Baylor University

Financial Statements

Years Ended May 31, 2014 and 2013,
and Report of Independent Certified Public Accountants

BAYLOR UNIVERSITY

FINANCIAL STATEMENTS

Years Ended May 31, 2014 and 2013

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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

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The Board of Regents
Baylor University

Report on the financial statements
We have audited the accompanying financial statements of Baylor University (the "University"), which comprise the balance sheets as of May 31, 2014 and 2013, 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.

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 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 Baylor University as of May 31, 2014 and 2013, 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.

GRANT THORNTON LLP

Dallas, Texas
September 24, 2014

BAYLOR UNIVERSITY
Balance Sheets

May 31, 2014 and 2013
(in thousands of dollars)

	2014	2013
ASSETS		
Cash & cash equivalents	$ 63,635	$ 103,424
Short-term investments	106,795	82,000
Bond proceeds held by trustees	540	125,966
Student accounts receivable, net	16,421	16,176
Contributions receivable, net	123,673	120,669
Grants & other receivables, net	23,918	29,471
Prepaid expenses & other	10,739	9,669
Student loans receivable, net	10,613	10,257
Long-term investments, at fair value	1,217,509	1,129,659
Property, plant & equipment, net	1,000,263	811,794
Total assets	**$ 2,574,106**	**$ 2,439,085**
LIABILITIES & NET ASSETS		
Liabilities		
Accounts payable	$ 61,127	$ 53,463
Personnel related current liabilities	20,578	19,704
Deposits & deferred revenue	81,004	74,642
Accrued postretirement benefits	48,227	59,605
Notes & bonds payable	624,777	631,789
Other liabilities	21,088	21,642
Total liabilities	**856,801**	**860,845**
Net Assets		
Unrestricted	518,650	483,639
Temporarily restricted	506,654	434,036
Permanently restricted	692,001	660,565
Total net assets	**1,717,305**	**1,578,240**
Total liabilities & net assets	**$ 2,574,106**	**$ 2,439,085**

See accompanying notes to financial statements.

BAYLOR UNIVERSITY
Statements of Activities

For the Years Ended May 31, 2014 and 2013
(in thousands of dollars)

	Year Ended May 31, 2014			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
OPERATING REVENUES				
Tuition & fees	$ 545,799	$ --	$ --	**$ 545,799**
Less scholarships	(222,135)	--	--	**(222,135)**
Net tuition & fees	323,664	--	--	**323,664**
Endowment distributions & investment income	51,352	7,468	--	**58,820**
Gifts & private grants	25,185	6,129	--	**31,314**
Grants & contracts	24,670	389	--	**25,059**
Other sources - educational & general	23,174	46	--	**23,220**
Other sources - intercollegiate athletics	40,642	--	--	**40,642**
Sales & services of auxiliary enterprises	56,227	--	--	**56,227**
Net assets released from restrictions	11,116	(11,116)	--	**--**
Total operating revenues	556,030	2,916	--	**558,946**
OPERATING EXPENSES				
Program expenses				
Instruction	225,333			**225,333**
Academic support	50,876			**50,876**
Research & public service	27,253			**27,253**
Student services & activities	115,544			**115,544**
Auxiliary enterprises	45,237			**45,237**
Support expenses				
Institutional support	67,764			**67,764**
Impairment of long-lived assets	15,384			**15,384**
Total operating expenses	547,391	--	--	**547,391**
Increase in net assets from operating activities	8,639	2,916	--	**11,555**
NON-OPERATING ACTIVITIES				
Return on long-term investments	23,963	86,089	5,749	**115,801**
Distributions from long-term investments	(12,310)	(48,685)	--	**(60,995)**
Endowment earnings & distributions re-invested	--	--	2,961	**2,961**
Change in value of split interest agreements	--	1,422	1,649	**3,071**
Gifts for annuity, living trusts & endowment	--	2,593	20,561	**23,154**
Gifts & grants for plant improvements	--	30,534	--	**30,534**
Net assets released from restrictions for plant improvements	7,678	(7,678)	--	**--**
Change in postretirement benefits obligation other than net periodic benefit cost	12,152	--	--	**12,152**
Other increases (decreases)	(5,111)	5,427	516	**832**
Total non-operating activities	26,372	69,702	31,436	**127,510**
Change in net assets	35,011	72,618	31,436	**139,065**
Net assets at beginning of year	483,639	434,036	660,565	**1,578,240**
Net assets at end of year	$ 518,650	$ 506,654	$ 692,001	**$ 1,717,305**

See accompanying notes to financial statements.

Year Ended May 31, 2013			
Unrestricted	**Temporarily Restricted**	**Permanently Restricted**	**Total**
$ 502,326	$ --	$ --	**$ 502,326**
(204,235)	--	--	**(204,235)**
298,091	--	--	**298,091**
50,507	6,868	--	**57,375**
17,693	5,851	--	**23,544**
21,717	699	--	**22,416**
21,859	73	--	**21,932**
39,235	--	--	**39,235**
50,829	--	--	**50,829**
9,851	(9,851)	--	**--**
509,782	3,640	--	**513,422**
219,335			**219,335**
50,618			**50,618**
20,051			**20,051**
106,017			**106,017**
39,347			**39,347**
64,791			**64,791**
--			**--**
500,159	--	--	**500,159**
9,623	3,640	--	**13,263**
31,427	87,333	6,449	**125,209**
(12,171)	(46,501)	--	**(58,672)**
--	--	2,101	**2,101**
86	1,931	3,047	**5,064**
--	1,467	23,457	**24,924**
--	91,812	--	**91,812**
4,465	(4,465)	--	**--**
(2,425)	--	--	**(2,425)**
2,507	236	822	**3,565**
23,889	131,813	35,876	**191,578**
33,512	135,453	35,876	**204,841**
450,127	298,583	624,689	**1,373,399**
$ 483,639	$ 434,036	$ 660,565	**$ 1,578,240**

