

Financial Statements and Report of Independent
Certified Public Accountants

Elizabethtown College

June 30, 2008 and 2007

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Report of Independent Certified Public Accountants

Board of Trustees
Elizabethtown College

We have audited the accompanying statements of financial position of Elizabethtown College (the College) as of June 30, 2008 and 2007 and the related statements of activities and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the College'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 as established by the American Institute of Certified Public Accountants. Those standards require that we plan and perform the audits 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 College's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Elizabethtown College as of June 30, 2008 and 2007, and the results of its activities and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Grant Thornton LLP

Philadelphia, Pennsylvania

October 15, 2008

Elizabethtown College

STATEMENTS OF FINANCIAL POSITION

June 30,

ASSETS	2008	2007
Current assets		
Cash and cash equivalents	\$ 2,881,548	\$ 1,374,880
Short-term investments	2,929,801	8,090,237
Accrued interest receivable	10,228	7,197
Accounts and notes receivable		
Students (net of allowance for uncollectible accounts of \$10,577 and \$17,829 in 2008 and 2007, respectively)	125,327	172,303
Other	1,039,650	1,491,839
Inventories	369,229	273,319
Prepaid expenses	203,179	458,934
Pledges receivable due in less than one year (net of allowance for uncollectible pledges of \$57,950 and \$59,073 in 2008 and 2007, respectively)	1,248,130	1,267,953
Total current assets	8,807,092	13,136,662
Construction fund held in trust	3,175,218	3,227,417
Pledges receivable (net of allowance for uncollectible pledges of \$276,648 and \$340,927 in 2008 and 2007, respectively)	5,809,466	7,317,772
Student loans (net of allowance for uncollectible loans of \$60,000 in 2008 and 2007)	1,326,050	1,331,721
Derivative instruments	274,900	-
Investments	62,825,604	63,762,475
Property, plant and equipment (net of accumulated depreciation of \$39,071,395 and \$36,028,949 in 2008 and 2007, respectively)	76,255,251	68,198,042
Other assets	882,723	927,134
Total assets	\$ 159,356,304	\$ 157,901,223
LIABILITIES AND NET ASSETS		
Liabilities		
Accounts payable	\$ 1,956,603	\$ 3,517,577
Accrued salaries, wages and benefits	1,267,796	1,013,730
Deposits and agency funds	1,801,076	1,816,011
Current liability on annuity contracts and trusts	161,691	155,412
Current portion of long-term debt	1,329,977	1,262,724
Total current liabilities	6,517,143	7,765,454
Advances from federal government for student loans	1,191,303	1,184,217
Annuity contracts and trusts liability	4,218,924	4,325,536
Post-retirement liability	6,700,884	6,218,576
Derivative instruments	1,129,518	976,470
Long-term debt	44,297,515	45,652,558
Total liabilities	64,055,287	66,122,811
Net assets		
Unrestricted	45,901,191	43,167,735
Temporarily restricted	23,332,578	23,210,765
Permanently restricted	26,067,248	25,399,912
Total net assets	95,301,017	91,778,412
Total liabilities and net assets	\$ 159,356,304	\$ 157,901,223

The accompanying notes are an integral part of these statements.

