HOOD COLLEGE OF FREDERICK, MARYLAND AND AFFILIATES

Consolidated Financial Statements

June 30, 2010 and 2009

(With Independent Auditors' Report Thereon)

HOOD COLLEGE OF FREDERICK, MARYLAND AND AFFILIATES

Table of Contents

KPMG LLP
2001 M Street, NW
Washington, DC 20036-3389

Independent Auditors' Report

The Audit Committee of the Board of Trustees
Hood College of Frederick, Maryland:

We have audited the accompanying consolidated balance sheets of Hood College of Frederick, Maryland and Affiliates (the College) as of June 30, 2010 and 2009, 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. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the College's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in notes 1, 4 and 8 to the consolidated financial statements, the College adopted the enhanced recognition and disclosure provisions of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 820, *Fair Value Measurements and Disclosures* as of July 1, 2008 and FASB ASC Section 958-205-45, *Other Presentation Matters*, as of July 1, 2008. The College has adopted the disclosure and measurement provisions of Accounting Standards Update (ASU) 2009-12 as of July 1, 2009.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Hood College of Frederick, Maryland and Affiliates as of June 30, 2010 and 2009, and their changes in net assets and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

KPMG LLP

November 12, 2010

HOOD COLLEGE OF FREDERICK, MARYLAND AND AFFILIATES

Consolidated Balance Sheets

June 30, 2010 and 2009

Assets		2010	2009
Cash and cash equivalents (note 2)	$	1,611,505	3,220,140
Inventories, prepaid expenses, and other assets		192,945	175,845
Receivables:			
Contributions, net (note 3)		1,112,425	36,829
Student fees, net of allowance of $96,252 in 2010 and $71,245 in 2009		474,799	501,928
Student loans, net of allowance of $44,510 in 2010 and $48,745 in 2009		2,624,156	2,714,087
Other		683,923	1,041,925
Total receivables, net		4,895,303	4,294,769
Investments (notes 4 and 5)		46,062,950	39,238,771
Interest in funds held in trust by others		14,528,712	14,933,855
Property and equipment, net (note 6)		36,958,407	34,806,541
Total assets	$	104,249,822	96,669,921
Liabilities and Net Assets			
Liabilities:			
Accounts payable and accrued expenses	$	5,276,897	4,502,610
Deferred tuition revenue and agency funds		411,110	479,845
Liabilities and deferred revenues under split-interest agreements		2,611,018	3,057,944
Refundable advances from U.S. government		2,411,075	2,381,178
Conditional asset retirement obligations (note 12)		1,566,541	1,579,621
Debt (note 7)		742,546	810,949
Total liabilities		13,019,187	12,812,147
Net assets:			
Unrestricted		36,440,552	34,002,572
Temporarily restricted (note 8)		17,607,047	14,652,104
Permanently restricted (note 8)		37,183,036	35,203,098
Total net assets		91,230,635	83,857,774
Commitments and contingencies (notes 7 and 14)			
Total liabilities and net assets	$	104,249,822	96,669,921

See accompanying notes to consolidated financial statements.

HOOD COLLEGE OF FREDERICK, MARYLAND AND AFFILIATES

Consolidated Statement of Activities

Year ended June 30, 2010

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Operating revenues, gains, and support:				
Gross tuition and fees	$ 40,414,117	—	—	40,414,117
Less discounts on tuition and fees	16,716,920	—	—	16,716,920
Tuition and fees, net	23,697,197	—	—	23,697,197
Contributions	3,336,990	2,328,342	1,041,077	6,706,409
Federal and state grants	2,093,890	—	—	2,093,890
Endowment spending and interest used in operations	626,566	1,727,774	—	2,354,340
Auxiliary enterprises, net of residence hall discounts of $211,375 (note 6)	6,860,673	—	—	6,860,673
Other educational and general	567,834	—	—	567,834
Net assets released from restrictions (note 7)	3,218,037	(3,218,037)	—	—
Total operating revenues, gains, and support	40,401,187	838,079	1,041,077	42,280,343
Operating expenses (note 11):				
Program services:				
Instructional	14,218,529	—	—	14,218,529
Student services	6,792,556	—	—	6,792,556
Auxiliary enterprises	5,243,139	—	—	5,243,139
Total program services	26,254,224	—	—	26,254,224
Management and general:				
Academic support	3,741,930	—	—	3,741,930
Institutional support	7,838,798	—	—	7,838,798
Total management and general	11,580,728	—	—	11,580,728
Total operating expenses	37,834,952	—	—	37,834,952
Change in net assets from operating activities	2,566,235	838,079	1,041,077	4,445,391
Nonoperating revenues and gains:				
Net investment gain (loss)	(99,313)	2,241,746	933,871	3,076,304
Change in value of split-interest agreements	(28,942)	(124,882)	4,990	(148,834)
Change in net assets from nonoperating activities	(128,255)	2,116,864	938,861	2,927,470
Change in net assets	2,437,980	2,954,943	1,979,938	7,372,861
Net assets at beginning of year	34,002,572	14,652,104	35,203,098	83,857,774
Net assets at end of year	$ 36,440,552	17,607,047	37,183,036	91,230,635

See accompanying notes to consolidated financial statements.

