Independent Auditors' Report

To the Board of Trustees of Northwestern University:

We have audited the accompanying consolidated statements of financial position of Northwestern University and subsidiaries (the "University") as of August 31, 2009 and 2008, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the University's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the University as of August 31, 2009 and 2008, and the changes in its net assets and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 5 to the consolidated financial statements, the University adopted Financial Accounting Standards Board Staff Position No. 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" during fiscal year 2009, which required the reclassification of certain unrestricted net assets to temporarily restricted net assets.

Deloitte & Touche LLP

Chicago, Illinois

January 20, 2010

Consolidated Statements of Financial Position

As of August 31, 2009, and August 31, 2008

(in thousands of dollars)	*2009*	*2008*
Assets		
Cash and cash equivalents	$161,610	$157,772
Accounts receivable	284,671	269,462
Notes receivable	52,718	87,488
Contributions receivable	153,886	116,698
Investments	5,759,604	7,135,378
Land, buildings, and equipment	1,436,227	1,349,548
Bond proceeds held by trustees	58,506	118,537
Other assets	61,953	61,287
Total assets	**$7,969,175**	**$9,296,170**
Liabilities		
Accounts payable and accrued expenses	$237,171	$223,333
Deferred revenue	303,352	261,384
Deposits payable and actuarial liability of annuities payable	75,484	65,868
Reserves for self-insurance	26,207	47,675
Government advances for student loans	38,821	38,936
Asset retirement obligations	109,810	104,533
Bonds, notes, and other debt payable	826,166	813,824
Total liabilities	**$1,617,011**	**$1,555,553**
Net assets		
Unrestricted	$3,721,731	$6,675,447
Temporarily restricted	1,621,873	130,814
Permanently restricted	1,008,560	934,356
Total net assets	**$6,352,164**	**$7,740,617**
Total liabilities and net assets	**$7,969,175**	**$9,296,170**

See Notes to the Consolidated Financial Statements, beginning on page 17.

Consolidated Statements of Activities

For the fiscal years ended August 31, 2009, and August 31, 2008

(in thousands of dollars)	*2009*				*2008*			
Operating revenues	**Unrestricted**	**Temporarily restricted**	**Permanently restricted**	**Total**	**Unrestricted**	**Temporarily restricted**	**Permanently restricted**	**Total**
Tuition and fees	$690,817			$690,817	$655,369			$655,369
(less scholarships and fellowships)	(218,207)			(218,207)	(195,624)			(195,624)
Net tuition and fees	472,610			472,610	459,745			459,745
Auxiliary services	69,625			69,625	67,115			67,115
Grants and contracts	421,324			421,324	378,172			378,172
Private gifts	30,964			30,964	120,577			120,577
Investment return designated for operations	242,631	$112,227		354,858	306,344			306,344
Sales and services	134,751			134,751	127,987			127,987
Professional fees	26,635			26,635	29,558			29,558
Royalties and trademarks	87,155			87,155	782,746			782,746
Other income	7,830			7,830	48,039			48,039
Total operating revenues	**1,493,525**	**112,227**	—	**1,605,752**	**2,320,283**	—	—	**2,320,283**
Operating expenses								
Instruction	574,231			574,231	544,018			544,018
Research	391,481			391,481	339,596			339,596
Academic support	176,266			176,266	169,360			169,360
Student services	137,906			137,906	109,045			109,045
Institutional support	189,685			189,685	294,716			294,716
Auxiliary services	118,574			118,574	106,300			106,300
Total operating expenses	**1,588,143**	—	—	**1,588,143**	**1,563,035**	—	—	**1,563,035**
Excess (deficit) of operating revenues over expenses	**(94,618)**	**112,227**	—	**17,609**	**757,248**	—	—	**757,248**
Nonoperating revenues and expenses								
Private gifts and grants for buildings and equipment	14,698			14,698	9,586			9,586
Restricted private gifts		74,390	$74,426	148,816		$30,928	$52,544	83,472
Net gain (loss) on annuity obligations		8,490	(222)	8,268		(1,222)	10,216	8,994
Investment returns, reduced by operating distribution	(983,305)	(596,861)		(1,580,166)	(324,916)			(324,916)
Nonoperating investment returns		2,322		2,322		3,341		3,341
Excess (deficit) of nonoperating revenues over expenses	**(968,607)**	**(511,659)**	**74,204**	**(1,406,062)**	**(315,330)**	**33,047**	**62,760**	**(219,523)**
Net assets released from restrictions	**161,132**	**(161,132)**		—	**51,372**	**(51,372)**		—
Change in net assets before reclassifications	**(902,093)**	**(560,564)**	**74,204**	**(1,388,453)**				
Net asset reclassifications	**(2,051,623)**	**2,051,623**		—				
Change in net assets	**(2,953,716)**	**1,491,059**	**74,204**	**(1,388,453)**	**493,290**	**(18,325)**	**62,760**	**537,725**
Beginning net assets	**6,675,447**	**130,814**	**934,356**	**7,740,617**	**6,182,157**	**149,139**	**871,596**	**7,202,892**
Ending net assets	**$3,721,731**	**$1,621,873**	**$1,008,560**	**$6,352,164**	**$6,675,447**	**$130,814**	**$934,356**	**$7,740,617**

See Notes to the Consolidated Financial Statements, beginning on page 17.

Consolidated Statements of Cash Flows

For the fiscal years ended August 31, 2009, and August 31, 2008

(in thousands of dollars)	*2009*	*2008*
Cash flows from operating activities		
Change in net assets	**($1,388,453)**	**$537,725**
Adjustments to reconcile change in net assets to net cash (used in) provided by operating activities		
Depreciation	91,264	87,858
Accretion for asset retirement obligations	5,277	5,083
Reduction in asset retirement obligations	—	(9,476)
Loss (gain) on retirement of building and equipment	932	(7,260)
Gain on sale of land and building	—	(31,529)
Amortization of discount on bonds payable	73	73
Accretion of premium on bonds payable	(151)	(152)
Net realized and unrealized losses on investments	1,290,361	68,434
Private gifts and grants for long-term investments	(14,698)	(9,586)
Changes in assets and liabilities		
Accounts receivable	(16,011)	(39,574)
Contributions receivable	(37,188)	(11,355)
Other assets	(666)	2,361
Accounts payable and accrued expenses	12,489	75,503
Deferred revenue	41,968	16,695
Reserves for self-insurance	(21,468)	(3,911)
Government advances for student loans	(115)	(148)
Net cash (used in) provided by operating activities	**(36,386)**	**680,741**
Cash flows used in investing activities		
Purchases of investments	(2,005,229)	(2,829,458)
Proceeds from sales of investments	2,091,992	2,124,887
Decrease in trusts held by others	802	3,051
Increase in investments held for others	(1,350)	(2,576)
Acquisitions of land, buildings, and equipment	(177,865)	(185,441)
Proceeds from sale of plant assets	339	38,520
Student loans disbursed	(66,704)	(74,816)
Principal collected on student loans	101,474	42,069
Net cash used in investing activities	**(56,541)**	**(883,764)**
Cash flows from (used in) financing activities		
Net proceeds from issuance of note, bonds and other debt payable	15,000	205,500
Principal payments on notes payable and bonds payable	(2,580)	(2,480)
Decrease (increase) in bond proceeds held by trustees	60,031	(37,401)
Proceeds from private gifts and grants for long-term investments	14,698	9,586
Increase in deposits payable and annuities payable	9,616	998
Net cash provided by financing activities	**96,765**	**176,203**
Increase (decrease) in cash and cash equivalents	**3,838**	**(26,820)**
Cash and cash equivalents at beginning of year	**157,772**	**184,592**
Cash and cash equivalents at end of year	**$161,610**	**$157,772**
Supplemental disclosure of cash flow information		
Accrued liabilities for construction in progress	$20,798	$19,449
Capitalized interest	1,638	2,694
Cash paid for interest	27,116	22,592

See Notes to the Consolidated Financial Statements, beginning on page 17.