STATEMENTS OF ACTIVITIES

Year ended June 30,

	2008			2007			
	Unrestricted	Temporarily restricted	Permanently restricted	Unrestricted	Temporarily restricted	Permanently restricted	Total
Revenue							
Student related revenue							
Student tuition and fees, gross	\$ 58,838,485	\$ -	\$ -	\$ 58,838,485	\$ -	\$ -	\$ 58,838,485
Less tuition discount	(21,625,794)	-	-	(21,625,794)	-	-	(21,029,938)
Student tuition and fees, net	37,212,691	-	-	37,212,691	-	-	34,460,893
Auxiliary enterprises	15,051,914	-	-	15,051,914	-	-	15,036,853
Private gifts and grants	894,877	2,013,957	667,336	3,576,170	3,156,408	3,555,417	7,557,089
Government grants	2,307,270	-	-	2,307,270	-	-	2,167,754
Investment income	976,059	800,029	-	1,776,088	241,188	-	1,450,717
Gains on investments	696,520	1,182,580	-	1,879,100	5,522,794	-	9,527,794
Gain on interest rate swap	121,852	-	-	121,852	-	-	737,649
Other	74,584	-	-	74,584	-	-	13,767
Net assets released from restrictions	3,874,753	(3,874,753)	-	4,207,011	(4,207,011)	-	-
Total revenue	61,210,520	121,813	667,336	61,999,669	4,713,379	3,555,417	70,952,516
Expenses							
Instruction	20,249,327	-	-	18,404,206	-	-	18,404,206
Academic support	2,305,676	-	-	2,305,676	-	-	2,793,683
Student services	6,257,379	-	-	5,650,136	-	-	5,650,136
Institutional support	10,951,027	-	-	10,951,027	-	-	9,667,869
Student aid	807,415	-	-	807,415	-	-	728,932
Facilities							
Operation and maintenance of plant	5,071,565	-	-	4,862,140	-	-	4,862,140
Depreciation and amortization	3,062,242	-	-	3,083,105	-	-	3,083,105
Interest	2,639,842	-	-	2,841,691	-	-	2,841,691
Auxiliary enterprises	6,942,481	-	-	6,922,972	-	-	6,922,972
Pension related changes other than net periodic pension cost	190,111	-	-	-	-	-	-
Total expenses	58,477,065	-	-	54,954,734	-	-	54,954,734
Change in net assets before cumulative effect of change in accounting principle	2,733,455	121,813	667,336	7,728,986	4,713,379	3,555,417	15,997,782
Cumulative effect of change in accounting principle	-	-	-	(2,345,855)	-	-	(2,345,855)
Change in net assets	2,733,455	121,813	667,336	5,383,131	4,713,379	3,555,417	13,651,927
Net assets							
Net assets, beginning of year	43,167,735	23,210,765	25,399,912	37,784,604	18,497,386	21,844,495	78,126,485
Net assets, end of year	\$ 45,901,190	\$ 23,332,578	\$ 26,067,248	\$ 43,167,735	\$ 23,210,765	\$ 25,399,912	\$ 91,778,412

The accompanying notes are an integral part of these statements.

Elizabethtown College

STATEMENTS OF CASH FLOWS

Year ended June 30,

	<u>2008</u>	<u>2007</u>
Cash flows from operating activities		
Change in net assets	\$ 3,522,604	\$ 13,651,927
Adjustments to reconcile increase in net assets to net cash provided by operating activities		
Depreciation of property and equipment	3,042,447	3,062,918
Amortization of bond issuance costs	44,411	44,802
Accretion of bond discount	(24,615)	(24,615)
Provision for uncollectible accounts	7,596	(14,423)
Net gain on investments	(1,879,100)	(9,527,794)
Gain on swap	(121,852)	(737,649)
Permanently restricted gifts and donations received	(488,836)	(3,267,917)
Changes in assets and liabilities		
Decrease in actuarial liability for annuities payable	(100,333)	(13,710)
Decrease (increase) in short-term investments	5,160,436	(2,315,968)
Decrease (increase) in accrued interest receivable	(3,031)	17,177
Decrease (increase) in due from students	39,380	(18,170)
Decrease (increase) in accounts receivable	452,189	(478,170)
Net change in pledges receivable	1,528,129	(489,890)
Increase in inventories	(95,910)	(82,113)
Decrease in prepaid expenses	255,755	106,196
(Decrease) increase in accounts payable	(1,666,106)	1,003,237
Increase (decrease) in accrued salaries and wages	254,066	(71,201)
(Decrease) increase in deposits and agency funds	(14,935)	49,130
Increase in post-retirement liability	482,308	2,774,762
(Decrease) in other liabilities	-	(25,334)
Net cash provided by operating activities	<u>10,394,603</u>	<u>3,643,195</u>
Cash flows from investing activities		
Purchases of investments	(22,871,159)	(25,718,899)
Proceeds from sales of investments	25,687,130	25,652,206
Purchase of property and equipment	(10,994,523)	(11,525,064)
Increase in construction fund held in trust	52,199	7,304,940
Loan disbursements to students	(230,400)	(269,043)
Repayments of students loans	<u>236,071</u>	<u>239,870</u>
Net cash used in investing activities	<u>(8,120,682)</u>	<u>(4,315,990)</u>
Cash flows from financing activities		
Payments of long-term debt	(1,263,175)	(1,229,081)
Permanently restricted gifts and donations received	488,836	3,267,917
Increase in advances from federal government for student loans	<u>7,086</u>	<u>8,839</u>
Net cash (used in) provided by financing activities	<u>(767,253)</u>	<u>2,047,675</u>
Net increase in cash and cash equivalents	1,506,668	1,374,880
Cash and cash equivalents		
Beginning of year	<u>1,374,880</u>	<u>-</u>
End of year	<u>\$ 2,881,548</u>	<u>\$ 1,374,880</u>
Interest paid	<u>\$ 2,670,421</u>	<u>\$ 2,847,520</u>

Noncash transactions

The College incurred capitalized construction costs of \$105,132 and \$880,033 which are included as accounts payable at June 30, 2008 and 2007, respectively.

The accompanying notes are an integral part of these statements.

