

PACIFIC LUTHERAN UNIVERSITY
Tacoma, Washington

Financial Statements
Including Independent Auditors' Report

May 31, 2008 and 2007

PACIFIC LUTHERAN UNIVERSITY

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May 31, 2008 and 2007

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INDEPENDENT AUDITORS' REPORT

To the Board of Regents
Pacific Lutheran University
Tacoma, Washington

We have audited the accompanying statements of financial position of Pacific Lutheran University as of May 31, 2008 and 2007 and the related 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. 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 also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 financial statements referred to above present fairly, in all material respects, the financial position of Pacific Lutheran University at May 31, 2008 and 2007 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.

Virchow, Krause & Company, LLP

Minneapolis, Minnesota
October 21, 2008

PACIFIC LUTHERAN UNIVERSITY
STATEMENTS OF FINANCIAL POSITION
 May 31, 2008 and 2007

ASSETS		
	2008	2007
Cash and cash equivalents	\$ 15,680,203	\$ 11,154,462
Student receivables, net of allowance for doubtful accounts of \$325,000 and \$313,000	1,117,185	916,964
Other receivables	203,320	210,822
Real estate contracts receivable	243,856	276,417
Grants receivable	1,903,320	591,607
Contributions receivable	6,968,630	11,252,800
Inventories	1,442,252	1,131,870
Prepaid expenses and deposits	1,381,404	1,012,307
Real estate	2,942,311	3,942,883
Student notes receivables, net of allowance for doubtful accounts of \$425,000 and \$400,000	8,073,111	7,589,495
Investments	13,500,461	13,785,736
Endowment investments	67,323,051	64,833,681
Deposits held by trustee		
Cash and short-term investments	5,833,880	24,974,688
U.S. government securities		
Bond acquisition costs	1,583,849	1,638,464
Construction in progress	5,099,723	9,460,147
Property, plant and equipment, net	102,010,178	80,222,640
TOTAL ASSETS	\$ 235,306,734	\$ 232,994,983
LIABILITIES AND NET ASSETS		
LIABILITIES		
Accounts payable	\$ 2,840,395	\$ 4,210,403
Accrued liabilities	7,444,602	6,161,551
Student deposits	1,603,741	1,315,391
Asset retirement obligation	1,062,045	1,392,904
Long-term debt	61,367,253	62,315,234
Unamortized premium on long-term debt	1,157,285	1,197,191
Annuities payable	6,563,645	6,203,360
Deposits held in custody for others	1,657,034	1,618,243
Government grants refundable	8,384,375	7,441,740
Total Liabilities	92,080,375	91,856,017
NET ASSETS		
Unrestricted	67,254,749	70,817,927
Temporarily restricted	14,044,539	11,198,665
Permanently restricted	61,927,071	59,122,374
Total Net Assets	143,226,359	141,138,966
TOTAL LIABILITIES AND NET ASSETS	\$ 235,306,734	\$ 232,994,983

See accompanying notes to financial statements.

PACIFIC LUTHERAN UNIVERSITY

STATEMENT OF ACTIVITIES
 Year Ended May 31, 2008
 With Comparative Totals for 2007

	2008			2007 Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
REVENUES, GAINS AND OTHER SUPPORT				
Tuition and fees	\$ 87,857,211			\$ 87,857,211
Less: Scholarships and grants	(31,441,679)			(28,113,326)
Net tuition and fees	56,415,532			53,621,112
Government grants	2,452,063			2,608,575
Private gifts	2,695,993	\$ 11,024,219	\$ 4,112,823	19,147,527
Endowment income and gains (losses)	(1,873,982)	3,049,908	(16,663)	6,846,298
Gains (losses) in perpetual trusts			(579,437)	916,271
Other investment income	228,311			890,683
Sales and services of educational activities	135,477			139,297
Other sources	641,274	374,463	70	585,567
Sales and services of auxiliary enterprises	16,565,263			15,595,974
	77,259,931	14,448,590	3,516,793	100,351,304
Reclassification of net assets	(180,877)	31,129	149,748	
Net assets released from restrictions	11,175,606	(11,175,606)		
Total Revenues, Gains and Other Support	88,254,660	3,304,113	3,666,541	95,225,314
EXPENSES AND LOSSES				
Program expenses				
Instruction	36,941,501			35,423,858
Research	468,757			333,734
Public service	7,032,397			6,772,929
Academic support	5,467,297			5,512,634
Student services	9,832,321			9,345,194
Auxiliary enterprises	15,929,682			13,298,773
Support expenses				
Institutional support	15,982,398			15,258,196
Allocable expenses				
Operation and maintenance of plant	7,668,290			7,876,684
Interest expense	2,900,624			2,335,146
Depreciation expense	4,214,499			3,834,290
Amortization expense	113,706			
Accretion expense	50,500			97,904
Less: Allocated expenses	(14,947,619)			(14,144,024)
Adjustment of actuarial liability for annuities payable	128,870	97,529	536,729	(618,348)
Loss on contributions receivable	34,615	360,710	325,115	53,580
Loss on debt refunding				2,287,479
Total Expenses and Losses	91,817,838	458,239	861,844	87,668,029
Change in Net Assets	(3,563,178)	2,845,874	2,804,697	12,683,275
NET ASSETS - Beginning of Year	70,817,927	11,198,665	59,122,374	128,455,691
NET ASSETS - END OF YEAR	\$ 67,254,749	\$ 14,044,539	\$ 61,927,071	\$ 141,138,966

See accompanying notes to financial statements.

