Consolidated Financial Statements and Report of Independent Certified Public Accountants

Abilene Christian University

May 31, 2011 and 2010

Davis Kinard & Co, PC
CERTIFIED PUBLIC ACCOUNTANTS
Quality. Integrity. Knowledge.

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Report of Independent Certified Public Accountants

Board of Trustees
Abilene Christian University

We have audited the accompanying consolidated statements of financial position of Abilene Christian University and its subsidiaries ("the University") as of May 31, 2011 and 2010, and the related consolidated statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Abilene Christian University and its subsidiaries as of May 31, 2011 and 2010, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 9, 2011, on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Davis Kinard & Co, PC
Certified Public Accountants

Abilene, Texas
August 9, 2011

Abilene Christian University

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

May 31, 2011 and 2010

ASSETS	2011	2010
Cash and cash equivalents	$ 4,718,671	$ 6,265,269
Accounts and notes receivable, net	5,962,289	6,956,633
Contributions receivable, net	5,609,496	9,179,024
Inventories	2,097,821	2,436,410
Prepaid expenses and other assets	2,129,762	2,135,954
Investments	304,405,502	269,933,487
Charitable trusts and annuities	31,201,840	26,421,502
Property and equipment, net	141,972,112	130,035,673
Total assets	$498,097,493	$453,363,952
LIABILITIES AND NET ASSETS		
Accounts payable	$ 2,992,986	$ 4,484,547
Accrued interest payable	472,254	418,431
Accrued salaries and benefits	14,062,220	13,971,778
Net advances on lines of credit	13,300,000	10,648,180
Deposits and other liabilities	10,446,578	10,128,987
Reserve for charitable trusts and annuities	18,422,349	15,155,918
Long-term obligations	61,896,117	59,275,551
Total liabilities	121,592,504	114,083,392
Net assets		
Unrestricted	182,906,704	164,352,664
Temporarily restricted	100,061,039	84,779,252
Permanently restricted	93,537,246	90,148,644
Total net assets	376,504,989	339,280,560
Total liabilities and net assets	$498,097,493	$453,363,952

The accompanying notes are an integral part of these consolidated statements.

Abilene Christian University

CONSOLIDATED STATEMENTS OF ACTIVITIES

Year ended May 31, 2011

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Operating:				
Revenues, gains, and other support				
Tuition and fees	$ 88,005,024	$ -	$ -	$ 88,005,024
Less scholarship allowances	(32,322,499)	-	-	(32,322,499)
Net tuition and fees	55,682,525	-	-	55,682,525
Auxiliary enterprises sales and services	21,465,518	-	-	21,465,518
Private gifts and grants	2,184,782	1,676,206	-	3,860,988
Endowment support	6,456,626	7,507,733	-	13,964,359
Government grants and contracts	6,596,203	-	-	6,596,203
Other revenue	4,447,246	-	-	4,447,246
Net assets released from restrictions	12,200,918	(12,200,918)	-	-
Total revenues, gains, and other support	109,033,818	(3,016,979)	-	106,016,839
Expenses				
Operating expenses:				
Instruction and research	34,703,513	-	-	34,703,513
Public services	2,865,871	-	-	2,865,871
Academic support	10,194,445	-	-	10,194,445
Student services	16,395,491	-	-	16,395,491
Expenses of auxiliary enterprises	22,549,020	-	-	22,549,020
Fundraising	3,803,249	-	-	3,803,249
Management and general	19,837,981	-	-	19,837,981
Total operating expenses	110,349,570	-	-	110,349,570
Decrease in net assets from operating activities	(1,315,752)	(3,016,979)	-	(4,332,731)
Non-operating:				
Contributions for endowment, plant, and other	2,179,683	2,990,341	1,533,464	6,703,488
Investment return, net of amount designated for operations	16,274,891	17,098,157	394,035	33,767,083
Other revenues	67,015	-	-	67,015
Net assets released from endowment, plant, and other	1,876,665	(1,876,665)	-	-
Expenses for endowment, plant, and other	(546,139)	-	-	(546,139)
Changes in value of split-interest agreements	17,677	86,933	1,461,103	1,565,713
Net non-operating revenues, expenses, and other changes	19,869,792	18,298,766	3,388,602	41,557,160
Total change in net assets	18,554,040	15,281,787	3,388,602	37,224,429
Net assets at beginning of year	164,352,664	84,779,252	90,148,644	339,280,560
Net assets at end of year	$182,906,704	$100,061,039	$ 93,537,246	$376,504,989

The accompanying notes are an integral part of these consolidated statements.

Abilene Christian University

CONSOLIDATED STATEMENTS OF ACTIVITIES

Year ended May 31, 2010

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Operating:				
Revenues, gains, and other support				
Tuition and fees	$ 79,374,657	$ -	$ -	$ 79,374,657
Less scholarship allowances	(28,853,192)	-	-	(28,853,192)
Net tuition and fees	50,521,465	-	-	50,521,465
Auxiliary enterprises sales and services	21,123,270	-	-	21,123,270
Private gifts and grants	2,694,683	4,253,303	-	6,947,986
Endowment support	6,126,956	7,772,301	-	13,899,257
Government grants and contracts	7,139,294	-	-	7,139,294
Other revenue	4,325,459	-	-	4,325,459
Net assets released from restrictions	11,279,321	(11,279,321)	-	-
Total revenues, gains, and other support	103,210,448	746,283	-	103,956,731
Expenses				
Operating expenses:				
Instruction and research	32,109,227	-	-	32,109,227
Public services	2,765,880	-	-	2,765,880
Academic support	9,575,898	-	-	9,575,898
Student services	15,594,011	-	-	15,594,011
Expenses of auxiliary enterprises	21,957,529	-	-	21,957,529
Fundraising	3,321,037	-	-	3,321,037
Management and general	20,123,462	-	-	20,123,462
Total operating expenses	105,447,044	-	-	105,447,044
Decrease in net assets from operating activities	(2,236,596)	746,283	-	(1,490,313)
Non-operating:				
Contributions for endowment, plant, and other	187,089	2,527,488	1,235,320	3,949,897
Investment return, net of amount designated for operations	11,433,883	13,605,226	216,533	25,255,642
Other revenues	8,546	-	-	8,546
Net assets released from endowment, plant, and other	2,712,980	(2,712,980)	-	-
Expenses for endowment, plant, and other	(532,557)	-	-	(532,557)
Changes in value of split-interest agreements	2,749	35,091	1,298,125	1,335,965
Net non-operating revenues, expenses, and other changes	13,812,690	13,454,825	2,749,978	30,017,493
Total change in net assets	11,576,094	14,201,108	2,749,978	28,527,180
Net assets at beginning of year	152,776,570	70,578,144	87,398,666	310,753,380
Net assets at end of year	$164,352,664	$ 84,779,252	$ 90,148,644	$339,280,560

The accompanying notes are an integral part of these consolidated statements.

Abilene Christian University

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended May 31, 2011 and 2010

	2011	2010
Cash flows from operating activities		
Change in net assets	$ 37,224,429	$ 28,527,180
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	7,109,656	6,986,626
Accretion of asset retirement obligations	-	98,395
Gain on sale of equipment	(97,317)	(2,000)
Bad debt expense	744,949	637,337
(Increase) decrease in:		
Accounts and notes receivable	246,922	(1,342,792)
Contributions receivable	3,569,528	227,236
Inventories	338,589	98,046
Prepaid expenses and other assets	6,192	(278,049)
Increase (decrease) in:		
Accounts payable	(1,491,561)	2,637,768
Accrued interest payable	53,823	36,965
Accrued salaries and benefits	90,442	824,015
Deposits and other liabilities	317,591	359
Noncash contributions	(1,699,665)	(652,892)
Contributions restricted for long-term investment	(5,003,824)	(3,297,005)
Interest and dividends restricted for reinvestment	(492,355)	(264,338)
Equity in loss of unconsolidated entity	64,974	68,352
Changes in value of split-interest agreements	(1,565,714)	(1,335,965)
Net unrealized and realized gains on investments	(36,147,202)	(30,350,687)
Net cash provided by operating activities	3,269,457	2,618,551
Cash flows from investing activities		
Purchases of property and equipment	(19,046,095)	(6,162,425)
Proceeds from sale of equipment	97,317	2,000
Disbursement of loans to students, faculty, and others	(655,433)	(547,427)
Repayment of loans from students, faculty, and others	657,906	583,029
Proceeds from sales and maturities of investments	8,127,264	5,348,717
Purchases of investments	(4,639,328)	(2,387,183)
Net cash used in investing activities	$ (15,458,369)	$ (3,163,289)

The accompanying notes are an integral part of these consolidated statements.

