LUTHER COLLEGE
Decorah, Iowa

CONSOLIDATED FINANCIAL STATEMENTS
Including Independent Auditors' Report

As of and for the Years Ended May 31, 2018 and 2017

LUTHER COLLEGE

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INDEPENDENT AUDITORS' REPORT

To the Board of Regents
Luther College
Decorah, Iowa

We have audited the accompanying consolidated financial statements of Luther College and subsidiary (the "College"), which comprise the consolidated statements of financial position as of May 31, 2018 and 2017, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated 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 audits to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Luther College and subsidiary as of May 31, 2018 and 2017, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Baker Tilly Virchow Krause, LLP

Minneapolis, Minnesota
September 17, 2018

LUTHER COLLEGE

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
As of May 31, 2018 and 2017

ASSETS

	2018	2017
Cash and cash equivalents	$ 15,046,238	$ 17,809,103
Student accounts receivable, net of allowance for doubtful accounts of $149,000 in 2018 and $170,000 in 2017	258,646	175,211
Government grants receivable	150,387	105,150
Contributions receivable, net (Note 5)	3,064,000	4,397,000
Other receivables	521,215	692,315
Inventories	517,147	473,214
Prepaid expenses and other assets	486,051	413,729
Investments		
Short term investments	6,558,893	6,405,471
Marketable securities (Note 6)	10,054,560	10,148,673
Mortgages and contracts receivable	1,916,000	1,916,000
Real estate	299,034	455,035
Endowment (Note 7)	165,853,626	157,096,112
Beneficial interest in funds held in trust	2,211,457	2,145,824
Cash surrender value of life insurance	5,419,190	5,270,937
Student notes receivable, net (Note 8)	6,218,847	5,953,358
Interest rate swap asset (Note 14)	338,998	
Cash restricted for plant acquisitions	2,740,813	4,816,857
Construction in progress (Note 9)	1,630,376	440,263
Property, plant and equipment, net (Note 10)	76,384,544	79,528,655
TOTAL ASSETS	$ 299,670,022	$ 298,242,907

LIABILITIES AND NET ASSETS

	2018	2017
LIABILITIES		
Accounts payable	$ 1,691,202	$ 1,889,086
Accrued liabilities (Note 11)	8,900,475	9,602,641
Deferred revenue	1,331,385	1,460,434
Asset retirement obligations (Note 1)	2,474,655	2,351,216
Capital lease obligation (Note 12)	577,092	635,877
Interest rate swap liability (Note 14)		1,470,652
Long term debt (Note 13)	26,733,947	28,343,039
Annuities payable	4,922,307	5,066,689
Deposits held in custody for others	423,113	409,239
Government grants refundable (Note 8)	5,023,293	5,154,711
Total Liabilities	52,077,469	56,383,584
NET ASSETS		
Unrestricted (Note 3)	95,885,043	95,643,168
Temporarily restricted (Note 3)	34,905,303	34,580,368
Permanently restricted (Note 3)	116,802,207	111,635,787
Total Net Assets	247,592,553	241,859,323
TOTAL LIABILITIES AND NET ASSETS	$ 299,670,022	$ 298,242,907

See accompanying notes to consolidated financial statements.

LUTHER COLLEGE

CONSOLIDATED STATEMENT OF ACTIVITIES
For the Year Ended May 31, 2018
(With Comparative Totals for 2017)

	2018					2017
	Operating	Long-Term Investment	Plant	Subsidiary	Total	Total
UNRESTRICTED NET ASSETS						
Revenues, Gains and Other Support						
Tuition and fees	$ 82,118,960	$ -	$ -	$ -	$ 82,118,960	$ 84,742,811
Less: Scholarships and grants	(48,159,058)	-	-	-	(48,159,058)	(47,162,048)
Net tuition and fees	33,959,902	-	-	-	33,959,902	37,580,763
Government grants and contracts	1,202,183	-	19,949	-	1,222,132	1,250,682
Private gifts and grants	5,581,213	-	542,323	-	6,123,536	5,381,517
Investment income	129,267	-	40,673	5,116	175,056	133,140
Endowment income	-	437,100	-	-	437,100	341,999
Gain on investments	-	986,910	2,193	-	989,103	1,446,736
Spending allowance appropriation	6,490,539	(668,158)	-	-	5,822,381	5,777,064
Other sources	1,730,824	-	-	228,720	1,959,544	2,358,150
Sales and services of educational activities	1,053,895	-	-	-	1,053,895	1,029,334
Sales and services of auxiliary enterprises	19,060,983	-	-	-	19,060,983	20,870,355
Gain on swap agreement valuation	-		610,451	-	610,451	675,896
Actuarial adjustment	-	327,164	-	-	327,164	97,415
	69,208,806	1,083,016	1,215,589	233,836	71,741,247	76,943,051
Net assets released from restrictions	1,297,760	195,925	2,466,626	-	3,960,311	1,812,965
Total Revenues, Gains and Other Support	70,506,566	1,278,941	3,682,215	233,836	75,701,558	78,756,016
Expenses						
Program Expenses						
Instruction	27,539,016	-	3,185,882	-	30,724,898	30,566,367
Research	609,220	-	33,140	-	642,360	734,639
Public service	450,803	-	2,481	-	453,284	555,687
Academic support	3,658,613	-	864,733	-	4,523,346	4,709,800
Student services	12,460,271	-	705,108	-	13,165,379	12,905,561
Auxiliary enterprises	12,165,935	-	2,468,805	-	14,634,740	17,304,492
Support Expenses						
Institutional support	10,615,656	-	333,951	-	10,949,607	12,528,660
Subsidiary	-	-	-	366,069	366,069	332,537
Allocable Expenses						
Operation and maintenance of plant	7,480,241	-		-	7,480,241	7,876,654
Depreciation and amortization	-	-	6,563,833	322,059	6,885,892	6,790,551
Accretion	-	-	123,439	-	123,439	117,282
Interest	-	-	884,660	16,022	900,682	1,180,289
Less: Allocated expenses	(7,480,241)	-	(7,571,932)	(338,081)	(15,390,254)	(15,964,776)
Total Expenses	67,499,514	-	7,594,100	366,069	75,459,683	79,637,743
Change in Unrestricted Net Assets	3,007,052	1,278,941	(3,911,885)	(132,233)	241,875	(881,727)

LUTHER COLLEGE

CONSOLIDATED STATEMENT OF ACTIVITIES
For the Year Ended May 31, 2018
(With Comparative Totals for 2017)

	2018					
	Operating	Long-Term Investment	Plant	Subsidiary	Total	2017 Total
TEMPORARILY RESTRICTED NET ASSETS						
Gifts and grants	$ 496,062	$ -	$ 86,881	$ -	$ 582,943	$ 1,545,394
Endowment income	-	2,081,394	-	-	2,081,394	1,772,297
Gain on investments	-	6,376,933	-	-	6,376,933	9,152,701
Spending allowance appropriation	355,560	(5,213,189)	-	-	(4,857,629)	(4,864,492)
Actuarial adjustment	-	97,366	-	-	97,366	55,882
Other sources	4,239	-	-	-	4,239	5,744
Net assets released from restrictions	(1,297,760)	(195,925)	(2,466,626)	-	(3,960,311)	(1,812,965)
Change in Temporarily Restricted Net Assets	(441,899)	3,146,579	(2,379,745)	-	324,935	5,854,561
PERMANENTLY RESTRICTED NET ASSETS						
Private gifts	-	4,043,397	-	-	4,043,397	2,592,436
Endowment income	-	390,821	-	-	390,821	340,851
Gain on investments	-	1,197,462	-	-	1,197,462	1,760,264
Spending allowance appropriation	-	(964,752)	-	-	(964,752)	(912,572)
Gain on investments (FHIT)	-	64,993	-	-	64,993	154,514
Actuarial adjustment	-	434,499	-	-	434,499	730,350
Change in Permanently Restricted Net Assets	-	5,166,420	-	-	5,166,420	4,665,843
TRANSFERS						
Transfer for debt service	(2,644,465)	-	2,644,465	-	-	-
Nonmandatory transfers	436,257	(3,505,440)	3,069,183	-	-	-
Total Transfers	(2,208,208)	(3,505,440)	5,713,648	-	-	-
CHANGE IN NET ASSETS	356,945	6,086,500	(577,982)	(132,233)	5,733,230	9,638,677
NET ASSETS - Beginning of Year	14,798,950	173,326,323	53,196,723	537,327	241,859,323	232,220,646
NET ASSETS - END OF YEAR	$ 15,155,895	$ 179,412,823	$ 52,618,741	$ 405,094	$ 247,592,553	$ 241,859,323