PACIFIC LUTHERAN UNIVERSITY

STATEMENT OF ACTIVITIES
Year Ended May 31, 2007

	2007			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
REVENUES, GAINS AND OTHER SUPPORT				
Tuition and fees	\$ 81,734,438			\$ 81,734,438
Less: Scholarships and grants	(28,113,326)			(28,113,326)
Net tuition and fees	53,621,112			53,621,112
Government grants	2,608,575			2,608,575
Private gifts	1,736,789	\$ 15,531,067	\$ 1,879,671	19,147,527
Endowment income and gains	961,690	5,314,800	569,808	6,846,298
Gains on perpetual trusts			916,271	916,271
Other investment income	890,683			890,683
Sales and services of educational activities	139,297			139,297
Other sources	555,037		30,530	585,567
Sales and services of auxiliary enterprises	15,595,974			15,595,974
	76,109,157	20,845,867	3,396,280	100,351,304
Reclassification of net assets per donor request		400,000	(400,000)	
Net assets released from restrictions	15,974,824	(15,974,824)		
Total Revenues, Gains and Other Support	92,083,981	5,271,043	2,996,280	100,351,304
EXPENSES AND LOSSES				
Program expenses				
Instruction	35,423,858			35,423,858
Research	333,734			333,734
Public service	6,772,929			6,772,929
Academic support	5,512,634			5,512,634
Student services	9,345,194			9,345,194
Auxiliary enterprises	13,298,773			13,298,773
Support expenses				
Institutional support	15,258,196			15,258,196
Allocable expenses				
Operation and maintenance of plant	7,876,684			7,876,684
Interest expense	2,335,146			2,335,146
Depreciation expense	3,834,290			3,834,290
Accretion expense	97,904			97,904
Less: Allocated expenses	(14,144,024)			(14,144,024)
Adjustment of actuarial liability for annuities payable	(897,605)	248,228	31,029	(618,348)
Loss on contributions receivable		24,309	29,271	53,580
Loss on debt refunding	2,287,479			2,287,479
Total Expenses and Losses	87,335,192	272,537	60,300	87,668,029
Change in Net Assets	4,748,789	4,998,506	2,935,980	12,683,275
NET ASSETS - Beginning of Year	66,069,138	6,200,159	56,186,394	128,455,691
NET ASSETS - END OF YEAR	\$ 70,817,927	\$ 11,198,665	\$ 59,122,374	\$ 141,138,966

See accompanying notes to financial statements.

PACIFIC LUTHERAN UNIVERSITY
 STATEMENTS OF CASH FLOWS
 Years Ended May 31, 2008 and 2007

