

UNIVERSITY OF ILLINOIS

Annual Financial Report

June 30, 2017

(With Independent Auditors' Report Thereon)

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UNIVERSITY OF ILLINOIS

Annual Financial Report

June 30, 2017

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UNIVERSITY OF ILLINOIS SYSTEM
URBANA-CHAMPAIGN • CHICAGO • SPRINGFIELD

Office of the Vice President, Chief Financial Officer
and Comptroller
349 Henry Administration Building
506 South Wright Street
Urbana, Illinois 61801

January 30, 2018

I am pleased to present the Annual Financial Report for the University of Illinois. The report provides financial information regarding the University of Illinois' financial position as of June 30, 2017, and results of operations and cash flows for the fiscal year then ended.

The report reveals a strong financial position despite the ongoing economic challenges, including a significant delay and reduction in appropriations from the State of Illinois. Through effective and efficient utilization of resources, prudent decision making and a commitment to excellence by faculty, administrators and staff, the institution continued to advance its mission.

The University of Illinois' tradition of excellence in teaching, research, public service, health care and economic development has made it a distinguished leader in higher education. Our efforts focus on continuing that tradition, while increasing the stature of the University of Illinois and the return on investment it provides to the State and the nation.

Respectfully submitted,



Avijit Ghosh,
Interim Vice President, Chief Financial Officer and Comptroller



INDEPENDENT AUDITORS' REPORT

Honorable Frank J. Mautino
Auditor General, State of Illinois
and Board of Trustees
University of Illinois

Report on the Financial Statements

As Special Assistant Auditors for the Auditor General, we have audited the accompanying financial statements of the business-type activities and aggregate discretely presented component units of University of Illinois (the University), collectively a component unit of the State of Illinois, as of and for the year ended June 30, 2017, and the related notes to the financial statements, which collectively comprise the University's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of the University's aggregate discretely presented component units (the University Related Organizations), as described in Note 1 of the financial statements. Those statements were audited by other auditors whose reports thereon have been provided to us, and our opinion on the financial statements, insofar as it relates to the amounts included for the University Related Organizations, is based solely on the reports of the other auditors. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits 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 from material misstatement.

The financial statements of The University of Illinois Alumni Association; Wolcott, Wood, and Taylor, Inc.; Prairieland Energy, Inc.; Illinois Ventures, LLC; The University of Illinois Research Park, LLC, and UI Singapore Research, LLC (discretely presented component units) were not audited in accordance with Government Auditing Standards.

Honorable Frank J. Mautino
Auditor General, State of Illinois
and Board of Trustees
University of Illinois

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

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

Opinions

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of University of Illinois and its aggregate discretely presented component units as of June 30, 2017, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

As discussed in Note 17 to the financial statements, Public Act 100-0021 granted the University fiscal year 2017 appropriations, totaling approximately \$300 million. Even though this law appropriated funds for the fiscal year ended June 30, 2017, it was enacted on July 6, 2017. To comply with GASB reporting requirements, the University intends to report this appropriation as revenue in the fiscal year ending June 30, 2018.

Other Matters

Report on Summarized Comparative Information

We have previously reported on the University of Illinois' 2016 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated February 1, 2017, prior to the identification of an error described in Note 1(t) Reclassifications. Because the University reclassified all Auxiliary Facilities System net position and Health Services Facilities System renewal and replacement reserve net position to restricted from unrestricted, we express no opinion on the University of Illinois summarized comparative information presented herein.

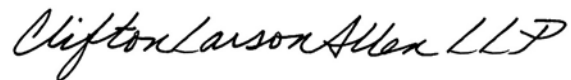
Honorable Frank J. Mautino
Auditor General, State of Illinois
and Board of Trustees
University of Illinois

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 5 through 12 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with Government Auditing Standards, we have also issued under separate cover our report dated January 30, 2018, on our consideration of University of Illinois' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the University's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards in considering University of Illinois's internal control over financial reporting and compliance.



CliftonLarsonAllen LLP

Peoria, Illinois
January 30, 2018

UNIVERSITY OF ILLINOIS

Management's Discussion and Analysis (Unaudited)

June 30, 2017

Introduction and Background

The following Management's Discussion and Analysis (MD&A) provides an overview of the financial position and activities of the University of Illinois (University) for the year ended June 30, 2017. The MD&A should be read in conjunction with the audited financial statements and notes appearing in this report.

The University was founded in 1867 in response to the federal Land Grant Act of 1862. The University's evolution as a land-grant institution has produced a set of core values that underlie all aspects of its present and future programs. The University is a comprehensive public university, with three primary locations –Urbana-Champaign, Chicago and Springfield - serving the people of Illinois through a shared commitment to the University's mission of excellence in teaching, research, public service, healthcare and economic development.

The University currently enrolls approximately 81,500 students. The University has internationally renowned faculty that are known for being world leaders in research and currently employs approximately 6,000 faculty members. The University offers a diverse range of degree programs from baccalaureate to doctoral levels. Approximately 21,500 degrees are awarded annually. University faculty, staff and students share their knowledge and expertise and the resources of the University with citizens in every corner of Illinois through more than 700 public service and outreach programs.

Using the Financial Statements

The University's financial report includes three financial statements: the Statement of Net Position; the Statement of Revenues, Expenses and Changes in Net Position, and the Statement of Cash Flows. The financial statements are prepared in accordance with Governmental Accounting Standards Board (GASB) principles, which establish standards for external financial reporting for public colleges and universities and require that financial statements focus on the University as a whole.

The financial statements encompass the University and its discretely presented component units: University of Illinois Foundation; University of Illinois Alumni Association; Wolcott, Wood and Taylor, Inc.; Illinois Ventures, LLC; University of Illinois Research Park, LLC; Prairieland Energy, Inc., and UI Singapore Research, LLC. This MD&A focuses on the University, excluding the discretely presented component units. Condensed financial information is disclosed separately for each of the discretely presented component units in Note 16 to the financial statements.

Financial Highlights and Key Trends

In fiscal year 2017, state appropriations (excluding capital) were \$356 million, up from \$182 million in fiscal year 2016. This increase, along with growth in tuition revenue, gifts received, investment-related gains and other factors, resulted in a \$53 million increase in net position. As in the past, the University relied on diverse sources of funding to support its mission.

Net position represents the residual interest in the University's assets and deferred outflows of resources after liabilities and deferred inflows of resources.

Statement of Net Position

The Statement of Net Position presents the financial position of the University at the end of the fiscal year and includes all assets, deferred outflows of resources, and liabilities of the University using the accrual basis of accounting. As of June 30, 2017 and 2016, the University did not have any deferred inflows of resources. Net position is one indicator of the current financial condition of the University. The changes in net position that occur over time indicate improvement or deterioration in the University's financial condition. Generally, assets and liabilities are reported at cost with the exception of investments, which are reported at fair value. Capital assets are reported at historical cost less accumulated depreciation. Deferred outflows of resources represent the losses on debt refundings, the change in fair value of the swap agreements associated with the related debt and the fiscal year 2017 employer pension contributions. A summarized comparison of the University's assets, deferred outflows of resources, liabilities and net position at June 30, 2017 and 2016 is as follows:

| | <u>2017</u> | <u>2016</u> |
|--|---------------------|------------------|
| | (In thousands) | |
| Current assets: | | |
| Cash and investments | \$ 815,430 | 876,476 |
| Accounts and notes receivable | 548,977 | 525,112 |
| Appropriations receivable from State of Illinois | 714 | 1,537 |
| Other current assets | 81,212 | 81,324 |
| Noncurrent assets: | | |
| Cash and investments | 1,827,011 | 1,813,963 |
| Notes receivable | 49,178 | 51,504 |
| Capital assets, net of accumulated depreciation | 3,751,300 | 3,711,559 |
| Other assets | 5,848 | 5,515 |
| Deferred outflows of resources | <u>76,876</u> | <u>99,473</u> |
| Total assets and deferred outflows of resources | <u>\$ 7,156,546</u> | <u>7,166,463</u> |
| Current liabilities: | | |
| Accounts payable, accrued liabilities and unearned revenue | \$ 702,021 | 698,838 |
| Bonds payable | 58,790 | 57,849 |
| Leaseholds payable and other obligations | 41,356 | 38,816 |
| Accrued self-insurance | 45,097 | 49,086 |
| Other current liabilities | 71,278 | 65,787 |
| Noncurrent liabilities: | | |
| Bonds payable | 1,226,540 | 1,283,023 |
| Leaseholds payable and other obligations | 252,656 | 285,169 |
| Accrued self-insurance | 194,388 | 170,148 |
| Accrued compensated absences | 184,214 | 176,896 |
| Derivative instruments – swap liability | <u>5,620</u> | <u>18,970</u> |
| Total liabilities | <u>2,781,960</u> | <u>2,844,582</u> |
| Net position | <u>4,374,586</u> | <u>4,321,881</u> |
| Total liabilities and net position | <u>\$ 7,156,546</u> | <u>7,166,463</u> |

Total assets and deferred outflows of resources decreased by \$10 million or 0.1% during fiscal year 2017. The relatively stable level of assets and deferred outflows was consistent with the improved stability of the University's financial condition, which is explained in connection with the Statement of Revenues, Expenses and Changes in Net Position.

Total liabilities decreased \$63 million, or 2.2% for fiscal year 2017. This change largely resulted from retirement of long term debt.

Capital Assets and Long-Term Debt

The University’s policy requires the capitalization of equipment at \$5,000, software and other intangibles at \$100,000, buildings and improvements at \$100,000, infrastructure at \$1,000,000 and all land and collection purchases regardless of cost. The University depreciates capital assets on a straight-line basis, using estimated useful lives ranging from 3 to 50 years. The following table illustrates the composition of the University’s capital assets, net of accumulated depreciation, by category:

Capital Assets, Net of Accumulated Depreciation
(In thousands)

| | <u>2017</u> | | <u>2016</u> | |
|---------------------------------|---------------------|---------------|---------------------|---------------|
| Buildings | \$ 2,661,729 | 71.0% | \$ 2,449,116 | 66.0% |
| Improvements and infrastructure | 263,793 | 7.0 | 282,352 | 7.6 |
| Construction in progress | 280,143 | 7.5 | 400,531 | 10.8 |
| Land | 136,472 | 3.6 | 135,822 | 3.6 |
| Equipment and software | 268,584 | 7.2 | 307,249 | 8.3 |
| Collections | 140,579 | 3.7 | 136,489 | 3.7 |
| | <u>\$ 3,751,300</u> | <u>100.0%</u> | <u>\$ 3,711,559</u> | <u>100.0%</u> |

Capital assets, net of accumulated depreciation, increased by \$40 million in fiscal year 2017. This increase included current year additions to buildings, partially offset by current year depreciation. Facilities improvements under construction were funded by revenue bonds, federal grants, private gifts, internal funds and State capital appropriations. Improvements to buildings included the Chemistry Annex, the University of Illinois Hospital (Hospital), State Farm Center and Willard Airport.

The University has historically utilized revenue bonds to finance capital projects related to the Auxiliary Facilities System (AFS), the Health Services Facilities System (HSFS) and the University of Illinois – Chicago (UIC) South Campus project. The following table details the various bonded debt outstanding at June 30, 2017 and 2016:

Bonds Payable
(In thousands)

| | <u>2017</u> | <u>2016</u> |
|------------------|---------------------|------------------|
| AFS | \$ 1,136,422 | 1,182,615 |
| HSFS | 112,758 | 116,144 |
| UIC South Campus | 36,150 | 42,113 |
| | <u>\$ 1,285,330</u> | <u>1,340,872</u> |

The University has issued Certificates of Participation (Certificates), which are reported as leaseholds payable in the financial statements. The outstanding Certificates have funded projects such as utility infrastructure, College of Medicine facilities and deferred maintenance on medical, academic and research facilities. The reduction in the outstanding balance of the Certificates was due to scheduled redemptions. As discussed in Note 8, certain Certificates of Participation were refunded during fiscal year 2017. The outstanding balances of the Certificates as of June 30, 2017 and 2016 were \$229,570,000 and \$253,155,000 respectively.

Net Position

The University's resources are classified into net position categories on the Statement of Net Position. These categories are defined as (a) Net investment in capital assets, (b) Restricted nonexpendable – net position restricted by externally imposed stipulations, (c) Restricted expendable – net position subject to externally imposed restrictions that can be fulfilled by actions of the University pursuant to those stipulations or that expire by the passage of time and (d) Unrestricted – net position not subject to externally imposed stipulations but may be designated for specific purposes by action of management or the Board of Trustees. The University's net position increased by \$53 million during fiscal year 2017. Net position balances are detailed below:

| | Net Position | |
|----------------------------------|-----------------------|--------------------|
| | (In thousands) | |
| | <u>2017</u> | <u>2016</u> |
| Net position: | | |
| Net investment in capital assets | \$ 2,297,463 | 2,248,166 |
| Restricted | 992,450 | 903,346 |
| Unrestricted | <u>1,084,673</u> | <u>1,170,369</u> |
| | <u>\$ 4,374,586</u> | <u>4,321,881</u> |

The overall increase in net position of \$53 million included growth in resources restricted for research, scholarships, fellowships, medical service plans and other specified programs, partially offset by a reduction in unrestricted net position resulting from State appropriations that were significantly below historic levels.

Statement of Revenues, Expenses and Changes in Net Position

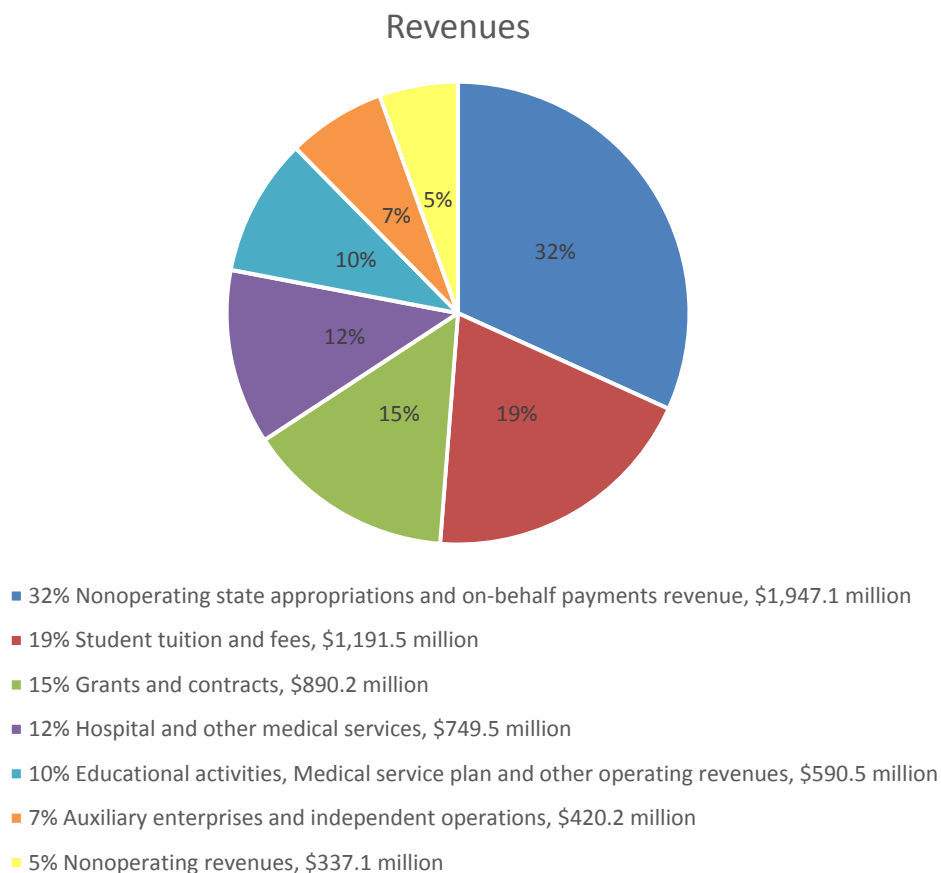
The Statement of Revenues, Expenses and Changes in Net Position presents the University’s results of operations. In accordance with GASB reporting standards, revenues and expenses are classified as either operating or nonoperating. A summarized comparison of the University’s Statement of Revenues, Expenses and Changes in Net Position for the years ended June 30, 2017 and 2016 is as follows:

| | <u>2017</u> | <u>2016</u> |
|--|---------------------|--------------------|
| | (In thousands) | |
| Operating revenues: | | |
| Student tuition and fees | \$ 1,191,498 | 1,145,945 |
| Grants and contracts | 890,162 | 831,651 |
| Hospital and other medical activities | 749,504 | 703,177 |
| Auxiliary enterprises and independent operations | 420,213 | 417,222 |
| Educational activities | 309,371 | 302,581 |
| Medical service plan | 261,072 | 206,513 |
| Other | 20,117 | 17,115 |
| Total operating revenues | <u>3,841,937</u> | <u>3,624,204</u> |
| Operating expenses | <u>6,136,621</u> | <u>5,702,494</u> |
| Operating loss | <u>(2,294,684)</u> | <u>(2,078,290)</u> |
| Nonoperating revenues (expenses): | | |
| State appropriations and on behalf payments | 1,967,236 | 1,517,993 |
| Transfer of state appropriation to the Illinois Hospital Services Fund | (20,177) | (11,105) |
| Private gifts | 190,183 | 158,913 |
| Grants, nonoperating | 110,561 | 111,067 |
| Investment income | 36,376 | 42,863 |
| Net increase (decrease) in the fair value of investments | 50,713 | (22,439) |
| Other nonoperating expenses, net | (12,431) | (7,157) |
| Net nonoperating revenues | <u>2,322,461</u> | <u>1,790,135</u> |
| Capital state appropriations and capital gifts and grants | 18,601 | 12,185 |
| Endowment gifts | <u>6,327</u> | <u>4</u> |
| Increase (decrease) in net position | 52,705 | (275,966) |
| Net position, beginning of year | 4,321,881 | 4,561,961 |
| Change in accounting principles | | 35,886 |
| Net position, end of year | <u>\$ 4,374,586</u> | <u>4,321,881</u> |

Revenues

The University’s revenues are generated from multiple sources, which supplement what is received from state appropriations and student tuition and fees. GASB reporting standards require revenues to be categorized as operating or nonoperating. Operating revenues are derived from activities associated with providing goods and services by the University and generally result from exchange transactions where each of the parties to the transaction either give up or receive something of equal or similar value. The University also relies on revenue, such as state appropriations, gifts, certain grants and investment income to support operations, which GASB reporting standards define as nonoperating.

