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SOUTHERN METHODIST UNIVERSITY

CONSOLIDATED FINANCIAL STATEMENTS

May 31, 2011 and 2010

(With Independent Auditors' Report Thereon)

KPMG LLP
Suite 3100
717 North Harwood Street
Dallas, TX 75201-6585

Independent Auditors' Report

The Board of Trustees
Southern Methodist University:

We have audited the accompanying consolidated balance sheets of Southern Methodist University (the University) as of May 31, 2011 and 2010, and the related consolidated statements of activities and cash flows for the years then ended. These consolidated financial statements are the responsibility of the University's management. 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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

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

KPMG LLP

September 8, 2011

KPMG LLP is a Delaware limited liability partnership, the U.S. member firm of KPMG International Cooperative ("KPMG International"), a Swiss entity.

Southern Methodist University
Consolidated Balance Sheets
As of May 31, 2011 and 2010
(Dollars in Thousands)

Assets	2011	2010
Cash and cash equivalents (restricted for capital projects: $16,608 in 2011 and $13,330 in 2010)	$ 123,525	$ 115,154
Accounts receivable, less allowance for doubtful accounts of $1,044 in 2011 and $682 in 2010	27,146	21,124
Pledges receivable, net	67,765	63,105
Investments:		
Short-term paper (restricted for debt retirement: $961 in 2011 and $475 in 2010)	$ 86,851	$ 87,537
Stocks	218,261	157,030
Bonds (restricted for debt retirement: $50,787 in 2011 and $51,451 in 2010; restricted for capital projects; $110,082 in 2011 and $0 in 2010)	241,361	140,513
Venture capital	39,202	36,946
Mortgage and other notes receivable, less allowance for doubtful accounts of $642 in 2011 and $504 in 2010	9,855	11,608
Real estate	127,030	112,734
Funds held in trust by others	19,281	16,421
Other	505,763	505,771
Total investments	$ 1,247,604	$ 1,068,560
Property, plant and equipment, at cost, net of accumulated depreciation	683,145	668,662
Other assets	10,982	11,132
Total Assets	$ 2,160,167	$ 1,947,737

Liabilities and Net Assets	2011	2010
Liabilities:		
Accounts payable and accrued expenses	$ 153,425	$ 111,325
Deposits and deferred income	25,518	26,984
Notes payable	781	841
Bonds payable	476,268	360,115
Advances for student loans	2,771	2,708
Total Liabilities	$ 658,763	$ 501,973
Net Assets:		
Unrestricted	$ 457,983	$ 459,313
Temporarily restricted	534,475	493,818
Permanently restricted	508,946	492,633
Total Net Assets	$ 1,501,404	$ 1,445,764
Total Liabilities and Net Assets	$ 2,160,167	$ 1,947,737

See accompanying notes to the consolidated financial statements.

Southern Methodist University
Consolidated Statements of Activities
For the Years Ended May 31, 2011 and 2010
(Dollars in Thousands)

	2011				2010			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenue:								
Tuition and fees	$ 344,008	$ -	$ -	$ 344,008	$ 324,171	$ -	$ -	$ 324,171
Scholarship allowance - tuition and fees	(120,098)	-	-	(120,098)	(107,713)	-	-	(107,713)
Net tuition	$ 223,910	$ -	$ -	$ 223,910	$ 216,458	$ -	$ -	$ 216,458
Gifts	11,360	29,974	15,254	56,588	13,781	19,493	17,593	50,867
Endowment income, net of investment expenses	11,963	11	1,173	13,147	3,906	109	754	4,769
Net realized and unrealized gains on investments	4,943	105,234	(114)	110,063	20,037	47,016	277	67,330
Grants and contracts	30,761	-	-	30,761	24,920	-	-	24,920
Organized activities	8,898	-	-	8,898	9,206	-	-	9,206
Other sources	30,194	-	-	30,194	26,491	-	-	26,491
Auxiliary activities	43,887	-	-	43,887	40,850	-	-	40,850
Scholarship allowance - room and board	(2,557)	-	-	(2,557)	(2,353)	-	-	(2,353)
Independent operations	3,495	-	-	3,495	3,801	-	-	3,801
Total revenue	$ 366,854	$ 135,219	$ 16,313	$ 518,386	$ 357,097	$ 66,618	$ 18,624	$ 442,339
Net assets released from restrictions	94,562	(94,562)	-	-	93,184	(93,184)	-	-
Total adjusted revenue	$ 461,416	$ 40,657	$ 16,313	$ 518,386	$ 450,281	$ (26,566)	$ 18,624	$ 442,339
Expenses:								
Program expenses:								
Instructional	$ 145,451	$ -	$ -	$ 145,451	$ 138,682	$ -	$ -	$ 138,682
Academic support	51,429	-	-	51,429	50,192	-	-	50,192
Research	22,563	-	-	22,563	16,551	-	-	16,551
Organized activities	10,431	-	-	10,431	11,364	-	-	11,364
Student services	40,097	-	-	40,097	36,333	-	-	36,333
Auxiliary activities	55,847	-	-	55,847	50,128	-	-	50,128
Total program expenses	$ 325,818	$ -	$ -	$ 325,818	$ 303,250	$ -	$ -	$ 303,250
Institutional support	131,997	-	-	131,997	86,945	-	-	86,945
Independent operations	4,499	-	-	4,499	4,032	-	-	4,032
Total expenses	$ 462,314	$ -	$ -	$ 462,314	$ 394,227	$ -	$ -	$ 394,227
Postretirement plan changes other than net periodic postretirement benefit cost	432	-	-	432	272	-	-	272
Total expenses and actuarial adjustment	$ 462,746	$ -	$ -	$ 462,746	$ 394,499	$ -	$ -	$ 394,499
Change in net assets	$ (1,330)	$ 40,657	$ 16,313	$ 55,640	$ 55,782	$ (26,566)	$ 18,624	$ 47,840
Net assets at beginning of year	459,313	493,818	492,633	1,445,764	403,531	520,384	474,009	1,397,924
Net assets at end of year	$ 457,983	$ 534,475	$ 508,946	$ 1,501,404	$ 459,313	$ 493,818	$ 492,633	$ 1,445,764

See accompanying notes to the consolidated financial statements.

Southern Methodist University
Consolidated Statements of Cash Flows
For the Years May 31, 2011 and 2010
(Dollars in Thousands)