HOOD COLLEGE OF FREDERICK, MARYLAND AND AFFILIATES

Consolidated Statement of Activities

Year ended June 30, 2009

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Operating revenues, gains, and support:				
Gross tuition and fees	$ 38,441,623	—	—	38,441,623
Less discounts on tuition and fees	15,228,535	—	—	15,228,535
Tuition and fees, net	23,213,088	—	—	23,213,088
Contributions	5,128,213	901,971	268,456	6,298,640
Federal and state grants	2,702,172	—	—	2,702,172
Endowment spending and interest used in operations	677,190	1,900,703	—	2,577,893
Auxiliary enterprises, net of residence hall discounts of $375,800 (note 6)	6,716,370	—	—	6,716,370
Other educational and general	461,489	—	—	461,489
Net assets released from restrictions (note 7)	3,027,530	(3,030,857)	3,327	—
Total operating revenues, gains, and support	41,926,052	(228,183)	271,783	41,969,652
Program services:				
Instructional	14,627,845	—	—	14,627,845
Student services	6,617,932	—	—	6,617,932
Auxiliary enterprises	5,166,264	—	—	5,166,264
Total program services	26,412,041	—	—	26,412,041
Management and general:				
Academic support	3,931,910	—	—	3,931,910
Institutional support	8,421,824	—	—	8,421,824
Total management and general	12,353,734	—	—	12,353,734
Total operating expenses	38,765,775	—	—	38,765,775
Change in net assets from operating activities	3,160,277	(228,183)	271,783	3,203,877
Nonoperating revenues and gains:				
Net investment gain (loss)	(1,536,652)	(8,713,253)	(2,866,155)	(13,116,060)
Change in value of split-interest agreements	(66,553)	235,836	(19,406)	149,877
Change in net assets from nonoperating activities	(1,603,205)	(8,477,417)	(2,885,561)	(12,966,183)
Change in net assets	1,557,072	(8,705,600)	(2,613,778)	(9,762,306)
Net assets at beginning of year	33,183,611	22,596,836	37,839,633	93,620,080
Reclassification of net assets for FSP 117-1	(738,111)	760,868	(22,757)	—
Net assets at end of year	$ 34,002,572	14,652,104	35,203,098	83,857,774

See accompanying notes to consolidated financial statements.

HOOD COLLEGE OF FREDERICK, MARYLAND AND AFFILIATES

Consolidated Statements of Cash Flows

Years ended June 30, 2010 and 2009

		2010	2009
Cash flows from operating activities:			
Change in net assets	$	7,372,861	(9,762,306)
Adjustments to reconcile change in net assets to net cash provided by operating activities:			
Depreciation and amortization		1,614,313	1,494,970
Loss on sale of land held for sale and property and equipment		—	42,092
Accretion on asset retirement obligation		49,860	62,684
Settlement on asset retirement obligation		(62,940)	(6,461)
Bad debt expense		20,772	8,447
Net realized and unrealized (gain) loss on investments		(4,222,466)	12,740,049
Changes in value of split interest agreements		148,834	(149,877)
Proceeds from contributions restricted for long-term investment		(2,438,168)	(3,267,667)
Changes in assets and liabilities:			
Inventories, prepaid expenses, and other assets		(17,100)	(72,525)
Receivables		(713,249)	(370,914)
Accounts payable and accrued expenses		774,287	1,124,743
Deferred tuition revenue and agency funds		(68,735)	(55,595)
Liabilities and deferred revenues under split-interest agreements		(446,926)	(946,028)
Net cash provided by operating activities		2,011,343	841,612
Cash flows from investing activities:			
Purchases of property and equipment		(3,766,179)	(1,179,677)
Purchases of investments		(26,513,743)	(40,094,028)
Proceeds from sales and maturities of investments		24,168,339	37,997,014
Disbursements for loans to students		(186,798)	(410,240)
Repayments of loans by students		278,741	173,741
Net cash used in investing activities		(6,019,640)	(3,513,190)
Cash flows from financing activities:			
Principal repayments on lines of credit		—	(615,733)
Proceeds from borrowing under line of credit		—	615,733
Principal repayments on bond debt obligations and other debt		(269,683)	(106,804)
Proceeds from debt borrowings		201,280	40,250
Proceeds from contributions restricted for long-term investment		2,438,168	3,267,678
Net change in refundable advances from U.S. government		29,897	23,230
Net cash provided by financing activities		2,399,662	3,224,354
Net increase in cash and cash equivalents		(1,608,635)	552,776
Cash and cash equivalents at beginning of year		3,220,140	2,667,364
Cash and cash equivalents at end of year	$	1,611,505	3,220,140
Supplemental disclosure:			
Cash paid for interest	$	116,148	126,173
Capital lease		427,970	226,690

See accompanying notes to consolidated financial statements.

(1) Summary of Significant Accounting Policies

(a) Organization

Hood College of Frederick, Maryland was founded in 1893. It is a private institution of higher learning with an established tradition of providing a comprehensive academic program in the liberal arts and professional studies to approximately 2,500 undergraduate, graduate, and adult learner students. The students are predominantly from the mid-Atlantic region.

