



Report of Independent Auditors  
and Financial Statements for  
**Pacific Lutheran University**  
May 31, 2015 and 2014

**MOSS ADAMS** LLP

Certified Public Accountants | Business Consultants

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## REPORT OF INDEPENDENT AUDITORS

To the Board of Directors  
Pacific Lutheran University

### **Report on the Financial Statements**

We have audited the accompanying financial statements of Pacific Lutheran University (the University), which comprise the statement of financial position as of May 31, 2015, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements.

### ***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### ***Auditor's Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence obtained is sufficient and appropriate to provide a basis for our audit opinion.

***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Pacific Lutheran University as of May 31, 2015, and the changes in its net assets and its cash flows for the year then ended, in accordance with accounting principles generally accepted in the United States of America.

***Prior Period Financial Statements***

The financial statements of Pacific Lutheran University as of May 31, 2014, were audited by other auditors whose report, dated December 16, 2014, expressed an unmodified opinion on those statements.

*Moss Adams LLP*

Yakima, Washington  
January 14, 2016

**PACIFIC LUTHERAN UNIVERSITY**  
**STATEMENT OF FINANCIAL POSITION**

	May 31,	
	2015	2014
<b>ASSETS</b>		
Cash and cash equivalents	\$ 5,332,993	\$ 4,250,129
Student accounts receivable, net of allowance for doubtful accounts of \$463,120 and \$451,500	2,002,112	1,285,627
Other receivables	1,311,540	1,330,802
Estate gift receivable	-	25,000
Real estate contracts receivable	86,687	116,551
Grants receivable	983,964	908,014
Contributions receivable, net	1,261,407	1,711,621
Inventories	718,251	864,658
Prepaid expenses and deposits	989,591	1,197,579
Real estate held for sale	457,920	1,967,020
Student loans receivable, net	6,795,169	7,186,738
Investments	12,853,900	12,697,622
Endowment investments	82,547,124	82,251,836
Deposits held by trustee - government obligations	11,427,689	4,801,810
Bond acquisition costs	1,402,709	1,256,156
Other assets	400,000	400,000
Construction in progress	5,554,597	1,361,012
Property, plant, and equipment, net	119,069,620	121,261,916
<b>TOTAL ASSETS</b>	<b>\$ 253,195,273</b>	<b>\$ 244,874,091</b>
<b>LIABILITIES AND NET ASSETS</b>		
<b>LIABILITIES</b>		
Accounts payable	\$ 2,311,883	\$ 1,855,632
Accrued liabilities	8,332,485	9,274,439
Student deposits	2,331,817	1,793,122
Asset retirement obligation	963,506	917,623
Long-term debt	63,230,995	54,575,944
Unamortized premium on long-term debt	759,182	917,846
Annuities payable	6,761,533	6,561,595
Deposits held in custody for others	1,191,855	1,111,053
Government grants refundable	7,590,287	7,391,775
Total liabilities	93,473,543	84,399,029
<b>NET ASSETS</b>		
Unrestricted	65,917,282	70,470,694
Temporarily restricted	11,348,180	11,330,335
Permanently restricted	82,456,268	78,674,033
Total net assets	159,721,730	160,475,062
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<b>\$ 253,195,273</b>	<b>\$ 244,874,091</b>

See accompanying notes.

**PACIFIC LUTHERAN UNIVERSITY**  
**STATEMENT OF ACTIVITIES**  
**YEAR ENDED MAY 31, 2015**

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>REVENUES AND GAINS</b>				
Tuition and fees	\$ 112,574,826	\$ -	\$ -	\$ 112,574,826
Less scholarships and grants	(48,575,832)	-	-	(48,575,832)
	63,998,994	-	-	63,998,994
Government grants	2,203,822	-	-	2,203,822
Contributions	1,726,623	6,009,739	3,671,480	11,407,842
Other investment income (loss)	(2,237,147)	3,377,422	532,101	1,672,376
Sales and services of auxiliary enterprises	17,283,354	-	-	17,283,354
Other revenue	4,028,386	-	126,036	4,154,422
	87,004,032	9,387,161	4,329,617	100,720,810
Reclassification of net assets	287,304	-	(287,304)	-
Net assets released from restrictions	9,367,239	(9,367,239)	-	-
	96,658,575	19,922	4,042,313	100,720,810
<b>EXPENSES AND LOSSES</b>				
Program expenses				
Instruction	32,518,319	-	-	32,518,319
Research	251,696	-	-	251,696
Public service	6,941,273	-	-	6,941,273
Academic support	5,372,843	-	-	5,372,843
Student services	10,605,913	-	-	10,605,913
Auxiliary enterprises	12,621,089	-	-	12,621,089
Supporting expenses				
Institutional support	18,720,998	-	-	18,720,998
Allocable expenses				
Operations and maintenance of plant	7,628,322	-	-	7,628,322
Interest expense	2,880,886	-	-	2,880,886
Depreciation and amortization	3,732,865	-	-	3,732,865
Adjustment of actuarial liability for annuities payable	(62,217)	2,077	260,078	199,938
	101,211,987	2,077	260,078	101,474,142
CHANGE IN NET ASSETS	(4,553,412)	17,845	3,782,235	(753,332)
NET ASSETS, beginning of year	70,470,694	11,330,335	78,674,033	160,475,062
NET ASSETS, end of year	\$ 65,917,282	\$ 11,348,180	\$ 82,456,268	\$ 159,721,730

**PACIFIC LUTHERAN UNIVERSITY**  
**STATEMENT OF ACTIVITIES**  
**YEAR ENDED MAY 31, 2014**

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>REVENUES AND GAINS</b>				
Tuition and fees	\$ 112,878,069	\$ -	\$ -	\$ 112,878,069
Less scholarships and grants	(47,097,692)	-	-	(47,097,692)
	65,780,377	-	-	65,780,377
Government grants	3,057,376	-	-	3,057,376
Contributions	1,259,798	6,908,659	2,278,065	10,446,522
Other investment income	1,245,655	4,251,639	582,389	6,079,683
Sales and services of auxiliary enterprises	17,339,375	-	-	17,339,375
Other income	943,147	2,119,000	-	3,062,147
	89,625,728	13,279,298	2,860,454	105,765,480
Reclassification of net assets	2,170,729	(2,194,609)	23,880	-
Net assets released from restrictions	21,332,334	(21,332,334)	-	-
	113,128,791	(10,247,645)	2,884,334	105,765,480
<b>EXPENSES AND LOSSES</b>				
Program expenses				
Instruction	33,787,434	-	-	33,787,434
Research	288,083	-	-	288,083
Public service	7,166,070	-	-	7,166,070
Academic support	5,280,966	-	-	5,280,966
Student services	10,921,894	-	-	10,921,894
Auxiliary enterprises	12,701,637	-	-	12,701,637
Supporting expenses				
Institutional support	17,302,001	-	-	17,302,001
Allocable expenses				
Operations and maintenance of plant	8,911,369	-	-	8,911,369
Interest expense	2,550,875	-	-	2,550,875
Depreciation and amortization	5,249,785	-	-	5,249,785
Adjustment of actuarial liability				
for annuities payable	(63,159)	(5,957)	(582,117)	(651,233)
Loss on disposal of plant facilities	99,300	-	-	99,300
Loss on contributions receivable	34,666	10,000	9,000	53,666
	104,230,921	4,043	(573,117)	103,661,847
CHANGE IN NET ASSETS	8,897,870	(10,251,688)	3,457,451	2,103,633
NET ASSETS, beginning of year	61,572,824	21,582,023	75,216,582	158,371,429
NET ASSETS, end of year	\$ 70,470,694	\$ 11,330,335	\$ 78,674,033	\$ 160,475,062

