | <u>2,258,005</u> |
| Total liabilities and net assets | <u>\$ 2,976,758</u> | <u>\$ 3,123,618</u> |

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

CASE WESTERN RESERVE UNIVERSITY

Consolidated Statement of Activities

For the Year Ended June 30, 2008

with summarized financial information for the year ended June 30, 2007

(in thousands)

| | <u>Unrestricted</u> | <u>Temporarily Restricted</u> | <u>Permanently Restricted</u> | <u>Year Ended June 30, 2008</u> | <u>Year Ended June 30, 2007</u> |
|-------------------------------------------------------------------------|---------------------|-----------------------------------|-----------------------------------|-------------------------------------|-------------------------------------|
| Operating revenues | | | | | |
| Student tuition and fees | \$ 267,554 | | | \$ 267,554 | \$ 247,071 |
| Less: Student aid | (105,584) | | | (105,584) | (96,226) |
| | <u>161,970</u> | | | <u>161,970</u> | <u>150,845</u> |
| Endowment income | 77,498 | | | 77,498 | 75,605 |
| Grants and contracts | 250,620 | | | 250,620 | 243,860 |
| CCLCM grants and contracts | 90,990 | | | 90,990 | 90,680 |
| Gifts and pledges | 5,775 | \$ 16,168 | \$ 25,581 | 47,524 | 36,587 |
| State of Ohio appropriation | 3,896 | | | 3,896 | 3,911 |
| Facilities and administrative cost recovery | 64,948 | | | 64,948 | 66,904 |
| Organized activities | 10,654 | | | 10,654 | 10,759 |
| Other sources | 45,690 | | 771 | 46,461 | 44,880 |
| Auxiliary services | 42,964 | | | 42,964 | 39,766 |
| Net assets released from restrictions | 22,189 | (19,956) | (2,233) | - | - |
| Total operating revenues | <u>777,194</u> | <u>(3,788)</u> | <u>24,119</u> | <u>797,525</u> | <u>763,797</u> |
| Operating expenses | | | | | |
| Instructional | 236,178 | | | 236,178 | 251,984 |
| Sponsored research and training | 244,279 | | | 244,279 | 238,703 |
| Other sponsored projects | 25,591 | | | 25,591 | 27,101 |
| CCLCM research and training | 90,990 | | | 90,990 | 90,680 |
| Libraries | 20,590 | | | 20,590 | 21,134 |
| Student services | 18,775 | | | 18,775 | 17,206 |
| University services | 79,069 | | | 79,069 | 89,528 |
| Auxiliary enterprises - students | 48,882 | | | 48,882 | 43,052 |
| Auxiliary enterprises - others | 10,452 | | | 10,452 | 12,262 |
| Total operating expenses | <u>774,806</u> | <u>-</u> | <u>-</u> | <u>774,806</u> | <u>791,650</u> |
| Net operating (deficit) revenues | <u>2,388</u> | <u>(3,788)</u> | <u>24,119</u> | <u>22,719</u> | <u>(27,853)</u> |
| Non-operating revenues and expenses | | | | | |
| Investment and other income | 50,896 | | (25,140) | 25,756 | 109,826 |
| Net (depreciation) appreciation in the fair market value of investments | (130,397) | | (7,951) | (138,348) | 130,929 |
| Actuarial adjustment to annuity payable | | | 3,056 | 3,056 | (4,355) |
| (Loss) gain on disposal of plant assets | (9,863) | | | (9,863) | 2,166 |
| Pension plan changes other than periodic benefit costs | 12,551 | | | 12,551 | - |
| Non-operating revenues, net | <u>(76,813)</u> | <u>-</u> | <u>(30,035)</u> | <u>(106,848)</u> | <u>238,566</u> |
| Increase in net assets before effect of accounting changes | <u>(74,425)</u> | <u>(3,788)</u> | <u>(5,916)</u> | <u>(84,129)</u> | <u>210,713</u> |
| Cumulative effect of change in accounting principle | | | | - | <u>(2,497)</u> |
| Increase in net assets | <u>(74,425)</u> | <u>(3,788)</u> | <u>(5,916)</u> | <u>(84,129)</u> | <u>208,216</u> |
| Beginning net assets | 1,376,105 | 27,297 | 854,603 | 2,258,005 | 2,049,789 |
| Ending net assets | <u>\$ 1,301,680</u> | <u>\$ 23,509</u> | <u>\$ 848,687</u> | <u>\$ 2,173,876</u> | <u>\$ 2,258,005</u> |

