

Worcester Polytechnic Institute

**Consolidated Financial Statements
June 30, 2008 and 2007**

Worcester Polytechnic Institute
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June 30, 2008 and 2007

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Report of Independent Auditors

To the Board of Trustees of
Worcester Polytechnic Institute

In our opinion, the accompanying consolidated statements of financial position and the related consolidated statements of activities and of cash flows present fairly, in all material respects, the financial position of Worcester Polytechnic Institute (the "University") at 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. 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 of these statements 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

September 19, 2008

Worcester Polytechnic Institute
Consolidated Statements of Financial Position
June 30, 2008 and 2007 (in thousands)

	2008	2007
Assets		
Cash and cash equivalents	\$ 11,065	\$ 7,441
Accounts receivable, net	6,297	3,827
Contributions receivable, net	11,315	3,943
Funds held under bond agreements	8,668	43,045
Prepaid expenses and other assets	4,551	5,717
Interest rate agreements	-	596
Student loans receivable, net	21,168	20,565
Beneficial interest in trusts	17,154	16,743
Investments	404,387	427,303
Land, buildings and equipment, net	176,797	145,426
Total assets	<u>\$ 661,402</u>	<u>\$ 674,606</u>
Liabilities		
Accounts payable and accrued liabilities	\$ 18,808	\$ 19,204
Deposits and deferred revenue	7,318	7,214
Split-interest agreements	11,193	12,558
Funds held for others	4,040	3,418
Asset retirement obligations	4,661	3,019
Refundable government loan funds	6,792	6,792
Bonds and notes payable	143,987	145,403
Interest rate agreements	4,021	997
Total liabilities	<u>200,820</u>	<u>198,605</u>
Net assets		
Unrestricted	234,037	252,731
Temporarily restricted	117,869	122,148
Permanently restricted	108,676	101,122
Total net assets	<u>460,582</u>	<u>476,001</u>
Total liabilities and net assets	<u>\$ 661,402</u>	<u>\$ 674,606</u>

The accompanying notes are an integral part of these consolidated financial statements.

Worcester Polytechnic Institute
Consolidated Statement of Activities
Year Ended June 30, 2008 (in thousands)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Operating revenues				
Tuition and fees	\$ 114,576	\$ -	\$ -	\$ 114,576
Less Unrestricted student aid	32,739	-	-	32,739
Endowed scholarships	5,005	-	-	5,005
Externally funded student aid	4,098	-	-	4,098
Total student aid	41,842	-	-	41,842
Net tuition and fees	72,734	-	-	72,734
Other educational activities	7,926	-	-	7,926
Contributions	3,754	475	-	4,229
Contract and exchange transactions	20,324	-	-	20,324
Investment income on endowment	4,711	36	83	4,830
Net realized gains on endowment used for operations	6,117	5,377	-	11,494
Other investment income	3,836	82	58	3,976
Sales and services of auxiliary enterprises	14,113	-	-	14,113
Other	1,006	-	-	1,006
Total revenues	134,521	5,970	141	140,632
Net assets released from restriction	5,963	(5,963)	-	-
Total revenues and other support	140,484	7	141	140,632
Operating expenses				
Instruction and department research	49,668	-	-	49,668
Sponsored research and other sponsored programs	12,634	-	-	12,634
External relations	6,314	-	-	6,314
Institution and academic support	30,424	-	-	30,424
Student services	8,236	-	-	8,236
Operation and maintenance of plant	23,451	-	-	23,451
Auxiliary enterprises	7,549	-	-	7,549
Increase in asset retirement cost	1,433	-	-	1,433
Total operating expenses	139,709	-	-	139,709
Change in net assets from operating activities	775	7	141	923
Nonoperating				
Net realized and unrealized gains (losses) on investments	(7,142)	(6,564)	(99)	(13,805)
Net realized gains on endowment used for operations	(6,117)	(5,377)	-	(11,494)
Change in value of split interest agreements	(821)	626	12	(183)
Contributions	-	7,029	7,500	14,529
Net realized and unrealized losses on interest rate agreements	(4,180)	-	-	(4,180)
Loss on extinguishment of debt	(1,209)	-	-	(1,209)
Change in net assets from nonoperating activities	(19,469)	(4,286)	7,413	(16,342)
Total change in net assets	(18,694)	(4,279)	7,554	(15,419)
Net assets, beginning of year	252,731	122,148	101,122	476,001
Net assets, end of year	\$ 234,037	\$ 117,869	\$ 108,676	\$ 460,582

The accompanying notes are an integral part of these consolidated financial statements.

Worcester Polytechnic Institute
Consolidated Statement of Activities
Year Ended June 30, 2007 (in thousands)

