LUTHER COLLEGE
Decorah, Iowa

CONSOLIDATED FINANCIAL STATEMENTS
Including Independent Auditors' Report

As of and for the Years Ended May 31, 2019 and 2018

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, 2019 and 2018, 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, 2019 and 2018, 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.

Emphasis of Matter

As discussed in Note 1 to the financial statements, Luther College adopted ASU 2016-14, *Not-for-Profit (Topic 958): Presentation of Financial Statements of Not-for-profit Entities*, effective June 1, 2018. Our opinion is not modified with respect to this matter.

Baker Tilly Virchow Krause, LLP

Minneapolis, Minnesota
September 10, 2019

LUTHER COLLEGE

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
As of May 31, 2019 and 2018

ASSETS

	2019	2018
Cash and cash equivalents	$ 13,917,714	$ 15,046,238
Student accounts receivable, net of allowance for doubtful accounts of $170,000 in 2019 and $149,000 in 2018	319,612	258,646
Government grants receivable	196,901	150,387
Contributions receivable, net (Note 5)	6,234,000	3,064,000
Other receivables	500,863	521,215
Inventories	445,043	517,147
Prepaid expenses and other assets	706,548	486,051
Investments		
Short term investments	8,545,016	6,558,893
Marketable securities	9,681,002	10,054,560
Mortgages and contracts receivable	1,916,000	1,916,000
Real estate	1,006,534	299,034
Endowment (Note 6)	161,986,406	165,853,626
Beneficial interest in funds held in trust	2,111,413	2,211,457
Cash surrender value of life insurance	5,326,803	5,419,190
Student notes receivable, net (Note 8)	5,782,024	6,218,847
Interest rate swap asset (Note 14)		338,998
Cash restricted for plant acquisitions	3,219,672	2,740,813
Construction in progress (Note 9)	856,232	1,630,376
Property, plant and equipment, net (Note 10)	72,675,659	76,384,544
TOTAL ASSETS	$ 295,427,442	$ 299,670,022

LIABILITIES AND NET ASSETS

	2019	2018
LIABILITIES		
Accounts payable	$ 1,620,474	$ 1,691,202
Accrued liabilities (Note 11)	8,397,562	8,900,475
Deferred revenue	1,110,167	1,331,385
Asset retirement obligations (Note 1)	2,604,574	2,474,655
Capital lease obligation (Note 12)	516,156	577,092
Interest rate swap liability (Note 14)	516,628	
Long term debt (Note 13)	24,949,012	26,733,947
Annuities payable	4,835,646	4,922,307
Deposits held in custody for others	419,346	423,113
Government grants refundable (Note 8)	5,041,630	5,023,293
Total Liabilities	50,011,195	52,077,469
NET ASSETS		
Without donor restrictions (Note 3)	91,102,651	96,061,310
With restrictions (Note 3)	154,313,596	151,531,243
Total Net Assets	245,416,247	247,592,553
TOTAL LIABILITIES AND NET ASSETS	$ 295,427,442	$ 299,670,022

See accompanying notes to consolidated financial statements.

LUTHER COLLEGE

CONSOLIDATED STATEMENT OF ACTIVITIES
For the Year Ended May 31, 2019
(With Comparative Totals for 2018)