(b) Basis of Presentation

The consolidated financial statements of Hood College of Frederick, Maryland and Affiliates, (collectively, the College) include the accounts of the College, the Hood College Foundation (the Foundation), and the Hood College Limited Partnership (the Partnership), of which the College owns a 98% limited partnership interest and a 1% general partnership interest and the Foundation owns a 1% limited partnership interest. The Partnership owns the Frederick Airport Park Associates (FAPA), of which the Partnership owns a 94% limited partnership interest. All significant intercompany balances and transactions have been eliminated in consolidation.

FAPA ceased operations prior to June 30, 2010 and all capital was distributed prior to that date. The partners are in the process of dissolving the partnership and expect this to be completed by the end of December 2010. FAPA filed its final IRS Form 1065, U.S. Return of Partnership Income, for the calendar year 2009.

The consolidated financial statements of the College have been prepared on the accrual basis of accounting. Resources are reported, for accounting purposes, in separate classes of net assets based on the existence or absence of donor-imposed restrictions. In the accompanying consolidated financial statements, net assets that have similar characteristics have been combined into categories as follows:

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

Temporarily restricted – Net assets whose use by the College is subject to donor-imposed stipulations that can be fulfilled by actions of the College pursuant to those stipulations or that expire by the passage of time.

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

Revenues are reported as increases in unrestricted net assets unless the use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulations or by law. Expirations of temporary restrictions recognized on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassifications from temporarily restricted net assets (see note 8). 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.

In order to provide more information about operating results, the College instituted an operating measure within the Statements of Activities for the years ended June 30, 2010 and 2009. This change makes a distinction between operating and non-operating revenues and expenses and facilitates the ability to monitor financial activity relative to the College's operating budget.

(c) Cash and Cash Equivalents

Cash and cash equivalents consist of short-term, highly liquid investments with original maturities of three months or less at dates of purchase, except that any such investments purchased with funds held by endowment fund investment managers are classified with investments. Cash equivalents are carried at cost, which approximates market value.

(d) Contributions

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

(e) Student Loans and Refundable Advances from U.S. Government

Student loans consist primarily of funds loaned to students under the Federal Perkins Loan Program (FPL). Funds provided by the U.S. government under FPL are loaned to qualified students and may be reloaned after subsequent student repayments. These funds are ultimately refundable to the U.S. government and are included in liabilities.

(f) Investments and Interest in Funds Held in Trust by Others

Investments are reported at fair value based on quoted market prices, except for certain alternative investments such as hedge funds for which quoted market prices are not available. The estimated fair value of these investments is based on valuations provided by external investment managers. The College believes the carrying amount of these financial instruments is a reasonable estimate of fair value. Because these alternative investments are not readily marketable, their estimated value is subject to additional uncertainty, and therefore values realized upon disposition may vary significantly from currently reported values. The cost of investments sold is determined using the average cost method. Net realized and unrealized gains and losses on investments are reflected in the statements of activities. Dividends and interest are reflected as income when earned.

(Continued)

Pooled endowment and similar funds are invested on the basis of a total return policy to provide income and to realize appreciation in investment values. The income from the investment pool is proportionately allocated to the individual funds and used for purposes designated by the donors. Realized investment gains accumulated by these funds may be used to support operations. The College has specified a spending rate of 5% of the trailing 12-quarter average balance of its investment portfolio to fund operations.

(g) Split-Interest Agreements

The College's split-interest agreements consist primarily of irrevocable charitable remainder trusts held by others. At the dates these trusts are established, receivables and contribution revenues are recognized at the present value of the estimated future benefits to be received when the trust assets are distributed. The receivables are adjusted during the term of the trusts for changes in the value of assets, accretion of the discount and other changes in the estimates of future benefits. The present value is determined using management's estimate or expected timing of collections. The discount rates used for the years ended June 30, 2010 and 2009 ranged between 3.8% and 7.9%.

The College is also trustee of certain assets under split-interest agreements which provide for payments to the donors or their beneficiaries of income earned on related investments or specified annuity amounts. Assets held under these agreements are included in investments. Contribution revenues are recognized at the dates of the agreements after providing for the present value of estimated future payments to be made to the donors and/or their beneficiaries. The liabilities are adjusted during the terms of the agreements for accretion of the discount, payments made, and other changes in the estimates.

(h) Property and Equipment

Fixed assets are recorded at cost or, if donated, at estimated fair value at date of donation. Additions or improvements that extend the useful life of existing facilities are capitalized. Depreciation and amortization is computed on a straight-line basis over the estimated useful lives of the assets as follows:

Buildings and building improvements	40 years
Land improvements	15 years
Equipment, library books, and software	5 years

(i) Deferred Compensation

The College is obligated on a deferred compensation plan for the President of the College. The amount of deferred compensation is included in accounts payable and accrued expenses in the accompanying consolidated balance sheets.

(j) Conditional Asset Retirement Obligations

Conditional asset retirement obligations are reported at the estimated fair value of the liability associated with legal obligations related to an asset retirement in the period in which an obligation is incurred. The College capitalizes such costs and depreciates them over the useful life of the related asset.

