

DREXEL UNIVERSITY AND SUBSIDIARIES

FINANCIAL REPORT

June 30, 2008



INDEPENDENT AUDITORS' REPORT

Board of Trustees
Drexel University
Philadelphia, Pennsylvania

We have audited the accompanying consolidated statements of financial position of Drexel University and subsidiaries (the "University") as of June 30, 2008 and 2007, and the related consolidated statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the University as of June 30, 2008 and 2007, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the consolidated financial statements, the University changed its method of accounting in 2007 for postretirement obligations.

Our audits were conducted for the purposes of forming an opinion on the basic consolidated financial statements taken as a whole. The supplemental consolidating schedules on pages 21-24 are presented for the purpose of additional analysis of the basic consolidated financial statements rather than to present the financial position and change in net assets of the individual entities, and are not a required part of the basic consolidated financial statements. These schedules are the responsibility of the University's management. Such schedules have been subject to the auditing procedures applied in our audits of the basic consolidated financial statements and, in our opinion, are fairly presented in all material respects when considered in relation to the basic consolidated financial statements taken as a whole.

Deloitte & Touche LLP

September 23, 2008

DREXEL UNIVERSITY and SUBSIDIARIES
CONSOLIDATED STATEMENTS of FINANCIAL POSITION
as of June 30, 2008 and 2007 (in thousands)

ASSETS	<u>2008</u>	<u>2007</u>
Cash and cash equivalents:		
Operating cash	\$ 41,214	\$ 45,637
Risk Retention Group cash	3,354	3,139
Accounts receivable, net:		
Tuition	39,081	27,995
Patients	6,194	5,377
Grants, contracts and other	29,070	31,580
Tenet HealthSystem	801	1,243
Total accounts receivable	<u>75,146</u>	<u>66,195</u>
Contributions receivable, net	42,483	31,351
Other assets	37,608	32,763
Deposits with bond trustees	145,028	15,075
Student loans receivable, net	32,786	32,097
Beneficial interests in trusts	26,658	29,309
Investments	576,846	646,508
Land, buildings and equipment, net	<u>446,612</u>	<u>428,009</u>
Total assets	<u>\$ 1,427,735</u>	<u>\$ 1,330,083</u>
 LIABILITIES		
Accounts payable	\$ 44,696	\$ 41,360
Accrued expenses	72,779	62,619
Lines of credit	195	4,874
Deposits	22,745	20,548
Deferred revenue	58,292	54,332
Government advances for student loans	26,151	25,700
Postretirement benefits	25,331	25,119
Bonds and notes payable	<u>389,311</u>	<u>252,624</u>
Total liabilities	<u>639,500</u>	<u>487,176</u>
 NET ASSETS		
Unrestricted	401,487	428,668
Temporarily restricted	192,644	222,858
Permanently restricted	<u>194,104</u>	<u>191,381</u>
Total net assets	<u>788,235</u>	<u>842,907</u>
Total liabilities and net assets	<u>\$ 1,427,735</u>	<u>\$ 1,330,083</u>

See notes to consolidated financial statements.

DREXEL UNIVERSITY and SUBSIDIARIES
CONSOLIDATED STATEMENT of ACTIVITIES
for the year ended June 30, 2008 (in thousands)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
OPERATING REVENUE				
Tuition and fees	\$ 472,010			\$ 472,010
Less: institutional financial aid	(111,137)			(111,137)
Net student revenue	360,873			360,873
Patient care activities	83,415			83,415
State appropriations	18,806			18,806
Government grants and contracts	89,894			89,894
Private grants and contracts	14,367			14,367
Private gifts	4,174	\$ 35,222		39,396
Endowment payout under spending formula	10,365	14,453	\$ 216	25,034
Investment income	6,359	5,082		11,441
Sales and services of auxiliary enterprises	59,516			59,516
Other sources	19,320			19,320
Net assets released from restrictions	30,135	(30,135)		
Total operating revenue	697,224	24,622	216	722,062
OPERATING EXPENSE				
College programs	230,179			230,179
Research and public service	85,495			85,495
Academic support	19,425			19,425
Student services	33,261			33,261
Institutional support	88,131			88,131
Scholarships and fellowships	14,547			14,547
Auxiliary enterprises	32,347			32,347
Total education and general	503,385			503,385
Patient care activities	93,191			93,191
Operation and maintenance	41,967			41,967
Interest	15,846			15,846
Depreciation	25,132			25,132
Total operating expense	679,521			679,521
Change in net assets from operating activities	17,703	24,622	216	42,541
NON-OPERATING ACTIVITY				
Endowment and other gifts			4,746	4,746
Realized/unrealized loss on investments, including endowment payout of \$18,322	(37,257)	(54,836)	(2,239)	(94,332)
Other non-operating expense	(7,627)			(7,627)
Change in net assets from non-operating activities	(44,884)	(54,836)	2,507	(97,213)
Change in net assets	(27,181)	(30,214)	2,723	(54,672)
Net assets at beginning of year	428,668	222,858	191,381	842,907
Net assets at end of year	\$ 401,487	\$ 192,644	\$ 194,104	\$ 788,235