	2019			
	Without Donor Restrictions	With Donor Restrictions	Total	2018 Total
OPERATING REVENUES				
Revenues, Gains and Other Support				
Tuition and fees	$ 82,907,605	$ -	$ 82,907,605	$ 82,118,960
Less: Scholarships and grants	(51,187,937)	-	(51,187,937)	(48,159,058)
Net tuition and fees	31,719,668	-	31,719,668	33,959,902
Government grants and contracts	1,256,398	175,412	1,431,810	1,301,875
Private gifts and grants	6,390,939	1,695,169	8,086,108	5,977,583
Investment income	345,981	-	345,981	169,940
Spending allowance appropriation	6,764,132	363,024	7,127,156	6,846,099
Other sources	1,811,455	3,665	1,815,120	1,735,063
Subsidiary	189,776	-	189,776	233,836
Sales and services of educational activities	1,509,269	-	1,509,269	1,053,895
Sales and services of auxiliary enterprises	19,394,356	-	19,394,356	19,060,983
Transfer from/(to) non-operating	(121,843)	-	(121,843)	436,257
	69,260,131	2,237,270	71,497,401	70,775,433
Net assets released from restrictions	780,873	(780,873)	-	-
Total Revenues, Gains and Other Support	70,041,004	1,456,397	71,497,401	70,775,433
OPERATING EXPENSES				
Program Expenses				
Instruction	29,361,078	-	29,361,078	30,724,898
Research	385,790	-	385,790	642,360
Public service	389,270	-	389,270	453,284
Academic support	4,532,845	-	4,532,845	4,523,346
Student services	13,551,939	-	13,551,939	13,165,379
Auxiliary enterprises	14,370,487	-	14,370,487	14,634,740
Support Expenses				
Institutional support	11,561,374	-	11,561,374	10,949,607
Subsidiary	345,841	-	345,841	366,069
Allocable Expenses				
Operation and maintenance of plant	7,360,662	-	7,360,662	7,480,241
Depreciation and amortization	6,588,801	-	6,588,801	6,885,892
Accretion	129,919	-	129,919	123,439
Interest	803,677	-	803,677	900,682
Less: Allocated expenses	(14,883,059)	-	(14,883,059)	(15,390,254)
Total Expenses	74,498,624	-	74,498,624	75,459,683
Change in Net Assets from Operating Activities	(4,457,620)	1,456,397	(3,001,223)	(4,684,250)
NONOPERATING ACTIVITIES				
Gifts and grants	$ 324,206	$ 5,859,384	$ 6,183,590	$ 4,694,743
Endowment income	523,484	2,694,423	3,217,907	2,909,315
Gain (loss) on investments	(92,139)	(715,782)	(807,921)	8,561,305
Spending allowance appropriation	(823,550)	(6,303,606)	(7,127,156)	(6,846,099)
Gain (loss) on investments (FHIT)	-	(100,044)	(100,044)	64,993
Actuarial adjustment	196,883	(4,559)	192,324	859,029
Gain (Loss) on swap agreement	(855,626)	-	(855,626)	610,451
Transfer from/(to) non-operating	121,843	-	121,843	(436,257)
Reclassification of donor designated	26,114	(26,114)	-	-
Net assets released from restrictions	77,746	(77,746)	-	-
Change in Net Assets from Nonoperatig Activities	(501,039)	1,325,956	824,917	10,417,480
CHANGE IN NET ASSETS	(4,958,659)	2,782,353	(2,176,306)	5,733,230
NET ASSETS - Beginning of Year	96,061,310	151,531,243	247,592,553	241,859,323
NET ASSETS - END OF YEAR	$ 91,102,651	$ 154,313,596	$ 245,416,247	$ 247,592,553

See accompanying notes to consolidated financial statements.

LUTHER COLLEGE

CONSOLIDATED STATEMENT OF ACTIVITIES
For the Year Ended May 31, 2018

	Without Donor Restrictions	With Donor Restrictions	Total
OPERATING REVENUES			
Revenues, Gains and Other Support			
Tuition and fees	$ 82,118,960	$ -	$ 82,118,960
Less: Scholarships and grants	(48,159,058)	-	(48,159,058)
Net tuition and fees	33,959,902	-	33,959,902
Government grants and contracts	1,202,183	99,692	1,301,875
Private gifts and grants	5,581,213	396,370	5,977,583
Investment income	169,940	-	169,940
Spending allowance appropriation	6,490,539	355,560	6,846,099
Other sources	1,730,824	4,239	1,735,063
Subsidiary	233,836	-	233,836
Sales and services of educational activities	1,053,895	-	1,053,895
Sales and services of auxiliary enterprises	19,060,983	-	19,060,983
Transfer from/(to) non-operating	484,771	(48,514)	436,257
	69,968,086	807,347	70,775,433
Net assets released from restrictions	1,297,760	(1,297,760)	-
Total Revenues, Gains and Other Support	71,265,846	(490,413)	70,775,433
OPERATING EXPENSES			
Program Expenses			
Instruction	30,724,898	-	30,724,898
Research	642,360	-	642,360
Public service	453,284	-	453,284
Academic support	4,523,346	-	4,523,346
Student services	13,165,379	-	13,165,379
Auxiliary enterprises	14,634,740	-	14,634,740
Support Expenses			
Institutional support	10,949,607	-	10,949,607
Subsidiary	366,069	-	366,069
Allocable Expenses			
Operation and maintenance of plant	7,480,241	-	7,480,241
Depreciation and amortization	6,885,892	-	6,885,892
Accretion	123,439	-	123,439
Interest	900,682	-	900,682
Less: Allocated expenses	(15,390,254)	-	(15,390,254)
Total Expenses	75,459,683	-	75,459,683
Change in Net Assets from Operating Activities	(4,193,837)	(490,413)	(4,684,250)
NONOPERATING ACTIVITIES			
Gifts and grants	$ 564,465	$ 4,130,278	$ 4,694,743
Endowment income	437,100	2,472,215	2,909,315
Gain on investments	986,910	7,574,395	8,561,305
Spending allowance appropriation	(668,158)	(6,177,941)	(6,846,099)
Gain on investments (FHIT)	-	64,993	64,993
Actuarial adjustment	327,164	531,865	859,029
Gain on swap agreement	610,451	-	610,451
Transfer from/(to) non-operating	(436,257)	-	(436,257)
Reclassification of prior year net assets	127,753	(127,753)	-
Net assets released from restrictions	2,662,551	(2,662,551)	-
Change in Net Assets from Nonoperatig Activities	4,611,979	5,805,501	10,417,480
CHANGE IN NET ASSETS	418,142	5,315,088	5,733,230
NET ASSETS - Beginning of Year	95,643,168	146,216,155	241,859,323
NET ASSETS - END OF YEAR	$ 96,061,310	$ 151,531,243	$ 247,592,553

See accompanying notes to consolidated financial statements.