(k) Functional Expenses

The College allocates its expenses on a functional basis among its various programs and supporting services. Expenses that can be identified with a specific program or supporting service are charged directly to the specific program or supporting service. Other expenses that are common to several functions are allocated.

The College revised the methodology used for allocating the expenses associated with occupying and maintaining the physical plant, such as depreciation, utilities, repairs, and maintenance. Previously such expenses were allocated to functions based on the relative cost of each function to total expenses. For the years ending June 30, 2010 and 2009, the College adopted a methodology consistent with Financial Accounting Standards Board (FASB) ASC 958, *Not For Profit Entities*, whereby expenses for operating and maintaining the physical plant are allocated based on the square footage of space occupied by each program and supporting service.

(l) Tax Status

Hood College is recognized as exempt from federal income tax, except on unrelated business activities, under the provisions of Section 501(c)(3) of the Internal Revenue Code.

In June 2006, the Financial Accounting Standards Board (FASB) issued Interpretation Number 48, *Accounting for Uncertainty in Income Taxes* (included in FASB ASC 740-10 – *Income Taxes - Overall*). ASC 740-10 prescribes a threshold of more-likely-than-not for recognition and derecognition of tax positions taken or expected to be taken in a tax return. ASC 740-10 also provides related guidance on measurement classification, interest and penalties and disclosure. As provided in FASB Staff Position FIN 48-3, *Effective Date of FASB Interpretation No. 48 for Certain Non-Public Enterprises*, Hood College has implemented ASC 740-10 for the year ended June 30, 2010. This implementation of ASC 740-10 had no impact on the College’s statement of financial position or statement of activities, as there were no unrecognized tax benefits or liabilities that needed to be recorded.

(m) Fair Values of Financial Instruments

As indicated above, investments are stated at fair value. The fair values of substantially all other financial instruments approximate their carrying values in the consolidated financial statements.

Effective July 1, 2008, the College adopted FASB ASC 820, *Fair Value Measurements and Disclosures* (ASC 820). ASC 820 defines fair value, requires expanded disclosures about fair value measurements, and establishes a three-level hierarchy for fair value measurements based on the inputs to the valuations of an asset or liability at the measurement date. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The following three-level hierarchy classifies the inputs used to determine fair value:

- Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities;

(Continued)

- Level 2 – Other observable inputs, either directly or indirectly, including:
  - Quoted prices for similar assets/liabilities in active markets;
  - Quoted prices for identical or similar assets in nonactive markets;
  - Inputs other than quoted prices that are observable for the asset/liability; and
  - Inputs that are derived principally from or corroborated by other observable market data.
- Level 3 – Unobservable inputs that are significant to the fair value measurement.

Effective July 1, 2009, the College applied the guidance in FASB Accounting Standards Update (ASU) 2009-12, *Fair Value Measurements and Disclosures – Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)* (ASU 2009-12), to its investments including equities, bonds and fixed income, hedge funds, real assets and private equity. This guidance permits, as a practical expedient, the fair values of investments within its scope to be estimated using net asset value per share or its equivalent.

(n) Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and judgments that affect the reported amounts of assets and liabilities and the disclosures of contingencies at the date of the consolidated financial statements and revenues and expenses recognized during the reporting period. Actual results could differ from those estimates.

(o) Other Recently Issued Accounting Pronouncements

In August 2008, the FASB issued FASB Staff Position No. 117-1, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds* (FSP No. 117-1). FSP No. 117-1 provides guidance on classifying the net assets associated with donor-restricted endowment funds held by organizations that are subject to an enacted version of Uniform Prudent Management Institutional Funds Act of 2006 (UPMIFA), which serves as a model act for states to modernize their laws governing donor-restricted endowment funds. The State of Maryland enacted a version of UPMIFA effective April 14, 2009, the provisions of which apply to funds existing on or established after that date. Based on the interpretation of UPMIFA, FSP No. 117-1 required reclassifications of portions of donor-restricted endowment funds to different net asset categories. The provisions of FSP No. 117-1 are effective for the College for fiscal 2009 (note 18). In 2009, FSP FAS 117-1 was incorporated into FASB ASC 958, *Not-for-Profit Entities.*

(2) Cash and Cash Equivalents

Cash and cash equivalents are summarized as follows at June 30, 2010 and 2009:

		2010	2009
Cash on hand and in banks	$	1,536,593	3,121,555
Designated cash in banks:			
Federal Perkins Loan Fund		18,786	6,727
Split-interest agreements		56,126	91,858
	$	1,611,505	3,220,140

(3) Contributions Receivable

Contributions receivable at June 30, 2010 and 2009 are expected to be received as follows:

		2010	2009
Within one year	$	955,500	22,700
Between one and five years		389,345	20,700
		1,344,845	43,400
Allowance for uncollectible contributions		(46,425)	(6,510)
Unamortized discount (0.25%)		(185,995)	(61)
Gross Receivable	$	1,112,425	36,829

Approximately 86% and 77%, respectively, of contributions receivable and 48% and 69%, respectively, of total contributions revenue for the years ended June 30, 2010 and 2009 was received from three donors.