BAYLOR UNIVERSITY
Statements of Cash Flows

For the Years Ended May 31, 2014 and 2013
(in thousands of dollars)

	Year Ended May 31, 2014	Year Ended May 31, 2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	**$ 139,065**	**$ 204,841**
Adjustments to reconcile change in net assets to net cash provided by (used for) operating activities:		
Depreciation	34,750	31,046
Return on long-term investments	(115,801)	(125,209)
Distributions from long-term investments	60,995	58,672
Amortization of bond premium	(902)	(953)
Impairment of long-lived assets	15,384	--
Losses on disposal of property & equipment	2,308	4,563
Fixed assets gifts-in-kind	(322)	(164)
Contributions for endowment & plant improvements	(50,682)	(108,730)
Provision for bad debts	687	2,087
Changes in assets & liabilities:		
Short-term investments	(24,795)	(46,242)
Student accounts receivable	(760)	(1,817)
Contributions receivable	(3,048)	(64,062)
Grants & other receivables	5,553	(5,759)
Prepaid expenses & other	(1,070)	(1,776)
Accounts payable	7,664	17,206
Personnel related current liabilities	874	1,670
Deposits & deferred revenue	6,362	13,015
Accrued postretirement benefits	(11,378)	6,756
Other liabilities	(557)	(4,194)
Net cash provided by (used for) operating activities	**64,327**	**(19,050)**
CASH FLOWS FROM INVESTING ACTIVITIES		
Student loans made	(1,507)	(855)
Proceeds from collections of student loans	1,023	845
Proceeds from sales of long-term investments	28,623	39,826
Purchases of long-term investments	(61,667)	(73,086)
Unexpended bond proceeds decrease (increase)	125,426	(21,497)
Purchases of property, plant & equipment	(240,589)	(175,399)
Net cash used for investing activities	**(148,691)**	**(230,166)**
CASH FLOWS FROM FINANCING ACTIVITIES		
Contributions for endowment & plant improvements:		
Endowment & Annuity/Living Trusts	23,148	24,922
Plant	27,534	83,808
Proceeds from long-term debt	--	200,652
Repayment of long-term debt	(6,110)	(5,961)
Increase in federal student loan funds refundable	3	14
Net cash provided by financing activities	**44,575**	**303,435**
Net change in cash & cash equivalents	**(39,789)**	**54,219**
Cash & cash equivalents at beginning of year	**103,424**	**49,205**
Cash & cash equivalents at end of year	**$ 63,635**	**$ 103,424**

See accompanying notes to financial statements.

OVERVIEW OF BAYLOR UNIVERSITY

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

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

While remaining true to its Christian heritage, the University has grown to over 15,500 students, and its nationally recognized academic units offer 141 undergraduate, 75 masters, and 36 doctoral degree programs. In addition, the education specialist degree is offered by the School of Education, and the Juris Doctor degree is offered by the School of Law.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting & Reporting

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

The financial statements of the University are prepared in conformity with accounting principles generally accepted in the United States of America (US GAAP). The University's net assets, revenues, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified as follows:

Unrestricted -- net assets that are not subject to donor-imposed or legal restrictions. Unrestricted net assets may be designated for specific purposes by the University's Board of Regents (the "Board").

Temporarily restricted -- net assets subject to donor-imposed or legal restrictions that must be met either by actions of the University and/or the passage of time.

Permanently restricted -- net assets subject to donor-imposed restrictions that the assets be maintained permanently. Generally, the donors of these assets permit the University to use all or part of the earnings on the related investments for general or specific purposes.

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

Fund Accounting

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

Cash & Cash Equivalents

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

Short-Term Investments

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

Student Accounts & Loans Receivable

Student accounts receivable are stated net of allowance for doubtful accounts of $835,000 and $866,000 as of May 31, 2014 and 2013, respectively.

Student loans receivable are stated net of allowance for doubtful accounts of $861,000 and $852,000 as of May 31, 2014 and 2013, respectively. The University considered the allowance recorded at May 31, 2014 and 2013 to be reasonable and adequate to absorb potential credit losses inherent in the student loan portfolio.

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

Split Interest Agreements

Split interest agreements consist primarily of gift annuities, charitable remainder trusts, life income funds, and perpetual trusts. Assets held under these agreements are included primarily in long-term investments (see Note 4). The agreements administered by the Baptist Foundation of Texas ("BFT") and others as temporary trustees, in which the assets will be distributed to the University upon termination, are reflected at their net present value as contributions receivable (see Note 5). Annuities payable are recorded at the present value of future payments, based on the Internal Revenue Service ("IRS") discount rate at the time of the original gift, and are included in other liabilities in the accompanying balance sheets.

Property, Plant & Equipment

Property, plant and equipment valued at $5,000 or more are recorded at cost at the date of acquisition or, if acquired by gift, at estimated fair value at the date of gift. Additions to plant assets are capitalized, while maintenance and minor renovations are charged to operations. Plant assets are reflected net of accumulated depreciation calculated on a straight-line basis over the estimated useful lives ranging from three to fifty years. Land and art/collections are considered non-depreciable given the nature of the assets. Equipment is removed from the records at the time of disposal.

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

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

Deposits & Deferred Revenue

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

Other Liabilities

Other liabilities consist of annuities payable, interest rate swap liability, liability for conditional asset retirement obligations, and federal student loan funds refundable.