	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	\$ 2,087,393	\$ 12,683,275
Adjustments to reconcile change in net assets to net cash flows from operating activities		
Depreciation and amortization	4,342,914	3,834,290
Accretion	50,500	97,904
(Gains) losses on endowment investments and perpetual trusts	2,609,501	(5,206,654)
(Gains) losses on investments	347,212	(1,253,036)
Loss on sale of real estate	772,428	10,846
Actuarial adjustment on annuities payable	445,637	1,309,911
Loan cancellations, assignments and write-offs	111,962	108,322
Losses on contributions receivable	720,440	53,580
Loss on debt refunding		2,287,479
Increase in allowance on student receivables	12,000	13,000
Increase in allowance on student notes	25,000	6,000
Change in assets and liabilities		
Student receivables	(212,221)	62,007
Other receivables	7,502	119,124
Grant receivables	(1,311,713)	81,993
Contributions receivable for operations	(528,086)	(104,552)
Inventories, prepaid expense and deposits	(679,479)	(83,040)
Accounts payable and accrued liabilities	872,820	228,312
Student deposits	288,350	111,061
Deposits held in custody for others	38,791	352,982
Contributions of noncash investments	(1,381,090)	(39,846)
Contributions restricted for long-term investment, loans and plant	(5,743,518)	(9,418,354)
Contributions under split-interest agreements	(720,674)	(127,298)
Interest and dividends restricted for reinvestment	(5,338)	(5,074)
Net Cash Flows From Operating Activities	2,150,331	5,122,232
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of endowment investments	(17,468,134)	(20,300,853)
Sales of endowment investments	12,449,353	18,347,739
Purchases of investments	(3,593,619)	(48,676,134)
Sales of investments	3,531,682	49,799,972
Proceeds from sale of real estate	1,529,144	299,535
Withdrawals of deposits held by trustee, net	19,140,808	6,495,806
Purchases of property, plant and equipment	(22,715,096)	(11,645,177)
Reductions of asset retirement obligation	(381,359)	
Disbursements for real estate contracts		(295,000)
Repayments of real estate contract receivables	32,561	32,694
Disbursements of loans to students	(1,759,441)	(1,860,171)
Repayments of loans from students	1,138,863	1,633,096
Net Cash Flows From Investing Activities	(8,095,238)	(6,168,493)
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayments of principal on indebtedness	(947,981)	(717,296)
Contributions received restricted for long-term investment, loans and plant	9,835,334	7,032,087
Proceeds from issuance of split-interest agreements	1,532,297	260,203
Receipts of interest and dividends restricted for reinvestment	5,338	5,074
Payments to annuitants	(896,975)	(923,738)
(Increase) decrease in government grants refundable	942,635	(48,910)
Net Cash Flows From Financing Activities	10,470,648	5,607,420
 Net Change in Cash and Cash Equivalents	 4,525,741	 4,561,159
CASH AND CASH EQUIVALENTS - Beginning of year	11,154,462	6,593,303
 CASH AND CASH EQUIVALENTS - END OF YEAR	 \$ 15,680,203	 \$ 11,154,462
Supplemental disclosure of cash flow statement		
Interest paid	\$ 2,889,832	\$ 2,252,518
Noncash investing and financing activities		
Property, plant and equipment acquired through accounts payable	1,580,687	2,540,464
Principal on debt defeased with new debt proceeds		12,185,000
Principal on debt repaid with new debt proceeds		20,535,000
Debt acquisition costs paid with debt proceeds		1,638,464
Debt proceeds deposited into trustee accounts		27,792,368

PACIFIC LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS May 31, 2008 and 2007

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

Pacific Lutheran University (the "University") is an institution of higher education affiliated with the Evangelical Lutheran Church in America. The accounting policies of the University reflect practices common to universities and colleges and conform to accounting principles generally accepted in the United States of America. The more significant accounting policies are summarized below:

General - The University maintains its accounts in accordance with the principles and practices of fund accounting. Fund accounting is the procedure by which resources for various purposes are classified for accounting purposes in accordance with activities or objectives specified by donors.

These financial statements, which are presented on the accrual basis of accounting, have been prepared to focus on 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 fund balances and transactions into three classes of net assets-permanently restricted, temporarily restricted or unrestricted, as follows.

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

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

Unrestricted Net Assets - Net assets not subject to donor-imposed stipulations.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassifications between the applicable classes of net assets.

Contributions of assets other than cash are recorded at their estimated fair value at the date of the gift.

Income and net gains on investments of endowment and similar funds are reported as follows:

- 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;
- as increases in unrestricted net assets in all other cases.

PACIFIC LUTHERAN UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
May 31, 2008 and 2007

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Losses from investments on permanently restricted endowment funds are reported as reductions in temporarily restricted assets to the extent of prior accumulated earnings reported as such, if any, with the remaining net losses reported as reductions in the unrestricted quasi-endowment funds.

Temporarily Restricted Net Assets - With respect to temporarily restricted net assets, the University has adopted the following accounting policies:

Reporting as Temporarily Restricted Revenues - 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 reclassification to unrestricted net assets is made to reflect the expiration of such restrictions.

Release of Restrictions on Net Assets for Acquisition of Land, Buildings and Equipment - Contributions of land, buildings and equipment are reported as revenues of the unrestricted net asset class. Contributions of cash or other assets to be used to acquire land, buildings and equipment are reported as revenues of the temporarily restricted net asset class; the restrictions are considered to be released at the time such long-lived assets are placed in service.

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

Receivables - Student accounts receivable are carried at the unpaid balance of the original amount billed to students and student notes receivable are carried at the amount of unpaid principal. Both receivables are less an estimate made for doubtful accounts based on a review of all outstanding amounts. Management determines the allowance for doubtful accounts by identifying troubled accounts and by using historical experience applied to an aging of accounts. Student accounts and loans receivable are written-off when deemed uncollectible. Recoveries of student accounts and loans receivable previously written-off are recorded when received. Receivables are generally unsecured.

After a student is no longer enrolled in an institution of higher education and after a grace period, interest is charged on Perkins and Nursing student loan receivables and is recognized as it is charged. Perkins and Nursing student loan receivables 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. 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. The Perkins Loan Program receivables may be assigned to the U.S. Department of Education.

