**UNIVERSITY OF MINNESOTA FOUNDATION**

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Independent Auditors’ Report

The Board of Trustees
University of Minnesota Foundation:

We have audited the accompanying consolidated statement of financial position of the University of Minnesota Foundation (the Foundation) as of June 30, 2000, and the related consolidated statements of activities and cash flows for the year then ended. These financial statements are the responsibility of the Foundation’s management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the Foundation’s fiscal 1999 financial statements and, in our report dated September 10, 1999, we expressed an unqualified opinion on those financial statements.

We conducted our audit 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides 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 Foundation as of June 30, 2000, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

September 1, 2000
(1) Organization and Summary of Significant Accounting Policies

The University of Minnesota Foundation (the Foundation) was incorporated as a not-for-profit corporation in the state of Minnesota in 1962 and operates exclusively for the benefit of the University of Minnesota (the University).

The accounting policies of the Foundation conform to generally accepted accounting principles. The following is a summary of the more significant policies:

(a) Principles of Consolidation

The consolidated financial statements include those of the Foundation and its related entity, the University of Minnesota Foundation Investment Advisors (UMFIA). UMFIA is a nonprofit organization established to oversee the investment and management of the investments of the Foundation. All significant intercompany accounts and transactions have been eliminated in the consolidated financial statements.

The Foundation does not report the University Gateway Corporation (Gateway) as part of its consolidated financial statements. Gateway is a nonprofit organization established to construct, own, and operate a facility to be used to support its beneficiary organizations and the University in student recruiting, alumni relations, fundraising activities, and general operations. Under accounting principles generally accepted in the United States of America, consolidation of Gateway is permitted, but not required.

(b) Basis of Presentation

Net assets and revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Net assets of the Foundation and changes therein are classified into the following three categories:

- Unrestricted net assets represent the portion of expendable funds that are available for support of the operations of the Foundation.
- Temporarily restricted net assets consist of contributions that have been restricted by the donor for specific purposes or are time restricted.
- Permanently restricted net assets consist of contributions that have been restricted by the donor that stipulate the resources be maintained permanently, but permit the Foundation to use or expend part or all of the income derived from the donated assets for either specified or unspecified purposes.

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

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

(d) **Contributions**

Contributions, including unconditional promises to give, are recognized as revenues in the period 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 to be received after one year are discounted at 6.36%. Amortization of discounts is recorded as additional contribution revenue. An allowance for uncollectible contributions receivable is provided based upon management’s judgment including such factors as prior collection history.

(e) **Unitrusts, Pooled Income, and Annuity Agreements**

The Foundation has entered into unitrust, pooled income, and annuity agreements that provide, among other matters, that the trustee shall pay to the beneficiaries an annual income payment until the income obligation is completed in accordance with the donor’s trust agreement. The Foundation records its interest in these trusts at the current market value of the related assets and a corresponding liability recorded for the actuarially determined present value of payments to be made to the designated beneficiaries with the residual amount recorded for the purposes designated when the gift is received. Upon termination of the income obligation, property in the trust or pooled income fund is held by the Foundation in accordance with the donor’s trust agreement.

(f) **Gift Annuity Agreements**

The Foundation has entered into gift annuity agreements that provide that the Foundation shall pay to the designated beneficiaries an annual amount until the death of the designated beneficiaries. The payments continue even if the assets of the gift annuity fund have been exhausted. The Foundation records these gift annuities at market value and a corresponding liability recorded for the actuarially determined present value of payments to be made to the designated beneficiaries, with the residual amount recorded for the purposes designated when the gift is received. Upon the death of the beneficiaries, property in the gift annuity fund is held by the Foundation in accordance with the agreements.

(g) **Trusts Held by Other Entities**

The Foundation may be a charitable remainder or perpetual beneficiary of trust accounts that are held by another entity such as a bank or another charitable organization. The Foundation records these trusts, after discovery of their existence, at the present value of the estimated future cash receipts from the assets of the trust. Because of the complex issues related to collecting the data for these transactions, there can be a time delay in the recording of the asset because of the time needed for discovery, verification of the Foundation’s rights, and the determination of the valuation of future payments.
(h) Income Taxes

The Internal Revenue Service has ruled that the Foundation is a publicly supported organization under Internal Revenue Code, Section 170(b)(1)(A) and is not a private foundation as defined under Section 509(a)(2). The Foundation is a tax-exempt organization under Section 501(c)(3) and, as such, is subject to federal income tax only on net unrelated business income.

