

FINANCIAL STATEMENTS

Bethune-Cookman University, Inc.
Years Ended June 30, 2010 and 2009
With Report of Independent Certified Public Accountants

Ernst & Young LLP



This page intentionally left blank.

Bethune-Cookman University, Inc.

Financial Statements

Years Ended June 30, 2010 and 2009

Contents

Report of Independent Certified Public Accountants1

Financial Statements

Statements of Financial Position.....2

Statements of Activities3

Statements of Cash Flows.....5

Notes to Financial Statements.....6

Report of Independent Certified Public Accountants on Internal Control Over
Financial Reporting and on Compliance and Other Matters Based on an Audit of
the Financial Statements Performed in Accordance With *Government Auditing
Standards*25

This page intentionally left blank.

Report of Independent Certified Public Accountants

This page intentionally left blank.

Report of Independent Certified Public Accountants

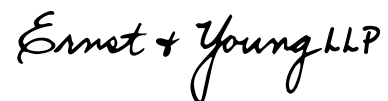
The Board of Trustees
Bethune-Cookman University, Inc.

We have audited the accompanying statements of financial position of Bethune-Cookman University, Inc. (the University) as of June 30, 2010 and 2009, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the University's administration. 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the University's internal control over financial reporting. Our audits included 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 the administration, and 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 Bethune-Cookman University, Inc. as of June 30, 2010 and 2009, 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 1, 2010, on our consideration of the University's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.



October 1, 2010

This page intentionally left blank.

Financial Statements

This page intentionally left blank.

Bethune-Cookman University, Inc.

Statements of Financial Position

	June 30	
	2010	2009
Assets		
Cash and cash equivalents	\$ 20,765,842	\$ 25,404,701
Restricted cash	872,298	864,726
Student receivables, net of allowance for doubtful accounts of \$857,683 and \$787,227 in 2010 and 2009, respectively	1,191,776	1,563,432
Grant and student aid receivables	4,712,312	661,926
Investments	34,035,220	30,366,485
Assets held in trust by others	315,783	304,641
Prepaid expenses	464,816	384,435
Contributions receivable, net	257,518	267,396
Property, plant, and equipment, net	67,767,728	62,554,494
Other assets	331,689	348,428
Total assets	<u>\$ 130,714,982</u>	<u>\$ 122,720,664</u>
Liabilities		
Accounts payable	\$ 1,378,258	\$ 1,548,818
Student deposits	243,282	263,461
Accrued expenses and other liabilities	3,747,322	2,585,105
Long-term debt	25,127,147	26,320,572
Total liabilities	<u>30,496,009</u>	<u>30,717,956</u>
Net assets:		
Unrestricted	74,408,854	67,669,689
Temporarily restricted	16,686,391	15,453,324
Permanently restricted	9,123,728	8,879,695
Total net assets	<u>100,218,973</u>	<u>92,002,708</u>
Total liabilities and net assets	<u>\$ 130,714,982</u>	<u>\$ 122,720,664</u>

See accompanying notes.

Bethune-Cookman University, Inc.

Statements of Activities

Year Ended June 30, 2010

	Unrestricted	Temporarily Unrestricted	Permanently Restricted	Total
Revenues, gains, and support:				
Tuition and fees	\$ 46,790,583	\$ —	\$ —	\$ 46,790,583
Less scholarship allowance	(11,623,095)	—	—	(11,623,095)
Net tuition and fees	35,167,488	—	—	35,167,488
Federal grants and contracts	114,439	5,420,139	—	5,534,578
State grants	—	3,962,253	—	3,962,253
Private gifts and grants	2,209,447	2,413,722	244,033	4,867,202
Interest and dividend income	480,454	438,391	—	918,845
Other income	854,934	121,645	—	976,579
Auxiliary enterprises	15,636,669	143,660	—	15,780,329
Net realized and unrealized gains on investments	1,176,996	1,588,578	—	2,765,574
Change in value of interest rate swaps	(817,916)	—	—	(817,916)
Net assets released from restrictions	12,855,321	(12,855,321)	—	—
Total revenues, gains, and support	67,677,832	1,233,067	244,033	69,154,932
Expenses and losses:				
Educational and general:				
Instruction and research	18,680,212	—	—	18,680,212
Academic support	1,312,494	—	—	1,312,494
Student services and activities	7,050,800	—	—	7,050,800
Institutional support	12,773,197	—	—	12,773,197
Operation and maintenance	8,525,895	—	—	8,525,895
Auxiliary enterprises	12,596,069	—	—	12,596,069
Total expenses and losses	60,938,667	—	—	60,938,667
Change in net assets	6,739,165	1,233,067	244,033	8,216,265
Net assets at beginning of year	67,669,689	15,453,324	8,879,695	92,002,708
Net assets at end of year	\$ 74,408,854	\$ 16,686,391	\$ 9,123,728	\$ 100,218,973

See accompanying notes.