	2011	2010
Cash flows from operating activities:		
Change in net assets	$ 55,640	$ 47,840
Adjustments to reconcile change in net assets to cash used for operating activities:		
Depreciation	31,627	26,495
Loss on disposal of property, plant and equipment	1,995	96
(Increase) decrease in accounts and pledges receivable	(10,682)	14,157
Decrease in other assets	150	96
Increase (decrease) in accounts payable and accrued expenses for operations	47,591	(5,783)
Decrease in deposits and deferred income and advances for student loans	(1,403)	(480)
Contributions restricted for long-term investment	(21,296)	(30,717)
Non-cash contributions	(7,255)	(12,590)
Net realized and unrealized gains on investments	(110,063)	(63,336)
Income restricted for long-term investment	(1,224)	(952)
Annuity obligation payments	734	687
Other adjustments	(1,955)	(764)
Net cash used for operating activities	$ (16,141)	$ (25,251)
Cash flows from investing activities:		
Purchase of property, plant and equipment	$ (47,970)	$ (64,076)
Proceeds from sales of property, plant and equipment	19	3
Purchase of investments	(344,670)	(379,812)
Proceeds from the sale of investments	281,037	471,996
Decrease in accounts payable and accrued expenses for investments and property, plant and equipment	(5,491)	(17,492)
Disbursements of mortgage and other notes receivable	(1,047)	(2,018)
Principal payments received on and sales of mortgage and other notes receivable	2,800	12,875
Net cash (used for) provided by investing activities	$ (115,322)	$ 21,476
Cash flows from financing activities:		
Contributions restricted for long-term investment	$ 21,296	$ 30,717
Income restricted for long-term investment	1,224	952
Annuity obligation payments	(734)	(687)
Proceeds from notes payable	-	5,911
Payments on notes payable	(60)	(59,992)
Proceeds from bond issue	124,998	162,036
Long-term bond payments	(6,890)	(132,615)
Net cash provided by financing activities	$ 139,834	$ 6,322
Net increase in cash and cash equivalents	8,371	2,547
Cash and cash equivalents at beginning of year	115,154	112,607
Cash and cash equivalents at end of year	$ 123,525	$ 115,154
Supplemental data:		
Gifts of investments and real estate	$ 7,101	$ 11,081
Gifts of property, plant and equipment	154	1,509
Cash paid for interest	17,912	14,310

See accompanying notes to the consolidated financial statements.

1. Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations:

Southern Methodist University (the University) is a private higher education institution providing undergraduate, graduate, and continuing educational opportunities. In addition to the revenue generated by the tuition and fees charged for these educational services, the University receives support from donations, and revenue from investment earnings, sponsored research, athletic events and other auxiliary activities, and other sources.

The University currently has nine corporations under its control that are included in the consolidated financial statements. Peruna Properties, Inc., Pony Properties, Inc., Peruna Holdings Corporation, Mustang Mockingbird Corporation, Mustang Mockingbird Properties, and Mustang Airline Corporation are corporations the University established to acquire, own and manage, on behalf of the University, real estate adjacent to or in the near vicinity of the University campus. The University also has established the Stadium Club, Inc. to operate a private club in the Gerald J. Ford Stadium, the Southern Methodist University Foundation for Research to support academic scholarship and scientific research in the public interest for the benefit of the University and to assist in fulfilling the educational and research purposes of the University, and SMU Corp. in connection with the location of the George W. Bush Presidential Library and Museum at the University. Subsequent to year end, Peruna East Corporation was formed to acquire, own and manage real estate on the east side of campus.

Financial Reporting:

The consolidated financial statements have been prepared in accordance with accounting standards established to provide meaningful information about the financial resources and operations of the University as a whole and to present balances and transactions based on the existence or absence of donor-imposed restrictions. Accordingly, transactions and balances have been classified into three categories of net assets:

Unrestricted net assets include funds that have no donor-imposed restrictions, time restrictions or whose restrictions have been satisfied. The University has determined that any donor-imposed restrictions for currently budgeted programs and activities generally are met within the operating cycle of the University. Therefore, the University's policy is to record these funds as unrestricted.

Temporarily restricted net assets include funds for which donor-imposed restrictions have not been met. This classification includes gifts, annuities and unconditional promises to give for which the ultimate purpose of the proceeds is not permanently restricted.

Permanently restricted net assets include gifts, annuities, and unconditional promises to give that are restricted by the donor to be invested or held in perpetuity. Only the income from these funds is made available for program operations specified by the donor.

Basis of Accounting:

The consolidated financial statements have been prepared on the accrual basis of accounting. The costs of providing various programs and support services have been summarized on a functional basis in the consolidated statements of activities. Accordingly, expenses such as depreciation and the operation and maintenance of University facilities have been allocated among the functional categories. Fundraising expenses of approximately $19,941,000 and $18,765,000 incurred by the University in fiscal years 2011 and 2010, respectively, are included primarily as institutional support expenses reported in the consolidated statements of activities.

Cash equivalents include operating cash investments, U.S. Treasury bills and short-term paper with maturities of three months or less from the date of purchase. However, such assets when purchased with endowment, loan, annuity and life income assets or trust funds are classified as investments.

Investments in short-term paper, stocks, bonds and funds held in trust by others with readily determinable fair values are recorded at fair value. Equity method investments are valued at the University's percentage of the net asset values reported by the fund managers, which are used as practical expedients to estimate the fair values. All other investments are recorded at cost, with disclosure of most recently reported fair values in Note 5, herein. Management monitors the managers and investment strategies of these and other investments to ascertain whether valuations are reasonable and whether the assets are permanently impaired. Permanent impairment losses are recognized when investments' fair values are below their carrying amounts and verifiable positive evidence does not exist to support the recoverability of the investments within a reasonable period of time. Permanent impairment losses were $18,276,000 as of May 31, 2010. None were recognized in fiscal year 2011. For the year ended May 31, 2011, the University has investments in venture capital funds, real estate and other investments that have fair values lower than cost by $30,418,000 that are not reported as permanently impaired. The aggregate related fair value of these investments is $143,039,000.

Gifts are recorded at fair value at the date of donation or a nominal value if fair value is not readily determinable. Recorded realized and unrealized gains on investments are reported in the appropriate net asset classifications in the consolidated statements of activities. Gifts and income thereon that are restricted in perpetuity by the donors for the purpose of making loans to students are reported as permanently restricted net assets. Refundable advances from the federal government for student loans are reported as long-term liabilities. University resources designated for student loans are reported as unrestricted net assets. Federally funded student loan programs consist of $2,771,000 and $2,708,000 of refundable government advances and $318,000 and $311,000 of matching University funds in fiscal years 2011 and 2010, respectively.

Property, plant and equipment (including art objects) are recorded at cost, if purchased, or at the fair value at the time of donation, if donated. During the period qualifying construction projects are in progress, net interest costs are capitalized as part of the basis of capital assets. Capital assets include property, plant and equipment that have an acquisition cost of $5,000 and over and have an estimated useful life of at least two (2) years, with the exception of software, where the cost must exceed $75,000 before the asset will be capitalized. Property, plant and equipment (except for art objects) are depreciated on the straight-line basis over their estimated useful lives with equipment, vehicles, furniture, software and "other" depreciating in 5 to 15 years; land improvements depreciating in 15 to 50 years; and buildings depreciating in 20 to 40 years.

Contributions of land, buildings, and equipment without donor stipulations concerning the use of such long-lived assets are reported as revenue of the unrestricted net asset class. Contributions of cash or other assets to be used to acquire land, buildings, and equipment without such donor stipulations are reported as revenue of the temporarily restricted net asset class. The restrictions are considered to be released when the long-lived assets are placed in service.

The University has adopted an endowment spending policy whereby annually the Board of Trustees authorizes amounts to be spent for the purposes intended by the donors based in part on an index of the prior year allocation for spending and in part on a stipulated percentage of the fair value of endowments participating in the investment pool. If the current income of the endowment investments is not sufficient to cover the authorized level of spending, the difference is taken from the market value in excess of the historical gift value, to the extent available.

The expiration of donor-imposed restrictions on contributions or endowment income is recognized in the period in which the restrictions are satisfied. At that time, the related resources are reclassified from temporarily restricted to unrestricted net assets. Restrictions expire when the stipulated time has elapsed or when the stipulated purpose for which the resource was restricted has been fulfilled. Endowment income and contributions received with donor-imposed restrictions that are satisfied in the same period as received are reported as unrestricted revenues.