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

PACIFIC LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS
May 31, 2008 and 2007

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Real Estate - Real estate consists of land held for resale of \$2,498,241 and \$3,498,813 and other real estate of \$444,070 and \$444,070 at May 31, 2008 and 2007, respectively. The land held for resale is recorded at cost except those items received as gifts which are valued at fair market value at the date of the gift. The other real estate is recorded at market value.

Deposits Held By Trustee - Deposits held by trustee include amounts restricted for debt service as required by the trust indentures.

Bond Acquisition Costs - Costs of bond issuance are deferred and amortized over the term of the related indebtedness.

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

Pension Plans - The University has certain contributory defined contribution pension plans for academic and nonacademic personnel. Individual contributions are based on a percentage of compensation. The University pays the cost of the retirement plans currently. The contributions amounted to approximately \$3,107,000 and \$2,935,000 for the years ended May 31, 2008 and 2007, respectively.

Grants to Specified Students - Amounts received from state and federal agencies designated for the benefit of specified students are considered agency transactions and, therefore, are not reflected as revenues and expenses of the University. The amount of such grants for the years ended May 31, 2008 and 2007 were as follows:

	<u>2008</u>	<u>2007</u>
State agency grants	\$ 3,560,366	\$ 3,173,214
Federal agency grants	2,169,797	2,149,781

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

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

PACIFIC LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS

May 31, 2008 and 2007

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Federal Income Taxes - The Internal Revenue Service has determined the University qualifies under the provisions of Section 501(c)(3) of the Internal Revenue Code as a not-for-profit organization. However, any unrelated business may be subject to taxation. Donations to the University are tax deductible.

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

Fair Value of Financial Instruments - The carrying amounts of cash and cash equivalents, student receivables, other receivables, accounts payable and deposits held in custody for others are reasonable estimates of fair value due to the short-term maturity of these financial instruments. The beneficial interest in perpetual trusts is reported at fair value of the trust assets.

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 annuities payable approximate fair value based on life expectancies, quoted market prices, and the present value discount included in the carrying amount. The carrying amounts of long-term debt approximate fair value because these financial instruments bear interest at rates which approximate current market rates for notes with similar maturities and credit quality.

Investments in securities traded on national or international securities exchanges are carried at fair value based on values provided by external investment managers or quoted market values. Investments in hedge funds, private equity funds, real estate funds, fund of hedge funds and similar nonmarketable equity interests consist primarily of investments that are not readily marketable. Investments in these categories, which are managed externally, are valued utilizing the most current information provided by the general partner or investment manager. These valuations generally reflect discounts for illiquidity and consider variables such as financial performance of investments, recent sales prices of investments and other pertinent information. Where applicable, independent appraisers are utilized to assist in the valuation. These values are determined under the direction of, and subject to approval by, management and the Investment Committee of Pacific Lutheran University.

PACIFIC LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS
May 31, 2008 and 2007

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

The preparation of financial statements requires management to make estimates and assumptions about the effects of matters that are inherently uncertain. The accounting policies considered potentially significant in this respect are the valuation of the hedge funds, private equity funds, real estate funds, fund of hedge funds and similar nonmarketable equity interests. Values for these instruments are often estimated using techniques such as discounted cash flow analysis and comparisons to similar instruments. Estimates developed using these methods are subjective and require judgment regarding significant matters such as the amount and timing of future cash flows and the selection of discount rates that appropriately reflect market and credit risks. Estimates, by their nature, are based on judgment and available information. Changes in assumptions could have a significant effect on the fair value of the instruments. Actual results could differ from these estimates and could have a material impact on the financial statements.

Fund-Raising and Advertising Expenses - Fund-raising expenses totaled \$2,762,000 and \$2,301,000 for the years ended May 31, 2008 and 2007, respectively. Advertising costs are expensed when incurred.

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

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 estimate of the losses that are probable from environmental remediation liabilities for asbestos removal was calculated using the expected cash flow approach and based on an inventory of the University's long-lived assets combined with an estimate of the current market prices to remove the asbestos. The University utilized a credit-adjusted risk-free rate to discount the asset retirement obligation. It is reasonably possible that changes in this estimate could occur and that actual results could differ from this estimate and could have a significant effect on the financial statements.

New Accounting Pronouncements - In February 2007, the FASB issued Statement on Financial Accounting Standards No. 159 (SFAS 159), *The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment of FASB Statement No. 115*, which provides all entities with an option to report selected financial assets and liabilities at fair value. Certain specified items are eligible for the irrevocable fair value measurement option as established by SFAS 159. SFAS 159 is effective as of the beginning of an entity's first fiscal year beginning after November 15, 2007. The University is currently evaluating the impact that the adoption of this Statement will have on its financial position, results of operations and cash flows.