Tuition & Fees

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

Contributions

Contributions are recorded as revenues in the appropriate net asset class based on donor-imposed restrictions. Expiration of temporary restrictions on donor contributions are reported as net assets released from restrictions. Contributions received with donor-imposed restrictions that are anticipated to be met in the same year as received are reported as revenues of the unrestricted net asset class.

Donor contributions to fund construction projects are classified as temporarily restricted net assets until the facility is placed in service. At that time, the temporarily restricted net assets are released from restriction and replenish unrestricted net asset balances designated for plant projects. The University follows the policy of recording contributions of long-lived assets directly as invested in plant assets. Donor contributions for the construction of a new football stadium and Business School facility totaled $12,505,000 and $74,209,000 for the years ended May 31, 2014 and 2013, respectively.

Contributions receivable are recorded at the present value of estimated future cash flows using a discount rate appropriate to the effective date of the gift agreement.

Functional Allocation of Expenses

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

Fundraising expenses of $16,566,000 and $13,067,000 incurred by the University in 2014 and 2013, respectively, are included primarily in the institutional support category in the statements of activities.

Use of Estimates & Assumptions

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

2. FAIR VALUE MEASUREMENTS

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

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

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

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

The estimated fair value of alternative assets managed and held in limited partnership or other private investment fund structures is based upon the practical expedient of the reported net asset values provided by the respective external investment fund managers, adjusted for cash flows through May 31. The University reviewed and evaluated the net asset values provided by the managers and agreed with the valuation methods and assumptions used to determine those values except in a few immaterial instances. In those limited instances, the University applied additional valuation procedures furnished by qualified third parties or incorporated additional related financial data provided by fund managers to arrive at a fair value different than manager provided values. When the University determines a different value, the investment is carried at the more conservative of the two values. Therefore, the University believes the carrying amount of these financial instruments is a reasonable estimate of the fair value. Because alternative assets are not readily marketable, their estimated value is subject to uncertainty and, therefore, may differ from the value that would have been used had a ready market for such investments existed.

The fair value of direct real estate holdings is determined from the most recent information available to the University (i.e., appraisals and/or property tax statements).

The fair value of mineral interests is estimated based on the expected net revenues generated by those assets. With certain holdings, geological reserve analysis can provide additional information for estimating fair value. For the years ended May 31, 2014 and 2013, the University utilized an engineering report and geological study of its largest mineral interest holding to obtain a more informed estimate of fair value and incorporated the results of the study into its estimate of expected net revenues and fair value for this holding.

The fair value of income interests/perpetual trusts is estimated based on the underlying assets contributed to the trusts.

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

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

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

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

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

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

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

3. ENDOWMENT

The University's endowment totals $1,151,201,000 and $1,061,157,000 as of May 31, 2014 and 2013, respectively, and is a component of the University's long-term investment pool. The endowment consists of $950,578,000 and $882,090,000 of donor-restricted endowment net assets and $200,623,000 and $179,067,000 of board designated endowment net assets as of May 31, 2014 and 2013, respectively. The management of the endowment is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA). The Board of the University has an established policy consistent with UPMIFA as adopted by the State of Texas. The University seeks to preserve the fair value of the original gift as of the gift date of the donor restricted endowment funds absent explicit donor stipulations to the contrary. Accordingly, the University classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor agreement at the time the accumulation is added to the fund. The remaining portion of the donor restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the University in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the University considers the following factors in making a determination to appropriate or accumulate donor restricted endowment funds:

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

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

Changes in endowment net assets for the year ended May 31, 2014 are as follows *(in thousands of dollars)*:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, May 31, 2013	$ 158,114	$ 266,647	$ 636,396	$ 1,061,157
Investment earnings, net of expenses	2,681	13,447	800	16,928
Net realized & unrealized gains on investments	16,569	72,671	7,788	97,028
Contributions	--	22	19,881	19,903
Terminated annuities & other	--	--	1,107	1,107
Transfers to board designated	7,763	5,666	--	13,429
Distributions	(9,666)	(48,685)	--	(58,351)
Endowment net assets, May 31, 2014	$ 175,461	309,768	665,972	1,151,201

Changes in endowment net assets for the year ended May 31, 2013 are as follows *(in thousands of dollars)*:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, May 31, 2012	$ 137,805	$ 224,114	$ 602,242	$ 964,161
Investment earnings, net of expenses	2,725	13,064	571	16,360
Net realized & unrealized gains on investments	23,515	74,665	7,839	106,019
Contributions	--	408	23,093	23,501
Terminated annuities & other	--	--	2,651	2,651
Transfers to board designated	3,597	897	--	4,494
Distributions	(9,528)	(46,501)	--	(56,029)
Endowment net assets, May 31, 2013	$ 158,114	$ 266,647	$ 636,396	$ 1,061,157

Funds totaling $2,669,000 and $4,971,000, which market values are less than original values, are reported in unrestricted net assets in the accompanying balance sheets as of May 31, 2014 and 2013, respectively.

Return Objectives & Risk Parameters

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

Spending Policy & How the Investment Objectives Relate to Spending Policy

The Baylor University Fund (“BUF”) is a unitized fund consisting of publicly traded equity and fixed income securities, alternative assets, and mineral rights; and serves as the primary investment vehicle for the University’s endowment and other long-term investments. As permitted under Texas law, the Board has adopted a spending policy for the BUF that authorizes a dividend to be paid for endowments participating in the BUF to be used for the purposes intended by donors. For the years ended May 31, 2014 and 2013, this dollar dividend per BUF unit was based on 5% of the previous 48-months’ rolling average net asset market value per unit of the BUF. The permitted change in this dividend amount from the previous year shall be no less than 0% and no more than 6%, and in no case shall the annual fiscal year distribution (dollar dividend amount per BUF unit) exceed 7% of the previous 48-months’ rolling average net asset market value per BUF unit. The dividend amount remained the same for the years ended May 31, 2014 and 2013. Endowment earnings distributed include endowment distributions in accordance with the University’s BUF spending policy, as well as, distributions of income from other endowment assets.