Abilene Christian University

CONSOLIDATED STATEMENTS OF CASH FLOWS - CONTINUED

Years ended May 31, 2011 and 2010

	2011	2010
Cash flows from financing activities		
Proceeds from contributions restricted for:		
Investment in endowment	$ 3,168,285	$ 2,017,238
Investment in plant	1,835,539	1,279,767
	5,003,824	3,297,005
Other financing activities:		
Interest and dividends restricted for reinvestment	492,355	264,338
Payments of split-interest obligations	(126,251)	(84,672)
Payments of notes payable	(509,356)	(1,290,053)
Proceeds from lines of credit	74,892,838	53,883,785
Payments of lines of credit	(72,241,018)	(54,021,820)
Proceeds from long-term obligations	7,383,423	6,500,000
Payments of long-term obligations	(4,253,501)	(4,095,027)
	5,638,490	1,156,551
Net cash provided by financing activities	10,642,314	4,453,556
Net increase (decrease) in cash and cash equivalents	(1,546,598)	3,908,818
Cash and cash equivalents at beginning of year	6,265,269	2,356,451
Cash and cash equivalents at end of year	$ 4,718,671	$ 6,265,269
Non-cash transactions:		
Improvements capitalized and recorded in accounts payable	$ 1,137,008	$ 1,642,085
Non-cash contributions	1,699,665	652,892
Other required disclosures:		
Cash paid for interest	$ 2,960,337	$ 2,881,625

The accompanying notes are an integral part of these consolidated statements.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Consolidation

The accompanying consolidated financial statements include the financial position, activities, and cash flows of Abilene Christian University (the "University" or "ACU"), a not for profit institution of higher education in Abilene, Texas, and its subsidiaries, the ACU Foundation (the "Foundation"), the Stone-Campbell Restoration Movement Publishers ("SCRMP"), ACIMCO, and ACU in Oxford (UK). All significant interrelated accounts and transactions have been eliminated in the accompanying consolidated financial statements. The University has controlling interests in the Foundation, SCRMP, ACIMCO, and ACU in Oxford.

Basis of Accounting

The consolidated financial statements of the University have been prepared in accordance with accounting principles generally accepted in the United States of America ("US GAAP"). The focus of these financial statements is to present the University as a whole and to present balances and transactions according to the existence or absence of donor-imposed restrictions. This has been accomplished by classification of transactions into three classes of net assets - unrestricted, temporarily restricted, or permanently restricted.

- Unrestricted net assets—Net assets not subject to donor-imposed stipulations.

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

- 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 institution to use all or part of the income earned on related investments for general or specific purposes.

Statement of Activities

The University defines operating activities, as included in the accompanying statement of activities, as the revenue and expenses resulting from its educational programs and other core mission activities. Donor-restricted contributions to endowments and capital contributions, as well as investment returns in excess of the University's defined spending limit, are excluded from operating activities and separately reported as nonoperating activities in the accompanying statement of activities.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Contributions

Contributions, including unconditional promises to give, are recognized as revenues in the period received. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value. 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.

Contributions to be received after one year are discounted at an appropriate discount rate commensurate with the risks involved. Amortization of discount is recorded as additional contribution revenue in accordance with donor-imposed restrictions, if any. An allowance for uncollectible contributions receivable is provided based upon management's judgment, including such factors as prior collection history, type of contribution, and nature of fund-raising activity. Contributions of land, building, and equipment without donor stipulations concerning the use of such assets are reported as revenues of the unrestricted net asset class. Contributions of cash or other assets to be used to acquire land, building, and equipment with such donor stipulations are reported as revenues of the temporarily restricted net asset class; the restrictions are considered to be released upon the acquisition of such assets.

Endowment

The University's endowment is subject to the version of the *Uniform Prudent Management of Institutional Funds Act* ("UPMIFA") enacted by the state of Texas, which is described in Note H. Under Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 958 *Not-for-Profit Entities*, a not-for-profit organization that is subject to an enacted version of UPMIFA shall classify a portion of a donor-restricted endowment fund of perpetual duration as permanently restricted net assets. The amount classified as permanently restricted shall be the amount of the fund (a) that must be retained permanently in accordance with explicit donor stipulations, or (b) that in the absence of such stipulations, the organization's governing board determines must be retained (preserved) permanently consistent with the relevant law.

Fair Value Measurements

ASC Topic 820 *Fair Value Measurements and Disclosures* ("ASC 820") provides a framework for measuring the fair value of assets and liabilities and illustrates key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. The standard establishes a hierarchy that prioritizes the inputs to fair value measurements based on the extent to which inputs to valuation techniques are observable in the marketplace. The University considered this standard with respect to the valuation of its financial assets and liabilities and their corresponding designations within the fair value hierarchy described in Note O.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Fair Value Option

For certain assets and liabilities, the University has elected the fair value option provided by ASC Topic 825 *Financial Instruments* ("ASC 825"), which allows entities to measure eligible financial instruments at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported within the change in net assets. The decision to elect the fair value option is determined on an instrument by instrument basis, must be applied to an entire instrument, and is irrevocable once elected. The University has elected to apply the fair value option to its investments in real estate and mineral interests in order to present the most relevant values on these investments.

Investments

Readily marketable equity and fixed income securities (investments readily marketable on national exchanges) are carried at fair value, as determined by the last reported sales price on the date of valuation, or if there has been no sale on that date, the average of the bid and asked prices. Real estate and mineral interests are carried at fair value based on appraised values or reserve analyses. In addition, the University maintains non-marketable alternative investments (primarily limited partnerships) carried at fair value based on information provided by external investment managers at the most recent valuation date prior to fiscal year-end. Other investments include cash and cash equivalents carried at cost, which approximates fair value, and notes receivable carried at net realizable value, which approximates fair value. The net realized and unrealized gains (losses) in fair value of investments are reflected in the consolidated statements of activities within investment return. The value of endowment support is determined by the amounts provided from the endowment to support the operations of the University.

Income and realized and unrealized gains and losses on investments of endowments and similar funds are reported as increases in permanently restricted net assets if the terms of the gift require that they be added to the principal of a permanent endowment fund; as increases in temporarily restricted net assets if the terms of the gift impose restrictions on the use of the income or if the funds have not been appropriated for use in operations; and as increases in unrestricted net assets in all other cases.

Non-endowment investments in for-profit entities in which the University does not own a controlling interest in the investee but possesses the ability to significantly influence the operating and financial policies of the investee are recorded on the equity method of accounting. The equity method of accounting requires investments to be initially recorded at cost and subsequently increased (decreased) for the University's share of the investee's net income (loss) and reduced when distributions are received. At May 31, 2011 and 2010, the University owned 25% of the outstanding common stock of Genesis Network Solutions, Inc. ("Genesis"), which is the University's only investment recorded on the equity method. The value of the University's investment in Genesis under the equity method was $115,130 and $180,104 at May 31, 2011 and 2010, respectively. Two board members have an indirect ownership in Genesis.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Use of Estimates

The preparation of consolidated financial statements in conformity with US GAAP 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 revenue and expenses during the reporting period. Significant estimates include the valuation of investments and other financial instruments, provisions for uncollectible accounts and notes receivable and pledges, asset retirement obligations, and the accumulated post-retirement benefit obligation. Actual results could differ from those estimates.

U.S. Income Tax Status

The University is a tax-exempt institution as an organization described in Section 501(c)(3) of the Internal Revenue Code of 1986, as amended ("IRC") and is not a "private foundation" under Section 501(a) of the IRC; accordingly, no provision for income taxes has been made in the consolidated financial statements. The Foundation, SCRMP, and ACIMCO have also been accorded recognition as exempt from income tax under Section 501(a) of the IRC, as organizations described in Section 501(c)(3) and 509(a)(3) of the IRC. For the years ended May 31, 2011 and 2010, the University incurred unrelated business income related to certain bookstore sales, oil and gas working interest, and certain alternative investments, resulting in an immaterial amount of unrelated business income. As of May 31, 2011, the University's tax years 2006 to 2010 remain subject to examination.

Cash and Cash Equivalents

For the purposes of the consolidated statements of cash flows, the University considers all cash and other highly liquid investments with original maturities of three months or less to be cash equivalents. The University places its cash and cash equivalents with high quality financial institutions, which at times may exceed federally insured limits. The University has not experienced any losses on such accounts.