See notes to consolidated financial statements.

DREXEL UNIVERSITY and SUBSIDIARIES
CONSOLIDATED STATEMENT of ACTIVITIES
for the year ended June 30, 2007 (in thousands)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
OPERATING REVENUE				
Tuition and fees	\$ 424,313			\$ 424,313
Less: institutional financial aid	(91,302)			(91,302)
Net student revenue	333,011			333,011
Patient care activities	79,508			79,508
State appropriations	18,711			18,711
Government grants and contracts	90,357			90,357
Private grants and contracts	12,349			12,349
Private gifts	6,545	\$ 13,775		20,320
Endowment payout under spending formula	9,398	13,138	\$ 198	22,734
Investment income	5,509	4,605		10,114
Sales and services of auxiliary enterprises	52,594			52,594
Other sources	16,670			16,670
Net assets released from restrictions	25,668	(26,107)	439	
Total operating revenue	650,320	5,411	637	656,368
OPERATING EXPENSE				
College programs	204,129			204,129
Research and public service	81,928			81,928
Academic support	17,732			17,732
Student services	30,508			30,508
Institutional support	84,836			84,836
Scholarships and fellowships	12,470			12,470
Auxiliary enterprises	30,245			30,245
Total education and general	461,848			461,848
Patient care activities	87,517			87,517
Operation and maintenance	41,719			41,719
Interest	11,840			11,840
Depreciation	21,832			21,832
Total operating expense	624,756			624,756
Change in net assets from operating activities	25,564	5,411	637	31,612
NON-OPERATING ACTIVITY				
Endowment and other gifts			2,995	2,995
Settlements			256	256
Realized/unrealized gain on investments, net of endowment payout of \$13,507	45,424	46,978	2,816	95,218
Other non-operating expense	(9,229)			(9,229)
Change in net assets from non-operating activities	36,195	46,978	6,067	89,240
Cumulative effect of accounting change	(8,283)			(8,283)
Change in net assets	53,476	52,389	6,704	112,569
Net assets at beginning of year	375,192	170,469	184,677	730,338
Net assets at end of year	\$ 428,668	\$ 222,858	\$ 191,381	\$ 842,907

See notes to consolidated financial statements.

DREXEL UNIVERSITY and SUBSIDIARIES

CONSOLIDATED STATEMENTS of CASH FLOWS

for the years ended June 30, 2008 and 2007 (in thousands)

	<u>2008</u>	<u>2007</u>
CASH FLOW FROM OPERATING ACTIVITIES		
(Decrease) increase in net assets	\$ (54,672)	\$ 112,569
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	25,132	21,832
Other changes and disposals of property and equipment	218	2,719
Decrease (increase) in beneficial interests in trusts	2,651	(1,847)
Contributions for long-term investment	(4,746)	(2,985)
Settlements		(256)
Actuarial change on annuity liabilities	(511)	1,463
Realized/unrealized loss (gain) on investments	94,332	(95,218)
Changes in operating assets and liabilities:		
Accounts receivable	(8,951)	8,199
Contributions receivable	(11,132)	(4,385)
Accounts payable and accrued expenses	10,818	10,024
Postretirement benefits	212	9,127
Other changes	1,312	(5,949)
Net cash provided by operating activities	<u>54,663</u>	<u>55,293</u>
CASH FLOW FROM INVESTING ACTIVITIES		
Purchase of investments	(242,053)	(370,839)
Proceeds from sale of investments	217,383	363,899
Proceeds from student loan collections	10,080	12,874
Student loans issued	(10,769)	(12,646)
Purchase of land, buildings and equipment	(40,000)	(66,187)
Deposits placed with bond trustees	(144,320)	
Use of deposits with bond trustees	14,367	17,452
Net cash used in investing activities	<u>(195,312)</u>	<u>(55,447)</u>
CASH FLOW FROM FINANCING ACTIVITIES		
Contributions restricted for endowments	4,746	2,985
Payments on annuity obligations	(764)	(968)
Government advances for student loans	451	64
Proceeds from long-term borrowings	149,206	
Repayment of short-term debt	(4,679)	(1,197)
Repayment of long-term debt	(12,519)	(6,042)
Net cash provided by (used in) financing activities	<u>136,441</u>	<u>(5,158)</u>
Net decrease in cash and cash equivalents	<u>(4,208)</u>	<u>(5,312)</u>
Cash and cash equivalents at beginning of year	<u>48,776</u>	<u>54,088</u>
Cash and cash equivalents at end of year	<u>\$ 44,568</u>	<u>\$ 48,776</u>
SUPPLEMENTAL INFORMATION		
Gifts in kind	\$ 533	\$ 236
Cash paid for interest	\$ 14,830	\$ 11,923

