

# UNIVERSITY OF PITTSBURGH



## FINANCIAL REPORT FISCAL YEAR 2013



**KPMG LLP**  
BNY Mellon Center  
Suite 2500  
500 Grant Street  
Pittsburgh, PA 15219-2598

## **Independent Auditors' Report**

The Board of Trustees of the  
University of Pittsburgh - Of the Commonwealth  
System of Higher Education:

We have audited the accompanying consolidated financial statements of The University of Pittsburgh - Of the Commonwealth System of Higher Education (the University), which comprise the consolidated balance sheets as of June 30, 2013 and 2012, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements.

### ***Management's Responsibility for the Financial Statements***

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

### ***Auditors' Responsibility***

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

### ***Opinion***

In our opinion, the consolidated financial statements referred to above present fairly in all material respects, the financial position of the University of Pittsburgh - Of the Commonwealth System of Higher Education as of June 30, 2013 and 2012, and the changes in their net assets and their cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

**KPMG LLP**

Pittsburgh, Pennsylvania  
September 17, 2013

CONSOLIDATED FINANCIAL STATEMENTS

UNIVERSITY OF PITTSBURGH  
CONSOLIDATED BALANCE SHEETS  
JUNE 30, 2013 AND 2012  
*(in thousands of dollars)*

	2013	2012
<b>ASSETS:</b>		
Cash and cash equivalents <i>(Notes 1 and 5)</i>	\$ 196,807	\$ 47,751
Operating investments <i>(Notes 4 and 5)</i>	407,586	627,386
Inventories and deferred charges	22,700	21,986
Accounts and notes receivable, net <i>(Note 2)</i>	160,053	158,464
Contributions receivable, net <i>(Note 3)</i>	32,857	58,994
Student loans receivable, net	48,569	48,027
Deposits of bond and note proceeds <i>(Notes 1 and 5)</i>	90,403	8,514
Foundation assets <i>(Note 1)</i>	22,726	21,234
Endowment investments <i>(Notes 4 and 5)</i>	2,994,207	2,635,487
Endowed funds held by third parties <i>(Note 5)</i>	19,954	18,074
Property, plant, and equipment, net <i>(Note 6)</i>	1,788,475	1,715,731
<b>TOTAL ASSETS</b>	<b>\$ 5,784,337</b>	<b>\$ 5,361,648</b>
<b>LIABILITIES:</b>		
Accounts payable and accrued expenses	\$ 103,358	\$ 100,310
Accrued payroll and related liabilities	75,008	76,713
Deferred student and other revenue	43,775	37,815
Advanced receipt of grant funds	71,582	82,853
Refundable U.S. government student loans	32,928	32,559
Other liabilities <i>(Notes 5 and 9)</i>	103,685	140,955
Pension and postretirement obligations <i>(Note 10)</i>	406,825	431,957
Conditional asset remediation obligation <i>(Note 7)</i>	40,571	40,946
Bonds and notes payable <i>(Note 8)</i>	1,103,491	1,017,134
<b>TOTAL LIABILITIES</b>	<b>1,981,223</b>	<b>1,961,242</b>
<b>NET ASSETS:</b>		
Unrestricted <i>(Notes 1 and 11)</i>	2,506,552	2,184,101
Temporarily restricted <i>(Notes 1 and 11)</i>	674,134	622,629
Permanently restricted <i>(Notes 1 and 11)</i>	622,428	593,676
<b>TOTAL NET ASSETS</b>	<b>3,803,114</b>	<b>3,400,406</b>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<b>\$ 5,784,337</b>	<b>\$ 5,361,648</b>

*The accompanying notes are an integral part of these consolidated financial statements.*

CONSOLIDATED FINANCIAL STATEMENTS

UNIVERSITY OF PITTSBURGH  
CONSOLIDATED STATEMENT OF ACTIVITIES  
FOR THE YEAR ENDED JUNE 30, 2013  
COMPARED TO SUMMARY INFORMATION FOR THE YEAR ENDED JUNE 30, 2012  
(in thousands of dollars)

	2013			Total	2012
	Unrestricted	Temporarily Restricted	Permanently Restricted		
<b>OPERATING REVENUES:</b>					
Tuition and fees	\$ 703,914	\$ -	\$ -	\$ 703,914	\$ 682,545
Tuition discounts	(158,216)	-	-	(158,216)	(157,468)
Net tuition and fees	545,698	-	-	545,698	525,077
Commonwealth appropriation	144,308	-	-	144,308	137,649
Commonwealth construction grants	43,996	-	-	43,996	38,019
Grants and contracts	738,502	-	-	738,502	730,085
Grants and contracts - ARRA	20,890	-	-	20,890	50,320
Contributions for operations	31,967	5,392	-	37,359	43,248
Investment income - operating investments	8,532	-	-	8,532	13,679
Endowment distributions for operations	87,513	-	-	87,513	82,595
Sales and services, educational and other	143,042	-	-	143,042	136,129
Sales and services, auxiliary	132,565	-	-	132,565	132,926
Rental revenue	18,353	-	-	18,353	18,182
Other	65,073	-	-	65,073	68,961
Net assets released from restrictions	19,687	(19,687)	-	-	-
<b>Total operating revenues</b>	<b>2,000,126</b>	<b>(14,295)</b>	<b>-</b>	<b>1,985,831</b>	<b>1,976,870</b>
<b>OPERATING EXPENSES:</b>					
Salaries and wages	867,745	-	-	867,745	869,173
Fringe benefits	264,221	-	-	264,221	266,108
Total compensation	1,131,966	-	-	1,131,966	1,135,281
Supplies	107,384	-	-	107,384	114,140
Business and professional	297,487	-	-	297,487	300,322
Utilities	47,093	-	-	47,093	47,536
Maintenance and facilities	43,248	-	-	43,248	44,906
Depreciation	151,542	-	-	151,542	145,716
Interest	44,784	-	-	44,784	46,631
Other	57,216	-	-	57,216	54,598
<b>Total operating expenses (Note 12)</b>	<b>1,880,720</b>	<b>-</b>	<b>-</b>	<b>1,880,720</b>	<b>1,889,130</b>
<b>Change in net assets from operating activities</b>	<b>119,406</b>	<b>(14,295)</b>	<b>-</b>	<b>105,111</b>	<b>87,740</b>
<b>OTHER ACTIVITIES:</b>					
Investment gains (losses), net of endowment distributions for operations	118,481	65,800	2,737	187,018	(40,699)
Contributions for endowment	-	-	26,015	26,015	35,790
Change in fair value of interest rate swaps	41,166	-	-	41,166	(61,629)
Nonperiodic changes in benefit plans including special termination (Note 10)	43,398	-	-	43,398	(111,750)
<b>Total other activities</b>	<b>203,045</b>	<b>65,800</b>	<b>28,752</b>	<b>297,597</b>	<b>(178,288)</b>
<b>CHANGE IN NET ASSETS</b>	<b>322,451</b>	<b>51,505</b>	<b>28,752</b>	<b>402,708</b>	<b>(90,548)</b>
<b>NET ASSETS, BEGINNING OF YEAR</b>	<b>2,184,101</b>	<b>622,629</b>	<b>593,676</b>	<b>3,400,406</b>	<b>3,490,954</b>
<b>NET ASSETS, END OF YEAR</b>	<b>\$ 2,506,552</b>	<b>\$ 674,134</b>	<b>\$ 622,428</b>	<b>\$ 3,803,114</b>	<b>\$ 3,400,406</b>

The accompanying notes are an integral part of these consolidated financial statements.

UNIVERSITY OF PITTSBURGH  
CONSOLIDATED STATEMENT OF ACTIVITIES  
FOR THE YEAR ENDED JUNE 30, 2012  
(in thousands of dollars)

	2012			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
<b>OPERATING REVENUES:</b>				
Tuition and fees	\$ 682,545	\$ -	\$ -	\$ 682,545
Tuition discounts	(157,468)	-	-	(157,468)
Net tuition and fees	525,077	-	-	525,077
Commonwealth appropriation	137,649	-	-	137,649
Commonwealth construction grants	38,019	-	-	38,019
Grants and contracts	730,085	-	-	730,085
Grants and contracts - ARRA	50,320	-	-	50,320
Contributions for operations	24,234	19,014	-	43,248
Investment income - operating investments	13,679	-	-	13,679
Endowment distributions for operations	82,595	-	-	82,595
Sales and services, educational and other	136,129	-	-	136,129
Sales and services, auxiliary	132,926	-	-	132,926
Rental revenue	18,182	-	-	18,182
Other	68,961	-	-	68,961
Net assets released from restrictions	14,797	(14,797)	-	-
<b>Total operating revenues</b>	<b>1,972,653</b>	<b>4,217</b>	<b>-</b>	<b>1,976,870</b>
<b>OPERATING EXPENSES:</b>				
Salaries and wages	869,173	-	-	869,173
Fringe benefits	266,108	-	-	266,108
Total compensation	1,135,281	-	-	1,135,281
Supplies	114,140	-	-	114,140
Business and professional	300,322	-	-	300,322
Utilities	47,536	-	-	47,536
Maintenance and facilities	44,906	-	-	44,906
Depreciation	145,716	-	-	145,716
Interest	46,631	-	-	46,631
Other	54,598	-	-	54,598
<b>Total operating expenses (Note 12)</b>	<b>1,889,130</b>	<b>-</b>	<b>-</b>	<b>1,889,130</b>
<b>Change in net assets from operating activities</b>	<b>83,523</b>	<b>4,217</b>	<b>-</b>	<b>87,740</b>
<b>OTHER ACTIVITIES:</b>				
Investment (losses) gains, net of endowment distributions for operations	(9,740)	(33,892)	2,933	(40,699)
Contributions for endowment	-	-	35,790	35,790
Change in fair value of interest rate swaps	(61,629)	-	-	(61,629)
Nonperiodic changes in benefit plans including special termination (Note 10)	(111,750)	-	-	(111,750)
<b>Total other activities</b>	<b>(183,119)</b>	<b>(33,892)</b>	<b>38,723</b>	<b>(178,288)</b>
<b>CHANGE IN NET ASSETS</b>	<b>(99,596)</b>	<b>(29,675)</b>	<b>38,723</b>	<b>(90,548)</b>
<b>NET ASSETS, BEGINNING OF YEAR</b>	<b>2,283,697</b>	<b>652,304</b>	<b>554,953</b>	<b>3,490,954</b>
<b>NET ASSETS, END OF YEAR</b>	<b>\$ 2,184,101</b>	<b>\$ 622,629</b>	<b>\$ 593,676</b>	<b>\$ 3,400,406</b>