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

CASE WESTERN RESERVE UNIVERSITY
Consolidated Statement of Cash Flows
For the Years Ended June 30, 2008 and 2007
(in thousands)

| | Year Ended June 30, 2008 | Year Ended June 30, 2007 |
|----------------------------------------------------------------------------------------------------|-----------------------------|-----------------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Change in net assets | \$ (84,129) | \$ 208,216 |
| <i>Adjustments to reconcile change in net assets to net cash provided by operating activities:</i> | | |
| Cumulative effect - change in accounting principle | - | 2,497 |
| Depreciation | 60,402 | 57,477 |
| Amortization of bond issuance costs | 44 | 41 |
| Change in asset retirement obligation related to sale | - | 3,239 |
| Loss on debt refinancing | 719 | 3,015 |
| Net unrealized depreciation (appreciation) in the fair market value of investments | 138,348 | (130,929) |
| Realized gains on investments | (28,592) | (71,661) |
| Increase to annuities payable resulting from actuarial adjustments | 1,469 | 4,355 |
| Gifts of property and equipment | (625) | (43) |
| Receipt of contributed securities | (6,371) | (5,198) |
| Loss (gain) on disposal of plant assets | 9,863 | (2,166) |
| Contributions restricted for long-term investment | (23,498) | (10,898) |
| Decrease in accounts and notes receivable, net | 20,515 | 7,955 |
| Decrease in pledges receivable, net | 8,602 | 14,344 |
| (Increase) decrease in prepaid expenses and other assets | (3,406) | 4,238 |
| (Increase) decrease in prepaid pension assets | (11,418) | 2,028 |
| Decrease (increase) in funds held in trust by others | 25,314 | (30,629) |
| (Decrease) increase in accounts payable and accrued expenses | (6,734) | 21,289 |
| Increase (decrease) in deferred income and other liabilities | 10,762 | (1,706) |
| (Decrease) increase in refundable advances | (6,337) | 3,971 |
| Decrease in accrued pension liability | (1,133) | (9,364) |
| Net cash provided by operating activities | <u>103,795</u> | <u>70,071</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Student loans collected | 6,405 | 6,541 |
| Student loans issued | (7,183) | (9,559) |
| Proceeds from the sale of investments | 1,984,801 | 1,759,571 |
| Purchase of investments | (2,095,907) | (1,755,709) |
| Proceeds from the sale of buildings and land | 1,771 | 3,427 |
| Purchase of property, plant, equipment and books | (51,559) | (56,088) |
| Net cash used for investing activities | <u>(161,672)</u> | <u>(51,817)</u> |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Decrease in federal advances for student loans | (848) | (270) |
| Decrease in securities pledged under lending agreements | 47,737 | 7,729 |
| Decrease in payables under securities lending agreements | (49,237) | (6,982) |
| Contributions restricted for long-term investment | 23,498 | 10,898 |
| Proceeds from bond issues and long-term debt | 199,559 | 115,737 |
| Payment of bond issuance costs | (1,233) | (1,530) |
| Repayment of debt | (198,637) | (151,902) |
| Payments on annuities payable | (11,835) | (4,100) |
| Increase to annuities payable resulting from new gifts | 1,546 | 676 |
| Net cash provided by (used for) financing activities | <u>10,550</u> | <u>(29,744)</u> |
| Net decrease in cash and cash equivalents | (47,327) | (11,490) |
| Cash and cash equivalents, beginning of year | 100,417 | 111,907 |
| Cash and cash equivalents, end of year | <u>\$ 53,090</u> | <u>\$ 100,417</u> |
| SUPPLEMENTAL SCHEDULE OF NON-CASH ACTIVITIES | | |
| Construction in progress payments included in accounts payable | \$ 5,817 | \$ 7,842 |

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

Part 2 – Summary of Significant Accounting Policies and Terms

This part explains the accounting practices the University uses in its consolidated financial statements.

Basis of Accounting Presentation

The consolidated financial statements use the accrual basis of accounting. These statements include the accounts of the University, Triangle Residential LP and Triangle Residential LLC.

Triangle Residential LP is a limited partnership formed in 2005 that owns and operates two apartment buildings, a parking garage and a commercial structure located in the Ford-Euclid-Mayfield Road area. The University is the sole limited partner. The general partner is Triangle Residential LLC, a wholly owned subsidiary of the University, also formed in 2005. The University, through Triangle Residential LP, plans to operate the properties pending finalization of plans to develop an arts, entertainment and residential complex in the area.

Net Asset Categories

The consolidated financial statements present information about the University's financial position and activities using three categories of net assets:

- **Unrestricted net assets** have no donor-imposed restrictions. They are available for any purpose consistent with the University's mission.
- **Temporarily restricted net assets** are subject to specific donor-imposed restrictions that must be met by University actions or through the passage of time.
- **Permanently restricted net assets** are subject to donor-imposed restrictions that the University must honor in perpetuity. Usually, donors allow part or all of the income to be used for a designated purpose.

Cash and Temporary Investments

Investments with a maturity of three months or less when purchased are reported as temporary investments (i.e., cash equivalents) unless they are part of long-term investment pools.

