

**MEHARRY MEDICAL COLLEGE**  
**CONSOLIDATED FINANCIAL STATEMENTS**  
**JUNE 30, 2012 AND 2011**

MEHARRY MEDICAL COLLEGE

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## Independent Auditors' Report

The Board of Trustees  
Meharry Medical College  
Nashville, Tennessee

We have audited the accompanying consolidated statements of financial position of Meharry Medical College and Subsidiary (the "College") as of June 30, 2012 and 2011, and the related consolidated statements of activities and cash flows for the years then ended. These consolidated financial statements are the responsibility of the College's management. 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, and the standards applicable to a financial audit contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Meharry Medical College and Subsidiary as of June 30, 2012 and 2011, the changes in their net assets and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

*Crosslin & Associates, P.C.*

Nashville, Tennessee  
October 15, 2012

MEHARRY MEDICAL COLLEGE  
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

ASSETS

	June 30,	
	2012	2011
Cash and cash equivalents	\$ 18,549,746	\$ 17,275,219
Accounts receivable, net	15,887,082	15,964,217
Student loans receivable, net	13,539,909	13,468,235
Contributions receivable, net	2,675,067	1,149,577
Investments	116,770,677	111,318,214
Investment in real estate, net	27,525,774	28,659,730
Plant facilities, net	66,573,041	61,592,539
Funds held by trustees	1,847,050	1,636,474
Deferred charges	657,959	796,887
Other assets	659,567	19,935
Total assets	\$264,685,872	\$251,881,027

LIABILITIES AND NET ASSETS

Notes payable to banks	\$ 9,396,728	\$ -
Accounts payable	3,493,449	3,696,227
Accrued liabilities	14,415,600	14,418,778
Advances under grants and contracts	2,212,365	2,889,558
Deferred revenue	6,560,233	7,296,467
Bonds payable	37,473,169	48,757,223
Government advances for student loans	12,829,930	12,586,529
Funds held in trust for others	3,645,034	299,115
Total liabilities	90,026,508	89,943,897
Unrestricted:		
Undesignated	27,813,228	23,137,356
Pension asset	659,567	54,757
Unrealized loss on interest rate swap agreement	( 5,257,184)	( 3,913,893)
Refunding loss on debt service of bonds refinanced	( 5,585,658)	( 5,837,811)
Total unrestricted net assets	17,629,953	13,440,409
Temporarily restricted	34,836,030	32,349,359
Permanently restricted	122,193,381	116,147,362
Total net assets	174,659,364	161,937,130
Total liabilities and net assets	\$ 264,685,872	\$ 251,881,027

See accompanying notes to consolidated financial statements.

MEHARRY MEDICAL COLLEGE  
CONSOLIDATED STATEMENTS OF ACTIVITIES

	Year Ended June 30,	
	2012	2011
Changes in unrestricted net assets:		
Operating revenues:		
Tuition and fees	\$ 26,770,038	\$ 24,091,202
Less College funded scholarships	<u>( 4,446,641)</u>	<u>( 4,284,547)</u>
Net tuition and fees	22,323,397	19,806,655
Government grants and contracts	61,824,102	62,455,359
Private gifts, grants, and contracts	3,174,789	3,041,134
Sales and services of educational departments	1,026,233	886,968
Other sources	4,365,144	4,046,762
Health services division	36,974,540	36,888,565
Net assets released from restrictions	<u>10,294,797</u>	<u>9,767,496</u>
Total operating revenues	<u>139,983,002</u>	<u>136,892,939</u>
Operating expenses:		
Instruction	24,321,071	22,503,402
Research	20,749,587	21,755,663
Public service	12,418,206	14,445,486
Academic support	13,028,397	11,745,784
Student services	3,658,051	3,112,150
Institutional support	27,316,536	27,369,818
Health services division	<u>33,191,129</u>	<u>33,565,482</u>
Total operating expenses	<u>134,682,977</u>	<u>134,497,785</u>
Increase in unrestricted net assets from operating activities	5,300,025	2,395,154
Nonoperating items:		
Change in net minimum pension asset	607,810	884,962
Change in market value of interest rate swap agreement, net	<u>( 1,718,291)</u>	<u>525,227</u>
Increase in unrestricted net assets	<u>4,189,544</u>	<u>3,805,343</u>

MEHARRY MEDICAL COLLEGE  
CONSOLIDATED STATEMENTS OF ACTIVITIES - Continued

	Year Ended June 30,	
	2012	2011
Changes in temporarily restricted net assets:		
Gifts, grants, and contracts	9,272,526	6,960,850
Income on long-term investments, net	4,663,133	3,953,492
Net (loss) gain on investments	( 1,154,191)	12,183,879
Net assets released from restrictions	<u>( 10,294,797)</u>	<u>( 9,767,497)</u>
Increase in temporarily restricted net assets	<u>2,486,671</u>	<u>13,330,724</u>
Change in permanently restricted net assets:		
Gifts and grants	<u>6,046,019</u>	<u>5,526,043</u>
Increase in permanently restricted net assets	<u>6,046,019</u>	<u>5,526,043</u>
Increase in net assets	12,722,234	22,662,110
Net assets at beginning of year	<u>161,937,130</u>	<u>139,275,020</u>
Net assets at end of year	<u>\$ 174,659,364</u>	<u>\$ 161,937,130</u>

See accompanying notes to consolidated financial statements.