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

4. LONG-TERM INVESTMENTS

The University diversifies its investments among various financial instruments and asset categories and uses multiple investment strategies. As with most large endowments, these financial assets are managed primarily through external investment management firms selected and monitored by the University's Office of Investments and the Baylor Executive Investment Committee in accordance with the University's Endowment Investment Policy. The investment management firms are predominately organized in limited partnership, registered investment company (mutual fund), and trust format. At May 31, 2014 and 2013, excluding income interests and perpetual trusts, the University's long-term investments were invested with 86 and 79 different managers, respectively. Of those, alternative assets were invested with 72 and 65 managers, respectively.

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

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

Alternative assets consist of private equities, real assets, and hedge funds investments and are primarily held in partnership format. Capital is allocated to domestic and international markets in the various alternative investment funds. Most of the underlying assets in the private equity and real asset partnerships and trusts are not immediately liquid. Private equity fund strategies include buyouts, venture capital, distressed/special situations, emerging markets, and secondary markets. Real asset funds are predominately private limited partnerships investing in numerous types of properties and strategies such as commercial real estate, energy, power, and infrastructure, as well as timber and other natural resources and commodities including industrial and precious metals. Private equity and real asset funds are held as long-term investments and are structured as closed-end, commitment-based investment funds where the investor commits a specified amount of capital upon inception of the fund which is then drawn down over a specified period of the fund's life. These funds generally cannot be redeemed prior to the specified termination date and will only receive distributions upon a disposition of the underlying assets of the portfolio. As a limited partner, the University will not generally have any influence over the amount and timing of capital contributions and distributions. At May 31, 2014, the remaining life of private equity and real asset funds ranged from one to twelve years. Hedge fund investments are generally open-end funds structured in limited partnership format. These funds employ various investment strategies such as long/short equity, fundamental value, multi-strategy (including a small allocation to fund-of-funds), distressed asset and debt, and short credit. The amount of liquidity available to investors is directly related to the liquidity and risk associated with the underlying portfolio. Hedge funds typically offer subscription and redemption options to investors over time periods shorter than private equity/real asset funds; however, the frequency of subscriptions or redemptions is dictated by each fund's governing documents. Liquidity of individual hedge funds also varies due to illiquid "side-pocket" investments, as well as contractual restrictions on redemption such as gating and holdback provisions. Redemption terms of hedge funds range from monthly upon thirty day notice to rolling three years upon forty-five day notice. At May 31, 2014, of twenty-seven hedge funds totaling $264,311,000, nine funds totaling $12,547,000 have been suspended or gated; eight of these nine are in liquidation mode. These nine funds are included in level 3 assets as discussed in Note 2.

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

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

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

The following table presents information about the University's long-term investments that are measured at fair value as of May 31, 2014 and indicates the fair value hierarchy of the valuation techniques utilized to determine such fair value *(in thousands of dollars)*:

	Level 1	Level 2	Level 3	Total
Fixed income securities	$ 63,568	$ --	$ --	$ 63,568
Public equities	359,885	--	656	360,541
Alternative assets	--	161,471	412,302	573,773
Real estate & other	--	--	5,401	5,401
Mineral rights	--	--	27,595	27,595
Income interests/perpetual trusts	--	--	186,631	186,631
Total	$ 423,453	$ 161,471	$ 632,585	$ 1,217,509

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

The following table presents additional information about assets that have been measured at fair value as of May 31, 2014 on a recurring basis using significant unobservable inputs (Level 3) *(in thousands of dollars)*:

	May 31, 2013 Balance	Transfers In (Out) of Level 3	Additions	Distributions	Realized & Unrealized Gains (Losses)	May 31, 2014 Balance
Public equities	$ 667	$ --	$ --	$ --	$ (11)	$ 656
Alternative assets	358,182	(15,572)	110,184	(77,479)	36,987	412,302
Real estate & other	4,374	--	1,279	(174)	(78)	5,401
Mineral rights	26,461	--	5,514	(5,478)	1,098	27,595
Income interests/ perpetual trusts	172,463	--	2,273	(27)	11,922	186,631
Total	$ 562,147	$ (15,572)	$ 119,250	$ (83,158)	$ 49,918	$ 632,585

For the year ended May 31, 2014, transfers of $15,572,000 were made out of Level 3 into Level 2 based upon information related to investment asset fund structures, characteristics, holdings, and liquidity provisions. These transfers were valued using May 31, 2013 balances. There were no other transfers in or out of Levels 1, 2, or 3 for the year ended May 31, 2014.