Accounts and Notes Receivable

Receivables are recorded at the contractual amounts owed by students and others adjusted for unamortized discounts, and an allowance for uncollectible accounts and notes receivable. Interest income on notes receivable is recorded on the accrual basis in accordance with the terms of receivables.

The estimated allowances for uncollectible accounts and notes receivable are accounted for using the reserve method. Under this method, allowances are maintained at a level that, in the judgment of management, is adequate to meet the present and potential future risks of uncollectibility of the accounts and notes receivable. Management's judgment is based on a variety of factors, which include experience related to charge-offs and recoveries, and scrutiny of individual accounts and notes receivable. Receivables are unsecured and considered past due based on contractual terms. Amounts deemed by management to be uncollectible are charged to expense. Recoveries on receivables previously charged-off are credited to expense. Provisions for receivable losses are charged to expense and credited to the allowance for uncollectible accounts and notes receivable. At May 31, 2011 and 2010, the allowance for uncollectible accounts and notes receivable was $452,611 and $444,763, respectively.

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Inventories

Inventories are valued at amounts, which, in the aggregate, approximate the lower of cost or market on the first-in, first-out basis. No losses for obsolete inventory were recorded for the year ended May 31, 2011. The University recorded losses for obsolete inventory of $96,621 for the year ended May 31, 2010.

Taxes Collected from Customers and Remitted to Governmental Authorities

Sales and use taxes are reported on a gross basis within revenues and costs. These taxes amounted to $558,274 and $484,444 for the years ended May 31, 2011 and 2010, respectively.

Property and Equipment

Investments in the physical plant are recorded at cost. Significant renovations to existing buildings are capitalized, while maintenance and repairs are expensed when incurred. Purchases and improvements under $5,000 are not capitalized. Provision for depreciation is made on a straight-line basis over the estimated useful life of the asset. Currently, these estimated useful lives are as follows:

Buildings and building improvements	10-55 years
Improvements other than buildings	10-15 years
Equipment	5-20 years

When disposition is made of plant assets, the cost and accumulated depreciation are removed from the accounting records, and the resulting gain or loss is recognized in the consolidated statements of activities.

Advertising Costs

Advertising costs are expensed as incurred and totaled $448,091 and $301,026 for the years ended May 31, 2011 and 2010, respectively.

Recent Accounting Pronouncements

In May 2011, FASB issued Accounting Standards Update ("ASU") No. 2011-04, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*. The amendments in this Update generally represent clarifications of ASC 820, but also include some instances where a particular principle or requirement for measuring fair value or disclosing information about fair value measurements has changed. The standard is effective for reporting periods beginning after December 15, 2011. The University does not believe that the adoption of this standard will have a material impact on its consolidated financial statements.

NOTE B - CONTRIBUTIONS RECEIVABLE

Contributions receivable consisted of the following at May 31, 2011 and 2010:

	2011	2010
Unconditional promises expected to be collected in:		
Less than one year	$ 4,339,047	$ 5,195,350
One year to five years	2,193,909	5,109,450
Over five years	-	-
	6,532,956	10,304,800
Less discount for net present value	(192,347)	(179,773)
Less allowance for uncollectible contributions receivable	(731,113)	(946,003)
	$ 5,609,496	$ 9,179,024

The contributions are to be utilized for the following purposes:

	2011	2010
Operations and scholarships	$ 3,185,468	$ 6,309,750
Endowment	789,189	1,188,075
Acquisition of land, building and equipment	1,634,839	1,681,199
	$ 5,609,496	$ 9,179,024

Contributions receivable as of May 31, 2011 and 2010, have been discounted using rates ranging from 0.26% to 4.72% and 0.96% to 4.72%, respectively.

NOTE C - INVESTMENTS

Investments consisted of the following at May 31, 2011 and 2010:

	2011	2010
Mutual funds and investment partnerships managed by third parties	$ 227,123,699	$ 193,090,010
Notes receivable	293,991	394,757
Stocks and bonds	14,871,800	16,901,188
Real estate and mineral interests	58,582,414	56,460,116
Outside managed	2,334,177	2,028,218
Other investments	1,199,421	1,059,198
	$ 304,405,502	$ 269,933,487

The University invests in non-marketable alternative investments (primarily limited partnerships) that are carried at estimated fair value provided by the management of the investment partnerships. The University believes that the carrying value of its alternative investments is a reasonable estimate of fair value as of May 31, 2011 and 2010. The University has pledged equity securities valued at $22,161,972 and $13,778,875 at May 31, 2011 and 2010, respectively, under a pledge agreement in connection with a line of credit (see Note F).

Outside managed investments primarily include several outside managed trusts comprised of stocks, bonds, real estate, mineral interests, and other assets.

Investment income consisted of the following for the years ended May 31, 2011 and 2010:

	2011	2010
Interest income	$ 346,150	$ 187,765
Dividend income	1,276,308	1,368,854
Mineral income	9,728,649	7,135,753
Ranch income	298,107	180,192
Equity in loss of unconsolidated entity	(64,974)	(68,352)
Net realized and unrealized gains	36,147,202	30,350,687
Total investment income	$ 47,731,442	$ 39,154,899

The University maintains an investment pool for use by its endowment (excluding assets held in trust by the Foundation). The University's policy allows the pool to invest in domestic equities, international equities, fixed income securities, marketable alternative investments, real estate, mineral interests, and other investments determined appropriate by management. Investments in mutual funds and investment partnerships are invested by professional third-party managers with different investment styles to diversify risk and maximize returns. For the years ended May 31, 2011 and 2010, the spendable income allocated from these investments was $9,174,716 and $8,777,595, respectively. The total return for the pool, including interest, dividends, and net realized and unrealized investment depreciation and appreciation, was approximately 27.7% and 18.7% for the years ended May 31, 2011 and 2010, respectively.

NOTE C - INVESTMENTS - Continued

External investment management fees were approximately $381,991 and $373,669 for the years ended May 31, 2011 and 2010, respectively. Investment management fees are recorded as a reduction to investment return in the accompanying statement of activities.

The investment pool consisted of the following at May 31, 2011 and 2010:

	2011	2010
Mutual funds and investment partnerships managed by third parties	$ 206,120,275	$ 169,993,930
Cash and cash equivalents	475,815	5,308,528
	$ 206,596,090	$ 175,302,458

NOTE D - PROPERTY AND EQUIPMENT

Property and equipment consisted of the following at May 31, 2011 and 2010:

	2011	2010
Land	$ 3,438,702	$ 3,438,702
Buildings	128,586,287	128,305,656
Improvements to land and buildings	49,822,086	41,249,381
Equipment	30,330,535	29,148,450
	212,177,610	202,142,189
Less accumulated depreciation and amortization	(86,486,477)	(79,400,749)
	125,691,133	122,741,440
Assets held for sale	1,409,477	1,433,405
Construction in progress	14,871,502	5,860,828
	$ 141,972,112	$ 130,035,673

Depreciation and amortization expense for the years ending May 31, 2011 and 2010, was $7,109,656 and $6,986,626, respectively. Interest costs of $233,072 were capitalized during the year ended May 31, 2011. No interest costs were capitalized during the year ended May 31, 2010.

Construction in progress as of May 31, 2011, consisted of planning and construction costs for the Student Recreation and Wellness Center. Construction in progress as of May 31, 2010, consisted of various projects including planning costs for the Zoe Conference and Retreat Center, construction costs for the Student Recreation and Wellness Center, and costs for replacing the campus heating/cooling loop line.

In 2011, the University entered into a plan to dispose of an educational facility in Irving, Texas. The costs of this facility, net of accumulated depreciation of $78,047 and $54,119 at May 31, 2011 and 2010, respectively, are classified as assets held for sale in the table above.