Bethune-Cookman University, Inc.

Statements of Activities

Year Ended June 30, 2009

	Unrestricted	Temporarily Unrestricted	Permanently Restricted	Total
Revenues, gains, and support:				
Tuition and fees	\$ 46,935,273	\$ —	\$ —	\$ 46,935,273
Less scholarship allowance	(11,645,884)	—	—	(11,645,884)
Net tuition and fees	35,289,389	—	—	35,289,389
Federal grants and contracts	91,390	5,862,350	—	5,953,740
State grants	4,018	4,720,263	—	4,724,281
Private gifts and grants	2,565,022	2,795,378	156,553	5,516,953
Interest and dividend income	722,966	679,433	—	1,402,399
Other income	1,335,771	218,446	—	1,554,217
Auxiliary enterprises	16,133,118	29,500	—	16,162,618
Net realized and unrealized losses on investments	(5,082,175)	(5,492,257)	—	(10,574,432)
Change in value of interest rate swaps	(1,194,971)	—	—	(1,194,971)
Net assets released from restrictions	19,488,089	(19,488,089)	—	—
Total revenues, gains, and support	69,352,617	(10,674,976)	156,553	58,834,194
Expenses and losses:				
Educational and general:				
Instruction and research	19,374,630	—	—	19,374,630
Academic support	1,435,768	—	—	1,435,768
Student services and activities	7,348,576	—	—	7,348,576
Institutional support	12,625,114	—	—	12,625,114
Operation and maintenance	8,828,906	—	—	8,828,906
Auxiliary enterprises	13,780,495	—	—	13,780,495
Total expenses and losses	63,393,489	—	—	63,393,489
Change in net assets	5,959,128	(10,674,976)	156,553	(4,559,295)
Net assets at beginning of year	61,710,561	26,128,300	8,723,142	96,562,003
Net assets at end of year	\$ 67,669,689	\$ 15,453,324	\$ 8,879,695	\$ 92,002,708

See accompanying notes.

Bethune-Cookman University, Inc.

Statements of Cash Flows

	Year Ended June 30	
	2010	2009
Operating activities		
Change in net assets	\$ 8,216,265	\$ (4,559,295)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Contributions for long-term endowments	(244,033)	(156,553)
Net realized and unrealized (gains) losses on investments	(2,765,574)	10,574,432
Depreciation and amortization	3,218,407	3,032,819
Change in value of interest rate swap	817,916	1,194,971
Bad debt expense	718,770	701,241
Increase in student receivables	(347,114)	(895,190)
(Increase) decrease in grant and student aid receivables	(4,050,386)	150,644
(Increase) decrease in prepaid expenses	(80,381)	15,021
Decrease (increase) in contributions receivable, net	9,878	(131,825)
(Increase) decrease in assets held in trust by others	(11,142)	36,990
Decrease in other assets	16,739	16,738
(Decrease) increase in accounts payable	(170,560)	995,099
Decrease in student deposits	(20,179)	(2,279)
Increase (decrease) in accrued expenses and other liabilities	344,301	(144,136)
Loss on disposal of fixed assets	159,376	—
Net cash provided by operating activities	5,812,283	10,828,677
Investing activities		
Purchase of property, plant, and equipment	(8,591,017)	(1,199,190)
Purchases of investments	(13,447,782)	(15,989,254)
Proceeds from sales and maturities of investments	12,544,621	14,656,653
Net cash used in investing activities	(9,494,178)	(2,531,791)
Financing activities		
Contributions for long-term endowments	244,033	156,553
Proceeds from borrowings	645,154	109,476
Repayment of note payable and long-term debt	(1,838,579)	(1,160,745)
Net cash used in financing activities	(949,392)	(894,716)
Net change in cash and cash equivalents	(4,631,287)	7,402,170
Cash and cash equivalents at beginning of year	26,269,427	18,867,257
Cash and cash equivalents at end of year	\$ 21,638,140	\$ 26,269,427
Reconciliation to statements of financial position		
Cash and cash equivalents	\$ 20,765,842	\$ 25,404,701
Restricted cash	872,298	864,726
Cash and cash equivalents at end of year	\$ 21,638,140	\$ 26,269,427
Supplemental cash flow information		
Interest paid	\$ 1,287,635	\$ 1,357,785

See accompanying notes.