1. Summary of Significant Accounting Policies

UNIVERSITY ACTIVITIES

Northwestern University (the University) is a major private research university with more than 17,000 students enrolled in 11 academic divisions on two lakefront campuses in Evanston and Chicago and an international campus in Doha, Qatar.

Northwestern's mission is to provide the highest-quality education for its students, to develop innovative programs in research, and to sustain an academic community that embraces these enterprises. Activities supporting its mission may be classified as either operating or nonoperating.

BASIS OF ACCOUNTING

General

The University maintains its accounts and prepares its consolidated financial statements on the accrual basis of accounting in conformity with generally accepted accounting principles in the United States of America (GAAP). These statements include all wholly owned subsidiaries. All significant intercompany transactions and accounts have been eliminated.

Contributions

The University prepares its financial statements in accordance with Statement of Financial Accounting Standards (SFAS) No. 116, "Accounting for Contributions Received and Contributions Made." SFAS No. 116 requires that contributions received, including unconditional promises to give (pledges), be recognized as revenues at their fair values. Private gifts, including unconditional promises to give, are recognized as revenues in the period received. Conditional promises to give are not included in revenue until the conditions are substantially met. Pledges receivable due in more than one year are recorded at the present value of the estimated future cash flows.

Net Asset Classifications

SFAS No. 117, "Financial Statements of Not-for-Profit Organizations," establishes standards for external financial reporting by not-for-profit organizations and requires that net assets and the flow of those assets be classified in three net asset categories according to the existence or absence of donor-imposed restrictions.

In fiscal year 2009, the University adopted Staff Position No. 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 (UPMIFA) and Enhanced Disclosures for all Endowment Funds" (FSP 117-1). The guideline applies to the classification of donor-restricted endowment funds and disclosures about both donor-restricted and board-designated endowment funds regardless of whether the organization is subject to UPMIFA. For further discussion, see note 5 to the consolidated statements.

The category *Permanently Restricted Net Assets* applies to gifts, trusts, and pledges whose donors required that the principal be held in perpetuity and that only the income be available for stipulated program operations.

The category *Temporarily Restricted Net Assets* includes gifts for which donor-imposed restrictions have not been met (these are primarily future capital projects) and trust activity and pledges receivable whose ultimate use is not permanently restricted.

The category *Unrestricted Net Assets* describes funds that are legally available for any purpose and have no donor-imposed restrictions. All revenues, expenses, gains, and losses are classified as unrestricted net assets unless they are changes in temporarily or permanently restricted net assets. Net unrealized losses on permanently restricted endowment funds for which the historical cost exceeds market value are recorded as a reduction to unrestricted net assets.

Income from temporarily restricted sources is reclassified as unrestricted income when the circumstances of the restriction have been fulfilled. Donor-restricted revenues whose restrictions are met within the same fiscal year are reported as unrestricted income. The expiration of a donor-imposed restriction on a contribution is recognized in the period in which the restriction expires. All expenditures are reported in the unrestricted class of net assets, since the use of restricted contributions in accordance with the donor's stipulations causes the release of the restriction.

FAIR VALUE MEASUREMENTS

In fiscal year 2009, the University implemented SFAS No. 157, "Fair Value Measurements." It redefines fair value, provides a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. For further discussion, see note 4 to the consolidated statements.

The University also adopted SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities — Including an Amendment of Financial Accounting Standards Board (FASB) Statement No. 115." The statement provides the option of reporting selected financial assets at fair value and includes presentation and disclosure requirements to facilitate comparisons between entities using different measurement attributes for similar kinds of assets and liabilities. The University has not elected the fair value option under SFAS No. 159.

CASH AND CASH EQUIVALENTS

Cash reflects currency and deposits or other accounts with financial institutions that may be deposited or withdrawn without restriction or penalty. Cash equivalents represent short-term and highly liquid investments that convert readily to cash and carry little risk of change in value at maturity due to interest rate changes.

INVESTMENTS

Investments are recorded at fair value in accordance with the provisions of SFAS No. 157, determined on the following basis:

- Equity securities with readily determinable fair values and debt securities are valued at the last sale price (if quotations are readily available) or at the closing bid price in the principal market in which such securities are normally traded (if no sale price is available). Certain fixed income securities are valued based on dealer-supplied valuations.
- The estimated fair values of equity securities that do not have readily determined fair values, and of other investments, are based on estimates provided by external investment managers and are examined through a valuation review process performed by management. After this review, management may determine that an adjustment to the external managers' valuations is appropriate in recording the securities' fair value at August 31. The aggregate carrying value of these securities included within fixed income, high-yield credit, absolute return, private investments, and real assets was $3,611.9 million (45.3 percent of total assets) and $4,380.6 million (47.1 percent of total assets) at August 31, 2009, and 2008, respectively. These investments are generally less liquid than other investments.

During the examination process management reviewed the valuation policies for all partnerships in which Northwestern University is invested and deemed those policies appropriate. In addition to receiving the most recent available audited and unaudited financial statements from the external managers, management contacted the majority of general partners regarding the aggregate carrying value of the respective investments at August 31, 2009.

A range of possible values exists for these partnership investments, and therefore the estimated values may be materially different from the values that would have been used had a ready market for these partnerships existed. In the absence of another basis, management has determined that cost represents an approximation of the fair value of such investments. A small number of investments within certain partnerships may have holdings at a carrying value of cost, and management has determined this to be appropriate for these specific investments.

Investment income is recorded on the accrual basis, and purchases and sales of investment securities are reflected on a trade-date basis.

DERIVATIVE FINANCIAL INSTRUMENTS

The University uses various financial instruments to hedge the risk of decline in fair value of certain equity securities. Equity options and equity-indexed options are used to reduce the primary market risk exposure (e.g., equity price risk) of the hedged item in conjunction with the specific hedged strategy; if applicable, these have a reference index (e.g., S&P 500) that is the same, or highly correlated with, the reference index of the hedged item. In addition, the University uses various financial instruments to hedge foreign currency liabilities. Similarly, the University also enters into swap agreements to hedge public real estate equity exposure and obtain S&P 500 equity index exposure, and it uses futures contracts on equity and bond indices. Such instruments are not designated as hedges for accounting purposes and are recorded at fair value.

In fiscal year 2009, the University entered into swap agreements to hedge future interest rate movements. In fiscal year 2008, the University entered into a euro-denominated foreign currency swap as a hedge against a portion of future capital commitments to foreign currencies. The University also added various interest rate options to hedge the overall portfolio and used an interest-rate swap agreement to hedge variable interest rate exposure.