CONSOLIDATED FINANCIAL STATEMENTS

UNIVERSITY OF PITTSBURGH  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED JUNE 30, 2013 AND 2012  
(in thousands of dollars)

	2013	2012
<b>CASH AND CASH EQUIVALENTS:</b>		
End of year	\$ 196,807	\$ 47,751
Beginning of year	47,751	87,061
<b>CHANGE IN CASH AND CASH EQUIVALENTS</b>	<b>\$ 149,056</b>	<b>\$ (39,310)</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Change in net assets	\$ 402,708	\$ (90,548)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	151,542	145,716
Net bond premium amortization	(5,961)	(6,226)
Loss on disposal of plant assets	3,814	2,408
Investment gains	(245,311)	(16,432)
Change in fair value of interest rate swaps	(41,166)	61,629
Contributions restricted for long-term investment	(87,130)	(76,621)
Changes in operating assets and liabilities:		
Accounts, notes, contributions, and loan receivables, net	24,006	(11,937)
Other assets	(714)	852
Accounts payable and accrued expenses	442	(9,892)
Pension and postretirement obligations	(25,132)	126,712
Conditional asset remediation obligation	(375)	87
Other liabilities	2,191	(2,178)
Government student loans and deferred revenue	(4,942)	1,138
<b>Net cash provided by operating activities</b>	<b>173,972</b>	<b>124,708</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Expended for property, plant, and equipment - University	(184,104)	(151,079)
Expended for property, plant, and equipment - commonwealth	(43,996)	(38,019)
Change in accounts payable for property, plant, and equipment	2,606	(7,904)
Change in investments held under securities lending program	-	101,855
Change in liabilities under securities lending program	-	(101,855)
Purchases/sales of operating investments, net	218,145	(11,017)
Purchases of endowment investments	(1,352,853)	(1,424,870)
Proceeds from sales/maturities of endowment investments	1,239,205	1,357,327
Change in endowed funds held by third parties, excluding gains	14	-
Change in foundation assets	(1,492)	3,531
<b>Net cash used for investing activities</b>	<b>(122,475)</b>	<b>(272,031)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Principal repayment of debt	(30,000)	(131,500)
Proceeds from issuance of debt	122,318	122,262
Change in deposits of bond and note proceeds	(81,889)	40,630
Contributions restricted for long-term investment	87,130	76,621
<b>Net cash provided by financing activities</b>	<b>97,559</b>	<b>108,013</b>
<b>CHANGE IN CASH AND CASH EQUIVALENTS</b>	<b>\$ 149,056</b>	<b>\$ (39,310)</b>
<b>Supplemental disclosure of cash flow information:</b>		
Cash paid for interest (excluding fees)	\$ 51,117	\$ 53,268
<b>Noncash investing activity for property, plant, and equipment-accounts payable</b>	<b>\$ 34,786</b>	<b>\$ 32,180</b>

The accompanying notes are an integral part of these consolidated financial statements.

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING  
AND REPORTING PRACTICES**Organization**

Founded in 1787, the University of Pittsburgh of the Commonwealth System of Higher Education (the University) is an institution of higher education with a three-pronged mission to provide the highest-quality instruction for its students, engage in innovative research activities, and support the state and local community through public service programs. In its 226 year history, the University has evolved into an internationally recognized center of learning and research. The University's main campus in the City of Pittsburgh is comprised of 16 schools and several academic centers educating nearly 29,000 students in various undergraduate, graduate, and first professional programs. Four regional campuses with a total enrollment approximating 6,500 students are located throughout western Pennsylvania.

**Relationship with the Commonwealth of Pennsylvania**

The University derives its corporate existence under the laws of the Commonwealth of Pennsylvania (the commonwealth) by reason of the act of the General Assembly of the commonwealth establishing an "Academy or Public School in the town of Pittsburgh" on February 28, 1787 and from the act of February 18, 1819 incorporating the "Western University of Pennsylvania." In 1908, the University's name was changed to the "University of Pittsburgh" by order of the Court of Common Pleas of Allegheny County. In 1966, the Pennsylvania State Legislature enacted the "University of Pittsburgh-Commonwealth Act," which changed the name of the University to the "University of Pittsburgh – of the Commonwealth System of Higher Education" and established the University as an instrumentality of the commonwealth to serve as a state-related institution in the Commonwealth System of Higher Education. The University is a Pennsylvania nonprofit corporation subject to the Nonprofit Corporation Law of 1988.

The entire management, control, and conduct of the instructional, administrative, and financial affairs of the University are vested in the Board of Trustees. The Board of Trustees is composed of fifty-two members (thirty-six voting members), including twelve commonwealth trustees and sixteen special trustees elected by the board. Special trustees may attend all meetings of the board and are entitled to and exercise all rights, responsibilities, and privileges of trusteeship, except the right to vote at board meetings.

As a state-related institution, the University receives an annual operating appropriation from the commonwealth. The appropriation is subject to the commonwealth's annual budget process. There is no assurance that such appropriation will continue to be made, or will be made, at current levels or at levels requested by the University. The appropriation from the commonwealth was \$144.3 million in 2013 and \$137.6 million in 2012.

In addition to the annual appropriation, the commonwealth also funds certain capital projects in support of the University's mission. Amounts funded by the commonwealth for capital projects were \$44.0 million in 2013 and \$38.0 million in 2012.

**Basis of Presentation**

The consolidated financial statements include the accounts of the University, which do not include the net assets or activities of the University of Pittsburgh Medical Center (UPMC) or the University of Pittsburgh Physicians (UPP) clinical practice plans, as they are separate legal entities not controlled by the University. The University does have the right to designate one-third of the members of the UPMC Governing Board and its Executive Committee.

The other activities section of the Consolidated Statements of Activities includes investment gains (losses), net of endowment distributions for operations; contributions for endowment; changes in fair value of interest rate swaps; nonperiodic changes in pension and postretirement benefit plans; and other nonrecurring or unusual revenues or expenses. Endowment distributions for operations represent endowment income distributions that are not reinvested in the endowment (see Note 11).

**Basis of Accounting**

The consolidated financial statements have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America (GAAP) as promulgated by the Financial Accounting Standards Board (FASB).

In accordance with GAAP, the University's net assets have been classified as either unrestricted, temporarily restricted, or permanently restricted based upon the existence or absence of donor-imposed restrictions. Unrestricted net assets are not subject to donor-imposed restrictions and are used for general operating purposes of

the University. This class of net assets also includes certain contributions and endowment earnings whose donor-imposed restrictions have been met within the fiscal year. Temporarily restricted net assets are subject to certain time or purpose restrictions by the donor. Upon satisfaction of these restrictions, the net assets are transferred to unrestricted. Amounts released from restrictions in fiscal 2013 and 2012 relate primarily to cash collections on pledges where purpose restrictions had already been met. Temporarily restricted net assets at June 30, 2013 and 2012 consist of endowment balances (\$648.9 million and \$583.5 million, respectively); the net present value of temporarily restricted contributions and unconditional pledges (\$20.6 million and \$34.5 million, respectively); and split-interest agreements (\$4.6 million in both years). Permanently restricted net assets are those subject to permanent donor-imposed restrictions and at June 30, 2013 and 2012 consist of endowment balances (\$597.5 million and \$556.3 million, respectively); the net present value of permanently restricted contributions and unconditional pledges (\$12.8 million and \$25.5 million, respectively); and private student loan funds (\$12.1 million and \$11.9 million, respectively).

Donor-restricted endowed contributions require that the original corpus of the contributions be maintained in perpetuity. The distributions from earnings generated by these contributions may be either expended or reinvested in the endowment, in accordance with donor restrictions and contribution and spending policies (see Note 11).

#### **Estimates**

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from those estimates.

#### **Revenue Recognition**

Revenue for programs or activities to be conducted in future periods such as student tuition and room and board are classified as deferred revenue. Revenue for these activities is recognized as services are provided. Advanced receipt of exchange transactions such as grants and contracts are also classified as deferred revenue, with

revenue being recognized as funds are expended and sponsored programs are executed.

Tuition discounts are recorded to the extent that either institutional financial aid or aid funded by contributions, endowment distributions, and grant activities are awarded. Tuition discounts attributable to institutional funds in 2013 and 2012 were \$136.9 million and \$135.1 million, respectively. Tuition discounts attributable to contributions, endowment distributions, and grant activities in 2013 and 2012 were \$21.3 million and \$22.4 million, respectively.

#### **Government Loan Funds**

U.S. government-sponsored student loan funds are recorded as liabilities because these funds are refundable to the federal government under certain conditions. Student loan funds donated by private groups, organizations, or individuals are recorded as permanently restricted net assets since such funds operate on a revolving fund basis with principal and interest payments remaining in the fund for future lending.

#### **Cash and Cash Equivalents and Operating Investments**

Cash equivalents consist of investments with original maturities of three months or less and all assets invested in the University's short-term investment fund, which the University utilizes to fund daily cash needs. The fund invests in short-term Treasury securities and other short-term, high quality securities, all of which can be liquidated without penalty within 7 days. All securities held in the fund must be rated A3/P-1 or better by Moody's Investors Service or A-/A-1 or better by Standard & Poor's Ratings Services at the time of purchase. Cash and cash equivalents that are part of endowment investments are shown therewith as these funds are used for endowment purposes rather than University operating needs.

Operating investments primarily include high quality obligations of the U.S. government and government agencies, bank certificates, commercial paper, corporate notes, and other fixed income obligations. Operating investments are reported at fair value, generally based on quoted market prices, and are used for general operating purposes.



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### **Allowance for Doubtful Accounts**

The University maintains allowances for doubtful accounts to reflect management's best estimate of probable losses inherent in receivable balances. Management determines the allowances for doubtful accounts based on known troubled accounts, historical experience, and other currently available evidence. Receivables are written off when management determines they will not be collected.

### **Deposits of Bond and Note Proceeds**

Deposits of bond and note proceeds consist of unspent funds which will be used for certain capital projects and for repayment of certain debt obligations. These funds are invested in cash, cash equivalents, and U.S. Treasury securities and are reported in the Consolidated Balance Sheets at fair value.

### **Endowment Investments**

The University's endowment investments are reported at fair value. The fair value of direct University holdings in publicly traded securities is based upon quoted market prices. The fair value of all other investments, which consist of indirect holdings in both privately and publicly traded assets, is determined using net asset value (NAV) per share or unit of interest. Used as a practical expedient for the estimated fair value, NAV per share or its equivalent is provided by the fund manager and reviewed by the University. Indirect holdings of private assets primarily consist of University interests in funds investing in nonmarketable alternatives, real assets, and/or distressed securities, whereas indirect holdings of publicly traded assets primarily consist of University interests in marketable alternatives or other commingled funds.