The following table presents information about the University's long-term investments that are measured at fair value as of May 31, 2013 and indicates the fair value hierarchy of the valuation techniques utilized to determine such fair value *(in thousands of dollars)*:

	Level 1	Level 2	Level 3	Total
Fixed income securities	$ 70,952	$ --	$ --	$ 70,952
Public equities	311,198	--	667	311,865
Alternative assets	--	185,362	358,182	543,544
Real estate & other	--	--	4,374	4,374
Mineral rights	--	--	26,461	26,461
Income interests/perpetual trusts	--	--	172,463	172,463
Total	$ 382,150	$ 185,362	$ 562,147	$ 1,129,659

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

The following table presents additional information about assets that have been measured at fair value as of May 31, 2013 on a recurring basis using significant unobservable inputs (Level 3) *(in thousands of dollars)*:

	May 31, 2012 Balance	Transfers In (Out) of Level 3	Additions	Distributions	Realized & Unrealized Gains (Losses)	May 31, 2013 Balance
Public equities	$ 559	$ --	$ --	$ --	$ 108	$ 667
Alternative assets	405,254	(25,384)	47,491	(87,556)	18,377	358,182
Real estate & other	3,089	--	1,256	(1)	30	4,374
Mineral rights	29,553	--	5,525	(5,526)	(3,091)	26,461
Income interests/ perpetual trusts	156,475	--	5,668	(4,783)	15,103	172,463
Total	$ 594,930	$ (25,384)	$ 59,940	$ (97,866)	$ 30,527	$ 562,147

For the year ended May 31, 2013, transfers of $25,384,000 were made out of Level 3 into Level 2 based upon information related to investment asset fund structures, characteristics, holdings, and liquidity provisions. These transfers were valued using May 31, 2012 balances. There were no other transfers in or out of Levels 1, 2, or 3 for the year ended May 31, 2013.

Whereas the preceding tables reflect income interests and perpetual trusts separately based on fair value hierarchy, the following table reflects total investments, regardless of fair value hierarchy, using traditional classification descriptions as used by the University to manage its investment portfolio. Accordingly, the underlying assets of income interests/perpetual trusts are reflected within the traditional investment classifications. Additionally, alternative assets are reflected by major asset category. Estimated fair value of long-term investments as of May 31, 2014 and 2013, are as follows *(in thousands of dollars)*:

	2014	2013
Fixed income securities:		
Short term funds	$ 7,492	$ 10,453
Bonds	95,753	98,424
Public equities:		
Domestic	260,340	208,589
International	201,130	204,014
Alternative assets:		
Private equities	171,347	155,623
Hedge funds	278,262	234,932
Real assets	166,611	182,572
Mineral rights	36,574	35,052
Total	$ 1,217,509	$ 1,129,659

Long-term investments include operating, endowment, and annuity and life income assets. The annuity and life income assets under split-interest agreements total $26,892,000 and $23,954,000 as of May 31, 2014 and 2013, respectively.

The cost of long-term investments was $924,223,000 and $891,605,000 as of May 31, 2014 and 2013, respectively.

Return on long-term investments for the years ended May 31, 2014 and 2013, consist of the following *(in thousands of dollars)*:

	2014	2013
Investment earnings	$ 20,489	$ 19,987
Investment expenses	(4,297)	(3,795)
Net realized & unrealized gains	99,609	109,017
Total return on long-term investments	$ 115,801	$ 125,209

Investment earnings consist of interest income, dividends, mineral, and other earnings. Investment expenses include consulting, custodian, and direct investment management expenses.

Distributions from long-term investments include distributions of endowment assets invested in long-term investments as well as distributions from funds other than endowment that are included in the long-term investments pool. Endowment distributions and other distributions are included in endowment distributions & investment income in the statements of activities.

Both the return on long-term investments and distributions from long-term investments are shown under non-operating activities in the statements of activities.

As part of the University's alternative assets program, the University is obligated under certain limited partnership agreements to advance funding up to specified levels upon the request of the general partner. The University had unfunded commitments consisting of the following at May 31, 2014 and 2013, respectively, which are expected to be called over the next three years *(in thousands of dollars)*.

	2014	2013
Alternative assets:		
Private equities	$ 110,981	$ 107,496
Real assets	65,314	27,064
Total unfunded commitments	$ 176,295	$ 134,560

5. CONTRIBUTIONS RECEIVABLE

As gift pledges are made to the University, the intent of the donor, the circumstances surrounding the pledge and any action taken by the University in response to the pledge are considered in determining whether the pledge is an "intent to give" or an "unconditional promise to give." An unconditional promise to give is recorded as a contribution receivable at the present value of the estimated future cash flows. Unconditional promises to give related to split interest agreements are discounted based on life expectancies of the annuity recipients.

As of May 31, 2014 and 2013, contributions receivable consist of the following *(in thousands of dollars)*:

	2014	2013
Due in 1 year	$ 24,380	$ 23,001
Due in 2 to 5 years	64,261	68,681
Due in 6 to 10 years	24,978	19,082
Due in greater than 10 years	600	863
Split interest agreements	25,488	22,843
Less: Present value adjustment	(14,321)	(12,132)
Less: Allowance for uncollectible contributions receivable	(1,713)	(1,669)
Total contributions receivable, net	$ 123,673	$ 120,669

Contributions receivable expected to be fulfilled more than one year from the date of the financial statements are discounted at .33% to 2.89%, with the discount amortized over the life of the unconditional promise. At May 31, 2014, contributions receivable primarily consisted of unconditional promises related to the construction of a new football stadium, Business School facility, and other building projects, of which ten donors represented 61% of the total.

An intent to give is not recorded as gifts revenue until collected or converted to an unconditional promise to give. Intents to give totaled $34,417,000 and $29,535,000 as of May 31, 2014 and 2013, respectively. Payments on these intents to give are due in varying periods. Additionally, the University is the beneficiary under various wills and trust agreements of which the realizable amounts are not presently determinable. The University's share of such bequests is recorded when the University has an irrevocable right to the bequest and the proceeds are measurable.