PACIFIC LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS
May 31, 2008 and 2007

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

In September 2006, the FASB issued Statement on Financial Accounting Standards No. 157 (SFAS 157), *Fair Value Measurements*. SFAS 157 establishes a single authoritative definition of fair value, sets out a framework for measuring fair value and requires additional disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. The University has not yet completed its analysis of the effects of this interpretation and has not determined if the adoption of SFAS 157 will have a material impact on the financial statements.

In August 2008, the FASB issued FASB Staff Position FSP 117-1, *Endowments of Not-for-Profit Organizations: Net Asset Classifications of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures*. The FSP provides guidance on classifying net assets associated with donor-restricted endowment funds held by organizations that are subject to an enacted version of Uniform Prudent Management of Institutional Funds Act (UPMIFA) which serves as a model act for states to modernize their laws governing donor-restricted endowment funds. FSP 117-1 is effective for financial statements issued for fiscal years ending after December 15, 2008. The University is currently evaluating the impact that the adoption of this Statement will have on its net assets.

NOTE 2 - RESTRICTIONS AND LIMITATIONS ON NET ASSET BALANCES

Permanently restricted net assets consist of the following at May 31, 2008 and 2007:

	2008	2007
Endowment funds	\$ 54,694,227	\$ 50,163,492
Contributions receivable	2,692,017	4,291,105
Student loan funds	231,233	225,825
Annuity, life income and similar funds	4,309,594	4,441,952
	\$ 61,927,071	\$ 59,122,374

Temporarily restricted net assets consist of the following at May 31, 2008 and 2007:

Gifts and other unexpended revenues and gains		
Available for:		
Scholarships, instruction and other departmental support	\$ 3,332,042	\$ 3,368,301
Contributions receivable for operations	528,086	123,609
Acquisition of buildings and equipment	5,735,497	2,442,319
Contributions receivable for acquisition of buildings and equipment	2,965,426	3,652,242
	12,561,051	9,586,471
Annuity, life income and similar funds	1,483,488	1,612,194
	\$ 14,044,539	\$ 11,198,665

PACIFIC LUTHERAN UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
 May 31, 2008 and 2007

NOTE 2 - RESTRICTIONS AND LIMITATIONS ON NET ASSET BALANCES (Continued)

At May 31, 2008 and 2007, the University's unrestricted net assets were allocated as follows:

	2008	2007
Operations	\$ 1,404,397	\$ 2,184,513
Long-term investment (quasi-endowment funds)	17,086,498	18,304,677
Annuity, life income and similar funds	1,046,614	1,328,217
Loans to students	833,673	813,834
Plant	46,883,567	48,186,686
	\$ 67,254,749	\$ 70,817,927

NOTE 3 - NET ASSETS RELEASED FROM RESTRICTIONS

Net assets released from temporary donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of events specified by the donors during the years ended May 31, 2008 and 2007 were as follows:

	2008	2007
Acquisition of land, building and equipment	\$	\$ 14,502
Expended for plant facilities	26,167	2,753,742
Scholarships, instruction and other departmental support	11,149,439	13,206,580
	\$ 11,175,606	\$ 15,974,824

These assets were reclassified to unrestricted net assets.

PACIFIC LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS
May 31, 2008 and 2007

NOTE 4 - CONTRIBUTIONS RECEIVABLE

Contributions receivable at May 31, 2008 and 2007 include the following unconditional promises to give:

	2008	2007
Unrestricted - completed construction projects	\$ 900,641	\$ 3,644,347
Temporarily restricted - operations	639,222	122,910
Temporarily restricted - plant projects	3,938,392	4,799,235
Permanently restricted - endowment	3,623,608	5,194,197
Gross unconditional promises to give	9,101,863	13,760,689
Less: Allowance for uncollectible promises	(910,186)	(1,376,069)
Less: Unamortized discount	(1,223,047)	(1,131,820)
Net Unconditional Promises to Give	\$ 6,968,630	\$ 11,252,800
Amounts due in:		
Less than one year	\$ 2,464,378	
One to five years	5,123,751	
More than five years	1,513,734	
	\$ 9,101,863	

Promises due in more than one year were discounted at an interest rate of 6% at May 31, 2008 and 2007. Promises due in less than one year were not discounted. Contributions receivable from related parties at May 31, 2008 and 2007 were \$792,268 and \$2,925,851, respectively.