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Operating revenues				
Tuition and fees	\$ 103,716	\$ -	\$ -	\$ 103,716
Less Unrestricted student aid	30,405	-	-	30,405
Endowed scholarships	4,465	-	-	4,465
Externally funded student aid	4,051	-	-	4,051
Total student aid	38,921	-	-	38,921
Net tuition and fees	64,795	-	-	64,795
Other educational activities	7,290	-	-	7,290
Contributions	4,369	1,451	-	5,820
Contract and exchange transactions	18,837	-	-	18,837
Investment income on endowment	1,771	8	80	1,859
Net realized gains on endowment used for operations	7,254	6,299	-	13,553
Other investment income	2,144	1,693	52	3,889
Sales and services of auxiliary enterprises	12,952	-	-	12,952
Other	1,365	-	-	1,365
Total revenues	120,777	9,451	132	130,360
Net assets released from restriction	10,333	(10,333)	-	-
Total revenues and other support	131,110	(882)	132	130,360
Operating expenses				
Instruction and department research	48,571	-	-	48,571
Sponsored research and other sponsored programs	12,346	-	-	12,346
External relations	5,906	-	-	5,906
Institution and academic support	26,190	-	-	26,190
Student services	8,122	-	-	8,122
Operation and maintenance of plant	20,461	-	-	20,461
Auxiliary enterprises	7,583	-	-	7,583
Total operating expenses	129,179	-	-	129,179
Change in net assets from operating activities	1,931	(882)	132	1,181
Nonoperating				
Net realized and unrealized gains (losses) on investments	32,713	27,521	(127)	60,107
Net realized gains on endowment used for operations	(7,254)	(6,299)	-	(13,553)
Change in value of split interest agreements	329	(836)	54	(453)
Contributions	1,176	1,133	8,403	10,712
Reclassification of net assets related to split interest agreements	-	1,181	(1,181)	-
Net realized and unrealized losses on interest rate agreements	(476)	-	-	(476)
Loss on extinguishment of debt	(1,877)	-	-	(1,877)
Change in net assets from nonoperating activities	24,611	22,700	7,149	54,460
Total change in net assets	26,542	21,818	7,281	55,641
Net assets, beginning of year	226,189	100,330	93,841	420,360
Net assets, end of year	\$ 252,731	\$ 122,148	\$ 101,122	\$ 476,001

The accompanying notes are an integral part of these consolidated financial statements.

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Consolidated Statements of Cash Flows
Years Ended June 30, 2008 and 2007 (in thousands)

	2008	2007
Cash flows from operating activities		
Change in net assets	\$ (15,419)	\$ 55,641
Adjustments to reconcile change in net assets to net cash used in operating activities		
Depreciation, amortization, and accretion	11,949	10,566
Provision for uncollectible receivables	1,675	90
Net realized and unrealized losses (gains) on investments	13,805	(61,951)
Net unrealized loss on interest rate agreements	3,620	366
Increase in asset retirement cost	1,433	-
Loss on extinguishment of debt	1,209	1,877
Contributions other than cash	(904)	(6,477)
Contributions restricted for long-term investment	(6,716)	(650)
Changes in assets and liabilities:		
Accounts receivable	(2,470)	1,935
Contributions receivable	(9,047)	(1,290)
Prepaid expenses and other assets	310	(1,400)
Accounts payable and accrued liabilities	2,440	545
Deposits and deferred revenue	229	725
Asset retirement obligations	(96)	97
Split-interest agreements	(1,506)	(1,174)
Funds held for others	622	335
Total adjustments	16,553	(56,406)
Net cash provided by (used in) operating activities	1,134	(765)
Cash flows from investing activities		
Proceeds from sales and maturities of investments	63,620	86,355
Purchase of investments	(53,875)	(74,934)
Purchase of land, building, and equipment	(45,871)	(35,260)
Proceeds from bonds deposited with trustees	-	(39,094)
Use of funds held under bond agreements	34,377	24,878
Disbursement of loans to students	(3,709)	(3,735)
Repayment of loans from students	3,106	3,198
Net cash used in investing activities	(2,352)	(38,592)
Cash flows from financing activities		
Contributions restricted for long-term investment	6,716	650
Deferred financing costs	(377)	(1,690)
Proceeds from long-term debt and rate lock agreement	54,815	86,922
Repayment of long-term debt	(56,312)	(46,835)
Net cash provided by financing activities	4,842	39,047
Net change in cash and cash equivalents	3,624	(310)
Cash and cash equivalent at beginning of year	7,441	7,751
Cash and cash equivalents at end of year	\$ 11,065	\$ 7,441
Supplemental disclosures of cash flow information		
Interest paid	\$ 5,932	\$ 3,928
Gifts-in-kind	\$ 201	\$ 1,106
Purchases of buildings and equipment included in accounts payable	\$ 6,157	\$ 8,993

The accompanying notes are an integral part of these consolidated financial statements.

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Notes to Consolidated Financial Statements

June 30, 2008 and 2007

1. Organization

Worcester Polytechnic Institute (the "University"), founded in 1865, is the nation's third oldest private engineering university. Approximately 3,800 undergraduate and graduate students attend the University annually. The University is located in Worcester, Massachusetts and serves a diverse student body from almost every state and over 60 foreign countries.

2. Summary of Significant Accounting Policies

Basis of Financial Statement Presentation

The accompanying consolidated financial statements are prepared on the accrual basis of accounting with the net assets and revenues, expenses, gains and losses classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the University and changes therein are classified and reported as follows:

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 related investments for general or specific purposes.

Temporarily Restricted

Net assets whose use is restricted by state law or subject to donor-imposed stipulations that can be fulfilled by actions of the University pursuant to these stipulations or that expire by the passage of time.

Unrestricted

Net assets not subject to explicit 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.

Consolidation

The accompanying consolidated financial statements include the accounts of the University and its wholly owned or controlled subsidiaries. Intercompany accounts and transactions have been eliminated.

Related entities for which the University does not have a majority ownership or controlling financial interest have been accounted for under the equity method. Under this method, investments are recorded based upon the University's original contribution and adjusted for the University's proportionate share of undistributed earnings and losses.