LUTHER COLLEGE

CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Years Ended May 31, 2019 and 2018

	2019	2018
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	$ (2,176,306)	$ 5,733,230
Adjustments to reconcile change in net assets to net cash flows from operating activities		
Depreciation, amortization, and accretion	6,718,720	7,009,331
Loss on disposal of property	50,989	22,168
(Gain) loss on interest rate swap valuation	855,626	(610,451)
(Gain) loss on investments, net	1,157,336	(8,823,785)
Decrease (increase) in beneficial interest in funds held in trust	100,044	(65,633)
Change in allowance on student notes receivable	29,200	-
Noncash contributions of investment assets	(707,500)	(145,000)
Actuarial adjustment of annuities payable	(120,438)	(91,599)
Loan cancellations, reinstatements and write-offs	81,196	129,124
Changes in assets and liabilities		
Receivables	(60,966)	(83,435)
Contributions receivable for operations	(1,051,422)	(96,578)
Accrued interest, grants and other receivables	(26,162)	125,863
Prepaid expenses, inventories, and other assets	(56,006)	(264,508)
Accounts payable and accrued liabilities	(504,593)	(828,198)
Deferred revenue and deposits held for others	(224,985)	(115,175)
Contributions restricted for loans, long-term investment and plant	(6,183,466)	(4,692,550)
Investment income restricted for reinvestment	(417,281)	(390,821)
Cash Flows from Operating Activities	(2,536,014)	(3,188,017)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of investments	(29,002,516)	(26,132,550)
Sales of investments	30,099,835	26,440,513
Purchases of property, plant and equipment	(2,212,134)	(5,002,337)
Disbursements of loans to students	(574,326)	(1,283,829)
Repayments of loans from students	900,753	889,216
Cash Flows from Investing Activities	(788,388)	(5,088,987)
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	(1,798,611)	(1,635,652)
Payments on capital lease obligations	(60,936)	(58,785)
Receipt of investment income restricted for reinvestment	417,281	390,821
Contributions and grants received restricted for loans, long-term investment and plant	4,064,888	6,122,128
Change in cash held for plant acquisitions	(478,859)	2,076,044
Decrease in government grants refundable	18,337	(131,418)
Proceeds from issuance of split-interest agreements	210,000	127,397
Payments to annuitants	(176,222)	(180,180)
Cash Flows from Financing Activities	2,195,878	5,514,139
Change in Cash and Cash Equivalents	(1,128,524)	(2,762,865)
CASH AND CASH EQUIVALENTS - Beginning of year	15,046,238	17,809,103
CASH AND CASH EQUIVALENTS - END OF YEAR	$ 13,917,714	$ 15,046,238
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Interest paid, net of capitalized amounts of $27,900 in 2019 and $22,900 in 2018	$ 810,426	$ 924,069
Payments on swap settlements	19,025	241,483
NONCASH INVESTMENT AND FINANCING ACTIVITIES		
Property, plant and equipment acquired through accounts payable	7,077	76,125
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 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 two 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:

Net Assets Without Donor Restrictions – Net assets that are not subject to donor-imposed stipulations. The governing board has established policies to designate net assets without donor restrictions for endowment, investment in property, plant, and equipment and other purposes.

Net Assets With Donor Restrictions – Net assets subject to donor-imposed restrictions. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposed restrictions are perpetual in nature where the donor stipulates that resources be maintained in perpetuity. Donor-imposed restrictions are released when a restriction expires, that is, when the stipulated time has elapsed, when the stipulated purpose for which the resource was restricted has been fulfilled, or both.

Revenues from sources other than contributions are generally reported as increases in net assets without donor restrictions. Investment income received with donor-imposed restrictions that are met in the same year as received are reported as revenues without donor restrictions. In all other cases, income earned on donor restricted funds is initially classified as net assets with donor restrictions and is reclassified as net assets without door restrictions when expenses are incurred for their intended purpose. Expenses are reported as decreases in net assets without donor restrictions.

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 without donor restrictions. 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 $750,000 and $900,000 at May 31, 2019 and 2018, respectively.

Contributions of property and equipment without donor stipulations concerning the use of such long-lived assets are reported as revenues without donor restrictions. Contributions of cash or other assets to be used to acquire property and equipment are reported as donor 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, gains and losses on the investments of a donor-restricted endowment fund are included in net assets with donor restrictions.

Gains and losses on investments of endowment funds created by a board designation of funds without donor restrictions are included in changes in net assets without donor restrictions.