FAIR VALUES OF FINANCIAL INSTRUMENTS OTHER THAN INVESTMENTS

The fair values of financial instruments other than investments are based on a variety of factors. In some cases, fair values represent quoted market prices for identical or comparable instruments. In other cases, fair values have been estimated based on assumptions about the amount and timing of estimated future cash flows and assumed discount rates reflecting varying degrees of risk. Accordingly, the fair values may not represent actual values that could have been realized at year-end or that will be realized in the future. At August 31, 2009, the fair value of the University's fixed rate debt of $356.1 million exceeded the carrying value of $345.6 million by $10.5 million. At August 31, 2008, the fair value of the University's fixed rate debt of $351.7 million exceeded the carrying value of $348.2 million by $3.5 million.

ACCOUNTS AND NOTES RECEIVABLE

Student accounts receivable arising from tuition and fees are carried net of an allowance for doubtful accounts of $446,000 and $475,000 as of August 31, 2009, and 2008, respectively. Notes receivable resulting from student loans are carried net of an allowance for doubtful accounts of $381,000 and $1.3 million as of August 31, 2009, and 2008, respectively.

Receivables from Northwestern Medical Faculty Foundation, a related party (see page 20), arose out of operational activities. They totaled $12.1 million and $18.9 million as of August 31, 2009, and 2008, respectively.

CONTRIBUTIONS RECEIVABLE

Contributions receivable arising from unconditional promises to give are carried net of an allowance for uncollectible pledges that totaled $20.5 million and $17.9 million at August 31, 2009, and 2008, respectively. Additionally, unconditional promises expected to be collected in periods from more than one year are discounted to present value. The discount rates for pledges made in fiscal years 2009 and 2008 were 2.9 and 3.6 percent, respectively; the discount rate for pledges made in prior fiscal years ranged from 4.5 to 6.5 percent. There were no significant conditional promises to give as of August 31, 2009; such promises totaled $25.8 million at August 31, 2008.

LAND, BUILDINGS, AND EQUIPMENT

The value of land, buildings, and equipment is recorded at cost or, if received as gifts, at fair market value at the date of the gift. Significant renewals and replacements are capitalized. The cost of repairs and maintenance is expensed as incurred. Purchases of library books are also expensed.

Depreciation is calculated using the straight-line method over the useful lives of the buildings and equipment, which are estimated to be 3 to 20 years for equipment and a maximum of 40 years for buildings. The University follows SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." The provisions under this statement include a requirement that long-lived assets be reviewed for impairment by comparing the future cash flows expected from the asset to the carrying value of the asset. If the carrying value of an asset exceeds the sum of estimated undiscounted future cash flows, an impairment loss is recognized for the difference between estimated fair value and carrying value. In management's opinion, no impairment existed as of August 31, 2009.

CHARITABLE REMAINDER TRUSTS

Charitable remainder trusts are classified as permanently restricted net assets if, upon termination of the trust, the donor permanently restricts the remaining trust assets. If the remainder is temporarily restricted or unrestricted by the donor, the charitable remainder trust assets are recorded as temporarily restricted net assets.

ANNUITIES PAYABLE

Annuities payable consist of annuity payments currently due and the actuarial amount of annuities payable. The actuarial amount of annuities payable is the present value of the aggregate liability for annuity payments over the expected lives of the beneficiaries (based on the 90CM mortality tables in the Internal Revenue Code, Publication 1458, July 1999, and Publication 939, April 2003).

SELF-INSURANCE RESERVES

The University maintains a self-insurance program for general liability, professional liability, and certain employee and student insurance coverages. This program is supplemented with commercial excess insurance above the University's self-insurance retention.

ASSET RETIREMENT OBLIGATIONS

The University follows the FASB Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations—An Interpretation of FASB Statement No. 143" (FIN 47). FIN 47 clarifies the term conditional asset retirement obligation as it is used in SFAS No. 143, "Accounting for Asset Retirement Obligations," and requires a liability to be recorded if the fair value of the obligation to retire an asset can be reasonably estimated. Asset retirement obligations covered by FIN 47 include those for which an entity has a legal obligation to perform an asset retirement activity; however, the timing and/or method of settling the obligation are conditional on a future event that may or may not be within the control of the entity. In accordance with FIN 47, the University records all known asset retirement obligations for which the fair value of the liability can be reasonably estimated, including certain obligations relating to regulatory remediation.

REVENUE RECOGNITION

Revenues from tuition and fees are reported in the fiscal year in which educational programs are predominantly conducted. Fiscal year 2010 fall-quarter tuition and fees, billed in fiscal year 2009, are reported as deferred revenue in fiscal year 2009. Similarly, fiscal year 2009 fall-quarter tuition and fees, billed in fiscal year 2008, are reported as deferred revenue in fiscal year 2008.

Revenues from auxiliary services, such as residence and food services, represent fees for goods and services furnished to University students, faculty, and staff; these revenues are recognized in the fiscal year in which the goods and services are provided. Grants and contracts revenue is recognized as expenses are incurred on a project. Professional fees arise from faculty and department services provided to external institutions such as hospitals. Sales and services revenues represent fees for services and goods provided to external parties in the course of educational activities and also include revenues from the provision of physical plant services and goods to external institutions contiguous to the University campuses. Trademark and royalty revenues arise from licensing of innovative technologies, copyrights, and other intellectual property; these revenues are recognized in the fiscal year in which they are earned. Other income includes revenues not otherwise categorized, such as rental revenues from property not held for investment, reimbursements for goods and services, and sundry payments to the University; these revenues are also recognized in the fiscal year in which they are earned.

INCOME TAXES

The Internal Revenue Service has determined that the University is exempt from income taxes under Section 501(c)(3) of the U.S. Internal Revenue Code, except with regard to unrelated business income, which is taxed at corporate income tax rates. The University files U.S. federal and various state and local tax returns. The statute of limitations on the University's U.S. federal tax returns remains open for fiscal years 2006 through 2009.

In fiscal year 2008, the University adopted FIN No. 48, "Accounting for Uncertainty in Income Taxes," an interpretation of FASB Statement No. 109, "Accounting for Income Taxes," that clarifies accounting for uncertainty in income taxes reported in the financial statements. The interpretation provides criteria for assessment of individual tax positions and a process for recognition and measurement of uncertain tax positions. Tax positions are evaluated on whether they meet the "more likely than not" standard for sustainability on examination by tax authorities. There was no material impact on the University's consolidated financial statements for fiscal years 2009 and 2008 as a result of adoption.

RELATED PARTIES

Northwestern Medical Faculty Foundation (NMFF) is a multispecialty physician organization committed to providing clinical care to patients and to supporting the research and academic endeavors of Northwestern's Feinberg School of Medicine. An independent not-for-profit organization, NMFF is governed by a board of directors. NMFF physicians are full-time faculty members or researchers at Feinberg and attending physicians at Northwestern Memorial Hospital. Under the terms of an agreement with Northwestern University, NMFF contributes a percentage of its revenue to a research and education fund, medical education programs, basic and applied biomedical research facilities and programs, and research and educational support services. NMFF also contributes funds to Feinberg's teaching and research activities on a discretionary basis. These contributions totaled $26.3 million in fiscal year 2009 and $25 million in fiscal year 2008.