Nonmarketable alternatives are private equity or equity-like holdings, such as mezzanine and subordinated debt interests, in venture, buyout, or recapitalized companies or properties. Real assets are physical assets, or financial assets associated with such physical assets, whose income streams and/or fair values tend to rise with inflation; they include real estate, natural resources, commodities, and other hard assets. Marketable alternatives consist of distressed debt and hedging strategies, including event-driven hedging strategies, such as merger or credit arbitrage, and value-driven hedging strategies, such as long/short, market neutral, and other hedging strategies.

Due to the nature of the investments held by the funds, changes in market conditions, economic environment, regulatory environment, currency exchange rates, interest rates, and commodity price fluctuations may significantly impact the NAV of the funds and, consequently, the fair value of the University's interest in the funds and could materially affect the amounts reported in the consolidated financial statements. Although a secondary market exists for these investments, it is not active, and individual transactions are typically not observable. When transactions do occur in this limited secondary market, they may occur at discounts to the reported NAV. It is therefore at least reasonably possible that if the University were to sell these investments in the secondary market, a buyer may require a discount to the reported NAV, and the discount could be significant. The University attempts to manage these risks through diversification, ongoing due diligence of fund managers, maintaining adequate liquidity, and continuously monitoring economic and market conditions.

### **Derivative Financial Instruments**

The University records derivatives at fair value in the Consolidated Balance Sheets with changes in fair value reflected in the Consolidated Statements of Activities (see Note 9).

### **Contributions**

The University records at fair value unconditional pledges (which are agreements with donors involving nonreciprocal transfers of cash, other assets, or services) as either temporarily restricted or permanently restricted contributions dependent upon the nature of the donor-imposed restrictions. Contributions whose restrictions are met in the same fiscal year as receipt are combined and reported with unrestricted contributions. Contributions receivable are discounted at a risk-adjusted rate commensurate with the donor's payment plan.

Conditional pledges of cash or other assets are recognized as contribution revenues and receivables when the conditions surrounding the pledge are substantially met.

Bequests are considered to be intentions to give and do not fall within the definition of an unconditional pledge, and hence, are not recognized in the consolidated financial statements.

**Split-Interest Agreements**

These agreements with donors consist primarily of charitable gift annuities, pooled income funds, and irrevocable charitable remainder trusts for which the University serves as trustee. Assets are invested and payments are made to donors and/or other beneficiaries in accordance with the respective agreements. Other liabilities include \$9.0 million at June 30, 2013 and 2012 for split-interest agreements.

**Foundation Assets**

The University's foundation assets include the Bradford Educational Foundation (BEF). The BEF is a 509(a)(3) Type III supporting organization whose sole purpose is to receive, administer, and distribute property for the benefit of the University of Pittsburgh Bradford campus. The BEF is governed by an independent board of directors, with the majority of members being non-University members. Although the University does not exercise control of the BEF, all assets held by the BEF are held for the financial benefit of the University. As such, the consolidated financial statements include the net assets and annual change in net assets of the BEF.

**Property, Plant, and Equipment**

Property, plant, and equipment is recorded at cost, or if acquired by contribution, at fair value as of the date of the contribution. Depreciation is calculated using the straight-line method. Useful lives generally range from 15 to 40 years for buildings and improvements and 5 to 10 years for furnishings and equipment. As assets are retired, sold, or otherwise disposed, the cost and related accumulated depreciation are removed from the accounts, and gains or losses are recognized in the Consolidated Statements of Activities. Costs associated with the construction of new facilities and renovation and expansion of existing facilities are capitalized within construction in progress until such projects are placed in service. The University capitalizes software and related implementation costs and generally depreciates such assets over 5 to 10 years. Works of art, historical treasures, and similar assets include a variety of paintings, sculptures, photographs, antiques, and furnishings, as well as scholarly papers and archives. These assets are used for public exhibition, the preservation of artifacts and antiques for

future generations, and scholarly research. Due to their nature, these assets are not depreciated. Library books, which include hard copy publications, periodicals, and electronic publications with rights to archival content, are depreciated over a period of 7 years. Maintenance and repairs are expensed as incurred.

**Insurance Liabilities**

The University is self-insured through an agreement with UPMC to provide medical coverage for its employees. A liability for estimated incurred but unreported claims of \$7.4 million and \$7.6 million has been recorded at June 30, 2013 and 2012, respectively, based upon management's analysis of claims history. This liability is reflected in accrued payroll and related liabilities in the Consolidated Balance Sheets.

The University is also self-insured for certain other activities, including workers' compensation, unemployment compensation, and litigation claims. Liabilities have been established for these programs generally based on third-party administrators' estimates using the University's historical loss experience. The self-insurance accrual is subject to periodic adjustment by the University based on actual loss experience factors. Liabilities for these other self-insured obligations aggregated \$9.5 million and \$9.1 million at June 30, 2013 and 2012, respectively, and are included in accrued payroll and related liabilities on the Consolidated Balance Sheets.

**Grants and Contracts**

The University conducts sponsored program activity with various sponsors, including agencies and departments of the federal government, the commonwealth, local government entities, companies, and foundations. Sponsored activity in 2013 and 2012 was \$759.4 million and \$780.4 million, respectively, with approximately 60% of the funding awarded through the National Institutes of Health. Grants and contracts - ARRA represents funding received through the American Recovery and Reinvestment Act of 2009. Most University sponsored activity is conducted on a cost reimbursable basis with the University receiving funding after the related expenses have been incurred. Certain sponsors, however, provide funding in advance of related expenses, and such

funding is recorded as advanced receipt of grant funds on the Consolidated Balance Sheets. Revenue from sponsored awards is recognized as the related expenses are incurred. There is no assurance that sponsored awards will continue to be made at current levels.

The University incurs both direct and indirect costs in the conduct of its sponsored activity. Recovery of indirect costs through federal awards is based upon predetermined rates negotiated with the Department of Health and Human Services. Indirect cost recovery rates from non-federal sources may vary. Funds received through federal sources are subject to audit each year in accordance with the Office of Management and Budget Circular A-133.

#### **Securities Lending**

Through an agreement with its primary investment custodian, the University made available its securities for loan to borrowers identified by the custodian. In exchange for lending a security, the University received a fee and continued earning applicable interest and dividends on the loaned security. In September 2011, the University terminated its securities lending agreement and all loans were recalled. There were no securities lending transactions in 2013.

#### **Reclassifications**

Certain amounts in the 2012 consolidated financial statements have been reclassified to conform to the presentation of the 2013 consolidated financial statements. Endowment earnings, including gains and losses, in the Consolidated Statements of Activities have been presented as endowment distributions for operations and investment gains (losses), net of endowment distributions for operations.

#### **Tax-Exempt Status**

The University is exempt from federal income tax under Section 501(c)(3) of the United States Internal Revenue Code. Accordingly, it is not subject to income taxes except to the extent it has taxable income from activities that are not related to its exempt purpose.

The University annually reviews its tax positions and has determined that there are no material uncertain tax positions that require recognition in the consolidated financial statements. No provision for income taxes was required for 2013 or 2012.

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#### NOTE 2: ACCOUNTS AND NOTES RECEIVABLE, NET

Accounts and notes receivable, net at June 30 consists of the following:

	2013	2012
	<i>(in thousands of dollars)</i>	
Sponsored research receivables, net	\$ 91,491	\$ 93,284
Plant construction receivables due from commonwealth	22,615	16,039
Hospitals and affiliated organizations receivables, net	19,834	17,429
Student receivables, net	9,837	10,421
Interest income receivables	1,809	3,073
Other receivables, net	14,467	18,218
<b>Total accounts and notes receivable, net</b>	<b>\$ 160,053</b>	<b>\$ 158,464</b>

NOTE 3: CONTRIBUTIONS RECEIVABLE, NET

Contributions receivable, net at June 30 consists of the following:

	2013	2012
	<i>(in thousands of dollars)</i>	
Amounts due in:		
Less than one year	\$ 14,350	\$ 33,797
One to five years	19,602	26,053
Greater than five years	841	1,432
Gross contributions receivable	<u>34,793</u>	<u>61,282</u>
Less:		
Allowance for uncollectible pledges	(1,299)	(1,636)
Unamortized discounts	<u>(637)</u>	<u>(652)</u>
<b>Total contributions receivable, net</b>	<b><u>\$ 32,857</u></b>	<b><u>\$ 58,994</u></b>

At June 30, 2013 and 2012, the five largest outstanding pledge balances represented 37% and 52%, respectively, of the University's net contributions receivable.

The University has been named a beneficiary in the wills of numerous donors or has received conditional pledges totaling \$147.4 million and \$128.8 million at June 30, 2013 and 2012, respectively. These bequests and conditional pledges are not included in the consolidated financial statements.

The University is one of the beneficiaries of the Dietrich Foundation (the Foundation), a public charity created by William S. Dietrich II pursuant to an Amended and Restated Declaration of Trust dated August 23, 2011 (the Trust). The Foundation is a 509(a)(3) Type I supporting organization, organized and operated exclusively for charitable, scientific, and educational purposes. Its primary mission is to provide ongoing support to a number of educational institutions, largely in the greater Pittsburgh area, including the University. The Trust provides that five of the Foundation's nine trustees shall be educational institution trustees, two of whom shall be

appointed by the University. The Foundation expects to make annual distributions to its named charitable beneficiaries, pursuant to which the University would receive 25% of the amount distributed.

The market value of the Foundation's net assets at June 30, 2013 was reported to be approximately \$552.1 million, of which approximately \$138.0 million is attributable to the University based upon current beneficiary allocations. The University has not recognized an interest in the Foundation because the Foundation's trustees, by a super-majority vote, have the authority to adjust the allocation of annual distributions among the educational institution beneficiaries. Distributions from the Foundation are recorded as contributions for endowment in the Consolidated Statement of Activities and are held by the University in separate, permanently restricted funds within the University's endowment; each is designated appropriately as a Dietrich Foundation endowment fund. Distributions received from the Foundation in 2013 totaled \$3.6 million. No distributions were made in 2012.