Investments

Investments are stated at fair value. The fair value of all debt and equity securities with readily determinable fair value are based on quotations obtained from national securities exchanges. The alternative investments, which are not readily marketable, are carried at estimated fair values as provided by the investment managers. The University reviews and evaluates the values provided by the investment managers and agrees with the valuation methods and assumptions used in determining the fair value of the alternative investments. Those estimated fair values may differ significantly from the values that would have been used had a ready market for these securities existed. Realized gains and losses on investments are included in investment income. Average cost is generally used to determine gains or losses on securities sold. Unrealized changes in the fair market value of investments are shown as net unrealized appreciation or depreciation.

| | |
|------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Contributions | Contributions (including unconditional pledges) are recognized as either temporarily restricted or permanently restricted net assets when donors' commitments are received. Conditional pledges become revenue when the conditions are substantially met. Gifts whose restrictions are met in the same fiscal year in which they are received are reported with unrestricted contribution revenues. |
| Grants and Contracts (Government and Private) | Revenues from government and private grants and contracts are recognized as earned in accordance with the terms of the contract. Any government revenue received before it is expended is recorded as a refundable advance. Expenses incurred for government grants before revenue is received are recorded as receivables. |
| Collections | The University's collections of historically significant artifacts, scientific specimens, and art objects are held for education, research, scientific inquiry, and public exhibition. Therefore, their value is not reflected in the University's financial statements. |
| Funds Held in Trust by Others | Funds held in trust by others are assets held and administered by outside trustees from which the University derives income or residual interest. Funds held in trust by others are reported at their fair value as of June 30, 2008, which approximates the present value of the future income flows from these funds. |
| Conditional Asset Retirement Obligations | The University accounts for asset retirement obligations in accordance with Statement of Financial Accounting Standard No. 143, "Accounting for Asset Retirement Obligations," and FAS Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations." The University accrues for asset retirement obligations in the period in which they are incurred if sufficient information is available to reasonably estimate the fair value of the obligation. Over time, the liability is accreted to its settlement value. Upon settlement of the liability, the University will recognize a gain or loss for any difference between the settlement amount and liability recorded. |
| Allocation of Certain Expenses | The statement of activities presents expenses by function. Some expenses – such as depreciation, amortization, and expenses related to the operation of the physical plant – are allocated by square footage. Interest expense is allocated to the functions that derive the greatest benefit from the facilities financed. |
| Use of Estimates | Financial statements using accounting principles generally accepted in the United States of America rely on estimates. At June 30, management makes certain estimates and assumptions, which affect assets and liabilities, disclosures of contingent assets and liabilities, and reported revenues and expenses during the period. Actual results may differ from these estimates. |

**Comparative
Information**

The statement of activities includes prior year summarized comparative information in total, but not by net asset category. Such information does not include enough detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the University's financial statements for the year ending June 30, 2007, from which it was derived.

Certain reclassifications have been made to the summarized prior year financial information for comparative purposes. Certain allocated expenses in 2007 have been reclassified consistent with an updated 2008 space survey.

During fiscal 2008, the University reviewed certain activities related to contributed securities and determined that \$5,198 should have been treated as non-cash activity within the statement of cash flows at June 30, 2007. Additionally, the University corrected the misclassification of \$4,275 in operating cash flows of contributions restricted for long-term investment. The impact of these revisions was a decrease of \$923 in cash flows provided by operating activities, an increase of \$5,198 in cash flows used for investing activities, and a decrease in cash flows used for financing activities of \$4,275.

The University also reclassified changes in the asset retirement obligation related to the sale of a plant asset in the 2007 statement of cash flows. Cumulative effect - change in accounting principle was reduced by \$3,239 while the change in asset retirement obligation related to sale increased by \$3,239. The impact of this change had no effect on cash flows provided by operating activities.

**Income
Taxes**

The University is generally exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code. Accordingly, no provision for income taxes is made in the financial statements. Effective July 1, 2007, the University adopted FASB Interpretation No. 48 (FIN 48), "Accounting for Uncertainty in Income Taxes - An Interpretation of SFAS No. 109, Accounting for Income Taxes." FIN 48 addresses the accounting, classification, measurement and disclosure of uncertainty in income tax recognition. The adoption did not have a material effect on the University's consolidated financial statements.

Part 3 – Notes

These notes clarify and amplify data in the financial statements. Unless otherwise indicated, all dollar values are listed in thousands as of June 30.