**PACIFIC LUTHERAN UNIVERSITY**  
**STATEMENT OF CASH FLOWS**

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	Year Ended May 31,	
	2015	2014
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Change in net assets	\$ (753,332)	\$ 2,103,633
Adjustments to reconcile change in net assets to net cash from operating activities		
Depreciation and amortization	3,824,421	5,206,087
Accretion	45,883	43,698
Change in gifts of investments	-	577
Loss (gain) on endowment investment and perpetual trusts	286,514	(4,802,551)
Gain on investments	(19,991)	(964,395)
Actuarial adjustment on annuities payable	298,814	691,149
Loss on sale of real estate	1,047,236	-
Unrealized loss on real estate	-	38,000
Increase in allowance on student accounts receivable	11,620	33,900
Decrease in allowance on student loans receivable	(20,000)	(14,000)
Change in cash surrender value of life insurance held as endowment investment	(26,912)	(210,407)
Contribution of real estate held for sale	(282,920)	-
Contributions restricted for long-term investment, loans, and plant	(3,353,748)	(3,551,017)
Increase (decrease) in cash due to changes in assets and liabilities		
Student accounts receivable	(728,105)	(105,736)
Other receivables	19,262	(150,502)
Estate gift receivable	25,000	425,000
Grant receivables	(75,950)	122,892
Contributions receivable for operations	450,214	109,859
Inventories, prepaid expense, and deposits	354,395	(96,483)
Accounts payable and accrued liabilities	123,735	1,727,100
Student deposits	538,695	70,158
Deposits held in custody for others	80,802	(42,365)
Government grants refundable	198,512	(39,045)
Net cash from operating activities	<u>\$ 2,044,145</u>	<u>\$ 595,552</u>



**PACIFIC LUTHERAN UNIVERSITY**  
**STATEMENT OF CASH FLOWS**

	Year Ended May 31,	
	2015	2014
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchases of investments	\$ (11,237,296)	\$ (10,236,580)
Sales of investments	10,526,690	9,619,292
Proceeds from partial redemption of life insurance policy	19,429	114,080
Proceeds from sale of real estate	744,784	-
Additions to deposits held by trustee, net	(6,625,879)	(32,201)
Purchases of property, plant, and equipment, including construction in progress	(6,420,439)	(9,657,425)
Repayments of real estate contract receivables	29,864	29,500
Net change in student loans receivable	411,569	250,123
Net cash from investing activities	(12,551,278)	(9,913,211)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from issuance of indebtedness, net of discount	9,881,242	-
Repayments of principal on indebtedness	(1,344,949)	(1,278,668)
Loan fees	(201,168)	-
Contributions received restricted for long-term investment, loans, and plant	3,353,748	3,839,116
Proceeds from issuance of split-interest agreements	755,000	45,000
Payments to annuitants	(853,876)	(822,680)
Net cash from financing activities	11,589,997	1,782,768
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	1,082,864	(7,534,891)
<b>CASH AND CASH EQUIVALENTS, beginning of year</b>	4,250,129	11,785,020
<b>CASH AND CASH EQUIVALENTS, end of year</b>	\$ 5,332,993	\$ 4,250,129
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>		
Interest paid	\$ 2,886,293	\$ 2,556,020
Property, plant, and equipment acquired through accounts payable	-	609,438

**Note 1 – Organization**

Pacific Lutheran University (the University) is a private non-profit institution that offers a full range of liberal arts academic programs to undergraduate and graduate students. Affiliated with the Evangelical Lutheran Church in America, the University enrolls approximately 3,300 students. The University offers 44 majors and 54 minors, as well as graduate and professional programs in business administration, creative writing, education, finance, marketing research, marriage and family therapy, and nursing.

**Note 2 – Summary of Significant Accounting Policies**

**Basis of accounting** – The accounting policies of the University reflect practices common to universities and colleges and conform to accounting principles generally accepted in the United States of America. The more significant accounting policies are summarized below.

**Use of estimates** – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Recent accounting pronouncement** – In April 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2015-07, Fair Value Measurement (Topic 820): *Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*.

The amendments remove the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient (NAV practical expedient). ASU 2015-07 has been adopted for the year ended May 31, 2015; however, the retrospective approach requires that an investment for which fair value is measured using a NAV practical expedient be removed from the fair value hierarchy in all periods presented in the financial statements. Accordingly, the investment disclosures in Note 3 have been modified as of May 31, 2014 as well.

**Cash and cash equivalents** – Cash and cash equivalents consist of short-term, highly liquid investments with an original maturity of three months or less, except for those held for long-term investment. Certain cash held by the University is restricted for the Federal Perkins and Nursing Loan Funds. The University's cash balances exceed Federal Deposit Insurance Corporation (FDIC) and Securities Investor Protection Corporation (SIPC) insured amounts at times. The University has not experienced any significant losses on its cash investments.

**Student accounts receivable** – Student accounts receivable are carried at the unpaid balance of the original amount billed to students less an allowance for doubtful accounts. Management determines the sufficiency of the allowance based on the length of time past due and historical experience. Student accounts are written off when all means of collection has been exhausted and collection is deemed unlikely.

**Estate gift receivable** – During the year ended May 31, 2011, the University received a gift of several properties and other assets from an estate. The amount recorded as estate gift receivable at May 31, 2014 represents the non-liquidated portion of the estate, which was valued at the estimated fair value of assets at the date of the gift based on market appraisals, signed purchase agreements or other reliable expedients. The estate was liquidated during 2015.

**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 2 – Summary of Significant Accounting Policies (continued)**

**Inventories** – Bookstore inventories are valued at a percentage of retail value, which approximates cost and is not in excess of market. All other inventories are valued at the lower of cost or market, determined on a first-in, first-out basis.

**Deposits held by trustee** – Deposits held by trustee include amounts restricted for debt service as required by the trust indentures.

