



Report of Independent Auditors
and Consolidated Financial Statements
with Supplementary Information for

California Lutheran University and Affiliate

May 31, 2014 and 2013

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REPORT OF INDEPENDENT AUDITORS

The Board of Regents
California Lutheran University and Affiliate

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of California Lutheran University and Affiliate, which comprise the consolidated statements of financial position as of May 31, 2014 and the related consolidated statements of activities and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statements.

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

MOSS ADAMS LLP***Opinion***

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of California Lutheran University and Affiliate as of May 31, 2014, and the change in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters***Report on Summarized Comparative Information***

We have previously audited the California Lutheran University and Affiliate's May 31, 2013 consolidated financial statements, and our report dated September 9, 2013, expressed an unmodified audit opinion on those audited consolidated financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended May 31, 2013, is consistent, in all material respects, with the audited consolidated financial statements from which it has been derived.

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying supplementary information is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.



Los Angeles, California
September 16, 2014

**CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
AS OF MAY 31, 2014 AND 2013**

ASSETS	<u>2014</u>	<u>2013</u>
Cash and cash equivalents	\$ 48,184,334	\$ 42,234,154
Deposits with trustees	-	1,455,972
Receivables		
Student accounts, net	1,637,839	1,791,698
Grants	230,388	188,739
Contributions	7,180,884	3,820,353
Other	1,556,374	1,312,789
Student loans receivable, net	1,647,347	1,530,171
Prepaid expenses, inventories and deposits	1,796,556	1,083,279
Investments		
Endowment	86,235,853	61,760,588
Deferred gifts held by University	2,998,072	3,226,587
California Lutheran Educational Foundation investments	6,129,479	6,075,306
Other	972,004	297,866
Funds held in trust by others	1,127,054	417,617
Deposits with trustee - reserved funds	6,932,024	8,121,324
Debt acquisition costs	1,894,135	1,982,899
Construction in progress	13,524,373	4,089,560
Property, plant, and equipment, net	126,600,397	122,917,827
Other intangible assets	475,000	475,000
	<u>\$ 309,122,113</u>	<u>\$ 262,781,729</u>
LIABILITIES AND NET ASSETS		
LIABILITIES		
Accounts payable	\$ 2,714,049	\$ 2,067,596
Accrued liabilities	9,276,885	7,484,712
Student housing deposits	720,378	724,670
Deferred revenue	1,804,449	1,255,117
Interest rate exchange agreement liability	111,605	167,653
Annuities payable	4,671,074	4,941,089
Deposits held in trust for others	2,020,183	1,847,631
Government grants refundable	1,579,490	1,569,287
Long-term debt	70,887,514	71,278,750
	<u>93,785,627</u>	<u>91,336,505</u>
NET ASSETS		
Unrestricted	133,662,405	116,608,814
Temporarily restricted	30,741,084	17,651,209
Permanently restricted	50,932,997	37,185,201
	<u>215,336,486</u>	<u>171,445,224</u>
TOTAL NET ASSETS	<u>215,336,486</u>	<u>171,445,224</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 309,122,113</u>	<u>\$ 262,781,729</u>

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
CONSOLIDATED STATEMENTS OF ACTIVITIES
FOR THE YEARS ENDED MAY 31, 2014 WITH SUMMARIZED TOTALS FOR 2013

	2014			2013	
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Total
OPERATING					
Revenues, gains and other support					
Tuition and fees	\$ 117,987,734	\$ -	\$ -	\$ 117,987,734	\$ 109,952,612
Less: Scholarships and grants	(39,001,331)	-	-	(39,001,331)	(34,417,681)
Net tuition and fees	78,986,403	-	-	78,986,403	75,534,931
Government and grants	2,196,088	-	-	\$ 2,196,088	2,146,897
Contributions	1,781,014	2,098,933	-	3,879,947	3,053,860
Short-term investment gain	47,485	-	-	47,485	-
Long-term investment income and gains allocated for operations	716,910	1,822,710	-	2,539,620	2,059,392
Interest and dividends	129,815	-	-	129,815	100,448
Sales and services of educational activities	941,317	-	-	941,317	944,056
Other sources	2,739,455	-	-	2,739,455	2,654,510
Sales and services of auxiliary enterprises	16,422,770	-	-	16,422,770	15,422,180
	103,961,257	3,921,643	-	107,882,900	101,916,274
Net assets released from restrictions	3,314,839	(3,314,839)	-	-	-
Reclassifications and re-designations	268,233	(738,958)	470,725	-	-
	107,544,329	(132,154)	470,725	107,882,900	101,916,274
TOTAL REVENUES, GAINS AND OTHER SUPPORT					
Expenses					
Program Expenses					
Instruction	35,365,289	-	-	35,365,289	34,234,489
Public service	4,372,595	-	-	4,372,595	4,140,396
Academic support	6,870,618	-	-	6,870,618	5,769,290
Student services	19,174,455	-	-	19,174,455	17,284,767
Auxiliary enterprises	17,619,513	-	-	17,619,513	16,711,660
Support Expenses					
Institutional support	15,400,191	-	-	15,400,191	13,616,153
Allocable expenses					
Operation and maintenance of plant	8,356,407	-	-	8,356,407	7,989,607
Depreciation	6,654,441	-	-	6,654,441	6,634,137
Interest	3,293,799	-	-	3,293,799	3,571,395
Less: Allocated expenses	(18,304,647)	-	-	(18,304,647)	(18,195,139)
	98,802,661	-	-	98,802,661	91,756,755
TOTAL OPERATING EXPENSES					
Change in net assets from operating activities	8,741,668	(132,154)	470,725	9,080,239	10,159,519
NON-OPERATING					
Endowment income	1,846,151	4,729,320	-	6,575,471	6,337,671
Less: Long-term investment income and gains allocated for operations	(716,910)	(1,822,710)	-	(2,539,620)	(2,059,392)
Investment return distributed	1,129,241	2,906,610	-	4,035,851	4,278,279
Net gains (losses) on other investments	(6,306)	5,412	-	(894)	3,190
Net (loss) on CEFA bond reserve	(388,572)	-	-	(388,572)	(249,801)
Unrealized gain on interest rate exchange agreement	56,048	-	-	56,048	59,525
Deferred giving - gifts	8,213	-	5,111,303	5,119,516	1,896,964
Capital giving - gifts	-	6,293,744	-	6,293,744	1,267,722
Gains (losses) on funds held in trust by others	6,884	(8)	350,465	357,341	97,885
Adjustment to actuarial liability for annuities payable	(36,088)	82,475	144,086	190,473	308,060
Loss on disposal of property, plant and equipment	(75,936)	-	-	(75,936)	(356,019)
Acquisition - inherent contribution	7,415,868	4,136,367	7,671,217	19,223,452	-
Net assets released from restrictions - nonoperating	202,571	(202,571)	-	-	-
	8,311,923	13,222,029	13,277,071	34,811,023	7,305,805
Change in net assets from nonoperating activities					
CHANGE IN NET ASSETS	17,053,591	13,089,875	13,747,796	43,891,262	17,465,324
NET ASSETS, beginning of year	116,608,814	17,651,209	37,185,201	171,445,224	153,979,900
NET ASSETS, end of year	\$ 133,662,405	\$ 30,741,084	\$ 50,932,997	\$ 215,336,486	\$ 171,445,224

**CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED MAY 31, 2014 AND 2013**

	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	\$ 43,891,262	\$ 17,465,324
Adjustments to reconcile change in net assets to net cash provided from operating activities:		
Depreciation, amortization, and accretion	6,743,205	6,722,902
Gain on investments, net	(6,574,576)	(6,340,861)
Unrealized loss on CEFA bond proceeds	388,572	249,801
Change in allowance for doubtful accounts	(3,602)	77,006
Change in interest rate exchange agreement liability	(56,048)	(59,525)
Actuarial adjustment of annuities payable	(190,473)	(308,060)
Loss on disposal of assets	75,936	356,019
Gain on funds held in trust by others	(357,341)	(97,885)
Acquisition-inherent contribution	(19,223,452)	-
Changes in current assets and liabilities:		
Student accounts receivable	216,134	(276,696)
Grants receivable	(41,650)	(23,568)
Contributions receivable	(3,360,530)	300,066
Other receivables	(232,354)	(121,050)
Prepaid expenses, inventories and deposits	(668,227)	(304,933)
Accounts payable	994,856	373,509
Accrued liabilities	1,515,965	293,733
Student housing deposits	549,332	(24,905)
Deferred revenue	(8,580)	(178,639)
Deposits held in trust for others	172,552	16,722
Contributions restricted for plant, loans, and long-term investment	(11,413,259)	(3,164,687)
NET CASH FLOWS FROM OPERATING ACTIVITIES	12,417,722	14,954,273
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of investments	(36,952,741)	(5,702,540)
Sales of investments	30,776,838	6,727,789
Cash acquired with merger with Pacific Lutheran Theological Seminary	904,759	-
Deposits from trustee accounts	(149,841)	13,555,257
Interest earned on deposits with trustee	(164,915)	(103,451)
Purchases of property, plant, and equipment, and CIP	(12,309,478)	(6,499,979)
Disbursements of loans to students	(351,000)	(130,000)
Repayments of loans from students	207,740	201,583
NET CASH (USED IN) FROM INVESTING ACTIVITIES	(18,038,638)	8,048,659
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from long term debt	2,571,456	-
Payments of principal on indebtedness	(1,698,952)	(2,306,378)
Increase in refundable governmental grants, net	10,203	16,415
Loan cancellations and write-offs	26,083	21,437
Payments to annuitants	(755,212)	(686,159)
Increase in annuities payable from new gifts	4,259	422,723
Contributions received restricted for plant, loans and long-term investment	11,413,259	3,164,687
NET CASH FROM FINANCING ACTIVITIES	11,571,096	632,725
NET INCREASE IN CASH AND CASH EQUIVALENTS	5,950,180	23,635,657
CASH AND CASH EQUIVALENTS, beginning of year	42,234,154	18,598,497
CASH AND CASH EQUIVALENTS, end of year	\$ 48,184,334	\$ 42,234,154

See accompanying notes.

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE NOTES TO FINANCIAL STATEMENTS

Note 1 - Organization

California Lutheran University ("Cal Lutheran") is an institution of higher education affiliated with the Evangelical Lutheran Church in America. Cal Lutheran offers undergraduate and graduate degrees in the liberal arts and sciences and professional fields.

California Lutheran Educational Foundation (the "Foundation") is a private foundation whose primary function is to provide fundraising support for California Lutheran University.

KCLU-FM California Lutheran University (the "Station") is a noncommercial radio station owned and operated by Cal Lutheran. The accounts and reports of the Station are a part of the University's general accounting system and have been identified and segregated from the books of the University. The accounting policies of the University reflect practices common to colleges and universities and conform to accounting principles generally accepted in the United States of America.

On January 1, 2014, Cal Lutheran merged with Pacific Lutheran Theological Seminary ("PLTS") with Cal Lutheran as the surviving entity. There were no noncash contributions received or transferred in relation to the merger, other than the inherent contribution noted below. The merger supports the Cal Lutheran vision of expanding its geographical footprint in California with an institution having a complementary mission and contributes to the growth of Cal Lutheran graduate programs. The following table summarizes the value of the assets acquired and liabilities assumed:

Cash	\$	904,759
Current assets		114,955
Investments		11,905,271
Property, plant and equipment, net		7,886,683
Less: Current liabilities		(280,499)
Less: Long term liabilities		<u>(1,307,717)</u>
Inherent contribution	\$	<u>19,223,452</u>

Principles of consolidation - The consolidated financial statements include the accounts of California Lutheran University and California Lutheran Educational Foundation (collectively referred to as the "University"). All significant intercompany balances and transactions have been eliminated in consolidation.

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE NOTES TO FINANCIAL STATEMENTS

Note 2 – Summary of Significant Accounting Policies

Basis of presentation – These consolidated financial statements, which are presented on the accrual basis of accounting, have been prepared to focus on the University as a whole. For the purpose of financial reporting, the University classifies resources into three net asset categories pursuant to any donor-imposed restrictions and applicable law. Accordingly, the net assets of the University are classified in the accompanying consolidated financial statements in the categories that follow:

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

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

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

The 2014 consolidated statement of activities is presented with 2013 summarized comparative information in total, but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with Generally Accepted Accounting Principles (“GAAP”). Accordingly, such information should be read in conjunction with the University’s consolidated financial statements for the year ended May 31, 2013, from which the summarized information was derived.

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

Contributions, including unconditional promises to give, are recognized as revenues in the period received and are reported as increases in the appropriate categories of net assets in accordance with donor restrictions. Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as net assets released from restriction between the applicable classes of net assets. Contributions received with donor-imposed restrictions that are met in the same year as received are reported as revenues of the temporarily restricted net asset class, and a release to unrestricted net assets is made to reflect the expiration of such restrictions. Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met.

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE

NOTES TO FINANCIAL STATEMENTS

Note 2 – Summary of Significant Accounting Policies (continued)

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

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

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

Certain revenue related to summer courses and programs is deferred and recognized as revenue in the same period expenses are recognized. Students are generally billed for courses and programs prior to the start of the course or program.

Cash equivalents – The University considers all highly liquid investments, except those held for long-term investment, with original maturities of three months or less when purchased to be cash equivalents.

Student accounts receivable – Student accounts receivable are carried at the unpaid balance of the original amount billed to students less an estimate made for doubtful accounts based on historical experience and management's evaluation of receivables at the end of each year. Student accounts are written off when deemed uncollectible. Recoveries of student accounts previously written off are recorded when received. A student account receivable is considered to be delinquent if any portion of the balance is outstanding for more than 90 days after the billing date. Interest is charged on past due accounts receivable. Receivables are generally unsecured.

Deposits with trustee – Deposits with trustee include amounts restricted for debt service as required by the trust indenture as well as bond construction funds for property additions. In prior years, the University sold its future interest to earnings on certain trustee bond reserves. Revenue from such sale had been deferred and recognized as income as earned.

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE NOTES TO FINANCIAL STATEMENTS

Note 2 – Summary of Significant Accounting Policies (continued)

Debt acquisition costs – Costs of bond issuance are deferred and amortized on a straight-line basis over the term of the related indebtedness. Amortization of approximately \$89,000 was recorded for the years ended May 31, 2014 and 2013.

Property and equipment – Physical property assets are stated at cost (or at fair value if donated), less accumulated depreciation, computed on a straight-line basis over the estimated useful lives of buildings and improvements (10 – 40 years) and equipment (3 – 10 years). Normal repair and maintenance expenses are charged to operations as incurred. The University capitalizes physical property additions in excess of \$10,000.