NOTE A Accounts and Loans Receivable

Accounts and loans receivable are as follows:

| | 2008 | 2007 |
|-----------------------------------|-------------------|-------------------|
| Accounts receivable, net: | | |
| Grants, contracts and others | \$ 54,817 | \$ 74,838 |
| Students | 5,557 | 6,562 |
| Student loans, net | 45,181 | 43,892 |
| | <u>\$ 105,555</u> | <u>\$ 125,292</u> |
| Allowances for doubtful accounts: | | |
| Accounts receivable | \$ 14,971 | \$ 19,907 |
| Loans receivable | \$ 2,835 | \$ 2,290 |

NOTE B Pledges Receivable

Unconditional pledges are expected to be realized in the following periods:

| | 2008 | 2007 |
|---------------------------------|------------------|------------------|
| In one year or less | \$ 6,173 | \$ 6,993 |
| Between one year and five years | 40,316 | 38,308 |
| More than five years | 3,701 | 14,593 |
| | 50,190 | 59,894 |
| Less: Discount | (2,789) | (3,633) |
| Less: Allowance | (3,075) | (3,333) |
| | <u>\$ 44,326</u> | <u>\$ 52,928</u> |

Pledges receivable have been made for the following purposes:

| | 2008 | 2007 |
|-----------------------------------------------------------------------|------------------|------------------|
| Department programs and activities | \$ 17,482 | \$ 15,246 |
| Endowments for scholarships and department programs and activities | 14,349 | 19,699 |
| Building construction | 12,495 | 17,983 |
| | <u>\$ 44,326</u> | <u>\$ 52,928</u> |

The University had conditional pledge commitments totaling \$32,986 (2008) and \$31,071 (2007).

Uncollectible pledges totaling \$5,953 (2008) were written off against the allowance for uncollectible pledges. Uncollectible pledges totaling \$11,904 (2007) were written off against the allowance for uncollectible pledges and University Services expense.

NOTE C
Investments

Investments (except funds held in trust by others) are as follows:

| | 2008 | |
|--------------------------------|--------------|--------------|
| | Fair Market | |
| | Value | Cost |
| Short-term investments | \$ 140,335 | \$ 140,335 |
| Domestic stocks | 50,032 | 52,758 |
| International securities | 295,967 | 273,207 |
| Bonds | | |
| • U.S. Government | 49,239 | 54,249 |
| • Corporate | 82,625 | 83,988 |
| Mutual funds | 137,600 | 122,456 |
| Limited partnerships and other | | |
| • Venture capital | 55,691 | 47,350 |
| • Private equity | 261,157 | 208,921 |
| • Hedge funds | 380,421 | 306,027 |
| • Other | 43,402 | 42,549 |
| Equity real estate | 110,808 | 100,807 |
| Total | \$ 1,607,277 | \$ 1,432,647 |
| | | |
| | 2007 | |
| | Fair Market | |
| | Value | Cost |
| Short-term investments | \$ 110,762 | \$ 110,762 |
| Domestic stocks | 124,072 | 96,322 |
| International securities | 281,836 | 183,711 |
| Bonds | | |
| • U.S. Government | 254 | 253 |
| • Corporate | 133,406 | 134,826 |
| Mutual funds | 100,168 | 89,714 |
| Limited partnerships and other | | |
| • Venture capital | 42,878 | 34,673 |
| • Private equity | 242,529 | 188,531 |
| • Hedge funds | 386,597 | 300,312 |
| • Other | 101,440 | 76,568 |
| Equity real estate | 75,614 | 70,905 |
| Total | \$ 1,599,556 | \$ 1,286,577 |

Included in the University's investments are **unexpended bond proceeds**. These funds are temporarily held by trustees under the bond indenture for future capital expenditures. The proceeds are invested in cash, U.S. government and corporate bonds and mutual funds. The fair value of these assets totaled \$52,638 (2008) and \$65,243 (2007).

The University invested a portion of its **operating cash funds** in variable rate demand bonds that are included in investments. The University chose

NOTE C
Investments
(continued)

to invest in these notes, which are remarketed every seven days, in order to maximize its return. The fair value of these assets totaled \$22,215 (2008).

The University's **spending policy** determines the amount of endowment income to be used as operating revenue and distributed for spending during the year. Distributions in excess or deficit of amounts actually earned are transferred to or from the endowment pool, honoring any donor restrictions. The fiscal 2008 endowment and similar funds distribution of \$2.13 per unit totaled \$65,126, of which \$50,050 was accumulated realized gains. For fiscal 2007, the distribution of \$2.03 per unit totaled \$61,170, of which \$48,751 was accumulated realized gains.

Certain endowment and similar fund assets are pooled for efficient investment purposes. The unit market value for each pool is used to account for **pooled transactions**. The unit market values are \$45.35 (2008) and \$47.70 (2007). Total **investment return** for the pooled and unpooled endowment was 0.47% (2008) and 19.75% (2007).

Investments in stocks, bonds, mutual funds, and other investments are exposed to a variety of uncertainties, including interest rate, market fluctuation, and credit risks. Due to the **level of risk** associated with certain investments, the value of these investments could change. Such changes could materially affect the amounts reported in the financial statements.