MEHARRY MEDICAL COLLEGE  
CONSOLIDATED STATEMENTS OF CASH FLOWS

	<u>Year Ended June 30,</u>	
	<u>2012</u>	<u>2011</u>
Cash flows from operating activities:		
Increase in net assets	\$ 12,722,234	\$ 22,662,110
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Depreciation	5,499,109	5,512,575
Amortization of deferred charges and bond discount	139,873	78,670
Contributions restricted for long-term investment	( 6,046,019)	( 5,489,923)
Net realized and unrealized loss (gain) on long-term investments	1,154,191	(12,183,879)
Loss from disposal of fixed assets	-	45,914
Changes in:		
Accounts receivable, net	77,135	5,334,856
Contributions receivable	( 1,525,490)	763,350
Inventory and other assets	( 639,632)	( 1,630)
Accounts payable	( 202,778)	( 382,209)
Accrued liabilities	( 3,178)	( 826,106)
Advances under grants and contracts	( 677,193)	1,278,535
Deferred revenue	( 736,234)	( 527,039)
Funds held in trust for others	<u>( 3,345,919)</u>	<u>( 1,516,626)</u>
Net cash provided by operating activities	<u>13,107,937</u>	<u>14,748,598</u>
Cash flows from investing activities:		
Acquisition of plant facilities	( 9,345,654)	( 3,383,559)
Purchases of investments, net	( 6,606,654)	( 5,232,788)
Funds held by trustees	<u>( 210,576)</u>	<u>( 176,763)</u>
Net cash used in investing activities	<u>(16,162,884)</u>	<u>( 8,793,110)</u>
Cash flows from financing activities:		
Proceeds from contributions restricted for long-term investment	6,046,019	5,489,923
Student loans receivable, net	( 71,674)	1,810,366
Change in government advances for student loans	243,401	215,818
Borrowings (repayments) on lines of credit and notes payable	-	( 2,500,000)
Proceeds of notes payable	9,548,395	-
Principal repayments of notes payable	( 151,667)	-
Principal repayments of bonds	<u>(11,285,000)</u>	<u>( 2,980,000)</u>
Net cash provided by financing activities	<u>4,329,474</u>	<u>2,036,107</u>
Net increase in cash and cash equivalents	1,274,527	7,991,595
Cash and cash equivalents at beginning of year	<u>17,275,219</u>	<u>9,283,624</u>
Cash and cash equivalents at end of year	<u>\$ 18,549,746</u>	<u>\$ 17,275,219</u>
Supplemental cash flow information:		
Cash paid for interest	<u>\$ 2,855,750</u>	<u>\$ 2,934,002</u>

See accompanying notes to consolidated financial statements.

MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 AND 2011

A. ORGANIZATION AND PURPOSE

Meharry Medical College (the “College”) is a fully accredited, private college committed to training health care professionals and leaders in many medical and health related fields. The College exists to provide an excellent education in the health sciences, while maintaining a center of excellence for the practice and delivery of health care, and the conduct of both basic and clinical research.

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation and Accounting

The consolidated financial statements of the College have been prepared on the accrual basis of accounting and in accordance with the accounting principles generally accepted in the United States of America.

The consolidated financial statements include the operations of the College and its wholly owned subsidiary, Meharry Housing Corporation. All significant intercompany activity has been eliminated in consolidation.

To ensure observance of limitations and restrictions placed on the use of resources available, the College maintains its accounts in accordance with the principles and practices of fund accounting. Fund accounting is the procedure by which resources for various purposes are classified for accounting purposes into funds that are maintained in accordance with activities or objectives of the College.

For external financial reporting purposes, Accounting Standard Codification (“ASC”) 958 *Not-for-Profit Entities*, requires that resources be classified into three net asset categories according to donor-imposed restrictions. Net assets of the college and changes therein are classified as follows:

Unrestricted - Unrestricted net assets (which are free of donor-imposed restrictions) generally result from tuition and fees, revenues derived from providing educational and health services, receiving unrestricted government and private gifts, grants and contracts, less expenses incurred in providing educational and health services, raising contributions and performing administrative functions.



MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 AND 2011

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Temporarily Restricted - Temporarily restricted net assets generally result from contributions, earnings from endowed funds and other inflows of assets whose use by the organization is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the College pursuant to those stipulations.

Permanently Restricted - Permanently restricted net assets generally represent the contributions and other inflows of assets whose use by the College is limited by donor-imposed stipulations that neither expire by the passage of time nor can be fulfilled or otherwise removed by the College.

Use of Estimates in the Preparation of Financial Statements

Judgment and estimation are exercised by management in certain areas of the preparation of the consolidated financial statements. The more significant areas include the recovery period for plant facilities, the allocation of certain operating and maintenance expenses to functional categories, the collection of contributions receivable, and the valuation of receivables including the allowances for contractual adjustments and doubtful patient accounts receivable. Management believes that such estimates have been based on reasonable assumptions and that such estimates are adequate, however, actual results could differ from those estimates.

Contributions

The College reports gifts of cash and other assets as temporarily restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statements of activities as net assets released from restrictions. However, donor-restricted contributions whose restrictions are met in the same reporting period as received are reported in the consolidated statements of activities as unrestricted contributions. Expenses are reported as decreases in unrestricted net assets. Temporary restrictions on gifts to acquire long-lived assets are considered met in the period in which the assets are acquired or placed in service.

MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 AND 2011

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Contributions, including unconditional promises to give, are recognized as revenue in the period received. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value at the date of the gift. Contributions to be received after one year are discounted at a rate commensurate with the risk involved. Amortization of the discount is recorded as additional contribution revenue and used in accordance with donor-composed restrictions, if any, on the contributions. An allowance is made for uncollectible contributions based upon management's judgment and analysis of the creditworthiness of the donors, past collection experience and other relevant factors.