The following graph illustrates the revenues by source (both operating and certain nonoperating), which were used to fund the University’s operating activities for the year ended June 30, 2017:



Operating and nonoperating revenues experienced a net increase of \$682 million in fiscal year 2017. This increase included \$275 million for payments on behalf by the State for employee fringe benefits (primarily retirement benefits) largely due to the State retirement system’s unfavorable investment performance, the recognition of certain assumption changes by the State’s actuaries, and the growth of the total actuarial-calculated pension liability exceeding the fiscal year contributions from the State. In addition, the increase included \$174 million for appropriations resulting from the stop-gap State budget. The University also achieved revenue growth from student tuition and fees, associated with rising enrollment, along with increased activity levels across a variety of operations.

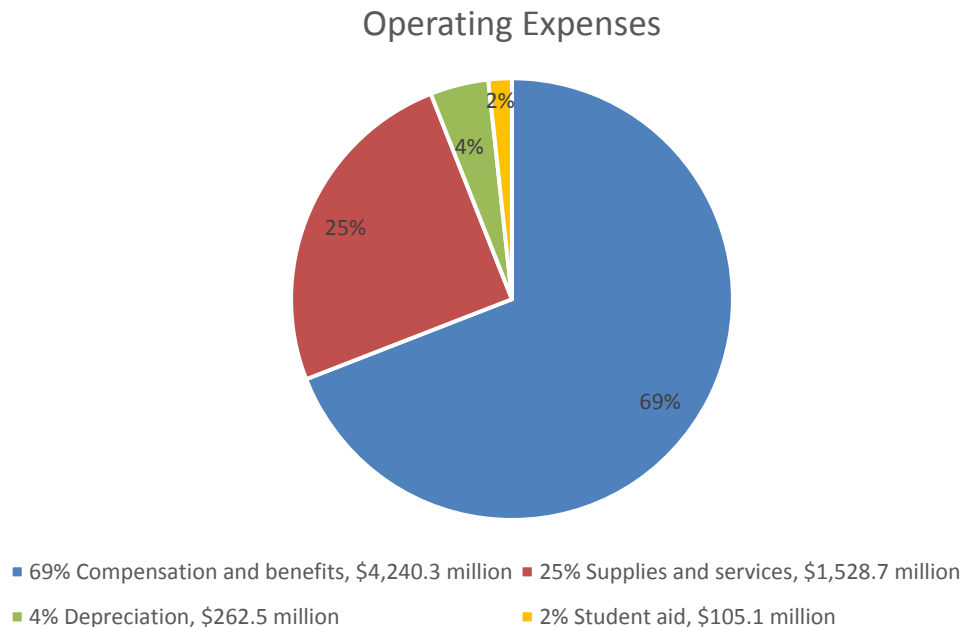
Expenses

The majority of the University’s expenses are exchange transactions, which GASB standards define as operating expenses. Nonoperating expenses include capital financing and other costs related to capital assets.

| | <u>2017</u> | | <u>2016</u> | |
|--|---------------------|---------------|---------------------|---------------|
| | (In thousands) | | | |
| Operating expenses: | | | | |
| Instruction | \$ 1,503,069 | 24.5% | \$ 1,380,175 | 24.2% |
| Research | 794,526 | 12.9 | 740,788 | 13.0 |
| Public service | 481,976 | 7.8 | 470,175 | 8.2 |
| Support services | 1,078,608 | 17.6 | 1,019,048 | 17.9 |
| Hospital and medical activities | 992,956 | 16.2 | 895,572 | 15.7 |
| Auxiliary enterprises and independent operations | 412,684 | 6.7 | 363,206 | 6.4 |
| Scholarships and fellowships | 298,955 | 4.9 | 278,994 | 4.9 |
| Operation and maintenance of plant | 311,313 | 5.1 | 299,657 | 5.2 |
| Depreciation | 262,534 | 4.3 | 254,879 | 4.5 |
| Total operating expenses | <u>\$ 6,136,621</u> | <u>100.0%</u> | <u>\$ 5,702,494</u> | <u>100.0%</u> |

The increase in operating expenses was \$434 million, or 7.6%. This change included increases in payments on behalf by the State for employee fringe benefits of \$275 million, which are allocated across the operating functions. Excluding the increase in on behalf payments, operating expenses increased by \$159 million, or 3.7%. Significant components of the rise in operating expenses from the prior fiscal year included increases in research, scholarship and support functions to facilitate student and faculty achievement, along with increases in self-supporting activities such as auxiliary enterprises, hospital and other medical activities.

The University chooses to report its expenses by functional classifications in the Statement of Revenues, Expenses and Changes in Net Position. For the reader’s information, the expenses are displayed in their natural classifications in Note 14. The following graph illustrates the \$6,136.6 million of operating expenses by natural classification:



The University's Economic Outlook

The University continues to maintain its level of excellence in service to students, patients, the research community, the State of Illinois (State) and the nation. A critical element to the University's future continues to be a strong partnership with the State, since State appropriations from the Governor and General Assembly provide essential operating support for University programs. The State appropriated a total of \$656 million which could be utilized to fund fiscal year 2017 expenditures. Due to the timing of two separate legislative actions authorizing the related appropriations, \$356 million of this amount was recognized by the University in fiscal year 2017 and the remaining \$300 million will be recognized in fiscal year 2018. Appropriations of \$589 million were enacted on July 6, 2017, which are intended to fund expenditures occurring in fiscal year 2018. This amount reflects a reduction of 10% from the appropriations which could be utilized to fund fiscal year 2017 expenditures.

Tuition rates are largely being held level between fiscal years 2017 and 2018. However, based on multiple factors (such as enrollment levels and student mix), the University projects an increase in the tuition revenue budget of approximately \$29 million. Undergraduate students have a four-year tuition guarantee. The incremental tuition revenue for fiscal year 2018 includes changes in enrollment patterns, entering undergraduate students paying higher tuition rates than the recent graduating class and varying increases in graduate and professional programs.

Research is an important component of the University's mission. The University consistently ranks among the top universities in research and development expenditures in the country. Research leading to the development of new products and services is also an engine driving economic development, another component of the University's mission. The University continues to advance the economic development mission by supporting research and innovation activities that elevate ideas into sustainable businesses and global solutions.

To maintain its financial position, the University continues to develop multiple sources of revenue to support its mission of teaching, research, public service, healthcare and economic development. The University's Board of Trustees, the administration, faculty and staff are committed to upholding the University's outstanding academic reputation and strong financial condition.

UNIVERSITY OF ILLINOIS

Statement of Net Position

June 30, 2017

(with summarized comparative information for June 30, 2016)

(In thousands)

| Assets and Deferred Outflows of Resources | University | | University Related Organizations | |
|--|--------------|--------------|----------------------------------|--------------|
| | 2017 | 2016 | 2017 | 2016 |
| Current assets: | | | | |
| Cash and cash equivalents | \$ 340,287 | \$ 391,466 | \$ 8,582 | \$ 6,548 |
| Cash and cash equivalents, restricted | 140,055 | 154,494 | 1,395 | 1,120 |
| Investments | 239,673 | 238,827 | 288 | 146 |
| Investments, restricted | 95,415 | 91,689 | | |
| Accrued investment income | 5,813 | 5,298 | 357 | 320 |
| Accounts receivable, net of allowance for uncollectible | 539,233 | 515,338 | 10,953 | 33,974 |
| Appropriations receivable from State of Illinois | 714 | 1,537 | | |
| Pledges receivable, net of allowance | | | 52,065 | 59,495 |
| Notes receivable, net of allowance for uncollectible | 9,744 | 9,774 | | |
| Accrued interest on notes receivable | 4,127 | 4,006 | | |
| Inventories | 32,017 | 31,989 | 6 | 6 |
| Prepaid expenses | 35,132 | 33,259 | 1,340 | 1,265 |
| Due from related organizations | 4,123 | 6,772 | | |
| Total current assets | 1,446,333 | 1,484,449 | 74,986 | 102,874 |
| Noncurrent assets: | | | | |
| Cash and cash equivalents, restricted | | 1,577 | 594 | 325 |
| Investments | 1,167,690 | 1,159,268 | 17,883 | 18,334 |
| Investments, restricted | 659,321 | 653,118 | 1,965,865 | 1,705,844 |
| Pledges receivable, net of allowance | | | 90,936 | 115,508 |
| Notes receivable, net of allowance for uncollectible | 49,178 | 51,504 | | |
| Capital assets, net of accumulated depreciation | 3,751,300 | 3,711,559 | 14,953 | 15,328 |
| Other assets | 5,848 | 5,515 | 131 | 127 |
| Total noncurrent assets | 5,633,337 | 5,582,541 | 2,090,362 | 1,855,466 |
| Deferred outflows of resources | 76,876 | 99,473 | 154 | 42 |
| Total assets and deferred outflows of resources | \$ 7,156,546 | \$ 7,166,463 | \$ 2,165,502 | \$ 1,958,382 |
| Liabilities, Deferred Inflows of Resources and Net Position | | | | |
| Current liabilities: | | | | |
| Accounts payable and accrued liabilities | \$ 380,616 | \$ 378,609 | \$ 7,324 | \$ 23,805 |
| Accrued payroll | 156,216 | 149,425 | 295 | 280 |
| Accrued compensated absences, current portion | 18,682 | 19,023 | 1,296 | 1,240 |
| Accrued self-insurance, current portion | 45,097 | 49,086 | | |
| Unearned revenue and student deposits | 165,189 | 170,804 | 31 | 210 |
| Accrued interest payable | 15,461 | 16,234 | | |
| Notes payable | | | 3,963 | 4,757 |
| Bonds payable, current portion | 58,790 | 57,849 | | |
| Due to related organizations, current portion | | | 4,123 | 6,772 |
| Leaseholds payable and other obligations, current portion | 41,356 | 38,816 | 5,950 | 6,280 |
| Assets held for others | 37,135 | 30,530 | 2,000 | 2,000 |
| Total current liabilities | 918,542 | 910,376 | 24,982 | 45,344 |
| Noncurrent liabilities: | | | | |
| Bonds payable | 1,226,540 | 1,283,023 | | |
| Leaseholds payable and other obligations | 252,656 | 285,169 | 43,899 | 47,125 |
| Accrued compensated absences | 184,214 | 176,896 | | |
| Accrued self-insurance | 194,388 | 170,148 | | |
| Unearned distributions | | | 126 | 128 |
| Derivative instruments— liability | 5,620 | 18,970 | 36 | |
| Total noncurrent liabilities | 1,863,418 | 1,934,206 | 44,061 | 47,253 |
| Deferred inflows of resources | | | 118 | 125 |
| Total liabilities and deferred inflows of resources | 2,781,960 | 2,844,582 | 69,161 | 92,722 |
| Net investment in capital assets | 2,297,463 | 2,248,166 | 10,990 | 10,571 |
| Restricted: | | | | |
| Nonexpendable | 111,302 | 101,756 | 1,047,433 | 990,278 |
| Expendable | 881,148 | 801,590 | 997,326 | 858,112 |
| Unrestricted | 1,084,673 | 1,170,369 | 40,592 | 6,699 |
| Total net position | 4,374,586 | 4,321,881 | 2,096,341 | 1,865,660 |
| Total liabilities, deferred inflows of resources and net position | \$ 7,156,546 | \$ 7,166,463 | \$ 2,165,502 | \$ 1,958,382 |

See accompanying notes to financial statements.

UNIVERSITY OF ILLINOIS

Statement of Revenues, Expenses and Changes in Net Position

Year Ended June 30, 2017

(with summarized comparative information for the year ended June 30, 2016)

(In thousands)

| | University | | University Related Organizations | |
|---|---------------------|---------------------|----------------------------------|---------------------|
| | 2017 | 2016 | 2017 | 2016 |
| Operating revenues: | | | | |
| Student tuition and fees, net | \$ 1,191,498 | \$ 1,145,945 | \$ | \$ |
| Federal appropriations | 18,264 | 15,826 | | |
| Federal grants and contracts | 672,091 | 653,156 | | |
| State of Illinois grants and contracts | 71,347 | 40,376 | | |
| Private and other government agency grants and contracts | 146,724 | 138,119 | 125,637 | 120,284 |
| Educational activities | 309,371 | 302,581 | | |
| Auxiliary enterprises, net | 409,484 | 406,620 | | |
| Hospital and other medical activities, net | 749,504 | 703,177 | | |
| Medical service plan | 261,072 | 206,513 | | |
| Independent operations | 10,729 | 10,602 | | |
| Interest and service charges on student loans | 1,853 | 1,289 | | |
| Allocation from the University | | | 13,997 | 13,804 |
| Other sources | | | 77,578 | 76,666 |
| Total operating revenues | <u>3,841,937</u> | <u>3,624,204</u> | <u>217,212</u> | <u>210,754</u> |
| Operating expenses: | | | | |
| Instruction | 1,503,069 | 1,380,175 | | |
| Research | 794,526 | 740,788 | | |
| Public service | 481,976 | 470,175 | | |
| Academic support | 573,787 | 523,540 | | |
| Student services | 218,887 | 198,433 | | |
| Institutional support | 285,934 | 297,075 | 107,743 | 109,072 |
| Operation and maintenance of plant | 311,313 | 299,657 | | |
| Scholarships and fellowships | 298,955 | 278,994 | | |
| Auxiliary enterprises | 402,930 | 353,159 | | |
| Hospital and medical activities | 992,956 | 895,572 | | |
| Independent operations | 9,754 | 10,047 | | |
| Depreciation | 262,534 | 254,879 | 1,823 | 1,878 |
| Distributions on behalf of the University | | | 196,666 | 163,132 |
| Total operating expenses | <u>6,136,621</u> | <u>5,702,494</u> | <u>306,232</u> | <u>274,082</u> |
| Operating loss | <u>(2,294,684)</u> | <u>(2,078,290)</u> | <u>(89,020)</u> | <u>(63,328)</u> |
| Nonoperating revenues (expenses): | | | | |
| State appropriations | 355,792 | 181,502 | | |
| Transfer of state appropriations to the Illinois Hospital Services Fund | (20,177) | (11,105) | | |
| Private gifts | 190,183 | 158,913 | | |
| Grants, nonoperating | 110,561 | 111,067 | | |
| On-behalf payments for fringe benefits | 1,611,444 | 1,336,491 | | |
| Net investment income (net of investment expense of \$5,687) | 36,376 | 42,863 | 5,570 | 12,285 |
| Net increase (decrease) in the fair value of investments | 50,713 | (22,439) | 256,393 | (76,441) |
| Interest expense | (65,734) | (62,188) | (101) | (72) |
| Loss on disposal of capital assets | (1,990) | (11,136) | | |
| Other nonoperating revenues, net | 55,293 | 66,167 | 213 | 110 |
| Net nonoperating revenues (expenses) | <u>2,322,461</u> | <u>1,790,135</u> | <u>262,075</u> | <u>(64,118)</u> |
| Income (loss) before other revenues | <u>27,777</u> | <u>(288,155)</u> | <u>173,055</u> | <u>(127,446)</u> |
| Capital state appropriations | 13,622 | 3,366 | | |
| Capital gifts and grants | 4,979 | 8,819 | | |
| Private gifts for endowment purposes | 6,327 | 4 | 57,160 | 32,271 |
| Increase (decrease) in net position | <u>52,705</u> | <u>(275,966)</u> | <u>230,215</u> | <u>(95,175)</u> |
| Net position, beginning of year | 4,321,881 | 4,561,961 | 1,865,660 | 1,960,835 |
| Cumulative effect of change in accounting principle | | 35,886 | | |
| Restatement, correction of an error | | | 466 | |
| Net position, beginning of year, as adjusted | <u>4,321,881</u> | <u>4,597,847</u> | <u>1,866,126</u> | <u>1,960,835</u> |
| Net position, end of year | <u>\$ 4,374,586</u> | <u>\$ 4,321,881</u> | <u>\$ 2,096,341</u> | <u>\$ 1,865,660</u> |

See accompanying notes to financial statements.