Classifications

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions or by law. 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 or by law. Expirations of temporary restrictions on net assets (that is, the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as net assets released from restrictions between the applicable classes of net assets.

Operating and Nonoperating Activities

In the consolidated statements of activities, the University has defined its primary activities between operating and nonoperating. Operating activities consist primarily of activities supporting the educational mission and purpose of the University. Nonoperating activities consist primarily of unspent

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Notes to Consolidated Financial Statements

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appreciation on endowment, change in value of split-interest agreements, net contributions for endowment and capital use, gains or losses on interest rate swap agreements, and realized losses on extinguishment of debt.

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 University's significant estimates include the valuation of its investments as well as the estimated net realizable value of receivables for contributions, gifts, pledges, student loans, accounts and other receivables, the estimated useful lives of buildings and equipment, and its liabilities for its asset retirement obligations and its split-interest agreements. Actual results could differ from those estimates.

Financial Instruments

The University has estimated, where practicable, the fair values of its financial instruments by using valuation methodologies. Except where otherwise noted, the University has determined that the differences between the carrying values and the estimated fair values of its other financial instruments are not material.

Cash and Cash Equivalents

For the purposes of reporting cash flows, the University considers all short-term highly liquid investments to be cash equivalents. Cash equivalents consist of time deposits and short-term investments with maturities at the date of purchase of ninety days or less, stated at cost, which approximates fair value. Certain balances meeting the definition of cash and cash equivalents have been classified as investments as a result of the University's intent to segregate funds from cash available for current operations.

Most of the University's banking activity, including cash and cash equivalents, is maintained with regional banks and from time to time exceeds federal insurance limits. It is the University's policy to monitor these banks' financial strength on an ongoing basis.

Contributions

Contributions, including unconditional promises to give, are recognized as revenues in the period received. Contributions subject to donor-imposed stipulations that are met in the same reporting period are reported as unrestricted support. Promises to give that are scheduled to be received after the fiscal year-end are shown as increases in temporarily restricted net assets and are reclassified to unrestricted net assets when the purpose or time restrictions are met. Promises to give subject to donor-imposed stipulations that the corpus be maintained permanently are recognized as increases in permanently restricted net assets. 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 that are expected to be collected after one year are recorded at the present value of estimated future cash flows. The discounts on these amounts are computed using risk-free rates applicable to the year in which the promises are received. The discount rates used range from approximately 3% to 8%. Amortization of the discount is recorded as additional contribution revenue in the applicable net asset class.

The carrying amount of contributions receivable approximates fair value as such amounts are recorded net of an allowance for uncollectibles and a discount to their present value. The allowance for uncollectible contributions receivable is based upon management's judgment including such factors as prior collection history, type of contribution and nature of fundraising activity.

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Notes to Consolidated Financial Statements

June 30, 2008 and 2007

The University reports contributions of land, buildings, or equipment as unrestricted support unless the donor places restrictions on their use. Contributions of cash or other assets that must be used to acquire long-lived assets are reported as unrestricted support provided the long-lived assets are placed in service in the same reporting period, otherwise, the contributions are reported as temporarily restricted support until the assets are acquired and placed in service and then, such amounts are reclassified to unrestricted net assets.

Deferred Financing Costs

Included in prepaid expenses and other assets are deferred financing costs that are being amortized over the life of the related bonds.

For the years ended June 30, 2008 and 2007, deferred financing costs, net totaled approximately \$2,047,000 and \$3,261,000, respectively. Amortization expense for the years ended June 30, 2008 and 2007 was approximately \$82,000 and \$119,000, respectively. During 2008, approximately \$1,567,000 of such costs were written off in connection with the extinguishment of certain of the University's debt. The aggregate estimated amortization expense for deferred financing costs for each of the next five years is approximately \$66,000.

Investments

Investments are reported at fair value and are comprised of the assets of the University's endowment and similar funds. Endowment funds are subject to the restrictions of gift instruments requiring that the principal be invested in perpetuity and that only income be utilized. Funds functioning as endowment, also known as quasi-endowment funds, have been established by the Trustees for the same purposes as endowment funds. However, any portion of the funds functioning as endowment may be expended with the approval of the trustees.

Assets of endowment funds are pooled on a market value basis with each individual fund subscribing to or disposing of units on the basis of the market value per unit at the beginning of the quarterly period within which the transactions take place. In addition, the University maintains separately invested funds as stipulated by donors. Endowment income is distributed based on the number of units subscribed to at the end of each month.

Land, Buildings and Equipment

Land, buildings and equipment are recorded at cost at the date of acquisition or, if received as a gift, at the estimated fair value at the date of the gift. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is recorded. Expenditures for repairs and maintenance are charged to expense as incurred. Library books are expensed as incurred due to its short-term life and low cost per volume.

Depreciation expense is computed on a straight-line basis over the estimated useful lives using a half-year convention beginning in the year of acquisition or capitalization of construction in progress. Estimated useful lives are periodically reviewed and, when appropriate, changes are made prospectively. When certain events or changes in operating conditions occur, asset lives may be adjusted and an impairment assessment may be performed on the recoverability of the carrying amounts.