LUTHER COLLEGE

CONSOLIDATED STATEMENT OF ACTIVITIES
For the Year Ended May 31, 2017

	2017				
	Operating	Long-Term Investment	Plant	Subsidiary	Total
UNRESTRICTED NET ASSETS					
Revenues, Gains and Other Support					
Tuition and fees	$ 84,742,811	$ -	$ -	$ -	$ 84,742,811
Less: Scholarships and grants	(47,162,048)	-	-	-	(47,162,048)
Net tuition and fees	37,580,763	-	-	-	37,580,763
Government grants and contracts	1,250,682	-	-	-	1,250,682
Private gifts and grants	5,266,694	-	114,823	-	5,381,517
Investment income	98,868	-	31,249	3,023	133,140
Endowment income	-	341,999	-	-	341,999
Gain on investments	-	1,441,361	5,375	-	1,446,736
Spending allowance appropriation	6,200,712	(423,648)	-	-	5,777,064
Other sources	2,129,801	-	-	228,349	2,358,150
Sales and services of educational activities	1,029,334	-	-	-	1,029,334
Sales and services of auxiliary enterprises	20,870,355	-	-	-	20,870,355
Gain on swap agreement valuation	-	-	675,896	-	675,896
Actuarial adjustment	-	97,415	-	-	97,415
	74,427,209	1,457,127	827,343	231,372	76,943,051
Net assets released from restrictions	1,237,891	-	575,074	-	1,812,965
Total Revenues, Gains and Other Support	75,665,100	1,457,127	1,402,417	231,372	78,756,016
Expenses					
Program Expenses					
Instruction	27,376,271	-	3,190,096	-	30,566,367
Research	682,692	-	51,947	-	734,639
Public service	555,403	-	284	-	555,687
Academic support	3,785,111	-	924,689	-	4,709,800
Student services	12,324,458	-	581,103	-	12,905,561
Auxiliary enterprises	14,657,942	-	2,646,550	-	17,304,492
Support Expenses					
Institutional support	11,570,205	-	958,455	-	12,528,660
Subsidiary	-	-	-	332,537	332,537
Allocable Expenses					
Operation and maintenance of plant	7,876,654	-	-	-	7,876,654
Depreciation and amortization	-	-	6,468,491	322,060	6,790,551
Accretion	-	-	117,282	-	117,282
Interest	-	-	1,160,297	19,992	1,180,289
Less: Allocated expenses	(7,876,654)	-	(7,746,070)	(342,052)	(15,964,776)
Total Expenses	70,952,082	-	8,353,124	332,537	79,637,743
Change in Unrestricted Net Assets	4,713,018	1,457,127	(6,950,707)	(101,165)	(881,727)

LUTHER COLLEGE

CONSOLIDATED STATEMENT OF ACTIVITIES
For the Year Ended May 31, 2017

	2017				
	Operating	Long-Term Investment	Plant	Subsidiary	Total
TEMPORARILY RESTRICTED NET ASSETS					
Gifts and grants	$ 7,998	$ -	$ 1,537,396	$ -	$ 1,545,394
Endowment income	-	1,772,297	-	-	1,772,297
Gain on investments	-	9,152,701	-	-	9,152,701
Spending allowance appropriation	338,517	(5,203,009)	-	-	(4,864,492)
Actuarial adjustment	-	55,882	-	-	55,882
Other sources	5,744	-	-	-	5,744
Net assets released from restrictions	(1,237,891)	-	(575,074)	-	(1,812,965)
Change in Temporarily Restricted Net Assets	(885,632)	5,777,871	962,322	-	5,854,561
PERMANENTLY RESTRICTED NET ASSETS					
Private gifts	-	2,592,436	-	-	2,592,436
Endowment income	-	340,851	-	-	340,851
Gain on investments	-	1,760,264	-	-	1,760,264
Spending allowance appropriation	-	(912,572)	-	-	(912,572)
Gain on investments (FHIT)	-	154,514	-	-	154,514
Actuarial adjustment	-	730,350	-	-	730,350
Change in Permanently Restricted Net Assets	-	4,665,843	-	-	4,665,843
TRANSFERS					
Transfer for debt service	(2,751,964)	19,740	2,732,224	-	-
Nonmandatory transfers	(1,998,820)	450,148	1,548,672	-	-
Total Transfers	(4,750,784)	469,888	4,280,896	-	-
CHANGE IN NET ASSETS	(923,398)	12,370,729	(1,707,489)	(101,165)	9,638,677
NET ASSETS - Beginning of Year	15,722,348	160,955,594	54,904,212	638,492	232,220,646
NET ASSETS - END OF YEAR	$ 14,798,950	$ 173,326,323	$ 53,196,723	$ 537,327	$ 241,859,323

LUTHER COLLEGE

CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Years Ended May 31, 2018 and 2017

	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	$ 5,733,230	$ 9,638,677
Adjustments to reconcile change in net assets to net cash flows from operating activities		
Depreciation, amortization, and accretion	7,009,331	6,907,832
Loss on disposal of property	22,168	147,054
Gain on interest rate swap valuation	(610,451)	(675,896)
(Gain) loss on investments, net	(8,823,785)	(13,038,805)
Decrease (increase) in beneficial interest in funds held in trust	(65,633)	(155,337)
Noncash contributions of investment assets	(145,000)	-
Actuarial adjustment of annuities payable	(91,599)	(101,991)
Loan cancellations, reinstatements and write-offs	129,124	40,448
Changes in assets and liabilities		
Receivables	(83,435)	10,045
Contributions receivable for operations	(96,578)	843,000
Accrued interest, grants and other receivables	125,863	260,873
Prepaid expenses, inventories, and other assets	(264,508)	(181,327)
Accounts payable and accrued liabilities	(828,198)	(741,674)
Deferred revenue and deposits held for others	(115,175)	25,402
Asset retirement obligation	-	(22,175)
Contributions restricted for loans, long-term investment and plant	(4,692,550)	(4,244,655)
Investment income restricted for reinvestment	(390,821)	(340,851)
Cash Flows from Operating Activities	(3,188,017)	(1,629,380)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of investments	(26,132,550)	(65,729,865)
Sales of investments	26,440,513	66,790,205
Decrease (increase) in mortgages and contracts receivable, net of repayments	-	(1,419,999)
Purchases of property, plant and equipment	(5,002,337)	(2,633,218)
Disbursements of loans to students	(1,283,829)	(971,680)
Repayments of loans from students	889,216	1,097,547
Cash Flows from Investing Activities	(5,088,987)	(2,867,010)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from issuance of long-term debt	2,983	-
Interest rate swap termination payment	(1,199,199)	-
Payments of principal on indebtedness	(1,635,652)	(1,622,707)
Payments on capital lease obligations	(58,785)	(56,709)
Receipt of investment income restricted for reinvestment	390,821	340,851
Contributions and grants received restricted for loans, long-term investment and plant	6,122,128	4,778,655
Increase in cash held for plant acquisitions	2,076,044	(940,839)
Decrease in government grants refundable	(131,418)	(50,318)
Proceeds from issuance of split-interest agreements	127,397	62,000
Payments to annuitants	(180,180)	(193,081)
Cash Flows from Financing Activities	5,514,139	2,317,852
Change in Cash and Cash Equivalents	(2,762,865)	(2,178,538)
CASH AND CASH EQUIVALENTS - Beginning of year	17,809,103	19,987,641
CASH AND CASH EQUIVALENTS - END OF YEAR	$ 15,046,238	$ 17,809,103

	2018	2017
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Interest paid, net of capitalized amounts of $22,900 in 2018 and $30,400 in 2017	$ 924,069	$ 1,182,198
Payments on swap settlements	241,483	621,942
NONCASH INVESTMENT AND FINANCING ACTIVITIES		
Property, plant and equipment acquired through accounts payable	76,125	147,977
Bond proceeds used to refinance Series 2011 Bonds	(20,830,000)	-
Bond issuance costs paid from bond proceeds	(112,017)	-

See accompanying notes to consolidated financial statements.