Bethune-Cookman University, Inc.

Notes to Financial Statements

June 30, 2010

1. Summary of Significant Accounting Policies

Bethune-Cookman University, Inc. (the University), located in Daytona Beach, Florida, is affiliated with the General Board of Higher Education and Ministry, an agency of the United Methodist Church. The University offers undergraduate, graduate, and continuing education courses to students on its main campus and six satellite locations, and is accredited by the Commission on Colleges of the Southern Association of Colleges and Schools.

Basis of Accounting

The financial statements of the University have been prepared on the accrual basis of accounting.

Basis of Presentation

The financial statements 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 classifying net assets and changes therein as follows:

- **Unrestricted net assets** – net assets that are not subject to donor-imposed stipulations.
- **Temporarily restricted net assets** – net assets subject to donor-imposed stipulations that may or will be met either by actions of the University and/or the passage of time.
- **Permanently restricted net assets** – net assets subject to donor-imposed stipulations that the corpus be maintained permanently by the University. Donors of these assets permit the University to use all, or part of, the earnings on related investments for general or specific purposes.

Revenues and support 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. Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as net assets released from restrictions in the statements of activities.

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Contributions, including unconditional promises to give, are recognized as revenues in the period they are made or received. Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met.

Contributions of assets other than cash are recorded at their estimated fair value at the date of the gift. Contributions to be received after one year are discounted at an appropriate discount rate commensurate with the risks involved. Amortization of discounts is recorded as a component of contributions revenue in accordance with donor-imposed restrictions, if any, on the contributions. An allowance for uncollectible contributions receivable is provided when, based upon the administration's judgment and including such factors as the prior collection history, type of contribution, and nature of fund-raising activity, an allowance is considered necessary.

Interest and dividend income and realized and unrealized gains and losses on investments of endowments and similar funds are reported as follows:

- As increases in permanently restricted net assets if the terms of the gift or the University's interpretation of relevant state law requires that they be added to the principal of a permanent endowment fund
- As increases or decreases in temporarily restricted net assets if the terms of the gift impose restrictions on the use of the income
- As increases or decreases in unrestricted net assets in all other cases

Reclassifications

Certain prior year balance sheet amounts have been reclassified to conform to current year presentation. Specifically, the amounts previously classified as mortgage, notes and other receivables are now classified as grants and student aid receivables.

Liquidity

Assets are presented in the accompanying statements of financial position according to their nearness of conversion to cash, and liabilities are presented according to the nearness of their maturity and resulting use of cash.

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Cash and Cash Equivalents and Restricted Cash

Cash and cash equivalents include all highly liquid investments with an original maturity of 90 days or less. Restricted cash consists of debt proceeds, certain sinking funds, and escrow accounts required under the terms of certain debt covenants.

Investments

Investments primarily consist of equity securities and bonds, as further detailed on Note 3. All investments are carried at fair value.

Pooled endowment and board-designated funds are invested on the basis of a total return policy to provide income and to realize appreciation in investment values. Under this policy, a portion of realized and unrealized gains accumulated, in addition to accumulated earnings, are used to support operations. Any such gains used to support operations are utilized in accordance with the same restrictions, if any, imposed by donors on the use of income earned by the endowment and similar funds.

Investment income and net realized and unrealized gains/losses on investments are included in the statement of activities according to the net asset category affected.

Investments Without Readily Determinable Values

Investments without readily determinable values consist of funds-of-funds, partnerships, and limited liability companies and are included with investments. Investments for which there is no readily determinable fair value are classified as level 2 or 3 (see Note 7) depending on the valuation technique. Depending on the underlying asset, the fair value is determined through national exchange prices for securities with a readily determinable value, or valuations and estimates typically determined by the underlying asset's manager. Due to the inherent uncertainty of these estimates, these values may differ from the value that would have been used had a ready market for these investments existed and the difference could be material.

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Property, Plant, and Equipment

Property, plant, and equipment are stated at cost at the date of acquisition, or fair value at the date of donation in the case of gifts. The University's policy is to capitalize assets acquired for \$5,000 or greater with a useful life in excess of one year. Depreciation on plant and equipment is provided using the straight-line method, based on the estimated useful lives. Equipment under capital lease is amortized over the shorter of the asset's useful life or the life of the lease using the straight-line method. The estimated useful life of buildings is 30 years. The estimated useful lives of equipment range from 6 to 20 years.

Student Receivables

The University grants credit without collateral to its students. These receivables are distributed among a wide range of students. These student receivable are evaluated for collectibility and allowances are established based on student account activity and other factors.