Useful lives of the assets are as follows:

Land improvement	10 to 20 years
Building and improvements	20 to 40 years
Equipment	3 to 10 years

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Split-Interest Agreements

The University is a recipient of funds under perpetual trust and irrevocable split-interest agreements, the income on which may be restricted by the donor. Amounts held by third-party trustees in perpetuity for the benefit of the University are reported at their fair value. Under the terms of these agreements, the University has the irrevocable right to its share of the income earned on the trust assets. Amounts received under split-interest agreements, including charitable gift annuities, charitable lead trusts, charitable remainder trusts, and pooled income arrangements, may be invested by the University or third-party trustees, and at the end of each agreement's term are distributed either to the University or other beneficiaries. Annual distributions to beneficiaries may be for a specified dollar amount or percentage of the trust's fair value. Upon receipt, gifts requiring the University or trustee to pay donors a specified periodic amount are recorded at fair value with corresponding estimated liabilities for future amounts payable to other beneficiaries, where applicable. The liabilities associated with these gifts are adjusted during the term of these gift instruments. The University is aware of certain split-interest arrangements in which it has been named as beneficiary and has adopted a policy that until such amounts are estimable and probable, such amounts are not recognized in the financial statements.

The present value of payments to beneficiaries under split-interest arrangements is calculated using discount rates in effect at the date of the gift; these rates range from approximately 2.9% to 11.6%.

Asset Retirement Obligations

An asset retirement obligation ("ARO") is a legal obligation associated with the retirement of long-lived assets. These liabilities are initially recorded at fair value and the related asset retirement costs are capitalized by increasing the carrying amount of the related assets by the same amount as the liability. Asset retirement costs are subsequently depreciated over the useful lives of the related assets. Subsequent to initial recognition, the University records period-to-period changes in the ARO liability resulting from the passage of time and revisions to either the timing or the amount of the original estimate of undiscounted cash flows. The University derecognizes ARO liabilities when the related obligations are settled.

Tax-Exempt Status

The University is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code.

Sponsored Research

Revenues associated with research and other contracts and grants at the University are recognized as related costs are incurred. Indirect cost recovery by the University is based on a predetermined rate.

Reclassification

Certain prior year amounts have been reclassified to conform to the current year presentation.

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Notes to Consolidated Financial Statements
June 30, 2008 and 2007

3. Accounts Receivable

Accounts receivable consist of the following at June 30, 2008 and 2007 (in thousands):

	2008	2007
Sponsored research	\$ 3,245	\$ 2,471
Student receivables	2,252	1,113
Other receivables	1,041	540
	<u>6,538</u>	<u>4,124</u>
Less: Allowance for doubtful accounts	(241)	(297)
	<u>\$ 6,297</u>	<u>\$ 3,827</u>

4. Contributions Receivable

Unconditional promises are expected to be realized in the following periods at June 30, 2008 and 2007 (in thousands):

	2008	2007
In one year or less	\$ 3,208	\$ 2,054
Between one and five years	9,460	1,579
Greater than five years	627	3,110
	<u>13,295</u>	<u>6,743</u>
Less:		
Discount to present value	(1,335)	(139)
Allowance for doubtful contributions	(645)	(2,661)
	<u>\$ 11,315</u>	<u>\$ 3,943</u>

In addition, as of June 30, 2008 and 2007, the University has approximately \$2,883,000 and \$293,000, respectively, of cumulative conditional promises to give that are not recognized as assets in the accompanying consolidated statement of financial position.

5. Student Loans Receivable

Student loans receivable consist of the following at June 30, 2008 and 2007 (in thousands):

	2008	2007
Student loans	\$ 21,484	\$ 20,878
Other	194	213
	<u>21,678</u>	<u>21,091</u>
Less: Allowance for doubtful accounts	(510)	(526)
	<u>\$ 21,168</u>	<u>\$ 20,565</u>

Student loans receivable include amounts due from students under federally sponsored loan programs that are subject to significant restrictions.

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6. Investments

Investments at June 30, 2008 were as follows (comparative totals are included for 2007) (in thousands):

	2008			2007 Total
	Endowment	Split-Interest Agreements	Total	
Cash and cash equivalents	\$ 12,398	\$ 1,014	\$ 13,412	\$ 2,573
Equity securities	153,766	10,941	164,707	189,066
Fixed income securities	48,223	7,679	55,902	53,039
Commodities	10,385	-	10,385	6,611
Hedge fund and alternative investments				
Equity funds	78,148	-	78,148	103,843
Fixed income funds	27,681	-	27,681	24,251
Private equities	33,953	-	33,953	29,091
Real estate	20,199	-	20,199	18,829
Total investments	\$ 384,753	\$ 19,634	\$ 404,387	\$ 427,303
Beneficial interest in trusts	\$ -	\$ 17,154	\$ 17,154	\$ 16,743

Fair values for equity securities and fixed income securities are generally based on published market values. The University invests in hedge funds, private equity, and real estate investments through various limited partnerships and similar vehicles. Hedge funds utilize a variety of investment strategies incorporating marketable securities and, in some cases, derivative instruments, all of which are reported at estimated fair value by the fund managers. Private equity consists of long-term private investments and has been valued based on estimates provided by the general partners of the investment vehicles. Estimates of fair value may differ significantly from values that would have been used had a ready market for the investments existed. Real estate consists mainly of direct real estate holdings and investments in privately held entities and has been valued at management's estimates of fair value. At June 30, 2008 and 2007, respectively, approximately \$17,210,000 and \$17,092,000 of such investments do not have readily determinable fair values and have been valued at management's estimate of fair value.