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

Luther College is an institution of higher education affiliated with the Evangelical Lutheran Church in America. The accounting policies of the College reflect practices common to universities and colleges and conform to accounting principles generally accepted in the United States of America. The more significant accounting policies are summarized below:

Consolidation – The consolidated financial statements include the accounts of Luther College and Luther College Ventures, Inc. (collectively referred to as the "College"). Luther College owns 100% interest in Luther College Ventures, Inc. Luther College Ventures, Inc. was formed on November 3, 2010 and is the sole member of Luther College Wind Energy Project, LLC. Luther College Wind Energy Project, LLC was formed on July 13, 2005 to construct a wind turbine. The wind turbine was placed in service on October 31, 2011. All material transactions and balances between the entities have been eliminated in the consolidated financial statements.

Net Asset Classifications – For purposes of financial reporting, the College classifies resources into three net asset categories pursuant to any donor-imposed restrictions and applicable law. Accordingly, the net assets of the College are classified in the accompanying financial statements in the categories that follow:

Permanently Restricted Net Assets – Net assets subject to donor-imposed stipulations that they be maintained permanently by the College. Generally, the donors of these assets permit the College to use all or part of the income earned on related investments for general or specific purposes.

Temporarily Restricted Net Assets – Net assets subject to donor-imposed stipulations that will be met by action of the College and/or the passage of time.

Unrestricted Net Assets – Net assets not subject to donor-imposed stipulations.

Revenues from sources other than contributions are generally reported as increases in unrestricted net assets. Investment income received with donor-imposed restrictions that are met in the same year as received are reported as revenues of the unrestricted net asset class. In all other cases, income earned on donor restricted funds is initially classified as temporarily restricted net assets and is reclassified as unrestricted net assets when expenses are incurred for their intended purpose. Expenses are reported as decreases in unrestricted net assets.

Contributions, including unconditional promises to give, are recognized as revenues in the period received and are reported as increases in the appropriate categories of net assets in accordance with donor restrictions. Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassification between the applicable classes of net assets. However, contributions received with donor-imposed restrictions that are met in the same year as received are initially reported as revenues of the unrestricted net asset class. Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met. The College had conditional promises to give of $900,000 and $1,050,000 at May 31, 2018 and 2017, respectively.

Contributions of property and equipment without donor stipulations concerning the use of such long-lived assets are reported as unrestricted revenues. Contributions of cash or other assets to be used to acquire property and equipment are reported as temporarily restricted revenues; the restrictions are considered to be released at the time such long-lived assets are placed in service.

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

Net Asset Classifications (cont.) **–** In the absence of donor stipulations or law to the contrary, losses on the investments of a donor-restricted endowment fund reduce temporarily restricted net assets to the extent that donor-imposed temporary restrictions on net appreciation of the fund have not been met before the loss occurs. Any remaining loss reduces unrestricted net assets. If losses reduce the assets of a donor-restricted endowment fund below the level required by the donor stipulations or law, gains that restore the fair value of the assets of the endowment fund to the required level are classified as increases in unrestricted net assets.

Gains and losses on investments of endowment funds created by a board designation of unrestricted funds are included in changes in unrestricted net assets.

***Cash Equivalents* –** The College considers all highly liquid investments, except for those held for plant and long-term investments, with a maturity of three months or less when purchased to be cash equivalents. Certain cash held by the College is restricted for the Perkins Loan Fund.

***Student Accounts Receivable and Other Receivables* –** Student accounts receivable are carried at the unpaid balance of the original amount billed to students less an estimate made for doubtful accounts which is based on a review of all outstanding amounts. Management determines the allowance for doubtful accounts by identifying troubled accounts and by using historical experience applied to an aging of accounts. Student accounts are written off when deemed uncollectible. Recoveries of student accounts previously written off are recorded when received. Receivables are generally unsecured. Other receivables include campus charges due from employees of $3,769 and $1,876 at May 31, 2018 and 2017, respectively.

***Inventories* –** All inventories are valued at cost.

***Deferred Debt Acquisition Costs* –** Costs of debt issuance are deferred and amortized over the term of the related indebtedness. The unamortized balance is included as a reduction to long-term debt on the statement of financial position.

***Physical Plant and Equipment* –** Physical plant assets are stated at cost at the date of acquisition less accumulated depreciation. The College depreciates its assets on the straight-line basis over estimated useful lives as follows: buildings – 30 years; improvements – 15 years; equipment and library books – 10 years; computer and vehicles – 4 years. Normal repair and maintenance expenses are charged to operations as incurred. The College capitalizes physical plant additions in excess of $10,000 for 2018 and $5,000 for 2017.

***Deferred Revenue* –** Certain revenue related to summer courses and programs is deferred and recognized as revenue in the same period expenses are recognized. Students are generally billed for courses and programs prior to the start of the course or program.

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

Asset Retirement Obligations – The College recognizes the fair value of a liability for legal obligations associated with asset retirements in the period in which it is incurred, if a reasonable estimate of the fair value of the obligation can be made. When the liability is initially recorded, the cost of the retirement obligation is capitalized by increasing the carrying value of the related asset. Over time, the liability is accreted to its present value each year and the capitalized cost associated with the retirement obligation is depreciated over the useful life of the related asset. Upon settlement of the obligation, any difference between the cost to settle the asset retirement obligation and the liability recorded is recognized as a gain or loss in the statement of activities. The College reviews its estimates annually and adjusts the recorded liability as needed.

Substantially all of the College’s asset retirement obligations relate to estimated costs to remove asbestos from campus facilities. The estimate of the losses that are probable for asbestos removal was calculated using the expected cash flow approach and based on an inventory of the College's long-lived assets combined with an estimate of the current market prices to remove the asbestos. The College utilized a credit-adjusted risk-free rate to discount the asset retirement obligation.

Changes in the accrual for asset retirement obligations during the years ended May 31, 2018 and 2017 are as follows:

	2018	2017
Balance, Beginning of the year	$ 2,351,216	$ 2,256,109
Abatements	-	(22,175)
Accretion expense	123,439	117,282
Balance, End of the year	$ 2,474,655	$ 2,351,216

Grants to Specified Students – Amounts received from state and federal agencies designated for the benefit of specified students are considered agency transactions and, therefore, are not reflected as revenues and expenses of the College.

Government Grants Refundable – Funds provided by the United States government under the Federal Perkins Loan Program are loaned to qualified students and may be reloaned after collections. These funds are ultimately refundable to the government and are included as liabilities in the statements of financial position. Revenues from other government grants are recognized as they are earned in accordance with the agreement. Any funding received before it is earned is recorded as a refundable advance. Expenses incurred before cash is received are recorded as receivables.

Tuition and Fees and Auxiliary Revenues – Tuition revenue is recognized in the period the classes are provided. Revenue from auxiliary enterprises is recognized when goods or services are provided. Financial assistance in the form of scholarships and grants that cover a portion of tuition, living and other costs is reflected as a reduction of tuition and fees revenues.

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

Fund-Raising and Advertising Expenses – Fund-raising expenses totaled approximately $2,482,000 and $2,524,000 for the years ended May 31, 2018 and 2017, respectively. Advertising expenses totaled approximately $551,000 and $606,000 for the years ended May 31, 2018 and 2017, respectively. Advertising costs are expensed when incurred.

Functional Allocation of Expenses – The costs of providing the various programs and other activities have been summarized on a functional basis in the statement of activities. Accordingly, certain expenses have been allocated among the programs and supporting services benefited.

Income Tax Status – The Internal Revenue Service has determined that the College is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code. The College is also exempt from state income tax. However, any unrelated business income may be subject to taxation. Luther College Ventures, Inc. is organized as a C corporation pursuant to the provisions of the Internal Revenue code. As of May 31, 2018 and 2017, Luther College Ventures, Inc. had recorded tax deductions, principally depreciation, in excess of financial statement expenses. Income tax benefits of $80,000 in both 2018 and 2017 are included in the subsidiary’s institutional support expenses. No tax expense was recorded for other College operations.

The College follows the accounting standards for contingencies in evaluating uncertain tax positions. This guidance prescribes recognition threshold principles for the financial statement recognition of tax positions taken or expected to be taken on a tax return that are not certain to be realized. No liability has been recognized by the College for uncertain tax positions as of May 31, 2018 and 2017. The College’s tax returns are subject to review and examination by federal and state authorities.