NOTE 4: ENDOWMENT AND OPERATING INVESTMENTS

Investments at June 30 consist of the following:

	2013	2012
	<i>(in thousands of dollars)</i>	
Endowment investments:		
Pooled	\$ 2,965,077	\$ 2,609,706
Nonpooled	29,130	25,781
Subtotal endowment investments	2,994,207	2,635,487
Operating investments ( <i>Note 1</i> )	407,586	627,386
<b>Total endowment and operating investments</b>	<b>\$ 3,401,793</b>	<b>\$ 3,262,873</b>
Composition of endowment investments:		
Cash and cash equivalents	\$ 58,095	\$ 73,066
Domestic equities	417,065	325,719
International equities	567,732	467,779
U.S. government and government agencies' securities, bank acceptances and certificates, and commercial paper	162,552	161,875
Corporate bonds and other obligations	150,745	136,592
Alternative investment funds and partnerships:		
Marketable alternatives	598,232	458,333
Private equities/venture capital	561,120	574,187
Real assets	478,666	437,936
<b>Total endowment investments</b>	<b>\$ 2,994,207</b>	<b>\$ 2,635,487</b>
Composition of operating investments:		
U.S. government and government agencies' securities, bank acceptances and certificates, and commercial paper	\$ 230,993	\$ 395,246
Corporate bonds and other obligations	159,072	218,950
Other	17,521	13,190
<b>Total operating investments</b>	<b>\$ 407,586</b>	<b>\$ 627,386</b>

Unless precluded by size or donor restrictions, individual endowment fund assets are pooled and collectively managed on a unitized basis. Each endowment fund subscribes to or disposes of units in the pool, using fair value per unit at the beginning of the month such subscription or disposition occurs to account for the transaction.

The philosophies and policies employed in the management of the endowment are long-term by definition, as they are based on the expectation that the endowment will continue to provide financial support to the University in perpetuity. Accordingly, the University's

investment policy is intended to optimize long-term total return—income plus capital appreciation—relative to the level of risk taken.

The University's investment policy contemplates the effects of its spending policy. The endowment spending policy balances the need for reliable and predictable earnings distributions to support current University activities with the desire to maintain the purchasing power of endowment assets so that they can continue providing financial support for future generations (see Note 11).

The following table summarizes the University's investments at June 30, 2013 and 2012 for which net asset value (NAV) was used as a practical expedient to estimate fair value:

Asset Class/Investment Description	Fair Value Determined using NAV		Unfunded Commitments at June 30, 2013	Unfunded Commitments at June 30, 2012
	2013	2012		
<i>(in thousands of dollars)</i>				
Emerging markets equities				
Commingled emerging markets fund	\$ 118,428	\$ 83,357	\$ -	\$ -
Marketable alternatives				
Distressed debt - redeemable	10,704	20,911	-	-
Distressed debt - nonredeemable	41,441	66,269	491	3,320
Multi-strategy/arbitrage	251,953	169,008	-	-
Long/short equity	294,134	202,145	-	-
Total marketable alternatives	598,232	458,333	491	3,320
Nonmarketable alternatives				
Private equity funds	327,174	333,953	237,092	186,162
Venture capital funds	233,946	240,234	85,843	80,877
Total nonmarketable alternatives	561,120	574,187	322,935	267,039
Real assets				
Real assets - redeemable	58,428	36,576	-	-
Private real estate funds	201,423	185,622	67,520	85,504
Private energy funds	165,244	163,607	107,318	42,671
Private timber funds	53,571	52,131	-	3,632
Total real assets	478,666	437,936	174,838	131,807
<b>Total</b>	<b>\$ 1,756,446</b>	<b>\$ 1,553,813</b>	<b>\$ 498,264</b>	<b>\$ 402,166</b>

Descriptions follow for each of the investments set forth in the table above:

#### **Commingled Emerging Markets Fund**

The University's investment is in a commingled fund that holds publicly traded emerging market equities. The investment may be liquidated without penalty within 120 days of providing a month-end notice.

#### **Distressed Debt – Redeemable**

The University's investment is in one commingled fund. The fund is a hedge fund that holds both long and short positions in publicly traded, and some privately traded, distressed securities. Half of the University's interest in

the fund may be redeemed without penalty within the next three months and the other half can be redeemed without penalty in the next 15 months.

#### **Distressed Debt – Nonredeemable**

The University's investments are interests in nine commingled funds managed by three investment managers. All of the funds hold distressed securities traded publicly and/or privately, and all have investment periods of three years or longer, during which committed capital may be called. The University's interests in the funds are reduced typically over multi-year periods as the managers return invested capital and distribute proceeds realized from underlying fund assets.

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### **Multi-Strategy/Arbitrage**

The University's investments are interests in seven commingled funds. These funds are hedge funds that hold both long and short positions in equities, fixed income, and financial derivatives. The University's interests in four of the funds may be liquidated without penalty as follows: (a) two on an annual basis with 45-day notice; (b) one on a quarterly basis with 30-day notice; and (c) one on an annual basis with 30-day notice beginning September 30, 2012. The University's interests in two of the funds may be liquidated in quarterly increments of 25%. One of the funds has a 65-day notice; the other fund has a 75-day notice. The University's interest in the seventh fund is being liquidated, and the University will receive distributions over 2-4 years upon the realization of asset sales.

### **Long/Short Equity**

The University's investments are interests in nine commingled funds. These funds are hedge funds that hold both long and short positions in publicly traded global equities. The University's interests in all but four of the funds may be liquidated without penalty on a quarterly or monthly basis with 30-60 day notice. The University's interests in the remaining four funds may be liquidated without penalty as follows: (a) one on a quarterly basis with 180-day notice; (b) one on a quarterly basis in increments of 25% with 60-day notice; (c) one on an annual basis at calendar year-end with 60-day notice; and (d) one with 60-day notice every three years for 80% of the assets, annually for 10% of the assets, and quarterly for the remaining 10% of the assets.

### **Private Equity Funds**

The University's investments are interests in 70 commingled, private equity funds. These funds are invested in equity and equity-like securities of mostly nonpublicly traded companies over periods of typically three to five years, during which committed capital may be called. The University's interests in private equity funds are considered to be relatively illiquid in that they are not easily transferable and typically achieve liquidity over multi-year periods when and if the fund managers return invested capital or distribute proceeds realized from underlying fund assets.

### **Venture Capital Funds**

The University's investments are interests in 50 commingled, venture capital funds, a form of private equity. These funds are invested in equity and equity-like securities of mostly nonpublicly traded, immature companies over periods of typically three to five years, during which committed capital may be called. The University's interests in venture capital funds are considered to be illiquid in that they are in riskier assets, they are not easily transferable, and they typically can only achieve liquidity over multi-year periods when and if the fund managers return invested capital or distribute proceeds from the underlying fund assets.

### **Real Assets - Redeemable**

The University's investments are interests in two commingled funds. These funds hold publicly traded physical assets, as well as financial assets associated with such physical assets, including real estate, natural resources, commodities, and the global equities of hard asset companies. The University's interest in one of the funds is currently being liquidated; its interest in the other fund is fully redeemable without penalty on a monthly basis with 10-day notice.

### **Private Real Estate Funds**

The University's investments are interests in 31 commingled, private real estate funds. These funds are primarily invested in privately traded real estate-related properties and interests, including interests in companies engaged in real estate operations, and are invested over periods of typically three to five years, during which committed capital may be called. The University's interests in private real estate funds are considered to be relatively illiquid in that they are not easily transferable and typically achieve liquidity over multi-year periods when and if the fund managers return invested capital or distribute proceeds realized from underlying fund assets.

### **Private Energy Funds**

The University's investments are interests in 29 commingled, private energy funds. These funds are primarily invested in privately traded energy-related properties and interests, including interests in oil and gas and other fossil fuel reserves, production, storage, and transporta-

tion facilities, power generating plants, and companies engaged in energy-related activities, and are invested over periods of typically three to five years, during which committed capital may be called. The University's interests in private energy funds are considered to be relatively illiquid in that they are not easily transferable and typically achieve liquidity over multi-year periods when and if the fund managers return invested capital or distribute proceeds realized from underlying fund assets.

**Private Timber Funds**

The University's investments are interests in four commingled, private timber funds. These funds are primarily

invested in privately traded timber properties and interests, including interests in companies that acquire, manage, and sell timberland, and are invested over periods of typically three to five years, during which committed capital may be called. The University's interests in private timber funds are considered to be relatively illiquid in that they are not easily transferable and typically achieve liquidity over extended, multi-year periods as the fund managers return invested capital or distribute proceeds realized from underlying fund assets.



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NOTE 5: FAIR VALUE MEASUREMENTS

As of June 30, 2013 and 2012, the carrying values of the University's inventories and deferred charges, accounts and notes receivable, contributions receivable, accounts payable, accrued expenses, deferred student and other revenue approximate their fair values because of the terms and relatively short maturity. An estimate of the fair value of student loan receivables administered by the University under federal government loan programs is not practical because the receivables can only be assigned to the United States government or its designees.

Assets and liabilities that are reported at fair value on a recurring basis are categorized into a fair value hierarchy. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The three levels of the fair value hierarchy are as follows:

- Level 1 - Quoted prices (unadjusted) in active markets for identical assets that the University has the ability to access at the measurement date. This level of the fair value hierarchy provides the most reliable evidence of fair value and is used to measure fair value whenever available. Instruments valued by Level 1 measures primarily consist of directly held securities that are actively traded in public markets.
- Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. These inputs include quoted prices for similar investments in active markets; quoted prices for identical or similar assets

or liabilities in markets that are not active; inputs other than quoted prices that are observable; and inputs that are derived from observable market data by correlation or other means. Instruments valued by Level 2 measures include University holdings in certain structured debt obligations, University interests in certain commingled investment funds, interest rate swap agreements, certain fund investments for which NAV is used as a practical expedient, and other thinly-traded instruments.

- Level 3 - Inputs that are unobservable for the asset or liability that are used to measure fair value when observable inputs are not available. These are inputs that are developed based on the best information available in the circumstances, which might include the University's own data. Instruments valued by Level 3 measures primarily include University interests in certain fund investments for which NAV per share or its equivalent is used as a practical expedient.

University investments for which NAV is used as a practical expedient to estimate fair value are classified as either Level 2 or 3 assets in the fair value hierarchy, depending on the University's ability to redeem its interest in the fund. If the University's interest can be redeemed without penalty within the near term (generally within 90 days of June 30), the University's interest in the fund is classified as a Level 2 investment, otherwise, the University's interest is classified as a Level 3 investment.

