

# **TEXAS LUTHERAN UNIVERSITY**

FINANCIAL STATEMENTS  
Including Independent Auditors' Report

As of and for the Years Ended May 31, 2016 and 2015

# TEXAS LUTHERAN UNIVERSITY

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## INDEPENDENT AUDITORS' REPORT

To the Board of Regents  
Texas Lutheran University  
Seguin, Texas

We have audited the accompanying financial statements of Texas Lutheran University (the "University"), which comprise the statements of financial position as of May 31, 2016 and 2015, and the related statements of activities and cash flows for the years 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.

### ***Auditors' Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits 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 auditors' 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 we have 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 Texas Lutheran University as of May 31, 2016 and 2015, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*Baker Tilly Virchow Krause, LLP*

Minneapolis, Minnesota  
October 6, 2016

**TEXAS LUTHERAN UNIVERSITY**

**STATEMENTS OF FINANCIAL POSITION**

As of May 31, 2016 and 2015

<b>ASSETS</b>		
	2016	2015
Cash and cash equivalents	\$ 4,619,113	\$ 6,692,126
Receivables		
Student accounts, net of allowance for doubtful accounts	192,941	233,070
Contributions, net	1,653,402	2,590,627
Other	349,782	354,747
Inventories	368,061	366,286
Other assets	1,742,624	1,733,589
Student loans receivable, net	3,868,555	3,996,952
Investments	76,320,444	81,608,265
Mineral rights and royalties, net	4,391,622	4,777,117
Funds administered by third parties	12,016,122	11,180,736
Cash - restricted	3,282,047	3,071
Property, plant and equipment, net	52,506,320	53,921,062
<b>TOTAL ASSETS</b>	<b>\$ 161,311,033</b>	<b>\$ 167,457,648</b>
<b>LIABILITIES AND NET ASSETS</b>		
<b>LIABILITIES</b>		
Accounts payable	\$ 673,551	\$ 635,603
Payroll related liabilities	2,711,813	2,463,917
Deposits and other unearned revenue	1,593,567	1,552,073
Liabilities related to split-interest agreements	2,593,743	2,713,227
Other accrued liabilities	545,892	600,428
Asset retirement obligations	895,941	826,180
Advances from U.S. Government for student loans	2,979,164	2,910,026
Bonds payable, net	24,251,373	25,430,564
Total Liabilities	36,245,044	37,132,018
<b>NET ASSETS</b>		
Unrestricted	50,744,913	53,206,785
Temporarily restricted	14,851,484	18,451,162
Permanently restricted	59,469,592	58,667,683
Total Net Assets	125,065,989	130,325,630
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<b>\$ 161,311,033</b>	<b>\$ 167,457,648</b>

See accompanying notes to financial statements.

**TEXAS LUTHERAN UNIVERSITY**

STATEMENT OF ACTIVITIES  
For the Year Ended May 31, 2016  
With Comparative Totals for 2015

	2016			Total	2015 Total
	Unrestricted	Temporarily Restricted	Permanently Restricted		
<b>REVENUES, GAINS AND OTHER SUPPORT</b>					
Tuition and fees	\$ 35,144,827	\$ -	\$ -	\$ 35,144,827	\$ 32,507,975
Less: Scholarship allowances	(20,199,499)	-	-	(20,199,499)	(18,287,309)
Net tuition and fees	14,945,328	-	-	14,945,328	14,220,666
Investment return	(1,703,617)	(1,209,526)	(223,362)	(3,136,505)	18,521,147
Contributions	2,124,239	2,446,233	1,843,342	6,413,814	6,233,494
Government and private grants	2,948,286	-	-	2,948,286	2,146,275
Change in value of split interest agreements	43,826	(12,769)	862,778	893,835	(127,479)
Auxiliary enterprises	7,329,756	-	-	7,329,756	6,847,274
Gain on sale of property	1,052,828	-	-	1,052,828	-
Other revenue	1,155,015	-	-	1,155,015	1,304,762
	<u>27,895,661</u>	<u>1,223,938</u>	<u>2,482,758</u>	<u>31,602,357</u>	<u>49,146,139</u>
Net assets released from restrictions	4,823,616	(4,823,616)	-	-	-
Reclassification of net assets	1,680,849	-	(1,680,849)	-	-
Total Revenues, Gains and Other Support	<u>34,400,126</u>	<u>(3,599,678)</u>	<u>801,909</u>	<u>31,602,357</u>	<u>49,146,139</u>
<b>EXPENSES</b>					
Instruction	11,629,419	-	-	11,629,419	11,341,486
Academic support	2,614,044	-	-	2,614,044	2,806,047
Public service	642,911	-	-	642,911	545,558
Research	43,102	-	-	43,102	43,897
Student services	6,703,866	-	-	6,703,866	6,438,930
Institutional support	8,555,961	-	-	8,555,961	8,939,268
Development and fund-raising	1,345,801	-	-	1,345,801	1,250,093
Auxiliary enterprises	5,326,894	-	-	5,326,894	5,192,838
Total Expenses	<u>36,861,998</u>	<u>-</u>	<u>-</u>	<u>36,861,998</u>	<u>36,558,117</u>
<b>Change in Net Assets</b>	(2,461,872)	(3,599,678)	801,909	(5,259,641)	12,588,022
Net Assets - Beginning of Year	<u>53,206,785</u>	<u>18,451,162</u>	<u>58,667,683</u>	<u>130,325,630</u>	<u>117,737,608</u>
<b>NET ASSETS - END OF YEAR</b>	<u>\$ 50,744,913</u>	<u>\$ 14,851,484</u>	<u>\$ 59,469,592</u>	<u>\$ 125,065,989</u>	<u>\$ 130,325,630</u>

See accompanying notes to financial statements.