Cash and Cash Equivalents

Cash and cash equivalents include cash and highly liquid investments with original maturities of three months or less.

Inventories

Inventories consisting of supplies are stated at the lower of cost (first-in, first out) or market (net realizable value).

Accounts Receivable

The College records accounts receivable at their estimated net realizable value. An allowance for doubtful accounts is recorded based upon management's estimate of uncollectible accounts determined by analysis of specific balances and a general reserve based upon aging of outstanding balances. Past due balances are charged against the allowance when they are determined to be uncollectible.

Investments

Investments in equity securities with readily determinable fair value and all investments in debt securities are reported at fair value with gains and losses included in the consolidated statements of activities. Works of art, historical treasures, and similar assets held as part of collections are reported at the fair or appraisal value at the date of acquisition or contribution, respectively.

MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 AND 2011

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Investment in hospital facility is based upon the estimated fair value of the facility, which equates to the discounted payments to be received from the 30-year lease of the facility. The investment is being depreciated on a straight-line basis over the estimated useful life of the facility and equipment which range from ten to forty years.

Life Income and Gift Annuities

The College's split interest agreements with donors consist primarily of irrevocable charitable remainder trusts for which the College serves as trustee. Assets held in these trusts are included in investments. Contribution revenues are recognized at the dates the trusts are established after recording liabilities for the present value of the estimated future payments to be made to the donors and/or other beneficiaries. The liabilities are adjusted annually for changes in the value of the assets, accretion of the discount and other changes in the estimate of future benefits.

Plant Facilities

Plant facilities are stated at cost or estimated fair value at dates of gifts, less accumulated depreciation, computed on the straight-line basis over the estimated useful lives of the various assets, which range from 5 years to 40 years. Depreciation and operation and maintenance charges are allocated to appropriate functional expense categories. Plant disposals are removed from the records at time of disposal. The College lifts restrictions on contributions for long-lived assets at the time the assets are acquired.

Deferred Charges

Deferred charges consist of bond issuance costs, which are amortized on a straight-line basis over the lives of the related bond issues. As of June 30, 2012 and 2011, accumulated amortization was \$1,130,455 and \$1,051,611, respectively. The estimated future amortization expense for each of the next five years is approximately \$140,000.

Deferred Revenue

Early fall registration revenue and expenditures are deferred and are reported within the fiscal year in which the activities are completed.

MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 AND 2011

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Derivative Financial Instruments

The College employs derivatives in the form of interest rate swap agreements to manage market risk associated with outstanding variable-rate debt. Derivative financial instruments are reported at fair value with any resulting change in fair value recognized as a nonoperating item in the consolidated statements of activities.

Government Advances for Student Loans

Funds provided by the United States government under the Federal Perkins and Health Professions Student Loan programs are loaned to qualified students and may be reloaned after collection. These funds are ultimately refundable to the government and are therefore recorded as liabilities.

Health Services Division Revenue

Included in health services division revenue are amounts from the Meharry Medical Group, various clinics operated by the College and the Lloyd C. Elam Mental Health Center. The College has agreements with third-party payors that provide for payments to the College at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, per diem payments and capitation. Such revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Contractual adjustments are accrued on an estimated basis in the period that the related services are rendered and adjusted in future periods as final settlements are determined.

Program Services

The College's primary program services are instruction, research, health services, and public service. Expenses reported as academic support, student services, and auxiliary enterprises are incurred in support of these primary program services. Institutional support includes fundraising expenses of \$3,207,529 and \$2,727,987 in 2012 and 2011, respectively. For purposes of reporting fundraising expenses, the College includes those fundraising costs incurred by its Development Office as well as an estimate of payroll-related expenditures incurred by members of management in fundraising activities.

MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 AND 2011

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Income Taxes

The College has received a determination letter from the Internal Revenue service indicating it is exempt from Federal income taxes under Section 501(c)(3) of the Internal Revenue Code; accordingly, no provision for income taxes is made in the consolidated financial statements. The College is not classified as a private foundation.

The College accounts for the effect of any uncertain tax positions based on a more likely than not threshold to the recognition of the tax positions being sustained based on the technical merits of the position under examination by the applicable taxing authority. If a tax position or positions are deemed to result in uncertainties of those positions, any unrecognized tax benefit is estimated based on a cumulative probability assessment that aggregates the estimated tax liability for all uncertain tax positions. Tax positions for the College include, but are not limited to, its' tax-exempt status and determination of whether certain income is subject to unrelated business income tax. The College has determined that such tax positions do not result in an uncertainty requiring recognition.

Fair Value Measurements

Assets and liabilities recorded at fair value in the consolidated statements of financial position are categorized based on the level of judgment associated with the inputs used to measure their fair value (Note M). Level inputs are defined by ASC 820, *Fair Value Measurements*.

C. ACCOUNTS RECEIVABLE

Accounts receivable consist of the following at June 30, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Receivable from grantors	\$ 5,759,834	\$ 3,305,920
Professional services receivable	3,709,676	4,320,750
Patient receivables, net of contractual and doubtful account allowances of \$10,597,929 and \$18,767,376 at June 30, 2012 and 2011, respectively	3,602,695	4,850,219
Student accounts receivable, net of allowance of \$689,285 and \$358,721 at June 30, 2012 and 2011, respectively	1,805,885	3,324,998
Other accounts receivable	<u>1,008,992</u>	<u>162,330</u>
Total accounts receivable, net	<u>\$15,887,082</u>	<u>\$15,964,217</u>

MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 AND 2011

D. CONTRIBUTIONS RECEIVABLE

The College includes unconditional promises to give as contributions receivable in accordance with the provisions of ASC 958, *Not-for-Profit Entities*.