(i) Investments

Marketable securities and mutual funds are recorded at fair value using public market quotations. Limited partnerships are recorded at the fair value determined by the partnership. Contract for deed is recorded at the remaining outstanding principal balance. Land is recorded at the fair market value at the date of donation.

Donated investments are recorded at their fair values, as determined on the date of donation. Investment income and gains and losses are recorded in the period incurred.

For management efficiency, investments of the unrestricted and restricted net assets are pooled, except for certain net assets that the Board of Trustees or the donors have designated to be segregated and maintained separately.

(j) Fair Value of Financial Instruments

The carrying amounts of cash, other receivables, due from related parties, and accounts payable approximate fair value because of the short maturity of these instruments. Investment collateral is reported at fair value using public market quotations of the underlying investments. The fair value of pledges receivable is determined as the present value of expected future cash flows using a discount rate. The fair value of interest in unitrusts, pooled income, and annuity trusts and gift annuities is based on quoted market prices at the reporting date of the underlying investments.

Unitrusts, pooled income, and annuity trusts payable, and gift annuities payable are reported at fair value based on the life expectancy of the beneficiaries and the present value of expected cash flows using a discount rate. Investments held for the custody of others are reported at fair value based on the fair value of the underlying investments. Payable under investment loan agreement is reported at fair value using public market quotations of the underlying investments.

(k) Property and Equipment

Property and equipment are stated at cost and depreciated over their estimated useful lives using the straight-line method.

(l) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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 these estimates.
(m) **Reclassifications**

Certain 1999 amounts have been reclassified to conform with the 2000 presentation.

(n) **Prior-year Information**

The consolidated financial statements include certain prior year information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in accordance with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Foundation’s financial statements for the year ended June 30, 1999, from which the summarized information was derived.

(2) **Gifts and Pledges**

New pledge commitments are reported as pledges receivable. Contributions not related to previous pledges and new pledge commitments received during the year are reported as revenue. The total of gifts and pledges generated is as follows:

- Contributions not related to previous pledges $45,354,812
- New pledge commitments 63,371,653

Total new gifts and pledges $108,726,465

Contributions as stated in the statement of activities include $816,929 of indirect support received by the Foundation.

(3) **Investments**

The investments at June 30, 2000, are summarized as follows:

**Marketable securities:**
- Cash and cash equivalents $47,668,434
- Corporate stocks & bonds 250,010,938
- U.S. Government obligations 143,549,958
- Municipal bonds 5,610,576
- Other investments 105,333

Total marketable securities 446,945,239

<table>
<thead>
<tr>
<th>Category</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity mutual funds</td>
<td>132,480,734</td>
</tr>
<tr>
<td>Limited partnerships</td>
<td>215,775,968</td>
</tr>
<tr>
<td>Contract for deed</td>
<td>48,729</td>
</tr>
<tr>
<td>Land</td>
<td>1,082,743</td>
</tr>
</tbody>
</table>

Total investments $796,333,413
Investments include funds held for the custody of others of $41,269,528 at June 30, 2000.
The Foundation’s investment in limited partnerships includes approximately $86,790,000 invested in a limited partnership which is organized as a commodity pool for the purpose of investing stock index futures, options and short-term and other liquid debt instruments to approximate the total return of the Standard and Poor’s 500 Index.

(4) Pledges Receivable

Pledges receivable, net of unamortized discount of $6,764,744, are summarized as follows at June 30, 2000:

<table>
<thead>
<tr>
<th>Unconditional promises expected to be collected in:</th>
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<tbody>
<tr>
<td>Less than one year</td>
<td>$22,362,483</td>
</tr>
<tr>
<td>One year to five years</td>
<td>22,715,014</td>
</tr>
<tr>
<td>Greater than five years</td>
<td>5,010,838</td>
</tr>
<tr>
<td></td>
<td>50,088,335</td>
</tr>
</tbody>
</table>

Reserve for uncollectible pledges (669,546)

Pledges receivable $49,418,789

In addition, the Foundation has received conditional promises to give in the amount of $18,372,096 as of June 30, 2000. These gifts are primarily conditioned on completion of building or fundraising projects, evaluation of progress on projects, or matching funds.