**TEXAS LUTHERAN UNIVERSITY**

STATEMENT OF ACTIVITIES  
For the Year Ended May 31, 2015

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>REVENUES, GAINS AND OTHER SUPPORT</b>				
Tuition and fees	\$ 32,507,975	\$ -	\$ -	\$ 32,507,975
Less: Scholarship allowances	(18,287,309)	-	-	(18,287,309)
Net tuition and fees	14,220,666	-	-	14,220,666
Investment return	17,182,647	1,253,934	84,566	18,521,147
Contributions	1,144,779	3,717,790	1,370,925	6,233,494
Government and private grants	2,146,275	-	-	2,146,275
Change in value of split interest agreements	(217,314)	(6,744)	96,579	(127,479)
Auxiliary enterprises	6,847,274	-	-	6,847,274
Other revenue	1,304,762	-	-	1,304,762
	42,629,089	4,964,980	1,552,070	49,146,139
Net assets released from restrictions	3,806,752	(3,806,752)	-	-
<b>Total Revenues, Gains and Other Support</b>	<b>46,435,841</b>	<b>1,158,228</b>	<b>1,552,070</b>	<b>49,146,139</b>
<b>EXPENSES</b>				
Instruction	11,341,486	-	-	11,341,486
Academic support	2,806,047	-	-	2,806,047
Public service	545,558	-	-	545,558
Research	43,897	-	-	43,897
Student services	6,438,930	-	-	6,438,930
Institutional support	8,939,268	-	-	8,939,268
Development and fund-raising	1,250,093	-	-	1,250,093
Auxiliary enterprises	5,192,838	-	-	5,192,838
<b>Total Expenses</b>	<b>36,558,117</b>	<b>-</b>	<b>-</b>	<b>36,558,117</b>
<b>Change in Net Assets</b>	<b>9,877,724</b>	<b>1,158,228</b>	<b>1,552,070</b>	<b>12,588,022</b>
Net Assets - Beginning of Year	43,329,061	17,292,934	57,115,613	117,737,608
<b>NET ASSETS - END OF YEAR</b>	<b>\$ 53,206,785</b>	<b>\$ 18,451,162</b>	<b>\$ 58,667,683</b>	<b>\$ 130,325,630</b>

See accompanying notes to financial statements.

TEXAS LUTHERAN UNIVERSITY

STATEMENTS OF CASH FLOWS  
For the Years Ended May 31, 2016 and 2015

	2016	2015
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Change in net assets	\$ (5,259,641)	\$ 12,588,022
Adjustments to reconcile change in net assets to net cash flows from operating activities		
Depreciation and amortization	3,256,374	3,040,878
Accretion of asset retirement obligations	51,876	47,815
Net realized and unrealized (gains) losses on investments	3,959,266	(15,718,650)
Gain on sale of property	(1,052,828)	-
Gifts and grants restricted for long-term purposes - plant	(1,477,621)	(2,164,708)
Gifts and grants restricted for long-term purposes - endowment	(1,768,945)	(1,368,781)
Change in value of split-interest agreements	(567,116)	506,633
(Increase) decrease in assets		
Receivables	478,696	(844,338)
Inventories	(1,775)	(51,937)
Other assets	(9,035)	12,456
Increase (decrease) in liabilities		
Accounts payable	(39,856)	147,868
Payroll related liabilities	247,896	95,739
Deposits and other unearned revenue	41,494	(17,285)
Other accrued liabilities	(54,536)	25,771
Net Cash Flows From Operating Activities	<u>(2,195,751)</u>	<u>(3,700,517)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Proceeds from sales and maturities of investments	4,792,023	25,423,142
Purchases of investments	(3,213,077)	(7,395,980)
Disbursement of student loans	(341,345)	(530,903)
Proceeds from repayment of student loans	469,742	679,837
Proceeds from sale of property, plant, and equipment	1,988,128	-
Purchases of property and equipment	(2,655,434)	(6,048,430)
Change in cash - restricted	<u>(3,278,976)</u>	<u>(1,099)</u>
Net Cash Flows From Investing Activities	<u>(2,238,939)</u>	<u>12,126,567</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Repayments of principal on bonds payable	(1,205,000)	(1,160,000)
Proceeds on long-term line of credit	-	2,290,000
Repayments of principal on long-term line of credit	-	(5,725,000)
Proceeds from short-term borrowings	3,000,000	8,225,000
Payments of short-term borrowings	(3,000,000)	(8,975,000)
Restricted gifts and grants proceeds for long-term purposes - plant	1,974,294	1,214,887
Restricted gifts and grants proceeds for long-term purposes - endowment	1,775,895	1,355,266
Payments to annuitants	(252,650)	(265,525)
Advances from U.S. Government	69,138	90,874
Net Cash Flows From Financing Activities	<u>2,361,677</u>	<u>(2,949,498)</u>
<b>Net Change in Cash and Cash Equivalents</b>	<u>(2,073,013)</u>	<u>5,476,552</u>
CASH AND CASH EQUIVALENTS - Beginning of Year	<u>6,692,126</u>	<u>1,215,574</u>
<b>CASH AND CASH EQUIVALENTS - END OF YEAR</b>	<u>\$ 4,619,113</u>	<u>\$ 6,692,126</u>
Supplemental disclosures of cash flow information		
Cash paid for interest, net of capitalized interest of \$39,458 in 2015	\$ 971,438	\$ 1,071,479
Property, plant, and equipment additions in accounts payable	\$ 129,865	\$ 52,061

See accompanying notes to financial statements.



# TEXAS LUTHERAN UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS As of and for the Years Ended May 31, 2016 and 2015

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### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

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Texas Lutheran University ("the University") is an independent institution providing graduate and undergraduate education in a variety of programs. The University has an enrollment averaging approximately 1,300 students. The main campus and administrative offices are located in Seguin, Texas. The University is supported primarily by tuition and fees from students.

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

**Net Asset Classifications** - For the purposes of financial reporting, the University classifies resources into three net asset categories pursuant to any donor-imposed restrictions and applicable law. Accordingly, the net assets of the University are classified in the accompanying financial statements in the categories that follow:

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

**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.

**Unrestricted Net Assets** - Net assets not subject to donor-imposed stipulations. Unrestricted net assets may be designated for specific purposes by actions of the Board. In 2016 the Board designated funds of \$1.5 million for the Performing Arts Center.

Revenues from sources other than contributions are generally reported as increases in unrestricted net assets. Expenses are reported as decreases in unrestricted net assets. Investment income and gains and losses on investments are reported in the statement of activities as increases and decreases in unrestricted net assets unless their use is temporarily or permanently restricted by explicit donor stipulations or by law. Investment income and gains received with donor-imposed restrictions that are met in the same year as received are reported as revenues of the unrestricted net asset class. Investment income and gains earned on donor restricted funds that are classified as temporarily restricted net assets are reclassified as unrestricted net assets when expenses are incurred for their intended purpose.

In the absence of donor stipulations or law to the contrary, losses on the investments of a donor-restricted endowment fund reduce temporarily restricted net assets to the extent that donor-imposed temporary restrictions on net appreciation of the fund have not been met before the loss occurs. Any remaining loss reduces unrestricted net assets. If losses reduce the assets of a donor-restricted endowment fund below the level required by the donor stipulations or law, gains that restore the fair value of the assets of the endowment fund to the required level are classified as increases in unrestricted net assets.

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. Contributions received with donor-imposed restrictions that are met in the same year as received are reported as revenues of the unrestricted net asset class. Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassifications between the applicable classes of net assets. Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met.

# TEXAS LUTHERAN UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS As of and for the Years Ended May 31, 2016 and 2015

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### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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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.

Government grants received from the Department of Education and the State of Texas in which the agency has placed limitations on the use of the resources are reported as unrestricted revenues when grants are awarded to students because the limitations are not considered donor-imposed restrictions.

***Tuition and Fees and Auxiliary Enterprises Revenues*** - Tuition revenue is recognized in the period the classes are provided. Revenue from auxiliary enterprises is recognized when goods or services are provided. Financial assistance in the form of scholarships and grants that cover a portion of tuition, living and other costs is reflected as a reduction of tuition and fees revenues.