Investment strategies employed by outside managers incorporate the use of financial instruments with off-balance sheet risk. These financial instruments include international investment funds with underlying equity interests as well as forward and futures contracts that are subject to foreign currency translation gains and losses. Management does not anticipate that losses, if any, resulting from its off-balance sheet market or credit risks would materially affect the financial position of the University; however, there can be no assurances.

The University is obligated under certain limited partnerships and similar agreements to provide future funding for further investment. The University had **unfunded commitments** of approximately \$233,334 (2008) and \$201,278 (2007) that are likely to be called in the future.

The University has a **securities lending** agency agreement for the purpose of lending securities held or beneficially owned by the University. Under this agreement, the University's agent receives collateral in the form of cash or U.S. government securities in exchange for loaning securities to approved borrowers. The agent invests these funds on behalf of the University until the securities are returned. The amount of collateral required for securities traded principally in the United States is equal to 102% of the market value of the securities borrowed. For equities traded principally outside the United States, the amount of collateral required is 105%. For fixed income securities traded principally outside the United States, the amount of collateral required is 102%. The fair value of securities on loan is \$36,346 (2008) and \$84,083 (2007). The fair value of collateral received is \$37,655 (2008) and \$86,892 (2007). Cash collateral is reflected in the cash and temporary investments balance.

**NOTE D
 Property,
 Plant,
 Equipment,
 and Books**

Property, plant, equipment, and library books are stated at cost, less accumulated depreciation. Depreciation is computed on the straight-line method over the estimated useful life of 28 years for buildings, 5 to 12 years for equipment, and 10 years for books.

Components of property, plant, equipment, and books are as follows:

| | 2008 | 2007 |
|------------------------------------|-------------------|-------------------|
| Land and land improvements | \$ 39,263 | \$ 38,920 |
| Building and building improvements | 1,030,473 | 982,817 |
| Equipment and software | 234,674 | 213,340 |
| Library books | 31,687 | 30,688 |
| Construction-in-progress | 35,120 | 70,479 |
| | <u>1,371,217</u> | <u>1,336,244</u> |
| Less: accumulated depreciation | <u>(570,153)</u> | <u>(513,303)</u> |
| | <u>\$ 801,064</u> | <u>\$ 822,941</u> |

The above assets include \$453,092 leased from the Ohio Higher Education Facility Commission (OHEFC). The University may purchase each of the leased assets for a nominal amount at the end of the lease period. Therefore, these assets have been capitalized and are included in the above listing. Also included in the University's financial statements is the obligation for related bonds issued by the OHEFC.

NOTE E
Bonds and
Notes
Payable

Bonds and notes payable are as follows:

| | Interest | Maturity | 2008 | 2007 |
|----------------------------------------------------------------------|---------------|-----------|------------------|------------------|
| Ohio Higher Education Facilities Commission revenue bonds and notes: | | | | |
| Series 1988 | 7.85 - 7.90% | 2009-2013 | \$ 25,051 | \$ 23,188 |
| Series 1990 | 6.50 - 7.15% | 2007-2020 | 11,830 | 11,968 |
| Series 1994 | 6.00 - 6.25% | 2014-2018 | 20,000 | 20,000 |
| Series 1997 | 4.90 - 6.25% | 2009-2014 | 8,920 | 8,920 |
| Series 2001 | Variable | 2007-2022 | 14,790 | 16,200 |
| Series 2002 | Variable | 2023-2031 | 64,875 | 64,875 |
| Series 2004 | 3.625 - 5.00% | 2016-2034 | 78,001 | 78,158 |
| Series 2004 | Variable | 2008-2044 | - | 177,826 |
| Series 2006 | 3.75 - 5.25% | 2012-2044 | 90,569 | 90,917 |
| Series 2008 | Variable | 2030-2044 | 60,000 | - |
| Series 2008 | Variable | 2030-2044 | 67,500 | - |
| Series 2008 | 4.00 - 5.00% | 2014-2033 | 52,764 | - |
| United States government housing bonds: | | | | |
| Series 1966 | 3.00 - 3.50% | 2007-2016 | 990 | 1,135 |
| Series 1971 | 3.00% | 2006-2016 | 1,015 | 1,125 |
| Ohio Higher Education Facilities Commission commercial paper | -Various- | -Various- | 63,000 | 63,000 |
| Ohio Higher Education Facilities Commission capital lease 2006 | 6.75% | 2008-2018 | 710 | 710 |
| Ohio Higher Education Facilities Commission capital lease 2006 | 4.123% | 2008-2018 | 12,880 | 12,880 |
| Compass Group USA note | -n/a- | 2007-2014 | 938 | 1,088 |
| Department of Housing and Urban Development mortgages: | | | | |
| HUD - Part A | 4.96% | 2007-2041 | 12,779 | 12,932 |
| HUD - Part B | 5.33% | 2007-2041 | 4,386 | 4,435 |
| | | | <u>\$590,998</u> | <u>\$589,357</u> |

The housing bonds are collateralized by securities and pledges of net revenues from the University's student housing and dining facilities.