The following tables summarize the inputs used in valuing the University's assets and liabilities carried at fair value at June 30, 2013 and 2012:

	2013			
	Level 1	Level 2	Level 3	Total
Assets	<i>(in thousands of dollars)</i>			
Cash and cash equivalents	\$ 91,964	\$ 104,843	\$ -	\$ 196,807
Endowment investments:				
Cash and cash equivalents	56,607	1,488	-	58,095
Domestic equities	416,635	430	-	417,065
International equities	441,914	118,428	7,390	567,732
U.S. government, corporate bonds, and other obligations	219,414	89,661	4,222	313,297
Marketable alternatives	-	251,831	346,401	598,232
Private equities/venture capital	-	-	561,120	561,120
Real assets	-	58,003	420,663	478,666
Operating investments:				
U.S. government, corporate bonds, and other obligations	320,355	69,710	-	390,065
Other	737	-	16,784	17,521
Deposits of bond and note proceeds	42,399	48,004	-	90,403
Endowed funds held by third parties	-	-	19,954	19,954
<b>Total assets</b>	<b>\$ 1,590,025</b>	<b>\$ 742,398</b>	<b>\$ 1,376,534</b>	<b>\$ 3,708,957</b>
Liabilities				
<b>Interest rate swaps</b>	<b>\$ -</b>	<b>\$ 67,691</b>	<b>\$ -</b>	<b>\$ 67,691</b>
	2012			
	Level 1	Level 2	Level 3	Total
Assets	<i>(in thousands of dollars)</i>			
Cash and cash equivalents	\$ 19,109	\$ 28,642	\$ -	\$ 47,751
Endowment investments:				
Cash and cash equivalents	30,517	42,549	-	73,066
Domestic equities	315,262	10,457	-	325,719
International equities	376,751	83,664	7,364	467,779
U.S. government, corporate bonds, and other obligations	224,484	71,180	2,803	298,467
Marketable alternatives	-	184,338	273,995	458,333
Private equities/venture capital	-	-	574,187	574,187
Real assets	-	35,846	402,090	437,936
Operating investments:				
U.S. government, corporate bonds, and other obligations	511,596	102,600	-	614,196
Other	1,190	-	12,000	13,190
Deposits of bond and note proceeds	4,942	3,572	-	8,514
Endowed funds held by third parties	-	-	18,074	18,074
<b>Total assets</b>	<b>\$ 1,483,851</b>	<b>\$ 562,848</b>	<b>\$ 1,290,513</b>	<b>\$ 3,337,212</b>
Liabilities				
<b>Interest rate swaps</b>	<b>\$ -</b>	<b>\$ 109,127</b>	<b>\$ -</b>	<b>\$ 109,127</b>

The following tables summarize the change in the Level 3 activity for the years ended June 30, 2013 and 2012:

2013							
<i>(in thousands of dollars)</i>							
	U.S. Government						
	International Equities	Corporate and Other	Marketable Alternatives	Real Assets	Private Equities	Other	Total
Balance - June 30, 2012	\$ 7,364	\$ 2,803	\$ 273,995	\$ 402,090	\$ 574,187	\$ 30,074	\$1,290,513
Capital calls/purchases	4,650	-	111,625	48,665	74,782	560	240,282
Distributions/sales	(5,225)	(296)	(43,388)	(60,583)	(139,483)	(784)	(249,759)
Transfers out	-	-	(24,352)	-	-	-	(24,352)
Realized losses	(22)	-	-	-	-	-	(22)
Unrealized gains	623	1,715	28,521	30,491	51,634	6,888	119,872
<b>Balance - June 30, 2013</b>	<b>\$ 7,390</b>	<b>\$ 4,222</b>	<b>\$ 346,401</b>	<b>\$ 420,663</b>	<b>\$ 561,120</b>	<b>\$ 36,738</b>	<b>\$1,376,534</b>

2012							
<i>(in thousands of dollars)</i>							
	U.S. Government						
	International Equities	Corporate and Other	Marketable Alternatives	Real Assets	Private Equities	Other	Total
Balance - June 30, 2011	\$ 12,084	\$ 3,098	\$ 304,350	\$ 357,060	\$ 552,904	\$ 32,020	\$1,261,516
Capital calls/purchases	1,855	-	60,000	58,923	70,564	953	192,295
Distributions/sales	(4,558)	(295)	(35,757)	(62,701)	(91,635)	(2,146)	(197,092)
Transfers out	-	-	(52,306)	-	-	-	(52,306)
Realized losses	(184)	-	-	-	-	-	(184)
Unrealized (losses) gains	(1,833)	-	(2,292)	48,808	42,354	(753)	86,284
<b>Balance - June 30, 2012</b>	<b>\$ 7,364</b>	<b>\$ 2,803</b>	<b>\$ 273,995</b>	<b>\$ 402,090</b>	<b>\$ 574,187</b>	<b>\$ 30,074</b>	<b>\$1,290,513</b>

Gains and losses (realized and unrealized) for Level 3 activity are reported in other activities in the Consolidated Statements of Activities. The unrealized gains related to investments held at June 30, 2013 and 2012 were \$118.3 million and \$89.4 million, respectively.

For the year ended June 30, 2013, \$24.4 million of Level 3 assets were transferred to Level 2 as a result of the expiration of lock-up periods for three marketable alternatives funds; now these investments may be redeemed within 90 days of June 30. There were \$52.3 million of Level 3 assets transferred to Level 2 in 2012 as a result of the expiration of lock-up periods for five marketable alternatives funds.

There were no transfers of investments between Level 1 and Level 2 in 2013 and 2012.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6: PROPERTY, PLANT, AND EQUIPMENT, NET

Property, plant, and equipment, net at June 30 is summarized below:

	2013	2012
	<i>(in thousands of dollars)</i>	
Land	\$ 51,352	\$ 51,255
Buildings and improvements	2,586,824	2,517,555
Equipment	663,045	647,034
Library books	246,905	237,145
Works of art, historical treasures, and similar assets	17,174	14,836
Construction in progress	260,070	160,695
Subtotal	3,825,370	3,628,520
Less: Accumulated depreciation	(2,036,895)	(1,912,789)
<b>Total property, plant, and equipment, net</b>	<b>\$ 1,788,475</b>	<b>\$ 1,715,731</b>

The amount capitalized in property, plant, and equipment related to expenditures funded by the commonwealth on behalf of the University totaled \$530.5 million and

\$526.7 million at June 30, 2013 and 2012, respectively. The net book value of these items was \$226.3 million and \$239.8 million at June 30, 2013 and 2012, respectively.

NOTE 7: CONDITIONAL ASSET REMEDIATION OBLIGATION

The University has recognized liabilities for conditional asset retirement obligations. The University performed an analysis of such obligations and determined that asbestos remediation costs represented the primary source of such liabilities. The University reviewed facilities on all campuses and estimated the timing, method, and cost of remediation. The analysis included an estimated inflation factor and discount rate, which were used to determine the present value of the obligation.

The following table details the change in the liabilities for the year ended June 30:

	2013	2012
	<i>(in thousands of dollars)</i>	
Balance - beginning of year	\$ 40,946	\$ 40,859
Accretion	107	576
Liabilities settled	(482)	(489)
<b>Balance - end of year</b>	<b>\$ 40,571</b>	<b>\$ 40,946</b>

NOTE 8: BONDS AND NOTES PAYABLE

Bonds and notes payable at June 30 are reported based upon outstanding principal and consist of the following:

	Range of Years		Outstanding Principal	
	Remaining to Maturity	2013 Effective Interest Rates	<i>(in thousands of dollars)</i>	
			2013	2012
Variable-rate bonds:				
Series 2007-B Bonds	27-28	0.14%-0.20%	\$ 44,621	\$ 44,621
Series 2005-B Bonds	18-25	0.13%-0.20%	45,000	45,000
Series 2005-C Bonds	19-22	0.14%-0.21%	30,000	30,000
<b>Total variable-rate bonds</b>			<b>119,621</b>	<b>119,621</b>
Term-rate bonds:				
Series 2005-A Bonds	24-26	5.00%	40,000	40,000
Series 2002-B Bonds	18-23	5.00%	15,000	15,000
<b>Total term-rate bonds</b>			<b>55,000</b>	<b>55,000</b>
Fixed-rate bonds and notes:				
Series 2009-A/B Bonds	1-18	3.18%-5.10%	373,140	398,140
Series 2007-B Bonds	10-15	4.28%-4.69%	60,000	60,000
Series 2005-A Bonds	15-17	4.69%-4.83%	35,000	35,000
Series 2002-A Bonds	2-10	2.68%-4.31%	30,000	35,000
Series 2002-B Bonds	13-14	4.53%-4.74%	14,500	14,500
Series 2000-A/B/C Bonds	3 mos.- 22	4.00%-5.07%	154,800	154,800
Series 2012 PANTHER Notes, due July 2, 2013		0.21%	120,000	120,000
Series 2013 PANTHER Notes, due July 11, 2014		0.18%	120,000	-
Noninterest-bearing promissory note			171	171
<b>Total fixed-rate bonds and notes</b>			<b>907,611</b>	<b>817,611</b>
Unamortized net premium			21,259	24,902
<b>Total bonds and notes payable</b>			<b>\$ 1,103,491</b>	<b>\$ 1,017,134</b>

Fair value estimates of the variable-rate bonds are based upon quoted market prices and signify Level 1 liabilities of the fair value hierarchy, whereas fair value estimates of the term-rate bonds, fixed-rate bonds, and notes are based upon observable interest rates and maturity schedules, signifying Level 2 liabilities. The following are the fair value estimates at June 30:

	2013	2012
	<i>(in thousands of dollars)</i>	
Variable-rate bonds (Level 1)	\$ 119,621	\$ 119,621
Term-rate bonds (Level 2)	\$ 55,613	\$ 58,275
Fixed-rate bonds and notes (Level 2)	\$1,005,794	\$ 948,932

The principal payments of bonds and notes payable for the next five years ending June 30 in millions of dollars are:

2014	\$ 150.4
2015	\$ 155.0
2016	\$ 30.5
2017	\$ 27.4
2018	\$ 26.4

The foregoing principal payments do not include \$119.6 million of variable-rate demand bonds (VRDBs) in commercial paper (CP) mode, all of which have final maturity dates between 2031 and 2041. These bonds bear short-term rates that are fixed over staggered periods of approximately 90 days each and are remarketed at the expiry of each rate period.

Liquidity support for the \$119.6 million of outstanding VRDBs in CP mode is provided by the University. In the event the University receives notice of an optional tender on its VRDBs in CP mode, the purchase price of the bonds will be paid from the remarketing of such bonds. However, if the remarketing proceeds are insufficient, the University will have a current obligation to purchase the tendered bonds. To provide a secondary source of liquidity for this type of event, the University entered into a \$100.0 million unsecured standby liquidity agreement with a financial institution that matures in June 2016. Since the October 2009 effective date of the liquidity agreement, no draws have occurred.

The \$55.0 million of term-rate bonds have a mandatory tender date of September 16, 2013. On such date, the University may elect to convert the bonds to CP mode, a new term-rate mode, fixed-rate mode, or some combination thereof.

In June 2013, the University issued its Pitt Asset Notes - Tax Exempt Higher Education Series 2013 (PANTHERS of 2013) in the amount of \$120.0 million. Of this amount, \$70.0 million was used to partially refund the \$120.0 million of PANTHERS of 2012 that matured on July 2, 2013, and \$50.0 million was used for equipment expenditures. The PANTHERS of 2013 mature on July 11, 2014.