***Cash and Cash Equivalents and Restricted Cash*** - The University considers all highly liquid investments with an initial maturity of three months or less, except for those held in the investment portfolio, to be cash and cash equivalents.

Restricted cash is cash from donors held for funding capital projects and cash held as required for certain grants until appropriate expenditures occur.

***Student Accounts Receivable*** - The University's student accounts receivable are due from students. Credit is extended to students and collateral is not required. Student accounts receivable are due at the end of the semester and are stated at amounts due from students net of an allowance for doubtful accounts. Accounts inactive (no payments have been received) for more than six months are considered past due. The University does not charge interest on past due accounts. The University determines its allowance based on accounts that have been inactive for over 360 days. The University writes off student accounts receivable when they become uncollectible, and payments subsequently received on such receivables are credited to the allowance for doubtful accounts. Students whose accounts are not current are not allowed to enroll in classes.

***Inventories*** - Bookstore inventories are valued using the retail method, which approximates cost and is not in excess of market. Other inventories consist of supplies and are carried at the lower of cost (first-in, first-out) or market.

***Other Assets*** - The University's other assets consist of life insurance - cash surrender values, a health insurance trust, other prepaids and other assets.

***Investments*** - Investments in publically traded securities are stated at fair value based on quoted market prices from national security exchanges. Other investments, for which quoted prices are not available, are stated at fair value as estimated by management using values provided by external investment managers or general partners. Land held for investment and privately held stock is recorded at the fair value on the date of the contribution. Certificates of deposit are recorded at cost. Cash held in transition for investments are included in investments and are recorded at fair value, which approximates cost.

# TEXAS LUTHERAN UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS As of and for the Years Ended May 31, 2016 and 2015

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### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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**Mineral Rights and Royalties** - Mineral rights and royalties are valued at estimated fair value. The University of Texas has estimated the value of certain oil and gas assets for which Texas Lutheran University holds 5% of this interest and the University of Texas holds the remaining 95%. The University is following the valuation methodology used by the University of Texas, and valued the 5% interest in these oil and gas assets at \$4,391,622 and \$4,777,117 at May 31, 2016 and 2015, respectively.

**Beneficial Interest in Trusts** - The University receives assets that will be divided between the University and other beneficiaries upon the death of the donor. Investments held in these split-interest agreements are stated at fair value. The net realized and unrealized gains (losses) in market value of investments are reflected as change in value of split-interest agreements in the statement of activities.

**Property, Plant and Equipment, Net** - Property, plant and equipment are stated at cost or fair value at the date of gift if donated, less accumulated depreciation. The University capitalizes items in excess of \$5,000 with a useful life of at least three years. Depreciation is provided on the straight-line method over estimated useful lives as follows: buildings 10-50 years, improvements other than building 10-20 years, software 3-10 years and equipment 3-20 years.

**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. As of May 31, 2016 and 2015, there have been no such losses.

**Unearned Revenue** - Unearned revenue, primarily tuition and fees, consists of payments received before services or products are provided to the payer. Tuition and fees are normally recognized as revenues at the beginning of each semester. The portion of payments received relating to future services or products are recorded as unearned revenue.

**Assets and Liabilities Related to Split-Interest Agreements** - Under charitable gift annuity and charitable remainder trust agreements, the University agrees to pay a donor an annuity in consideration for a specific gift. For these types of agreements, assets are generally recorded at fair value when received with a liability recognized equal to the present value of amounts which the University expects to pay to annuity beneficiaries. Changes in the calculated liability due to increases or decreases in the actuarially determined life expectancy of annuity beneficiaries are reflected as change in value of split-interest agreements in the statement of activities. To calculate the present value of the gift annuities, life expectancy tables with discount rates ranging from 1.2% to 7.4% were used.

Total assets held by the University under split interest agreements totaled \$841,615 and \$1,105,683 at May 31, 2016 and 2015, respectively. The University did not receive new gifts under split interest agreements for the years ended May 31, 2016 and 2015.

**TEXAS LUTHERAN UNIVERSITY**

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

**NOTE 1 - 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. When the liability is initially recorded, the cost of the retirement obligation is capitalized by increasing the carrying value of the related asset. Over time, the liability is accreted to its present value each year and the capitalized cost associated with the retirement obligation is depreciated over the useful life of the related asset. Upon settlement of the obligation, any difference between the cost to settle the asset retirement obligation and the liability recorded is recognized as a gain or loss in the statement of activities. The University reviews its estimates annually and adjusts the recorded liability as needed.

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, 2016 and 2015 are as follows:

	2016	2015
Balance, Beginning of the year	\$ 826,180	\$ 778,365
Accretion expense	51,876	47,815
Additions	17,885	-
Balance, End of the year	\$ 895,941	\$ 826,180

**Advances from U. S. Government for Student Loans** - Funds provided by the United States Government under the Federal Perkins Loan Program 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. 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.

**Advertising Expenses** - Advertising expenses approximated \$355,000 and \$370,000 for the years ended May 31, 2016 and 2015, respectively. Advertising costs are expensed when incurred.

**Income Taxes** - The University is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code according to an Internal Revenue Service determination letter dated November 1961. Accordingly, the University is not subject to federal income taxes except to the extent it derives income from certain activities not substantially related to its tax-exempt purposes (unrelated trade or business activities). The University had no material unrelated business income during the year.

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, 2016 and 2015. The University's tax returns are subject to review and examination by federal authorities.

# TEXAS LUTHERAN UNIVERSITY

## NOTES TO FINANCIAL STATEMENTS As of and for the Years Ended May 31, 2016 and 2015

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### NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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**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.

**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.

**Concentrations of Credit Risk** - Financial instruments that potentially subject the University to concentrations of credit risk consist principally of cash and cash equivalents, receivables and investments. Cash and cash equivalents in excess of federally insured limits are subject to the usual risks of balances in excess of those limits. At May 31, 2016, approximately 94% of the University's cash and cash equivalents are on deposit with two banks. Investments are generally placed in a variety of managed funds administered by different investment managers in order to limit credit risk. At May 31, 2016, approximately 58% of the University's investments are held by one custodian. Other receivables are due from a variety of sources concentrated primarily in the Southern 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.

**New Accounting Pronouncements** - In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, *Revenue from Contracts with Customers*. This new accounting guidance outlines a single comprehensive model for entities to use in accounting for revenue from contracts with customers. ASU No. 2014-09 is effective for fiscal years beginning after December 15, 2017. Early application is permitted for fiscal years beginning after December 15, 2016. The University is assessing the impact this new standard will have on its financial statements.