Grant and Student Aid Receivables

The University receives funding from various agencies, and receives student aid funding on behalf of its students. The related receivables are the result of timing of reimbursement requests made by the University. There is no allowance for uncollectible amounts, as these receivables are generally from the government and are supported by contractual agreements.

Income Taxes

The University is recognized as exempt from federal income taxes under Section 501(a) as an organization described in Section 501(c)(3) of the Internal Revenue Code. Accordingly, the financial statements do not reflect a provision for income taxes.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States 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.

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Concentration of Credit Risk

The University maintains cash accounts with several large financial institutions. All accounts at each financial institution are guaranteed by the Federal Deposit Insurance Corporation up to \$250,000 per bank. The University has cash deposited that exceeds the federally insured deposit amount. Management does not anticipate nonperformance by the financial institutions. The University also places its cash equivalents and short-term investments with high-quality institutions.

Fair Value Measurements

Effective July 1, 2008, the University adopted the Financial Accounting Standards Board (FASB) Accounting Standards Codification No. 820, *Fair Value Measurements and Disclosures* (ASC 820), for financial assets and liabilities. The statement defines fair value, provides guidance for measuring fair value, and requires certain disclosures. This standard discusses valuation techniques, such as the market approach (comparable market prices), the income approach (present value of future income or cash flow), and the cost approach (cost to replace the service capacity of an asset or replacement cost). The statement establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The following is a brief description of those three levels:

- *Level 1:* Observable inputs such as quoted prices (unadjusted) in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.
- *Level 2:* Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active.
- *Level 3:* Unobservable inputs that are used when little or no market data is available and reflect the reporting entity's own assumptions. These include pricing models, discounted cash flow methodologies, and similar techniques that use significant unobservable inputs.

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

2. Contributions Receivable

Included in contributions receivable at June 30, 2010 and 2009, are the following unconditional promises to give for the purposes indicated:

	<u>2010</u>	<u>2009</u>
Total unconditional promises to give	\$ 332,497	\$ 374,850
Less allowance for doubtful accounts	(69,179)	(99,084)
	<u>263,318</u>	275,766
Less discounts	(5,800)	(8,370)
Net unconditional promises to give	<u>\$ 257,518</u>	<u>\$ 267,396</u>

Unconditional pledges at June 30, 2010, are due in the following fiscal years:

2011	\$ 166,597
2012	60,710
2013	56,360
2014	48,330
2015 and later	500
Total	<u>\$ 332,497</u>

Pledges to be collected after one year from the fiscal year-end are discounted using a risk-free rate determined at pledge date and applied to the schedule of payments and due during each ensuing fiscal year.

From time to time, the University is informed of intentions to give by prospective donors. Such expressions of intent are revocable and unenforceable. The ultimate value of these expressions has not been established or recognized in the accompanying financial statements.

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

3. Investments

The composition of investments as of June 30, 2010 and 2009, is set forth in the following table. Investments are stated at fair value.

	<u>2010</u>	<u>2009</u>
U.S. mid to large-cap equity	\$ 10,069,658	\$ 8,951,690
U.S. small-cap equity	1,714,990	1,416,443
Global ex-U.S. equity	7,363,474	6,662,611
Hedge funds	3,209,191	—
Commingled funds	3,031,812	2,592,996
Bonds	8,625,277	7,744,069
Short-term investment funds	20,818	2,998,676
	<u>\$ 34,035,220</u>	<u>\$ 30,366,485</u>

4. Property, Plant, and Equipment

Property, plant, and equipment and related accumulated depreciation and amortization at June 30, were as follows:

	<u>2010</u>	<u>2009</u>
Land and improvements	\$ 6,457,468	\$ 6,409,918
Buildings	83,061,974	82,523,985
Equipment purchased under capital leases	2,180,577	2,025,571
Equipment	7,222,665	5,809,783
Construction-in-progress	6,179,883	479,167
	<u>105,102,567</u>	<u>97,248,424</u>
Less accumulated depreciation and amortization	<u>(37,334,839)</u>	<u>(34,693,930)</u>
Property, plant, and equipment, net	<u>\$ 67,767,728</u>	<u>\$ 62,554,494</u>

Amortization expense on the assets under capital leases of \$309,667 and \$323,911 for the years ended June 30, 2010 and 2009, respectively, is included in depreciation and amortization expense. Depreciation expense for the remaining property and equipment was \$2,908,740 and \$2,708,908 for the years ended June 30, 2010 and 2009, respectively.