See notes to consolidated financial statements.

DREXEL UNIVERSITY and SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

for the Years Ended June 30, 2008 and 2007

Note 1: Summary of Significant Accounting Policies

Basis of Financial Statements: Drexel University (the "University") is a private research university located in Philadelphia, Pennsylvania. The University is an exempt organization under Section 501 (c) (3) of the Internal Revenue Code. The financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for not-for-profit organizations. Under these principles, contributions or unconditional promises to give are recognized as revenues in the period received at their net present value, less an allowance for uncollectible pledges. Resources are reported for accounting purposes in separate classes of net assets based on the existence or absence of donor-imposed restrictions. In the accompanying financial statements, net assets that have similar characteristics have been combined into similar categories as shown below.

Permanently restricted: Net assets subject to donor-imposed stipulations that they be maintained permanently by the University. Generally, the donors of these assets permit the University to use all or part of the income earned on these assets. Such assets are included in the University's permanent endowment funds.

Temporarily restricted: Net assets whose use by the University is subject to donor-imposed restriction that can be fulfilled by actions of the University in accordance with those stipulations or by the passage of time, including the following:

Endowment income and contributions with donor-imposed restrictions are reported as temporarily restricted and are reclassified to unrestricted net assets when the donor-imposed restrictions have been met.

The University utilizes endowment gains under a spending formula, subject to certain limitations. Since endowment net realized and unrealized gains may eventually be spent by the University, these gains are recorded in the financial statements as temporarily restricted net assets until transferred to unrestricted net assets.

Unrestricted: Net assets that are not subject to donor-imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of the Board of Trustees or may otherwise be limited by contractual agreements with outside parties.

Expenses are generally reported as decreases in unrestricted net assets. Expirations of donor-imposed stipulations are reported as net assets released from restrictions.

All revenues received and expenditures paid prior to the end of the fiscal year which relate to the following fiscal year are recorded and reflected as deferred revenues and deferred charges, respectively.

Note 1: Summary of Significant Accounting Policies, continued...

Philadelphia Health & Education Corporation: The University owns 100% of the Philadelphia Health & Education Corporation, doing business as Drexel University College of Medicine ("PHEC"). PHEC is party to an Academic Affiliation Agreement with Tenet HealthSystem Philadelphia, Inc. ("Tenet") intended to establish a relationship to foster continued coordination and integration between PHEC and the Tenet hospitals. This agreement, dated November 10, 1998 and subsequently amended on April 25, 2002, is effective until June 30, 2022 and may be renewed thereafter for separate and successive five-year terms. Under the terms of the agreement, PHEC commits to furnish administrative, supervisory, and teaching services to Tenet at budgeted levels through June 30, 2022 (see Note 11).

PHEC is also party to an agreement with the University to provide teaching and administrative services for the education of the University's medical students. The agreement, which automatically renews annually, is effective until June 30, 2009. In addition, PHEC has engaged the University to provide service and personnel for its administrative and academic operations.

Academic Properties, Inc.: The University owns 100% of Academic Properties, Inc. ("API"), a tax-exempt organization. API manages properties utilized by the University as well as other strategically located properties contiguous to the campus. The balances and activities of API are consolidated in the University's financial statements.