In April 2015, FASB issued ASU 2015-03, *Interest- Imputation of interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs*. Under the new guidance, debt issuance costs related to a recognized debt liability are presented as a direct reduction to the carrying amount of that debt liability. ASU 2015-03 is effective for fiscal years beginning after December 15, 2015, with early adoption permitted. The University elected to adopt the guidance in fiscal 2016. ASU 2015-03 is to be applied retrospectively, and as a result, the guidance was retrospectively applied to fiscal 2015. The adoption of the standard did not have a significant impact on the University's statement of financial position or results of operations.

In May 2015, FASB issued ASU 2015-07, *Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*. Under the new guidance, investments measured at net asset value, as a practical expedient for fair value, are excluded from the fair value hierarchy disclosure requirements. For non-public business entities, ASU 2015-07 is effective for fiscal years beginning after December 15, 2016 with early application permitted. The University elected to adopt the guidance in fiscal 2016. ASU 2015-07 is to be applied retrospectively, and as a result, the guidance was retrospectively applied to fiscal 2015. The adoption of the standard did not have a significant impact on the University's statement of financial position or results of operations.

TEXAS LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

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**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

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***New Accounting Pronouncements (continued)*** - In January 2016, FASB issued ASU 2016-01, *Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*. This new guidance is intended to improve the recognition and measurement of financial instruments and eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost for Institutions that are not public business entities. ASU 2016-01 is effective for fiscal years beginning after December 15, 2018, with early adoption permitted for fiscal years beginning after December 15, 2017. However, the new guidance permits entities that are not public business entities to adopt upon issuance the provision that eliminates the requirement to disclose the fair value of financial instruments measured at amortized cost. The University elected to adopt this provision in fiscal 2016. ASU 2016-01 is to be applied by means of a cumulative-effect adjustment to the statement of financial position as of the beginning of the fiscal year of adoption. The amendments related to equity securities without readily determinable fair values (including disclosure requirements) should be applied prospectively to equity investments that exist as of the date of adoption of ASU 2016-01. The University is assessing the impact the remainder of this standard will have on its financial statements.

In February 2016, FASB issued ASU No. 2016-02, *Leases*. ASU No. 2016-02 was issued to increase transparency and comparability among entities. Lessees will need to recognize nearly all lease transactions (other than leases that meet the definition of a short-term lease) on the statement of financial position as a lease liability and a right-of-use asset (as defined). Lessor accounting under the new guidance will be similar to the current model. ASU No. 2016-02 is effective for fiscal years beginning after December 15, 2018. Early application is permitted. Upon adoption, lessees and lessors will be required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach, which includes a number of optional practical expedients that entities may elect to apply. The University is assessing the impact this standard will have on its financial statements.

In August 2016, FASB issued ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. The new guidance improves and simplifies the current net asset classification requirements and information presented in financial statements and notes that is useful in assessing a not-for-profit's liquidity, financial performance and cash flows. ASU 2016-14 is effective for fiscal years beginning after December 15, 2017, with early adoption permitted. ASU 2016-14 is to be applied retroactively with transition provisions. The University is assessing the impact this standard will have on its financial statements.

TEXAS LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

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**NOTE 2 - FAIR VALUE MEASUREMENTS**

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**Fair Value Hierarchy** - 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 - Inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity can access at the measurement date.

Level 2 - Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. This includes quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, or market-corroborated data.

Level 3 - Inputs are unobservable for the asset or liability. Unobservable inputs reflect the assumptions that market participants would use in pricing the asset or liability (including assumptions about risk) using the best information available in the circumstances, which may include using the reporting entity's own data.

**Valuation Techniques and Inputs**

Level 1 - Level 1 assets include investments in short-term investments (consisting primarily of money market funds) and bond and equity mutual funds for which quoted prices are readily available.

Level 2 - Level 2 assets include:

- > Investments in short-term investments, bond and equity mutual funds and a natural resource fund 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.

Level 3 - Level 3 assets include:

- > Mineral rights and royalties, net, for which quoted prices are not readily available. The University of Texas has valued certain oil and gas assets, of which Texas Lutheran University holds 5% interest, based on current production through June 2015 and 2014, respectively, future production with a decline curve to July 2044, effective fair market oil and gas prices, and an annual discount factor to arrive at the net present value of the geological estimates over the decline period.
- > Funds administered by a third party for which quoted prices are not readily available. The fair values are estimated using an income approach by calculating the present value of the future distributions expected to be received based on a combination of Level 2 inputs (interest rates and yield curves) and significant unobservable inputs (entity specific estimates of cash flows).

TEXAS LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

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**NOTE 2 - FAIR VALUE MEASUREMENTS (CONTINUED)**

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***Valuation Techniques and Inputs (continued)***

Transfers between levels of the fair value hierarchy are considered to be made as of the beginning of the fiscal year. There were no such transfers during the years ended May 31, 2016 and 2015.

Certain mutual funds and alternative investments are measured at fair value using the net asset value (NAV) per share (or its equivalent) of such investment funds as a practical expedient for fair value. The University has estimated the fair value of these funds by using the net asset value provided by the investee. The University adopted ASU 2015-07, *Disclosures for Investment in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*, during the year ended May 31, 2016. Under the new guidance, investments measured using the net asset value per share (or its equivalent) practical expedient are not classified in the fair value hierarchy.

Except for the implementation of ASU 2015-7, there have been no changes in the techniques and inputs used as of May 31, 2016, and 2015.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

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.



**TEXAS LUTHERAN UNIVERSITY**

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

**NOTE 2 - FAIR VALUE MEASUREMENTS (CONTINUED)**

The following table presents financial instruments that are measured at fair value on a recurring basis as of May 31, 2016:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total May 31, 2016</u>
<b>ASSETS</b>				
Investments				
Short-term investments	\$ 3,073,201	\$ -	\$ -	\$ 3,073,201
Mutual funds - bond funds				
U.S. fixed income	4,745,946	-	-	4,745,946
Global fixed income	2,286,747	-	-	2,286,747
Other fixed income	7,374	359,683	-	367,057
Mutual funds - equity funds				
U.S. equities	21,816,150	274,768	-	22,090,918
Non-U.S. equities	12,442,222	-	-	12,442,222
Natural resource fund	-	1,916,404	-	1,916,404
Total investments	<u>44,371,640</u>	<u>2,550,855</u>	-	<u>46,922,495</u>
Mineral rights and royalties, net	-	-	4,391,622	4,391,622
Funds administered by third parties	-	-	<u>12,016,122</u>	<u>12,016,122</u>
Subtotal assets by valuation hierarchy	<u>\$ 44,371,640</u>	<u>\$ 2,550,855</u>	<u>\$ 16,407,744</u>	<u>63,330,239</u>
Investments measured using NAV				
Alternative investments				
Private equity funds				3,564,681
Real asset funds				2,879,659
Hedge funds				14,928,197
Limited partnership				4,338,392
Offshore fund				<u>3,682,520</u>
Subtotal assets by NAV				<u>29,393,449</u>
Total assets at fair value				<u>\$ 92,723,668</u>