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

4. Property, Plant, and Equipment (continued)

In June 2009, the University entered into a contract for \$4,000,000 for the construction of an Athletic Training Center. As of June 30, 2010, this project had not yet begun construction but is expected to be completed in Fall 2011.

5. Long-Term Debt

Details of long-term debt at June 30, 2010 and 2009, are as follows:

	<u>2010</u>	<u>2009</u>
HBCU Dormitory Capital Project Loan, bearing interest at 6.01% payable in monthly installments of \$30,850, including interest through September 2027, collateralized by land and building.	\$ 3,931,052	\$ 4,058,820
2001 Series Bonds, bearing variable interest rate that resembles BMA rate (0.43% at June 30, 2010) with principal and interest payments starting in October 2001 and maturing serially through July 2032, collateralized by the University's unrestricted revenues.	18,855,000	19,755,000
Loan payable bearing variable interest rate of LIBOR plus 185 basis points. Interest due monthly and principal due semiannually. Matures October 1, 2015, collateralized by land and building.	1,365,000	1,570,000
Various capital equipment leases, bearing variable interest rates and payable in monthly installments totaling \$30,705 through August 30, 2015, collateralized by underlying assets.	976,095	936,752
	<u>\$25,127,147</u>	<u>\$ 26,320,572</u>

Under the terms of the bond agreements, the University is required to make sinking fund deposits for the periodic payment of bond interest and the retirement of bond principal.

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

5. Long-Term Debt (continued)

The University has a promissory note agreement of \$1,000,000 with a commercial bank, under which the University may borrow for working capital purposes. This note is renewable annually and is payable on demand, subject to certain restrictions. At June 30, 2010 and 2009, the University had no amounts outstanding under these agreements. The interest rate varies with the LIBOR rate.

The following is a schedule by years of future minimum lease payments under capital leases together with the present value of the net minimum lease payments as of June 30, 2010:

Year ending June 30:	
2011	\$ 368,455
2012	242,944
2013	204,569
2014	179,408
2015	160,301
Thereafter	<u>38,824</u>
Total minimum lease payments	1,194,501
Less amount representing interest	<u>(218,406)</u>
Present value of net minimum lease payments	<u>\$ 976,095</u>

Temporarily restricted assets of \$1,131,259 and \$1,013,237 at June 30, 2010 and 2009, respectively, provided by a National Endowment for the Humanities matching grant, are restricted for retirement of indebtedness. The income from the investment of these monies and principal is to be utilized for retirement of plant indebtedness and is available to supplement the amount of unrestricted asset payments.

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

5. Long-Term Debt (continued)

Future annual principal and interest payments on notes and bonds payable as of June 30, 2010, are as follows:

Year	Bond and Mortgage Principal	Bond and Mortgage Interest	Total
2011	\$ 839,618	\$ 1,130,312	\$ 1,969,930
2012	876,943	1,094,115	1,971,058
2013	925,802	1,054,954	1,980,756
2014	968,612	1,015,357	1,983,969
2015	1,024,638	971,032	1,995,670
Thereafter	19,515,439	8,706,681	28,222,120
	\$ 24,151,052	\$ 13,972,451	\$ 38,123,503

On October 3, 2001, the University entered into a financing agreement designed to pay off the remaining principal balances of the Living Learning Center loan, science hall annex mortgage note payable, and the HBCU Loan No. 2, in addition to financing the construction of the music building annex, portions of the fine arts auditorium, and the purchase of a phone system and land surrounding the campus. The outstanding principal of the bond was originally backed by a \$21,960,042, three-year letter of credit agreement that matured on October 15, 2006, and was renewed each year until April 15, 2008. In October 2007, the letter of credit was amended and restated and matures October 15, 2012. It is then renewable until the July 1, 2032 maturity date of the bonds. The variable interest rate resembles the BMA rate.

Interest expense totaled \$1,252,018 for the year ended June 30, 2010, and \$1,390,696 for the year ended June 30, 2009. No interest was capitalized during the years ended June 30, 2009 or 2010.

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

6. Interest Rate Swaps

In November 2001, the University entered into a hedging relationship, the purpose of which was to hedge the variability of future cash flows attributed to interest rate fluctuations and, therefore, holds only cash flow hedges. The University entered into two variable-to-fixed interest rate swap contracts for 80% of the total outstanding bonds, leaving the remaining balance subject to market fluctuations. These swap agreements were to terminate on November 1, 2008. In May 2005, the University elected to extend the term of the swaps until November 1, 2015. On November 1, 2007, the University canceled these two swap agreements and replaced them with a single swap agreement terminating July 1, 2032, for the entire outstanding principal of the bonds. The University pays a blended average interest rate of approximately 4.777%.