***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 $4,437 and $3,769 at May 31, 2019 and 2018, 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 as of 2018 and $5,000 prior to 2018.

***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, 2019 and 2018 are as follows:

	2019	2018
Balance, Beginning of the year	$ 2,474,655	$ 2,351,216
Accretion expense	129,919	123,439
Balance, End of the year	$ 2,604,574	$ 2,474,655

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 were loaned to qualified students prior to June 30, 2018, the date at which the federal program ended. 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.)

Measure of Operations – The College's operating revenues in excess of (less than) expenses and transfers includes all operating revenues and expenses that are an integral part of its programs and supporting activities, net assets released from donor restrictions to support operating expenditures, and transfers from board-designated and other non-operating funds to support current operating activities. The measure of operations includes support for operating activities from both donor-restricted net assets and net assets without donor restrictions designated for long-term investment (the donor-restricted and quasi-endowment) according to the College's spending policy, which is detailed in Note 15. The measure of operations excludes endowment and plant support for non-operating activities, investment return in excess of (less than) amounts made available for current support, gains and losses on extinguishment of debt, and changes in fair value of the interest rate swap. The net transfer line item includes $2,521,440 and $2,781,746 transferred from quasi-endowment to operations; $335,363 and $195,925 transferred to operations from matured deferred gifts; $692,210 and $361,663 of contributions board designated to the plant fund for special projects; and $2,286,436 and $2,179,751 transferred to the plant fund for capital projects, for the years ended May 31, 2019 and 2018, respectively.

Fund-Raising and Advertising Expenses – Fund-raising expenses totaled approximately $2,434,000 and $2,482,000 for the years ended May 31, 2019 and 2018, respectively. Advertising expenses totaled approximately $760,000 and $551,000 for the years ended May 31, 2019 and 2018, 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, 2019 and 2018, Luther College Ventures, Inc. had recorded tax deductions, principally depreciation, in excess of financial statement expenses. Income tax benefits of $80,000 in both 2019 and 2018 are included in the subsidiary's institutional support expenses. The college had no material unrelated business income during the year.

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, 2019 and 2018. 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.

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (cont.)

New Accounting Pronouncements Adopted in Current Year – In August 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities.* The College adopted the provisions of this new standard during the year ended May 31, 2019. The primary changes include presenting two classes of net assets versus the three categories previously required and recognition of underwater endowment funds as a reduction to the net assets with donor restrictions class. The standard also provides for enhanced disclosures for board designated amounts, composition of net assets without donor restrictions, liquidity, and expenses by both natural and functional classification. This standard has been retrospectively applied to the prior period presented with certain transition provisions.

New Accounting Pronouncements Not Yet Effective – In May 2014, the FASB issued 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. ASU No. 2014-09 is effective for fiscal years beginning after December 15, 2018 (fiscal year 2020). The College is assessing the impact this standard will have on its financial statements.

In February 2016, the 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. ASU No. 2016-02 is effective for fiscal years beginning after December 15, 2019 (fiscal year 2021). 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.

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 new 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. ASU 2018-08 is effective for fiscal years beginning after December 15, 2018 (fiscal year 2020). The College is currently assessing the impact that this standard will have on its financial statements.

Reclassifications – Certain amounts appearing in the 2018 financial statements have been reclassified to conform with the 2019 presentation. The reclassifications have no effect on the reported amounts of total net assets or the change in total net assets.

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, 2019 and 2018.

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, 2019:

	Total	Level 1	Level 2	Level 3
ASSETS				
Mutual funds				
U.S. equity funds	$ 42,438,534	$ 42,438,534	$ -	$ -
Non-U.S. equity funds	41,728,721	41,728,721	-	-
U.S. fixed income funds	36,243,119	36,243,119	-	-
Non-U.S. fixed income funds	303,636	303,636	-	-
Beneficial interest in funds held in trust	2,111,413	-	-	2,111,413
Subtotal assets by valuation hierarchy	122,825,423	$120,714,010	$ -	$ 2,111,413
Investments measured using NAV				
Alternative investments				
Hedge funds	4,012,769			
Private equity funds	7,748,985			
Funds of funds	21,718,401			
Real assets	4,684,406			
Subtotal assets by NAV	38,164,561			
Total assets at fair value	160,989,984			
Investments at cost				
Short term investments	8,545,016			
Short term endowment investments	12,778,426			
Real estate investments	1,006,534			
Real estate endowment investments	6			
Equity endowment investments	10,405			
Mortgage and contract receivable	1,916,000			
	24,256,387			
Total investments	$ 185,246,371			
LIABILITIES				
Interest rate exchange agreements	$ 516,628	$ –	$ 516,628	$ –

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, 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			
Funds of funds	21,301,341			
Real assets	4,578,779			
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 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, 2019.