Tuition revenue is recognized in the fiscal year in which the predominant portion of instruction occurs. Accordingly, deferred revenue as of May 31, 2011 includes the amount received from the students prior to May 31, 2011 for the 2011 summer session.

The University receives grant and contract revenue for research and other services it provides pursuant to arrangements with governmental and private entities. For financial statement purposes, grant and contract revenue is recorded at the time corresponding expenses have been incurred.

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from these estimates.

Certain fiscal year 2010 amounts have been reclassified to conform to the University's financial presentation in fiscal year 2011. On the consolidated statements of cash flows, an increase in accounts payable of $11,336,000 was reclassified from decrease in accounts payable and accrued expenses for investments and property, plant and equipment in the investing activities section to operating activities.

2. Accounting Pronouncements or Laws Affecting Subsequent Year Financial Statements:

In July 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2010-20, *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*, to provide financial statement users with greater transparency about an entity's allowance for credit losses and the credit quality of its financing receivables. The University will implement the disclosure requirements in fiscal 2012.

3. Cash, Cash Equivalents, and Accounts Receivable

The fair value of cash, cash equivalents, and accounts receivable is estimated to be the same as carrying (book) value because of their short maturities. Operating funds invested in short-term paper are included as cash equivalents, the value of which may fluctuate based on the financial environment and the type of short-term investment. The fair value of cash equivalents is at market. The fair value of cash, cash equivalents, and accounts receivable totaled $150,671,000 and $136,278,000 of which $4,783,000 and $6,994,000 represent donations restricted for property, plant and equipment as of May 31, 2011 and 2010, respectively. The University reserves accounts receivable determined to be impaired or otherwise uncollectible.

4. Pledges Receivable

Unconditional promises to give are included in the consolidated financial statements as pledges receivable with gifts reported in the appropriate net asset categories. Pledges receivable are initially recorded at their fair value, which is determined by computing the present value of future cash flows discounted at rates ranging from 4% to 7%. The present value and the associated incremental income are reflected as gift revenue in the period the agreement is made and in the period accreted, respectively.

Unconditional pledges receivable as of May 31 are expected to be realized in the following periods (dollars in thousands):

	2011	2010
In one year or less	$ 20,216	$ 22,730
Between one year and five years	40,112	33,114
More than five years	30,268	26,285
Less discount	(22,831)	(19,024)
	$ 67,765	$ 63,105

Unconditional pledges receivable as of May 31 have the following restrictions (dollars in thousands):

	2011	2010
Endowment for departmental programs and activities	$ 13,165	$ 12,603
Endowment for scholarships	8,264	8,566
Construction projects	11,968	4,967
Scholarships, departmental programs and activities	26,089	26,179
Purpose restriction met	8,279	10,790
	$ 67,765	$ 63,105

Conditional promises to give are not recorded in the financial statements until the conditions on which they depend are substantially met. As of May 31, the University has received pledges contingent on the following conditions (dollars in thousands):

	2011	2010
Contingent on donor's earnings	$ 4,375	$ 5,625
Matching donation requirement	26,917	13,017
Other	4,500	5,500
	$ 35,792	$ 24,142

5. Investments

Total investments as of May 31 are as follows (dollars in thousands):

	2011		2010	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Short-term paper	$ 86,851	$ 86,851	$ 87,537	$ 87,537
Stocks	218,261	218,261	157,030	157,030
Bonds	241,361	241,361	140,513	140,513
Venture capital	39,202	44,028	36,946	36,843
Mortgage and other notes receivable	9,855	9,855	11,608	11,608
Real estate:				
Real properties	$ 127,030	$ 113,430	$ 112,734	$ 99,527
Mineral rights	-	51,952	-	22,407
Total real estate	$ 127,030	$ 165,382	$ 112,734	$ 121,934
Funds held in trust by others	19,281	19,281	16,421	16,421
Other investments:				
Private equity	$ 225,017	$ 303,122	$ 217,724	$ 266,764
Absolute return	121,576	213,323	141,131	249,069
Equity funds without daily liquidity	101,129	110,859	85,765	82,667
Fixed income funds without daily liquidity	499	533	479	486
Equity method investments (carrying value is fair value)	57,542	57,542	60,672	60,672
Total other investments	$ 505,763	$ 685,379	$ 505,771	$ 659,658
Total investments	$ 1,247,604	$ 1,470,398	$ 1,068,560	$ 1,231,544

The fair value of short-term paper, stocks, bonds and funds held in trust by others is based on quoted market prices. The fair value of the University's interest in venture capital, real estate funds and other investments is based on the net asset value (NAV) reported by the fund managers, which is used as a practical expedient to estimate the fair value of the University's investment therein, unless it is probable that all or a portion of the value is different from NAV. The fair value of real estate mineral rights is estimated based on the income stream those assets generate. Where the fair value of mortgage and other notes receivable and University individually owned and managed real estate surface rights is not available and cannot be determined without incurring excessive costs, the amounts reflected as fair value are the same as carrying value.

Investments include assets associated with split-interest agreements. The University's split-interest agreements consist of perpetual trusts held and administered by others, gift annuities, unitrusts, and annuity trusts. Perpetual trusts held and administered by others are recorded at the current fair value of the University's interest in the trust assets.

Under split-interest agreements, the University has the right to receive income distributions that are reported as revenue. The gains associated with split-interest agreements were $1,249,000 and $809,000 in fiscal years 2011 and 2010, respectively. The fair value of split-interest agreements increased from $27,517,000 as of May 31, 2010 to $31,117,000 as of May 31, 2011.

Assets associated with gift annuities, unitrusts and annuity trusts held by the University are included in the applicable investment classifications. Under these split-interest agreements, the University makes periodic payments to named beneficiaries in return for assets received. Liabilities associated with split-interest agreements are recorded as accounts payable and accrued expenses on the consolidated balance sheets at current fair value by discounting estimated cash flows using discount rates of 4.98% and 5.11% per annum in fiscal years 2011 and 2010, respectively. The anticipated future payments to the income beneficiaries are based on their life expectancies determined from the actuarial tables published by the Internal Revenue Service, using the prevailing rate as of the date of each agreement. As of May 31, 2011 and 2010, the present values of the University's financial obligations to beneficiaries were $6,521,000 and $6,464,000, respectively.

The University also owns foreign investments that are included in the applicable investment classifications on the consolidated balance sheets. To mitigate foreign exchange risk, the investment managers may purchase foreign currency futures contracts, the unrealized gains and losses on which are reflected in the fair values of appropriate investment categories.

Investment return is comprised of investment income and net realized and unrealized gains. Investment income of $22,500,000 and $13,313,000 for the years ended May 31, 2011 and 2010, respectively, is net of related expenses, such as custodial fees and investment advisory fees. These expenses are approximately $9,689,000 and $9,047,000 for the years ended May 31, 2011 and 2010, respectively. Net realized and unrealized gains on investments totaled $110,063,000 and $63,336,000 for the years ended May 31, 2011 and 2010, respectively. Included in these amounts are realized and unrealized gains attributed to assets reported at fair value of approximately $46,630,000 and $37,873,000 for the years ended May 31, 2011 and 2010, respectively, and realized gains attributed to assets reported at cost of approximately $63,433,000 and $25,463,000 for the years ended May 31, 2011 and 2010, respectively.