NOTE E - LONG-TERM OBLIGATIONS

Long-term obligations consisted of the following as of May 31, 2011 and 2010:

	2011	2010
1998 - Higher Education Revenue Refunding and Improvement Bonds; payable in annual installments; maturing in fiscal year 2019; interest rate of 4.75%; secured by revenues.	$ 7,730,000	$ 8,010,000
2001 - Higher Education Revenue Improvement Bonds; payable in semi-annual installments; maturing in fiscal year 2021; interest rate of 5.0%; secured by revenues.	6,022,241	6,476,637
2003 - Higher Education Revenue Bonds; payable in semi-annual installments; maturing in fiscal year 2024; variable interest rate; secured by revenues.	6,802,393	7,207,446
2005 - Higher Education Revenue Bonds; payable in semi-annual installments; maturing in fiscal year 2026; variable interest rate; secured by revenues.	5,025,000	5,360,000
2005B - Higher Education Revenue Bonds; payable in semi-annual installments; maturing in fiscal year 2026; variable interest rate; secured by revenues.	1,471,750	1,573,250
2006 - Higher Education Revenue Bonds; payable in semi-annual installments; maturing in fiscal year 2026; variable interest rate; secured by revenues.	1,711,693	3,157,472
2006B - Higher Education Revenue Bonds; payable in semi-annual installments; maturing in fiscal year 2027; variable interest rate; secured by revenues.	2,029,018	2,159,988
2006 Taxable - Higher Education Revenue Bonds; payable in semi-annual installments; maturing in fiscal year 2026; variable interest rate; secured by revenues.	4,500,000	4,800,000
2009 - Higher Education Revenue Bonds; payable in semi-annual installments; maturing in fiscal year 2029; variable interest rate; secured by revenues.	8,750,000	9,250,000

NOTE E - LONG-TERM OBLIGATIONS - Continued

	2011	2010
2010 - Higher Education Bonds; payable in semi-annual installments; maturing in fiscal year 2025; interest rate of 5.596%; secured by revenues.	$ 6,199,199	$ 6,500,000
2011 - Higher Education Bonds; payable in quarterly installments; maturing in fiscal year 2026; at 65% of the three-month LIBOR rate plus 2.06%; secured by revenues.	7,383,423	-
Miscellaneous notes payable	4,303,105	4,843,349
Less discount on miscellaneous note payable	(31,705)	(62,591)
	$ 61,896,117	$ 59,275,551

Miscellaneous notes payable include a note with principal values of $548,338 and $822,807 at May 31, 2011 and 2010, respectively, that require imputation of interest at an effective rate of 4.06%.

On June 8, 2010, the University issued $16,000,000 in Series 2011 tax-exempt debt to finance the construction of a Student Recreation and Wellness Center. The agreement matures on June 8, 2025, with interest payable quarterly at 65% of the three-month LIBOR rate plus 2.06% (2.24% at May 31, 2011) but not less than 3.25% and is subject to certain covenants. Beginning in May 2012, principal payments shall be due quarterly based on a 20-year straight-line amortization schedule, which shall be calculated based on the principal amount outstanding as of March 8, 2012, with any remaining principal due on June 8, 2025.

On December 18, 2009, the University issued $6,500,000 in Series 2010 tax-exempt debt to finance the installation of HVAC and energy conservation upgrades, including a chilled and hot water loop system. This debt is payable in semiannual payments of $330,196 including interest at a fixed rate of 5.596% beginning on October 1, 2010. The debt matures on October 1, 2024, and principal and interest are amortized over the life of the debt.

On June 1, 2008, the University issued $10,000,000 in Series 2009 tax-exempt revenue bonds to finance construction and renovations on certain education and housing facilities (The Hunter Welcome Center, masonry cornice work on various buildings, and renovations to Mabee Hall). The bonds are payable in equal semiannual principal installments of $250,000 beginning on April 1, 2009, and ending on October 1, 2028, plus interest accruing at 62.075% of the 30-day LIBOR rate plus 0.90% (1.03% and 1.08% as of May 31, 2011 and 2010, respectively).

On August 7, 2008, the University entered into a $2,200,000 loan agreement with a commercial bank to finance a portion of the renovation costs on an existing building (the "Cafeteria Loan"). The Cafeteria Loan is payable in thirteen semiannual payments of $115,643, including interest at a fixed rate of 6.5%, beginning on February 10, 2009, and one final payment of $1,565,942 due on August 10, 2015, at which time all unpaid principal and interest are due. The Cafeteria Loan is secured by the University's gross revenues on a parity basis with the lender of the Series 2009 tax-exempt revenue bonds. The Cafeteria Loan is subject to certain financial covenants.

NOTE E - LONG-TERM OBLIGATIONS - Continued

On November 9, 2006, the University issued $2,619,410 in Series 2006B debt for the purpose of renovation of the Sikes Residence Hall, reconstruction of ornamental cornice work on various buildings, replacing the HVAC system in the Gibson Center, and paying costs of issuance. The debt matures on October 1, 2026, and has a variable interest rate based on 65% of the 30-day LIBOR rate plus 0.90% (1.04% and 1.08% at May 31, 2011 and 2010, respectively). Principal and interest are amortized over the life of the debt and are payable semiannually.

On July 17, 2006, the University issued $6,000,000 in 2006 taxable debt for the purpose of refunding the remaining Series 2002 debt that matured on that date. The new note matures on April 1, 2026 and has a variable interest rate of the 30-day LIBOR rate plus 0.65% (0.86% and 0.93% at May 31, 2011 and 2010, respectively). Principal and interest are amortized over the life of the debt and are payable semiannually.

The variable rates for Series 2005, 2005B, and 2003 are based on 65% of the 30-day LIBOR rate plus 1.00% (1.18% and 1.27% as of May 31, 2011 and 2010, respectively). The variable rate for Series 2006 is based on 65% of the 30-day LIBOR rate plus 0.55% (0.76% and 0.83% as of May 31, 2011 and 2010, respectively). However, the University has obtained interest rate swap agreements on the 2003, 2005, 2006, 2006B, 2006 taxable, and 2009 debt issues (collectively "the Bond Agreements"). Refer to Note P for a further discussion of derivative instruments.

A schedule of future fiscal year principal payments of long-term obligations is as follows:

2012	$ 4,740,090
2013	4,498,038
2014	4,339,510
2015	4,463,925
2016	5,974,356
Thereafter	37,911,903
	61,927,822
Less discount on miscellaneous note payable	(31,705)
	$ 61,896,117

The Omnibus Agreement to the Bond Agreements, amended in February 2010, requires the University to comply with three financial covenants including a debt service coverage ratio, liquidity ratio, and a primary reserve ratio. As of May 31, 2011 and 2010, the University was in compliance with all bond covenants.

Total interest expense for long-term obligations for the years ended May 31, 2011 and 2010, was $2,780,889 and $2,918,590, respectively.

NOTE F - NET ADVANCES ON LINES OF CREDIT

The University has entered into line of credit agreements to provide operating cash flows, maximize endowment earnings, and facilitate cash management. On October 1, 2008, the University executed a line of credit agreement with Bank of America, N.A. (the "Vision Debt"), which matures on October 1, 2013, and provides for maximum borrowings of up to $20,000,000. For each draw request, the University has the option to pay interest at prime minus 1.75% (1.50% at May 31, 2011 and 2010) or LIBOR plus 0.50% (0.71% and 0.78% at May 31, 2011 and 2010, respectively). $10,300,000 and $7,800,000 were outstanding on the Vision Debt May 31, 2011 and May 31, 2010, respectively. The Vision Debt is subject to a pledge agreement that grants the lender a security interest in certain types of investment securities that are pledged as collateral for advances on the Vision Debt. The pledge agreement sets a maximum borrowing base ($17,760,746 and $10,334,156 at May 31, 2011 and 2010, respectively) on the Vision Debt relative to the value of the securities pledged.

An agreement with First Financial Bank, Abilene (the "FFIN Line"), matures on September 30, 2011, and provides for maximum borrowings of up to $9,500,000 with interest payable at prime (3.25% at May 31, 2011 and 2010). No amount was outstanding on the FFIN line at May 31, 2011. $2,848,180 were outstanding on the FFIN Line at May 31, 2010. An agreement with Bank of America, N.A. (the "BOA Line") matures on March 6, 2012, and provides for maximum borrowings of $8,000,000. For each new request, the University has the option to pay interest at prime (3.25% at May 31, 2011 and 2010) or the 30-day LIBOR rate plus 1.25% (1.46% and 1.53% at May 31, 2011 and 2010, respectively). $3,000,000 were outstanding on the BOA Line at May 31, 2011. No amount was outstanding on the BOA Line at May 31, 2010. The FFIN and BOA Lines are unsecured.

NOTE G - RESTRICTIONS ON NET ASSET BALANCES

Permanently restricted net assets are listed below according to the purpose for which the income for these items is to be used at May 31, 2011 and 2010:

	2011	2010
Student loans	$ 697,643	$ 499,867
Scholarships	58,562,467	56,848,801
Instruction, research, and divisional support	17,005,407	16,419,871
General operations	3,325,048	3,494,213
	79,590,565	77,262,752
Life income, student loan funds, and other accounts	13,946,681	12,885,892
	$ 93,537,246	$ 90,148,644

NOTE G - RESTRICTIONS ON NET ASSET BALANCES - Continued

Temporarily restricted net assets are listed below according to the purpose for which the income for these items is to be used at May 31, 2011 and 2010:

	2011	2010
Gifts and other unexpended revenues and gains available for:		
Student loans	$ 764,103	$ 749,630
Scholarships	53,995,940	41,484,015
Instruction, research, and divisional support	30,374,571	25,448,702
General operations and unappropriated earnings	11,436,672	13,643,812
Acquisition of property and equipment	1,793,574	1,834,700
Life income, student loan funds, and other accounts	1,696,179	1,618,393
	$100,061,039	$ 84,779,252

NOTE H - ENDOWMENT

The University's endowment consists of individual endowment funds established for a variety of purposes including both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. Net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions. Unrestricted endowment represents board designated funds.