UNIVERSITY OF ILLINOIS

Statement of Cash Flows

Year ended June 30, 2017

(with summarized comparative information for the year ended June 30, 2016)

(In thousands)

| | University | |
|--|--------------|--------------|
| | 2017 | 2016 |
| Cash flows from operating activities: | | |
| Student tuition and fees | \$ 1,191,756 | \$ 1,135,487 |
| Federal appropriations | 14,698 | 16,074 |
| Federal, state, and local grants and contracts | 724,577 | 668,082 |
| Other governmental agencies and private grants and contracts | 137,323 | 148,681 |
| Sales and services of educational activities | 311,171 | 307,615 |
| Auxiliary activities and independent operations | 421,197 | 414,891 |
| Hospital and other medical activities | 770,079 | 656,541 |
| Medical service plan | 233,834 | 213,677 |
| Payments to employees and for benefits | (2,609,201) | (2,559,958) |
| Payments to suppliers | (1,521,932) | (1,521,097) |
| Payments for scholarships and fellowships | (104,554) | (79,427) |
| Student loans issued | (7,571) | (6,794) |
| Student loans collected | 9,382 | 9,554 |
| Student loan interest and fees collected | 1,732 | 1,751 |
| Net cash used in operating activities | (427,509) | (594,923) |
| Cash flows from noncapital financing activities: | | |
| State appropriations | 336,438 | 286,986 |
| Gifts transferred from University of Illinois Foundation | 190,183 | 158,913 |
| Direct lending receipts | 470,070 | 461,127 |
| Direct lending payments | (470,383) | (462,567) |
| Grants, nonoperating | 110,561 | 111,067 |
| Private gifts for endowment purposes | 6,327 | 4 |
| Repayments from (advances to) related organizations, net | 2,649 | (2,019) |
| Other receipts | 59,002 | 68,806 |
| Other disbursements | (653) | (125) |
| Net cash provided by noncapital financing activities | 704,194 | 622,192 |
| Cash flows from capital and related financing activities: | | |
| Proceeds from issuance of capital debt | 128,055 | 160,722 |
| Capital gifts and grants | 338 | 170 |
| Purchase of capital assets | (264,266) | (315,201) |
| Principal payments on bonds, capital leases, and other obligations | (214,715) | (233,073) |
| Interest payments on bonds, capital leases, and other obligations | (64,285) | (65,536) |
| Payment related to termination of interest rate swap agreement | (7,780) | |
| Payment of capital debt issuance costs | (868) | (1,078) |
| Net cash used in capital and related financing activities | (423,521) | (453,996) |
| Cash flows from investing activities: | | |
| Interest and dividends on investments, net | 32,277 | 34,648 |
| Proceeds from sales and maturities of investments | 2,514,938 | 1,918,151 |
| Purchase of investments | (2,467,574) | (1,646,907) |
| Net cash provided by investing activities | 79,641 | 305,892 |
| Net decrease in cash and cash equivalents | (67,195) | (120,835) |
| Cash and cash equivalents, beginning of year | 547,537 | 668,372 |
| Cash and cash equivalents, end of year | \$ 480,342 | \$ 547,537 |

UNIVERSITY OF ILLINOIS

Statement of Cash Flows

Year ended June 30, 2017

(with summarized comparative information for the year ended June 30, 2016)

(In thousands)

| | University | |
|---|-------------------|----------------|
| | 2017 | 2016 |
| Reconciliation of operating loss to net cash used in operating activities: | | |
| Operating loss | \$ (2,294,684) | \$ (2,078,290) |
| Adjustments to reconcile operating loss to net cash used in operating activities: | | |
| On-behalf payments for fringe benefits expense | 1,611,444 | 1,336,491 |
| Depreciation expense | 262,534 | 254,879 |
| Changes in assets, deferred outflows of resources and liabilities: | | |
| Accounts receivable, net | (29,834) | (55,220) |
| Notes receivable, net | 2,356 | 2,692 |
| Accrued interest on notes receivable | (121) | 462 |
| Inventories | (28) | (2,786) |
| Prepaid expenses | (1,873) | (5,735) |
| Deferred outflow of resources | (730) | (1,280) |
| Accounts payable and accrued liabilities | (11,582) | 11,333 |
| Accrued payroll | 6,791 | (20,378) |
| Unearned revenue and student deposits | (5,615) | (6,646) |
| Accrued compensated absences | 6,977 | (6,465) |
| Accrued self-insurance | 20,251 | (24,725) |
| Assets held for others | 6,605 | 745 |
| Net cash used in operating activities | \$ (427,509) | \$ (594,923) |
| Noncash investing, capital, and financing activities: | | |
| On-behalf payments for fringe benefits | \$ 1,611,444 | \$ 1,336,491 |
| State appropriation | 20,177 | 11,105 |
| Transfers to Illinois Hospital Services Fund | (20,177) | (11,105) |
| Net increase (decrease) in fair value of investments | 50,713 | (22,439) |
| Gifts in kind – capital assets | 4,825 | 8,614 |
| Increase (decrease) of capital asset obligations in accounts payable | 11,415 | (1,694) |
| Capital asset acquisitions by Capital Development Board | 13,622 | 3,366 |
| Capital asset acquisitions via leaseholds payable | 260 | 307 |
| Net interest capitalized | 8,669 | 9,966 |
| Other capital asset adjustments | 1,208 | (1,361) |
| Loss on disposal of capital assets | (1,990) | (11,136) |
| Capital appreciation on bonds payable | 6,234 | 7,039 |

See accompanying notes to financial statements.

UNIVERSITY OF ILLINOIS

Notes to Financial Statements

June 30, 2017

(1) Organization and Summary of Significant Accounting Policies

Organization

The University of Illinois (University), a federal land grant institution, founded in 1867 and a component unit of the State, conducts education, research, public service and related activities principally at its three locations in Urbana-Champaign, Chicago, which includes the University of Illinois Hospital (Hospital) and other healthcare facilities, and Springfield. The governing body of the University is The Board of Trustees of the University of Illinois (Board).

As required by U.S. generally accepted accounting principles, as prescribed by the Governmental Accounting Standards Board (GASB), these financial statements present the financial position and financial activities of the University (the primary government) and its component units as well as certain activities and expenses funded by other State agencies on behalf of the University or its employees. The component units discussed below are included in the University's financial reporting entity (Entity) because of the significance of their financial relationship with the University.

The University Related Organizations (UROs) column in the financial statements includes the financial data of the University's discretely presented component units. The University of Illinois Foundation (Foundation), the University of Illinois Alumni Association (Alumni Association), Wolcott, Wood and Taylor, Inc. (WWT), Prairieland Energy, Inc. (Prairieland), Illinois Ventures, LLC (Illinois Ventures), the University of Illinois Research Park, LLC (Research Park) and UI Singapore Research, LLC (Singapore Research) are included in the University's reporting entity because of the significance of their operational or financial relationship with the University. These component units are discretely presented in a separate column and are legally separate from the University.

The Foundation was formed for the purpose of providing fundraising and other assistance to the University in order to attract private gifts to support the University's instructional, research and public service activities. In this capacity, the Foundation solicits, receives, holds and administers gifts for the benefit of the University. Complete financial statements for the Foundation may be obtained by writing the Chief Financial Officer, 400 Harker Hall, 1305 W. Green Street, Urbana, Illinois 61801.

The Alumni Association was formed to promote the general welfare of the University and to encourage and stimulate interest among students, former students and others in the University's programs. In this capacity, the Alumni Association offers memberships in the Alumni Association to former students, conducts various activities for students and alumni, and publishes periodicals for the benefit of alumni. Complete financial statements for the Alumni Association may be obtained by writing the Controller, Alice Campbell Alumni Center, 601 S. Lincoln Avenue, Urbana, Illinois 61801.

WWT was formed to provide practice management support services and operate as a billing/collection entity for healthcare activities under the laws of the State. Complete financial information may be obtained by writing the President and CEO, 200 W. Adams, Suite 225, Chicago, Illinois 60606.

Prairieland was formed for the purpose of providing support for the University through delivery of comprehensive economical utility services to the University and other organizations. Complete financial information may be obtained by writing the Controller, 807 S. Wright Street, Suite 340, Champaign, Illinois 61820.

Illinois Ventures exists to facilitate the development of new companies commercializing technology originated or developed by faculty, staff and/or students of the University and other organizations. The University desires Illinois Ventures to foster technology commercialization and economic development in accordance with the teaching, research and public service missions of the University. Complete financial information may be obtained by writing the CEO and Managing Director, 2242 W. Harrison, Suite 201, Chicago, Illinois 60612.

Research Park was formed to aid and assist the University and other organizations by establishing and operating a research park with offices located in Champaign, Illinois. Research Park's jurisdiction extends to oversight of the research park in Urbana-Champaign. This jurisdiction also extends to potential research parks in Chicago and any other research parks in Illinois where the University has some operating responsibility by statute or contract. The Research Park was designed to promote the development of new companies, which commercialize University technologies. Complete financial information may be obtained by writing the Finance Manager, University of Illinois Research Park, LLC, 60 Hazelwood Drive, Champaign, Illinois 61820.

Singapore Research was formed to organize, develop, hold and operate, through a Singapore entity, a research center in Singapore to encourage and facilitate research, development and commercialization of the intellectual assets of the University. Complete financial information may be obtained by writing the Treasurer, UI Singapore Research, LLC, 349 Henry Administration Building, 506 South Wright Street, Urbana, Illinois 61801.

The Foundation, Alumni Association, WWT, Prairieland, Illinois Ventures, Research Park and Singapore Research are related organizations as defined under *University Guidelines* adopted by the State of Illinois Legislative Audit Commission.

The University is a component unit of the State for financial reporting purposes. The financial balances and activities included in these financial statements are, therefore, also included in the State's comprehensive annual financial report.

Significant Accounting Policies

(a) *Financial Statement Presentation and Basis of Accounting*

University

The University prepared its financial statements as a Business-Type Activity, as defined by GASB Statement No. 35, *Basic Financial Statements – and Management's Discussion and Analysis – for Public Colleges and Universities*, using the economic resources measurement focus and the accrual basis of accounting. Business-Type Activities are those financed in whole or in part by fees charged to external parties for goods and services.

Under the accrual basis, revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows. Grant and contract revenues, which are received or receivable from external sources, are recognized as revenues to the extent of related expenses or satisfaction of eligibility requirements. Advances are classified as unearned revenue. Appropriations made from the State for the benefit of the University are recognized as nonoperating revenues when eligibility requirements are satisfied.

The financial statements include certain prior year comparative information, which has been derived from the University's 2016 financial statements. Such information does not include all of the information required to constitute a presentation in conformity with U.S. generally accepted accounting principles. Accordingly, such information should be read in conjunction with the University's financial statements for the year ended June 30, 2016.

Certain items in the June 30, 2016 comparative information have been reclassified to correspond to the June 30, 2017 financial statement presentation.

UROs

The financial statements of WWT, Prairieland, Illinois Ventures, Research Park and Singapore Research are prepared using the same presentation and basis of accounting as the University, as described above.

The Foundation and Alumni Association follow Financial Accounting Standards Board (FASB) standards for financial statement presentation. Consequently, reclassifications have been made to reformat their financial statements to the GASB format for inclusion in the UROs column of the financial statements and disclosure in Note 16.

(b) *Cash and Cash Equivalents*

The Statement of Cash Flows details the change in the cash and cash equivalents balance for the fiscal year. Cash and cash equivalents include bank accounts and investments with original maturities of ninety days or less at the time of purchase. Such investments consist primarily of money market funds.

(c) *Inventories*

Inventories are stated at the lower of cost or market. Cost is determined principally by the average cost method or the first-in, first-out method, depending on the type of inventory.

(d) *Investments*

Investments are reported at fair value in accordance with guidelines defined by GASB Statement No. 72. Fair value is determined for the University's investments based upon a framework described in Note 2(f). The fair values of the farm properties held as investments are determined by a periodic appraisal of the property by a certified real estate appraiser. Fair value for investments in certain mutual funds, hedge funds and private equity is determined using net asset values (NAV) as provided by external investment managers. Bank deposits, money market funds, and Illinois public treasurer's investment pool are recorded at cost.

Changes in fair value during the reporting period are reported as a net increase (decrease) in the fair value of investments. Net investment income includes interest, dividends, and realized gains and losses.

(e) *Endowments*

For donor-restricted endowments, the Uniform Prudent Management of Institutional Funds Act (UPMIFA), as adopted in Illinois, permits the respective Boards of both the University and the Foundation to appropriate an amount of realized and unrealized endowment appreciation as they determine to be prudent. The University's policy is to retain the realized and unrealized appreciation (net appreciation) within the endowment pool after spending rule distributions.

University

The University's endowment pool investment policy follows the total return concept. The focus is to preserve the real value or purchasing power of endowment pool assets and the annual support the assets provide. Distributions are made from the University Endowment Fund to the University entities that benefit from the endowment funds. The endowment spending rule provides for an annual distribution of 4.0% of the two-quarter lagged, six-year moving average market value of fund units. At June 30, 2017, net appreciation of \$107,903,000 was available to be spent, of which \$82,406,000 was restricted to specific purposes.

URO – Foundation

Interpretation of Relevant Law: The board of directors of the Foundation interprets UPMIFA to require consideration of the following factors, if relevant, in making a determination to appropriate or accumulate donor-restricted endowment funds:

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

In accordance with the Foundation’s interpretation of UPMIFA, absent explicit donor stipulations to the contrary, the Foundation shall classify as permanently restricted net assets (restricted – nonexpendable) the original value of the gifts donated to the permanent endowment, but such classification does not limit the expenditures from the endowment fund only to income, interest, dividends, or rents, issues or profits. The portion of the fund’s value spendable annually for the donor-designated purpose is to be determined, from time to time, by the Foundation’s board of directors, acting in good faith, with the care that an ordinarily prudent person in a like position would exercise under similar circumstances, considering the above relevant factors. The Foundation’s Board approved spending was \$78,222,000 for fiscal year ended June 30, 2017.

(f) Capital Assets

Capital assets are recorded at cost or, if donated, at acquisition value at the date of a gift. Depreciation of the capital assets is calculated on a straight-line basis over the estimated useful lives (noted below) of the assets. The University’s policy requires the capitalization of land and collection purchases regardless of cost, equipment over \$5,000, software, easements, buildings and improvements over \$100,000 and infrastructure over \$1,000,000. The University does not capitalize collections, such as works of art or historical treasures, which are held for public exhibition, education or research in furtherance of public service rather than capital gain, unless they were previously capitalized as of June 30, 1999. Proceeds from the sale, exchange or other disposal of any item belonging to a collection must be applied to the acquisition of additional items for the same collection. Estimated useful lives for capital assets are as follows:

| | <u>Useful life (in years)</u> | | <u>Useful life (in years)</u> |
|-----------------|-----------------------------------|------------------------------------|-----------------------------------|
| Buildings: | | Improvements other than buildings: | |
| Shell | 50 | Site improvements | 20 |
| Service systems | 25 | Infrastructure | 25 |
| Fixed equipment | 15 | | |
| Remodeling | 25 | Moveable equipment | 3 – 20 |
| Intangibles: | | | |
| Software | 5 – 10 | | |

(g) **Deferred Outflows of Resources**

Under hedge accounting, the University has determined that the interest rate swap agreements on bonds payable and certificates of participation, as hedging derivative instruments, are an effective hedge. Accordingly, changes in the fair values of the interest rate swaps, since being associated with the related outstanding bonds or certificates, are reported as deferred outflows of resources on the accompanying Statement of Net Position. Additionally, interest rate swaps reassigned to new debt, after a refunding of debt that the swap was previously hedging, normally have an other than zero fair value upon the reassociation. For swaps with a fair value of other than zero upon reassociation with a hedgeable item, the fair value is amortized as an adjustment to interest expense in a systematic manner.

Losses on refunding of the University's bonds and certificates of participation are reported as deferred outflow of resources on the accompanying Statement of Net Position. The losses on refundings are amortized over the life of the debt using the straight-line method.

Employer pension contributions made in fiscal year 2017 are also reported as deferred outflows of resources.

| Deferred Outflow of Resources | | | | | |
|---|------------------------------|------------------|-------------------|---------------------------------|---------------------------|
| (In thousands) | | | | | |
| | Beginning balance | Additions | Deductions | Change in fair value | Ending balance |
| Interest rate swap | \$ 16,410 | 395 | 7,780 | (5,570) | \$ 3,455 |
| Unamortized deferred loss on refunding | 48,310 | 6,094 | 16,466 | | 37,938 |
| Pension contributions | 34,753 | 35,483 | 34,753 | | 35,483 |
| Total deferred outflow of resources | \$ 99,473 | 41,972 | 58,999 | (5,570) | \$ 76,876 |

(h) **Compensated Absences**

Accrued compensated absences for University personnel are charged as an operating expense, using the vesting method, based on earned but unused vacation and sick leave days including the University's share of Social Security and Medicare taxes. At June 30, 2017, the University estimates that \$95,614,000 of the accrued compensated absences liability will be paid from revenue to be recognized in subsequent years, rather than from unrestricted net position available at June 30, 2017. The amount associated with future State appropriations was calculated based upon the unused vacation and sick leave days and pay rates for the applicable employees.

(i) **Premiums**

Premiums for bonds and certificates of participation are reported within bonds payable and leaseholds payable, respectively, and are amortized over the life of the debt issue using the straight-line method.

(j) *Net Position*

The Entity's resources are classified into net position categories and reported in the Statement of Net Position. These categories are defined as (a) Net investment in capital assets – capital assets net of accumulated depreciation and related outstanding debt balances attributable to the acquisition, construction, or improvement of those assets; (b) Restricted nonexpendable – net position restricted by externally imposed stipulations; (c) Restricted expendable – net position subject to externally imposed restrictions that can be fulfilled by actions of the Entity pursuant to those stipulations or that expire by the passage of time, and (d) Unrestricted – net position not subject to externally imposed stipulations but may be designated for specific purposes by action of management or the Board. The Entity first applies resources in restricted net position when an expense or outlay is incurred for purposes for which resources in both restricted and unrestricted net positions are available.

(k) *Classification of Revenues*

The Statement of Revenues, Expenses and Changes in Net Position classifies the Entity's fiscal year activity as operating and nonoperating. Operating revenues generally result from exchange transactions such as payments received for providing goods and services, including tuition and fees, net of scholarships and fellowships, certain grants and contracts, sales and services of educational activities, hospital, medical service plans, and auxiliary enterprises revenues. Certain revenue sources that the Entity relies on to provide funding for operations including State appropriations, gifts, on-behalf payments for fringe benefits and investment income are defined by GASB Statement No. 35 as nonoperating revenues. In addition, transactions related to capital and financing activities are components of nonoperating revenues.

In fiscal year 2017, \$20,177,000 of State appropriations were transferred to the University of Illinois Hospital Services Fund, which is a special fund established in the State Treasury pursuant to the State Finance Act, 30 ILCS 105/6z-30. This fund is owned and operated by the Illinois Department of Healthcare and Family Services and this fund is not part of or a related organization of the University.

(l) *Tuition, Scholarships and Fellowships*

Scholarships and fellowships of \$346,147,000 and \$7,826,000 are netted against student tuition and fees and auxiliary enterprises revenues, respectively. Stipends and other payments made directly to students are reported as scholarship and fellowship expense. Net tuition and fees, except for summer session, are recognized as revenues as they are assessed. The portion of summer session tuition and fees applicable to the following fiscal year are unearned and recognized in the next fiscal year.

(m) *Patient Services Revenue – Hospital*

With respect to the Hospital, patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors and others for services rendered, including estimated adjustments under reimbursement agreements with third-party payors and others for services rendered, including estimated adjustments under reimbursement agreements with third-party payors, certain of which are subject to audit by administering agencies. These adjustments are accrued on an estimated basis and are adjusted in future periods. The Hospital has agreements with third-party payors that provide for payments to the Hospital at amounts different from its established rates. Payment arrangements include prospectively determined rates, discounted charges and per diem payments. Approximately 94% of the Hospital's net patient service revenues were derived from Medicare, Medicaid and managed care programs for the year ended June 30, 2017. Reimbursement under these programs provided for payments to the Hospital at amounts different from its established rates, based on a specific amount per case, or a contracted price, for rendering services to program beneficiaries. The Hospital records contractual allowances in the current period representing the difference between charges for services rendered and the expected payments under these programs, and adjusts them in future periods as final settlements through cost reports or other means are determined. For the year ended June 30, 2017, the contractual allowances totaled \$1,678,651,000.