	2012	2011
Unconditional promises to give	\$ 2,954,140	\$ 1,183,492
Less unamortized discount at 5%	<u>( 279,073)</u>	<u>( 33,915)</u>
Unconditional promise to give, net	<u>\$ 2,675,067</u>	<u>\$ 1,149,577</u>
Amounts due in:		
Less than one year	\$1,144,140	\$1,083,492
Two to five years	<u>1,810,000</u>	<u>100,000</u>
	<u>\$2,954,140</u>	<u>\$1,183,492</u>

At June 30, 2012 and 2011, the College had also received bequest intentions and certain other conditional promises to give. These intentions and conditional promises to give are not recognized as assets and, if they are received, they will generally be restricted for specific purposes stipulated by the donors, primarily for faculty support, scholarships, or general operating support of a particular department or division of the College.

The College receives contributed services from alumni and other volunteers who assist in fundraising efforts through their participation in various fundraising drives. The value of such services, which the College considers not practicable to estimate, has not been recognized in the consolidated statements of activities.

E. STUDENTS LOANS RECEIVABLE

Student loans receivable at June 30, 2012 and 2011, consisted of the following:

	2012	2011
Notes receivable - students	\$ 13,860,685	\$ 13,817,735
Less allowance for doubtful loans	<u>( 320,776)</u>	<u>( 349,500)</u>
	<u>\$ 13,539,909</u>	<u>\$ 13,468,235</u>

MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 AND 2011

F. INVESTMENTS

Investments at June 30, 2012 and 2011, are summarized below:

	<u>2012</u>		<u>2011</u>	
	<u>Fair Value</u>	<u>Cost</u>	<u>Fair Value</u>	<u>Cost</u>
Marketable securities:				
Cash equivalents	\$ 1,204,862	\$ 1,204,862	\$ 408,754	\$ 408,754
Mutual funds	4,780,394	4,411,059	7,375,478	7,097,473
Common stocks	67,907,504	58,902,864	65,665,834	53,983,756
Bonds	38,658,955	38,358,614	34,177,547	33,806,897
Other	<u>4,218,962</u>	<u>4,218,962</u>	<u>3,690,601</u>	<u>3,690,601</u>
Total investments	<u>\$116,770,677</u>	<u>\$107,096,360</u>	<u>\$111,318,214</u>	<u>\$98,987,481</u>
Investment in real estate, net of accumulated depreciation		<u>\$27,525,774</u>		<u>\$28,659,730</u>

Mutual funds for 2012 and 2011 are comprised solely of fixed income securities.

The College's investments are substantially all permanently restricted endowment funds. The investment in real estate is comprised of the College's net investment in hospital facilities, which are leased to the Metropolitan Government of Nashville and Davidson County (the Metropolitan Government) to house the operations of the Metropolitan Government's Nashville General Hospital. The thirty-year lease with the Metropolitan Government began in December 1994 and provides for rent payments of \$4,000,000 per year.

G. PLANT FACILITIES

Plant facilities consist of the following at June 30, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Land and land improvements	\$ 6,461,224	\$ 5,466,046
Buildings and building improvements	109,061,090	104,124,495
Equipment	27,819,868	24,663,104
Art	433,194	433,194
Library and visual aids	4,262,147	4,262,147
Construction in progress	<u>255,813</u>	<u>-</u>
	148,293,336	138,948,986
Less accumulated depreciation	<u>( 81,720,295)</u>	<u>( 77,356,447)</u>
Plant facilities, net	<u>\$ 66,573,041</u>	<u>\$ 61,592,539</u>

MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 AND 2011

G. PLANT FACILITIES - Continued

Plant operations and maintenance expenditures of \$10,155,040 and \$8,139,346 for the fiscal years ended June 30, 2012 and 2011, respectively, are allocated among functional expenses based on square footage percentages.

Depreciation expense was \$5,499,109 and \$5,512,575 for 2012 and 2011, respectively (of which \$1,133,957, was depreciation on the College's investment in real estate), is allocated among the various functional expense categories. No interest expense was capitalized in 2012 or 2011.

H. NOTES PAYABLE TO BANKS

On December 13, 2011, the College entered into a \$910,000 note payable to a local bank for the purpose of purchasing certain property located in Nashville, Tennessee. Under this agreement, the related property serves as collateral. Pursuant to the promissory note, the College will make 12 consecutive quarterly payments of \$75,833 plus interest through December 13, 2014 at a fixed interest rate of 3.25%. As of June 30, 2012 the outstanding balance on this note totaled \$758,333.

In June 2012, the College entered into a \$8,638,395 note payable to a financial institution to provide funding for refinancing the unpaid balances from Revenue Bonds, Series 1998 and Revenue Bonds, Series 2001. Pursuant to the promissory note, the College will make 20 consecutive semi-annual principal payments of \$431,920 plus interest through June 1, 2022 at a fixed interest rate of 3.04%. The note is collateralized by certain property on the College's campus. As of June 30, 2012 the outstanding balance on this note totaled \$8,638,395.

In April 2012, the College entered into a \$5,000,000 revolving line of credit with a financial institution. All accrued interest shall be paid on the first (1<sup>st</sup>) day of each quarter and the principal balance and all unpaid accrued interest shall be due on the maturity date, April 26, 2015. Interest shall accrue at the 1 month LIBOR rate on the first (1<sup>st</sup>) day of each calendar month. As of June 31, 2012, there was no outstanding balance on the line of credit.