The estimated value of the swap agreement at June 30, 2010 and 2009, is a liability of \$2,895,160 and \$2,077,244, respectively, and is included in accrued expenses and other liabilities in the statements of financial position. The fair value of interest rate swaps is the estimated market rates that the University would receive or pay to terminate the swaps at the reporting date. Net settlements under this agreement are recorded as adjustments to interest expense. These adjustments increased interest expense by \$656,777 and \$516,864 for the years ended June 30, 2010 and 2009, respectively. Changes in the fair value of the agreement are included in the change in value of interest rate swaps in the accompanying statements of activities as the instrument does not qualify for hedge accounting treatment. These adjustments total \$(817,916) and \$(1,194,971) for the years ended June 30, 2010 and 2009, respectively.

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

7. Fair Value of Financial Instruments and Fair Value Disclosures

The following table presents the fair values for assets and liabilities measured on a recurring basis by ASC 820 hierarchy level as of June 30, 2010:

Description	Fair Value	Level 1: Quoted prices in active markets for identical assets or liabilities	Level 2: Significant other observable inputs	Level 3: Significant unobservable inputs
Assets (liabilities)				
Cash and cash equivalents	\$ 20,765,842	\$ 20,765,842	\$ —	\$ —
Investments:				
U.S. mid to large-cap equity	10,069,658	10,069,658	—	—
U.S. small-cap equity	1,714,990	1,714,990	—	—
Global ex-U.S. equity	7,363,474	2,439,220	4,924,254 ⁽¹⁾	—
Hedge funds	3,209,191	—	—	3,209,191 ⁽²⁾
Commingled funds	3,031,812	—	3,031,812 ⁽¹⁾	—
Bonds	8,625,277	6,286,097	2,339,180 ⁽¹⁾	—
Short-term investment funds	20,818	20,818	—	—
Assets held in trust by others	315,783	—	—	315,783 ⁽⁴⁾
Interest rate swap	(2,895,160)	—	(2,895,160) ⁽³⁾	—

(1) The valuation of investments in certain global ex-U.S. equity funds, commingled funds, and bond funds are based on the values of the underlying investments, for which quoted market prices are readily available. The University then determines its share of the overall fair value. The global ex-U.S. equity investment classified as Level 2 is organized as a limited partnership. Participating shares are redeemable on a weekly basis (i.e., first day of the calendar month and every Friday) at the option of the University upon four days written notice. The bonds investment classified as Level 2 is organized as a limited partnership. Participating shares are redeemable on a monthly basis (i.e., first day of each calendar month) at the option of the University upon 15 days written notice.

(2) The fair value of this investment is based on the net asset value per share. The net asset value is determined by the fund manager, based on the values of the underlying investments. This investment is organized as a limited company. Participating shares are redeemable on a quarterly basis (i.e., first business day of the calendar quarter) at the option of the University upon 45 days written notice, after October 1, 2010 (one year from the date of initial subscription of participating shares).

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

7. Fair Value of Financial Instruments and Fair Value Disclosures (continued)

- (3) The valuation of this instrument is determined using market standard valuation techniques including discounted cash flow analysis on the expected cash flow of the derivative. The analysis reflects the contractual terms of the derivatives, including the period to maturity, and uses observable market-based inputs, such as interest rate curves. To comply with the provisions of ASC 820, the University incorporates credit valuation adjustments to appropriately reflect both its own nonperformance risk and the respective counterparty's nonperformance risk in the fair value measurements. In adjusting the fair value of the derivative contract for the effect of nonperformance risk, the University has considered the impact of netting and any applicable credit enhancements. The University has classified the entire derivative valuation in Level 2 of the hierarchy, as the impact of the credit valuation adjustment is not significant to the overall valuation.
- (4) The University is the irrevocable remainder beneficiary of several split-interest agreements. The assets of these charitable remainder trusts are held by an independent trustee. The University's interest in these trusts has been recorded at fair value using a payout rate of approximately 3.0% and a discount rate of 3.2%. The change in fair value since the prior year is driven by unrealized losses on the investments held by the trust. This change is included in net realized and unrealized losses on investments within the statement of activities.

The carrying value of receivables, accounts payable, and accrued expenses are reasonable estimates of their fair value due to the short-term nature of these financial instruments. The fair value of debt obligations is estimated based on quoted market prices for the same or similar issues or based on the current rates offered to the University for debt of the same maturities. The fair value of debt obligations approximates carrying value as of June 30, 2010 and 2009.