**TEXAS LUTHERAN UNIVERSITY**

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

**NOTE 2 - FAIR VALUE MEASUREMENTS (CONTINUED)**

The following table presents financial instruments that are measured at fair value on a recurring basis as of May 31, 2015:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total May 31, 2015</u>
<b>ASSETS</b>				
Investments				
Short-term investments	\$ 12,939,482	\$ 8,491	\$ -	\$ 12,947,973
Mutual funds - bond funds				
U.S. fixed income	7,567,233	-	-	7,567,233
Global fixed income	3,692,762	-	-	3,692,762
Other fixed income	9,533	230,958	-	240,491
Mutual funds - equity funds				
U.S. equities	25,929,228	526,830	-	26,456,058
Non-U.S. equities	12,426,135	-	-	12,426,135
Natural resource fund	-	2,208,794	-	2,208,794
Total investments	<u>62,564,373</u>	<u>2,975,073</u>	-	<u>65,539,446</u>
Mineral rights and royalties, net	-	-	4,777,117	4,777,117
Funds administered by third parties	-	-	<u>11,180,736</u>	<u>11,180,736</u>
Subtotal assets by valuation hierarchy	<u>\$ 62,564,373</u>	<u>\$ 2,975,073</u>	<u>\$ 15,957,853</u>	<u>81,497,299</u>
Investments measured using NAV				
Alternative investments				
Private equity funds				3,745,314
Real asset funds				2,733,031
Hedge funds				9,585,974
Subtotal assets by NAV				<u>16,064,319</u>
Total assets at fair value				<u>\$ 97,561,618</u>

The following table presents a reconciliation of the statement of financial position amounts for financial instruments measured at fair value on a recurring basis using significant unobservable inputs (level 3) for the year ended May 31, 2016:

	<u>Balance May 31, 2015</u>	<u>Transfers in (out)</u>	<u>Purchases</u>	<u>Sales/ Distributions</u>	<u>Realized gains</u>	<u>Unrealized gains (losses)</u>	<u>Balance May 31, 2016</u>
<b>Assets</b>							
Mineral rights and royalties, net	\$ 4,777,117	\$ -	\$ -	\$ -	\$ -	\$ (385,495)	\$ 4,391,622
Funds administered by third parties	<u>11,180,736</u>	-	<u>338,613</u>	<u>(201,546)</u>	<u>20,944</u>	<u>677,375</u>	<u>12,016,122</u>
	<u>\$ 15,957,853</u>	<u>\$ -</u>	<u>\$ 338,613</u>	<u>\$ (201,546)</u>	<u>\$ 20,944</u>	<u>\$ 291,880</u>	<u>\$ 16,407,744</u>

The amount of total gains for the period included in change in net assets attributable to the change in unrealized gains or losses relating to assets measured at fair value still held at May 31, 2016

\$ 291,880

**TEXAS LUTHERAN UNIVERSITY**

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

**NOTE 2 - FAIR VALUE MEASUREMENTS (CONTINUED)**

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

	Balance May 31, 2014	Transfers in (out)	Purchases	Sales/ Distributions	Realized gains	Unrealized losses	Balance May 31, 2015
<b>Assets</b>							
Mineral rights and royalties, net	\$ 4,878,092	-	-	-	-	\$ (100,975)	\$ 4,777,117
Funds administered by third parties	<u>11,232,452</u>	-	<u>317,880</u>	<u>(227,769)</u>	<u>99,924</u>	<u>(241,751)</u>	<u>11,180,736</u>
	<u>\$ 16,110,544</u>	<u>\$ -</u>	<u>\$ 317,880</u>	<u>\$ (227,769)</u>	<u>\$ 99,924</u>	<u>\$ (342,726)</u>	<u>\$ 15,957,853</u>

The amount of total losses for the period included in change in net assets attributable to the change in unrealized gains or losses relating to assets measured at fair value still held at May 31, 2015 \$ (342,726)

The University uses the net asset value ("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.

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, 2016:

Investment Type	Unfunded Commitments	Fair Value	Redemption Frequency	Redemption Notice Period	Remaining Life (Years)
Alternative Investments					
Private equity funds (a)	\$ 1,659,574	\$ 3,564,681	Not redeemable	N/A	1 to 10
Real asset funds (b)	1,188,000	2,879,659	Not redeemable/ Quarterly	N/A	1 to 12
Hedge funds (c)	-	14,928,197	Last day of fiscal year or anniversary date subject to lock up period	100 days	N/A
Limited partnership (d)	-	4,338,392	Last day of calendar month	30 days	N/A
Offshore fund (e)	-	<u>3,682,520</u>	Last day of calendar month	30 days	N/A
<b>Total</b>	<u>\$ 2,847,574</u>	<u>\$ 29,393,449</u>			

(a) Comprised of various private equity funds. The primary objectives of these funds are to achieve long-term returns and capital appreciation through investments in a diversified portfolio of private equity limited partnerships and closed-end private funds focused on investment partnerships. The investment is not redeemable. Instead, distributions are received through the liquidation of the underlying assets of the fund.

(b) Comprised of various real asset funds which invest in real estate, infrastructure, natural resources or income producing timberlands. Real asset strategies generally seek to capitalize on transitional real estate assets and build/maintain exposures to hard assets expected to protect against long-term inflation. The total fair value of \$2,879,659 consists of \$982,830 that is non-redeemable and \$1,896,829 that is redeemable on a quarterly basis.

TEXAS LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

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**NOTE 2 - FAIR VALUE MEASUREMENTS (CONTINUED)**

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- (c) Comprised of various hedge funds which seek to protect capital in down markets and produce high return in the context of reasonable volatility. Hedge fund investments primarily consist of long/short equity and absolute return strategies. Funds can be redeemed on the last day of the fiscal year or anniversary date, subject to a lock up period, with 100 days written notice.
- (d) Comprised of a limited partnership fund. The objective of this fund is to seek long-term capital appreciation by investing primarily in equity securities of issuers located outside the United States. Funds can be redeemed on the last day of each calendar month with thirty days written notice.
- (e) Comprised of an offshore fund which invests in equity securities. The primary objective of this fund is to achieve maximum total return. Funds can be redeemed on the last day of each calendar month with thirty days written notice

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**NOTE 3 - STUDENT ACCOUNTS RECEIVABLE**

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The University's student accounts receivable relate to tuition and fees for student attendance as well as room and board charges. At May 31, student accounts receivable consisted of the following:

	<u>2016</u>	<u>2015</u>
Student accounts receivable - gross	\$ 1,368,772	\$ 1,366,587
Less allowance for doubtful accounts		
Beginning of year	(1,133,517)	(1,053,060)
Increases	<u>(42,314)</u>	<u>(80,457)</u>
End of year	<u>(1,175,831)</u>	<u>(1,133,517)</u>
Student accounts receivable, net	<u>\$ 192,941</u>	<u>\$ 233,070</u>