USES OF ESTIMATES IN THE PREPARATION OF FINANCIAL STATEMENTS

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities; the disclosure of contingent assets and liabilities at the date of the financial statements; and the reported amounts of revenues and expenses during the relevant period. Actual results could differ from those estimates.

At August 31, 2009, and 2008, reserves were established for uncollectible accounts, student loans, and pledges receivable. These reserves were estimated based on historical collection and allowance practices as well as on management's evaluation of current trends.

The reserves for self-insurance and postretirement medical and life insurance benefits were based on actuarial studies and management estimates.

The reserves for asset retirement obligations were based on analyses of University assets, review of applicable regulatory and other guidance, and management estimates.

The University believes that the methods and assumptions used in computing these reserves and liabilities are appropriate.

ACCOUNTING PRONOUNCEMENTS

In March 2008, the FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities." This statement is intended to improve financial reporting by requiring enhanced disclosures about the effects of derivative instruments and hedging activities on an entity's financial position, financial performance, and cash flows. It will be effective in fiscal year 2010 for the University. The University is evaluating the impact of its implementation on the consolidated financial statements.

In May 2009, the FASB issued SFAS No. 165, "Subsequent Events." This statement prescribes the period for evaluation of subsequent events and disclosure of the date through which the evaluation occurred, and whether that date is the date the financial statements were issued or available to be issued. SFAS No. 165 is effective in fiscal year 2009 for the University. See note 11 to the consolidated statements.

In June 2009, the FASB issued SFAS No. 168, "FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles — a replacement of FASB Statement No. 162." SFAS No. 162 identified the sources of accounting principles and the framework for selecting the principles used in preparing financial statements presented in conformity with GAAP, and arranged the sources of GAAP in a hierarchy. SFAS No. 168 modifies the GAAP hierarchy to include only two levels, authoritative and nonauthoritative. SFAS No. 168 is effective in fiscal year 2010. The University is evaluating the impact of its implementation on the consolidated financial statements.

2. Bonds, Notes, and Other Debt Payable

Bonds, notes, and other debt payable are as follows:

(in thousands of dollars)	*August 31, 2009*	*August 31, 2008*
Demand revenue bonds		
IEFA–Series 1993	$15,435	$18,015
Less unamortized discount on IEFA–Series 1993	(365)	(438)
IEFA–Series 2003	185,010	185,010
IFA–Series 2004	135,800	135,800
IFA–Series 2006	145,130	145,130
Plus unaccreted premium on IFA–Series 2006	5,156	5,307
IFA–Series 2008	125,000	125,000
Bonds payable subtotal	**611,166**	**613,824**
Notes payable — commercial paper, taxable	165,000	200,000
Other debt payable — lines of credit	50,000	—
Total bonds, notes, and other debt payable	**$826,166**	**$813,824**

Debt issuance	**Interest rate mode**	**Interest rate**	**Maturity**
IEFA–Series 1993	Fixed	5.51%*	December 1, 2009, to December 1, 2013
IEFA–Series 2003	Fixed	5%*	December 1, 2014, to December 1, 2038
IFA–Series 2004	Variable, annual rate	.5% and .58%†	December 1, 2034
IFA–Series 2006	Fixed	5%*	December 1, 2042
IFA–Series 2008	Variable, annual rate	.5%, .6%, and .58%†	December 1, 2046
Notes payable —commercial paper, taxable	Fixed	.45%*	September 10, 2009, to November 12, 2009
Other debt payable — lines of credit	Fixed	1.96%*	September 9, 2009, to September 10, 2009

** Weighted average interest rate at August 31, 2009* † *Annual variable rates at August 31, 2009*

Total obligations including notes and other debt payable at August 31, 2009, are scheduled to mature through August 31 of each period as noted at right. The schedule has been prepared based on the contractual maturities of the debt outstanding at August 31, 2009. Accordingly, if remarketing of bonds fails in future periods, debt repayments may become more accelerated than presented here.

(in thousands of dollars)	
2010	$217,754
2011	2,954
2012	3,149
2013	3,344
2014	3,629
2015–2019	20,783
2020–2024	15,743
2025–2029	758
2030–2034	22,738
Thereafter	535,314
Total	**$826,166**

BONDS PAYABLE

The IEFA–Series 1993 Revenue Refunding Bonds operate in a fixed mode until maturity, bearing interest at fixed rates ranging from 3 percent to 5.55 percent. Proceeds of the refunding bonds were invested in United States government securities with a cost of $75.4 million and placed in escrow to satisfy scheduled payments of $66.4 million of the IEFA–Series 1985 bonds and related interest until maturity.

The IEFA–Series 2003 Fixed Rate Revenue Bonds were issued to acquire, construct, or renovate certain University facilities and to refund $35 million of the University's outstanding IEFA–Series 1993 bonds, subject to conditions set forth in a trust indenture and loan agreement between the University and the Illinois Facilities Authority.

The IFA–Series 2004 Adjustable Rate Revenue Bonds were issued to acquire, construct, renovate, remodel, improve, and equip capital projects on both the Evanston and the Chicago campuses, subject to conditions set forth in a trust indenture and loan agreement between the University and the Illinois Finance Authority. The bonds may operate in a daily, weekly, adjustable, or auction-rate mode. In fiscal year 2009, the revenue bonds were remarketed to operate in an annual rate mode from a weekly rate mode.

The IFA–Series 2006 Revenue Bonds were issued in October 2006 to refund the University's outstanding IEFA–Series 1997 Adjustable Medium-Term Revenue Bonds totaling $145 million. The refunding bonds are subject to conditions set forth in a trust indenture and loan agreement between the University and the authority.

The IFA–Series 2008 Adjustable Rate Revenue Bonds were issued on June 25, 2008, to acquire, construct, renovate, remodel, improve, and equip capital projects, subject to conditions set forth in a trust indenture and loan agreement between the University and the Illinois Finance Authority. The bonds may operate in a daily, weekly, adjustable, or auction-rate mode. In fiscal year 2009, the revenue bonds were remarketed to operate in an annual rate mode from a weekly rate mode.

DERIVATIVE FINANCIAL INSTRUMENTS

On May 30, 2008, the University terminated the interest-rate swap agreements and executed new interest-rate swap agreements to hedge variable interest rate exposure. The University recognized a realized loss on the swap termination totaling $9.1 million. The agreements effectively fix the interest rate from 4.2 percent to 4.38 percent and expire on December 1, 2046. The notional value is $262.1 million through December 1, 2034, and reduces to $125 million effective December 2, 2034, through expiration. The University recognized unrealized losses on the swap investment totaling $17.9 million at August 31, 2009, and $14.5 million at August 31, 2008. The fair values of the swap position were ($41.5) million and ($23.6) million as of August 31, 2009, and 2008, respectively, and are included in accounts payable and accrued expenses on the consolidated statements of financial position.

NOTES PAYABLE

The University places commercial paper under a $200 million Taxable Commercial Paper Note.

OTHER DEBT PAYABLE

During the fiscal year, the University established $325 million in standby lines of credit to supplement working capital requirements as follows: $100 million established on July 22, 2009, expires July 22, 2010; $50 million established on August 19, 2009, expires August 19, 2010; $50 million established on March 27, 2009, expires March 26, 2010; $50 million established on April 24, 2009, expires on April 23, 2010; and $75 million established on June 17, 2009, expires June 16, 2010.