Impairment of Long-Lived Assets – The College reviews long-lived assets, including property and equipment and intangible assets, for impairment whenever events or changes in business circumstances indicate that the carrying amount of an asset may not be fully recoverable. An impairment loss would be recognized when the estimated future cash flows from the use of the asset are less than the carrying amount of that asset. To date, there have been no such losses.

Use of Estimates – 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. Actual results could differ from those estimates.

Reclassifications – Certain amounts appearing in the 2017 financial statements have been reclassified to conform with the 2018 presentation. The reclassifications have no effect on the reported amounts of total net assets or change in total assets.

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

New Pronouncements – In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, *Revenue from Contracts with Customers*. This new accounting guidance outlines a single comprehensive model for entities to use in accounting for revenue from contracts with customers. For public business entities, including not-for-profit organizations that have issued, or are a conduit bond obligor for, securities that are traded, listed or quoted on an exchange or an over-the-counter market, ASU No. 2014-09 is effective for fiscal years beginning after December 15, 2017 (fiscal year 2019). The College is assessing the impact this standard will have on its financial statements.

In February 2016, FASB issued ASU No. 2016-02, *Leases*. ASU No. 2016-02 was issued to increase transparency and comparability among entities. Lessees will need to recognize nearly all lease transactions (other than leases that meet the definition of a short-term lease) on the statement of financial position as a lease liability and a right-of-use asset (as defined). Lessor accounting under the new guidance will be similar to the current model. For public business entities, including not-for-profit organizations that have issued, or are a conduit bond obligor for, securities that are traded, listed or quoted on an exchange or an over-the-counter market, ASU No. 2016-02 is effective for fiscal years beginning after December 15, 2018 (fiscal year 2020). Early application is permitted. Upon adoption, lessees and lessors will be required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach, which includes a number of optional practical expedients that entities may elect to apply. The College is assessing the impact this standard will have on its financial statements.

In August 2016, FASB issued ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. The new guidance improves and simplifies the current net asset classification requirements and information presented in financial statements and notes that is useful in assessing a not-for-profit's liquidity, financial performance and cash flows. ASU 2016-14 is effective for fiscal years beginning after December 15, 2017 (fiscal year 2019), with early adoption permitted. ASU 2016-14 is to be applied retroactively with transition provisions. The College is assessing the impact this standard will have on its financial statements.

During June 2018, the FASB issued ASU 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. The guidance is intended to clarify and improve accounting guidance for contributions received and contributions made. The amendments in this ASU should assist entities in (1) evaluating whether transactions should be accounted for as contributions (nonreciprocal transactions) or as exchange (reciprocal) transactions subject to other guidance and (2) determining whether a contribution is conditional. For not-for-profit entities that have conduit debt, ASU 2018-08 is effective for fiscal years beginning after June 15, 2018 (fiscal year 2020). The College is currently assessing the impact that ASU 2018-08 will have on its financial statements.

NOTE 2 - FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair Value Hierarchy – Fair value is defined in the accounting guidance as the exchange price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the assets or liability in an orderly transaction between market participants at the measurement date. Under this guidance, a three-level hierarchy is used for fair value measurements which is based on the transparency of information, such as the pricing source, used in the valuation of an asset or liability as of the measurement date.

Financial instruments measured and reported at fair value are classified and disclosed in one of the following three categories.

Level 1 - Inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity can access at the measurement date.

Level 2 - Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. This includes quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, or market-corroborated inputs.

Level 3 - Inputs are unobservable for the asset or liability. Unobservable inputs reflect the assumptions that market participants would use in pricing the asset or liability (including assumptions about risk) using the best information available in the circumstances, which may include using the reporting entity's own data.

Assets and Liabilities

Level 1 - Level 1 assets include investments in publicly traded domestic and international mutual funds for which quoted prices are readily available or that trade with sufficient frequency and volume to enable the College to obtain pricing information on an ongoing basis.

Level 2 - Level 2 assets and liabilities include interest rate exchange agreements as the fair value is based on observable inputs to a valuation model (interest rates, credit spreads, etc.) which take into account the present value of the estimated future cash flows and credit valuation adjustments.

Level 3 - Level 3 assets include beneficial interest in funds held in trust by others as the fair values are estimated using an income approach by calculating the present value of the future distributions expected to be received based on a combination of Level 2 inputs (interest rates and yield curves) and significant unobservable inputs (entity specific estimates of cash flows). Since the College has an irrevocable right to receive the income earned from the trust's assets, the fair value of the College's beneficial interest is estimated to approximate the fair value of the trusts' assets.

Certain fixed income securities and alternative investments are measured at fair value using the net asset value (NAV) per share (or its equivalent) of such investment funds as a practical expedient for fair value. The College has estimated the fair value of these funds by using the net asset value provided by the investee. Under accounting guidance, investments measured using the net asset value per share (or its equivalent) practical expedient are not classified in the fair value hierarchy.

There have been no changes in the techniques and inputs used as of May 31, 2018 and 2017.

NOTE 2 - FAIR VALUE OF FINANCIAL INSTRUMENTS (cont.)

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

While the College 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 table summarizes financial instruments measured at fair value on a recurring basis by the fair value hierarchy as of May 31, 2018:

	Total	Level 1	Level 2	Level 3
ASSETS				
Mutual funds				
U.S. equity funds	$ 44,262,059	$ 44,262,059	$ –	$ –
Non-U.S. equity funds	43,496,992	43,496,992	–	–
U.S. fixed income funds	34,496,733	34,496,733	–	–
Non-U.S. fixed income funds	314,916	314,916	–	–
Beneficial interest in funds held in trust	2,211,457	–	–	2,211,457
Interest rate exchange agreements	338,998	–	338,998	–
Subtotal assets by valuation hierarchy	125,121,155	$ 122,570,700	$ 338,998	$ 2,211,457
Investments measured using NAV				
Alternative investments				
Hedge funds	3,565,226			
Private equity funds	7,345,774			
Real estate partnerships	123,395			
Real estate funds (REIT)	1,835			
Funds of funds	21,301,341			
Partnerships, real assets	4,453,549			
Subtotal assets by NAV	36,791,120			
Total assets at fair value	161,912,275			
Investments at cost				
Short term investments	6,558,893			
Short term endowment investments	16,546,360			
Real estate investments	299,034			
Real estate endowment investments	6			
Mortgage and contract receivable	1,916,000			
	25,320,293			
Less: Interest rate exchange agreement	(338,998)			
Total investments	$ 186,893,570			

NOTE 2 - FAIR VALUE OF FINANCIAL INSTRUMENTS (cont.)

The following table summarizes financial instruments measured at fair value on a recurring basis by the fair value hierarchy as of May 31, 2017:

	Total	Level 1	Level 2	Level 3
ASSETS				
Mutual funds				
U.S. equity funds	$ 40,454,337	$ 40,454,337	$ –	$ –
Non-U.S. equity funds	43,405,575	43,405,575	–	–
U.S. fixed income funds	27,051,276	27,051,276	–	–
Non-U.S. fixed income funds	323,669	323,669	–	–
Beneficial interest in funds held in trust	2,145,824	–	–	2,145,824
Subtotal assets by valuation hierarchy	113,380,681	$ 111,234,857	$ –	$ 2,145,824
Investments measured using NAV				
Fixed income securities	5,661,098			
Alternative investments				
Hedge funds	3,419,131			
Private equity funds	6,341,882			
Real estate partnerships	321,424			
Real estate funds (REIT)	16,187			
Funds of funds	20,033,285			
Partnerships, real assets	4,096,929			
Subtotal assets by NAV	39,889,936			
Total assets at fair value	153,270,617			
Investments at cost				
Short term investments	6,405,471			
Short term endowment investments	15,508,886			
Real estate investments	455,035			
Real estate endowment investments	610,006			
Mortgage and contract receivable	1,916,000			
Equity endowment investments	1,100			
	24,896,498			
Total investments	$ 178,167,115			
LIABILITIES				
Interest rate exchange agreements	$ 1,470,652	$ –	$ 1,470,652	$ –

NOTE 2 - FAIR VALUE OF FINANCIAL INSTRUMENTS (cont.)

The following table presents a reconciliation of the statement of financial position amounts for financial instruments measured at fair value on a recurring basis using significant unobservable inputs (level 3) for the year ended May 31, 2018.