(4) Investments

Investments are summarized at fair value as follows at June 30, 2010 and 2009:

		2010	2009
Cash and cash equivalents	$	2,026,736	638,950
Equities		19,594,948	18,080,728
Hedge funds		7,831,188	6,864,906
Fixed income		15,606,362	12,582,978
Life insurance		51,168	85,705
Real estate investments		952,548	985,504
	$	46,062,950	39,238,771

(Continued)

Investments are professionally managed by outside organizations, subject to direction and oversight by a committee of the Board of Trustees (the Board). The Board has established investment policies and guidelines that cover asset allocations and performance objectives, and impose various restrictions and limitations on the managers. These restrictions and limitations are specific to each asset classification and cover concentration of market risk (at both the individual issuer and industry group levels), credit quality of fixed-income and short-term investments, use of derivative securities, investments in foreign securities and various other matters.

On September 29, 2008, the College was notified that the then-trustee of the Short-Term Fund of the Common Fund (the STF), Wachovia Bank, N.A., was resigning as trustee and had initiated the process of terminating the STF and had established procedures for the orderly liquidation and distribution of the assets of the STF over a period of time. On December 22, 2008, there was $2,163,963 remaining in the STF that was transferred to the new and current trustee, Law Debenture Trust Company of New York. Distributions from the Fund continue to be made as permitted. At June 30, 2010 and 2009, the College had $0 and $745,341, respectively, invested in the STF.

Net investment income (loss) consists of the following for the years ended June 30, 2010 and 2009:

		2010	2009
Investment income	$	1,311,917	2,492,326
Net realized gains (losses) on investments		95,704	(196,376)
Net unrealized appreciation (depreciation) in fair value		2,964,944	(3,296,002)
Net increase (decrease) in value of trusts held by others		1,161,818	(1,573,130)
Less investment management fees		(103,739)	(108,574)
	$	5,430,644	(2,681,756)

(5) Fair Value Measurements

The following table classifies all investments into the hierarchy set forth by ASC 820. The table includes those investments that are held and managed by the College (investments) and those investments that are held in trust by others for the benefit of Hood College (interest in funds held in trust by others).

The fair value of equity and bonds/fixed income securities are measured using quoted market prices at the reporting date when quoted market prices are available. When quoted market prices are not available, the College has used a practical expedient allowed under ASU 2009-12, where each investment's net asset value as reported by each fund manager is an acceptable measurement of fair value owned when coinciding with the College's measurement date. Equity fund investments are generally classified as Level 2 investments except where the fund is publicly traded.

	Level 1	Percentage	Level 2	Percentage	Level 3	Percentage	Total
Investments:							
Cash and cash equivalents	$ 2,026,736		$ —		$ —		$ 2,026,736
Equities	17,832,827		1,762,121		—		19,594,948
Hedge funds	1,121,105		6,710,083		—		7,831,188
Fixed income	15,394,250		212,112		—		15,606,362
Life insurance	—		51,168		—		51,168
Real assets investments	—		—		952,548		952,548
	$ 36,374,918	79%	$ 8,735,484	19%	$ 952,548	2%	$ 46,062,950
Interest in funds held in trust by others	$ —		$ 14,528,712	100%	$ —		$ 14,528,712

a) Cash & cash equivalents are comprised of cash held in the College's bank accounts, investments in money market funds awaiting reinvestment in the categories shown below and accrued interest receivable.
b) Equity investments are made through commingled accounts, managed accounts or mutual funds that hold primarily common stock of U.S., non-U.S., emerging markets and global companies.
c) Hedge funds are investments made through domestic or offshore mutual funds and fund of funds that may invest in a wide variety of assets globally, including equity and debt.
d) Fixed income investments are made through commingled accounts, managed accounts or mutual funds that may hold a variety of debt securities such as U.S. and international sovereign, agency, and corporate debt.
e) Life Insurance represents the cash surrender value of life insurance policies for which the College is beneficiary
f) Real assets are investments in REIT private funds, real estate partnerships, and joint ventures.

The College relies on a total return strategy in which investment returns are achieved through both capital appreciation and current yield. The long term objective is achieved by employing a diversified asset allocation and use of specialized investment managers.

The following table summarizes activity for assets measured at fair value on a recurrent basis using significant unobservable inputs (Level 3), which include real assets for the period from July 1, 2009 to June 30, 2010.

	Level 3 Assets Year ended June 30, 2010
Beginning balance	$ 985,504
Additions	-
Redemptions	-
Net realized gains (losses)	-
Net unrealized gains (losses)	(32,956)
Ending balance	$ 952,548

Gains and losses (realized and unrealized) included in changes in net assets for the period above are reported in net investment gain (loss) in the Statement of Activities.