6. PROPERTY, PLANT & EQUIPMENT

At May 31, 2014 and 2013, property, plant and equipment assets consist of the following *(in thousands of dollars)*:

	2014	2013
Land	$ 70,773	$ 73,823
Land/leasehold improvements	79,446	73,272
Buildings	813,882	744,213
Equipment	92,171	80,216
Arts/collections	11,469	10,915
Other	40,635	39,019
	1,108,376	1,021,458
Less accumulated depreciation	(385,227)	(375,826)
	723,149	645,632
Construction-in-progress	277,114	166,162
Property, plant & equipment, net	$ 1,000,263	$ 811,794

Depreciation expense was $34,750,000 and $31,046,000 as of May 31, 2014 and 2013, respectively. The "Equipment" category includes computers, software and other types of equipment above the $5,000 threshold. The "Other" category includes vehicles, library materials, and miscellaneous other assets. Real and personal property were insured for $1.4 billion at May 31, 2014. The liability for conditional asset retirement obligations was $4,037,000 and $3,809,000 as of May 31, 2014 and 2013, respectively, and is included in other liabilities in the accompanying balance sheets.

During the year ended May 31, 2014, the University determined that the carrying amount of the football stadium property being replaced by a new stadium was not recoverable. An impairment charge of $15,384,000 was recognized at May 31, 2014 in the statements of activities to reduce the value of the property to estimated fair value.

7. DEPOSITS & DEFERRED REVENUE

At May 31, 2014 and 2013, deposits and deferred revenue consist of the following *(in thousands of dollars)*:

	2014	2013
Tuition & fees	$ 34,837	$ 30,959
Student enrollment deposits	2,822	1,949
Intercollegiate athletics income	33,226	31,424
Sponsored research income	1,267	817
Rental & other income	8,852	9,493
Total deposits & deferred revenue	$ 81,004	$ 74,642

The deferred tuition and fees, student enrollment deposits, sponsored research, and other income will primarily be earned in the subsequent fiscal year. Intercollegiate athletics and rental deferred income includes advance ticket and event sales, football suite revenues, television income, advertising income, and rental contracts advance payments that will be earned over the next one to eleven years.

8. NOTES & BONDS PAYABLE

Notes and bonds payable consist of both non-interest bearing unsecured notes and interest bearing unsecured and secured notes, commercial paper with varying maturities, and bonds with varying terms and maturity dates to March 1, 2043. Interest payments on a cash basis totaled $26,700,000 and $21,177,000, and interest expense was $26,680,000 and $23,177,000 for the years ended May 31, 2014 and 2013, respectively. These amounts are exclusive of premium amortization. The amount of bond premium amortization that offset interest expense was $902,000 and $953,000 for the years ended May 31, 2014 and 2013, respectively. Interest expense (net of earnings) of $4,431,000 and $3,519,000 was capitalized to projects for the year ended May 31, 2014 and 2013, respectively.

As of May 31, 2014 and 2013, unamortized bond and commercial paper issuance costs of $4,103,000 and $4,302,000, respectively, were included in prepaid expenses and other in the University's balance sheets. Amortization expense for issuance costs was $199,000 and $177,000 for the years ended May 31, 2014 and 2013, respectively.

Notes and bonds payable at May 31, 2014 and 2013, consist of the following *(in thousands of dollars)*:

	2014	2013
Non-interest bearing unsecured note payable to a foundation, due in annual installments beginning June 30, 2004 to June 30, 2013	$ -	$ 500
Non-interest bearing unsecured note payable to a corporation, due in annual installments through July 31, 2022	2,348	2,658
Taxable Commercial Paper Notes, Series A, with varying maturities and discount rates rolled at each maturity	15,000	15,000
Series 2008A Waco Education Finance Corporation Tax-Exempt Variable Rate Demand Bonds, swapped to a fixed rate of 2.476% (see Note 10), interest payable monthly, principal payable annually to February 1, 2032	67,325	69,610
Series 2008C Waco Education Finance Corporation Tax-Exempt Fixed Rate Bonds, interest ranging from 5.0% to 5.25% payable semiannually, principal payable annually beginning March 1, 2019 to March 1, 2036	112,100	112,100
Series 2011 Clifton Higher Education Finance Corporation Tax-Exempt Fixed Rate Bonds, interest ranging from 3.0% to 5.25% payable semiannually, principal payable annually beginning March 1, 2012 to March 1, 2032	94,230	97,245
Series 2012 Waco Education Finance Corporation Tax-Exempt Fixed Rate Bonds, interest ranging from 4.125% to 5.00% payable semiannually, principal payable March 1, 2043	120,000	120,000
Series 2012A Baylor University Taxable Fixed Rate Bonds, bearing interest at 4.313% payable semiannually, principal payable March 1, 2042	200,000	200,000
Total notes & bonds payable prior to unamortized bond premium	611,003	617,113
Unamortized bond premium	13,774	14,676
Total notes & bonds payable	$ 624,777	$ 631,789

The fair values of notes and bonds payable were approximately $637,694,000 and $636,340,000 as of May 31, 2014 and 2013, respectively. These fair values were measured using Level 2 valuation techniques.

Bond premiums are being amortized using the effective interest method over the life of the bonds.

The Series 2008A Tax-Exempt Variable Rate Demand Bonds are subject to purchase upon tender with proper notice and delivery to the remarketing agent. On May 22, 2014, the University replaced its Standby Bond Purchase Agreement with an Irrevocable Transferable Letter of Credit (LOC). The direct-pay LOC, used for all debt service payments, is for a three-year term, renewable in May 2017, and includes a term out period of twenty equal quarterly installments.

During the year ended May 31, 2013, the University issued $200,000,000 of taxable bonds to provide funds for additions and improvements to facilities and infrastructure.