In May 2008, the FASB issued ASC 958-810, *Reporting of Related Entities by Not-for-Profit Entities - Consolidation*, which makes several changes to the guidance for consolidation and the equity method of accounting. The University applies the guidance in ASC 970-323, *Investments - Equity Method and Joint Ventures*, on the equity method of accounting for its non-controlling interests in for-profit real estate partnerships, limited liability companies (LLCs), and similar entities unless those investments are reported at fair value. The ASC was effective for the University's financial statements issued for its fiscal year ended May 31, 2010. The University has determined those investments in which it holds an interest equal to or greater than 5% will be reported using the equity method of accounting. The University holds interests in various LLCs and a for-profit real estate partnership for investment purposes that meet this 5% threshold and have been recorded using the equity method. All disclosures and unrealized gain (loss) adjustments are based on the most recently reported fair values and financial statements of the investment companies.

The University's percentage ownership and the fair value of its ownership using the most recent (unaudited) financial information of the investment companies as of May 31, 2011 and 2010 are reflected in the table below (dollars in thousands):

	2011		2010	
Investment Companies	Percentage of Ownership	Fair Value	Percentage of Ownership	Fair Value
Venture capital:				
Silver Creek Ventures III, L.P.	16.1%	$ 2,762	16.1%	$ 1,984
Pinnacle Ventures Equity Fund I	14.3	5,767	14.3	4,971
Knightsbridge III	9.9	885	9.9	749
Silver Creek Ventures II, L.P.	8.5	2,021	8.5	2,445
Endowment Venture Partners	5.6	121	5.6	114
Commonfund Capital New Leaders II, L.P.	5.0	2,033	5.0	2,093
Real estate properties:				
Sustainable Woodlands Fund, L.P.	5.4	10,028	5.4	9,416
Private equity:				
Amberbrook IV, LLC	5.9	4,949	5.9	5,619
Private Advisors Small Company Buyout Fund, L.P.	5.7	5,851	5.7	6,141
Absolute return:				
Whippoorwill Offshore Distressed Opportunity Fund, Ltd.	7.3	23,125	6.5	17,604
Maple Leaf Offshore, Ltd.	-	-	5.3	9,536
Total		$ 57,542		$ 60,672

6. Endowment Fund

The University applies the provisions of ASC 958-205, *Endowments of Not-for-Profit Entities - Presentation of Financial Statements*, which provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA or the Act) and also requires disclosures about endowment funds, including both donor-restricted endowment funds and funds functioning as endowment funds.

The University's endowment consists of approximately 1,475 individual funds established for a variety of purposes including both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. Net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of Relevant Law:

The Board of Trustees of the University has interpreted the UPMIFA as requiring the preservation of the fair value of the original gifts as of the gift dates, absent explicit donor stipulations to the contrary. As a result of this interpretation, the University classifies as permanently restricted net assets, (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund.

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 Board of Trustees in a manner consistent with the standard of prudence prescribed by the Act. In accordance with the Act, the Board of Trustees 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 appreciation of investments
6. Other resources
7. The investment policies of the University

Temporarily restricted and permanently restricted donor-restricted endowment funds were $456,316,000 and $483,796,000, respectively, as of May 31, 2011 and $408,673,000 and $467,697,000, respectively, as of May 31, 2010. Funds functioning as endowment funds were $78,379,000 and $70,851,000 as of May 31, 2011 and 2010, respectively, and are included in unrestricted net assets.

Changes in endowment net assets for the years ended May 31 are as follows (dollars in thousands):

	2011				2010			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Net assets at beginning of year	$ 64,947	$ 408,673	$ 467,697	$ 941,317	$ 51,393	$ 420,712	$ 449,410	$ 921,515
Gifts	-	-	15,147	15,147	-	-	17,370	17,370
Investment return:								
Investment income, net of distributions	$ 60	$ -	$ 1,172	$ 1,232	$ 1	$ 557	$ 753	$ 1,311
Net realized and unrealized gains	9,942	100,126	-	110,068	14,158	47,206	-	61,364
Total investment return	$ 10,002	$ 100,126	$ 1,172	$ 111,300	$ 14,159	$ 47,763	$ 753	$ 62,675
Endowment gains transferred for spending	(3,783)	(47,053)	-	(50,836)	(4,439)	(55,881)	-	(60,320)
Funds functioning as endowment net transfers	1,309	-	-	1,309	(204)	-	-	(204)
Other revenues and transfers	4,934	(5,430)	(220)	(716)	4,038	(3,921)	164	281
Net assets at end of year	$ 77,409	$ 456,316	$ 483,796	$ 1,017,521	$ 64,947	$ 408,673	$ 467,697	$ 941,317

Changes in endowment net assets split between donor-restricted and funds functioning as endowment for the years ended May 31 are as follows (dollars in thousands):

	2011			2010		
	Donor Restricted Endowment	Funds Functioning as Endowment	Total	Donor Restricted Endowment	Funds Functioning as Endowment	Total
Gifts	$ 15,147	$ -	$ 15,147	$ 17,370	$ -	$ 17,370
Investment return						
Investment income, net of distribution	$ 1,172	$ 60	$ 1,232	$ 1,310	$ 1	$ 1,311
Net realized and unrealized gains	100,126	9,942	110,068	47,206	14,158	61,364
Total investment return	$ 101,298	$ 10,002	$ 111,300	$ 48,516	$ 14,159	$ 62,675
Endowment gains transferred for spending	(47,053)	(3,783)	(50,836)	(55,881)	(4,439)	(60,320)
Funds functioning as endowment net transfers	-	1,309	1,309	-	(204)	(204)
Other revenues and transfers	(716)	-	(716)	281	-	281
Total change in endowment funds	$ 68,676	$ 7,528	$ 76,204	$ 10,286	$ 9,516	$ 19,802

Endowment funds classified as permanently restricted net assets of $483,796,000 and $467,697,000 as of May 31, 2011 and 2010, respectively, represent the portion of perpetual endowment funds that is required to be retained permanently by explicit donor stipulation.

Endowment funds classified as temporarily restricted net assets and subject to a time restriction under UPMIFA as of May 31 are as follows (dollars in thousands):

	2011	2010
With purpose restrictions	$ 146,690	$ 134,645
Without purpose restrictions	309,626	274,028
Total endowment funds classified as temporarily restricted net assets	$ 456,316	$ 408,673

Funds with Deficiencies:

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level the donor or the Act requires the University to retain as a fund of perpetual duration. Deficiencies of this nature that are reported in unrestricted net assets were $970,000 and $5,904,000 as of May 31, 2011 and 2010, respectively. These deficiencies resulted from unfavorable market fluctuations that occurred after the investment of the permanently restricted contributions. Subsequent gains that restore the fair value of the assets of the endowment fund to the required level will be classified as increases in unrestricted net assets.

Return Objectives and Risk Parameters:

The University has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the University must hold in perpetuity or for a donor-specified period, as well as funds functioning as endowment funds. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to outperform over the long term (defined as rolling three and five year periods) a blended benchmark composed of 75% of the Russell 3000 and 25% of Barclay's Government/Credit Index. The University expects its endowment funds, over time, to provide an average rate of return of approximately 9 percent annually (or 5.5% after an expected average rate of University inflation of 3.5% per year), net of all costs of management fees, trading expenses and custody services over the long term. Actual returns in any given year may vary from this target.