The Ohio Higher Education Facilities Commission (OHEFC) authorized a tax-exempt commercial paper program in February 2000 to provide construction funds for several approved capital projects and to refinance earlier projects. The program authorizes the University to issue up to \$63,000 for as long as 30 years. The amount outstanding under this program as of June 30 is \$63,000, with maturities not exceeding 270 days from the issuance date. Interest rates for this program averaged 2.67% (2008) and 3.59% (2007).

In November 2004, the University opened a line of credit with a financial institution to finance working capital. The line was increased to \$100,000 in

NOTE E
Bonds and
Notes
Payable
(continued)

November 2005, and reduced to \$60,000 in December 2007. There were no amounts outstanding at June 30.

In January 2006, the University borrowed \$17,637 from the Department of Housing and Urban Development (HUD). The proceeds from this loan were used to refund the portion of the commercial note used to acquire the Triangle properties. The balance due for Part A of the HUD loan was \$12,779 (2008) and \$12,932 (2007). The balance due for Part B of the HUD loan was \$4,386 (2008) and \$4,435 (2007).

In December 2006, the OHEFC series 2006 bonds were issued to refinance certain previously issued and outstanding OHEFC bonds. The issues refinanced and amounts defeased are as follows:

| | |
|----------------------|-----------|
| OHEFC series 1997A — | \$ 7,245 |
| OHEFC series 1997C — | \$ 15,245 |
| OHEFC series 2002B — | \$ 35,125 |
| OHEFC series 2004A — | \$ 28,260 |

The unamortized balance of deferred financing fees is included in prepaid expenses and other assets. The balance was \$1,490 (2008) and \$1,530 (2007).

In May 2008, the OHEFC series 2008 bonds were issued to refinance the OHEFC series 2004B bonds. The amount refinanced was \$177,826. The variable portion of the debt is supported by two lines of credit with financial institutions. Deferred financing fees of \$1,233 were paid and are included in prepaid expenses and other assets.

Principal payment requirements for bonds, notes, and capital lease obligations for the next five years, excluding commercial paper, are approximately as follows:

| | |
|--------|----------|
| 2009 — | \$ 2,173 |
| 2010 — | \$ 4,446 |
| 2011 — | \$ 4,571 |
| 2012 — | \$ 4,960 |
| 2013 — | \$ 6,374 |

Interest payments for fiscal year 2008, including payments for variable rate debt, were \$24,393. Interest payments under interest rate swap agreements during fiscal 2008 totaled \$1,031. See Note J.

Certain borrowing agreements require the University to maintain reserves as additional collateral against its borrowings. These agreements also require that the University comply with certain covenants. The University is in compliance with these provisions.

NOTE F
Fair Value of
Investments

The University's financial instruments consist principally of cash, temporary investments, accounts and pledges receivable, loans receivable, and long-term investments, as well as obligations under bonds and notes payable. Cash and temporary investments, pledges receivable, investments and other assets are recorded at approximate fair value.

Loans receivable are amounts due from students primarily under federally sponsored programs. Since notes receivable under federal student loan programs are not saleable and can be assigned only to the U.S. government or its designee, it is not practical to determine their fair value.

The fair value of the University's bonds and notes payable is approximately \$571,925 (2008) and \$572,037 (2007). These values were estimated utilizing the discounted future cash outflows at rates for similar debt.

NOTE G
Retirement
Plans

In September 2006, the FASB issued Statement of Financial Accounting Standard No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an Amendment of FASB Statements No. 87, 88, 106, and 132(R)" (SFAS 158). SFAS 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its balance sheet in the year in which the change occurs, with an offsetting impact to unrestricted net assets. The University adopted the provisions of SFAS 158 effective June 30, 2007.

The University has both defined benefit and defined contribution pension plans for its employees. In accordance with ERISA requirements, the University has established a trust to hold plan assets for its defined benefit plan.

The **funded status** of the University's **defined benefit plan** is as follows:

| | 2008 | 2007 |
|--------------------------------------|------------------|-------------------|
| Benefit obligation at June 30 | \$ 88,378 | \$ 89,846 |
| Fair value of plan assets at June 30 | 99,796 | 88,713 |
| Funded status at June 30 | <u>\$ 11,418</u> | <u>\$ (1,133)</u> |
| Accumulated benefit obligation | \$ 87,924 | \$ 88,976 |

Benefit plan costs for the defined benefit plan are as follows:

| | 2008 | 2007 |
|---------------------------|----------|----------|
| Net periodic benefit cost | \$ 1,914 | \$ 3,108 |
| Employer contributions | 7,098 | 12,941 |
| Benefits paid | 3,056 | 3,276 |

NOTE G
Retirement
Plans
(continued)

Estimated benefits expected to be paid under the defined benefit plan for the next five years are as follows:

| | |
|--------|----------|
| 2009 – | \$ 3,525 |
| 2010 – | \$ 3,696 |
| 2011 – | \$ 3,712 |
| 2012 – | \$ 3,765 |
| 2013 – | \$ 4,782 |

Amounts expected to be paid between 2014 and 2018 total \$30,271. The University's **estimated employer contribution** for the defined benefit plan in fiscal 2009 is \$0. This amount may change based on the results of the July 1, 2008 actuarial valuation.