Excluding the maturity of commercial paper, scheduled principal payments on long-term notes and bonds for the periods subsequent to May 31, 2014, are as follows *(in thousands of dollars)*:

2015	$ 5,850
2016	6,130
2017	6,420
2018	6,715
2019	9,824
2020 and thereafter	561,064
Total	$ 596,003

The University has a taxable commercial paper program that provides for borrowings in the form of individual notes up to an aggregate of $50,000,000. The notes bear a fixed discount rate, established on the borrowing date, with no more than $15,000,000 maturing on any one day and maturities not to exceed 270 days. At May 31, 2014, the University had an outstanding balance of $15,000,000 in commercial paper notes with a discount rate of 0.16%. The University anticipates that the commercial paper will continue to be rolled at maturity until such time that it is refunded by long-term debt or repaid by the University.

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

9. NET ASSETS

The University's unrestricted, temporarily restricted, and permanently restricted net assets for the year ended May 31, 2014 are categorized by purpose as follows *(in thousands of dollars)*:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Unrestricted-designated for operations	$ 62,104	$ --	$ --	$ 62,104
Unrestricted-designated for plant	48,323	--	--	48,323
Restricted	--	17,125	5,862	22,987
Endowment	(2,669)	287,275	665,972	950,578
Endowment-Board designated	178,130	22,493	--	200,623
Annuity & living trusts	--	18,284	20,167	38,451
Invested in or restricted for plant	232,762	161,477	--	394,239
Total net assets	$ 518,650	$ 506,654	$ 692,001	$ 1,717,305

The University's unrestricted, temporarily restricted, and permanently restricted net assets for the year ended May 31, 2013 are categorized by purpose as follows *(in thousands of dollars)*:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Unrestricted-designated for operations	$ 40,185	$ --	$ --	$ 40,185
Unrestricted-designated for plant	45,657	--	--	45,657
Restricted	--	14,188	5,815	20,003
Endowment	(4,971)	250,665	636,396	882,090
Endowment-Board designated	163,085	15,982	--	179,067
Annuity & living trusts	--	14,529	18,354	32,883
Invested in or restricted for plant	239,683	138,672	--	378,355
Total net assets	$ 483,639	$ 434,036	$ 660,565	$ 1,578,240

10. DERIVATIVE FINANCIAL INSTRUMENTS

On June 11, 2010, the University entered into a swap arrangement with a financial institution counterparty in order to swap the University's Series 2008A variable rate demand bonds with an original balance of $75,860,000 as of May 31, 2010 for a fixed rate of 2.476% through February 1, 2032, in exchange for monthly payments equal to 68% of three-month London Interbank Offered Rate (LIBOR). The notional amount of the swap declines in accordance with the repayment of the Series 2008A bonds. The fair value of the University's interest rate swap liability was $3,962,000 and $4,871,000 at May 31, 2014 and 2013, respectively, and is included in other liabilities in the balance sheets. The gain on the change in the fair value of the interest rate swap was $909,000 and $3,572,000 for the years ended May 31, 2014 and 2013, respectively. The fair value was measured using Level 2 valuation techniques.

11. EXPENSES BY NATURAL CLASSIFICATION

While the statements of activities present expenses by function, the University's expenses by natural classification are as follows *(in thousands of dollars)*:

	2014	2013
Salaries & wages	$ 215,638	$ 200,042
Personnel benefits	66,233	67,732
Student wages & fellowships	26,839	26,250
Operating expenses	166,978	156,173
Depreciation & accretion	34,972	31,257
Impairment of long-lived assets	15,384	--
Interest on indebtedness	21,347	18,705
Total expenses	$ 547,391	$ 500,159

12. RETIREMENT PLAN

The University provides a defined contribution retirement income plan and a voluntary tax deferred annuity program for faculty and staff that are administered by outside sources. The defined contribution plan is not a matching plan. Retirement benefits equal the amount accumulated to each individual employee's credit at the date of retirement. The University's contributions to the plan for the years ended May 31, 2014 and 2013 were $20,489,000 and $19,352,000, respectively.

13. POSTRETIREMENT BENEFITS

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

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

Effective January 1, 2014, retirees age 65 and over transitioned from the existing medical benefits plan to a Health Reimbursement Arrangement to provide fixed annual contributions for medical expenses. This change resulted in a prior service cost decrease of $14,491,000 which is included in the change in postretirement benefits obligation in the statements of activities. Retirees age 65 and over, with twenty years of continuous, full-time service at the University as of May 31, 2007, continue to receive a Medicare Part B premium reimbursement.

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

	2014	2013
Change in benefit obligation:		
Measurement date	5/31/2014	5/31/2013
Accumulated postretirement benefit obligation (APBO) at beginning of year	$ 59,605	$ 52,849
Service cost	1,026	1,771
Interest cost	2,164	2,536
Plan participants' contributions	1,033	1,576
Plan changes	(14,491)	--
Actuarial (gain) loss	1,901	3,907
Retiree drug subsidy paid	146	191
Benefit payments	(3,157)	(3,225)
Accumulated postretirement benefit obligation (APBO) at end of year	$ 48,227	$ 59,605
Change in plan assets:		
Fair value of plan assets at beginning of year	$ --	$ --
Employer contributions	2,124	1,649
Plan participants' contributions	1,033	1,576
Benefit payments	(3,157)	(3,225)
Fair value of plan assets at end of year	$ --	$ --
Funded (unfunded) status of plan	$ (48,227)	$ (59,605)

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

	2014	2013
Transition obligation	$ --	$ --
Prior service cost (credit)	(12,591)	868
Net loss	19,287	17,981
Total	$ 6,696	$ 18,849

The University expects to amortize, from accumulated unrestricted net assets, $1,368,000 of prior service cost credits and $903,000 of net losses as components of net periodic benefit cost during the year ending May 31, 2015.