3. Contributions Receivable

Contributions receivable consisted of the following:

(in thousands of dollars)	*August 31, 2009*	*August 31, 2008*
Unconditional promises expected to be collected in		
Less than one year	$124,449	$80,646
One year to five years	54,896	61,721
More than five years	1,619	—
Less discount to present value and other reserves		
Discount to present value	(6,606)	(7,784)
Other reserves	(20,472)	(17,885)
Total	**$153,886**	**$116,698**

Contributions receivable are discounted based on the weighted average borrowing rates for short-term and long-term bonds, notes, and other debt payable to correspond to the terms of the pledges receivable. The University deems these yields to be a Level 3 input under the SFAS 157 hierarchy. See note 4 for further discussion of SFAS 157.

The table at right summarizes the change in contributions receivable for the year ended August 31, 2009.

(in thousands of dollars)	
Balance — beginning of year	$116,698
New pledges	94,202
Collections on pledges	(55,605)
Decrease in discount to present value	1,178
Increase in other reserves	(2,587)
Balance — end of year	**$153,886**

4. Investments

The University's investments are overseen by the Investment Committee of the Board of Trustees. Guided by the policies established by the Investment Committee, the University's Investment Office or external equity investment managers, external and internal fixed income and cash managers, and various limited partnership managers direct the investment of endowment and trust assets, certain working capital, temporarily invested expendable funds, and commercial real estate.

Substantially all of these assets are merged into internally managed investment pools on a market-value basis. Each holder of units in the investment pools subscribes to or disposes of units on the basis of the market value per unit at the beginning of each month.

INVESTMENT MARKET VALUE

As discussed in note 1, as of September 1, 2009, the University adopted SFAS No. 157 and has valued its investments in accordance with the principles of this standard.

SFAS No. 157 establishes a hierarchy of valuation inputs based on the extent to which the inputs are observable in the marketplace. Observable inputs reflect market data obtained from sources independent of the reporting entity; unobservable inputs reflect the entity's own assumptions about how market participants would value an asset or a liability based on the best information available. Valuation techniques used to measure fair value under SFAS No. 157 must maximize the use of observable inputs and minimize the use of unobservable inputs. SFAS No. 157 describes a fair-value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value.

The following describes the hierarchy of inputs used to measure fair value and the primary valuation methodologies used by the University for financial instruments measured at fair value on a recurring basis.

Level 1: Quoted prices in active markets for identical assets or liabilities. Market price data are generally obtained from relevant exchanges or dealer markets.

Level 2: Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the same term of the assets or liabilities. Inputs are obtained from various sources, including market participants, dealers, and brokers.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

A financial instrument's categorization within the valuation hierarchy is based on the lowest level of input that is significant to the fair value measurement.

The following chart shows the estimated fair value of investments held by the University, grouped by the SFAS No. 157 valuation hierarchy as defined above:

(in thousands of dollars)				*August 31, 2009*	*August 31, 2008*
	Quoted prices in active markets (Level 1)	**Significant other observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**	**Total fair value**	**Total fair value**
U.S. equity securities	$177,466	$166,060	$278,138	$621,664	$953,953
International equity	258,873	294,176	181,004	734,053	872,147
Fixed income	79,998	532,700	187,666	800,364	821,981
High-yield credit	—	—	490,098	490,098	494,425
Absolute return	—	49,139	889,401	938,540	1,216,526
Private investments	16,985	—	1,177,180	1,194,165	1,460,793
Real assets	39,869	787	889,178	929,834	1,245,622
Other investments	—	1,455	49,431	50,886	69,931
Subtotal investments	**573,191**	**1,044,317**	**4,142,096**	**5,759,604**	**7,135,378**
Interest-rate swaps	—	—	(41,518)	(41,518)	(23,654)
Total	**$573,191**	**$1,044,317**	**$4,100,578**	**$5,718,086**	**$7,111,724**

Investments included in Level 3 primarily consist of the University's ownership in alternative investments (principally limited partnership interests in hedge, private equity, real estate, and other similar funds).

Interest-rate swaps are valued using observable inputs, such as quotations received from the counterparty, dealers, or brokers, whenever available and considered reliable. In instances where models are used, the value of the interest-rate swap depends on the contractual terms of, and specific risks inherent in, the instrument as well as the availability and reliability of observable inputs. Such inputs include market prices for reference securities, yield curves, credit curves, measures of volatility, prepayment rates, and correlations of such inputs. The interest-rate swap arrangements have inputs that are unobservable and have little or no market activity and therefore are classified within Level 3.

Perpetual trusts held by third parties are valued at the present value of the future distributions expected to be received over the term of the agreement and are included in other investments in the summary of changes in investments within Level 3.

The methods described above may produce a fair value that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the University believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

The following is a a summary of changes in the investments classified by the University within Level 3 of the fair value hierarchy:

(in thousands of dollars)	*August 31, 2008*				*August 31, 2009*
	Fair value	**Realized gains (losses)**	**Unrealized gains (losses)**	**Net purchases, sales, and settlements**	**Fair value**
U.S. equity securities	$405,738	(4,889)	(72,583)	(50,127)	$278,139
International equity	101,767	(621)	(16,035)	95,893	181,004
Fixed income	161,851	2,359	40,337	(16,881)	187,666
High-yield credit	494,406	1,764	(66,939)	60,866	490,097
Absolute return	1,213,836	33,085	(201,707)	(155,813)	889,401
Private investments	1,383,444	10	(306,523)	100,249	1,177,180
Real assets	1,121,775	(6,962)	(351,562)	125,927	889,178
Other investments	69,035	(4,319)	166	(15,451)	49,431
Subtotal investments	**4,951,852**	**20,427**	**(974,846)**	**144,663**	**4,142,096**
Interest-rate swaps	(23,654)	—	(17,864)	—	(41,518)
Total	**$4,928,198**	**20,427**	**(992,710)**	**144,663**	**$4,100,578**

At August 31, 2009, the University was committed to making future capital contributions in other investments in the amount of $1,615 million, primarily in the next five years.

INVESTMENT RETURN

The components of total investment return were as follows:

(in thousands of dollars)	*August 31, 2009*	*August 31, 2008*
Investment income	$68,177	$56,254
Net realized (losses) gains	(226,384)	388,026
Change in net unrealized (losses) gains on investments reported at fair value	(1,064,779)	(459,511)
Total investment return	**($1,222,986)**	**($15,231)**

Investment return designated for operations is defined as the investment payout, according to the spending guideline for the Long-Term Balanced Pool and the actual investment income for all other investments. Other investment returns are categorized as nonoperating. As reflected in the consolidated statements of activities, investment return was as follows:

(in thousands of dollars)	*August 31, 2009*	*August 31, 2008*
Changes in unrestricted net assets		
Operating: investment return	$242,631	$306,344
Nonoperating: investment returns, reduced by operating distribution	(983,305)	(324,916)
Changes in temporarily restricted net assets		
Operating: investment return	112,227	—
Nonoperating: investment returns, reduced by operating distribution	(596,861)	—
Investment return	2,322	3,341
Total investment return	**($1,222,986)**	**($15,231)**

DERIVATIVE FINANCIAL INSTRUMENTS

In fiscal year 2009, the University entered into a swap agreement to gain equity exposure to a subindex of the S&P 500 index and terminated exposure to various subindices as well as a commodity index. The notional value of these swaps outstanding at August 31, 2009, and August 31, 2008, was $26.2 million and $122.2 million, respectively. The equity index swap had an unrealized gain of $144,000 at August 31, 2009. The swaps had a realized loss of $38.7 million during fiscal year 2009 and a realized gain of $8.8 million during fiscal year 2008.