	Balances May 31, 2017	Net realized and unrealized gains included in change in net assets	Purchases	Sales	Net transfers in (out) of Level 3	Balances May 31, 2018
Beneficial interest in funds held in trust	$ 2,145,824	$ 65,633	$ –	$ –	$ –	$ 2,211,457

The amount of total gain for the periods included in change in net assets attributable to the change in unrealized gains relating to financial instruments still held at May 31, 2018.	$ 65,633

The following table presents a reconciliation of the statement of financial position amounts for financial instruments measured at fair value on a recurring basis using significant unobservable inputs (level 3) for the year ended May 31, 2017.

	Balances May 31, 2016	Net realized and unrealized gains included in change in net assets	Purchases	Sales	Net transfers in (out) of Level 3	Balances May 31, 2017
Beneficial interest in funds held in trust	$ 1,990,487	$ 155,337	$ –	$ –	$ –	$ 2,145,824

The amount of total gain for the periods included in change in net assets attributable to the change in unrealized gains relating to financial instruments still held at May 31, 2017.	$ 155,337

NOTE 2 - FAIR VALUE OF FINANCIAL INSTRUMENTS (cont.)

The College's interests in many of its partnership investments represent commitments that are not subject to redemption; instead the College is a limited partner in funds that invest in private companies or properties, or pursue specific investment strategies. The nature of these investments is that distributions are received through the liquidation of the underlying assets of the partnership. The "NAV" reported by each fund is used as a "practical expedient" to estimate the fair value of the College's interest therein, unless management has deemed the "NAV" to be an inappropriate representation of the fair value under the College's valuation policy.

A summary of the significant categories of such investments and their attributes is as follows:

	Private Equity Funds	Real Assets	Hedge Funds and Funds of Funds	Fund of Funds - Balanced Fund with Options Strategy	Fixed Income Securities
Fair value, May 31, 2018	$7,345,774	$4,578,779	$15,843,857	$9,022,710	$ -
Fair value, May 31, 2017	$6,314,882	$4,434,540	$23,452,417	$ -	$5,661,098
Significant Investment Strategy	Venture and buyout, secondaries and in special situations the U.S. and internationally	Real estate and natural resources, primarily in the U.S.	Absolute return including multi-strategy, long/short equity, long/short credit, global macro, special situations and short credit	Balanced with 50% equity and 50% cash combined with writing covered call and covered put options	Global sovereign bonds, US floating rate bonds, and U.S. Broad core bonds
Remaining Life	0 to 13 years	0 to 13 years	N.A.	N.A.	N.A.
Dollar Amount of Unfunded Commitments	$9,187,580	$6,810,744	None	None	None
Timing to Draw Down Commitments	0 to 13 years	0 to 13 years	N.A.	N.A.	N.A.
Redemption Terms	N.A.	Quarterly for two funds, N.A. for others	Monthly, quarterly, and yearly	Monthly	Monthly and daily
Redemption Restrictions	N.A.	None	Ranges between quarterly with 100 days notice, calendar year end with 100 days notice and monthly with 60 days notice	Monthly with 5 days notice	Ranges between none and monthly with 10 days notice and monthly with 60 days notice
Redemption Restrictions in Place at Year End	N.A.	Two funds currently being redeemed	None	None	None

NOTE 3 - RESTRICTIONS AND LIMITATIONS ON NET ASSET BALANCES

At May 31, 2018 and 2017, the College's unrestricted net assets were allocated as follows:

	2018	2017
Operations	$ 10,885,644	$ 7,370,087
Long-term investment (board designated endowment funds less underwater donor restricted endowment funds)	28,760,895	31,063,064
Annuity, life income and similar funds	1,842,945	1,767,273
Loans to students	2,305,692	2,317,313
Replacement of plant facilities	5,222,241	3,441,621
Net investment in plant	46,867,626	49,683,810
Totals	$ 95,885,043	$ 95,643,168

Temporarily restricted net assets consist of the following at May 31, 2018 and 2017:

	2018	2017
Gifts and other unexpended revenues and gains available for:		
Scholarships, instruction and other support – Operating	$ 804,836	$ 1,174,974
Scholarships, instruction and other support – Endowment	31,091,560	27,846,422
Acquisition of buildings and equipment	481,135	2,860,880
	32,377,531	31,882,276
Annuity, life income and similar funds	925,501	1,024,700
Beneficial interest in funds held in trust - Deferred Gifts	37,457	36,816
Loans to students	418,814	414,576
Contributions receivable	1,146,000	1,222,000
Totals	$ 34,905,303	$ 34,580,368

Permanently restricted net assets consist of the following at May 31, 2018 and 2017:

	2018	2017
Endowment funds	$ 105,912,960	$ 100,637,313
Beneficial interest in funds held in trust - Endowment	1,578,231	1,537,610
Contributions receivable	874,000	1,242,000
	108,365,191	103,416,923
Beneficial interest in funds held in trust - Deferred Gifts	595,769	571,398
Annuity, life income and similar funds	7,841,247	7,647,466
Totals	$ 116,802,207	$ 111,635,787

NOTE 4 - NET ASSETS RELEASED FROM RESTRICTIONS

Net assets were released from temporary donor restrictions during the years ended May 31, 2018 and 2017 by incurring expenses satisfying the restricted purposes or by occurrence of events specified by the donors as follows:

	2018	2017
Scholarships, instruction and other departmental support	$ 1,297,760	$ 1,237,891
Matured deferred gifts	195,925	-
Acquisition of land, building, and equipment	2,466,626	575,074
Totals	$ 3,960,311	$ 1,812,965

These assets were reclassified to unrestricted net assets.

NOTE 5 - CONTRIBUTIONS RECEIVABLE

Contributions receivable include the following unconditional promises to give at May 31, 2018 and 2017:

	2018	2017
Unrestricted – completed plant projects	$ 1,477,000	$ 1,293,000
Temporarily restricted – operations	1,234,000	1,326,000
Temporarily restricted – plant projects	287,000	1,426,000
Permanently restricted – endowment	966,000	1,354,000
Gross unconditional promises to give	3,964,000	5,399,000
Less: Unamortized discount	(183,000)	(216,000)
Less: Allowance for uncollectible accounts	(717,000)	(786,000)
Net unconditional promises to give	$ 3,064,000	$ 4,397,000

Amounts due in:	
Less than one year	$ 1,630,000
One to five years	1,434,000
Totals	$ 3,064,000

At May 31, 2018 and 2017, respectively, promises due in one to five years were discounted using historical interest rates ranging between 1.67% and 6.0%. Promises due in less than one year were not discounted.

Net unconditional promises to give at May 31, 2018 and 2017 include $150,000 and $370,000, respectively, due from Cabinet members and Board members. The College received total contributions from Board members and officers of $555,000 and $602,000, respectively, for the years ended May 31, 2018 and 2017.

NOTE 6 - MARKETABLE SECURITIES

The following summarizes the College's marketable securities in funds other than endowment at May 31, 2018 and 2017:

	2018	2017
Equity securities	$ -	$ 4,878
Mutual funds	10,054,560	10,143,795
Totals	$ 10,054,560	$ 10,148,673

NOTE 7 - ENDOWMENT INVESTMENTS

The following summarizes the College's endowment investments at May 31, 2018 and 2017:

	2018	2017
Cash and short-term investments	$ 16,546,360	$ 15,508,886
Equity securities	-	1,100
Fixed income securities	-	5,661,098
Mutual / Commingled funds	112,516,140	101,086,184
Real estate, at cost	6	610,006
Alternative investments	36,791,120	34,228,838
Totals	$ 165,853,626	$ 157,096,112

Through the College's alternative investments, the College is indirectly involved in investment activities such as securities lending, trading in futures, forward contracts and other derivative products. Derivatives are used to adjust portfolio risk exposure. While these instruments may contain varying degrees of risk, the College’s risk with respect to such transactions is limited to its respective share in each investment pool.

Investments, in general, are subject to various risks, including credit, interest and overall market volatility risks. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in values of investment securities will occur in the near term and such changes could materially affect the amounts reported in the financial statements.

NOTE 8 - CREDIT QUALITY OF STUDENT LOAN RECEIVABLES

The College issues uncollateralized loans to students based on financial need. Student loans are funded through federal government loan programs or institutional resources. Student loans receivable are carried at the amount of unpaid principal less an estimate for doubtful accounts. Allowances for doubtful accounts are established based on prior collection experience and current economic factors which, in management's judgment, could influence the ability of loan recipients to repay the amounts per the loan terms. At May 31, 2018 and 2017, student loans represented 2.1% and 2.0% of total assets, respectively.