NOTES TO FINANCIAL STATEMENTS

June 30, 2008 and 2007

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. General

Elizabethtown College (the College), founded in 1899, is a comprehensive residential college located in Pennsylvania's historic Lancaster County. More than 45 major programs of study in liberal arts, sciences and professional studies are offered to 1,900 students. Elizabethtown College is a community of learners dedicated to educating students intellectually, socially, aesthetically and ethically for lives of service and leadership as citizens of the world.

2. Basis of Presentation

The financial statements of the College have been prepared in conformity with accounting principles generally accepted in the United States of America. The College presents its financial statements in accordance with the provisions of Statement of Financial Accounting Standards (SFAS) No. 117, *Financial Statements of Not for Profit Organizations*. This statement requires that net assets and revenues, gains, expenses and losses be classified as unrestricted, temporarily restricted or permanently restricted based on the existence or absence of donor-imposed restrictions as follows:

- Unrestricted - Net assets that are not subject to donor-imposed restrictions. Unrestricted net assets may be designated for specific purposes by action of the Board of Trustees, and accordingly include "quasi" endowment investments.
- Temporarily Restricted - Net assets whose use by the College is subject to donor-imposed restrictions that can be fulfilled by actions of the College pursuant to those restrictions or that expire by the passage of time.
- Permanently Restricted - Net assets subject to donor-imposed restrictions that they be maintained permanently by the College. Permanently restricted assets are primarily comprised of original endowment gifts given to the College by donors. Generally, the donors of these assets permit the College to use all or part of the income on these assets.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are generally reported as decreases in unrestricted net assets. Expirations of donor-imposed restrictions that simultaneously increase one class of net assets and decrease another are reported as releases between the applicable classes of net assets.

3. Cash and Cash Equivalents

Cash and cash equivalents represent demand deposits and other investments with purchased maturities of 90 days or less. Each night, the College sweeps all cash into a short-term investment account which is considered cash equivalent to maximize interest earned.

(Continued)

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2008 and 2007

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

4. Short-Term Investments

The College holds funds in certain short-form investment accounts which are used primarily for operating activities at the College. Refer to Note N for further information.

5. Concentrations of Credit Risk

Financial instruments which subject the College to concentrations of credit risk consist primarily of investments in long-term corporate and governmental fixed income instruments, and equity holdings of domestic and foreign corporations. In addition, the College typically maintains cash and cash equivalents and short-term investments in local banks which may, at times, exceed the FDIC limits.

The College's operations are located in Elizabethtown, Pennsylvania and its students come primarily from Pennsylvania and surrounding states. The College's major source of revenue is from tuition, and room and board fees.

6. Student Accounts and Loans Receivable

Student accounts and loans receivable are reported net of allowance for doubtful loans. The allowance for doubtful loans was \$70,577 and \$77,829 at June 30, 2008 and 2007, respectively. The allowance is intended to provide for loans, both in repayment status and not yet in repayment status (borrowers still in school or in the grace period following graduation), that may not be collected.

A reasonable estimate of fair value of student loans receivable under government loan programs is not made because the notes are not transferable to outside parties and can only be assigned to the U.S. Government or its designees.

7. Pledges Receivable

Pledges receivable are reported net of allowance for doubtful accounts. The allowance for doubtful accounts was \$334,598 and \$400,000 at June 30, 2008 and 2007, respectively. The provision is intended to provide for pledges receivable that may not be collected.

8. Allowance for Doubtful Accounts

The allowance for doubtful accounts is provided based upon management's judgments including such factors as prior collection history and type of receivables. The College writes-off receivables when they become uncollectible, and payments subsequently received on such receivables are credited to the allowance for doubtful accounts.

(Continued)

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2008 and 2007

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

9. Construction Fund Held in Trust

Construction fund held in trust under bond indenture agreements represents funds held by the designated trustee for payment of construction costs and maintenance of debt service reserve funds.

10. Inventories

Inventories consist of items for the College Store and Dining Services, and are valued at the lower of cost or market. Cost is determined by the first-in, first-out method.

11. Investments

The College records investments at fair value. Debt securities, equity securities and mutual funds are valued at quoted market prices. Mortgage investments and cash surrender values of life insurance policies, are carried at the stated value which approximates the market value of these assets. Alternative investments are recorded at the estimated fair value established by the fund managers and reviewed by the investment consultant. Alternative investments consist of private equity securities, real estate investment, mortgages and hedge funds. Because such investments are not readily marketable, their estimated value is subject to uncertainty, and, therefore, may differ from the value that would have been used had a ready market for such investments existed. The College reviews and evaluates the values provided by the outside parties and agrees with the valuation methods and assumptions used in determining the fair value of alternative investments.