**TEXAS LUTHERAN UNIVERSITY**

NOTES TO FINANCIAL STATEMENTS  
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**NOTE 4 - CONTRIBUTIONS RECEIVABLE**

Contributions receivable consist of the following unconditional promises to give as of May 31:

	2016	2015
Contributions receivable - gross	\$ 1,757,006	\$ 2,748,129
Less unamortized discount	(9,617)	(20,096)
	1,747,389	2,728,033
Less allowance for doubtful accounts	(93,987)	(137,406)
Contributions receivable, net	\$ 1,653,402	\$ 2,590,627

The maturity of contributions receivable at May 31, 2016 is as follows:

Less than one year	\$ 1,196,256
One to five years	560,750
Total contributions receivable - gross	\$ 1,757,006

At May 31, 2016 and 2015, promises due in one to five years were discounted using interest rates ranging between 1.2% and 2.4%. Promises due in less than one year were not discounted. At May 31, 2016, 30% of the outstanding balance was due from one donor.

**NOTE 5 - CREDIT QUALITY OF STUDENT LOANS RECEIVABLE**

The University issues uncollateralized loans to students based on financial need. Student loans are funded through a Federal government loan program. Student notes 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 May 31, 2016 and 2015, student loans represented 2.4% of total assets.

At May 31, student loans receivable consisted of the following:

	2016	2015
Federal government programs	\$ 4,079,555	\$ 4,207,952
Less allowance for doubtful accounts:		
Beginning of year	(211,000)	(211,000)
Change	-	-
End of year	(211,000)	(211,000)
Student loans receivable, net	\$ 3,868,555	\$ 3,996,952

Perkins Loan funds advanced by the Federal government totaled \$2,979,164 and \$2,910,026 at May 31, 2016 and 2015, respectively, are ultimately refundable to the government and are classified as liabilities in the statement of financial position.

**TEXAS LUTHERAN UNIVERSITY**

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

**NOTE 5 - CREDIT QUALITY OF 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 Loan Program receivables may be assigned to the U.S. Department of Education. Students may be granted a deferment, forbearance, or cancellation of their student loan receivable based on eligibility requirements defined by the U.S. Department of Education.

At May 31, 2016 and 2015, the following amounts were past due under student loan programs:

	Amounts Past Due			
	1-60 days	60-90 days	90+ days	Total
May 31,				
2016	\$ 10,148	\$ 2,456	\$ 752,099	\$ 764,703
2015	9,651	1,531	721,604	732,786

**NOTE 6 - INVESTMENTS**

Investments consist of the following as of May 31:

	2016	2015
Investment - at fair value		
Short-term investments	\$ 3,073,201	\$ 12,947,973
Mutual funds - bond funds	7,399,750	11,500,486
Mutual funds - equity funds	34,533,140	38,882,193
Alternative investments	29,393,449	16,064,319
Natural resource fund	1,916,404	2,208,794
	76,315,944	81,603,765
Investments - at cost or original gift value		
Land held for investment	4,500	4,500
Total investments	\$ 76,320,444	\$ 81,608,265

The following summarizes total investment return for the year ended May 31:

Dividend, interest and royalty income, net of fees of \$225,000 and \$151,000 for 2016 and 2015, respectively	\$ 822,761	\$ 2,802,497
Net realized gains on sales of investments	890,603	22,610,858
Net unrealized (losses) gains on investments	(4,849,869)	(6,892,208)
	\$ (3,136,505)	\$ 18,521,147

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 such changes could materially affect the amounts reported in the financial statements.

The net investment return on alternative investments and the natural resource fund was \$(1,241,763) and \$600,337 for the years ended May 31, 2016 and 2015, respectively.

**TEXAS LUTHERAN UNIVERSITY**

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

**NOTE 7 - PROPERTY, PLANT AND EQUIPMENT, NET**

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

	2016	2015
Buildings	\$ 61,497,424	\$ 61,359,318
Improvements other than buildings	22,095,080	21,062,104
Software	1,521,950	1,403,571
Equipment	15,133,312	14,215,331
	100,247,766	98,040,324
Less accumulated depreciation	(51,918,474)	(48,751,220)
	48,329,292	49,289,104
Construction in progress	531,427	143,729
Land	3,645,601	4,488,229
Total property, plant and equipment, net	\$ 52,506,320	\$ 53,921,062

**NOTE 8 - BONDS PAYABLE, NET**

Bonds and notes payable consist of the following as of May 31:

	2016	2015
City of Seguin Higher Education Facilities Corporation Higher Education Revenue and Refunding Bonds (Texas Lutheran University Project), Series 2004	\$ 380,000	\$ 745,000
The City of Terrell Hills, Texas Higher Education Facilities Corporation Higher Education Revenue Bonds (Texas Lutheran University Project), Series 2007	5,865,000	6,230,000
City of Olmos Park, Texas Higher Education Facilities Corporation Higher Education Revenue Bonds (Texas Lutheran University Project), Series 2011	8,740,000	9,070,000
City of Olmos Park, Texas Higher Education Facilities Corporation Higher Education Revenue Bonds (Texas Lutheran University Project), Series 2013	9,530,000	9,675,000
Total bonds payable	24,515,000	25,720,000
Debt issuance costs, net of accumulated amortization	(263,627)	(289,436)
Total bonds payable, net	\$ 24,251,373	\$ 25,430,564

TEXAS LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

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**NOTE 8 - BONDS PAYABLE, NET (CONTINUED)**

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The University has the following bonds outstanding:

City of Seguin Higher Education Facilities Corporation Higher Education Revenue and Refunding Bonds (Texas Lutheran University Project), Series 2004 - Tax-exempt bonds used for renovation of residence halls and student apartments, parking facilities and student activity building, with semi-annual interest payments ranging from 4.5% to 5.0% due each March 1<sup>st</sup> and September 1<sup>st</sup>. The final principal payment of \$380,000 is due September 2016.

City of Terrell Hills, Texas Higher Education Facilities Corporation Higher Education Revenue Bonds (Texas Lutheran University Project), Series 2007 - Tax-exempt bonds used for renovation of the University HVAC system with semi-annual interest payments ranging from 4.17% to 4.81% due each March 1<sup>st</sup> and September 1<sup>st</sup>. Annual principal payments ranging from \$380,000 to \$625,000 are due September 2016 through September 2027.

City of Olmos Park, Texas Higher Education Facilities Corporation Higher Education Revenue Bonds (Texas Lutheran University Project), Series 2011 - Tax-exempt bonds used for construction of new residence hall, with semi-annual interest payments of 4.34% due each March 1<sup>st</sup> and September 1<sup>st</sup>. Annual principal payments ranging from \$345,000 to \$845,000 are due September 2016 through September 2031.