**Bond acquisition costs** – Costs of bond issuance are deferred and amortized over the term of the related indebtedness.

**Property, plant, and equipment** – Physical plant assets are stated at cost at date of acquisition less accumulated depreciation. The University depreciates its assets on the straight-line basis over estimated useful lives as follows: buildings and building improvements, 10 to 50 years; improvements other than buildings, 10 years; automobiles, 5 years; library books, 15 years; equipment, 10 years; and leasehold improvements, 15 years. Normal repair and maintenance expenses are charged to operations as incurred. The University capitalizes asset additions in excess of \$5,000.

**Impairment of long-lived assets** – The University reviews long-lived assets, including property and equipment and intangible assets, for impairment whenever events or changes in business circumstances indicate that the carrying amount of an asset may not be fully recoverable. An impairment loss would be recognized when the estimated future cash flows from the use of the asset are less than the carrying amount of that asset. To date, there have been no such losses.

**Fair value of financial instruments** – The carrying values of cash and cash equivalents, receivables, prepaid expenses, deposits held in custody for others, accounts payable and accrued liabilities, annuities payable and related-party notes payable are reasonable estimates of their fair value due to discounting or the short-term nature and terms of these financial instruments. Investments are recorded at fair value as discussed in Note 3. The fair value of bonds payable approximates the carrying value, as it is based on current rates offered to the University for similar debt of the same remaining maturities and, additionally, the University considers its creditworthiness in determining the fair value of the bonds payable. The bonds are considered a Level 2 within the fair value hierarchy as described in Note 3. It is not practical to estimate the fair value of student receivables and the liability for governmental grants refundable, as these loans are subject to restrictions on interest rates and transferability. Real estate is recorded at cost except those items received as gifts, which are valued at fair value at the date of the gift. The investments in Garfield Commons, LLC, and Garfield North, LLC, are carried at cost.

**Fair value measurements** – The Fair Value Measurements and Disclosures Topic of the Financial Accounting Standards Board's (FASB) Accounting Standards Codification defines fair value, establishes a framework for measuring fair value, and expands disclosure of fair value measurements, which applies to all assets and liabilities that are measured and reported on a fair value basis. See Note 3 for additional information.

**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 2 – Summary of Significant Accounting Policies (continued)**

**Asset retirement obligations** – The University recognizes the fair value of a liability for legal obligations associated with asset retirements in the period in which it is incurred, if a reasonable estimate of the fair value of the obligation can be made.

Substantially all of the University's asset retirement obligations relate to estimated costs to remove asbestos from campus facilities. The estimate of the losses that are probable for asbestos removal was calculated using the expected cash flow approach and based on an inventory of the University's long-lived assets combined with an estimate of the current market prices to remove the asbestos. The University utilized a credit-adjusted risk-free rate to discount the asset retirement obligation.

Changes in the accrual for asset retirement obligations during the years ended May 31, 2015 and 2014 are as follows:

	<u>2015</u>	<u>2014</u>
Balance, beginning of year	\$ 917,623	\$ 873,925
Accretion expense	<u>45,883</u>	<u>43,698</u>
Balance, end of year	<u><u>\$ 963,506</u></u>	<u><u>\$ 917,623</u></u>

**Government grants refundable** – Funds provided by the United States Government under the Federal Perkins and Nursing Loan Programs are loaned to qualified students and may be reloaned after collections. These funds are ultimately refundable to the government and are included as liabilities in the statements of financial position.

**Income tax status** – The Internal Revenue Service has determined that the University is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code. However, any unrelated business income may be subject to taxation.

The University follows the accounting standards for contingencies in evaluating uncertain tax positions. This guidance prescribes recognition threshold principles for the financial statement recognition of tax positions taken or expected to be taken on a tax return that are not certain to be realized. No liability has been recognized by the University for uncertain tax positions as of May 31, 2015 and 2014. The University's tax returns are subject to review and examination by federal authorities. The tax returns for fiscal years 2012 and thereafter are open to examination by federal authorities.

**Financial statement presentation** – The University reports information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. Net assets of the University and changes therein are classified and reported as follows:

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

**Temporarily restricted net assets** – Net assets subject to donor-imposed stipulations that will be met by action of the University and/or the passage of time.

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

**Note 2 – Summary of Significant Accounting Policies (continued)**

**Releases from restrictions** - Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed and the law allows the release of the restriction) are reported on the statement of activities as net assets released from restrictions. Occasionally donor restrictions related to net assets may be clarified or changed, at which time they are reflected as reclassification of prior year net assets on the statement of activities.

**Tuition and fees** – Student tuition and fees are recorded as revenue on a ratable basis over the term of instruction. The majority of the University’s students rely on funds received from various federal financial aid programs under Title IV of the Higher Education Act of 1965, as amended, to pay for a substantial portion of their tuition. These programs are subject to periodic review by the United States Department of Education (USDE). Disbursements under each program are subject to disallowance by the USDE and repayment by the University. In addition, as an educational institution, the University is subject to licensure from various accrediting and state authorities and other regulatory requirements of the USDE. Deferred revenues represent primarily tuition from enrollment in summer school classes, which is attributable to the following fiscal year, and tuition deposits made by students in the current fiscal year that are to be used in following years.

**Auxiliary enterprises** – Auxiliary enterprises consist of revenues and expenses relating to the operation of the residence halls, food services, bookstore, and the rental of facilities. Revenues from auxiliary enterprises are recorded at the time the related services are provided.

**Other revenue and expenses** – Revenues from sources other than contributions are generally reported as increases in unrestricted net assets. Expenses are reported as decreases in unrestricted net assets. Income earned on donor-restricted funds is initially classified as temporarily restricted net assets and is reclassified as unrestricted net assets when expenses are incurred for their intended purpose.

**Contributions** – Contributions, including unconditional promises to give, are recognized as revenues in the period received and are reported as increases in the appropriate categories of net assets in accordance with donor restrictions. Expirations of temporary restrictions on net assets are reported as reclassifications between the applicable classes of net assets. Conditional promises to give are recognized when the donor-imposed conditions are substantially met. Unconditional promises to give, due after one year, are reported at the present value of net realizable value, using appropriate interest rates applicable to the years in which the promises were received. Amortization of discounts is recorded as an additional contribution, if any.

Contributions of property and equipment without donor stipulations concerning the use of such long-lived assets are reported as unrestricted revenues. Contributions of cash or other assets to be used to acquire property and equipment are reported as temporarily restricted revenues; the restrictions are considered to be released at the time such long-lived assets are placed in service.

**Grant revenue** – Revenues from other government grants are recognized as they are earned in accordance with the agreement. Any funding received before it is earned is recorded as a refundable advance. Expenses incurred before cash is received are recorded as receivables.