The policy of the Hospital is to treat patients in immediate need of medical services without regard to their ability to pay for such services. The Hospital provides care without charge or at amounts less than its established rates to patients who meet the criteria of its charity care policy. This policy defines charity care and provides guidelines for assessing a patient's ability to pay. Eligibility is based on a patient qualification, financial resources and service criteria. Because the Hospital does not pursue collection of amounts determined to be charity care, they are not reported as revenue.

The Hospital maintains records to identify and monitor the level of charity care provided. These records include the amount of estimated costs for services rendered and supplies furnished under its charity care policy. The estimated cost of charity care using the Hospital's cost-to-charge ratio was \$13,454,000 for fiscal year 2017, an increase of 37% from the prior year, primarily as a result of patients who lost Medicaid coverage or opted out of exchange plans, patients who qualified under the presumptive requirement of the financial assistance policy and changes in the financial assistance policy. The ratio of costs to charges is calculated based on the Hospital's total operating expenses. Unreimbursed costs of providing care to Medicare and Medicaid patients are not included as charity care.

(n) *Classification of Expenses*

The majority of the Entity's expenses are exchange transactions, which GASB defines as operating expenses for financial statement presentation. Nonoperating expenses include transfers of state appropriations and capital financing costs.

(o) *Employment Contracts*

Employment contracts for certain academic personnel provide for twelve monthly salary payments, although the contracted services are rendered during a nine-month period. The liability for those employees who have completed their contracted services, but have not yet received final payment, was \$64,670,000 at June 30, 2017 and is recorded in the accompanying financial statements as accrued payroll. This amount will be paid from revenues to be recognized in fiscal year 2018 rather than from the unrestricted net position available at June 30, 2017.

(p) *On-Behalf Payments for Fringe Benefits*

In accordance with GASB Statement No. 24, *Accounting and Financial Reporting for Certain Grants and Other Financial Assistance*, the University reported payments made to the State Universities Retirement System on behalf of the Entity for contributions to retirement programs for Entity employees of \$1,086,779,000 for the year ended June 30, 2017. Substantially all employees participate in group health insurance plans administered by the State. The employer contributions to these plans for University employees paid by State appropriations and auxiliary enterprises are paid by the Department of Central Management Services (CMS) on behalf of the Entity and include postemployment benefits. The employer contributions to these plans on behalf of employees paid from other Entity held funds are paid by the Entity. The on-behalf payments were \$524,665,000 for year ended June 30, 2017. The on-behalf payments amount that relates to State group health insurance is an allocation of estimated costs incurred by CMS on behalf of the University.

On-behalf payments for fringe benefits are reflected as nonoperating revenues. The corresponding on-behalf expense is reflected as an operating expense and is allocated by function.

(q) *Pensions*

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the plan net position of the State Universities Retirement System (SURS) and additions to/deductions from SURS' plan net position has been determined on the same basis as they are reported by SURS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

For the purposes of financial reporting, the State of Illinois and participating employers are considered to be under a special funding situation. A special funding situation is defined as a circumstance in which a non-employer entity is legally responsible for making contributions directly to a pension plan that is used to provide pensions to the employees of another entity or entities and either (1) the amount of the contributions for which the non-employer entity is legally responsible is not dependent upon one or more events unrelated to pensions or (2) the non-employer is the only entity with a legal obligation to make contributions directly to a pension plan. The State of Illinois is considered a non-employer contributing entity. Participating employers are considered employer contributing entities.

(r) *Use of Estimates*

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

(s) *New Accounting Pronouncements*

In fiscal year 2017, the University adopted certain provisions of GASB Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*, which was effective for periods beginning after June 15, 2016. The requirements of this Statement extend the approach to accounting and financial reporting established in Statement 68 to all pensions, with modifications as necessary to reflect that for accounting and financial reporting purposes, any assets accumulated for pensions that are provided through pension plans that are not administered through trusts that meet the criteria specified in Statement 68 should not be considered pension plan assets. It also requires that information similar to that required by Statement 68 be included in notes to the financial statements and required supplementary information by all similarly situated employers and

non-employer contributing entities. Implementation of this pronouncement did not impact the University's financial statements.

The University adopted the provisions of GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which was effective for periods beginning after June 15, 2016. For defined benefit other postemployment benefits (OPEB) plans that are administered through trusts that meet the specified criteria, this Statement requires two financial statements – a statement of fiduciary net position and a statement of changes in fiduciary net position. In addition to the requirements of this Statement, those plans also are required to follow all accounting and financial reporting requirements of other standards, as applicable. Implementation of this pronouncement did not impact the University's financial statements.

The University adopted the provisions of GASB Statement No. 77, *Tax Abatement Disclosures*, which was effective for periods beginning after December 15, 2015. This Statement defines a tax abatement as resulting from an agreement between a government and an individual or entity in which the government promises to forgo tax revenues and the individual or entity promises to subsequently take a specific action that contributes to economic development or otherwise benefits the government or its citizens. This Statement requires disclosure of tax abatement information about (1) a reporting government's own tax abatement agreements and (2) those that are entered into by other governments and that reduce the reporting government's tax revenues. Implementation of this pronouncement did not impact the University's financial statements.

The University adopted the provisions of GASB Statement No. 78, *Pensions Provided through Certain Multiple-Employer Defined Benefit Pension Plans*, which was effective for periods beginning after December 15, 2015. The objective of this Statement is to address a practice issue regarding the scope and applicability of Statement No. 68, *Accounting and Financial Reporting for Pensions*. This issue is associated with pensions provided through certain multiple-employer defined benefit pension plans and to state or local governmental employers whose employees are provided with such pensions. This Statement amends the scope and applicability of Statement 68 to exclude pensions provided to employees of state or local governmental employers through a cost-sharing multiple-employer defined benefit pension plan that (1) is not a state or local governmental pension plan, (2) is used to provide defined benefit pensions both to employees of state or local governmental employers and to employees of employers that are not state or local governmental employers, and (3) has no predominant state or local governmental employer (either individually or collectively with other state or local governmental employers that provide pensions through the pension plan). This Statement establishes requirements for recognition and measurement of pension expense, expenditures, and liabilities; note disclosures; and required supplementary information for pensions that have the characteristics described above. Implementation of this pronouncement did not impact the University's financial Statements.

The University adopted the provisions of GASB Statement No. 80, *Blending Requirements for Certain Component Units – an amendment of GASB Statement No. 14*, which was effective for periods beginning after June 15, 2016. This Statement amends the blending requirements for the financial statement presentation of component units of all state and local governments. The additional criterion requires blending of a component unit incorporated as a not-for-profit corporation in which the primary government is the sole corporate member. The additional criterion does not apply to component units included in the financial reporting entity pursuant to the provisions of Statement No. 39, *Determining Whether Certain Organizations Are Component Units*. Implementation of this pronouncement did not impact the University's financial statements.

The University adopted the provisions of GASB Statement No. 82, *Pension Issues – an amendment of GASB Statements No. 67, No. 68, and No. 73*, which was effective for periods beginning after June 15, 2016. This Statement addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations

from the guidance in an Actuarial Standard Practice for financial reporting purposes, and (3) the classification of payments made by employers to satisfy employee (plan member) contribution requirements. The requirements of this Statement will improve financial reporting by enhancing consistency in the application of financial reporting requirements to certain pension issues. Implementation of this pronouncement did not impact the University's financial statements.

(t) *Reclassifications*

Certain prior year amounts were reclassified from unrestricted net position to restricted net position to conform to current year presentations due to the identification of an error in segment reporting which resulted in the University reclassifying all AFS net position and HSFS renewal and replacement reserve net position and the related assets to restricted from unrestricted.

(2) Cash, Cash Equivalents and Investments

The carrying amount of the University's cash totaled \$5,068,000 at June 30, 2017. The June 30, 2017 total bank account balances for the University aggregated \$31,664,000 all of which was covered by federal depository insurance or by collateral held by an agent in the University's name.

The Board follows the State of Illinois Uniform Prudent Management of Institutional Funds Act, 760 ILCS 51/1-11, when managing the University's investments. The Board fulfills its fiduciary responsibility for the management of investments, including endowment farm real estate, by adopting policies to maximize investment return with a prudent level of risk.

Nearly all of the University's investments are managed by external professional investment managers, who have full discretion to manage their portfolios subject to investment policy and manager guidelines established by the University, and in the case of mutual funds and other commingled vehicles, in accordance with the applicable prospectus or limited partnership agreement.

The following details the carrying value of the University's cash, cash equivalents and investments as of June 30, 2017:

| University Cash, Cash Equivalents and Investments | |
|---|--------------|
| (In thousands) | |
| U.S. Treasury bonds and bills | \$ 272,697 |
| U.S. government agencies | 107,971 |
| International government bonds and governmental agencies | 10,998 |
| Nongovernment mortgage-backed securities | 71,202 |
| Asset backed securities | 247,473 |
| Corporate bonds | 679,909 |
| Commercial paper | 31,960 |
| Municipal bonds | 14,529 |
| Bond funds | 137,834 |
| Money market funds | 456,264 |
| Illinois public treasurer's investment pool | 2,885 |
| Subtotal before cash deposits, equities and other investments | 2,033,722 |
| Equities | 57,464 |
| Equity funds | 321,742 |
| Hedge funds | 46,680 |
| Private equity | 38,865 |
| Farm properties | 102,409 |
| Real estate | 36,491 |
| Cash deposits | 5,068 |
| Total | \$ 2,642,441 |

(a) **Interest Rate Risk**

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. In accordance with its investment policy, the University employs multiple investment managers, of which each has specific maturity assignments related to the operating funds. The funds are structured with different layers of liquidity. Funds expected to be used within one year are invested using the Barclay's Capital 90-Day and Bank of America Merrill Lynch 12 month Treasury Bill Index as performance benchmarks. Core operating funds are invested in longer maturity investments. Core operating funds investment manager's performance benchmarks are the Barclays Capital one-year to three-year Government Bond Index, the Barclays Capital one-year to three-year Government Credit Bond Index, the Barclays Capital Intermediate Government Credit Bond Index and the Barclays Capital Intermediate Aggregate Bond Index.

The University's investment maturities at June 30, 2017 are illustrated below:

| University Investment Maturities | | | | | |
|---|--------------|-----------------------------|--------------------|---------------------|----------------------------------|
| (In thousands) | | | | | |
| | Total | Less than 1 year | 1 - 5 years | 5 - 10 years | Greater than 10 years |
| U.S. Treasury bonds and bills | \$ 272,697 | 62,245 | 196,264 | 14,188 | |
| U.S. government agencies | 107,971 | 9,499 | 17,819 | 6,034 | 74,619 |
| International government bonds and governmental agencies | 10,998 | 7,070 | 2,895 | 1,033 | |
| Nongovernment mortgage- backed securities | 71,202 | | | 326 | 70,876 |
| Asset backed securities | 247,473 | 926 | 227,047 | 16,405 | 3,095 |
| Corporate bonds | 679,909 | 264,267 | 363,387 | 48,071 | 4,184 |
| Commercial paper | 31,960 | 31,960 | | | |
| Municipal bonds | 14,529 | 4,899 | 9,056 | | 574 |
| Bond funds | 137,834 | 1,182 | 829 | 133,866 | 1,957 |
| Money market funds | 456,264 | 456,264 | | | |
| Illinois public treasurer's investment pool | 2,885 | 2,885 | | | |
| Total | \$ 2,033,722 | 841,197 | 817,297 | 219,923 | 155,305 |

At June 30, 2017, the University's operating funds pool portfolio had an effective duration of 1.3 years.

(b) **Credit Risk**

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The University's investment policy requires that the University's short-term operating funds be invested in fixed income securities and other short-term fixed income instruments (e.g., money markets). Fixed income securities shall be rated investment grade or better by one or more nationally recognized statistical rating organizations. Securities not covered by the investment grade standard are allowed if, in the manager's judgment, those instruments are of comparable credit quality. Securities that fall below the stated minimum credit requirements subsequent to initial purchase may be held at the manager's discretion.

The University reports the credit ratings of fixed income securities and short term instruments using Standard and Poor's and Moody's ratings. Securities with split ratings or with a different rating assignment are disclosed using the rating indicative of the greatest degree of risk.

The University's investment quality ratings at June 30, 2017 are illustrated below:

| University Investments Quality Ratings | | | | | | | |
|---|---------------------|----------------|------------------------------|----------------|----------------|--------------|--|
| (In thousands) | | | | | | | |
| | Total | AAA/Aaa | AA/Aa/ TSY/AGY[1] | A/A [2] | BBB/Baa | BB/Ba | Less than BB or not rated |
| U.S. Treasury bonds and bills \$ | 272,697 | | 272,697 | | | | |
| U.S. government agencies | 107,971 | | 107,971 | | | | |
| International government bonds and governmental agencies | 10,998 | 2,895 | 2,096 | | | | 6,007 |
| Nongovernment mortgage- backed securities | 71,202 | 71,202 | | | | | |
| Asset backed securities | 247,473 | 247,465 | | 8 | | | |
| Corporate bonds | 679,909 | 10,510 | 77,888 | 326,340 | 258,485 | 5,329 | 1,357 |
| Commercial paper | 31,960 | | 23,200 | 8,760 | | | |
| Municipal bonds | 14,529 | 2,129 | 9,128 | 228 | 3,044 | | |
| Bond funds | 137,834 | 76,601 | 7,622 | 18,263 | 24,311 | 1,000 | 10,037 |
| Money market funds | 456,264 | 456,264 | | | | | |
| Illinois public treasurer's investment pool | 2,885 | 2,885 | | | | | |
| Total | \$ 2,033,722 | 869,951 | 500,602 | 353,599 | 285,840 | 6,329 | 17,401 |

[1] TSY (U.S. Treasury Securities) & AGY (U.S. Agency Securities) is a reporting convention used by the University's custodian to identify investments that have not received individual security ratings. These securities have an explicit or implicit guarantee by the U.S. government which has been rated AA+ by Standard and Poor's and Aaa by Moody's. Short term Standard and Poor's ratings of A-1+ and Moody's ratings of P1 are placed in this category.

[2] Short term Standard and Poor's ratings of A-1 and A-2 and Moody's short-term ratings of P1 and P2 are placed in this category.

(c) Custodial Credit Risk

Custodial credit risk is the risk that in the event of the failure of the counterparty, the University will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. Exposure to custodial credit risk relates to investment securities that are held by someone other than the University and are not registered in the University's name. The University investment policy does not limit the value of investments that may be held by an outside party. At June 30, 2017, the University's investments were not subject to custodial credit risk.

(d) Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of the University's investment in a single issuer. The University's investment policy provides that the total operating funds portfolio will be broadly diversified across securities in a manner that is consistent with fiduciary standards of diversification. Issuer concentrations are limited to 5% per issuer of the total market value of the portfolio at the time of purchase, or in the case of securitized investments (e.g., mortgage-backed securities), concentration is limited to an individual issuance trust (e.g., pooled receivables). These concentration limits do not apply to investments in money market funds, tri-party repurchase agreements or obligations of, or issues guaranteed by, the U.S. Treasury, U.S. agencies or U.S. government sponsored enterprises.

As of June 30, 2017, not more than 5% of the University's total investments were invested in securities of any one issuer, excluding money market funds, tri-party repurchase agreements or obligations of, or issues guaranteed by, the U.S. Treasury, U.S. agencies or U.S. government sponsored enterprises.

(e) ***Foreign Currency Risk***

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or deposit. The University's operating fund investments generally are not exposed to foreign currency risk. The University does not have an overarching policy related to foreign currency risk; however, under each investment manager's respective fund agreement, the portfolio's foreign currency exposure may be unhedged or hedged back into U.S. dollars.

The University invests in non-U.S. developed and emerging markets through commingled funds invested in non-U.S. equities, private equity and absolute return strategies. As these funds are reported in U.S. dollars, both price changes of the underlying securities in local markets and changes to the value of local currencies relative to the U.S. dollar are embedded in investment returns.

(f) ***Investments and Fair Value Measurements***

GASB standards established a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The fair value hierarchy is as follows:

Level 1 - Quoted prices (unadjusted) for identical assets or liabilities in active markets that the University has the ability to access as of the measurement date. Level 1 inputs would also include investments valued at prices in active markets that the University has access to where transactions occur with sufficient frequency and volume to provide reliable pricing information.

Level 2 - Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data.

Level 3 - Significant unobservable inputs that reflect a reporting entity's own assumptions about what market participants would use in pricing an asset or liability.

A description of the valuation methodologies used for assets and liabilities measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

Investments may be classified as Level 1 when the values are based upon unadjusted quoted prices in active markets for identical assets and generally include active listed equities. Publicly-traded investments that have no or insignificant restrictions are classified in Level 1 of the fair value hierarchy. Level 1 securities would include exchange traded equities.

Investments may be classified as Level 2 when the values include inputs that are directly observable for an asset (including quoted prices for similar assets), as well as inputs that are not directly observable for the asset. These inputs are derived principally from or corroborated by observable market data through correlation or by other means (market corroborated inputs). The concept of market-corroborated inputs is intended to incorporate observable market data (such as interest rates and yield curves that are observable at commonly quoted intervals) based upon an assessment of factors relevant to the asset or liability. Level 2 securities include US Treasury bonds and bills, US government agencies, international government bonds and agencies, nongovernment mortgage-backed securities, asset backed securities, corporate bonds, commercial paper, and municipal bonds.

Investments may be classified as Level 3 when the values include inputs that are unobservable and Level 1 and Level 2 inputs are not available. The values are based upon the best information available under the circumstances and may include management's own data. Level 3 securities include certain types of inactively traded corporate bonds and equities and farm properties.

There have been no changes in valuation techniques used for any assets measured at fair value during the year ended June 30, 2017.