At May 31, 2018 and 2017, student loans consisted of the following:

	2018	2017
Federal government programs	$ 6,305,001	$ 5,956,714
Institutional programs	379,646	462,444
	6,684,647	6,419,158
Less allowance for doubtful accounts		
Beginning of year	(465,800)	(465,800)
Increases	(102,702)	(2,272)
Write-offs	102,702	2,272
End of year	(465,800)	(465,800)
Student notes receivable, net	$ 6,218,847	$ 5,953,358

Funds advanced by the federal government of $5,023,293 and $5,154,711 at May 31, 2018 and 2017, respectively, are ultimately refundable to the government and are classified as liabilities in the statement of financial position.

After a student is no longer enrolled in an institution of higher education and after a grace period, interest is charged on student loans receivable and is recognized as it is charged. Student loans receivable through the loan programs are considered to be past due if a payment is not made within 30 days of the payment due date, at which time, late charges are charged and recognized. The Federal Perkins Loan Program receivables may be assigned to the U.S. Department of Education. Students may be granted a deferment, forbearance, or cancellation of their student loan receivable based on eligibility requirements defined by the U.S. Department of Education.

At May 31, 2018 and 2017, the following amounts were past due under student loan programs:

	Amounts Past Due			
May 31	1-59 days	60-89 days	90+ days	Total
2018	$ 47,191	$ 147,014	$ 587,850	$ 782,055
2017	39,930	111,400	713,068	864,398

NOTE 9 - CONSTRUCTION IN PROGRESS

At May 31, 2018, the following construction projects were in progress:

	Estimated Total Cost	Cost To Date	Funding Source
Dike Road upgrade	$ 1,800,000	$ 253,324	Operations
Main renovation	12,000,000	41,267	Operations
Farwell hall	2,000,000	1,227,287	Operations
Regent Center	Undetermined	108,498	Operations and gifts
Totals	$ 15,800,000	$ 1,630,376	

Outstanding commitments on construction contracts totaled $462,087 at May 31, 2018.

NOTE 10 - PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consisted of the following as of May 31, 2018 and 2017:

	2018	2017
Land	$ 663,581	$ 663,581
Buildings	138,632,299	137,905,947
Improvements other than buildings	14,875,737	12,562,417
Wind turbine	3,237,495	3,237,495
Equipment and library books	36,894,377	36,532,172
Equipment under capital lease	888,866	888,866
	195,192,355	191,790,478
Less: Accumulated depreciation	(118,807,811)	(112,261,823)
Totals	$ 76,384,544	$ 79,528,655

NOTE 11 - ACCRUED LIABILITIES

Accrued liabilities consisted of the following as of May 31, 2018 and 2017:

	2018	2017
Payroll	$ 5,460,212	$ 5,573,670
Post-retirement benefit obligation (Note 17)	2,503,330	2,688,133
Interest	89,307	112,694
Other	847,626	1,228,144
Totals	$ 8,900,475	$ 9,602,641

NOTE 12 - CAPITAL LEASE OBLIGATIONS

The College entered into one capital lease for a solar panel array during the year ended May 31, 2013.

Capitalized cost and accumulated amortization for the equipment is as follows at May 31, 2018:

Leased equipment	$ 888,866
Less: Accumulated amortization	(533,319)
Net	$ 355,547

The following is a schedule of future minimum lease payments under the capital lease together with the present value of the minimum lease payments as of May 31, 2018:

Year Ending May 31:	
2019	$ 80,715
2020	46,722
2021	36,500
2022	36,500
2023	36,500
2024 - 2039	555,939
Total minimum lease payments	792,876
Less: Amount representing interest	(215,784)
Present value of minimum lease payments	$ 577,092

Amortization expense is included with depreciation expense in the financial statements.

NOTE 13 - LONG TERM DEBT

Long-term debt outstanding at May 31, 2018 and 2017 are as follows:

	2018	2017
Iowa Higher Education Loan Authority, Private College Facility Revenue Refunding Bonds, Series 2017	$ 20,246,833	$ -
City of Decorah, Iowa Private College Facility Revenue Bonds, Series 2011	-	20,830,000
Decorah Bank & Trust Company loan payable	84,247	123,137
Decorah Bank & Trust Company loan payable	357,458	460,420
First Citizens National Bank loan payable	278,343	746,928
Bonds, Series 2015	5,886,387	6,213,435
Principal outstanding on bonds	26,853,268	28,373,920
Deferred debt acquisition costs, net	(119,321)	(30,881)
Total Long Term Debt	$ 26,733,947	$ 28,343,039

NOTE 13 - LONG TERM DEBT (cont.)

In December 2011, the Iowa Higher Education Loan Authority Revenue Bonds, Series 2011, in the amount of $24,065,000 were issued on behalf of the College. The proceeds were used to pay off Iowa Higher Education Loan Authority Private College Facility Revenue Bonds, Series 2002 in the amount of $13,065,000 and Iowa Higher Education Loan Authority Private College Facility Revenue Bonds, Series 2008 in the amount of $11,000,000. The bonds were the subject of an advance refunding as a portion of the Series 2017 Bonds. The Series 2017 Bonds were settled on September 1, 2017.

In July 2011, Luther College Wind Energy Project, LLC entered into an agreement with Decorah Bank & Trust Company through the Iowa Alternate Energy Revolving Loan Program. The proceeds in the amount of $350,000 were used to finance the construction of a wind turbine. The loan is interest free and monthly payments of $3,241 are due until final maturity on July 27, 2020. The loan is unsecured.

In November 2011, Luther College Wind Energy Project, LLC entered into an agreement with Decorah Bank & Trust Company in the amount of $928,200. The proceeds were used to finance the construction of a wind turbine. In February 2015, the interest rate was reduced from 5.125% to 3.875% and is fixed until maturity. Monthly payments of $9,936, including principal and interest, are due until August 2021. The loan agreement requires that certain covenants be maintained. As of May 31, 2018, the College is in compliance with these covenants. The loan is secured by the equipment purchased with the loan proceeds.

In January 2015, the City of Decorah, Iowa sold its Private College Facility Revenue Refunding Bonds, Series 2015, in the amount of $6,868,000. The proceeds from the sale of the bonds were loaned to the College and were used to pay off the City of Decorah, Iowa Private College Facility Revenue Bonds, Series 2010 in the amount of $6,847,826 and pay the costs of issuance of the bonds. The bonds are unsecured. The interest rate on the proceeds is 3.29% and is fixed until June 30, 2030. Annual principal payments are $327,025. The bonds have a maturity date of June 30, 2035 with an optional put date of June 30, 2030. The loan agreement requires that certain covenants be maintained. As of May 31, 2018, the College is in compliance with these covenants.

In January 2015, Luther College entered into an agreement with First Citizens National Bank in the amount of $1,836,650. The proceeds were used to pay off the City of Decorah, Iowa Private Facility Revenue Bonds, Series 1998B. The interest rate is 2.3% and is fixed until final maturity on December 31, 2018. Monthly payments of $40,082, including principal and interest, are due until final maturity. The loan is unsecured. The loan agreement requires that certain covenants be maintained. As of May 31, 2018, the College is in compliance with these covenants.

On September 1, 2017, the Iowa Higher Education Loan Authority Private College Facility Revenue Refunding Bonds, Series 2017, in the amount $20,945,000 were issued on behalf of the College. The proceeds were used to pay off Iowa Higher Education Loan Authority Private College Facility Revenue Refunding Bonds, Series 2011 in the amount of $20,830,000 and pay costs of issuing the bonds. The bonds are unsecured. The interest rate, which is variable and is calculated monthly at 85.08% of USD-LIBOR-BBA, was 2.656% as of May 31, 2018. The Series 2017 Bonds mature monthly in the amount of $87,271 until September 2037. The loan agreement requires that certain covenants be maintained. As of May 31, 2018, the College is in compliance with these covenants.

In order to minimize the effect of changes in the interest rate, the College has entered into interest rate swap contracts. The interest rate swap contracts are disclosed in Note 14.

Total interest expense amounted to $900,682 and $1,180,289 for the years ended May 31, 2018 and 2017, respectively. Interest totaling $22,900 and $30,400 was capitalized for the years ended May 31, 2018 and 2017, respectively.

NOTE 13 - LONG TERM DEBT (cont.)