NOTE 5 - INVESTMENTS

The following summarizes the University's investments in funds other than endowment funds at May 31, 2008 and 2007:

	2008		2007	
	Fair Value	Cost	Fair Value	Cost
Cash and short term investments	\$ 299,854	\$ 299,854	\$ 88,004	\$ 88,004
Marketable securities				
Stocks	7,216,480	7,415,963	7,384,821	6,794,798
Corporate bonds and federal government obligations	5,529,308	5,600,008	5,930,989	5,944,334
Other	454,819	454,819	381,922	446,960
	\$ 13,500,461	\$ 13,770,644	\$ 13,785,736	\$ 13,274,096

PACIFIC LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS
May 31, 2008 and 2007

NOTE 6 - ENDOWMENT INVESTMENTS

The following summarizes the University's endowment investments at May 31, 2008 and 2007:

	2008		2007	
	Fair Value	Cost	Fair Value	Cost
Cash and short term investments	\$ 4,409,606	\$ 4,409,606	\$ 5,555,561	\$ 5,555,561
Commodity mutual funds	4,703,297	2,931,971	3,690,017	3,188,148
Domestic equity mutual funds	8,748,992	7,539,165	12,418,089	9,079,649
Fixed income mutual funds	2,800,316	2,734,916	5,020,769	5,078,960
Index funds			1,322,297	1,134,387
International equity mutual funds	10,046,890	9,334,607	6,598,000	4,284,291
Alternative investments				
Hedge funds	18,523,656	15,590,178	13,754,920	10,635,437
Funds of hedge funds	2,027,044	1,179,764	2,056,739	1,329,764
Real estate	7,339,220	6,868,347	4,417,872	4,076,827
Real estate contracts	774,288	774,288	792,151	792,151
Private equity funds	1,097,017	2,090,033	1,032,009	1,944,635
	60,470,326	53,452,875	56,658,424	47,099,810
Perpetual trusts held by others	10,212,044	10,212,044	10,791,481	10,791,481
Life insurance	1,098,355	1,098,355	1,018,265	1,018,265
	71,780,725	64,763,274	68,468,170	58,909,556
Less Interfund Amounts:				
Cash and short term investments	3,831,876	3,831,876	2,990,828	2,990,828
Real estate contracts	625,798	625,798	643,661	643,661
	\$ 67,323,051	\$ 60,305,600	\$ 64,833,681	\$ 55,275,067

Total investment return on endowment funds for the years ended May 31, 2008 and 2007 follows:

	2008	2007
Dividends and interest, net of fees of \$261,380 and \$182,482	\$ 2,725,178	\$ 1,552,478
Investment income distributed from perpetual trusts held by others	464,148	490,256
Net gains (losses) on investments recorded at market value	(2,030,063)	4,285,859
Gain on sale of perpetual trust property		517,705
	\$ 1,159,263	\$ 6,846,298

Included in the above investment listing are alternative investments. These 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 investment subcommittee of the Board of Regents and the University's external investment consultants review reports provided by the general partners and 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 the investment policy.

PACIFIC LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS
May 31, 2008 and 2007

NOTE 6 - ENDOWMENT INVESTMENTS (Continued)

The amount of investment income and realized and unrealized gains and losses from hedge funds, funds of hedge funds, real estate, real estate contracts and private equity funds totaled \$506,223 and \$1,488,706 for the years ended May 31, 2008 and 2007, respectively, and are included in the above gains (losses) on investments.

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

As of May 31, 2008, the University has commitments to make further investments in several of its alternative investments totaling approximately \$3,787,000.

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

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

NOTE 7 - CONSTRUCTION IN PROGRESS

At May 31, 2008, the following major building projects were in progress:

	<u>Cost To Date</u>	<u>Estimated Completion Date</u>	<u>Funding Source</u>
Hinderlie Residence Hall	\$ 67,966	August 2008	Operations
Eastvold	2,207,900	Unknown	Private Grants
Martin J. Neeb Broadcast Center	2,450,559	February 2009	Private Grants
Rieke Science Center	86,834	Unknown	Operations
Olson Auditorium	286,464	Unknown	Private Grants
	<u>\$ 5,099,723</u>		

Remaining commitments on signed construction contracts totaled approximately \$7,313,000 as of May 31, 2008.

PACIFIC LUTHERAN UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
 May 31, 2008 and 2007

NOTE 8 - PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consisted of the following at May 31, 2008 and 2007:

	2008	2007
Land	\$ 1,797,038	\$ 1,797,038
Buildings and building improvements	120,243,320	98,856,359
Improvements other than buildings	5,104,025	5,040,608
Equipment and automobiles	30,080,851	27,818,774
Library books	12,600,225	12,475,754
Leasehold improvements	1,712,955	
Nondepreciated assets	928,700	928,700
	172,467,114	146,917,233
Less: Accumulated depreciation and amortization	(70,456,936)	(66,694,593)
	\$ 102,010,178	\$ 80,222,640

NOTE 9 - LONG-TERM DEBT

Long-term debt at May 31, 2008 and 2007 consisted of the following:

	2008	2007
Loan payable to Washington Higher Education Facilities Authority, Series 2006	\$ 61,220,000	\$ 62,160,000
Note payable to Jacqueline Colacurcio	147,253	155,234
	\$ 61,367,253	\$ 62,315,234