The PANTHERS of 2012 were issued in June 2012 in the amount of \$120.0 million and were repaid on July 2, 2013.

The University had three general unsecured credit facilities, aggregating \$75.0 million, at June 30, 2013. No draws were made under the facilities during 2013 or 2012. Although each of the three credit facilities carry an expiry date of October 28, 2013, it is management's intention to extend each facility for another 364-day term.

Interest costs incurred in 2013 and 2012 were \$44.8 million and \$46.6 million, respectively. Included in these amounts is capitalized interest associated with various construction projects. Capitalized interest for 2013 and 2012 was \$2.6 million and \$1.3 million, respectively.

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NOTE 9: DERIVATIVE AND OTHER FINANCIAL INSTRUMENTS

The University does not issue or trade derivative financial instruments except as described herein. University financial assets are invested on its behalf with various investment managers, some of whom are authorized to employ derivative instruments, including swaps, futures, forwards, and options. These derivatives are generally used for managing interest rate or foreign currency risk or to attain or hedge a specific financial market position. Additionally, the University has entered into various interest rate swap agreements to hedge its interest rate risk associated with certain debt obligations.

The University may be exposed to financial loss should a derivative counterparty fail to perform pursuant to the instrument. In the case of exchange-traded derivatives, the counterparty is the exchange itself. In the case of over-the-counter derivatives, the counterparty is typically a financial institution. Counterparty risks are mitigated by using creditworthy counterparties, settling positions periodically, and requiring collateral to be posted at predetermined levels of exposure.

Not including University derivative instruments held by various alternative investment funds, University financial assets invested in derivative instruments had a fair value, based upon Level 1 of the fair value hierarchy, of \$24.4 million and \$19.9 million at June 30, 2013 and 2012, respectively, which are included in endowment investments on the Consolidated Balance Sheets.

The University liabilities arising from variable-to-fixed interest rate swap agreements associated with certain

University debt obligations had an aggregated fair value of \$67.9 million and \$109.1 million at June 30, 2013 and 2012, respectively, and are included in other liabilities on the Consolidated Balance Sheets (see Note 5). The fair value represents the estimated amount the University would be required to pay to terminate these agreements as of the respective fiscal year-end. The University recorded in the Consolidated Statements of Activities an unrealized gain of \$41.2 million and an unrealized loss of \$61.6 million in 2013 and 2012, respectively, due to changes in fair value of the swaps.

The aggregate notional amount of the swap agreements associated with University debt was \$425.7 million at June 30, 2013 and 2012, respectively. These swaps were entered into for the sole purpose of hedging interest payable on certain University VRDBs. The variable interest rates received by the University under the swap agreements are either 67% or 70% of one- or three-month LIBOR, while the fixed rates paid by the University range from 3.25% to 5.14%. Net swap payments made or received by the University are reported in interest expense in the Consolidated Statements of Activities. No collateral was called or posted during 2013 or 2012 with respect to these swap agreements. Furthermore, the University does not anticipate posting collateral pursuant to these swap agreements since the collateral thresholds applicable to the University are infinite at the University's current credit ratings.

## NOTE 10: PENSION AND POSTRETIREMENT OBLIGATIONS

**Pension**

The University provides retirement benefits under contributory or noncontributory plans to substantially all employees. The University's contributory plan provides for participation in the Teachers Insurance and Annuity Association (TIAA) and College Retirement Equities Fund (CREF) and in investment funds of the Vanguard Group. The plan is fully funded and requires three years of service for vesting of the University contribution. Employees hired before January 1, 1995 were immediately vested. University contributions to this plan in 2013 and 2012 were \$71.9 million and \$70.6 million, respectively.

The noncontributory plan is a defined benefit pension plan that covers employees who do not participate in the contributory plan. The plan provides for vesting after five years with pension benefits accruing at 2.1% of base salary or the Social Security wage base, whichever is lower. Pension benefits are payable upon normal retirement at age 65 or early retirement at age 55, in accordance with the conditions and pension eligibility criteria described in the plan. University contributions to this plan in 2013 and 2012 were \$7.2 million and \$2.7 million, respectively.

**Postretirement**

The University also provides postretirement medical and life insurance benefits to eligible employees and their spouses upon retirement through a contributory benefit plan.

Though funding is not required, the University has elected to fund the medical and life insurance portions of its postretirement liability via a quasi-endowment fund, which is managed together with the University's pooled endowment investments (see Notes 4 and 11). The fair value of these investments at June 30, 2013 and 2012 was \$279.4 million and \$244.9 million, respectively, and is included in endowment investments in the Consolidated Balance Sheets. Although the University has established this quasi-endowment for the postretirement plan, payments to beneficiaries of this plan are currently made through nonendowed operating funds.

Under the Medicare Prescription Drug, Improvement, and Modernization Act of 2003, the federal government provides a subsidy to employers equal to 28% of the employer's qualifying prescription drug costs for retirees if the plan offered by the employer is at least actuarially equivalent to Medicare Part D. The University is qualified for and receives the subsidy via a reduction in premiums charged by its provider.

In 2010, the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act (collectively, the Health Care Acts) were signed into law. The Health Care Acts include several provisions that are included in the measurement of the postretirement benefit obligation.



The University uses a measurement date of June 30 for plan assets and the benefit obligations. Information related to the benefit obligation, assets, and funded status of the defined benefit pension plan and the postretirement benefit plan as of and for the years ended June 30, 2013 and 2012 is summarized in the table below:

	Defined Benefit Plan		Postretirement Plan	
	2013	2012	2013	2012
	<i>(in thousands of dollars)</i>			
<b>Net periodic benefit cost:</b>				
Service cost	\$ 5,856	\$ 3,570	\$ 14,687	\$ 10,746
Interest cost	3,908	3,562	17,559	17,471
Expected return on plan assets	(4,303)	(4,180)	-	-
Actuarial loss	1,809	-	3,025	516
Amortization of transition obligation	-	-	3,031	3,031
Amortization of prior service credit	(53)	(224)	(3,965)	(3,965)
<b>Net periodic benefit cost</b>	<b>\$ 7,217</b>	<b>\$ 2,728</b>	<b>\$ 34,337</b>	<b>\$ 27,799</b>
<b>Funded status:</b>				
Benefit obligation at beginning of year	\$ 87,482	\$ 59,969	\$ 398,916	\$ 298,130
Service cost	5,856	3,570	14,687	10,746
Interest cost	3,908	3,562	17,559	17,471
Actuarial (gain) loss	(9,959)	20,981	(26,615)	61,283
Special termination benefit	-	-	-	24,123
Benefits paid	(718)	(600)	(16,071)	(12,837)
<b>Benefit obligation at end of year</b>	<b>\$ 86,569</b>	<b>\$ 87,482</b>	<b>\$ 388,476</b>	<b>\$ 398,916</b>
Fair value of plan assets at beginning of year	\$ 54,441	\$ 52,854		
Actual return on plan assets	7,280	(541)		
Actual plan contributions	7,217	2,728		
Benefits paid	(718)	(600)		
<b>Fair value of plan assets at end of year</b>	<b>\$ 68,220</b>	<b>\$ 54,441</b>		
<b>Funded status - liability recognized in Consolidated Balance Sheets:</b>				
<b>Pension and postretirement obligations</b>	<b>\$ (18,349)</b>	<b>\$ (33,041)</b>	<b>\$(388,476)</b>	<b>\$(398,916)</b>
<b>Accumulated benefit obligation</b>	<b>\$ 82,977</b>	<b>\$ 83,404</b>		

Estimated 2014 employer contribution to the defined benefit plan:

*(in thousands of dollars)* \$ 4,431

	Defined Benefit Plan		Postretirement Plan	
	2013	2012	2013	2012
<b>Weighted-average assumptions used to determine the benefit obligation (liability) at June 30:</b>				
Discount rate	5.0%	4.5%	5.0%	4.5%
Rate of compensation increase	3.0%	3.0%	-	-
Assumed health care trend cost:				
Initial trend - pre-age 65 retirees	-	-	8.0%	8.0%
Initial trend - post-age 65 retirees	-	-	6.0%	7.0%
Ultimate trend	-	-	4.5%	4.5%
Year to reach ultimate	-	-	2021	2020

**Weighted-average assumptions used to determine the net periodic cost (expense) for the years ended June 30:**

Discount rate	4.5%	6.0%	4.5%	6.0%
Rate of compensation increase	3.0%	3.0%	-	-
Expected long-term return on plan assets	8.0%	8.0%	-	-
Assumed health care trend cost:				
Initial trend - pre-age 65 retirees	-	-	8.0%	9.0%
Initial trend - post-age 65 retirees	-	-	7.0%	10.0%
Ultimate trend	-	-	4.5%	5.0%
Year to reach ultimate	-	-	2020	2017

Estimated future benefit payments:	Defined	Postretirement
	Benefit Plan	Plan
	<i>(in thousands of dollars)</i>	
2014	\$ 1,571	\$ 16,789
2015	\$ 1,776	\$ 18,299
2016	\$ 1,990	\$ 18,844
2017	\$ 2,256	\$ 19,278
2018	\$ 2,561	\$ 19,611
2019 - 2023	\$ 17,974	\$ 107,969

A one percentage point change in assumed health care cost trend rates would have the following effects on the postretirement plan:

	Increase		Decrease	
	Revised Amount	Percent Change	Revised Amount	Percent Change
	<i>(in millions of dollars)</i>			
Service and interest cost (medical component only)	\$ 31.8	7.9%	\$ 25.8	12.6%
Total periodic benefit cost	\$ 38.3	11.4%	\$ 28.3	17.6%
Benefit obligation for health care benefits	\$ 376.6	7.4%	\$ 314.5	10.3%
Total benefit obligation	\$ 414.5	6.7%	\$ 352.3	9.3%

#### Pension Assets

Assets related to the University's defined benefit pension plan are segregated in a trust managed by a third-party investment manager. The fair value of these assets at June 30, 2013 and 2012 was \$68.2 million and \$54.4 million, respectively. The fund is invested through common collective trust funds in domestic and international equities and fixed income securities using the S&P 500 Index as a benchmark for domestic equities, the MSCI EAFE Index for international equities, and the Barclays Intermediate Government/Credit Bond Index for the fixed income securities. The specific investment objective is to meet or exceed the investment policy benchmark over the long term. Plan investments are determined using NAV per share as a practical expedient for estimated fair value and are classified in the fair value hierarchy as Level 2, as the University can redeem its interest without penalty, generally within 90 days of June 30.