The principal risk to the endowment is the possibility of prolonged or severe asset depreciation that impairs the ability of the fund to preserve the value of the corpus after inflation, fees, and the yearly spending distribution. The endowment's broadly diversified portfolio is designed to reduce the volatility of returns. Also, the endowment is invested in asset classes that are projected to perform well and act as a hedge in environments that could cause prolonged or severe asset deprecation such as high inflation or deflation. Risk management is a dynamic process that takes into account general market developments, the proliferation of new investments, and the changing nature of correlation across asset classes. The University and its Investment Committee are responsible for this process, monitoring and managing the factors pertaining to credit, liquidity, market, and operational risks.

Strategies Employed for Achieving Objectives:

To satisfy its long-term 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, etc.). The University targets a diversified asset allocation that places emphasis on global equities, absolute return, private markets, real assets and fixed income strategies to achieve its long-term return objectives within prudent risk constraints.

Spending Policy and the Investment Objectives Relationship to Spending Policy:

University Administration is authorized to distribute for spending from all endowment funds invested in the Investment Pool that have sufficient realized and unrealized capital gains, an amount equal to seventy percent (70%) of the spending calculated for the previous fiscal year increased by an inflation factor to be determined each fiscal year (1% for fiscal year 2011), and a percent determined for each fiscal year (currently 4.75%) of thirty percent (30%) of the four-quarter average of market values for the preceding calendar year. In establishing this policy, the University considers 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 maintain its purchasing power by growing a rate at least equal to planned payouts and inflationary increases. Additional real growth will be provided through new gifts and excess investment returns.

7. Fair Value of Financial Instruments

The University complies with ASC 820, *Fair Value Measurement*. This codification provides a new definition for fair value, as well as establishing a framework for measuring it and expanding disclosures about fair value measurements. The financial assets recorded at fair value on a recurring basis primarily relate to investments. ASC 820 establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entities (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entities' own assumptions about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy).

Additional disclosures are required under ASC 820, including segregating asset values among three levels that identify how investments are valued. In general, fair values determined by Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets. Fair values determined by Level 2 inputs utilize data points that are observable, such as quoted prices for comparable assets, interest rates and yield curves. Fair values determined by Level 3 inputs are unobservable data points for the assets and include situations where there is little, if any, market activity for the assets.

ASC 825, *Financial Instruments*, permits entities to choose to measure financial instruments and other items at fair value. The unrealized gains and losses on items for which the fair value option has been elected would be classified as revenue. The University has not elected to value investments or other financial instruments at fair value other than equity method investments.

For financial statement purposes (balance sheets), venture capital, real estate and other investments (other than equity method investments) are carried on the cost basis. The following tables present information about the University's investments by major category in the fair value hierarchy for year ended May 31, 2011 and the year ended May 31, 2010, as well as related strategy, liquidity and funding commitments.

The following table presents information about the University's investments at fair value as of May 31, 2011, including the fair value hierarchy to determine such fair value, as well as the strategies, liquidity and commitments related to them (dollars in thousands):

	Quoted Prices in Active Markets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)	Total	Unfunded Commitments	Level 3 Investment Redemption Frequency	Level 3 Investment Redemption Notice Period (Days)
Short-term paper	$ 86,851	$ -	$ -	$ 86,851	$ -		
Stocks	218,261	-	-	218,261	30,000		
Bonds	193,249	48,112	-	241,361	-		
Venture capital	-	-	44,028	44,028	17,685	Illiquid	N/A
Mortgage and other notes receivable	-	9,855	-	9,855	-		
Real estate:							
Real properties							
Directly held real estate	-	5,735	290	6,025	-	Illiquid	N/A
Real estate funds	-	-	83,184	83,184	29,938	Illiquid	N/A
Timber funds	-	-	24,221	24,221	36	Illiquid	N/A
Mineral rights	-	51,952	-	51,952	-		
Funds held in trust by others	-	14,141	5,140	19,281	-		
Other investments:							
Private equity	-	-	303,122	303,122	76,837	Illiquid	N/A
Absolute return:							
Single strategy hedge funds	-	-	38,392	38,392	-	Annually	45 to 90
Single strategy hedge funds	-	-	15,989	15,989	-	Locked up (1)	45
Single strategy hedge funds	-	-	37,884	37,884	-	Quarterly	30 to 90
Multi strategy hedge funds	-	-	23,021	23,021	-	Annually	90
Multi strategy hedge funds	-	-	74,815	74,815	-	Quarterly	60 to 90
Multi strategy hedge funds	-	-	17,115	17,115	-	Monthly	60
Side pockets/private-like hedge funds	-	-	6,107	6,107	-	Illiquid	N/A
Equity funds without daily liquidity:							
International equities emerging markets	-	-	23,310	23,310	-	Quarterly	90
International equities emerging markets	-	-	727	727	-	Illiquid	N/A
International equities developing markets	-	-	1,399	1,399	-	Illiquid	N/A
International equities developing markets	-	-	19,763	19,763	-	Quarterly	90
International equities developing markets	-	-	32,977	32,977	-	Monthly	6 business days
International equities developing markets	-	-	31,953	31,953	-	Monthly	15 business days
Multi strategy equity funds	-	-	730	730	-	End of Month	5
Fixed Income funds without daily liquidity	-	-	533	533	-	End of Month	5
Equity method investments:							
Venture capital	-	-	13,590	13,590	7,995	Illiquid	N/A
Private equity	-	-	10,800	10,800	760	Illiquid	N/A
Single strategy hedge funds	-	-	23,124	23,124	-	Quarterly	30 to 90
Timber funds	-	-	10,028	10,028	-	Illiquid	N/A
Total investments	$ 498,361	$ 129,795	$ 842,242	$ 1,470,398	$ 163,251		

(1) Semiannual liquidity after completion of 2 year lockup expiring December 31, 2012.

The following table presents information about the University's investments at fair value as of May 31, 2010, including the fair value hierarchy to determine such fair value, as well as the strategies, liquidity and commitments related to them (dollars in thousands):

	Quoted Prices in Active Markets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)	Total	Unfunded Commitments	Level 3 Investment Redemption Frequency	Level 3 Investment Redemption Notice Period (Days)
Short-term paper	$ 87,537	$ -	$ -	$ 87,537	$ -		
Stocks	157,030	-	-	157,030	35,000		
Bonds	91,966	48,547	-	140,513	-		
Venture capital	-	-	36,843	36,843	24,293	Illiquid	N/A
Mortgage and other notes receivable	-	11,608	-	11,608	-		
Real estate:							
Real properties							
Directly held real estate	-	5,795	290	6,085	-	Illiquid	N/A
Real estate funds	-	-	67,987	67,987	44,340	Illiquid	N/A
Timber funds	-	-	25,455	25,455	36	Illiquid	N/A
Mineral rights	-	22,407	-	22,407	-		
Funds held in trust by others	-	11,846	4,575	16,421	-		
Other investments:							
Private equity	-	-	266,764	266,764	112,896	Illiquid	N/A
Absolute return:							
Single strategy hedge funds	-	-	13,130	13,130	-	Annually	45 to 90
Single strategy hedge funds	-	-	71,345	71,345	-	Quarterly	30 to 90
Multi strategy hedge funds	-	-	20,735	20,735	-	Annually	90
Multi strategy hedge funds	-	-	79,866	79,866	-	Quarterly	60 to 90
Multi strategy hedge funds	-	-	17,452	17,452	-	Monthly	60
Multi strategy hedge funds	-	-	24,795	24,795	-	Locked up (1)	60
Side pockets/private-like hedge funds	-	-	21,746	21,746	-	Illiquid	N/A
Equity funds without daily liquidity:							
International equities emerging markets	-	-	21,206	21,206	-	Quarterly	90
International equities emerging markets	-	-	8,078	8,078	-	Illiquid	N/A
International equities developing markets	-	-	1,481	1,481	-	Illiquid	N/A
International equities developing markets	-	-	26,043	26,043	-	Monthly	6 business days
International equities developing markets	-	-	25,266	25,266	-	Monthly	15 business days
Multi strategy equity funds	-	-	593	593	-	End of Month	5
Fixed Income funds without daily liquidity	-	-	486	486	-	End of Month	5
Equity method investments:							
Venture capital	-	-	12,356	12,356	11,620	Illiquid	N/A
Private equity	-	-	11,760	11,760	960	Illiquid	N/A
Single strategy hedge funds	-	-	27,139	27,139	-	Quarterly	30 to 90
Timber funds	-	-	9,417	9,417	-	Illiquid	N/A
Total investments	$ 336,533	$ 100,203	$ 794,808	$ 1,231,544	$ 229,145		