Anticipated principal payments on long-term debt are as follows:

Year Ending May 31:	
2019	$ 1,798,617
2020	1,524,542
2021	1,496,589
2022	1,397,491
2023	1,374,298
Thereafter	19,261,731
Total	$ 26,853,268

NOTE 14 - DERIVATIVES

The College uses interest rate exchange agreements as part of its risk management strategy to manage exposure to fluctuations in interest rates and to manage the overall cost of its debt. Interest rate exchange agreements are used to manage identified and approved exposures and are not used for speculative purposes. The interest rate exchange agreements are recognized as either assets or liabilities on the statements of financial position and are measured at fair value. Interest rate exchange agreements are often held for the life of the strategy, but may reflect significant interim unrealized gains or losses depending on the change in value since the inception of the contract. All unrealized and realized gains and losses from the interest rate exchange agreements are reflected in the statements of activities.

Interest rate exchange agreements between the College and a third party (counterparty) provide for periodic exchange of payments between the parties based on changes in a defined index and a fixed rate and include counterparty credit risk. Counterparty credit risk is the risk that contractual obligations of the counterparties will not be fulfilled. Concentrations of credit risk relate to groups of counterparties that have similar economic or industry characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions. Counterparty credit risk is managed by requiring high credit standards for the College’s counterparties. The counterparties to these contracts are financial institutions that carry investment-grade credit ratings. The interest rate exchange agreements contain collateral provisions applicable to both parties to mitigate credit risk. The College does not anticipate non-performance by its counterparties.

In fiscal years 2018 and 2017, the College paid $241,483 and $621,942, respectively, more than it received in interest under the swap agreements. The difference between interest received and interest paid under the swap agreements is recorded as interest expense in the statements of activities.

As of May 31, 2018, the College had the following the outstanding position under an interest rate exchange agreement:

Instrument Type	Effective Date	Notional Amount	Maturity Date	Rate Paid	Rate Received
Variable to fixed rate swap	September 1, 2017	$ 20,246,833	September 1, 2027	2.05%	85.0768% of USD-LIBOR-BBA

NOTE 14 - DERIVATIVES (cont.)

As of May 31, 2017, the College had the following outstanding positions under interest rate exchange agreements. The College settled both agreements on September 1, 2017 with a termination payment of $1,199,199. The realized loss from the settlement is included in the gain on swap agreement valuation reported on the statement of activities.

Instrument Type	Effective Date	Notional Amount	Maturity Date	Rate Paid	Rate Received
Variable to fixed rate swap	November 1, 2011	$ 11,000,000	November 1, 2026	3.22%	74.0% of USD-LIBOR-BBA
Variable to fixed rate swap	June 15, 2009	$ 9,830,000	September 1, 2027	3.624%	67.0% of USD-LIBOR-BBA

Derivative instruments are reported in the statements of financial position at fair value as of May 31, 2018 and 2017 as follows:

Derivatives Not Designated as Hedging Instruments	Liabilities Derivative: Statement of Financial Position Location	Fair Value 2018	Fair Value 2017
Interest rate swap	Interest rate swap (liability) asset	$ 338,998	$ (1,470,652)

The effect of derivative instruments is reported in the statements of activities as follows:

Derivatives Not Designated as Hedging Instruments	Location of Gain on Derivatives Recognized in the Statement of Changes in Net Assets	Amount of Gain on Derivatives Recognized in the Statement of Changes in Net Assets 2018	2017
Interest rate swap	Gain on swap agreement valuation	$ 610,451	$ 675,896

NOTE 15 - ENDOWMENT

The College's endowment consists of approximately 900 individual funds established for a variety of purposes. Its endowment includes both donor-restricted endowment funds and funds designated by the governing board to function as endowments. As required by GAAP, net assets associated with endowment funds, including funds designated by the governing board to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of Relevant Law – The Board of Regents of the College has interpreted the Iowa enacted version of Uniform Prudent Management of Institutional Funds Act (UPMIFA) as allowing the College to appropriate for expenditure or accumulate so much of an endowment fund as the College determines is prudent for the uses, benefits, purposes, and duration for which the endowment fund is established, subject to the intent of the donor as expressed in the gift instrument. Unless stated otherwise in the gift instrument, the assets in an endowment fund shall be donor-restricted assets until appropriated for expenditure by the Board of Regents. See Note 1 for further information on net asset classification.

NOTE 15 - ENDOWMENT (cont.)

The remaining portion of the donor-restricted endowment fund that is not classified as permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the College in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the College considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. The duration and preservation of the fund
2. The purposes of the College and the donor-restricted endowment fund
3. General economic conditions
4. The possible effect of inflation and deflation
5. The expected total return from income and the appreciation of investments
6. Other resources of the College
7. The investment policies of the College

Endowment net asset composition by type of fund consists of the following as of May 31, 2018:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	$ (176,267)	$ 31,091,560	$ 105,912,960	$ 136,828,253
Donor-restricted funds held in trust	–	–	1,578,231	1,578,231
Board-designated endowment funds	28,937,162	–	–	28,937,162
Contributions receivable	–	–	874,000	874,000
Total endowment net assets	$ 28,760,895	$ 31,091,560	$ 108,365,191	$ 168,217,646

Endowment net asset composition by type of fund consists of the following as of May 31, 2017:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	$ (315,038)	$ 27,846,422	$ 100,637,313	$ 128,168,697
Donor-restricted funds held in trust	–	–	1,537,610	1,537,610
Board-designated endowment funds	31,378,102	–	–	31,378,102
Contributions receivable	–	–	1,242,000	1,242,000
Total endowment net assets	$ 31,063,064	$ 27,846,422	$ 103,416,923	$ 162,326,409

NOTE 15 - ENDOWMENT (cont.)

Changes in endowment net assets for the year ended May 31, 2018 are as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, May 31, 2017	$ 31,063,064	$ 27,846,422	$ 103,416,923	$ 162,326,409
Investment return:				
Investment income, net of investment fees of $107,712	437,100	2,081,394	390,821	2,909,315
Net appreciation – realized and unrealized	986,910	6,376,933	1,197,462	8,561,305
Net appreciation – realized and unrealized funds held in trust	–	–	40,622	40,622
Total investment return	1,424,010	8,458,327	1,628,905	11,511,242
Contributions	–	–	4,350,130	4,350,130
Matured deferred gifts	251,494	–	301,985	553,479
Change in contributions receivable	–	–	(368,000)	(368,000)
Appropriation of endowment assets for expenditure	(668,158)	(5,213,189)	(964,752)	(6,846,099)
Other changes:				
Transfer from operating reserve	(2,661,236)	–	–	(2,661,236)
Other transfers from board / college designated endowment funds	(648,279)	–	–	(648,279)
Endowment net assets, May 31, 2018	$ 28,760,895	$ 31,091,560	$ 108,365,191	$ 168,217,646

Changes in endowment net assets for the year ended May 31, 2017 are as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, May 31, 2016	$ 29,233,464	$ 22,124,433	$ 98,991,224	$ 150,349,121
Investment return:				
Investment income, net of investment fees of $103,332	341,999	1,772,297	340,851	2,455,147
Net appreciation – realized and unrealized	1,441,361	9,152,701	1,760,264	12,354,326
Net appreciation – realized and unrealized funds held in trust	–	–	91,019	91,019
Total investment return	1,783,360	10,924,998	2,192,134	14,900,492
Contributions	–	–	3,735,912	3,735,912
Matured deferred gifts	–	–	585,225	585,225
Change in contributions receivable	–	–	(1,175,000)	(1,175,000)
Appropriation of endowment assets for expenditure	(423,648)	(5,203,009)	(912,572)	(6,539,229)
Other changes:				
Transfers to board / college designated endowment funds	469,888	–	–	469,888
Endowment net assets, May 31, 2017	$ 31,063,064	$ 27,846,422	$ 103,416,923	$ 162,326,409

NOTE 15 - ENDOWMENT (cont.)

***Funds with Deficiencies* –** From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the College to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature that are reported in unrestricted net assets were $176,267 and $315,038 as of May 31, 2018 and 2017, respectively. These deficiencies resulted from unfavorable market fluctuations that occurred after the investment of new permanently restricted contributions and continued appropriation for certain programs that was deemed prudent by the governing board. Subsequent gains that restore the fair value of the assets of the endowment fund to the required level will be classified as an increase in unrestricted net assets.