In July 2007, a hedge fund investment partnership of which the University was a limited partner came under significant pressure resulting from tightening credit spreads and margin requirements, and had to sell, at a significant discount, substantially all of its assets to another hedge fund. Based on information provided by the general partner of the investment, the partnership incurred a loss of approximately 56% of its value in this transaction. The partnership is distributing the remaining net asset value to its investors. For the year ended June 30, 2008, the University recorded a decline in the valuation of its investment in this partnership of approximately \$5,891,000.

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The investment return in the consolidated statements of activities for the year ended June 30, 2008 with comparative totals for 2007 is summarized as follows (in thousands):

	2008			Total	2007 Total
	Unrestricted	Temporarily Restricted	Permanently Restricted		
Investment income on endowment	\$ 4,711	\$ 36	\$ 83	\$ 4,830	\$ 1,859
Net realized and unrealized gains (losses) on investments	(7,142)	(6,564)	(99)	(13,805)	60,107
Return on endowment	(2,431)	(6,528)	(16)	(8,975)	61,966
Other investment income	3,836	82	58	3,976	3,889
Total return on investments	1,405	(6,446)	42	(4,999)	65,855
Investment return designated for current unrestricted operations	14,664	5,495	141	20,300	19,301
Investment return (utilized) reinvested	\$ (13,259)	\$ (11,941)	\$ (99)	\$ (25,299)	\$ 46,554

Investment income is net of investment management expenses of approximately \$1,059,000 and \$1,207,000 for the years ended June 30, 2008 and 2007, respectively.

To the extent that accumulated realized and unrealized losses are in excess of accumulated gains for certain endowment funds, they are reported as decreases in unrestricted net assets. As a result of market declines, the fair value of certain donor-restricted endowments is less than the historical cost value of such funds by approximately \$391,000 and \$52,000 at June 30, 2008 and 2007, respectively. These unrealized losses have been recorded as reductions in unrestricted net assets. Future market gains will be used to restore this deficiency in unrestricted net assets before any net appreciation above the historical cost value of such funds increases temporarily restricted net assets.

Endowment Income and Spending

The University observes a spending rule with respect to total return (interest, dividends and appreciation) on investments of the endowment. The spending rule distributions for fiscal years 2008 and 2007, respectively, were \$0.312 and \$0.300 per time weighted unit, comprised of \$0.115 and \$0.035 of income and \$0.197 and \$0.265 of distributions from current and accumulated realized gains. At June 30, 2008 there was a total of 59,014,330 units in the pooled endowment fund, each having a fair value of \$6.479. Of the total units, 27,747,310 were owned by endowment funds and 31,267,020 were owned by internally designated funds.

A summary of the fair value per unit and the income per time-weighted unit for the pooled investments held as of June 30, 2008 and in each of the prior four years is as follows:

	Income Per Time Weighted Unit	Fair Value Per Unit
2008	\$ 0.115	\$ 6.479
2007	0.035	6.876
2006	0.072	6.104
2005	0.039	5.720
2004	0.052	5.562

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Split-Interest Agreements

Investments include the following split-interest agreements at June 30, 2008 and 2007 (in thousands):

	2008	2007
Charitable gift annuities	\$ 8,201	\$ 8,775
Charitable remainder trusts	8,669	10,166
Pooled income funds	2,764	2,709
	<u>\$ 19,634</u>	<u>\$ 21,650</u>

7. Land, Buildings and Equipment

Land, buildings and equipment consist of the following at June 30, 2008 and 2007 (in thousands):

	2008	2007
Land and land improvements	\$ 12,391	\$ 9,553
Buildings	202,669	200,250
Equipment	27,344	22,336
	<u>242,404</u>	<u>232,139</u>
Less: Accumulated depreciation	<u>(108,647)</u>	<u>(98,969)</u>
	133,757	133,170
Construction-in-progress	43,040	12,256
	<u>\$ 176,797</u>	<u>\$ 145,426</u>

Depreciation expense charged to operations was approximately \$11,521,000 and \$10,447,000 for the years ended June 30, 2008 and 2007, respectively. Net interest cost capitalized was approximately \$951,000 and \$732,000 for the years ended June 30, 2008 and 2007, respectively.

For the year ended June 30, 2008, the University recorded a change in its estimate of asset retirement costs which resulted in a loss of approximately \$1,433,000.

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8. Bonds and Notes Payable

Bonds and notes payable consist of the following (in thousands):

Purpose and Definition	Maturity Date	Interest Rate %	Original Issue	Amount Due Within One Year	Balance, June 30, 2008	Balance, June 30, 2007
Bonds payable						
Housing and Urban Development 1969 Series C (1)	4/1/2019	3.0	\$ 1,160	\$ 35	\$ 422	\$ 452
Massachusetts Health and Educational Facilities Authority 2005 Series M-3B (2)	7/31/2010	Variable	8,000	1,423	2,817	4,144
Massachusetts Development Finance Agency 2003 Series A (3)	10/3/2033	Variable	15,000	-	-	14,619
Massachusetts Development Finance Agency 2005 Series A & B (4)	9/1/2035	Variable	39,975	-	-	39,975
Massachusetts Development Finance Agency 2007 Series (5)	9/1/2047	4.0-5.0	81,915	100	84,058	84,113
Massachusetts Development Finance Agency 2008 Series A & B (6)	9/1/2035	Variable	54,815	360	54,815	-
Uncollateralized notes						
Sovereign Bank	4/25/2010	7.0	4,500	225	1,875	2,100
Total bonds and notes payable				<u>\$ 2,143</u>	<u>\$ 143,987</u>	<u>\$ 145,403</u>