Asset retirement obligations – Asset retirement obligations are estimated costs and obligations associated with the retirement of long-lived assets. These liabilities were initially recorded at fair value and the related asset retirement costs were recorded as decreases in unrestricted net assets. Asset retirement costs are subsequently accreted over the useful lives of the related assets. The asset retirement obligation of \$791,607 and \$767,845 at May 31, 2014 and 2013, respectively, is included in accrued liabilities on the consolidated statements of financial position. The asset retirement obligation was reduced in 2014 and 2013 due to remediation of buildings on campus. Therefore, there was no accretion expense for the years ending May 31, 2014 and 2013.

Government grants refundable – Funds provided by the United States Government under the Federal Perkins Loan Program are loaned to qualified students and may be re-loaned after collections. These funds are ultimately refundable to the government and are included as liabilities in the consolidated statements of financial position. Revenues from other government grants are recognized as they are earned in accordance with the agreement. Any funding received before it is earned is recorded as a refundable advance. Expenses incurred before cash is received are recorded as receivables.

Deferred revenue – The University has deferred revenue/advances from prepayments on student accounts and from vendors related to its bookstore and food service operations.

Unemployment compensation – The University has elected to pay unemployment compensation claims as they arise.

Retirement plans – The University has certain contributory retirement plans for academic and nonacademic personnel. Contributions for employees are determined on a percentage of annual compensation. The cost of the retirement plans is paid currently and approximated \$3,390,000 and \$3,206,000 for the years ended May 31, 2014 and 2013, respectively.

Fundraising and advertising expenses – Fundraising expenses approximated \$2,763,000 and \$2,166,000 for the years ended May 31, 2014 and 2013, respectively. Advertising costs approximated \$860,000 and \$759,000 for the years ended May 31, 2014 and 2013, respectively, and are expensed as incurred.

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE

NOTES TO FINANCIAL STATEMENTS

Note 2 – Summary of Significant Accounting Policies (continued)

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

Use of estimates – The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

Income tax status – The Internal Revenue Service has determined that the University and Foundation are exempt from federal income tax under Section 501c(3) of the Internal Revenue Code as non-profit organizations. It is also exempt from state income taxes. However, any unrelated business income may be subject to taxation.

The University follows the accounting standards for contingencies in evaluating uncertain tax positions. This guidance prescribes recognition threshold principles for the consolidated financial statements recognition of tax positions taken or expected to be taken on a tax return that are not certain to be realized. No liability has been recognized by the University for uncertain tax positions as of May 31, 2014. The University's tax returns are subject to review and examination by federal and state authorities. The University is no longer subject to income tax examinations by taxing authorities for the years before 2011 for its federal filings and for years before 2010 for its state filings.

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

Reclassifications – Certain amounts appearing in the 2013 consolidated financial statements have been reclassified to conform with the 2014 presentation. The reclassifications have no effect on reported amounts of total net assets or change in total net assets. Reclassifications of net assets from unrestricted to temporarily and permanently restricted net assets occurred to show donor re-designations.

Investments and investment income – Investments are measured at fair value in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification Topic 820, *Fair Value Measurements and Disclosures* in the consolidated statements of financial position (see Note 3). Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in non-operating unrestricted revenues, gains and other support unless the income or loss is restricted by donor or law.

**CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
NOTES TO FINANCIAL STATEMENTS**

Note 2 – Summary of Significant Accounting Policies (continued)

Fair value of financial instruments – The carrying amounts of cash and cash equivalents, accounts receivable and other receivables, accounts payable and accrued liabilities, deposits and deferred revenue approximate fair value because of the short-term maturity of these financial instruments.

A reasonable estimate of the fair value of the receivables from students under government loan programs and grants refundable to the government for student loans could not be made because the notes receivable are not saleable and can only be assigned to the U.S. government or its designee. The fair value of receivables under institutional loan programs approximates carrying value.

The carrying amounts of the actuarial liability for trusts and annuities payable are based on life expectancies, quoted market prices, and the applicable discount rates in effect at the time the agreements were received by the University. The carrying amounts of long-term debt approximates fair value because these financial instruments bear interest at rates which approximate current market rates for notes with similar maturities and credit quality.

Contributions of assets other than cash are recorded at their estimated fair value at the date of the gift. Estimates of fair value involve assumptions and estimation methods that are uncertain and, therefore, the estimates could differ from actual results.

Cash surrender value of life insurance policies is considered to approximate fair value and is included in investments.

The fair values for investments and other financial instruments recorded at fair value on a recurring basis are included in Note 3.

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE

NOTES TO FINANCIAL STATEMENTS

Note 3 – Fair Value Measurements

Accounting Standards Codification (“ASC”) 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The three levels are defined as follows:

Level 1 – Quoted prices in active markets for identical assets or liabilities.

Level 2 – Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

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

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
NOTES TO FINANCIAL STATEMENTS

Note 3 – Fair Value Measurements (continued)

The following table summarizes financial instruments measured at fair value on a recurring basis by classification within the fair value hierarchy as of May 31, 2014:

	2014			
	Total	Level 1	Level 2	Level 3
ASSETS				
Deposits with trustee				
Cash and short term investments	\$ 938,708	\$ 938,708	\$ -	\$ -
Government bonds	5,993,316	5,993,316	-	-
Funds held in trust by others	1,127,054	-	-	1,127,054
Total funds held by others	8,059,078	6,932,024	-	1,127,054
Investments				
Cash equivalents and short term investments	6,057,348	6,057,348	-	-
Equity securities funds - U.S.	16,946,915	2,958,511	13,988,404	-
Equity securities funds - Non-U.S.	23,325,747	8,084,380	15,241,367	-
Total equity securities	40,272,662	11,042,891	29,229,771	-
Comingled funds - U.S.	21,508,049	2,537,739	18,970,310	-
Comingled funds - Non-U.S.	12,908,083	12,908,083	-	-
Corporate bonds	4,165,976	4,165,976	-	-
Government bonds	2,085,498	2,085,498	-	-
Total fixed income	40,667,606	21,697,296	18,970,310	-
Commodities and other investments	4,757,871	207,052	3,860,514	690,305
Hedge funds	13,310	-	-	13,310
Partnerships				
Private equity	3,242,456	-	-	3,242,456
Venture capital	1,042,499	-	-	1,042,499
Real estate	281,656	-	-	281,656
Total partnerships	4,566,611	-	-	4,566,611
Total investments	96,335,408	39,004,587	52,060,595	5,270,226
TOTAL ASSETS	\$ 104,394,486	\$ 45,936,611	\$ 52,060,595	\$ 6,397,280
LIABILITIES				
Interest rate exchange agreement	\$ 111,605	\$ -	\$ 111,605	\$ -
Deposits held in trust for others	442,408	442,408	-	-
TOTAL LIABILITIES	\$ 554,013	\$ 442,408	\$ 111,605	\$ -

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE

NOTES TO FINANCIAL STATEMENTS

Note 3 – Fair Value Measurements (continued)

The following table summarizes financial instruments measured at fair value on a recurring basis by classification within the fair value hierarchy as of May 31, 2013:

	2013			
	Total	Level 1	Level 2	Level 3
ASSETS				
Deposits with trustee				
Cash and short term investments	\$ 3,194,132	\$ 3,194,132	\$ -	\$ -
Government bonds	6,383,163	6,383,163	-	-
Funds held in trust by others	417,617	-	-	417,617
Total funds held by others	9,994,912	9,577,295	-	417,617
Investments				
Cash equivalents and short term investments	5,563,587	3,200,911	2,362,676	-
Equity securities funds - U.S.	16,584,461	2,490,343	14,094,118	-
Equity securities funds - Non-U.S.	11,773,700	7,014,581	4,759,119	-
Total equity securities	28,358,161	9,504,924	18,853,237	-
Comingled funds - U.S.	16,785,932	2,885,371	13,900,561	-
Comingled funds - Non-U.S.	10,667,506	10,667,506	-	-
Corporate bonds	1,972,509	1,972,509	-	-
Government bonds	2,052,875	2,052,875	-	-
Total fixed income	31,478,822	17,578,261	13,900,561	-
Commodities and other investments	1,362,146	182,551	1,157,098	22,497
Hedge funds	24,132	-	-	24,132
Partnerships				
Private equity	3,243,653	-	-	3,243,653
Venture capital	881,688	-	-	881,688
Real estate	448,159	-	-	448,159
Total partnerships	4,573,500	-	-	4,573,500
Total investments	71,360,348	30,466,647	36,273,572	4,620,129
TOTAL ASSETS	\$ 81,355,260	\$ 40,043,942	\$ 36,273,572	\$ 5,037,746
LIABILITIES				
Interest rate exchange agreement	\$ 167,653	\$ -	\$ 167,653	\$ -
Deposits held in trust for others	417,024	417,024	-	-
TOTAL LIABILITIES	\$ 584,677	\$ 417,024	\$ 167,653	\$ -

The following is a description of the valuation methodologies used for instruments measured at fair value on a recurring basis and recognized in the accompanying consolidated statements of financial position, as well as general classification of such instruments pursuant to the valuation hierarchy.

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities include highly liquid fixed-income securities, inflation protected equity funds, and emerging and developed market equity funds. Level 2 securities include any highly liquid funds not traded in an active market. In addition, fixed income funds and certain equity funds in Level 2, while lacking in liquidity, are readily priced based on net asset values (“NAV”) of the funds, or its equivalent fair value based on ownership percentages in the limited partnerships as of and for the fiscal years ended May 31, 2014 and 2013. In certain cases where Level 1 or Level 2 inputs are not available, or redemption is restricted for greater than 90 days, securities are classified within Level 3 of the hierarchy.

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE NOTES TO FINANCIAL STATEMENTS

Note 3 – Fair Value Measurements (continued)

Securities classified within Level 3 investments are based on valuations provided by the external investment managers. The Investment Committee and Management, in conjunction with the external investment advisors, monitors and analyzes the valuation of the investments on a quarterly basis. The Investment Committee reports to the Board of Regents. The valuations consider variables such as financial performance of investments, recent sales prices of investments, and other pertinent information. All investment objectives and strategies used by the fund managers comply with the University's Investment Policy.

The University's beneficial interest in irrevocable split interest agreements held or controlled by a third party is classified as Level 3 as the fair values are based on significant unobservable inputs. Since the University has an irrevocable right to receive the income earned from the trust's assets, the fair value of the University's beneficial interest is estimated to approximate the fair value of the trust's assets. The fair values are based on the market values of the trust assets.

The interest rate exchange agreement is classified as Level 2 as the fair value is based on observable inputs to a valuation model (interest rates, credit spreads, etc.) which take into account the present value of the estimated future cash flows and credit valuation adjustments.

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

This paragraph presents information about the level in the fair value hierarchy for the University's assets and liabilities that are not reported at fair value as of May 31, 2014 and 2013. Most financial assets and financial liabilities for which the carrying amount equals fair value are considered by the University to be Level 1 measurements in the fair value hierarchy. The University issued CEFA bonds that are reported at an amortized cost of \$67,120,000 and \$68,260,000 as of May 31, 2014 and 2013, respectively, in the statement of financial position. These CEFA bonds have an approximate fair value of \$70,151,398 and \$71,971,466 as of May 31, 2014 and 2013, respectively. The University determined these CEFA bonds to be Level 2 measurements in the fair value hierarchy.

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE

NOTES TO FINANCIAL STATEMENTS

Note 3 – Fair Value Measurements (continued)

The following table presents a reconciliation of the consolidated statements of financial position amounts for financial instruments measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the years ended May 31, 2014 and 2013:

	Partnerships			Hedge Funds	Commodities and Other	Funds Held in Trust by Others	Total
	Private Equity	Venture Capital	Real Estate				
Balance at June 1, 2013	\$ 3,243,653	\$ 881,688	\$ 448,159	\$ 24,132	\$ 22,497	\$ 417,617	\$ 5,037,746
Total realized gain (loss)	-	-	-	1,521	-	369,852	371,373
Total unrealized gain (loss)	1,211	144,491	(53,653)	(454)	2,758	-	94,353
Purchases	409,605	48,750	-	-	665,050	359,585	1,482,990
Sales	(412,013)	(32,430)	(112,850)	(11,889)	-	(20,000)	(589,182)
Balance at May 31, 2014	<u>\$ 3,242,456</u>	<u>\$ 1,042,499</u>	<u>\$ 281,656</u>	<u>\$ 13,310</u>	<u>\$ 690,305</u>	<u>\$ 1,127,054</u>	<u>\$ 6,397,280</u>

The amount of total gains or losses for the period included in change in net assets attributable to the change in unrealized gains or losses relating to financial instruments still held at May 31, 2014

\$ 94,353

	Partnerships			Hedge Funds	Commodities and Other	Funds Held in Trust by Others	Total
	Private Equity	Venture Capital	Real Estate				
Balance at June 1, 2012	\$ 3,256,187	\$ 867,022	\$ 623,740	\$ 52,776	\$ 20,805	\$ 321,519	\$ 5,142,049
Total realized gain (loss)	283,541	-	-	(227)	-	116,098	399,412
Total unrealized gain (loss)	(508,300)	(46,492)	(20,481)	3,082	1,692	-	(570,499)
Purchases	610,000	84,375	-	-	-	-	694,375
Sales	(397,775)	(23,217)	(155,100)	(31,499)	-	(20,000)	(627,591)
Balance at May 31, 2013	<u>\$ 3,243,653</u>	<u>\$ 881,688</u>	<u>\$ 448,159</u>	<u>\$ 24,132</u>	<u>\$ 22,497</u>	<u>\$ 417,617</u>	<u>\$ 5,037,746</u>

The amount of total gains or losses for the period included in change in net assets attributable to the change in unrealized gains or losses relating to financial instruments still held at May 31, 2013

\$ (574,197)

The University's policy is to recognize transfers in and transfers out as of the last day of the reporting period.

**CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
NOTES TO FINANCIAL STATEMENTS**

Note 3 – Fair Value Measurements (continued)

The following table lists investments valued at NAV by major class:

	Fair Value at May 31, 2014	Unfunded Commitments	Redemption Frequency	Redemption Notice Period	Investee Strategies and Other Restrictions
Hedge funds	\$ 13,310	\$ -	Not permitted	n/a	[1]
Equity securities funds - U.S.	13,988,404	-	Daily/Monthly	2-5 days	[1]
Equity securities funds - Non U.S.	15,241,367	-	Daily/Monthly	2-5 days	[1]
Comingled funds - U.S.	18,970,310	-	Daily/Monthly	2-5 days	[1]
Comingled funds - Non-U.S.	4,550,819	-	Daily/Monthly	2-5 days	[1]
Partnerships					
Private equity	3,242,456	1,366,000	Not permitted	n/a	[2]
Venture capital	1,042,499	115,000	Not permitted	n/a	[2]
Real estate	281,656	169,000	Not permitted	n/a	[2]
Balance at May 31, 2014	<u>\$ 57,330,821</u>	<u>\$ 1,650,000</u>			

[1] Absolute total return in long/short equity and multi-strategy hedge funds.

[2] Venture and buyout, in the U.S. and international.

The University's investment strategy incorporates a diversified asset allocation approach and maintains, within defined limits, exposure to the world equity, fixed-income, commodities, real estate and private equity markets. This strategy provides the University with a long-term asset mix that is most likely to meet the University's long-term return goals with the appropriate level of risk.

The alternative investments were entered into to diversify the University's portfolio, to provide predictability in overall earnings and to provide market-neutral holdings. The University's management, the finance and investment committee of the Board of Regents and the University's external investment consultants regularly review performance reports provided by the general partners of these investments. The University's external investment consultants attend meetings of the various general partners in order to evaluate the risk associated with these investments. In addition, the University monitors its portfolio mix to ensure that it is in accordance with Board policy.

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

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
NOTES TO FINANCIAL STATEMENTS

Note 4 – Credit Quality of Student Loans Receivable

The University issues uncollateralized loans to students based on financial need. Student loans are funded through Federal government loan programs or institutional resources. Student loans receivable are carried at the amount of unpaid principal less an estimate for doubtful accounts. Allowances for doubtful accounts are established based on prior collection experience and current economic factors which, in management’s judgment, could influence the ability of loan recipients to repay the amounts per the loan terms. At May 31, 2014 and 2013, student loans represented 0.53% and 0.59% of total assets, respectively.

Student loans consist of the following at May 31:

	<u>2014</u>	<u>2013</u>
Federal government programs	\$ 1,727,233	\$ 1,608,179
Institutional programs	<u>5,114</u>	<u>6,992</u>
	1,732,347	1,615,171
Less: Allowance for doubtful accounts	<u>(85,000)</u>	<u>(85,000)</u>
Student loans receivable, net	<u>\$ 1,647,347</u>	<u>\$ 1,530,171</u>

Funds advanced by the Federal government of approximately \$1,600,000 at May 31, 2014 and 2013 are ultimately refundable to the government and are classified as liabilities in the consolidated statements of financial position.

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

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

<u>May 31,</u>	<u>1-30 days</u>	<u>31-60 days</u>	<u>61-90 days</u>	<u>91+ days</u>	<u>Total</u>
2014	\$ 12,962	\$ 36,773	\$ 3,424	\$ 105,785	\$ 158,944
2013	\$ 21,996	\$ 32,610	\$ 2,059	\$ 106,727	\$ 163,392

**CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
NOTES TO FINANCIAL STATEMENTS**

Note 5 – Contributions Receivable

Contributions receivable include the following unconditional promises to give at May 31:

	<u>2014</u>	<u>2013</u>
Temporarily restricted - plant projects	\$ 9,352,324	\$ 4,128,606
Less: Present value discount	<u>(2,171,440)</u>	<u>(308,253)</u>
Contributions receivable, net	<u>\$ 7,180,884</u>	<u>\$ 3,820,353</u>
Amounts due in:		
Less than one year	\$ 246,989	
One to five years	5,019,720	
More than five years	<u>1,914,175</u>	
	<u>\$ 7,180,884</u>	

Gross unconditional promises to give have been reduced by an allowance for unfulfilled pledges of \$287,687 and \$102,719 at May 31, 2014 and 2013, respectively. An interest rate of 5% was used at May 31, 2014 and 2013 to discount net unconditional promises to give.

Approximately \$6,300,000 and \$1,600,000 of the contributions receivable at May 31, 2014 and 2013, respectively, are due from members of the governing board of the University.

Note 6 – Construction in Progress

At May 31, 2014, the following major projects were in progress:

	<u>Estimated Total Cost</u>	<u>Cost to Date</u>	<u>Funding Plan</u>
New dining commons	\$ 15,000,000	\$ 13,198,526	Donations/operations
Other projects		<u>325,847</u>	Donations/operations
		<u>\$ 13,524,373</u>	

At May 31, 2013, the following major projects were in progress:

	<u>Estimated Total Cost</u>	<u>Cost to Date</u>	<u>Funding Plan</u>
New dining commons	\$ 15,000,000	\$ 3,994,955	Donations/operations
Other projects		<u>94,605</u>	Operations
		<u>\$ 4,089,560</u>	

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
NOTES TO FINANCIAL STATEMENTS

Note 7 – Property and Equipment

Property and equipment consist of the following at May 31:

	<u>2014</u>	<u>2013</u>
Land	\$ 7,584,992	\$ 1,096,660
Improvements other than buildings	31,366,594	30,775,629
Buildings	136,397,345	132,322,027
Equipment	9,312,509	8,256,133
Library books or materials	4,153,059	3,771,360
	<u>188,814,499</u>	<u>176,221,808</u>
Less: Accumulated depreciation	<u>(62,214,103)</u>	<u>(53,303,981)</u>
Property and equipment, net	<u>\$ 126,600,397</u>	<u>\$ 122,917,827</u>

Depreciation expense totaled \$6,654,441 and \$6,636,432 for the years ended May 31, 2014 and 2013, respectively.

Note 8 – Restrictions and Limitations on Net Asset Balances

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

	<u>2014</u>	<u>2013</u>
Endowment funds	\$ 48,610,873	\$ 35,091,890
Funds held in trust by others	650,361	364,126
Student loan funds	304,278	304,278
Annuity, life income and similar funds	1,367,485	1,424,907
	<u>\$ 50,932,997</u>	<u>\$ 37,185,201</u>

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

	<u>2014</u>	<u>2013</u>
Gifts and other unexpended revenues and gains available for:		
Scholarships, instruction and other departmental support	\$ 5,168,568	\$ 3,389,148
Acquisition of buildings and equipment	8,309,036	2,226,425
Endowment funds	15,698,207	10,650,826
Funds held in trust by others	101,799	-
	<u>29,277,610</u>	<u>16,266,399</u>
Annuity, life income and similar funds	1,463,474	1,384,810
	<u>\$ 30,741,084</u>	<u>\$ 17,651,209</u>

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
NOTES TO FINANCIAL STATEMENTS

Note 8 – Restrictions and Limitations on Net Asset Balances (continued)

The University's unrestricted net assets were allocated as follows at May 31:

	<u>2014</u>	<u>2013</u>
Operations	\$ 49,557,459	\$ 42,621,189
Endowment funds	21,529,414	15,684,477
Funds held in trust by others	374,894	53,491
Property	62,152,896	58,129,177
Annuity, life income and similar funds	<u>47,742</u>	<u>120,480</u>
	<u>\$ 133,662,405</u>	<u>\$ 116,608,814</u>

Note 9 – Net Assets Released from Restrictions

Net assets were released from temporary donor restrictions during the years ended May 31, 2014 and 2013 by incurring expenses satisfying the restricted purposes or by occurrence of events specified by the donors as follows:

	<u>2014</u>	<u>2013</u>
Scholarships, instruction and other departmental support	\$ 3,270,410	\$ 2,602,243
Acquisition of buildings and equipment	<u>202,571</u>	<u>2,267,009</u>
	<u>\$ 3,472,981</u>	<u>\$ 4,869,252</u>

Note 10 – Long-Term Debt

The University had the following long-term debt outstanding at May 31:

	<u>2014</u>	<u>2013</u>
Notes payable	\$ 2,493,750	\$ 3,018,750
Mission Investment Fund note	1,273,764	-
California Educational Facilities Authority (CEFA) Revenue Bonds		
1999 Series	1,550,000	1,665,000
2004 Series A	5,465,000	5,465,000
2004 Series C	23,570,000	24,195,000
2008 Series	<u>36,535,000</u>	<u>36,935,000</u>
	<u>\$ 70,887,514</u>	<u>\$ 71,278,750</u>

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE

NOTES TO FINANCIAL STATEMENTS

Note 10 – Long-Term Debt (continued)

The University has a bank note outstanding, secured by 14 individual homes, and totaling \$ 2,493,750 and \$3,018,750 at May 31, 2014 and 2013, respectively, which matures through February 1, 2019. The required monthly payment ranges between \$48,000 and \$50,000. The University entered into an interest rate exchange agreement related to this note to fix the interest rate at 4.18% (see Note 17).

The University inherited a variable rate loan from the Mission Investment Fund as a part of the merger with PLTS. The balance as of May 31, 2014 was \$1,213,764 at an interest rate of 3.75% adjusted quarterly.

The 1999 Series bonds (“CEFA 99”) were issued to finance a portion of the costs for a new residence hall. The 1999 series bonds have interest rates varying from 5.125% to 5.25% and mature annually on April 1, 2014 through April 1, 2024 in amounts from \$115, 000 to \$195,000. The CEFA 99 indenture is secured by real property.

The 2004 Series A bonds were issued to finance the cost of the construction and equipping of certain educational facilities and paying certain costs of issuance of the 2004 Series A bonds. The bonds were issued November 16, 2004 and will mature on October 1, 2029. Interest on the bonds is payable monthly and no principal payments are required until the maturity date. The bonds bear interest at a variable (weekly reset) rate, which at May 31, 2014 was 0.14%, with an average rate of 0.10% for the 2014 fiscal year. In addition to the variable rate interest, the bonds incur an annual effective letter of credit fee of 130 basis points on the letter credit amount outstanding and an annual remarketing fee equal to 0.125%. The bonds are secured by an irrevocable direct-pay-letter of credit to the trustee. The letter of credit expires September 14, 2014. The letter of credit is secured by certain real property and a pledge on future revenue.

The 2004 Series C bonds were issued to finance construction activities, refunding the University’s outstanding Revenue Bonds 1993 Series B, advance refunding a portion of the University’s outstanding Revenue Bonds 1998 Series A, refinancing the April 1, 2004 principal payment with respect to CEFA Revenue Bonds 1999 Series B, paying certain costs of issuance of the 2004 Series C bonds, and funding a reserve fund for the 2004 Series C bonds. The 2004 Series C bonds include one serial series of bonds and three term bonds. The 2004 Series C bonds have interest rates varying from 3.625% to 4.75% and mature annually on October 1, 2013 to October 1, 2016 in amounts from \$625,000 to \$710,000. The term bonds have interest rates varying from 4.50% to 5.00% and mature from October 1, 2017 to October 1, 2029 in amounts from \$745,000 to \$2,545,000. The bonds are secured by certain real property and a pledge on future revenue.

**CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
NOTES TO FINANCIAL STATEMENTS**

Note 10 - Long-Term Debt (continued)

The 2008 Series bonds were issued to finance construction activities and the refunding of the University's outstanding Revenue Bonds 2004 Series B. The 2008 Series bonds include one serial series bond and three term bonds. The 2008 serial series bonds have interest rates varying from 3.50% to 4.50% and mature annually on October 1, 2013 to October 1, 2016 in amounts from \$400,000 to \$460,000. The term bonds have interest rates varying from 5.25% to 5.75% and mature from October 1, 2017 to October 1, 2038 in amounts from \$480,000 to \$3,650,000. The bonds are secured by certain real property and a pledge on future revenue.

The University is required to maintain debt service reserve funds of approximately \$6,603,000 which were partially funded from bond proceeds. The bond agreements require that certain financial and other covenants be maintained. As of May 31, 2014, the University is in compliance with these covenants.

Annual maturities of long-term debt for each of the five years subsequent to May 31, 2014 approximate \$1,864,000, \$1,933,000, \$1,997,000, \$2,166,000, and \$2,414,000 respectively, and approximately \$60,514,000 thereafter.

Note 11 - Operating Leases

The University has operating leases for offsite student facilities and one vehicle. Rental expense associated with these leases totaled approximately \$855,000 and \$833,000 for the years ended May 31, 2014 and 2013, respectively.

Future minimum lease payments on leases in effect on May 31, 2014, are as follows:

Years Ended May 31,	Operating Leases
2015	\$ 1,034,635
2016	1,175,688
2017	996,971
2018	957,355
2019	701,295
Thereafter	<u>2,726,265</u>
	<u>\$ 7,592,209</u>

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE

NOTES TO FINANCIAL STATEMENTS

Note 12 – Short-Term Credit Arrangements

The University has a secured revolving line of credit in the amount of \$4,000,000, with interest at either the LIBOR interest rate plus 1.50% per year or the prime rate minus 0.375% determined by the University at the time of borrowing. There was no balance outstanding as of May 31, 2014 and 2013. The revolving credit line is secured by residential real estate.

Note 13 – Deferred Gift Agreements

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

When a gift is received under one of these arrangements, it is split into the amount representing the actuarial present value of the future distributions to the donor and the remaining gift value to be retained for the benefit of the University or third-party beneficiaries. The actuarial liability is adjusted annually using actuarial tables appropriate for the type of arrangement, number of lives covered and age and sex characteristics of the donor. The University used historical interest rates varying from 5% to 10% in making the calculations.

The University received \$4,313 and \$218,159 of gift value relating to deferred gift agreements for the years ended May 31, 2014 and 2013, respectively. The gift value relating to deferred gift agreements are recorded in deferred gifts held by University and the related liability is recorded to annuities payable on the consolidated statements of financial position.

Note 14 – Other Concentrations of Credit Risk

Financial instruments that potentially subject the University to concentrations of credit risk consist principally of cash, investments, and accounts receivable. Cash, cash equivalents and investments are concentrated in a limited number of financial institutions and amounts in excess of FDIC and similar coverages are subject to the usual risks of balances in excess of those limits.

Student notes and receivables and other receivables are due from a variety of sources concentrated primarily in the western United States.

**CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
NOTES TO FINANCIAL STATEMENTS**

Note 14 – Other Concentrations of Credit Risk (continued)

In addition, the University's students receive a substantial amount of support from state and federal student financial assistance programs which are subject to audit by governmental agencies. A significant reduction in the level of this support, if this were to occur, could have an adverse effect on the University's programs and activities. Contributions receivable as of May 31, 2014 are principally due from two major contributors.