Changes in Fair Value of Level 3 Instruments

The University classifies the fair values of financial instruments within Level 3 if there are no observable markets for the instruments, or, in the absence of active markets, the majority of the inputs used to determine the fair value of the instruments are based on assumptions about market participants. The following is a rollforward table of Level 3 financial instruments for which we have used significant unobservable inputs in the fair value measurement on a recurring basis:

	Investment Hedge Funds	Assets Held in Trust by Others
Fair value as of June 30, 2009	\$ —	\$ 304,641
Purchases of investments	3,119,096	—
Unrealized gains included in change in net assets	90,095	11,142
Fair value as of June 30, 2010	<u>\$ 3,209,191</u>	<u>\$ 315,783</u>

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

8. Restricted Net Assets

Temporarily restricted net assets at June 30, 2010 and 2009, are available for the following purposes:

	<u>2010</u>	<u>2009</u>
Institution support programs and passage of time	\$ 257,518	\$ 267,396
Restricted programs	1,433,009	1,220,955
Acquisition of building and equipment	2,373,246	2,555,292
Student aid	6,664,269	6,071,459
Other educational and general operations	5,958,349	5,338,222
	<u>\$ 16,686,391</u>	<u>\$ 15,453,324</u>

Permanently restricted net assets at June 30, 2010 and 2009, are restricted in perpetuity, the income from which is expendable to support:

	<u>2010</u>	<u>2009</u>
Student aid	\$ 8,638,279	\$ 8,398,530
Other educational and general operations	485,449	481,165
	<u>\$ 9,123,728</u>	<u>\$ 8,879,695</u>

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes, principally for instruction, research, and departmental support, and as assets acquired with donor-restricted funds were placed into service.

9. Endowment

The University's endowment consists of approximately 160 individual funds established for a variety of purposes. Its endowment includes both donor-restricted endowment funds, either permanently or temporarily restricted, and funds designated by the Board of Trustees to function as endowments. As required by generally accepted accounting principles (GAAP), 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.

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

9. Endowment (continued)

Interpretation of Relevant Law

The State of Florida operates under the Florida Uniform Management of Institutional Funds Act (UMIFA), enacted in 2003. The Board of Trustees of the University has interpreted UMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. 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 in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the organization in a manner consistent with the standard of prudence prescribed by UMIFA. In accordance with UMIFA, the University considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

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

Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UMIFA requires the University to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature are reported in unrestricted net assets. As of June 30, 2010 and 2009, the amount of permanently restricted endowments whose fair value of assets was less than the level required by donor stipulation totaled \$419,078 and \$703,730, respectively. These deficiencies resulted from unfavorable market fluctuations that occurred shortly after the investment of new permanently restricted contributions and continued appropriation for certain programs that was deemed prudent by the Board of Trustees.

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

9. Endowment (continued)

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 organization must hold in perpetuity or for a donor-specified period(s) as well as board-designated funds. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner to attain an average annual real total return (net of investment management fees) of at least 5.0% over the long term (rolling 20-quarter periods). It is recognized that the real return objective may be difficult to attain in every such period, but should be attainable over a series of such periods.

Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, the University's investments are diversified by asset class, within asset classes and by manager. The purpose of diversification is to provide reasonable assurance that no class of securities, manager, or individual holding will have a disproportionate impact on the endowment's aggregate results. To achieve its long-term investment objective, the endowment's assets are invested primarily in equities, but also include allocations to asset classes that might serve as partial hedges against inflation and deflation. The asset allocation of the endowment reflects the University's long-term financial objectives as well as the University's tolerance for risk. Endowment results are measured relative to blended benchmarks composed of the appropriate asset class indices and weighted based upon the endowment's policy target and actual allocations.

Spending Policy and How the Investment Objectives Relate to Spending Policy

The endowment seeks to achieve reasonable stability in budgeting for University operations and to maintain intergenerational equity between near-term and long-term priorities. The Board of Trustees believe that, subject to exigent circumstances, a long-term spending rate of 3.0% of the endowment is appropriate and, therefore, has adopted the following spending policy: Spending from the endowment in any given fiscal year shall equal 3.0% of the endowment's average market value for the preceding 12 quarters. In establishing this policy, the University considered the long-term return objective of at least 5.0% over the long term.