The long-term investment strategy for pension plan assets is to meet present and future benefit obligations to all participants and beneficiaries; cover reasonable expenses incurred to provide such benefits, including expenses incurred in the administration of the trust and the plan; provide sufficient liquidity to meet benefit and expense payment requirements on a timely basis; and provide a total return that, over the long term, maximizes the ratio of trust assets to liabilities by maximizing investment return, at an appropriate level of risk. The expected return on plan assets is based on a weighted average of

the individual expected return for each asset category in the plan's portfolio. Expected return comprises inflation plus the real rate of return for each asset class.

Over the long term, asset allocation is believed to be the single greatest determinant of risk and return. Asset allocation will deviate from the target percentages due to market movement, cash flows, and investment manager performance. Material deviations from the asset allocation target can alter the expected return and risk of the trust. However, frequent rebalancing to the asset allocation targets may result in significant transaction costs, which can impair the trust's ability to meet its investment objective. Accordingly, the trust portfolio is periodically rebalanced to maintain asset allocations that approximate the targets shown below.

	Target Asset Allocation
Domestic equity	35%
International equity	35%
Fixed income	30%

The actual asset allocation as of June 30, 2013 and 2012 was 63% and 67%, respectively, for combined equities and 37% and 33%, respectively, for fixed income securities.

The fair value of the University's pension plan assets at June 30, by asset category, was as follows:

Asset class	2013	2012
	<i>(in thousands of dollars)</i>	
	<u>Level 2</u>	<u>Level 2</u>
Equity securities:		
Stock index	\$ 20,038	\$ 17,268
Small cap	2,199	1,833
International	21,065	17,272
Debt securities	17,591	15,336
Cash and cash equivalents	7,327	2,732
<b>Total</b>	<b>\$ 68,220</b>	<b>\$ 54,441</b>

In 2012, the University adopted a Voluntary Early Retirement Plan (VERP) for qualified staff who had completed at least 10 years of service and attained age 59 by April 1, 2012. Ultimately, 352 staff accepted the VERP option. The VERP included a separation payment equal to six-month's pay, along with certain medical and other benefits for the staff, spouse, and dependent children.

The separation payment, along with accumulated vacation and sick-day payments, aggregated \$11.1 million and was recognized in the fiscal 2012 Consolidated Statement of Activities and included in accrued payroll and related liabilities on the Consolidated Balance Sheet. The June 30, 2012 postretirement benefit obligation includes \$24.1 million related to the accelerated vesting for the VERP.

NOTE 11: ENDOWMENT NET ASSETS

The commonwealth has not adopted The Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA) and, instead, enacted in December 1998 Pennsylvania Act 141 (codified as Title 15 of the Pennsylvania Consolidated Statutes §5548(c) and referred to herein as “Title 15”) to govern the investment of restricted funds held in trust by Pennsylvania nonprofit corporations. Title 15 permits Pennsylvania nonprofit corporations to elect a total return approach for determining income distributions from restricted funds held in trust, whereby income is defined as a stipulated percentage of the value of the assets held; the stipulated percentage must be determined at least annually and may be no less than 2% nor more than 7%, and the value of the assets held must be averaged over a period of three or more preceding years. A resolution to elect a total return approach for determining endowment income distributions for the University’s consolidated investment pool was passed by the University’s Board of Trustees on October 21, 1999. The University’s endowment income distribution is determined annually using a stipulated per-

centage of 4.25% of the endowment’s three-year average fair value, provided that such distribution is not less than the amount distributed in the previous year. The endowment income distribution amounts for 2013 and 2012 were approximately 4.45% and 4.68%, respectively, of the endowment’s three-year average fair value.

Employing the total return approach, the University records the original value of an endowed contribution as a permanently restricted asset, along with any endowment income distributions that are reinvested in the endowment. Nonendowed funds that lack third party donor restrictions but function as endowments (quasi-endowments) are classified as unrestricted net assets. Gains and losses attributable to donor-restricted endowed funds are recorded as temporarily restricted net assets, whereas gains and losses attributable to quasi-endowment funds are recorded as unrestricted net assets. Temporarily restricted net assets also include nonendowed contributions that are subject to third party donor restrictions with respect to purpose or time.

The University’s endowment net assets at June 30 were as follows:

	2013			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
	<i>(in thousands of dollars)</i>			
Donor-restricted endowment funds	\$ -	\$ 648,930	\$ 597,494	\$ 1,246,424
Quasi-endowment funds	1,735,312	-	-	1,735,312
<b>Total endowment net assets</b>	<b>\$ 1,735,312</b>	<b>\$ 648,930</b>	<b>\$ 597,494</b>	<b>\$ 2,981,736</b>

  

	2012			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
	<i>(in thousands of dollars)</i>			
Donor-restricted endowment funds	\$ -	\$ 583,459	\$ 556,271	\$ 1,139,730
Quasi-endowment funds	1,480,978	-	-	1,480,978
<b>Total endowment net assets</b>	<b>\$ 1,480,978</b>	<b>\$ 583,459</b>	<b>\$ 556,271</b>	<b>\$ 2,620,708</b>

The change in endowment net assets for the years ended June 30, 2013 and 2012 were as follows:

	2013			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
	<i>(in thousands of dollars)</i>			
Endowment net assets - beginning of year	\$ 1,480,978	\$ 583,459	\$ 556,271	\$ 2,620,708
Endowment return:				
Endowment earnings	25,756	-	2,441	28,197
Gains	178,998	65,471	76	244,545
Total endowment return	204,754	65,471	2,517	272,742
Contributions	103	-	38,706	38,809
Distributions for operations	(87,513)	-	-	(87,513)
Net transfers	136,990	-	-	136,990
<b>Endowment net assets - end of year</b>	<b>\$ 1,735,312</b>	<b>\$ 648,930</b>	<b>\$ 597,494</b>	<b>\$ 2,981,736</b>
	2012			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
	<i>(in thousands of dollars)</i>			
Endowment net assets - beginning of year	\$ 1,369,918	\$ 618,607	\$ 519,695	\$ 2,508,220
Endowment return:				
Endowment earnings	23,649	-	1,651	25,300
Gains (losses)	54,792	(35,148)	874	20,518
Total endowment return	78,441	(35,148)	2,525	45,818
Contributions	32	-	34,051	34,083
Distributions for operations	(82,595)	-	-	(82,595)
Net transfers	115,182	-	-	115,182
<b>Endowment net assets - end of year</b>	<b>\$ 1,480,978</b>	<b>\$ 583,459</b>	<b>\$ 556,271</b>	<b>\$ 2,620,708</b>

Approximately 99 percent of the University's endowment funds are collectively managed in a broadly diversified pool of assets called the consolidated investment pool. The Investment Committee of the Board of Trustees pro-

vides general oversight, policy guidance and performance review of the consolidated investment pool and approves asset allocation and spending policies.

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**NOTE 12: FUNCTIONAL EXPENSES**

The University accounts for expenses according to major classes of program services or functions. Functional expenses for the years ended June 30 consist of the following:

	2013	2012
	<i>(in thousands of dollars)</i>	
Instruction	\$ 526,347	\$ 514,625
Research	671,241	690,645
Public service	86,827	88,973
Academic support	174,345	172,910
Libraries	48,537	44,413
Student services	124,437	126,268
Institutional support	125,691	123,324
Auxiliary enterprises	123,295	127,972
<b>Total functional expenses</b>	<b>\$ 1,880,720</b>	<b>\$ 1,889,130</b>

Costs related to the operation and maintenance of property, including depreciation of property and equipment and interest on related debt, are primarily allocated to program and support activities based upon salary effort.

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**NOTE 13: RELATED PARTIES**

The University has relationships and affiliation agreements with separately incorporated entities including UPMC and affiliated hospitals and UPP. These relationships include a common paymaster arrangement for certain University School of Medicine (SOM) faculty with academic and clinical responsibilities; contractual obligations for UPMC and UPP to support certain educational and research functions at the University; and property rental agreements. Transactions with all related entities are conducted in the ordinary course of business and are discussed below.

Certain University SOM faculty and staff provide clinical services through their University appointments to UPMC, UPP, and affiliated hospitals. The University invoices these entities monthly for reimbursement of the clinical portion of the associated compensation costs. SOM faculty members having both a University academic appointment and a separate, external appointment for clinical responsibilities participate in the common paymaster arrangement for purposes of determining appropriate FICA taxation. In addition to the reimbursable compensation costs, the University also engages in other

transactions with these entities, which include providing certain facilities-related services, telephone, mailing, printing, and various other services, which are reimbursed at cost. Reimbursements from UPMC, UPP, and affiliated hospitals for clinical compensation and other costs totaled \$137.2 million and \$128.6 million in 2013 and 2012, respectively.

In 1998, the University signed a 10-year agreement with UPMC that included financial commitments designed to further the two entities' commitment to their interrelated teaching, research, clinical care, and community service missions. As part of the agreement, UPMC provides \$12.5 million annually in funding for the SOM. UPMC also provides additional funding up to \$2.5 million annually on a matching basis. The match is on a one-to-two basis with UPMC matching \$1 for every \$2 provided by the University to support health sciences programs. The University has received this match each year since the inception of the agreement. This agreement was amended in 2007 under essentially the same terms, except for a provision to provide an additional \$10.0 million per year in 2007, increased annually by \$0.5 million

from 2008 through 2016. The University received \$28.0 million and \$27.5 million (including the annual match) in 2013 and 2012, respectively. These amounts are reported as other revenue in the Consolidated Statements of Activities.

UPMC also provided \$13.4 million and \$13.1 million in 2013 and 2012, respectively, of contractual dean's tax, which represents support for the academic and research activities of the SOM. This activity is reported as sales and services, educational and other in the Consolidated Statements of Activities.

The agreement was further amended in 2009 to include additional financial support from UPMC through the Children's Hospital of Pittsburgh of UPMC (CHP) to the University of at least \$7.5 million annually related to an agreement detailing the transfer of certain pediatric research programs from CHP to the University. This transfer standardized procedures, eliminated duplication of services, improved efficiency, reduced costs, and enhanced recruitment efforts for pediatric programs. The University received \$9.6 million and \$8.8 million in 2013 and 2012, respectively, related to this additional support. These amounts are reported as sales and services, educational and other in the Consolidated Statements of Activities.

UPMC also provides additional academic support to the School of Medicine. These funds are used to support new programs, recruit faculty, and for general support of the School's academic mission. The University recorded \$37.7 million and \$32.1 million in 2013 and 2012, respectively. These amounts are reported as sales and services, educational and other in the Consolidated Statements of Activities.

Additionally, UPMC provided support to various departments within the SOM to augment their operating budgets. These payments were made to those departments which do not generate sufficient revenues to meet their research and academic costs. Payments made by UPMC for this purpose totaled \$8.6 million in both 2013 and 2012, and are reported as sales and services, educational and other in the Consolidated Statements of Activities.