The following table represents information on the College investments by major category where net asseet value as a practical expedient was used:

	Fair value as June 30, 2010	Redemption frequency	Redemption notice period
Equities - domestic (a)	$ 1,750,981	Daily	1 day
Hedge funds (b)	6,633,925	Quarterly to Annually	65 to 90 days
Real estate (c)	952,548	Quarterly	90 days
Total investments values using the practical expedient	$ 9,337,454		

The nature and risks inherent in each of the College's major categories of investments where the fair value was estimated using the practical expedient are summarized as follows:

a. Equities – Domestic - This category includes U.S. equity investments which share in the returns and risks associated with exposure to the U.S. equity markets.
b. Hedge Funds - Hedge fund investments are 14% of total investments and are comprised of domestic fund of funds, offshore low volatility multi-strategy funds, and international fund of funds. These hedge funds share in the returns and risks associated with U.S. and non-U.S. equity and credit markets, interest rates and foreign currencies. In addition, some of these funds may present lower liquidity, organizational risk, event and deal risks, leverage, and counterparty risk. Reduced redemption rights have been accepted for certain funds in order to achieve more desirable terms such as lower management fees. The College estimates that $3 million or 7% of total investments may not be redeemed until July 2011.
c. Real Estate - Real asset investments are 2% of total investments and consist of REIT private funds, real estate partnerships, joint ventures, mezzanine financing and commercial mortgage-backed securities. As a limited partner in these funds, the College's downside risk is limited to its investment in each fund. This investment's unique structure has been adversely impacted by the illiquid real estate market and the impairment has increased risks going forward. The College requested redemption of $650,000 on December 10, 2008 then expanded the request to 100% on June 14, 2010. Due to market conditions the fund postponed distributions until the underlying investments could be reasonably liquidated. The distributions are made pro rata based on the College's total investment in the Fund relative to the total of all redeeming investors' investments in the Fund. The fund made distributions in July and September 2010 representing 23% of the College's holdings. The College expects to receive the remaining balance during 2012.

(6) Property and Equipment

Property and equipment, net, consist of the following at June 30, 2010 and 2009:

	2010	2009
Land	$ 265,048	265,048
Land improvements	4,779,071	2,011,927
Buildings and building improvements	60,167,065	59,597,933
Equipment and library books	15,549,680	15,258,950
Software	515,445	473,561
Construction-in-progress	426,838	689,074
	81,703,147	78,296,493
Less accumulated depreciation and amortization	44,744,740	43,489,952
	$ 36,958,407	34,806,541

(7) Debt

Debt consists of the following at June 30, 2010 and 2009:

	2010	2009
Dormitory mortgage bonds	$ 106,000	127,000
Academic facilities loan	116,478	125,788
Promissory notes	335,681	513,159
Capital lease	184,387	32,904
Other	—	12,098
	$ 742,546	810,949

The dormitory mortgage bonds are due to the United States Department of Housing and Urban Development. The bonds bear interest at 3.625%, are due in annual installments through 2014, and are secured by a pledge of dormitory revenues.

The academic facilities loan is due to the United States Department of Education under its College Facilities program. The loan bears interest at 3% and interest and principal are due in semiannual installments through 2021. The loan is secured by certain energy conservation projects at the College.

One promissory note is due in January 2016 to an unrelated party. The note bears interest at 6.5% and interest and principal are due in quarterly installments through 2016.

Two capital leases are due to unrelated parties. One lease is due in 2012 and bears interest at 11.52%. A second lease is due in 2014 and bears interest at 7.31%. Payments are due in monthly installments of principal and interest. Future minimum payments as of June 30, 2010 are as follows:

		Capital Leases
Year ending June 30:		
2011	$	66,310
2012		48,932
2013		48,176
2014		48,176
Total minimum lease payments		211,594
Less – interest		(27,207)
Present value of minimum capital lease payments	$	184,387

Total lease payments were approximately $66,310 in 2010.

A summary of long-term debt principal payments, excluding capital lease, to maturity as follows:

2011	$	84,102
2012		87,896
2013		92,931
2014		98,225
2015		93,793
Thereafter		101,212
Total	$	558,159

Total interest expense on debt was $116,148 and $126,173 for the years ended June 30, 2010 and 2009, respectively.

(8) Net Assets

Temporarily restricted net assets are summarized as follows at June 30, 2010 and 2009:

	2010	2009
Instruction, scholarships, and academic support	$ 13,542,698	11,123,386
Property and equipment additions	1,720,134	1,299,430
Annuity and life income agreements	2,344,215	2,229,288
	$ 17,607,047	14,652,104

Permanently restricted net assets to be used primarily for instruction, scholarships, and academic support are summarized as follows at June 30, 2010 and 2009:

	2010	2009
Permanent endowment funds	$ 24,842,373	22,190,841
Endowment funds held in trust by third parties	12,340,663	13,012,257
	$ 37,183,036	35,203,098

During the years ended June 30, 2010 and 2009, temporarily restricted net assets were released from donor restrictions by incurring expenses of $3,218,037 and $3,001,298, respectively, satisfying the restricted purposes specified by the donors. In addition, during FY2009, $29,559 was received from trusts that were liquidated due to the death of the donors. Due to market value losses in a permanently restricted endowment held in trust by others that was liquidated and transferred to the pooled endowment investments, it was necessary for the College to replenish $3,327 of restricted endowment during FY2009.

(9) Endowment Net Assets

Interpretation of Relevant Law

Effective April 14, 2009, the state of Maryland enacted the Uniform Prudent Management of Institutional Funds Act (UPMIFA), the provisions of which apply to funds existing on or established after that date. In addition, in August 2008, the FASB issued FASB Staff Position No. 117-1, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act and Enhanced Disclosures for All Endowment Funds* (FSP No. 117-1). FSP No. 117-1 provides guidance on classifying the net assets associated with donor-restricted endowment funds held by organizations that are subject to the enacted version of UPMIFA. The provisions of the enacted version of UPMIFA and of FSP No. 117-1 are effective for the College for fiscal year 2009.