	Balances May 31, 2018	Net realized and unrealized losses included in change in net assets	Purchases	Sales	Net transfers in (out) of Level 3	Balances May 31, 2019
Beneficial interest in funds held in trust	$ 2,211,457	$ (100,044)	$ -	$ -	$ -	$ 2,111,413

The amount of total loss for the period included in change in net assets attributable to the change in unrealized losses relating to financial instruments still held at May 31, 2019.	$ (100,044)

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 period 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

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
Fair value, May 31, 2019	$7,748,985	$4,684,406	$16,541,093	$9,190,077
Fair value, May 31, 2018	$7,345,774	$4,578,779	$15,843,857	$9,022,710
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
Remaining Life	0 to 13 years	0 to 13 years	N.A.	N.A.
Dollar Amount of Unfunded Commitments	$9,645,030	$5,939,891	None	None
Timing to Draw Down Commitments	0 to 13 years	0 to 13 years	N.A.	N.A.
Redemption Terms	N.A.	Quarterly for two funds, N.A. for others	Monthly, quarterly, and yearly	Monthly
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
Redemption Restrictions in Place at Year-End	N.A.	Two funds currently being redeemed	None	None

NOTE 3 - Restrictions and Limitations on Net Asset Balances

At May 31, 2019 and 2018, the College's net assets without donor restrictions were allocated as follows:

	2019	2018
Operations	$ 11,110,415	$ 10,885,644
Long-term investment (board designated endowment funds)	21,399,349	23,022,377
Long-term investment (management designated endowment funds)	4,624,168	5,914,785
Annuity, life income and similar funds	1,730,846	1,842,945
Loans to students	2,301,520	2,305,692
Replacement of plant facilities	1,501,966	3,880,103
Contributions receivable	621,000	785,578
Board designated for special projects	1,128,660	556,560
Net investment in plant	46,684,727	46,867,626
Totals	$ 91,102,651	$ 96,061,310

Net assets with donor restrictions consist of the following at May 31, 2019 and 2018:

Gifts and other unexpended revenues and gains available for:		
Scholarships, instruction and other support – Operating	$ 1,041,568	$ 804,836
Scholarships, instruction and other support – Endowment	135,712,330	136,828,253
Acquisition of buildings and equipment	230,407	222,713
	136,984,305	137,855,802
Annuity, life income and similar funds	9,182,398	8,766,748
Beneficial interest in funds held in trust - Endowment	1,508,515	1,578,231
Beneficial interest in funds held in trust - Deferred Gifts	602,898	633,226
Loans to students	422,480	418,814
Contributions receivable	5,613,000	2,278,422
Totals	$ 154,313,596	$ 151,531,243

NOTE 4 - NET ASSETS RELEASED FROM RESTRICTIONS

Net assets were released from donor restrictions during the years ended May 31, 2019 and 2018 by incurring expenses satisfying the restricted purposes or by occurrence of events specified by the donors as follows:

	2019	2018
Operating		
Scholarships, instruction and other departmental support	$ 780,873	$ 1,297,760
Nonoperating		
Matured deferred gifts	167	195,925
Acquisition of land, building, and equipment	77,579	2,466,626
Totals	$ 858,619	$ 3,960,311

These assets were reclassified to net assets without donor restrictions.

NOTE 5 - CONTRIBUTIONS RECEIVABLE

Contributions receivable include the following unconditional promises to give at May 31, 2019 and 2018:

	2019	2018
Without donor restrictions – completed plant projects	$ 1,281,000	$ 1,477,000
With donor restrictions:		
Operations	2,595,000	1,234,000
Plant projects	528,000	287,000
Endowment	3,108,000	966,000
Gross unconditional promises to give	7,512,000	3,964,000
Less: Unamortized discount	(394,000)	(183,000)
Less: Allowance for uncollectible accounts	(884,000)	(717,000)
Net unconditional promises to give	$ 6,234,000	$ 3,064,000

Amounts due in:	
Less than one year	$ 2,665,000
One to five years	3,569,000
Totals	$ 6,234,000

At May 31, 2019 and 2018, 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, 2019 and 2018 include $2,253,000 and $150,000, respectively, due from Cabinet members and Board members. The College received gifts and pledge payments from Board members and officers of $896,000 and $555,000, respectively, for the years ended May 31, 2019 and 2018.