City of Olmos Park, Texas Higher Education Facilities Corporation Higher Education Revenue Refunding Bonds (Texas Lutheran University Project), Series 2013 - Tax-exempt bonds with semi-annual interest payments of 2.70% due each March 1<sup>st</sup> and September 1<sup>st</sup>. Annual principal payments ranging from \$145,000 to \$610,000 are due September 2016 through September 2022, with a \$5,940,000 balloon payment due September 2023.

The bond agreements include certain nonfinancial covenants. At May 31, 2016 and 2015, the University was in compliance with those covenants.

Aggregate maturities of bonds and notes payable at May 31:

2017	\$ 1,250,000
2018	1,295,000
2019	1,345,000
2020	1,395,000
2021	1,450,000
Thereafter	<u>17,780,000</u>
	<u>\$ 24,515,000</u>

The University adopted ASU 2015-03, *Interest- Imputation of interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs*, during the year ended May 31, 2016. Under the new guidance, debt issuance costs related to a recognized debt liability are presented as a direct reduction to the carrying amount of that debt liability. As required by the new guidance, the amendments were applied retrospectively to the year ended May 31, 2015.

Debt issuance costs consist of costs incurred in connection with bond financing and are amortized using the straight-line method which approximates the effective interest rate over the term of the bonds. Amortization expense was approximately \$25,800 for each of the years ended May 31, 2016 and 2015.



TEXAS LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

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**NOTE 8 - BONDS PAYABLE, NET (CONTINUED)**

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The University has the following lines of credit available:

At May 31, 2016, the University had a \$4,000,000 operating line of credit agreement with a bank. The interest rate is at the floating prime rate plus 0.25% and was 3.75% at May 31, 2016. Interest only payments are due monthly. The line of credit matures on March 2, 2017. There was no outstanding balance at May 31, 2016 and 2015.

At May 31, 2016, the University had a \$5,725,000 secured line of credit agreement with a bank to finance the construction cost of an athletic facility construction project. The line of credit is secured by board-designated endowment funds totaling approximately \$9,130,000. The interest rate is at the three month London Interbank Offered Rate plus 2.50% and was 3.12% at May 31, 2016. Interest only payments are due monthly. The line of credit matures on October 25, 2018. There was no outstanding balance at May 31, 2016 and 2015.

Interest expense was approximately \$959,000 and \$1,060,000 for the years ended May 31, 2016 and 2015, respectively. There was no interest capitalized for the year ended May 31, 2016. Interest of approximately \$39,000 was capitalized for the year ended May 31, 2015.

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**NOTE 9 - NET ASSETS**

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Permanently restricted net assets consist of the following categories as of May 31:

	<u>2016</u>	<u>2015</u>
Pooled endowment	\$ 46,882,059	\$ 45,230,518
Split-interest agreements	11,811,357	10,963,201
Annuity contracts, contributions receivable and other assets held for endowment	<u>776,176</u>	<u>2,473,964</u>
	<u>\$ 59,469,592</u>	<u>\$ 58,667,683</u>

The income generated from permanently restricted net assets is used for scholarships and University operations.

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

	<u>2016</u>	<u>2015</u>
Gifts and other unexpended revenues and gains available for:		
Scholarships, instruction and other support - operating	\$ 2,701,130	\$ 1,939,473
Scholarships, instruction and other support - endowment	8,839,101	13,666,913
Acquisition of buildings and equipment	2,961,457	2,028,203
Contributions receivable - operating and restricted	145,032	599,039
Split-interest agreements	<u>204,764</u>	<u>217,534</u>
	<u>\$ 14,851,484</u>	<u>\$ 18,451,162</u>

TEXAS LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

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**NOTE 9 - NET ASSETS (CONTINUED)**

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Net assets were released from temporary donor restrictions during the years ended May 31, 2016 and 2015 by incurring expenses satisfying the restricted purpose or by occurrence of events specified by the donor as follows:

	<u>2016</u>	<u>2015</u>
Scholarships, instruction and other support	\$ 4,415,582	\$ 3,491,627
Property, plant and equipment acquired and placed into service	<u>408,034</u>	<u>315,125</u>
	<u>\$ 4,823,616</u>	<u>\$ 3,806,752</u>

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**NOTE 10 - ENDOWMENT**

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The University's endowment consists of approximately 640 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 generally accepted accounting principles ("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.

**Interpretation of Relevant Law** - The University's governing board has interpreted the Texas enacted version of Uniform Prudent Management of Institutional Funds Act (UPMIFA) as allowing the University to appropriate for expenditure or accumulate so much of an endowment fund as the University determines is prudent for the uses, benefits, purposes and duration for which the endowment fund is established, subject to the intent of the donor as expressed in the gift instrument. Unless stated otherwise in the gift instrument, the assets in an endowment fund shall be donor-restricted assets until appropriated for expenditure by the Board of Regents. See Note 1 for further information on net asset classifications. The remaining portion of the donor-restricted endowment fund that is not classified as permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the University in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the University considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

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

The University's endowment net assets include funds invested in the University's investment pool and excludes net assets related to contributions receivable, funds administered by others and annuities.

**TEXAS LUTHERAN UNIVERSITY**

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

**NOTE 10 - ENDOWMENT (CONTINUED)**

Endowment net asset composition by type of fund consists of the following as of May 31, 2016:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ -	\$ 8,839,101	\$ 46,882,059	\$ 56,721,160
Board-designated endowment funds	<u>19,752,530</u>	<u>-</u>	<u>-</u>	<u>19,752,530</u>
Total endowment net assets	<u>\$ 19,752,530</u>	<u>\$ 8,839,101</u>	<u>\$ 46,882,059</u>	<u>\$ 75,473,690</u>

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	\$ -	\$ 13,666,913	\$ 45,230,518	\$ 58,897,431
Board-designated endowment funds	<u>21,542,824</u>	<u>-</u>	<u>-</u>	<u>21,542,824</u>
Total endowment net assets	<u>\$ 21,542,824</u>	<u>\$ 13,666,913</u>	<u>\$ 45,230,518</u>	<u>\$ 80,440,255</u>

Changes in endowment net assets for the year ended May 31, 2016 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, May 31, 2015	\$ 21,542,824	\$ 13,666,913	\$ 45,230,518	\$ 80,440,255
Investment return:				
Investment income	257,034	578,590	-	835,624
Net depreciation - realized and unrealized	<u>(794,356)</u>	<u>(1,788,115)</u>	<u>-</u>	<u>(2,582,471)</u>
Total investment return	<u>(537,322)</u>	<u>(1,209,525)</u>	<u>-</u>	<u>(1,746,847)</u>
Additions to endowment	75,270	-	1,651,541	1,726,811
Appropriation of endowment assets for expenditure	<u>(1,328,242)</u>	<u>(3,618,287)</u>	<u>-</u>	<u>(4,946,529)</u>
Endowment net assets, May 31, 2016	<u>\$ 19,752,530</u>	<u>\$ 8,839,101</u>	<u>\$ 46,882,059</u>	<u>\$ 75,473,690</u>