Interpretation of Relevant Law

The University interprets the State of Texas UPMIFA as allowing the University, absent donor stipulations to the contrary as stated in the gift instrument, to appropriate so much of a donor-restricted endowment fund as the University determines is prudent for the uses, benefits, purposes, and duration for which the endowment is established. In the absence of explicit donor stipulations, the University designates 50% of endowment gifts to permanently restricted net assets and 50% to temporarily restricted net assets. The assets in the endowment fund remain restricted until appropriated for expenditure by the University.

The following factors are considered 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.

NOTE H – ENDOWMENT - Continued

Changes in endowment net assets for the year ended May 31, 2011, are as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	$ 113,064,565	$ 75,807,820	$ 77,262,754	$ 266,135,139
Contributions	19,133	1,154,801	1,154,801	2,328,735
Net investment income	9,699,658	166,419	-	9,866,077
Dividends and interest	349,019	1,207,691	-	1,556,710
Net realized and unrealized gains	11,896,417	23,430,567	-	35,326,984
Endowment support	(6,456,626)	(7,507,733)	-	(13,964,359)
Transfers	-	(189,639)	1,173,010	983,371
Endowment net assets, end of year	$ 128,572,166	$ 94,069,926	$ 79,590,565	$ 302,232,657

Changes in endowment net assets for the year ended May 31, 2010, are as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	$ 102,338,348	$ 61,255,974	$ 75,938,536	$ 239,532,858
Contributions	161,000	1,247,721	1,217,644	2,626,365
Net investment income	7,087,037	(113,382)	99,952	7,073,607
Dividends and interest	738,921	755,784	-	1,494,705
Net realized and unrealized losses	8,866,205	20,427,403	-	29,293,608
Endowment support	(6,126,946)	(7,772,301)	-	(13,899,247)
Transfers	-	6,621	6,622	13,243
Endowment net assets, end of year	$ 113,064,565	$ 75,807,820	$ 77,262,754	$ 266,135,139

NOTE H - ENDOWMENT - Continued

Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the University to retain as a fund of perpetual duration. There were no such deficiencies at May 31, 2011 and 2010.

Return Objective 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. Endowments include those assets of donor restricted funds that the University must hold in perpetuity or for a donor specified period as well as board designated funds. The University expects its endowment funds, over time, to provide an average rate of return in excess of 5.5% annually plus inflation. Actual returns in any given 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 capital appreciation (realized and unrealized) and current yield (interest, dividends, rents and royalties). 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 each year an amount equal to 70% of an endowment's prior year distribution for spending, adjusted for inflation plus 1%, plus 30% of its beginning of year market value, times the target rate of 4.5%. Distributions are then limited to no less than 2% nor greater than 6% of beginning endowment market value and annual increases for an individual endowment to 7%. Accordingly, over time, the University expects the current spending policy to allow its endowment to grow at an average of at least 1% plus inflation 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.

NOTE I - CHARITABLE TRUSTS AND ANNUITIES

The University is party to a number of charitable trusts and annuities, the majority of which the University, or the University through its affiliate Foundation, is the trustee. Assets under charitable trusts and annuities consist of the following at May 31, 2011 and 2010:

	2011	2010
University and Foundation as trustee:		
Charitable trusts	$26,273,171	$23,484,579
Charitable gift annuities	3,819,881	1,085,626
	30,093,052	24,570,205
Third-party trustee	1,108,788	1,851,297
	$31,201,840	$26,421,502

For charitable trusts and annuities for which the University is trustee, contributions are recorded at fair value in the year of the agreement and are reflected as charitable trusts and annuities in the accompanying consolidated financial statements. For the years ended May 31, 2011 and 2010, $2,475,000 and $43,764, respectively, were recorded as contribution revenue related to these types of agreements. In addition to the recording of the asset, a liability is recorded representing the discounted future cash flows expected to be paid to the specified beneficiary designated by the donor. The estimated liability of future cash flows is based upon the life expectancy of the donor, the current market value of the trust, and the applicable federal rate (AFR) related to each trust based on the AFR in effect at the date the trust was created. Investment income, payments to beneficiaries, and adjustments to the liability are reflected as changes in value of split-interest agreements in the consolidated statements of activities. The estimated liability for the future cash flows, as of May 31, 2011 and 2010, was $18,422,349 and $15,155,918, respectively.

For charitable trusts of which the University is not the trustee, contributions are recognized in the year the University becomes aware of the existence of the agreement and are valued at the discounted present value of expected future cash flows. The expected future cash flows have been discounted at a rate of 6% over the life expectancy of the parties involved and calculated based upon the current market value of the trust's assets and other factors stipulated in the agreements. The present value of the expected future cash flows has been reflected as a component of charitable trusts and annuities in the consolidated statements of financial position. The change in estimated present value is reflected as a change in value of split-interest agreements in the consolidated statements of activities.

NOTE J - RETIREMENT PLAN

The University has a 403(b) defined contribution retirement plan covering substantially all full and part-time personnel. Employees are required to contribute 2% of salary to participate in the 403(b) plan for which the University contributes up to 4% of the employee's salary. Employees have the option of contributing an additional 1% or 2% of base pay into the 403(b) plan, for which the University contributes a corresponding 2% or 4% of the employee's salary. University contributions under the plan, net of forfeitures, totaled $2,932,090 and $2,745,568 for the years ended May 31, 2011 and 2010, respectively.

Effective January 1, 2009, the University's 401(a) and 401(k) defined contribution plans were frozen to new participants and new contributions. Assets remaining in those plans will be distributed to participants in accordance with the provisions of the plan agreements.

The University has a 457(b) deferred compensation plan covering a select group of key employees. Qualified employees may defer a portion of their compensation as contributions to the plan. The University does not contribute to the plan. The values of the plan assets at May 31, 2011 and 2010 were $238,907 and $179,082, respectively, which are recorded as assets and liabilities on the consolidated statements of financial position.

NOTE K - POSTRETIREMENT BENEFITS OTHER THAN PENSIONS

In addition to the University's defined contribution pension plans, the University sponsors a defined benefit health care plan that provides post-retirement medical benefits to certain retired employees who had worked 10 years and attained age 55 while in service with the University as of May 31, 1995. The University is required to recognize the funded status of this benefit plan, measured as the difference between plan assets at fair value and the benefit obligation, as an asset or liability in its statement of financial position and to recognize previously unrecognized gains or losses and prior service costs or credits as a component of its consolidated statement of activities.

The following presents the plan's funded status as of May 31:

	2011	2010
Accumulated postretirement benefit obligation	$(4,856,430)	$(4,847,344)
Plan assets at fair value	-	-
Unfunded status	$(4,856,430)	$(4,847,344)
Accrued postretirement benefit cost	$(4,856,430)	$(4,847,344)

NOTE K - POSTRETIREMENT BENEFITS OTHER THAN PENSIONS - Continued

Approximate annual benefit costs for the year ended May 31:

	2011	2010
Net periodic postretirement benefit cost	$ 308,196	$ 308,196
Employer contributions	$ 325,435	$ 335,116
Plan participant contributions	22,609	24,719
Benefits paid	$ 348,044	$ 359,835

The accrued postretirement benefit cost is recorded in accrued salaries and benefit expenses on the accompanying consolidated statements of financial position.

The weighted average assumptions related to the postretirement benefit plan are as follows at May 31, 2011 and 2010:

	2011	2010
Discount rate	4.5%	6.5%
Health care cost trend rate	8.5%	8.5%
Ultimate health care cost trend rate	5.0%	5.0%
Years to reach ultimate cost trend	7	7

The University expects to contribute $436,547 to the post-retirement benefit plan in fiscal year 2012. Benefits expected to be paid over the next five years and the five fiscal years thereafter are as follows:

2012	$ 436,547
2013	428,618
2014	426,684
2015	430,071
2016	429,263
2017-2021	1,982,267

NOTE L - HEALTH INSURANCE

The University maintains a partially self-funded health insurance plan with insured specific and aggregate stop-loss coverage, administered by a third party administrator. The administrator acts as the University's agent in making benefit payments on the University's behalf. The total liability for outstanding health claims was $263,211 and $441,982 at May 31, 2011 and 2010, respectively, and is recorded in accrued salaries and benefit expenses in the accompanying consolidated statements of financial position. Management believes the liability is adequate to fund any health claims incurred but not paid or reported as of the end of the fiscal year.