The following table summarizes assets measured at fair value as of June 30, 2017, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

| University Fair Value Measurements as of June 30, 2017 | | | | |
|---|---------------------|---|---|---|
| (In thousands) | | | | |
| | Total | Quoted prices in active markets (Level 1) | Significant other observable inputs (Level 2) | Quoted prices unobservable inputs (Level 3) |
| U.S. Treasury bonds and bills | \$ 272,697 | | 272,697 | |
| U.S. government agencies | 107,971 | | 107,971 | |
| International government bonds and governmental agencies | 10,998 | | 6,024 | 4,974 |
| Nongovernment mortgage- backed securities | 71,202 | | 71,202 | |
| Asset backed securities | 247,473 | | 247,473 | |
| Corporate bonds | 679,909 | | 679,909 | |
| Commercial paper | 31,960 | | 31,960 | |
| Municipal bonds | 14,529 | | 14,529 | |
| Bond funds | 3,968 | 3,968 | | |
| Equities | 57,464 | 57,379 | | 85 |
| Equity funds | 5,862 | 5,862 | | |
| Farm properties | 102,409 | | | 102,409 |
| Total subject to fair value hierarchy | \$ 1,606,442 | 67,209 | 1,431,765 | 107,468 |
| Investments measured at the NAV | | | | |
| Bond funds | 133,866 | | | |
| Equity funds | 315,880 | | | |
| Hedge funds | 46,680 | | | |
| Private equity | 38,865 | | | |
| Real estate | 36,491 | | | |
| Total investments measured at NAV | \$ 571,782 | | | |
| Investments measured at cost | | | | |
| Money market funds | 456,264 | | | |
| Cash deposits | 5,068 | | | |
| Illinois public treasurer's investment pool | 2,885 | | | |
| Total investments measured at cost | \$ 464,217 | | | |
| Total cash, cash equivalents and investments | \$ 2,642,441 | | | |

The following table sets forth additional disclosure of the University's investments whose fair value is estimated using NAV per share (or its equivalent) as of June 30, 2017:

| | Fair value | Unfunded commitment | Redemption frequency | Redemption notice period |
|--------------------|-------------------|------------------------|-------------------------|-----------------------------|
| (In thousands) | | | | |
| Investments: | | | | |
| Bond funds (A) | \$ 133,866 | \$ | (A) | (A) |
| Equity funds (B) | 315,880 | | (B) | (B) |
| Hedge funds (C) | 46,680 | | (C) | (C) |
| Private equity (D) | 38,865 | 25,206 | (D) | (D) |
| Real estate (E) | 36,491 | | (E) | (E) |
| | <u>\$ 571,782</u> | <u>\$ 25,206</u> | | |

- (A) The funds in this category invest in bonds and other debt instruments. Investments may include government, corporate, municipal and convertible bonds, along with other debt securities such as mortgage-backed and asset-backed securities. These funds can be redeemed with same business day to two business days' redemption notification requirement determined by the managers. Settlement may take up to seven business days.
- (B) The funds in this category invest in marketable equities that are exchange traded in the United States of America (USA) and in countries outside of the USA. These funds can be redeemed with same business day to two business days' redemption notification requirement determined by the managers. Settlement may take up to seven business days.
- (C) The funds in this category are generally not restricted in the types of securities in which they can invest. They may invest in limited partnership vehicles or directly in equity, fixed income and derivative instruments to achieve a stated investment objective. These funds can be redeemed bi-monthly or quarterly depending on the partnership agreement within redemption notice periods of less than one month to 60 days. The fund values of these investments have been estimated using the NAV per share provided by the fund manager.
- (D) The funds in this category invest in the following types of investments in the USA and outside of the USA: venture capital partnerships, buyout partnerships, mezzanine/subordinated debt partnerships, restructuring/distressed debt partnerships, special situation partnerships, and directly in portfolio companies. These investments cannot be redeemed during the life of the partnership; however they can be transferred to another eligible investor. Distributions will be received as the underlying investments of the funds are liquidated over time. The fair value of this investment has been estimated using the NAV provided by the fund manager and an adjustment determined by management for the time period between the dates of the last available NAV and June 30, 2017.
- (E) The funds in this category invest in real estate. Subject to general partner approval and available cash, these funds can be redeemed quarterly with up to a 3 month notice period. Distributions of operating cash flow are paid out on a quarterly basis as determined by the general partner. The fair value of this investment has been estimated using the NAV provided by the fund manager and an adjustment determined by management for the time period between the dates of the last available NAV and June 30, 2017.

(g) ***URO – Foundation Investments***

As the investments of the University's URO-Foundation are considered material to the University's financial statements taken as a whole, the following disclosures are made:

The Foundation financial statements follow FASB standards; therefore, the required disclosures, within the University's statements, for the Foundation investments differ from GASB requirements.

FASB standards have established a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The fair value hierarchy is as follows:

Level 1 – Quoted prices (unadjusted) for identical assets or liabilities in active markets that the Foundation has the ability to access as of the measurement date. Level 1 inputs would also include investments valued at prices in active markets that the Foundation has access to where transactions occur with sufficient frequency and volume to provide reliable pricing information.

Level 2 – Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data.

Level 3 – Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

A description of the valuation methodologies used for assets and liabilities measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

Investments: Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities would include highly liquid government bonds, exchange-traded equities and mutual funds.

If quoted market prices are not available, then the fair values are estimated by using pricing models, quoted prices of securities with similar characteristics and other valuation methodologies. Level 2 securities would include mortgage-backed agency securities, certain corporate securities and other certain securities. These securities are valued primarily through a multi-dimensional relational model including standard inputs such as benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, offers and reference data.

In certain cases where there is limited activity or less transparency around inputs to the valuation, including alternative investments, securities are classified within Level 3 of the valuation hierarchy and may include equity and/or debt securities issued by private entities. Level 3 investments would include direct private investments and co-investments using performance multiples applicable to the investment's industry, determined through the use of a market-based approach, which utilizes comparable companies' data and equity mutual funds that have underlying marketable securities but have significant redemption restrictions.

Beneficial interest in trusts and trusts held by others: The values of the beneficial interest in trusts are derived from the underlying investments of the trusts. The value of those investments is determined in the same manner as investments described above. The value of trusts held by others is based on the Foundation owning an interest in trust and not the underlying investments. The estimated future value of that interest in the trust is based on management's estimate of the trusts' expected performance

which is then present valued back to the date of the financial statements based on life expectancy factors published by the Internal Revenue Service.

The following table summarizes assets measured at fair value on a recurring basis as of June 30, 2017, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

URO – Foundation Fair Value Measurements as of June 30, 2017

| | <u>Fair value</u> | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u> |
|--|-------------------|----------------|----------------|----------------|
| U.S. Treasury bonds and bills | \$ 47,537 | | 47,537 | |
| International government bonds | 36,030 | | 32,378 | 3,652 |
| U.S. government agencies | 10 | | 10 | |
| Municipal bonds | 2,662 | | 2,662 | |
| Corporate bonds and notes | 30,921 | | 30,921 | |
| Commercial mortgage-backed securities | 4,824 | | 4,824 | |
| Asset backed securities | 13,052 | | 13,052 | |
| Mortgage-backed securities | 2,389 | | 2,389 | |
| Common stock, international: | | | | |
| Information technology | 1,845 | 1,845 | | |
| Other investments | 892 | 892 | | |
| Common stock, domestic: | | | | |
| Consumer goods | 267 | 267 | | |
| Energy | 50 | 50 | | |
| Financial services | 1,181 | 1,181 | | |
| Healthcare | 844 | 844 | | |
| Industrials | 4,972 | 4,972 | | |
| Information technology | 14,852 | 14,852 | | |
| Materials | 7,846 | 7,846 | | |
| Real estate | 31 | 31 | | |
| Telecommunications | 3 | 3 | | |
| Utilities | 3 | 3 | | |
| Bond mutual funds: | | | | |
| U.S. government | 5,694 | 449 | 5,245 | |
| Mortgages | 8,476 | 684 | 7,792 | |
| Corporate bonds and notes | 4,057 | 321 | 3,736 | |
| High Yield | 617 | 50 | 567 | |
| Municipals | 763 | 18 | 745 | |
| Internationals | 58,621 | 70 | 58,551 | |
| Equity mutual funds: | | | | |
| Small cap | 43,379 | 364 | 120 | 42,895 |
| Mid cap | 714 | 714 | | |
| Large cap | 40,510 | 39,029 | 1,481 | |
| International | 238,886 | 78,754 | 160,132 | |
| Money market mutual funds | 52,041 | 52,041 | | |
| Other | 3,438 | | | 3,438 |
| Farms | 62,112 | | 62,112 | |
| Beneficial interest in trusts | 46,821 | | | 46,821 |
| Trusts held by others | 20,068 | | | 20,068 |
| Cash surrender value of life insurance | 6,100 | | | 6,100 |
| Partnership interests | 5,050 | | 5,050 | |
| | <u>5,050</u> | | <u>5,050</u> | |
| Total subject to fair value hierarchy | <u>\$ 767,558</u> | <u>205,280</u> | <u>439,304</u> | <u>122,974</u> |

There have been no changes in valuation techniques used for any assets measured at fair value during the year ended June 30, 2017.

The investments above exclude \$8,972,000 of real estate and \$6,640,000 of private equities which are carried at cost and \$1,182,695,000 of investments where values are based on NAV using the practical expedient.

There were no transfers between Level 1 or 2 of the fair value hierarchy during the year ended June 30, 2017.

The following table presents additional information about investments measured at fair value on a recurring basis for which the URO – Foundation has utilized Level 3 inputs to determine fair value:

URO -Foundation Significant Unobservable Inputs (Level 3) as of June 30, 2017

(In thousands)

| | <u>Beginning balance</u> | <u>Purchases</u> | <u>Sales (distributions)</u> | <u>Total gains or losses*</u> | <u>Ending balance</u> |
|--|------------------------------|------------------|----------------------------------|---------------------------------------|---------------------------|
| Other investments | \$ 3,287 | 2,459 | (2,508) | 200 | \$ 3,438 |
| Beneficial interest in trusts | 42,147 | | | 4,674 | 46,821 |
| Equity mutual funds | 10,728 | 26,143 | (219) | 6,243 | 42,895 |
| International government bonds | 4,518 | 756 | (89) | (1,533) | 3,652 |
| Trusts held by others | 19,804 | | | 264 | 20,068 |
| Cash surrender value of life insurance | 6,879 | | | (779) | 6,100 |
| Total | <u>\$ 87,363</u> | <u>29,358</u> | <u>(2,816)</u> | <u>9,069</u> | <u>\$ 122,974</u> |

*Total gains or losses included in change in net assets attributable to the change in unrealized gains or losses relating to financial instruments still held at fiscal year-end. Includes net transfers in/out of level.

Gains and losses on Level 3 investments included in change in net position for the period above are reported as net increase (decrease) in fair value of investments.

The following table sets forth additional disclosure of the URO-Foundation's investments whose fair value is estimated using NAV per share (or its equivalent) as of June 30, 2017:

URO – Foundation Investments, Fair Value Estimated Using NAV (or its equivalent)

(In thousands)

| | <u>Fair value</u> | <u>Unfunded commitment</u> | <u>Redemption frequency</u> | <u>Redemption notice period</u> |
|---|---------------------|--------------------------------|---------------------------------|---------------------------------|
| Hedged/alternative investments (A) | \$ 953,300 | \$ | (A) | (A) |
| Private equity (B) | 171,666 | 205,690 | (B) | (B) |
| Real estate trusts and partnerships (B) | <u>57,729</u> | <u>26,276</u> | (B) | (B) |
| | <u>\$ 1,182,695</u> | <u>\$ 231,966</u> | | |

- (A) The partnerships in this category consist of funds that invest in multiple limited partnerships with various investment strategies and long and short positions in equity securities of companies within the USA and outside of the USA. These funds can be redeemed daily, monthly, quarterly or annually depending on the partnership agreement within redemption notice periods of 1 to 36 months.
- (B) The partnerships in this category consist of funds that invest in the following types of investments in the USA and outside of the USA: venture capital partnerships, buyout partnerships, mezzanine/subordinated debt partnerships, restructuring/distressed debt partnerships and special situation partnerships, and real estate. These investments cannot be redeemed during the life of the partnership, which can be up to 12 years; however, they can be transferred to another eligible investor. Distributions will be received as the underlying investments of the funds are liquidated over time. The fair value of this investment has been estimated using the NAV provided by the fund manager and an adjustment determined by management for the time period between the date of the last available NAV from the investment manager and June 30, 2017.

All URO – Foundation investments are considered noncurrent assets.

(3) Accounts, Notes and Pledges Receivable

The University provides allowances for uncollectible accounts and notes receivable based upon management’s best estimate considering type, age, collection history of receivables and any other factors as considered appropriate. Accounts and notes receivable are reported net of allowances at June 30, 2017.

The composition of accounts receivable and notes and pledges receivable at June 30, 2017 is summarized as follows:

| University Accounts Receivable, Net of Allowance | | | |
|---|------------------------------|--|----------------------------|
| (In thousands) | | | |
| | Gross receivables | Allowance for uncollectible | Net receivables |
| Receivables from sponsoring agencies | \$ 206,738 | (2,871) | 203,867 |
| Hospital and other medical activities | 432,278 | (268,182) | 164,096 |
| Student tuition and fees | 45,358 | (14,841) | 30,517 |
| Auxiliaries | 16,640 | (6,307) | 10,333 |
| Medical service plan | 94,252 | (24,824) | 69,428 |
| Educational activities | 51,370 | (13,657) | 37,713 |
| Other | 23,588 | (309) | 23,279 |
| Total | <u>\$ 870,224</u> | <u>(330,991)</u> | <u>539,233</u> |

Notes and Pledges Receivable

(In thousands)

Student notes receivable – University:

| | |
|---|------------------|
| Student notes outstanding - Perkins loan program* | \$ 34,923 |
| Student notes outstanding - other programs | 27,395 |
| Allowance for uncollectible loans | <u>(3,396)</u> |
| Total student notes receivable, net | <u>\$ 58,922</u> |

* Perkins loan program is planned to expire September 30, 2017. The University is waiting on guidance from the Department of Education regarding the potential close out of this program.

| | |
|--|-------------------|
| Gift pledges receivable, URO – Foundation: | \$ 155,725 |
| Less: | |
| Allowance for doubtful pledges | (10,463) |
| Present value discount | <u>(2,262)</u> |
| Total gift pledges outstanding, net | <u>\$ 143,000</u> |

(4) Capital Assets

Net interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets. Net interest of \$8,669,000 was capitalized during the year ended June 30, 2017.

Capital assets activity during the year ended June 30, 2017 is summarized as follows:

| University Capital Assets | | | | | |
|--------------------------------------|------------------------------|------------------|--------------------|------------------|---------------------------|
| (In thousands) | | | | | |
| | Beginning balance | Additions | Retirements | Transfers | Ending balance |
| Nondepreciable capital assets: | | | | | |
| Land | \$ 135,822 | 790 | (140) | | \$ 136,472 |
| Construction in progress | 400,531 | 221,098 | | (341,486) | 280,143 |
| Inexhaustible collections | 23,275 | 191 | (6) | | 23,460 |
| Total nondepreciable capital assets | <u>559,628</u> | <u>222,079</u> | <u>(146)</u> | <u>(341,486)</u> | <u>440,075</u> |
| Depreciable capital assets: | | | | | |
| Buildings | 4,150,360 | | (696) | 321,978 | 4,471,642 |
| Improvements and infrastructure | 725,329 | | | 5,442 | 730,771 |
| Equipment | 1,247,841 | 55,349 | (46,690) | 4,298 | 1,260,798 |
| Software | 178,890 | | (104) | 9,768 | 188,554 |
| Exhaustible collections | 636,339 | 27,627 | (9,135) | | 654,831 |
| Total depreciable capital assets | <u>6,938,759</u> | <u>82,976</u> | <u>(56,625)</u> | <u>341,486</u> | <u>7,306,596</u> |
| Less accumulated depreciation: | | | | | |
| Buildings | 1,701,244 | 108,900 | (391) | 160 | 1,809,913 |
| Improvements and infrastructure | 442,977 | 24,001 | | | 466,978 |
| Equipment | 947,118 | 102,348 | (44,394) | (160) | 1,004,912 |
| Software | 172,364 | 3,596 | (104) | | 175,856 |
| Exhaustible collections | 523,125 | 23,689 | (9,102) | | 537,712 |
| Total accumulated depreciation | <u>3,786,828</u> | <u>262,534</u> | <u>(53,991)</u> | <u>—</u> | <u>3,995,371</u> |
| Total net depreciable capital assets | <u>3,151,931</u> | <u>(179,558)</u> | <u>(2,634)</u> | <u>341,486</u> | <u>3,311,225</u> |
| Total | <u>\$ 3,711,559</u> | <u>42,521</u> | <u>(2,780)</u> | <u>—</u> | <u>\$ 3,751,300</u> |

(5) Accrued Self-Insurance and Loss Contingency

The University's accrued self-insurance liability of \$239,485,000, as of June 30, 2017 covers hospital patient liability; hospital and medical professional liability; estimated general and contract liability, and workers' compensation liability related to employees paid from local funds. The accrued self-insurance liability was discounted at rates of 2% to 4.5% at June 30, 2017. Amounts increasing the accrued self-insurance liability are charged as expenses based upon estimates made by actuaries and the University's risk management division. An additional workers' compensation self-insurance liability of \$17,360,000 at June 30, 2017 related to employees who are paid from State appropriations is included in the University's accounts payable. These claims will be paid from State appropriations in the year in which the claims are finalized, rather than from unrestricted net position as of June 30, 2017.

The accrued self-insurance liability includes \$172,140,000 at June 30, 2017 for the currently estimated ultimate cost of uninsured medical malpractice liabilities. Ultimate cost consists of amounts estimated by the University's risk management division and independent actuaries for asserted claims, unasserted claims arising from reported incidents, expected litigation expenses and amounts determined by actuaries using relevant industry data and hospital specific data to cover projected losses for claims incurred but not reported. Because the amounts accrued are estimates, the aggregate claims actually incurred could differ significantly from the accrued self-insurance liability at June 30, 2017. Changes in these estimates will be reflected in the Statement of Revenues, Expenses and Changes in Net Position in the period when additional information is available.

Changes in Accrued Self-Insurance

(In thousands)

| | <u>2017</u> | <u>2016</u> |
|---|-------------------|-------------------|
| Balance, beginning of year | \$ 219,234 | \$ 243,959 |
| Claims incurred and changes in estimates | 60,984 | 49,926 |
| Claim payments and other deductions | <u>(40,733)</u> | <u>(74,651)</u> |
| Balance, end of year | 239,485 | 219,234 |
| Less current portion | <u>(45,097)</u> | <u>(49,086)</u> |
| Balance, end of year – noncurrent portion | <u>\$ 194,388</u> | <u>\$ 170,148</u> |

The University has contracted with several commercial carriers to provide varying levels and upper limits of excess liability coverage. These coverages have been considered in determining the required accrued self-insurance liability. There were no material settlements that exceeded insurance coverage during the last three years.