In addition, the University terminated a euro-dominated foreign currency swap during fiscal year 2009 as an economic hedge against a portion of future capital commitments on foreign currencies. The swap had a realized loss of $13.5 million.

The University also entered into hedging transactions via various interest-rate swaps and options in fiscal years 2008 and 2009. The remaining net cost of these swaps and options was $6.4 million, and they had a realized gain of $800,000 during fiscal year 2009 and a realized loss of $1.2 million during fiscal year 2008. The positions carried an unrealized gain of $26.1 million as of August 31, 2009. These swaps and options had a notional value of $3,000 million at August 31, 2009. These instruments are held in the fixed income asset class in the summary of changes in investments within Level 3.

The University bought and sold futures contracts on a domestic equity index during fiscal years 2009 and 2008 and incurred realized losses of $12.4 million and $5.1 million, respectively. As of August 31, 2009, the University had no S&P 500 index futures contracts outstanding.

The University also bought and sold futures contracts on international equity indices during 2009 and 2008 and incurred realized losses of $11.5 million and $5.1 million, respectively. As of August 31, 2009, there were no international equity index contracts outstanding.

Such equity instruments are not designated as hedges for accounting purposes and are recorded at fair value and included in investments on the consolidated statements of financial position.

Credit exposure represents the University's potential loss if all the counterparties fail to perform under the terms of the contracts, and if all collateral, if any, becomes worthless. This exposure is measured by the fair value of the cash collateral held at the counterparties at the reporting date. The University manages its exposure to credit risk by using highly rated counterparties, establishing risk control limits, and obtaining collateral where appropriate. As a result, the University has limited credit risk. In fiscal year 2009, the University entered into a margin collateral agreement with a major counterparty that imposes a $1 million threshold on both parties. As of August 31, 2009, the collateral account at the University's custodian bank held $32.7 million of treasury securities pledged by the counterparty to support the University's unrealized gains at fiscal year end. To date, the University has not incurred any losses on derivative financial instruments due to counterparty nonperformance.

The University regularly reviews the use of derivative financial instruments by each of the managers of alternative investment funds in which it participates. While these outside managers generally use such instruments for hedging purposes, derivative financial instruments are employed for trading purposes by 32 independent asset managers of the University funds totaling approximately $1,650 million and $2,165 million at August 31, 2009, and 2008, respectively.

5. Endowments

The Financial Accounting Standards Board issued FSP 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," in August 2008. The standard provides guidance on the net asset classification of donor-restricted endowment funds for not-for-profit organizations subject to an enacted version of UPMIFA. FSP 117-1 also improves disclosure about an organization's endowment funds, both donor-restricted and board-designated, regardless of whether the organization is subject to UPMIFA. Illinois adopted UPMIFA effective for institutional funds existing on or established after June 30, 2009. The University adopted FSP 117-1 for the year ended August 31, 2009.

The University interprets UPMIFA as requiring that the fair value of the original donor-restricted endowment gift be preserved as of the gift date unless there are explicit donor stipulations to the contrary. Therefore, the University classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment, the original value of subsequent gifts, and accumulations to the permanent endowment made in accordance with the applicable donor gift instrument at the time the accumulation was added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for University expenditure in a manner consistent with UPMIFA's standard of prudence. In accordance with UPMIFA, the University considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- The duration and preservation of the endowment fund
- The purposes of the institution and of the endowment fund
- General economic conditions
- The possible effects of inflation or deflation
- The expected total return from income and appreciation of investments
- Other resources of the institution
- The institutional investment policy

The University's endowment consists of about 2,000 individual donor-restricted endowment funds and about 800 funds it designates to function as endowments. The net assets associated with endowment funds, including funds designated by the University to function as endowments, are classified and reported based on whether there are donor-imposed restrictions. Institution-designated endowment funds include quasi-endowments established by specific Board of Trustees approval as well as endowments created by management under general guidelines and policies approved by the Board of Trustees.

As a result of the University's adopting FSP 117-1 at the beginning of fiscal year 2009, the portion of donor-restricted net assets not classified as permanently restricted in the amount of $2,052 million was reclassified from unrestricted net assets to temporarily restricted net assets to conform with the prescribed reporting requirements.

The following table presents the endowment net asset composition by type of fund for the years ended August 31, 2009, and 2008, at fair value:

(in thousands of dollars)				*August 31, 2009*
Endowment net asset composition by type of fund	**Unrestricted**	**Temporarily restricted**	**Permanently restricted**	**Total**
Donor-restricted endowment funds		$1,470,149	$865,525	$2,335,674
Institution-designated endowment funds	$2,062,526			2,062,526
Total endowment funds	**$2,062,526**	**$1,470,149**	**$865,525**	**$4,398,200**

(in thousands of dollars)				*August 31, 2008*
Endowment net asset composition by type of fund	**Unrestricted**	**Temporarily restricted**	**Permanently restricted**	**Total**
Donor-restricted endowment funds		$20,395	$819,091	$839,486
Institution-designated endowment funds	$4,538,656			4,538,656
Total endowment funds	**$4,538,656**	**$20,395**	**$819,091**	**$5,378,142**

INVESTMENT AND SPENDING POLICIES

The University's endowment is primarily invested in the Long-Term Balanced Pool, which is managed with the objective of long-term total return. The Investment Committee of the Board of Trustees annually reviews asset allocation policy for the pool.

The principal objective for the Long-Term Balanced Pool is to preserve purchasing power and to provide a growing stream of income to fund University programs. On average, the pool seeks to achieve an annual total rate of return (i.e., actual income plus appreciation) equal to inflation plus actual spending. This objective of preserving purchasing power emphasizes the need for a long-term perspective in formulating both spending and investment policies.

The Board of Trustees has adopted a guideline for the annual spending rate from the University's Long-Term Balanced Pool. The calculation blends market and spending elements for the total annual spending rate.

The market element is an amount equal to 4.35 percent of the market value of a unit in the pool, averaged for the 12 months ending October 31 of the prior fiscal year. It is weighted at 30 percent in determining the total. The spending element is an amount equal to the current fiscal year's spending amount increased by 1.5 percent plus the actual rate of inflation. It is weighted at 70 percent in determining the total.

If investment income received is not sufficient to support the total-return objective, the balance is provided from realized and unrealized gains. If the income received is in excess of the objective, the balance is reinvested in the Long-Term Balanced Pool on behalf of the unit holders.

The University's Policy is to allocate the current income of all other investment pools.