Note 15 – Supplemental Disclosure of Cash Flow Information

Supplemental disclosure of cash flow information is as follows for the years ended May 31:

	<u>2014</u>	<u>2013</u>
Interest paid, net of interest capitalized of \$233,372 and \$81,592 for 2014 and 2013, respectively	\$ 3,293,799	\$ 3,571,395
Noncash investing and financing activities		
Retirement of fully depreciated assets	870,582	11,721,737
Construction in progress included in accounts payable	504,909	853,311

Note 16 – Endowment

The University's endowment consists of approximately 300 individual funds established for a variety of purposes. Its endowment includes both donor-restricted endowment funds and funds designated by the governing board to function as endowments. As required by GAAP, net assets associated with endowment funds, including funds designated by the governing board to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of relevant law – The University's governing board has interpreted the California enacted version of Uniform Prudent Management of Institutional Funds Act ("UPMIFA") as allowing the University to appropriate for expenditure or accumulate so much of an endowment fund as the University determines is prudent for the uses, benefits, purposes and duration for which the endowment fund is established, subject to the intent of the donor as expressed in the gift instrument. Unless stated otherwise in the gift instrument, the assets in an endowment fund shall be donor-restricted assets until appropriated for expenditure by the Board of Regents. See Note 2 for further information on net asset classifications.

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
NOTES TO FINANCIAL STATEMENTS

Note 16 – Endowment (continued)

The remaining portion of the donor-restricted endowment fund that is not classified as permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the University in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the University considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

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

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

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ (1,292)	\$ 15,058,176	\$ 48,610,873	\$ 63,667,757
Board-designated endowment funds*	<u>21,530,706</u>	<u>640,031</u>	<u>-</u>	<u>22,170,737</u>
Total endowment net assets	<u>\$ 21,529,414</u>	<u>\$ 15,698,207</u>	<u>\$ 48,610,873</u>	<u>\$ 85,838,494</u>

*Amounts shown as temporarily restricted Board-designated have a donor-restriction as to purpose but are not donor-endowed.

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
NOTES TO FINANCIAL STATEMENTS

Note 16 – Endowment (continued)

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

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, May 31, 2013	\$ 15,684,477	\$ 10,650,826	\$ 35,091,890	\$ 61,427,193
Investment return				
Investment income, net of fees of \$275,133	208,452	522,168	-	730,620
Net appreciation - realized and unrealized	<u>1,637,698</u>	<u>4,207,151</u>	-	<u>5,844,849</u>
Total investment return	1,846,150	4,729,319	-	6,575,469
Contributions	3,900	-	5,111,303	5,115,203
Changes in cash surrender values	40,962	10,833	137,786	189,581
Appropriation of endowment assets for expenditure	(716,910)	(1,822,710)	-	(2,539,620)
Other changes:				
Transfers	3,660,415	(774,125)	598,677	3,484,967
Acquired in merger	<u>1,010,420</u>	<u>2,904,064</u>	<u>7,671,217</u>	<u>11,585,701</u>
Endowment net assets, May 31, 2014	<u>\$ 21,529,414</u>	<u>\$ 15,698,207</u>	<u>\$ 48,610,873</u>	<u>\$ 85,838,494</u>

Endowment net asset composition by type of fund consists of the following as of May 31, 2013:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ (3,648)	\$ 10,100,557	\$ 35,091,890	\$ 45,188,799
Board-designated endowment funds*	<u>15,688,125</u>	<u>550,269</u>	-	<u>16,238,394</u>
Total endowment net assets	<u>\$ 15,684,477</u>	<u>\$ 10,650,826</u>	<u>\$ 35,091,890</u>	<u>\$ 61,427,193</u>

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
NOTES TO FINANCIAL STATEMENTS

Note 16 – Endowment (continued)

Changes in endowment net assets for the year ended May 31, 2013 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, May 31, 2012	\$ 14,852,675	\$ 7,130,836	\$ 33,302,302	\$ 55,285,813
Investment return				
Investment income, net of fees of \$260,923	200,315	529,269	-	729,584
Net depreciation - realized and unrealized	<u>1,536,825</u>	<u>4,071,262</u>	<u>-</u>	<u>5,608,087</u>
Total investment return	1,737,140	4,600,531	-	6,337,671
Contributions	500	226,025	1,452,281	1,678,806
Changes in cash surrender values	18,060	16,607	115,097	149,764
Appropriation of endowment assets for expenditure	(679,540)	(1,379,852)	-	(2,059,392)
Other changes:				
Transfers	<u>(244,358)</u>	<u>56,679</u>	<u>222,210</u>	<u>34,531</u>
Endowment net assets, May 31, 2013	<u>\$ 15,684,477</u>	<u>\$ 10,650,826</u>	<u>\$ 35,091,890</u>	<u>\$ 61,427,193</u>

Funds with deficiencies – From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the University to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature that are reported in unrestricted net assets were approximately \$1,300 and \$4,000 as of May 31, 2014 and 2013, respectively. These deficiencies resulted from unfavorable market fluctuations that occurred shortly after the investment of new permanently restricted contributions and continued appropriation for certain programs that were deemed prudent by the governing board. Subsequent gains that restore the fair value of the assets of the endowment fund to the required level will be classified as an increase in unrestricted net assets.

Return objectives and risk parameters – The University has adopted investment and spending policies that attempt to be prudent and provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the University must hold in perpetuity or for a donor-specified period(s) as well as board-designated funds. Under this policy, the long-term minimum need of the endowment is to exceed a total return averaging at least the annual spending rate plus inflation, fees and costs. Actual returns in any year may vary from this amount. The long-term objective is to build endowment value over time by achieving incremental returns in excess of need while appropriately managing portfolio risk.

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE NOTES TO FINANCIAL STATEMENTS

Note 16 – Endowment (continued)

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

Spending policy and how the investment objectives relate to spending policy – The University has a policy of appropriating for distribution each year 5.00% of its endowment fund's average fair value for the twelve quarters prior to and including December 31 preceding the fiscal year-end. In establishing this policy, the University considered the long-term expected return on its endowment. Accordingly, over the long-term, the University expects the current spending policy to allow its endowment to grow at an average of 4.00% 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 17 – Derivative Instruments

The University uses an interest rate exchange agreement as part of its risk management strategy to manage exposure to fluctuations in interest rates and to manage the overall cost of its debt. Interest rate exchange agreements are used to manage identified and approved exposures and are not used for speculative purposes. The interest rate exchange agreement is recognized as either an asset or liability on the consolidated statements of financial position and is measured at fair value. Interest rate exchange agreements are often held for the life of the strategy, but may reflect significant interim unrealized gains or losses depending on the change in value since the inception of the contract. All unrealized and realized gain or loss from the interest rate exchange agreement is reflected in the consolidated statements of activities.

The University entered into an interest rate exchange agreement during 2011. The interest rate exchange agreement has an original notional amount of \$4,200,000. The agreement fixes the University's one month LIBOR interest rate at 4.18% through the February 1, 2019 expiration date.

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE

NOTES TO FINANCIAL STATEMENTS

Note 17 – Derivative Instruments (continued)

The interest rate exchange agreement between the University and a third party (“counterparty”) provides for periodic exchange of payments between the parties based on changes in a defined index and a fixed rate and include counterparty credit risk. Counterparty credit risk is the risk that contractual obligations of the counterparties will not be fulfilled. Concentrations of credit risk relate to groups of counterparties that have similar economic or industry characteristics that could cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. Counterparty credit risk is managed by requiring high credit standards for the University’s counterparties. The counterparties to these contracts are financial institutions that carry investment-grade credit ratings. The interest rate exchange agreement contains collateral provisions applicable to both parties to mitigate credit risk. The University does not anticipate non-performance by its counterparty.