**Note 2 – Summary of Significant Accounting Policies (continued)**

**Investment gains and losses** – Income net gains and losses on investments of endowment and similar funds are reported as follows:

- Increases or decreases in permanently restricted net assets if the terms of the gift or the University's interpretation of relevant state law requires they be added to the principal of a permanently restricted net asset.
- Increases or decreases in temporarily restricted net assets if the terms of the gift impose restrictions on the use of the income.
- Increases or decreases in unrestricted net assets in all other cases.

**Retirement plans** – The University has a defined contribution retirement plan for academic and nonacademic personnel. Individual contributions are based on a percentage of compensation. The University contribution rate was 7.5% as of May 31, 2015 and 2014, resulting in total contributions of approximately \$3,775,000 and \$3,659,000 for 2015 and 2014, respectively.

**Grants to specified students** – Amounts received from state and federal agencies designated for the benefit of specified students are considered agency transactions and, therefore, are not reflected as revenues and expenses of the University.

**Fundraising and advertising expenses** – Fund-raising expenses totaled \$2,193,044 and \$2,450,000 for the years ended May 31, 2015 and 2014, respectively. Advertising costs are expensed when incurred.

**Functional allocation of expenses** – The costs of providing the various programs and other activities have been summarized on a functional basis in the statement of activities. Accordingly, certain expenses have been allocated among the programs and supporting services benefited.

**Reclassification** – Certain amounts from the prior year statement of net assets available for benefits have been reclassified, in order to conform to the current year presentation.

**Note 3 – Fair Value Measurements**

Fair value is defined in the accounting guidance as the exchange price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the assets or liability in an orderly transaction between market participants at the measurement date. Under this guidance, a three-level hierarchy is used for fair value measurements which are based on the transparency of information, such as the pricing source, used in the valuation of an asset or liability as of the measurement date.

Financial instruments measured and reported at fair value are classified and disclosed in one of the following three categories.

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

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at May 31, 2015 and 2014.

*Mutual and commodity funds:* Valued at the daily closing price as reported by the fund. Mutual funds held by the University are open-end mutual funds that are registered with the U.S. Securities and Exchange Commission. These funds are required to publish their daily net asset value (NAV) and to transact at that price. The mutual funds held by the Plan are deemed to be actively traded.

*Short-term investments:* Primarily consist of money market funds for which quoted prices are not readily available. The fair values are estimated using Level 2 inputs based on multiple sources of information, which may include market data and/or quoted market prices from either markets that are not active or are for the same or similar assets in active markets.

*Perpetual trusts held by others:* Estimate of fair value is based on fair value of underlying investments of the University's proportionate interest in the trusts based on information received from trustees. Trust assets consist of, but are not limited to, cash and cash equivalents, corporate and government bonds, mutual funds and equity securities. These assets are not subject to control or direction by the University.

*Hedge funds, private equity funds and funds of funds:* Quoted prices are not readily available and funds cannot be redeemed within a short period of time. The University has estimated the fair value of these funds using the NAV provided by the investee as of the most recent date, adjusted for cash receipts, cash disbursements, and significant known valuation changes in market values of publicly held securities contained in the portfolio and security distributions through May 31, 2015 and 2014.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

**Note 3 – Fair Value Measurements (continued)**

While the University believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

The following table presents information about the University's assets measured at fair value on a recurring basis as of May 31, 2015 by level:

	Level 1	Level 2	Level 3	Total
<b>ASSETS</b>				
Short-term investments	\$ -	\$ 5,375,235	\$ -	\$ 5,375,235
Mutual funds				
Domestic equity funds	10,995,964	-	-	10,995,964
International equity funds	28,055,821	-	-	28,055,821
Global fixed income funds	6,776,294	884,129	-	7,660,423
Index funds	3,957,315	-	-	3,957,315
U.S. government bond funds	-	1,292,370	-	1,292,370
Corporate bond funds	-	2,018,336	-	2,018,336
High yield bond funds	-	288,297	-	288,297
Real estate funds	-	-	-	-
Commodity funds	3,424,232	-	-	3,424,232
Perpetual trusts held by endowment	-	-	11,257,950	11,257,950
Government obligations	11,427,689	-	-	11,427,689
Total assets in the fair value hierarchy	<u>\$ 64,637,315</u>	<u>\$ 9,858,367</u>	<u>\$ 11,257,950</u>	<u>85,753,632</u>
Investments measured at NAV (practical expedient)				<u>12,675,300</u>
				<u>\$ 98,428,932</u>



**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

**Note 3 – Fair Value Measurements (continued)**

The following table presents information about the University's assets measured at fair value on a recurring basis as of May 31, 2014 by level:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
<b>ASSETS</b>				
Short-term investments	\$ -	\$ 2,353,510	\$ -	\$ 2,353,510
Mutual funds				
Domestic equity funds	13,938,292	-	-	13,938,292
International equity funds	26,884,956	-	-	26,884,956
Global fixed income funds	6,707,579	911,937	-	7,619,516
U.S. government bond funds	-	1,254,639	-	1,254,639
Corporate bond funds	-	2,064,731	-	2,064,731
High yield bond funds	-	289,018	-	289,018
Real estate funds	-	1,708,830	-	1,708,830
Commodity funds	1,801,994	-	-	1,801,994
Perpetual trusts held by endowment	-	-	10,140,973	10,140,973
Government obligations	4,801,810	-	-	4,801,810
Total assets in the fair value hierarchy	<u>\$ 54,134,631</u>	<u>\$ 8,582,665</u>	<u>\$ 10,140,973</u>	<u>72,858,269</u>
Investments measured at NAV (practical expedient)				<u>18,412,755</u>
				<u>\$ 91,271,024</u>

The following table presents a reconciliation of the statement of financial position amounts for assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the year ended May 31, 2015:

	<u>Balance</u> <u>May 31, 2014</u>	<u>Net Realized</u> <u>and Unrealized</u> <u>Gains</u>	<u>Purchases</u>	<u>Sales</u>	<u>Balance</u> <u>May 31, 2015</u>
<b>Assets</b>					
Perpetual trusts held by endowment	<u>\$ 10,140,973</u>	<u>\$ 101,890</u>	<u>\$ 1,015,087</u>	<u>\$ -</u>	<u>\$ 11,257,950</u>
	<u>\$ 10,140,973</u>	<u>\$ 101,890</u>	<u>\$ 1,015,087</u>	<u>\$ -</u>	<u>\$ 11,257,950</u>

The amount of net gains for the period included in change in net assets attributable to the change in unrealized gains and losses relating to assets measured at fair value still held at May 31, 2015 was \$101,890.