(1) Liquidity available December 31, 2011, subject to multi-year lockup thereafter.

For fiscal years 2011 and 2010, fair value for assets in the previous table using significant unobservable inputs (Level 3) is as follows (dollars in thousands):

	2011					
	Opening Balance	Investment reclass	Realized gains (losses)	Unrealized gains (losses)	Net purchases (sales)	Ending Balance
Venture capital	$ 36,843	$ -	$ 2,619	$ 4,930	$ (364)	$ 44,028
Real estate	93,732	-	7,944	(268)	6,287	107,695
Funds held in trust	4,575	-	(83)	664	(16)	5,140
Other investments	659,658	-	52,869	30,078	(57,226)	685,379
Total	$ 794,808	$ -	$ 63,349	$ 35,404	$ (51,319)	$ 842,242

	2010					
	Opening Balance	Investment reclass	Realized gains (losses)	Unrealized gains (losses)	Net purchases (sales)	Ending Balance
Venture capital	$ 33,435	$ -	$ 1,296	$ 1,523	$ 589	$ 36,843
Real estate	97,598	-	338	(15,329)	11,125	93,732
Funds held in trust	4,224	-	(121)	481	(9)	4,575
Other investments	610,044	37,418	23,829	8,564	(20,197)	659,658
Total	$ 745,301	$ 37,418	$ 25,342	$ (4,761)	$ (8,492)	$ 794,808

As of May 31, 2011, the University has annuity obligations, notes payable and bonds payable that have fair values of $6,521,000, $671,000 and $514,718,000, respectively, which are measured using Level 2 valuation techniques. As of May 31, 2010, these fair values were $6,464,000, $705,000 and $392,026,000, respectively.

8. Property, Plant and Equipment

Plant assets include net interest expense of $2,040,000 and $91,000 capitalized for construction bond projects during fiscal years 2011 and 2010, respectively, and included in property, plant and equipment in the following table (dollars in thousands):

	2011	2010
Land	$ 150,780	$ 143,843
Land improvements	46,768	42,842
Buildings	648,103	632,393
Equipment	83,208	79,941
Art	36,090	34,321
Construction in progress	20,402	13,974
Total plant assets	$ 985,351	$ 947,314
Less accumulated depreciation	(302,206)	(278,652)
Total, net of accumulated depreciation	$ 683,145	$ 668,662

The fair value of a liability for the legal obligation for asbestos and lead paint abatement associated with the retirement of long-lived assets is recognized in the period in which it is incurred, at the present value of expected future cash flows, and is added to the carrying value of the associated asset to be depreciated over the asset's useful life.

The following table summarizes the change in the asset retirement obligation for fiscal years ended May 31, 2011 and 2010 (dollars in thousands):

	2011	2010
Asset retirement obligations at beginning of year	$ 14,007	$ 13,455
Disposal of asset retirement obligations	(1,033)	(132)
Increase (decrease) in property, plant and equipment, net of accumulated depreciation	81	(77)
Current year accretion and depreciation expense	803	761
Asset retirement obligations at end of year	$ 13,858	$ 14,007

9. Accounts Payable and Accrued Expenses

The University has $153,425,000 and $111,325,000 reported as accounts payable and accrued expenses as of May 31, 2011 and 2010, respectively. Included in these amounts is the present value of conditional asset retirement obligations and performance on a long-term lease obligation, which are adjusted annually. Due to the use of present value calculations or the short maturity of the obligations included in accounts payable and accrued expenses, the carrying values reflected on the consolidated financial statements approximate their fair values.

10. Notes and Bonds Payable (dollars in thousands):

Notes payable as of May 31 consist of the following:

	2011	2010
Total notes payable, includes notes due at various dates through 2021, with average interest rates of 1.58% and 1.56% as of May 31, 2011 and May 31, 2010, respectively, with $381 and $401 secured by equipment and property as of May 31, 2011 and May 31, 2010, respectively. The University did not draw on its $15 million line of credit as of May 31, 2011 and 2010.	$ 781	$ 841

Bonds payable as of May 31 consist of the following:

	2011	2010
Bonds payable due serially at various dates through 2013, with a fixed interest rate of 3.50%; collateralized by certain revenue	$ 480	$ 630
1985 Refunding Series; weekly demand put bonds due 2015 with a variable interest rate of 0.21% on May 31, 2011; secured by unrestricted receivables supported by self liquidity	19,200	19,200
2002 Serial Bonds; maturing from 2010 through 2012 with fixed interest rates ranging from 5.25% to 5.50% and Serial Bonds and Term Bonds with fixed interest rates of 5.00% to 5.50% to be refunded from escrow funds in 2012; secured by unrestricted receivables and escrow investments in state and local government bonds	50,125	52,725
2003 Serial Bonds; maturing from 2010 through 2024 with fixed interest rates ranging from 3.50% to 4.60% and Term Bonds maturing in 2029 and 2033 with fixed interest rates of 4.50% and 4.75%, respectively; secured by unrestricted receivables	26,620	27,300
2007 Serial Bonds; maturing from 2010 through 2029 with fixed interest rates ranging from 4.00% to 5.25% and Term Bonds maturing in 2032 with a fixed rate of 4.30%; secured by unrestricted receivables	93,745	95,205
2009 Serial Bonds; maturing from 2010 through 2029 with fixed interest rates ranging from 2.00% to 5.00% and Term Bonds maturing in 2032 and 2036 with fixed interest rates of 4.25% and 5.00%, respectively; secured by unrestricted receivables	145,635	147,635
2010 Serial Bonds; maturing from 2014 through 2030 with fixed interest rates ranging from 3.00% to 5.00% and Term Bonds maturing in 2035 and 2041 with fixed interest rates of 5.00%, respectively; secured by unrestricted receivables	116,330	-
Total bonds payable prior to unamortized net premium	$ 452,135	$ 342,695
Unamortized net premium	24,133	17,420
Total bonds payable	$ 476,268	$ 360,115

As of May 31, 2011, the fair values of the notes and bonds payable are approximately $671,000 and $514,718,000, respectively. Notes and bonds payable were valued at the present value of future payments discounted at the prevailing interest rates for comparable debt instruments as of May 31, 2011.