Derivative instruments are reported in the consolidated statements of financial position at fair value as of May 31, 2014 and 2013 as follows:

Derivates Not Designated as Hedging Instruments	Liabilities Derivative		
	Statement of Financial Position Location	Fair Value	
		2014	2013
Interest exchange agreement	Interest rate exchange agreement liability	\$ 111,605	\$ 167,653

Derivates Not Designated as Hedging Instruments	Location of Gain on Derivates Recognized in the Statement of Changes in Net Assets	Amount of Loss on Derivatives Recognized in the Statement of Changes in Net Assets	
		2014	2013
Interest exchange agreement	Unrealized gain on interest rate exchange agreement	\$ 56,048	\$ 59,525

Note 18 – Subsequent Events

ASC 855, *Subsequent Events*, establishes financial general standards of accounting for and disclosure of events that occur after the consolidated statement of position date but before the financial statements are issued. The University has evaluated subsequent events through September 16, 2014, which is the date the consolidated financial statements were available to be issued. The University recognizes in the consolidated financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the consolidated statement of financial position, including the estimates inherent in the process of preparing the financial statements. The University does not recognize subsequent events that provide evidence about conditions that did not exist at the date of the consolidated statement of financial position but arose after the consolidated statement of financial position date and before the financial statements are available to be issued.

SUPPLEMENTARY INFORMATION

**CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
CONSOLIDATING STATEMENT OF FINANCIAL POSITION
AS OF MAY 31, 2014**

ASSETS	California Lutheran University	California Lutheran Education Foundation	Total
Cash and cash equivalents	\$ 48,184,334	\$ -	\$ 48,184,334
Receivables			
Student accounts, net	1,637,839	-	1,637,839
Grants	230,388	-	230,388
Contributions	7,180,884	-	7,180,884
Other	1,556,374	-	1,556,374
Student loans receivable, net	1,647,347	-	1,647,347
Prepaid expenses, inventories and deposits	1,796,556	-	1,796,556
Investments			
Endowment	85,671,078	564,775	86,235,853
Deferred gifts held by University	2,998,072	-	2,998,072
California Lutheran Educational Foundation investments	-	6,129,479	6,129,479
Other	972,004	-	972,004
Funds held in trust by others	1,127,054	-	1,127,054
Deposits with trustee - reserved funds	6,932,024	-	6,932,024
Debt acquisition costs	1,894,135	-	1,894,135
Construction in progress	13,524,373	-	13,524,373
Property, plant, and equipment, net	126,600,397	-	126,600,397
Other intangible assets	475,000	-	475,000
TOTAL ASSETS	\$ 302,427,859	\$ 6,694,254	\$ 309,122,113
LIABILITIES AND NET ASSETS			
LIABILITIES			
Accounts payable	\$ 2,714,049	\$ -	\$ 2,714,049
Accrued liabilities	9,276,885	-	9,276,885
Student housing deposits	720,378	-	720,378
Deferred revenue	1,804,449	-	1,804,449
Interest rate exchange agreement liability	111,605	-	111,605
Annuities payable	2,398,073	2,273,001	4,671,074
Deposits held in trust for others	(707,357)	2,727,540	2,020,183
Government grants refundable	1,579,490	-	1,579,490
Long-term debt	70,887,514	-	70,887,514
TOTAL LIABILITIES	88,785,086	5,000,541	93,785,627
NET ASSETS			
Unrestricted	133,643,174	19,231	133,662,405
Temporarily restricted	29,980,248	760,836	30,741,084
Permanently restricted	50,019,351	913,646	50,932,997
TOTAL NET ASSETS	213,642,773	1,693,713	215,336,486
TOTAL LIABILITIES AND NET ASSETS	\$ 302,427,859	\$ 6,694,254	\$ 309,122,113

CALIFORNIA LUTHERAN UNIVERSITY AND AFFILIATE
CONSOLIDATING STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED MAY 31, 2014

	California Lutheran University	California Lutheran Education Foundation	Total
OPERATING			
Revenues, gains and other support			
Tuition and fees	\$ 117,987,734	\$ -	\$ 117,987,734
Less: Scholarships and grants	<u>(39,001,331)</u>	<u>-</u>	<u>(39,001,331)</u>
Net tuition and fees	78,986,403	-	78,986,403
Government and grants	2,196,088	-	2,196,088
Contributions	3,879,947	-	3,879,947
Short-term investment gain	47,485	-	47,485
Long-term investment income and gains allocated for operations	2,539,620	-	2,539,620
Interest and dividends	129,815	-	129,815
Sales and services of educational activities	941,317	-	941,317
Other sources	2,739,455	-	2,739,455
Sales and services of auxiliary enterprises	<u>16,422,770</u>	<u>-</u>	<u>16,422,770</u>
TOTAL REVENUES, GAINS AND OTHER SUPPORT	<u>107,882,900</u>	<u>-</u>	<u>107,882,900</u>
Expenses			
Program Expenses			
Instruction	35,365,289	-	35,365,289
Public service	4,372,595	-	4,372,595
Academic support	6,870,618	-	6,870,618
Student services	19,174,455	-	19,174,455
Auxiliary enterprises	17,619,513	-	17,619,513
Support Expenses			
Institutional support	15,400,191	-	15,400,191
Allocable expenses			
Operation and maintenance of plant	8,356,407	-	8,356,407
Depreciation	6,654,441	-	6,654,441
Interest	3,293,799	-	3,293,799
Less: Allocated expenses	<u>(18,304,647)</u>	<u>-</u>	<u>(18,304,647)</u>
TOTAL OPERATING EXPENSES	<u>98,802,661</u>	<u>-</u>	<u>98,802,661</u>
Change in net assets from operating activities	<u>9,080,239</u>	<u>-</u>	<u>9,080,239</u>
NON-OPERATING			
Endowment income	6,575,471	-	6,575,471
Less: Long-term investment income and gains allocated for operations	<u>(2,539,620)</u>	<u>-</u>	<u>(2,539,620)</u>
Investment return distributed	4,035,851	-	4,035,851
Net gains (losses) on other investments	(52,025)	51,131	(894)
Net (loss) on CEFA bond reserve	(388,572)	-	(388,572)
Unrealized gain on interest rate exchange agreement	56,048	-	56,048
Deferred giving - gifts	5,119,516	-	5,119,516
Capital giving - gifts	6,293,744	-	6,293,744
Gains on funds held in trust by others	357,341	-	357,341
Adjustment to actuarial liability for annuities payable	175,717	14,756	190,473
Loss on disposal of property, plant and equipment	(75,936)	-	(75,936)
Acquisition - inherent contribution	<u>19,223,452</u>	<u>-</u>	<u>19,223,452</u>
Change in net assets from nonoperating activities	<u>34,745,136</u>	<u>65,887</u>	<u>34,811,023</u>
CHANGE IN NET ASSETS	<u>43,825,375</u>	<u>65,887</u>	<u>43,891,262</u>
NET ASSETS, beginning of year	<u>169,817,398</u>	<u>1,627,826</u>	<u>171,445,224</u>
NET ASSETS, end of year	<u>\$ 213,642,773</u>	<u>\$ 1,693,713</u>	<u>\$ 215,336,486</u>