NOTE M - COMMITMENTS AND CONTINGENCIES

The University leases facilities and equipment to support its study abroad programs and other operating activities under noncancelable operating agreements through 2020. Rent expense related to these agreements for the years ended May 31, 2011 and 2010, was $616,320 and $728,960, respectively. Future minimum rentals under the noncancelable leases as of May 31, 2010 are as follows:

Year ending May 31,	
2012	$ 349,479
2013	113,506
2014	34,848
2015	34,838
2016	38,333
Thereafter	153,331

The University has open construction contracts for the Student Recreation and Wellness Center with remaining commitments of approximately $5,315,554 at May 31, 2011.

In the normal course of operations, the University is named as a defendant in lawsuits and is subject to periodic examinations by regulatory agencies. An estimate of the possible loss or range of loss on these events cannot be made. However, after consultation with legal counsel, management believes that liabilities, if any, arising from such litigation and examinations would not have a material effect on the University's financial position, results of operations, or cash flows.

NOTE N - SIGNIFICANT CONCENTRATIONS OF CREDIT RISK

The University grants credit in the form of accounts and notes receivable to students and others, a substantial portion of which are enrolled at the University. The University does not require collateral for the extension of credit with the exception of notes made to facilitate real estate sales, in which case, the collateral is typically the real estate being sold. Counterparty risks related to interest rate swap agreements are described in Note P. Management periodically monitors credit risk through the evaluation of the account's status and ability to repay.

NOTE O - FAIR VALUE MEASUREMENTS

ASC 820 requires certain disclosures about assets and liabilities measured and reported at fair value and emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, ASC 820 establishes a three-tier hierarchy described below to distinguish between various types of inputs used in determining the value of the University's investments and liabilities.

NOTE O - FAIR VALUE MEASUREMENTS - Continued

The University has adopted ASU No. 2009-12, *Investments in Certain Entities that Calculate Net Asset Value per Share (or Its Equivalent)*, which became effective for annual periods ending after December 15, 2009. This update provides amendments to ASC 820 for the fair value measurement of investments in certain entities that calculate net asset value per share (or its equivalent) and also requires disclosures by major category of investment about the attributes of these investments. For classification purposes, the standard provides that if a reporting entity has the ability to redeem an investment with a private investment fund at the net asset value per share (or its equivalent) at the measurement date or within the near term and there are no other liquidity restrictions, the private investment shall be categorized as Level 2 within the hierarchy of inputs described below:

Level 1 Inputs - Quoted prices (unadjusted) in active markets for identical assets and liabilities. Level 1 assets include publicly traded securities and mutual funds. Valuations of these instruments do not require a high degree of judgment as the valuations are based on quoted prices in active markets that are readily available.

Level 2 Inputs - Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities that are not active; and inputs other than quoted prices that are observable, such as models or other valuation methodologies as described below. Assets in this category generally include real estate, certain hedge funds of funds, managed long/short funds, and other equity instruments. If the University has the ability to redeem its investment at the net asset value per share (or its equivalent) at the measurement date or within 120 days thereof and upon no greater than 90 days prior written notice and there are no other potential liquidity restrictions, the investment is categorized within Level 2. Liabilities in this category include interest rate swaps and bonds payable subject to interest rate swaps.

Level 3 Inputs - Unobservable inputs for the valuation of the asset or liability. Level 3 assets include investments for which there is little, if any, market activity. These inputs require significant management judgment or estimation. Assets in this category generally include certain hedge funds of funds, private equity funds, privately held stock, other similar assets, and mineral interests. Liabilities in this category include the reserve for charitable trusts and annuities, the asset retirement obligation, and postretirement benefits other than pensions. These financial instruments have inputs that cannot be validated by readily determinable market data and generally involve considerable judgment by management.

The University's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the financial instrument.

The following schedules classify the University's assets and liabilities carried at fair value based upon the three-tier hierarchy required by ASC 820:

NOTE O - FAIR VALUE MEASUREMENTS - Continued

Description	May 31, 2011	Fair Value Measurements at May 31, 2011 Using Quoted Prices In Active Markets For Identical Assets (Level 1)	Significant other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Investments:				
Mutual funds and investment partnerships managed by third parties	$ 227,123,699	$ 54,054,532	$ 63,073,508	$ 109,995,659
Notes receivable	293,991	-	293,991	-
Stocks and bonds	14,871,800	14,746,771	125,029	-
Real estate and mineral interests	58,582,414	-	15,265,902	43,316,512
Outside managed	2,334,177	-	2,334,177	-
Other investments	1,199,421	-	1,199,421	-
Total investments	$ 304,405,502	$ 68,801,303	$ 82,292,028	$ 153,312,171
Charitable trusts and annuities:				
Mutual funds and investment partnerships managed by third parties	$ 28,406,265	$ 28,406,265	$ -	$ -
Privately held stock	1,556,787	-	-	1,556,787
Real estate	130,000	-	130,000	-
Outside managed	1,108,788	-	1,108,788	-
Total charitable trusts and annuities	$ 31,201,840	$ 28,406,265	$ 1,238,788	$ 1,556,787
Total assets	$ 335,607,342	$ 97,207,568	$ 83,530,816	$ 154,868,958
Liabilities:				
Interest rate swaps (Note P)	$ 2,924,175	$ -	$ 2,924,175	$ -
Bonds payable subject to interest rate swaps	25,893,928	-	25,893,928	-
Reserve for charitable trusts and annuities	18,422,349	-	-	18,422,349
Asset retirement obligation	2,090,712	-	-	2,090,712
Post-retirement benefits other than pensions	4,856,430	-	-	4,856,430
Total liabilities	$ 54,187,594	$ -	$ 28,818,103	$ 25,369,491

NOTE O - FAIR VALUE MEASUREMENTS - Continued

Description	May 31, 2010	Fair Value Measurements at May 31, 2010 Using: Quoted Prices In Active Markets For Identical Assets (Level 1)	Significant other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Investments:				
Mutual funds and investment partnerships managed by third parties	$ 193,090,010	$ 41,382,563	$ 55,945,049	$ 95,762,398
Notes receivable	394,757	-	394,757	-
Stocks and bonds	16,901,188	16,582,159	319,029	-
Real estate and mineral interests	56,460,116	-	15,205,549	41,254,567
Outside managed	2,028,218	-	2,028,218	-
Other investments	1,059,198	-	1,059,198	-
Total investments	$ 269,933,487	$ 57,964,722	$ 74,951,800	$ 137,016,965
Charitable trusts and annuities:				
Mutual funds and investment partnerships managed by third parties	$ 22,808,770	$ 22,808,770	$ -	$ -
Privately held stock	1,459,435	-	-	1,459,435
Real estate	302,000	-	302,000	-
Outside managed	1,851,297	-	1,851,297	-
Total charitable trusts and annuities	$ 26,421,502	$ 22,808,770	$ 2,153,297	$ 1,459,435
Total assets	$ 296,354,989	$ 80,773,492	$ 77,105,097	$ 138,476,400
Liabilities:				
Interest rate swaps (Note P)	$ 2,904,618	$ -	$ 2,904,618	$ -
Bonds payable subject to interest rate swaps	29,030,288	-	29,030,288	-
Reserve for charitable trusts and annuities	15,155,918	-	-	15,155,918
Asset retirement obligation	2,141,299	-	-	2,141,299
Post-retirement benefits other than pensions	4,847,344	-	-	4,847,344
Total liabilities	$ 54,079,467	$ -	$ 31,934,906	$ 22,144,561

NOTE O - FAIR VALUE MEASUREMENTS - Continued

The schedule below summarizes the activity for items classified as Level 3 assets for the year ended May 31, 2011:

	Investments			Charitable trusts and annuities
	Hedge funds of funds	Private equity	Mineral interests	Privately held stock
Beginning balance	$ 29,919,749	$ 65,842,649	$ 41,254,567	$ 1,459,435
Total gains:				
Included in net realized and unrealized gains	4,112,247	5,696,849	2,061,945	97,352
Purchases	12,108	14,813,267	-	-
Redemptions	(1,595,711)	(8,805,499)	-	-
Ending balance	$ 32,448,393	$ 77,547,266	$ 43,316,512	$ 1,556,787