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

9. Endowment (continued)

Changes in Endowment Net Assets

June 30, 2010

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	\$ 12,226,711	\$ 9,247,200	\$ 8,879,695	\$ 30,353,606
Investment return:				
Investment income	332,276	438,391	–	770,667
Net appreciation (realized and unrealized)	1,459,730	1,303,926	–	2,763,656
Total investment return	1,792,006	1,742,317	–	3,534,323
Contributions	–	19,330	244,033	263,363
Appropriation of endowment assets for expenditure	(123,867)	(378,504)	–	(502,371)
Other changes:				
Transfers to create board-designated endowment funds	386,299	–	–	386,299
Endowment net assets, end of year	<u>\$ 14,281,149</u>	<u>\$ 10,630,343</u>	<u>\$ 9,123,728</u>	<u>\$ 34,035,220</u>

Endowment Net Asset Composition by Type of Fund

June 30, 2010

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ (419,079)	\$ 10,630,343	\$ 9,123,728	\$ 19,334,992
Board-designated endowment funds	14,700,228	–	–	14,700,228
Total funds	<u>\$ 14,281,149</u>	<u>\$ 10,630,343</u>	<u>\$ 9,123,728</u>	<u>\$ 34,035,220</u>

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

9. Endowment (continued)

Changes in Endowment Net Assets

June 30, 2009

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	\$ 16,477,446	\$ 14,406,198	\$ 8,723,142	\$ 39,606,786
Investment return:				
Investment income	491,665	679,433	–	1,171,098
Net appreciation (realized and unrealized)	(5,025,101)	(5,549,331)	–	(10,574,432)
Total investment return	(4,533,436)	(4,869,898)	–	(9,403,334)
Contributions	–	–	156,553	156,553
Appropriation of endowment assets for expenditure	(135,857)	(289,100)	–	(424,957)
Other changes:				
Transfers to create board-designated endowment funds	418,558	–	–	418,558
Endowment net assets, end of year	<u>\$ 12,226,711</u>	<u>\$ 9,247,200</u>	<u>\$ 8,879,695</u>	<u>\$ 30,353,606</u>

Endowment Net Asset Composition by Type of Fund

June 30, 2009

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ (703,731)	\$ 9,247,200	\$ 8,879,695	\$ 17,423,164
Board-designated endowment funds	12,930,442	–	–	12,930,442
Total funds	<u>\$ 12,226,711</u>	<u>\$ 9,247,200</u>	<u>\$ 8,879,695</u>	<u>\$ 30,353,606</u>

Bethune-Cookman University, Inc.

Notes to Financial Statements (continued)

10. Retirement Plan

The University maintains a tax-sheltered annuity plan that is available to employees on a voluntary basis. The total expenses for this plan were \$825,595 and \$958,639 for the years ended June 30, 2010 and 2009, respectively.

11. Contingent Liabilities and Commitments

Litigation

In the normal course of business, the University is party to other various matters involving disputes and/or litigation. While it is not possible at this time to determine the ultimate outcome of these matters, the administration believes that any ultimate liability will not be material to the financial statements.

Contingencies

Amounts received by the University under federal and state financial assistance programs are subject to audit and adjustment by those grantor agencies. If expenses under those programs were to be disallowed as a result of such audits, the reimbursement to the federal or state government would be recorded as a liability of the University. In the opinion of the administration, any such adjustment would not be material to the University's financial statements or its financial assistance programs.

12. Subsequent Events

In preparing these financial statements, the University has evaluated events and transactions for potential recognition or disclosure through October 1, 2010, the date the financial statements were available to be issued. During this period, there were no subsequent events that required recognition in the financial statements. Additionally, there were no nonrecognized subsequent events that required disclosure.

This page intentionally left blank

Report of Independent Certified Public Accountants on
Internal Control Over Financial Reporting and on Compliance
and Other Matters Based on an Audit of the Financial Statements
Performed in Accordance With *Government Auditing Standards*

The Board of Trustees
Bethune-Cookman University, Inc.

We have audited the financial statements of Bethune-Cookman University, Inc. as of and for the year ended June 30, 2010, and have issued our report thereon dated October 1, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the University's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the University's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the University's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

This page intentionally left blank.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the University's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of management, the Board of Trustees, others within the entity, federal and state awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties.

Ernst + Young LLP

October 1, 2010

This page intentionally left blank.

Ernst & Young LLP

Assurance | Tax | Transactions | Advisory

About Ernst & Young

Ernst & Young is a global leader in assurance, tax, transaction and advisory services. Worldwide, our 144,000 people are united by our shared values and an unwavering commitment to quality. We make a difference by helping our people, our clients and our wider communities achieve their potential.

For more information, please visit www.ey.com

Ernst & Young refers to the global organization of member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. This Report has been prepared by Ernst & Young LLP, a client serving member firm located in the United States.