(5) Property and Equipment

The following is a summary of property and equipment at June 30, 2000:

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<table>
<thead>
<tr>
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<tbody>
<tr>
<td>Leasehold improvements</td>
<td>$472,305</td>
</tr>
<tr>
<td>Furniture &amp; fixtures</td>
<td>1,843,645</td>
</tr>
<tr>
<td>Less accumulated depreciation</td>
<td>(726,926)</td>
</tr>
<tr>
<td></td>
<td>$1,589,024</td>
</tr>
</tbody>
</table>
(6) **Temporarily Restricted Net Assets**

Temporarily restricted net assets are available as of June 30, 2000, for the following purposes:

- Capital improvement/facilities $39,613,642
- Faculty support $12,486,304
- Scholarships and fellowships $105,891,359
- Lectureships, professorships, and chairs $135,395,450
- College program support $198,393,244
- Research $27,704,068
- Trusts $13,695,429
- Other $2,423,366

**Total:** $535,602,862

(7) **Permanently Restricted Net Assets**

Permanently restricted net assets are restricted to investment in perpetuity. The permanent restricted net asset balances and purposes the income is expendable to support as of June 30, 2000, are as follows:

- Capital improvement/facilities $3,334,435
- Faculty support $15,133,839
- Scholarships and fellowships $65,596,510
- Lectureships, professorships, and chairs $105,535,383
- College program support $54,738,175
- Research $6,826,648
- Trusts $23,229,422
- Other $34,386

**Total:** $274,428,798

(8) **Support Services Revenue and Expense**

The Foundation provides much of the development functions for the University. An annual amount is allocated by the University to reimburse the Foundation for a portion of the direct costs of support services provided by the Foundation on behalf of the University.

The costs of the various programs and other activities have been summarized on a functional basis in the statement of activities. Accordingly, certain costs have been allocated among the programs and support services benefited.

(9) **Loan Guaranty**
The Foundation is the guarantor of principal and interest payments on long-term debt outstanding that is the obligation of Gateway. The total amount of long-term debt outstanding subject to this guaranty is $40,000,000. Principal is scheduled to be paid starting in fiscal year 2002.
(10) **Summarized Financial Data for Gateway (Unaudited)**

Summarized financial data for Gateway as of and for the year ended June 30, 2000 was as follows:

- **Total assets**: $55,731,813
- **Total liabilities**: $43,300,897
- **Net assets**: $12,430,916
- **Revenues**: $3,193,298
- **Expenses**: $3,390,605
- **Decrease in net assets**: $(197,307)

(11) **Restatement of Net Assets**

The Foundation maintains funds on deposit with the University which are drawn upon throughout the year to meet support service and fundraising expenses. Such amounts are available in subsequent years if not used during the current fiscal year and, accordingly, are considered an asset of the Foundation.

As of June 30, 1999, the Foundation had $1,062,187 on deposit with the University which was not reported in the financial statements as of and for the year ended June 30, 1999. Accordingly, the Foundation has restated opening net assets as of July 1, 1999 as follows:

- **Unrestricted net assets, beginning of year**: $34,305,872
- **Restatement of unrestricted net assets to record amounts on deposit with the University**: $1,062,187
- **Unrestricted net assets, beginning of year, as restated**: $35,368,059
(12) Leases

During fiscal 1999, the Foundation entered into an operating lease for office space with the University Gateway Corporation, a related party. Terms of the lease call for minimum base rent of $637,415 annually through 2024. Rent expense for the year ended June 30, 2000 was $479,869. Minimum annual payments under terms of the lease are as follows:

<table>
<thead>
<tr>
<th>Year ending June 30</th>
<th></th>
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<tbody>
<tr>
<td>2001</td>
<td>637.415</td>
</tr>
<tr>
<td>2002</td>
<td>637.415</td>
</tr>
<tr>
<td>2003</td>
<td>637.415</td>
</tr>
<tr>
<td>2004</td>
<td>637.415</td>
</tr>
<tr>
<td>2005</td>
<td>637.415</td>
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<tr>
<td>Thereafter</td>
<td>637.415</td>
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