**TEXAS LUTHERAN UNIVERSITY**

NOTES TO FINANCIAL STATEMENTS  
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**NOTE 10 - ENDOWMENT (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	\$ 22,511,716	\$ 15,766,837	\$ 42,788,447	\$ 81,067,000
Investment return:				
Investment income	370,200	2,047,424	-	2,417,624
Net depreciation - realized and unrealized	<u>(143,473)</u>	<u>(793,490)</u>	<u>-</u>	<u>(936,963)</u>
Total investment return	226,727	1,253,934	-	1,480,661
Additions to endowment	93,780	-	1,442,071	1,535,851
Transfer to endowment	-	-	1,000,000	1,000,000
Appropriation of endowment assets for expenditure	<u>(1,289,399)</u>	<u>(3,353,858)</u>	<u>-</u>	<u>(4,643,257)</u>
Endowment net assets, May 31, 2015	<u>\$ 21,542,824</u>	<u>\$ 13,666,913</u>	<u>\$ 45,230,518</u>	<u>\$ 80,440,255</u>

**Funds with Deficiencies** - From time to time, the fair value of assets associated with individual donor-restricted pooled endowment funds may fall below the level that the donor or UPMIFA requires the University to retain as a fund of perpetual duration. There were no deficiencies of this nature that are reported in unrestricted net assets as of May 31, 2016 and 2015, respectively.

**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(s) as well as board-designated funds. Under this policy, as approved by the governing board, the endowment assets follow the asset allocation policy that diversifies investments among several asset provide an average annual rate between 7% and 8% annually. 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 equity-based 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 of appropriating for distribution of 6.5% for each of the years ending in 2016 and 2015 of its endowment fund's average fair value over the prior 12-quarters moving average of the market value of the pooled endowment through the calendar year-end preceding the fiscal year in which the distribution is planned. In establishing this policy, the University considered the long-term expected return on its endowment. Accordingly, over the long term, the University expects the current spending policy to allow its endowment to grow at an average of 1% to 2% annually. 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.

**TEXAS LUTHERAN UNIVERSITY**

NOTES TO FINANCIAL STATEMENTS  
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**NOTE 11 - EMPLOYEE BENEFIT PLANS**

The University has a contributory defined contribution retirement plan covering academic and nonacademic personnel who have one year of service and are employed at least half-time. Contributions for employees are based on a percentage of compensation. Contributions to the retirement plan amounted to approximately \$702,000 and \$703,000 for the years ended May 31, 2016 and 2015, respectively.

The University also provides medical benefits through a self-funded health plan. Specific and aggregate stop loss coverage on the health plan is provided to limit the ultimate exposure of the University. A liability is provided for claims incurred but not reported. Management reviews this accrual on an on-going basis and believes it is adequate to cover such claims. The balance of the accrual at May 31, 2016 and 2015 was \$263,000 and \$282,000, respectively.

**NOTE 12 - OPERATING LEASES**

The University leases certain equipment under non-cancelable operating leases expiring through July 2018. Total rental expenses approximated \$190,000 and \$207,000 for the years ended May 31, 2016 and 2015, respectively. Future minimum rentals under non-cancelable operating leases with terms of more than one year are as follows:

2017	\$	137,100
2018		41,880
2019		<u>5,914</u>
	<b>\$</b>	<b><u>184,894</u></b>

**NOTE 13 - SUPPLEMENTAL SCHEDULE OF EXPENSES**

The following table presents the allocation of operations and maintenance to the functional expenses as of May 31, 2016:

	Functional Expenses	Allocations	Total
<b>EXPENSES</b>			
Instruction	\$ 9,070,824	\$ 2,558,595	\$ 11,629,419
Academic support	2,002,611	611,433	2,614,044
Public service	610,377	32,534	642,911
Research	25,018	18,084	43,102
Student services	6,320,443	383,423	6,703,866
Institutional support	7,122,379	1,433,582	8,555,961
Development and fund-raising	1,310,676	35,125	1,345,801
Auxiliary enterprises	<u>2,951,523</u>	<u>2,375,371</u>	<u>5,326,894</u>
Total Expenses	<u>\$ 29,413,851</u>	<u>\$ 7,448,147</u>	<u>\$ 36,861,998</u>

TEXAS LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS  
As of and for the Years Ended May 31, 2016 and 2015

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**NOTE 13 - SUPPLEMENTAL SCHEDULE OF EXPENSES (CONTINUED)**

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The following table presents the allocation of operations and maintenance to the functional expenses as of May 31, 2015:

	<u>Functional Expenses</u>	<u>Allocations</u>	<u>Total</u>
EXPENSES			
Instruction	\$ 8,758,235	\$ 2,583,251	\$ 11,341,486
Academic support	2,185,434	620,613	2,806,047
Public service	512,541	33,017	545,558
Research	25,548	18,349	43,897
Student services	6,058,001	380,929	6,438,930
Institutional support	7,464,902	1,474,366	8,939,268
Development and fund-raising	1,214,438	35,655	1,250,093
Auxiliary enterprises	<u>2,781,808</u>	<u>2,411,030</u>	<u>5,192,838</u>
Total Expenses	<u>\$ 29,000,907</u>	<u>\$ 7,557,210</u>	<u>\$ 36,558,117</u>

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**NOTE 14 - COMMITMENTS AND CONTINGENCIES**

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The University participates in various federal loan programs. The amount of loans disbursed under the Federal Direct Loan Program for each of the years ending May 31, 2016 and 2015 approximated \$8,100,000 and \$7,500,000, respectively. The amount of loans disbursed under the Federal Perkins Loan Program for the years ended May 31, 2016 and 2015 was approximately \$341,000 and \$531,000, respectively. Amounts questioned as a result of audits, if any, may result in the University purchasing the loan(s) from the lender as the loan(s) may have lost its (their) guaranteed status. Management believes that such amounts, if any, would be immaterial to the financial statements.

Activity of the Federal Pell Grant program is not reflected in the statement of activities as the transactions are considered to be agency transactions. Students received approximately \$1,950,000 and \$2,200,000 from the Federal Pell Grant program for the years ended May 31, 2016 and 2015, respectively.

In order to participate in the various Federal Title IV financial aid programs, the U.S. Department of Education requires private nonprofit institutions to demonstrate financial responsibility by meeting certain ratio requirements. The University was in compliance with these requirements at May 31, 2016 and 2015.

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**NOTE 15 - SUBSEQUENT EVENTS**

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On August 19, 2016, the Board approved to move forward with the Performing Arts Center with a commitment of \$15.5 million for construction. To date, approximately \$5.7 million in gifts and pledges have been received and \$6 million from the sale of property and privately-held stock has been designated by the Board for the project.

The University has evaluated its financial statements for subsequent events through October 6, 2016 which is the date the financial statements were issued.