The University purchases excess liability coverage for certain areas such as commercial general liability, Board legal liability, and hospital and medical liability.

(6) Accrued Compensated Absences

Accrued compensated absences includes personnel earned but unused vacation and sick leave days, including the University's share of Social Security and Medicare taxes, valued at the current rate of pay.

Section 14a of the State Finance Act (30 ILCS 105/14a) provides that employees eligible to participate in the State Universities Retirement System or the Federal Retirement System are eligible for compensation at time of resignation, retirement, death or other termination of University employment for one-half (1/2) of the unused sick leave earned between January 1, 1984 and December 31, 1997. Any sick leave days that were earned before or after this period of time are noncompensable.

Changes in Compensated Absences Balance

(In thousands)

| | |
|---|-------------------|
| Balance, beginning of year | \$ 195,919 |
| Additions | 25,377 |
| Deductions | <u>(18,400)</u> |
| Balance, end of year | 202,896 |
| Less current portion | <u>(18,682)</u> |
| Balance, end of year – noncurrent portion | <u>\$ 184,214</u> |

(7) **Bonds Payable**

Bonds payable activity for the year ended June 30, 2017 consists of the following:

| Bonds Payable | | | | | | |
|-----------------------------------|-----------------------|--------------------------|------------------|-------------------|-----------------------|------------------------|
| (In thousands) | | | | | | |
| | <u>Maturity dates</u> | <u>Beginning balance</u> | <u>Additions</u> | <u>Deductions</u> | <u>Ending balance</u> | <u>Current portion</u> |
| Auxiliary Facilities System: | | | | | | |
| Current interest bonds | 2018 – 2046 | \$ 1,023,900 | | (30,545) | \$ 993,355 | \$ 28,025 |
| Capital appreciation bonds | 2018 – 2030 | 118,165 | | (17,895) | 100,270 | 17,975 |
| Health Services Facilities System | 2018 – 2043 | 115,610 | | (3,365) | 112,245 | 3,485 |
| UIC South Campus | 2018 – 2023 | 42,090 | | (5,960) | 36,130 | 6,225 |
| | | <u>1,299,765</u> | <u>—</u> | <u>(57,765)</u> | <u>1,242,000</u> | <u>55,710</u> |
| Unaccrued appreciation | | <u>(26,949)</u> | <u>6,234</u> | | <u>(20,715)</u> | <u>(931)</u> |
| | | <u>1,272,816</u> | <u>6,234</u> | <u>(57,765)</u> | <u>1,221,285</u> | <u>54,779</u> |
| Unamortized debt premium | | <u>68,056</u> | | <u>(4,011)</u> | <u>64,045</u> | <u>4,011</u> |
| Total | | <u>\$ 1,340,872</u> | <u>6,234</u> | <u>(61,776)</u> | <u>\$ 1,285,330</u> | <u>\$ 58,790</u> |

None of the University's bonds described above constitute obligations of the State.

Capital appreciation bonds of \$100,270,000 outstanding at June 30, 2017 do not require current interest payments and have a net unappreciated value of \$79,555,000. The University records the annual increase in the principal amount of these bonds as interest expense and accretion on bonds payable.

Included in bonds payable is \$127,535,000 of variable rate demand bonds. These bonds mature serially through April 2044. These bonds have variable interest rates that are adjusted periodically (e.g., daily, weekly, or monthly), generally with interest paid at the beginning of each month. The bonds are subject to purchase on the demand of the holder at a price equal to principal plus accrued interest on seven days notice and delivery to the University's several remarketing agents. The University pays the remarketing agent fees on the outstanding bond balance. If the remarketing agent is unable to resell any bonds that are "put" to the agent, the University has a standby bond purchase agreement with a liquidity facility entity. The University has several such agreements, with the fees on the Bond Purchase Commitment (formula based on outstanding bonds plus pro forma interest). The University, in the event a liquidity facility is utilized, has reimbursement agreements with associated financial entities. Generally, the payback period is three to five years, at an interest rate initially set at slightly above prime or the federal funds rate. The due date of the initial payment per the reimbursement agreements varies depending upon the variable rate bond issue. Certain reimbursement agreements require an initial payment due date 366 days after the event which caused the liquidity facility to be utilized.

The required future interest payments for these variable rate bonds have been calculated using the current interest rate, based upon short-term rates, or the synthetic fixed rate, as illustrated in the table below. Other outstanding bond issues bear interest at fixed rates ranging from 1.766% to 6.250%.

Variable Rate Bonds

| Bond issues | Interest rate at June 30, 2017 | Remarketing agent | Remarketing fee | Liquidity facility | | | Liquidity fee |
|-------------------------------|--------------------------------|---------------------|-----------------|--------------------|------------|------------------|---------------|
| | | | | Bank | Expiration | Insured by | |
| UIC South Campus, Series 2008 | 0.91% | JPMorgan Securities | 0.075% | JPMorgan Chase | 6/24/2019 | Letter of Credit | 0.550% |
| AFS, Series 2008 | 1.30 | Loop Capital | 0.075 | JPMorgan Chase | 5/19/2021 | None | 0.600 |
| AFS, Series 2014C | 1.18 | Wells Fargo | 0.080 | Northern Trust | 2/19/2019 | Letter of Credit | 0.350 |
| HSFS, Series 1997B | 0.91 | JPMorgan Securities | 0.070 | Wells Fargo | 5/30/2019 | Letter of Credit | 0.720 |
| HSFS, Series 2008 | 0.93 | Goldman Sachs | 0.070 | Wells Fargo | 5/30/2019 | Letter of Credit | 0.720 |

(a) Interest Rate Swap Agreements on Bonds Payable

The University has entered into three separate pay-fixed/receive-variable interest rate swap agreements. The objective of these swaps was to effectively change the University's variable interest rate on the bonds to a synthetic fixed rate. The notional amount of the interest rate swaps is equal to the par amount of the related bonds, except for HSFS Series 2008, of which \$235,000 is not covered by the swap agreement. In addition, the swaps were entered at the same time as the original bonds were issued and terminate with maturity of the existing bonds. No cash was paid or received when the original swap agreements were entered into.

Credit Risk – As of June 30, 2017, the University was not exposed to credit risk because the swaps had a negative fair value. If interest rates change and the fair value of the swap became positive, the University would be exposed to credit risk in the amount of the derivative's fair value. The terms, fair values and credit ratings of the outstanding swaps as of June 30, 2017 are listed below:

| Bond issues | Interest Rate Swaps | | | | | | | |
|-------------|-----------------------------|----------------|-----------------|------------------------|--------------------|-----------------------|----------------|--|
| | Outstanding notional amount | Effective date | Fixed rate paid | Variable rate received | Level 2 Fair value | Swap termination date | Counterparty | Counterparty credit rating (S&P/Moody's) |
| HSFS 2008 | \$ 28,825,000 | Nov 2008* | 3.534% | 68% of LIBOR** | \$ (3,072,000) | Oct-2026 | Loop | A-/Baa2 |
| UIC SC 2008 | 16,162,500 | Feb 2006* | 4.086 | 68% of LIBOR** | (1,290,000) | Jan-2022 | Morgan Stanley | BBB+/A3 |
| UIC SC 2008 | 15,827,500 | Feb 2006* | 4.092 | 68% of LIBOR** | (1,258,000) | Jan-2022 | JPMorgan Chase | A+/Aa3 |

* Swap agreement was transferred from original issue to refunded bond issues.

** LIBOR – London Interbank Offered Rate

The University engaged a third-party consultant to determine the fair value of the swap agreements. The fair values provided by the consultant were derived from proprietary models based upon well-recognized financial principles and reasonable estimates about relevant market conditions. Since these are negative numbers, they represent an approximation of the amount of money that the University may have to pay a swap provider to terminate the swap. The counterparty may have to post collateral in the University's favor in certain conditions, and the University would never be required to post collateral in the counterparty's favor.

Interest Rate Risk – Since inception of the swaps, declining interest rates exposed the University to interest rate risk, which adversely affected the fair values of the swap agreements.

Termination Risk – The University has the option to terminate any of the swaps early. The University or the counterparties may terminate a swap if the other party fails to perform under the terms of the contract. The University may terminate a swap if both credit ratings of the counterparties fall below BBB+ as issued by Standard & Poor's and Baa1 as issued by Moody's Investors Service. If a swap is terminated, the variable-rate bonds would no longer carry a synthetic fixed interest rate. In addition, if at the time of termination, a swap has a negative fair value, the University would be liable to the counterparties for a payment equal to the swap's fair value.

Basis Risk – The swaps expose the University to basis risk should the relationship between LIBOR and the variable weekly rate determined by remarketing agents change, changing the synthetic rate on the bonds. If a change occurs that results in the difference in rates widening, the expected cost savings may not be realized.

Other Risks – Since the swap agreements extend to the maturity of the related bond, the University is not exposed to rollover risk. In addition, the University is not exposed to foreign currency risk or to market access risk as of June 30, 2017. However, if the University decides to issue refunding bonds and credit is more costly at that time, it could be exposed to market access risk.

(b) Pledged Revenues and Debt Service Requirements

The University has pledged specific revenues, net of specified operating expenses, to repay the principal and pay the interest of revenue bonds. The following is a schedule of the pledged revenues and related debt:

| Pledged Revenues | | | | | Debt service to pledged revenues (current year) |
|-------------------------|---|---|---|---------------------------|--|
| Bond issues | Purpose | Source of revenue pledged | Future revenues pledged ² | Term of commitment | |
| | | | (In thousands) | | |
| AFS | Refunding, various improvements and additions to the System | Net AFS revenue, student tuition and fees | \$ 1,650,848 | 2046 | 7.81% |
| HSFS | Additions to System and refunding | Net HSFS revenue, Medical Service Plan revenue net of bad debt expense, College of Medicine net tuition revenue | 200,444 | 2043 | 2.60 |
| UIC South Campus | South Campus Development Project ¹ and refunding | Defined Tax Increment Financing District revenue, student tuition and fees, and sales of certain land in the UIC South Campus project | <u>40,477</u> | 2023 | 2.07 |
| | | Total future revenues pledged | <u>\$ 1,891,769</u> | | |

¹An integrated academic, residential, recreational and commercial development south of UIC's main campus

²Total estimated future principal and interest payments on debt

Future debt service requirements for all bonds outstanding at June 30, 2017 are as follows:

| Debt Service Requirements | | | |
|----------------------------------|---------------------|-----------|-----------------|
| (In thousands) | | | |
| | <u>Principal</u> | | <u>Interest</u> |
| 2018 | \$ 55,710 | \$ | 51,288 |
| 2019 | 56,445 | | 49,706 |
| 2020 | 59,075 | | 47,945 |
| 2021 | 66,510 | | 46,208 |
| 2022 | 69,365 | | 44,112 |
| 2023 – 2027 | 262,415 | | 181,559 |
| 2028 – 2032 | 268,310 | | 122,659 |
| 2033 – 2037 | 196,385 | | 68,917 |
| 2038 – 2042 | 142,175 | | 33,474 |
| 2043 – 2046 | 65,610 | | 3,901 |
| Total | <u>\$ 1,242,000</u> | <u>\$</u> | <u>649,769</u> |

Using the actual rates of 0.91% (UIC South Campus, Series 2008) and 0.93% (Health Services Facilities System, Series 2008), in effect as of June 30, 2017, debt service requirements of the variable-rate debt and net swap payments, assuming current interest rates remain the same for their term, were as follows. As rates vary, variable-rate bond interest payments and net swap payments will also vary.

| UIC South Campus Revenue Refunding Bonds, Series 2008 | | | | |
|--|----------------------------|-----------------|----------------------|------------------|
| Variable-Rate Debt Service Requirements | | | | |
| (In thousands) | | | | |
| | <u>Variable-rate bonds</u> | | <u>Interest rate</u> | |
| | <u>Principal</u> | <u>Interest</u> | <u>swaps, net</u> | <u>Total</u> |
| 2018 | \$ 5,610 | 291 | 930 | \$ 6,831 |
| 2019 | 5,855 | 240 | 748 | 6,843 |
| 2020 | 6,520 | 187 | 552 | 7,259 |
| 2021 | 6,845 | 127 | 340 | 7,312 |
| 2022 | 7,160 | 65 | 117 | 7,342 |
| Total | <u>\$ 31,990</u> | <u>910</u> | <u>2,687</u> | <u>\$ 35,587</u> |

**Health Services Facilities System Revenue Bonds, Series 2008
Variable-Rate Debt Service Requirements**

(In thousands)

| | Variable-rate bonds | | Interest rate swaps, net | Total |
|--------------|----------------------------|-----------------|-------------------------------------|------------------|
| | Principal | Interest | | |
| 2018 | \$ 2,485 | 270 | 693 | \$ 3,448 |
| 2019 | 2,520 | 247 | 627 | 3,394 |
| 2020 | 2,655 | 224 | 559 | 3,438 |
| 2021 | 2,700 | 199 | 489 | 3,388 |
| 2022 | 2,845 | 174 | 417 | 3,436 |
| 2023 - 2027 | 15,855 | 453 | 888 | 17,196 |
| Total | \$ 29,060 | 1,567 | 3,673 | \$ 34,300 |

Certain bonds of the University (AFS Series 1991) have debt service reserve requirements. The Maximum Annual Net Debt Service for those bonds, as defined, is \$14,927,000.

(c) Advanced Refunded Bonds Payable

The University has defeased bonds through advanced refunding in the prior years, and accordingly, they are not reflected in the accompanying financial statements. The amount of bonds that have been defeased as of June 30, 2017 consists of the following:

Advanced Refunded Bonds

(In thousands)

| Series | Outstanding at June 30, 2017 |
|---|---|
| Auxiliary Facilities System, Series 2009A | \$ 76,305 |

(8) Leaseholds Payable and Other Obligations

On September 29, 2016, the University issued \$116,845,000 of Certificates of Participation. The proceeds from this issuance refunded the outstanding balance of existing Certificates of Participation, Series 2004 and partially refunded the outstanding balance of Certificates of Participation, Series 2007A, Series 2007B, and Series 2009A. The Series 2004 Certificates had an interest rate swap agreement associated with them, which terminated as a result of the refunding. The University utilized proceeds from the issuance to pay \$7,780,000 of costs related to the termination. The issuance, projected savings, and loss on refunding of the certificates of participation were as follows:

| Certificates of Participation Issued on September 29, 2016 | | | |
|---|------------------------|------------------------------|------------------------------|
| (In thousands) | | | |
| <u>Proceeds of these Certificates were used to (1)</u> | <u>Issuance Amount</u> | <u>Projected Savings (2)</u> | <u>Loss on Refunding (3)</u> |
| Certificate of Participation: | | | |
| Series 2016A refund Series 2004 and pay termination costs | \$ 87,435 | \$ 940 | \$ 3,133 |
| Series 2016B partially refund Series 2007A | 4,495 | 742 | 254 |
| Series 2016C partially refund Series 2007B | 15,400 | 869 | 627 |
| Series 2016D partially refund Series 2009A | 9,515 | 1,374 | 2,081 |
| Total Issuances | <u>\$ 116,845</u> | <u>\$ 3,925</u> | <u>\$ 6,095</u> |

(1) Proceeds of each issuance were also used to fund all costs incidental to issuance.

(2) The net present value of the projected savings over the life of the issue that resulted from the refunding.

(3) The difference between the reacquisition price and the net carrying amount of the old debt. This loss is deferred and amortized as a component of interest expense over the remaining life of the old debt or the life of the new debt, whichever is shorter.

Leaseholds payable and other obligations activity for the year ended June 30, 2017 consists of the following:

| Leaseholds Payable and Other Obligations | | | | | |
|---|--------------------------|------------------|-------------------|-----------------------|------------------------|
| (In thousands) | | | | | |
| | <u>Beginning balance</u> | <u>Additions</u> | <u>Deductions</u> | <u>Ending balance</u> | <u>Current portion</u> |
| University: | | | | | |
| Certificates of participation | \$ 244,100 | 116,845 | (148,215) | \$ 212,730 | \$ 32,480 |
| Unamortized debt premium | 9,055 | 11,210 | (3,425) | 16,840 | 2,958 |
| | 253,155 | 128,055 | (151,640) | 229,570 | 35,438 |
| Other capital leases | 30,132 | 260 | (3,594) | 26,798 | 2,753 |
| Energy services agreement installment payment contracts | 40,599 | | (3,054) | 37,545 | 3,145 |
| Environmental remediation liability | 99 | | | 99 | 20 |
| Total University | <u>\$ 323,985</u> | <u>128,315</u> | <u>(158,288)</u> | <u>294,012</u> | <u>41,356</u> |
| URO – Foundation: | | | | | |
| Annuities payable | \$ 48,468 | 4,329 | (6,280) | 46,517 | 5,950 |
| Other liabilities | 4,937 | | (1,605) | 3,332 | |
| Total URO – Foundation | <u>\$ 53,405</u> | <u>4,329</u> | <u>(7,885)</u> | <u>\$ 49,849</u> | <u>\$ 5,950</u> |

The University leases various plant facilities and equipment under capital leases. This includes assets obtained with certificates of participation proceeds and recorded as capital leases, as well as, other capital lease agreements funded through operations.