- (1) Collateralized by land, building and equipment known as Stoddard Residence Center and pledged net revenues from the operations of the dormitory.
- (2) The bonds, issued at par with no discount or premium, represent a general obligation of the University.
- (3) The bonds represented a general obligation of the University. The balance at June 30, 2007 was net of discounts of \$81,000. The obligation was paid in April 2008.
- (4) The bonds, issued at par with no discount or premium, represented a general obligation of the University. The obligation was paid in April 2008.
- (5) The bonds represent a general obligation of the University. The balances at June 30, 2008 and 2007 include a premium of \$2,143,000 and \$2,198,000, respectively.
- (6) The bonds, issued at par with no discount or premium, represent a general obligation of the University.

In compliance with the University's various bond indentures, funds held under bond agreements at June 30, 2008 and 2007 include investments of approximately \$8,668,000 and \$43,045,000, respectively, held for construction and debt service reserves.

The fair value of the University's debt has been calculated by determining the net present value of future cash outlays using an appropriate interest rate based on the length of time to maturity. The rates were based upon market conditions as of June 30, 2008 and 2007. The estimated fair value at June 30, 2008 and 2007, is approximately \$141,344,000 and \$147,700,000, respectively.

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Scheduled aggregate principal repayments on bonds and notes payable for each of the next five fiscal years and thereafter are as follows (in thousands):

2009	\$	2,143
2010		3,520
2011		2,050
2012		2,220
2013		2,255
Thereafter		<u>129,656</u>
Total cash payments	\$	141,844
Premium		<u>2,143</u>
	\$	<u>143,987</u>

In April 2008, the University borrowed \$54,815,000 in the form of Massachusetts Development Finance Agency (“MDFA”) Variable Rate Demand Revenue Bonds Series 2008A (tax-exempt) and 2008B (federally taxable), (the “2008 Bonds”). The proceeds from the issues were used to refund the University’s borrowings under the MDFA Revenue Bonds, Series 2005A (tax-exempt) and 2005B (federally taxable) Select Auction Variable Rate Securities (the “2005 Bonds”), and the MDFA, Revenue Bonds, Series 2003A Select Auction Variable Rate Securities (the “2003 Bonds”), and to pay the costs of issuance. The refunding resulted in a loss relating to the unamortized debt issuance costs of the 2005 and 2003 Bonds amounting to approximately \$1,209,000 that has been included in the accompanying consolidated statement of activities for the year ended June 30, 2008. The 2008 Bonds are payable in semiannual installments with principal payments ranging from \$360,000 to \$2,915,000, with a final maturity of September 1, 2035. Payment of the principal of, the purchase price of, and interest on each series of the 2008 Bonds, when due, is collateralized by an irrevocable direct pay letter of credit by TD Banknorth, N.A. (the “Letter of Credit”) that expires in 2013. As more fully described in Note 9, the interest rate swap agreements entered into as integral parts of the 2005 and 2003 Bonds remain in effect to economically hedge the interest rate risks associated with the 2008 Bonds.

The Letter of Credit includes financial covenants that require that the University maintain minimum expendable net assets to debt of at least 0.65 and a minimum long term credit rating of A3/A-.

In June 2007, the University borrowed \$81,915,000 in the form of MDFA Revenue Bonds, Worcester Polytechnic Institute, Series 2007. The proceeds from the issue were used, in part, to refund the University’s borrowings under the Massachusetts Industrial Finance Agency Revenue Bonds, Series 1997 I and II (the 1997 series bonds) and to pay the costs of issuance and the bond insurance premium; the remaining portion to be used to construct a residence facility and adjacent parking structure on the University’s campus. A portion of the proceeds was deposited in refunding trusts to refund, on a current basis on September 1, 2007, the outstanding 1997 series bonds, in the outstanding principal amounts of \$19,490,000 and \$22,100,000, respectively. As a result, the 1997 series bonds were defeased and are not reflected in the accompanying consolidated financial statements. The refunding resulted in a difference in the amount of approximately \$1,877,000 between the redemption price of the 1997 series bonds and its carrying value, including its unamortized debt issuance costs of approximately \$738,000, that has been recorded as a loss in the accompanying consolidated statement of activities for the year ended June 30, 2007. The Series 2007 Bonds are fixed rate bonds payable in semiannual installments with principal payments ranging from \$100,000 to \$3,105,000, and interest ranging from 4.0% to 5.0%. The final maturity is September 1, 2047.

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In anticipation of the delivery of the Series 2007 series bonds, the University entered into an actual rate rate-lock contract (the Contract) on March 8, 2007. The overall effect of the Contract was to lock in the true interest cost of the 2007 series bonds and the amount of the net bond proceeds on the basis of the market interest rates on such date. The Contract was terminated and the University received a cash payment in June 2007 resulting in a realized gain of approximately \$2,809,000. The University has recorded the amount as a deferred gain in deposits and deferred revenue as of June 30, 2007 and is amortizing the gain over the life of the 2007 series bonds.