CHANGE IN ENDOWMENT NET ASSETS

The following table represents the changes in endowment net assets for the year ended August 31, 2009:

(in thousands of dollars)				*August 31, 2009*
	Unrestricted	**Temporarily restricted**	**Permanently restricted**	**Total**
Endowment net assets, September 1, 2008	$4,538,656	$20,395	$819,091	$5,378,142
Reclassification due to adoption of FSP 117-1	(2,051,623)	2,051,623		—
Endowment net assets, beginning of year	2,487,033	2,072,018	819,091	5,378,142
Investment return				
Investment income	6,130	7,928		14,058
Net depreciation (realized and unrealized)	(420,752)	(496,189)		(916,941)
Total investment return	(414,622)	(488,261)	—	(902,883)
Contributions	8,670	898	39,888	49,456
Appropriation of endowment assets for expenditure	(98,770)	(114,056)	—	(212,826)
Other changes				
Transfers to create institutional funds	98,478			98,478
Transfers of institutional funds per donor requirement		402	5,694	6,096
Spending of institution-designated endowment fund	(18,263)			(18,263)
Other reclassifications		(852)	852	—
Endowment net assets, August 31, 2009	**$2,062,526**	**$1,470,149**	**$865,525**	**$4,398,200**

UNDERWATER ENDOWMENT FUNDS

The University monitors endowment funds to identify those for which historical cost was more than market value. As of August 31, 2009, and 2008, respectively, the historical cost for such accounts was approximately $197.7 million and $42 million, and the market value totaled $172 million and $38.8 million. Associated unrealized losses are recorded in the unrestricted net assets classification.

6. Retirement Plans

The University maintains two contributory retirement plans for its eligible faculty and staff. The plans offer employees the choice of two investment company options, Teachers Insurance and Annuity Association (TIAA) and College Retirement Equities Fund (CREF), and the mutual funds offered by Fidelity Investments. The measurement date for plans is August 31. Participating employee and University contributions are immediately vested. The University contributed $47.7 million and $38.5 million to the two plans in 2009 and 2008, respectively. It expects to contribute $49.5 million to the two plans in 2010.

The University currently sponsors a health care plan permitting retirees to continue participation on a "pay-all" basis. The retiree contribution is based on the average per-capita cost of coverage for the plan's entire group of active employees and retirees rather than the per-capita cost for retirees only. Retirees are also eligible to participate in certain tuition reimbursement plans and may receive a payment for sick days accumulated at retirement. The accrued cost for postemployment benefits was $7.7 million and $7.1 million at August 31, 2009, and 2008, respectively, and is included in accounts payable and accrued expenses on the consolidated statements of financial position.

In 2007, the University implemented FASB Statement No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Benefit Plans." SFAS No. 158 requires an employer sponsoring one or more single-employer defined-benefit plans to recognize an asset or a liability in the statements of financial position for the plans' overfunded or underfunded status. The asset or liability is the difference between the fair value of plan assets and the related benefit obligation, defined as the projected benefit obligation for pension plans and the accumulated postretirement benefit obligation for other postretirement benefit plans such as a retiree health care plan. SFAS No. 158 also requires an employer to recognize actuarial gains or losses and prior service costs or credits in the statements of activities that arise during the period but are not components of net periodic benefit cost. In addition, an employer must measure defined-benefit plan assets and obligations as of the date of its fiscal year-end and make specified disclosures for the upcoming fiscal year.

The University funds the benefit costs as they are incurred. The accumulated postretirement benefit obligation (APBO) was as follows:

(in thousands of dollars)	*August 31, 2009*	*August 31, 2008*
Active employees not yet eligible	$4,955	$3,245
Active employees eligible	5,710	4,209
Retirees	2,308	1,996
Total	**$12,973**	**$9,450**

The following table sets forth the plan's change in benefit obligation:

(in thousands of dollars)	*August 31, 2009*	*August 31, 2008*
Benefit obligation at beginning of year	$9,450	$8,695
Service cost (benefits attributed to employee service during the year)	439	464
Interest cost on accumulated postretirement benefit obligation	642	525
Actuarial loss	3,001	218
Benefits paid	(1,242)	(1,185)
Contributions from participants	683	733
Benefit obligation at end of year	**$12,973**	**$9,450**

The following table sets forth the change in plan assets:

(in thousands of dollars)	*August 31, 2009*	*August 31, 2008*
Fair value of plan assets at beginning of year	—	—
Employer contribution	559	453
Benefits paid	(559)	(453)
Fair value of plan assets at end of year	**—**	**—**

The accrued benefit cost recognized in the consolidated statements of financial position, which is included in accounts payable and accrued expenses, was $13 million and $9.5 million at August 31, 2009, and 2008, respectively.

The components of the net periodic postretirement benefit cost were as follows:

(in thousands of dollars)	*August 31, 2009*	*August 31, 2008*
Service cost (benefits attributed to employee		
service during the year)	$439	$464
Interest cost on accumulated postretirement		
benefit obligation	642	525
Amortization of prior service cost	109	89
Amortization of unrealized loss	92	109
Total	**$1,282**	**$1,187**

The following tables present key actuarial assumptions used in determining APBO as of August 31, 2009, and 2008. First, the assumptions used to determine benefit obligations:

	August 31, 2009	*August 31, 2008*
Settlement (discount) rate	6%	7%
Weighted average rate of increase in future compensation levels	4%	4%
Current pre-65 health cost trend rate	7%	8%
Current post-64 health cost trend rate	7%	8%
Ultimate health care cost trend rate	5%	5%
Year when trend rate will reach ultimate trend rate	2011	2011

Next, the assumptions used to define net periodic benefit cost:

	August 31, 2009	*August 31, 2008*
Discount rate	7%	6.2%
Weighted average rate of increase in future compensation levels	4%	4%
Current pre-65 health cost trend rate	8%	9%
Current post-64 health cost trend rate	8%	9%
Ultimate health care cost trend rate	5%	5%
Year when trend rate will reach ultimate trend rate	2011	2011

A one-percentage-point change in assumed health care cost trend rates would have had these effects in fiscal year 2009:

(in thousands of dollars)	*1% point increase*	*1% point decrease*
Increase (decrease) in total of service and interest cost	$88	($76)
Increase (decrease) in postretirement benefit obligation	915	(795)

Estimated future benefit payments reflecting anticipated service, as appropriate, are expected to be paid as shown at right.

(in thousands of dollars)	
2010	$644
2011	717
2012	841
2013	945
2014	1,061
2015–2019	6,836
Total	**$11,044**

The University offers a deferred compensation plan under Internal Revenue Code 457(b) to a select group of management and highly compensated employees. There is no University contribution related to this deferred compensation plan. The University has recorded both an asset and a liability related to the deferred compensation plan that totaled $18.2 million and $16.8 million in fiscal years 2009 and 2008, respectively; these are included in investments and actuarial liability of annuities payable and deposits payable on the consolidated statements of financial position.

FASB Staff Position SFAS No. 106-2, "Accounting and Disclosure Requirement Related to the Medicare Prescription Drug, Improvements, and Modernization Act of 2003," requires that the University disclose the effects of the act and assess the impact of the Medicare Part D subsidy on the accumulated postretirement benefit obligation and net periodic postretirement benefit cost. Since the University chose not to pursue the subsidy, measures of the APBO or net periodic postretirement benefit cost do not reflect any amount associated with it in 2009 or prior years.