Net proceeds from Series 2006 bonds are to fund the construction, renovation, equipping and expansion of various residence halls and Fondren Science building, construction and renovation of street and utility improvements associated with the realignment of University Boulevard, acquisition of land and buildings and building improvements on North Central Expressway, to refund the outstanding Series 1995 bonds, and to fund other educational facilities and housing facilities. Series 2006 bonds were refunded on October 1, 2009. As of May 31, 2011, the $1,570,000 of proceeds not expended was invested in cash and cash equivalents.

The proceeds of the University's Series 2007 bonds were used to refund portions of the Series 1999A bonds and the Series 2002 bonds. Proceeds from the Series 2007 bonds in escrow refunded $43,645,000 of Serial and Term bonds of the Series 1999A bonds in 2008. Proceeds from the Series 2007 bonds are in escrow to refund $44,470,000 of Serial and Term bonds of the Series 2002 bonds in 2012. The assets in the escrow account and the associated debt are included on the consolidated balance sheets of the University.

On October 1, 2009, the University issued Series 2009 bonds totaling $147,635,000. The proceeds were used to refund the Series 2006 bonds and a portion of the 1999D series bonds, refinance various notes payable, and purchase land, streets and alleys in the City of University Park, and fund acquisition or construction of other land, fixtures, equipment and improvements determined by the University to be useful for providing educational facilities and housing facilities incidental or related in connection therewith. As of May 31, 2011, all of the proceeds have been expended.

On October 28, 2010, the University issued Series 2010 bonds totaling $116,330,000. The proceeds are being used to begin construction of the new Residential Commons and related projects and to renovate existing educational facilities and housing facilities. As of May 31, 2011, the $120,337,000 of proceeds not expended was invested in cash and cash equivalents and United States Treasury notes.

Bond issuance costs of $3,845,000 and $3,188,000 as of May 31, 2011 and 2010, respectively, are capitalized and amortized using the effective interest method over the lives of the bonds.

As required by bond indenture agreements, the University has cash and securities on deposit with the trustee banks as of May 31, 2011, that have fair values totaling $6,660,000, of which $842,000 relates to the $480,000 bonds payable due through 2013, and $5,818,000 relates to the $19,200,000 bonds payable due in 2015. These assets are restricted for the payment of principal and interest on the related indebtedness. The University also has cash and securities on deposit with the trustee bank as of May 31, 2011, which have a fair value totaling $45,088,000, which relates to the $44,470,000 of bonds payable to be refunded in 2012, as required by the escrow agreement.

Interest expense on notes and bonds payable was $13,547,000 and $13,827,000 for the fiscal years ended May 31, 2011 and 2010, respectively. As of May 31, 2011, scheduled principal maturities are $7,223,000, $52,340,000, $9,025,000, $11,835,000 and $31,600,000 for the years ending May 31, 2012 through 2016, respectively, and $340,893,000 for 2017 and thereafter.

Included in long-term debt is $19,200,000 of general obligation demand bonds maturing in fiscal year 2016. In the event that the agents are unable to remarket the bonds, the bonds become demand notes and will be funded through self liquidity.

11. Derivative Financial Instrument

The University may enter into interest rate swap transactions to take advantage of market opportunities to reduce costs and/or reduce interest rate risk. The University considers the rating of the counterparty when entering into swap arrangements, and under no conditions will it enter into a swap with a firm carrying less than an “A” rating. The University does not enter into swap transactions for speculative purposes.

The University had a swap in fiscal year 2009 that was terminated in fiscal year 2010.

12. Related Party Transactions

In the ordinary course of business, the University may have business transactions with entities in which University board members or employees have an interest. Although generally such transactions are immaterial, the University does engage in such business transactions that may be material. The University has invested funds totaling $2,567,000 and $2,819,000 in fiscal years 2011 and 2010, respectively, with one investment firm with which a board member is affiliated.

13. Postemployment Benefits

The University accrues obligations for certain other future postemployment benefits payable to former or inactive employees, if they are determinable. The University has post-employment benefit obligations of $507,000 in fiscal year 2011 and $492,000 in fiscal year 2010.

14. Postretirement Health Care Benefits

The University provides postretirement health care benefits for employees who meet minimum age and service requirements and retire from the University. These benefits are provided by an insured Medicare supplement product with no lifetime maximum. The funding for the premium of this product is shared between the University and Plan participants.

The University accrues the expected cost of providing postretirement benefits, other than pensions, during the years that employees render services. The accumulated postretirement benefit obligation (APBO) initially recognized in fiscal year 1994 is being amortized over twenty years.

Actuarial assumptions used to determine the value of the APBO and the benefit costs included discount rates of 4.98% and 5.11% per annum for fiscal years 2011 and 2010, respectively. Health care cost trends graded from 10.0% in 2012 to 5.0% in 2023.

ASC 715, *Compensation - Retirement Benefits*, requires the funded status of the postretirement benefit plan to be reported as an asset (for overfunded plans) or a liability (for underfunded plans). ASC 715 also requires disclosure of the incremental effect of adopting the standard on certain individual line items of the consolidated balance sheet.

The components of the net periodic benefit cost for the years ended May 31 are as follows (dollars in thousands):

	2011	2010
Service cost	$ 944	$ 951
Interest cost	1,693	1,761
Amortization:		
Transition obligation	307	307
Prior service cost	132	132
Unrecognized loss	668	593
Net periodic benefit cost	$ 3,744	$ 3,744

The transition obligation, prior service cost and unrecognized loss for the defined benefit postretirement plan that will be amortized from unrestricted net assets into net periodic benefit cost over the next fiscal year are $307,000, $132,000 and $799,000, respectively.

Net periodic benefit cost recognized and other changes in plan assets and benefit obligations recognized in unrestricted net assets in 2011 and 2010 are as follows (dollars in thousands):

	2011	2010
Net periodic benefit cost recognized	$ 3,744	$ 3,744
Other changes in plan assets and benefit obligations recognized in unrestricted net assets:		
Net actuarial loss	871	711
Prior service cost (credit)	(132)	(132)
Transition obligation (asset)	(307)	(307)
Total recognized in unrestricted net assets	432	272
Total recognized in net periodic benefit cost and unrestricted net assets	$ 4,176	$ 4,016

The accrued postretirement benefit obligations recognized in the University's consolidated balance sheets as of May 31 pursuant to the recognition provisions of ASC 715 are as follows (dollars in thousands):

	2011	2010
Benefit obligation, beginning of year	$ 33,785	$ 31,081
Service cost	944	951
Interest cost	1,693	1,761
Plan participants' contribution	1,008	820
Benefit payments	(2,679)	(2,132)
Actuarial loss	1,539	1,304
Benefit obligation, end of the year	$ 36,290	$ 33,785

The accumulated postretirement benefit includes a current liability of $1,393,000 for the claims and expenses that are expected to be paid out in the coming year and $34,897,000 of noncurrent postretirement benefit liabilities.

Health care cost trend assumptions have a significant impact on the amounts reported. A one percentage point increase in the assumed health care cost trend rate would result in a $257,000 increase in the net periodic postretirement benefit cost recognized in fiscal year 2011 and a $3,076,000 increase in the accumulated postretirement benefit obligation for health care benefits as of May 31, 2011. A one percentage point decrease in the assumed health care cost trend rate would result in a $235,000 decrease in the net periodic postretirement benefit cost recognized in fiscal year 2011 and a $2,814,000 decrease in the accumulated postretirement benefit obligation for health care benefits as of May 31, 2011.