**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 3 – Fair Value Measurements (continued)**

The following table presents a reconciliation of the statement of financial position amounts for assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the year ended May 31, 2014:

	Balance May 31, 2013	Net Realized and Unrealized Gains	Purchases	Sales	Balance May 31, 2014
Assets					
Perpetual trusts held by endowment	\$ 9,593,347	\$ 547,626	\$ -	\$ -	\$ 10,140,973
	<u>\$ 9,593,347</u>	<u>\$ 547,626</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 10,140,973</u>

The amount of total gains for the period included in change in net assets attributable to the change in unrealized gains relating to assets measured at fair value still held at May 31, 2014 was \$547,626.

The University uses the NAV as a practical expedient to determine fair value of all underlying investments which (a) do not have a readily determinable fair value, and (b) are in investment companies or similar entities that report their investment assets at fair values.

**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 3 – Fair Value Measurements (continued)**

The following table lists the alternative investments in which NAV was utilized as the practical expedient for estimating fair value by major category as of May 31, 2015:

	Hedge Funds	Private Equity Funds	Funds of Funds
Fair value, May 31, 2015	\$5,002,436	\$2,728,824	\$4,944,040
Significant investment strategy	Long and short global equities, fixed income, and their derivatives	Venture and buyout investments in private companies globally	Long and short equities and their derivatives
Remaining life	N/A	1 to 12 years	N/A
Dollar amount of unfunded commitments	N/A	\$811,000	N/A
Timing to draw down commitments	N/A	3 to 5 years	N/A
Redemption terms	Range from monthly to annual, on 60 to 90 days' notice	N/A	Annual with 100 days' notice
Redemption restrictions	Currently there are no lock-ups in effect. Upon full redemption, 90%-95% is returned, with the remaining 5%-10% held back until the completion of the annual audit	N/A	Upon full redemption, 90% is returned, with the remaining 10% held back until completion of the annual audit
Redemption restrictions in place at year end	Two funds have yet to return holdback positions following nearly-complete redemptions	N/A	None

**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

**Note 4 – Contributions Receivable**

Contributions receivable at May 31 include the following:

	<u>2015</u>	<u>2014</u>
Contributions	\$ 2,239,964	\$ 2,474,492
Less allowance for uncollectable contributions	(140,156)	(190,180)
Less unamortized discount	<u>(838,401)</u>	<u>(572,691)</u>
Net unconditional promises to give	<u>\$ 1,261,407</u>	<u>\$ 1,711,621</u>
Amounts due in:		
Less than one year	\$ 625,921	
One to five years	384,994	
More than five years	<u>1,229,049</u>	
	<u>\$ 2,239,964</u>	

Contributions due in more than one year received on or before May 31, 2009 were discounted at an interest rate of 6%. Contributions due in more than one year received after May 31, 2009 are discounted at interest rates that approximate the U.S. Daily Treasury Yield Curve at the date of the gift adjusted for a risk premium. The discount rates for these contributions ranged from 1.57% to 6.00% at May 31, 2015 and 2014. Contributions due in less than one year were not discounted.

**Note 5 – Student Loans Receivable**

The University issues uncollateralized loans to students based on financial need. Student loans are funded through Federal government loan programs or institutional resources. Student loans receivable are carried at the amount of unpaid principal less an estimate for doubtful accounts. Allowances for doubtful accounts are established based on prior collection experience and current economic factors which, in management's judgment, could influence the ability of loan recipients to repay the amounts per the loan terms. At both May 31, 2015 and 2014, student loans represented approximately 3% of total assets.

At May 31, 2015 and 2014, student loans consisted of the following:

	<u>2015</u>	<u>2014</u>
Federal government programs	\$ 7,152,169	\$ 7,563,738
Less allowance for doubtful accounts		
Beginning of year	377,000	391,000
Decrease in allowance	<u>20,000</u>	<u>14,000</u>
End of year	<u>357,000</u>	<u>377,000</u>
Student loans receivable, net	<u>\$ 6,795,169</u>	<u>\$ 7,186,738</u>

Funds advanced by the Federal government of \$7,377,399 and \$7,390,342 at May 31, 2015 and 2014, respectively, are ultimately refundable to the government and are classified as liabilities in the statement of financial position.

**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 5 – Student Loans Receivable (continued)**

After a student is no longer enrolled in an institution of higher education and after a grace period, interest is charged on student loans receivable and is recognized as it is charged. Student loans receivable through the loan programs are considered to be past due if a payment is not made within 30 days of the payment due date, at which time, late charges are charged and recognized. The Federal Perkins and Nursing Loan Program receivables may be assigned to the U.S. Department of Education and U.S. Department of Health and Human Services, respectively. Students may be granted a deferment, forbearance, or cancellation of their student loan based on eligibility requirements defined by the U.S. Department of Education and U.S. Department of Health and Human Services.

A student loan receivable is considered to be delinquent if any portion of the receivable balance is outstanding for more than 60 days after the billing date. At May 31, 2015 and 2014, the following amounts were past due under student loan programs:

May 31,	Amounts Past Due			Total
	60-89 Days	90-119 Days	120+ Days	
2015	\$ 5,977	\$ 4,152	\$ 741,760	\$ 751,889
2014	5,099	3,562	865,427	874,088

**Note 6 – Investments**

The following summarizes the University's investments in funds other than endowment funds at May 31:

	2015	2014
Stocks, at cost	\$ 2,600	\$ 2,600
Perpetual trusts held by others	12,755,981	12,554,796
Other, at cost	95,319	140,226
	<u>\$ 12,853,900</u>	<u>\$ 12,697,622</u>

**Note 7 – Endowment Investments**

The University's endowment consists of 497 individual funds established for a variety of purposes. Its endowment includes both donor-restricted endowment funds and funds designated by the governing board to function as endowments. As required by GAAP, net assets associated with endowment funds, including funds designated by the governing board to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

**Note 7 – Endowment Investments (continued)**

**Interpretation of relevant law** – The University has interpreted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) adopted by the 2009 Washington legislature as requiring the preservation of 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. As a result of this interpretation, 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 gift instrument 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 the state of Washington in its enacted version of 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 Endowment 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; and (7) the investment policies of the University.