Weighted-average assumptions at measurement date:	5/31/2014	5/31/2013
Discount rate	4.36%	4.64%
Health care cost trend rate	8.00%	7.00%
Ultimate health care cost trend rate	5.00%	5.00%
Year ultimate trend rate reached	2020	2017

Beginning in 2018, 0.3% has been added to the health care cost trend rates for the expected effect of provisions of the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010, i.e. trend rates in 2018 are 6.3%. The inflation rates for retiree contributions are assumed to be the same as the medical cost inflation rates.

Plan contributions:

The University expects to contribute $1,984,000 to its postretirement benefit plan during the year ending May 31, 2015.

Projected cash flows:	Gross Benefit Payments Net of Employee Contributions	Gross Subsidy Receipts
2015 fiscal year	$ 1,984	$ --
2016 fiscal year	2,117	--
2017 fiscal year	2,232	--
2018 fiscal year	2,357	--
2019 fiscal year	2,469	--
2020-2024 fiscal years	14,233	--

Components of net periodic postretirement benefit cost:	6/1/2013-5/31/2014	6/1/2012-5/31/2013
Measurement date	5/31/2013	5/31/2012
Service cost	$ 1,026	$ 1,771
Interest cost	2,164	2,536
Amortization of:		
Transition obligation	--	274
Prior service cost	(1,032)	643
Actuarial loss	594	565
Net periodic postretirement benefit cost	$ 2,752	$ 5,789

Other changes in plan assets & benefit obligation recognized:		
Net actuarial loss	$ 1,901	$ 3,907
Prior service cost	(14,491)	--
Amortization of:		
Transition obligation	--	(274)
Prior service cost	1,032	(643)
Actuarial gain	(594)	(565)
Total (gain) loss recognized in net assets	$ (12,152)	$ 2,425
Total recognized in net assets & net periodic benefit cost	$ (9,400)	$ 8,214

Weighted-average assumptions for net periodic postretirement benefit cost:

Measurement date	5/31/2013 / 7/31/2013*	5/31/2012
Discount rate	4.64%/5.09%	4.87%
Health care cost trend rate	7.00%	7.50%
Ultimate health care cost trend rate	5.00%	5.00%
Year ultimate trend rate reached	2017	2017
Average future working lifetime (years)	16.3	16.6

* As of July 31, 2013, the plan was amended to reflect the transition of retirees age 65 and over to the Health Reimbursement Arrangement.

Other information:		6/1/2013-5/31/2014		6/1/2012-5/31/2013
1% increase in trend rates				
Effect on service + interest cost	$	128	$	974
Effect on APBO		1,941		10,168
1% decrease in trend rates				
Effect on service + interest cost	$	(108)	$	(729)
Effect on APBO		(1,650)		(7,939)

14. TAX STATUS & ACCOUNTING FOR UNCERTAINTY IN INCOME TAXES

The University is exempt from income tax under section 501(a) of the Internal Revenue Code ("IRC") of 1986, as amended, as an organization described in section 501(c)(3) of the IRC as evidenced by its most recent determination letter dated May 23, 2002. The University has been classified as an organization that is not a private foundation because it qualifies under section 509(a)(1) as an educational institution, and donations to it qualify for deduction as charitable contributions. However, income generated from activities unrelated to the University's exempt purpose is subject to tax under IRC section 511. The University files unrelated business income tax and other returns as required by government authorities.

Tax positions taken relating to the University's tax-exempt status, unrelated business income activities taxable income and deductibility of expenses, and other miscellaneous tax positions taken by the University would more likely than not be sustained by examination. Accordingly, the University has not recorded an income tax liability for uncertain tax benefits. As of May 31, 2014, the University's tax years ended May 31, 2009 through 2014, generally, remain subject to examination.

15. RELATED PARTY TRANSACTIONS

Members of the University’s Board of Regents and senior administration may, from time to time, be associated, either directly or indirectly, with entities doing business with the University. Accordingly, the University has Board of Regents, faculty, and staff written conflict of interest policies that require any such association, including those of immediate family members, to be disclosed on an annual basis and updated as appropriate during the year. If such associations exist, measures are taken to mitigate any actual or perceived conflict. For the years ended May 31, 2014 and 2013, there were no related party transactions that were considered to be significant or that were not effectively mitigated.

16. COMMITMENTS & CONTINGENCIES

Capital Expenditures & Other Commitments

At May 31, 2014, the University has commitments to expend approximately $138,109,000 to fulfill contracts related to the construction of a new football stadium, a new building for the business school, and other capital projects.

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

Leases

The University incurred $1,546,000 and $1,337,000 in operating lease expenses for facilities and equipment in the years ended May 31, 2014 and 2013, respectively. As of May 31, 2014, the University has lease commitments for future periods as follows *(in thousands of dollars)*:

	2015	2016	2017	2018	2019	2020 and Thereafter	Total
Equipment	$ 421	$ 416	$ 50	$ 50	$ 50	$ --	$ 987
Other	1,279	1,229	673	645	91	--	3,917
Total	$ 1,700	$ 1,645	$ 723	$ 695	$ 141	$ --	$ 4,904

Contingencies

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

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

17. SUBSEQUENT EVENTS

The University has evaluated subsequent events through September 24, 2014, the date when financial statements were issued. Other than the items noted below, the University did not identify any subsequent events to be disclosed.

On June 1, 2014, the University entered into long-term agreements with a vendor to provide, for up to ten years, the University's facilities maintenance, utilities management, grounds maintenance, housekeeping, and dining services. These agreements include incentive payments to be received from the vendor that will be deferred until earned in accordance with the provisions of the agreements.

On June 26, 2014, the University entered into an agreement with an affiliated entity to purchase real estate for $13,000,000. It is anticipated that the purchase of this property will be completed during the year ending May 31, 2015.