In August 1996, the University entered into a loan and security agreement with the Washington Higher Education Facilities Authority for the Authority to sell Series 1996 Revenue and Refunding Bonds in the amount of \$24,980,000. Interest was payable semi-annually on each November 1 and May 1 at rates ranging from 5.10% to 5.80%. Serial bonds were payable in amounts ranging from \$575,000 to \$710,000 on November 1, 2007 through November 1, 2011. Term bonds in the amounts of \$4,220,000 and \$13,120,000 were due November 1, 2016 and 2026, respectively. The term bonds were subject to annual sinking fund payments on November 1, in the years 2012 to 2026, in amounts varying from \$750,000 to \$1,675,000. The bonds were issued for the purposes of refinancing the series 1990 loan and for construction and plant improvement projects. The debt was secured by a deed of trust on the dormitory buildings, the University Center, the Administration Building, the Mortvedt Library, Rieke Science Center, Aide Ingram Hall, the Mary Baker Russell Music Building and the land upon which each is located, certain unimproved land adjacent thereto and a security interest in the unrestricted current fund revenues of the University. In December, 2006, these bonds were repaid with proceeds from the 2006 borrowing.

PACIFIC LUTHERAN UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
 May 31, 2008 and 2007

NOTE 9 - LONG-TERM DEBT (Continued)

In September 1999, the University entered into a loan and security agreement with the Washington Higher Education Facilities Authority for the Authority to sell Series 1999 Revenue Bonds in the amount of \$13,000,000. Interest was payable semi-annually on each November 1 and May 1 at rates ranging from 4.95% to 5.95%. Term bonds in the amounts of \$1,000,000, \$1,330,000, \$1,850,000 and \$7,890,000 were due November 1, 2007, 2015, 2019 and 2029, respectively. The term bonds were subject to annual sinking fund payments on November 1, in 2007 and 2012 to 2029, in amounts varying from \$185,000 to \$1,050,000. Serial bonds were payable in amounts ranging from \$200,000 to \$265,000 on November 1, 2008 through 2011. The bonds were issued for the purpose of construction and plant improvement projects to the extent that proceeds were available. These projects include the construction of South Hall Residential Apartments, and other projects such as adding parking spaces, renovation of Xavier and Eastvold Halls, other residential halls, the University Center Dining Commons, and the Morken Center for Learning and Technology. In December, 2006, these bonds were defeased using proceeds of the 2006 borrowing.

In December 2006, the University entered into a loan and security agreement with the Washington Higher Education Facilities Authority for the Authority to sell Series 2006 Revenue and Refunding Bonds in the amount of \$62,160,000. Interest is payable semi-annually on each November 1 and May 1 at rates ranging from 4.25% to 5.00%. Serial bonds are payable in amounts ranging from \$985,000 to \$2,300,000 on November 1, 2008 through November 1, 2025. Term bonds in the amounts of \$16,085,000 and \$17,080,000 are due November 1, 2031 and 2036, respectively. The term bonds are subject to annual sinking fund payments on November 1, in the years 2026 to 2036, in amounts varying from \$2,400,000 to \$3,730,000. The bonds were issued for the purposes of refinancing the series 1996 and series 1999 loans and for construction and plant improvement projects to the extent that proceeds are available. These projects include the renovation and improvement of various residence halls on the University campus, including energy improvements, security system enhancement, utility system replacement and improvements, and space improvements to add additional bathrooms and enhance the efficiency of the residence halls. The University renovated and upgraded the dining facilities located in the University Center. The University Center expanded the commons area, relocated a number of offices and expanded meeting room space and student organization office space. The University has pledged its unrestricted revenues to the repayment of its obligations under the loan agreement.

In addition, the loan agreements with the Washington Higher Education Facilities Authority require the University to comply with certain financial and other covenants.

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

The approximate principal and sinking fund payment requirements for all long-term debt for the five years subsequent to May 31, 2008 are:

<u>Year Ended May 31</u>	<u>Principal</u>
2009	\$ 994,000
2010	1,044,000
2011	1,100,000
2012	1,156,000
2013	1,217,000

PACIFIC LUTHERAN UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
May 31, 2008 and 2007

NOTE 10 - OPERATING LEASES

The University has an operating lease for equipment. Rental expense associated with this lease totaled \$248,600 and \$232,600 for the years ended May 31, 2008 and 2007, respectively. Future minimum lease payments on this operating lease are as follows:

<u>Year Ended May 31</u>	<u>Amount</u>
2009	\$ 248,600
2010	248,600
2011	248,600
2012	41,400

The University is the lessee for a retail building facility under a 15 year operating lease agreement which expires in 2022. After 15 years, the University has the option to renew the lease up to seven five-year lease terms. Rental expense associated with this lease totaled \$292,404 for the year ended May 31, 2008. Future minimum lease payments are as follows:

<u>Year Ended May 31</u>	<u>Amount</u>
2009	\$ 347,910
2010	347,910
2011	347,910
2012	356,910
2013	374,910