Weighted-average assumptions used to determine the **benefit obligation** and **benefit plan costs** are as follows:

| | 2008 | 2007 |
|--------------------------------|---------|---------|
| Benefit obligation: | | |
| Discount rate | 7.00% | 6.50% |
| Rate of compensation increase | 4.50% | 4.50% |
| Measurement date | 6/30/08 | 6/30/07 |
| Census date | 7/1/07 | 7/1/06 |
| Net periodic benefit cost: | | |
| Discount rate | 6.50% | 6.50% |
| Expected return on plan assets | 9.00% | 9.00% |
| Rate of compensation increase | 4.50% | 4.50% |

The **expected long-term rate of return** for the defined benefit plan was estimated using market benchmarks for equities and bonds applied to the plan's target asset allocation. The expected return on equities was computed utilizing a valuation framework, which projected future returns based on current equity valuations rather than historical returns. Management estimated the rate by which the plan assets would outperform the market in the future based on historical experience adjusted for changes in asset allocation and expectations for overall lower future returns on equities compared to past periods.

The **investment objective** for the defined benefit plan is to maximize total return with tolerance for slightly above average risk, in order to meet the obligations that the University has to its plan beneficiaries. To accomplish this objective, the University has established a broadly-diversified asset allocation strategy that includes absolute return strategies (50%), equity investments (30%), real estate (10%), and inflation-indexed bonds and cash (10%). The weightings of the investments relative to each other in the total portfolio fluctuate as market conditions vary; they are adjusted regularly to remain within acceptable ranges.

NOTE G
Retirement
Plans
(continued)

The **weighted-average asset allocation** for the defined benefit plan is as follows:

| | 2008 | 2007 |
|-------------------------|----------------|----------------|
| Equity securities | 64.00% | 61.00% |
| Fixed income securities | 24.00% | 15.00% |
| Real estate | 10.00% | 18.00% |
| Other | 2.00% | 6.00% |
| Total | <u>100.00%</u> | <u>100.00%</u> |

The amounts recognized in the University's **balance sheet** and in **unrestricted net assets** related to the defined benefit plan are as follows:

| | 2008 | 2007 |
|--------------------------------------------------|---------------|-----------------|
| Balance sheet: | | |
| Net balance sheet asset (liability) | \$ 11,418 | \$ (1,133) |
| Prepaid benefit cost recognized in balance sheet | 12,029 | 6,845 |
| Additional liability recognized | <u>\$ 611</u> | <u>\$ 7,978</u> |
| Unrestricted net assets: | | |
| Prior service costs | 1,356 | 1,693 |
| Actuarial (gains) losses | (745) | 6,285 |
| | <u>\$ 611</u> | <u>\$ 7,978</u> |

The estimated **amortization of prior year service costs** expected in fiscal 2009 totals \$336.

Components of the **net periodic benefit cost and other changes in plan assets** that are recognized in the statement of activities for fiscal year 2008 are as follows:

| | |
|--------------------------------------------------|--------------------|
| Change in actuarial gains | \$ (7,030) |
| Amortization of prior service cost | (337) |
| Total gain recognized in unrestricted net assets | <u>\$ (7,367)</u> |
| Net periodic benefit cost | 1,914 |
| Employer contributions | (7,098) |
| Total gain recognized in statement of activities | <u>\$ (12,551)</u> |

Benefit plan costs for the defined contribution plan are \$17,051 (2008) and \$18,897 (2007).

**NOTE H
Commitments
and
Contingencies**

In its normal operations, the University is subject to various claims and lawsuits. In management's opinion, the resolution of these contingencies will not have a significant adverse effect on the University's financial position, operations, or cash flows.

In April 2006, the Boards of University Hospitals Health System and the University approved a new affiliation agreement between the School of Medicine and University Hospitals of Cleveland (UHC). This agreement significantly strengthened the historical relationship between the entities through the creation of the Case Medical Center, a virtual entity that encompasses certain teaching, research and clinical activities of the School of Medicine and UHC.

In May 2002, the University entered into an agreement with the Cleveland Clinic Foundation (CCF) to form a new medical education and research program, the Cleveland Clinic Lerner College of Medicine (CCLCM). Beginning in 2004, research grants from the National Institutes of Health to support work by CCF-based investigators were awarded to and administered through the University by CCLCM, which operates as an academic unit of the School of Medicine. Expenditures for research conducted under this joint agreement totaled \$90,990 (2008) and \$90,680 (2007).