Gains and losses on investments are determined using an average cost method for securities and the specific identification method for other investments. Gains and losses are based on the trade date for investments.

In 2003, the College established a target annual distribution from the endowment of 4% of the trailing 12 quarters' average market value, which included a multi-year plan to migrate from a previous annual distribution of 6%. The percentage expended for the years ended June 30, 2008 and 2007 was 3.69% and 4.16%, respectively. In addition, the Commonwealth of Pennsylvania law permits organizations to allocate to income each year a portion of permanently restricted investment net gains under a total return spending rate policy, not to exceed 7% of the average market value of the assets for the preceding three years. The College has authorized a draw down of 7% in both fiscal 2008 and 2007. To the extent that actual income from these permanently restricted investments is less than the predetermined amount, accumulated gains are made available for operations to fund the difference. For financial statement purposes, any excess of accumulated gains or accumulated losses are recorded as temporarily restricted net assets. Investment return in excess of or less than the spending distribution is reported as a component of temporarily restricted investment income.

(Continued)

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2008 and 2007

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

12. Funds Held in Trust

The College is the recipient/beneficiary of several irrevocable trust arrangements which are held by others. The related income from these arrangements is recognized as either temporarily restricted or unrestricted revenue by the College when received, depending on whether the donor-imposed restrictions exist. The recorded value of the stream of future revenue associated with these trusts is required to be measured using the present value of future cash receipts. The market value of the pro rata ownership portion of the trusts' assets is used as an approximation of the present value of the future receipts and is included in investments.

13. Property, Plant and Equipment

Property, plant and equipment is recorded at cost as of the date of acquisition or fair value as of the date of receipt in the case of gifts. Depreciation is computed on a straight-line basis over the estimated useful lives of land improvements (20 years), buildings (20-87 years) and equipment (3-15 years).

The cost and accumulated depreciation of property sold or retired is removed from the related asset and accumulated depreciation amounts and any resulting gain or loss is recorded in the period of disposal.

Renewals and improvements which extend the useful lives of assets are capitalized at cost. Library books are expensed when purchased. Maintenance and repairs are included as expenses in the statements of activities.

14. Other Assets

Other assets consist of costs associated with debt issuance. All deferred costs associated with issued debt are being amortized over the term of respective debt.

15. Deposits and Agency Funds

Deposits relate primarily to summer and fall session tuition and matriculation and breakage deposits received prior to June 30. Agency funds consist of assets held for others, primarily student organizations.

16. Net Student Tuition and Fees

Net student tuition revenue is reported at the net realizable amounts received from students. Net tuition and fees is reported net of institutional student aid, contributions, and investment income restricted for student aid and certain federal grants restricted for student aid.

17. Private Gifts and Grants

The College distinguishes between contributions received for each net asset category in accordance with donor-imposed restrictions. Under SFAS No. 116, *Accounting for Contributions Received and Contributions Made*, donor-restricted contributions are reported as unrestricted operating revenue when the restriction is satisfied within the same year that the contribution is received.

(Continued)

NOTES TO FINANCIAL STATEMENTS - CONTINUED

June 30, 2008 and 2007

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

18. Advertising Costs

The College follows the policy of expensing advertising and marketing costs when incurred. For the years ended June 30, 2008 and 2007, advertising related costs amounted to \$395,757 and \$392,117, respectively

19. Fundraising Expenses

The College follows the policy of expensing the costs of fundraising when incurred. For the years ended June 30, 2008 and 2007, fundraising costs amounted to \$1,482,985 and \$1,388,079, respectively.

20. Fair Value of Financial Instruments

Estimated fair values of financial instruments that differ from the carrying amount have been determined by the College using available market information. The estimates are not necessarily indicative of the amounts the College could realize in a current market exchange.

The carrying amount of cash and cash equivalents, accounts receivable, accounts payable, and accrued expenses approximates fair value because of the short maturity of these financial instruments.

It is not practical to estimate the fair value of student loans receivable since they contain federally-mandated interest rates and repayment terms subject to significant restrictions as to their transfer and disposition.

The fair values of investments in debt and equity securities are based upon values provided by the external investment managers or quoted market prices. The fair value of long-term debt is based on current market rates for loans with similar maturities and credit quality. At June 30, 2008 and 2007, the fair value of the College's long-term debt was approximately \$42,893,000 and \$46,875,000, respectively.

21. Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The most significant management estimates and assumptions relate to the determination of allowances for doubtful student accounts, pledges and other receivables, alternative investment values, useful lives of fixed assets, assumptions related to the post-retirement liability and the reported fair values of certain of the College's assets and liabilities. Actual results could differ from those estimates.

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