(a) **Capital Leases (includes Certificates of Participation)**

Assets held under capital leases are included in capital assets at June 30, 2017 as follows:

| Assets Held Under Capital Lease | |
|--|------------|
| (In thousands) | |
| Land | \$ 6,471 |
| Buildings | 140,486 |
| Improvements | 181,919 |
| Equipment | 2,306 |
| Subtotal | 331,182 |
| Less accumulated depreciation | 138,396 |
| Total | \$ 192,786 |

The net present value of outstanding capital leases at June 30, 2017 is as follows:

| Outstanding Capital Leases | |
|-----------------------------------|------------|
| (In thousands) | |
| Certificates of participation: | |
| Series 2007A | \$ 20,555 |
| Series 2007B | 17,960 |
| Series 2009A | 1,000 |
| Series 2014A | 20,785 |
| Series 2014B | 8,745 |
| Series 2014C | 26,840 |
| Series 2016A | 87,435 |
| Series 2016B | 4,495 |
| Series 2016C | 15,400 |
| Series 2016D | 9,515 |
| Other capital leases | 26,798 |
| Net present value | \$ 239,528 |

As of June 30, 2017, future minimum lease payments under capital leases are as follows:

| Future Minimum Lease Payments | |
|--------------------------------------|------------|
| Under Capital Leases | |
| (In thousands) | |
| 2018 | \$ 45,200 |
| 2019 | 44,032 |
| 2020 | 43,502 |
| 2021 | 43,057 |
| 2022 | 31,276 |
| 2023 – 2027 | 63,014 |
| 2028 – 2032 | 17,139 |
| 2033 | 215 |
| Total minimum lease payments | 287,435 |
| Amount representing interest | (47,907) |
| Net present value | \$ 239,528 |

(b) **Advanced Refunded Certificates Of Participation**

The University has defeased certificates through advanced refunding, and accordingly, they are not reflected in the accompanying financial statements. The amounts of certificates that have been defeased as of June 30, 2017 consist of the following:

| Advanced Refunded Certificates of Participation | |
|--|---|
| (In thousands) | |
| Series | Outstanding at June 30, 2017 |
| Series 2007A | \$ 45,770 |
| Series 2007B | 15,520 |
| Series 2009A | 25,600 |
| Total | <u>\$ 86,890</u> |

(c) **Other Obligations**

As part of energy services agreements, the University has entered into installment payment contracts to finance energy conservation measures. As of June 30, 2017, future minimum lease payments under installment payment contracts are as follows:

| Future Minimum Lease Payments Under Installment Payment Contracts | |
|--|------------------|
| (In thousands) | |
| 2018 | \$ 4,215 |
| 2019 | 4,215 |
| 2020 | 4,215 |
| 2021 | 4,216 |
| 2022 | 4,216 |
| 2023 – 2027 | 18,761 |
| 2028 – 2029 | 4,007 |
| Total minimum lease payments | <u>43,845</u> |
| Amount representing interest | <u>(6,300)</u> |
| Net present value | <u>\$ 37,545</u> |

The University monitors environmental matters and records an estimated liability for identified environmental remediation costs. The estimated liability at June 30, 2017 is \$99,000.

At June 30, 2017, the URO – Foundation had annuities payable outstanding of \$46,517,000. The Foundation recalculates the present value of these payments through the use of Internal Revenue Service (IRS) discount rates and IRS life expectancy tables.

(d) **Operating Leases**

The University also leases various buildings and equipment under operating lease agreements. Total rental expense under these agreements was \$14,007,000 for the year ended June 30, 2017. The future minimum lease payments (excluding those leases renewed on an annual basis) are as follows:

| Future Minimum Operating Lease Payments | |
|--|------------------|
| (In thousands) | |
| 2018 | \$ 11,906 |
| 2019 | 7,975 |
| 2020 | 4,981 |
| 2021 | 3,057 |
| 2022 | 4,785 |
| 2023 – 2027 | 3,446 |
| Total | <u>\$ 36,150</u> |

(9) **Net Position**

As discussed in Note 1(j), the University's net position is classified for accounting and reporting purposes into one of four net position categories according to externally imposed restrictions. The following tables include detail of the net position balances for the University and the URO-Foundation including major categories of restrictions and internal designation of unrestricted funds.

| University Net Position | |
|--|---------------------|
| (In thousands) | |
| Net investment in capital assets | \$ 2,297,463 |
| Restricted – nonexpendable: | |
| Invested in perpetuity to produce income expendable for – scholarships, academic programs, fellowships and research | 111,302 |
| Restricted – expendable for: | |
| Scholarships, academic programs, fellowships and research | 446,196 |
| Auxiliary Facilities System | 32,352 |
| Loans | 75,653 |
| Service plans | 134,627 |
| Retirement of indebtedness | 34,821 |
| Capital projects | 157,499 |
| Unrestricted: | |
| Designated | 1,084,673 |
| Undesignated | |
| Total | <u>\$ 4,374,586</u> |

| URO – Foundation Net Position | |
|--|---------------------|
| (In thousands) | |
| Net investment in capital assets | \$ 7,900 |
| Restricted – nonexpendable: | |
| Invested in perpetuity to produce income expendable for academic programs, scholarships, fellowships and research | 1,047,420 |
| Restricted – expendable for: | |
| Academic programs, scholarships, fellowships and research | 997,326 |
| Unrestricted | 16,569 |
| Total | <u>\$ 2,069,215</u> |

(10) Funds Held in Trust by Others

The University and URO-Foundation are income beneficiaries of several irrevocable trusts which are held and administered by outside trustees. The University and URO-Foundation have no control over these funds as to either investment decisions or income distributions. In accordance with GASB standards, the principal is not recorded in the accompanying financial statements for the University. The URO-Foundation has recorded the principal as investments in the accompanying financial statements in accordance with FASB standards. The fair value of these funds at June 30, 2017 and the amount of income received from these trusts during the year then ended were as follows:

| Funds Held in Trust by Others | | | | |
|--|-------------------|--------|-----------------------------|--------|
| (In thousands) | | | | |
| | University | | URO – Foundation | |
| Fair value of funds held in trust by others | \$ | 51,280 | \$ | 66,889 |
| Income received from funds held in trust by others | | 1,287 | | 1,137 |

(11) State Universities Retirement System

(a) General Information about the Pension Plan

Plan Description: The University contributes to the State Universities Retirement System of Illinois (SURS), a cost-sharing multiple-employer defined benefit plan with a special funding situation whereby the State makes substantially all actuarially determined required contributions on behalf of the participating employers. SURS was established July 21, 1941 to provide retirement annuities and other benefits for staff members and employees of State universities, certain affiliated organizations, and certain other State educational and scientific agencies and for survivors, dependents and other beneficiaries of such employees. SURS is considered a component unit of the State’s financial reporting entity and is included in the State’s financial reports as a pension trust fund. SURS is governed by Chapter 40, Act 5. Article 15 of the *Illinois Compiled Statutes*. SURS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by accessing the website at www.surs.org.

Benefits Provided: A traditional benefit plan was established in 1941. Public Act 90-0448 enacted effective January 1, 1998, established an alternative defined benefit program known as the portable benefit package. The traditional and portable plan Tier 1 refers to members that began participation prior to January 1, 2011. Public Act 96-0889 revised the traditional and portable benefit plans for members who begin participation on or after January 1, 2011, and who do not have other eligible Illinois reciprocal system services. The revised plan is referred to as Tier 2. New employees are allowed 6 months after their date of hire to make an irrevocable election. A summary of the benefit provisions as of June 30, 2016 can be found in the SURS’ comprehensive annual financial report (CAFR) Notes to the Financial Statements.

Eligible employees must participate upon initial employment. Employees are ineligible to participate if (a) employed after having attained age 68; (b) employed less than 50% of full time, or (c) employed less than full time and attending classes with an employer. Of those University employees ineligible to participate, the majority are students at the University.

Contributions: The State is primarily responsible for funding SURS on behalf of the individual employers at an actuarially determined amount. Public Act 88-0593 provides a Statutory Funding Plan consisting of two parts: (i) a ramp-up period from 1996 to 2010 and (ii) a period of contributions equal to a level percentage of the payroll of active members of SURS to reach 90% of the total Actuarial Accrued Liability by the end of Fiscal Year 2045. Employer contributions from “trust, federal, and other funds” are provided under Section 15-155(b) of the Illinois Pension Code and require employers to pay contributions which are sufficient to cover the accruing normal costs on behalf of applicable employees. The employer normal cost for fiscal year 2016 and 2017 respectively, was 12.69% and 12.53% of employee payroll. The normal cost is equal to the value of current year’s pension benefit and does not include any allocation for the past unfunded liability or interest on the unfunded liability. Plan members are required to contribute 8.0% of their annual covered salary. The contribution requirements of plan members and employers are established and may be amended by the Illinois General Assembly.

Participating employers make contributions toward separately financed specific liabilities under Section 15-139.5(e) of the Illinois Pension Code (relating to contributions payable due to the employment of “affected annuitants” or specific return to work annuitants) and Section 15-155(g) (relating to contributions payable due to earning increases exceeding 6% during the final rate of earnings period).

Pension Liabilities, Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

Net Pension Liability: The net pension liability was measured as of June 30, 2016. At June 30, 2016, SURS reported a net pension liability of \$25,965,272,000.

Employer Proportionate Share of Net Pension Liability: The amount of the proportionate share of the net pension liability to be recognized for the University is \$0. The proportionate share of the State’s net pension liability associated with the University is \$10,996,379,000. This amount should not be recognized in the financial statement. The net pension liability and total pension liability as of June 30, 2016 was determined based on the June 30, 2015 actuarial valuation rolled forward. The basis of allocation used in the proportionate share of net pension liability is the actual reported pensionable contributions made to SURS during fiscal year 2016.

Pension Expense: At June 30, 2016 SURS reported a collective net pension expense of \$2,566,165,000.

Employer Proportionate Share of Pension Expense: The employer proportionate share of collective pension expense should be recognized similarly to on-behalf payments as both revenue and matching expenditure in the financial statements. The basis of allocation used in the proportionate share of collective pension expense is the actual reported pensionable contributions made to SURS during fiscal year 2016. As a result, the University recognized on-behalf revenue and pension expense of \$1,086,779,000 for fiscal year ended June 30, 2017.

Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions: Deferred outflows of resources are the consumption of net position by SURS that is applicable to future reporting periods.

SURS Collective Deferred Outflows and Deferred Inflows of Resources by Sources

| | Deferred Outflows of Resources | Deferred Inflows of Resources |
|---|---|--|
| Difference between expected and actual experience | \$ 14,216,000 | \$ 2,299,000 |
| Changes in assumption | 655,464,000 | |
| Net difference between projected and actual earnings on pension plan investments | 795,529,000 | |
| Total | \$ <u>1,465,209,000</u> | \$ <u>2,299,000</u> |

**SURS Collective Deferred Outflows and Deferred Inflows of
Resources by Year to be Recognized in Future Pension Expenses**

| Year Ending June 30 | Net Deferred Outflows of Resources |
|----------------------------|---|
| 2017 | \$ 539,537,000 |
| 2018 | 275,427,000 |
| 2019 | 401,520,000 |
| 2020 | 246,425,000 |
| 2021 | |
| Thereafter | |
| Total | \$ <u>1,462,909,000</u> |

Employer Deferral of Fiscal Year 2017 Pension Expense

Employer paid \$35,483,000 in federal, trust or grant contributions for fiscal year ended June 30, 2017. These contributions were made subsequent to the pension liability date of June 30, 2016 and are recognized as Deferred Outflows of Resources as of June 30, 2017.

Assumptions and Other Inputs

Actuarial assumptions: The actuarial assumptions used in the June 30, 2016 valuation were based on the results of an actuarial experience study for the period June 30, 2010 – 2014. The total pension liability in the June 30, 2016 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

| | |
|---------------------------|---|
| Inflation | 2.75 percent |
| Salary increases | 3.75 to 15.00 percent, including inflation |
| Investment rate of return | 7.25 percent beginning with the actuarial valuation as of June 30, 2014 |

Mortality rates were based on the RP2014 Combined Mortality Table with projected generational mortality and a separate mortality assumption for disabled participants.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of arithmetic real rates of return were adopted by the plan's trustees after considering input from the plan's investment consultant(s) and actuary(s). For each major asset class that is included in the pension plan's target asset allocation as of June 30, 2016, these best estimates are summarized in the following table:

| Asset Class | Target Allocation | Weighted Average Long-Term Expected Real Rate of Return |
|---|--------------------------|--|
| U.S. Equity | 23% | 6.08% |
| Private Equity | 6% | 8.73% |
| Non-U.S. Equity | 19% | 6.95% |
| Global Equity | 8% | 6.78% |
| Fixed Income | 19% | 1.17% |
| Treasury-Inflation Protected Securities | 4% | 1.41% |
| Emerging Market Debt | 3% | 4.44% |
| Real Estate REITS | 4% | 5.75% |
| Direct Real Estate | 6% | 4.62% |
| Commodities | 2% | 4.23% |
| Hedged Strategies | 5% | 4.00% |
| Opportunity Fund | 1% | 6.54% |
| Total | 100% | 5.09% |
| Inflation | | 2.75% |
| Expected Arithmetic Return | | 7.84% |

Discount Rate: A single discount rate of 7.010% was used to measure the total pension liability. This single discount rate was based on an expected rate of return on pension plan investments of 7.250% and a municipal bond rate of 2.85% (based on the weekly rate closest to but not later than the measurement date of the 20-Year Bond Buyer Index as published by the Federal Reserve). The projection of cash flows used to determine this single discount rate were the amounts of contributions attributable to current plan members and assumed that plan member contributions will be made at the current contribution rate and that employer contributions will be made at rates equal to the statutory contribution rates under SURS' funding policy. Based on these assumptions, the pension plan's fiduciary net position and future contributions were sufficient to finance the benefit payments through the year 2073. As a result, the long-term expected rate of return on pension plan investments was applied to projected benefit payments through the year 2073, and the municipal bond rate was applied to all benefit payments after that date.

Sensitivity of the SURS' Net Pension Liability to Changes in the Discount Rate: Regarding the sensitivity of the net pension liability to changes in the single discount rate, the following presents the plan's net pension liability, calculated using a single discount rate of 7.01%, as well as what the plan's net pension liability would be if it were calculated using a single discount rate that is 1-percentage-point lower or 1-percentage-point higher:

| 1% Decrease 6.01% | Current Single Discount Rate Assumption 7.01% | 1% Increase 8.01% |
|--------------------------|--|--------------------------|
| <u>\$31,348,832,000</u> | <u>\$25,965,272,000</u> | <u>\$21,502,422,000</u> |

Additional information regarding the SURS basic financial statements including the Plan Net Position can be found in the SURS comprehensive annual financial report by accessing the website at www.SURS.org.

(12) Postemployment Benefits

The State Employees Group Insurance Act of 1971 (Act), as amended, authorizes the State to provide health, dental, vision, and life insurance benefits for certain retirees and their dependents. Substantially, all State and university employees become eligible for these other postemployment benefits (OPEB) if they eventually become annuitants of one of the State sponsored pension plans. CMS administers these benefits for annuitants with the assistance of the State's sponsored pension plans. The portions of the Act related to OPEB establish a cost-sharing multiple-employer defined-benefit OPEB plan (plan) with a special funding situation in which the State funds substantially all nonparticipant contributions. The plan does not issue a stand-alone financial report but is included as a part of the State's financial statements. A copy of the financial statements of the State can be obtained at www.ioc.state.il.us.

The health, dental, and vision benefits provided to and contribution amounts required from annuitants are the result of collective bargaining between the State and various unions that represent the State's and the University employees in accordance with limitations established in the Act. Therefore, the benefits provided and contribution amounts are subject to periodic change. The Act requires the State to provide life insurance benefits for annuitants equal to their annual salary as of the last day of employment until age 60, at which time the benefit amount becomes \$5,000.

The State makes substantially all of the contributions for OPEB on behalf of the State universities. Since the State contributes substantially all of the employer contributions, the single-employer provisions of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, have been followed for reporting the plan. The State is not required to and does not fund the plan other than the pay-as-you-go amount necessary to provide the current benefits.

(13) Commitments and Contingencies

At June 30, 2017, the University had commitments on various construction projects and contracts for repairs and renovation of facilities of \$234,793,000.

The University purchases the majority of natural gas and electricity from Prairieland and guarantees payment by Prairieland to its energy suppliers. Unconditional guaranty agreements are in place with Prairieland's energy suppliers for an aggregate amount not to exceed \$57,250,000. The exposure related to Prairieland at June 30, 2017 is \$4,967,000 for all energy suppliers. This exposure includes the mark-to-market positions on forward contracts and the accounts payable accrued for each vendor.

The University receives moneys from federal and state government agencies under grants and contracts for research and other activities. The costs, both direct and indirect, charged to these grants and contracts are subject to audit and disallowance by the granting agency. The University believes that any disallowances or adjustments would not have a material effect on the University's financial position.

The University also receives moneys under third-party payor arrangements for payment of medical services rendered at its hospital and clinics. Some of these arrangements allow for settlement adjustments based on costs and other factors. The University believes that any adjustments would not have a material effect on the University's financial position.

The University is a defendant in a number of legal actions primarily related to medical malpractice. These legal actions have been considered in estimating the University's accrued self-insurance liability. The total of amounts claimed under these legal actions, including potential settlements and amounts relating to losses incurred but not reported, could exceed the amount of the self-insurance liability. In the opinion of the University's administrative officers, the University's self-insurance liability and limited excess indemnity insurance coverage from commercial carriers are adequate to cover the ultimate liability of these legal actions, in all material respects.

In 2004, the Office of the Inspector General of the U.S. Department of Health and Human Services (OIG) conducted an audit of the Medicaid disproportionate share hospital (DSH) programs in ten states for the years 1997 through 2000, including the State of Illinois. The OIG's audit report indicated that the State of Illinois' Medicaid DSH payments exceeded hospital-specific limits, and that the Federal share of those overpayments was \$145.8 million, of which \$140.3 million related to payments made to the University's hospital. The Illinois Department of Healthcare and Family Services (IDHFS) believes it followed guidelines published by the U. S. Centers for Medicare and Medicaid Services (CMMS) and that its methodology for calculating the hospital-specific limit had consistently been approved by CMMS. However, on July 25, 2016, CMMS issued a formal notice to IDHFS that it had adopted the OIG's recommendation and was requesting repayment by IDHFS of the \$140.3 million associated with the University's hospital. In January 2017, IDHFS filed an appeal notice with the U.S. Department of Health and Human Services Departmental Appeals Board. At this time, neither CMMS nor IDHFS has made a repayment request to the University or its hospital. The impact to the University, if any, will be determined after the appeal process concludes.