The notes payable contain certain restrictive covenants, including a minimum debt service coverage ratio. The College was in compliance with the covenants and ratios at June 30, 2012.



MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 AND 2011

H. NOTES PAYABLE TO BANKS - Continued

Aggregate maturities associated with notes payable and line of credit as of June 30, 2012 are as follows:

2013	\$1,599,092
2014	1,167,173
2015	1,015,506
2016	863,840
2017	863,840
Thereafter	<u>3,887,277</u>
	<u>\$9,396,728</u>

I. BONDS PAYABLE

Bonds payable consist of the following at June 30, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Revenue Bonds, Series 2009	\$17,025,000	\$17,025,000
Revenue Bonds, Series 2001	-	6,110,000
Revenue Bonds, Series 1998	-	3,375,000
Revenue Bonds, Series 1996, net of unamortized discount of \$11,831 and \$12,777 at June 30, 2012 and 2011, respectively	19,033,169	20,832,223
Housing Revenue Bonds, Series 1992	<u>1,415,000</u>	<u>1,415,000</u>
Total bonds payable, net	<u>\$37,473,169</u>	<u>\$48,757,223</u>

MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
JUNE 30, 2012 AND 2011

I. BONDS PAYABLE

The aggregate scheduled principal maturities of bonds payable at June 30, 2012, are as follows:

Revenue Year Ending <u>June 30,</u>	Revenue Bonds <u>Series 2009</u>	Revenue Bonds <u>Series 1996</u>	Housing Revenue Bonds <u>Series 1992</u>	<u>Total</u>
2013	\$ -	\$ 1,910,000	\$ 30,000	\$ 1,970,000
2014	-	2,030,000	35,000	2,065,000
2015	-	2,155,000	35,000	2,190,000
2016	-	2,290,000	35,000	2,325,000
2017	-	2,430,000	40,000	2,470,000
2018 and thereafter	17,025,000	8,230,000	1,210,000	26,465,000
Principal maturities	17,025,000	19,045,000	1,415,000	37,485,007
Less unamortized discount	<u>-</u>	<u>( 11,831)</u>	<u>-</u>	<u>( 11,831)</u>
Total bonds payable	<u>\$17,025,000</u>	<u>\$ 19,033,169</u>	<u>\$1,415,000</u>	<u>\$ 37,473,169</u>

On December 3, 2009, the College issued Adjustable Rate Revenue Refunding Bond, Series 2009 (Series 2009 Bonds), in the amount of \$17,025,000 through the Health and Educational Facilities Board of the Metropolitan Government of Nashville and Davidson County, Tennessee. These bonds are collateralized by a \$17,934,555 letter of credit. Under the terms of the bond indenture, the proceeds were used to refinance \$17,025,000 of the outstanding Series 1996 Revenue Bonds. The Series 2009 Bonds bear interest as determined weekly by the Remarketing Agent (.26% at June 30, 2012). In the event the remarketing agent is unable to remarket the bonds, the bonds become a demand note under an irrevocable letter of credit with a commercial bank.

On June 29, 2001, the College issued Taxable Variable Rate Demand Bonds, Series 2001 (Series 2001 Bonds), in the amount of \$12,500,000 through a consortium of commercial banks. This bond was converted into a term note with a commercial bank during fiscal year 2012 (See Note H).

On December 3, 1998, the College issued Revenue Bonds, Series 1998, in the amount of \$21,770,000 through the Health and Educational Facilities Board of The Metropolitan Government. This bond was converted into a term note with a commercial bank during fiscal year 2012 (See Note H).

The 2009 bond issue contains certain restrictive covenants, including a minimum debt service coverage ratio. As of June 30, 2012 and 2011, the College was in compliance with the restrictive covenants including the minimum debt service coverage ratio.

MEHARRY MEDICAL COLLEGE  
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I. BONDS PAYABLE - Continued

On August 14, 1996, the College issued Revenue Bonds, Series 1996, in the amount of \$55,050,000 through the Health and Educational Facilities Board of The Metropolitan Government. Under the terms of the bond indenture, the proceeds were used to refinance the Revenue Bonds, Series 1994 in the amount of \$48,725,000. The Revenue Bonds, Series 1996 were also issued to provide additional funding for the hospital renovation, to improve and acquire equipment for other related facilities, and for working capital. The Series 1996 bonds bear interest semi-annually at 3.85% to 6.00%. These bonds are collateralized by (1) all right, title, and interest of the College to rental payments owed to the College pursuant to the lease of the Facility to the Metropolitan Government, (2) the lien on the Facility pursuant to a mortgage and a security agreement, and (3) all funds held under the indenture. The trustee handling the bond issue held funds aggregating \$1,638,437 and \$1,371,814 at June 30, 2012 and 2011, respectively.

The College issued Housing Revenue Bonds, Series 1992, in the amount of \$1,715,000 through the Health and Educational Facilities Board of the Metropolitan Government. The bonds bear interest semiannually at 6.50% to 7.25%. These bonds are collateralized by a mortgage on the property and the mortgage is guaranteed by the U.S. Department of Housing and Urban Development. The bonds are subject to mandatory redemption prior to maturity for mandatory sinking fund installments which are required to be made in amounts sufficient to redeem or pay on June 1 of each year, the respective principal amount plus accrued interest through the date fixed for redemption. The trustee handling the bond issue held funds aggregating \$209,473 and \$178,020 at June 30, 2012 and 2011, respectively.