The University also has a \$25,000,000 bank revolving line of credit. The line of credit bears interest at LIBOR plus 0.15% per annum for the first \$15,000,000 and LIBOR plus 0.30% per annum for amounts outstanding in excess of \$15,000,000. There were no amounts outstanding at June 30, 2008 and 2007.

9. Interest Rate Agreements

The University has entered into several interest rate swap agreements used to economically hedge the interest rate risk associated with certain of its variable rate debt. The following summarizes the terms for each of these agreements (in thousands):

	Series 2003A (2008A&B)	Series 2005A (2008A&B)	Series 2005B (2008A&B)	Sovereign Bank	
	Interest Rate	Interest Rate	Interest Rate	Interest Rate	
	Swap	Swap	Swap	Swap	
Trade date	Aug. 12, 2003	Jun. 13, 2005	Jun. 13, 2005	May 4, 2005	
Effective date	Oct. 1, 2006	Aug. 3, 2005	Aug. 3, 2005	May 4, 2005	
Initial notional amount	\$15,000	\$34,200	\$5,775	\$2,587	
Termination date	Oct. 1, 2033	Sept. 1, 2035	Sept. 1, 2016	Apr. 25, 2010	
Rate paid by University	4.650%	3.714%	4.631%	4.770%	
Rate paid by Counterparty	71% of one-month LIBOR	67% of one-month LIBOR when LIBOR is \geq 4.00%	71% of one-month LIBOR	one-month LIBOR + 35 bps	
		BMA when one-month LIBOR is < 4.00%			
<u>Fair Value Asset (Liability), net</u>					<u>Total, net</u>
June 30, 2008	(\$2,005)	(\$1,819)	(\$165)	(\$32)	(\$4,021)
June 30, 2007	(\$997)	\$313	\$243	\$40	(\$401)

The net unrealized loss that was recognized for the swaps for the years ended June 30, 2008 and 2007, was approximately \$3,620,000 and \$366,000, respectively and has been included in net realized and unrealized losses on interest rate agreements on the accompanying consolidated statement of activities.

10. Pension Plan

The University participates in a defined contribution retirement plan for substantially all of its employees. Employees may elect to invest in various accounts with the Teachers' Insurance and Annuity Association and College Retirement Equities Fund ("TIAA-CREF"), Fidelity Investments, or a combination of both. Contributions were approximately \$4,654,000 and \$4,520,000 for the years ended June 30, 2008 and 2007, respectively. Contributions are based upon a percentage of the employee's compensation.

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11. Net Assets

Net assets consist of the following at June 30, 2008 and 2007 (in thousands):

Permanently restricted net assets:

	2008	2007
Endowment funds - original principal	\$ 87,740	\$ 79,909
Split-interest agreements and perpetual trusts	18,047	18,465
Student loan funds	2,889	2,748
	<u>\$ 108,676</u>	<u>\$ 101,122</u>

Temporarily restricted net assets:

	2008	2007
Gifts and other unexpended revenues		
Instruction, research, and institutional support	\$ 3,648	\$ 2,717
Acquisition of building and equipment	11,699	5,893
	<u>15,347</u>	<u>8,610</u>
Endowment funds - unspent income and appreciation	96,121	107,045
Split-interest agreements	6,401	6,493
	<u>\$ 117,869</u>	<u>\$ 122,148</u>

Unrestricted net assets designated for the following specific purposes:

	2008	2007
Long-term investment (quasi-endowment funds)	\$ 184,272	\$ 195,787
Net investment in plant facilities	13,471	21,985
Student loan funds	9,791	9,115
Undesignated	26,503	25,844
	<u>\$ 234,037</u>	<u>\$ 252,731</u>

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12. Expenses by Functional Category

Following are expenses categorized by function (in thousands):

	2008	2007
Instruction and department research	\$ 57,149	\$ 54,722
Sponsored research	15,424	14,641
External relations	6,588	6,132
Institution and academic support	33,024	28,328
Student services	11,299	10,640
Auxiliary enterprises	16,225	14,716
	<u>\$ 139,709</u>	<u>\$ 129,179</u>

Depreciation, maintenance, interest and other expenses have been allocated to the various functions. Methods in allocating these expenses include actual expenses incurred and percentage of square footage for each functional area.

External relations expenditures include approximately \$4,362,000 and \$3,236,000 of fund-raising expenses for the years ended June 30, 2008 and 2007, respectively.

13. Related Parties

Newgate Properties, LLC (“Newgate”)

In 2005, the University formed Newgate to own, construct, and operate an approximately 124,600 square foot life sciences and bioengineering facility located in the Gateway Park area of Worcester. The University occupies approximately 90% of the new facility with the remaining 10% being leased to other entities. Occupancy commenced in June, 2007. The University is the sole member of Newgate and has consolidated its accounts in the accompanying consolidated financial statements.

75 Grove Street, LLC (“Grove Street”)

In 2008, the University purchased a vacant parcel of land from Gateway Park, LLC located on 75 Grove Street in Worcester for future development purposes. The University is the sole member of Grove Street and has consolidated its accounts in the accompanying consolidated financial statements.

Gateway Park, LLC (“Gateway”)

The University and Worcester Business Development Corporation (“WBDC”) jointly formed Gateway to purchase and develop land located in the Gateway Park area of Worcester. The University has a 50% interest and has accounted for its investment using the equity method.