The key component of FSP No. 117-1 is a requirement to classify the portion of a donor-restricted endowment fund that is not classified as permanently restricted net assets as temporarily restricted net assets until appropriated for expenditure. Prior to June 30, 2008, the College recorded unappropriated gains and losses on some donor-restricted endowment funds as unrestricted net assets. This policy has been revised resulting in a cumulative reclassification of FY2009 unrestricted net assets to restricted net assets in the amount of $738,111.

Return Objectives and Spending Policy

Pooled endowment funds are invested on the basis of a total return policy to preserve and enhance the principal of the funds. The income from the investment pool is proportionately allocated to the individual funds and appropriated for use according to the spending guidelines of the Board of Trustees. The spending rate is 5% of the trailing 12-quarter average balance of the investment portfolio. Spending is consistent with the purposes designated by the donors. The most recent Investment Policy was reviewed and approved by the Board of Trustees in February 2005 with a subsequent change in asset allocation in April 2007.

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. Deficiencies of this nature that are reported in permanently restricted net assets were approximately $1,555,000 as of June 30, 2010. These deficiencies resulted from unfavorable market fluctuations that occurred during the year, especially on investment of new permanently restricted contributions.

Endowment net assets composition by type of fund as of June 30, 2010:

		Unrestricted	Temporarily restricted	Permanently restricted	Total
Donor-restricted endowment funds	$	—	10,302,208	24,827,117	35,129,325
Board-designated endowment funds		3,254,615	—	—	3,254,615
Endowment funds held in trust (FHIT)		—	968,176	12,278,157	13,246,333
Total endowment net assets	$	3,254,615	11,270,384	37,105,274	51,630,273

Changes in endowment net assets for the fiscal year ended June 30, 2010:

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Endowment net assets, beginning of year	$ 3,111,097	9,251,282	35,125,742	47,488,121
Investment return:				
Pooled net investment income	585,678	3,202,747	—	3,788,425
FAPA investment loss	(35,535)	—	—	(35,535)
FHIT net investment income	204,125	525,981	933,871	1,663,977
	754,268	3,728,728	933,871	5,416,867
Contributions	—	17,166	1,045,661	1,062,827
Appropriation of endowment assets for expenditure:				
Spending withdrawal from pooled investments	(406,625)	(1,428,758)	—	(1,835,383)
Income distributions from funds-held-in-trust	(204,125)	(298,034)	—	(502,159)
	(610,750)	(1,726,792)	—	(2,337,542)
Replenish permanently restricted corpus	—	—	—	—
Endowment net assets, end of year	$ 3,254,615	11,270,384	37,105,274	51,630,273

Endowment net assets composition by type of fund as of June 30, 2009:

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Donor-restricted endowment funds	$ —	8,513,157	22,171,002	30,684,159
Board-designated endowment funds	3,111,097	—	—	3,111,097
Endowment funds held in trust (FHIT)	—	738,125	12,954,740	13,692,865
Total endowment net assets	$ 3,111,097	9,251,282	35,125,742	47,488,121

Changes in endowment net assets for the fiscal year ended June 30, 2009:

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Endowment net assets, beginning of year	$ 3,920,145	17,432,766	37,732,010	59,084,921
Investment return:				
Pooled net investment income	(411,003)	(6,175,691)	—	(6,586,694)
FAPA investment loss	(40,579)	—	—	(40,579)
FHIT net investment income	236,354	(115,873)	(2,866,155)	(2,745,674)
	(215,228)	(6,291,564)	(2,866,155)	(9,372,947)
Contributions	—	10,020	256,558	266,578
Appropriation of endowment assets for expenditure:				
Spending withdrawal from pooled investments	(357,466)	(1,204,492)	—	(1,561,958)
Income distributions from funds-held-in-trust	(236,354)	(695,448)	—	(931,802)
	(593,820)	(1,899,940)	—	(2,493,760)
Replenish permanently restricted corpus	—	—	3,329	3,329
Endowment net assets, end of year	$ 3,111,097	9,251,282	35,125,742	47,488,121

(10) Retirement Plans

Retirement benefits for substantially all full-time employees are provided under a defined contribution program with Teachers Insurance and Annuity Association (TIAA) and/or College Retirement Equities Fund (CREF). Other employees may enter the annuity program at their option. Participants are eligible for the program immediately upon employment and have a fully vested interest in the total contributions made on their behalf. Under the plan, the College has no obligations other than its annual contribution of approximately $436,323 and $1,126,737 for the years ended June 30, 2010 and 2009, respectively. Due to concerns about the impact of the economic downturn on enrollment and tuition revenue, the College reduced the employer match from twice to three-quarters of the employee contribution for FY2010. College contributions are dependent upon employee contributions and ranged from 1.13% to 3.75% during FY2010 and from 10% and 3% during FY2009 of each participant's regular salary. In July 2011, the College increased the employer contribution to 100% of the employee contribution.