J. INTEREST RATE SWAP ARRANGEMENTS

To manage variable interest rate exposure for its debt portfolio, in December 1998, September 2001 and December 2009, the College entered into interest rate swap arrangements with major financial institutions. The total notional amounts were \$50,180,000 for these swap arrangements. The swap notional amounts of each contract will gradually decline, corresponding to the principal amortization of the College's Series 1998, Series 2001 and Series 2009 bonds.

The swap arrangements for the Series 1998 and Series 2001 expired in 2012 upon the refinancing of these bounds. The arrangements for the Series 2009 bonds are scheduled to expire in December 2024. The College pays a fixed rate of 4.70% under the remaining arrangements.

MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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J. INTEREST RATE SWAP ARRANGEMENTS - Continued

As of June 30, 2012 and 2011, the estimated fair value loss of the Series 2009 bond swap arrangements was \$5,257,184 and \$3,913,893, and is included in accrued liabilities and as a component of unrestricted net assets.

K. EMPLOYEE BENEFIT PLANS

The College sponsors multiple plans which cover substantially all employees of the College. Effective January 1, 2009, all plans were amended to meet the Internal Revenue Service's 403(b) plan amendments. The details of the plans as amended are as follows:

403(b) Meharry Medical College Defined Contribution Plan

The Plan is a defined contribution plan which covers substantially all employees except those in the residency programs. Union and non-union employees are eligible to participate upon reaching the age of eighteen, and are eligible to receive matching contributions upon reaching the age of twenty-one and completing one year of service. The Plan is funded by employee contributions which may not exceed the Internal Revenue Service annual limitations (\$17,000 and \$16,500 calendar year 2012 and 2011, respectively).

The College provides a contribution to the non-union employees at a rate equal to 1% of the non-union employee's compensation. In addition, the non-union employees receive a matching contribution of 100% of their elective deferral up to 4% of their compensation not to exceed \$11,000. The College has the discretion to vary the contribution rate.

Expense under this plan for the years ended June 30, 2012 and 2011 amounted to \$1,885,855 and \$1,813,081.

Retirement Income Plan

This noncontributory defined benefit retirement plan that covers only union eligible employees was frozen by an amendment adopted January 1, 2009. Pursuant to ASC 715 *Compensation - Retirement Benefits*, the College recognizes in its consolidated statements of financial position the over-funded or under-funded status of the defined benefit retirement plan.

MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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K. EMPLOYEE BENEFIT PLANS - Continued

The status of the plan at June 30, 2012 and 2011, was as follows:

	<u>2012</u>	<u>2011</u>
Change in benefit obligation:		
Projected benefit obligation at beginning of year	\$ 3,699,829	\$ 3,396,552
Service cost	63,858	69,625
Interest cost	235,488	233,801
Loss (gain) due to plan experience	( 64,642)	183,100
Actual benefit disbursements	<u>( 275,694)</u>	<u>( 183,249)</u>
Projected benefit obligation at the end of year	<u>3,658,839</u>	<u>3,699,829</u>
Change in plan assets:		
Fair value of plan asset at beginning of year	3,754,586	2,566,347
Actual contributions	795,000	895,000
Actual benefit disbursements	( 275,694)	( 183,249)
Actual return on plan assets	<u>44,514</u>	<u>476,488</u>
Fair value of plan assets at end of year	<u>4,318,406</u>	<u>3,754,586</u>
Funded status:		
Net pension asset	<u>\$ 659,567</u>	<u>\$ 54,757</u>
Key assumptions:		
Discount rate	7.50%	7.50%

The College's expected long-term return on plan assets assumption is based on a periodic review and modeling of the plans' asset allocation and liability structure over a long-term horizon. Expectations of returns for each asset class are the most important of the assumptions used in the review and modeling and are based on comprehensive reviews of historical data and economical/financial market theory. The expected long term rate of return on assets was selected from within the reasonable range of rates determined by (a) historical returns, net of inflation, for the asset classes covered by the investment policy, and (b) projections of inflation over the long term period during which benefits are payable to plan participants.

The College's investment policy includes various guidelines and procedures designed to ensure assets are invested in a manner necessary to meet expected future benefits earned by participants. The investment guidelines consider a broad range of economic conditions. Central to the policy are target allocation ranges by major asset categories.

MEHARRY MEDICAL COLLEGE  
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K. EMPLOYEE BENEFIT PLANS - Continued

The objectives of the target allocations are to maintain investment portfolios that diversify risk through prudent asset allocation parameters, achieve asset returns that meet or exceed the plans' actuarial assumptions, and achieve asset returns that are competitive with like institutions employing similar investment strategies.

The investment policy is periodically reviewed by the College and a designated third-party fiduciary for investment matters. The policy is established and administered in a manner so as to comply at all times with applicable government regulations.

The College expects to contribute \$795,000 to its pension plan in the year ended June 30, 2013.

The following pension benefit payments, which reflect expected future services and participants electing life annuities at retirement age 65, as appropriate, are expected to be paid for the years ended June 30:

2013	\$ 241,239
2014	341,482
2015	261,626
2016	327,200
2017	278,025
2018 to 2012	1,705,743

If lump sum payouts are elected they can materially accelerate cash benefit payments estimated above.

MEHARRY MEDICAL COLLEGE  
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L. NET ASSETS

Under provisions of ASC 958, unrestricted net assets are those which are not subjected to donor-imposed restrictions. Substantially all of the net assets classified as unrestricted in the consolidated statements of financial position as of June 30, 2012 and 2011 have been invested in property and equipment.