NOTE 6 - ENDOWMENT INVESTMENTS

The following summarizes the College's endowment investments at May 31, 2019 and 2018:

	2019	2018
Cash and short-term investments	$ 12,778,426	$ 16,546,360
Equity securities	10,405	-
Mutual / Commingled funds	111,033,008	112,516,140
Real estate, at cost	6	6
Alternative investments	38,164,561	36,791,120
Totals	$ 161,986,406	$ 165,853,626

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 7 - LIQUIDITY AND AVAILABILITY

The College regularly monitors liquidity required to meet its operating needs and other contractual commitments. The following assets could be made readily available within one year to meet general expenditures:

	2019
Cash and cash equivalents	$ 13,917,714
Student accounts receivable, net of allowance for doubtful accounts	319,612
Government grants receivable	196,901
Contributions receivable	1,610,000
Other receivables	266,913
Investments	
Short-term investments	8,414,150
Endowment	
Spending rate appropriations	7,127,156
Management designated quasi-endowment	4,583,619
Cash designated by management for plant acquisitions	1,965,919
Financial assets available to meet cash needs for general expenditures within one year	$ 38,401,984

The majority of the College's liquidity is provided by cash and cash equivalents, as well as short-term investments made with cash in excess of daily needs. Principal and interest on student loans are not included above, as those amounts are used solely for new loans and are, therefore, not available to meet current operating needs. Based on historical experience, only the portions of contributions receivable due within the next year are included as liquid. Additionally, the College has a board designated quasi-endowment of $21,399,349. Although the College does not intend to spend from its board designated quasi-endowment other than amounts appropriated for general expenditure as part of its annual budget approval and appropriation process, amounts from its quasi-endowment could be made available with board approval, if necessary.

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, 2019 and 2018, student loans represented 2.0% and 2.1% of total assets, respectively.

At May 31, 2019 and 2018, student loans consisted of the following:

	2019	2018
Federal government programs	$ 5,395,851	$ 6,305,001
Institutional programs	881,173	379,646
	6,277,024	6,684,647
Less allowance for doubtful accounts		
Beginning of year	(465,800)	(465,800)
Increases	(81,256)	(102,702)
Write-offs	52,056	102,702
End of year	(495,000)	(465,800)
Student notes receivable, net	$ 5,782,024	$ 6,218,847

Funds advanced by the federal government of $5,041,630 and $5,023,293 at May 31, 2019 and 2018, 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, 2019 and 2018, the following amounts were past due under student loan programs:

	Amounts Past Due			
May 31	1-59 days	60-89 days	90+ days	Total
2019	$ 45,361	$ 58,611	$ 770,691	$ 874,663
2018	47,191	147,014	587,850	782,055

NOTE 9 - CONSTRUCTION IN PROGRESS

At May 31, 2019, the following construction projects were in progress:

	Estimated Total Cost	Cost To Date	Funding Source
Dike Road upgrade	$ 2,500,000	$ 706,467	Operations
Main renovation	12,800,000	41,267	Operations and gifts
Regent Center	Undetermined	108,498	Operations and gifts
Totals		$ 856,232	

The college had no outstanding commitments on construction contracts at May 31, 2019.

NOTE 10 - PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consisted of the following as of May 31, 2019 and 2018:

	2019	2018
Land	$ 663,581	$ 663,581
Buildings	140,040,256	138,632,299
Improvements other than buildings	14,927,600	14,875,737
Wind turbine	3,237,495	3,237,495
Equipment and library books	37,206,768	36,894,377
Equipment under capital lease	888,866	888,866
	196,964,566	195,192,355
Less: Accumulated depreciation	(124,288,907)	(118,807,811)
Totals	$ 72,675,659	$ 76,384,544

NOTE 11 - ACCRUED LIABILITIES

Accrued liabilities consisted of the following as of May 31, 2019 and 2018:

	2019	2018
Payroll	$ 4,925,161	$ 5,460,212
Post-retirement benefit obligation (Note 17)	2,589,045	2,503,330
Interest	83,630	89,307
Other	799,726	847,626
Totals	$ 8,397,562	$ 8,900,475

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, 2019:

Leased equipment	$ 888,886
Less: Accumulated amortization	(622,206)
Net	$ 266,660

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, 2019:

Year Ending May 31:	
2020	$ 46,722
2021	36,500
2022	36,500
2023	36,500
2024	36,500
2025 - 2039	519,439
Total minimum lease payments	712,161
Less: Amount representing interest	(196,005)
Present value of minimum lease payments	$ 516,156

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

NOTE 13 - LONG TERM DEBT

Long-term debt outstanding at May 31, 2019 and 2018 are as follows:

	2019	2018
Iowa Higher Education Loan Authority, Private College Facility Revenue Refunding Bonds, Series 2017	$ 19,199,584	$ 20,246,833
Decorah Bank & Trust Company loan payable	45,356	84,247
Decorah Bank & Trust Company loan payable	250,379	357,458
First Citizens National Bank loan payable	-	278,343
Bonds, Series 2015	5,559,339	5,886,387
Principal outstanding	25,054,658	26,853,268
Deferred debt acquisition costs, net	(105,646)	(119,321)
Total Long Term Debt	$ 24,949,012	$ 26,733,947

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, 2019, 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, 2019, 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 was 2.3% and was fixed until final maturity on December 31, 2018. Monthly payments of $40,082, including principal and interest, were due until final maturity. The loan was unsecured. Final payment of $40,019 was made in December 2018.