Drexel e-Learning, Inc.: The University owns 100% of the issued and outstanding stock of Drexel e-Learning, Inc. ("DeL"). DeL was created to provide educational products and services through distance learning. The balances and activities of DeL are consolidated in the University's financial statements.

Cash and Cash Equivalents: Cash and cash equivalents represent demand deposits and other investments with an initial maturity date not exceeding 90 days.

Beneficial Interests in Trusts: Gifts held by outside trustees for whom the University has a beneficial interest are recorded at the present value of expected future cash flows as unrestricted, temporarily and permanently restricted net assets and related beneficial interests in trusts in the consolidated financial statements.

Fair Value of Financial Instruments: Investments including real estate and property investments are recorded at fair market value. Gains or losses on investments are recognized as increases or decreases in unrestricted net assets unless their use is temporarily or permanently restricted by explicit donor stipulations or by law. The fair value of investments in publicly-traded debt and equity securities is based upon quoted market prices. The fair values for certain other investments including real estate and private equity held in limited partnerships or commingled funds is estimated by the respective external investment managers based on an assessment of the current market conditions or activities underlying each asset class as appropriate, if market values are not readily ascertainable. A reasonable estimate of the fair value of loans receivable from students under government loan programs and refundable federal student loans could not be made because the loans are not readily saleable. These loans are recorded at cost, less an allowance for doubtful accounts. The carrying amount of all other financial instruments approximates fair value (see Note 7).

Note 1: Summary of Significant Accounting Policies, continued...

Accounting for Derivative Instruments and Hedging Activities: The University entered into a fixed-to-variable interest rate swap agreement with Bank of America, N.A. ("Bank") that converts \$18,000,000 of the University's fixed rate term bonds (4.80%) to a USD floating rate obligation based on the BMA Municipal Swap Index. For 2008 and 2007, the agreement resulted in a gain on investments of \$5,000 and \$36,000, respectively, reported in the consolidated statement of activities. The estimated fair value of the agreement was \$176,000 at June 30, 2007. During 2008, the Bank exercised its right to terminate the agreement.

The University also entered into a variable-to-fixed swap agreement with Wachovia Bank, N.A. that converts the Series B of 2005 bonds to a fixed interest rate of 3.414% through the maturity of the bonds. The agreement resulted in losses of \$1,984,000 and \$108,000 in 2008 and 2007, respectively, reported as an unrealized loss on investments in the consolidated statement of activities. The estimated fair value of the agreement was (\$281,000) and \$1,703,000, respectively, at June 30, 2008 and 2007.

Patient Care Activities: PHEC faculty physicians participate in several physician practice plans that are managed by PHEC. Revenue and expenses related to these practice plans are recorded as patient care activities.

Patient care activities represent amounts received and the estimated net realizable amounts due from patients and third-party payers for services rendered. PHEC provides care to patients under various reimbursement arrangements, including Medicare and Medicaid. These arrangements provide for payment for covered services at agreed-upon rates and under certain fee schedules and various discounts from charges. Provisions have been made in the consolidated financial statements for estimated contractual adjustments, representing the difference between the customary charges for services rendered and related reimbursement. In both 2008 and 2007, revenue from Medicare and Medicaid programs combined and from managed care payers accounted for 18% and 53%, respectively, of gross patient service revenue.

Schuylkill Crossing Reciprocal Risk Retention Group: The Schuylkill Crossing Reciprocal Risk Retention Group (the "RRRG") operates to provide primary coverage for claims-made medical professional liability insurance for health care professionals employed by PHEC. The RRRG is owned 87% by PHEC and 13% by the University.

At June 30, 2008, the assets and ownership equity of the RRRG amounted to \$31,205,000 and \$2,747,000, respectively, and revenues and expenses for the year then ended were \$1,053,000 and \$1,038,000, respectively. At June 30, 2007, the assets and ownership equity of the RRRG were \$27,155,000 and \$2,482,000, respectively, and revenues and expenses were \$878,000 and \$1,254,000, respectively. The balances and activities of the RRRG are included in the accompanying consolidated financial statements.

Non-operating Activities: Non-operating activities include contributions restricted for endowment, gains/losses on investments in excess of payouts under the endowment spending policies, settlements of claims related to PHEC, loss on the disposal of equipment, postretirement benefit adjustment, start-up costs for the Drexel College of Law and for the University's Sacramento campus.