7. Land, Buildings, and Equipment

Land, buildings, and equipment consisted of the following:

(in thousands of dollars)	*August 31, 2009*	*August 31, 2008*
Land	$27,355	$27,355
Construction in progress	162,319	114,754
Buildings and leasehold improvements	1,744,632	1,658,042
Equipment	388,733	349,410
Accumulated depreciation	(886,812)	(800,013)
Total	**$1,436,227**	**$1,349,548**

The estimated cost to complete construction in progress at August 31, 2009, is $306.6 million. Costs included in construction in progress are future leasehold improvements and building and equipment capitalizations. Building costs are funded by loans, gifts (received or pledged), grants, and unrestricted funds.

Under the University's interest capitalization policy, actual interest expense incurred during the period of construction of an asset for University use is capitalized until that asset is substantially completed and ready for use. The capitalized cost is reflected in the total cost of the asset and depreciated over the useful life of the asset. Assets may include buildings and major equipment.

ASSET RETIREMENT OBLIGATIONS

Under FIN 47, the University records all known asset retirement obligations and changes to those obligations. Asset retirement obligations at August 31, 2008, were adjusted during 2009 as follows:

(in thousands of dollars)	*August 31, 2009*	*August 31, 2008*
Balance at beginning of year	$104,533	$108,926
Accretion expense	5,277	5,083
Revision in estimated cash flows	—	(9,476)
Balance at end of year	**$109,810**	**$104,533**

At August 31, 2009, the depreciation and accretion expenses were $408,000 and $5.3 million, respectively. At August 31, 2008, they were $431,000 and $5.1 million, respectively.

LEASE OBLIGATIONS

The University is obligated under numerous operating leases to pay base rent through the lease expiration dates. Operating leases consist primarily of leases for the use of real property and have terms expiring in various years through fiscal year 2025. Noncancelable real estate lease expenses allocated on a straight-line basis over the term of the leases totaled $8.4 million at August 31, 2009, and $6.8 million at August 31, 2008. The future minimum lease payments under noncancelable operating leases through August 31 of each period are as shown at right.

(in thousands of dollars)	
2010	$7,849
2011	7,387
2012	5,847
2013	5,678
2014 and thereafter	32,060
Total	**$58,821**

8. Allocation of Expenses

The University allocated depreciation, plant maintenance expenditures, and interest on indebtedness to the various functional expense categories in the consolidated statements of activities for the fiscal years ended August 31, 2009, and 2008. Those expenses have been distributed to the functional areas of the University as follows:

(in thousands of dollars)				*August 31, 2009*
	Accretion for ARO	**Depreciation**	**Plant maintenance**	**Interest on bond indebtedness**
Instruction	$746	$12,895	$19,807	$3,991
Research	1,249	21,615	33,203	6,690
Academic support	964	16,665	25,598	5,157
Student services	802	13,875	21,312	4,294
Institutional support	272	4,706	7,228	1,456
Auxiliary services	1,244	21,508	33,037	6,656
Total	**$5,277**	**$91,264**	**$140,185**	**$28,244**

(in thousands of dollars)				*August 31, 2008*
	Accretion for ARO	**Depreciation**	**Plant maintenance**	**Interest on bond indebtedness**
Instruction	$798	$13,792	$18,115	$3,597
Research	1,219	21,073	27,679	5,497
Academic support	984	17,016	22,350	4,438
Student services	473	8,180	10,744	2,134
Institutional support	337	5,816	7,640	1,517
Auxiliary services	1,272	21,981	28,869	5,733
Total	**$5,083**	**$87,858**	**$115,397**	**$22,916**

The allocations were based on the functional use of space on the University's campuses.

9. Self-Insurance Reserves and Other Contingencies

Reserves for losses under the University's self-insurance program, aggregating $26.2 million and $47.7 million at August 31, 2009, and 2008, respectively, include reserves for known losses and for losses incurred but not yet reported. A portion of the reserves pertaining to professional liability has been determined on a discounted present-value basis. The discount rate was 7.5 percent in fiscal years 2009 and 2008. Self-insurance reserves are based on estimates of historical loss experience, and while management believes that the reserves are adequate, the ultimate liabilities may be more or less than the amounts provided.

Under an agreement between the University and Northwestern Medical Faculty Foundation, a proportionate share of primary medical professional liability costs that arise out of events prior to November 1, 2004, is borne by NMFF. As of November 1, 2004, NMFF obtained excess medical liability coverage through another institution for all events after October 1, 2002, and reported after November 1, 2004. As of August 31, 2009, and 2008, there were no accounts receivable from NMFF related to professional liability insurance costs.

Under a borrowing agreement with a lending agency in effect through June 30, 2008, the University had authority to borrow monies for the purpose of originating student loans that when fully disbursed may be sold to the lending agency; no monies were advanced in fiscal year 2008 or 2009. Additionally, the University has contracted to service the loans sold to the lending agency under the currently existing agreement; these totaled $178.1 million at August 31, 2009.

Service revenues are the excess of the actual interest collected above the agreed-upon warehouse fees on the serviced loans. The University manages the program to break even and generates no servicing assets or liabilities through these activities. The University guarantees these loans against default up to 10 percent of the original domestic loan portfolio and 30 percent of the original international amounts. The maximum future total payments are $20.9 million as of August 31, 2009. At August 31, 2009, and 2008, $265,000 and $315,000, respectively, were reserved in anticipation of future defaults. Notes receivable on the consolidated statements of position are shown net of these reserves in fiscal years 2009 and 2008.

In August 2009, the University, as originating lender, began participation in a student loan securitization program. It sold $65 million of student loans to a school trust; the University issued University guaranteed notes, which were purchased by a funding trust that procures financing to support the lending program. The program is managed to break even and generate no servicing assets or liabilities. Guaranteed notes totaled $65 million as of August 31, 2009, and $97,000 was reserved in anticipation of future defaults. Notes receivable on the consolidated statements of position are shown net of this reserve in fiscal year 2009.

From time to time, various claims and suits generally incidental to the conduct of normal business are pending or may arise against the University. It is the opinion of management of the University, after taking into account insurance coverage, that any losses from the resolution of pending litigation should not have a material effect on the University's financial position or results of operations.

All funds expended in connection with government grants and contracts are subject to audit by government agencies. While any ultimate liability from audits of government grants and contracts by government agencies cannot be determined at present, management believes that it should not have a material effect on the University's financial position or results of operations.

10. Natural Classification of Expenses

Operating expenses incurred in the fiscal years ended August 31, 2009, and 2008, were as follows:

(in thousands of dollars)	*August 31, 2009*	*August 31, 2008*
Salaries, wages, and benefits	$804,594	$790,421
Services and professional fees	268,253	217,435
Supplies	99,871	84,676
Travel and promotion	75,527	71,485
Trademark and royalty fees	34,725	142,377
Other expenses	26,094	27,370
Maintenance, utilities, and equipment	154,294	113,414
Accretion for asset retirement obligations	5,277	5,083
Interest on bond indebtedness	28,244	22,916
Depreciation	91,264	87,858
Total	**$1,588,143**	**$1,563,035**

11. Subsequent Event

Pursuant to FASB SFAS No. 165, "Subsequent Events," the University has evaluated subsequent events through January 20, 2010, the date when financial statements were available to be issued. It did not identify any subsequent events to be disclosed.