Gateway has \$3,650,000 in mortgage notes payable with Flagship Bank and Trust for which the University has entered into a limited guarantee. The liability of the University under this guarantee is limited to 50% of the obligation as defined in the agreement.

New Garden Park, Inc. (“New Garden Park”)

New Garden Park, a Massachusetts not-for-profit corporation, was formed for the purpose of constructing and managing a parking facility located in the Gateway Park area of Worcester and whose members are the University and the WBDC. The University has an uncollateralized note receivable from New Garden Park with interest accruing at 7.0%. For the years ended June 30, 2008 and 2007, amounts due totaled approximately \$4,778,000 and \$4,435,000 respectively. The University has an interest in New Garden Park and records its investment using the equity method.

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New Garden Park has a \$348,000 loan obligation with MDFA, which the University has fully guaranteed.

Prescott Holdings, LLC (“Prescott Holdings”)

Prescott Holdings was formed to develop land in the Gateway Park area of Worcester. The University has a 12.5% interest and has recorded its investment at cost.

Prescott Holdings has \$7,476,000 in outstanding mortgage and construction notes payable with TD Banknorth, N.A. for which the University entered into limited guarantees. As of June 30, 2008, the amount guaranteed by the University totals \$1,398,000.

Alumni Association of Worcester Polytechnic Institute (“Alumni Association”)

The Alumni Association, a separate 501(c)(3) organization, invests the majority of its funds in the University’s endowment. At June 30, 2008 and 2007, funds held for others in the consolidated statements of financial position includes Alumni Association assets of \$2,382,000 and \$2,528,000, respectively.

14. Commitments and Contingencies

Operating Leases

The University is obligated under noncancelable operating leases for office space, and storage and parking facilities.

The future minimum rental commitments under these agreements as of June 30, 2008, are approximately as follows (in thousands):

2009	\$	426
2010		305
2011		342
2012		241
2013		220
Thereafter		<u>2,644</u>
	<u>\$</u>	<u>4,178</u>

Rental expense was approximately \$478,000 and \$381,000 for the years ended June 30, 2008 and 2007, respectively.

Guarantees

In addition to the amounts guaranteed by the University as disclosed in Note 13, the University has guaranteed commercial loans with an original principal amount of \$2,596,000 to five fraternities. These loans are collateralized by real property owned by the fraternities.

Other Commitments

As of June 30, 2008, the University has outstanding commitments under a guaranteed maximum price construction contract for the construction of a new residence hall and parking facility in the amount of approximately \$5,165,000. Funds to satisfy this commitment are included in funds held under bond agreements.

For the year ended June 30, 2007, Newgate had outstanding commitments under a guaranteed maximum price construction contract for the development of the facility in the amount of approximately

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\$4,723,000. Funds to satisfy this commitment were included in funds held under bond agreements. There were no outstanding commitments at June 30, 2008.

The University is obligated under certain limited partnership agreements and other alternative investment arrangements to advance additional funding periodically up to specified levels. At June 30, 2008, the University had unfunded commitments of approximately \$20,085,000 that can be called through 2018. These commitments will be funded from the University's existing cash and investments.

The University's sponsored research program and indirect cost recovery are subject to audit by the respective sponsoring federal agency as provided for in federal sponsored research regulations. Management believes that any such audit will not have a material adverse effect, individually or in the aggregate, upon the University's consolidated statements of financial position, or the related consolidated statements of activities, or cash flows.

The University is also involved in various legal actions arising in the normal course of its activities. Although the ultimate outcome is not determinable at this time, management after taking into consideration advice of legal counsel believes that the resolution of these pending matters will not have a material adverse effect, individually or in the aggregate, upon the University's consolidated statements of financial position, or the related consolidated statements of activities, or cash flows.

15. Upcoming Effective Accounting Standards

In September 2006, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* ("SFAS 157"), which defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 does not require any new fair value measurements, but provides guidance on how to measure fair value by providing a fair value hierarchy used to classify the source of the information. Relative to SFAS 157, the FASB issued FASB Staff Position ("FSP") 157-1, 157-2 and proposed 157-c. FSP 157-1 amends SFAS 157 to exclude SFAS 13 and its related interpretive accounting pronouncements that address leasing transactions, while FSP 157-2 delays the effective date of SFAS 157 for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis. FSP 157-c clarifies the principles in SFAS 157 on the fair value measurement of liabilities. Public comments on FSP 157-c were due in February 2008, and responses and recommendations were presented to the board on April 9, 2008. This statement is effective for the University beginning July 1, 2008. The University's management is currently assessing the potential impact that adoption of SFAS 157 may have on the consolidated financial statements.

In February 2007, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities – Including an amendment of SFAS No. 115* ("SFAS 159"). SFAS 159 provides the irrevocable option to carry many financial assets and liabilities at fair value, with changes in fair value recognized in earnings. SFAS 159 is effective for the University beginning July 1, 2008. The University's management is currently assessing the potential impact, that adoption of SFAS 159 may have on the consolidated financial statements should fair value options be elected.

The Financial Accounting Standards Board ("FASB") issued FASB Staff Position 117-1, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for all Endowment Funds*. The standard provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 ("UPMIFA") and expands disclosures about an organization's endowment (both donor-restricted and board-designated funds), whether or not the

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organization is subject to UPMIFA. The standard is to be effective for fiscal years ending after December 15, 2008. The standard will require significant additional footnote disclosures in next year's consolidated financial statements.