The refunding of debt service amounts shown as a reduction of unrestricted net assets resulted from refinancing transactions in 1997 and 1999, and represents the loss recognized under accounting principles generally accepted in the United States of America to enact the refinancing. This component of unrestricted net assets is being amortized into unrestricted net assets available for operations over the lives of the related bond issues.

Temporarily restricted net assets are primarily available for scholarships and instruction and research.

Permanently restricted net assets consist primarily of perpetual endowment funds, scholarships, and instruction and research.

MEHARRY MEDICAL COLLEGE  
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M. FAIR VALUES OF FINANCIAL INSTRUMENTS

Required disclosures concerning the estimated fair value of financial instruments are presented below. The estimated fair value amounts have been determined based on the College's assessment of available market information and appropriate valuation methodologies. The following table summarizes required fair value disclosures under ASC 825 *Financial Instruments* and measurements at June 30, 2012 and 2011 for the assets measured at fair value on a recurring basis under ASC 820 *Fair Value Measurements*:

June 30, 2012	Carrying Amount	ASC 825 Estimated Fair Value	Assets/Liabilities Measured at Fair Value	Fair Value Measurements Using		
				Level 1	Level 2	Level 3
Assets:						
Contributions receivable	\$ 2,675,067	\$ 2,675,067	\$ 2,675,067	\$ -	\$ 2,675,067	\$ -
Investments:						
Cash equivalents	1,204,862	1,204,862	1,204,862	1,204,862	-	-
Mutual funds	4,780,394	4,780,394	4,780,394	4,780,394	-	-
Common stocks	67,907,504	67,907,504	67,907,504	67,907,504	-	-
Corporate bonds	38,658,955	38,658,955	38,658,955	-	38,658,955	-
Other	4,218,962	4,218,962	4,218,962	4,218,962	-	-
Liabilities:						
Bonds payable	37,473,169	40,065,513	-	-	-	-
Note payable	9,396,728	9,308,086	-	-	-	-
Interest Rate Swap Agreement	5,257,184	5,257,184	5,257,184	-	5,257,184	-
June 30, 2011	Carrying Amount	ASC 825 Estimated Fair Value	Assets/Liabilities Measured at Fair Value	Fair Value Measurements Using		
				Level 1	Level 2	Level 3
Assets:						
Contributions receivable	\$ 1,149,577	\$ 1,149,577	\$ 1,149,577	\$ -	\$ 1,149,577	\$ -
Investments:						
Cash equivalents	408,754	408,754	408,754	408,754	-	-
Mutual funds	7,375,478	7,375,478	7,375,478	7,375,478	-	-
Common stocks	65,665,834	65,665,834	65,665,834	65,665,834	-	-
Corporate bonds	34,177,547	34,177,547	34,177,547	-	34,177,547	-
Other	3,690,601	3,690,601	3,690,601	3,690,601	-	-
Liabilities:						
Bonds payable	48,757,223	51,904,462	-	-	-	-
Interest Rate Swap Agreement	3,913,893	3,913,893	3,913,893	-	3,913,893	-



MEHARRY MEDICAL COLLEGE  
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M. FAIR VALUES OF FINANCIAL INSTRUMENTS - Continued

The following methods and assumptions were used to estimate the fair value of each class of financial instrument:

Cash and Cash Equivalents and Funds Held by Trustees

Cash is reflected at carrying value, which is considered its fair value.

Accounts and Student Loans Receivable

Accounts receivable consist primarily of receivables from grantor agencies, professional and patient receivables and other short-term receivables. The student loans receivable of \$13,539,909 and \$13,468,235 at June 30, 2012 and 2011, respectively, consist principally of government loan programs and are not readily marketable. The College has estimated their fair value to be the carrying value.

Accounts Payable, Accrued Liabilities, and Deferred Revenues

The carrying value of these items approximates fair value due to the short-term nature of the obligations.

Bonds Payable and Notes Payable

The bonds payable reflected in the consolidated financial statements bear interest at floating rates and fixed rates. Series 2009 bonds bear interest at floating rates. Series 1992 and 1996 bonds bear interest at fixed rates. The carrying value of the bonds will differ from their fair value depending on current market rates. The fair value was estimated by calculating the net present value of the future payment stream using the current market interest rate. The notes payable reflected in the consolidated financial statements are short-term revolving lines-of-credit. The carrying value of these items approximates fair value due to the short-term nature of the obligations.

Interest Rate Swap Agreements

Fair value has been estimated as the difference between the estimated future interest payments at contractual variable rates and expected future variable rates as of June 30, 2012 and 2011, respectively, and fixed interest rates specified in the related swap agreements, discounted to present value.

The fair value estimates presented herein are based on pertinent information available to management as of June 30, 2012 and 2011, respectively. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of the consolidated financial statements since that date, and current estimates of fair value may differ significantly from the amounts presented herein.

MEHARRY MEDICAL COLLEGE  
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N. COMMITMENTS AND CONTINGENT LIABILITIES

The College leases certain buildings and equipment under non-cancelable operating leases which expire at various dates through September 2013. Rent expense under these lease arrangements amounted to \$908,730 and \$980,430 for the years ended June 30, 2012 and 2011, respectively.

Future minimum rental payments required under operating leases that have initial or remaining lease terms in excess of one year as of June 30, 2012, are as follows:

<u>Year Ending June 30,</u>	<u>Amount</u>
2012	\$543,668
2013	<u>104,664</u>
	<u>\$648,332</u>

Certain revenues, particularly Federal and state grants and contracts, are subject to adjustments based upon review by the granting agencies. Management does not anticipate that adjustments, if any, arising from such reviews would have a material effect on the consolidated financial statements.