The University is the lessor for communications equipment and facilities under two operating lease agreements, one that began on October 1, 1999 and expires on September 30, 2014, and one that began on February 1, 2005 and expires on January 31, 2020. There are renewal options at the end of the lease terms for both. Rental income received was \$70,744 and \$67,860 for the years ended May 31, 2008 and 2007, respectively. Future minimum lease revenues on these operating leases are as follows:

<u>Year Ended May 31</u>	<u>Amount</u>
2009	\$ 74,000
2010	77,000
2011	80,000
2012	88,000
2013	88,000

PACIFIC LUTHERAN UNIVERSITY
NOTES TO FINANCIAL STATEMENTS
May 31, 2008 and 2007

NOTE 11 - DEFERRED GIFT AGREEMENTS

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

When a gift is received under one of these arrangements, it is split into the amount representing the actuarial present value of future distributions back to the donor and the remaining gift value to be retained for the benefit of the University or third-party beneficiaries. The actuarial liability is adjusted annually using actuarial tables appropriate for the type of arrangement, number of lives covered and age and sex characteristics of the donor. The University used interest rates ranging from of 3.1% to 11.7% in making the calculations at May 31, 2008 and 2007, respectively.

The University received \$720,674 and \$127,298 of gift value relating to deferred gift agreements for the years ended May 31, 2008 and 2007, respectively. Total assets held by the University under deferred gift agreements totaled \$14,304,343 and \$14,493,218 at May 31, 2008 and 2007, respectively.

NOTE 12 - CONCENTRATION OF CREDIT RISK

Financial instruments that potentially subject the University to concentrations of credit risk consist principally of cash, short-term investments, marketable securities and other investments, accounts, notes receivable, real estate contracts receivable and other receivables. The University limits the amount of credit exposure to any one financial institution; however, cash balances may periodically exceed federally insured limits. Marketable securities, consisting of both debt and equity instruments, are generally placed in a variety of managed funds administered by different investment managers in order to limit credit risk. Concentrations of credit risk with respect to the real estate contracts receivable are limited due to the University holding a secured position in these agreements. Student notes and receivables and other receivables are due from a variety of sources concentrated primarily in the northwestern United States. In addition, the University's students receive a substantial amount of support from state and federal student financial assistance programs which are subject to audit by governmental agencies. A significant reduction in the level of this support, if this were to occur, could have an adverse effect on the University's programs and activities.

PACIFIC LUTHERAN UNIVERSITY

NOTES TO FINANCIAL STATEMENTS
May 31, 2008 and 2007

NOTE 13 - RELATED PARTY TRANSACTIONS

As of May 31, 2008, the University has a signed contract with a construction company owned by the spouse of a member of the Board of Regents to construct the new Martin J. Neeb Broadcast Center in the amount of \$5,767,299. The contract was approved in accordance with the Board of Regents' conflict of interest policy. Also as of that date, the University owed the construction company \$813,417 which is included in accounts payable on the statements of financial position.

The University has entered into a partnership agreement, effective April 20, 2006 to form Garfield Commons LLC, a commercial retail project located in Parkland two blocks from the University's main entrance. The University has a 49% ownership interest in the LLC, and applies the equity method of accounting for its investment. The other investee, Lorig/Garfield Commons, LLC, has a 51% ownership in the partnership. The property upon which the commercial building was constructed constituted the University's capital contribution in the LLC. As part of the agreement, the University's bookstore became a tenant of the building in the summer of 2007. Terms of a separate lease agreement between the University, as a lessee and the LLC, as the lessor, commenced at that time (see Note 10).

NOTE 14 - SUBSEQUENT EVENT

Subsequent to May 31, 2008, the investment markets have experienced a significant decline in value. It is highly likely that the values of the University's investments have decreased by material amounts since May 31, 2008.

In addition, effective September 29, 2008, participants in the Common Fund Short Term Fund (the "Short Term Fund") have had their liquidity in the Short Term Fund substantially restricted. Wachovia Bank, as trustee, is initiating the termination of the Short Term Fund, no longer accepting deposits, establishing procedures for liquidation and distribution of the Short Term Fund's assets and is resigning as trustee. Wachovia Bank has limited the ability of institutions to withdraw funds from the Short Term Fund and has established a time line for liquidation based on the maturities of the underlying securities. Participants have not to date incurred any losses to their invested principal, and the Common Fund is seeking a successor trustee for the Short Term Fund in order to re-establish the program in largely the same form. At May 31, 2008, the University had \$14,339,778 invested in the Short Term Fund, which was included in Cash and Cash Equivalents on the Statements of Financial Position. However, as of October 10, 2008, the University had \$ 10,809,088 invested in the Short Term Fund. The University believes that it has sufficient cash reserves available from other resources to cover operating costs until it is able to withdraw all of its cash from the Short Term Fund.