Endowment net asset composition by type of fund consists of the following as of May 31, 2015:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ (2,171,445)	\$ 6,076,087	\$ 76,745,894	\$ 80,650,536
Board-designated endowment funds	<u>4,930,903</u>	<u>-</u>	<u>-</u>	<u>4,930,903</u>
	<u>\$ 2,759,458</u>	<u>\$ 6,076,087</u>	<u>\$ 76,745,894</u>	<u>\$ 85,581,439</u>

Endowment net asset composition by type of fund consists of the following as of May 31, 2014:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ (1,460,337)	\$ 7,368,650	\$ 73,378,427	\$ 79,286,740
Board-designated endowment funds	<u>5,078,336</u>	<u>-</u>	<u>-</u>	<u>5,078,336</u>
	<u>\$ 3,617,999</u>	<u>\$ 7,368,650</u>	<u>\$ 73,378,427</u>	<u>\$ 84,365,076</u>

**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

**Note 7 – Endowment Investments (continued)**

Changes in endowment net assets for the year ended May 31, 2015 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, May 31, 2014	\$ 3,617,999	\$ 7,368,650	\$ 73,378,427	\$ 84,365,076
Investment return				
Investment income, net of fees of \$203,793	635,697	1,613,184	-	2,248,881
Net appreciation, perpetual trusts - unrealized	-	-	101,890	101,890
Net appreciation (depreciation) - realized and unrealized	(858,841)	441,262	-	(417,579)
Total investment return	<u>(223,144)</u>	<u>2,054,446</u>	<u>101,890</u>	<u>1,933,192</u>
Contributions	300	-	3,233,325	3,233,625
Appropriation of endowment net assets for expenditure	(635,697)	(3,366,622)	-	(4,002,319)
Transfer from other funds	<u>-</u>	<u>19,613</u>	<u>32,252</u>	<u>51,865</u>
Endowment net assets, May 31, 2015	<u>\$ 2,759,458</u>	<u>\$ 6,076,087</u>	<u>\$ 76,745,894</u>	<u>\$ 85,581,439</u>

Changes in endowment net assets for the year ended May 31, 2014 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, May 31, 2013	\$ 2,940,979	\$ 6,256,854	\$ 70,387,873	\$ 79,585,706
Investment return				
Investment income, net of fees of \$242,845	588,297	658,626	-	1,246,923
Net appreciation, perpetual trusts - unrealized	-	-	547,625	547,625
Net appreciation - realized and unrealized	652,988	3,601,938	-	4,254,926
Total investment return	<u>1,241,285</u>	<u>4,260,564</u>	<u>547,625</u>	<u>6,049,474</u>
Contributions	24,032	-	2,308,470	2,332,502
Appropriation of endowment net assets for expenditure	(588,297)	(3,174,181)	-	(3,762,478)
Transfer from other funds	<u>-</u>	<u>25,413</u>	<u>134,459</u>	<u>159,872</u>
Endowment net assets, May 31, 2014	<u>\$ 3,617,999</u>	<u>\$ 7,368,650</u>	<u>\$ 73,378,427</u>	<u>\$ 84,365,076</u>

**Note 7 – Endowment Investments (continued)**

**Funds with deficiencies** – From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the University to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature that are reported in unrestricted net assets were \$2,171,445 and \$1,460,337 as of May 31, 2015 and 2014, respectively. These deficiencies resulted from unfavorable market fluctuations that occurred after the investment of new permanently restricted contributions and continued appropriation for certain programs that was deemed prudent by the governing board. Subsequent gains that restore the fair value of the assets of the endowment fund to the required level will be classified as an increase in unrestricted net assets.

**Return objectives and risk parameters** – The University has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the University must hold in perpetuity or for a donor-specified period as well as board-designated funds. Under this policy, as approved by the governing board, the endowment assets are invested in a manner that is intended to produce an acceptable level of return while assuming a moderate level of investment risk. The University expects its endowment funds, over time, to provide an average annual rate of approximately 10%. Actual returns in any year may vary from this amount.

**Strategies employed for achieving objectives** – To satisfy its long-term rate-of-return objectives, the University relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The University targets a diversified asset allocation that places a greater emphasis on alternative investments to achieve its long-term return objectives within prudent risk constraints.

**Spending policy and how the investment objectives relate to spending policy** – The University has a policy that limits the amount the endowment shall distribute annually to 5% of a three-year average market value of the principal, on a unit value basis. The average computation is to include the November 30 quarter end preceding the beginning of the fiscal year. In establishing this policy, the University considered the long-term expected return on its endowment. Accordingly, over the long term, the University expects to achieve a total return, over a three-year moving average basis, at least equal to the spending rate plus the rate of inflation as measured by the Consumer Price Index (CPI) for urban customers. This is consistent with the University's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.



**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

**Note 7 – Endowment Investments (continued)**

The following summarizes the University's endowment investments, which are recorded at fair value unless otherwise noted, at May 31:

	<u>2015</u>	<u>2014</u>
Cash and short-term investments	\$ 7,645,223	\$ 3,600,162
Commodity funds	2,550,429	3,635,294
Mutual funds	43,538,944	41,586,628
Alternative investments		
Hedge funds	4,159,285	8,780,894
Funds of hedge funds	4,944,041	4,761,055
Real estate contract, at cost	454,883	485,146
Real estate, at cost	6,630,214	6,673,254
Private equity funds	<u>2,728,823</u>	<u>3,037,506</u>
	72,651,842	72,559,939
Perpetual trusts held by others	11,257,950	10,140,973
Life insurance, at cost	<u>1,671,647</u>	<u>1,664,164</u>
	85,581,439	84,365,076
Less interfund amounts		
Cash and short-term investments, at cost	(2,579,432)	(1,628,094)
Real estate contracts, at cost	<u>(454,883)</u>	<u>(485,146)</u>
	<u>(3,034,315)</u>	<u>(2,113,240)</u>
	<u>\$ 82,547,124</u>	<u>\$ 82,251,836</u>

Endowment investments include interfund amounts, which have been eliminated in the financial statements.

Investments, in general, are subject to various risks, including credit, interest and overall market volatility risks. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the financial statements.

Through the University's investments in alternative investments, the University is indirectly involved in investment activities such as securities lending, trading in futures and forward contracts and other derivative products. Derivatives are used to adjust portfolio risk exposure or enhance returns. While these instruments may contain varying degrees of risk, the University's risk with respect to such transactions is limited to its capital balance in each investment. These interests have varying degrees of liquidity.

**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

**Note 8 – Restrictions and Limitations on Net Asset Balances**

Permanently restricted net assets consist of the following at May 31:

	2015	2014
Endowment funds	\$ 76,745,894	\$ 73,378,427
Contributions receivable	111,006	238,961
Student loan funds	164,604	164,604
Annuity, life income, and similar funds	5,434,764	4,892,041
	\$ 82,456,268	\$ 78,674,033

Temporarily restricted net assets consist of the following at May 31:

	2015	2014
Gifts and other unexpended revenues and gains available for:		
Scholarships, instruction, and other departmental support - operating	\$ 3,290,057	\$ 2,852,219
Scholarships, instruction, and other departmental support - endowment funds not yet appropriated for spending	6,076,087	7,368,650
Acquisition of buildings and equipment	742,191	788,154
	10,108,335	11,009,023
Contributions receivable for operations	181,015	131,128
Contributions receivable for acquisition of buildings and equipment	945,164	131,202
Annuity, life income, and similar funds	113,666	58,982
	\$ 11,348,180	\$ 11,330,335

At May 31, 2015 and 2014, the University's unrestricted net assets were allocated as follows:

	2015	2014
Operations	\$ 455,005	\$ 1,928,984
Endowment funds		
Donor restricted endowment funds (underwater)	(2,171,445)	(1,460,337)
Board designated endowment	4,930,903	5,078,336
Total endowment	2,759,458	3,617,999
Annuity, life income, and similar funds	235,639	677,973
Loans to students	791,714	804,598
Plant	61,675,466	63,441,140
	\$ 65,917,282	\$ 70,470,694

**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

**Note 9 – Net Assets Released from Restrictions**

Net assets released from temporary donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of events specified by the donors during the years ended May 31 were as follows:

	2015	2014
Expended for plant facilities	\$ 61,996	\$ 10,552,682
Scholarships, instruction, and other departmental support	9,305,243	10,779,652
	\$ 9,367,239	\$ 21,332,334

These assets were reclassified to unrestricted net assets.