The College is a defendant in lawsuits arising in the normal course of business. Management and legal counsel are of the opinion that insurance coverage is sufficient to satisfy any judgment or settlement liability.

O. CONCENTRATIONS OF CREDIT RISK

The College, in connection with its activities, grants credit that involves, to varying degrees, elements of risk. The maximum accounting loss from credit risk is limited to the amounts that are recognized in the accompanying consolidated statements of financial position as accounts receivable at June 30, 2012 and 2011.

Financial instruments which potentially subject the College to concentrations of credit risk consist principally of cash and investments held by the College and certain investment institutions. Cash at June 30, 2012 includes demand deposits at high quality financial institutions. The deposits are exposed to credit risk to the extent they exceed federally insured limits. The exposure to concentrations of credit risk relative to securities is dependent on the College's investment objectives and policies.

MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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P. ENDOWMENT

The College's endowment consists of individual donor-restricted funds established for a variety of purposes. As required by Generally Accepted Accounting Principles, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

*Interpretation of Relevant Law*

The Board of Trustees of Meharry Medical College has interpreted the applicable state laws as requiring the preservation of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the College classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the College in a manner consistent with the standard of prudence prescribed by applicable state laws. In accordance with applicable state laws, the College considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- the duration and preservation of the fund;
- the purposes of the College and the donor-restricted endowment fund;
- general economic conditions;
- the possible effect of inflation and deflation;
- the expected total return from income and the appreciation of investments;
- other resources of the College; and
- the investment policies of the College

MEHARRY MEDICAL COLLEGE  
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P. ENDOWMENT - Continued

*Changes in Endowment Net Assets*

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
<i>Endowment net assets,</i> July 1, 2010	\$ -	\$ 11,116,098	\$110,621,319	\$ 121,737,417
Investment return:				
Investment income	-	3,953,492	-	3,953,492
Net appreciation (realized and unrealized)	-	12,183,879	-	12,183,879
Total investment return	-	16,137,371	-	16,137,371
Contributions	-	-	5,526,043	5,526,043
Appropriation of endowment assets for expenditure	-	( 3,617,212)	-	( 3,617,212)
<i>Endowment net assets,</i> June 30, 2011	-	23,636,257	116,147,362	139,783,619
Investment return:				
Investment income	-	4,663,133	-	4,663,133
Net appreciation (realized and unrealized)	-	( 1,154,191)	-	( 1,154,191)
Total investment return	-	3,508,942	-	3,508,942
Contributions	-	-	6,046,019	6,046,019
Appropriation of endowment assets for expenditure	-	( 3,145,650)	-	( 3,145,650)
<i>Endowment net assets,</i> June 30, 2012	\$ -	\$ 23,999,549	\$122,193,381	\$ 146,192,390

MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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P. ENDOWMENT - Continued

***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). Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce on average, over a period of five years, a total rate of return between 6% to 9% per year. Actual returns in any given 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 places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

***Spending Policy and How the Investment Objectives Relate to Spending Policy***

The College's objective is 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. The Board of Trustees has decided that a prudent spending policy provides 4.5% of the market value of the Endowment Funds to the College for annual operating needs. To smooth out the short-term fluctuations in market prices, a three-year moving average of market value is used.

Q. SUBSEQUENT EVENTS

The College has evaluated subsequent events through October 15, 2012, the issuance date of the College's consolidated financial statements, and has determined that the following subsequent events require disclosure:

On July 10, 2012, the College entered into a Delayed Draw Loan Agreement with First Tennessee Bank National Association. The Bank has made a commitment to make a loan in the principal sum of \$7.5 million. The proceeds of this loan will be used for the refinancing of certain properties, certain capital improvements, and will assist with the modifications and development of a Physician Assistant Program. During the draw period, interest only will be computed on the unpaid principal balance from time to time and is due and payable monthly on the first day of each month commencing August 1, 2012 until the end of the draw period. During the repayment period, interest on the unpaid principal balance is due monthly, commencing on August 1, 2014.

MEHARRY MEDICAL COLLEGE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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Q. SUBSEQUENT EVENTS - Continued

The unpaid principal balance is due twice annually in sixteen consecutive installments of principal. The interest rate on this note is variable and is based on changes in an independent index, which is the LIBOR Rate plus 1.65%, adjusted monthly.

On August 30, 2012, the College closed on a capital project loan in the form of a Future Advance Project Funding Bond Series (A 2012-8) in an amount not to exceed \$60,000,000. This funding was financed through the U.S. Department of Education's Capital Financing Program via Rice Capital Access Program, LLC. The loan proceeds will be used for the following projects: new construction and equipping of a campus center; new construction of residential facilities to house students, faculty, staff and medical/dental residents; renovation and equipping of the Hulda Lyttle Hall campus building for administrative offices; rehabilitation and equipping of Dorothy L. Brown dormitory-style residence hall; and the creation of a new parking garage to serve faculty, staff and students. The loan is structured as follows: capitalized interest through October 1, 2014 and the first monthly deposit are due on October 1, 2014. This is a 30 year fixed rate loan to mature on March 1, 2042. During the construction phase, the rates will be based on U.S. Treasury yields prevailing at the dates of each advance plus applicable federal financing bank and designated bonding fees. The series 2012-8 will be a fixed rate, equal to the U.S. Treasury Bond + 22.5 basis points.