(11) Related Party Transactions

In 2003, the College and the Foundation petitioned the Circuit Court for Frederick County for approval for a loan of endowment funds from the College to the Foundation and a further loan of those funds by the Foundation to the College, as evidenced by a promissory note collateralized by a lien on the campus. The Court Order was issued on July 25, 2003. The Court found that $10.5 million of gifts to the College were made by donors who are deceased and that the donors manifested a general intention to devote their property to charity and to benefit the College.

The Court approved and authorized the College and the Foundation to proceed as follows, with the Court retaining jurisdiction over this matter:

- Loan of funds on condition that the Foundation devote the funds to purposes consistent with the intent of donors, and in accordance with the Order.
- Loan by the Foundation to the College of $10.5 million for 10 years at 6.25%, secured by the deed of trust on the College's main campus until repayment in full of the promissory note. The College cannot mortgage or pledge the main campus as security for any other existing or future loan until repayment in full.
- If, in the future, the College must cease operations, the loan shall be due and payable immediately.

The College and the Foundation signed a promissory note, secured by the deed of trust on the campus on September 9, 2003. As of June 30, 2010, the College owes the Foundation $4,160,955 under the note. The College's promissory note and the Foundation's related loan receivable have been eliminated in the consolidated balance sheets.

In July 2010, the College fully repaid the promissory note to the Foundation and the funds were subsequently invested in the College's endowment assets. See Footnote Number 15, Subsequent Events.

(12) Conditional Asset Retirement Obligations

The College has identified asbestos abatement and other required disposals as conditional asset retirement obligations. Asbestos abatement and other costs were estimated using per square and linear foot estimates.

The conditional asset retirement obligations are summarized as follows at June 30, 2010 and 2009:

		2010	2009
Asset retirement obligation, beginning of year	$	1,579,621	1,523,398
Accretion		49,860	62,684
Settlements		(62,940)	(6,461)
Asset retirement obligation, end of year	$	1,566,541	1,579,621

(13) Expenses

A summary of expenses by natural classification for the years ended June 30, 2010 and 2009 were as follows:

		2010	2009
Salaries and fringe benefits	$	19,150,694	20,316,474
Travel and related expenses		1,298,957	1,334,577
Professional and contractual services		7,665,882	7,573,310
Funded student financial aid		1,984,636	1,975,897
Books and publications		333,620	293,923
Advertising, marketing and recruitment		136,224	245,397
Utilities and telecommunications		1,801,873	1,948,626
Property and liability insurance		238,535	342,163
Repairs and maintenance		158,653	102,866
Depreciation and amortization		1,614,313	1,494,970
Interest expense		116,148	126,173
Supplies		1,374,390	1,190,088
Postage, duplicating and printing		751,123	784,388
Rentals and leases		718,683	636,398
Other		491,221	400,525
Total expenses	$	37,834,952	38,765,775

Total fundraising expenses were $1,312,091 and $1,388,907 for the years ended June 30, 2010 and 2009, respectively.

(14) Commitments and Contingencies

The College has a letter of credit in the amount of $221,927 at June 30, 2010, expiring on September 30, 2011.

In November 2004, the College signed an agreement with a local bank for a line of credit in the amount of $1,000,000. The interest rate is 30-day LIBOR plus 2.5%. There were no draws on this line of credit during fiscal year 2010 and no outstanding balance at June 30, 2010.

The College is a party to various litigation in the ordinary course of business. Although there can be no assurance as to the eventual outcome of litigation in which the College has been named, in the opinion of management, such litigation will not, in the aggregate, have a material adverse effect on the College's financial position.

Amounts received and expended by the College under various federal and state programs are subject to audit by governmental agencies. In the opinion of management, audit adjustments, if any, will not have a significant effect on the financial position of the College.

(Continued)

(15) Subsequent Events

In preparing these financial statements, the College evaluated events and transactions for potential recognition or disclosure through November 12, 2010, the date the financial statements were available to be issued.

On July 28, 2010, the College closed on two loans totaling $20 million that allowed the College to fully repay the promissory note to the Hood College Foundation (see Footnote No. 11, Related Party Transactions) and to finance capital improvement projects, including replacement of the campus-wide heating system. Both loans are secured by a first priority lien on net tuition revenues and a negative pledge whereby the College agrees that it will not incur any mortgage, pledge, security interest, encumbrance, lien or charge of any kind upon any of its property except as specifically permitted by the bank.

The tax-exempt economic development revenue bonds, par amount of $15,800,295, bear interest at 68% of the one-month LIBOR plus 1.71%. The first principal payment is due on August 1, 2018. Payments are due in monthly installments through 2032. The College secured an interest rate swap from the bank which will become effective January 1, 2012. The interest rate swap will be 3.84% through August 2, 2017 and the nominal amount of the swap is $15,800,295.

The taxable term loan in the amount of $4,199,705 bears interest at one-monthly LIBOR plus 2.625%. The first principal payment is due on August 1, 2012. Payments are due in monthly installments through August 1, 2018. Funds from this loan in the amount of $4,160,955 were used to pay-off the promissory note between the College and the Hood College Foundation.

There were no additional events or transactions that were discovered during the evaluation that required further disclosure.