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 3.148% and 2.656% as of May 31, 2019 and 2018, respectively. 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, 2019, 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.

NOTE 13 - LONG TERM DEBT (cont.)

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

Year Ending May 31:	
2020	$ 1,524,542
2021	1,496,589
2022	1,397,500
2023	1,374,298
2024	1,374,298
Thereafter	17,887,431
Total	$ 25,054,658

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 nonperformance by its counterparties.

In fiscal years 2019 and 2018, the College paid $19,025 and $241,483, 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, 2019, the College had the following 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	$ 19,199,583	September 1, 2027	2.05%	85.0768% of USD-LIBOR-BBA

NOTE 14 - DERIVATIVES (cont.)

Derivative instruments are reported in the statements of financial position at fair value as of May 31, 2019 and 2018 as follows:

	Liabilities Derivative		
Derivatives Not Designated as Hedging Instruments	Statement of Financial Position Location	Fair Value	
		2019	2018
Interest rate swap	Interest rate swap asset (liability)	$ (516,628)	$ 338,998

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

Derivatives Not Designated as Hedging Instruments	Location of Gain (Loss) 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	
		2019	2018
Interest rate swap	Gain (Loss) on swap agreement valuation	$ (855,626)	$ 610,451

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.)

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, 2019:

	Without Donor Restrictions	With Donor Restrictions	Total
Donor-restricted endowment funds	$ -	$ 108,434,293	$ 108,434,293
Donor-restricted accumulated earnings	-	27,278,037	27,278,037
Donor-restricted funds held in trust	-	1,508,515	1,508,515
Board-designated endowment funds	26,023,517	-	26,023,517
Contributions receivable	-	2,779,000	2,779,000
Total endowment net assets	$ 26,023,517	$ 139,999,845	$ 166,023,362

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

	Without Donor Restrictions	With Donor Restrictions	Total
Donor-restricted endowment funds	$ -	$ 105,912,960	$ 105,912,960
Donor-restricted accumulated earnings	-	30,915,293	30,915,293
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	$ 28,937,162	$ 139,280,484	$ 168,217,646

NOTE 15 - ENDOWMENT (cont.)

Changes in endowment net assets for the year ended May 31, 2019 are as follows:

	Without Donor Restrictions	With Donor Restrictions	Total
Endowment net assets, May 31, 2018	$ 28,937,162	$ 139,280,484	$ 168,217,646
Investment return:			
Investment income	523,484	2,694,423	3,217,907
Net appreciation (depreciation) – realized and unrealized	(92,139)	(715,782)	(807,921)
Net appreciation (depreciation) – realized and unrealized funds held in trust	-	(69,716)	(69,716)
Total investment return	431,345	1,908,925	2,340,270
Contributions	-	3,051,149	3,051,149
Matured deferred gifts	-	157,893	157,893
Change in contributions receivable	-	1,905,000	1,905,000
Appropriation of endowment assets for expenditure	(823,550)	(6,303,606)	(7,127,156)
Other changes:			
Transfer to operating reserve	(2,521,440)	-	(2,521,440)
Endowment net assets, May 31, 2019	$ 26,023,517	$ 139,999,845	$ 166,023,362

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

	Without Donor Restriction	With Donor Restriction	Total
Endowment net assets, May 31, 2017	$ 31,063,064	$ 131,263,345	$ 162,326,409
Investment return:			
Investment income	437,100	2,472,215	2,909,315
Net appreciation – realized and unrealized	986,910	7,574,395	8,561,305
Net appreciation – realized and unrealized funds held in trust	-	40,622	40,622
Total investment return	1,424,010	10,872,232	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)	(6,177,941)	(6,846,099)
Other changes:			
Reclassification due to ASU 2016-14	176,267	(176,267)	-
Transfers of board / college designated endowment funds	(3,309,515)	-	(3,309,515)
Endowment net assets, May 31, 2018	$ 28,937,162	$ 139,280,484	$ 168,217,646

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. As of May 31, 2019, funds with original gift values of $8,526,093 and fair values of $8,149,635, and deficiencies of $376,458 were reported in net assets with donor restrictions. As of May 31, 2018, funds with original gift values of $3,774,995 and fair values of $3,598,728, and deficiencies of $176,267 were reported in net assets with donor restrictions. These deficiencies, which the College believes are temporary, resulted from unfavorable market fluctuations that occurred after the investment of new permanently restricted contributions and continued appropriation has been 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 net assets with donor restrictions.

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.

Endowment net assets included in the Statements of Financial Position as of May 31, 2019 and 2018 include the following:

	2019	2018
Endowment investments (note 6)	$ 161,986,406	$ 165,853,626
Funds held in trust	1,508,515	1,578,231
Contributions receivable	2,779,000	874,000
Interest receivable	40,549	24,922
Interfund balance (due to operating)	(291,108)	(113,133)
Total Endowment Net Assets	$ 166,023,362	$ 168,217,646

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 with donor or without donor restricted net assets, or in some instances, distributed to third-party beneficiaries.