**Note 10 – Construction in Progress**

At May 31, 2015, the following major building projects were in progress:

	Cost to Date	Funding Source
Ordal Hall	\$ 1,129,440	Bond funding
South Hall	389,739	Bond funding
Stuen Hall	3,379,070	Bond funding
Campus Entrance	302,570	Private grants
Rieke Greenhouse	353,778	Private grants
	\$ 5,554,597	

**Note 11 – Property, Plant, and Equipment**

Property, plant, and equipment consisted of the following at May 31:

	2015	2014
Land	\$ 1,938,422	\$ 1,938,422
Buildings and building improvements	155,364,148	155,364,148
Improvements other than buildings	8,722,013	8,722,013
Equipment and automobiles	35,387,742	34,757,084
Library books	12,394,355	12,473,844
Leasehold improvements	1,495,189	1,840,955
Non-depreciated assets	835,950	835,950
	216,137,819	215,932,416
Less accumulated depreciation and amortization	(97,068,199)	(94,670,500)
	\$ 119,069,620	\$ 121,261,916

**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 12 – Long-Term Debt**

Long-term debt at May 31 consisted of the following:

	2015	2014
Loan payable to Washington Higher Education Facilities Authority, Series 2006	\$ 53,165,000	\$ 54,495,000
Loan payable to Washington Higher Education Facilities Authority, Series 2014	10,000,000	-
Note payable to an individual	65,995	80,944
	\$ 63,230,995	\$ 54,575,944

**Series 2006** – In December 2006, the University entered into a loan and security agreement with the Washington Higher Education Facilities Authority for the Authority to sell Series 2006 Revenue and Refunding Bonds in the amount of \$62,160,000. Interest is payable semi-annually on each November 1 and May 1 at rates ranging from 4.25% to 5.00%. Serial bonds are payable in amounts ranging from \$1,330,000 to \$2,300,000 on November 1, 2014 through November 1, 2025. Term bonds in the amounts of \$16,085,000 and \$17,080,000 are due November 1, 2031 and 2036, respectively. The term bonds are subject to annual sinking fund payments on November 1, in the years 2026 to 2036, in amounts varying from \$2,400,000 to \$3,730,000. The bonds were issued for the purposes of refinancing the series 1996 and series 1999 loans and for construction and plant improvement projects to the extent that proceeds were available. The University has pledged its unrestricted revenues to the repayment of its obligations under the loan agreement.

**Series 2014** – In June 2014, the Washington Higher Education Facilities Authority issued Revenue Bonds (Pacific Lutheran University) Series 2014 on behalf of the University totaling \$10,000,000. The bond proceeds were used to provide a portion of the funds to finance the renovations, additions and improvements to University residence halls, including Stuen Hall, Ordal Hall and South Hall, and to other University facilities located on its campus and to pay the costs of issuing the bonds. The Series 2014 Revenue Bonds consist of term bonds of \$5,800,000 maturing on November 1, 2041 and \$4,200,000 maturing on November 1, 2044. The term bonds have interest rates of 4.625% to 5.25%, respectively. The term bonds are subject to annual sinking fund payments on November 1 in the years 2037 through 2044 in amounts varying from \$1,055,000 to \$1,475,000. The bonds are secured by a pledge of, and lien on, all unrestricted revenues and the University's interest, if any, in the Project Fund and the Debt Service Fund.

The loan agreements with the Washington Higher Education Facilities Authority require the University to comply with certain financial and other covenants. The University was not in compliance with the liquidity ratio at May 31, 2015.

**Other** – The note payable to an individual, dated January 20, 1995, was issued to purchase land adjacent to the University and is secured by the land. The note bears interest at a rate of 9.0%, with monthly installments of \$1,800, including interest, due through February 1, 2018.

**PACIFIC LUTHERAN UNIVERSITY**  
**NOTES TO FINANCIAL STATEMENTS**

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**Note 12 – Long-Term Debt (continued)**

The approximate principal and sinking fund payment requirements for all long-term debt for the five years subsequent to May 31, 2015 are:

2016	\$ 1,416,000
2017	1,488,000
2018	1,564,000
2019	1,638,000
2020	1,710,000
Thereafter	<u>55,414,995</u>
	<u>\$ 63,230,995</u>

**Note 13 – Operating Leases**

The University has an operating lease for equipment, which expired in June 2015. The University also has three building facility leases. One lease term expires in January 2022 with an option to renew for up to seven five-year lease terms. The other lease term expires in October 2017. Rental expense under these leases totaled \$517,300 and \$574,000 for the years ended May 31, 2015 and 2014, respectively.

KPLU-FM Pacific Lutheran University, a noncommercial radio station owned and operated by the University, has two operating leases for communications equipment and facilities through June 2020 and January 2021, respectively. Rental expense associated with these leases totaled \$237,500 and \$269,200 for the years ended May 31, 2015 and 2014, respectively.

Future minimum lease payments under operating leases as of May 31, 2015 are:

2016	\$ 797,703
2017	807,603
2018	831,824
2019	838,930
2020	804,322

**Note 14 – Deferred Gift Agreements**

The University has arrangements with donors classified as charitable lead trusts, charitable remainder trusts and charitable gift annuities. In general, under these arrangements the University receives a gift from a donor in which it has a remainder interest and agrees to pay the donor stipulated amounts over the life of the donor. The arrangement may cover one or more lives. The University invests and administers the related assets and makes distributions to the beneficiaries as required. When the agreement reaches the end of its term, remaining assets are retained by the University as unrestricted, temporarily restricted or permanently restricted net assets, or in some instances, distributed to third-party beneficiaries.

**Note 14 – Deferred Gift Agreements (continued)**

When a gift is received under one of these arrangements, it is split into the amount representing the actuarial present value of future distributions back to the donor and the remaining gift value to be retained for the benefit of the University or third-party beneficiaries. The actuarial liability is adjusted annually using actuarial tables appropriate for the type of arrangement, number of lives covered and age of the donor. The University used interest rates ranging from of 1.2% to 11.6% in making the calculations at May 31, 2015 and 2014.