The University is self-insured for workers compensation and employee and student medical coverage. Property is commercially insured with an aggregate deductible of \$700. The University also carries general liability insurance with a deductible of \$100 per occurrence. The University believes its reserves for self-insured risks and the deductible portion of insured risks are sufficient.

The expected cost to complete construction in progress is approximately \$4,057.

**NOTE I
Related Party
Transaction
(Utilities)**

In 1998, the University entered into a thirty-year agreement with the Medical Center Company (a cooperative utility company formed by and serving institutions in the University Circle area) to purchase chilled water and other utilities for several University buildings. The amounts purchased were \$19,414 (2008) and \$16,248 (2007). No obligation associated with this agreement is recorded in the accompanying financial statements.

**NOTE J
 Derivatives
 and Other
 Financial
 Instruments**

The University uses floating-to-fixed interest rate swap agreements of various durations to manage both its funding cost and the interest rate risk associated with variable rate debt. Under these swap agreements, the University pays a fixed rate and receives from its counterparty a variable rate payment, each calculated by reference to specified notional principal amounts during the agreement period. Operations are charged the variable rate interest on the corresponding bonds; the difference between the fixed and variable interest amounts under the swap agreements is recorded in non-operating revenues and expenses as investment and other income.

Information related to the interest rate swap agreements to which the University is a party, including the associated OHEFC borrowing where applicable and the asset (liability) recognized in the balance sheets are as follows:

| Date of Agreement | OHEFC Borrowing | Notional Amount | Fixed Rate | Maturity Date | 2008 | 2007 |
|-------------------|-----------------|-----------------|------------|---------------|------------|----------|
| February 2001 | Series 2001 | \$ 18,875 | 4.34% | 2022 | \$ (1,163) | \$ (388) |
| May 2002 | Series 2002 | 15,000 | 4.43% | 2022 | (1,790) | (764) |
| September 2002 | Series 2002 | 15,000 | 3.60% | 2022 | (494) | 516 |
| October 2003 | n/a | 35,000 | 3.81% | 2034 | (2,187) | 774 |
| January 2007 | n/a | 100,000 | 3.37% | 2012 | (1,640) | 1,544 |
| January 2008 | Series 2008 | 100,000 | 3.37% | 2017 | (1,533) | - |

Changes in the fair value of derivative instruments are recorded in non-operating revenues and expenses as investment and other income.

**NOTE K
 Recently
 Issued
 Accounting
 Pronounce-
 ments**

In September 2006, the FASB issued Statement of Financial Accounting Standard No. 157, "Fair Value Measurements" (SFAS 157). The standard defines fair value, outlines a framework for measuring fair value, and details the required disclosures about fair value measurements. The standard is effective for the University as of and for the year ended June 30, 2009 except for certain provisions, which were deferred for an additional year. Management of the University is evaluating the impact of this pronouncement but does not believe the adoption of SFAS 157 will have a material impact on the financial statements.

In February 2007, the FASB issued Statement of Financial Accounting Standard No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" (SFAS 159). The standard permits entities to choose to measure many financial instruments and certain other items at fair value. The standard is effective for the University as of and for the year ended June 30, 2009. Management of the University is evaluating the impact of this pronouncement but does not believe the adoption of SFAS 159 will have a material impact on the financial statements.

In August 2008, the FASB issued FASB Staff Position 117-1, "Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an

NOTE K
Recently
Issued
Accounting
Pronounce-
ments
(continued)

Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for all Endowment Funds.” The standard provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA), and expands disclosures about an organization’s endowment (both donor-restricted and board-designated funds) whether or not the organization is subject to UPMIFA. The standard will be effective for the University as of and for the year ended June 30, 2009. Management is evaluating the impact of this pronouncement.

NOTE L
Subsequent
Event

The University invests a portion of its operating cash with the Commonfund Short Term Investment Fund (CSTIF), a bank commingled fund that uses Wachovia Bank N.A as trustee and is sponsored by The Commonfund for Nonprofits. The balance in the CSTIF as of June 30, 2008 was \$1,501. Subsequent to June 30, 2008, the University added to its CSTIF investment. On September 27, the trustee terminated the CSTIF and restricted redemptions pending an orderly liquidation of its assets. As of October 3, 2008, the University has received distributions in the amount of \$7,350; a total of \$12,199 remains in the CSTIF. The timing and amount of future distributions is dependent on the sale or maturity of the CSTIF’s underlying investments and the liquidity of markets into which those investments may be sold. At June 30, 2008, the University classified its investment in the CSTIF as a cash equivalent; subsequent to September 27, 2008, management has reclassified the balance to investments.