The schedule below summarizes the current year activity for items classified as Level 3 liabilities for the year ended May 31, 2011:

	Reserve for charitable trusts and annuities	Asset retirement obligation	Postretirement benefits other than pensions
Beginning balance	$ 15,155,918	$ 2,141,299	$ 4,847,344
Total gains:			
Included in changes in value of split-interest agreements	1,347,056	-	-
Purchases	2,045,626	-	-
Payments of split-interest obligations	(126,251)	-	-
Payments of asset retirement obligation	-	(17,312)	-
Change in estimate	-	(33,275)	-
Actuarial valuation adjustment	-	-	48,934
Periodic postretirement benefit cost	-	-	308,196
Postretirement benefits paid	-	-	(348,044)
Ending balance	$ 18,422,349	$ 2,090,712	$ 4,856,430

NOTE O - FAIR VALUE MEASUREMENTS - Continued

The schedule below summarizes the activity for items classified as Level 3 assets for the year ended May 31, 2010:

	Investments			Charitable trusts and annuities
	Hedge funds of funds	Private equity	Mineral interests	Privately held stock
Beginning balance	$ 39,865,065	$ 67,823,666	$ 40,155,209	$ 2,326,129
Total gains:				
Included in net realized and unrealized gains	4,260,059	8,207,642	1,099,358	85,184
Purchases	1,926,798	11,477,794	-	-
Redemptions	(16,132,173)	(13,186,653)	-	-
Transfers out	-	(8,479,800)	-	(951,878)
Ending balance	$ 29,919,749	$ 65,842,649	$ 41,254,567	$ 1,459,435

Transfers out are as result of the adoption of Accounting Standards Update 2009-12.

The schedule below summarizes the current year activity for items classified as Level 3 liabilities for the year ended May 31, 2010:

	Reserve for charitable trusts and annuities	Asset retirement obligation	Postretirement benefits other than pensions
Beginning balance	$ 13,681,662	$ 2,116,844	$ 4,898,983
Total gains:			
Included in changes in value of split-interest agreements	1,418,020	-	-
Purchases	140,908	-	-
Payments of split-interest obligations	(84,672)	-	-
Accretion expense	-	98,395	-
Payments of asset retirement obligation	-	(73,940)	-
Periodic postretirement benefit cost	-	-	308,196
Postretirement benefits paid	-	-	(359,835)
Ending balance	$ 15,155,918	$ 2,141,299	$ 4,847,344

NOTE O - FAIR VALUE MEASUREMENTS - Continued

ASC 820 requires additional disclosure for certain types of investments that calculate net asset value per share but are not publicly traded to assist in understanding the nature and risk of these investments by major category. The table below summarizes the fair value and other pertinent liquidity information of investments in major categories at May 31, 2011:

	Fair Value	Unfunded Commit-ments	Redemption Frequency*	Redemption Notice Period
Fixed income/absolute return funds (a)	$ 8,671,497	$ -	Daily	None
Emerging market long only funds (b)	10,968,612	-	Monthly	7 days
Equity long/short and other equity hedge funds (c)	35,669,357	-	Monthly to 31 months	30 days to 90 days
Global opportunities hedge funds (d)	28,595,796	1,500,000	Monthly to 7 months	2 days to 90 days
Multi-strategy hedge funds (e)	17,321,706	-	Monthly to semi-annually	33 days to 95 days
Real-estate funds (f)	3,642,167	-	Quarterly	90 days
Private equity funds (g)	52,376,798	26,318,562	(g)	(g)
Venture capital funds (h)	15,213,193	5,500,381	(h)	(h)
	$ 172,459,126	$ 33,318,943		

NOTE O - FAIR VALUE MEASUREMENTS - Continued

The table below summarizes the fair value and other pertinent liquidity information of investments in major categories at May 31, 2010:

	Fair Value	Unfunded Commit-ments	Redemption Frequency*	Redemption Notice Period
Fixed income/absolute return funds (a)	$ 20,675,423	$ -	Daily	None
Emerging market long only funds (b)	5,098,682	-	Monthly	7 days
Equity long/short and other equity hedge funds (c)	30,793,120	-	Monthly to 19 months	30 days to 95 days
Global opportunities hedge funds (d)	19,300,131	2,100,000	Monthly to 19 months	2 days to 90 days
Multi-strategy hedge funds (e)	13,798,414	-	Monthly to semi-annually	33 days to 95 days
Real-estate funds (f)	4,887,422	-	Quarterly	95 days
Private equity funds (g)	42,331,491	26,026,176	(g)	(g)
Venture capital funds (h)	12,300,188	7,938,131	(h)	(h)
	$ 149,184,871	$ 36,064,307		

* Redemption frequency and redemption notice periods reflect general redemption terms and exclude liquidity restrictions noted below:

(a) This category includes a single investment fund that invests in a diversified portfolio of primarily U.S. based fixed income securities including: corporate bonds, treasury, agency, MBS, futures, options and swaps. The management of the fund has discretion to allocate among the various asset groups within a risk management structure that imposes percentage allocation maximums to individual classes of securities based on rating, risk, and other criteria. Allocation to various asset types and selection of securities are influenced by economic growth, monetary policy, fiscal policy, dollar policy, commodity prices, and relative valuations. The fair value of the investment in this category has been established using the net asset value per share of the investments as provided by the fund manager.

(b) This category includes a single investment fund that invests long only in emerging market publicly traded common stock. Management of the fund focuses primarily on larger, more established companies and has the ability to shift concentrations to certain regions depending on perceived opportunities. The fair value of the investment in this category has been established using the net asset value per share of the investments as provided by the fund manager.

NOTE O - FAIR VALUE MEASUREMENTS - Continued

(c) This category includes investments in hedge funds and hedge fund of funds that invest primarily in U.S. and international common stocks (both long and short) as well as other publicly traded investments. Managers of the funds typically have the ability to shift investments from value to growth strategies, from small to large capitalization stocks, and from a net long position to a net short position. The fair values of investments in this category have been estimated using the net asset value per share of the investments as provided by the fund manager. At May 31, 2011, one investment representing approximately 4.2% of the value of this category cannot be redeemed until May 1, 2012. At May 31, 2010, one investment representing approximately 12.8% of the value of this category cannot be redeemed without a fee due to a lockup provision, which expires March 31, 2011. One investment representing approximately 0.1% and 0.3% of the value of this category at May 31, 2011 and 2010, respectively, has been placed in a "sidepocket," meaning that redemptions may not take place until the underlying investments in the sidepocket are sold. The timing of the sale of the sidepocket investments cannot be estimated.

(d) This category includes investments in hedge funds that invest in a variety of opportunistic strategies. Investments are global in scope and include: equities (long and long/short), bonds, commodities, crops, livestock and agricultural land, precious and base metals, credit, interest rate and FX trading, insurance, energy, and private investments in public companies, as well as investments in financial services startups and other co-investments. The fair values of the investments in this category have been estimated using the net asset value per share of the investments as provided by the fund manager. Investments representing approximately 13.3% and 24.1% of this category at May 31, 2011 and 2010, respectively, are "sidepocket" investments meaning that redemptions will not take place until the underlying investments in the sidepocket are sold. The timing of the sale of the sidepocket investments cannot be estimated.

(e) This category includes investments in hedge funds of funds that pursue multiple strategies to diversify risks and reduce volatility. Investments are global in scope and include strategies such as: equity long-short, arbitrage, credit, event driven, market neutral, relative value, systematic, and trade finance. The fair values of the investments in this category have been estimated using the net asset value per share of the investments as provided by the fund managers.

(f) This category includes a single real estate fund that invests primarily in U.S. commercial real estate. The fair value of the investment in this category has been estimated using the net asset value of the University's ownership interest in the partners' capital of the fund. Management of this fund has imposed a redemption gate, meaning that redemptions are temporarily suspended; however, the manager is making partial distributions as circumstances permit. The gate has been in place for 30 months and 18 months at May 31, 2011 and 2010, respectively, and the timing as to when this restriction will be lifted cannot be estimated.

NOTE O - FAIR VALUE MEASUREMENTS - Continued

(g) This category includes investments in private equity funds and fund of funds that invest primarily in: distressed debt, BRIC (Brazil, Russia, India, China) country investments, energy holdings, and buyouts. The fair values of the investments in this category have been estimated using the net asset value of the University's ownership interest in the partners' capital of each underlying fund. These investments cannot be redeemed at the request of the investor. Instead, the nature of the investments in this category is that distributions are made through the liquidation of the underlying holdings. It is estimated that the underlying holdings of the funds will be liquidated over 1 to 10 years depending on the vintage year of the fund and the exit opportunities over time.