(14) Operating Expenses by Natural Classification

Operating expenses by natural classification for the year ended June 30, 2017 for the University and the URO – Foundation are summarized as follows:

| University Operating Expenses by Natural Classification | | | | | |
|--|----------------------------------|------------------------------|--------------------|---------------------|---------------------|
| (In thousands) | | | | | |
| | Compensation and benefits | Supplies and services | Student aid | Depreciation | Total |
| Instruction | \$ 1,407,926 | 89,142 | 6,001 | | \$ 1,503,069 |
| Research | 539,813 | 251,433 | 3,280 | | 794,526 |
| Public service | 301,559 | 179,128 | 1,289 | | 481,976 |
| Academic support | 439,289 | 127,249 | 7,249 | | 573,787 |
| Student services | 163,129 | 49,845 | 5,913 | | 218,887 |
| Institutional support | 285,642 | 292 | | | 285,934 |
| Operation and maintenance of plant | 69,248 | 235,241 | 6,824 | | 311,313 |
| Scholarships and fellowships | 239,793 | 1,234 | 57,928 | | 298,955 |
| Auxiliary enterprises | 192,261 | 194,052 | 16,617 | | 402,930 |
| Hospital and medical activities | 599,442 | 393,514 | | | 992,956 |
| Independent operations | 2,186 | 7,568 | | | 9,754 |
| Depreciation | | | | 262,534 | 262,534 |
| Total | \$ 4,240,288 | 1,528,698 | 105,101 | 262,534 | \$ 6,136,621 |

| URO – Foundation Operating Expenses by Natural Classification | | | | |
|--|--|------------------------------|---------------------|-------------------|
| (In thousands) | | | | |
| | Distributions on behalf of the University | Institutional support | Depreciation | Total |
| Fund-raising | \$ | 16,399 | | \$ 16,399 |
| Distributions on behalf of the University | | 196,666 | | 196,666 |
| General and administrative | | 14,875 | | 14,875 |
| Actuarial adjustments | | 2,415 | | 2,415 |
| Depreciation | | | 1,513 | 1,513 |
| Total | \$ 196,666 | 33,689 | 1,513 | \$ 231,868 |

(15) Segment Information

The following information represents identifiable activities within the University financial statements for which one or more revenue bonds are outstanding.

(a) The Auxiliary Facilities System (AFS)

AFS financial activity mainly comprises housing, parking and student activities, which span across the three campuses of the University. The operating revenues of the AFS largely consist of student service fees, various user fees, room and board charges, sales from merchandise/vending and rental of certain facilities. Facilities primarily consist of buildings and other structures that have been constructed or remodeled with funding provided from issuance of related revenue bonds. AFS facilities include Memorial Stadium, the State Farm Center, student unions, housing residence halls, parking and other structures. Operating expenses of the AFS include all necessary current maintenance charges, expenses of reasonable upkeep and repairs, allocations of a share of certain charges for insurance and other expenses incidental to the operations of all of the various activities and facilities of the AFS in accordance with the bond indentures.

(b) The Health Services Facilities System (HSFS)

HSFS is comprised of the University of Illinois Hospital and associated clinical facilities providing patient care at, but not limited to, the University of Illinois at Chicago Medical Center. HSFS is a tertiary care facility located primarily in Chicago, Illinois offering a full range of clinical services. HSFS does not include the operations of the University Medical Service Plans or Colleges of Medicine. Management of the HSFS is the responsibility of the University.

Condensed Statements of Net Position

June 30, 2017

(In thousands)

| | <u>AFS</u> | <u>HSFS</u> | <u>Total</u> |
|---|---------------------|----------------|---------------------|
| Assets and deferred outflow of resources: | | | |
| Current assets | \$ 220,622 | 356,597 | \$ 577,219 |
| Noncurrent assets: | | | |
| Capital assets, net of accumulated depreciation | 1,135,778 | 201,619 | 1,337,397 |
| Other noncurrent assets | 41,688 | 32,772 | 74,460 |
| Deferred outflow of resources | 26,233 | 4,667 | 30,900 |
| Total assets and deferred outflow of resources | <u>\$ 1,424,321</u> | <u>595,655</u> | <u>\$ 2,019,976</u> |
| Liabilities: | | | |
| Current liabilities | \$ 95,229 | 132,610 | \$ 227,839 |
| Noncurrent liabilities: | | | |
| Long-term debt | 1,087,508 | 109,450 | 1,196,958 |
| Other liabilities | 13,701 | 25,902 | 39,603 |
| Total liabilities | <u>1,196,438</u> | <u>267,962</u> | <u>1,464,400</u> |
| Net position: | | | |
| Net investment in capital assets | 49,293 | 100,077 | 149,370 |
| Restricted: | | | |
| Expendable | 178,590 | 17,060 | 195,650 |
| Unrestricted | 227,883 | 210,556 | 210,556 |
| Total net position | <u>227,883</u> | <u>327,693</u> | <u>555,576</u> |
| Total liabilities and net position | <u>\$ 1,424,321</u> | <u>595,655</u> | <u>\$ 2,019,976</u> |

Condensed Statement of Revenues, Expenses and Changes in Net Position

Year ended June 30, 2017

(In thousands)

| | <u>AFS</u> | <u>HSFS</u> | <u>Total</u> |
|---------------------------------|-------------------|----------------|-------------------|
| Operating revenues | \$ 359,412 | 739,463 | \$ 1,098,875 |
| Operating expenses | 338,595 | 997,675 | 1,336,270 |
| Depreciation expense | 38,806 | 20,846 | 59,652 |
| Operating loss | (17,989) | (279,058) | (297,047) |
| Nonoperating revenues, net | 23,101 | 291,910 | 315,011 |
| Increase in net position | 5,112 | 12,852 | 17,964 |
| Net position, beginning of year | 222,771 | 314,841 | 537,612 |
| Net position, end of year | <u>\$ 227,883</u> | <u>327,693</u> | <u>\$ 555,576</u> |

Condensed Statement of Cash Flows

Year ended June 30, 2017

(In thousands)

| | | | |
|---|-------------------|----------------|-------------------|
| Net cash flows provided by operating activities | \$ 86,707 | 69,039 | \$ 155,746 |
| Net cash flows provided by noncapital financing activities | | 59 | 59 |
| Net cash flows used in capital and related financing activities | (133,077) | (43,204) | (176,281) |
| Net cash flows provided by investing activities | <u>41,068</u> | <u>15,461</u> | <u>56,529</u> |
| Net (decrease) increase in cash and cash equivalents | (5,302) | 41,355 | 36,053 |
| Cash and cash equivalents, beginning of year | <u>219,817</u> | <u>158,291</u> | <u>378,108</u> |
| Cash and cash equivalents, end of year | <u>\$ 214,515</u> | <u>199,646</u> | <u>\$ 414,161</u> |

(16) University Related Organizations

The Entity's financial statements include the activities of the University Related Organizations, which are presented as discretely presented component units in the accompanying financial statements. Since these component units are discretely presented, the activities between them and the University are not eliminated on the Entity's financial statements. Conversely, the University and its component units are consolidated on the State's comprehensive annual financial report, therefore, the following disclosure is presented.

**University and University Related Organizations Transactions
Presented to Facilitate State of Illinois Reporting**

(In thousands)

| | <u>Distributions on behalf of University</u> | <u>Advances from (Repayments to) University, net</u> | <u>Services/Goods Provided to University</u> | <u>Services/Goods Provided by University</u> | <u>Total</u> |
|--------------------|--|--|--|--|-------------------|
| Foundation | \$ 196,666 | | 9,038 | | \$ 205,704 |
| Alumni Association | | | 2,720 | | 2,720 |
| WWT | | | 15,468 | | 15,468 |
| Illinois Ventures | | | 2,020 | | 2,020 |
| Research Park | | | 219 | | 219 |
| Prairieland | | | 39,242 | 2,063 | 41,305 |
| Singapore Research | | (2,649) | | | (2,649) |
| Total | <u>\$ 196,666</u> | <u>(2,649)</u> | <u>68,707</u> | <u>2,063</u> | <u>\$ 264,787</u> |

The transactions disclosed in the table above are not all inclusive and represent those transactions the University deemed significant. Additional details regarding these transactions are provided on the financial statements of each related organization.

Below are condensed financial statements by organization:

Condensed Statements of Net Position

June 30, 2017

(In thousands)

| | <u>Foundation</u> | <u>Alumni Association</u> | <u>WWT</u> | <u>Illinois Ventures</u> |
|--|---------------------|-------------------------------|--------------|------------------------------|
| Assets and deferred outflow of resources: | | | | |
| Current assets | \$ 56,442 | 1,362 | 1,322 | 2,792 |
| Noncurrent assets: | | | | |
| Capital assets, net of accumulated depreciation | 11,863 | 1,428 | 15 | 1 |
| Other noncurrent assets | 2,057,463 | 14,625 | | 3,321 |
| Deferred outflow of resources | | | | |
| Total assets and deferred outflow of resources | <u>\$ 2,125,768</u> | <u>17,415</u> | <u>1,337</u> | <u>6,114</u> |
| Liabilities and deferred inflow of resources: | | | | |
| Current liabilities | \$ 12,537 | 418 | 1,319 | 122 |
| Due to related organizations | | | | |
| Noncurrent liabilities | 44,016 | 9 | | |
| Deferred inflow of resources | | | | |
| Total liabilities and deferred inflow of resources | <u>56,553</u> | <u>427</u> | <u>1,319</u> | <u>122</u> |
| Net position: | | | | |
| Net investment in capital assets | 7,900 | 1,428 | 15 | 1 |
| Restricted: | | | | |
| Nonexpendable | 1,047,420 | | | 13 |
| Expendable | 997,326 | | | |
| Unrestricted | <u>16,569</u> | <u>15,560</u> | <u>3</u> | <u>5,978</u> |
| Total net position | <u>2,069,215</u> | <u>16,988</u> | <u>18</u> | <u>5,992</u> |
| Total liabilities, deferred inflow of resources and net position | <u>\$ 2,125,768</u> | <u>17,415</u> | <u>1,337</u> | <u>6,114</u> |

Condensed Statement of Revenues, Expenses and Changes in Net Position

Year ended June 30, 2017

(In thousands)

| | | | | |
|--|---------------------|---------------|------------|--------------|
| Operating revenues | \$ 143,253 | 4,627 | 15,829 | 2,569 |
| Operating expenses | 230,355 | 5,971 | 15,468 | 2,087 |
| Depreciation expense | <u>1,513</u> | <u>18</u> | <u>13</u> | <u>1</u> |
| Operating income (loss) | (88,615) | (1,362) | 348 | 481 |
| Nonoperating revenues (expenses), net | 260,516 | 2,705 | | (957) |
| Contributions to endowments | <u>57,160</u> | | | |
| (Decrease) increase in net position | <u>229,061</u> | <u>1,343</u> | <u>348</u> | <u>(476)</u> |
| Net position, beginning of year | 1,840,154 | 15,645 | (330) | 6,002 |
| Adjustment for correction of error | | | | 466 |
| Net position, beginning of year, as restated | | | | <u>6,468</u> |
| Net position, end of year | <u>\$ 2,069,215</u> | <u>16,988</u> | <u>18</u> | <u>5,992</u> |

Condensed Statements of Net Position
June 30, 2017

| | (In thousands) | | | |
|---|--------------------------|--------------------|-------------------------------|---------------------|
| | <u>Research Park</u> | <u>PrairieLand</u> | <u>Singapore Research</u> | <u>Total</u> |
| Assets and Deferred Outflow of Resources: | | | | |
| Current assets | \$ 628 | 7,570 | 4,870 | \$ 74,986 |
| Noncurrent assets: | | | | |
| Capital assets, net of accumulated depreciation | 1,449 | 9 | 188 | 14,953 |
| Other noncurrent assets | | | | 2,075,409 |
| Deferred outflow of resources | | 154 | | 154 |
| Total assets and deferred outflow of resources | <u>\$ 2,077</u> | <u>7,733</u> | <u>5,058</u> | <u>\$ 2,165,502</u> |
| Liabilities and Deferred Inflow of Resources: | | | | |
| Current liabilities | \$ 32 | 5,790 | 641 | \$ 20,859 |
| Due to related organizations | | | 4,123 | 4,123 |
| Noncurrent liabilities | | 36 | | 44,061 |
| Deferred inflow of resources | | 118 | | 118 |
| Total liabilities and deferred inflow of resources | <u>32</u> | <u>5,944</u> | <u>4,764</u> | <u>69,161</u> |
| Net position: | | | | |
| Net investment in capital assets | 1,449 | 9 | 188 | 10,990 |
| Restricted: | | | | |
| Nonexpendable | | | | 1,047,433 |
| Expendable | | | | 997,326 |
| Unrestricted | 596 | 1,780 | 106 | 40,592 |
| Total net position | <u>2,045</u> | <u>1,789</u> | <u>294</u> | <u>2,096,341</u> |
| Total liabilities, deferred inflow of resources, and net position | <u>\$ 2,077</u> | <u>7,733</u> | <u>5,058</u> | <u>\$ 2,165,502</u> |

Condensed Statement of Revenues, Expenses and Changes in Net Position
Year ended June 30, 2017

| | (In thousands) | | | |
|--|-----------------|--------------|------------|---------------------|
| Operating revenues | \$ 667 | 41,966 | 8,301 | \$ 217,212 |
| Operating expenses | 553 | 41,872 | 8,103 | 304,409 |
| Depreciation expense | 79 | 9 | 190 | 1,823 |
| Operating income (loss) | 35 | 85 | 8 | (89,020) |
| Nonoperating revenues (expenses), net | | 2 | (191) | 262,075 |
| Contributions to endowments | | | | 57,160 |
| (Decrease) increase in net position | 35 | 87 | (183) | 230,215 |
| Net position, beginning of year | 2,010 | 1,702 | 477 | 1,865,660 |
| Adjustment for correction of error | | | | 466 |
| Net position, beginning of year, as restated | | | | 1,866,126 |
| Net position, end of year | <u>\$ 2,045</u> | <u>1,789</u> | <u>294</u> | <u>\$ 2,096,341</u> |

(17) Subsequent Events

On July 6, 2017, the State passed legislation, which included an appropriation of \$300 million to provide additional funding for fiscal year 2017 expenditures. This legislation also included an appropriation of \$589 million to fund fiscal year 2018 expenditures. To comply with GASB reporting requirements, the University plans to report the total amount of these appropriations, \$889 million, as revenue in fiscal year 2018. The legislation also included a provision to create a new pension plan option for SURS. Upon implementation of this plan option, normal employer pension costs for eligible newly-hired University employees will be shifted to the University. Additionally, certain existing University SURS-eligible employees hired on or after January 1, 2011 will also have an irrevocable option to enroll in this new plan option. For the eligible employees electing this option, normal employer pension costs, incurred on or after the implementation date of the plan option, will also be shifted to the University. The new plan option is under development by SURS and the implementation date has yet to be determined. Also, with this legislation, the University will become responsible for the normal pension cost of the portion of eligible employee earnings that exceeds the amount set for the State of Illinois Governor's salary, effective beginning fiscal year 2018.

In early fiscal year 2018, the Singapore Research URO secured new grant funding from Singapore's National Research Foundation. The new grant provides a level of program funding to allow Singapore Research to continue its research activities for an additional five years.

In November 2017, the Board approved a Public-Private Partnership for the construction of a mixed use facility, largely comprised of dormitory and academic space, at the University of Illinois at Chicago. The University will partner with CHF - Chicago, LLC (CHF) and its student housing developer, American Campus Communities SC Management, LLC (ACC). Through agreements among the parties, ACC will implement the design, development, construction, equipment, and operations of the facility. CHF will be the owner of the building and debtor on the bonds issued to finance the project. The total cost of this project is estimated at \$100 million. The project is slated to commence in fiscal year 2018, with anticipated completion to enable use by the University beginning in the fall 2019 semester.

UNIVERSITY OF ILLINOIS
Required Supplementary Information
Year Ended June 30, 2017
(In thousands)

| Schedule of Share of the Net Pension Liability | Fiscal Year 2016 | Fiscal Year 2015 | Fiscal Year 2014 |
|---|-----------------------------|-----------------------------|-----------------------------|
| (a) Proportion percentage of the collective net pension liability | 0% | 0% | 0% |
| (b) Proportion amount of the collective net pension liability | \$ - | \$ - | \$ - |
| (c) Portion of nonemployer contributing entities' total proportion of collective net pension liability associated with employer | 10,996,379 | 9,957,590 | 8,995,845 |
| Total (b) + (c) | 10,996,379 | 9,957,590 | 8,995,845 |
| Employer defined benefit covered payroll | \$ 2,059,866 | \$ 2,029,795 | \$ 1,953,692 |
| Proportion of collective net pension liability associated with employer as a percentage of defined benefit covered payroll | 533.84% | 490.57% | 460.45% |
| SURS plan net position as a percentage of total pension liability | 39.57% | 42.37% | 44.39% |

| Schedule of Contributions | Fiscal Year 2017 | Fiscal Year 2016 | Fiscal Year 2015 | Fiscal Year 2014 |
|---|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| Federal, trust, grant and other contribution | \$ 35,483 | \$ 34,753 | \$ 33,473 | \$ 34,200 |
| Contribution in relation to required contribution | 35,483 | 34,753 | 33,473 | 34,200 |
| Contribution deficiency (excess) | - | - | - | - |
| Employer covered payroll | \$ 2,090,578 | \$ 2,059,866 | \$ 2,029,795 | \$ 1,953,692 |
| Contributions as a percentage of covered payroll | 1.70% | 1.69% | 1.65% | 1.75% |

UNIVERSITY OF ILLINOIS
Notes to Required Supplementary Information
Year Ended June 30, 2017

Changes of benefit terms. There were no benefit changes recognized in the Total Pension Liability as of June 30, 2016.

Changes of assumptions. In accordance with Illinois Compiled Statutes, an actuarial review is to be performed at least once every three years to determine the reasonableness of actuarial assumptions regarding the retirement, disability, mortality, turnover, interest and salary of the members and benefit recipients of SURS. An experience review for the years June 30, 2010 to June 30, 2014 was performed in February 2015, resulting in the adoption of new assumptions as of June 30, 2015.

- Mortality rates. Change from the RP 2000 Mortality table projected to 2017, sex distinct, to the RP-2014 mortality tables with projected generational mortality improvement. Change to a separate mortality assumption for disabled participants.
- Salary increases. Change assumption to service-based rates, ranging from 3.75 percent to 15.00 percent based on years of service, with underlying wage inflation of 3.75 percent.
- Normal retirement rates. Change to retirement rates at ages younger than 60, age 66, and ages 70-79 to reflect observed experiences.
- Early retirement rates. Change to a slight increase to the rates at ages 55 and 56.
- Turnover rates. Change to produce lower expected turnover for members with less than 10 years of service and higher turnover for members with more than 10 years of service than the currently assumed rates.
- Disability rates. Decrease rates and have separate rates for males and females to reflect observed experience.
- Dependent assumption. Maintain the current assumption on marital status that varies by age and sex and the assumption that males are three years older than their spouses.

*Note: The University implemented GASB No. 68 in fiscal year 2015. The information above is presented for as many years as available. The Schedule is intended to show information for 10 years.