The University received \$243,695 and \$13,811 of gift value relating to deferred gift agreements for the years ended May 31, 2015 and 2014, respectively. Total assets held by the University under deferred gift agreements totaled \$13,300,587 and \$12,846,347 at May 31, 2015 and 2014, respectively. The University maintains separate reserve funds adequate to meet future payments under its charitable gift annuity contracts as required by governing states' law. The total amount held in separate reserve funds was \$2,632,663 and \$2,832,968 as of May 31, 2015 and 2014, respectively.

**Note 15 – Concentration of Credit Risk**

Financial instruments that potentially subject the University to concentrations of credit risk consist principally of cash, investments, accounts receivable, notes receivable, real estate contracts receivable and other receivables. Cash and cash equivalents in excess of federally insured limits are subject to the usual risks of balances in excess of those limits. The majority of the University's cash and cash equivalents are on deposit with a single bank. Investments are diversified in order to limit credit risk. Investments are generally placed in a variety of managed funds administered by different investment managers in order to limit credit risk. Concentrations of credit risk with respect to the real estate contracts receivable are limited due to the University holding a secured position in these agreements. Student notes and receivables and other receivables are due from a variety of sources concentrated primarily in the northwestern United States. In addition, the University's students receive a substantial amount of support from state and federal student financial assistance programs, which are subject to audit by governmental agencies. A significant reduction in the level of this support, if this were to occur, could have an adverse effect on the University's programs and activities.

**Note 16 – Related-Party Transactions**

**Garfield Commons, LLC** – The University entered into an agreement, effective April 20, 2006, to form Garfield Commons, LLC, a commercial retail project located in Parkland two blocks from the University's main entrance. The University has a 49% ownership interest in Garfield Commons, and applies the equity method of accounting for its investment. The other investee, Lorig/Garfield Commons, LLC, a Washington limited liability company, has a 51% ownership in the partnership. The property upon which the commercial building was constructed constituted the University's capital contribution in Garfield Commons. As part of the agreement, the University's bookstore became a tenant of the building in the summer of 2007. Terms of a separate lease agreement between the University, as a lessee and Garfield Commons, as the lessor, commenced at that time (see Note 13). At May 31, 2015 and 2014, the University's investment in Garfield Commons, LLC, totaled \$1,476,071 and \$1,519,112, respectively, and is included as real estate in Endowment Investments (see Note 7).

**Note 16 – Related-Party Transactions (continued)**

**Garfield North, LLC** – The University entered into an operating agreement with Garfield Partners, LLC (GP), a Washington limited liability company, effective October 17, 2011, to form Garfield North, LLC, a retail, commercial and residential project (Garfield Station) located in Parkland two blocks from the University's main entrance. The original agreement was amended on April 5, 2012 and July 18, 2013. As provided for in the operating agreement, as amended, the parties agreed to make specified capital contributions to Garfield North on or before July 26, 2013. In April 2012, the agreed upon value of the property to be contributed by the University was determined to be \$1,080,000 and the agreed upon value for the property to be contributed by GP was determined to be \$1,023,000.

The University contributed an additional \$500,000 in cash as part of its capital contributions and GP contributed an additional \$4,220,000 in cash as part of its capital contributions.

Following its capital contributions to Garfield North, the University has a 29% ownership interest, and is applying the equity method of accounting for its investment. GP has a 71% ownership. A spouse of a member of the University's Board of Regents (the related party) is a partner in GP. In addition, five members of the University's Board of Regents are personally invested in GP. At May 31, 2015 and 2014, the University's investment in Garfield North, LLC, totaled \$500,000 and is included as real estate in Endowment Investments (see Note 7).

Under the terms of the agreement, as amended, the University provided financing to Garfield North in the form of a loan in the amount of \$1,000,000. Interest is at 3%. Principal payments of \$150,000 shall be made annually until the loan is paid in full, unless sufficient funds are not available to pay the full \$150,000, in which case the balance shall be added to the amount to be paid in the next year. The loan is jointly and severally guaranteed by GP, the related party and another entity in an amount equal to their 71% of the loan. In addition, and as specified in the partnership agreement, the related party's construction company is acting as the general contractor on the construction contract. Construction on Garfield Station was completed during fiscal year ended May 31, 2015. At May 31, 2015 and 2014, the amount due from Garfield North, LLC, totaled \$1,000,000 and is included as other receivables on the statements of financial position.

The University has a contract totaling approximately \$600,000 with a construction company owned by the spouse of a member of the Board of Regents to complete tenant improvements in University leased property in Garfield Station. The contract was approved in accordance with the Board of Regents' conflict of interest policy. At May 31, 2015 and 2014, the University owed \$104,400 and \$207,000, respectively, on the contract, which was included in accounts payable on the statements of financial position.

Contributions receivable from non-compensated board members at May 31, 2015 and 2014 were \$30,500 and \$153,735, respectively. Gifts from non-compensated board members totaled \$192,325 and \$389,221 at May 31, 2015 and 2014, respectively.

**Note 17 – Commitments and Contingencies**

**Regulation and litigation** – The University receives funding or reimbursement from governmental agencies for various activities which are subject to numerous laws and regulations of federal, state, and local governments. Compliance with these laws and regulations can be subject to government review and interpretation, as well as regulatory actions. The University is subject to such regulatory reviews and, while these reviews may result in repayments and/or civil remedies, management believes, based on its current knowledge and information, that such repayments and/or civil remedies, if any, would not have a material effect on the University's financial position.

As of May 31, 2015 and 2014, the University is not currently involved in legal proceedings arising in the ordinary course of operations. In the opinion of management, there are no matters that will materially affect the University's financial position.

**Note 18 – Subsequent Events**

Subsequent events are events or transactions that occur after the statement of financial position date but before financial statements are issued. The University recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the statement of financial position, including the estimates inherent in the process of preparing the financial statements. The University's financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the statement of financial position but arose after the statement of financial position date and before financial statements are available to be issued.

On November 13, 2015 the University signed a letter of intent (LOI) to sell its broadcasting rights and facilities associated with the University's radio station, KPLU, to the University of Washington's radio station, KUOW. The purchase price for KPLU and its assets is set in the LOI at \$8 million, comprised of \$7 million in cash and \$1 million of underwriting announcements over 10 years. The sale excludes a number of assets including, but not limited to, equipment and facilities located on the University's campus in Parkland, Washington. The University and the University of Washington expect to sign a full asset purchase agreement on or before January 15, 2016. The final sale is subject to FCC approval.

The University has evaluated subsequent events through January 14, 2016, which is the date the financial statements are available to be issued.