***Return Objectives and Risk Parameters* –** The College has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the College must hold in perpetuity or for a donor-specified period(s) as well as board-designated funds. Under this policy, as approved by the governing board, the endowment assets are invested in a manner that is intended to produce returns to meet needs of the spending rate, inflation, and portfolio fees while assuming a moderate level of investment risk. The College expects its endowment funds, over time, to provide an average annual rate of approximately 8.75%. Actual returns in any year may vary from this amount.

***Strategies Employed for Achieving Objectives* –** To satisfy its long-term rate-of-return objectives, the College relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The College targets a diversified asset allocation that is weighted in equity based investments and balanced with fixed income and alternative investments to achieve its long-term return objectives within prudent risk constraints. The alternative investments were entered into to diversify the College's portfolio, to provide predictability in overall earnings and to provide market neutral holdings. The College monitors its portfolio mix to ensure that it is in accordance with Board policy. For the majority of alternative investments, the College utilizes fund of funds to diversify the risk inherent in alternative investments.

***Spending Policy and How the Investment Objectives Relate to Spending Policy* –** The Board has authorized that the amount to be allocated to operations from the endowment fund be determined by applying a spending rate of 5% to the average of the fair value of the endowment investments at the end of 20 trailing calendar quarters. In establishing this policy, the College considered the long-term expected return on its endowment. Accordingly, over the long term, the College expects the current spending policy to allow its endowment to grow at an average of 3% annually. This is consistent with the College's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

NOTE 16 - DEFERRED GIFT AGREEMENTS

The College has arrangements with donors classified as charitable lead trusts, charitable remainder trusts, and charitable gift annuities. In general, under these arrangements the College receives a gift from a donor in which it has a remainder interest and agrees to pay the donor stipulated amounts over the life of the donor. The arrangement may cover one or more lives. The College and its administrator invest and manage the related assets and makes distributions to the beneficiaries as required. When the agreement reaches the end of its term, remaining assets are retained by the College as unrestricted, temporarily restricted or permanently restricted net assets, or in some instances, distributed to third-party beneficiaries.

NOTE 16 - DEFERRED GIFT AGREEMENTS (cont.)

When a gift is received under one of these arrangements, it is split into the amount representing the actuarial present value of future distributions back to the donor and the remaining gift value to be retained for the benefit of the College or third-party beneficiaries. The actuarial liability is adjusted annually using actuarial tables appropriate for the type of arrangement, number of lives covered and age of the donor. The College used historic interest rates for each agreement ranging from 1.8% to 10.2% in making the calculation at May 31, 2018 and 2017.

During the years ended May 31, 2018 and 2017, the College received gift income relating to deferred gift agreements of approximately $61,266 and $31,524, respectively. Total assets (marketable securities, real estate, and cash value of life insurance) held by the College under deferred gift agreements were $15,804,726 and $15,799,628 at May 31, 2018 and 2017, respectively.

NOTE 17 - EMPLOYEE BENEFIT PLANS

The College has a 403(b) defined contribution retirement plan. Contributions for employees are determined on a percentage of annual compensation. The cost of the retirement plan is paid currently and amounted to approximately $1,924,000 and $2,283,000 for the years ended May 31, 2018 and 2017, respectively.

An early retirement plan is available to faculty members. The estimated accrued liability for the early retirement benefit is calculated using historical participation rates, current faculty membership and projected salary increases, discounted at a rate of 3.8% and 3.5% for May 31, 2018 and 2017, respectively. The plan is unfunded. The total accrued liability for the early retirement benefits is $199,330 and $469,133 for May 31, 2018 and 2017, respectively.

The College provides medical benefits through a self-insurance plan which is available to all eligible employees of the College for certain medical expenses. Estimates for claims incurred but not reported have been accrued by the College.

Faculty members who retired by May 31, 2005 with emeriti status, and their spouses, and faculty members who completed 25 years of service by May 31, 2005 and who may be granted emeriti status upon retirement, and their spouses, are eligible to receive health insurance coverage that supplements Medicare coverage. The plan is unfunded. The following tables set forth the postretirement healthcare benefit plan's status with amounts reported in the College's financial statements at May 31, 2018 and 2017:

	2018	2017
Total expected benefit obligation earned to date, based on service		
Current retirees and dependents		
Pre-65 payments	$ 458,000	$ 191,000
Post-65 payments	1,100,000	1,121,000
Active employees		
Pre-65 payments	683,000	807,000
Post-65 payments	63,000	100,000
Benefit obligation at end of year	$ 2,304,000	$ 2,219,000

NOTE 17 - EMPLOYEE BENEFIT PLANS (cont.)

	2018	2017
Change in projected benefit obligation		
Benefit obligation at beginning of year	$ 2,219,000	$ 2,321,000
Net benefits earned	143,000	143,000
Expected benefit payments	(98,000)	(99,000)
Total (gain) loss	40,000	(146,000)
Benefit obligation at end of year	$ 2,304,000	$ 2,219,000
Change in plan assets		
Fair value of plan assets at beginning of year	$ –	$ –
Employer contribution	98,000	99,000
Participant contribution		
Benefits paid	(98,000)	(99,000)
Fair value of plan assets at end of year	$ –	$ –
Funded status		
Underfunded status at year end	$ (2,304,000)	$ (2,219,000)
Amounts recognized in the statements of financial position consist of:		
Noncurrent assets	$ –	$ –
Current liabilities	(98,000)	(99,000)
Noncurrent liabilities	(2,206,000)	(2,120,000)
Net amount recognized in accrued liabilities	$ (2,304,000)	$ (2,219,000)
Weighted average assumptions used to calculate the benefit obligation at May 31		
Discount rate	3.8%	3.5%
Expected return on plan assets	–	–
Rate of compensation increase	–	–
Assumed health care cost trend rates at May 31		
Health care cost trend rate assumed for next year	3.9%	4.9%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	3.9%	4.1%
Year that the rate reaches the ultimate trend rate	2074	2070

Assumed medical cost trend rates have a significant effect on the amounts reported for the health care plan. A one-percentage point change in assumed medical trend rates would have the following effects:

	One-Percentage Point	
	Increase	Decrease
Effect on postretirement benefit obligation at May 31, 2018	$ 201,000	$ (232,000)

Annual premium payments were approximately $91,000 and $117,000 for the years ended May 31, 2018 and 2017, respectively. During the fiscal year ending May 31, 2019, the College expects to contribute $150,000 in benefit payments for the postretirement medical plan.

NOTE 17 - EMPLOYEE BENEFIT PLANS (cont.)

Estimated future postretirement medical payments (which reflect expected future service, as appropriate) as of May 31, 2018 are as follows:

Years Ending May 31		
2019	$	150,000
2020		147,000
2021		165,000
2022		180,000
2023		164,000
2024 - 2038		2,462,000

The estimate of the accumulated postretirement benefit obligation is based on actuarial assumptions and methods provided by a third party actuary and the selection of discount rates that appropriately reflect the time value of money as of the measurement date. The discount rate used was based on the rates of return for high quality fixed income investments whose cash flows match the timing and amount of expected benefit payments. It is reasonably possible that changes in these estimates could occur in the near term and that actual results could differ from these estimates and could have a material effect on the financial statements.

NOTE 18 – CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject the College to concentrations of credit risk consist principally of cash and cash equivalents, short-term investments, marketable securities and other investments, accounts receivable and notes, mortgages and contracts for deed. Cash and cash equivalents in excess of FDIC and similar coverages is subject to the usual risks of balances in excess of those limits. The College currently has 50% of its cash and cash equivalents and 100% of cash restricted for plant acquisitions in a well-capitalized bank with a tier 1 risk-based capital ratio of 12.2 and a total risk-based capital ratio of 13.18. Investments are generally placed in a variety of managed funds administered by different investment managers in order to limit credit risk. Concentrations of credit risk with respect to the mortgages and contracts for deed are limited due to the College holding a secured position in agreements. Student notes and receivables and other receivables are due from a variety of sources concentrated primarily in the Midwestern United States. In addition, the College's students receive a substantial amount of support from state and federal student financial assistance programs which are subject to audit by governmental agencies. A significant reduction in the level of this support, if this were to occur, could have an adverse effect on the College's programs and activities.

NOTE 19 - SUBSEQUENT EVENTS

Luther College has evaluated subsequent events through September 17, 2018, which is the date that the financial statements were issued.