(h) This category includes investments in venture capital funds of funds that invest primarily in venture capital funds that provide start-up funding primarily for U.S. companies and primarily in the technology and bio-sciences areas. The fair values of the investments in this category have been estimated using the net asset value of the University's ownership interest in the partners' capital of each underlying fund. These investments cannot be redeemed at the request of the investor. Instead, distributions are made through the liquidation of the underlying holdings. It is estimated that the underlying holdings of the funds will be liquidated over 1 to 11 years depending on the vintage year of the fund and the exit opportunities over time.

The following methods and assumptions were used to estimate the fair value of each class of financial instrument:

<u>Cash and Cash Equivalents, Accounts Receivable, and Net Advances on Lines of Credit</u>

The carrying amounts approximate fair value due to the short maturity of these instruments.

<u>Contributions Receivable</u>

The carrying amount approximates fair value as determined by discounting pledges at an appropriate discount rate commensurate with the risks involved.

<u>Investments and Charitable Trusts and Annuities</u>

The carrying amounts of money market funds, mutual funds, and marketable securities approximate fair value based on quoted market prices. The fair values of private equity instruments discussed above are determined in good faith by third party fund managers based on estimates of the underlying investments and appropriate market indices. The University uses these estimates as reported by the fund managers as the primary input to its estimation of fair valuation; however other inputs are reviewed and considered in the determination of fair value including audit reports of the underlying funds. The fair values of real estate assets are based on independent appraisals. The fair values of mineral interests are based on independent reserve analyses as well as internal analysis using management's knowledge of the properties.

<u>Reserve for Charitable Trusts and Annuities</u>

The carrying amount approximates fair value based on the discounted value of expected future cash flows.

NOTE O - FAIR VALUE MEASUREMENTS - Continued

Asset Retirement Obligation

The carrying amount approximates fair value as determined by discounted present value of expected cash flows based on internal analyses of costs associated with retiring properties similar to those on which the asset retirement obligation was calculated.

Postretirement Benefits Other than Pensions

The carrying amount approximates fair value based on independent actuarial assumptions and the periodic service costs and payments made to participants in the plan.

Long-term Obligations

Long-term obligations on the consolidated statements of position total $61,896,117 and $59,275,551 at May 31, 2011 and 2010, respectively. Included within these amounts are bonds payable subject to interest rate swaps designated as fair value hedges with fair values disclosed in the tables above, which are determined by adjusting the principal value of the debt by the fair value of the interest rate swaps designated as fair value hedges. Also included within long-term obligations are liabilities related to interest rate swaps with fair values disclosed in the tables above, which are determined by the counterparty's present value calculations and market pricing models. Long-term obligations also include bonds and notes payable that are not reported at fair value, which have carrying values of $33,078,014 and $27,340,645 at May 31, 2011 and 2010, respectively. The fair values of the bonds and notes payable not reported at fair value were $35,590,335 and $28,503,150 at May 31, 2011 and 2010, respectively, as determined by discounting future cash flows at an appropriate rate commensurate with the risks involved.

NOTE P - DERIVATIVE INSTRUMENTS

The University entered into three interest rate swap agreements during fiscal year 2005, two interest rate swap agreements during fiscal year 2007, and one interest rate swap agreement in fiscal year 2009. Each agreement is subject to a master netting arrangement with the lender for the debt instruments, which mitigates credit risks on the swap agreements. The University accounts for these contracts in accordance with ASC Topic 815 *Derivatives and Hedging* and has designated these swaps as fair value hedges. The primary reason for swapping from a variable to fixed rate is to stabilize the university's operating budget vis-à-vis interest expense.

Management has completed variable to fixed rate swaps on six debt issues: 1) Series 2003 has been swapped to a fixed rate of 4.59%, 2) Series 2005 has been swapped to a fixed rate of 4.59%, 3) Series 2006 has been swapped to a fixed rate of 3.29% until September 1, 2011, 4) Series 2006 Taxable has been swapped to a fixed rate of 6.06%, 5) Series 2006B has been swapped to a fixed rate of 4.43%, and 6) Series 2009 has been swapped to a fixed rate of 3.88%.

NOTE P - DERIVATIVE INSTRUMENTS - Continued

Management has identified the following benefits of using swap agreements to accomplish the above objectives: 1) a lower fixed rate is available using a swap than by refunding at a fixed rate; 2) less paperwork and due diligence is involved in executing a swap than in a refunding. A swap is an agreement separate from the debt but mimicking the debt repayment structure; and 3) a swap does not affect the University's bank qualified debt limit.

The risks of using the proposed interest rate swaps include: 1) credit risk—risk that the counterparty will not fulfill its obligation on the swap contract; 2) basis risk—mismatch between the interest rate received from the swap contract and the interest actually owed on the debt; and 3) opportunity cost—if the floating rate that the University can pay on the debt averages below the fixed rate the University pays on the swap, then the University realizes the opportunity cost associated with locking in the higher interest rate.

The effectiveness of the swaps is judged by comparing the interest rates and key terms of the swaps with the interest rates and key terms on the underlying debt. The key terms of the swaps match the key terms of the floating rate debt and are, therefore, expected to offset the hedged cash flows of the debt.

Management believes the swaps are fully effective as of May 31, 2011 and 2010.

The schedule below summarizes the fair value of the swap contracts at May 31, 2011 and 2010:

Derivatives designated as hedging instruments under FASB ASC 815-20	Statement of Financial Position Location	Liabilities 2011	Liabilities 2010
Interest rate swaps	Long-term Obligations	$ 2,924,175	$ 2,904,618

Because the swaps are fully effective, the University recognized gains on the hedged items (the debt issues noted above) that exactly offset the interest rate swap liabilities noted above within long-term obligations on the consolidated statements of financial position. Accordingly, the interest rate swaps have no net effect within liabilities on the consolidated statements of financial position at May 31, 2011 and 2010.

The University includes the gain or loss on the hedged items within the same location on the consolidated statement of activities—interest expense—as the offsetting loss or gain on the related interest rate swaps as follows for the years ended May 31, 2011 and 2010:

	Statement of Activities Location	2011	2010
Unrestricted loss on swaps	Interest expense	$ (19,557)	$ (26,903)
Unrestricted gain on debt issues	Interest expense	19,557	26,903

As of May 31, 2011 and 2010, the aggregate notional amounts of the swaps were $28,818,103 and $31,934,906, respectively.

NOTE Q - ASSET RETIREMENT OBLIGATION

The University records a liability included within deposits and other liabilities in the accompanying consolidated statements of financial position for the estimated costs associated to remediate its asset retirement obligation.

The following presents a summary of the asset retirement obligation activity as of and for the years ended May 31, 2011 and 2010:

Asset retirement obligations at June 1, 2009	$ 2,116,844
Payment of asset retirement obligation	(73,940)
Accretion expense	98,395
Asset retirement obligations at May 31, 2010	2,141,299
Payments of asset retirement obligation	(17,312)
Change in estimate	(33,275)
Asset retirement obligations at May 31, 2011	$ 2,090,712

NOTE R - RELATED PARTY TRANSACTIONS

The University had unsecured receivables from related parties of $323,047 and $413,275 at May 31, 2011 and 2010, respectively.

NOTE S - RECLASSIFICATION OF FUNCTIONAL EXPENSES

During the year ended May 31, 2011, the University determined that expenses for its athletics programs previously reported within expenses of auxiliary enterprises should be reported within student services. The University also determined that expenses for certain mobile learning initiatives previously reported within management and general should be reported within academic support and that expenses for the ACU Foundation previously reported within management and general should be reported within fundraising. To conform prior year expenses to the current year presentation, the University has restated its functional expenses within the statement of activities for the year ended May 31, 2010, as follows:

	As Previously Reported	As Restated	Change
Student services	$ 11,738,105	$ 15,594,011	$ 3,855,906
Expenses of auxiliary enterprises	25,813,435	21,957,529	(3,855,906)
Academic support	8,792,445	9,575,898	783,453
Fundraising	2,497,208	3,321,037	823,829
Management and general	21,730,744	20,123,462	(1,607,282)
			$ -

NOTE T - SUBSEQUENT EVENTS

The University has evaluated subsequent events through August 9, 2011, the date the consolidated financial statements were available to be issued. No subsequent events were identified for disclosure through this date.