The University is involved in certain rental arrangements where the University acts as both lessor or lessee with

UPMC and its affiliates. Rental revenue from UPMC and affiliates totaled \$10.2 million and \$9.9 million in 2013 and 2012, respectively. Rent expense paid to UPMC and affiliates totaled \$24.7 million and \$24.6 million in 2013 and 2012, respectively.

UPMC serves as the provider of health insurance coverage to all eligible University employees who enroll in the plan. The University is self-insured for these costs and reimburses UPMC for actual claims cost. Health insurance expense including administrative fees totaled \$105.7 million and \$110.8 million in 2013 and 2012, respectively, and is reported as fringe benefits on the Consolidated Statements of Activities.

UPMC receives federal matching funds for costs incurred by academic medical centers for medical assistance services. The funds are remitted to the University to support the activities of the SOM, the Western Psychiatric Institute and Clinic (WPIC), the Center for Public Health Practice, and the clinic within the School of Dental Medicine. These remittances were \$8.2 million and \$8.4 million in 2013 and 2012, respectively, and are reported as commonwealth appropriation revenue in the Consolidated Statements of Activities.

In 2003, the University and UPMC created the Medical and Health Sciences Foundation (MHSF), a separate 501(c)(3) organization. The mission of MHSF is to create a unified fundraising organization for the University's schools of the health sciences and UPMC. The arrangement calls for the cost of MHSF to be split evenly between the University and UPMC. In 2013 and 2012, UPMC's share of total operating costs for MHSF totaled \$4.4 million and \$4.0 million, respectively, and is reported as other revenue in the Consolidated Statements of Activities. All contributions generated by MHSF are credited to the University or UPMC based upon donor intent.

In November 2004, the University entered into an agreement with UPMC to jointly construct and own the Carillo Street steam plant, a gas-fired steam-generating facility. The plant provides steam to each entity's respective buildings and is managed by the University. The University maintains an ownership interest of 78.1%, with UPMC having an ownership interest of 21.9%.



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A lease arrangement exists between the University and the commonwealth for WPIC. Since 1949, the University has managed WPIC under an agreement between the University and the commonwealth whereby the University rents for a consideration of \$1 per year the land, building, equipment, and other items that are used by WPIC. The agreement provides for continuing terms of 10 years each; however, this agreement is cancelable by either party on one year's written notice. In 1992, the University subleased to UPMC the land, building, equipment, and other items subject to the current lease arrangement between the commonwealth and the University. This sublease arrangement continued to be in effect during 2013 and 2012. Included in property, plant, and equipment is \$194.9 million and \$197.9 million at June 30, 2013 and 2012, respectively, related to the land, buildings, and equipment used by WPIC. Accumulated depreciation related to these assets totaled \$156.7 million and \$157.0 million at June 30, 2013 and 2012, respectively.

The University also has an arrangement with UPMC whereby certain research-related costs incurred by UPMC (primarily staff compensation) in relation to WPIC and the University of Pittsburgh Cancer Institute (UPCI) research awards are charged to such awards via an electronic billing and reimbursed to UPMC each month. Payments totaled \$30.4 million in 2013 and \$33.6 million in 2012 and are recorded as expenses in the Consolidated Statements of Activities. All billings are recorded at cost.

UPMC provided support payments to UPCI for various subsidies, research initiatives, and general support. These payments totaled \$10.6 million and \$11.1 million in 2013 and 2012, respectively, and are primarily reported in other revenue in the Consolidated Statements of Activities.

NOTE 14: COMMITMENTS AND CONTINGENCIES

At June 30, 2013 and 2012, the University had outstanding contractual commitments of \$57.0 million and \$136.6 million, respectively, for property, plant, and equipment expenditures.

The University engages in various leasing activities as both a lessor and lessee. Rental revenue from operating leases was \$18.4 million and \$18.2 million in 2013 and 2012, respectively. Rental expense for operating leases was \$47.5 million in 2013 and \$48.7 million in 2012. Minimum future rental revenue and expense under operating leases that have initial or remaining noncancelable lease terms for the years ended June 30 are as follows:

	Rental Revenue	Rental Expense
	<i>(in thousands of dollars)</i>	
2014	\$ 17,141	\$ 42,747
2015	\$ 15,514	\$ 39,622
2016	\$ 14,763	\$ 27,239
2017	\$ 5,400	\$ 21,657
2018	\$ 4,362	\$ 20,436
Thereafter	\$ 11,681	\$ 137,225

The University is a defendant in a number of legal actions seeking damages and other relief from the University. While the final outcome of each action cannot be determined at this time, legal counsel and University management are of the opinion that the liability, if any, in these legal actions will not have a material adverse effect on the University's consolidated financial statements.

The University receives significant financial assistance from the federal government including the sponsorship of federal research projects. Grants and contracts normally

provide for the recovery of direct and indirect costs. Recovery of indirect costs is recorded at predetermined rates negotiated with the federal government. Entitlement to these resources for the recovery of the applicable direct and related indirect costs is generally conditioned upon compliance with the terms and conditions of the grant agreements and applicable federal regulations, including the expenditure of the resources for eligible purposes. Substantially all grants and the University's indirect cost rate are subject to financial and compliance reviews and audits by the grantors. In management's opinion, the likelihood of a material adverse outcome upon the University's financial position from those reviews and audits is remote.

As part of ongoing operations, the University enters into utility contracts to secure electric and natural gas rates. These contracts are with various utility suppliers and some of the contracts cover multiple years. The University monitors the energy markets on an ongoing basis, and will make commitments on new rates if deemed in the best interest of the University.

The University conducts a review of contracts and agreements that may contain guarantees, including loan guarantees such as standby letters of credit and indemnifications. In certain contracts, the University agrees to indemnify a third-party service provider under certain circumstances. Pursuant to its bylaws, the University provides indemnification to directors, officers and, in some cases, employees and agents against certain liabilities incurred as a result of service provided on behalf of or at the request of the University. The terms of indemnity vary from agreement to agreement, and the amount of indemnification, if any, cannot be reasonably determined.

NOTE 15: SUBSEQUENT EVENTS

The University has evaluated subsequent events through September 17, 2013, the date on which the consolidated financial statements were issued, and determined that there were no subsequent events requiring disclosure or adjustment to the consolidated financial statements.

MEMBERSHIP OF THE BOARD OF TRUSTEES FISCAL YEAR 2013

<p><b>MEMBERS EX-OFFICIO (NONVOTING)</b></p> <p>Tom Corbett, Governor of the Commonwealth of Pennsylvania</p> <p>Ronald J. Tomalis, Secretary of Education of the Commonwealth of Pennsylvania</p> <p>Rich Fitzgerald, Chief Executive of Allegheny County</p> <p>Luke Ravenstahl, Mayor of the City of Pittsburgh</p>	<p><i>2011 – 15</i></p> <p>Charles E. Bunch Robert G. Lovett Martha Hartle Munsch Stephen R. Tritch</p> <p><i>2012 – 16</i></p> <p>Eva Tansky Blum Catherine D. DeAngelis Brian Generalovich Marlee S. Myers Robert P. Randall</p>	<p><b>ALUMNI TRUSTEES</b></p> <p><i>2009 – 13</i></p> <p>Bobbie Gaunt Bryant J Salter</p> <p><i>2010 – 14</i></p> <p>F. James McCarl III Keith E. Schaefer</p> <p><i>2011 – 15</i></p> <p>Michael A. Bryson</p> <p><i>2012 – 16</i></p> <p>Jack D. Smith</p>	<p><b>EMERITUS TRUSTEES</b></p> <p>Ruggero J. Aldisert J. David Barnes Steven C. Beering Thomas G. Bigley Frank V. Cahouet John G. Conomikes George A. Davidson Jr. Herbert P. Douglas Jr. Helen S. Faison D. Michael Fisher E. Jeanne Gleason J. Roger Glunt Henry L. Hillman Earl F. Hord A. Alice Kindling Paul E. Lego George L. Miles Jr. Frank E. Mosier Alfred L. Moyé H. Lee Noble Thomas H. O'Brien Anthony J.F. O'Reilly James C. Roddey Farrell Rubenstein Richard P. Simmons Dick Thornburgh Edward P. Zemprelli</p>
<p><b>MEMBERS EX-OFFICIO (VOTING)</b></p> <p>Mark A. Nordenberg, Chancellor and Chief Executive Officer</p>	<p><b>SPECIAL TRUSTEES</b></p> <p><i>2009 – 13</i></p> <p>Roberta A. Luxbacher Susan P. McGalla Robert A. Paul Thomas E. Richards</p> <p><i>2010 – 14</i></p> <p>Mary Ellen Callahan Terrence P. Laughlin William E. Strickland Jr. Thomas J. Usher</p>	<p><b>COMMONWEALTH TRUSTEES</b></p> <p><i>G: Governor appointment</i> <i>H: House appointment</i> <i>S: Senate appointment</i></p> <p><i>2009 – 13</i></p> <p>Sy Holzer (G) William K. Lieberman (S) Thomas L. VanKirk (H)</p>	
<p><b>TERM TRUSTEES</b></p> <p><i>2009 – 13</i></p> <p>Suzanne W. Broadhurst Dawne S. Hickton Charles M. Steiner</p> <p><i>2010 – 14</i></p> <p>Robert M. Hernandez John A. Swanson Burton M. Tansky Sam S. Zacharias</p>	<p><i>2011 – 15</i></p> <p>G. Nicholas Beckwith III John H. Pelusi Jr. Emil M. Spadafore Jr. A. David Tilstone</p> <p><i>2012 – 16</i></p> <p>David C. Chavern Brenton L. Saunders Tracey T. Travis</p>	<p><i>2010 – 14</i></p> <p>John A. Maher III (H) Morgan K. O'Brien (G) John J. Verbanac (S)</p> <p><i>2011 – 15</i></p> <p>John A. Barbour (G) Herbert S. Shear (H) Peter C. Varischetti (S)</p> <p><i>2012 – 16</i></p> <p>Jay Costa, Jr. (S) Ira J. Gumberg (G 2008-2012) John Wright Joyce (H 2008-2012)</p>	

The consolidated financial statements have been reviewed and approved by the University's Audit Committee. The Audit Committee is comprised of outside directors having requisite financial expertise and meets regularly with University management and both internal and external auditors to review internal accounting controls, audit issues, and financial reporting matters. The committee meets with the external auditors in private sessions and is also responsible for approving the independent auditing firm retained each year. Nonvoting representatives on the committee include members of the University's administration as well as student, faculty, and staff representatives.