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, 2019 and 2018.

During the years ended May 31, 2019 and 2018, the College received gift income relating to deferred gift agreements of $604,483 and $61,266, respectively. Total assets (marketable securities, real estate, and cash value of life insurance) held by the College under deferred gift agreements were $16,019,140 and $15,804,726 at May 31, 2019 and 2018, 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 $1,584,000 and $1,924,000 for the years ended May 31, 2019 and 2018, 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 3.4% and 3.8% for May 31, 2019 and 2018, respectively. The plan is unfunded. The total accrued liability for the early retirement benefits is $214,045 and $199,330 for May 31, 2019 and 2018, 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.

NOTE 17 - EMPLOYEE BENEFIT PLANS (cont.)

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, 2019 and 2018:

	2019	2018
Total expected benefit obligation earned to date, based on service		
Current retirees and dependents		
Pre-65 payments	$ 417,000	$ 458,000
Post-65 payments	1,117,000	1,100,000
Active employees		
Pre-65 payments	774,000	683,000
Post-65 payments	67,000	63,000
Benefit obligation at end of year	$ 2,375,000	$ 2,304,000
Change in projected benefit obligation		
Benefit obligation at beginning of year	$ 2,304,000	$ 2,219,000
Net benefits earned	127,000	143,000
Expected benefit payments	(150,000)	(98,000)
Total loss	94,000	40,000
Benefit obligation at end of year	$ 2,375,000	$ 2,304,000
Change in plan assets		
Fair value of plan assets at beginning of year	$ -	$ -
Employer contribution	150,000	98,000
Participant contribution		
Benefits paid	(150,000)	(98,000)
Fair value of plan assets at end of year	$ -	$ -
Funded status		
Underfunded status at year end	$ (2,375,000)	$ (2,304,000)
Amounts recognized in the statements of financial position consist of:		
Noncurrent assets	$ -	$ -
Current liabilities	(150,000)	(98,000)
Noncurrent liabilities	(2,225,000)	(2,206,000)
Net amount recognized in accrued liabilities	$ (2,375,000)	$ (2,304,000)
Weighted average assumptions used to calculate the benefit obligation at May 31		
Discount rate	3.4%	3.8%
Expected return on plan assets	-	-
Rate of compensation increase	-	-

NOTE 17 - EMPLOYEE BENEFIT PLANS (cont.)

Assumed health care cost trend rates at May 31

Health care cost trend rate assumed for next year	3.9%	3.9%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	3.9%	3.9%
Year that the rate reaches the ultimate trend rate	2074	2074

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, 2019	$ 207,000	$ (239,000)

Annual premium payments were approximately $70,000 and $91,000 for the years ended May 31, 2019 and 2018, respectively. During the fiscal year ending May 31, 2020, the College expects to contribute $147,000 in benefit payments for the postretirement medical plan.

Estimated future postretirement medical payments (which reflect expected future service, as appropriate) as of May 31, 2019 are as follows:

Years Ending May 31	
2020	$ 147,000
2021	165,000
2022	180,000
2023	164,000
2024	151,000
2025 - 2039	2,475,000

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 - EXPENSE ALLOCATIONS

The financial statements report certain categories of expenses that are related to more than one program or supporting function. These expenses include depreciation and amortization, interest, information technology, and facilities operations and maintenance. Depreciation expense is allocated based on the use of the building or equipment. Expenses for the administration, supervision, operation, maintenance, preservation, and protection of the College's physical plant are allocated based on square footage methodology. Interest expense is allocated based on the use of space benefiting from debt proceeds. Costs of other categories are allocated on the basis of estimates of time and effort.

Expenses reported by function on the statement of activities are summarized by natural classification for the year ended May 31, 2019:

	Program Activities	Support Activities	Total Expenses
Salaries and wages	$ 23,666,776	$ 4,387,902	$ 28,054,678
Employee benefits	9,803,723	1,723,551	11,527,274
Student employment	2,326,876	174,951	2,501,827
Supplies and other operating expenses	3,036,657	2,337,876	5,374,533
Services and events	9,939,750	2,014,965	11,954,715
Occupancy and maintenance	3,093,957	289,359	3,383,316
Travel	3,843,065	336,819	4,179,884
Depreciation, amortization and accretion	6,100,451	618,269	6,718,720
Interest	780,154	23,523	803,677
Total expenses	$ 62,591,409	$ 11,907,215	$ 74,498,624

NOTE 19 – CONCENTRATIONS

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 65% 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 12.23 and a total risk-based capital ratio of 13.20. 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 20 - SUBSEQUENT EVENTS

Luther College has evaluated subsequent events through September 10, 2019, which is the date that the financial statements were issued.