As of May 31, 2011, the University has expected benefit payments through fiscal year 2021 of $20,910,000. Of these commitments, $1,393,000, $1,478,000, $1,551,000, $1,846,000 and $2,055,000 are the expected payments in the fiscal years ending 2012 through 2016 and $12,587,000 in the fiscal years ending 2017 through 2021.

The University also has a defined contribution retiree medical plan intended to replace the University's defined benefit retiree medical plan. Under this program, both the University and employees contribute monthly to the employees' retiree medical benefit. The University contributed $1,195,000 to this program in fiscal year 2011. The current defined benefit retiree medical plan will be phased out concurrently with funding of this defined contribution plan.

15. Retirement Plan

Full-time, benefits-eligible employees who are at least 21 years of age are eligible to participate in the 403(b) Retirement Plan when they first join SMU. Part-time employees working at least 20 hours/week are eligible after one year of employment. Full-time employees are required to enroll after one year of service, if age 36 or older. Retirement benefit expenses under this plan were approximately $14,181,000 and $13,713,000 in fiscal years 2011 and 2010, respectively.

16. Net Assets Released from Restrictions

The sources of net assets released from temporary restrictions by incurring expenses satisfying the restricted purposes or by occurrence of events specified by donors were as follows (dollars in thousands):

	2011	2010
Acquisition of buildings and equipment	$ 20,751	$ 25,039
Instruction, research, departmental support, scholarships and other	73,811	68,145
	$ 94,562	$ 93,184

17. Restrictions and Limitations on Net Asset Balances

Temporarily and permanently restricted net assets as of May 31 consist of the following (dollars in thousands):

	2011		2010	
	Temporarily Restricted	Permanently Restricted	Temporarily Restricted	Permanently Restricted
Donor-restricted endowment	$ 456,316	$ 483,796	$ 408,673	$ 467,697
Annuity trust and unitrust	-	5,038	-	4,743
Student loan funds	-	20,112	-	20,193
Gifts and other unexpended revenues and gains available for:				
Acquisition of building and equipment	13,417	-	26,982	-
Instruction, research, departmental support, scholarships and other	64,742	-	58,163	-
	$ 534,475	$ 508,946	$ 493,818	$ 492,633

18. Commitments and Contingencies

The University is contractually obligated for approximately $13,098,000 as of May 31, 2011 for construction projects with scheduled completion dates through fiscal year 2012.

The University incurred $983,000 and $1,162,000 in operating lease expenses for facilities and equipment in the fiscal years ended May 31, 2011 and 2010, respectively. As of May 31, 2011, the University has lease commitments for future periods totaling approximately $2,145,000. Of these commitments, $749,000, $596,000, $156,000, $143,000, and $146,000 are due in the fiscal years ending 2012 through 2016, respectively, and $355,000 is due in the fiscal year 2017 and thereafter.

The University also has rights to revenues from long-term leases it holds related to independent operations. The University received $3,174,000 and $3,429,000 in rental revenue from these leases in the fiscal years ended May 31, 2011 and 2010, respectively. As of May 31, 2011, the total of the future rental revenues from these leases is approximately $16,790,000. Of these commitments, $2,913,000, $2,414,000, $2,080,000, $1,731,000, and $1,510,000, is due in the fiscal years ending 2012 through 2016, respectively, and $6,142,000 are due in the fiscal year 2017 and thereafter.

Accounts payable and accrued expenses include $44,630,000, offsetting the amount reported as expense in the statements of activities and reflecting the fair value of a ground lease contribution to The George W. Bush Foundation for the location, construction and operation of the George W. Bush Presidential Library Center facilities at the University as of May 31, 2011. This balance is accreted over the 249 years of the lease, with extensions.

The University has committed to capital draws totaling $627,366,000 for venture capital, real estate funds and other investments, of which $464,115,000 had been drawn as of May 31, 2011. The University has committed to pay draws as required for the remaining $163,251,000 through fiscal year 2019.

The University participates in the federal Title IV student financial aid programs and must fulfill federal requirements to qualify for these programs. Management is of the opinion that the University is in compliance with the federal requirements.

The University enters into contracts with vendors, some of which may have penalties for early termination. It is the University's practice when entering into such contracts to not cancel the contracts prior to the end of their term. If, from a business standpoint, including consideration of the cancellation penalty, the University does cancel any such contract, it does not believe there would be any material adverse effect on the University's consolidated financial statements.

The University is a defendant in several legal actions. The outcomes of these actions cannot be determined at this time, but management is of the opinion that liability, if any, from these actions will not have a material effect on the University's financial position.

The University is subject to laws and regulations concerning environmental remediation and has established reserves for potential obligations that management considers to be probable and for which reasonable estimates can be made. The University's affiliated corporations own property that is in the Voluntary Cleanup Program of the Texas Commission on Environmental Quality, and depending on the ultimate use of the property, remediation is likely to be necessary. Environmental remediation in the amount of $496,000 has been recorded in the consolidated financial statements as a liability. These estimates may change substantially depending on new information regarding the nature and extent of contamination, appropriate remediation technologies and regulatory approvals. Costs of future expenditures for environmental remediation are adjusted, as required.

The University has entered into an agreement with a bank to guarantee the construction loan debt for a sorority house built on University land. Under this agreement if the debtor defaults on its obligation, the University may be required to satisfy all or part of the remaining obligation. As of May 31, 2011 and 2010, the guarantee is approximately $1,716,000 and $1,982,000, respectively. The guarantee is in place until 2013 unless the debt is retired earlier. A liability for this guarantee has been recorded as accounts payable and accrued expenses with an offsetting amount recorded as other assets.

19. Tax Status

The University has received a determination letter from the Internal Revenue Service indicating it is exempt from federal income taxes under Section 501(a) of the Internal Revenue Code of 1986, as amended, as an organization described in Section 501(c)(3). Peruna Properties, Inc., Pony Properties, Inc., the Southern Methodist University Foundation for Research, Peruna Holdings Corporation, Mustang Mockingbird Corporation, Mustang Mockingbird Properties, Mustang Airline Corporation, The Stadium Club, Inc., and SMU Corp. are controlled corporations included in the University's consolidated financial statements and exempt from federal income taxes under Section 501(a) of the Internal Revenue Code of 1986, as amended, as organizations described in Sections 501(c)(3) and 501(c)(7). The University, Peruna Properties, Inc., Pony Properties, Inc., the Southern Methodist University Foundation for Research, Peruna Holdings Corporation, Mustang Mockingbird Corporation, Mustang Mockingbird Properties, Mustang Airline Corporation, and SMU Corp. have been classified as organizations that are not private foundations under Sections 509(a)(1) and 509(a)(3), and as such, contributions to these entities qualify for deduction as charitable contributions. The University and its controlled corporations are exempt from federal income taxes except to the extent they have unrelated business income.

The University complies with the requirements of ASC 740, *Income Taxes*, which prescribes a recognition threshold and measurement requirements for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. In addition, ASC 740 provides guidance on recognition, classification, and accounting in interim periods and disclosure requirements for uncertain tax provisions. The University and its controlled corporations do not have any uncertain tax positions and therefore have recorded no liability or benefit for such positions for the years ended May 31, 2011 and 2010.

20. Subsequent Events

The University has evaluated subsequent events from the balance sheet date through September 8, 2011, the issue date of the financial statements, and determined that there are no other items to disclose.